



Fixed Based Operations Audit



City of Charlotte
Internal Audit Department
600 E. Fourth St.
Charlotte, NC 28202

Staff

City Auditor

Tina Adams, CPA, CIA

Deputy City Auditor

Craig Terrell, CPA, CISA

Auditor Supervisor

Marie Marsicano

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Fixed Based Operations Audit

Executive Summary

Objective

This audit was conducted to determine if revenue is accurately reported, and that Aviation has designed an adequate system of controls to monitor fixed based operator (FBO) compliance with the terms and conditions of the contract.

Background

General aviation services are provided by Wilson Air Center, who currently manages the FBO on behalf of the City. The FBO offers a full array of services to both transient and Charlotte-based aircraft to include refueling, ground handling services, and aircraft hangar rental.

Wilson receives an annual management fee of \$250,000, an incentive fee of 6% of the surplus revenues generated and is eligible for an additional 1% service incentive fee if certain service metrics are accomplished.

Conclusion

The fixed base operator (FBO) has complied with the FBO agreement. Implementing additional contract administration procedures would strengthen internal controls.

Highlights

Wilson Air has complied with the FBO agreement, generating net operating revenue of \$8 million in FY2022.

- Complied with significant contract terms
- Accurately reported revenue and expenses
- Earned incentive payment for being one of the top FBOs in the nation

Aviation has determined that the structure of the current FBO management agreement maximizes revenue and facilitates meeting management's objective of providing world-class general aviation services.

- Consultant performed an analysis of the FBO marketplace and alternatives in FY2022.
- Recommendations were made for each of three alternative FBO operating models.
- Aviation should update the FY2022 analysis, choose the most effective FBO alternative and implement the appropriate consultant recommendations related to the chosen alternative.

Aviation has performed limited contract administration duties. Implementing and documenting additional contract monitoring would further strengthen controls over the FBO agreement.

- Roles and responsibilities for FBO contract administration are not identified in policies and procedures.
- Key controls missing for the review of expenditures.
- Based on formal risk assessment, Aviation should implement additional controls to mitigate identified risks.

Actions Planned

Aviation has agreed to implement the recommendations in this report. Specific details regarding these improvements are included in Aviation's responses.

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Objective

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Background

The Charlotte Douglas International Airport (FAA Identifier CLT) is a large hub commercial service airport serving commercial airlines, cargo carriers, general aviation and military activities. The table below depicts aircraft operations (landings and take-offs) by category. The categories include:

- *Air Carrier* - Carriers certificated by the Secretary of the US Department of Transportation as Passenger Carrier under 49 U.S.C 41102 or a Cargo Carrier under U.S.C. 41103.
- *Air Taxi* - Commercial aircraft operator who conducts operations for hire or compensation on demand in accordance with FAR Part 135.
- *General Aviation* - all private, corporate/business, air-ambulance, news gathering, flight training, pipeline patrol, law enforcement, agricultural, and personal flying
- *Military operations* – National Guard, others

CHARLOTTE DOUGLAS INTERNATIONAL AIRPORT ANNUAL AIRCRAFT OPERATIONS					
Year	Total	Air Carrier	Air Taxi	General Aviation	Military
2017	547,812	421,837	99,458	24,917	1,600
2018	550,013	448,537	76,989	23,774	713
2019	578,263	475,102	78,396	23,970	795
2020	397,983	333,229	46,367	17,377	1,010
2021	519,895	428,968	62,239	27,356	1,332
2022	505,589	408,726	64,538	31,158	1,167

Wilson Air Center is the current fixed based operator and manages general aviation services on behalf of the City. The FBO provides fuel services to based tenants and traveling aircraft (to include transient military) at CLT but does not fuel scheduled commercial air carriers or scheduled cargo flights. In addition to the refueling services, the FBO also offers hangar storage and tiedowns, miscellaneous ground handling, and other pilot services.

