PERFORMANCE AUDIT

ARIZONA OFFICE OF TOURISM

Report to the Arizona Legislature
By the Auditor General
September 1994
Report 94-4

RECEIVED
SEP 27 1994

DOUGLAS R. NORTON, CPA
AUDITOR GENERAL

STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

DEBRA K. DAVENPORT, CPA
DEPUTY AUDITOR GENERAL

September 26, 1994

Members of the Arizona Legislature

The Honorable Fife Symington, Governor

Mr. Greg Gilstrap, Director
Office of Tourism

Transmitted herewith is a report of the Auditor General, A Performance Audit of the Arizona Office of Tourism. This report is in response to a May 5, 1993, resolution of the Joint Legislative Audit Committee.

The report addresses the important role the Office now plays in the State's multi-billion dollar tourism industry, and the need to professionalize the Office's operations and buffer it more effectively from the political process. We also address unjustified and wasteful payments that were made to the Office's previous advertising firm.

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

This report will be released to the public on September 27, 1994.

Sincerely,

Douglas R. Norton

Douglas R. Norton
Auditor General

2910 NORTH 44TH STREET • SUITE 410 • PHOENIX, ARIZONA 85018 • (602) 553-0333 • FAX (602) 553-0051

SUMMARY

The Office of the Auditor General has conducted a performance audit and Sunset review of the Arizona Office of Tourism, pursuant to a May 5, 1993, resolution of the Joint Legislative Audit Committee. This audit was conducted as part of the Sunset review as set forth in Arizona Revised Statutes §§41-2951 through 41-2957.

Promoting tourism was originally a responsibility of the Governor's Office of Economic Planning and Development. In 1975, the Governor created a separate Office of Tourism by executive order. The Office continued under this order until 1978, when the Legislature created the Arizona Office of Tourism (AOT). Under the statutes creating it, AOT is charged with developing tourism business in Arizona through the advertising, promotion, and dissemination of information regarding the state's attractions. Its responsibilities include conducting research for long-range tourism development, and formulating policies, plans, and programs to promote tourism.

Statutory Changes Are Needed to Professionalize the Arizona Office of Tourism (see pages 5 through 10)

Although the Arizona Office of Tourism began as a small program within the Governor's Office, it has grown to become a key player in the state's efforts to promote the tourism industry. However, the structure and conditions under which the Office functions have not changed to reflect the growth and increased importance of AOT's role. As a result, the Office has had difficulty managing such basic tasks as budgeting, contracting, and planning and research. For Arizona to have an effective, professional tourism organization, steps must be taken to stabilize turnover in the director's position, and buffer the Office from the political process. At a minimum, the Legislature should consider specifying qualifications for the director's position, and requiring the use of a search committee process to fill it, and placing clerical and administrative support positions under the state personnel system. The Legislature may also wish to consider several options used by other states, such as placing the Office under a commission, within the Department of Commerce, or combining it with another promotional group such as *Arizona Highways Magazine*.

Advertising Dollars Were Wasted In Unjustified Payments to the Former Advertising Firm (see pages 11 through 15)

Under the contract provisions, AOT's former advertising firm was not entitled to payment for services performed by AOT or a third party. However, in the projects we reviewed, AOT paid the firm nearly $100,000 for publishing and broadcasting services performed by AOT staff or a third party. For example, AOT paid the firm over $26,000 in commissions for broadcasting services performed by the Arizona Broadcasters Association as part of a public service campaign with AOT.

Our investigation revealed that poor judgment, and the former director's belief that the contract language was vague, may have contributed to the improper payment of commissions in these cases. AOT has improved the language of the current contract in an effort to eliminate opportunities for the advertising firm to bill for unearned commissions in the future; however, it has taken no action to recover these misspent funds. AOT should seek the opinion of the Attorney General's Office to determine the feasibility of recovering these funds. If recovery is feasible, a closeout audit could help identify any other charges paid to the advertising firm which were unjustified.

Table of Contents

Page

Introduction and Background 1

Finding I: Statutory Changes Are Needed To Professionalize The Arizona Office of Tourism 5

Director Turnover and Political Patronage Adversely Impact AOT Operations 5

Statutory Changes Are Needed to Address the Root Causes of AOT's Ineffectiveness 8

Recommendations 11

Finding II: Advertising Dollars Were Wasted In Unjustified Payments To The Former Advertising Firm 13

Advertising Firm Paid Commissions for Services Performed by Others 13

AOT Should Take Steps to Recover Misspent Contract Funds 16

Recommendations 17

Other Pertinent Information 19

Statutory and Budget Reform Mandates 19

AOT's Current Status on Budget Reform Issues 19

Sunset Factors 23

Agency Response

Tables

Page

Table 1 Arizona Office of Tourism
Actual and Approved Expenditures
Appropriated Funds
Fiscal Years 1992-93, 1993-94, and 1994-95
(unaudited) 3

INTRODUCTION AND BACKGROUND

The Office of the Auditor General has conducted a performance audit and Sunset review of the Arizona Office of Tourism, pursuant to a May 5, 1993, resolution of the Joint Legislative Audit Committee. This audit was conducted as part of the Sunset review as set forth in Arizona Revised Statutes §§41-2951 through 41-2957.

The Office of Tourism was created by Executive Order in 1975. At that time, all duties related to tourism were transferred from the Governor's Office of Economic Planning and Development to the Office of Tourism. The executive order was later repealed in 1978, after the Legislature passed a bill establishing the Arizona Office of Tourism (AOT).

AOT is charged with planning and developing tourism business in Arizona through advertising, promotion, and dissemination of information regarding the state's attractions. Its responsibilities include conducting research for long-range tourism development, establishing the Office as the central repository for tourism information, and formulating policies, plans, and programs designed to promote tourism in the state.

