
Office of Inspector General

Audit Report

**FAA OVERSIGHT IS INADEQUATE TO ENSURE
PROPER USE OF LOS ANGELES INTERNATIONAL
AIRPORT REVENUE FOR POLICE SERVICES AND
MAXIMIZATION OF RESOURCES**

Federal Aviation Administration

Report Number: AV-2014-035

Date Issued: April 8, 2014





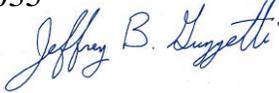
Memorandum

U.S. Department of
Transportation

Office of the Secretary
of Transportation
Office of Inspector General

Subject: **ACTION:** FAA Oversight Is Inadequate To
Ensure Proper Use of Los Angeles International
Airport Revenue for Police Services and
Maximization of Resources
Federal Aviation Administration
Report No. AV-2014-035

Date: April 8, 2014

From: Jeffrey B. Guzzetti 
Assistant Inspector General
for Aviation Audits

Reply to
Attn. of: JA-10

To: Federal Aviation Administrator

As the third busiest airport in the Nation,¹ Los Angeles International Airport (LAX) generated approximately \$822 million in airport revenues² and received nearly \$45 million in Airport Improvement Program (AIP) grant funding from the Federal Aviation Administration (FAA) in fiscal year 2012. LAX is owned and operated by the City of Los Angeles (the City) through Los Angeles World Airports (LAWA), a financially independent department of the City. As required by Federal law, recipients of Federal grant funds must ensure they use airport revenues for airport capital and operating costs and establish a fee and rental structure to make the airport as self-sustaining as possible. FAA, in turn, is responsible for effective oversight of airport revenue at airports that receive AIP grants.

Between June 2011 and February 2012, our office received letters from three Congressmen from California expressing concerns about potential revenue diversion at LAWA, including LAX, involving money spent for police and security services. In addition, the Chairman of the House Appropriations Subcommittee on Transportation, Housing, and Urban Development inquired about our work on revenue diversions at LAX during a March 2012 congressional hearing.³ Accordingly, we initiated this audit to assess FAA's oversight of LAX

¹ LAX had the third highest number of passenger boardings in calendar year 2012, according to FAA data.

² LAX earned approximately \$822 million in operating revenues for its fiscal year ending June 30, 2012.

³ *Top Management Challenges Facing the Department of Transportation* (OIG Testimony No. CC-2012-017), Mar. 29, 2012. OIG reports and testimonies are available on our Web site at www.oig.dot.gov.

revenue use. Specifically, we evaluated whether (1) FAA's oversight of LAWA ensures proper use of LAX revenues, (2) LAX is as self-sustaining as possible, and (3) LAX reported accurate financial data to FAA.

We conducted our audit in accordance with generally accepted Government auditing standards from July 2012 to January 2014. Exhibit A details our scope and methodology, and exhibit B lists organizations visited or contacted.

RESULTS IN BRIEF

FAA's oversight did not ensure that LAWA properly used over \$8 million in LAX revenues and funding from 2006 to 2012. Federal law requires that airport revenue be used for the capital and operating costs of the airport, and FAA's Airport Revenue Use Policy⁴ states that such costs may include reimbursements to a State or local agency for services received and supported by adequate documentation.⁵ However, we identified about \$7.87 million in unsupported charges without adequate documentation for services provided by the Los Angeles Police Department (LAPD)⁶ and over \$360,000 in unsupported administrative charges to AIP grants.⁷ Without adequate documentation or support, it is unclear if these charges were used for the capital and operating costs of the airport or allowable AIP project costs. However, under FAA policy, these costs should not have been charged to the airport or to AIP project funding. In addition, LAWA spent approximately \$192,000 of airport revenue on unauthorized⁸ LAPD personnel working at LAX, including overtime incurred by LAPD officers. FAA did not identify these instances of unsupported and unauthorized use of revenue at LAX, which indicates that its oversight of LAX revenues can be improved. In 2012, LAWA and FAA stated a record-keeping system to track LAPD non-airport work time would be implemented to address allegations of unlawful revenue diversion brought forward in congressional complaints received since mid-2011.⁹ However, because the City has yet to fully implement such a record-keeping system, LAWA may be incorrectly spending additional revenue on LAPD non-airport work.

⁴ The FAA "Policy and Procedures Concerning the Use of Airport Revenue" (Federal Register, Vol. 64, No. 30, Feb. 16, 1999) implements the statutory requirements that pertain to the use of airport revenue. The Policy describes prohibited and permitted uses of airport revenue and outlines FAA's enforcement policies and procedures.

⁵ Under the FAA policy, adequate documentation consists of underlying accounting records and corroborating evidence (i.e., invoices, vouchers, and cost allocation plans) to support payments of airport revenues to other government entities.

⁶ These charges occurred over 5 City fiscal years, beginning July 1, 2007, and ending June 30, 2012.

⁷ During our review, LAWA stated it would discontinue these administrative charges to AIP grants.

⁸ The term "unauthorized" describes instances where LAWA paid for LAPD personnel, including overtime, in a manner inconsistent with procedure set forth in the Memorandum of Agreement between LAPD and LAWA or the LAPD Fiscal Operations Division.

⁹ In November 2011, FAA requested LAWA to review the allegations made in the congressional complaint. LAWA responded to FAA in February 2012. In turn, FAA responded to the allegations in June 2012.

LAWA could not demonstrate that it met Federal requirements to be as self-sustaining as possible in establishing rental rates for several of its non-aeronautical¹⁰ land leases. FAA policy requires airport sponsors to ensure airports are as self-sufficient as possible, in part, by charging fair market value for non-aeronautical property leases. Although we did not have concerns with the majority of the 12 non-aeronautical leases reviewed,¹¹ 3 leases were below fair market value estimates from professional appraisals, rates established by the City's Board of Airport Commissioners, or LAWA's own internal review. For example, for one property, based on a 2010 internal LAWA review, we estimate that LAWA could have obtained up to approximately \$558,000 in additional annual rental income.¹²

Finally, we detected financial reporting discrepancies of about \$49 million between the amounts LAWA reported in (1) its statutorily required annual financial reports to FAA and (2) LAWA's own internal financial reports. For example, LAWA's 2009 report to FAA showed no expenditures for legal services at LAX. However, LAWA's internal financial data included about \$4.6 million for such services in 2009. According to LAWA, the discrepancies occurred, in part, because LAWA had issues with data integrity in 2009. According to FAA, LAWA re-submitted its financial reports to FAA in February 2014 and, by the end of March 2014, expects LAWA to provide supporting documentation for the re-submitted reports. Because FAA uses these financial reports as a source of information to detect whether airport revenue has been diverted from an airport, inaccurate information could reduce the effectiveness of FAA's oversight efforts and provide erroneous information to the public.

We are making recommendations to improve FAA's oversight of airport revenue and the airport's self-sustainability.

¹⁰ FAA defines "aeronautical use" as all activities that involve or are directly related to the operation of aircraft, including activities that make the operation of aircraft possible and safe. Aeronautical use includes services located on the airport that are directly and substantially related to the movement of passengers, baggage, mail, and cargo. Conversely, non-aeronautical use is activity which does not include aeronautical use. Non-aeronautical revenue includes revenue from such activities as concessions, parking, advertising, and land rent.

