

# AUDIT REPORT



CITY OF NEW YORK  
OFFICE OF THE COMPTROLLER  
BUREAU OF FINANCIAL AUDIT  
**WILLIAM C. THOMPSON, JR., COMPTROLLER**

## **Audit Report on the Compliance of Cablevision Systems New York City Corporation for Brooklyn with Its Franchise Agreement January 1, 2001–December 31, 2002**

*FN03-163A*

**December 22, 2003**



THE CITY OF NEW YORK  
OFFICE OF THE COMPTROLLER  
1 CENTRE STREET  
NEW YORK, N.Y. 10007-2341

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WILLIAM C. THOMPSON, JR.  
COMPTROLLER

**To the Citizens of the City of New York**

Ladies and Gentlemen:

In accordance with the Comptroller's responsibilities contained in Chapter 5, § 93, of the New York City Charter, my office has examined the compliance of Cablevision Systems New York City Corporation for Brooklyn (Cablevision), with the terms of its franchise agreement with the New York City Department of Information Technology and Telecommunications (DoITT). Under the provisions of the agreement, Cablevision is required to pay the City fees based on five percent of its annual gross revenues, less the mandatory payments that Cablevision makes to the New York State Public Service Commission and applicable taxes.

The results of our audit, which are presented in this report, have been discussed with officials from Cablevision and DoITT, and their comments have been considered in preparing this report.

These audits provide a means of ensuring that private concerns under contract with the City comply with the terms of their agreements, properly report revenues, and pay the City all fees due.

I trust that this report contains information that is of interest to you. If you have any questions concerning this report, please contact my audit bureau at 212-669-3747 or e-mail us at [audit@Comptroller.nyc.gov](mailto:audit@Comptroller.nyc.gov).

Very truly yours,

A handwritten signature in cursive script that reads "William C. Thompson, Jr.".

William C. Thompson, Jr.

WTC/GR

**Report:** FN03-163A  
**Filed:** December 22, 2003

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*The City of New York  
Office of the Comptroller  
Bureau of Financial Audit*

**Audit Report on the Compliance of  
Cablevision Systems New York City Corporation  
For Brooklyn with Its Franchise Agreement  
January 1, 2001–December 31, 2002**

**FN03-163A**

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**AUDIT REPORT IN BRIEF**

In 1998, the City, through the Department of Information Technology and Telecommunications (DoITT) renewed the Cablevision Systems New York City Corporation for Brooklyn (Cablevision-Brooklyn) franchise agreement for 10 years. The agreement requires that Cablevision-Brooklyn pay the City five percent of its annual gross revenues, less the mandatory payments that Cablevision-Brooklyn makes to the New York State Public Service Commission (PSC). Cablevision-Brooklyn is also required to carry a \$50 million combined insurance policy for property damage and bodily injury, naming the City as an additional insured; deposit \$4.38 million with the City Comptroller's Office as security; and provide \$4.60 per subscriber annually to support the Community Access Organization (CAO).

This audit determined whether Cablevision-Brooklyn: maintained adequate internal controls over recording and reporting of gross revenues; accurately reported its total gross revenues, and calculated and paid the City the appropriate franchise fees due on time; and complied with certain non-revenue-related requirements of its agreement. For the period January 1, 2001, through December 31, 2002, Cablevision-Brooklyn reported gross revenues amounting to \$385.7 million, and paid the City fees totaling \$18.9 million. In addition, Cablevision-Brooklyn paid the New York State Public Service Commission \$426,114.

**Audit Findings and Conclusions**

Cablevision had an adequate system of internal controls over its recording and reporting of revenues. Cablevision accurately reported its revenues to the City, and accurately calculated and paid its fees to the City on time. In addition, Cablevision maintained the required \$50 million insurance coverage, which named the City as an additional insured; remitted the appropriate security deposit to the Comptroller's Office; and made all required payments to the PSC and the CAO.

However, Cablevision overstated its allowable sales tax deductions by \$276,334 on its Quarterly Gross Revenue Statements to the City for 2001. Consequently, Cablevision owes the City \$14,804 in additional franchise fees and calculated interest for the period, January 1, 2001, through December 31, 2002.