Importance of Tourism in Arizona

Tourism plays an important role in our state's economy. While exact data on the impact of tourism is not available, the Arizona Hospitality Research and Resource Center at Northern Arizona University (NAU) estimates that travelers spent from $7 billion to $8 billion in Arizona in 1993. These expenditures directly supported over 100,000 tourism jobs, and resulted in over $288 million in tax revenues.

Organization

The current director recently reorganized AOT into four divisions, each headed by a manager. The responsibilities of each division are summarized below:

- **International & Domestic Trade Marketing** — This division is responsible for developing an international marketing strategy, and coordinating the state's participation in sales missions and marketing events. In addition, this division develops and implements all AOT marketing programs aimed at domestic tour operators, wholesalers, and travel agents.

- **Advertising and Tourism Development** — This division oversees the creation and placement of advertisements designed to attract travelers to Arizona. The division

works with the Department of Commerce in rural economic development as it relates to tourism. In addition, the division oversees the cooperative advertising grant program, an effort aimed at assisting Arizona's local communities in their marketing campaigns. This division is also responsible for coordinating and overseeing the agency's research projects.

- **Communications** – This division promotes the state's tourism attractions through nonadvertising formats such as media relations, industry cooperation, travel writer familiarization tours[1], and the publication of the Arizona Calendar of Events. This division serves as a key communication link with the public and private sectors for information about AOT programs, opportunities, and industry trends.

- **Business Affairs** – This division provides the administrative functions of the Office, including purchasing, budgeting, human resources, and other operational measures, such as response to requests for travel information, computer operations, and internal tracking procedures. In addition, this division is responsible for the dissemination and implementation of consistent office policies and procedures, as well as the management of the Office's administrative legal issues.

In addition to establishing the Office, AOT's statutes also provide for a Tourism Advisory Council (TAC) to advise the Office in preparing the budget and establishing policies and programs that promote and develop tourism. Membership of the council, which is established by statute, consists of representatives from various tourism related businesses, and represents different geographical areas of the state. The TAC is strictly advisory in nature, and has no authority over AOT.

Budget and Personnel

The Office's operating budget consists mostly of appropriated funds. In addition, AOT receives nonappropriated revenues from trade show registration fees, which are intended to reimburse AOT for expenses incurred in organizing trade show participation.

Actual and approved expenditures of appropriated funds for fiscal years 1993 through 1995 are shown in Table 1 (page 3). The Tourism Fund consists of an annual appropriation

---

[1] AOT organizes familiarization tours (fam tours) for travel writers with the expectation that they will write and publish a firsthand account of their travels in Arizona.

of $2 million, plus a portion of what is referred to as the "bed tax."[1] The Tourism Fund is designated for use in promotional activities.

Table 1

Arizona Office of Tourism
Actual and Approved Expenditures
Appropriated Funds
Fiscal Years 1992-93, 1993-94, and 1994-95
(unaudited)

General Fund	Fiscal Year 1993 (actual)	Fiscal Year 1994 (approved)	Fiscal Year 1995 (approved)
FTE Positions	17.0	18.0	19.0
Personal Services	$ 469,880	$ 564,500	$ 584,300
Employee Related	105,951	110,200	123,100
Prof. Outside Services	116,068	140,000	52,200
Travel, In-State	22,436	17,000	19,000
Travel, Out-of-State	39,392	50,000	50,000
Other Operating	630,195	665,000	548,400
Equipment	22,124	10,000	10,000
Operating Subtotal	$1,406,045	$1,556,700	$1,387,000
Toll-Free Line Production and Placement	N/A	N/A	2,810,300 (a)
Toll-Free Line Response	N/A	N/A	1,121,700
International & Domestic Marketing	N/A	N/A	877,200
Other Marketing	N/A	N/A	1,202,000
Media Advertising Fund	1,897,698	1,477,800	N/A
Tourism Fund	2,170,977	2,368,800	N/A
Total	$5,474,720	$5,403,300	$7,398,200

Source: Joint Legislative Budget Committee Appropriations Report for Fiscal Year 1995 and AFIS Expenditure Reports.

(a) In fiscal year 1995, below- the- line classifications were expanded from two categories to four to improve expenditure tracking. Of the $2,810,300 appropriated to Toll-Free Line Production and Placement, $2,365,000 shall be deposited in the Tourism Fund.

---

[1] Hotels and other lodging businesses pay one-half percent more in state sales taxes than other types of Arizona businesses. This extra one-half percent is known as the "bed tax." AOT is annually appropriated 75 percent of the growth in the amount of bed tax collected over the previous year. In fiscal year 1994, AOT received an estimated $368,800 as its portion of the bed tax.

Audit Scope

Our audit report of the Office of Tourism presents findings and recommendations in two areas:

- The need for statutory changes to improve AOT's efficiency and effectiveness and provide long-term stability, and
- The extent to which advertising expenditures have been unjustified and wasteful.

In addition to these audit areas, we present a section of Other Pertinent Information on AOT's status in meeting the mandates of Budget Reform (see pages 19 through 21), and a response to the 12 Sunset Factors (see pages 23 through 25).

This audit was conducted in accordance with government auditing standards.

The Auditor General and staff express appreciation to the Director and staff of the Office of Tourism for their cooperation and assistance throughout the audit.

FINDING I

STATUTORY CHANGES ARE NEEDED TO PROFESSIONALIZE THE ARIZONA OFFICE OF TOURISM

Beginning as a small program within the Governor's Office, the Arizona Office of Tourism (AOT) has grown significantly in size and importance. Now a key player in efforts to promote the state's tourism industry, the Office is an independent agency with a $7.4 million budget. However, in many ways the conditions under which the Office operates have not changed since it was smaller and was organized as part of the Governor's Office. As a result, AOT's efficiency and effectiveness have suffered. For Arizona to have an effective professional tourism organization, the Legislature should consider taking steps to provide more stability in the director's position and insulate the Office from the political process.

