Date: March 21, 2013

To: City of Miami Commissioners

From: Theodore P. Guba, CPA, CIA, CFE, Independent Auditor General
Office of the Independent Auditor General

Subject: Review of First American Telecommunication Corporation Permit Fees and Payphone Revenue Commissions Remitted to the City of Miami
Review No. 13-001

We have completed our review of the City of Miami’s (City) agreement with First American Telecommunication Corporation (FAT), which expired May 10, 2002. The one-year agreement was approved pursuant to City Resolution 01-449 (Res 01-449) on May 10, 2001. The resolution authorized City management to initiate, administer and evaluate a one-year pilot program in which FAT, at its sole cost and expense, installed payphone kiosks within selected City right-of-ways (ROW). According to the resolution, one of the main objectives of the program was to “Promote revitalization and redevelopment of the City and to encourage the reduction of visual blight.” In addition to remitting permit fees for payphone installations, as required by City Code Chapter 54, Article XI, FAT agreed, as part of the pilot program, to pay the City 15% of its advertising revenue generated by vendors placing ads on kiosk panels.

It should be noted that a previous “Audit of the Pay Telephone PILOT Program” (Audit No. 03-005) was performed covering the period primarily May 2001 through May 2002. Accordingly, we followed up on management’s implementation of previous relevant audit recommendations.

This review was conducted as a result of a special request by a Commissioner to the Office of the Independent Auditor General (OIA G). The observations and conclusions described herein are confidential and are exempt from Chapter 119, Florida Statutes (FS119).
SCOPE, OBJECTIVES AND METHODOLOGY

The scope of the review was to confirm that FAT complied with various commitments under the one-year pilot program as set forth in Res 01-449, and in a letter dated February 19, 2001 from FAT to the City Manager that addressed advertising. The review covered the period October 1, 2007 through September 30, 2012, and focused on the following objectives:

- To determine the actual amount of permit fees the City earned via the operation of FAT phones within the City during fiscal years 2008 (FY08) through 2012 (FY12).
- To determine the actual advertising revenue FAT earns from its phone kiosk panels and whether the City is receiving 15% from such revenue as stipulated in Res 01-449.
- To determine if there were kiosks sited outside of the designated pilot program area.

We conducted the review in accordance with Generally Accepted Government Auditing Standards. Those standards require that we plan and perform the review to obtain sufficient, appropriate evidence in order to provide a reasonable basis for our observations and conclusions based on our review objectives. We believe that the evidence obtained provides a reasonable basis for our observations and conclusions based on our review objectives. The review methodology included the following:

- Interviews and inquiries of appropriate personnel
- Review of City Code and State of Florida legislation
- Inspection of various payphone kiosk sites
- Calculation and verification of permit/advertising revenues
- Tests of applicable transactions and records
- Other audit procedures as deemed necessary

BACKGROUND

The terms of the agreement/pilot program were set forth in Res 01-449 and were also based on a letter dated February 19, 2001 from FAT to the City Manager. In the letter, FAT agreed: to pay the City 15% of the advertising revenue generated from the kiosk ads; to not advertise tobacco and liquor products; and to provide free advertising that promoted City services and events. During the course of our review we learned that FAT does not sell advertising, but instead, charges a “Guaranteed Minimum Rent” for exclusive use of the kiosk advertising panels to a third-party advertising agency (Vector Media). Accordingly, FAT pays the City a 15% commission from the advertising-related revenue it receives from Vector.

As noted previously, the term of the agreement/pilot program was only for one-year. However, FAT has continued to pay yearly permit fees and advertising-related revenue commissions to the City from 2001 to the present. During fiscal years 2008 (FY08) through 2012 (FY12), we verified that the City earned $107,820 and $41,805 in permit fees and commissions, respectively. Currently, FAT pays the City $9,360 annually in commissions. Permit fees are $185 per phone including a $10 inspection fee. For FY13, in order to operate 96 phones (including 52 kiosk phones) FAT paid permit fees of $17,760.

OBSERVATIONS
• Contrary to the provisions stipulated in Res 01-449, many advertising panels on the kiosks display liquor advertisements (ads). However, it should be noted that there is no City Code prohibition against liquor advertising and that other advertising platforms in the City, including billboards, bus bench panels, etc., advertise liquor.