## INTRODUCTION

### Background

On October 8, 1998, the City, through the Department of Information Technology and Telecommunications (DoITT), renewed the Cablevision Systems New York City Corporation for Brooklyn (Cablevision-Brooklyn) franchise agreement for 10 years. The franchise agreement requires that Cablevision-Brooklyn pay the City five percent of its annual gross revenues, less the mandatory payments that Cablevision-Brooklyn makes to the New York State Public Service Commission (PSC).<sup>1</sup> Cablevision-Brooklyn is required to submit to the City each quarter its franchise fee payments, with corresponding revenue reports for the preceding quarter by the 30<sup>th</sup> of January, April, July, and October. Interest on the late payment of franchise fees is assessed at the prime commercial lending rate of JP Morgan Chase Bank.

In addition, Cablevision-Brooklyn is required to:

- carry a \$50 million combined insurance policy for property damage and bodily injury, naming the City as an additional insured;
- remit \$4.38 million to the City Comptroller's Office as security—\$250,000 in cash or City bonds, and the remainder in a line of credit or in another form that is acceptable to both the Comptroller and the City's Corporation Counsel; and
- provide \$4.60 per subscriber annually to support the Community Access Organization (CAO).

Cablevision-Brooklyn distributes more than 200 channels to its subscribers. Cablevision-Brooklyn offers multiple service options consisting of basic service channels, cable programming channels, pay service channels, digital channels, and "Optimum Online," which provides customers with high-speed internet service. The signals are received, amplified, and distributed to subscribers. As of December 31, 2002, Cablevision-Brooklyn provided service to approximately 295,000 subscribers.

The monthly subscriber billings for Cablevision-Brooklyn are managed by DST Innovis.<sup>2</sup> DST Innovis processes subscriber billings and payments, and generates various management reports used by Cablevision-Brooklyn when compiling its financial records. Cablevision-Brooklyn also receives revenue from its weekly programming guides, equipment installation, non-subscriber revenue from home-shopping channel commissions, and revenue from the sales of advertising time. In addition, Cablevision provides free services to its employees and to apartment managers in Brooklyn, and includes the value of such services as revenue in gross revenues reported to the City.

For the period January 1, 2001, through December 31, 2002, Cablevision-Brooklyn reported gross revenues amounting to \$385.7 million, and paid the City franchise fees totaling \$18.9 million. In addition, Cablevision-Brooklyn paid the PSC \$426,114. (See Appendix I for details.) Since Cablevision included \$663,758 related to revenues received from advertising with its franchise fees

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<sup>1</sup> Article 11, § 217, of the New York State Public Service Law, states that PSC operating expenses are to be paid by all cable companies operating in the State. Each cable company's share of PSC operating expenses is based on the company's gross revenue proportion of the total gross revenue of all the cable companies operating in the State.

<sup>2</sup> DST Innovis is a third-party billing, collection, and management company under contract with Cablevision.

paid to the City for Brooklyn, we are conducting an audit of Cablevision's advertising revenue. The results of that audit will be covered in a separate report.

### **Objectives**

Our audit objectives were to determine whether Cablevision-Brooklyn:

- maintained adequate internal controls over recording and reporting of gross revenues;
- accurately reported its total gross revenues, and calculated and paid the City the appropriate franchise fees due, paying those franchise fees on time; and
- complied with certain non-revenue-related requirements of its franchise agreement, (i.e., maintained required liability insurance and security fund deposit, and made all required non-franchise fee payments to the New York State Public Service Commission and Community Access Organization).

### **Scope and Methodology**

This audit covered the period January 1, 2001, through December 31, 2002. To achieve our audit objectives, we reviewed and abstracted the relevant terms and conditions of the franchise agreement. We evaluated the internal control structure that Cablevision-Brooklyn had over its revenue functions. To obtain an understanding of Cablevision-Brooklyn's internal controls, we interviewed its Assistant Divisional Controller and other key personnel. We documented the results through flowcharts and memoranda, determining which areas required further testing. We reviewed the consistency of the gross revenue reported by Cablevision-Brooklyn by performing an analytical review of its quarterly gross revenue statements for the period January 1, 2001, through December 31, 2002.