Director Turnover and Political Patronage Adversely Impact AOT Operations

In many ways, AOT operates as though it were still part of the Governor's Office. Staffing has been fluid, with high turnover in the director's position, and few, if any, policies and procedures governing the employment of staff. Internal agency operations have little or no buffering from the political process. AOT's vulnerability to an ever-changing stream of directors and political influence has resulted in fundamental management weaknesses that undermine the agency's effectiveness.

Director turnover – Frequent turnover at the director level has had a significant impact on AOT's effectiveness. Since 1980, the directorship of AOT has changed hands ten times. Seven individuals served as director and three as acting director. Only two were in office for more than two years. By contrast, tourism directors in other states average about four years in office.

Director turnover has a ripple effect, causing additional turnover among managers and staff, and bringing new priorities to the Office. As directors have taken office and then left, activities have been initiated and then abandoned. For example, AOT developed a strategic plan covering years 1991 through 1996, under the leadership of one of its former directors. At the time of our audit, most managers currently with the Office were unaware of the plan's existence. The plan was essentially abandoned after the director who served during its development left the Office.

Although it is difficult to document the reasons for AOT's higher turnover level, AOT officials and tourism professionals point to poor director quality and changes within the Governor's Office. One method of minimizing director turnover employed by tourism offices in six other states is to classify the director position under the state personnel system. In most of these states, the tourism office is located within a larger commerce or economic development agency. Another way to reduce director turnover would be to specify a term of office for the tourism director. Five agencies in Arizona specify a term of office for the director in statute.

Political interference – In some cases, the political process impacts not only the staffing of AOT, but decisions regarding the way AOT conducts its work. All AOT positions are exempt from the state's classified personnel system. AOT lacks policies governing the hiring, employment, evaluation, and discipline of personnel. In addition, AOT has not defined specific responsibilities for each position and identified minimum qualifications for positions, nor has it established appropriate pay ranges. In fact, for some positions, jobs were developed to match the needs of the employee, rather than to accommodate the needs of the organization.

For example, an examination of personnel files confirmed that one individual had been hired as an administrative assistant at a substantially higher salary than that of comparable positions. AOT officials explained the circumstances surrounding this appointment, stating that the Office had been directed (by the Governor's Office) to hire the employee, and to set the annual compensation at a level above $30,000. Because there were no openings in the Office's professional ranks, AOT initially placed the individual in a support position. This employee was subsequently appointed to head a major functional area despite lacking the necessary experience and background.

In another case, we noted a series of letters and memos documenting the nonperformance, absenteeism, and drunkenness of a former AOT employee. In one letter to a foreign travel writer, AOT apologized for the employee's embarrassing behavior during a familiarization tour the agency hosted. The employee was first transferred to the Department of Commerce and then returned to AOT for six months before finally being terminated. When we inquired about the delay in taking disciplinary action, we were told the Office had encountered difficulty taking action because the employee was related to a state legislator.

AOT's lack of insulation from the political process has had impacts extending beyond personnel matters. In 1992, with the support of the advertising manager and the State Procurement Office, AOT's former director provided written notice to the former advertising firm that its contract would not be renewed for fiscal year 1993. AOT was concerned about excessive costs (see Finding II, pages 13 through 17) and limited creativity. Interviews with three former AOT officials and correspondence from the advertising firm indicate some legislators tied renewal of the contract into a larger political issue involving confirmation of one of the Governor's appointees. As a result, the contract was not terminated and the advertising firm was retained for another year.

Basic management weaknesses — High director turnover and political patronage has adversely impacted AOT's basic operations. AOT has had difficulty in managing its finances, overseeing its outside contracts and its grant program, and performing its research and planning functions. Many of the weaknesses we identified below were also identified by the current director after he took office, and corrective actions have been initiated to address these problems (see page 8).

- **Financial Management** — The Office has done a poor job of monitoring and controlling its budget, possibly because staff did not have sufficient expertise in the requirements of good financial management. No budgetary or expenditure reports were prepared and reviewed on a regular basis, and financial information was not reported to division managers.

  This mode of operation has led to repeated overspending of agency funds. In 1991, AOT was unaware that it had exceeded its quarterly allotment of funds, until the Department of Administration's general accounting office rejected AOT claims totaling over $10,000. In May 1992, the Joint Legislative Budget Committee discovered that because AOT had hired additional staff and granted salary raises for its top positions, it had overspent its personal services appropriation by $43,000. To help AOT recover from these overexpenditures, funds were transferred from future allotments and other AOT funding sources.

- **Contract and Grant Program Oversight** — AOT has also been lax in monitoring its outside contracts and grant program. When we requested copies of AOT's outside contracts and intergovernmental agreements, AOT did not have them readily available. Copies of some contracts were never provided. Others had to be obtained through the State Procurement Office or the contractor. We question AOT's ability to oversee contracts that it did not have in its possession.

  AOT's oversight of its Cooperative Advertising Grant Program has also been lacking. Under the grant program, AOT provides matching dollars to communities to help them advertise the tourist attractions in their area. According to a recent review of AOT's administrative rules (R4-41-101 through R4-41-104), the grant recipient is required to provide at least 50 percent of the cost of the joint project in cash or in-kind services. However, in fiscal year 1993, AOT paid grant recipients more than $82,000 in excess of the matching limit. In addition, AOT committed to overspending the 50 percent matching rate by over $25,000 in fiscal year 1994.

