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Performance Audit Division

Performance Audit

Arizona Tourism and Sports Authority

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STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

Debra K. Davenport
Auditor General

The **Auditor General** is appointed by the Joint Legislative Audit Committee, a bipartisan committee composed of five senators and five representatives. Her mission is to provide independent and impartial information and specific recommendations to improve the operations of state and local government entities. To this end, she provides financial audits and accounting services to the State and political subdivisions, investigates possible misuse of public monies, and conducts performance audits of school districts, state agencies, and the programs they administer.

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STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

DEBRA K. DAVENPORT, CPA
AUDITOR GENERAL

WILLIAM THOMSON
DEPUTY AUDITOR GENERAL

March 25, 2004

Members of the Arizona Legislature

The Honorable Janet Napolitano, Governor

Mr. John Benton, Chairman
Arizona Tourism and Sports Authority

Mr. Ted Ferris, President/CEO
Arizona Tourism and Sports Authority

Transmitted herewith is a report of the Auditor General, A Performance Audit of the Arizona Tourism and Sports Authority (TSA). This audit was conducted pursuant to Arizona Revised Statutes (A.R.S.) §5-812. This statute requires a performance audit no later than 2004 and at least every 5 years thereafter. This audit was conducted under the authority vested in the Auditor General by A.R.S. §41-1279.03. I am also transmitting with this report a copy of the Report Highlights for this audit to provide a quick summary for your convenience.

As outlined in its response, TSA agrees with 3 of the 4 the findings and indicates that it plans to implement or implement in a different manner all of the recommendations addressed to it.

My staff and I will be pleased to discuss or clarify items in the report.

This report will be released to the public on March 26, 2004.

Sincerely,

Debbie Davenport
Auditor General

Enclosure

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PROGRAM FACT SHEET

Arizona Tourism and Sports Authority

Funding priorities and responsibilities:

The Arizona Tourism and Sports Authority (TSA) has the following statutory funding priorities and responsibilities:

- Designing and constructing a new multipurpose facility, which will be the new home of the Arizona Cardinals football team and the Tostito's Fiesta Bowl, and which will also host the 2008 Super Bowl. The facility is currently under construction in Glendale;
- Funding tourism promotion in Maricopa County by distributing monies to the Arizona Office of Tourism;
- Awarding monies to renovate existing or construct new Cactus League spring training baseball facilities in Maricopa County;
- Awarding grants for youth and amateur sports facilities and programs in Maricopa County;
- Funding TSA operations, including staff salaries, travel, and insurance, as well as funding the operations of the multipurpose facility; and
- Establishing and funding reserves for its operations, youth and amateur sports, and for repairs and other long-term costs associated with the multipurpose facility.

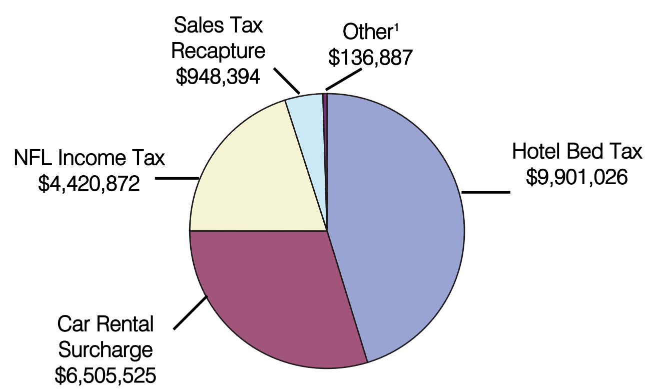
Funding sources:

TSA began receiving funding in 2001 from a variety of sources. Specifically:

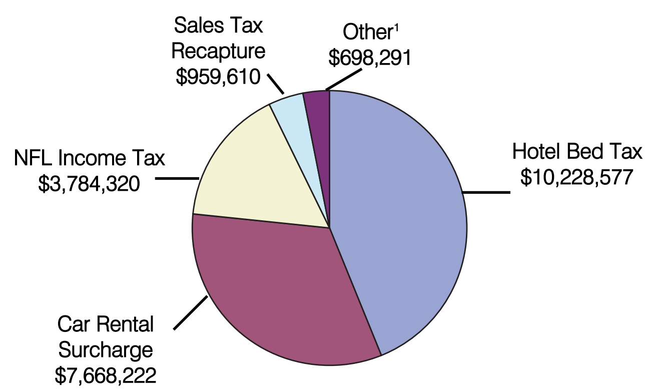
- Hotel bed tax increase—For 30 years, TSA receives revenue from a 1 percent increase in Maricopa County's hotel bed tax. TSA expects to receive a total of nearly $610 million from hotel bed taxes through February 2031.
- Car rental surcharge—For 30 years, TSA receives a portion of the revenues generated by a 3.25 percent car rental surcharge in Maricopa County. TSA projects that it will receive over $382 million from this surcharge through February 2031.

TSA funding:

$21,912,704 (fiscal year 2002)



$23,339,020 (fiscal year 2003)



1 Includes interest received from investment activities. TSA received substantially more interest income in fiscal year 2003 due to large account balances associated with the sale and deposit of $222 million in bond proceeds.

- **Sales tax recapture**—TSA recaptures all state sales tax paid at Cardinals games, including those played at Arizona State University's Sun Devil Stadium until the new facility is constructed, as well as any sales taxes paid on materials purchased for the new facility's construction. TSA projects receiving approximately $130 million from this revenue source through 2031; however, the sales tax recapture does not expire in 2031.
- **NFL tax**—TSA receives all state income taxes paid by the Cardinals' corporate organization, its employees (including players), and their spouses. Statute guarantees a minimum amount that TSA will receive, with this amount growing by 8 percent annually. TSA receives additional money from the State General Fund if the income tax revenues collected do not meet the required minimum amount. This distribution does not expire, but through fiscal year 2031, TSA will receive at least $397.8 million in state income tax revenue.
- **Other facility-generated revenue**—Once the facility is constructed and operating, TSA will also generate revenues from events held in the facility, including rent from the Cardinals and other users of the facility, concessions, and parking revenues. TSA projects that it will receive approximately $115.2 million from facility-generated revenue through 2031.

Personnel:

A nine-member board of directors, appointed to 5-year terms, governs TSA:

- The Governor appoints five board members, with one member representing the tourism industry, one representing the hotel and motel industry, one representing youth sports organizations, and one representing major league baseball spring training organizations. No more than three of these members may be from the same political party.
- The President of the Senate and the Speaker of the House each appoint two members who cannot both be from the same political party.

As of July 2003, TSA had five staff, including a president/chief executive officer, vice president for facilities, chief financial officer, and two administrative support staff.

Facilities and equipment:

TSA leases office space from a private company. TSA offices are located at 14500 North Northsight Boulevard in Scottsdale. Its equipment includes typical office equipment.

Program goals and performance measures:

TSA has not developed program goals and performance measures, but it is not required to do so since it is not a state agency. While TSA has specific statutory objectives it must meet, such as designing, constructing, and operating a multipurpose facility, and has developed and tracks completion of various action steps, measuring performance could help staff maintain its focus on important TSA functions and activities, enhance service quality, and aid in budget development and review.

SUMMARY

The Office of the Auditor General has conducted a performance audit of the Arizona Tourism and Sports Authority (TSA) pursuant to Arizona Revised Statutes (A.R.S.) §5-812. This statute requires a performance audit no later than 2004 and at least every 5 years thereafter. This audit was conducted under the authority vested in the Auditor General by A.R.S. §41-1279.03.

Established in 2000, TSA is in charge of designing and constructing a multipurpose facility in Glendale, which will be the new home of the Arizona Cardinals football team and Tostito's Fiesta Bowl, and which will host the 2008 Super Bowl. Construction of the facility began in July 2003 and is scheduled for completion during the summer of 2006. TSA also funds tourism promotion, expansion and renovation of Cactus League spring baseball facilities, and youth and amateur sports facilities and programs. TSA's responsibilities pertain only to Maricopa County. TSA's funding comes primarily from two voter-approved taxes in the County—a 1 percent increase in hotel bed taxes and a 3.25 percent rental car surcharge. TSA also receives funding from income taxes collected from the Cardinals' corporate organization, its employees (including players), and their spouses, and it will also receive all sales taxes collected at Cardinals home games and other events held in the new facility.

Multipurpose facility cost at $370.6 million (see pages 15 through 21)

While TSA has taken steps to help protect the public's interest during the construction of the multipurpose facility, the facility's total cost has increased by nearly $40 million from the original estimate. The facility was originally estimated to cost $331 million, but as of January 2004, was projected to cost $370.6 million. Statute does not cap facility construction costs, and as design plans for the facility were largely finalized in January 2004, construction costs increased. Specifically:

- **Design-build agreement established construction price**—In August 2003, TSA entered into a design-build agreement with the facility's contractor, which set a guaranteed maximum price of $346.3 million for the multipurpose facility's construction. At this time, the design plans were not finalized. However, the agreement required the contractor to be responsible for any planned construction costs that exceeded the guaranteed maximum price. As such, the price included $9 million in contingency that the contractor set aside to pay for unexpected cost increases to the planned construction. The Cardinals also committed an additional $9 million in contingency to pay for any new costs associated with upgraded design changes or improvements they request that were not in the facility designs at the time construction began, as well as any other increases in the guaranteed maximum price. Finally, TSA was planning to contribute an additional $6.5 million as part of a lease purchase of some cooling and central plant equipment for the facility. Altogether, the facility cost was budgeted at $361.8 million.

- **Design-build agreement price revised**—As facility design plans were largely finalized in January 2004, the contractor was able to provide more information regarding construction costs. TSA, in conjunction with the Cardinals, decided which features to retain, add, or remove. While some significant changes were made to try to stay within the original budget of $361.8 million, TSA and the Cardinals agreed to retain facility features with the project design at a higher cost or approved other changes. TSA modified the original design-build agreement and increased the guaranteed maximum price to $357.8 million. Additionally, there is nearly $12.9 million in costs for such things as city permit fees, facility testing and inspection, and insurance not included in the design-build agreement, bringing the total project cost to $370.6 million.

TSA has various mechanisms and a budget in place for overseeing construction that, if used properly, can help limit TSA's liability for future cost overruns, and ensure the project is completed on time and with sufficient quality. In collaboration with the Cardinals, TSA is overseeing the facility's construction through an onsite staff member, the use of construction consultants, and through budgeted allowances for facility construction inspections, contingencies, and insurance. The original amount budgeted for contingency was equal to about 5 percent of the original project budget, but the Cardinals and the construction contractor have both used some of their contingencies to cover some of the recent facility cost increases. However, a TSA official stated that with the completion of the facility's design, the risk of further construction cost increases has been significantly reduced.

Review needed of General Fund support for TSA (see pages 23 through 29)

The Legislature may wish to consider revising statute to reduce the burden placed on the General Fund when shortfalls occur in the amount of NFL tax available to TSA. Statute provides that TSA is to receive the greater of (1) all state income taxes paid by Cardinals players and other personnel, their spouses, and the Cardinals' corporation each year; or (2) a guaranteed minimum that was $3.5 million in fiscal year 2002 and rising at 8 percent a year. If NFL income tax collections do not equal the guaranteed minimum amount, additional General Fund monies must make up the difference, irrespective of whether they are needed to sustain TSA operations. By 2031, the minimum amount that must be transferred to TSA, either through actual NFL tax collections or any necessary General Fund subsidy, will increase to nearly $33 million and will continue growing after that as this tax does not expire.

For fiscal years 2003, 2004, and 2005, the NFL tax is expected to be over $2.6 million less than the guaranteed minimum. To comply with the law, TSA will receive this amount in General Fund revenues, although TSA's other revenue is adequate to fund all operations and begin establishing required reserves. Further payments from the General Fund may be needed because in any given year, several factors could negatively affect the amount of NFL tax collected. These factors include year-to-year fluctuations in the Cardinals' salaries, economic downturns that affect corporate and employee earnings, and potential players' strikes or other work stoppages.

The Legislature has several options available to limit or otherwise control General Fund disbursements that may not be necessary to sustain TSA's operations. These include:

- Retaining the statutory minimum amount, but requiring that any NFL tax collections above the minimum be maintained in the General Fund. This would allow the General Fund to collect some additional revenues in years when the NFL tax collections surpass the minimum amount.

- Requiring TSA to place any NFL tax collected in excess of the minimum in a reserve account, and requiring that it be used to cover future shortfalls before requesting any additional General Fund monies.

- Discontinuing the automatic transfer of non-NFL income tax General Fund monies to cover shortfalls in the guaranteed minimum amount. Instead, when shortfalls occur and TSA needs additional funding, it could still request General Fund appropriations from the Legislature. This option would give the Legislature greater discretion in providing funding based on the State's budget, economic conditions, and TSA's needs.

While two of these options would retain the statutory minimum distribution to the TSA, these options could potentially affect TSA's ability to meet its funding obligations. For example, TSA's ability to establish and fund required reserves for operations, repairs, and other long-term costs associated with the multipurpose facility could be affected. Additionally, reduction in or elimination of non-NFL income tax General Fund monies for TSA could affect its ability to adequately fund operations.

Defined processes will help TSA objectively evaluate funding requests (see pages 31 through 37)

Greater specificity in evaluation processes will better enable TSA to objectively evaluate funding requests for youth and amateur sports and Cactus League projects. TSA's decision-making process for committing approximately $5.2 million for three youth and amateur sports projects in 2001 and 2002 was not clearly defined. The three projects chosen are new sports fields at South Mountain YMCA, a regional sports complex in Avondale, and sports fields that will double as overflow parking at the new multipurpose facility in Glendale. However, the Glendale project is on hold until Glendale acquires the land, and TSA and Glendale enter into another agreement that will clarify the city's match and identify the project's total cost.

TSA has since implemented a new process for evaluating future requests to fund youth and amateur sports projects. Under this new process, TSA received and evaluated 92 grant applications requesting over $35.2 million. In February 2004, TSA awarded 13 grants, totaling over $1.3 million to various communities and community organizations in Maricopa County. However, this process can be improved. These improvements include establishing grant administration and oversight requirements; defining how long funded facilities must remain in existence and operational; and further clarifying what costs will be considered for the applicant's local match.

TSA should also develop and implement written guidelines for awarding Cactus League monies to spring training baseball facilities in Maricopa County. As of December 31, 2003, TSA had committed approximately one-quarter of the total estimated $205 million that will be available for Cactus League facilities over 30 years. The guidelines need to address the standards to which facilities will be built or renovated, and the length of the baseball team's lease extension. Guidelines could also help direct decisions about whether to fund new facilities or renovate existing ones. While TSA states that it considers some of these factors already, establishing a more clearly defined set of guidelines would better ensure consistency and fairness in the process.

TSA needs to make several changes to its administrative practices (see pages 39 through 46)

Although TSA is not a state agency and is therefore exempt from some requirements that state agencies must meet, it still should establish administrative policies to provide adequate control and oversight of its functions. Improvements are needed in the following areas:

- **Procurement practices**—Since its inception, TSA has entered into agreements totaling million of dollars in services, but it lacks a defined process for conducting procurements and overseeing its contracts. Although TSA is exempt from the State's procurement code, other exempt or municipal organizations have established their own procurement policies.

- **Attorney use**—Through June 30, 2003, TSA has spent nearly $4.1 million for attorney services. While these attorneys have handled complicated matters, TSA has also used them to draft board meeting minutes and to draft and review relatively simple agreements with consultants, organizations, and TSA staff. To the degree possible, TSA should have its own staff perform such tasks. TSA should also evaluate the need for an in-house attorney to handle routine legal matters and, except for litigation representation, issue requests for proposals for outside legal services in the future.

- **Controls over other expenditures**—TSA should follow its policies and establish some additional procedures to provide greater control over many of its other expenditures, including travel and gifts.

- **Luxury suite and ticket use**—TSA should develop a policy to guide and control the use of the luxury suite and tickets it will receive for all football events in the new multipurpose facility. TSA will have one suite and 16 additional tickets for all football events, including the Tostito's Fiesta Bowl—a valuable resource that requires clear policies to avoid potential misuse.

- **Oversight of tourism promotion expenditures**—TSA should continue to work with the Arizona Office of Tourism to ensure all monies TSA distributes to this agency are used solely to promote tourism in Maricopa County. Auditors reviewed the tourism promotion expenditures for fiscal years 2002 and 2003, and found that the Tourism Office used a small portion of these distributions to promote all of Arizona, rather than Maricopa County as required by statute.

Other pertinent information (see pages 47 through 54)

During the audit, auditors developed information regarding the projected revenue that the Arizona Tourism and Sports Authority expects to receive over the next several years and gathered information related to the funding of the multipurpose facility construction and surrounding infrastructure.

- **Projected revenues**—While TSA's revenues for fiscal years 2002 and 2003 have been sufficient to meet the agency's many funding obligations, future sufficiency is heavily dependent on the growth rate for key revenue sources—particularly for the hotel bed tax and car rental surcharges, the two largest revenue sources.

Thus far, hotel bed taxes have fallen below projections, while car rental surcharges have exceeded projections. Projections prepared to accompany the issuance of TSA's bonds assumed an annual growth rate of 5 percent for the hotel bed tax revenues in fiscal years 2005 through 2011, and for the car rental surcharge revenues in fiscal years 2003 through 2011. While TSA has fully funded its priorities to date, growth rates below 5 percent in the hotel bed tax and car rental surcharge revenues could limit TSA's ability to fund all activities and sustain operations in the future. According to statute, the State is not financially liable or responsible for any of TSA's operations or projects, and therefore, TSA is taking steps to prepare for possible revenue shortfalls. These steps include working to obtain a $3 million line of credit to cover short-term costs when revenue shortfalls occur and creating an operating reserve.

- **Multipurpose facility funding**—TSA, the Arizona Cardinals, and the City of Glendale will each contribute millions of dollars toward the construction of the multipurpose facility and its infrastructure, with TSA paying 72 percent of the anticipated $370.6 million in construction costs. Once the facility is constructed, TSA will own and operate it, and generate revenues from events held there. The Arizona Cardinals will also pay for a significant portion of facility construction costs, but will own the naming rights and receive concessions, advertising, and ticket sales revenues from all Cardinals games held there. The City of Glendale has established a Community Facilities District that will issue bonds to pay Glendale's costs for surrounding infrastructure, and plans to benefit from the economic impact on neighboring businesses and from local sales taxes the facility generates.

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INTRODUCTION & BACKGROUND

The Office of the Auditor General has conducted a performance audit of the Arizona Tourism and Sports Authority (TSA), pursuant to Arizona Revised Statutes (A.R.S.) §5-812. This statute requires a performance audit no later than 2004 and at least every 5 years thereafter. This audit was conducted under the authority vested in the Auditor General by A.R.S. §41-1279.03.

History and responsibilities of TSA

The creation of TSA resulted from the Governor's Stadium Plan "B" Advisory Task Force (task force) established by Governor Jane Hull in 1999. The Governor established this task force following the electoral defeat of an effort by the City of Mesa to finance a new stadium for the Arizona Cardinals. The task force was charged with studying funding options to construct a new football stadium, to prevent the potential economic loss that might occur if the Cardinals relocated to another state, to attract future Super Bowls, and to retain the Tostito's Fiesta Bowl as a participant in the Bowl Championship Series. The Governor directed the task force to research the need for a new stadium, assess potential economic impacts, and devise a possible funding package for stadium construction, but also stipulated that the funding package minimize the impact to the average Arizona resident.