### **Subscriber Revenue**

For the audit period, subscriber revenue for Cablevision-Brooklyn accounted for approximately 94 percent of total reported gross revenue. To determine whether Cablevision-Brooklyn accurately reported its gross revenue from subscribers, we traced the amounts reported on Cablevision's Quarterly Gross Revenue Statements to the City to its monthly "Schedule for Franchise Fees" and to the corresponding DST Innovis reports for 2001 and 2002. We also determined whether journal entries in Cablevision's general ledger were accurate and appropriate, and whether deductions from revenue were accurate and were made in compliance with the terms of the franchise agreement. Finally, to determine whether Cablevision-Brooklyn actually made its payments to the City, we reviewed Department of Finance payment records and DoITT franchise fee payment schedules.

To determine whether we could rely on the subscriber revenue reports generated by DST Innovis, we reviewed an "Independent Service Auditor's Report" prepared by PriceWaterhouse Coopers LLP for DST Innovis, as it applied to DST Innovis's data processing and applications. The report, in part, stated:

"Our examination included procedures to obtain reasonable assurance about whether (1) the accompanying description presents fairly, in all material respects, the aspects of DST Innovis' controls that may be relevant to a user organization's internal

controls as it relates to an audit of financial statements, (2) the controls included in the description were suitably designed to achieve the control objectives specified in the description . . . In our opinion, the controls that were tested were operating with sufficient effectiveness to provide reasonable, but not absolute, assurance that the control objectives specified were achieved during the period from January 1, 2002, to December 31, 2002.” [13 months.]

### **Non-Subscriber Revenue**

To determine whether non-subscriber revenue for Cablevision-Brooklyn was fairly stated, we traced the amounts reported on Cablevision’s “Schedule for Franchise Fees” for the period January 1, 2001, through December 31, 2002, to its trial balance, general ledger details, and year-end adjusting entries. Furthermore, to determine the reasonableness of the amounts Cablevision-Brooklyn included in its gross revenue for “free service,” we compared the “free service” rates to its rate cards and verified the number of employees and apartment managers receiving “free service” by reviewing the DST Innovis reports. We then traced the related dollar values to various Cablevision-Brooklyn “Free Service” schedules.

### **Contract Compliance Issues**

To determine whether Cablevision-Brooklyn complied with certain non-revenue-related conditions of its agreement, we determined whether Cablevision-Brooklyn had the required insurance coverage by reviewing the original insurance certificates. We also determined whether Cablevision had made the required security deposit and made the required payments to the PSC and CAO.

This audit was conducted in accordance with generally accepted government auditing standards (GAGAS) and included tests of the records and other auditing procedures considered necessary. The audit was performed in accordance with the audit responsibilities of the City Comptroller as set forth in Chapter 5, § 93, of the New York City Charter.

### **Discussion of Audit Results**

The matters covered in this report were discussed with Cablevision-Brooklyn and DoITT officials during and at the conclusion of this audit. A preliminary draft report was sent to Cablevision-Brooklyn and DoITT officials on October 17, 2003. On October 27, 2003, we received written notice from Cablevision officials waiving their right to an exit conference. On November 7, 2003, we submitted a draft report to Cablevision-Brooklyn and DoITT officials with a request for comments.

We received written responses from Cablevision and from DoITT officials on December 1, 2003. Both Cablevision and DoITT officials agreed with the audit findings and recommendations. Cablevision enclosed a check for \$14,804 with its response to cover the audit assessment.

The full texts of Cablevision’s and DoITT’s comments are included as addenda to this final report.

## FINDINGS

Cablevision had an adequate system of internal controls over its recording and reporting of revenues. Cablevision accurately reported its revenues to the City, and accurately calculated and paid its fees to the City on time. In addition, Cablevision maintained the required \$50 million insurance coverage, which named the City as an additional insured; remitted the appropriate security deposit to the Comptroller’s Office; and made all required payments to the PSC and the CAO.

