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To: Members of the Legislative Audit Committee

From: Kundinger, Corder & Engle, P.C.

Date: August 13, 2004

Re: Colorado Tourism Office

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## **Background**

The Colorado Tourism Office (Office) was created under Title 24, Article 49.7 of the Colorado Revised Statutes to promote the coordinated development of tourism and travel in Colorado. The Colorado Tourism Office is governed by a Board of Directors consisting of 13 members. Of the 13 members, one member is appointed by the Speaker of the House from the House of Representatives, one member is appointed by the President of the Senate from the Senate, and the remaining members, representing various tourism-based industries, are appointed by the Governor and approved by the Senate. Administrative oversight is provided by the Office of Economic Development and International Trade within the Governor's Office.

To carry out its mission, the Colorado Tourism Office oversees the following activities:

1. Operation of the State's eight Welcome Centers, located at the major highway gateways to Colorado, that provide travel information to motorists.
2. Advertising and public relations funded by the State in conjunction with private partners.
3. Customer response services and promotional materials, including maintenance of the official state travel Web site, [www.colorado.com](http://www.colorado.com), the 1-800-COLORADO telephone information center, and publication and distribution of the Colorado Official State Vacation Guide.
4. Research on trends in the Colorado travel and tourism industry and the economic impact of the industry in the State.

## Summary of Appropriations, Revenue, and Expenditures

The Office is primarily funded through general fund appropriations. The financial summary below also reflects non-state monies received by a contractor on behalf of the State from the sale of advertisements in the Colorado Official State Vacation Guide and on the Colorado.com Web site. The following summary is for Fiscal Years 2003 and 2004:

<b>Colorado Tourism Office Appropriations, Revenue, and Expenditure Summary For Fiscal Years 2003 and 2004</b>		
	<b>Fiscal Year 2003</b>	<b>Fiscal Year 2004</b>
<b>Appropriations and Revenue</b>		
<i>Appropriations</i>		
Cash and General Fund Appropriation	\$ 5,697,852	\$ 3,264,989
Economic Stimulus <sup>1</sup>	9,000,000	-
Limited Gaming <sup>2</sup>	181,964	-
Subtotal Appropriations	\$14,879,816	\$3,264,989
<i>Revenue</i>		
Advertising Income <sup>4</sup>	1,782,124	1,778,932
Sponsorships	121,425	144,560
In-kind Donations		30,040
Interest and Other	41,669	132,484
Subtotal Revenues	\$1,945,218	\$2,086,016
Total Appropriations and Revenue	16,825,034	5,351,005
<b>Expenditures</b>		
Professional Services <sup>3,4</sup>	7,589,453	12,076,264
Salaries	234,413	321,611
Grants	389,588	321,893
Other	169,789	398,407
Total Expenditures	8,383,243	13,118,175
<b>Net Income (Loss)</b>	<b>\$ 8,441,791</b>	<b>\$ (7,767,170)</b>
<p><b>Source:</b> Data obtained from the Colorado Tourism Office. Revenue and expenditures reflect adjustments identified during review of Fiscal Years 2003 and 2004, performed by Kunding, Corder &amp; Engle, P.C. under contract with the Office of the State Auditor.</p> <p><b>Note:</b> Statutes allow monies remaining in the Colorado Travel and Tourism Promotion Fund and the Colorado Travel and Tourism Additional Source Fund at fiscal year-end to remain in the funds and not revert to the State's General Fund. Total combined fund balance for both funds as of June 30, 2003 and June 30, 2004 was \$8,803,431, and \$1,036,261, respectively.</p> <p><sup>1</sup> Under S.B. 03-202, \$9,000,000 was transferred to the Colorado Tourism Office as part of a Supplemental General Fund appropriation to provide economic stimulus.</p> <p><sup>2</sup> Under S.B. 03-274, the annual transfer from the Limited Gaming Fund to the Colorado Tourism Office was suspended for Fiscal Year 2004.</p> <p><sup>3</sup> Contractual services for advertising and promotion.</p> <p><sup>4</sup> Reflects adjustments identified related to airline tickets received during Fiscal Years 2003 and 2004.</p>		

## **Purpose and Scope of Review**

This engagement was conducted under the authority of Section 24-49.7-108, C.R.S., which authorizes the Office of the State Auditor to review the manner in which moneys from the Office's Travel and Tourism Promotion Fund and the Travel and Tourism Additional Source Fund are expended, any contracts entered into pursuant to the statute, and the activities of the Board and the Office to ensure compliance with the statute. According to Section 24-49.7-106, C.R.S., all monies in the Travel and Tourism Promotion Fund and the Travel and Tourism Additional Source Fund remain within the Funds and do not revert to the State's General Fund.

