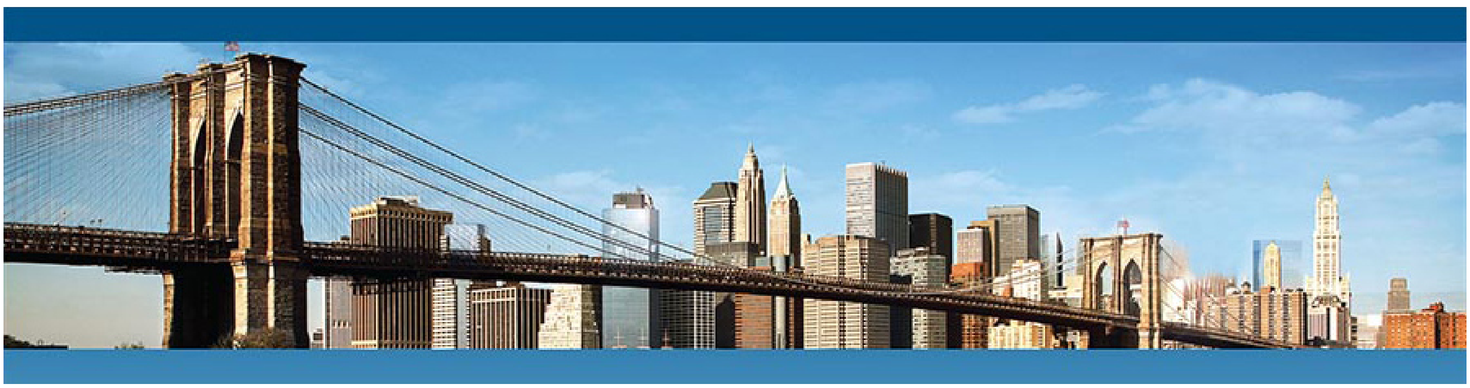
City of New York

OFFICE OF THE COMPTROLLER

Scott M. Stringer
COMPTROLLER



FINANCIAL AUDIT

Marjorie Landa
Deputy Comptroller for Audit

Audit Report on the Compliance of USTA National Tennis Center, Inc. with Its New York City Lease

FN18-082A

August 21, 2019

http://comptroller.nyc.gov

THE CITY OF NEW YORK
OFFICE OF THE COMPTROLLER
SCOTT M. STRINGER

August 21, 2019

To the Residents of the City of New York:

My office has audited the United States Tennis Association Incorporated (USTA) National Tennis Center, Inc. (NTC) on its compliance with its lease (the Lease) with the Department of Parks and Recreation (Parks) to construct, renovate, maintain, manage, and operate the USTA Billie Jean King National Tennis Center (the Tennis Center) at Flushing Meadow-Corona Park, Queens. The audit was performed to determine (1) whether NTC accurately reported its Gross Revenues, properly calculated the Percentage Rent due, and paid all rents on time; and (2) whether NTC complied with other major Lease terms.

The audit found that, although the rent payments NTC made were timely, it underpaid the Percentage Rent it owed to the City as a result of its underreporting at least $31 million in Gross Revenues generated through the Tennis Center for Calendar Years 2014 through 2017. In addition, we found that the USTA's certified financial statements reported $8 million more in US Open revenue and Tennis Center program revenue than the Gross Revenues reported by NTC to the City during Calendar Years 2015, 2016, and 2017. The audit also found that NTC did not consistently submit annual certified financial statements to the City. Further, although NTC paid its water and sewer charges and maintained the required insurance coverage for itself, the USTA did not ensure that sponsors, broadcasters, and vendors maintained the required insurance coverage.

With regard to Parks, the audit found that Parks is unable to properly monitor the Lease due to (1) restrictions placed on its access to critical information; (2) the limited information that NTC is required to report to Parks; and (3) Parks' staffing and capacity limitations. Lastly, the audit found that certain critical aspects in the Lease are not in the best interest of the City because they (1) limit Parks' ability to monitor and enforce NTC's compliance with the Lease, and (2) contain financial terms that are disadvantageous to the City.

The audit makes 11 recommendations including that NTC should remit and Parks should collect $311,202 in additional Percentage Rent due; that NTC should determine with Parks whether additional Percentage Rent is due to the City; and that NTC should ensure that all gross revenues are accurately reported to Parks and that all sponsors, broadcasters, and vendors maintain the required insurance. Further, Parks should review NTC's records for the years our audit did not cover to determine whether additional Percentage Rent is due, and conduct periodic reviews of NTC's compliance with the Lease and seek revision of Lease terms that are not in the City's best interest.

The results of the audit have been discussed with NTC, USTA, and Parks officials, and their comments have been considered in preparing this report. NTC's and Parks' complete written responses are attached to this report. If you have any questions concerning this report, please e-mail my Audit Bureau at audit@comptroller.nyc.gov.

Sincerely,

Scott M. Stringer

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THE CITY OF NEW YORK
OFFICE OF THE COMPTROLLER
FINANCIAL AUDIT

Audit Report on the Compliance of USTA National Tennis Center, Inc. with Its New York City Lease

FN18-082A

EXECUTIVE SUMMARY

On December 22, 1993, the City of New York (the City), through the Department of Parks and Recreation (Parks) entered into a 99-year lease (the Lease) with USTA National Tennis Center, Inc. (NTC) to construct, renovate, maintain, manage, and operate a public recreational facility, also known as USTA Billie Jean King National Tennis Center (the Tennis Center), at the Flushing Meadow-Corona Park, Queens.[1] The Tennis Center consists of four stadiums, indoor and outdoor tennis courts, a pro shop, restaurants, parking areas, and administrative offices. NTC is a wholly owned subsidiary of the United States Tennis Association Incorporated (USTA).

Under the Lease, NTC is expected to: (1) host the United States Open Tennis Championship (the US Open) and other major tennis tournaments and events at the Tennis Center; (2) rent tennis courts; (3) conduct tennis programs for the public; and (4) conduct special events, such as trade shows and graduation ceremonies. The US Open is an international tennis competition in the United States, which is sponsored and operated by NTC's parent corporation, USTA. Based on a separate agreement between USTA and NTC, USTA allows NTC to sell US Open admission tickets and parking privileges, and collect and retain a portion of the revenue from these activities. However, USTA retains the rights to conduct and promote all activities related to the US Open.

NTC is required to pay the City an annual fee of $400,000 (Base Rent) plus one percent of its Net Gross Revenues—Gross Revenues generated through the Tennis Center in excess of $20 million (Percentage Rent) during Calendar Years 2016 and 2017.[2] In addition, per the third amendment of the Lease, signed on March 8, 2010, NTC is allowed to deduct up to $180,000 per annum from the Percentage Rent for payments it makes to the Hall of Science of the City of New York Inc. (HOS) for using the Hall of Science's parking area during the US Open.

For Calendar Years 2016 and 2017, NTC:

- reported approximately $308 million and $349 million in Gross Revenues, respectively;

[1] The initial lease term is from December 22, 1993 through December 31, 2019. After the initial lease term, the Lease is automatically renewed every 10 years for six terms and the last renewal (seventh) term is 14 years.
[2] "Net Gross Revenues" is defined as "the balance of Gross Revenues for such Lease Year after deducting (x) $25 million with respect to each of the first twenty (20) Lease Years . . . and (y) $20 million with respect to each Lease Year thereafter."

- remitted a total of $800,000 ($33,333 per month) in Base Rent; and
- paid a total of $5.8 million in Percentage Rent to the City.

In this audit, we determined whether NTC accurately reported its Gross Revenues, properly calculated the Percentage Rent due, paid all rents on time, and complied with two major non-revenue Lease terms: the maintenance of required insurance coverage, and the payment of water and sewer charges.

Audit Findings and Conclusion

The audit found that while NTC made timely payments of Base Rent and Percentage Rent, maintained the required insurance coverage for itself, and paid water and sewer charges, it underpaid the Percentage Rent to the City as a result of it underreporting at least $31 million in Gross Revenues generated through the Tennis Center for Calendar Years 2014 through 2017. As a result, NTC owes the City at least $311,202 in additional Percentage Rent for that period. In addition, we found that the USTA's certified financial statements reported $8 million more in US Open revenue and Tennis Center program revenue than the Gross Revenues reported by NTC to the City during Calendar Years 2015, 2016, and 2017. Therefore, NTC could potentially owe the City up to $82,310 in additional Percentage Rent.

The audit also found that NTC did not consistently submit annual certified financial statements to the City. Further, we found that NTC did not ensure that sponsors, broadcasters, and vendors maintained the insurance coverage as required by their agreements with USTA.

With regard to Parks, we found that it is unable to properly monitor the Lease due to restrictions placed on its access to critical information similar to those placed on the New York City Comptroller's auditors, the limited information that NTC is required to report to it, and the agency's staffing and capacity limitations.

Further, we found that certain critical aspects of the Lease are not in the best interest of the City because they limit the ability of Parks to monitor and enforce NTC's compliance with the Lease, limit the Comptroller's ability to carry out its City Charter mandated function to independently audit NTC's compliance with the Lease, and contain financial terms that are disadvantageous to the City.

Audit Recommendations

To address these issues, we make five recommendations to NTC and six recommendations to Parks, as follows:

NTC should:

- Remit $311,202 in additional Percentage Rent due to Parks;
- Determine, with Parks, how much of the $82,310 should be remitted to the City as Percentage Rent;
- Ensure all Gross Revenues are accurately reported to Parks in accordance with the terms of the Lease by:
    - Accurately accounting for all in-kind benefits received from the sponsors, broadcasting companies, and vendors;

- Reviewing the Gross Revenues information provided by USTA to ensure there are no inappropriate exclusion or deductions from the Gross Revenues;
    - Including all fees collected from the activities that occurred at the Tennis Center;
    - Accurately recording Gross Revenues in its general ledger; and
    - Making an annual adjustment, when necessary, to the Gross Revenues reported to the City.
- Submit the certified financial statements to the City within the 90 days after the end of each Calendar Year; and
- Ensure all sponsors, broadcasters, and vendors maintain the required insurance coverage.

Parks should:

- Recoup $311,202 in additional Percentage Rent from NTC;
- Ensure NTC submit the certified financial statements annually to Parks;
- Review NTC's books and records for the years that were not covered in our scope period and determine whether NTC owes any additional Percentage Rent;
- Conduct periodic reviews of NTC's compliance of the terms of the Lease;
- Consider seeking revision of the terms of the Lease including, but not limited to:
    - Requiring NTC to submit annual certified financial statements for the entire operation of the Tennis Center or requiring all revenues generated from the Tennis Center be recorded in NTC's general ledger;
    - Allowing the City to copy all books and records relating to the Tennis Center's operation;
    - Requiring NTC to provide electronic copies of the books and records when requested;
    - Imposing late charges when the payments become overdue, not when underpayment exceeds five percent and 10 days after the demanded due date; and
    - Discontinue automatic renewal of the Lease;
    - Cease providing parking credits to NTC after the expiration of the current credits. If Parks finds it is necessary to provide support to NTC for the parking payments, the payments should be deducted from the Gross Revenues; and
- Consider the financial impact to the City before amending any financial terms in the Lease with NTC.

NTC Response

In its written response, NTC agreed with three of the five recommendations and partially agreed with one recommendation, specifically, that it remit $311,202 in additional Percentage Rent due to Parks. As to the partially agreed recommendation, NTC agreed to pay a portion of the Percentage Rent that it owes to Parks as a result of underreporting its Gross Revenues. NTC stated, "Following a thorough review of the Draft Audit's conclusions, the USTA NTC has concluded, based on the legal interpretation of the Lease and the consistent application of GAAP accounting standards, that it should report $14,329,660 as additional Gross Revenues and pay $143,297 in additional rent for the 2014-2017 period."

However, NTC also disputed $167,905 of the $311,202 in Percentage Rent the audit found due, stating, "The deficiencies that exist in the Draft Audit findings result from the auditor misinterpreting the Lease, which they failed to consider specific applicable Lease provisions or failed to comport with or apply GAAP accounting standards, which are mandated by the Lease."

We disagree with NTC's assertion that we misinterpreted the Lease. In fact, NTC's response shows that it did not adequately consider the Lease, which resulted in its having underreported Gross Revenues to the City. NTC does acknowledge a portion of its underreporting and agrees to report more than $14 million additional Gross Revenues, which the audit identified. We also disagree with NTC's contention that it correctly applied GAAP accounting standards, in that we found, for example, that certain Gross Revenues were incorrectly recorded in NTC's expense accounts. Moreover, no claim of compliance with GAAP can supplant NTC's responsibility to comply with the Lease terms when reporting Gross Revenues to the City.

For the remaining recommendation—that NTC ensure that all sponsors, broadcasters, and vendors maintain the required insurance coverage—NTC stated, "This is outside the scope of the audit," and did not address whether it agreed or disagreed with our recommendation.

Parks Response

Parks agreed with five of the six recommendations that were addressed to Parks and stated it will review the relevant records and contracts related to the disputed areas to determine whether additional Percentage Rent is due. In response to the remaining recommendation, Parks stated, "Financial impact to the City is always a critical consideration during any negotiation and Parks strongly disputes any insinuation that this was not the case in our prior negotiations with NTC."

We are glad that NTC remitted $143,297 of $311,202 in additional Percentage Rent due to the City. However, as outlined in our audit finding, NTC is responsible for remitting $311,202, and we urge Parks to collect the remaining balance of $167,905 due to the City.

With regard to the last recommendation, as stated in the report, Parks was unable to provide its rationale for the amendment related to the HOS parking lot arrangement—allowing NTC to deduct that expense directly from its rent. Based on our review of the revised terms, it appears that the amendment inadvertently provided a disproportionate benefit to NTC at the City's expense.

AUDIT REPORT

Background

On December 22, 1993, the City through Parks entered into a 99-year lease with NTC to construct, renovate, maintain, manage, and operate the Tennis Center at the Flushing Meadow-Corona Park, Queens. The Tennis Center consists of four stadiums, indoor and outdoor tennis courts, a pro shop, restaurants, parking areas, and administrative offices. NTC is a wholly owned subsidiary of USTA.

Under the Lease, NTC is expected to: (1) host the US Open and other major tennis tournaments and events at the Tennis Center; (2) rent tennis courts; (3) conduct tennis programs for the public; and (4) conduct special events, such as trade shows and graduation ceremonies. The US Open is an international tennis competition in the United States, which is sponsored and operated by NTC's parent corporation, USTA. Based on a separate agreement between USTA and NTC, USTA allows NTC to sell US Open admission tickets and parking privileges, and collect and retain a portion of the revenue from these activities.[3]

However, USTA retains the rights to conduct and promote all activities related to the US Open, including but not limited to: (a) the sale or license of any and all television, radio, film, and other media rights and any arrangements, and (b) the selection of the manufacturer of the official ball to be used in each US Open. Based on this relationship, NTC only records and accounts for a portion of revenue generated at the Tennis Center including US Open admission ticket sales, tennis court rental, tennis programs, and other miscellaneous income in its general ledger. For the remaining US Open revenue categories that must be reported to Parks as Gross Revenues (*e.g.*, broadcasting rights, sponsorships, catering services and hospitality charges, and commissions from food and merchandises sales), USTA is responsible for collecting and accounting for those revenues in its general ledger. USTA then provides the revenue information it maintains to NTC for the calculation of "Gross Revenues" as defined in the Lease that must be reported to the City.

NTC is required to pay $400,000 in Base Rent annually plus one percent of its Net Gross Revenues as Percentage Rent to the City during Calendar Years 2016 and 2017. In addition, per the third amendment of the Lease, signed on March 8, 2010, NTC is allowed to deduct up to $180,000 per annum from the Percentage Rent for payments it makes to HOS for using the HOS' parking area during the US Open. Base Rent is due on the first day of each month and Percentage Rent is due on February 15, May 15, August 15, and November 15, for the preceding calendar quarter (i.e., December, March, June, and September).

For Calendar Years 2016 and 2017, NTC:

- reported approximately $308 million and $349 million in Gross Revenues, respectively;
- remitted a total of $800,000 ($33,333 per month) in Base Rent; and
- paid a total of $5.8 million in Percentage Rent to the City.[4]

[3] NTC is allowed to retain a portion of the US Open ticket sales to pay for the debt service associated with the capital improvements at the Tennis Center and the operating expenses at the Tennis Center. NTC is also obligated to remit the remaining balance of the ticket sales to USTA.

[4] NTC paid approximately $2.7 million and $3.1 million in Percentage Rent in Calendar Years 2016 and 2017, respectively.

In addition to the rent payment obligation, NTC is also required to:

- submit statements of Gross Revenues (Percentage Rent Reports) to the City within 45 days after each March 31, June 30, and September 30;
- submit audited financial statements to the City within 90 days after each calendar year ended;
- maintain property, liability, and construction insurance coverage; and
- pay water and sewer charges.