- **Strategic Planning and Research** — AOT has lacked commitment in developing a research-based strategic plan. Literature and tourism professionals agree that strategic planning is important, because it provides long-term continuity for the Office's advertising and marketing activities, and focuses on making efficient and effective use of limited resources. At the time of the audit, AOT had no strategic plan. Moreover, AOT's research efforts have been limited and poorly coordinated. Although AOT spent over $360,000 on contracted research projects over a 3-year

period, much of the research had never been used. When we requested copies of the research reports developed under this agreement, only one of several reports requested was available in the AOT research department. Representatives of the research contractor and AOT officials stated that some of the research used questionable data and reporting methods. Without reliable research, AOT has no empirical basis for establishing and evaluating strategic goals.

Statutory Changes Are Needed to Address the Root Causes of AOT's Ineffectiveness

While AOT's current director is taking steps to improve Office management, his efforts alone cannot address the fundamental problems that continue to threaten the agency's effectiveness. Statutory changes are needed to stabilize the Office's leadership, and buffer it from the adverse impacts of political patronage.

Improvements initiated — Since assuming his responsibilities in June 1993, the current director of AOT has undertaken a number of significant initiatives to improve the Office's operations. These initiatives include:

- **Financial Management** — AOT developed a new internal accounting system that permits monitoring and reconciliation of program expenditures on a monthly basis. The new system is tied to the Arizona Financial Information System (AFIS) and relies on AFIS to generate financial reports useful to both AOT and state budget officials.

- **Contract and Grant Program** — The new accounting system facilitates contract oversight by enabling AOT to compare advertising expenditures to approved project estimates. AOT has also redefined the guidelines of the Cooperative Advertising Grant Program in fiscal year 1995 to adhere to the 50 percent matching rate limit.

- **Strategic Planning and Research** — AOT has conducted an internal evaluation to help determine the Office's role and establish its priorities. Also, AOT has contracted for the development of a research plan which makes use of existing tourism studies and identifies further research needed to achieve strategic goals.

In addition, AOT has developed position descriptions and responsibilities for its personnel. While these efforts have significantly improved Office management, further changes are needed to address the fundamental problems undermining long-term effectiveness.

Statutory changes needed — Statutory changes are needed to help stabilize AOT's leadership and reduce its vulnerability to political pressures. At a minimum, the following modifications could be implemented without altering AOT's status as an independent state agency:

- **Director Qualifications** – Minimum qualifications for the director of the Office of Tourism could be established in statute. These qualifications could specify education and training, and prior experience required for appointment. Fourteen Arizona state agencies specify qualifications their director must meet in state law. Two states we surveyed, Texas and Colorado, had established such minimum qualifications for their directors of tourism.

- **Search Committee** – Although not required by law, the Governor used a search committee process to fill the director's position in 1993. Representatives of the tourism industry and other tourism "stakeholders" identified candidates for the position of director and made recommendations to the Governor, who then selected the director from the list of recommended candidates. This process resulted in the appointment of a qualified and experienced tourism professional from out of state. The use of a search committee could be formalized in statute by assigning responsibility for recommending director candidates to the Tourism Advisory Council. However, if search committee responsibilities are assigned to the TAC, its membership should be reviewed to ensure that all stakeholders are adequately and fairly represented.

- **Classifying Personnel** – AOT personnel (at a minimum clerical and administrative support positions) should be covered by the state personnel system and subject to rules and requirements of the Personnel Division of the Department of Administration. Covering these positions would provide a buffer to political pressures that have been experienced in the past when personnel appointments have been made. Of the nine state tourism offices we surveyed for detailed information about their structure and operations, all reported that at least some positions are classified, nonexempt positions subject to state personnel rules. Five states specifically cited buffering from political pressures as one advantage of this arrangement.

Over the long term, these modifications to the existing structure may prove insufficient, and the Legislature may want to consider other, more extensive options for restructuring the Office of Tourism. We examined three potential options: (1) establishing the Office under a commission, (2) consolidating the Office within the Department of Commerce, and (3) combining AOT with the *Arizona Highways Magazine* (AHM) under a single office.

To assess these options, we reviewed alternative structures in other states, and conducted focus groups with industry and governmental representatives to solicit feedback on the feasibility of each option.[1] Despite concerns raised through the individual perspectives of our focus group members, we believe that each alternative is viable. Because these

---

[1] The industry focus group included representatives from: urban and rural chambers of commerce, or convention and visitors bureaus; Arizona's hotel/motel, tour operators, and restaurant associations; and the Native American Tourism Center. The government focus group included representatives from: Department of Commerce, *Arizona Highways* Magazine Division of the Department of Transportation; Arizona Office of Tourism; the Office for Excellence in Government; the Joint Legislative Budget Committee; the Office for Strategic Planning and Budgeting; and House and Senate Research.

options have been successfully implemented in other states, they deserve further consideration.

- **Commission** — Four of the nine highly regarded tourism programs we surveyed (California,[1] Colorado, Missouri, and Nevada) use commissions to oversee their tourism programs. In general, these commissions approve budget requests and marketing and advertising plans, hire (or nominate) and fire the director of tourism, and evaluate the success of tourism efforts through the use of performance measures.[2] Commissions tend to provide improved oversight due to high levels of tourism expertise provided by the stakeholders on the commission. Stakeholders and tourism professionals are uniquely qualified to select a capable director as well as evaluate the director's and program's effectiveness. Those states with commissions also indicated that the commission helped reduce political influences.

- **AOT under the Department of Commerce** — In 33 other states, tourism is placed under commerce or economic development agencies. Six of the nine states in our survey were structured in this manner. These states indicated that under a larger agency such as Commerce, a tourism office receives sufficient oversight and "political buffering." In addition, AOT and Commerce could benefit through shared resources and an increased synergy for economic development, especially between AOT and Commerce's motion picture and sports development divisions. However, one of the drawbacks of this structure is the perceived loss of focus and prestige for tourism activities.