However, Cablevision overstated its allowable sales tax deductions by \$276,334 on its Quarterly Gross Revenue Statements to the City for 2001. Consequently, Cablevision owes the City \$14,804 in additional franchise fees and calculated interest for the period, January 1, 2001, through December 31, 2002, as shown in Table I:

**Table I**

Schedule of Additional Franchise Fees and Interest Owed  
January 1, 2001, through December 31, 2002

Revenue Category	Amounts Deducted From Gross Revenues Reported to the City	Audited Amount	Difference
Sales Tax Deductions	\$446,202	\$169,868	\$276,334
Franchise Fees Due on Overstated Deductions @ 5%			\$ 13,817
Interest Owed the City (see Appendix II)			\$ 987
<b>Total Franchise Fees and Interest Due</b>			<b>\$ 14,804</b>

Specifically, for 2001, Cablevision-Brooklyn collected sales taxes of \$169,868 for installation work conducted during the year. However, it deducted \$446,202 in sales taxes from revenue on its Quarterly Gross Revenue Statements to the City for 2001, resulting in an overstated difference of \$276,334. Consequently, Cablevision owes the City an additional \$13,817 in franchise fees for 2001.

In addition, based on the franchise fees due, Cablevision-Brooklyn owes the City \$987 in interest. (See Appendix II.) Section 9.4 of its franchise agreement with the City requires that Cablevision-Brooklyn pay the City interest in accordance with the following:

“In the event that any payment required by this Agreement is not actually received by the City on or before the applicable date fixed in this Agreement, interest thereon shall accrue from such date at a rate equal to the then prevailing prime rate of interest charged by the Chase Manhattan Bank [JP Morgan Chase Bank] for commercial loans.”

## RECOMMENDATIONS

We recommend that Cablevision:

1. Pay the \$14,804 in additional franchise fees and interest due from January 1, 2001, through December 31, 2002.

***Cablevision's Response:*** Cablevision officials stated that they agreed with the audit findings and recommendations and remitted a check for \$14,804 to cover the audit assessment.

2. Deduct only actual amounts of sales taxes collected from reportable revenue on its Quarterly Gross Revenue Statements to the City.

***Cablevision's Response:*** Cablevision officials stated that: "Cablevision will deduct only actual amounts of sales taxes collected from reported revenues on its Quarterly Gross Revenue Statements to the City."

We recommend that DoITT:

3. Ensure that Cablevision complies with audit report's recommendations.

***DoITT's Response:*** DoITT officials responded that they have discussed the audit findings with Cablevision officials and have been assured that this error will not occur again. In addition, DoITT officials stated that payments from Cablevision will continue to be reviewed and monitored.

**Cablevision Systems New York City Corporation - Brooklyn  
Reported Revenues, Franchise Fees Paid, and NYSPSC Payments  
January 1, 2001 - December 31, 2002**

	<b>Reported Gross Revenue</b>	<b>Franchise Fees Paid</b>	<b>NYSPSC Payments</b>
<b>2001</b>			
1st Quarter	\$ 49,157,625	2,410,792	\$ 56,089
2nd Quarter	47,735,371	2,331,221	55,548
3rd Quarter	45,417,749	2,216,714	54,174
4th Quarter	50,115,264	2,450,244	55,519
<b>Subtotal</b>	<b>\$ 192,426,009</b>	<b>\$ 9,408,971</b>	<b>\$ 221,330</b>
<b>2002</b>			
1st Quarter	\$ 49,190,146	\$ 2,408,262	\$ 51,245
2nd Quarter	48,819,186	2,389,754	51,205
3rd Quarter	48,122,599	2,354,677	51,454
4th Quarter	47,177,664	2,308,004	50,880
<b>Subtotal</b>	<b>\$ 193,309,595</b>	<b>\$ 9,460,697</b>	<b>\$ 204,784</b>
<b>Total</b>	<b>\$ 385,735,604</b>	<b>\$ 18,869,668</b>	<b>\$ 426,114</b>





Via FedEx

December 1, 2003

Mr. Greg Brooks  
Deputy Comptroller  
Policy, Audits, Accountancy & Contracts  
The City of New York  
Office of the Comptroller  
Executive Offices  
1 Centre Street  
New York, NY 10007-2341

Re: Audit Report on the

Compliance of Cablevision Systems  
New York City Corporation for the  
Franchise Agreement with the Bronx  
January 1, 2001 - December 31, 2002  
FN03-162A

Compliance of Cablevision Systems  
New York City Corporation for the  
Franchise Agreement with Brooklyn  
January 1, 2001 - December 31, 2002  
FN03-163A

Dear Mr. Brooks:

We are in receipt of the draft reports for the above referenced audit(s). Cablevision Systems New York City Corporation ("Cablevision") has no objections or corrections to the findings in the report(s).