Objectives

The objectives of this audit were to determine whether NTC:

- accurately reported its Gross Revenues, properly calculated the Percentage Rent due, and paid all rents on time; and
- complied with two major non-revenue Lease terms: the maintenance of required insurance coverage and the payment of water and sewer charges.

Scope and Methodology Statement

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained during the audit provides a reasonable basis for our findings and conclusions except insofar as certain restrictions were imposed upon us by the Lease and USTA/NTC.

NTC's Lease to operate the Tennis Center contains language in Section 28.03 (a)(i) that states:

> Landlord, the Comptroller of the City . . . and/or Landlord's agents or representatives shall have the right from time to time during regular business hours, upon reasonable advance notice, to inspect and audit all of Tenant's books and records and all other papers and files of Tenant, . . . and such other papers and files as are materially relevant to Tenant's obligations under this Lease.

USTA/NTC limited our access and ability to review financial information that is relevant to the Tennis Center's operation. Specifically, USTA only provided records that it represented were responsive to our requests based on its judgment as to which records were relevant to the operations of the Tennis Center. For example, USTA did not provide certain accounts for our review and refused to provide contact information for a vendor. Without full access to the financial records, our ability to determine whether all revenues generated from the Tennis Center were reported to the City was impeded.

This audit was conducted in accordance with the audit responsibilities of the City Comptroller as set forth in Chapter 5, §93, of the New York City Charter.

The scope period of this audit was Calendar Years 2015 through 2017. However, during the course of the audit, we also found that USTA underreported certain sponsorship revenue in Calendar Year 2014, which was included in the underreported revenue reported in this report.

Please refer to the Detailed Scope and Methodology at the end of this report for the specific procedures and tests that were conducted.

Discussion of Audit Results

The matters covered in this report were discussed with NTC, USTA, and Parks officials during and at the conclusion of this audit. A preliminary draft report was sent to NTC, USTA, and Parks officials and was discussed at an exit conference held on May 30, 2019. Additional information provided by USTA/NTC at and following the exit was taken into consideration in the preparation of the draft report. On August 1, 2019, we submitted a draft report to NTC and Parks officials with a request for written comments. We received a written response from NTC and Parks officials on August 15, 2019.

In its written response, NTC agreed with three of the five recommendations and partially agreed with one recommendation, specifically, that it remit $311,202 in additional Percentage Rent due to Parks. As to the partial recommendation, NTC agreed to pay a portion of the Percentage Rent that it owes to Parks as a result of underreporting Gross Revenues. NTC stated, “Following a thorough review of the Draft Audit’s conclusions, the USTA NTC has concluded, based on the legal interpretation of the Lease and the consistent application of GAAP accounting standards, that it should report $14,329,660 as additional Gross Revenues and pay $143,297 in additional rent for the 2014-2017 period.”

However, NTC also disputed $167,905 of the $311,202 in Percentage Rent the audit found due, stating, “The deficiencies that exist in the Draft Audit findings result from the auditor misinterpreting the Lease, which they failed to consider specific applicable Lease provisions or failed to comport with or apply GAAP accounting standards, which are mandated by the Lease.”

We disagree with NTC’s assertion that we misinterpreted the Lease. In fact, NTC’s response shows that it did not adequately consider the Lease, which resulted in its having underreported Gross Revenues to the City. NTC does acknowledge a portion of its underreporting and agrees to report more than $14 million additional Gross Revenues, which the audit identified. We also disagree with NTC’s contention that it correctly applied GAAP accounting standards, in that we found, for example, that certain Gross Revenues were incorrectly recorded in NTC’s expense accounts. Moreover, no claim of compliance with GAAP can supplant NTC’s responsibility to comply with the Lease terms when reporting Gross Revenues to the City.

For the remaining recommendation—that NTC ensure that all sponsors, broadcasters, and vendors maintain the required insurance coverage—NTC stated, “This is outside the scope of the audit,” and did not address whether it agreed or disagreed with our recommendation.

In Parks’ response, Parks agreed with five of the six recommendations that were addressed to Parks and stated it will review the relevant records and contracts related to the disputed areas to determine whether additional Percentage Rent is due. In response to the remaining recommendation, Parks stated, “Financial impact to the City is always a critical consideration during any negotiation and Parks strongly disputes any insinuation that this was not the case in our prior negotiations with NTC.”

We are glad that NTC remitted $143,297 of $311,202 in additional Percentage Rent due to the City. However, as outlined in our audit finding, NTC is responsible for remitting $311,202, and we urge Parks to collect the remaining balance of $167,905 due to the City.

With regard to the last recommendation, as stated in the report, Parks was unable to provide its rationale for the amendment related to the HOS parking lot arrangement—allowing NTC to deduct that expense directly from its rent. Based on our review of the revised terms, it appears that the amendment inadvertently provided a disproportionate benefit to NTC at the City's expense.

The full text of NTC's and Parks' responses are included as addenda to this report.

FINDINGS

The audit found that while NTC made timely payments of Base Rent and Percentage Rent, maintained the required insurance coverage for itself, and paid water and sewer charges, it underpaid the Percentage Rent to the City as a result of it underreporting at least $31 million in Gross Revenues generated through the Tennis Center for Calendar Years 2014 through 2017. As a result, NTC owes the City at least $311,202 in additional Percentage Rent for that period. In addition, we found that the USTA's certified financial statements reported $8 million more in US Open revenue and Tennis Center program revenue than the Gross Revenues reported by NTC to the City during Calendar Years 2015, 2016, and 2017. Therefore, NTC could potentially owe the City up to $82,310 in additional Percentage Rent.

The audit also found that NTC did not consistently submit annual certified financial statements to the City. Further, we found that NTC did not ensure that sponsors, broadcasters, and vendors maintained the insurance coverage as required by their agreements with USTA.

With regard to Parks, we found that it is unable to properly monitor the Lease due to restrictions placed on its access to critical information similar to those placed on the New York City Comptroller's auditors; the limited information that NTC is required to report to it; and the agency's staffing and capacity limitations.

Further, we found that certain critical aspects of the Lease are not in the best interest of the City, limit the ability of Parks to monitor and enforce NTC's compliance with the Lease, limit the Comptroller's ability to carry out its City Charter mandated function to independently audit NTC's compliance with the Lease, and contain financial terms that are disadvantageous to the City.

NTC Understated Gross Revenues by at Least $31 Million and Owes the City at Least $311,202 in Percentage Rent

NTC failed to accurately report Gross Revenues, generated through the Tennis Center, to the City. As a result, it owes the City, at a minimum, $311,202 in additional Percentage Rent from Calendar Years 2014 through 2017. According to Section 3.03(a) of the Lease, NTC is required to pay the City an annual Percentage Rent in an amount equal to one percent of Net Gross Revenues. Gross Revenues is defined in Section 3.03(d)(ii) as

> any and all gross rents, receipts, fees, proceeds, property, and amounts of any kind (and anything else of monetary value), other than Excluded Revenues, accrued (in accordance with the [Generally Accepted] Accounting Principles) during such Lease Year, directly or indirectly, by or for the account of (x) Tenant, (y) USTA or any successor to the USTA that holds Tennis Events at the Project Site and/or (z) an Affiliate of any of the foregoing Persons . . . from, in connection with, or directly or indirectly arising from, activities occurring at the Project Site and from the operation of the Premises (including, without limitation, conducting Tennis Events)

Based on our review, NTC underreported at least $31 million in Gross Revenues from Calendar Years 2014 through 2017. A breakdown of the types and amounts of underreported revenue, over-reported revenue, and inappropriate deductions taken by NTC in connection with the Percentage Rent is provided in Table I below. Each of these areas is discussed in detail in the following sections of the report, along with a discrepancy between the Tennis Center revenue reported in USTA's financial statements and the amounts NTC reported to the City for the purpose of calculating Percentage Rent payments.

Table I

Summary of Underreported Gross Revenues
and Additional Percentage Rent Due from
Calendar Years 2014 through 2017

Types of Underreported/Over-Reported Revenue or Inappropriate Deductions	Calendar Year				Total Amount
	2014	2015	2016	2017	
Underreported In-Kind Benefits	$3,100,000	$2,980,575	$2,899,186	$2,536,874	$11,516,635
Inappropriate Deductions	-	$3,291,720	$3,234,061	$3,486,036	$10,011,817
Excluded Sponsorship Revenue	$425,000	$1,655,032	$1,392,013	$960,756	$4,432,801
Excluded Ticket Surcharges, Shipping Fees, Handling Fees, and Other Miscellaneous Revenues	-	$2,173,245	$2,314,131	$927,966	$5,415,342
Over-Reported Online Sales and Media Revenues	-	($116,758)	($139,668)	-	($256,426)
Total	**$3,525,000**	**$9,983,814**	**$9,699,723**	**$7,911,632**	**$31,120,169**
				Additional Percentage Rent Due	**$311,202**

NTC Response: "Following a thorough review of the Draft Audits conclusions, the USTA NTC has concluded, based on the legal interpretation of the Lease and the consistent application of GAAP accounting standards, that it should report $14,329,660 as additional Gross Revenues and pay $143,297 in additional rent for the 2014-2017 period.

In other words although the USTA NTC concurs with some of the Draft Audit findings, the Draft Audit and the USTA NTC differ as to $167,905 in additional percentage rent and fees, an average of $43,817 for each of the four (4) years examined between 2014-2017 (based on their difference as to $16,790,509 in additional Gross Revenues for that period)." [Emphasis original.]

Parks Response: "Parks is working with NTC to address the substance of this finding. NTC has acknowledged that there was unintentionally underreporting of Gross Revenues in the amount of $14,329,661, meaning that the additional Percentage Rent amount owed to the City is $143,296.61. Parks has received that amount from NTC. The remaining portion of Percentage Rent, $167,905.39, that the Report contends is owed to the City is disputed by NTC. For those areas that remain in dispute, Parks will review the relevant records and contracts related to the disputed amounts in order to determine if any additional Percentage Rent is due."

Auditor's Comment: We disagree with NTC's contention that it underreported only $14,329,661 and reiterate that NTC underreported $31,120,169. Based on our detailed analysis and review of the documents provided, we have concluded that NTC should pay the City the remaining $167,905. We are glad that NTC remitted $143,297 of $311,202 in additional Percentage Rent and we urge Parks to collect the remaining balance due.

NTC and USTA Did Not Report or Understated over $11 Million of In-Kind Benefits Received

NTC and USTA underreported at least $11,516,635 in Gross Revenues for Calendar Years 2014 through 2017 by either omitting or understating the value of certain in-kind benefits in the Gross Revenues reported to the City in each year.[5] In-kind benefits are goods and services provided by sponsors or broadcasters, in addition to payments made to USTA for sponsorship or broadcasting rights.

As noted, according to the Section 3.03(d)(ii) of the Lease, Gross Revenues include:

> any and all gross rents, receipts, fees, proceeds, property, and amounts of any kind (*and anything else of monetary value*) . . . arising from, activities occurring at the Project Site and from the operation of the Premises (including without limitation, conducting Tennis Events). . . . [Emphasis added.]

The Lease excludes from Gross Revenue only revenue items specifically identified in Section 3.03(d)(iii) as "Excluded Revenues." These Excluded Revenues do not include in-kind benefits that arise from the activities of the Tennis Center which are of "monetary value."

In accordance with the Lease, NTC does report some of its in-kind benefits as a component of the Gross Revenues it reports to the City. However, we found a number of instances where the value of in-kind benefits should have been included by NTC as Gross Revenues reported to the City, but they were not. In particular, we found:

Underreported In-Kind Media Services Provided by Company A

USTA reported some but not all of the in-kind media services provided by Company A pursuant to the sponsorship agreement between USTA and that company. Pursuant to its sponsorship agreement, Company A is required to provide various types of predefined in-kind commercials with a stated total value each year.[6] USTA reported that only a portion of these commercials were related to the US Open and so in accordance with USTA's agreement with NTC, USTA did not report the value it received for the non-US Open related commercials as a component of NTC's Gross Revenues. However, USTA was only able to provide supporting documentation for the in-kind commercials it received during Calendar Year 2017 and not for Calendar Years 2015 and 2016. Moreover, USTA only provided limited documentation (in the form of invoices for the aired commercials) for Calendar Year 2017 and we determined that the invoices do not support the valuation USTA made of the in-kind commercials received from Company A.

Further, we found that the methodology USTA used to allocate only 40 percent of the in-kind benefits to the US Open and 60 percent to other USTA-sponsored tournaments and community

[5] Based on USTA officials' claims that the terms in the sponsorship and broadcasting rights agreements are proprietary and confidential information, we are not disclosing the detail of the in-kind benefit terms in this audit report.

[6] The predefined commercials represent the minimum number of various types of commercials that are required to be provided prior to or during each US Open for promoting US Open or other pre-US Open tournaments. The duration of each commercial varies from 30 seconds to 2 minutes. Ten percent of the stated total value of the in-kind commercials is designated for the provision of three types of predefined commercials prescribed in the agreements.

tennis activities was not supported by the invoices provided. Based on our review of the number of commercials that aired prior to and during the US Open and the value of certain predefined commercials that are prescribed in the Company A's sponsorship agreement, we estimated that 96.3 percent, instead of 40 percent of the total value of the in-kind commercials, should have been reported to the City as in-kind benefits received during Calendar Year 2017. Since USTA was unable to provide any information on the commercials that aired prior to and during 2015 and 2016 US Opens, we applied the same methodology used to estimate the under-reported value for Calendar Year 2017 to Calendar Years 2015 and 2016.

In addition, we found that, contrary to requirements in the Lease, USTA did not report the total value of the in-kind commercials used for US Open promotion to the City *during the year they were received.* Specifically, 30 percent of the value of the in-kind commercials received during Calendar Years 2015 and 2016 was reported retroactively in 2017. However, according to the Lease, Gross Revenues should be reported to the City during the lease year that services were received. Therefore, NTC was not in compliance with the lease term when reporting the in-kind services received during Calendar Years 2015 and 2016.

These findings are reflected in Table II below.

Table II

Percentage of the Value of the In-Kind Commercials Reported to the City for Calendar Years 2015 through 2017

Calendar Year	Percentage of Total Value of In-Kind Commercials Reported to the City during the Calendar Year	Percentage of Total Value of In-Kind Commercials Reported to the City Retroactively during Calendar Year 2017	Percentage of Total Value of Commercials Used for US Open Promotion	
			Per USTA	Per Audit
2015	10%	30%	40%	96.3%
2016	10%	30%	40%	96.3%
2017	40%	-	40%	96.3%

Finally, we found that USTA did not report the value of general marketing and promotional support provided by Company A. According to Section 5A of the sponsorship agreement between USTA and Company A, Company A also agrees to provide general marketing and promotional support for each US Open. Since USTA was unable to provide any documentation to show the value of these in-kind benefits, we were unable to determine the full amount that USTA underreported.

NTC Response: "The Comptroller's audit is incorrectly applying inflated market values and/or incorrectly making allocation assumptions that are not appropriate.

- Underreported In-Kind Media Services Provided by Company A: The USTA NTC did include an allocation of the value of the in-kind media services in Gross Revenues. The basis for the audit finding is the auditor's assessment that USTA NTC was unable to provide sufficient documentation to support the allocation. Subsequently, the auditors used information that was not relevant to this barter in applying a greater value. USTA NTC will review such documentation with the Parks Department and make a determination after the Parks Department has had a chance to review such information."

Auditor's Comment: Contrary to NTC's claims, the audit did not inflate the market values and/or make incorrect allocation assumptions. The values used in the audit report are either stated in USTA's own sponsorship agreements or in the invoices of the media service provider. For the allocation of the in-kind benefits provided by Company A, we made multiple requests for specific documentation to support the allocated values included by NTC in Gross Revenues and were informed that we received all relevant documentation that was available. However, the USTA internal allocation schedule and the "Value in-kind Summaries" provided reflected discrepancies regarding the relevant terms of the agreements between USTA and Company A and lacked information on how USTA utilized the in-kind media services during the US Open in the month of September. Thus, the information used in the audit to determine the in-kind value was taken directly from the relevant agreements and Company A invoices. All other documentation received was created by USTA, and the allocation cannot be substantiated.

Underreported In-Kind Benefit from WiFi Infrastructure and Related Media Services Provided by Company C

USTA did not report the value of WiFi infrastructure and media service provided by Company C. In response to our inquiry about this matter, USTA officials initially stated that the value of the installed WiFi infrastructure at the Tennis Center was in dispute and as a result, the USTA did not report any of the infrastructure value to the City. However, USTA was unable to provide any correspondence with Company C or other documentation to support its contention of such a dispute. Further, documentation that USTA eventually provided to us contradicted its representation of a dispute resulting in the failure to report the WiFi value.[7] It also showed that USTA acknowledged and agreed that Company C had installed the agreed-upon WiFi infrastructure at the Tennis Center and that the value of the infrastructure was more than three times the original required value.