• The agreement specified that kiosks have “two single advertising panels located on opposite sides of the new standardized enclosure”. However, we observed that most kiosks have three advertising panels. This is in conformity with Florida Statute Chapter 337.408 (FS 337.408), which expressly authorizes three advertising panels of payphone kiosk advertising. FAT informed us that 40 free panels (the third panel) are provided to the City’s Downtown Development Authority (DDA) for city use, as well as “wayfarer” maps at the majority of kiosk locations as requested and designed by DDA. As such, FAT is forgoing revenue of $50 a panel, or $2,000 a month. In addition, FAT informed us that they absorb costs of $30 to print each advertisement poster (or $1,200 for 40 posters) and another $25 in installation costs (or $1,000 for 40 posters). As previously noted, the use of free advertising kiosk space to promote City services and events is in accordance with the provisions of the agreement.

• Of the 52 kiosk phones currently permitted, only one (1) phone is situated outside of the designated pilot program area. The phone is located at NE 60th Street and US 1 and has a valid City permit. Proper permits appear to have been issued by the City for all pay phones and kiosks under both the City Code and state law since the expiration of the pilot program in 2003.

**FINDINGS AND RECOMMENDATIONS**

The City should formalize the current payphone revenue commission arrangement by entering into a written contractual agreement with FAT and clarify the above observations. The agreement should set forth provisions that not only facilitate the collection of rent/advertising revenue commissions, but also the City’s right to audit FAT contracts and accounting records in order to ensure that the City’s commission revenue is optimized. If this is done the following should be considered:

1. **Enhance Recurring City Revenue by at Least $25,000 by Amending the City Code to Require the Collection of Permits and Commissions for All Phones Installed On All City Right of Ways:**

For the 52 kiosk phones permitted for FY13, FAT rents two advertising panels per kiosk to Vector Media for $50 per panel (or $100 per kiosk). As such, FAT receives $5,200 monthly ($62,400 annually) from Vector of which 15% is remitted to the City as a commission. However the City is currently foregoing additional revenues from pay phones located on Florida Department of Transportation Right-of-Ways (FDOT ROWs) due to Chapter 54 of the City Code which states that, “No pay telephone permit shall be issued by the city within a state road right-of-way.” It should be noted that the City Code apparently contradicts FS 337.408 which requires public payphone providers (such as
FAT) to obtain written authorization (i.e., a permit) from the City in order to install public payphones within FDOT ROWs.

We observed that there are 70 kiosk phones sited along the FDOT ROW at Biscayne Boulevard and Brickell Avenue (US 1), Flagler Street, 79th Street, and SE and SW 8th Street (US 41). As such, Chapter 54 of the Code prevents the City from earning at least an additional $25,550 of annual revenues ($12,950 permit fees and $12,600 rent commissions of 15%).

Finally, we were informed that the cost of purchasing and installing a phone kiosk approximates $4,000-$4,500. Given monthly rent collections of $50 per advertising panel or $100 per kiosk; and the 15% commission paid to the city, the cost of a kiosk is recovered within four to five years of its installation. Since most installations occurred more than five years ago, the costs of current installed kiosks have most likely been fully recovered. Therefore, it would be reasonable for the City to collect a commission percentage in excess of 15%.

**Recommendation 1**

To increase City revenue, we recommend that the City Code be amended to allow the permitting of public pay telephones (PPT’s) on all ROW’s within the City limits. Revenue would be further enhanced by collecting a percentage of the rent/advertising income generated by kiosks in excess of the current rate of 15%

**Management Response**

**City Manager**

“Written authorization” may not necessarily mean a city permit. For ROW permit requests with FDOT, concurrence letters are typically provided by the City on behalf of private entities who enter into a covenant with the city to abide with certain stipulations. This might be the way to proceed. Upon direction from the City Commission, PW will prepare the necessary legislation. Lastly, other locations of payphones and kiosks are being inspected on state ROW’s.

2. **Require a Benefit to the City for Any Advertising Revenue Share Paid to FAT:**

FAT’s legal counsel informed us that FAT’s advertising agreement with Vector contains confidentiality provisions which prevent the disclosure of certain business information. Therefore, in order to better understand the advertising fees being charged for the kiosk panels, we contacted Vector and inquired about its advertising rates. We learned that including a $75 set-up charge, an advertising panel could cost $800 per month or $1,600 per kiosk (for two panels)—such prices are negotiable depending on the number of kiosks used.