Under contract with the Office of the State Auditor, the firm of Kunding, Corder & Engle, P.C. conducted certain agreed-upon procedures in order to evaluate and report on the activities of the Colorado Tourism Office and the Board of Directors to ensure compliance with the provisions of Article 24-49.7, C.R.S. The procedures performed included a review of the annual operating budget; examining contracts held by the Office and its vendors; and the manner in which monies from the Travel and Tourism Promotion Fund and the Travel and Tourism Additional Source Fund were expended and whether those moneys were expended in accordance with the statute; review of the advertising contractor policies for applying doubtful accounts, discounts, or price breaks to advertisers; and evaluating the Office's system of internal controls over revenues and expenditures. For the revenues tested, we verified that revenues agreed to the contracts and the rates set by the Board. For expenditure testing, we verified that expenditures were properly recorded. In addition, we assessed the implementation status of prior recommendations from the August 16, 2002 report on the Office conducted by Kunding, Corder & Engle, P.C. The current report covers the period from July 1, 2002 to June 30, 2004 or Fiscal Years 2003 and 2004. The following presents the findings and recommendations resulting from this review.

## **Comments and Recommendations**

The Colorado Tourism Office engaged the services of Checkmark/PDI, LLC., (Checkmark) to publish and print the Official State Vacation Guide (Guide) for Fiscal Years 2003 and 2004. Checkmark's responsibilities also included maintaining and enhancing the official State tourism internet Web site (Colorado.com), operating the visitor information telephone service (1-800-COLORADO), and filling requests for travel information from the database of Colorado travel information gathered from in-bound calls, reader's service leads, and mail-in and Internet page requests. In addition, Checkmark was responsible for selling and collecting all revenues generated from advertising sales related to the Guide and the Colorado.com Web site and applying these revenues to pay for advertising sales commissions and other related contract expenses as directed by the Board. For Fiscal Years 2003 and 2004, Checkmark was paid \$716,237 and \$1,519,750, respectively. Advertising revenue generated by Checkmark totaled \$1,782,124 and \$1,778,932 for Fiscal Year 2003 and Fiscal Year 2004, respectively. The contract with Checkmark was due to expire on June 30, 2004 but was extended through July 31, 2004 in order to complete the transfer of responsibility to the new vendor, Weaver Publications, Inc.

The new contractor was engaged as of August 27, 2004 after a request for proposal process and is responsible for the same scope of services as those specified under the agreement with Checkmark. However, the new contract is structured differently, which could change the nature of the relationship between the Office and the contractor and may, therefore, affect the responsibilities of the Office and the way revenues and expenditures are recorded on the State's accounting system. Since these issues were not resolved at the conclusion of our audit, Recommendation No.1 below assumes that the Office will

have the same responsibilities as under the previous contract. Issues related to the new contract are discussed in Recommendation No. 3.

### **Oversight of Monitoring Financial Information and Vendor Contracts**

During our onsite fieldwork at Checkmark, we tested revenues and expenditures for Fiscal Year 2003 and 2004. We were able to agree revenue and expenditures from Checkmark's accounting records to those recorded on the State's financial system by the Office, although several adjustments related to noncash transactions were noted which are discussed later in this report. We found opportunities for strengthening the Office's controls over the contractor (referred to below as the "advertising contractor").

*Monitoring of financial information.* The Office's contract with its advertising contractor states that Checkmark shall maintain appropriate accounting records and shall provide the Board with a full accounting of all revenues and their application on a monthly basis.

- In our report issued on August 16, 2002, we recommended that the Office develop procedures to monitor Checkmark's activities to ensure the completeness and accuracy of advertising revenues collected and expended. The Office agreed with the recommendation. During our current review, we noted that the Office performed a review of Checkmark's activities for Fiscal Year 2003 and tested a random sample of 100 advertisers to verify the accuracy of revenues reported by Checkmark for that year. The Office did not perform a review for Fiscal Year 2004, in part because the Office believed the review by the auditors would be sufficient. The Office's management is responsible for having adequate controls in place to monitor the revenues and expenditures on an on-going basis.
- We also noted that the only financial report provided by Checkmark to the Office was the profit and loss statement. During Fiscal Year 2003, this statement was provided to the Board on a sporadic basis and in Fiscal Year 2004 the statement was provided on a more regular basis, but not on a monthly basis, as required under the agreement. Therefore, the Office was not able to monitor the activity of Checkmark on a regular basis. In addition, because the profit and loss statement is only part of the financial picture, the Office should also obtain the balance sheet and budget information in order to review cash, accounts receivable, accounts payable balances, and compare the financial information with the budget approved by the Office. These balances directly affect advertising revenue and expenditures.