Governor's task force researched stadium financing options.

The task force, comprising 35 of Arizona's business and community leaders, issued its final report in January 2000. The report proposed new tourism taxes and other revenue sources, including a contribution from the Cardinals, to finance a new multipurpose facility. Additionally, the task force believed that other threats to the State's tourism tax base existed, such as competing tourism destinations and the possible loss of Cactus League spring training teams to other states. It concluded that any effort to finance and build a stadium should also include resources to promote tourism in Arizona and protect and expand the Cactus League.

In response to the task force's recommendations, the Legislature established TSA. Legislation establishing TSA largely followed the task force's recommendations, but included some changes. For example, the legislation added youth and amateur sports as one of TSA's funding priorities, increased the Cardinals' minimum required contribution by $10 million to $85 million, and stipulated that the Arizona School Facilities Board certify, after review by the Joint Legislative Budget Committee, that adequate financial resources be in place to bring Arizona's schools up to standards before TSA could begin receiving the new tax revenues. The School Facilities Board provided this certification in May 2001 after Joint Legislative Budget Committee review.

Maricopa County voters approved the creation of TSA in November 2000.

The Legislature established TSA in 2000 as a separate legal body of the State, and Maricopa County voters subsequently approved TSA's creation in the November 2000 election through the passage of Proposition 302. A.R.S. §5-802 establishes TSA as a separate legal body with all of the rights, powers, and immunities of a municipal corporation. Statute also recognizes TSA as a performing governmental function with authority to sue and be sued, to acquire, hold, and dispose of property; to hire attorneys and consultants; and to issue bonds, which according to statute, are its own obligations and not the State's. TSA has the following responsibilities, all of which pertain to Maricopa County:

- Designing and constructing a new multipurpose facility, which will be the new home of the Arizona Cardinals football team and Tostito's Fiesta Bowl, and which will also host the 2008 Super Bowl. The facility is currently under construction in Glendale;
- Distributing monies to the Arizona Office of Tourism for tourism promotion;
- Reviewing, approving, and funding Cactus League baseball facility improvements; and
- Reviewing, approving, and funding grants for youth and amateur sports facilities and programs.

Funding sources

TSA receives funding from a variety of sources. A.R.S. §5-835 requires TSA to maintain a tourism revenue clearing account consisting of monies generated by a hotel bed tax and car rental surcharge. Specifically:

- **Hotel bed tax increase**—TSA receives revenue from a 1 percent increase in Maricopa County's hotel bed tax.[1] The tax began on March 1, 2001, and will continue through February 28, 2031. From the time this tax began until December 31, 2003, TSA had received nearly $26.7 million. TSA expects to receive a total of nearly $610 million from hotel bed taxes through 2031.

1 Hotel bed tax rates vary among cities in Maricopa County. For example, as of August 2003, hotel bed taxes were 12.07 percent in Phoenix and Tempe and 11.67 percent in Scottsdale.

- **Car rental surcharge**—Proposition 302 established a 3.25 percent car rental surcharge in Maricopa County, which also began on March 1, 2001, and expires on February 28, 2031. Prior to the passage of Proposition 302, a flat surcharge of $2.50 per car rental contract existed in Maricopa County. These revenues were distributed to the Maricopa County Stadium District and used to renovate existing and construct new Cactus League baseball facilities. The new 3.25 percent surcharge replaced the $2.50 surcharge, but the Maricopa County Stadium District currently receives the first $2.50 from each rental car surcharge, and TSA receives the remaining portion. Persons who are renting a car can be exempted from paying this tax if the car rental serves as a replacement while their own car is being repaired. From the inception of this tax until December 31, 2003, TSA had received over $19.1 million from the rental car surcharge. Through 2031, TSA projects it will receive over $382 million from this surcharge.

In addition to these tax revenues, A.R.S. §5-834 requires TSA to maintain a facility revenue clearing account consisting of the following revenues:

- **Sales tax recapture**—Beginning in July 2001, TSA recaptured all state sales taxes paid at Cardinals games, including those played at Arizona State University's Sun Devil Stadium, until the new facility is constructed, as well as any sales taxes paid on materials purchased for the construction of the new facility in Glendale. This sales tax recapture does not have an expiration date. As of December 31, 2003, TSA had received over $3.9 million from sales taxes paid at Cardinals games and from sales taxes paid for the new facility's construction. It expects to receive much more from this source once the new facility is completed, and projects receiving approximately $130 million through 2031.

Sales tax recapture and NFL tax revenues do not expire.

- **NFL tax**—TSA received all state income taxes paid by the Cardinals' corporate organization, its employees (including players), and their spouses beginning in July 2001. Specifically, A.R.S. §42-1116(C) requires the State Treasurer to give TSA the greater of the amount collected from the NFL tax or $3.5 million in fiscal year 2002, growing at 8 percent each year. If the tax revenues collected under this category do not meet required minimum amounts, TSA is to receive the remainder from the State General Fund. In fiscal year 2002, the amount of NFL tax distributed to TSA was approximately $915,000 greater than the minimum floor; therefore, no General Fund money was distributed to TSA. However, by the end of fiscal year 2005, over $2.6 million in General Fund money will have gone to TSA because NFL tax collections did not reach the required minimum amounts. As of December 31, 2003, TSA had received over $10.2 million in NFL tax and General Fund monies (see Finding 2, pages 23 through 29).

  The distribution of NFL taxes and General Fund monies to TSA has no expiration date. Given the statutory guarantee, TSA anticipates that this distribution will provide at least $397.8 million from July 2001 through June 2031.

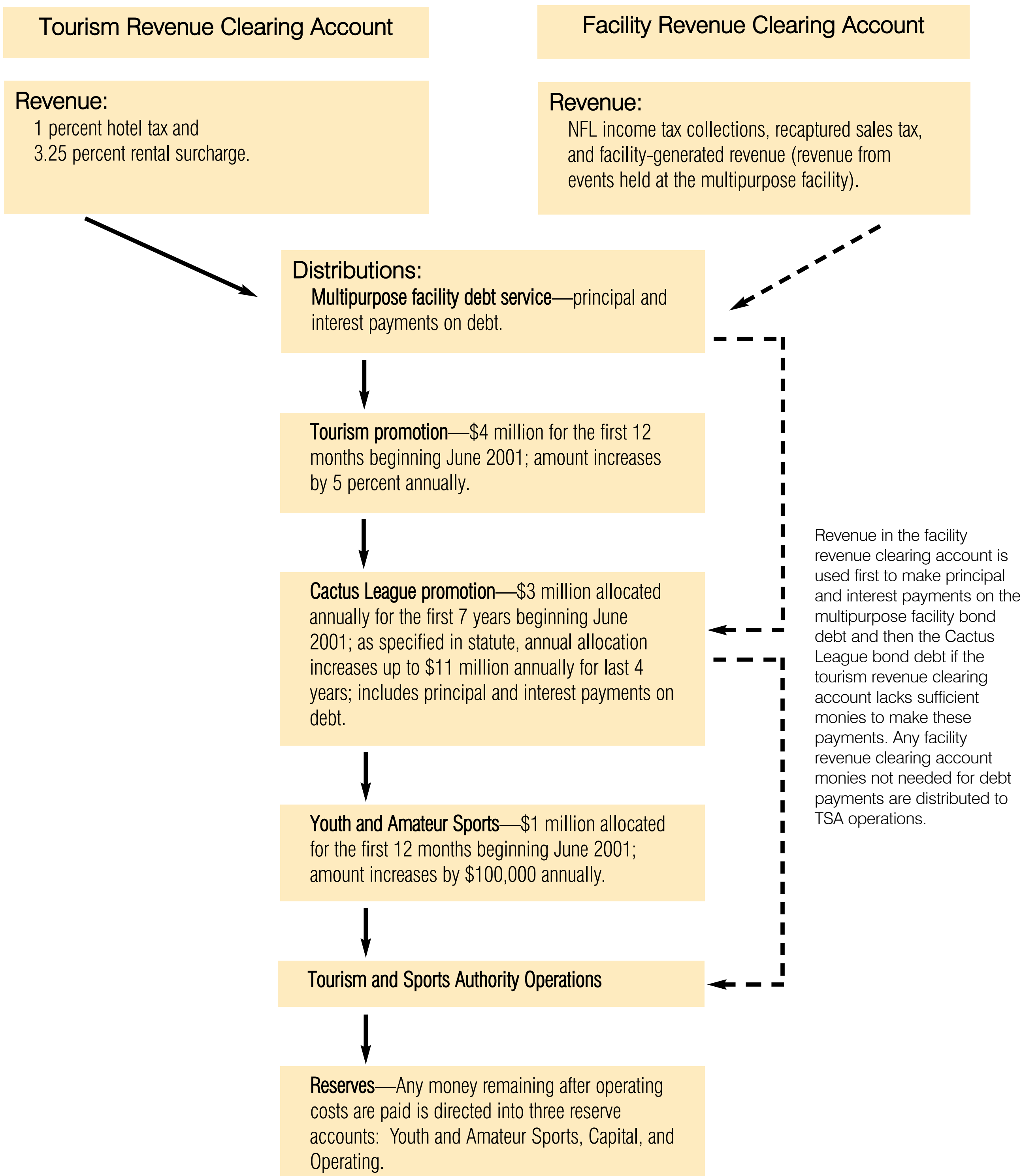
- **Other facility-generated revenue**—Once the facility is constructed and operating, TSA will also generate additional revenues from many of the events held there. According to its agreement with the Cardinals, TSA will receive $250,000 (increasing by 2 percent each year) in rent per year from the Cardinals to play in the facility as long as the Cardinals play there. The Cardinals are contractually obligated to pay this rent for the first 30 years after the stadium opens, at which time the fee can be renewed for up to six 5-year periods. The multipurpose facility will also host the Tostito's Fiesta Bowl, an annual National Collegiate Athletic Association post-season football game, for at least 30 years. Per its agreement with the Fiesta Bowl, TSA will receive $2.50 for each Fiesta Bowl ticket sold for the first game played at the multipurpose facility. This amount increases by $0.20 per ticket annually. Finally, TSA will receive revenue from rent, concessions, and parking from other events it stages at the facility. TSA projects that it will receive approximately $115.2 million from facility-generated revenue through 2031.

TSA's funding priorities

As shown in Figure 1 (see page 5), statute directs the use and distribution of TSA's revenues in its tourism revenue clearing and facility revenue clearing accounts, and specifies that certain projects and priorities cannot be funded until higher priorities are fully funded. While revenues in the tourism clearing account are to be used to fund all of TSA's activities in a specified priority, the use of revenues in the facility revenue clearing account is restricted. Specifically, these revenues are to be used to make principal and interest payments on the multipurpose facility bond debt and the Cactus League bond debt if there are insufficient monies in the tourism revenue clearing account to satisfy these obligations. Additionally, facility revenue clearing account monies help fund TSA operations and establish required reserves. TSA's funding priorities, in order of priority and the amount of funding they receive, are outlined below.

- **Multipurpose facility (facility)**—TSA's first funding priority is to pay existing debt service on bonds it issued to pay its share of the design and construction of a new multipurpose facility. In February 2003, TSA issued $222 million in bonds to finance the majority of its share of facility construction costs. The bonds are due to be retired in 2031. The amount of TSA money dedicated to paying debt service for these bonds will vary during the 29-year period. For example, from fiscal year 2005 through fiscal year 2007, TSA will need approximately $11.1 million per year to make principal and interest payments on the bonds. From fiscal year 2018 through fiscal year 2032, TSA will need approximately $19 million per year to make these payments. In all, total principal and interest payments are projected to cost approximately $457 million. Combined with other facility costs, such as payments TSA made before issuing the bonds, TSA will pay a total of over $500 million for the facility.

Figure 1 Arizona Tourism and Sports Authority
Revenue Distributions in Statutory Priority Order



Source: Auditor General staff analysis of A.R.S. §§5-834 and 5-835.

TSA will own and operate the multipurpose facility.

In addition to TSA's contribution to the costs of facility construction, the Cardinals will share in the facility construction, land acquisition, and infrastructure development costs, while the City of Glendale will be primarily responsible for infrastructure development. TSA will ultimately own and operate the facility, and the Cardinals will be its primary occupant. Currently under construction, the facility will be a 63,000-seat, enclosed, air-conditioned structure with an opening roof and a natural grass playing surface that will roll out of the facility so that the grass may grow in sunlight. TSA states that having a removable field will also make it easier to use the facility for nonsporting events, such as trade shows, conventions, and concerts. However, another feature that would contribute to the facility's multipurpose functionality may not be fully developed when the facility opens. Specifically, over 100,000 square feet that could be developed into meeting space will be undeveloped upon initial occupancy due to budgetary constraints. However, in its facility management and marketing request for proposals, TSA has asked responders to indicate their willingness to fund the build out of some or all of this space. After more than a year of delays related to flight hazard issues associated with the original site in Tempe, a second site selection process, and a lawsuit from a Phoenix area developer, construction began in July 2003 in Glendale. The facility is scheduled to be completed during the summer of 2006 (see Finding 1, pages 15 through 21).

- **Tourism promotion for Maricopa County**—As part of the voter-approved proposition, TSA will distribute monies to the Office of Tourism to promote tourism in Maricopa County. According to A.R.S. §5-835, TSA must distribute $4 million annually, increasing by 5 percent each year. In fiscal year 2002, the Office of Tourism received the entire amount. However, in fiscal year 2003, the Legislature retained $2.2 million for use in balancing the State's budget, which left the Office of Tourism with only $2 million from this source. As of December 2003, nearly $8.6 million had been distributed for tourism promotion, and through 2031, an estimated $264 million will be distributed for tourism promotion.

  The Office of Tourism has established a grants program to award these monies to entities such as convention and visitors' bureaus and cities in Maricopa County. However, the Office of Tourism keeps 5 percent of these monies for its own tourism promotion efforts (see Finding 4, pages 39 through 46).

- **Cactus League baseball**—As outlined in statute, TSA next funds the construction, renovation, marketing, or promotion of new or existing Cactus League baseball spring training facilities in an effort to lure new teams to and/or keep existing teams in Maricopa County. As of December 2003, TSA had distributed $32 million to the City of Surprise to build a new two-team training facility, which brought two new teams from Florida—the Kansas City Royals and the Texas Rangers. TSA had also distributed more than $4.3 million to the City of Phoenix to renovate Phoenix Municipal Stadium, which is the spring training home of the Oakland Athletics. TSA plans to make awards for other training facilities in Maricopa County as leases between the communities and teams expire. For example, the San Francisco Giants' lease at Scottsdale Stadium will expire in 2007. Additionally, in December 2003, the TSA Board adopted a resolution preliminarily approving $20 million in funding for the planned design and construction of a new spring training facility in the City of Goodyear for the Anaheim Angels. However, the resolution also stipulates that TSA must first enter into intergovernmental agreements with the Cities of Tempe and Scottsdale regarding TSA's funding contribution towards those cities' spring training facilities. Further, it stipulates that a suitable replacement team must be identified and committed to a minimum 20-year lease to conduct spring training at Tempe Diablo Stadium.

To assist in financing such projects, in February 2003, TSA issued $32.4 million in uninsured bonds, which are subordinate to both the bonds issued for the multipurpose facility as well as to monies provided for tourism promotion funding. As of December 31, 2003, TSA had distributed over $36.3 million for Cactus League projects, and estimates that a total of $205 million will be spent by 2031 (see Finding 3, pages 31 through 37).

- Youth and amateur sports—After Cactus League baseball, statute requires TSA to fund youth and amateur sports facilities and programs. TSA will grant monies for youth and amateur sports facilities and programs throughout Maricopa County. In 2001 and 2002, TSA committed funding to three projects: the South Mountain YMCA, a sports complex in Avondale, and youth sports fields in Glendale, which will double as overflow parking at the new facility. In February 2004, TSA awarded grants for an additional 13 projects to communities and community organizations in Maricopa County. According to A.R.S. §5-835, youth and amateur sports will initially receive $1 million for the 12-month period beginning June 2001, and this amount will increase by $100,000 each year. As of February 2004, TSA had committed nearly $6.6 million for youth and amateur sports facilities, and estimates that it will allocate $73.5 million through 2031.

- Operations and administration—After funding all of the program areas identified above, remaining tax revenues are available for TSA operations. This includes TSA staff salaries, travel, and insurance, and funding the multipurpose facility's operations. TSA had operating expenses of $1.9 million in fiscal year 2003. TSA expects that its operating costs will remain at this level for fiscal years 2004 and 2005. However, TSA expects its operating costs to grow significantly in fiscal year 2006 to an estimated $5 million and in fiscal year 2007 to an estimated $11.6 million as it prepares to open and becomes responsible for operating the multipurpose facility and expands its staff and other expenses to do so. Information from TSA's audited financial statements is presented in Tables 1 and 2 (see pages 8 and 9).

Table 1: Schedule of Revenues, Expenses, and Changes in Net Assets
Years Ended June 30, 2002 and 2003
(As audited by Ernst & Young, LLP)

	2002	2003
Operating revenues:		
Other	$ 494	
Total operating revenues	494	
Operating expenses:		
Legal	1,390,313	$ 215,666
Arizona tourism distribution	4,033,333	4,235,000
Consulting	763,492	127,450
Payroll	707,331	581,988
Professional fees	568,624	268,875
Marketing and promotion	118,767	106,626
Bank management and service fees	16,537	199,905
Insurance	138,584	102,164
Travel	3,006	11,192
Meetings	9,555	10,901
Office	56,432	30,272
Site selection	172,973	51,626
Communications	38,420	26,549
Rent	93,591	104,981
Depreciation	27,628	31,944
Amortization of deferred bond issue costs		31,032
Total operating expenses	8,138,586	6,136,171
Operating loss	(8,138,092)	(6,136,171)
Nonoperating revenues (expenses):		
Cactus League facility expense	(3,600,000)	(6,765,000)
City of Avondale facility income (expense)	(3,430,820)	820
Hotel bed tax	9,811,027	10,281,047
Rental car tax	6,824,977	7,547,102
NFL income tax	4,420,872	3,784,320
Sales tax recapture	946,394	959,610
Interest income	136,887	869,291
Interest expense	(58,011)	(616,398)
Loss on disposal of property and equipment [1]	(1,114,316)	
Total nonoperating revenues	13,937,010	16,060,792
Net income before contributions	5,798,918	9,924,621
Capital contributions	3,570,523	1,061,189
Increase in net assets	9,369,441	10,985,810
Net assets, beginning of year	(21,946,996)	(12,577,555)
Net assets, end of year	$(12,577,555)	$(1,591,745)

[1] This is primarily for a one-time write-off of the original stadium site in Tempe that was abandoned in November 2001.

Source: Tourism and Sports Authority's audited *Financial Statements* report for the years ended June 30, 2002 and 2003. The statements were audited by Ernst & Young, LLP.