In addition, with the permission of FAT’s legal counsel, we reviewed a “Revenue Share” provision in FAT’s agreement with Vector which stipulated that Vector must calculate and pay to FAT on an annual basis, any excess of 50% of Annual Net Advertising
Revenue earned during a contract year over the total of the guaranteed minimum rent and the Lease of Equipment ($10 per panel per month which FAT uses to offset its repair and maintenance costs) paid to FAT for that time period. Although we noted that no revenue share has been paid to FAT for the scope period of our review, if such “Revenue Share” thresholds are met, there might be other advertising revenue streams accruing to FAT that could, potentially, accrue to the City. However, the City currently has no contractual arrangements with FAT which give the City the right to audit this arrangement and demand such revenue.

**Recommendation 2**

We recommend that revenue sharing, as well as “right to audit”, provisions be inserted into a contract with FAT to operate PPT’s within the City limits.

**Management Response**

**Public Works**

Upon direction from the City Commission, PW will work with other departments to prepare the necessary legislation and procurement.

3. **Assign Responsibility to Monitor Compliance with the Provisions of the FAT Contract:**
   The total number of PPT kiosks with ad panels on all ROW’s within the City’s boundaries (i.e. City, County, and State roads) as well as the applicable ad-related revenues should be monitored. Currently, PW staff is only responsible for the initial permitting and inspection of such kiosks.

**Recommendation 3**

We recommend that once a contract is in place with FAT, that the City’s Finance Department (FD) work with PW in order to ensure that the number of kiosks and advertising panels are counted and used as a basis for collecting and monitoring permit and commission revenues.

**Management Response**

**Public Works**

Upon direction from the City Commission, PW will work with other departments to prepare the necessary legislation. In addition, verification is needed before implementation that the state statute (F.S.) allows local municipalities to grant permits on FDOT ROW.

**Finance Department**

Agree with recommendation. Once a Director of Finance is hired, this will be assigned for follow-up to work closely with Public Works to monitor and report information to the CMO.

**Overall Recommendation for Consideration**
As an alternative to entering into a specific contractual arrangement with FAT, the City may also consider amending Chapter 54 of the City Code to allow any pay telephone provider to operate advertising kiosks within City or FDOT rights-of-way under a uniform set of standards and criteria, including the requirement of yearly audit, a formula for sharing advertising revenue, etc.

The City may also wish to consider creating greater value for the pay phones as an advertising and revenue-generating platform for both FAT and the City. This could include working with FAT to improve locations and visibility of the kiosks to enhance the advertising value of the advertising panels. The greater the advertising revenue stream to FAT, the higher the revenue to the City. As a corollary to this recommendation, the City should undertake a broader review of the value of all other advertising platforms and street furniture on City streets and rights-of-ways to determine if it is receiving a reasonable return from them.

We appreciate the cooperation extended to us by all City and FAT personnel contacted during this review. If you have any questions, please feel free to contact me at 305-416-2044 or by email.

Cc: Tomas Regalado, Mayor
    Johnny Martinez, City Manager
    Julie O. Bru, City Attorney
    Todd Hannon, City Clerk
    Alice Bravo, Assistant City Manager/ Chief of Infrastructure
    Janice Larned, Assistant City Manager/ Chief Financial Officer
    Daniel S. Goldberg, Esquire, Legislative Aide
    Frank Castaneda, Executive Assistant
    Ron Nelson, Chief of Staff
    Diana Valeriano, Chief Administrative Assistant
    Mike Lorente, Chief of Staff
    Cornelius Shiver, Chief of Staff
    Erick Duran, Administrative Assistant
    Zerry Ihekwaba, PhD, PE, Director, Public Works Department
    Fabiola Dubuisson, Engineer II, Public Works Department
    Members of the Audit Advisory Committee
    Audit Documentation File

Special project conducted by: Lewis Blake, CPA, CIA Senior Staff Auditor
Special project reviewed by: Munirah Daniel, CPA Senior Staff Auditor