*Oversight of vendor contracts.* Under the terms of the contract with the Office, the advertising contractor is responsible for entering into contracts with vendors who advertise on the State's Web site or in the Guide. We noted the following problems with respect to these vendor contracts.

- The Board of Directors approves the advertising rates charged to the various companies that advertise in the Guide or on the Colorado.com Web site. We reviewed a sample of 35 contracts and in 16 cases we found that contracts did not detail the rates and amounts charged for the ads or specifically note when discounts were given. In addition, we encountered some difficulty in trying to recalculate the total sale amount for those contracts that had multiple ads, various ad sizes, and ads on more than one Web site location. After assistance from Checkmark staff, we were able to verify the amount of the contract sales. All terms and factors affecting the calculation of sales revenue should be clearly detailed in the contracts with ad vendors.

- We noted that the Office does not receive a detailed listing by vendor or contracts. In order for the Office to adequately oversee the advertising contractor, this information should be provided on a monthly basis. The Office should review this information and compare it to the income statement furnished by the vendor.
- We found that Checkmark wrote off accounts receivable totaling \$9,670 and \$4,769 during Fiscal Years 2003 and 2004, respectively. The contract between the Office and Checkmark did not require that Checkmark receive approval prior to writing off accounts deemed uncollectible. The Office should establish criteria for writing off accounts receivable and, on a periodic basis, obtain a listing of accounts receivable and the status of collections. The Office should review and approve all receivable balances that are determined to be uncollectible before they are written off.

Under good business practices contract management should include, among other things, monitoring the agreement. Although the contractor is obligated to perform the services outlined in the contract, the agency issuing the contract retains the overall responsibility to ensure that the services are provided and to protect the State's interests. By improving controls over contract activities, the Office will help ensure the terms of the contract are met and that the financial activity of the contractor is accurately and completely reported on the State's financial reporting system.

### **Recommendation No. 1:**

The Colorado Tourism Office should ensure the accuracy and completeness of financial activity reported on the State's financial system and improve its monitoring of its advertising contractor by:

- a. Ensuring that all advertising contracts issued by the advertising contractor accurately reflect all terms, such as rates and discounts, affecting sales revenue and contain appropriate detail, such as locations, size, and frequency of ads.
- b. Receiving detailed information, on a monthly basis, on all advertising sales generated by the advertising contractor;
- c. Establishing criteria for writing off uncollectible accounts receivable and requiring that the advertising contractor receive approval prior to recording such write offs.
- d. Ensuring that additional financial information is furnished to the Office, including monthly balance sheets and income statements, including comparisons with the budget approved by the Office and detailed information on expenditures made by the advertising contractor.
- e. Ensuring that routine onsite reviews of the financial activity of the advertising contractor are performed at least semiannually to determine that advertising revenue is properly reported and collected and expenditures are consistent with the budget approved by the Office.

### **Colorado Tourism Office Response:**

Agree. The Colorado Tourism Office has been exploring the concept of privatizing this function for some time but has been unable to fully explore this option until recently. By selecting a new contractor, Weaver Publications Inc., the nature of the relationship between the Office and the contractor has been changed. The new contract moves toward privatization and implements improvements in reporting. The Office is continuing to

improve and refine the deliverables from the new contractor as we move toward full privatization. Implementation Date: Fiscal Year 05.

### **Recording and Reporting Barter Transactions and Donations**

During our 2002 review, we found that the Office was not recording revenue and the related expenditures for airline tickets received from Frontier Airlines. The airlines provided the tickets in exchange for advertising space. The tickets were used by the Office for official business activities. We recommended that the Office record the revenue and expenditures related to the tickets, and the Office agreed with the recommendation. Currently, we found that the Office has the same type of arrangement with Frontier Airlines and is still not accounting for the tickets.

