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Audit Report

**AUDIT OF SMIRNOFF MUSIC CENTRE'S
LEASE PAYMENTS**

Calendar Years 2001 to 2006

(Report No. A08-011)

May 9, 2008

City Auditor

Craig D. Kinton

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Executive Summary

We reviewed Smirnoff Music Centre’s lease payments required by the Lease Agreement (Lease) between the City of Dallas (City) and Smirnoff Music Centre (Smirnoff / Live Nation, formerly House of Blues Concerts / Pace Amphitheatres).

We believe that, based upon our work and the work of Weaver and Tidwell, LLP (the outside Certified Public Accountants), Live Nation (formerly the House of Blues) owes the City a total of \$842,970. This amount is comprised of \$777,213 for underpaid Lease revenues and interest for calendar years 2001 through 2006, in addition to \$65,757 for the Certified Public Accountants’ fee.

Background Summary

Smirnoff Music Centre (SMC) is located at Fair Park in the City of Dallas. Prior to November 2006, SMC was leased and operated by House of Blues Entertainment, Inc. In November 2006, Live Nation, a publicly-traded live music company, acquired House of Blues. On January 30, 2008, the Smirnoff Music Centre changed its name to SuperPages.com Center.

Smirnoff Music Centre held 155 events during 2001 through 2004 and reported total revenue of \$79,295,241. The City received \$3,127,801 in lease payments and South Dallas Fair Park Trust Fund received an additional \$166,135.

The cause for the underpayment was House of Blues / Live Nation did not report and calculate the lease payments to the City in accordance with the Lease.

In addition, the City’s policy on complimentary tickets is unclear. It was customary for the House of Blues / Live Nation to make complimentary tickets available to City officials for events held at the Smirnoff Music Centre. Gift (complimentary) tickets were one of the items not reported by House of Blues / Live Nation in the revenue lease payments. However, without clear policies regarding the solicitation or acceptance of complimentary tickets, these transactions could be viewed as potential violations of either State statutes or City ordinances.

Summary of Recommendations

We recommend the City Attorney continue with the negotiation process with Live Nation for a settlement, take the necessary steps to collect the money due to the City, and provide proposals to the City Council and City Management to clarify the City’s policy on solicitation and acceptance of complimentary tickets to events held at Smirnoff Music Centre and other City-owned facilities.

Summary of Management’s Response

The City Attorney’s Office prepared the responses for the two recommendations identified in this report. They agreed with the two recommendations and provided comments with corrective action plans, as well as implementation dates. The complete response is included as Appendix III to this report.

Summary of Objective, Scope and Methodology

Our audit objective was to determine whether House of Blues / Live Nation’s payments to the City are accurate and calculated in accordance with the Lease.

The audit covered the period of January 1, 2001 through December 31, 2006. To achieve the audit objective, we:

- Interviewed House of Blues / Live Nation personnel regarding relevant business practices and procedures
- Reviewed and analyzed the House of Blues / Live Nation Lease Agreement with the City, payments to the City, income statements, general ledgers, sub-schedules, worksheets, event listings, schedules, contracts, and other relevant documentation

Based upon the audit work we performed for the audit period of 2001 through 2004, the City Attorney employed the services of outside Certified Public Accountants Weaver & Tidwell, LLP to conduct additional audit tests and determine an amount owed to the City.

Audit Results

Overall Conclusions

Based upon our work and the work of Weaver and Tidwell, LLP (the outside Certified Public Accountants), Live Nation (formerly the House of Blues) owes the City a total of \$842,970. This amount is comprised of \$777,213 for underpaid Lease revenues and interest for calendar years 2001 through 2006, plus an additional \$65,757 for the outside Certified Public Accountants' fee. The cause for the underpayment was the inaccurate calculation of revenue owed to the City by the House of Blues.

In addition, the City's policy on complimentary tickets is unclear. It was customary for the House of Blues / Live Nation to make complimentary tickets available to City officials and certain City employees for events held at the Smirnoff Music Centre. Gift (complimentary) tickets were one of the items not reported by House of Blues / Live Nation in the revenue lease payments. There may be valid reasons why the attendance of City officials or employees at events being held at City-owned facilities serves a public purpose. However, without clear policies regarding the solicitation or acceptance of complimentary tickets, these transactions could be viewed as potential violations of either State statutes or City ordinances.