USTA officials acknowledged that they did not report the value to the City in Calendar Year 2014 of the WiFi infrastructure supplied by Company C. In addition, while USTA officials stated that it did not report the media service to the City in Calendar Years 2015 and 2016 because it did not utilize the service. However, USTA was unable to provide any documentation, including correspondence from Company C, to support the claim.

***NTC Response*:** "Included in the Comptroller's findings are value-in-kind infrastructure received from a sponsor at the facility. For a variety of reasons this was not assigned a value, however, USTA NTC is reluctantly remitting payment to the Parks Department in the amount of $31,000.

The Comptroller audit findings incorrectly assume $800K of co-branded media from Sponsor C should be included in the leasehold fee. The USTA NTC extensively explained to the Comptroller Office and provided written certifications from USTA NTC operations that this co-branded media was not of value and not used for the years of the audit finding, specifically 2015 and 2016. The USTA NTC explained to the Comptroller's office that the USTA NTC already had a media plan in place and the cost to redevelop a new co-branded media plan far exceeded the $400K media from the Sponsor. In accordance with GAAP and guidance from our legal counsel, and because the co-branded media was not used and had no value, the USTA NTC is of the opinion such amounts should not be included in the leasehold fee. For further

[7] This additional documentation, which consisted of an amendment to the sponsorship agreement with Company C, dated October 2014, was produced in response to our request for an explanation from USTA as to why USTA provided extra suite sessions (packages of 24 suite sessions sold, as opposed to individual sessions) to Company C in addition to the required number of sessions stated in the sponsorship agreement. The amendment provided justification for USTA providing extra suite sessions to Company C.

clarification, in 2017 USTA NTC used this barter and as required by GAAP recorded $400,000 as barter revenue in the audited financial statements and included it as part of the leasehold fee payment."

Auditor's Comment: During the course of the audit, we repeatedly asked NTC to provide correspondence from Company C to support USTA's claim that it did not utilize the $800,000 media service that Company C was obligated to provide to USTA under the terms specified in its sponsorship agreement. NTC did not provide the requested correspondence; had NTC done so, we would have taken the information provided into consideration when determining the value of this in-kind media service in our audit report. Without corroborating documentation from Company C verifying that its $800,000 media service was not utilized, there is no evidence that confirms NTC's position.

Other Miscellaneous Unreported In-Kind Revenue

- USTA did not report the value of the beverages provided by Company D. USTA officials stated that it was an oversight to not include the value of the beverages provided by this sponsor in Calendar Year 2015.
- USTA did not report the value of complimentary advertising pages provided in the US Open Program by Company T for each of the Calendar Years 2015, 2016, and 2017.
- NTC did not report the value of admission tickets that was provided to a company in exchange for marketing services. These tickets were misclassified as complimentary tickets in the ticket sales record.

Based on our findings above, we determined that NTC understated the value of in-kind benefits received by at least $11,516,635. Therefore, NTC owes the City at least $115,166 in additional Percentage Rent from Calendar Years 2014 through 2017.

NTC Response: "Included in the Comptroller's audit findings are complimentary pages in the US Open Program which can be obtained by fans after they enter the US Open grounds. This arrangement enhances the program with the USTA NTC by providing content to the program, but the complimentary pages do not result in any additional revenue for the US Open Program, nor does it provide any value (financially or otherwise) to the USTA NTC. The Comptroller draft report incorrectly assigns a value to these pages based on the premise this is US Open advertising; however, these pages are not advertising. The pages provide content to the Program rather than procuring independent advertising. As such the USTA correctly did not assign any value to these pages as they are not advertising pages. These programs are sold at the US Open and, in turn, the USTA NTC includes the revenues received from the concessionaire for the US Open Program in the rent paid to the City of New York. The Comptroller's finding is incorrect because the complimentary pages are not advertisements; there is no financial or other benefit to the USTA NTC, other than the revenues reported for the US Open Program.

Included in the Comptroller's findings were other de minimis items for beverage and tickets for which USTA NTC concurs with the Comptroller's finding and has remitted payment to Parks in the amount of $8,325.

<u>USTA NTC Recalculation.</u> As a result of the audit review process with the Comptrollers Office, the USTA NTC has concluded it is appropriate to include in Gross Revenues the value-in-kind infrastructure received from the sponsor and other de

minimis items for beverage and tickets. Accordingly, the USTA NTC has remitted payment to the Parks Department in the amount of $39,325."

> ***Auditor's Comment:*** We disagree with NTC's contention that the complimentary pages had no value. As NTC acknowledges in its response, these complimentary pages enhance the program and thereby provide value. Further, USTA received these pages at no cost, while the sponsors paid for similar pages. Had USTA not received the complimentary pages it would have had to pay for the pages at the same rate as the sponsors to enhance the program.

USTA Inappropriately Deducted over $10 Million in Operating Expenses from Gross Revenues

USTA inappropriately deducted $10,011,817 in operating expenses from the Gross Revenues for Calendar Years 2015 through 2017. As a result, NTC underpaid the City by $100,118 in Percentage Rent. Specifically, USTA inappropriately deducted:

- $4,500,688 in catering and set up costs from hospitality revenue;
- $3,833,362 in commissions and advertising expenses paid to vendors from sponsorship revenue for promoting US Opens;
- $1,114,000 in broadcasting commissions and production costs from broadcasting revenue;
- $430,144 in a vendor's credit card fees from commissions of the food sales; and
- $133,623 in cost of goods sold from merchandise revenue.

NTC is not entitled to take any of the deductions noted above from the rent paid to the City according to Section 3.08 of Lease, which states:

> It is the intention of Landlord and Tenant that except as expressly provided, . . . (a) Rental be absolutely net to Landlord without any abatement, diminution, reductions, deduction, counterclaim, setoff or offset whatsoever, so that each Lease Year of the Term shall yield, net to Landlord, all Rental which is payable pursuant to the terms of this Lease to Landlord, and (b) Tenant pay all costs, expenses and charges of every kind relating or allocable to the Premises . . . that may arise or become due or payable during or after . . . the Term.

None of the deductions taken by USTA noted above are among the exceptions "expressly provided" in the Lease that would constitute permissible offsets to be netted against Gross Revenues reported.

Since USTA oversees the sponsorship, broadcasting, catering, hospitality, and merchandise sales operations, the revenues generated from these operations are also all recorded in USTA's general ledger. NTC relies on the information USTA provided when determining the Gross Revenues that should be reported to the City. Due to USTA's inappropriate deductions totaling $10,011,817, NTC underpaid an additional $100,118 in Percentage Rent.

> ***NTC Response*:** "The Draft Audit is applying Section 3.08 of the Lease, however, it does not take into account the other relevant sections of the Lease for the proper and complete analysis. The 2nd Amendment and 4th Amendment Section 3.03(d)(iii) and (iv) Excluded Revenues are applicable:

a. <u>*Section 3.03(d)(iii) of the Lease states:*</u>
'(7) any payments received by Subtenant, licensee or concessionaire that are not passed on to Tenant or Affiliate; provided that any such payments which are received by a Subtenant, licensee or concessionaire which is an Affiliate, shall be included as "Gross Revenues" to the extent provided in Section…
(8) so called "pass-through" made by Subtenants to Tenants for payment of … and other like pass through payments
(11) the value of any product, equipment or supply to Tenant by a sponsor for the primary purpose of supporting or benefiting the sponsor.'

b. <u>*Section 3.03(d)(iv) states*</u>*: 'to facilitate the determination of what constitutes Gross Revenues, Tenants shall insure that all Subleases, concessions and licensee agreements, and all contracts it enters into … provide for fair allocations of Gross Revenues.'*

- The Comptroller's audit finding concludes an audit finding of $4,500,688 in catering and setup costs from hospitality. A substantial portion of the audit findings in the amount of $3,777,958 is for a 'pass-through' amounts to our concessionaire and licensee, which is recognized as Excluded Revenues under the Lease. The concessionaire/licensee in turn provides a payment to the USTA NTC, which payment was included in Gross Revenues and remitted to the City as Rent consistent with Section 3.03(d)(7) above. Effectively, the Comptroller's audit finding is incorrectly concluding that the USTA NTC should duplicate and inflate gross revenues resulting in USTA NTC paying rent twice. The remainder of the audit finding of $722,730 USTA NTC concurs with the audit finding and has remitted payment to the Parks Department in the amount of $7,227.

- The Comptroller's audit findings conclude $3,833,362 in commissions and advertising expenses should be included in Gross Revenues. Approximately $565,423 were from the Tenant procuring advertising in the US Open Program on behalf of the sponsor which is a pass-through payment purely for the benefit of the sponsor as mentioned in Section 3.03(d)(iii)(11) of the Lease as described above and are Excluded Revenues. The remaining balance are commissions deducted from gross revenues that after further review the USTA NTC concurs with the audit finding and has remitted payment to the Parks Department in the amount of $32,679.

- The Comptroller's audit findings include $1,114,000 for additional production costs and commissions for a territory outside of the international broadcast agreement. The USTA NTC contributed $1,000,000 of the $1,114,000, and should be allowed to offset that amount. However, the Comptroller concludes there is not sufficient documentation provided and disallowed the offset. While it is unclear that the offset should be disallowed, the USTA NTC will accept the audit finding and has remitted payment to the Parks Department in the amount of $11,140.

- In regards to the $430,144 audit finding for concessionaire credit card fees, USTA NTC correctly reported revenues from concessions rental in accordance with Section 3.02(d)(ii)(10) of the Lease which allows reportable sales on the basis of 'sales and other criteria', all of which was clearly outlined in the agreement with the concessionaire and reported by USTA NTC. The Comptroller audit findings of

$430,144 incorrectly recalculates the revenues from the concessionaire which is outlined in the agreement with the concessionaire on arriving at commissionable sales inclusive of fees payable to credit cards. Essentially, the Comptroller adds the credit card fees that get paid out of the sales to the credit card vendors as Gross Sales. The Comptroller's audit finding incorrectly recalculates the contractual revenues due to the USTA NTC from the concessionaire. Additionally such amounts were recorded in accordance with GAAP as required by the Lease in arriving at reported revenues, but the Comptroller also failed to consider this in its conclusion.

- The Comptroller concluded $133,623 was incorrectly deducted for cost of goods sold from merchandise revenue. The USTA NTC agrees with the audit finding and subsequently reimbursed the City of NY for this audit finding in the amount of $1,336.

<u>USTA NTC Recalculation</u>. As a result of the audit review process with the Comptroller's Office, the USTA NTC has concluded it is appropriate to include in Gross Revenues the commissions, host telecast fee and value of the cost of goods sold from merchandise revenue of $45,019."

Auditor's Comment: We disagree with NTC's contentions as described below:

- NTC contends, incorrectly, that $3,777,958 of the $4,500,688 should be excluded as "pass-through" amounts. According to Section 3.03(d)(7) of the Lease, excluded revenues are defined as "any payments **received** by a Subtenant, licensee or concessionaire . . . that **are not passed on to Tenant** [emphasis added]." However, the $3,777,958 was hospitality revenue received **by** USTA, not the subtenant, licensee, or concessionaire. These were payments to the concessionaire for services provided during hospitality events. Therefore, these are expenses to USTA that should have been included in Gross Revenues.

- NTC contends, incorrectly, that $565,423 of the $3,833,362 in advertising expenses should be considered as Excluded Revenue under Section 3.03(d)(iii)(11) of the Lease, which states, "the value of any product, equipment or supply **provided to Tenant by a sponsor** [emphasis added] for the primary purpose of supporting or benefiting the sponsor." Since these advertisements were part of the benefit package that USTA agreed to provide **to the sponsors** and were not provided **to USTA by a sponsor**, these amounts should not be treated as Excluded Revenues.

- NTC contends, incorrectly, that $430,144 in credit card fees should be allowed as Excluded Revenues. According to the agreement between USTA and the food and beverage concessionaire, the commission to USTA is calculated based on the total sales generated, which explicitly states credit card fees should not be deducted from the gross receipts when calculating the commission owed to USTA. Since the credit card fees are expenses that USTA agreed to pay, we disallowed such deductions from the Gross Revenues reported to the City.

USTA Did Not Report over $4 Million in Sponsorship Revenue Collected from Sponsors

USTA inappropriately excluded $4,432,801 in sponsorship payments from the Gross Revenues. As a result, NTC underpaid the City by $44,328 during Calendar Years 2014 through 2017. Specifically, USTA excluded $1,275,000 in revenue collected from a sponsor from Calendar Years 2014 through 2016. USTA officials claimed that this revenue was a grant from the sponsor and should be excluded from the Gross Revenues. However, we found no provisions in the sponsorship agreement or the Lease to support this treatment of the sponsor's payment. Thus, an additional $1,275,000 in revenue should have been reported by USTA for the purpose of calculating Percentage Rent.

In addition, we found that USTA underreported $3,157,801 in sponsorship revenue by inappropriately categorizing it as sponsorship revenue allocated to US Open Series (USOS) from Calendar Years 2015 through 2017. USOS is a series of professional tennis tournaments, held prior to the US Open, in various cities in North America.[8] Among the 15 sponsorship agreements that we reviewed, 3 agreements contained provisions for providing support to USOS.

However, USTA did not allocate the USOS sponsorship payments based on the amounts stated in the sponsorship agreements.[9] USTA officials claimed that the actual allocated amounts were based on other factors that are not stated on the sponsorship agreements. However, USTA officials were unable to provide the methodology to show how they determined the amounts that were allocated to USOS. Section 3.03(d)(iv) of the Lease requires that any amounts excluded from the Gross Revenues should be expressly stated in the sponsorship agreements:

> To facilitate the determination of what constitutes Gross Revenues, Tenant shall insure all Subleases, concession and license agreements, and all contracts that it enters into related to . . . sponsorships and advertising revenues, shall, to the extent appropriate, either (A) be structured so that those contracts which generate solely Gross Revenues are separated from other contracts or (B) expressly provide for fair allocations of Gross Revenues and Excluded Revenues.

Based on our comparison of the amounts allocated to USOS with the amounts stated in the three agreements that include support for USOS, we determined that USTA understated $3,157,801 in sponsorship revenue from the USOS events for Calendar Years 2015 through 2017.

> ***NTC Response*****:** "On page 12 of the Draft Audit Report it states that '*Section 3.03(d)(iv) of the Lease requires that any amounts excluded from the Gross Revenues should be expressly stated in the sponsorship agreement.'* This statement does not accurately summarize the language in the Lease, which expressly states '*sponsorships and advertising revenues, shall, to the extent appropriate, either (A) be structured so that those contracts which generate solely Gross Revenues are separated from other contracts or (B) expressly provide for fair allocations of Gross Revenues and Excluded Revenues.*' In regards to the US Open Series, the USTA NTC clearly demonstrated (as shown in the General Ledger and in its certified audited financial statements) it provided a fair allocation of Gross Revenues to the Comptroller's Office. These factors include (i) a $2 million sponsorship fee reduction per year if it is not staged in one sponsorship agreement, (ii) a

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[8] USTA established a separate entity, US Open Series, LLC, to operate and manage television and marketing initiatives for USOS. USTA is a sole member of US Open Series, LLC.

[9] One of the agreements contains an annual allocation schedule. The remaining two sponsorship agreements do not have an explicated amount to be allocated to USOS; however, the agreements each contain a provision that states if a tournament is canceled, the sponsorship fee will be deducted by a stated amount.

valuation placed on title/umbrella presenting sponsor rights and the associated exposure (including direct and indirect expenses for deliverables), (iii) revenue allocation to cover Player Bonus (maximum payout of $3 million) and (iv) player appearance fees to participate in the USOS. The USTA NTC included an allocation in the USTA NTC Consolidated financial statements prepared in accordance with GAAP. The allocation was prepared and shown in accordance with the Lease requirements and should be viewed as fair and appropriate.

Additionally in regard to the $1,275,000 annual contribution received by the sponsor as a donation, the agreement clearly provides consideration paid for the sponsorship benefits separately from the donation that the not-for-profit entity made independent of the sponsorship benefits. This donation is clearly bifurcated in the sponsorship agreement and as mentioned above is appropriately separated in the agreement. Therefore, the $1,275,000 should not be considered as revenues for purposes of Gross Sales."

Auditor's Comment: While the Lease allows certain sponsorship revenues to be excluded, it requires USTA to have contracts "(A) be structured so that those contracts which generate solely Gross Revenues are separated from other contracts or (B) expressly provided for fair allocation of Gross Revenues and Excluded Revenues." However, only one sponsorship agreement expressly provides an allocation of sponsorship revenue to USOS. The other two agreements include only the number of tournaments in which the sponsors participated and the amounts that should be deducted from the sponsorship fees if any of the tournaments are canceled.