¹¹ A description of the leases we selected for review is contained in Exhibit A, Scope and Methodology.

¹² Based on these estimates, LAWA could have obtained between approximately \$80,000 and \$558,000 in additional annual rental income, depending on how the property is valued (e.g., as separate parcels or as vacant).

BACKGROUND

LAX is the busiest of three airports owned and operated by the City of Los Angeles through LAWA, a financially independent department of the City.¹³ As airport sponsor, the City must comply with U.S. law and FAA policy, including the Airport and Airway Improvement Act of 1982 and FAA's Airport Revenue Use Policy. Specifically, the airport sponsor must use airport revenue for the airport's capital or operating costs. Also, when airport owners or sponsors accept funds from FAA-administered airport financial assistance programs, they must agree to certain obligations called grant assurances. These obligations require the recipients to maintain and operate their facilities safely and efficiently and in accordance with specified conditions. The assurances may be attached to the application or the grant for Federal assistance and become part of the final grant offer. In addition, the airport sponsor must also receive fair market value for property leased or used for non-aeronautical purposes.

Revenue diversion is the use of airport revenue for purposes other than the capital or operating costs of the airport, the local airport system, or other local facilities that are owned or operated by the owner or operator of the airport and directly related to the actual transportation of passengers or property. These restrictions on airport revenue use are part of the grant assurances that airport sponsors must make in order to receive Airport Improvement Program grant funds.¹⁴ The FAA Authorization Act of 1994¹⁵ required the Secretary to establish policies and procedures that prohibit the diversion of airport revenues through, among other things, direct payments or indirect payments, other than payments reflecting the value of services and facilities provided to the airport. In 1999, FAA published the Policy and Procedures Concerning Use of Airport Revenues (Airport Revenue Use Policy), as required by the FAA Authorization Act of 1994. The Airport Revenue Use Policy requires that reimbursements for capital and operating costs of the airport made by a government entity be supported by adequate documentary evidence. Such costs may include reimbursements to a State or local agency for the costs of services actually received and documented.

FAA is responsible for advising airport sponsors and providing oversight to ensure that they are not in violation of Federal obligations regarding airport revenue, self-sustainability, and other matters. According to FAA's Airport Revenue Use Policy, the Agency will use all means at its disposal to monitor and enforce the revenue-use requirements and will take appropriate action when a potential violation is brought to its attention by any means. To detect whether airport revenue has been diverted, FAA uses (1) annual airport financial reports submitted

¹³ LAWA also operates Ontario International Airport and Van Nuys Airport.

¹⁴ Airport and Airway Improvement Act of 1982, Public Law 97-248, Title V, Section 511(a)(12) (September 3, 1982), (codified at 49 U.S.C. § 47107(b)(1)).

¹⁵ Public Law 103-305, Section 112 (August 23, 1994) (codified at 49 U.S.C. § 47107(l)(2)).

by the sponsor, (2) findings from a single audit conducted in accordance with OMB Circular A-133, (3) investigations following a third-party complaint, and (4) DOT Office of Inspector General audits. FAA states that it will seek penalties for the diversion of airport funds if the airport sponsor is not willing to correct a diversion and make restitution, with interest, in a timely manner.

Over the past 2 decades, LAX has undergone reviews by the City, FAA, and our office for airport revenue use. For example:

- In 1995,¹⁶ we reported that FAA was unaware that the sponsor's airports, including LAX,¹⁷ did not maintain fee and rental structures to make airports as self-sustaining as possible, and that airport revenues were not properly accounted for and used.
- In 1997, we reported that several revenue diversions identified in our 1995 audit were still unresolved.¹⁸ We also identified three areas where prohibited airport revenue diversion to the City occurred.

In 2012, LAWA¹⁹ identified that the City incorrectly charged LAWA approximately \$1.7 million, including statutory interest, for off-airport responses by the City's Bomb K-9²⁰ unit. LAWA also identified approximately \$1.9 million, including statutory interest, in billing errors uncovered during the investigative process. LAWA's discovery of these improper charges was prompted by the allegations received by our investigative office that we subsequently referred to FAA. Our investigative office will be issuing a separate report on the allegations.

¹⁶ *Monitoring of Accountability and Use of Airport Revenues by City of Los Angeles Department of Airports* (OIG Report No. R9-FA-6-001), Oct. 30, 1995.

¹⁷ At the time of the audit, there were four airports sponsored by the City of Los Angeles, Department of Airports: LAX, Ontario International, Van Nuys, and Palmdale. The audit's scope included all four airports.

¹⁸ *Management Advisory Memorandum on City of Los Angeles Department of Airports Revenue Retention* (OIG Report No. R9-FA-7-005), Mar. 7, 1997. Limited-scope audit conducted at the request of FTA.

¹⁹ Letters from Anderson and Kreiger, LLP to FAA's Airport Branch dated May 8, 2012, and May 31, 2012. These letters were in response to a letter by FAA that was prompted by congressional inquiries of revenue diversion at LAX.

²⁰ This unit's mission is to deter and detect the introduction of explosive devices both in transportation systems, such as the airport, and the City.

FAA OVERSIGHT DID NOT ENSURE PROPER USE OF AIRPORT REVENUE FOR POLICE SERVICES AND AIP ADMINISTRATIVE COSTS

FAA's oversight did not ensure that LAWA always used airport revenue properly. Specifically, over a 5-year period,²¹ the LAPD charged LAWA nearly \$8 million dollars for police services without adequate documentation to substantiate the charges. The majority of this amount—\$6.2 million—was for LAPD divisional overhead rates that were based on outdated cost allocation plan calculations instead of annually updated actual rates. The full extent of unsupported charges is unknown because the City has not fully implemented a record-keeping system to track off-airport time by LAPD officers assigned to the airport. LAWA also used Federal funds to pay for administrative fees without proper justification that the fees were for allowable AIP project costs. Finally, LAPD charged LAWA for unauthorized LAPD personnel working at LAX and also for overtime incurred by unauthorized LAPD officers.

LAPD Charged Unsupported Police Costs to the Airport Contrary to FAA's Airport Revenue Use Policy

Over 5 fiscal years, LAPD charged LAWA approximately \$7.87 million for police services without adequate documentation to substantiate the charges. Under FAA's Airport Revenue Use Policy, airport revenue can be used only for the capital or operating costs of the airport. Such costs may include reimbursements to a State or local agency, such as LAPD, for services received, provided they are based on adequate documentation that demonstrates the funds were expended for the benefit of the airport (e.g., accounting records accompanied by invoices, vouchers, and cost allocation plans). FAA policy allows airports to recover illegal charges for up to 6 years, with interest.

The \$7.87 million includes unsupported charges without adequate documentation (see table 1 below) from the following five areas over 5 fiscal years:

- **Police Forgery Unit.** LAPD charged LAWA \$968,742²² for services by its Forgery Unit.²³ This amount represents 20 percent of the unit's personnel salary. However, LAPD did not provide adequate documentation, such as accounting records or tracking of airport-related and non-airport related time, to show that this charge was actually expended for airport-related work.