Table 2: Statement of Cash Flows
Years Ended June 30, 2002 and 2003
(As audited by Ernst & Young, LLP)

	2002	2003
Cash flows from operating activities		
Payments to suppliers	$(10,815,568)	$(11,122,751)
Payments to employees	(628,035)	(581,988)
Other receipts	494	
Net cash used in operating activities	(11,443,109)	(11,704,739)
Cash flows from noncapital financing activities		
Payments for Cactus League facilities—City of Surprise	(3,257,197)	(28,742,803)
Payments for Cactus League—City of Phoenix		(4,365,000)
Payments for Youth and Amateur Sports—City of Avondale		(290,404)
Payments for Youth and Amateur Sports—South Mountain YMCA		(150,000)
Receipts from hotel bed tax	9,901,026	10,228,577
Receipts from rental car tax	6,505,525	7,668,222
Receipts from NFL income tax	4,420,872	3,784,320
Receipts from sales tax recapture	948,394	959,610
Interest payments	(39,807)	(135,198)
Net cash (used in) provided by noncapital financing activities	18,478,813	(11,042,676)
Cash flows from capital and related financing activities		
Capital contributions	3,570,523	1,061,189
Proceeds from line of credit	2,000,000	
Payments on line of credit	(3,000,000)	
Proceeds from stadium term loan	8,087,500	
Payments on stadium term loan	(7,000,000)	(5,000,000)
Proceeds from senior and subordinate bonds		255,890,434
Payments for bond issue costs		(448,631)
Payments on capital leases	(11,426)	(12,748)
Acquisition and construction of capital assets	(11,508,610)	(2,285,857)
Net cash provided by (used in) capital and related financing activities	(7,862,013)	249,204,387
Cash flows from investing activities		
Interest received	136,887	698,291
Net cash provided by investing activities	136,887	698,291
Net increase (decrease) in cash and cash equivalents	(689,422)	227,155,263
Cash and cash equivalents at beginning of year	6,264,299	5,574,877
Cash at and cash equivalents at end of year	$ 5,574,877	$232,730,140

Source: Tourism and Sports Authority's audited *Financial Statements* report for the years ended June 30, 2002 and 2003. The statements were audited by Ernst & Young, LLP.

In addition to these funding priorities, statute also requires TSA to establish and fund reserves for its operations, youth and amateur sports, and for repairs and other long-term costs associated with the multipurpose facility. Once these reserves are funded at the minimum amounts required by statute, TSA can use excess monies for early retirement of any outstanding bonds, including the multipurpose facility and Cactus League bonds. Once all bond debt is retired, A.R.S. §5-835 requires TSA to spend 70 percent of its excess monies on Maricopa County tourism promotion and 30 percent of excess monies for further expansion and renovation of Cactus League facilities.

Organization and staffing

TSA is governed by a nine-member board of directors. The Governor appoints five board members, with one member representing the tourism industry, one representing the hotel and motel industry, one representing youth sports organizations, and one representing major league baseball spring training organizations. The President of the Senate and the Speaker of the House each appoint two members who cannot both be from the same political party. All members serve 5-year terms and may be reappointed for one full subsequent term.

As of March 2004, TSA had five staff, including a president/chief executive officer, vice president for facilities, chief financial officer, and two administrative support staff. Additionally, TSA has contracted for various professional services, including legal, engineering, construction management, and public relations. For fiscal year 2004, TSA anticipates adding four full-time positions, including individuals to assist in TSA's marketing efforts for the multipurpose facility, manage and coordinate the youth and amateur sports grant process, and assist with administrative and financial tasks. The fourth position will be a physical plant specialist who will work with the vice president for facilities during the multipurpose facility construction.

Scope and methodology

This audit focused on TSA's efforts to oversee the multipurpose facility construction, how shortfalls in the NFL tax have affected the General Fund, TSA's processes for distributing youth and amateur sports and Cactus League funding, administrative practices, revenue projections, and funding of the multipurpose facility and surrounding infrastructure. This report includes findings in the following four areas:

- The multipurpose facility's cost has increased to $370.6 million. However, TSA has various mechanisms and a budget in place for overseeing construction that, if used properly, can help limit TSA's liability for future cost overruns, and ensure the project is completed on time and with sufficient quality.

- The Legislature may want to consider statutory changes to reduce the burden that a shortfall in one of TSA's revenue sources has placed on the General Fund.

- While TSA has developed a process for awarding grants to youth and amateur sports projects, TSA should further enhance this process and also establish criteria for awarding Cactus League monies to baseball spring training facilities in Maricopa County.

- TSA needs to make several changes to its administrative practices to ensure the most efficient and effective use of its operating funds, and to ensure that all tourism promotion monies it distributes to the Arizona Office of Tourism are used correctly.

This report also includes other pertinent information regarding the projected revenue that TSA expects to receive over the next several years, as well as information related to the funding of the multipurpose facility and surrounding infrastructure by TSA, the Cardinals, and the City of Glendale, and the benefits those parties will receive from the facility.

Auditors used a number of methods to study the issues addressed in this report. They attended three TSA board meetings; interviewed TSA staff and six board members; and reviewed statutes, TSA board meeting minutes from July 2000 to December 2002, and TSA monthly reports from April 2001 through December 2002. Auditors also reviewed documents related to Proposition 302 (2000) and the creation of TSA, such as the final report of the Governor's Stadium Plan "B" Advisory Task Force, the Proposition 302 voter information pamphlet, and legislative meeting minutes. Auditors also used the following methods:

- To determine the costs for constructing the multipurpose facility and the mechanisms TSA has in place to help reduce its liability for future cost overruns and to ensure the quality and timeliness of construction, auditors reviewed project construction documents, including the project management agreement and TSA's construction agreement with the contractor and the Cardinals, as well as TSA's facility agreements with the Arizona Cardinals and the City of Glendale. Auditors also interviewed TSA's primary construction consultant, a representative of the Department of Administration who specializes in government construction projects, and representatives of similar sports-related authorities in five states that have recently constructed football stadiums.[1] Auditors also researched the design-build method of construction by interviewing the director of the Alliance for Construction Excellence at Arizona State University's Del E. Webb School of Construction and reviewing information from the Design-Build Institute of America's Web site.

1 Auditors contacted sports authorities in Colorado, Florida, Michigan, Texas, and Washington.

- To determine the effect of potential shortfalls in NFL tax collections on the General Fund, auditors analyzed NFL tax collection and distribution information from the Department of Revenue and the State Treasurer's Office, and a National Football League Players Association report on salary information for NFL teams, including the Arizona Cardinals.[1] Auditors also reviewed the official statements for TSA multipurpose facility bonds and a Court of Appeals ruling in a lawsuit against TSA. Finally, auditors interviewed TSA consultants who were involved in the NFL tax revenue projections, as well as the company that insured the multipurpose facility bonds.

- To evaluate TSA's processes for awarding youth and amateur sports and Cactus League funding, auditors observed two meetings of the Youth and Amateur Sports Advisory Committee, one meeting of the Committee's Grant Process subcommittee, TSA's youth and amateur sports summit meeting in February 2003, and the TSA youth and amateur sports town hall meeting held in Peoria in April 2003. Auditors also reviewed the 26 youth and amateur sports funding requests received in calendar year 2001, TSA's funding agreements with the City of Avondale and South Mountain YMCA, TSA's multipurpose facility development agreement with the City of Glendale, the Arizona Cardinals' original and restated agreements with Glendale, and the grant process developed by the Youth and Amateur Sports Advisory Committee. Auditors also obtained and reviewed granting criteria from the Arizona Commission on the Arts, the Arizona State Parks Local, Regional and State Parks Heritage Fund program, and the Maricopa County Stadium District. Finally, auditors interviewed TSA's youth and amateur sports consultant.

- To assess TSA's administrative practices, auditors reviewed contract documentation for 14 TSA vendors, 15 billing statements for attorneys who TSA used, and documentation related to the Attorney General's process for securing outside legal counsel services. Auditors also interviewed officials at the Attorney General's Office and State Procurement Office. Additionally, auditors reviewed TSA travel and credit card documentation, and TSA's financial internal controls. Further, auditors reviewed the portions of TSA's agreements with the Arizona Cardinals and the Fiesta Bowl related to the luxury suite and tickets it will receive in the new multipurpose facility, and reviewed the Maricopa County Stadium District's agreement with two nonprofit organizations for the use of its suite for all Diamondbacks baseball games played in Bank One Ballpark. Finally, auditors reviewed statutes related to the manner in which tourism promotions monies must be spent, and reviewed advertisements the Arizona Office of Tourism placed using these monies.

- To develop information on TSA's revenue projections, auditors reviewed and analyzed revenue projections developed by the Governor's Stadium Plan "B" Advisory Task Force and by TSA for the voters' pamphlet and multipurpose

1 Duberstein, M.J., NFL Economics Primer 2002, National Football League Players Association, www.nflpa.org, April 2002.

facility bonds. In the absence of supporting documentation for these projections, auditors interviewed TSA consultants who helped TSA develop these projections.

- To develop information on the shared multipurpose facility costs and benefits, auditors reviewed TSA's facility agreements with the Arizona Cardinals and the City of Glendale, the Cardinals' original and restated agreements with the City of Glendale, project construction documents, including the project management agreement and TSA's construction agreement with the contractor and the Cardinals, and the Arizona Cardinals agreement with Arizona State University. Auditors also interviewed an official with the Glendale City Attorney's office.

This audit was conducted in accordance with government auditing standards.

The Auditor General and staff express appreciation to the Arizona Tourism and Sports Authority Board of Directors, the president/CEO, and staff for their cooperation and assistance throughout the audit.

FINDING 1

Multipurpose facility cost at $370.6 million

While TSA has undertaken steps to help protect the public's interest during construction of the multipurpose facility, the facility's estimated cost has increased to $370.6 million. The facility was originally estimated to cost $331 million, but by the time design plans were largely finalized in January 2004, the facility cost increased to nearly $40 million more than the original estimate. However, various mechanisms are in place that, if used properly, should limit TSA's liability for future cost overruns. Additionally, in collaboration with the Cardinals, TSA is overseeing the facility's construction through an onsite staff member, the use of construction consultants, and through budgeted allowances for facility inspections, contingencies, and insurance.

Artist's rendering of multipurpose facility.

Source: Arizona Tourism and Sports Authority.

Facility cost has increased, but various mechanisms should help limit TSA's liability for future cost overruns

Statutes do not cap the facility's cost, and the facility's overall expected cost has increased; however, if used properly, TSA's agreements with the construction contractor and the Cardinals should help limit TSA's responsibility for future cost overruns. When voters approved Proposition 302, the facility was estimated to cost $331 million, but as the design plans were largely finalized in January 2004, the total facility cost increased to $370.6 million. However, if used properly, TSA's use of the design-build method of construction as well its agreement with the Cardinals that requires the Cardinals to pay for facility changes that they request should help limit TSA's liability for future cost overruns. Further, the amount of funding TSA can contribute is limited by TSA's ability to sell additional bonds.

Statute does not cap the cost of the multipurpose facility.

Statutes do not limit the facility's cost—Although the voter publicity pamphlet for Proposition 302 stated that "the cost of the facility is anticipated to be approximately, but not in excess of $331 million," statutes do not place a cap on the cost. In January 2004, 6 months into the facility's construction, the design plans were largely finalized and the facility is now estimated to cost approximately $370.6 million. Of this amount, TSA plans to contribute approximately $266.6 million and the Cardinals will pay approximately $104 million, although statutorily the Cardinals are required to contribute only $85 million. Statutes allow TSA to issue bonds in whatever amounts it deems necessary, and TSA can also use monies left over after fully funding other priorities to help pay the cost.[1] TSA officials have stated that the cost listed in the voters' pamphlet was only an estimate, and that is was not possible to have a more accurate cost estimate because no detailed plans existed at that time.

Facility cost has increased—In August 2003, TSA entered into a design-build agreement with the contractor, which set a guaranteed maximum price of $346.3 million for the multipurpose facility's construction. At the time this agreement was entered into, the design plans were not finalized. However, the agreement required the contractor to be responsible for any planned construction costs that exceeded that amount. As such, included in this price was $9 million that the contractor set aside, referred to as contractor contingency, to pay for unexpected cost increases during construction. Unexpected costs could include delays due to design flaws or items either not budgeted or budgeted too low by the contractor.

The Cardinals also committed an additional $9 million in contingency to pay for items not included in the agreed upon scope of the project, but necessary to complete the project, or for potential facility upgrades that may be requested to the approved design. TSA also planned to contribute approximately $6.5 million as part of a lease purchase of some cooling and central plant equipment for the facility. This actually brought the overall construction budget for the facility to $361.8 million.

The multipurpose facility construction cost is now estimated at $370.6 million.

However, total project costs have increased to approximately $370.6 million. Specifically, as the design plans were largely finalized in January 2004, the contractor was able to provide more information regarding the facility construction costs. TSA, in conjunction with the Cardinals, decided which features it wanted to retain, add, or remove. While some significant changes were made to try to stay within the original construction budget, TSA and the Cardinals agreed to retain facility features within the project design at a higher cost or approved other changes. For example, the roof opening will now be smaller and simpler than originally planned; however, TSA has added plans for a utility grid in the floor of the facility intended to make it easier to host nonsporting events such as trade shows, conventions, and concerts. Once these changes were finalized, TSA modified the original design-build agreement with the contractor and set a new guaranteed maximum price of $357.8 million.

1 A.R.S. §5-835(B)(1) refers to a facility cost of $331 million, but this sets the limit for only the amount of hotel tax and car rental tax revenue that is designated to service the debt. That amount is one-half of $331 million paid over 30 years, but TSA will have revenue from other sources, such as the sales tax recapture or the NFL tax, that it can contribute to the facility's cost.

In addition to the $357.8 million in construction costs, there is nearly $12.9 million in costs for such things as city permit fees, facility testing and inspection, and insurance. This amount also includes over $3.2 million of the Cardinals original $9 million in contingency monies that remain available for use in the project. As a result, total project costs are now estimated at approximately $370.6 million.

The total project cost has increased $8.8 million from August 2003 to January 2004. TSA will pay $7.8 million of this increase and the Cardinals are paying $1 million of it. TSA also required the contractor to reduce its fees by $500,000 and use over $5.1 million of the contingency it set aside under the original agreement to help prevent a further increase in construction costs.

TSA using design-build method for construction—Design-build construction agreements enable an owner to enter a contract with one "designer-builder" who then coordinates with architects, consultants, and other subcontractors, and acts as a single point of contact for the owner. This allows the owner to interact with and oversee just one entity who is accountable for all aspects of the project, including keeping it within budget. Generally, design-build projects also include a guaranteed maximum price or lump-sum amount and require the contractor to cover any cost overruns not included in the scope of the contracted work. This type of arrangement can be especially helpful to ownership entities with small staffs and limited resources to oversee large-scale projects such as the multipurpose facility because the contractor handles day-to-day project administration. Also, with contractor involvement in both design and construction, project design changes and associated costs can be better managed. Finally, projects can often avoid delays that occur with other types of construction when the owner must manage separate contracts and possible disputes between the architect and the contractor.

Design-Build Construction

A construction method in which the owner, such as the TSA, enters into a single contract with a design-builder entity to provide architectural, engineering, design, and construction services. This provides for a more simple construction process for the owner. Guaranteed construction costs are also known earlier than other construction methods, while total design and construction time can be significantly reduced.

Source: Design-Build Institute of America, www.dbia.org.

Cardinals responsible for added costs through project management agreement—While the contractor is required to pay for construction cost overruns, the project management agreement between TSA and the Cardinals requires the team to pay for all other cost increases. If project savings are not available, the Cardinals must pay for design changes they request that upgrade or otherwise improve upon the originally agreed-upon design and that increase the project budget. Some design changes are possible during construction that were not in the original plans with the guaranteed maximum price. For example, as the facility is nearly completed, the Cardinals could decide that they want to upgrade locker room or press box facilities. Additionally, if for some reason the guaranteed maximum price must be increased further during construction and the increased costs are not the responsibility of the contractor or TSA, and TSA does not have excess monies to contribute, the Cardinals would be required to cover the full amount of that increase.

The Arizona Cardinals must pay for upgrades or improvements they request to facility design.

TSA has limited ability to contribute additional funding—Even though TSA will contribute additional monies to cover most of the January 2004 cost increase for facility construction, it will be limited in its ability to further contribute funding to the project. TSA has identified additional funding sources that it has designated to cover the majority of the facility's cost increase. This includes additional sales tax recapture revenues from the increased facility construction costs and facility infrastructure development, additional monies that TSA will make available through its planned lease purchase of some cooling and central plant equipment for the facility, and contingency monies that TSA will receive from the City of Glendale related to the City's construction of a pedestrian plaza.

However, further TSA contributions may be limited. First, when TSA issued facility construction bonds in February 2003, it issued the maximum amount of bonds it could while still receiving the highest bond rating. These bonds received a AAA rating because they are fully insured, meaning bond investors are guaranteed a specified rate of return and return of their principal investment. While TSA can issue additional bonds, according to its project management agreement with the Cardinals, these bonds must also be insured. According to a TSA official, given its many funding obligations, including making principal and interest payments on its facility bonds, TSA will not have the ability to issue additional insured bonds until at least 2008. Facility construction is scheduled for completion in 2006. Additionally, TSA cannot contribute more monies from its various revenue streams until it fully funds all of its other obligations.

Procedures and budget in place for overseeing facility construction

TSA has processes and a budget in place to oversee the construction of the facility to help ensure that the project is completed on time, within budget, and with sufficient quality. TSA is collaborating oversight of the project with the Cardinals, and is using a qualified staff member and several construction consultants to help oversee daily progress. Additionally, as part of the overall cost of constructing the facility, TSA established budgets for insurance and construction contingencies. However, some of the contingency has already been used to help offset the January 2004 facility construction cost increases.

TSA collaborating on construction oversight with the Cardinals—Because both TSA and the Cardinals are contributing significantly to the cost of the facility and have substantial interests in construction costs and quality, both are involved in oversight. Both have designated representatives for construction matters who are onsite and have unlimited access to the facility during construction. TSA's vice president for facilities has 25 years of design and construction oversight experience, including experience overseeing large-scale municipal projects, and represents TSA's interest during construction. In September 2003, the contractor began to provide TSA and the Cardinals with monthly reports that summarize construction progress and the costs being incurred. These reports also provide information on the procurement of materials and subcontractor services, the quality control and testing inspections conducted, updated schedule information, and a cost management section that includes the contractor's application for payment and an associated payment schedule. The TSA and Cardinals' representatives also meet twice a month with representatives of the contractor to review construction progress and to discuss potential solutions to problems that arise. Finally, TSA's executive director and board members with expertise in construction meet periodically to receive updates from TSA staff and consultants on construction progress.

The contractor is providing monthly construction reports.

Consultants to help oversee facility construction—To assist in construction oversight, TSA and the Cardinals have set aside $3.1 million of the construction budget, and TSA has set aside additional monies for the use of consultants. Specifically, the project is using testing consultants to help ensure that the project is carried out with proper building techniques. For example, TSA has retained a consultant that is performing stress tests on samples of concrete used during facility construction to ensure that they were poured correctly and that the proper-strength grade of concrete was used.

TSA also contracted with a recently retired division president of one of the United States' largest construction firms to assist in reviewing project designs and developing the design-build agreement. This consultant is also helping to oversee construction. Before working for TSA, the principal construction consultant oversaw large-scale construction projects, such as Sky Harbor Airport's Terminal 4 and the new Arizona State Hospital that was completed in 2003. Finally, TSA is in the process of identifying a qualified firm to provide construction auditing services. Services provided by a construction auditor would include periodically reviewing billing statements to ensure that a proper amount was charged for the type of work and materials used.

Facility budget includes money for contingency and insurance—In addition to budgeting for the use of construction consultants, monies have been set aside for construction contingencies and insurance.