The valuations of the title/umbrella presenting sponsor rights and the associated exposure, revenue allocations to cover Player Bonus, and player appearance fees to participate in the USOS are not stated in the sponsorship agreements as the criteria for the allocations. In addition, USTA cannot support its determination of the amounts it allocated to the USOS.

Regarding the $1.275 million that NTC received, these are "annual contributions" that the sponsor is *required* to pay under the terms of its sponsorship agreement—in *addition* to the sponsorship fees. Since the sponsor imposed no restriction on how USTA or NTC could use these contributions, and the sponsorship agreement failed to expressly state that the contributions were "Excluded Revenues," the contributions should have been included in the Gross Revenues reported to the City. Moreover, nothing in the Lease expressly allows NTC, a 501(c)(3) not-for-profit corporation, to exclude such contributions in reporting its Gross Revenues.

NTC Inappropriately Excluded over $5 Million from Gross Revenues from Ticket Surcharges and Other Fees

NTC inappropriately excluded certain Gross Revenues from the calculation of Percentage Rent, totaling $5,415,342 from Calendar Years 2015 through 2017 as a result of it failing to properly account for ticket surcharges, shipping and handling fees, and excluded other miscellaneous revenues.

Specifically, NTC incorrectly recorded ticket surcharges and shipping fees it collected as credits (i.e., deductions of expenses) in two NTC expense accounts; therefore, it underreported Gross Revenues by $4,580,975 from Calendar Years 2015 through 2017.[10]

According to Section 28.02 of the Lease,

> [NTC] shall keep and maintain at an office in New York City complete and accurate books and records of accounts of the operations of the Project Site (including all information relevant to Special Events, such as records relating to the calculation of Event Revenues and Net Event Revenues, and the calculation of Gross Revenues and Percentage Rent, such as records relating to contracts for Broadcasting, sponsorships, advertising, licenses, etc.)

Since ticket surcharges and shipping fees were associated with the ticket sales and hospitality packages for the US Open held at the Tennis Center, they should have been recorded as part of the Gross Revenues in the general ledger and not as expenses.

In addition, NTC did not report revenues collected from a concession and a vending machines provider, film or photo shootings, and other special events, such as graduation ceremonies that were held at the Tennis Center.

As noted above, according to Section 3.03(d)(ii) of the Lease,

> any and all gross rents, receipts, fees, proceeds, property, and amounts of any kind . . . accrued (in accordance with the [Generally Accepted] Accounting Principles) during such Lease Year, . . . from, in connection with, or directly or indirectly arising from, activities occurring at the Project Site and from the operation of the Premises (including, without limitation, conducting Tennis Events).

An NTC official claimed that, based on his "understanding and the definition in the lease agreement," revenues collected from these activities were not required to be reported to the City as part of the Gross Revenues. However, this NTC official did not provide any provisions in the Lease to support his claim. Accordingly, we determined that NTC underreported $834,367 in revenues collected from concession and vending machines providers, film or photo shoots, and other special events for Calendar Years 2015 through 2017.

> ***NTC Response***: "The USTA NTC concurs with the Draft Audits inclusion in Gross Revenues, at page 12, of the $5,415,342 and has accordingly paid $54,153 as additional rent to the City of New York prior to the issuance of the Draft Audit."

NTC Overreported $256,426 in Online Sales and Media Revenue to the City

NTC overreported $256,426 in Gross Revenues to the City during Calendar Years 2015 and 2016. Thus, NTC over-paid $2,564 in Percentage Rent. Of the $256,426 overreported Gross Revenues, $236,426 was online merchandise sales in Calendar Years 2015 and 2016. NTC reported the same revenue in two revenue categories on the Percentage Rent Reports submitted to the City.

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[10] Of the $4,580,975 cited, we did not include the handling fees remitted by NTC's ticketing vendor in Calendar Year 2017 because NTC was unable to provide documentation to show the amount that was remitted and whether it reported these fees to the City as part of the Gross Revenues. Based on the prior years' information, we estimated the handling fees were approximately $1.8 million.

Specifically, the same amount was reported under "FMI License & Third Party Vendor Rentals" and again under "Digital Strategy and Partnerships."

"FMI License & Third Party Vendor Rentals" is the revenue category associated with commissions and rental payments received from vendors selling merchandise to the public during the US Open while "Digital Strategy and Partnerships" includes revenue received from sponsors that are attributed to Internet promotions. When we inquired about the amounts being reported under both revenue categories, NTC stated, "This was an error in the NYC Leasehold fee schedule. . . . . We accidentally reported and paid on e-commerce twice." The errors occurred in 2015 and 2016 causing $236,426 in over-reported Gross Revenues to the City.

Additionally, a "last minute" revenue reduction adjustment of $20,000 was not reflected in the Percentage Rent Report for Calendar Year 2016. When we inquired about the difference, NTC stated, "There was a last minute journal entry posted . . . that represented an adjustment made . . . in the amount of $20,000 reducing the [general ledger] account balance." The adjustment entry was posted to bring the estimated accrued revenue amount to the actual amount received from a social media company. However, this adjustment was excluded when NTC prepared the Percentage Rent Report to the City. As a result, NTC overreported an additional $20,000 to the City.

> ***NTC Response*:** "The USTA NTC concurs with the Draft Audits NTC over -reported, at page 13, $256,426 in Gross Revenues to the City during Calendar Years 2015 and 2016. Thus, the NTC over-paid $2,564 in Percentage Rent and has taken a credit to the additional rent paid to the City of New York as part of the remittance of agreed to audit findings in the Draft Audit."

Over $8 Million of Revenue Discrepancies Found Between USTA Financial Statements and Percentage Rent Reports Submitted to the City

Our comparison of the USTA's certified consolidated financial statements and NTC's Percentage Rent Reports submitted to Parks found that revenues reported in the certified financial statements did not match the Gross Revenues reported to the City.[11] Specifically, USTA's certified financial statements reported more than $8.2 million in the Tennis Center revenues compared to the Gross Revenues reported to the City during Calendar Years 2015, 2016, and 2017. We determined that NTC may owe up to $82,310 in additional Percentage Rent. See Table III below:

[11] We did not compare the Percentage Rental Reports submitted to Parks to NTC's certified financial statements because NTC only recorded a portion of the revenue generated from the Tennis Center, while USTA provided consolidated financial statements that included NTC's revenue.

Table III

Gross Revenue Variances between
USTA Certified Financial Statements
and NTC Percentage Rent Reports
Submitted to the City

Calendar Year	Revenues (in Thousands)				
	Reported in USTA Financial Statements			Reported to the City (D)	Variances (E) = (C)-(D)
	US Open (A)	NTC Tennis Facility Program (B)	Total (C) = (A)+(B)		
2015	$298,106	$3,835	$301,941[ǂ]	$300,818	$1,123
2016	$307,209	$3,737	$310,946	$309,214*	$1,732
2017	$347,593	$4,395	$351,988	$346,612[^]	$5,376
Total	**$952,908**	**$11,967**	**$964,875**	**$956,644**	**$8,231**

ǂ The 2015 financial statements did not include $3.6 million of in-kind benefits received.
* Included $1.2 million of in-kind benefits that was reported to the City retroactively in Calendar Year 2017.
^ Excluded $2.4 million of prior period's in-kind benefits that were reported in Calendar Year 2017.

Our assessment of the $31 million in underreported Gross Revenues discussed above was based on the available records provided by NTC and USTA. Since we did not have complete unrestricted access to USTA's books and records, we were unable to determine with reasonable certainty how much of the US Open revenue was received by USTA and its affiliates, and if any portion of the $8.2 million difference between the amount of US Open revenue reported in USTA's certified financial statements and the Gross Revenues reported to Parks might have already been included in the $31 million underreported Gross Revenues discussed above. However, the discrepancies between (1) the US Open revenues and the Tennis Center program revenues reported on USTA's certified financial statements, and (2) the Gross Revenues reported to the City, reflect that Gross Revenues were consistently underreported to the City.

According to Section 3.03(c) of the Lease, NTC is required to make an annual adjustment of the Percentage Rent payment if it underpays the City. In addition, if the underpayment exceeds five percent of the Percentage Rent, NTC is required to pay interest at 9.5 percent per annum. However, NTC failed to make that annual adjustment as required by the Lease.

> ***NTC Response***: "The USTA NTC audited financial statements and general ledger were provided to the comptroller audit team at the onset of the audit. This finding was brought to the attention of USTA NTC in the final stages of wrapping up the audit, not allowing the USTA NTC sufficient time to review the auditor's analysis and/or to respond. The USTA NTC will review this conclusion with the Parks Department to reconcile any difference that may exist."

> ***Auditor's Comment:*** We brought this issue to the attention of NTC/USTA on May 1, 2019. NTC/USTA officials had over three months to review the issue, which concerns variances between *its own* financial reports.

NTC Did Not Consistently Submit Annual Certified Financial Statements to Parks

NTC did not submit its certified financial statements to Parks within 90 days after the Calendar Years 2016 and 2017 ended, as required by the Lease. According Section 28.01(b) of the Lease,

> as soon as practicable after the end of each calendar year during the Term and, in any event, within ninety (90) days thereafter, financial statements of Tenant and of the operations of the Project Site (including, without limitation, balance sheets, income statements and funds statements showing changes in financial positions) and setting forth, in accordance with Accounting Principles, in comparative form, the corresponding figures for the previous calendar year, all in reasonable detail and examined and reported upon in accordance with generally accepted audit standards by a Certified Public Accountant, together with the notes and report thereon to Tenant.

Instead of submitting the 2016 and 2017 certified financial statements to Parks, NTC only submitted a cumulative year-ended Percentage Rent Report that is not audited by a Certified Public Accountant. Certified financial statements provide reasonable assurance that the financial information are fairly presented and free of material misstatements.

> ***NTC Response:*** "The USTA NTC will revisit the process of providing its certified financial statements to the Parks Department. The USTA NTC publishes its financial statements on its website, and it is available for the public and the Parks Department to review. USTA NTC will work with the Parks Department to have a more formal process in place for submission of financial statements."

Other Issues

NTC Was Unable to Provide Documentation to Substantiate That Certain Companies Maintained the Required Insurance Coverage

NTC did not ensure sponsors, broadcasters, and vendors maintained the required insurance coverage as required by their agreements with USTA. Although all of 15 sponsorship agreements that we reviewed required each sponsor to maintain certain insurance coverage during the 2016 US Open, USTA was unable to provide supporting documentation such as insurance certificates, that reflected that two sponsors had obtained the requisite insurance coverage. In addition, we found that two sponsors did not maintain all of the required insurance coverage per the sponsorship agreements. Specifically, one sponsor did not maintain $1,000,000 in automobile coverage as required and another sponsor did not maintain $1,000,000 in media professional liability as required by agreement.

Similarly, USTA was unable to provide the insurance certificates for four broadcasting companies and two vendors that required insurance coverage.

Although the Lease does not have a mandated requirement that NTC's or USTA's sponsors, broadcasters, and vendors maintain specific insurance coverage, NTC should ensure the self-imposed insurance requirements were fulfilled as part of its obligation to properly manage the Tennis Center under the Lease. Insurance requirements are in place as a control to ensure USTA, NTC, the City, and all other related parties are sufficiently protected against any claims or potential claims that may arise in connection with the operation of the Tennis Center. Due to lack of oversight, USTA failed to mitigate the risk of potential damages and legal actions which may occur during the US Open.

> ***NTC Response:*** **"**This comment appears to be outside the purpose of the Draft Audit, which is to review the USTA NTC's compliance with the rent provisions of the Lease. We do, however, point out that the USTA NTC does comply with all of the insurance obligations under the Lease as was noted in the Draft Audit on page 2. The USTA NTC takes great precaution in all of its agreements and, as a standard practice, requires insurance coverage from its sponsors and vendors, even though this is not mandated by the Lease. The USTA NTC also, as a standard practice, includes an indemnification obligation in each of its sponsor/vendor agreements. Having said that, the Draft Audit comment is outside of the purpose of this audit. Accordingly, we do not understand the inclusion of this comment in the Draft Audit, especially since the Draft Audit recognizes the USTA NTC complies with the insurance obligations."

> ***Auditor's Comment:*** As a Tenant of the premises, NTC has the fiduciary duty to properly manage the property. By not ensuring that its sponsors, broadcasters, and vendors complied with the insurance requirements outlined in their respective contracts, NTC places itself and the City at unnecessary risk for liability.

Parks Is Unable to Properly Monitor the Financial Terms in the Lease

Parks is unable to provide adequate oversight over the financial terms of the Lease. According the Parks officials, they do not have enough resources to conduct audits of large entities such as the Tennis Center; therefore, they can only verify the mathematical accuracy of the financial reports that NTC submitted. In addition, we found that certain terms in the Lease hinder Parks' ability to properly oversee NTC's compliance of the financial terms of Lease. For example,

- Section 28.01(b) of the Lease requires NTC to submit certified financial statements of "the Tenant and of the operations of the Project Site" to the City within 90 days after the end of each calendar year. However, since NTC (*i.e.*, the Tenant) records only a portion of the Tennis Center's operations in its general ledger, its financial statements do not reflect the actual financial position of the Tennis Center's operation. For instance, NTC's 2016 financial statements only showed $74 million in operating revenues while the "2016 Percentage Rent Report" that NTC submitted to Parks showed $308 million in Gross Revenues. The majority of the revenues generated from the US Open is reported on USTA's financial statements, not NTC's. Therefore, Parks is unable to analyze or verify the completeness of US Open's revenues. The incomplete financial information prohibits the City from determining whether all revenues were accurately reported without conducting a full scale audit.

  If the Lease explicitly required NTC to record all revenues generated from the Tennis Center in its general ledger, or if NTC were required to submit the certified financial statements of USTA with a detail breakdown of the Tennis Center's operations, Parks would have a more transparent view of the Tennis Center's operations and would be in a better position to evaluate NTC's compliance with the Lease terms. This would improve Parks' ability to determine whether the Gross Revenues reported by NTC are reasonable, and would help to minimize or even eliminate the discrepancies noted in Table III on page 11 of this report.

Since NTC is not required to submit USTA's certified financial statements under the Lease, Parks lacks necessary data with which to perform any useful analysis. In addition, since most of the findings cited in this report are related to how USTA reported the US Open revenues in its general ledger, it is essential for the City to have complete financial information of the Tennis Center operations to fully evaluate Lease compliance.

- Section 28.03(a) of the Lease imposes restrictions on copying books and records that are relating to the operations of the Tennis Center. Specifically, the Lease states,

  > Landlord and Landlord's agents and representative shall not, without Tenant's prior written consent, be permitted to duplicate, or otherwise remove from the possession of Tenant, any books, records or any other papers or files inspected by any of the foregoing.

  The imposed restrictions affect the ability to conduct a meaningful review of NTC's books and records during an audit because, when NTC refuses to give the City permission to make copies as it has done in the case of this audit, City officials need to take notes or summarize the information that is necessary for the review which limits the ability to most effectively and efficiently engage in analysis and oversight. In addition, due to NTC's unwillingness to provide books and records in electronic format, the City is further hindered in its efforts to effectively oversee the Tennis Center's operations. For example, during our audit, since all of the documents NTC and USTA provided were hardcopies, the auditors needed to manually input financial information into Excel spreadsheets and summarize the relevant contract terms before the auditors started their analyses. As a result, NTC made the analyses of NTC's and USTA's financial data more difficult to conduct and needlessly prolonged the audit process.

- Section 3.03(c) of the Lease only allows the City to impose late charges on delinquent Percentage Rent when the underpayment exceeds 5 percent and 10 days after the demand due date. Since Parks does not receive sufficient information to enable it to properly monitor the accuracy of the Percentage Rent calculation, Parks will not be able to determine when and if such an underpayment occurs. As a result, Parks will not be able to impose any late charge.

- Section 2.02(a) of the Lease states that the Lease is automatically renewed after the initial Lease term. This provision restricts the City's negotiating leverage to execute fair and equitable terms with NTC in the future.

Allowing NTC to Deduct Parking Lot Payments as Credits Reduced the Percentage Rent Paid to the City by up to $1,584,000 over 10 Years

Parks agreed to amend the Lease in 2010 to allow NTC to deduct parking payments to HOS as direct credits against Percentage Rent due, instead of a deduction of the Gross Revenue. In doing so, the City has forgone up to $1,584,000 in Percentage Rent from Calendar Years 2009 through 2018.[12] Under the third amendment of the Lease, the City allowed NTC to deduct up to $180,000 a year for parking fees that NTC pays to HOS for the use of HOS's parking lots during the US Open. That amendment states, in part:

[12] The HOS parking lot has approximately 90 parking spaces and it was capable to generate approximately $50,000 ($23 per space x 90 spaces x 24 sessions = $49,680) during the US Open.