²¹ This includes the following City of Los Angeles fiscal years: (1) 2007-2008, (2) 2008-2009, (3) 2009-2010, (4) 2010-2011, and (5) 2011-2012. The final costs for the 2012-2013 fiscal year were not available in time to be included in this report.

²² This amount comprises the unit's gross salary and indirect costs and excludes the divisional overhead amount.

²³ The Forgery Unit investigates crimes involving fraud and fraudulent credit card usage as they apply to air travel, including car rental agencies located at or near the airport.

- **Police Fiscal Operations Division.** LAPD charged LAWA \$436,359 for a management assistant position in the Police Fiscal Operations Division.²⁴ This amount represents the assistant's salary plus additional indirect charges. The assistant stated that she conducted both airport and non-airport work. Yet, LAPD did not provide documentation showing how much time the assistant spent on airport-related work. LAPD charged LAWA the assistant's full salary, without any discount for the non-airport related work. FAA policy only allows reimbursement of the airport's capital and operating costs.
- **Police Gang and Narcotics Division.** LAPD charged \$216,162 for the salary of a lieutenant in the Gang and Narcotics Division.²⁵ The lieutenant stated that he conducted both airport and non-airport work, and LAPD charged the airport one-third of the lieutenant's salary to the airport. However, according to division representatives, the basis of this rate is unknown, and the time spent on airport-related work is not tracked. As a result, the documentation does not support that the lieutenant spent one-third of his time for the benefit of the airport.
- **Police Pacific Area Operations Support Division.** LAPD charged LAWA \$32,224 for the salary of a supervisory lieutenant in this division.²⁶ This amount is 5 percent of the supervisor's salary. However, LAPD did not provide adequate documentation or rationale to demonstrate that the charge was expended for airport-related work. For example, the documentation lacked accounting records or other tracking of the supervisory lieutenant's airport related and non-airport related time.
- **Divisional Overhead.** LAWA paid about \$6.2 million in unsupported charges without adequate documentation for all of LAPD's divisional overhead rates for LAPD services to the airport. LAPD's divisional overhead rates that were charged to LAWA were based on a cost allocation plan that was calculated over 15 years ago instead of determining the actual divisional overhead rates each year. According to correspondence between LAWA and FAA (dated February 2012), the divisional overhead rate apparently had never been subject to an independent audit, and LAWA stated it will ask the City to include the divisional overhead rate in future audits. However, we consider the entire amount of the divisional overhead rates charged over 5 fiscal years—the scope of our audit—to be unsupported costs because LAPD did not provide

²⁴ Among other responsibilities, this Department prepares and distributes the payroll, which includes liaising with the other operational LAPD departments for the billing and reimbursements of police services at the airport.

²⁵ The Gang and Narcotics Division at LAX investigates illegal drugs and drug money that comes through the airport. This effort supports the greater Division mission to disrupt violent street gangs and the means by which they support their lifestyle, including the transportation of illicit drugs and sales of firearms in the greater Los Angeles area.

²⁶ This Division performs preliminary investigations of specific enumerated crimes, and follows up on felony and misdemeanor investigations not cleared by arrest.

documentation to support that it is the actual cost of divisional overhead to the airport.²⁷

Table 1. Unsupported Costs for Police Services to the Airport

| Fiscal Year | Police Forgery Unit ^A | Police Fiscal Operations Div. ^A | Police Gang & Narcotics ^B | Police Pacific Area Operations Support Div. ^B | Police Divisional Overhead Amount | Total Unsupported Costs |
|--------------------|----------------------------------|--|--------------------------------------|--|-----------------------------------|-------------------------|
| 2007-2008 | \$195,663 | \$88,090 | \$41,933 | \$6,290 | \$1,163,475 | \$1,495,451 |
| 2008-2009 | \$207,689 | \$88,171 | \$43,507 | \$6,571 | \$1,243,731 | \$1,589,669 |
| 2009-2010 | \$223,457 | \$81,055 | \$43,507 | \$6,526 | \$1,260,457 | \$1,615,002 |
| 2010-2011 | \$203,220 | \$90,541 | \$43,507 | \$6,526 | \$1,252,800 | \$1,596,594 |
| 2011-2012 | \$138,713 | \$88,502 | \$43,708 | \$6,311 | \$1,292,539 | \$1,569,773 |
| Total ^C | \$968,742 | \$436,359 | \$216,162 | \$32,224 | \$6,213,002 | \$7,866,489 |

Source: OIG calculation of data from the City of Los Angeles

Notes

Dollar figures rounded to the nearest whole number.

A: The figures in these columns do not contain the divisional overhead amount.

B: The amounts in these columns only contain the direct salary of the supervisory lieutenant. Indirect and divisional overhead rates are not added to this amount.

C: The final costs for the 2012-2013 fiscal year were not available in time to be included in this report.

Although we identified approximately \$7.87 million in unsupported police costs without adequate documentation, the full extent of these costs is unknown because, at the time of our visits to LAX in February 2013, LAPD had not fully implemented a record-keeping system to track and account for time that its officers assigned to the airport spent conducting off-airport duties. LAWA had agreed to implement the tracking system for LAPD officers assigned to the airport on a full time or full time equivalent basis starting July 2012 and stated it would

²⁷ In May 2012, LAWA identified that approximately \$1.7 million, including statutory interest, for off-airport responses by the City's Bomb Squad K-9 unit was charged incorrectly to LAWA between fiscal year 2004-2005 through fiscal year 2009-2010. This amount was later credited back to the airport. As such, of the approximate \$6.2 million of unsupported divisional overhead costs we identified, potentially about \$66,377 (the divisional overhead amount charged by the Bomb Squad K-9 unit multiplied by the average rate of time spent by the Bomb Squad K-9 unit for off-airport assignments) of the \$1.7 million was returned to the airport. However, since the divisional overhead rate charged by LAPD was based on a cost allocation plan that was calculated over 15 years ago and because LAPD did not provide documentation to support that the rate is the correct rate, we cannot be certain whether the approximate \$66,377 was the correct amount to be credited back to the airport.

require LAPD to credit LAWA for any use of LAWA-paid officers²⁸ for non-airport purposes. The recordkeeping system is a key part of agreed-upon actions between FAA and LAWA to resolve issues stemming from a congressional complaint regarding allegations of unlawful revenue diversion at LAWA.