- **Contingency budget**—At the start of facility construction in July 2003, the original $361.8 million facility construction budget included a total of $18 million to cover unexpected construction costs. This amount included $9 million in the design-build agreement with the contractor to cover cost overruns, and the $9 million that the Cardinals would control for facility upgrades. However, after approximately 6 months into construction, both contingencies have been significantly reduced to help prevent further cost increases. Specifically:

- **Contractor contingency**—Included in the original $346.3 million guaranteed maximum price was $9 million in contractor contingency to pay for unexpected cost increases during construction. Unexpected costs could include delays due to design flaws or items either not budgeted or budgeted too low by the contractor. As mentioned previously, during the first 6 months of construction and while facility design plans were finalized, cost increases did occur, resulting in the guaranteed maximum price increasing to $357.8 million. To help retain as much of the facility design as possible, over $5.1 million in contractor contingency was used, reducing the remaining available amount to approximately $3.9 million as of January 2004. Should the project be completed under the guaranteed maximum price of $357.8 million, the contractor will keep 25 percent of the amount saved. This acts as an incentive to help reduce costs.

- **Cardinals' contingency**—As mentioned previously, separate from the $346.3 million was an additional $9 million in contingency that is part of the Cardinals' contribution. This was to be used for change orders to the construction plans, which the Cardinals controlled, or for any costs arising from upgrades or improvements to the facility or increases in the guaranteed maximum price. The Cardinals agreed to commit approximately $5.8 million of their contingency to help pay for the recent construction cost increases. Because the Cardinals are paying more than is required by law, the Cardinals will keep any unused portion of their contingency.

The $18 million originally budgeted for contingency was equal to about 5 percent of the original project budget and appeared to be in-line with amounts recommended by the Arizona Department of Administration (DOA) and other recent stadium construction projects in the U.S. According to DOA, state government construction projects should reserve approximately 5 percent of the overall budget for contingencies. Additionally, according to representatives of five authorities who constructed football stadiums since 1998, contingency budgets for their projects ranged from approximately 3 percent to approximately 6 percent of the total stadium project budgets.[1] However, because much of the monies set-aside for contingency has been used for construction cost increases as of January 2004, the remaining contingency budget represents only 1.9 percent of the total project cost. The budgeted contingency has been reduced by over 60 percent; however, according to a board official, since the facility's design has mostly been completed, the risk of further construction cost increases has been significantly reduced.

1 Auditors contacted officials from organizations that built National Football League stadiums in Denver, Detroit, Houston, Seattle, and Tampa.

- **Insurance budget and coverage**—The facility project costs include approximately $12.5 million for insurance coverage to cover costs that may arise from construction errors, catastrophic damage, and other liabilities during construction. TSA established this amount in consultation with the contractor's insurance broker, TSA's chief construction consultant, and an insurance company that has insured various stadium projects, and the Cardinals. The following insurance coverages have been obtained:

  - **Errors and omissions**—This type of insurance covers any losses due to architectural design inadequacies or construction errors. The contractor has obtained $50 million in coverage at a cost of nearly $4.1 million.

  - **Builders' risk**—This insurance covers the complete value of the facility in case of catastrophic damage due to fire and other natural disasters. TSA has obtained builders' risk insurance at a cost of $1.56 million. This insurance does not cover losses due to mold growth or terrorism.

  - **General liability**—The contractor has also obtained insurance to cover its liability in general areas such as workers' compensation, auto insurance, and other damage to property or materials related to construction. Primary coverage limits for bodily injury, including death resulting from injury, and property damage are $2 million per occurrence with an annual maximum of $4 million. Premiums for these insurance coverages cost $6.84 million. Included in this insurance coverage is an umbrella liability policy for $50 million.

Recommendation

This finding presents information only. Therefore, no recommendations are presented.

FINDING 2

Review needed of General Fund support for TSA

The Legislature may wish to consider revising statute to reduce the burden placed on the General Fund when shortfalls occur in the amount of NFL tax available to TSA. The NFL tax consists of all state income taxes paid by the Cardinals' corporate organization, its employees (including players), and their spouses. Statute guarantees a minimum amount that TSA will receive from the tax and provides for additional General Fund monies to make up any shortfalls. By the end of fiscal year 2005, TSA will have received over $2.6 million in additional General Fund monies, and such distributions may also be needed in future years. Several options exist for modifying the current statutory requirement.

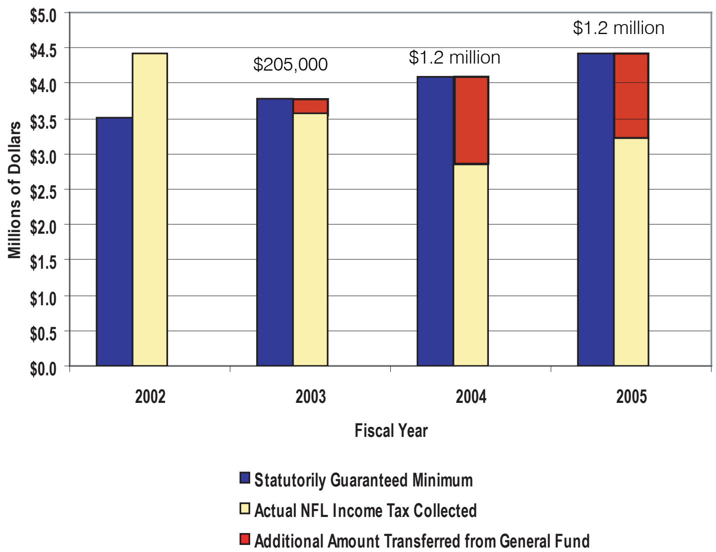
TSA receiving General Fund monies

The General Fund has already provided monies to TSA that do not include NFL income tax collections and may need to provide additional funding in the future if NFL tax collections continue to fall short of the required minimum amount. Under current statute, TSA receives these General Fund monies, even if the TSA has excess revenues from other sources and does not need these additional General Fund monies to sustain operations.

TSA receives General Fund monies—While TSA activities are projected to generate revenue for the General Fund, statute requires that TSA receive a minimum amount in NFL tax collections each year. If there are shortfalls in NFL tax collections, additional General Fund monies must make up the difference. Specifically, TSA was to receive a minimum of approximately $3.5 million in NFL tax revenues for fiscal year 2002. This amount increases by 8 percent each year, and this statutory requirement does not have an end date. If NFL tax collections are greater than the minimum amount, TSA receives the full amount collected. When the NFL tax collections are less than the minimum amount, TSA receives the NFL tax collected and additional General Fund monies necessary to total the minimum amount required by statute. Each fiscal year, the State Treasurer transfers to TSA prior calendar year income tax collected or the required minimum distribution.[1]

1 Each month, the State Treasurer remits one-twelfth of the total amount to be distributed to TSA during the fiscal year.

Figure 2 Statutorily Guaranteed Minimum Distribution Compared To Actual NFL Income Taxes Collected Fiscal Years 2002 through 2005



Source: Auditor General staff analysis of A.R.S. §§42-1116(C) and 43-209(C), and information provided by the Arizona State Treasurer.

Although NFL tax collections exceeded the required minimum amount to be distributed in fiscal year 2002 by more than $915,000, collections in subsequent years fell short of the statutory minimum by more than $2.6 million, and additional money has had to be paid from the General Fund to ensure that TSA receives the minimum amount prescribed by statute. As shown in Figure 2, the General Fund made up the difference to TSA during fiscal years 2003 and 2004 because NFL tax collections did not meet the required minimum amounts. Specifically, the NFL income taxes collected for fiscal year 2003 fell short of the statutory minimum by $205,376. The NFL income taxes collected for fiscal year 2004 fell short of the minimum by more than $1.2 million, while in fiscal year 2005, another nearly $1.2 million in additional tax General Fund monies may be needed to make up a shortfall. For fiscal year 2006, the NFL tax collections must increase by nearly 48 percent over the actual collections of the prior year, or additional General Fund monies will again have to make up the shortfall.

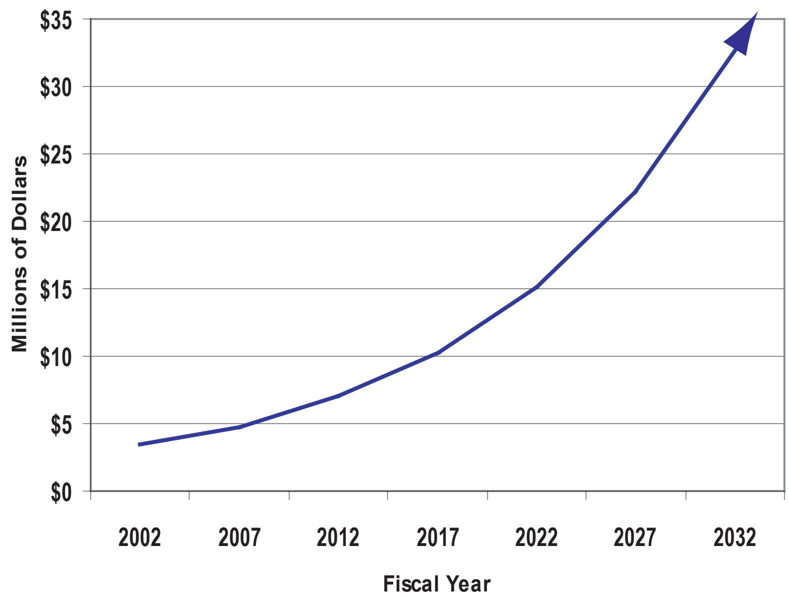
General Fund will contribute more than $1.2 million in additional monies to TSA in fiscal year 2004.

TSA receives additional General Fund monies while establishing reserves—TSA receives monies from the General Fund even during fiscal years when TSA's revenues from all sources are greater than distributions. As required by statute, monthly revenues in excess of distributions are deposited in TSA's operating reserve. Statute requires TSA to establish and fund reserves for its operations, youth and amateur sports, and for repairs and other long-term costs associated with the multipurpose facility. TSA must also establish reserves for its Cactus League bonds. However, as of the end of fiscal year 2003, TSA had fully funded the youth and amateur sports reserve and had begun to fund its Cactus League bond reserves. Additionally, in fiscal year 2004, the General Fund will contribute more than $1.2 million in non-NFL income tax monies to TSA to meet the statutory minimum amount, although TSA had established an operating reserve of over $2.5 million at the end of fiscal year 2003.

Statute's minimum amount represents a future liability

This liability to the General Fund could increase significantly in the future. As shown in Figure 3 (see page 25), the minimum guaranteed amount that TSA will receive from a combination of the NFL tax and additional General Fund coverage of shortfalls increases from $3.5 million in fiscal year 2002 to nearly $33 million in 2031, and continues to grow by 8 percent each year thereafter. As the minimum amount required to be distributed to TSA increases, so does the potential for future additional

Figure 3 Statutorily Guaranteed Minimum NFL Income Tax/General Fund Distribution Fiscal Year 2002 and Beyond



Source: Auditor General staff analysis of A.R.S. §42-1116(C).

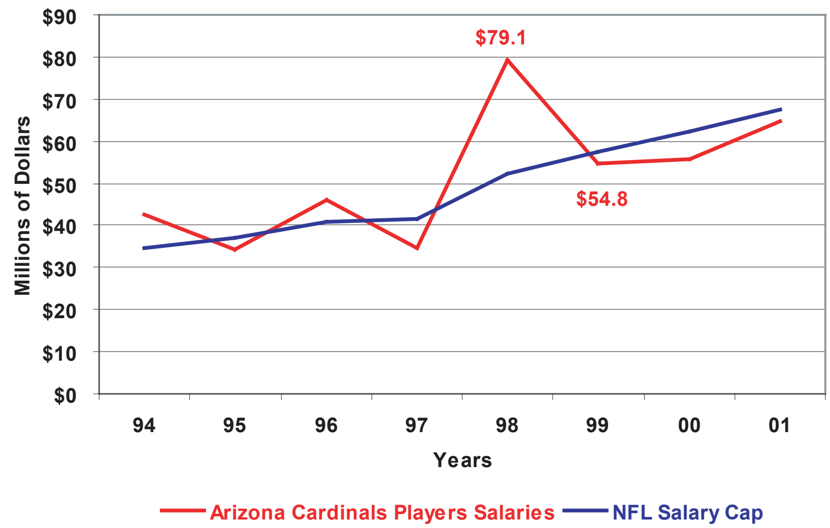
transfers of General Fund monies. In a given year, several factors could affect the amount of monies the General Fund must transfer to TSA.

NFL tax collections are affected by the Cardinals' total payroll.

- **Arizona Cardinals players' salaries fluctuate too much to project 8 percent annual growth**—Arizona Cardinals players' salaries have historically fluctuated annually, and such fluctuation makes it difficult to project growth. When reviewing salary (salaries and bonus) information for the Arizona Cardinals players from 1994 to 2001, auditors found that the Cardinals' organization total player salaries fluctuated significantly until 1999, as illustrated in Figure 4 (see page 26). For example, in 1998, salaries grew by 129 percent over the previous year, while in 1999, the total salaries dropped by 31 percent from the previous year. However, in 2000 salaries increased by about 1.5 percent, and in 2001, salaries increased by more than 15.5 percent, for an average increase of 8.5 percent.

  Governor's Stadium Plan "B" Advisory Task Force consultants who assisted in developing the amount of revenue that the TSA would receive from the NFL tax

Figure 4 Arizona Cardinals' Players Total Annual Salary Compared To NFL Salary Cap Calendar Years 1994 through 2001



Source: Auditor General staff analysis of the *NFL Economic Primer 2002* report prepared by the National Football League Players Association.

used 8 percent growth as a basis for annual growth. However, the rate was not based on actual Cardinals' salaries and other income, but on growth rates in the NFL salary cap, which follows a more linear upward trend than Cardinals' salaries. Since Cardinals' salaries have not exhibited consistent growth, in years when the Cardinals' salaries decline from previous levels or do not meet a projected growth target, the State Treasurer may need to transfer additional monies from the General Fund to ensure the TSA receives the required minimum distribution.

NFL tax shortfalls could coincide with state budget shortfalls.

- Economic downturn—The NFL tax collection is affected not only by players' salaries, but also by the negative impact of economic downturns on the income tax collected from the Cardinals' organization, its employees, and their spouses. The income taxes paid from these sources can decrease during economic downturns, and TSA officials have speculated that NFL income tax collections have been lower than expected because the recent economic downturn has affected employees' other income, such as from investments. However, economic downturns also negatively affect the General Fund due to the decrease in income tax collections. Therefore, the State could be contributing monies to TSA at the same time it is facing budget difficulties, as has been the case in fiscal years 2003 and 2004.

- **Work stoppages or loss of Cardinals**—The statutory minimum amount as currently outlined in statute is guaranteed, regardless of the reasons for lower-than-anticipated revenues. For example, the General Fund obligation could potentially be significantly and negatively affected by an NFL work stoppage, or if the Cardinals were to move to another state. The NFL's last work stoppage happened in 1987, and its current labor agreement expires in 2007. Additionally, although the Cardinals have strong incentives not to leave town because of a requirement to pay off the balance of bond debt if they do so before 2031, this possibility exists. In any case, the statutorily guaranteed minimum amount that is transferred to TSA is supported by General Fund monies when necessary and does not expire—even if the Cardinals decide to leave town before 2031.

Despite these reasons for potential continued payments from the General Fund to TSA, TSA officials expect NFL tax collection revenues to increase, thereby minimizing the amount of additional General Fund monies needed to reach the statutory minimum amount. Specifically, according to a TSA representative, the new facility in Glendale will generate additional income for the Cardinals, and in turn, the Cardinals will likely pay more in player salaries. As both the Cardinals' corporate earnings and the players' salaries increase, they will pay more in income tax, which will be turned over to TSA in the form of the NFL tax.

Legislature could explore options to limit additional General Fund contributions

The Legislature could explore several options to potentially limit or otherwise control General Fund disbursements consisting of non-NFL income tax monies that may not be necessary to sustain TSA operations. Specifically, the Legislature could consider three options or a combination of these options:

- **General Fund could keep excess revenues**—The Legislature could amend A.R.S. §42-1116(C) to require NFL income tax collections in excess of the minimum to be deposited into the General Fund, while retaining provisions for General Fund contributions to TSA to cover NFL tax shortfalls. Under this option, TSA would continue to receive the minimum amount, which increases by 8 percent annually, but would not receive any NFL tax collected that is above the minimum amount. This option would allow the General Fund to collect some additional revenues in years when the NFL tax collections surpass the minimum amount. However, as previously mentioned, there is the potential that NFL tax collections will continue to fall short of the required minimum amount.

- **Require TSA to establish an NFL tax reserve**—The Legislature could amend A.R.S. §42-1116(C) to require TSA to hold NFL tax revenues that exceed the statutory minimum amount in a separate account for use during years that NFL tax collections do not meet the required minimum amount. Then, the Legislature could require that monies from this newly created reserve account be used to cover any NFL tax shortfalls before TSA would receive additional monies from the General Fund. TSA could also be allowed to use these monies during periods when other revenue sources fall short of projections and TSA has difficulty meeting operating expenses (see Other Pertinent Information, pages 47 through 54). Under this option, after the reserve funds are exhausted, the Legislature could either continue to fund shortfalls in NFL income tax revenues automatically, or require TSA to ask the Legislature to cover the remaining shortfall.

- **Restrict distribution to actual NFL tax collections**—The Legislature could amend A.R.S. §42-1116(C) to restrict the TSA distribution to only the actual NFL income tax collections, and eliminate the requirement for a minimum distribution amount, annual growth, and additional General Fund contributions. Under this option, TSA would no longer be guaranteed a minimum amount, but would still receive actual NFL tax collections. The General Fund would no longer be obligated to cover a revenue shortfall if NFL tax collections were insufficient to meet a required minimum amount. However, TSA would still have the option of requesting additional funding through specific legislation. This would give the Legislature the discretion to provide funding based on the State's budget, economic conditions, and TSA's needs.

While two of these options would retain the statutory minimum distribution to the TSA, these options could potentially affect TSA's ability to meet its funding obligations. This could include TSA's ability to establish and fund required reserves for operations and repairs, and other long-term costs associated with the multipurpose facility. Reduction in or elimination of the additional General Fund monies for TSA could also affect its ability to adequately fund current operations. The statutorily established minimum amount that TSA is to receive from NFL income tax collections represents its only guaranteed level of funding. Should revenues from its other sources of funding fall short of projections and thus affect its ability to make required bond debt payments and distribute required monies to its other funding priorities, such as youth and amateur sports and the Cactus League, TSA could use monies received from the NFL tax to assist in meeting these obligations.

If it so decides, the Legislature could amend statute, since there are no legal or other circumstances that would limit its ability to do so. Specifically, the Legislature is not limited by the following:

- **Proposition 105**—A constitutional amendment approved in 1998 limited the Legislature's ability to alter voter-approved initiatives or referendums. However, when Maricopa County voters approved Proposition 302 in November 2000, they approved an additional hotel tax and a car rental surcharge, but not

General Fund contributions. The NFL tax was not part of the referendum authorizing the car rental surcharge and the hotel tax to fund a new facility, but rather was part of a legislative bill. Therefore, Proposition 105 does not apply and does not affect the Legislature's ability to change statute.