> If and to the extent Tenant is obligated or required at any time to make payments to the Hall of Science of the City of New York, Inc. ("HOS") for use of the HOS's parking areas for vehicular parking during the US Open, and Tenant obtain Landlord's prior approval to make such payments, then Landlord shall reimburse Tenant for such payments by allowing Tenant to credit such payments against Rental due under the Lease, up to the amount of such payments actually made by Tenant to HOS and in no event in excess of payment amounts approved by Landlord. Subject to the provisions of this Section 23.04(e), for Lease Years 2009 through 2018, Landlord hereby acknowledges that the payment amounts set forth in the following schedule have been approved by Landlord:
>
> | Lease Year | Amount Not to Exceed |
> |---|---|
> | 2009 | $140,000 |
> | 2010 | $140,000 |
> | 2011 | $150,000 |
> | 2012 | $150,000 |
> | 2013 | $160,000 |
> | 2014 | $160,000 |
> | 2015 | $170,000 |
> | 2016 | $170,000 |
> | 2017 | $180,000 |
> | 2018 | $180,000 |

However, since the City was not obligated to reimburse NTC for any payments made to HOS for the use of the parking areas in the original Lease, as shown below, the amended terms were not beneficial to the City. The original Lease provides that

> [p]arking at the Hall of Science is subject to an existing agreement between Hall of Science of the City of New York Inc. and Tenant, and Tenant may be required to pay a separate fee for the use of the Hall of Science parking area for Tennis Event parking, pursuant to such agreement.

Specifically, the HOS parking lot has approximately 90 parking spaces and it was capable to generate approximately $50,000 during the US Open.

Further, this amendment also contradicts Section 3.08 of the Lease which states,

> It is the intention of Landlord and Tenant that except as expressly provided, . . . (a) Rental be absolutely net to Landlord without any abatement, diminution, reductions, deduction, counterclaim, setoff or offset whatsoever, so that each Lease Year of the Term shall yield, net to Landlord, all Rental which is payable pursuant to the terms of this Lease to Landlord, and (b) Tenant pay all costs, expenses and charges of every kind relating or allocable to the Premises . . . that may arise or become due or payable during or after . . . the Term.

When we asked Parks officials for the basis of its decision to allow NTC to deduct the parking payments as a credit against the Percentage Rent due, Parks officials were unable to provide any rationale for its agreeing to this amendment to the Lease in 2010.

Without the rationale, we were unable to determine the justifications for modifying the lease terms, which appears not to be in the best interest of the City.

NTC Response: "Under the Lease, the Parks Department was required to provide a certain number of parking spaces for use by the USTA NTC. When the Parks Department could not comply with the Lease obligation, the Parks Department agreed to remedy the issue by providing to USTA NTC the parking spaces at the Hall of Science ('HOS'). In this arm-length agreement, the Parks Department requested the USTA NTC to pay the amounts due to the HOS on behalf of the Parks Department and to deduct said amounts from rents payable to the Parks Department. The transaction allowed the Parks Department to comply with its Lease obligations to provide parking to the USTA NTC. The terms of the arrangement is set forth in the Fourth Amendment to the Lease."

Auditor's Comment: NTC did not provide evidence on how the City ostensibly falls short in providing the required amount of parking spaces for the US Open. It should be noted that the City provides *thousands* of parking spaces to the patrons attending the US Open in several parking areas, including parking lots around the Tennis Center and the nearby baseball stadium. The HOS parking lot provides only approximately 90 spaces, the majority of which were assigned by the NTC/USTA to their sponsors. Therefore, the City should not bear the cost of the parking arrangement between HOS and NTC while NTC/USTA is the ultimate beneficiary.

RECOMMENDATIONS

We recommend that NTC should:

1. Remit $311,202 in additional Percentage Rent due to Parks;

   NTC Response: "USTA NTC concurs with $143,297 of the Audit Finding and has remitted payment to the Parks Department."

   Auditor's Comment: We are pleased that NTC remitted $143,297; however, as outlined in our audit finding, NTC is responsible for remitting $311,202, and we urge NTC to remit the remaining balance of $167,905 due to the City.

2. Determine, with Parks, how much of the $82,310 should be remitted to the City as Percentage Rent;

   NTC Response: "USTA NTC will review this conclusion with the Parks Department to reconcile any differences. USTA NTC will review the disputed audit findings with Parks and come to a resolution."

3. Ensure all Gross Revenues are accurately reported to Parks in accordance with the terms of the Lease by:

   a. Accurately accounting for all in-kind benefits received from the sponsors, broadcasting companies, and vendors;

   b. Reviewing the Gross Revenues information provided by USTA to ensure there are no inappropriate exclusion or deductions from the Gross Revenues;

   c. Including all fees collected from the activities that occurred at the Tennis Center;

   d. Accurately recording Gross Revenues in its general ledger; and

   e. Making an annual adjustment, when necessary, to the Gross Revenues reported to the City.

   NTC Response: "USTA NTC has made and will continue to report Gross Revenues accurately in accordance with the terms of the Lease. Prospectively management will ensure that any agreed to audit findings will also be reported."

4. Submit the certified financial statements to the City within the 90 days after the end of each Calendar Year; and

   NTC Response: "USTA NTC will put a formal process in place with the Parks Department for delivery and receipt of financial statements."

5. Ensure all sponsors, broadcasters, and vendors maintain the required insurance coverage.

   NTC Response: "This is outside the scope of the audit, USTA NTC maintained appropriate insurance coverage as required by the Lease."

   Auditor's Comment: NTC should take this opportunity to review and require all sponsors, broadcasters, and vendors to maintain the required insurance, naming the City, the landlord of the premises, as additional insured, which is in the City's best interest and that of NTC to ensure the City is protected from unnecessary risk and liability. We urge the USTA to ensure that all sponsors, broadcasters, and vendors maintain the required insurance coverage.

Parks should:

6. Recoup $311,202 in additional Percentage Rent from NTC;

   Parks Response: "Parks is working with NTC to address the substance of this finding. NTC has acknowledged that there was unintentionally underreporting of Gross Revenues in the amount of $14,329,661, meaning that the additional Percentage Rent amount owed to the City is $143,296.61. Parks has received that amount from NTC. The remaining portion of Percentage Rent, $167,905.39, that the Report contends is owed to the City is disputed by NTC. For those areas that remain in dispute, Parks will review the relevant records and contracts related to the disputed amounts in order to determine if any additional Percentage Rent is due."

   Auditor's Comment: Based on our detailed analysis and review of the documents provided, we have concluded that NTC owes additional Percentage Rent of $311,202. NTC remitted $143,297 of $311,202 in additional Percentage Rent, and we urge Parks to collect the remaining balance of $167,905 due to the City.

7. Ensure NTC submit the certified financial statements annually to Parks;

   Parks Response: "Parks will work with NTC to ensure that their certified financial statements are annually submitted to Parks, in addition to all of the quarterly financial reports that are routinely received and analyzed."

8. Review NTC's books and records for the years that were not covered in our scope period and determine whether NTC owes any additional Percentage Rent;

   Parks Response: "Parks will consider where we can perform targeted reviews of NTCs income. However, we must first focus our attention on reviewing the monetary findings raised by this Report, in order to resolve any disputes and ensure that the City recoups any fees that are owed."

9. Conduct periodic reviews of NTC's compliance of the terms of the Lease;

   Parks Response: "Parks will consider where we can perform targeted reviews of NTCs compliance, where appropriate."

10. Consider seeking revision of the terms of the Lease including, but not limited to:

    a. Requiring NTC to submit annual certified financial statements for the entire operation of the Tennis Center or requiring all revenues generated from the Tennis Center be recorded in NTC's general ledger;

    b. Allowing the City to copy all books and records relating to the Tennis Center's operation;

    c. Requiring NTC to provide electronic copies of the books and records when requested;

    d. Imposing late charges when the payments become overdue, not when underpayment exceeds five percent and 10 days after the demanded due date; and

    e. Discontinue automatic renewal of the Lease;

f. Cease providing parking credits to NTC after the expiration of the current credits. If Parks finds it is necessary to provide support to NTC for the parking payments, the payments should be deducted from the Gross Revenues, and

Parks Response: "While we will take these recommendations under advisement during any future lease negotiations, it must be emphasized that Parks cannot unilaterally revise the terms of the existing lease. Any amendment to the lease would need to be the product of good faith negotiations between the City and NTC, and would require the approval of the Citys Corporation Counsel. Moreover, it does not appear likely that NTC would agree to the Reports suggested amendments and certainly not without other concessions from the City in exchange for such revisions."

11. Consider the financial impact to the City before amending any financial terms in the Lease with NTC.

Parks Response: "Financial impact to the City is always a critical consideration during any negotiation and Parks strongly disputes any insinuation that this was not the case in our prior negotiations with NTC. We do not see any evidence in the Report to support a finding that financial impact is not considered, other than a matter raised concerning the deduction of parking payments to the Hall of Science. As communicated during the audit, the City is required under the original lease to provide parking and the provisions of the relevant amendments were a product of good faith negotiations between the City and NTC, which was approved as to form by the Corporation Counsel."

Auditor's Comment: The original Lease had no provision that the City was obligated to pay for NTC's use of the HOS parking lot, and Parks did not provide the reason as to why Parks amended the terms of the Lease. We reiterate that, in the future, if Parks decides to consider the cost NTC pays to HOS, the payments should be deducted from the Gross Revenues, instead of the Percentage Rent due to the City.

DETAILED SCOPE AND METHODOLOGY

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained during the audit provides a reasonable basis for our findings and conclusions except insofar as certain restrictions were imposed upon us by the Lease and USTA/NTC.

NTC's Lease to operate the Tennis Center contains language in Section 28.03 (a)(i) that states,

> Landlord, the Comptroller of the City . . . and/or Landlord's agents or representatives shall have the right from time to time during regular business hours, upon reasonable advance notice, to inspect and audit all of Tenant's books and records and all other papers and files of Tenant, . . . and such other papers and files as are materially relevant to Tenant's obligations under this Lease.

USTA/NTC limited our access and ability to review financial information that are relevant to the Tennis Center's operation. Specifically, USTA only provided records that it represented were responsive to our requests based on its judgment as to which records were relevant to the operations of the Tennis Center. For example, USTA did not provide certain accounts for our review and refused to provide contact information of a vendor. Without full access to the financial records, our ability to determine whether all revenues generated from the Tennis Center were reported to the City was impeded.

This audit was conducted in accordance with the audit responsibilities of the City Comptroller as set forth in Chapter 5, §93, of the New York City Charter.

The scope of this audit was Calendar Years 2015 through 2017. However, during the course of the audit, we found that USTA underreported certain sponsorship revenue in Calendar Year 2014, which was included in the underreported revenue reported in this report.

To gain a general understanding of NTC's responsibilities, we reviewed the Lease and the four subsequent amendments between the City and NTC. To obtain an understanding of USTA's involvement at the US Open operation, we reviewed the US Open agreement between NTC and USTA. We also interviewed various NTC and USTA officials who are responsible for US Opens' ticket sales, sponsorship and advertising arrangements, broadcasting, restaurant operations, merchandise sales, and hospitality services. To obtain an understanding of the court rentals and tennis program operation, we interviewed NTC's Director of Finance and Administration and the Senior Business Manager for the tennis programs. To obtain an understanding of the revenue reporting process, we interviewed NTC's Senior Accountant, NTC's Director of Finance and Administration, USTA's Chief Revenue Officer, and USTA's Senior Director of Finance. We documented our understanding of NTC's and USTA's operations in various memoranda.

To determine whether NTC accurately report its Gross Revenues to the City, we reviewed and analyzed NTC's general ledger, financial statements, and federal tax forms 990–*Return of Organization Exempt from Income Tax* and compared amounts to the Gross Revenues stated on Percentage Rent Report submitted to the City. Since revenues generated from sponsorship and advertising, broadcasting rights, food and merchandise sales, hospitality, in-kind benefits, and certain miscellaneous US Open revenues were recorded in USTA's general ledger, we also obtained the general ledger accounts that were relevant to those revenue streams for our review.

To determine whether NTC accurately recorded US Open ticket revenue in its general ledger, we analyzed the Daily Box Office ticket sales at the Tennis Center during the 2016 US Open period and judgmentally selected the highest gross sales week (August 29, 2016 to September 4, 2016) to be our sample. We then obtained the supporting documentation for the Box Office ticket sales, such as, daily income reports, sales journals, close out reports, credit card reports, and deposit slips, and traced the Box Office ticket revenue from the supporting documentation to the bank statements, which recorded both online and Box Office ticket sales. We additionally traced the monthly sales amounts from the ticket sales worksheet as well as ticket sales related to luxury suites to NTC's general ledger. Finally, we matched luxury suite sales with the terms of the sponsorship contracts to ensure accuracy.

To determine whether NTC accurately reported other US Open revenue to the City, we conducted an unannounced observation on August 25, 2017. Based on our observations, we identified the sponsors, broadcasters, and other sources of income, such as food and merchandise sales.[13] We then compared the sponsors that we observed to the sponsorship list provided by USTA. To determine whether USTA accurately recorded sponsorship revenue, we judgmentally selected and reviewed a sample of 15 out of 33 sponsorship contracts.[14] Based on our review, we identified the sponsorship payments, in-kind benefits, and other obligations, such as insurance requirements, from each contract. We then traced the sponsorship revenue from the contract to a spreadsheet that USTA used to record the gross sponsorship revenue and adjustments to the gross sponsorship revenue. For all the sponsorship revenue adjustments, we obtained and reviewed the supporting documentation to determine whether the adjustments were reasonable and appropriate. We also traced all the sponsorship revenue from the spreadsheet to USTA's general ledger to determine whether USTA accurately reported the sponsorship revenue in its general ledger. For the in-kind products and services provided by the sponsors, we compared the in-kind benefits described in the sponsorship contracts with the list of in-kind benefits that NTC reported to the City. In addition, we determined whether the reported values were reasonable.

To determine whether NTC accurately reported broadcasting revenue to the City, we compared the broadcasters' signs that we observed during our observation to the list of broadcasting companies that NTC provided. We then judgmentally selected 5 of 19 broadcasting rights contracts for our review.[15] Based on our review, we identified the broadcasting fee, in-kind benefits, and other obligations, such as insurance requirements, from each contract. In addition to the sampled broadcasting rights contracts, we also reviewed the contract between USTA and a media company that handled the licensing of certain international broadcasting rights and collected those international broadcasting fees on behalf of USTA and the contract with a media service vendor that provided exclusive cloud based asset management for storing, retrieving, managing, and delivering video footage for the US Open. We traced the fee payments to USTA's general ledger and reviewed the relevant supporting documentation. We also compared the in-kind benefits required to be provided by the agreements to the amounts reported to the City and determined whether the reported values were reasonable. Since USTA did not provide sufficient documentation to support the allocation of in-kind media services received from Company A, we used the limited information provided for Calendar Year 2017 associated with the number of commercials aired prior to and during the US Open and the value of certain pre-defined commercial slots with the stated amount in the contract to determine the portion of the in-kind

[13] Sponsors, broadcasting companies, and concessionaires generally sign multiple-year contracts with USTA.
[14] Our samples contain 10 sponsors with the highest sponsorship payments and 5 sponsors with the lowest sponsorship payments, which represented 80 percent of the recorded gross sponsorship revenue.
[15] Our samples include a domestic broadcasting contract and four of the highest revenue international broadcasting contracts, which represented 87 percent of the recorded gross broadcasting revenue.

benefit to be reported to the City. We then applied the same methodology to estimate the underreported in-kind benefits for the Calendar Years 2015 and 2016.

To determine whether NTC accurately reported hospitality revenue, we first analyzed the hospitality space rental, suite sales, USTA member packages and tickets, such as complimentary tickets, distributed to various internal departments. We then summarized the Archtics reports[16] for hospitality space rental and suite sales, and randomly selected 44 companies as our samples.[17] In addition to our random sample selection, we also judgmentally selected six companies that we identified as outliers (i.e., per suite session payments were substantially lower than the average suite payment for the similar suite sessions) to be part of our sample. We obtained and reviewed the hospitality agreements, invoices, and payments. We then verified whether the corresponding invoices and payments were accurate and in accordance with the hospitality agreement.

To determine whether NTC properly reported the commissions received from concessionaires for food and merchandise sales, we reviewed the operating agreements between the concessionaires and USTA. Based on our review, we determined how the commissions due USTA should be calculated and identified other payment obligations that were stated in each operating agreements. We then reviewed the sales report submitted by the concessionaires to determine whether the concessionaires correctly calculated the commissions per the agreements with USTA. We then traced the commissions from the sales reports with the amounts reported on USTA's general ledger.