Live Nation, formerly the House of Blues, owes the City of Dallas \$842,970

During the period, January 1, 2001 to December 31, 2006, Live Nation, formerly the House of Blues, did not accurately calculate and remit payments to the City in accordance with the Lease Agreement (Lease). Based upon our work and a projection by Weaver & Tidwell, LLP, Live Nation owes the City \$842,970 for underpaid lease revenue, interest and the outside Certified Public Accountants' fee.

Examples where House of Blues / Live Nation's revenue lease payments to the City were not reported, calculated, and submitted in accordance with the Lease include:

- Barter income reflected on House of Blues financial statements
- Assessments on interest income subject to the Lease
- Ticket sales
- Sponsorship income
- Parking and concessionaire income
- Gift tickets

**An Audit Report on –
Smirnoff Music Centre’s Lease Payments**

The Lease provides for the City to share revenues as follows:

1. Annual minimum guaranteed rental \$300,000 each year 2001 to 2003, and \$350,000 for 2004 and each year thereafter
2. Percentage of revenue, which is calculated as a percentage of Smirnoff / Live Nation’s gross ticket proceeds and revenues from other sources, less the annual minimum guaranteed rental
3. Flat fee of \$0.15 per ticket sold

The Department of Park and Recreation (PKR) receives the annual minimum guaranteed rental and the percentage of revenue. The South Dallas Fair Park Trust Fund administered by the Department of Economic Development (ECO) receives the flat fee lease payments.

As a result of the above mentioned errors and omissions, Weaver & Tidwell, LLP projected that Live Nation owes the City additional Lease revenue, plus interest, totaling \$777,213. Of this amount, \$694,893 is owed to PKR, and \$82,320 is owed to the South Dallas Fair Park Trust Fund.

In addition, the Lease states that audit costs will be recovered by the City if the underpayment exceeds 5 percent of the total rent actually paid. As a result, Live Nation also owes the City \$65,757 for the outside Certified Public Accountants’ fee.

Recommendation 1:

We recommend the City Attorney finalize the negotiation process with Live Nation for a settlement and take the necessary steps to collect the money due to the City.

Management’s Response

Agree. The City Attorney’s Office will continue the negotiation process with Live Nation and will make a recommendation to the Dallas City Council regarding a proposed settlement regarding the additional lease revenues identified in the audit. Upon approval of the City Council, the City Attorney’s Office will take all necessary steps to collect the money due to the City pursuant to the settlement agreement with Live Nation.

The City’s policy on complimentary tickets is unclear

During the course of this audit, we became aware that it was customary for the House of Blues / Live Nation to make complimentary tickets available to City officials and certain employees for events held at the Smirnoff Music Centre. Gift (complimentary) tickets were one of the items not reported by the House of Blues / Live Nation in the revenue lease payments.

The City’s policy regarding the solicitation and acceptance of complimentary tickets to events held at the Smirnoff Music Centre and other City-owned facilities is not clear. Texas law prohibits the acceptance of gifts with a value of \$50 or more by public servants from those subject to the public servants jurisdiction (class A misdemeanor). The City of Dallas Code of Ethics prohibits the acceptance of any gift or benefit that reasonably tends to influence or reward official conduct or that the official or employee knows is intended to influence or reward the discharge of official duties.

There may be valid reasons why the attendance of City officials or employees at events being held at City-owned facilities serves a public purpose. Without clear policies regarding the solicitation or acceptance of complimentary tickets, however, these transactions could be viewed as potential violations of either State statutes or City ordinances.

Recommendation 2:

We recommend the City Attorney develop proposals to enable the City Council and City Management to clarify the City’s policy on solicitation and acceptance of complimentary tickets to events held at the Smirnoff Music Centre and other City-owned facilities.

Management’s Response

Agree. The City Attorney’s Office will work with the City Council to clarify the City’s policy regarding the solicitation and acceptance of complimentary tickets to events held at Smirnoff Music Centre (currently named SuperPages.com) and other City-owned facilities.

Background, Objective, Scope and Methodology

Background

Smirnoff Music Centre (SMC) is located at Fair Park in the City of Dallas (City). Prior to November 2006, SMC was leased and operated by House of Blues Entertainment, Inc. In November 2006, Live Nation, a publicly-traded live music company, acquired House of Blues. On January 30, 2008, the Smirnoff Music Centre changed its name to SuperPages.com Center.