- **General Fund monies not pledged to bonds**—TSA's issuance of tax revenue bonds does not limit the Legislature's ability to amend statute. In fact, the official statement of the revenue bonds notifies bond buyers that the statute providing for General Fund subsidy of the NFL tax shortfall may be reduced or eliminated by the Legislature. Due to a 2002 Court of Appeals ruling, the TSA cannot pledge or guarantee General Fund monies for payment of tax revenue bonds.

Recommendations

1. The Legislature may want to consider amending A.R.S. §42-1116(C) to implement one of the following options to help minimize the impact that continued NFL tax collection shortfalls could have on the General Fund:

    - Require the State Treasurer to distribute only the required minimum amount in tax collections and maintain any excess NFL tax collections in the General Fund to offset the disbursement of additional General Fund monies to cover the NFL tax shortfall in other years;
    - Require TSA to deposit monies in excess of the minimum NFL tax collections amount in a separate reserve account to be used during years when NFL tax collections are less than the required minimum amount. Then, only after monies in that account have been used, additional General Fund monies would be distributed to TSA, or TSA could be required to request any needed monies; or
    - Remove the requirement that the State Treasurer distribute additional General Fund monies to TSA in the event that NFL tax collections do not meet the required minimum amount and instead require TSA to request any needed monies through specific legislation.

FINDING 3

Defined processes will help TSA objectively evaluate funding requests

Greater specificity in evaluation processes will better enable TSA to objectively evaluate funding requests for youth and amateur sports and Cactus League projects. TSA lacked a clear process when it initially awarded more than $5.2 million toward youth and amateur sports projects, and for one of the three projects chosen, there are uncertainties about total project costs and the availability of sufficient matching monies from the local sponsor. Since that time, TSA has developed a new granting process for evaluating funding requests and awarded 13 grants under this process in February 2004, but this process could be further enhanced through additional changes. Such changes are important to ensure the most benefit is realized from the limited funding available for youth and amateur sports. Additionally, TSA should develop and implement written guidelines for awarding Cactus League monies to baseball spring training facilities in Maricopa County.

TSA developing youth sports grants process

TSA's decision-making process for committing $5.2 million in initial funding for youth and amateur sports projects in 2001 and 2002 was not clearly defined. The procedures that TSA has since developed could be improved through greater monitoring of recipients, establishing minimum lengths of time that facilities must remain in existence, and defining the kinds of contributions that are acceptable as part of the local match.

Decision-making process unclear for initially approved projects—

TSA's Board of Directors first issued a request for proposals for youth and amateur sports projects in the fall of 2000, and received 26 funding requests during calendar year 2001. From these requests, TSA selected and approved two proposed projects and approved a separate project for the City of Glendale. TSA committed approximately $5.2 million of the anticipated $73 million it will have for youth and

No documented process existed for initial award decisions.

Youth and Amateur Sports

Purpose—To acquire land or construct, finance, furnish, maintain, improve, operate, market, or promote the use of community youth and amateur sports facilities, recreational facilities, and other community facilities or programs in Maricopa County.

Funding—First-year funding of $1 million growing at $100,000 annually for 30 years.

Total Funding—Over life of funding, $73.5 million estimated.

TSA Contribution—Up to two-thirds of a project's cost.

amateur sports projects through 2031 to these three projects. While TSA lacked a documented process for reviewing, evaluating, and awarding funding for these projects, four board members stated that an important reason they selected two projects was due to their locations outside of the East Valley, since the Cardinals stadium was initially going to be built in Tempe. TSA selected and committed funding to the following three projects:

- **New sports fields at South Mountain YMCA**—In May 2001, the Board approved $150,000 for new sports fields at South Mountain YMCA in Phoenix. The complex opened in June 2003, with a football/soccer field and a baseball field. According to a Valley of the Sun YMCA official, other funding sources for the project included the Arizona Diamondbacks, the National Football League, a Community Development Block Grant, and several individuals. Valley of the Sun YMCA officials also indicated that TSA's contribution represented approximately 18 percent of the project's total estimated costs, and that it helped generate additional contributions.

- **Regional sports complex in Avondale**—In September 2001, TSA's Board approved approximately $3.4 million toward the development of an estimated $5.5 million regional sports complex in Avondale. According to a city official, the City of Avondale paid cash for its portion and per the agreement, TSA's contribution will be paid over a 12-year period. In addition to its $3.4 million contribution, TSA will also give Avondale approximately $666,000 to make interest payments on bonds issued by the City to assist in making monies immediately available to construct the sports complex.[1] The complex, which is anticipated to be completed by spring 2004, will include nine soccer/football fields and two youth baseball fields. According to Avondale's proposal, the quality of the site would place it in demand to host regional and potentially multi-state tournaments.

- **Turf fields/overflow parking at new multipurpose facility**—In August 2002, as part of TSA's agreement with the City of Glendale for the development of the multipurpose facility, the Board approved $1 million in youth and amateur sports monies for turf fields that will double as overflow parking and event staging at the new facility. According to a TSA official, as of September 24, 2003, TSA has not provided Glendale with any of these monies because negotiations for this land continue, but TSA continues to keep these monies set aside for Glendale. These fields are anticipated to be completed in conjunction with the multipurpose facility and will help Glendale to meet its requirement to provide facility infrastructure, including parking (see Other Pertinent Information, pages 43 through 50). Glendale's agreement with the Arizona Cardinals states that the use of this space as fields could end within 10 years after the multipurpose

1 Per A.R.S. §5-809, financing is a statutorily permitted use for youth and amateur sports monies.

facility opens, and the Cardinals will have property development rights. Statute does not specify how long a facility receiving TSA monies must be used for youth and amateur sports.

A.R.S. §5-809(B) requires youth and amateur sports funding recipients to contribute at least one-third of a project's costs. TSA's development agreement with Glendale does not indicate a Glendale match for the project. Further, it is unclear how much the fields will cost. However, according to a TSA official, TSA will enter into a separate agreement with Glendale that will clarify the City's match and identify the project's total cost. Additionally, A.R.S. §5-809(D) requires that TSA give priority to recreational facilities located near or of benefit to public schools. However, since a proposal was not submitted for this project, auditors could not assess whether TSA determined if any schools would benefit.

Separate agreement should indicate the required one-third match.

TSA develops grant process—Since these initial awards, TSA postponed further grants and developed a process for evaluating future requests to fund youth and amateur sports projects. In May 2002, TSA formed the Youth and Amateur Sports Advisory Committee, which includes 20 members, to assist TSA in establishing and prioritizing youth and amateur sports facility needs. With a consultant's assistance, the committee developed a process for reviewing proposed projects and granting awards. The committee has developed six criteria for consideration when reviewing applications, including the project's benefit to a local school, which is a statutory requirement. TSA solicited applications under its new process in July 2003. In response to the solicitation, TSA received and reviewed 92 grant applications requesting over $35.2 million in assistance. In February 2004, TSA awarded 13 grants totaling over $1.3 million to communities and community organizations in Maricopa County.

In addition to the grant process, the Advisory Committee is helping TSA to create a database of existing youth and amateur sports facilities in Maricopa County. This database, which is being developed through an agreement with Arizona State University, will assist TSA in evaluating the need for facilities in particular areas in Maricopa County. When completed, this database will show existing facility locations and include demographic census data. TSA then plans to use the database when evaluating funding requests to determine, for example, the number of fields that already exist in an area and the population that will be served.

Youth and Amateur Sports Grant Criteria in Priority Order

- **Statement of Need**—Describes the community's or organization's needs, how the proposed project will benefit the community, and its potential economic impact.
- **Budget and Ability To Maintain/Operate**—Addresses the project's cost and proof of the applicant's ability to provide continued project support.
- **Partnerships**—Describes the project's outside funding support, including in-kind and matching donations.
- **Documentation of Support**—Describes public and organizational input and involvement in the project.
- **Benefit To a Local School**—Statutory requirement that considers whether the project is near or of benefit to schools.
- **First-Time TSA Grant Recipient**—Considers whether the applicant has previously received TSA grant monies.

Changes could enhance new granting process—Because funding for youth and amateur sports projects is limited and is only provided after the multipurpose facility, tourism promotion, and Cactus League projects are adequately funded, it is important that TSA uses youth and amateur sports project monies as effectively as possible. Therefore, as part of its granting process, TSA should establish additional procedures to help ensure grant projects are properly overseen and administered, and further define grant requirements. Specifically, TSA, in consultation with the Youth and Amateur Sports Advisory Committee, should establish and implement policies and procedures for the following:

- **Guidelines for grant administration and oversight**—TSA could benefit from guidelines for grant administration and oversight. These guidelines would not only inform grant recipients up-front of TSA's expectations for administering grants, but also guide TSA's efforts to monitor and oversee recipients' use of grant monies. While TSA lacks defined administrative guidelines, it has used a consultant to monitor construction of the Avondale Sports Complex because of its high dollar value. However, other entities have developed administration and monitoring guidelines for all grant recipients. For example, Arizona State Parks (Parks) has developed an oversight process for its Local, Regional, and State Parks Heritage Fund grants program that includes regular progress reports submitted by the recipient, staff site inspection visits during the project, and inspection reports that the recipient must submit after the project is completed to ensure compliance with Parks' maintenance requirements. The Commission on the Arts (Arts) requires program grant recipients to submit within 30 days of a project's completion a report describing program accomplishments and benefits. These processes could possibly serve as starting points for TSA in developing a structure that meets its needs.

- **Establishing facility length of use**—TSA should define its expectation for how long facilities that it helps fund must remain in existence and operational. TSA asks applicants to comment on how long the applicant anticipates supporting a facility. However, TSA has not defined its expectations for applicants. Other programs that provide monies for facilities have established time frames for how long these facilities must be maintained. For example, facilities built with Parks' Heritage Fund monies must be available for public recreational use for 25 years. Since TSA is making an investment of public monies in youth and amateur sports facilities, it should define how long these facilities must remain in existence and operational.

- **Defining contributions**—TSA could also benefit from further defining what the applicant may count for its local match. TSA's application packet mentions that the applicant's match may take many forms, including cash, donations, or in-kind contributions. However, as part of an earlier project evaluation, a TSA consultant suggested that TSA's Board define which expenditures will count toward the local match and which ones will not. Specifically, the consultant raised three issues, including whether expenditures for existing development should be counted toward the local match and whether applicant personnel expenses for planning and/or maintaining a project should be included. As of July 2003, TSA's Board had not developed guidelines.

Procedures needed for distributing Cactus League monies

TSA has committed one-quarter of expected Cactus League monies.

In addition to developing guidelines for youth and amateur sports funding, TSA should develop and implement written guidelines for awarding Cactus League monies to spring training baseball facilities in Maricopa County. As of December 31, 2003, TSA had committed approximately one-quarter of the total estimated funding that will be available through 2031 for Cactus League facilities. However, for future requests, TSA should establish written procedures to guide its funding efforts.

Cactus League

Purpose—To acquire land or construct, finance, furnish, improve, market or promote the use of existing or proposed major league baseball spring training facilities in Maricopa County and other structures, utilities, roads, parking areas, or buildings necessary for full use of the training facilities for sports and other purposes.

Funding—$3 million each year in the first 7 years, growing to $11 million each year in the last 4 years over a 30-year period.

Total Funding—Over life of funding, $205 million estimated.

TSA Contribution—Up to two-thirds of a project's cost.

Two spring training facilities receive funding—As of December 31, 2003, TSA had committed approximately $51.4 million of the estimated $205 million that will be available for Cactus League facilities over 30 years. TSA awarded funding to two projects:

- **New stadium in Surprise**—TSA provided $32 million toward the approximately $48 million in construction costs of a new spring training facility in Surprise. This facility was built for two new Cactus League teams—the Kansas City Royals and the Texas Rangers. The Surprise project, which was completed in December 2002, includes a 10,500-seat baseball stadium and 14 practice fields.

- **Renovations at Phoenix Municipal Stadium**—TSA provided two-thirds of the costs toward the $6.5 million renovation project at Phoenix Municipal Stadium, which is the spring training home of the Oakland Athletics. The Phoenix project includes new dugouts and field improvements, clubhouse improvements, and a new press box. The renovations were completed in February 2004.

In addition to the combined contributions of over $36.3 million to these projects, TSA has also obligated additional monies to pay interest on Cactus League bonds it issued. Statute permits TSA to issue bonds to build or improve Cactus League spring training facilities. In February 2003, TSA issued $32.4 million in bonds, which along with available cash, funded these two projects. Over the 14-year term of the bonds, TSA will also pay approximately $15 million in interest.

Finally, in December 2003, the TSA Board adopted a resolution preliminarily approving $20 million in funding for the planned design and construction of a new spring training facility in the City of Goodyear for the Anaheim Angels. The Anaheim Angels currently conduct spring training at Tempe Diablo Stadium, but their lease expires in 2007. However, the resolution also stipulates that TSA must first enter into intergovernmental agreements with the Cities of Tempe and Scottsdale regarding TSA's funding contribution towards those cities' spring training facilities. Further, it stipulates that a suitable replacement team must be identified and committed to a minimum 20-year lease to conduct spring training at Tempe Diablo Stadium.

TSA should adopt guidelines and procedures for awarding Cactus League monies.

Procedures would help guide funding efforts—TSA should develop Cactus League funding guidelines to help ensure its future award decisions use the monies as effectively as possible. Prior to awarding monies to build the new Surprise stadium and renovate Phoenix Municipal Stadium, TSA consulted with the host city and a consultant with sports-related management experience, but it did not have a written process to guide its decisions. TSA states it will meet with other host cities as their leases with Cactus League teams come up for renewal to determine their needs and appropriate TSA funding amounts. However, a more clearly defined set of guidelines could help host cities know how to obtain assistance and help ensure a consistent review of funding requests. For example, the Maricopa County Stadium District, which also provides monies for Cactus League facilities, developed procedures for its process. The District's Citizens' Advisory Committee adopted guidelines that addressed its funding priorities, evaluation process and criteria, and the types of projects and costs that could be funded. Specifically, the District's advisory committee identified 12 criteria to use when evaluating proposals, including the length of the community's lease with the Cactus League team, the size and type of the community's match, and Cactus League facility standards. Additionally, the District's Citizens' Advisory Committee defined the information it expected communities to include in their preliminary applications.

TSA states that it considers some of these factors already, but a formal set of guidelines and processes would better ensure consistency and fairness. In developing its guidelines, TSA could address such things as how it determines what standard spring training facilities will be built or renovated to, what it will consider for matching monies, and how long the baseball team's lease extension must be relative to TSA's contribution and the facility renovation. Further, these guidelines and processes could help guide TSA Board decisions regarding funding new facilities versus renovating existing facilities. The District's Citizens' Advisory Committee stated that the District's top priority should be providing adequate facilities necessary to retain current Cactus League teams. Additionally, since TSA and the Maricopa County Stadium District are developing an agreement that would allow TSA to begin receiving and distributing the District's excess revenues from the car rental surcharge for Cactus League facility improvements, TSA should consider modeling its procedures after those the District uses.[1]

Recommendations

1. In consultation with the Youth and Amateur Sports Advisory Committee, TSA should develop and implement policies and procedures that:

    a. Establish grant administration, oversight, and funding distribution requirements;
    b. Define how long funding youth and amateur sports facilities must remain in existence and operational; and
    c. Define further what expenditures will be considered for the applicant's local match.

2. TSA should develop and implement written Cactus League funding guidelines to help ensure its future award decisions for spring training facilities in Maricopa County use the funds as effectively as possible. These guidelines could address such things as how it determines what standard facilities will be built or renovated to, sources of matching monies, length of team leases, and funding new stadiums versus renovating existing facilities.

1 Under this agreement TSA would not receive monies needed for district operations or for principal and interest payments and other costs related to the District's bonds.

FINDING 4

TSA needs to make several changes to its administrative practices

To ensure the most efficient and effective use of its operating funds, which consist of public monies, and to ensure the appropriate use of monies it provides for tourism promotion, TSA needs to make several changes to its administrative practices. Although TSA is not a state agency and is therefore exempt from some requirements that state agencies must meet, it still should establish administrative policies to provide adequate control and oversight of its functions. TSA should establish policies and procedures to guide its procurement, use of attorneys, and use of its game tickets and luxury suite. Finally, TSA should work with the Arizona Office of Tourism to ensure all monies TSA distributes to this agency are used solely to promote tourism in Maricopa County, as required by statute.

TSA is not a state agency

As a separate legal body, TSA is exempt from some requirements that state agencies must follow. Specifically, A.R.S. §5-802 established TSA as a separate legal body with all of the rights, powers, and immunities of a municipal corporation. While TSA must comply with open meeting and public records laws, its status as a separate legal body exempts it from other state requirements. For instance, TSA is exempted from procurement laws. Further, its status as a tax-levying public improvement district exempts it from the State Constitution's ban on providing gifts.

TSA is exempt from several state requirements.

Procurement policies needed

TSA should establish policies and procedures to guide its procurement and contract oversight activities. Since its inception, TSA has entered into several agreements totaling millions of dollars in services, yet has lacked a defined process for conducting procurements and monitoring its contracts. TSA has contracted for various services, including legal, engineering, construction management, and other professional services. However, without a defined process, TSA's procurements may not have been consistently conducted or services may not have been obtained at the best price possible. For example, TSA has issued requests for proposals for some contracts, including the review and evaluation of multipurpose facility design and planning and management and marketing services. In other cases, according to a TSA official, TSA has selected contractors and entered into contracts based on direct selection or on the contractor's prior experience with related entities that predated TSA's formation. However, there was no available documentation that showed how these services were procured or how responses to the request for proposal were evaluated.

Other municipal corporations have established procurement guidelines.

State agencies that are exempt from the State's procurement code have developed procurement policies, and TSA should similarly develop policies and procedures to guide its procurement and contract oversight activities. For example, the Arizona Health Care Cost Containment System (AHCCCS), which is Arizona's Medicaid agency, is exempt from state procurement statutes for its medical services contracting, but is statutorily required to adopt administrative rules for its request for proposal process. AHCCCS has established these rules and also established procurement policies and procedures that are consistent with the requirements imposed on other state agencies. Similarly, according to information obtained from two other municipal corporations in the State, these municipal corporations have established procurement policies, even though they are not required to do so by statute. Establishing and following procurement and contract oversight policies helps to ensure the highest-quality product or service is received at the most economical price, and helps to ensure fair competition, prevent fraudulent activities, and protect the entity from the appearance of fraud. In establishing procurement and contract monitoring policies and procedures, TSA should consider several factors:

- **Procurement thresholds and processes**—TSA's policy should establish procurement thresholds and request-for-proposal and review processes. These thresholds would specify the process TSA will follow, depending on the total dollar value of the goods or services being purchased. For example, under the State's procurement code, purchases between $10,000 and $25,000 require the governmental entity to issue a request for proposals, while verbal or written quotations from at least three bidders are acceptable for purchases totaling $1,001 to $5,000.

- **Agreement ratification time frames**—TSA's policy should establish time frames on how soon an agreement TSA staff enter into must be brought to the Board for its ratification. While the Board has authorized TSA's president/CEO to enter into any contract up to $100,000 without prior board approval, the Board must ratify these contracts. However, in some instances, these contracts have not been provided to the Board in a timely manner for its ratification. For example, at its February 2003 meeting, the Board was asked to ratify an agreement that TSA entered into in September 2002 that would expire at the end of March 2003.