To determine whether NTC accurately reported other miscellaneous revenues to the City, we judgmentally selected May 2016 to be our sample.[18] We reviewed and analyzed the general ledger analysis reports and compared it to the amount reported to the City. We then selected all transactions for the month of May to verify completeness and accuracy. We obtained various supporting documentation and traced the revenues collected from the supporting documentation to the general ledger.

The results of the above tests, while not statistically projectable to their respective populations, provided a reasonable basis for us to assess and to support our findings and conclusions about NTC's compliance of the financial terms and certain non-revenue terms of the Lease.

[16] NTC and USTA utilize the Archtics system to record the sales of various ticket plans, tickets issued to the sponsors and broadcasting companies, complimentary tickets, suite sales, and hospitality space rental.
[17] Twenty of 107 companies were selected for the hospitality space rental and 24 companies were selected for the suite sales (20 for individual suite sales and 4 for individual Supersuite seat sales).
[18] Miscellaneous revenues include court rental, tennis program fees, school trips revenue, summer camp fees, and special event revenue.

BILLIE JEAN KING
NATIONAL TENNIS CENTER

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August 15, 2019

Marjorie Landa
Deputy Comptroller
The City of New York Office of the Comptroller Executive Offices
1 Centre Street
New York, NY 10007-2341

Dear Deputy Comptroller Landa:

Enclosed with this letter is the response by USTA National Tennis Center Incorporated ("USTA NTC") to the Comptroller's August 1, 2019 Draft Audit Report on the Compliance of The USTA National Tennis Center, Inc., with its New York City Lease (the "Draft Audit")1. The USTA NTC received from the Comptroller the Draft Audit on August 2, 2019, following the June 6, 2019 exit conference with the Comptroller's Office.

In 2001, the Comptroller's Office issued a joint release with the USTA recognizing that the US Open generated more in direct revenue to the City of New York and tristate area than any other annual sports or entertainment event in any city in the United States. Since that time, the US Open has continued to have a highly beneficial financial impact. Over 8 years ago in 2011, AKRF conducted a study which found that the US Open provided an economic impact of over $900 million annually to New York State, and over $750 million annually to the City of New York, numbers which have continued to grow since that point in time. When the USTA NTC was notified of this audit in October of 2017, it welcomed the opportunity to demonstrate the benefits of the revenue flowing directly to the City of New York, which we are extremely proud to call the home of the USTA Billie Jean King National Tennis Center ("NTC") and the US Open. By way of example, in the last 25 years US Open revenue has grown by approximately 936%, and in turn, rent paid to the City of New York by the USTA NTC has increased from $320,000 in 1994 to $3.45 million in 2018 - a $3.1 million annual increase in rent of over 1,078%.

Over the last two years since this audit was initiated, USTA NTC has engaged in a professional, courteous and detailed exchange with the Comptroller's Office and we sincerely appreciate the time and effort devoted to this audit by the Comptroller's staff.

[1] The United States Tennis Association Incorporated, a 501(c)(6) tax exempt organization ("USTA), is the sole member of USTA National Tennis Center Incorporated, a 501(c)(3) tax exempt organization ("USTA NTC"). In 1993, the USTA NTC entered into a 99-year lease with the City of New York to construct, renovate, maintain and operate the USTA National Tennis Center in Flushing Meadows-Corona Park.

USTA NTC is committed to transparency and compliance with the letter and spirit of the USTA NTC Lease. In fact, as noted by the Comptroller, USTA NTC made timely payments of Base Rent and Percentage Rent, has maintained the required property and liability insurance, and paid water and sewer charges (Draft Audit, p2).

Despite this important finding, and despite the narrowing of certain differences between our organizations on select issues, there nonetheless remain areas of non-alignment between USTA NTC and the Comptroller's Office. Although USTA NTC disagrees with certain Draft Audit findings, which are significant in a number of respects, we view those differences as ones between reasonable partners in a remarkably successful and mutually beneficial joint venture, starting from the inception of the USTA NTC in Flushing Meadows – Corona Park (the "Park") in August 1978.

At that time, USTA NTC and the City of New York embarked on an extraordinary, long-term journey that has defied the well-known trends of tax breaks, concessions and the use of municipalities as bargaining chips to select the city a sports entity calls "home." Over four decades from its opening, the NTC remains one of, if not "the," greatest and most unique venues in the country. In addition to hosting US Open (the world's largest annually attended sporting event), the NTC serves as one of the world's largest public tennis facilities, open to the public 11 months of the year. The NTC also represents a rare example of a world-class sports venue that pays over $3.45 million in municipal rent each year despite the fact that it was constructed without the use of any taxpayer money, a win-win for USTA NTC and the people of New York City.

Over the years, USTA NTC has invested over $1.2 billion in the NTC facility. In 1997 USTA NTC opened the Arthur Ashe Stadium, the crown jewel of the NTC and a stadium that has played host to some of the greatest tennis matches of all time, each seen in person by 23,000+ spectators and viewed by worldwide television audiences that have exceeded tens of millions of people. In fact, the opening shot in many broadcasts of the US Open is a picture of the Unisphere – the perfect picture postcard welcoming fans from around the world to New York City, Queens, and Park. In 2014, the USTA NTC embarked on a Strategic Transformation of the facility, self-funding, through debt and operating funds, of over $660 million dollars in order to ensure that the US Open remains a world-class, preeminent sporting event and that the venue maintains its stature as a world-class tennis venue. No City money has been required or requested. Our approach to stadium construction was so unique that Mayor Bloomberg acknowledged in 2002 that it was "the only good athletic sports stadium deal, not just in New York, but in the country." The same has been true of the USTA NTC's approach to the balance of the facility, including the Strategic Vision and the 34 public tennis courts now in use at the NTC. In addition to the substantial investments made by USTA NTC to the NTC facilities, and the rent payments noted above, in 2013 USTA NTC committed to pay over $10 million dollars as a good will gesture to fund improvements to and maintenance of the Park for decades to come and also provides and maintains 12 tennis courts for Parks outside the NTC property without cost to NYC for the benefit of those who use the Park.

We are confident that our commitment to this City is also reflected in the considered analysis we conducted in connection with the Comptroller's Draft Audit. Our position is outlined in the attached USTA National Tennis Center's Principal Corrections and Concurring Responses. We thank you in advance for your review.

Sincerely,

USTA National Tennis Center, Incorporated
Gordon Smith
Chief Executive Officer & Executive Director, USTA
Vice President, USTA NTC

Attachment

cc: Scott M. Stringer, Jr.; Comptroller
The City of New York, Office of the Comptroller;
Amy Man; Audit Manager,
The City of New York, Office of the Comptroller;
Mitchell J. Silver; Commissioner
New York City Department of Parks & Recreation;
Phil Abramson, Revenue Communications Director
New York City Department of Parks & Recreation;
Alessandro Olivieri, General Counsel/Records Access Appeals Officer
New York City Department of Parks & Recreation;
David Cerron, Assistant Commissioner for Concessions and Internal Audit
New York City Department of Parks & Recreation;
Danny Zausner, Chief Operating Officer, NTC;
Andrea Hirsch, Chief Admin Officer & General Counsel, USTA;
Ed Neppl; Chief Financial Officer & Director of Administration, USTA

USTA NATIONAL TENNIS CENTER'S PRINCIPAL CORRECTIONS AND CONCURRING RESPONSES

Respecting:

COMPTROLLER'S AUGUST 1, 2019 DRAFT AUDIT REPORT ON THE FEES DUE FROM THE USTA NATIONAL TENNIS CENTER, INC.,

AND THE CENTER'S COMPLIANCE WITH ITS LEASE AGREEMENT

August 15, 2019

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The United States Tennis Association Incorporated, a 501(c)(6) tax exempt organization ("USTA"), is the sole member of the USTA National Tennis Center Incorporated, a 501(c)(3) tax exempt organization ("USTA NTC"). In 1993, the USTA NTC entered into a 99-year lease with the City of New York to construct, renovate, maintain and operate the USTA National Tennis Center in Flushing Meadows-Corona Park.

I. INTRODUCTION: THE COMPTROLLER'S AUGUST 1, 2019 DRAFT AUDIT'S PRINCIPAL CONCLUSION CONFIRMS USTA NTC'S LEASE COMPLIANCE; IMPORTANCE OF THE USTA BILLIE JEAK KING NATIONAL TENNIS CENTER (NTC).[1]

Commencing in November of 2017, the City of New York Comptroller's Office ("Comptroller's Office") conducted for nearly two years an extensive audit of the USTA NTC to principally determine USTA NTC's compliance with its obligations under the 1993 City of New York-USTA NTC 99-year lease ("Lease") requirements of payment of Base Rent and Gross Revenues percentage rent to the City of New York's Department of Parks & Recreation ("Parks Department") for revenue-producing USTA tennis events (e.g., the US Open), and using the City-owned NTC facilities and related Flushing Meadows-Corona Park land. On June 6, 2019, a formal audit "exit conference" was convened by the Comptroller's Office and attended by representatives of the Comptroller's Office, the Parks Department, the City of New York and the USTA NTC. On Thursday August 1, 2019, the Comptroller's Office issued a final draft audit ("Draft Audit") that was hand delivered to the USTA NTC on Friday, August 2, 2019, attached hereto at Tab l. The Parks Department and USTA NTC were requested to submit written comments, if any, to the Draft Audit by close of business on Thursday, August 15, 2019.

Subsequent to receiving the Draft Audit, USTA NTC and the Parks Department discussed in principle each of the Draft Audit findings. The USTA NTC agreed to remit payment for the audit findings it agreed with and reviewed with the Parks Department the audit findings that the USTA NTC was disputing.

This document prepared by the USTA NTC, and dated and submitted on Thursday, August 15, 2019, contains the USTA NTC's principal corrections of and concurring responses to the Draft Audit.

A. Most Significant Finding.

Over a period of almost 21 months, from November 2017 to July 2019, in conducting the Draft Audit, the Comptroller's experienced professional audit staff spent what appears to have been thousands of hours investigating the USTA NTC's tennis and administrative operations and interviewing its operating and financial staff; reviewing immense quantities of financial records, including sponsorship agreements, broadcast agreements, hospitality agreements, contracts for goods and services, ledgers and trial balance, computer records, rent receipts, invoices, Parks Department files, insurance certificates, correspondence files, computerized advanced ticket payment reports, sub-licensee annual sales reports and daily cash register reports, and many other documents; reviewing and testing financial reporting systems and procedures (including, among others, internal controls for revenue recording and reporting, USTA NTC's ticketing agent's computerized ticket sales system, reporting systems and procedures for all daily box office transactions); and undertaking a wide variety of independent allocation valuation studies and procedures to determine the allocation and/or market value or cost of numerous goods and services. After nearly two years of vast investigation and extensive, wide-ranging and exhaustive auditing activities, the central and fundamental conclusion of the Draft Audit is USTA NTC made timely payments of Base

Rent and Percentage Rent, maintained the required insurance coverage for itself and paid water and sewer charges.

As one would expect in any audit of this scope, the Draft Audit discusses some circumstances and transactions, where it differs with the methods or results of USTA NTC accounting, business or reporting decisions. Such differences are by no means widespread or numerous, nor unexpected given the amount of time and effort the Comptroller's Office devoted to the USTA NTC audit and the complex USTA NTC operations, revenues and financial procedures. However, in most instance noted in the Draft Audit, the matter discussed involves differences in Lease interpretation and accounting judgments, in which reasonable professionals with expertise in these areas can and do differ. Therefore, it is not surprising that the USTA NTC, after conducting a detailed ·and thorough review of the Draft Audit, and after conferring with its financial and legal advisors, both firmly differs with several of the Draft Audit's most significant findings, and, at the same time, concurs willingly with other of the Draft Audit's findings. The specific areas of agreement and disagreement are covered in detail in Part III below.

B. The Importance of the NTC to New York City.

Any audit by the Comptroller's Office of USTA NTC's compliance with the Lease must be considered in a broader context that places the relatively narrow and limited financial, accounting and Lease interpretation issues covered by the Draft Audit in the wider lens of the overall financial benefits to the City of New York by having the NTC located in the Borough of Queens, in one of the City's most important and celebrated public parks, Flushing Meadows-Corona Park.

Ordinarily, an official audit or a response to an official audit would contain a standard cost-benefit analysis of the underlying publicly owned, privately operated world-class sports facility and would describe certain routine economic impact, employment creation and tax generation analyses and their results. Much of the information and data concerning the impact of the NTC has already been made public, including the findings of a study jointly announced by the Comptroller's Office and the USTA NTC in 2001. Instead of repeating or summarizing that information here, it seems more fitting and appropriate to quote words used by the USTA NTC’s Vice President, Gordon Smith, in his letter of this date transmitting this response of the USTA NTC to Deputy Comptroller Marjorie Landa. His comments vividly convey not only the benefits of the NTC but also the spirit of the USTA NTC's commitment to New York City and its dedication to operate and maintain facilities and programs at the NTC that generate the highest possible return, financial and otherwise, to the City and to the public. Mr. Smith's letter, referring to the completion of the NTC in August 1978, states in part:

> "At that time, the USTA NTC and the City of New York embarked on an extraordinary, long-term journey that has defied the well-known trends of tax breaks, concessions and the use of municipalities as bargaining chips to select the city a sports entity calls 'home'. Nearly three decades removed from its opening, the NTC remains one of, if not 'the', greatest and most unique venues in the country. In addition to hosting the US Open (one of the world's largest annually attended sporting events), the NTC serves as the world's largest public tennis

facility, open to the public 11 months of the year. The NTC also represents a rare example of a world-class sports venue that currently pays $3.45 million in municipal rent each year despite the fact that it was constructed without the use of any taxpayer money, a win-win for the USTA NTC and the people of New York City.

Over the years, the USTA NTC has invested over a $1.2 billion in the NTC; no City money was required or requested. Our biggest investment to date made its debut in 1997 with the opening of Arthur Ashe Stadium, the crown jewel of the NTC and a court that has played host to some of the greatest tennis matches of all time, each seen in person by 23,000+ spectators and viewed by worldwide television audiences that have exceeded tens of millions of people. In 2014 the USTA NTC embarked on a Strategic Transformation of the facility, self-funding through debt and operating funds over $660 million dollars in order to ensure that the US Open remains a world-class, preeminent sporting event and the venue maintains its stature as a world-class tennis venue. Our approach to stadium construction was so unique that Mayor Bloomberg acknowledged in 2002 that it was 'the only good athletic sports stadium deal, not just in New York, but in the country."

II. PRINCIPAL DIFFERENCE BETWEEN USTA NTC AND DRAFT AUDIT: $311,201 ADDITIONAL RENT AND FEES FOR FOUR (4) YEARS (AVERAGE OF $77,800 PER YEAR).

One clear measure of the success and benefits of the Lease to the City is the significant growth in revenues, and consequently the rental fees paid by USTA NTC to the Parks Department. In the 25 full calendar years since the Lease was signed, US Open revenues have grown by 935% and base rent and percentage rent paid to the Parks Department have grown from $320,000 in 1994 to over $3.45 million in 2018, a 1,078% increase. In that same period, total rent paid was approximately $51,478,994. Clearly, the Lease is a favorable arrangement for the City of New York.

Against this backdrop of swelling revenues and rent payments benefiting the City, the Comptroller's Draft Audit nevertheless asks whether a more liberal and broader definition of “Gross Revenues” in Section 3.03(d) of the Lease can be applied to yield even more Gross Revenues from which additional percentage rental payments could be paid. Not altogether surprisingly, as a result of the Comptroller applying a broader interpretation of Gross Revenues, the Draft Audit concludes that over the four (4) year period of 2014-2017, the USTA NTC should have reported $31,120,169 million in additional Gross Revenues which would result in an additional $311,202 in rent and late fees.

Following a thorough review of the Draft Audit's conclusions, the USTA NTC has concluded, based on the legal interpretation of the Lease and the consistent application of GAAP accounting standards, that it should report $14,329,660 as additional Gross Revenues and pay $143,297 in additional rent for the 2014-2017 period.

In other words although the USTA NTC concurs with some of the Draft Audit findings, the Draft Audit and the USTA NTC differ as to $167,905 in additional

percentage rent and fees, an average of $43,817 for each of the four (4) years examined between 2014-2017 (based on their difference as to $16,790,509 in additional Gross Revenues for that period).

Draft Audit's Table 1 summarizes the calculations and analysis on which its additional Gross Revenue and rent conclusions are based, as set forth on the following page. The USTA NTC's analysis of the Draft Audit and corrections of the Draft Audit's Table 1 summary findings appear on Table II of the following page.

Table I – <u>Comptroller's Schedule of Underreported Revenue, Additional Rent and Late Charges Due</u>.