Our review of four LAPD units revealed that only two units—the Bomb Squad K-9 (canine) unit and the non-K-9 Bomb Squad—were maintaining records of non-airport work. While the Bomb Squad K-9 unit provided information on its non-airport time to the Police Fiscal Operations Division to ensure LAWA was not billed for this time, the non-K-9 Bomb Squad stated it does not provide information on non-airport time to other entities, so it is unclear if LAWA is being billed for the non-K-9 Bomb Squad’s non-airport time. However, a LAWA official stated in August 2013 that reporting off-airport time by full time LAPD personnel at LAX, other than the Bomb Squad K-9 unit, will not be necessary because LAWA believes the other full time LAPD personnel rarely engage in non-airport related activities. We requested documentation to support this statement as well as the rationale for the change in the agreed upon actions for record keeping. However, we have not received this documentation to date. By only requiring the Bomb Squad K-9 unit to track off-airport time instead of any LAPD personnel assigned to LAX on a full-time or full-time equivalent basis, LAWA could be paying for police services not related to the airport, which would be a diversion of airport revenue.²⁹

When we discussed these deficiencies with senior FAA officials in March 2013, they were not aware of why only one of the LAPD units was tracking charges for non-airport time.³⁰ While FAA stated it has limited staff, FAA’s Airport Revenue Use Policy states congressional intent that FAA focus compliance efforts on the lawful use of airport revenue. Despite FAA’s knowledge of revenue misuse concerns at LAX, the Agency did not ensure that LAWA implemented effective corrective actions (i.e., recordkeeping and tracking mechanisms for off-airport time) to prevent future potential revenue diversions.

²⁸ This tracking requirement applies to the following police units: Field Services, Narcotics Division, Narcotics Division-K-9, non-K-9 Bomb Squad, and Bomb Squad K-9 unit. We met with the Field Services Division, Gang and Narcotics Task Force, Bomb Squad-K-9 (canine) unit, and the non-K-9 Bomb Squad unit. LAWA stated that services rendered by a specialty LAPD division on an as-needed basis should only be billed to LAWA based on work performed for the airport.

²⁹ As a result of this recordkeeping and tracking system, LAWA was able to identify that the City incorrectly charged LAWA approximately \$1.7 million, including statutory interest, for off-airport use of the City’s Bomb Squad K-9 unit. This amount was credited back to LAWA.

³⁰ When we met with FAA in March 2013, only one unit, the Bomb Squad K-9 unit, was tracking non-airport time. In December 2013, the non-K-9 Bomb Squad stated it started tracking time worked away from LAX in April 2013, after we met with FAA in March 2013.

LAWA Charged Unsupported Administrative Costs to AIP Grants

Since 2006, LAWA has charged over \$360,000 to AIP funding for administrative fees. However, LAWA did not provide us with a basis for how the fees were determined or used. FAA's AIP Handbook³¹ states that administrative costs may be allowed only if they are properly supported and substantiated. Without providing a basis for the administrative fees, LAWA cannot charge them to AIP funds.

We identified these administrative expenses by reviewing LAWA's pay reimbursement requests in the "Outlay Report and Request for Reimbursement for Construction Programs" form that LAWA sent to FAA. Although FAA received these reports from LAWA, the Agency did not identify that the administrative costs were unsupported. The airport received about \$356 million from fiscal years 2006 to 2012 in AIP funding. Although the administrative fees are only a small portion of the total AIP funding received, their expense does not comply with FAA's policy that use of AIP funds must be properly supported. During our review, LAWA officials stated they will no longer charge this fee.

LAX Airport Revenue Funded Unauthorized Costs

Over 5 fiscal years, LAPD charged approximately \$192,000 for unauthorized positions and overtime in its bill to LAWA. The June 2006 memorandum of agreement (MOA)³² between LAWA and LAPD states that reimbursements to LAPD are based on the deployment and operations plan—a document describing the staffing, equipment, goals, and objectives for the next fiscal year. In addition, according to staff at the LAPD Fiscal Operations Division, overtime is only charged to the airport for those LAPD personnel that are LAWA-funded. Yet, we identified instances where LAPD charged LAWA for personnel not identified in the deployment and operations plan. We also identified instances in which overtime was charged for non-LAWA funded personnel. Specifically:

- **Charges to LAWA for Unauthorized Positions.** LAPD's LAX Field Services Division provides uniformed patrol and participates in a joint crime task force with the Airport Police Division (APD) to conduct investigations. LAPD personnel working in this division are paid by LAWA or LAPD. For fiscal year 2011-2012, LAWA authorized and funded 38 positions of different ranks, while LAPD funded 8 positions. However, during this time, LAPD billed LAWA for 39 positions instead of 38. As a result, LAWA funded an unauthorized LAPD position, resulting in a \$42,665 overcharge to LAWA. According to the LAPD Fiscal Operations Division, the position should have

³¹ The FAA AIP Handbook provides guidance and sets forth policies and procedures for the administration of the AIP.

³² The purpose of the MOA is to ensure that effective and efficient public safety services are provided at LAX. The MOA was updated in May 2013.

been excluded from the charges. As a result, LAPD Fiscal Operations Division plans on preparing the information into a revised bill to LAWA.

- **Overtime Charges to LAWA for Unauthorized Personnel.** We found LAPD charged LAWA \$149,233 of unauthorized overtime over 5 fiscal years. For example:
 - **LAX Field Services Division.** The LAX Field Services Division charged LAWA unauthorized overtime in the amount of \$100,551—or 18 percent—of the total overtime incurred by this division over 5 fiscal years. However, approximately half of that amount—\$53,014—was overtime charged by the same two officers. Although the two officers were assigned to the Division, LAPD—not LAWA—funded the positions. As LAPD-funded employees, their overtime should not have been charged to LAWA. When we discussed this with LAPD’s Fiscal Operations Division, the staff acknowledged that these officers’ overtime should not be charged. Further, they stated that these officers’ overtime will not be billed in the future.
 - **Gang and Narcotics Division.** The Gang and Narcotics Division charged \$477,292 in overtime to LAWA over 5 fiscal years. However, approximately \$48,680, or about 10 percent, of that amount was unauthorized. For example, in fiscal year 2008-2009 and fiscal year 2010-2011, the Gang and Narcotics Division included overtime for detectives who were not assigned to the Division at LAX. These overcharges respectively amounted to \$11,461 and \$8,557.³³

In addition, overtime incurred either before or after an officer’s assignment period at LAX was also inappropriately charged to LAWA. This typically occurred for officers who were only assigned to LAX for a portion of the fiscal year. For example, in fiscal year 2007-2008, the Division included \$24,967³⁴ of unauthorized overtime charges that were earned outside of the officers’ assignment period at LAX. Although one detective was assigned to LAX until December 8, 2007, \$9,308 of overtime earned *after* that date was included in the charge to LAWA. In another example, one officer was assigned at LAX during the middle of the fiscal year 2007-2008. Yet, the officer incurred \$13,041 of overtime both *before* and *after* the assignment period at LAX that was charged to LAWA. Similarly, in fiscal year 2011-2012, a detective charged overtime of \$2,984 that was earned *prior* to the assignment at LAX.

³³ These overcharges comprised of 21.6 percent (\$11,461 of \$52,943) in fiscal year 2008-2009 and 7.8 percent (\$8,557 of \$109,176) in fiscal year 2010-2011 of the total overtime charged to LAWA in each respective fiscal year.

³⁴ \$24,967 represents 18.8 percent (\$24,967 of \$132,868) of the Division’s total overtime charges in fiscal year 2007 through 2008.