- **Agreement monitoring procedures**—TSA's policy should provide procedures for overseeing agreements once they are in place. While procedures have been included within specific agreements, TSA should develop guidelines for monitoring all contractors, including those providing consulting services. For example, TSA could establish guidelines for reviewing contractor invoices and the services provided to ensure that the contract terms have been met before payment is made.

- **Process for smaller purchases**—Finally, TSA's policy should establish a preapproval process for purchases of lesser dollar values and establish guidelines for appropriate credit card use. While TSA has issued credit cards to several of its staff, it has not defined the types of purchases for which they may be used. As a result, staff have used the credit cards to make purchases that could have been made through a purchase order process or otherwise be approved prior to the purchase. For example, TSA used its credit cards to purchase U.S., Arizona, and TSA flags; to upgrade cell phones; and to frame multipurpose facility groundbreaking photographs for board members. Using purchase orders would allow TSA to review the need for and preapprove the purchase, whereas approval of credit card purchases comes after the purchase has already been made. While auditors found evidence that preapproval was obtained for some computer software and hardware purchases, this evidence was lacking for other purchases. However, a TSA official said approval was given for all purchases.

TSA should take steps to more efficiently use attorney services

TSA could save costs by more strictly limiting and monitoring the types of services it pays attorneys to perform. Statute permits TSA to retain legal counsel, and TSA has used private law firms for its legal services. Statute does not give the Office of the Attorney General authority to represent TSA. From its inception through June 30, 2003, TSA has spent nearly $4.1 million for attorney services. These services include assistance in preparing documents related to the bonds it has issued and providing representation against a lawsuit. Much of TSA's legal expenses have been paid to the firm that serves as TSA's general legal counsel, and this firm has assisted TSA with developing several complicated, one-time agreements. For example, the law firm assisted TSA with the site selection process, the facility use agreement with the Arizona Cardinals, and other agreements related to the facility's construction, and TSA's relationship with the facility host city, Glendale.

However, the firm that serves as TSA's general counsel has also provided services that could have been accomplished more cost-effectively through other means. For example, TSA's general counsel billed between $120 and $160 per hour to draft TSA Board meeting minutes, and $160 per hour to draft TSA's agreement with its youth and amateur sports consultant and to develop the agreement for one of its first youth and amateur sports grants. It also billed $200 per hour to draft a conflict-of-interest policy, and up to $325 per hour to draft or review agreements with consultants, organizations, and TSA staff.

TSA staff could perform many duties now handled by TSA's attorneys.

TSA should take steps to ensure it makes the most effective and efficient use of its attorneys in the future. For example, TSA staff should take and record board meeting minutes and develop TSA policies instead of paying attorneys to perform these functions. TSA should also evaluate the need for an in-house attorney who could handle routine legal matters, such as simpler agreements, rather than paying high hourly rates for these services. Additionally, with the exception of litigation representation where time constraints possibly would not permit it, TSA should issue requests for proposals for legal services it requires in the future. The Office of the Attorney General annually issues a request for proposal for outside legal services that it may need during the year, and this document could serve as a starting point for TSA to similarly issue a request for proposal for legal services.

Policies needed to better control certain expenditures

TSA should establish policies to provide greater control over many of its other expenditures. TSA should ensure that all of its staff follow its travel policy. Further, although TSA is allowed to use its monies for gifts, it needs to establish guidelines regarding its gift giving. Finally, TSA should take additional steps to strengthen its internal controls over its finances.

TSA should ensure travel policy followed—TSA needs to ensure all TSA staff adhere to its travel policy and that all travel is properly approved. Although TSA is exempt from the State's travel policy, it established its own out-of-town travel policy for its staff in January 2003, which required that all travel outside of Maricopa County be approved by TSA's president/CEO or his designee and that wherever possible, lodging costs should conform to the State's travel policy. From its inception through December 2002, TSA operated without a travel policy. Auditors reviewed some of TSA's travel receipts from trips prior to this policy's establishment and found that TSA's travel did not conform to the State's travel policy. For example, in February 2002, one TSA staff member stayed overnight in a Scottsdale hotel approximately 3 miles from TSA's offices so that he would be available to pick up photocopies from a printing company early the next day. The staff member received approval from TSA's president/CEO for the overnight stay, and TSA paid $89 for the room. In September 2003, TSA's president/CEO reimbursed TSA $89 for the room.

Although TSA established a travel policy in 2003, auditors' review of travel receipts for three trips that staff have taken in 2003 found no evidence that these trips had been approved by the president/CEO. Further, for two of these trips, lodging reimbursements did not follow the State's travel policy, even though per TSA's procedures they should have. Evidence of an exemption from these policies was not included in the trip files. For example, in one instance a TSA staff member traveled to Kansas City, Missouri, in February 2003 to meet with the project and design team about the new multipurpose facility. No documented exception existed in this file for the overnight stay, and TSA paid $139 for the hotel room.[1] However, under the State's travel policy, the maximum hotel reimbursement would have been $85. TSA documented approval for this trip in October 2003 after auditors discussed it with TSA officials.

Additionally, auditors' review of trips taken by TSA's president/CEO did not find evidence of documented approval to exceed the State's travel policy reimbursement schedule. While exceptions to the State's travel policy rates are allowed under TSA's travel policy with approval from the president/CEO, TSA's policy did not establish any type of approval for travel costs incurred by the president/CEO himself. TSA documented approval for this trip in October 2003 after auditors discussed it with TSA officials. Additionally, TSA has since revised its travel procedures to require trips taken by the president/CEO to be approved by the Chairman of the Tourism and Sports Authority Board of Directors. However, TSA should also ensure that all staff adhere to the travel policy and document required approvals and reasons for exceptions.

Further guidance needed for providing gifts—Although TSA adopted a policy for providing gifts in December 2003, it should establish additional guidelines for reviewing and approving gifts. TSA's classification as a tax-levying public improvement district permits it to provide gifts, unlike most governmental entities. However, prior to December 2003, TSA had not developed any guidance regarding under what circumstances it may provide gifts. Auditors' review of TSA expenditures identified several instances in which TSA has provided gifts. While most of the items TSA purchased were under $100 each, on several occasions TSA has provided flowers to a board member and contractor, and paid for meals with TSA staff, board members, potential hires, and consultants. In just 2 months, between April 19, 2003, and June 18, 2003, TSA spent approximately $918 on such meals. While TSA adopted a policy for providing gifts in December 2003, it should also implement procedures for reviewing and approving gifts.

TSA is allowed to provide gifts.

Financial controls should be strengthened—TSA should take additional steps to strengthen its internal controls over its finances. Effective internal controls help ensure the reliability of an entity's financial reporting, ensure compliance with laws and regulations, and help protect against fraud or error. Based on a review of TSA's internal controls, auditors identified several weaknesses. These include:

1 The State's travel policy rates differ based on the travel destination and the time of year. The $85 per night reflects the reimbursement for travel to Kansas City in February.

- **Lack of written policies and procedures**—While TSA has informal practices, it has not incorporated these into written policies and procedures, but could benefit from doing so. For example, TSA lacks written policies and procedures for recording and explaining journal entries, transferring monies from one account to another, and its financing activities, such as investments and bond proceeds. TSA should establish written policies and procedures to guide its internal control practices.

- **Lack of separation of duties**—Auditors identified instances where financial and accounting duties were not separated. For example, one staff member prepares and posts all journal entries, but no review and approval of this work occurs by another TSA staff person. Segregation of duties provides a means to detect errors since one person reviews another person's work. Further, it helps to deter fraudulent activities, as no individual is in the position of being able to both commit an irregularity and then to conceal it. The *Arizona Accounting Manual* requires all state agencies to separate duties so that no one person has complete authority or responsibility for an entire transaction. Although TSA is not a state agency and has a small staff, its staff is sufficient to provide needed review and approval of these activities. Therefore, to the extent possible, TSA needs to ensure that financial and accounting responsibilities are adequately segregated.

TSA often paid credit card bills late.

- **Lack of timely credit card payments**—Auditors' review of credit card statements identified six instances where TSA was assessed $35 late fees, and one instance where TSA was assessed a $29 late fee. Auditors also identified five occasions where TSA paid financing charges at 19.8 percent annual interest on balances that were not completely paid. To avoid paying interest and penalties, TSA should pay its credit card balances in full each month and in a timely manner.

TSA will have a luxury suite and other tickets for football games.

TSA needs policy to control use of game tickets and luxury suite—Because of the potential value involved, TSA should develop a policy to guide and control the use of the luxury suite and tickets it will receive for all football events in the new multipurpose facility. Per its agreements with the Arizona Cardinals and the Tostito's Fiesta Bowl, TSA will have one suite for all football events, including the Super Bowl, as well as 16 additional tickets for all Cardinals' home games and Fiesta Bowl games. While the Cardinals and Fiesta Bowl agreements state that the suite and tickets will be used for promoting the facility, TSA has not developed specific policies to address the use of these tickets. Even though the facility will not open until 2006, the potential use and value of these tickets indicates that TSA needs a policy in place to guide their use. For example, these tickets' potential resale value could be significantly higher than their face value. Specifically, lower-level tickets for the 2003 Tostito's Fiesta Bowl—a national championship game—had a face value of $150, but were reportedly selling for as much as $2,025. TSA has indicated that when no promotion opportunity exists, it expects that the suite and tickets will be used for charitable purposes, but has not defined how this would occur. The Maricopa County Stadium District, which owns Bank One Ballpark, has developed an agreement with two nonprofit organizations for the sole use of the suite the District receives for all Diamondbacks regular season baseball games. TSA should develop a policy that clearly defines how the suite and tickets will be used. Such a policy should contain guidance on how the tickets will be used for either promoting the facility or for charitable purposes.

TSA should help ensure monies spent on tourism promotion benefit Maricopa County

TSA should work with the Arizona Office of Tourism to ensure all monies TSA distributes to this agency are used solely to promote tourism in Maricopa County. According to A.R.S. §5-835(B)(2), TSA must distribute to the Office of Tourism $4 million annually, increasing by 5 percent each year. However, in fiscal year 2003, the Legislature appropriated only $2 million of these monies to the Office of Tourism, and retained $2.2 million for use in balancing the State's budget. The Office of Tourism has established a grants program to award these monies to entities such as convention and visitors' bureaus, cities, and other local tourism promotion entities in Maricopa County. However, the Office of Tourism keeps 5 percent of these monies for other promotion efforts. The Office of Tourism is a state-wide tourism marketing organization, and when auditors reviewed its use of this 5 percent retention in fiscal years 2002 and 2003, they determined that much of it was used to promote tourism for all of Arizona rather than Maricopa County, as required by A.R.S. §41-2306(A)(2).[1] Specifically, auditors found that the television advertisements paid for with the 5 percent retention were not specific to Maricopa County or places within the County, but included scenes depicting Monument Valley and the Colorado River, while the radio advertisements focused on the Grand Canyon. To ensure statutory requirements are met, TSA should encourage the Office of Tourism to distribute all monies it receives from TSA to convention and visitors' bureaus, cities, and other local tourism promotion entities in Maricopa County, as they are better suited for promoting Maricopa County than the Office of Tourism is.

Some tourism promotion monies not spent in accordance with statutory requirements.

According to TSA's president/CEO, TSA officials met with the Office of Tourism in December 2003 to discuss the expenditure of these monies. TSA plans to continue working with the Office.

1 The Office of Tourism's expenditures were $200,000 in fiscal year 2002 and $100,000 in fiscal year 2003, both of which represented 5 percent of the total amount of TSA tourism promotion monies during those years.

Recommendations

1. TSA should establish and implement a procurement policy that includes guidelines in areas such as purchasing thresholds, request for proposal and review processes, oversight of contracts once they are in place, and guidelines for appropriate use of the credit cards, obtaining advance approval for purchases, or for using purchase orders instead of credit cards for its purchases.

2. TSA should take steps to ensure it is making the most effective and efficient use of its attorneys. Specifically, TSA should:

    a. Identify administrative tasks, such as developing board meeting minutes, that existing TSA staff could perform and no longer have their attorneys perform these tasks;
    b. Evaluate the need for an in-house attorney to handle routine legal matters, such as simpler agreements, rather than paying hourly rates for these services; and
    c. Issue requests for proposals for all outside legal services it needs, with the exception of litigation representation, where time constraints would not permit this process.

3. TSA should ensure all staff, including its president/CEO, adhere to TSA's travel policy and obtain and document approval for all travel and reasons for exceptions to the State's travel policy reimbursement rates.

4. TSA should implement procedures for reviewing and approving gifts.

5 TSA should strengthen its internal controls by:

    a. Establishing written internal control policies and procedures;
    b. Ensuring that financial and accounting responsibilities are adequately separated to the extent possible; and
    c. Paying its credit card balances in full each month and making payments to its credit card company on time each month.

6 TSA should establish a policy that outlines the proper use and control of tickets it will have for a luxury suite and other seats for football events at the multipurpose facility.

7. TSA should continue its efforts to encourage the Office of Tourism to distribute all tourism monies it receives from TSA to convention and visitors' bureaus, cities, and other tourism promotion entities in Maricopa County, as they are better suited to promote Maricopa County, which is the required use of these monies.

OTHER PERTINENT INFORMATION

As part of the audit, auditors gathered other pertinent information regarding the projected revenue that the Tourism and Sports Authority expects to receive over the next several years. Auditors also gathered information related to the funding of the multipurpose facility construction and surrounding infrastructure contributed by TSA, the Cardinals, and the City of Glendale, and the benefits that those parties plan to gain from the facility.

Continued revenue growth is key to funding all TSA objectives

TSA solvency depends on growth in revenue sources.

While TSA's revenues for fiscal years 2002 and 2003 have been sufficient to meet the agency's many funding obligations, future sufficiency is heavily dependent on the growth rate for key revenue sources—and particularly for the hotel bed tax and car rental surcharges, the two largest revenue sources. Thus far, hotel bed tax revenues have fallen below projections, while car rental surcharge revenues have exceeded projections. Projections prepared to accompany the issuance of TSA's bonds assumed an annual growth rate of 5 percent for the hotel bed tax revenues in fiscal years 2005 through 2011, and for the car rental surcharge revenues in fiscal years 2003 through 2011. Growth rates below this amount could limit TSA's ability to fund those activities that have a lower statutory funding priority, such as youth and amateur sports and TSA's operations. TSA is taking steps to prepare for this possibility.

Two sets of revenue projections calculated at different points in the process—During different phases of the effort to fund a multipurpose facility and other projects, revenue projections were offered to provide critical information to various stakeholders. Revenue projections are significant because they provided and will continue to provide information to the public on whether it appears sufficient revenues will be generated to fund all of TSA's priorities. These projections have estimated the amount of revenue that TSA might receive from all of its revenue sources including the hotel bed tax; car rental surcharge; sales taxes recaptured at Cardinals' football games and other events at the multipurpose facility and from the construction of the multipurpose facility; the income taxes of the Cardinals' organization, its employees (including players), and their spouses (NFL tax); and from rent and other revenue generated from events held at the facility.

Two sets of revenue projections have been calculated. The first set was calculated for the Proposition 302 Publicity Pamphlet and Sample Ballot for the General Election on November 7, 2000 ("the pamphlet"), which provided information to Maricopa County voters regarding the projected revenue that would be available to fund TSA's priorities. TSA consultants prepared 30-year revenue and expense projections based on information gathered by the Governor's Stadium Plan "B" Advisory Task Force, approved legislation, and the Arizona Department of Revenue. The second set was calculated by the same consultants prior to TSA's construction bond offering in February 2003 and was included in the bonds' official statements to inform potential investors regarding the revenues available to service the bond debt. These projections were based on revisions that reflected changes in the tourism industry after the terrorist attacks of September 11, 2001, and an economic downturn. The two major sources of funding were the 1 percent increase in the hotel bed tax and a 3.25 percent car rental surcharge. As of June 30, 2003, TSA had received 79 percent of its revenues from these sources. The voters' pamphlet and the official bond statements included the following projections for these two sources:[1]

- **Hotel bed tax**—To project potential revenues from an increase in the hotel bed tax, consultants analyzed hotel sales in Maricopa County from 1989 through 1998. The consultants determined that the average annual rate of growth in Maricopa County room sales during that period was approximately 9 percent. For the voter information pamphlet, the consultants used this information to set an expected rate of growth of 8 percent during the first 10 years, and declining after that during the remainder of the 30-year period of the tax. According to the consultants, due to the changes in the tourism industry, this initial expected growth rate was reduced to 5 percent beginning in fiscal year 2005 for the official bond statements.

- **Rental car surcharge**—According to TSA's consultants, less data was available for projecting possible revenue from the rental car surcharge because there had not been a tax applied against rental cars—only a flat fee of $2.50 to fund Cactus League facility improvements through the Maricopa County Stadium District. To make these projections for the voters' information pamphlet, consultants met with various representatives of the rental car industry to estimate how much rental car business Maricopa County has had in recent years and how much it might grow. Rental car surcharge revenue was projected to increase by 5 percent per year for the first 20 years of the tax and then decline for the remainder of the 30-year tax. These projections were not revised downward for the bond statement projections, because revenues have been coming in at higher amounts than the initial estimates.

1 Information for TSA's other revenue sources is contained elsewhere in this report. For a summary of all of TSA's revenue sources, please refer to the Introduction and Background (see pages 1 through 13). For more specific information related to revenue that TSA expects to receive from the NFL tax, please see Finding 2 (see pages 23 through 29).

Actual collections vary from projected amounts—Actual revenue collections for these two major revenue sources have differed considerably from projections in the voters' pamphlet, and to a lesser degree, from projections in the bond statement (see Table 3). Revenue collected for the hotel bed tax in fiscal year 2003 was more than $1.3 million, or approximately 11.5 percent short of the amount projected in the voter information pamphlet, but only about $450,000, or approximately 4 percent short of the fiscal year 2003 revised projections done prior to the February 2003 bond offering. By contrast, car rental surcharge collections have been greater than expected. In fiscal year 2003, car rental surcharge collections were more than $2.7 million, or 55 percent more than the amount projected in the voter information pamphlet. Similarly, for fiscal year 2003, car rental surcharge collections were greater than $830,000, or 12 percent more than the amount projected in the official bond statement.

Some revenues have exceeded projections, while others have fallen short.

Table 3 Hotel Bed Tax and Car Rental Surcharge Collections
Projected vs. Actual
Fiscal Years 2002 and 2003

	Voters' Pamphlet			
	Hotel Bed Tax		Car Rental Surcharge	
Year Ended February 28	Projected	Actual	Projected	Actual
2002	$10,700,000	$10,048,920	$4,700,000	$6,195,582
2003	11,556,000	10,227,368	4,935,000	7,657,703

	Official Bond Statement			
	Hotel Bed Tax		Car Rental Surcharge	
Year Ended June 30	Projected	Actual	Projected	Actual
2003	$10,673,458	$10,228,577	$6,830,802	$7,668,222

Source: Auditor General staff analysis of revenue projections provided in the Proposition 302 voters' pamphlet and in the February 2003 Official Bond Statement, and Arizona State Treasurer's Office Distribution Recipient Reports.

Limited growth may hamper TSA's efforts—Although TSA has fully funded its priorities and established reserves to date, it may become difficult for TSA to continue doing so in future years if revenue growth does not match projections. At growth rates less than 5 percent in the hotel bed tax and car rental surcharge revenues, TSA's annual projected revenue may not be sufficient to meet all of its future obligations and sustain operations, leaving TSA dependent on its operating reserves to make up the difference. However, continued reliance on its reserve could

Revenue shortfalls could exhaust TSA's operating reserves.

quickly exhaust these monies. While TSA should receive sufficient revenue to cover its multipurpose facility bond debt, as it is the first funding priority, constant, significant revenue shortfalls could affect the funding available for TSA's other priorities. This would primarily affect TSA's operating budget, and then funding for youth and amateur sports.