On October 11, 2004, Council approved a management contract with Wilson Air Center for an initial five-year term with the option to extend the agreement for an additional five years. The contract is for staffing and expertise to provide FBO services. Wilson receives an annual

management fee of \$250,000, an incentive fee of 6% of the surplus revenues generated and is eligible for an additional 1% service incentive fee if certain service metrics are accomplished.

Wilson Air Center has annually been one of the top ranked FBOs in the country according to industry publications, contributing to the Airport's success during growth and expansion. For those reasons, the Airport has continued to extend Wilson Air Center's agreements and has waived the formal solicitation requirements. City Council approved Amendment No. 6 on August 9, 2021, to add three one-year renewal options. Amendment No. 8 exercised the option to enact the second renewal to the FBO agreement for an additional year with a term expiration date of June 30, 2024. Under the current agreement, there is an option for one additional year which would extend the expiration date to June 30, 2025.

For Fiscal Year 2022, Aviation approved an operating budget for Wilson of \$16,988,479 inclusive of the fixed management fee. Due to rising fuel costs, the budget was increased to \$27,225,895 in April 2022.

Scope, Methodology, and Compliance

Scope

This audit focused on FBO operations for Fiscal Year 2022.

Methodology

To achieve the audit objectives, auditors performed the following:

- Interviewed Aviation and FBO staff to gain an understanding of operations.
- Obtained an understanding of internal controls in place for the administration of the FBO agreement.
- Conducted analyses of reported FBO revenue and expenses.
- Selected a judgmental sample of operating expenditures and reviewed the expenditures for reasonableness and allowability.
- Selected a judgmental sample of payroll expenditures and reviewed for accuracy.
- Verified that FBO revenue and expenditures were accurately recorded in the City's financial system.

Judgmental samples of operating expenditures and payroll transactions were selected for review based on dollar value and risk of non-compliance with contract terms.

Compliance

We conducted this performance audit 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.

Government auditing standards require that we determine which internal controls are material to the audit objective and obtain an understanding of those controls. To evaluate internal controls, the City Auditor's Office follows the Committee of Sponsoring Organizations of the Treadway Commission's Internal Control – Integrated Framework (COSO Framework) as included in Standards for Internal Control in the Federal Government (GAO Green Book).

In planning and performing the audit, auditors obtained an understanding of Aviation's processes and the associated internal controls for administering the FBO agreement. Auditors assessed the internal control risks and determined the following internal control components were significant to the audit objectives:

- **Control Environment** – The set of standards, processes and structures that provide the basis for carrying out internal controls.

- **Risk Assessment** – The process for identifying and assessing risks that may limit the achievement of objectives.
- **Control Activities** – The actions management establishes through policies and procedures to achieve objectives and respond to risks.

The internal control deficiencies that are significant within the context of the audit objective are discussed in the Findings and Recommendations section of this report. For additional information regarding internal control components and the related principles of internal control, please see Appendix A.

Findings and Recommendations

1. Wilson Air has complied with the FBO agreement, generating net operating revenue of \$8 million in FY2022.

The FBO agreement requires that Wilson Air submit monthly Financial Summary Reports to Aviation that detail gross revenues, allowable expenses, uncontrollable expenses, and the resulting operating surplus or deficit. Other key requirements include:

- Remittance to Aviation of all revenues attributable to the FBO, including the gross amount of all monies received or receivable by Wilson Air in connection with the agreement on cash or credit basis.
- Adherence to financial, employment and operating policies that are in accordance with the agreement as well as federal, state, and local laws.
- Avoiding or mitigating the amount of uncontrollable expenses.
- Submission of an Annual Certified Revenue Statement.

Auditors conducted analytical reviews and tested a sample of expenditures to verify that Wilson Air accurately reported results of operations for FY 2022, as shown in the table below.