Types of Underreported/Over-Reported Revenue or Inappropriate Deductions	Calendar Year				Total Amount
	2014	2015	2016	2017	
Underreported In-Kind Benefits	$3,100,000	$2,980,575	$2,899,186	$2,536,874	$11,516,635
Inappropriate Deductions	-0-	$3,291,720	$3,234,061	$3,486,036	$10,011,817
Excluded Sponsorship Revenue	$425,000	$1,655,032	$1,392,013	$960,756	$4,432,801
Excluded Ticket Surcharges, Shipping & Handling Fees, & Other Miscellaneous Revenues	-0-	$2,173,245	$2,314,131	$927,966	$5,415,342
Over-Reported Online Sales & Media Revenues	-0-	($116,758)	($139,668)	-0-	($256,426)
Total	$3,525,000	$9,983,814	$9,699,723	$7,911,632	$31,120,169
Additional Percentage Rent Due					$311,202

The USTA NTC's analysis of the Draft Audit and correction of the Draft Audit's Table 1 summary findings are as follows:

Table II – <u>USTA NTC's Recalculation of Revenue, Additional Rent and Late Charges.</u>

Types of Underreported/Over-Reported Revenue or Inappropriate Deductions	Calendar Year				Total Amount
	2014	2015	2016	2017	
Underreported In-Kind Benefits	$3,100,000	$322,261	$236,252	$273,940	$3,932,453
Inappropriate Deductions	-0-	$1,888,108	$1,614,973	$1,735,211	$5,238,292
Excluded Sponsorship Revenue	-0-	-0-	-0-	-0-	-0-
Excluded Ticket Surcharges, Shipping Fees, Handling Fees, and Other Miscellaneous Revenues	-0-	$2,173,245	$2,314,131	$927,966	$5,415,342
Over-Reported Online Sales and Media Revenues	-0-	($116,758)	($139,668)	-0-	($256,426)
Total	$3,100,000	$4,266,856	$4,025,687	$2,937,117	$14,329,660
Additional Percentage Rent Due					$143,297

The Draft Audit findings in Table 1 concluded $311,202 of percentage rent was due for the 4 year period covered by the audit. This is an average of $77,800 per year. The USTA NTC does not agree with $167,905 of the $311,202 Draft Audit's findings of percentage rent revenues because the methodology and other standards required by the Lease were not followed. USTA NTC does, however, concur that it should pay $143,297 of percentage rent to the City as shown in Table II. Compliance with the Lease is paramount to both parties and is the foundation of their successful partnership and the success of the NTC.

III. DRAFT AUDIT'S ERRORS AND DEFICIENCIES; USTA NTC'S CONCURRING RESPONSES.

Draft Audit Findings	$31,120,169	Additional Gross Revenues
	$ 311,202	Additional Rent Due
Correct Findings	$14,329,660	Correct Total Additional Gross Revenues
USTA NTC: (Lease/GAAP Based Analysis)	$ 143,297	Correct Total Rent Due

Table II in Part II above summarize the USTA NTC's corrections to, recalculations of and concurring responses with respect to the specific findings, and Gross Revenues and additional rent determinations, set forth in pages 7-20 of the Draft Audit ("Findings and Recommendations"). The USTA NTC's detailed analysis of each of the areas summarized in Table II is set forth in the sections lettered A-H which follow.

The USTA NTC’s specific responses to the Draft Audit involve three (3) discrete categories:

- A total of $6,882,713 Draft Audit findings are due to the auditors misinterpretation of or a failure to consider specific applicable Lease provisions and/or a failure to comport with or apply GAAP accounting standards which are mandated by the Lease respecting determinations of USTA NTC Gross Revenues and Excluded Revenues (revenues not to be included in Gross Revenues) related to the US Open and other "Tennis Events."

- A total of $9,907,796 Draft Audit findings also involve substantial deficiencies in critical allocations and in-kind valuation calculations respecting certain goods, services or payments provided to the USTA NTC under various sponsorship agreements.

- There are a total of $14,329,660 Draft Audit findings with which the USTA NTC concurs and accordingly it has made appropriate additional rental payments prior to the issuance of the Draft Audit or any final Audit.

The USTA NTC's evaluation of errors and deficiencies in the Comptroller's findings, as well as the analysis of those matters as to which the USTA NTC concurs with the Comptroller, were guided by two fundamental measures, to wit: **each USTA NTC response in the numbered paragraphs below was based on: (1) the advice and interpretations of the USTA NTC General Counsel and outside counsel as to the definition of "Gross Revenues" in Lease Section 3.03(d)(ii) and related provisions of the Lease; and (2) the USTA NTC's independent outside auditor's review and acceptance of the USTA NTC's accounting treatment and reporting in the USTA**

NTC's GAAP-based audited financial statements for the appropriate time periods in question, which include the transactions and payments addressed by the Draft Audit.

In this regard, it should be noted that while Section 3.03(d) (ii) of the Lease requires the USTA NTC to strictly adhere to GAAP standards in its financial records and reporting as well as in its calculation of Gross Revenues and annual rental payments, the Draft Audit makes no mention of and does not appear to apply GAAP standards in its evaluation of USTA NTC financial transactions and Gross Revenues calculations and reporting.

A. The Draft Audit Report substantially overstates the amounts USTA NTC did not report or unreported revenues of in-kind benefits received.

Draft Audit Finding (p.8)	$11,516,635	Additional Gross Revenues
	$115,166	Additional Rent Due
Correct Finding	$3,932,453	Correct Additional Gross Revenues
USTA NTC: (Lease/GAAP Based Analysis)	$39,325	Correct Additional Rent Due

1. Comptroller's Position: The Draft Audit at page 8 incorrectly states that the USTA NTC underreported at least $11,516,635 in Gross Revenues for calendar years 2014 through 2017 by either omitting or understating the value of certain in-kind benefits in the Gross Revenues reported to the City in each year. In-kind benefits are goods and services provided by sponsors or broadcasters, in addition to payments made to USTA for sponsorship or broadcasting rights.

2. Correct Analysis: The Comptroller's audit is incorrectly applying inflated market values and/or incorrectly making allocation assumptions that are not appropriate.

   - Underreported In-Kind Media Services Provided by Company A: The USTA NTC did include an allocation of the value of the in-kind media services in Gross Revenues. The basis for the audit finding is the auditor's assessment that USTA NTC was unable to provide sufficient documentation to support the allocation. Subsequently, the auditors used information that was not relevant to this barter in applying a greater value. USTA NTC will review such documentation with the Parks Department and make a determination after the Parks Department has had a chance to review such information.

   - Underreported In-Kind Benefit from WiFi Infrastructure and Related Media Services Provided by Company C:

     Included in the Comptroller's findings are value-in-kind infrastructure received from a sponsor at the facility. For a variety of reasons this was not assigned a value, however, USTA NTC is reluctantly remitting payment to the Parks Department in the amount of $31,000.

The Comptroller audit findings incorrectly assume $800K of co-branded media from Sponsor C should be included in the leasehold fee. The USTA NTC extensively explained to the Comptroller Office and provided written certifications from USTA NTC operations that this co-branded media was not of value and not used for the years of the audit finding, specifically 2015 and 2016. The USTA NTC explained to the Comptroller's office that the USTA NTC already had a media plan in place and the cost to redevelop a new co-branded media plan far exceeded the $400K media from the Sponsor. In accordance with GAAP and guidance from our legal counsel, and because the co-branded media was not used and had no value, the USTA NTC is of the opinion such amounts should not be included in the leasehold fee. For further clarification, in 2017 USTA NTC used this barter and as required by GAAP recorded $400,000 as barter revenue in the audited financial statements and included it as part of the leasehold fee payment.

- Other Miscellaneous Unreported In-Kind Revenue:

  Included in the Comptroller's audit findings are complimentary pages in the US Open Program which can be obtained by fans after they enter the US Open grounds. This arrangement enhances the program with the USTA NTC by providing content to the program, but the complimentary pages do not result in any additional revenue for the US Open Program, nor does it provide any value (financially or otherwise) to the USTA NTC. The Comptroller draft report incorrectly assigns a value to these pages based on the premise this is US Open advertising; however, these pages are not advertising. The pages provide content to the Program rather than procuring independent advertising. As such the USTA correctly did not assign any value to these pages as they are not advertising pages. These programs are sold at the US Open and, in turn, the USTA NTC includes the revenues received from the concessionaire for the US Open Program in the rent paid to the City of New York. The Comptroller's finding is incorrect because the complimentary pages are not advertisements; there is no financial or other benefit to the USTA NTC, other than the revenues reported for the US Open Program.

  Included in the Comptroller's findings were other de minimis items for beverage and tickets for which USTA NTC concurs with the Comptroller's finding and has remitted payment to Parks in the amount of $8,325.

3. <u>USTA NTC Recalculation</u>. As a result of the audit review process with the Comptroller's Office, the USTA NTC has concluded it is appropriate to include in Gross Revenues the value-in-kind infrastructure received from the sponsor and other de minimis items for beverage and tickets. Accordingly, the USTA NTC has remitted payment to the Parks Department in the amount of $39,325.

B. Draft Audit Report substantially overstates that USTA NTC Inappropriately Deducted Over $10 million in Operating Expenses from Gross Revenues:

Draft Audit Finding (p.11)	$10,011,817	Additional Gross Revenues
	$100,118	Additional Rent Due
Correct Finding	$5,238,292	Correct Additional Gross Revenues
USTA NTC: (Lease/GAAP Based)	$52,383	Correct Additional Rent Due

1. Comptroller's Position: The Draft Audit at page 11 incorrectly concludes that the USTA NTC inappropriately deducted $10,011,817 in operating expenses from the Gross Revenues for Calendar Years 2015 through 2017. As a result, USTA NTC underpaid the City by $100,118 in Percentage Rent. Specifically, USTA NTC inappropriately deducted:

   - $4,500,688 in catering and set up costs from hospitality revenue;
   - $3,833,362 in commissions and advertising expenses paid to vendors from sponsorship revenue for promoting US Opens;
   - $1,114,000 in broadcasting commissions and production costs from broadcasting revenue;
   - $430,144 in a vendor's credit card fees from commissions of the food sales; and
   - $133,623 in cost of goods sold from merchandise revenue.

2. Correct Analysis: The Draft Audit is applying Section 3.08 of the Lease, however, it does not take into account the other relevant sections of the Lease for the proper and complete analysis. The 2nd Amendment and 4th Amendment Section 3.03(d)(iii) and (iv) Excluded Revenues are applicable:

   a. Section 3.03(d)(iii) of the Lease states:
   "(7) any payments received by Subtenant, licensee or concessionaire that are not passed on to Tenant or Affiliate; provided that any such payments which are received by a Subtenant, licensee or concessionaire which is an Affiliate, shall be included as "Gross Revenues" to the extent provided in Section …
   (8) so called "pass-through" made by Subtenants to Tenants for payment of … and other like pass through payments
   (11) the value of any product, equipment or supply to Tenant by a sponsor for the primary purpose of supporting or benefiting the sponsor."

   b. Section 3.03(d)(iv) states: "*to facilitate the determination of what constitutes Gross Revenues, Tenants shall insure that all Subleases, concessions and licensee* *agreements, and all contracts it enters into … provide for fair allocations of Gross Revenues*."

- The Comptroller's audit finding concludes an audit finding of $4,500,688 in catering and setup costs from hospitality. A substantial portion of the audit findings in the amount of $3,777,958 is for a "pass-through" amounts to our concessionaire and licensee, which is recognized as Excluded Revenues under the Lease. The concessionaire/licensee in turn provides a payment to the USTA NTC, which payment was included in Gross Revenues and remitted to the City as Rent consistent with Section 3.03(d)(7) above. Effectively, the Comptroller's audit finding is incorrectly concluding that the USTA NTC should duplicate and inflate gross revenues resulting in USTA NTC paying rent twice. The remainder of the audit finding of $722,730 USTA NTC concurs with the audit finding and has remitted payment to the Parks Department in the amount of $7,227.

- The Comptroller's audit findings conclude $3,833,362 in commissions and advertising expenses should be included in Gross Revenues. Approximately $565,423 were from the Tenant procuring advertising in the US Open Program on behalf of the sponsor which is a pass-through payment purely for the benefit of the sponsor as mentioned in Section 3.03(d)(iii)(11) of the Lease as described above and are Excluded Revenues. The remaining balance are commissions deducted from gross revenues that after further review the USTA NTC concurs with the audit finding and has remitted payment to the Parks Department in the amount of $32,679.

- The Comptroller's audit findings include $1,114,000 for additional production costs and commissions for a territory outside of the international broadcast agreement. The USTA NTC contributed $1,000,000 of the $1,114,000, and should be allowed to offset that amount. However, the Comptroller concludes there is not sufficient documentation provided and disallowed the offset. While it is unclear that the offset should be disallowed, the USTA NTC will accept the audit finding and has remitted payment to the Parks Department in the amount of $11,140.

- In regards to the $430,144 audit finding for concessionaire credit card fees, USTA NTC correctly reported revenues from concessions rental in accordance with Section 3.02(d)(ii)(10) of the Lease which allows reportable sales on the basis of "sales and other criteria", all of which was clearly outlined in the agreement with the concessionaire and reported by USTA NTC. The Comptroller audit findings of $430,144 incorrectly recalculates the revenues from the concessionaire which is outlined in the agreement with the concessionaire on arriving at commissionable sales inclusive of fees payable to credit cards. Essentially, the Comptroller adds the credit card fees that get paid out of the sales to the credit card vendors as Gross Sales. The Comptroller's audit finding incorrectly recalculates the contractual revenues due to the USTA NTC from the concessionaire. Additionally such amounts were recorded in accordance with GAAP as required by the Lease in arriving at reported revenues, but the Comptroller also failed to consider this in its conclusion.

- The Comptroller concluded $133,623 was incorrectly deducted for cost of goods sold from merchandise revenue. The USTA NTC agrees with the audit finding and subsequently reimbursed the City of NY for this audit finding in the amount of $1,336.

3. USTA NTC Recalculation. As a result of the audit review process with the Comptroller's Office, the USTA NTC has concluded it is appropriate to include in Gross Revenues the commissions, host telecast fee and value of the cost of goods sold from merchandise revenue of $45,019. (Draft Audit, page 11)

C. Draft Audit Report Incorrectly Concludes USTA NTC Did Not Report Over $4 Million in Sponsorship Revenue Collected from Sponsors.

Draft Audit Finding (p.12)	$4,432,801	Additional Gross Revenues
	$44,328	Additional Rent Due
Correct Finding	-0-	Correct Additional Gross Revenues
USTA NTC: (Lease/GAAP Based Analysis)	-0-	Correct Additional Rent Paid

1. Comptroller's Position: USTA NTC excluded $1,275,000 in revenue collected from a sponsor from Calendar Years 2014 through 2016. USTA NTC officials claimed that this revenue was a grant from the sponsor and should be excluded from the Gross Revenue. However, we found no provisions in the sponsorship agreement or the Lease to support this treatment of the sponsor's payment. Thus, an additional $1,275,000 in revenue should have been reported by USTA NTC for the purpose of calculating Percentage Rent.

   In addition, we found that USTA NTC underreported $3,157,801 in sponsorship revenue by inappropriately categorizing it as sponsorship revenue allocated to US Open Series (USOS) from Calendar Years 2015 through 2017. USOS is a series of professional tennis tournaments, held prior to the US Open, in various cities in North America. Among the 15 sponsorship agreements that we reviewed, 3 agreements contained provisions for providing support to USOS.

   Correct Analysis: On page 12 of the Draft Audit Report it states that "*Section 3.03(d)(iv) of the Lease requires that any amounts excluded from the Gross Revenues should be expressly stated in the sponsorship agreement.*" This statement does not accurately summarize the language in the Lease, which expressly states "*sponsorships and advertising revenues, shall, to the extent appropriate, either (A) be structured so that those contracts which generate solely Gross Revenues are separated from other contracts or (B) expressly provide for fair allocations of Gross Revenues and Excluded Revenues.*" In regards to the US Open Series, the USTA NTC clearly demonstrated (as shown in the General Ledger and in its certified audited financial statements) it provided a fair allocation of Gross Revenues to the Comptroller's Office. These factors include (i) a $2 million sponsorship fee reduction per year if it is not staged in one sponsorship agreement, (ii) a valuation placed on title/umbrella presenting sponsor rights and the associated exposure (including direct and indirect expenses for deliverables), (iii) revenue allocation to cover Player Bonus (maximum payout of $3 million) and (iv) player appearance fees to participate in the USOS. The USTA NTC included an allocation in the USTA NTC Consolidated financial statements prepared in accordance with GAAP. The allocation was prepared and shown in accordance with the Lease requirements and should be viewed as fair and appropriate.

Additionally in regard to the $1,275,000 annual contribution received by the sponsor as a donation, the agreement clearly provides consideration paid for the sponsorship benefits separately from the donation that the not-for-profit entity made independent of the sponsorship benefits. This donation is clearly bifurcated in the sponsorship agreement and as mentioned above is appropriately separated in the agreement. Therefore, the $1,275,000 should not be considered as revenues for purposes of Gross Sales.