In addition to the potential effects of limited revenue growth, TSA's operational costs will increase significantly, from an estimated $5 million in fiscal year 2006 to an estimated $11.6 million in fiscal year 2007, when the multipurpose facility is scheduled to open. However, TSA also expects to begin generating additional revenue from facility events. The increased revenue will come from all sales taxes paid at Cardinals games and other events held at the facility, as well as rent and other revenue generated from the Fiesta Bowl and other events held at the facility. Because its operational costs will increase, TSA should maximize the amount of revenue it can generate from these events.

The State is not financially liable for any TSA functions.

TSA is responsible for addressing revenue shortfalls—TSA is taking steps to prepare for the possibility that revenue growth may not match projections. The responsibility for addressing revenue shortfalls rests with TSA, as A.R.S. §5-836 clearly states that the State is not financially liable or responsible for costs associated with TSA's operations, the multipurpose facility, or any other facility or project funded by TSA.

TSA has taken the following steps:

- Working to obtain a $3 million line of credit to cover short-term operating costs when revenue shortfalls occur.

- Creating an operating reserve and planning to add to it as it continues to receive revenues greater than its funding obligations. As of June 30, 2003, TSA had over $2.5 million in operating reserves.

- If necessary, according to TSA officials, TSA could also reduce its operating expenses and renegotiate some of its agreements if it experienced significant revenue shortfalls.

While most of TSA's revenue sources, such as hotel bed tax revenues, are outside of its control, it will be important in the years following the facility's opening to maximize the revenue that it generates. This will come through TSA's marketing efforts and its ability to maximize the use of the facility throughout the year with events that will generate revenue from rent, sales taxes, and other sources.

TSA will share facility costs and benefits

TSA, the Arizona Cardinals, and the City of Glendale will each share in the total cost of constructing the facility and its surrounding infrastructure, and will benefit from the facility in various ways. Each of these organizations will contribute millions of dollars toward the construction of the multipurpose facility and its infrastructure, with TSA paying for 72 percent of the anticipated $370.6 million in construction costs for the facility itself. Once the facility is built, their respective benefits will be as follows:

- TSA will own and operate the facility, and generate revenues from events at the facility.
- The Cardinals will own the facility naming rights and receive concessions, parking, and ticket sales revenues from all Cardinals games held at the facility.
- The City of Glendale plans to benefit from the economic impact on neighboring businesses and from sales taxes generated by the multipurpose facility.

TSA will pay for most construction costs—TSA will pay for a majority of design and construction costs, and will also pay a large amount for financing its contribution, but will own the facility and collect revenue from events held at the facility. As of January 2004, the cost for designing and constructing the facility was expected to be $370.6 million, which does not include infrastructure costs (for information on infrastructure costs, see page 53). TSA will pay an estimated $266.6 million, or 72 percent of the facility construction costs, but the exact amount may vary depending upon TSA's ability to generate additional monies. Per its agreement with the Cardinals, TSA could pay as much as 74.3 percent of the total construction costs if it generates more revenue than expected from sources such as the hotel bed tax and car rental surcharge. Additionally, the total amount that TSA will pay for the facility will be much more than $266.6 million because it has financed a majority of its share of construction costs through approximately $222 million in 30-year construction bonds that it issued in February 2003. These costs, which include principal and an estimated $235 million in interest on the bond proceeds, are expected to exceed $500 million, although this amount could be lower if TSA can retire the bonds in less than 30 years. Once completed, TSA will also be responsible for all Arizona Cardinals' game-day expenses for the facility.

TSA issued $222 million in bonds in February 2003.

While TSA will pay a large majority of the construction costs, it will own and operate the facility and will generate revenues and other benefits from many of the events staged at the facility:

- **Revenue from nonfootball events**—Per its enabling statutes, TSA will own, operate, maintain, market, and improve the facility. As owner and operator, TSA will generate facility revenue from nonfootball events held at the facility. TSA expects to host sporting events including professional soccer games, and college championship basketball tournament games, as well as nonsporting events such as tradeshows, conventions, and concerts. Event revenue will come from rent and concessions. In its first full year of facility operation, TSA projects generating an estimated $2 million in facility revenue.

TSA hopes to host major national sporting events such as the NFL's Super Bowl.

- **National Exposure for Arizona**—TSA expects to generate national and international exposure for Arizona by hosting major sporting events such as the NFL's Super Bowl and the National Collegiate Athletic Association's Final Four (college basketball's championship series). TSA's president states that such events will likely operate at a loss for TSA, but that the area will benefit through money spent by event attendees, and Arizona's tourism industry will greatly benefit from the national exposure that such events provide.

- **Sales tax recapture**—Statute allows TSA to recapture state sales taxes on all events held at the facility, including Arizona Cardinals' football games. TSA projects that sales tax recapture from all events will generate approximately $16.3 million during the facility's first 5 years of operation.[1]

Arizona Cardinals also contribute significantly, but gain several benefits

—As the primary occupant and user of the facility, the Cardinals' organization is paying a significant portion of construction costs and has purchased the land, but will gain several financial benefits from the new facility. Specifically, Laws 2000, Ch. 372 §15(1) requires the Cardinals to enter an agreement with TSA to provide $85 million toward the facility's cost. Subsequently, as the cost of the facility increased, the Cardinals agreed to contribute an additional $19 million, and are now obligated to pay approximately $104 million toward facility construction. In addition, the Cardinals paid approximately $17.8 million to purchase 160 acres of land including 25.3 acres for the facility site, which it deeded to TSA for a $10 fee. However, the facility property is subject to reversion to the Cardinals after the initial 30-year term of its agreement with TSA if the Cardinals are no longer using the facility and other facility events do not meet minimum attendance requirements. Additionally, according to an agreement between the City of Glendale and the Cardinals, Glendale will reimburse the cost of acquiring the property to the Cardinals at 5 percent interest. Finally, the Cardinals will pay $250,000 per year (increasing by 2 percent per year) in rent to TSA for use of the facility.

Arizona Cardinals are contributing more than statute required.

1 The facility is scheduled to be open for the 2006 National Football League preseason, and the first 5 full fiscal years of operation will be fiscal years 2007 through 2011. TSA currently receives sales tax revenues from facility construction costs and Cardinals' home games played at Arizona State University's Sun Devil Stadium.

The Cardinals will gain several financial benefits from the new facility. These benefits include potential increased ticket revenue, increased game-day revenues, and selling the rights to name the new facility:

- **Increased ticket revenue**—The Cardinals may benefit from increased ticket prices and will keep revenue from luxury seating. Most NFL teams that have built new stadiums in recent years have increased their ticket prices when their new stadiums open. For example, when the Denver Broncos began playing in a new stadium in 2001, ticket prices increased by 13.1 percent. Additionally, the Cardinals will be responsible for marketing premium seating, including luxury suites and club seats, and will receive all game-day revenue that premium seating generates. The new facility will have 88 luxury suites and several club seats. Luxury suite and club seating often offer better views, preferred parking, and higher-quality food and beverage services. Suites in NFL stadiums averaged from approximately $50,000 to $152,000 for the 2000 season. According to a Cardinal official, the Cardinals anticipate beginning to market the suites in February 2004.

- **Other game-day revenue**—The Cardinals will receive more game-day revenue from sources such as advertising signage and concessions in the new facility compared to their current agreement to play in Arizona State University's Sun Devil Stadium. For example, the Cardinals will retain nearly all revenues generated from permanent advertising signage in the new facility. ASU keeps all profits from permanent signage in Sun Devil Stadium and receives a portion of any temporary advertising signage that it allows the Cardinals to post during games. Additionally, the Cardinals will receive all profits from game-day concessions in the new facility, but receive only one-half of all Sun Devil Stadium's game-day concession profits.

- **Naming rights**—The Cardinals will own the naming rights to the new facility. The Cardinals have not yet entered an agreement for naming the facility, but naming rights agreements can potentially be worth several million dollars. For example, in 1995, the Bank One Corporation entered a 30-year, approximately $66.4 million agreement with the Arizona Diamondbacks baseball team to name the baseball stadium in downtown Phoenix "Bank One Ballpark." Recent naming rights deals for new National Football League stadiums were sold for much more. For example, in 2001, a 20-year naming rights agreement for a new football stadium in Denver, Colorado, was sold for $120 million, and a 32-year agreement for a new football stadium in Houston, Texas, was sold for $300 million.

The Cardinals will retain the valuable facility naming rights.

City of Glendale responsible for infrastructure costs—Statute required TSA to enter an agreement with a site host to provide for facility land, infrastructure, and parking. As the facility's host, the City of Glendale estimates that costs for infrastructure at the facility and surrounding areas will be approximately $61.9 million.

This amount includes onsite parking, surrounding road improvements, sewer and utility connections, landscaping, and a pedestrian plaza. The same contractor who is building the facility is expected to perform all infrastructure construction.

The City of Glendale has formed a Community Facilities District that will issue bonds to finance much of infrastructure construction costs. The District will also receive revenue from several other sources. First, Glendale is dedicating revenue from local sales taxes generated from events at the facility, a facility user fee collected by TSA at all events subject to Glendale's city sales tax, event ticket surcharges, and a portion of Fiesta Bowl parking revenue. TSA is also providing approximately $1.7 million in state sales taxes recaptured from infrastructure construction costs. Finally, Glendale is pursuing a $3 million contribution from the Tostito's Fiesta Bowl. Glendale anticipates benefiting from the facility through sales taxes generated in the City and from the general economic development it expects to occur because the facility is located in Glendale.

AGENCY RESPONSE

A R I Z O N A TSA TOURISM & SPORTS AUTHORITY

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March 23, 2004

Ms. Debra K. Davenport, CPA
Auditor General
State of Arizona
2910 N. 44th Street, Suite 410
Phoenix, AZ 85018

RE: Audit of the Tourism & Sports Authority

Dear Auditor General Davenport:

On behalf of the Board of Directors and staff of the Arizona Tourism and Sports Authority, thank you for the opportunity to respond to the 2004 Performance Audit of the TSA.

We want to acknowledge the challenges presented to both the audit team and the Authority by the fact that this audit commenced in February 2003, slightly more than two years since the Authority began its work following voter approval of Proposition 302 in November 2000. Whereas, the original TSA legislation called for a performance audit to be conducted 10 years later, amendatory legislation in 2002 (Ch. 288) moved that date up to 2004.

Consequently, the audit reflects the absence of certain policies and procedures that likely would have been in place had the audit taken place in 2010, as originally designed. The pressing business of launching an entirely new enterprise while dealing with site issues, constitutional lawsuits, contract negotiations, revenue shortfalls, bond financings, and myriad other issues was deemed a higher short-term priority. At the same time, we appreciate that the performance audit has provided some valuable recommendations that we are pleased to implement. Nonetheless, even though the Authority is in its infancy, we are pleased that the audit has reported on the substantial accomplishments of the Authority, and has found our activities to be in accordance with our statutory duties.

The Authority is also appreciative of the time taken by the audit team to understand the complexities of planning, designing, and constructing a dome football stadium with a retractable field. The conclusion that while the costs have risen from earlier estimates, the TSA is taking steps to protect the public, is one that we have worked very hard to achieve. The Board of Directors takes its fiduciary responsibilities very seriously.

Likewise, suggestions to improve the process by which the Board makes decisions regarding Cactus League and Youth and Amateur Sports projects are also welcomed. We were already hard at work involving community stakeholders and interested parties in a major overhaul of the youth and amateur sports facilities grant program when the audit commence a year ago, and are encouraged that the changes we have made are exactly in line with the recommendations contained in the performance audit.

With one exception, we concur with the audit recommendations having to do with improved administrative practices, some of which have already been implemented, and others which will be implemented soon. The exception is in the area of legal services, where we will not be re-bidding our outside counsel services prior to completing the many contracts and agreements governing the development and use of the new multipurpose stadium facility in Glendale.

The most significant disagreement we have with the performance audit has to do with the audit finding that review is needed of general fund support of the TSA. This finding and related recommendations appear to be outside of the stated purpose of the performance audit, which according to A.R.S. 5-812.B. is to "issue a public report of the performance audit including findings and specific recommendations for statutory and administrative changes to improve the operation of the authority" (emphasis added). The recommendation that the legislature "explore options to limit additional general fund contributions" (the non-NFL income tax revenues that may be forwarded to the Authority in certain situations) has the potential to harm the Authority's ability to repay its debt or to sustain its operations, including our ability to maximize the number of events available to the community at the new stadium. As you correctly pointed out later in the audit, "although TSA has fully funded its priorities and established reserves to date, it may be difficult for TSA to continue doing so in future years if revenue growth does not match projections".

Again, thank you for the opportunity to respond. We look forward to reporting back to your office as these recommendations are implemented.

Sincerely,

Ted A. Ferris
President/CEO

cc: John Benton, Chairman, Tourism and Sports Authority
Tourism and Sports Authority Board of Directors

Enclosure

Summary Response

Finding 1:
Facility cost has increased, but various mechanisms should help limit TSA's liability for future cost overruns.

Recommendations:
The Authority agrees with this finding. There were no recommendations for this finding.

Finding 2:
Review needed of General Fund support for TSA

Recommendations:
The finding of the Auditor General is not agreed to and the recommendation will not be implemented. (Note: In this case, the Authority cannot implement this recommendation, because the Auditor is recommending that the Legislature consider amending the TSA statute to reduce certain revenues that are earmarked for the multipurpose stadium facility. We would oppose implementation of these recommendations for reasons given in our Agency response).

Finding 3:
Defined processes will help TSA objectively evaluate funding requests.

Recommendations:
The finding of the Auditor General is agreed to and the audit recommendations will be implemented.

Finding 4:
TSA needs to make several changes to its administrative practices.

Recommendations:
This finding contains 11 recommendations. For 10 of the 11 recommendations, the finding of the Auditor General is agreed to and the audit recommendations will be implemented. For one of the recommendations having to do with procurement of outside legal services, the finding of the Auditor General is agreed to and a different method of dealing with the finding will be implemented.

Tourism and Sports Authority Response to Findings and Recommendations

Tourism and Sports Authority is Making Solid Progress Toward Attainment of Statutory Goals While Keeping the Public Informed

We believe that the Performance Audit shows that the TSA is working hard to implement all of our statutory duties as spelled out in our enabling statute and as affirmed by the voters of Maricopa County in November 2000. While the TSA statute establishes a "waterfall" of funding the priorities for specific activities, it is left to the Board of Directors and staff of the Authority to develop specific policies and procedures for creating the new multipurpose stadium facility, for making grant awards for the Cactus League and youth and amateur sports, and for a variety of other matters. We are pleased that the extensive performance audit of the Authority's operations has determined that all of our activities are in support of our statutory responsibilities.

The performance audit reveals the following with respect to our major funding responsibilities:

Multipurpose Facility ("Cardinals Stadium")—The stadium is 8 months into a 36-month construction timetable and is slated to be completed by August 1, 2006. The Design-Build Agreement with Hunt Construction is in place and a "guaranteed maximum price" has been set. The total project cost is $370.6 million and the Glendale support infrastructure outside of the stadium is separately budgeted at $61 million. The Cardinals acquired 165 acres of land for nearly $18 million and deeded 25 acres to the TSA for the stadium and pedestrian plaza.

The stadium design has won critical acclaim internationally and has been featured in numerous architectural, construction and trade journals. A major coup was achieved in late 2003 when we were selected to host the 2008 Super Bowl.

The stadium continues to feature a retractable roof, a retractable natural turf field (the first of its kind outside of Europe or Asia), and a full utility grid embedded in the stadium floor that makes our stadium a very flexible and easily transformed building for a wide variety of events. The field tray will be in the outboard position except for days when football or soccer is being played in the stadium. Effectively, this means that our stadium will operate as the world's biggest arena, a far more useful building than a typical open-air football stadium with a fixed field.

Tourism Promotion—The TSA has forwarded $9.675 million to the Arizona Office of Tourism for tourism promotion in Maricopa County (pursuant to budget-related legislation another $2.2 million was forwarded to the general fund in FY2003). This year, these monies are being used in part to fund a Cactus League supplement that ran in the major newspapers in 9 metropolitan areas whose teams hold their spring training in the Valley of the Sun. This cooperative advertising supplement between AOT, our

Convention and Visitor Bureaus and Valley hoteliers has contributed to what is shaping up to be a record attendance year for the Cactus League.

Cactus League—Also contributing to record attendance are the stadium construction and renovation projects funded through the TSA. In late 2002, we completed construction of a $48 million spring training complex in Surprise that is the new home of the Texas Rangers and the Kansas City Royals. They are now playing their second season. This year, we completed $6.6 million of renovations at Phoenix Municipal Stadium that led to a 10-year lease extension with the Oakland Athletics. One-third of the funding for these projects came from the host city, which owns and operates the facilities pursuant to operating agreements with the Major League Baseball teams.

In 2004, we anticipate completing agreements with the cities of Scottsdale and Tempe for major upgrades of the practice facilities for the San Francisco Giants and Anaheim Angels. The Angels are considering a move to Goodyear, and the TSA has indicated we will help finance a new stadium there, but only if a replacement team is contractually obligated for a long-term lease at Tempe Diablo Stadium.

Youth Sports—The TSA helped finance a $750,000 youth sports complex at the Phoenix South Mountain YMCA. Included are lighted football and baseball fields and other amenities. We are also funding two-thirds of a $5.5 million regional sports complex in Avondale, which includes 9 lighted soccer/football fields, two baseball fields, parking and concessions, and other amenities. This project broke ground in 2003 and will be completed later this year. It has the potential to help attract regional or national tournaments. In February 2004, the Authority concluded a 7-month public procurement process with the awarding of $1.3 million for 13 new youth and amateur sports projects throughout "the Valley of the Sun".

Operations and Reserves—The Authority has established reserves for the cactus league per our bond covenants, for youth sports as required by statute, and for agency operations per the policy of our Board of Directors. Our reserves for the cactus league must reach $3.24 million, and our reserves for youth sports and Authority operations are intended to cover one year's worth of funding. The operating expenses for the Authority have declined in each of the past two years as legal and consulting expenses have dropped dramatically with the completion of key agreements, the conclusion of litigation, and the completion of site selection and design of the facility.

Open Public Meetings and Public Communications—The Board of Directors of the TSA has held 49 public board meetings and several "open houses" in 44 months of existence. While the Authority's Board of Directors is entitled to per diem payments and expenses for Board related business, the Board has chosen to not accept such payments at any time during its existence. The members have elected to do so in order to truly operate as an unpaid, volunteer citizen board.

Extensive and timely communications with the public have been a high priority for the TSA. The Authority has maintained a robust internet website since early 2001, which can be found at www.az-tsa.com. It has grown to include a comprehensive archive that includes all public documents such as board member agendas, meeting minutes, and board adopted resolutions. Included as well are links to the Authority's Monthly Report to the Legislature and Governor, which provides a monthly progress report and analysis of Authority revenue collections for the month and year-to-date.

At the end of calendar year 2003, the TSA's Public Information Officer produced a web-based Annual Report (http://www.az-tsa.com/archives/annual-report-2003.pdf) as well as an 11-minute DVD that provided a video chronicle of the Authority's annual progress toward all of our goals and objectives. Each of these reports was produced entirely in-house.