- **Merging AOT with AHM under a single office** — Both AOT's and *Arizona Highways Magazine's* missions include bringing travelers to Arizona. AOT accomplishes this through various advertising media such as television, radio, newspapers and magazines. AHM advertises Arizona through *Arizona Highways Magazine* and the various books, calendars, maps and clothing it sells at its retail locations. A few states combine these various promotional activities under a single office. Combining these two entities could provide several benefits. For example, AOT could combine its expertise in advertising and marketing with AHM's expertise in printing and mailing. While AOT is weak in financial management and performance tracking, and lacks a personnel system, AHM is self-funded, tracks its performance, and has an established personnel evaluation system.

---

(1) The California Division of Tourism resides within, and is also overseen by, the Department of Commerce.

(2) See section on Other Pertinent Information (pages 19 through 21) for information on AOT's status in the use of performance measures.

RECOMMENDATIONS

1. The Legislature should consider amending AOT statutes by:

   - Adding minimum qualifications, and possibly establishing a term of office for the director of AOT,
   - Establishing a search committee process for selecting the AOT director, and
   - Placing all clerical and administrative support positions under the state personnel system.

2. If the Legislature feels that stronger action is needed, it should consider restructuring the agency. Three structural options that should be considered include: (1) creating a tourism commission, (2) combining AOT with the Department of Commerce, and (3) merging AOT with the *Arizona Highways Magazine* under a single office.

FINDING II

ADVERTISING DOLLARS WERE WASTED IN UNJUSTIFIED PAYMENTS TO THE FORMER ADVERTISING FIRM

Between fiscal years 1991 and 1993, AOT paid nearly $100,000 to its former advertising firm for publishing and broadcast services that the firm did not perform. Although AOT has terminated its relationship with this advertising firm and has taken action to correct the factors contributing to these unjustified payments, steps should be taken to recover misspent funds.

Between fiscal years 1991 and 1993, AOT designated about 70 percent of its budget for advertising use. AOT promotes tourism in the state through various means, such as radio and television commercials, printed brochures, calendars of events, public service announcements, and sponsorship of national sporting events. For 11 of the last 16 years, AOT has contracted most of the production and placement of its advertising through a single private advertising agency. AOT's latest advertising contract with this agency was in effect from July 1, 1990, to June 30, 1993. During this time, AOT paid over $6.6 million to the advertising contractor.

During the audit, concern was expressed that AOT may have improperly paid the contractor for several advertising projects during this time period. In this finding, we present four case examples based on our investigation of these allegations. A limited review of expenditures claims for over 240 other advertising projects suggests that similar overpayment may have occurred in several other sponsorship and printing projects under this contract. Therefore, the cases presented do not represent the full extent of the wasted resources that may exist under this or previous contracts; rather, they illustrate the consequences of inadequate contract management.

Advertising Firm Paid Commissions for Services Performed by Others

Under the contract provisions, the advertising firm was not entitled to payment for work performed by AOT staff or a third party. However, between fiscal years 1991 and 1993 AOT paid the firm $50,900 in commissions for publishing services performed by AOT's own staff and not by the firm. In addition, AOT paid $46,278 in commissions for broadcasting services the firm did not perform.

Payment provisions — AOT's advertising contract established the manner in which the advertising firm was to receive payment. The contract listed compensable services related to creating and producing advertisements for radio and television broadcast, or for print media advertising. If the firm's internal personnel performed these services, the firm was reimbursed according to an hourly fee schedule. If the work was subcontracted out -of-house, the firm was reimbursed and paid a 17.65 percent commission on the subcontracted production services. In addition, if AOT gave authorization, the advertising firm was required to select, contract for, and supervise the placement of advertisements. For these placement services, AOT paid the firm its net placement costs plus a 17.65 percent commission on these costs.

Contract provisions limit payments — In each of the cases discussed below, the advertising firm argued that it was entitled to a commission on all of AOT's publishing or broadcasting projects, if two conditions were met: (1) if the firm performed any production services on the project, and (2) if the funding for the project came from AOT's advertising budget. Thus, the firm believed it was entitled to a commission on the cost of publishing or broadcasting an advertisement, regardless of whether it actually performed the publishing or broadcasting services.

However, the firm's argument was not supported by the contract terms. Payment for production services was separate from payment for publishing and broadcasting services. Having created or produced advertisements only entitled the firm to compensation for production services — it did not entitle the firm to commissions on the cost of publishing or broadcasting those advertisements. Furthermore, because AOT owned the advertising material created under the contract, AOT could place the advertisement itself in print, outdoor, or electronic media, with no obligation to pay the firm for the use of the advertising materials.

Moreover, the advertising firm was not automatically entitled to any amount of AOT's advertising budget solely on the basis of being the successful bidder. The contract states that the amount of the contract *"is subject to a reduction by ... administrative policy of (AOT) when deemed to be in the best interest of the State of Arizona."* In addition, the contract provided that, *"... this contract shall not be construed as an exclusive arrangement...(AOT) may secure identical and/or similar services from other sources at any time in conjunction with, or in replacement of, the contractor's service."* AOT's direct procurement of printing and broadcasting services with a third party fell within these provisions.

Publishing services — Under the terms of the contract, publishing services are described as the selecting and contracting for space in publications, or printing. The following are examples of projects in which a commission was improperly paid to the advertising firm for publishing services performed by AOT staff.

Case 1: From September 1990 to September 1991, AOT published four quarterly issues of the Calendar of Events in the *Arizona Republic* and *Phoenix Gazette*. AOT staff had produced the listings in the calendars, and paid the contractor for

its work involved in making the calendar suitable for print. A former AOT director during 1990 had selected, contracted, and paid for the publication of the Calendar directly with the newspaper. When the next director came to AOT in 1991, AOT paid the advertising firm $37,418 in commissions for publishing services on this project.