FAA's oversight did not detect the \$7.87 million in unsupported charges or the approximately \$192,000 in unauthorized personnel and overtime charges, even though FAA was aware of other revenue use problems at the airport. For example, in June 2012, FAA provided a response to a DOT OIG Hotline complaint alleging improper revenue use and poor LAPD billing practices. FAA's response identified two inappropriate charges, including statutory interest: approximately \$1.7 million for the LAPD Bomb Squad K-9 unit's off-airport responses and about \$1.9 million³⁵ for billing errors uncovered during the investigative process. However, the issues we identified are not included in FAA's response.

FAA DID NOT TAKE ADEQUATE STEPS TO ENSURE THAT LAWA RECEIVED FAIR MARKET VALUE AND MAXIMIZED AIRPORT REVENUES FOR SEVERAL LEASES

Contrary to FAA policy,³⁶ LAWA did not demonstrate that three of its non-aeronautical land leases of airport property were set at fair market value, which is a requirement for the airport to be as self-sustaining as possible. According to FAA policy, fair market pricing can be determined either by reference to negotiated fees charged for similar uses of the airport or an appraisal of comparable properties.

We identified areas where LAWA did not demonstrate receipt of fair market value for several rental properties. Specifically:

- **The rate LAWA charges for three non-aeronautical properties is lower than rates estimated by two professional appraisals, established by the Board of Airport Commissioners, or in LAWA's internal review.** In 2010, the City's Board of Airport Commissioners set the land rental rates ranging from \$2.40 per square foot per year (psfpy) to \$5.50 psfpy, beginning retroactively in January 2009.³⁷ According to the Board, LAWA retained the

³⁵ LAWA uncovered these billing errors. After our investigative office provided the Hotline complaint to FAA, FAA requested LAWA to investigate the allegations contained in the Hotline. LAWA found that approximately \$1.9 million of billing errors was a result of (1) inappropriate upward adjustment of salaries by a compensated time off rate, (2) transposed numbers of wage data in the spreadsheet used to calculate LAPD charges to LAWA, and (3) applying the wrong cost allocation plan (CAP) rate. This amount was credited back to LAWA.

³⁶ Each federally assisted airport owner/operator is required by statute and grant assurance to have an airport fee and rental structure that will make the airport as self-sustaining as possible under the particular airport circumstances in order to minimize the airport's reliance on Federal funds and local tax revenues. The FAA has generally interpreted the self-sustaining assurance to require airport sponsors to charge fair market commercial rates for non-aeronautical uses of airport property.

³⁷ The Board set these rates for on-airport industrial and off-airport commercial land.

services of independent appraisal firms to estimate the fair market value of the land.³⁸

However, 3 of the 12 properties we reviewed were paying rent below amounts established by the Board, appraisal firms, or LAWA's internal review. For example, LAWA charged about \$33,711 for monthly rental payment for one property, according to the most recent invoice LAWA provided to us.³⁹ However, if LAWA were receiving a rate for land lease in accordance with at least the \$2.40 rate set forth by the Board,⁴⁰ LAWA could have received a rental payment of up to about \$62,358 per month.⁴¹ Furthermore, two appraisal firms estimated land rental rates ranging from \$3.20 to \$6.30 psfpy.⁴² If LAWA were receiving rent in accordance with at least the lower appraised rate of the range, it would have received a rental payment of up to about \$83,144 per month.⁴³

Also, one tenant has paid LAWA the same base yearly rent of about \$383,117, for property containing a motel and a restaurant, since LAWA acquired the property in 2000. In 2010, LAWA conducted an in-house review of the property, in part to estimate "a fair market rental value." The review established a fair market rental value ranging from \$463,118 (if the property was valued as separate parcels) to \$941,259 (if the property were vacant, the highest and best use). Based on these estimates, LAWA could have obtained between approximately \$80,000 and \$558,000 in additional rental income, depending on how the property is valued (e.g., as separate parcels or as vacant).

- **LAWA lease files do not contain records of negotiations to reach fair market value.** When asked whether documentation exists to show how fair market value was reached, staff did not recall documenting or preparing memoranda to support the determination.

³⁸ According to the Board, the appraisal firms estimated the fair market value of land including over 61.4 acres of land used for non-airline industrial operations and 6.6 acres of land used for off-airport commercial purposes.

³⁹ This invoice is dated January 2013.

⁴⁰ The Board set the \$2.40 rate in 2010. The rate was scheduled to increase to \$2.45 in 2012, \$2.50 in 2013, and \$2.55 in 2014.

⁴¹ This estimate is based on charging the \$2.40 psfpy rate for paved and unpaved land on the property.

⁴² The appraisal firms estimated rates for non-airport industrial land and off airport commercial land as of January 1, 2009.

⁴³ This estimate is based on charging the \$3.20 psfpy rate for paved and unpaved land on the property.

LAWA staff had various explanations for charging less than the appraised fair market value for non-aeronautical leases:

- **Staff members used appraisals but relied on their professional judgment after considerable analysis to determine rental rates because staff considered professional appraisals and internal reviews to be limited.** According to LAWA staff, professional appraisals and internal reviews do not consider special circumstances of airport property. These include use of comparables that do not have the same characteristics as property on airport land and leases with height restrictions when property is in the path of land aircraft, which can lead to discounted rental rates. However, the two appraisals we reviewed discuss height restrictions. One appraisal stated that “generally there are height restrictions and the only uses permitted are those that would not conflict with the airport, but most commercial and industrial uses would be allowed.” The other appraisal stated “in general industrial-related uses for which land parcels are intended, reflect low-density use and are not impacted by the transitional surface height restrictions.” In addition, FAA guidance specifically states appraisers will need to account for restrictions on the use of airport property when determining fair market value.⁴⁴
- **Staff considered other factors that led to an adjustment of initial appraised rates.** In April 2013, we emailed LAWA staff requesting further clarification on the basis for charging rates lower than those identified in independent appraisals. In August 2013, LAWA officials responded, reiterating their views on the limitations of independent appraisals⁴⁵ but also emphasizing other factors that could lead to an adjustment to the initial appraised rates. According to LAWA, these factors include (1) cost of a vacancy when LAWA and a current or prospective tenant fail to reach agreement and a property sits empty and (2) higher costs inherent in airport property because of security considerations and compliance with City ordinances, such as living wage, which must be built into LAWA leases. However, because LAWA did not document the justification for charging rates below appraised values, the degree to which these factors and data affected the rent charged is unclear. LAWA staff did acknowledge, however, that, in contrast to current practice, providing a memorandum for the file describing the specific factors involved when a lease rate deviates from an appraised rate would be beneficial for documenting those decisions.

⁴⁴ FAA Compliance Order 5190.6B states: “In view of the various restrictions on use of property on an airport (i.e., limits on the use of airport property, height restrictions, etc.) appraisers will need to account for such restrictions when comparing on-airport with off-airport commercial non-aeronautical properties in making fair market value determinations.”

⁴⁵ According to LAWA staff, other data points can be important in determining fair market value, such as (1) actual rents paid for similar uses or properties, (2) comparison of rents for comparable properties at other area airports, and (3) appraisals and market comparables provided by prospective tenants.