Goals and Objectives – The Arizona Tourism & Sports Authority's purposes are very clearly spelled out in our enabling statute and the publicity pamphlet that led to voter approval of Proposition 302 in November 2000. Senate Bill 1220 (Ch.372, L2000) as amended by House Bill 2177 (Ch.288, L2002) establishes fairly precise objectives within a "waterfall" of funding priorities. Tourism taxes make up 60% of Authority revenues and must be spent in a precise order and in precise amounts for stadium senior bond debt service, tourism promotion, Cactus League, youth sports, Authority operations and required reserves. Facility-related revenues make up the other 40% of authority revenues and must be spent first on the balance of required debt service, and thereafter on authority operations and required reserves.

The performance audit states that "TSA has not developed program goals and performance measures, but it is not required to do so since it is not a state agency…measuring performance could help staff maintain its focus on important TSA functions and activities, enhance service quality, and aid in budget development and review." We agree that the planning and the establishment of goals and objectives is essential to organizational success. This is why our Board of Directors met in open session on October 30, 2003, to review our attainment of goals and objectives established for calendar year 2003, and to establish objectives for calendar year 2004, all of which were shared with the Auditor General. The Authority believes that a public planning process is an essential feature of achieving our statutorily-defined responsibilities.

During calendar year 2003, the Authority operated with 21 key objectives that placed the authority on a clear path toward the aforementioned legislative priorities. As of December 31, 2003, all 21 objectives had been completed and consequently, the TSA was making enormous strides toward achieving all of our statutory duties. As mentioned above, the Authority has established 37 objectives for 2004 and will measure ourselves against these objectives at year's end (our 2004 objectives are appended to this response).

<u>Finding No. 1—Multipurpose facility cost at $370.6 million, but various mechanisms should help limit TSA's liability for future cost overruns</u>

We are gratified that the chief conclusion regarding the most visible and important project of the TSA is that the Authority has taken steps to protect the public with respect to the construction of Cardinals Stadium. While the stadium's cost has risen to $370.6 million from the 5-year old estimate of $331 million, it is now governed by a 'guaranteed maximum price' through our design-build agreement with Hunt Construction. Any unanticipated costs above $370.6 million will either be the responsibility of Hunt or the Arizona Cardinals.

While the TSA's funding responsibility has risen roughly $20 million from that contemplated at the time of voter approval of Proposition 302, the Authority has negotiated an increase in the Cardinals capital contribution from the statutorily-required $85 million to a current estimate of $104 million. And, should the Authority's estimated revenues from bond interest earnings or contracting sales tax recapture come short of estimates, the Cardinals would have to make up the difference. Furthermore, the Cardinals have also paid for the 165 acres of land ($18 million) upon which the stadium and parking reside, and have deeded 25.3 acres over to the control of the Authority for the Stadium and pedestrian plaza for the nominal amount of $10.

Working with the Cardinals, we have established a Project Management Agreement governing the relationship between the Cardinals and the TSA over the course of construction. Given their increased capital contribution and their risk for cost overruns, the Team requested and received a leading role in overseeing construction of the stadium, with the Authority bearing primary responsibility for features of the stadium that are defined as "public interest criteria". Examples include the retractable roof and field, the utility grid, and other features that make the stadium a truly multipurpose facility.

While it is true that remaining construction contingency amounts are roughly two percent of the project budget, they are roughly three percent of the "cost of work", when certain fixed "soft costs" such as insurance, taxes, general conditions, and builder's fee are removed from the equation. Given that the project is roughly three-quarters "hard bid" at this juncture, this size of the contingency appears reasonable.

The Cardinals are paying for several construction experts outside of the project budget that have experience overseeing major stadium projects. The TSA has added outside construction expertise as well, with the addition of the services of the recently retired CEO of McCarthy Construction, one of the Valley's largest construction companies. His services are a strong complement to the Authority's project representative. Both the TSA and the Cardinals have a strong presence at the site, with staff and consultants that are housed at the construction site on a daily basis.

Hunt Construction is the leading builder of sports facilities in the U.S. They have constructed over 70 stadiums and arenas including Bank One Ballpark and America West Arena. Hunt maintains corporate offices in Scottsdale and operations offices in Phoenix. Its Chairman and President both reside in the Valley of the Sun.

<u>Finding No. 2—TSA is Receiving General Fund Monies</u>

Because we feel this finding and recommendation is outside of the scope of this performance audit (which calls for recommendations that are to "improve" agency operations) and because it would, in fact, be harmful to our operations, we must oppose any change to the statute in this regard.

The Auditor General's premise that the general fund is losing monies due to this provision is fundamentally flawed. It is a "static economic analysis" that ignores the many different ways that the economic benefits of Proposition 302 result in increased revenues to the state general fund. For example, had Proposition 302 not passed, and if the stadium were not built, we would undoubtedly lose our NFL franchise, a $150 million (annual) business that generates roughly $7.5 million of total general fund revenue annually. We would also not be the chosen host for Super Bowl XLII in 2008, an event worth close to $400 million to the states economy.

Similarly, the Audit ignores the estimated $20 million that will accrue to the state general fund over the course of construction from the multipurpose stadium facility, in addition to many millions of dollars from Cactus League and youth sports projects. The Audit also overlooks the positive impacts of increased Tourism promotion for the state general fund. According to fiscal analyses performed at the time of legislative enactment, the state general fund stands to gain $30-50 million per year on average over the next 30 years from all of these Prop 302 activities. The independent economic analysis that was included in the publicity pamphlet predicted an average annual economic impact of $1.95 billion over the next 30 years from all of the sports, entertainment and tourism activities resulting from Proposition 302.

It was understood by the Legislature and disclosed in the Official Statement accompanying our Senior Bond (stadium) debt, that the TSA would accumulate operating reserves in the early years, while the stadium is constructed, and would draw upon those same reserves after the stadium opens and our operating costs are increased dramatically. Furthermore, we are obligated to establish several reserves: Capital repair and replacement at a level of $25 million (2000 Net Present Value), Cactus League bond reserve at $3.24 million, Youth & Amateur Sports at the prior year funding level (currently $1.2 million), and an operating fund reserve equal to one year's spending (board policy).

The Performance Audit does not suggest how to measure what contributions are "not necessary to sustain TSA operations". In fact, each of the options that are suggested would potentially take operating revenues away when they are most needed, in the event of a future calamitous drop in tourism taxes along the lines of the more than 20% decline experienced after the events of "9-11". A change to the NFL Income Tax via legislation would undo the original intent of the legislation which was to provide a stable source of funding for the Authority – one that was not only meant to meet debt service, but also to help provide funding for the Authority's operations.

A change would also be viewed by bondholders as not only impacting the Authority's ability to re-pay debt service, but also as a negative influence on the Authority's ability to operate at a standard sufficient to operate the future stadium. This has a reciprocal effect of potentially diminishing our revenues from other events which further diminishes the Authority's financial standing. Furthermore, a change would also create an uncertainty and mistrust in the marketplace for future bond issues of the Authority, and any other agency or subdivision of the State of Arizona.

While it is true that the Appeals Court ruling in the Long litigation limits our ability to pledge the income taxes toward our Senior Bonds, and this fact is pointed out in our Official Statement, that should not be confused as an invitation to do something that is highly unusual; namely, to reduce or eliminate a funding source that is relied upon to make bond debt service payments, after the bonds have been sold. The Official Statement disclosure regarding the legislature's ability to change the NFL Income tax was included for one of the primary reasons that an Official Statement exists – to provide prospective bond purchasers with all of the risks and issues surrounding a sale – whether or not there is a likelihood of such a risk actually occurring. Its inclusion was not intended to be a catalyst for such a change, but to meet all securities disclosure requirements.

Finding No. 3—Defined Processes will help TSA Effectively Evaluate Grant Applicants

The Authority has spent the better part of 2003 working to elevate the public's understanding of our youth & amateur sports grant program and our Cactus League facilities grant program. In particular, we have placed a heavy emphasis on involvement of stakeholders in our youth & amateur sports grant award process through the establishment of a 20-member Youth & Amateur Sports Advisory Committee, the conducting of a Youth Sports Summit in February 2003, and the conducting of three youth sports town halls in April 2003. We have also worked with the Maricopa County Stadium District, various municipalities, and other stakeholders of Cactus League baseball to improve communication on Cactus League spring training matters and to initiate discussions regarding Cactus League baseball leases well in advance of the lease expiration dates.

We are pleased that the audit acknowledges the Authority's work that is well underway to improve the youth sports grant award process. As a result, in response to a Request for Proposals that was posted and advertised in July 2003, the TSA received 92 applications totaling $35.2 million in September 2003. With the help of our 20-person Youth & Amateur Sports Advisory Committee of citizen stakeholders, we spent the next three months extensively reviewing each of the 92 applications. Last month, the TSA Board of Directors awarded $1.3 million worth of grants to the 13 projects ranked most highly by our citizen advisory committee. Another $600,000 worth of grant monies are under further review for possible grant awards by this summer.

Meanwhile, a $6.6 million Cactus League improvement project was completed at Phoenix Municipal Stadium, while two others are under discussion and negotiation with Scottsdale (the Giants) and Tempe (the Angels).

Finding No. 4—Administrative Practices; TSA is not a State Agency; Procurement Policies Needed: Legal Services; Travel Policy; Financial Controls

TSA is not a State Agency—The TSA agrees that as a municipal corporation, many of the usual standards or guidelines applied to state agencies do not apply to the Authority. We understand that three other municipal corporations examined by the Auditor General have policies in place in these areas to one degree or another. However, we also understand that those three agencies are from 32 to 100 years old and question whether or not their policies were in place when they were just barely two years old. (The three were SRP, the Arizona Power Authority, and the Central Arizona Water Conservation District).

Nevertheless, we agree that we need to establish more formal procedures in each of the areas outlined in the audit and are already in the process of implementing these recommendations as follows:

Procurement Policy—Although the TSA is exempt from the procurement code, we have used a procurement process for many major contracts. For example, construction consulting, stadium concessionaire, stadium management and marketing, and youth and amateur sports grants are a few of the very important contracts resulting from an open, competitive bidding process. As we evolve into a more normal operating mode, without the crunch of tight timelines associated with the major stadium project in Glendale, we will adhere to a formal procurement policy that is currently under development for approval of the Board of Directors.

Agreement Ratification Timeframes and Monitoring Procedures—These recommendations are agreed to and are being implemented.

Use of Legal Services-- TSA disagrees with this conclusion and believes that our outside law firm has done an outstanding job representing the TSA in our negotiations with a wide variety of interests, both public and private. The Board of Directors is very satisfied with their work and do not see the need to issue a request for proposals for legal services until the multipurpose facility is completed, at the earliest. Continuity is critical until we complete the major agreements that will govern our relationships and our interests over the next three decades. Short of another lawsuit, we do not see ourselves retaining the services of any other law firm during the next three years.

We are continuing to negotiate and draft complex legal agreements that will govern the operation and maintenance of the $370.6 million multipurpose stadium facility in Glendale over the next three decades, and now is not the time to be "changing horses in mid-stream" with respect to our expert outside legal advisors. The firm we are using has great experience in these areas and is very familiar with our legislative and organizational history.

The use of in-house attorney was considered and deemed less cost-effective than the use of outside counsel until the stadium is opened and an in-house attorney is hired to handle more routine claims and contracts. An in-house attorney would have been more expensive than outside counsel for the very limited work that would have been entrusted to the quality of attorney likely to come to work for TSA as in-house counsel (in-house would have only handled minor agreements and limited board matters such as agendas and minutes). The public would not be well served by the TSA's use of a relatively inexperienced attorney on anything other than the basics. The conundrum for the Authority is that once the complex, 30-year development, management, and use agreements are in place, in-house counsel will help prepare and update vendor and promoter contracts, and deal with injury claims from patrons and users of the facility. This is not the type of legal work that would lead a seasoned attorney to leave private practice. Therefore, the plan is to continue using our present legal firm until all major agreements are in place, and to hire an in-house attorney as the opening of the facility draws near.

Policies to Better Control Certain Expenditures--The Authority agrees that strong internal financial controls are a requirement in any size organization and has, from its inception, taken steps to ensure that these controls are in place. The Authority agrees that it will formalize its already established financial and accounting practices and policies. These controls and financial transactions have been reviewed and tested by the Authority's independent, outside audit firm, Ernst & Young, in accordance with A.R.S. 5-841, which requires an annual financial audit be performed. Ernst & Young has completed three annual audits of the Authority with no qualifying opinions.

The Authority has an established, well-documented audit trail with respect to its financial transactions that focuses on involving at least two employees in the completion of those transactions. This system has been created due to the Authority's small staff size of five full-time employees. Of the Authority's five person staff, three employees are typically involved in the handling, recording and payment of all vendor/contract transactions. In addition, the President/CEO reviews and approves the monthly bank statement reconciliations prepared by the Chief Financial Officer. The Authority agrees to create a matrix that details the Authority's financial transactions, the employees involved and their respective roles to further strengthen the already existing separation of duties.

TSA Should Ensure that Travel Policy is Followed--As a municipal corporation, the Authority is not governed by state travel regulations. However, the Authority has voluntarily developed travel reimbursement policies that are similar to state travel regulations. Contrary to the finding in the performance audit, all travel, in fact, was approved by either the Executive Director (President/CEO), or in the case of the Executive Director, by the TSA Board Chairman. The Authority has developed and is using forms for trip requests, trip expenses, and trip reports that will provide the necessary written record of such approvals and will address any expenses that deviate from written guidelines.

Further Guidance Needed for Providing Gifts—The Authority disagrees that it has provided "gifts". The items in question were for business meals, flowers, and commemorative photos and plaques—all items that are not considered to be "gifts" under state law. In fact, while the TSA may be exempt from the constitutional gift giving ban, we have gone beyond the requirements of state statute by developing a restrictive board policy that covers both gift-giving and gift-receiving that all board members and employees are expected to follow.

TSA Should Strengthen its Internal Controls—We agree with these recommendations and are in the process of implementing the suggested changes. We should note that three consecutive annual financial audits from the firm of Ernst &Young have not raised any issues.

TSA Should have a Policy Governing the Use of Game Tickets and Suite Controlled by the Authority—The Authority already has a policy, which is referred to in both our Cardinals' and Fiesta Bowl Use Agreements. The suite and tickets that are controlled by the TSA were a negotiated concession from our two tenants (who otherwise had the rights to these seats) so that the Authority would have these seats to use in conjunction with the promotion and marketing of the multipurpose facility. We will be using them to help attract additional events and promoters to the facility as well as to recognize those companies that are already bringing business to the multipurpose facility. It is the Board's intent and fervent goal to bring numerous non-football events to the multipurpose facility, and the suite and game tickets will be used to help promote and secure those events. As the opening of the multipurpose facility nears, the Board will work with our stadium management and marketing partners to ensure the use of the suite and allotted tickets has a favorable business impact.

TSA Should help Ensure that Prop 302 Monies only Benefit Maricopa County--We agree and met with the Arizona Office of Tourism and their Prop 302 implementation team in November 2003 to discuss their past use of these funds and their plans for 2004. At our meeting we learned that 5% of these monies are retained by the Arizona Office of Tourism (the other 95% is apportioned amongst various local convention and visitor bureaus); however, the AOT insists that their 5% was spent by AOT in ways that benefited tourism in Maricopa County, not statewide, which is consistent with the statute.

ARIZONA TOURISM & SPORTS AUTHORITY
2004 OBJECTIVES

MULTIPURPOSE STADIUM FACILITY MATTERS

- Keep the MPF Project "On-Time" and "On-Budget"
- Preserve Public Interest Criteria
- Successful Integration of Support Infrastructure Work into Overall Project
- Conclude Negotiations and Execute Contract with Stadium Management and Marketing Firm(s)
- Begin to Build Marketing Campaign for Events in 2007 and Beyond
- Work with the Fiesta Bowl on Design, Cost and Build-out of any Additional Spaces and Features Requested and Paid for by the Bowl to Help Ensure our Selection as the Site for the 2007 BCS National Championship Game.
- Planning for Super Bowl XLII in 2008
- Aggressively seek to host NCAA Men's Basketball games and tournaments, including the Regional Finals and the "Final Four" championships
- Successful Utilization of Glendale Community Advisory Committee on Neighborhood Matters
- Access for the Disabled Advisory Committee
- Achieve Disadvantaged Business Enterprise Goals
- Create VIP Observation Program to Track Progress on Construction

TOURISM PROMOTION AND MARKETING

- Ensure the effective integration of the MPF Marketing Team with the City of Glendale, the Glendale Chamber of Commerce, Westmarc, the Arizona Office of Tourism and the established Valley Convention & Visitor's Bureaus (Greater Phoenix, Scottsdale, Tempe, and Mesa).
- Develop ways to market with a "tourism angle" those bookings and events at the MPF that will positively impact the tourism industry and generate room revenue.
- Coordinate with the AZ Office of Tourism's "Prop 302 Committee" their recommendations for tourism promotion to be funded from Authority's "pass-through" monies to the AZ Office of Tourism.

CACTUS LEAGUE MATTERS

- Complete Phoenix Municipal Stadium Renovations by Feb. 2004
- Conclude Negotiations, Execute Necessary IGA's, and Begin Improvements for Scottsdale Giants and Tempe Diablo Stadiums
- Implementation of TSA-MCSD Intergovernmental Agreement
- Continue Discussions with Interested Host Communities regarding Future Expansion of Cactus League
- Develop Ways to Market the Cactus League Experience in Maricopa County and Boost Related Tourism
- Coordinate with State Department of Commerce on Publication of the Cactus League Guide and making it available on the AZ-STA website.
- Develop "Cactus League Fan Fest" for Board consideration that ultimately could be held at the new stadium in Glendale during the Cactus League season in March.

ARIZONA TOURISM & SPORTS AUTHORITY
2004 OBJECTIVES

YOUTH AND AMATEUR SPORTS MATTERS

- Make Grant Awards to be Effective July 1, 2004, Totaling a Minimum of $2M, to be matched by at Least $1M
- Increased Leverage of TSA Grant Awards to Produce a Larger Total Project Amount
- Implement Robert Wood Johnson Foundation Initiative (assuming we get award)
- Conduct 2nd Youth Sports Summit
- Complete Geographic Information System
- Begin Assessment and Evaluation of Effectiveness of Youth Sports Grants
- Consider Biennial Budget Cycle for YAS Grant Awards

TSA OPERATIONS

- Continue Increased Focus on Cactus League and YAS Matters
- Add Marketing/Outreach Position
- Add Accounting Position to Assist with More Complex Fund Accounting and Increased Transactions
- Address Issues Related to 2004 Performance Audit
- Integrate with Activities of Selected Stadium Management and Marketing Firm(s)
- Take steps to protect the Authority's bond ratings and financial condition
- Develop possible framework for a AZ-STA Foundation that would raise monies for scholarships and/or charitable purposes

Performance Audit Division reports issued within the last 12 months

02-03 Department of Economic Security—Kinship Foster Care and Kinship Care Pilot Program
02-04 State Parks Board—Heritage Fund
02-05 Arizona Health Care Cost Containment System—Member Services Division
02-06 Arizona Health Care Cost Containment System—Rate Setting Processes
02-07 Arizona Health Care Cost Containment System—Medical Services Contracting
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