Case 2: Early in 1991, AOT asked the firm to update two brochures to include a letter from the new governor and some revisions to the listings of tourism contacts. AOT paid the firm for the production work involved in making these revisions according to the terms of the contract. AOT selected and contracted for the publishing of both brochures through the State Procurement Office's bidding process. However, in October 1991, AOT paid the advertising firm $13,482 in commissions for these services in the publication of the two brochures.

Broadcasting services — Under the terms of the contract, broadcasting services are described as the selection, supervision, and contracting for radio or television time. The following are examples of projects in which AOT paid the advertising firm commissions for donated broadcasting.

Case 3: In October of 1991, a former director of AOT agreed to donate $100,000 annually to the Arizona Broadcasters Association's (ABA) scholarship programs and various public service projects. The Arizona Constitution permits state agencies to make donations to private entities, provided there is a public purpose and the state receives "valuable consideration" for the donation. In return for AOT's donation, ABA agreed to encourage radio and television stations to participate in a public service campaign promoting in-state tourism. ABA coordinated the campaign activities and monitored the amount of airtime donated by participating stations for AOT's public service announcements. In the one and one-half years the agreement was in effect, AOT donated a total of $150,000 and received approximately $668,000 in airtime on the project. Despite not being directly involved in the placement of these announcements, AOT's advertising firm requested and received a commission of $26,475 for these services, based on the $150,000 donation.

Case 4: Late in 1992, due to the loss of its corporate sponsor, the Fiesta Bowl asked 5 governmental entities to jointly contribute the $2 million it needed to join the Nationwide Bowl Coalition, and thereby remain 1 of the 4 major New Year's Day Bowls. AOT contributed a payment of $400,000 which, according to the Fiesta Bowl's Executive Director, was "applied directly to (paying the) teams that appeared in (the) game." The Fiesta Bowl donated airtime for nine commercials, which aired during the game and the parade, in consideration for the government group's sponsorship. The commercials were jointly produced by the government sponsors' advertising firms. According to AOT's former director and the Fiesta Bowl's Executive Director, AOT's advertising firm played

a minimal role in creating the commercials. In addition, AOT's advertising firm was present at a meeting where all of the governmental sponsors' advertising firms agreed not to charge commissions on the project. Reportedly, none of the other firms received a commission for broadcasting services. However, although AOT's advertising firm had not provided the required broadcasting services, it asked AOT for commissions on the $400,000 contribution. AOT paid the firm $19,803 in commissions on the value of AOT's share ($112,200) of the airtime.

AOT Should Take Steps to Recover Misspent Contract Funds

Poor judgment and misunderstanding of the contract may have contributed to the improper payment of commissions. While the agency has substantially clarified the terms of its current contract, AOT should take steps to recover misspent advertising funds under its previous contract.

- **Poor Judgment** — When the former director was appointed in 1991, his assistant director and the advertising manager advised against paying commissions on the printing projects. AOT's staff argued that the advertising firm was not entitled to commission on any printing jobs that AOT had procured itself. In the past, no commission had been paid to the firm on similar printing projects. However, the director chose not to follow the advice of his staff. According to the advertising manager, the former director said he would pay the commissions because he wanted to start off "in a friendly way" with the advertising firm.

- **Contract Terms** — We believe the contract provisions do not support the advertising firm's claim for commissions on the projects discussed above. However, the former AOT director found the firm to be "very persuasive", and believed the contract was sufficiently vague to warrant payment.

AOT has taken some steps to address the problems associated with unclear contract provisions. The current contract, with a different advertising agency, represents a substantial improvement in clarifying AOT's intent regarding the payment of commission for projects performed by AOT staff or a third party. The language of the new contract specifically states that AOT has the *"full right to reprint, reproduce and/or use any products derived from the contractor's work...without payment of any royalties, commissions, fees, etc."*

Although these changes may help prevent wasted advertising funds in the future, further steps should be taken. AOT should seek the opinion of the Attorney General's Office to determine the feasibility of recovering the funds misspent under the previous contract. If recovery of these funds is feasible, an independent closeout audit of previous contracts

could help identify any other charges paid to the former advertising firm which were unjustified.

RECOMMENDATIONS

1. AOT should request the Attorney General's Office to review the feasibility of recovering misspent funds under its contracts with the former advertising firm. If recovery is feasible, AOT should contract for an independent audit of the contracts to identify all monies improperly paid to its former advertising firm.

2. AOT should seek legal advice prior to authorizing payment when it is unsure of how to interpret a contract's terms.

(This Page Intentionally Left Blank)

OTHER PERTINENT INFORMATION

During the audit, we obtained other pertinent information regarding AOT's status in meeting its statutory objectives and the requirements of budget reform.

Statutory and Budget Reform Mandates

The statutory requirements of the Office of Tourism and its director are stated in A.R.S. §§41-2305 and 41-2302, respectively. These requirements can be grouped into three overall objective areas:

1. The promoting, planning, and development of tourism business;

2. The development of a campaign of information, advertising, publicity, promotion, and exhibition to attract travelers to the state; and,

3. The dissemination of such tourism information to the public through various media.

The Arizona Budget Reform Act of 1993 (Chapter 252; House Bill 2332) requires AOT to develop a strategic plan for accomplishing its objectives. The plan must cover a minimum three-year period, and include mission statements, goals, objectives, and evaluation criteria for each of AOT's budget programs. Initial submission of the plan is due by October 1, 1994. Beginning in fiscal year 1997, AOT will be required to include in their budget requests a summary of productivity measures, including the associated unit costs of services they provide.