Accordingly, enclosed is check number 878859 in the amount of \$18,232.00 in additional franchise fees and interest due from January 1, 2001 through December 31, 2002 for the Bronx franchise and check number 878860 in the amount of \$14,804.00 for the Brooklyn franchise.

Pursuant to the Recommendations in the report(s), Cablevision will deduct only actual amounts of sales taxes collected from reported revenue on its Quarterly Gross Revenue Statements to the City.

Sincerely,

A handwritten signature in black ink, appearing to read "Elizabeth A. Losinski".

Elizabeth A. Losinski  
Vice President, Cable Policy

Enclosures

cc: Deputy Commissioner Agostino Cangemi, DOITT  
Bruce Regal, Esq., Corporation Counsel  
Lou Cestra, V.P. Divisional Controller, Cablevision  
Tom Johnson, Assistant Divisional Controller, Cablevision

**ADDENDUM I**

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**CSC HOLDINGS, INC.**  
**Disbursement Account - Cablevision Systems**  
**(516) 803-1500**

THE BANK OF NEW YORK (DELAWARE)  
White Clay Center  
Newark, Delaware 19711

CHECK DATE	CHECK NUMBER
11-NOV-03	878860
VENDOR NUMBER	AMOUNT
1452588050	***\$14,804.00***

**PAY** \*\*\*Fourteen thousand eight hundred four and 00/100 Dollars\*\*\*

TO THE ORDER OF NYC DEPARTMENT OF FINANCE  
25 ELM PL 4TH FL  
BROOKLYN, NY 11201-5807



DETACH AT PERFORATION BEFORE DEPOSITING CHECK

CSC HOLDINGS, INC.  
Disbursement Account - Cablevision Systems  
(516) 803-1500

VENDOR NUMBER: 1452588050

REMITTANCE ADVICE 020000

CHECK NUMBER: 878860

INVOICE NO.	VOUCHER NO.	PO NUMBER	INVOICE DATE	DESCRIPTION	AMOUNT	ENC
0310025			04-NOV-03	2003 NYC AUDIT SETT	14,804.00	
<b>TOTAL:</b>					<b>\$14,804.00</b>	



**DEPARTMENT OF INFORMATION TECHNOLOGY AND  
TELECOMMUNICATIONS**

75 Park Place, 9<sup>th</sup> Floor  
New York, NY 10007  
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**GINO P. MENCHINI**  
*Commissioner*  
*Chief Information Officer*

**AGOSTINO CANGEMI**  
*Deputy Commissioner*  
*Franchise Administration and*  
*Planning/General Counsel*

December 1, 2003

Greg Brooks  
Deputy Comptroller  
Office of the Comptroller  
One Centre Street, Room 530  
New York, NY 10007-2341

Re: Audit reports on the Compliance of Cablevision Systems New York City Corporation for the Bronx and Brooklyn franchise agreements for the period January 1, 2001 to December 31, 2002.  
FN03-162A & FN03-163A

Dear Deputy Comptroller Brooks:

We have discussed the audit findings with Cablevision officials. Cablevision reported that their accountants made an error in calculating sales tax solely for the purposes of deducting them from gross revenues for franchise fee calculations. We have been assured that this error will not occur again. The company has agreed to pay the additional franchise fees and interest due as calculated by the auditors for the period January 1, 2001 through December 31, 2002.

Franchise fee payments will continue to be reviewed and monitored by this agency accordingly. Should you have any questions please contact me at 212-788-6490.

Sincerely,

Marvin E Fields  
Executive Director  
Franchise Administration

c: Gino Menchini, Commissioner (DoITT)  
Agostino Cangemi, Deputy Commissioner/ General Counsel (DoITT)  
Margery Brown, Deputy Commissioner (DoITT)  
Susan Morrison-Goldfine, Executive Assistant, Office of the Comptroller  
Susan Kupferman, Mayors Office of Operations