- **Staff considered the status of several non-aeronautical properties adjacent to the airport to be in flux because of proposed changes to the LAX Master Plan.**⁴⁶ These proposed changes include construction of an Intermodal Transportation Facility, a People Mover System, and a Consolidated Rent-a-Car facility. We recognize that the situation has been in flux for some time. However, LAWA has been leasing a non-aeronautical property adjacent to proposed changes in the Master Plan at rental rates substantially below rates established by the Board, which ranged from \$2.40 to \$5.50 psfpy.⁴⁷ This property consists of a sizeable piece of land—311,789 square feet—yet we estimate it returned only about \$1.30 per square foot of land per year.⁴⁸ When questioned about the discrepancy, LAWA staff responded the lease requires a minimum rent or percentage of gross receipts, whichever is greater. However, based on the information we received, the rents charged were below the rent set by the Board.

Although LAWA staff provided these explanations, without either adherence to appraised values or documentation to justify rates charged for non-aeronautical properties below appraised values, it is impossible to determine whether LAWA took reasonable⁴⁹ efforts to obtain a fair market rate for these properties and therefore maximize airport revenue.

In response to our concerns about LAWA’s leasing rates, FAA officials stated that they do not review leases and have limited tools to identify this type of problem. However, airport sponsors that receive Federal grants are required to ensure their airport is as self-sustainable as possible through their fee and rental structures,⁵⁰ and FAA is responsible for monitoring and ensuring airport sponsor compliance with applicable Federal requirements. FAA’s Airport Compliance Manual states that as part of the compliance program,⁵¹ FAA district or regional officials may

⁴⁶ In December 2004, the Los Angeles City Council approved the LAX Master Plan and related entitlements for the airport’s future development. According to LAWA, the Plan provided the first major new facilities for, and improvements to, the airport since 1984 and planned to accommodate projected passenger and cargo growth through 2015. In January 2005, several cities challenged approval of the Master Plan. In 2006, the Court approved a Stipulated Settlement, which required LAWA to conduct a Specific Plan Amendment Study (SPAS). In January 2013, LAWA completed the SPAS. According to the City, the SPAS process includes the identification and evaluation of potential alternative designs, technologies, and configurations for the LAX Master Plan Program that would provide solutions to the problems that certain improvements with the Master Plan, referred to as “Yellow Light Projects” were designed to address.

⁴⁷ In 2010, the Board established rates of \$2.40 for on-airport industrial land. It also established rates of \$4.50 and \$5.50 for off-airport commercial land depending on the type of off-airport commercial land.

⁴⁸ According to the most recent invoice LAWA provided to us dated January 14, 2013. This estimate is based on paved and unpaved land on the property.

⁴⁹ Appendix E, FAA Order 5190.6B, Section VII B4 states airport proprietors are encouraged, when entering into new or revised agreements, or otherwise establishing rates, charges, and fees, to undertake reasonable efforts to make their particular airports as self-sustaining as possible in the circumstances existing at such airport.

⁵⁰ Specifically, grant assurance No. 24 states that a sponsor will maintain a fee and rental structure that will make the airport as self-sustaining as possible under the circumstances existing at the particular airport, taking into account such factors as the volume of traffic and economy of collection.

⁵¹ The FAA Airport Compliance Program ensures airport sponsors’ compliance with their Federal obligations in the form of grant assurances, obligations, or other applicable Federal law.

review lease agreements between airport sponsors and aeronautical users. In our opinion, FAA could similarly review non-aeronautical leases to ensure the lease terms do not violate the sponsor's Federal obligations to ensure that its airport is as self-sustainable as possible.

LAWA DID NOT REPORT ACCURATE FINANCIAL DATA TO FAA

We detected financial reporting discrepancies of about \$49 million between the amounts LAWA reported in required annual financial reports to FAA and LAWA's own financial records. Federal law requires airports to annually report financial information so that FAA can evaluate an airport sponsor's compliance with revenue use requirements. To meet this requirement, FAA requires airports to report annual financial information showing the payments and revenues for governmental entities. Airports are required to complete the Financial Governmental Payment Report to document the amounts airports pay to governmental units and all services and property provided to such units. The report is due within 120 days of the end of the airports' fiscal year.⁵² However, we found discrepancies between the Financial Governmental Payment Report and LAWA's internal financial reports.⁵³ For example:

- The airport's report to FAA for 2011 was missing revenues from parking and sales tax of about \$7.2 million that were included on LAWA's financial statements.
- The airport's report to FAA for 2009 contained approximately \$41.6 million less than the sponsor's financial data (see table 2). For example, the report showed no expenditures for legal services. However, LAWA's financial data included about \$4.6 million for such services.

⁵² According to FAA, airport financial information is certified and validated by the Principal Financial Officer at the airport.

⁵³ To fill out the Financial Governmental Payment Report (FAA Form 5100-126), LAWA runs an internal report that shows government customers, vendors, and their revenues and expenditures, which comes from LAWA's internal accounting system.

Table 2. Differences in LAX Expenditures Between LAWA's Financial Data and Data It Reported to FAA in Fiscal Year 2009

| FAA Reporting Classification | Data in LAWA Financial Documents for LAX | Data LAWA Reported to FAA | Difference |
|------------------------------|--|---------------------------|-----------------------|
| Central Services | \$5,331,240 | \$65,506 | \$(5,265,734) |
| Engineering | \$11,040,203 | \$8,413,629 | \$(2,626,574) |
| Firefighting | \$20,267,636 | \$23,225 | \$(20,244,411) |
| Law Enforcement | \$29,295,239 | \$16,990,094 | \$(12,305,145) |
| Legal Services | \$4,648,333 | - | \$(4,648,333) |
| Parking and Sales Tax | \$7,122,955 | \$7,122,955 | \$0 |
| Utilities | \$21,702,666 | \$25,721,026 | \$4,018,360 |
| Mayor & City Council | \$511,499 | - | \$(511,499) |
| TOTAL | \$99,919,771 | \$58,336,435 | \$(41,583,336) |

Source: OIG comparison of Financial Governmental Payment Report (FAA Form 5100-126) and LAWA's financial data for LAX

Note: The table includes differences between LAWA's data and the data that LAWA reported to FAA in 2009. In 2011, LAWA reported \$7,162,978 of Parking and Sales Tax in its financial data for LAX, but did not report this amount to FAA. For more information on the types of payments we reviewed, see Exhibit A to this report. Dollar figures rounded to the nearest whole number.

According to LAWA, the discrepancies occurred, in part, because LAWA had issues with data integrity in 2009. According to FAA, it is generally not FAA's role to review and reconcile airport financial information and the airport is required to certify and validate their annual financial information. However, because FAA uses these financial reports as a source of information to detect whether airport revenue has been diverted from an airport, inaccurate information could reduce the effectiveness of its oversight efforts and provide erroneous information to the public. According to FAA, LAWA re-submitted its financial reports to FAA in February 2014 and, by the end of March 2014, expects LAWA to provide supporting documentation for the re-submitted reports.