The budget reform process begins to shift the focus in state government toward accountability for program performance and results. According to the Office of Strategic Planning and Budgeting, budget reform *"formally introduces an overdue era for state government in which performance and results will count for far more than departmental spending histories in allocating resources."*

AOT's Current Status on Budget Reform Issues

Strategic planning — AOT does not have a current strategic plan encompassing all aspects of its statutory objectives. (See Finding I, page 7 for further information.) The only planning

document that AOT regularly develops is its annual media plan, which directly addresses only the second statutory objective listed above. The media plan contains relatively few specific performance goals. Goals mentioned in the fiscal year 1993 media plan include such measures as the percentage of the targeted audience reached, and the percentage of times viewers see the advertisement. However, these statistics do not measure how effective the media campaign is in attracting viewers of the advertisement to Arizona.

Performance measures — Performance measures specific to evaluating AOT's efforts in promoting tourism and tourism development and informing the public are needed. Traditional evaluation measures assess the productivity/efficiency of the process, which is defined as the cost or time per unit of output. In addition, performance measures must assess agency input (determining needs, goals, strategies, and allocating resources), output (what a program does in terms of the quantity of goods and services provided), and most importantly, outcomes (the actual impact of the agency's actions on the public, and on meeting its goals).

For example, one of AOT's activities includes the development of a Calendar of Events. The calendar is a listing of tourism events scheduled to take place in various communities around the state. The development of the calendar is an activity that is primarily aimed at satisfying the statutory objective of providing information. For the Calendar of Events, performance measures might include:

- **Inputs** — resources (dollars and FTEs) allocated to identifying the needs of the calendar's stakeholders and the type of information to include, resources allocated to producing the calendar, and the projected demand for it.

- **Productivity/efficiency** — How long did it take to develop and distribute the calendar? What was the per-unit cost to produce it?

- **Outputs** — How many calendars did AOT distribute in a given period of time? Who is requesting/receiving the calendars (distribution statistics)?

- **Outcomes** — Were AOT's customers satisfied with the calendar (do customers view it as attractive, useful, persuasive in encouraging travel, and sufficient in content)? Were there enough/too many calendars distributed to meet demand?

The majority of performance measures currently reported in AOT's budget request focus on input and output measures, with very little consideration given to efficiency or outcome measures. In other words, AOT has begun to track <u>what</u> they are doing, but not <u>how well</u> it is being done.

Furthermore, these measures tend to cluster around one statutory objective — providing information — with little data reported on efforts being made in the other objective areas.

Moreover, most of the data reported by AOT at this time are "guesstimates" and therefore do not provide a reliable means of tracking performance.

(This Page Intentionally Left Blank)

SUNSET FACTORS

In accordance with A.R.S. §41-2954, the Legislature should consider the following 12 factors in determining whether the Arizona Office of Tourism should be continued or terminated.

1. The objective and purpose in establishing the agency

The statutes do not specifically state the objectives of the Office of Tourism. However, A.R.S. §41-2302 defines the director's responsibilities to include, *"promoting and developing tourism business and planning, and developing a campaign of information, advertising, promotion, exhibition, and publicity relating to tourism business."*

In addition, the Office is statutorily mandated (A.R.S. §41-2305) to stimulate and encourage public and private entities to participate and cooperate in the promotion of tourism and tourism development; perform research necessary for long-term planning and establishing the Office as a clearinghouse for tourism data; and provide tourism information and advice to public agencies, private citizens, and business enterprises.

2. The effectiveness with which the agency has met its objective and purpose and the efficiency with which it has operated

It is difficult to assess the true effectiveness of the Office in accomplishing its objectives. There are numerous entities promoting tourism in the state. Chambers of commerce, convention and visitors bureaus, and private businesses can all claim some contribution to bringing visitors to Arizona through their own advertising efforts. AOT has done relatively little over the years to track its own impact on tourism, separate from that of other tourism entities. As the new director stated, *"measurement and evaluation appear to not have been a consistent portion of the Office's previous operations."*

Furthermore, AOT has not been managed efficiently. The Office's method of operation has lacked standard management practices such as research-based planning, and systems for managing contracts, finances, and personnel. (See Finding I, pages 6 through 8). In addition, AOT has wasted agency resources in improper payments to its advertising contractor (see Finding II, pages 13 through 17). AOT's new management team is in the process of developing a policy and procedures manual to govern the agency's operations. However, it is unknown at this time whether the new policies will adequately address the problems identified in the audit.

3. **The extent to which the agency has operated within the public interest**

AOT attempts to operate in the public interest and be responsive to its public "customers." AOT defines its "customers" as the tourism industry, the traveling public, and the state's taxpayers. AOT has recently met with and surveyed the public to obtain input on tourism issues.

4. **The extent to which rules and regulations promulgated by the agency are consistent with the legislative mandate**

AOT has been given statutory authority under A.R.S. §41-2305 to adopt rules necessary or desirable to govern its procedures and business. In 1983, AOT adopted rules R4-41-101 through R4-41-104 which govern joint ventures undertaken with private corporations. These rules appear to be consistent with the legislative mandates placed on the Office.

5. **The extent to which the agency has encouraged input from the public before promulgating rules and regulations and the extent to which it has informed the public as to its actions and their expected impact on the public**

AOT has not promulgated any rules since 1983, and has not identified any areas requiring such actions at this time.

6. **The extent to which the agency has been able to investigate and resolve complaints that are within its jurisdiction**

This factor is not applicable because the Office of Tourism does not have investigative or regulatory authority.

7. **The extent to which the Attorney General or any other applicable agency of state government has the authority to prosecute actions under the enabling legislation**

This factor is not applicable because the Office of Tourism is not a regulatory agency with enforcement or oversight responsibilities.

8. **The extent to which the agency has addressed deficiencies in its enabling statutes that prevent it from fulfilling its statutory mandate**

AOT has not proposed any statutory changes in recent years.