Fixed Based Operations Income Statement Year Ending June 30, 2022	
Revenue	\$ 34,288,929
Cost of Goods Sold	20,043,745
Gross Profit	\$ 14,245,184
Operating Expenses	
Payroll and Benefits	\$ 3,770,894
Other General Operating Expenses	2,211,978
Management Fee	250,000
Total Operating Expenses	\$ 6,232,872
Operating Cash Flow	\$ 8,012,312

Based on the FY 2022 results, Wilson Air earned \$522,037 in service incentive fees for being recognized in the Aviation International News and the Professional Pilot Magazine as attaining a 20% or higher grade as compared to other FBO's in a nationwide survey.

2. Aviation has determined that the structure of the current FBO management agreement maximizes revenue and facilitates meeting management's objective of providing world-class general aviation services.

In FY 2022, Aviation hired Airport Business Solutions to review the general aviation marketplace at CLT and provide recommendations related to the following three management/leasing alternatives:

1. City issues a Request for Proposals (RFP) for a traditional lease agreement for FBO services.
2. City takes over the FBO facilities and operations and manages them with City staff.
3. City continues operation of FBO through a third-party management contractor.

The consultants identified the second and third options as the best choices based on current and anticipated market circumstances. The consultant's report noted several drawbacks to the second option (Aviation management of the FBO) including:

- The need for additional Aviation staff resources and oversight
- Potential pushback from industry associations, airport users, and tenants
- The need to implement a transition plan

The consultant offered recommendations based on Aviation's potential selection of each of the three options. For example, for the third option (third-party management contractor), the consultants recommended that Aviation focus on structuring an agreement that maximizes revenues through incentivizing the management company to grow the business. Aviation should also assess potential incentive benchmarks to maximize growth in net revenue. The consultants noted that other vendors would likely be interested in managing fixed based operations for Aviation.

Airport Business Solutions recognized that their analysis was based on a snapshot in time and that the airport and FBO marketplace conditions are constantly changing. The study was performed during the pandemic and various assumptions were made regarding the return to pre-pandemic conditions. According to the consultants, management should constantly evaluate the changing conditions.

Recommendation: Aviation should update the FY 2022 analysis, choose the most effective FBO alternative, implement appropriate consultant recommendations and incorporate any changes to the scope and contract terms for the next FBO RFP.

Value Added: Compliance; Efficiency; Risk Reduction

Aviation Response: Agree. Aviation will review and consider additional analysis by December 31, 2024.

3. Aviation has performed limited contract administration duties. Implementing and documenting additional contract monitoring would strengthen controls over the FBO agreement.

In Finding #1, auditors noted that Wilson Air has complied with the FBO agreement. However, Aviation has only performed limited contract administration responsibilities and has not performed a formal risk assessment. Based on the inherent risks associated with third-party management contracts, best practices suggest that controls should be put in place to mitigate risks to a tolerable level. Mitigating activities could include more focus on contract monitoring activities of the third party such as conducting compliance audits.

Auditors determined that the following were the most significant **risks** to fixed based operations:

- Aviation does not receive all revenue collected by the FBO
- FBO is reimbursed for expenditures not made (payroll and operating expenses)
- Aviation incurs increased expenditures due to non-existent (due to loss or theft) or inadequately maintained capital assets

Auditors performed a risk and control assessment and noted that Aviation records FBO *reported* revenue in the City's financial system as a receivable but does not periodically reconcile or verify outstanding receivable amounts. As of June 30, 2022, the City's financial system (Munis) noted a balance of \$2.4 million in the revenue clearing account (accounts receivable), compared to a FBO Wilson Air Accounts Receivable report of \$576,190. Reconciling the revenue clearing account to FBO accounts receivable is an opportunity to check for fraudulent activity and to prevent financial statement errors.