CONCLUSION

With limited Federal funding available for airport improvement projects, strong oversight of airport revenue use is critical. Because FAA did not ensure that millions of dollars of LAX airport revenues were used for proper airport purposes or that the airport was as self-sustaining as possible, LAX could continue to be deprived of significant funds each year that could be used to reduce its reliance on Federal funding. Given the airport's past problems, FAA needs to strengthen its oversight of LAX to ensure the airport is as self sustainable as possible and that the airport sponsor does not misuse revenues from its operations.

RECOMMENDATIONS

To improve FAA's oversight of airport revenue, we recommend that FAA:

1. Determine the amount of AIP funds used for unsupported administrative fees that are recoverable and require LAWA to repay these costs to the Federal Government, if appropriate.
2. Require LAWA to justify and document the basis for determining fair market value for each non-aeronautical land lease, particularly in cases where appraised value and/or negotiation do not support lease rates.
3. For reporting years 2009 through 2011, require that LAWA reconcile its financial statement revenues and expenses with the Financial Governmental Payment Report (FAA Form 5100-126), document any discrepancies found, and resubmit the forms, along with supporting documentation, to FAA.
4. Determine the amount of diverted revenue, if any, from payments of unsupported or unauthorized police services that are recoverable by LAWA and require LAWA to recover these costs, plus interest, from the City of Los Angeles.

We also recommend that FAA ensure that the following actions take place:

5. The City of Los Angeles fully implements a recordkeeping system to track when Los Angeles Police Department officers assigned to the airport conduct non-airport work.
6. LAWA develops a process to verify that payments for police services are only for airport purposes and that any time spent on non-airport police assignments is credited back to the airport.

AGENCY COMMENTS AND OFFICE OF INSPECTOR GENERAL RESPONSE

We provided FAA with our draft report on January 29, 2014, and received its formal response on March 19, 2014. FAA's response is included in its entirety as an appendix to this report. In its response, FAA concurred with five of our recommendations and partially concurred with one recommendation. FAA provided appropriate planned actions and timeframes for all recommendations. Accordingly, we consider all six recommendations resolved but open pending completion of planned actions.

ACTIONS REQUIRED

FAA's planned actions for all six recommendations are responsive, and we consider the recommendations resolved but open pending completion of the planned actions.

We appreciate the courtesies and cooperation of FAA, LAWA, LAX, and City of Los Angeles representatives during this audit. If you have any questions concerning this report, please call me at (202) 366-0500 or Scott Macey, Program Director, at (415) 744-3090.

#

cc: DOT Audit Liaison, M-1
FAA Audit Liaison, AAE-100

EXHIBIT A. SCOPE AND METHODOLOGY

We conducted this performance audit from July 2012 through January 2014 in accordance with generally accepted Government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Our audit objective was to assess FAA's oversight of LAX revenue use. Specifically, we evaluated these three sub-objectives: (1) whether FAA's oversight of LAWA ensures proper use of LAX revenues, (2) whether LAX is as self-sustaining as possible, and (3) discrepancies with financial data reported by LAWA to FAA.

As part of our assessment of FAA oversight, we held entrance conferences with FAA officials at Headquarters and the Airport District Office in Los Angeles and also with officials at LAWA. We also met with the FAA Regional Planner, Safety Standards Branch Manager, and the Compliance Program Manager in the Western Pacific Region.

We reviewed prior relevant audit findings and recommendations from GAO, OIG, independent CPA's, and Single Audits reports performed from 2006 through 2010. We also reviewed pertinent legislation, testimony, policy, and orders, such as the Airport and Airway Improvement Act of 1982, as amended, Airway Safety and Capacity Expansion Act of 1987, FAA Authorization Act of 1994, FAA Reauthorization Act of 1996, Title 49 United States Code, Chapter 471, the FAA Revenue Use Policy, the FAA Airport Compliance Manual Order 5190.6B, and the FAA Airport Improvement Program Handbook Order 5100.38C.

For the first sub-objective, to determine FAA's oversight of LAWA ensures proper use of LAX revenue, we analyzed LAPD charges to LAWA. Specifically, to determine how LAPD charges LAWA for police services at the airport, we met with the LAPD Fiscal Operation Division and Budget Section. We also met with LAPD units that work and/or are stationed at LAX, such as the LAPD non-K-9 Bomb Squad, the Gang and Narcotics Division, the Bomb K-9 unit at LAX, and the LAX Field Services Division. We obtained LAPD's billing records, including underlying documentation detailing how the charges for all 12 LAPD units providing services to LAX were formulated, for fiscal year 2011-2012. We reviewed and analyzed these documents to assess how charges were formulated and supported. Based on conclusions drawn from the analysis of fiscal year 2011-2012 LAPD billings, we subsequently obtained and analyzed the billings of 5 of

the 12 units that provide service to LAX (i.e., the LAX Field Services Division, Gang and Narcotics Division, West LA Forgery Unit, Pacific Operations Support Division and Fiscal Operations Division) for fiscal years 2010-2011, 2009-2010, 2008-2009, and 2007-2008. We analyzed this set of documentation to determine whether similar issues existed in those units as identified from the analysis performed on the fiscal year 2011-2012 LAPD charges to LAWA.

We similarly interviewed personnel from the Los Angeles Fire Department (LAFD) Revenue Section to learn how data are captured to ensure the airport is billed only for airport-related work. We toured fire stations near and on the airport and interviewed personnel at the fire stations. We obtained background information on how costs are calculated for providing services to LAX by LAFD, the computer systems used to track operations, and how the individual fire stations distinguish between airport-related and off-airport work for billing.

In addition, we met with the CPAs who performed the 2006 through 2011 Single Audits of LAWA. We met with the Office of the City Administrative personnel regarding the development and billing of City costs to LAX and discussed with the City's Cost Allocation Plan Supervisor how the City's police department charges LAX a divisional overhead rate. At LAWA, we met with the Account operations team for accounts payable and receivable. To determine what audits the City auditors were performing, we discussed current and past audit work with the Office of the Comptroller auditors and contract auditor.

For the second sub-objective, we met with LAWA's Commercial Development staff to determine the process followed to establish fair market rental rates for non-aeronautical leases. We obtained a list of 73 non-airline, non-terminal leases from LAWA. From this list, we reviewed 12 leases which we determined were non-aeronautical. We excluded leases which we ascertained could be potentially considered aeronautical.

For the third sub-objective, we analyzed the 2009 to 2011 FAA Form 126 and 127 airport financial reports to look for agreement to LAWA's financial records. We reviewed the types of payments on the FAA Form 5100-126 (under the "Payments to Governmental Entity" section) for which LAWA provided information to us on how the payments were calculated in its internal financial reports. We excluded the types of payments for which LAWA did not provide information on how they were calculated in its internal financial reports.