The Lease Agreement (Lease) between the City and Smirnoff Music Centre (Smirnoff / Live Nation, formerly House of Blues Concerts / Pace Amphitheatres) requires House of Blues / Live Nation to pay the City a “percentage rental” in addition to an “annual minimum guaranteed rental”. The “percentage rental” is calculated as a percentage of Smirnoff / Live Nation’s gross ticket proceeds and revenues from other sources, less the annual minimum guaranteed rental. The Lease also requires Smirnoff / Live Nation to pay South Dallas Fair Park Trust Fund for the Leased Premises and the Parking Tract Rights as additional rental. The payment is derived by multiplying fifteen cents (\$0.15) times the total number of admission tickets sold. South Dallas Fair Park Trust Fund is administered by the Department of Economic Development (ECO).

Smirnoff / Live Nation has revenues that are related to each event and additional non-event revenues, such as barter and interest incomes. The event based revenues include the revenues generated directly from each event, such as ticket sales, Ticketmaster rebate, facility fee, rental charge, food and beverage, merchandise revenue, parking revenue, etc. The non-event based revenue is generated from transactions throughout the year which generally can not be traced to an individual event. This includes revenues such as barter income, interest income, sponsorship income, box suites / super seat / club seat income, season ticket income, etc.

Based upon information provided by House of Blues / Live Nation, 155 events were held during January 1, 2001 through December 31, 2004. These events included 129 regular events and 26 special (rental) events and reported total revenue of \$79,295,241. The City received \$3,127,801 in lease payments and South Dallas Fair Park Trust Fund received an additional \$166,135.

Objective, Scope and Methodology

This audit was conducted under authority of the City Charter, Chapter IX, Section 3 and in accordance with generally accepted government auditing standards. The audit period covered January 1, 2001 through December 31, 2006. We also examined certain events, records, and transactions occurring before and after this period.

**An Audit Report on –
Smirnoff Music Centre’s Lease Payments**

Our audit objective was to determine whether House of Blues / Live Nation’s payments to the City are accurate and calculated in accordance with the Lease. To achieve the audit objective the following steps were performed:

- Interviewed House of Blues / Live Nation personnel regarding relevant business practices and procedures

- Reviewed and analyzed the House of Blues / Live Nation:
 - Lease Agreement with the City
 - Payments to the City
 - Income statements, general ledgers, sub-schedules, and worksheets; and
 - Event listings, schedules, contracts, and other relevant documentation

- Conducted both statistical and judgmental sampling

Based upon the audit work we performed for the audit period 2001 through 2004, the City Attorney employed the services of outside Certified Public Accountants Weaver & Tidwell, LLP to conduct additional audit tests. The work conducted by Weaver and Tidwell, LLP included the audit period 2001 through 2004, and a methodology was developed to provide a projection for the estimated underpayments for the 2005 through 2006 period. Based upon the work of Weaver & Tidwell, LLP, an amount due to the City was determined.

Major Contributors to This Report

Paul T. Garner, Assistant City Auditor
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Management's Response

RECEIVED

MAY 08 2008

CITY AUDITOR'S OFFICE



CITY OF DALLAS

Memorandum

DATE May 8, 2008
TO Craig D. Kinton
City Auditor
SUBJECT Response to Audit Report on Smirnoff Music Centre's Lease Payments

Our responses to the audit report recommendations are as follows:

Recommendation 1:

The City Attorney's Office will continue the negotiation process with Live Nation and will make a recommendation to the Dallas City Council regarding a proposed settlement regarding the additional lease revenues identified in the audit. Upon approval of the City Council, the City Attorney's Office will take all necessary steps to collect the money due to the City pursuant to the settlement agreement with Live Nation.

Management Responses / Corrective Action Plan

Agree

Implementation date:

Sixty (60) days after council authorization to proceed with a proposed settlement.

Responsible Manager

Pete Haskel

Recommendation 2:

The City Attorney's Office will work with the City Council to clarify the City's policy regarding the solicitation and acceptance of complimentary tickets to events held at Smirnoff Music Center (currently named Superpages.com) and other City-owned facilities.

Management Responses / Corrective Action Plan

Agree

**An Audit Report on –
Smirnoff Music Centre’s Lease Payments**


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Implementation date:

Upon City Council authorization.

Responsible Manager

Tom Perkins



Thomas P. Perkins, Jr.
City Attorney

“Dallas – **Together**, we do it better!”