In our previous review we found that in Fiscal Year 2002, \$12,000 worth of airline tickets were received and \$3,000 was not properly recorded or adjusted as revenue for the year ended June 30, 2002. Because the agreement with the airlines spanned two fiscal years, the Office had \$9,000 worth of tickets remaining to be used in Fiscal Year 2003. Per inquiry of Office management, we found that about \$6,500 worth of tickets were used by the Office and not recorded in Fiscal Year 2003. As a result, Fiscal Year 2003 revenue and expenditures were understated by \$6,500. The remaining \$2,500 worth of tickets expired.

In Fiscal Year 2004, the Office entered into another agreement with Frontier for \$16,000 worth of airline tickets in exchange for advertising space. At June 30, 2004, the Office had used, and properly recorded the use of, \$4,000 worth of tickets. However, three tickets valued at \$800 were used by Checkmark employees on official business and were not recorded by the Office. The Office needs to implement procedures to ensure that all revenues and expenditures related to the airline tickets are appropriately reflected on the State's financial system. The remaining balance of \$11,200 in unused tickets at fiscal year end is due to expire on December 31, 2004. The Office was not certain that all of the tickets would be used by that date.

In addition, we found that Checkmark entered into a separate agreement with Frontier Airlines to receive tickets in the amount of \$9,500 in exchange for advertising space. At June 30, 2004, tickets valued at about \$1,130 had been used on official business by Checkmark, but not recorded by the Office. Checkmark therefore had approximately \$8,370 worth of tickets left at fiscal year end. Prior to the expiration of Checkmark's contract on July 31, 2004, it used an additional \$900 of the tickets. Because Checkmark was no longer under contract after that date, the remaining tickets worth \$7,470 expired. Although the Office was aware of Checkmark's agreement with the airlines, it did not monitor the use of the tickets. The advertising contractor should be required to notify the Office of the use of such tickets, including the individual's name, date of travel, and purpose of the trip. The advertising contractor should also inform the Office of in-lieu-of-payment agreements since these agreements affect recording of revenues and expenditures.

Under generally accepted accounting principles (GAAP), nonmonetary transactions should be recorded in a similar manner as monetary transactions. Amounts relating to nonmonetary transactions should be based on the fair value of the assets or services involved. The Office should record the advertising revenue and offsetting expenditure as the tickets are used. Further, *State Fiscal Rules* state that State agencies shall implement internal accounting and administrative controls that reasonably ensure that financial transactions are accurate, reliable, and conform to *State Fiscal Rules*. The Office is responsible for recording all transactions on the State's financial system in accordance with GAAP and should ensure that all such activities are recorded. The lack of procedures to track and record all activity related to the

airline tickets increases the risk of fraud and misappropriation of state assets. Further, the balance of unused airline tickets at both the Office and at Checkmark suggests that the Office should reevaluate the number of airline tickets that it and the advertising contractor are receiving through these arrangements. There should be sufficient business need to justify the amount of advertising being provided to the airlines in return for the tickets received.

**Recommendation No. 2:**

The Colorado Tourism Office should properly record barter transactions on the State's financial system in accordance with generally accepted accounting principles. In addition, the Office should reevaluate the number of airline tickets that it is receiving to ensure that all tickets are used before the expiration date. Furthermore, the Office should monitor the advertising contractor's use of agreements involving noncash payments in return for advertising and ensure that all related transactions by the contractor are recorded.

**Colorado Tourism Office Response:**

Partially Agree. The CTO substantially agrees with the recommendations. The Office has always maintained a tracking system for airline tickets and will require a similar tracking system from the contractor. For accounting purposes, this information will be reported on a quarterly basis to the Office of Economic Development and International Trade, which provides administrative oversight for the Office. A new contractor has been engaged to provide the services formerly provided by Checkmark and the new contract requires monthly reporting, including both cash and non-cash transactions.

The reason the CTO partially agrees is because the Board does not accept airline tickets if it believes the number is unreasonable relative to the importance of the advertising. The Contractor, Board, and Office evaluate barter transactions to ensure the value of advertising does not materially exceed the value of the airline tickets and that projected travel needs are compatible with the number of ticket vouchers received. The Board not only considers the cash value of barter transactions but also the goodwill that is generated by these arrangements. The Office makes every attempt to use airline tickets received in barter transactions but is obligated to use these tickets wisely by not authorizing unnecessary travel. Implementation Date: Fiscal Year 05.