D. USTA NTC Inappropriately Excluded Over $5 Million from Gross Revenues From Ticket Surcharges and Other Fees.

Draft Audit Finding (p.12)	$5,415,342	Additional Gross Revenues
	$54,153	Additional Rent Due
Concurring Finding	$5,415,342	Additional Gross Revenues
USTA NTC: (Lease/GAAP Based Analysis)	$54,153	Additional Rent Paid

1. Comptroller's Position: The USTA NTC concurs with the Draft Audit's inclusion in Gross Revenues, at page 12, of the $5,415,342 and has accordingly paid $54,153 as additional rent to the City of New York prior to the issuance of the Draft Audit.

E. USTA NTC Over-Reported $256,426 in Online Sales and Media Revenue to the City.

Draft Audit Finding (p.13)	($256,426)	Additional Gross Revenues
	($2,564)	Additional Rent Due
Concurring Finding	($256,426)	Additional Gross Revenues
USTA NTC: (Lease/GAAP Based Analysis)	($2,564)	Additional Rent Paid

1. Comptroller's Position: The USTA NTC concurs with the Draft Audit's NTC over-reported, at page 13, $256,426 in Gross Revenues to the City during Calendar Years 2015 and 2016. Thus, the NTC over-paid $2,564 in Percentage Rent and has taken a credit to the additional

rent paid to the City of New York as part of the remittance of agreed to audit findings in the Draft Audit.

F. Over $8 Million of Revenue Discrepancies Found Between USTA NTC Financial Statements and Percentage Rent Reports Submitted to the City.

USTA NTC Response. The USTA NTC audited financial statements and general ledger were provided to the comptroller audit team at the onset of the audit. This finding was brought to the attention of USTA NTC in the final stages of wrapping up the audit, not allowing the USTA NTC sufficient time to review the auditor's analysis and/or to respond. The USTA NTC will review this conclusion with the Parks Department to reconcile any difference that may exist.

G. USTA NTC was unable to Provide Documentation to Substantiate that Certain Companies Maintained the Required Insurance Coverage.

USTA NTC Response: This comment appears to be outside the purpose of the Draft Audit, which is to review the USTA NTC's compliance with the rent provisions of the Lease. We do, however, point out that the USTA NTC does comply with all of the insurance obligations under the Lease as was noted in the Draft Audit on page 2. The USTA NTC takes great precaution in all of its agreements and, as a standard practice, requires insurance coverage from its sponsors and vendors, even though this is not mandated by the Lease. The USTA NTC also, as a standard practice, includes an indemnification obligation in each of its sponsor/vendor agreements. Having said that, the Draft Audit comment is outside of the purpose of this audit. Accordingly, we do not understand the inclusion of this comment in the Draft Audit, especially since the Draft Audit recognizes the USTA NTC complies with the insurance obligations.

H. USTA NTC Did Not Consistently Submit Annual Certified Financial Statements to the Parks Department.

USTA Response: The USTA NTC will revisit the process of providing its certified financial statements to the Parks Department. The USTA NTC publishes its financial statements on its website, and it is available for the public and the Parks Department to review. USTA NTC will work with the Parks Department to have a more formal process in place for submission of financial statements.

I. Allowing USTA NTC to Deduct Parking Lot Payments as Credits Reduced the percentage Rent Paid to the City by up to $1,584,000 Over 10 years. [Draft Audit, Page 17.]

USTA NTC Response: Under the Lease, the Parks Department was required to provide a certain number of parking spaces for use by the USTA NTC. When the Parks Department could not comply with the Lease obligation, the Parks Department agreed to remedy the issue by providing to USTA NTC the parking spaces at the Hall of Science ("HOS"). In this arm-length agreement, the Parks Department requested the USTA NTC to pay the amounts due to the HOS on behalf of the Parks Department and to deduct said amounts from rents payable to the Parks Department. The transaction allowed the Parks Department to comply with its Lease obligations to provide parking to the USTA NTC. The terms of the arrangement is set forth in the Fourth Amendment to the Lease.

**DRAFT AUDIT
RECOMMENDATIONS [PAGE 19]**

1. Draft Audit: Remit $311,202 in additional Percentage Rent due to Parks.

   USTA NTC Response:
   USTA NTC concurs with $143,297 of the Audit Finding and has remitted payment to the Parks Department.

2. Draft Audit: Determine, with Parks, how much of the $82,310 should be remitted to the City as Percentage Rent.

   USTA NTC Response:
   USTA NTC will review this conclusion with the Parks Department to reconcile any differences. USTA NTC will review the disputed audit findings with Parks and come to a resolution.

3. Draft Audit: Ensure all Gross Revenues are accurately reported to Parks in accordance with the terms of the Lease by:
   a. Accurately accounting for all in-kind benefits received from the sponsors, broadcasting companies, and vendors;
   b. Reviewing the Gross Revenues information provided by USTA NTC to ensure there are no inappropriate exclusion or deductions from the Gross Revenues;
   c. Including all fees collected from the activities that occurred at the Tennis Center;
   d. Accurately recording Gross Revenues in its general ledger; and
   e. Making annual adjustments, when necessary, to the Gross Revenues reported to the City.

   USTA NTC Response:
   USTA NTC has made and will continue to report Gross Revenues accurately in accordance with the terms of the Lease. Prospectively management will ensure that any agreed to audit findings will also be reported.

4. Draft Audit: Submit the certified financial statements to the City within the 90 days after the end of each Calendar Year.

   USTA NTC Response:
   USTA NTC will put a formal process in place with the Parks Department for delivery and receipt of financial statements.

5. Draft Audit: Ensure all sponsors, broadcasters, and vendors maintain the required insurance coverage.

   USTA NTC Response:
   This is outside the scope of the audit, USTA NTC maintained appropriate insurance coverage as required by the Lease.

Executive Summary

In 1993, the City of New York and the USTA NTC entered into a long term lease, which is the home of the world famous USTA Billie Jean King National Tennis Center and the preeminent sport event, the US Open Tennis Championship. Over the years, USTA NTC has invested over $1.2 billion dollars in the NTC facility. In 1997, the USTA NTC opened Arthur Ashe Stadium, the crown jewel of the NTC and a court that has played host to some of the greatest tennis matches of all time, each seen in person by 23,000+ spectators and viewed by worldwide television audiences that have exceeded tens of millions of people.

In 2001, the Comptroller's Office issued a joint release with the USTA NTC recognizing that the US Open generated more in direct revenue to the City of New York's tristate area than any other annual sports or entertainment event in any city in the United States. Our approach to stadium construction was so unique that Mayor Bloomberg acknowledged in 2002 that it was "*the only good athletic sports stadium deal, not just in New York, but in the country.*"

In 2014, the USTA NTC embarked on a Strategic Transformation of the NTC facility, self-funding, through debt and operating funds, over $660 million dollars in order to ensure that the US Open remains a world-class, preeminent sporting event and that the venue maintains its stature as a world-class tennis venue. No City money has been required or requested. Since that time the US Open has continued to have a great financial benefit to NYC and the tristate area. In 2013, the USTA NTC committed to pay over $10 million dollars to NYC as a goodwill gesture to fund improvements to and maintenance of Flushing Meadows-Corona Park for decades to come, and in addition to the 34 public tennis courts at the NTC, the USTA NTC provides 12 tennis courts to the Parks Department outside the NTC premises without cost to NYC for the benefit of those who use the park.

In 2014, AKRF conducted a study which found that the US Open provided an economic impact of over $900 million to NYS annually and over $750 million annually to the City of New York, which have continued to grow since that point in time. Over four decades from its opening, the NTC remains one of, if not "the," greatest and most unique venues in the country. In addition to hosting the US Open (the world's largest annually attended sporting event), the NTC serves as the world's largest public tennis facility, open to the public 11 months of the year. The USTA NTC also represents a rare example of a world-class sports venue that pays over $3.45 million in municipal rent each year despite the fact that it was constructed without the use of any taxpayer money, a win-win for the USTA NTC and the people of New York City.

The Lease has been a large success for both the City and the USTA NTC. Over the past 25 years there has been a significant growth in revenues, and consequently in the lease fees paid by the USTA NTC to the Parks Department. In the 25 full calendar years since the Lease was signed, US Open revenues have grown by 935% and base rent and percentage rent paid to the Parks Department have grown from $320,000 in 1994 to over $3.45 million in 2018, a 1,078% increase. In that same period, total rent paid was approximately $51,478,994. The Lease has proven to be a favorable arrangement for the City of New York.

Starting in November of 2017, the City of New York Comptroller's Office conducted an extensive audit that took place for nearly 21 months, of the USTA NTC to principally determine the USTA

NTC's compliance with its obligations under the Lease requirements of payment of base rent and gross revenues percentage rent to the Parks Department. On June 6, 2019, a formal audit "exit conference" was convened by the Comptroller's Office and attended by representatives of the Comptroller's Office, the Parks Department, the City of New York and the USTA NTC. On Thursday August 1, 2019, the Comptroller's Office issued a Draft Audit that was received by the USTA NTC on Friday, August 2, 2019. The USTA NTC was requested to submit written comments to the Draft Audit by close of business on Thursday, August 15, 2019.

During the 21 months that the audit was conducted, the USTA NTC produced hundreds, if not thousands, of documents, and made available throughout the prolonged audit period all staff, all of the financial books and records, and other documents that were requested by the Comptroller. The USTA NTC even went beyond the Lease requirements in providing detailed information and copies, in an effort to accommodate the conclusion of a thorough audit. In sum, USTA NTC spent many, many hours in assisting the audit and in answering questions, providing back up information, explanations and whatever details were requested for the audit to be complete.

Upon receipt of the Draft Audit, the USTA NTC thoroughly reviewed the findings stated in the Draft Audit report. As noted by the Comptroller, the USTA NTC "made timely payments of Base Rent and Percentage Rent, has maintained the required property and liability insurance, and paid water and sewer charges…" Despite this important and accurate finding, there remain disparities in the Draft Audit. While the Comptroller's Office is of the view that $31,120,169 should be considered additional gross revenue reportable under the Lease, the USTA NTC's view, which is based on the advice of its independent financial advisors and legal counsel, is that only $14,329,660 constitutes gross revenue reportable under the Lease. Although the Draft Audit finding constitutes slightly more than 2% of the USTA NTC's annual rental payments, $167,905 of the $311,202 Draft Audit's findings is incorrect because the methodology and other standards required by the Lease were not followed. The USTA NTC, however, does concur that it should pay $143,297 of percentage rent to the City. The payment of $143,297 was remitted to the Parks Department prior to this report.

The deficiencies that exist in the Draft Audit findings result from the auditor misinterpreting the Lease, which they failed to consider specific applicable Lease provisions or failed to comport with or apply GAAP accounting standards, which are mandated by the Lease. Each one of the incorrect analysis in the Draft Audit has been discussed in the USTA NTC response above. In addition, some of the Draft Audit findings were introduced to the USTA NTC at the conclusion of the audit. As a consequence, some of the findings are based on a lack of information by the auditor. Other comments made in the Draft Audit are beyond the scope of the purpose of the audit. Nevertheless, as mentioned before with respect to the Draft Report findings the USTA NTC did concur with $14,329,660, the USTA NTC made payment of those additional percentage rents to the Parks Department. With respect to any existing differences between the Draft Audit and the USTA NTC's analysis, the USTA NTC will review each of the findings with the Parks Department to reconcile any differences.

After 21 months, the Draft Audit finding constitutes only slightly more than 2% of the USTA NTC annual rental payments. Nevertheless, the USTA NTC supports that the City should be paid every amount due under the Lease. The USTA NTC further believes compliance with the Lease is paramount to both parties and is the foundation of its successful partnership with the City, and the success of the NTC.

NYC Parks

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August 15, 2019

Marjorie Landa
Deputy Comptroller for Audit
City of New York Office of the Comptroller
1 Centre Street, Room 1100
New York, NY 10007

Re: Draft Audit Report on the Compliance of USTA National Tennis Center, Inc. ("NTC") with its New York City Lease (Audit Number FN18-082A)

Dear Deputy Comptroller Landa:

This letter addresses the findings and recommendations contained in the New York City Comptroller's Draft Audit Report ("Report"), dated August 1, 2019, regarding the above subject matter.

We appreciate your work in reviewing the City's lease agreement with NTC and are pleased that your Report found that NTC made timely payments of Base Rent and Percentage Rent, maintained the required insurance coverage for itself, and paid water and sewer charges.

The NTC is a huge boon for New York City's economy, generating more than $750 million annually in economic impact for the City. Further, NTC has invested more than $1.2 billion in capital investments to expand and revitalize its facility in Flushing Meadows Corona Park, ensuring that the U.S. Open remains one of the world's premier sporting events for years to come.

The primary finding of this Report is that NTC understated their Gross Revenues from Calendar Years 2014 – 2017 by approximately $31 million. During those years, NTC generated $1.226 billion in Gross Revenues reported to the City. The amount cited by the auditors that was allegedly underreported represents approximately 2 1/2 % of that total. While we are working with NTC to address this matter and ensure that any fees properly owed to the City are recouped, it is important to note the small percentage of Gross Revenues that this Report seeks to address.

The first five recommendations in the Report are directed to NTC and the latter six are directed to Parks. In response to the recommendations directed to Parks:

Recommendation 6 – Recoup $311,202 in additional Percentage Rent from NTC.

Parks is working with NTC to address the substance of this finding. NTC has acknowledged that there was unintentionally underreporting of Gross Revenues in the amount of $14,329,661, meaning that the additional Percentage Rent amount owed to the City is $143,296.61. Parks has received that amount from NTC. The remaining portion of Percentage Rent, $167,905.39, that the Report contends is owed to the City is disputed by NTC. For those areas that remain in dispute, Parks will review the relevant records and contracts related to the disputed amounts in order to determine if any additional Percentage Rent is due.

Recommendation 7 – Ensure NTC submit the certified financial statements annually to Parks.

Parks will work with NTC to ensure that their certified financial statements are annually submitted to Parks, in addition to all of the quarterly financial reports that are routinely received and analyzed.

Recommendation 8 – Review NTC's books and records for the years that were not covered in our scope period and determine whether NTC owes any additional Percentage Rent.

Parks will consider where we can perform targeted reviews of NTC's income. However, we must first focus our attention on reviewing the monetary findings raised by this Report, in order to resolve any disputes and ensure that the City recoups any fees that are owed.

Recommendation 9 – Conduct periodic reviews of NTC's compliance of the terms of the Lease.

Parks will consider where we can perform targeted reviews of NTC's compliance, where appropriate.

Recommendation 10 – Consider seeking revision of the terms of the Lease including, but not limited to:

- **Requiring NTC to submit annual certified financial statements for the entire operation of the Tennis Center or requiring all revenues generated from the Tennis Center be recorded in NTC's general ledger;**
- **Allowing the City to copy all books and records relating to the Tennis Center's operation;**
- **Requiring NTC to provide electronic copies of the books and records when requested;**
- **Imposing late charges when the payments become overdue, not when underpayment exceeds five percent and 10 days after the demanded due date; and**
- **Discontinue automatic renewal of the Lease;**
- **Cease providing parking credits to NTC after the expiration of the current credits. If Parks finds it is necessary to provide support to NTC for the parking payments, the payments should be deducted from the Gross Revenues**

While we will take these recommendations under advisement during any future lease negotiations, it must be emphasized that Parks cannot unilaterally revise the terms of the existing lease. Any amendment to the lease would need to be the product of good faith negotiations between the City and NTC, and would require the approval of the City's Corporation Counsel. Moreover, it does not appear likely that NTC would agree to the Report's suggested amendments and certainly not without other concessions from the City in exchange for such revisions.

Recommendation 11 - Consider the financial impact to the City before amending any financial terms in the Lease with NTC.

Financial impact to the City is always a critical consideration during any negotiation and Parks strongly disputes any insinuation that this was not the case in our prior negotiations with NTC. We do not see any evidence in the Report to support a finding that financial impact is not considered, other than a matter raised concerning the deduction of parking payments to the Hall of Science. As communicated during the audit, the City is required under the original lease to provide parking and the provisions of the relevant amendments were a product of good faith negotiations between the City and NTC, which was approved as to form by the Corporation Counsel.

Further, in addition to their payments of Base and Percentage Rent, NTC generates more than $750 million in annual economic impact for the City, the strongest indicator of the positive financial benefit it provides. The Report makes no comment about the many economic benefits of the NTC, nor did the auditors inquire about such benefits from either NTC or Parks.

Parks wishes to thank you and your audit staff for the time and effort devoted to completing this Report.

Sincerely,

David Cerron
Assistant Commissioner, Concessions & Audit