EXHIBIT B. ORGANIZATIONS VISITED OR CONTACTED

Federal Aviation Administration (FAA)

- Headquarters
 - (1) Office of the Associate Administrator for Airports
 - (2) Office of Airport Compliance and Management Analysis
 - (3) Office of Airport Safety & Standards
 - (4) Office of Airport Planning & Programming, including Airports Financial Assistance
- Western-Pacific Region - Airports Division
 - (1) Planning
 - (2) Safety Standards, including Compliance Program
- Los Angeles ADO

City of Los Angeles, CA

- Office of the Comptroller
- Office of the City Administrative Officer
- Office of the Controller/Financial Analysis and Reporting Division
- LAPD Fiscal Operation Division and Budget Section
- LAPD Hazardous Devices and Materials Section
 - (1) LAPD Bomb Squad
 - (2) LAPD Bomb Squad K-9 Unit
- LAPD – Gang and Narcotics Division
- LAPD – LAX Field Services Division
- Los Angeles Fire Department Revenue Section
- LAFD Stations 5, 80, and 51

Los Angeles World Airports (LAWA)

- LAWA Planning staff
- LAWA Accounts Receivable and Payable staff
- LAWA Commercial Development Group
- Director of Capital Development and Budget, Finance and Budget Division



Federal Aviation Administration

Memorandum

Date: March 19, 2014

To: Jeffrey B. Guzzetti, Assistant Inspector General for Aviation

From: H. Clayton Foushee, Director, Office of Audit and Evaluation, AAE-1 

Subject: Federal Aviation Administration's (FAA) Response to Office of Inspector General (OIG) Draft Report: FAA's Oversight of Los Angeles International Airport's Use of Airport Revenues

The FAA's Airport Improvement Program (AIP) provides grants to public agencies for the planning and development of public-use airports. When airport owners and operators accept Federal grants, they agree to ensure that airport revenues are used exclusively for airport capital and operating costs and each must establish a fee and rate structure to make the airport as self-sustaining as possible. The FAA is responsible for advising airport sponsors and providing oversight to ensure that they are not in violation of Federal obligations regarding airport revenue, self-sustainability, and other matters. In July 2012, the FAA issued its response to a hotline complaint which alleged airports revenues at Los Angeles International Airport (LAX) were being misappropriated for services unrelated to the airport. After a review, the FAA found two billing errors by the Los Angeles Police Department (LAPD). The finding identified the need for a police officer tracking system that tracks when LAPD officers assigned to the airport conduct non-airport work.

Following the issuance of FAA's response to the hotline complaint, the OIG initiated the subject audit on FAA's oversight at LAX. The FAA provides the following formal response to this audit, respective rationale, actions to be taken, and the time frame for completion of any agreed upon corrective actions.

RECOMMENDATIONS AND RESPONSES

Recommendation 1: Determine the amount of Airport Improvement Program (AIP) funds used for unsupported administrative fees that are recoverable and require Los Angeles World Airports (LAWA) to repay these costs to the Federal Government, if appropriate.

FAA Response: Concur. The FAA's Los Angeles Airports District Office will work with LAWA to determine the amount of unsupported administrative fees charged by LAWA on AIP projects at LAX from 2006 through 2012. To aid the FAA in this review, the FAA requests that the OIG provide the agency with its list of AIP grants for which unsupported administrative costs were found totaling \$360,000. When the amount of unsupported administrative costs is verified, the FAA will determine which of those funds are recoverable and require LAWA to repay them. The FAA plans to implement this recommendation by December 31, 2014.

Recommendation 2: Require LAWA to justify and document the basis for determining fair market value for each non-aeronautical land lease, particularly in cases where appraised value and/or negotiation do not support lease rates.

FAA Response: Partially Concur. The FAA agrees with elements of this recommendation, but we do not agree in its entirety. Federal Register Volume 64, No. 30, Policy and Procedures Concerning the Use of Airport Revenue (Revenue Use Policy) Section VI, B.8 requires that nonaeronautical leases should not be less than fair rental/market value except to the extent permitted for community use purposes (Revenue Use Policy, Section VII.D). However, in the administration of airport agreements, the FAA does not dictate the processes to be used by airports and their sponsors. The airports and their sponsors should clearly provide support and documentation of such agreements.

The FAA will request that LAWA develop a systematic process to document the records of negotiations and any deviations from fair market value determination of all future leases by September 30, 2014.

Recommendation 3: For reporting years 2009 through 2011, require that LAWA reconcile its financial statement revenues and expenses with the Financial Governmental Payment Report (FAA Form 5100-126), document any discrepancies found, and resubmit the forms, along with supporting documentation, to FAA.

FAA Response: Concur. LAWA electronically re-submitted Form 126 for years 2009-2011 to the FAA on February 12, 2014. However, the FAA is awaiting the documentation to support the re-submission and expects to receive this by March 31, 2014. The FAA will report back to OIG by June 30, 2014, if any discrepancies are noted.

Recommendation 4: Determine the amount of diverted revenue, if any, from payments of unsupported or unauthorized police services that are recoverable by LAWA and require LAWA to recover these costs, plus interest, from the City of Los Angeles.

FAA Response: Concur. As stated in FAA's response to the hotline complaint, payments for police services are allowable provided the payment is proportionate to the services rendered. In addition, airports can only pay for actual costs that are documented and substantiated. The FAA will request the City of Los Angeles to provide documentation to support the positions the OIG identified as unsupported. As stated in

FAA's response to recommendation three above, the FAA is awaiting LAWA's reconciliation report, and once this is received, the FAA will be able to determine the amount of diverted revenue, if any. If LAWA cannot provide justification that shows the unsupported or unauthorized police services charged to the airport, then the entire amount should be refunded to LAX, plus applicable interest. The FAA will request that LAWA provide justification for these positions to the FAA no later than September 30, 2014.

For the divisional overhead rate, the FAA will ask LAWA to provide documentation to show how the rate was determined and what it was based upon. In addition, the FAA will request LAWA to provide a full accounting of the divisional overhead rate and bring it up to date, if necessary, for the FAA to gain assurance that the rate conforms to FAA's Policy and Procedures Concerning the Use of Airport Revenue. The FAA will request that LAWA provide an updated divisional overhead rate by September 30, 2014. In addition, any amounts in excess of the value of services received during the last six years should be refunded to LAX.

Recommendation 5: Ensure that the City of Los Angeles fully implements a recordkeeping system to track when Los Angeles Police Department officers assigned to the airport conduct non-airport work.

FAA Response: Concur. In response to the hotline complaint in July 2012 and prior to the initiation of this audit, the FAA had identified the need for an upgraded record-keeping system that tracks when LAPD officers are assigned to airport security and when they are assigned off-airport work. The City concurred with our finding and agreed to implement an upgraded tracking system. The FAA expects LAWA to implement a tracking system that ensures that LAX only pays for airport security-related police services by September 30, 2014.

Recommendation 6: Ensure that LAWA develops a process to verify that payments for police services are only for airport purposes and that any time spent on non-airport police assignments is credited back to the airport.

FAA Response: Concur. As stated in response to recommendation 5, the FAA expects LAWA to implement a tracking system that ensures the airport only pays for airport security-related police services by September 30, 2014. As part of the tracking system, the FAA expects personnel assigned to LAX on a full-time or full-time equivalent basis (the number of total hours worked divided by the maximum number of compensable hours in a full-time schedule) will track the time spent off-airport and the total time deployed. Periodically, the LAPD will report the cost of off-airport time for each position. The aggregate of all off-airport costs will then be deducted from LAWA's payments of the City's bi-monthly bills, if any.