***Clarification of New Advertising Contract***

As previously stated, the Office contracts with a vendor to publish and print the Official State Vacation Guide (Guide), maintain and enhance the official State tourism Web site (Colorado.com), operate the visitor information telephone service (1-800-COLORADO), and fill requests for travel. The vendor for Fiscal Years 2003 and 2004 was responsible for selling and collecting all revenues generated from advertising sales related to the Guide and the Colorado.com Web site and applying these revenues to pay for advertising sales commissions and other related contract expenses as directed by the Board. If revenue was not sufficient to cover the costs related to these services, the State was responsible for funding the shortfall. All revenues and expenditures related to the contract were required to be recorded on the State's accounting system.

Similarly, the advertising contractor for Fiscal Year 2005, Weaver Publications, is responsible for selling and collecting all revenue generated from advertising sales related to the Guide and the Colorado.com Web site. The Office will pay about \$480,000 to Weaver Publications; however, the contract provides

that Weaver Publications will be responsible for collecting sufficient advertising revenue, estimated to be about \$2.2 million, to fully fund the activities specified under the contract. Further, Weaver Publications will bear the risk of revenue falling short of the expenditures for services required under the contract. This means that if Weaver Publications does not collect enough revenue to cover the costs related to scope of services, Weaver Publications will still be required to complete the services without seeking additional compensation from the Office.

Because Weaver Publications is bearing the financial risk, the question has been raised as to whether this is a fully privatized contract, or possibly a type of joint venture or partnership since the State will be contributing some funding. As of the end of our audit, the Office was consulting with legal counsel from the Governor's Office regarding possible contract amendments. In addition to consulting with legal counsel, the Office should continue to work with the State Controller's Office to ensure that transactions related to the contract are properly reported on the State's accounting system. Further, the Office should develop appropriate oversight activities to ensure that the responsibilities outlined in terms of the contract are fulfilled.

**Recommendation No. 3:**

The Colorado Tourism Office should continue to work with legal counsel and determine whether the arrangement with Weaver Publications, Inc., for Fiscal Year 2005 is a fully privatized contract, joint venture, or some other type of arrangement. Upon obtaining that information, the Office should:

- a. Consult with the State Controller's Office to ensure that financial activity related to the contract is appropriately reported on the State's accounting system.
- b. Establish appropriate oversight activities to ensure that the products and services required under the contract are successfully delivered. Activities should include submission of monthly financial information such as balance sheets, income statements and budget-to-actual comparisons based on the Office-approved budget, and detailed information on expenditures made by the contractor, including travel and other such costs incurred under the contract.

**Colorado Tourism Office Response:**

Agree. The Office has initiated conversations with the State Controller's Office to ensure that financial activity related to the contract and possible amendments will be correctly reported. The current contract requires monthly reporting of financial information including Profit and Loss, Balance Sheet, and accounts receivables. This should improve the monitoring of material issues affecting performance. The Office is continuing to work with the legal counsel from the Governor's Office and the State Controller's Office regarding possible contract amendments and further movement toward privatization. Implementation Date: Fiscal Year 05.

**Status of Prior Recommendations**

**Recommendation No. 1** - The Office should properly record the advertising revenue and related expenditures that are being collected and spent by the advertising contractor, the Office's contractor to publish the Official State Vacation Guide (OSVG), on behalf of the Office.



**Partially Implemented.** Although the Office recorded the majority of revenues and expenditures on the State's accounting system, some barter transactions were not recorded. See current year Recommendation No. 2.

**Recommendation No. 2** - The Office should develop procedures to monitor the contract activities of Checkmark to ensure the completeness and accuracy of advertising revenues collected and expended by advertising contractor and reported to the Office.

**Partially Implemented.** During 2003, the Office conducted a review of advertising contracts and compared the contracts to the accuracy of the information recorded on the advertising contractor's general ledger. Two discrepancies were noted and were satisfactorily resolved. However, the Office's review only covered Fiscal Year 2003. See current year Recommendation No. 1.

**Recommendation No. 3** - The Office should consider the feasibility and desirability of fully privatizing the contract with Checkmark (or the replacement vendor) upon expiration of the existing contract.

**In Process.** The Office has a new contract in place with a replacement vendor (Weaver Publications, Inc.) and is working with legal counsel to establish an arrangement that would privatize this activity.

**Recommendation No. 4** - The Office should record the usage of Frontier Airline tickets received in exchange for advertising space sold on the State's Web site.

**Partially Implemented.** See current year Recommendation No. 2.

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