9. The extent to which changes are necessary in the agency's laws to adequately comply with the factors listed in the Sunset law

To fulfill its legislative mandate in a more effective and efficient manner, statutory changes are needed to provide stable leadership, and insulation from the political process. The changes that are needed include establishing minimum director qualifications, establishing a search committee to nominate the AOT director, and classifying some AOT personnel. If these changes prove to be insufficient, the Legislature may wish to consider establishing a tourism commission, placing AOT under the Department of Commerce, or combining AOT with the *Arizona Highways Magazine* under a single office. Further discussion of each of these options can be found in Finding I, pages 8 through 10.

10. The extent to which the termination of the agency would significantly harm the public health, safety, or welfare

Because other private and public sector entities across the state are involved in promoting tourism and tourism development, we believe that terminating the agency would not significantly harm public health, safety, or welfare. However, the elimination of the agency could have some negative effects, because the traveling public would have no statewide clearinghouse of travel information. In addition, eliminating the Office of Tourism may adversely impact the ability of many areas to attract tourists. Many areas lack the funding and expertise to develop tourism, and rely on AOT to provide those resources.

11. The extent to which the level of regulation exercised by the agency is appropriate and whether less or more stringent levels of regulation would be appropriate

The Office of Tourism is not a regulatory agency, thus this factor does not apply.

12. The extent to which the agency has used private contractors in the performance of its duties and how effective use of private contractors could be accomplished

AOT has made extensive use of private contractors. Services contracted include the production and placement of most of its advertising projects; the administration and conduct of tourism research; the operation of its "800" line; and the fulfillment of requests for travel information.

(This Page Intentionally Left Blank)

ARIZONA
OFFICE OF TOURISM

September 20, 1994

Mr. Douglas R. Norton
Auditor General
State of Arizona
2910 North 44TH Street, Suite 410
Phoenix, Arizona 85015

Dear Mr. Norton:

Thank you for the opportunity to respond to the preliminary report draft that was delivered to the Arizona Office of Tourism on September 13, 1994.

Your findings regarding improved management and business practices on page 8 of the document help demonstrate why our staff and many leaders of the Arizona tourism industry believe the Office of Tourism is functioning at one of the highest performance levels in the history of this agency. In addition to the improvements acknowledged in your audit, the list of achievements the office can now document includes:

* record levels of advertising-generated requests for travel planning assistance,
* enhanced telecommunications effectiveness,
* consistent customer-focused policies and practices,
* state-of-the-art performance tracking systems, and
* an unprecedented ability to leverage the state's marketing budget through strategic partnerships with the private sector.

1100 West Washington Street Phoenix, Arizona 85007 (P) 602.542.8687 (F) 602 542 4068
Fife Symington, Governor ◇ Greg Gilstrap, Director

Based on our review of previous performance audits conducted by your office, we understand your efforts are primarily directed at the identification of problems and the delivery of related problem solving recommendations. Therefore, we greatly appreciate the documentation of AOT progress.

Because we are confident the agency is now headed in a progressive direction, it is difficult to respond to an audit that primarily focuses on perceived historical problems. However, in the following paragraphs, we will do our best to communicate our reaction and professional response to some of the key recommendations offered in your report.

In regards to the recommendations listed on page 11, we again turn to the current state of the agency. Governor Symington utilized a search committee to select the new director. As a result, even your comments on page 9 indicate this process helped accomplish the goal of securing the services of what you refer to as a "qualified and experienced tourism professional." Because the merits of this process have been proven, we question the need to add minimum qualifications to AOT statutes.

The fact that the current system is working efficiently also mitigates the need to consider merging AOT with a larger agency or placing all clerical and administrative support positions under the state personnel system. Such a move would not ensure competence, and would make it increasingly difficult and time consuming to remove incompetence.

In regards to your reference to issues resulting from perceived political patronage, it appears rumors and innuendoes have contributed to such conclusions. In the 16 months I have served the state, I have been given the complete ability to put together an extremely qualified staff. If you compared the qualifications of our staff with any other state tourism office, I feel confident you would find Arizona currently employs one of the nation's best qualified and top performing units. I am extremely proud of our team.

In regards to Finding II, we feel your office was remiss in not pointing out the fact that the contract in question was inherited by the former director mentioned in your report and was awarded "on or about" May 30, 1990 by the previous administration. The contract has also been described as unduly vague by those that worked with it. It is reasonable to assume the vague nature of the contract resulted in problems for both the agency and the contractor. Repeated correspondence from the former advertising agency indicate the firm's owner sincerely believed he had a right to such commissions.

Your "poor judgment" finding on page 16 represents an unusual conclusion for an audit staff when you consider the report fails to recognize the former director exercised due diligence by contacting the Attorney General's office for advice on this issue. This fact has been verified by a former Assistant Attorney General, who also indicated he concluded the contract was vague in

nature. He indicated he was unable to recommend non-payment as an appropriate course of action for the Office of Tourism.

We also want to underscore the fact that such agreement is no longer in service, the contract deficiencies have been corrected, and the services of a new advertising agency have been secured.

Because you indicate the audit provides a factual basis for exploring methods of retrieving the commissions in question, we have again approached the Attorney General's Office for further assistance. We are asking them to further determine if there is, in fact, a sound legal basis for recovering the disputed commission amounts. AOT is moving forward with implementing the page 17 recommendations.

Throughout this process, we were impressed with the level of professionalism that was exhibited by the field staff that worked on this audit. You should be proud of the manner in which they conducted business. However, we respectfully suggest stronger management practices would have resulted in the delivery of a timely audit. Significant field work was completed nearly eight months ago. Initially, we were told to expect a final report in the March - May time frame. Obviously, the delivery was delayed several times since then. As a result, we believe you are now presenting a document that lacks the impact and usefulness it might have featured had it been delivered in a timely manner.

In conclusion, we stand ready to discuss the audit with you in greater detail. Thank you for your interest in our agency.

Sincerely,

Greg W. Gilstrap
Director