The following additional missing or ineffective controls were identified:

- **Policies and procedures** outlining responsibilities for contract monitoring.
- **Documented periodic (annual) risk assessment** to identify necessary changes to the internal control system.
- **Analytical review of reported revenue.** Aviation staff regularly monitors revenue trends but does not obtain detailed revenue reports. Review of detailed transactions could reveal discrepancies between expected and actual revenue. For example, if different fuel prices were charged to various classes of clients - resulting in inconsistent or lower than expected operating margins.
- **Periodic review of operating expenditures.** Aviation staff informally review the monthly financial reports for reasonableness but have not required the FBO to submit detailed expenditure ledgers.
- **Validation of payroll expenditures** through verification of the existence of employees through floor checks and periodic review of payroll registers to confirm labor rates.
- **Physical observation of capital assets.** Aviation staff obtains certification from the FBO and validates (as part of Citywide annual equipment audit) that the capital asset

inventory is accurate (with the exception during COVID pandemic shut down time frame). While the Aviation Contract Manager approves and validates capital asset purchases, the Contract Manager currently does not ensure that capital asset purchases are added to inventory. Aviation does not review records to verify that the FBO is adhering to recommended maintenance schedules for capital assets.

Based on a formal risk assessment, Aviation staff could choose to implement some, or all, of the controls listed above. Controls designated as periodic could be performed on a set schedule or on an as needed basis. The controls could be performed by Aviation staff, consultants, or Internal Audit on request. Without a formal risk assessment and documented control activities, there is no assurance that the inherent risks associated with the third-party management contract are mitigated or reduced to an acceptable level.

Recommendation 3A: Aviation should establish additional procedures that identify responsibilities for contract administration of the FBO agreement, including periodic risk assessment. Based on risk assessment, additional contract administration tasks should be implemented.

Value Added: Risk Reduction

Aviation Response: Agree. Aviation has identified the need for additional staffing resources. As a result, Aviation has recently hired a Business and Revenue Contract Manager. This Manager is dedicated to managing the FBO/Wilson Air management contract. As part of this, the new Contract Manager will review all aspects related to managing the FBO contract and will actively manage the FBO agreement. Implementation anticipated by June 30, 2024.

Recommendation 3B: Aviation should periodically reconcile the FBO revenue clearing account to the FBO Accounts Receivable balance.

Value Added: Risk Reduction

Aviation Response: Agree. Aviation will work with City Finance and FBO Wilson Air to develop a resolution going forward that makes sense based on risk and staffing resources. Implementation anticipated by June 30, 2024.

Conclusion

The fixed base operator has complied with FBO agreement. Implementing additional contract administration procedures would strengthen internal controls.

Distribution of Report

This report is intended for the use of the City Manager's Office, City Council, and Aviation. Following issuance, audit reports are sent to City Council and subsequently posted to the [Internal Audit website](#).

Appendix A

The Five Components and 17 Principles of Internal Control

Control Environment

1. The oversight body and management should demonstrate a commitment to integrity and ethical values.
2. The oversight body should oversee the entity's internal control system.
3. Management should establish an organizational structure, assign responsibility and delegate authority to achieve the entity's objectives.
4. Management should demonstrate a commitment to recruit, develop and retain competent individuals.
5. Management should evaluate performance and hold individuals accountable for their internal control responsibilities.

Risk Assessment

6. Management should define objectives clearly to enable the identification of risks and define risk tolerances.
7. Management should identify, analyze, and respond to risks related to achieving the defined objectives.
8. Management should consider the potential for fraud when identifying, analyzing and responding to risks.
9. Management should identify, analyze and respond to significant changes that could impact the internal control system.

Control Activities

10. Management should design control activities to achieve objectives and respond to risks.
11. Management should design the entity's information system and related control activities to achieve objectives and respond to risks.
12. Management should implement control activities through policies.

Information & Communication

13. Management should use quality information to achieve the entity's objectives.
14. Management should internally communicate the necessary quality information to achieve the entity's objectives.
15. Management should externally communicate the necessary quality information to achieve the entity's objectives.

Monitoring

16. Management should establish and operate a monitoring mechanism that monitors both internal and external activities that impact the control system and evaluate the results.
17. Management should remediate identified internal control deficiencies on a timely basis.