COUNTY OF ORANGE
INTERNAL AUDIT DEPARTMENT

OFFICE OF THE DIRECTOR

Integrity
Objectivity
Independence

PETER HUGHES
Ph.D. MBA, CPA, CIA, CFE, CITP
DIRECTOR

MAILING ADDRESS:
400 CIVIC CENTER DRIVE WEST
BUILDING 12, ROOM 232
SANTA ANA, CA 92701

TELEPHONE: (714) 834-5475
FAX: (714) 834-2880
EMAIL: peter.hughes@ocgov.com
WEBSITE: www.oc.ca.gov/audit/

Audit No. 2340

July 2, 2004

TO: Bryan G. Speegle, Director
Resources and Development Management Department

SUBJECT: Limited Review of Sand Canyon LLC (Strawberry Farms Golf Club)
Parcel PR48A-28

We have performed a limited review of certain records and documents for the year ended March 31, 2003, pertinent to the lease agreement (Agreement) between the County of Orange (County) and Sand Canyon LLC, a California limited liability company (Sand Canyon), dated November 8, 1996, as amended. The Agreement is primarily to maintain and operate an eighteen-hole golf course, driving range, and pro-shop on properties owned by the County and the Irvine Ranch Water District (IRWD). The facilities are named the Strawberry Farms Golf Club (SFGC).

The primary purpose of our review was to determine whether SFGC's records adequately supported their computation of monthly gross receipt payments to the County. We also reviewed compliance with certain other provisions of the Agreement, such as accounting methods and payment procedures. The County manages the Agreement on behalf of the County and IRWD based on a concession management agreement between the agencies dated August 22, 1995. Our review did not cover the concession management agreement.

Based on our review, we find that Sand Canyon has overall retained sufficient documentation to adequately support monthly gross receipts reported to the County. However, we did identify rent owed, areas of non-compliance with the Agreement, and areas for improvement as presented below.

1. Reallocation of Advance Reservation Fee, Pro-Shop Fee, Tee Pack Fee, and Environmental Fee
   The Agreement provides for different rent percentages based on the categories of gross receipts, i.e. green fees (includes driving range and cart rentals), pro-shop activities (merchandise, repairs, and lessons), and food and beverage (includes banquets). Green fees are the highest percentage rent category.

   When a customer is charged for a round of golf, the amount paid is shown as a flat amount on the customer receipt, but is typically allocated within Sand Canyon's point of sale cashiering system to more specific revenue accounts as shown below:

   - Green Fee
   - Tee Pack
   - Pro Shop Fee (began May 2002)
   - Advance Reservation Fee
   - Environmental Fee (only for month of May 2002)

Of the above five bulleted items, only green fees were included in the green fee category (currently 10%). The other items were reported in other categories for which the percentage rent is lower (5%). Specific details are:

- Advance Reservation Fee: Sand Canyon indicated that it "charges" this fee for the service of making advance golf reservations. According to Sand Canyon, most customers make reservations in advance. This item is reported as a separate line item on the monthly rent report to the County and 5% rent is paid.
- "Premium" or Pro-Shop Fee: Beginning in May 2002, Sand Canyon indicated that it "charges" this fee to cover the "extra service and ambience" provided by the golf course that is typically not found at a publicly-leased golf course. This item is reported as miscellaneous income on the monthly rent report to the County and 5% rent is paid.
- Tee Pack Fee: Sand Canyon indicated that it "charges" this fee to cover the cost of complimentary tees provided to the customer when playing a round of golf. This item is considered to be merchandise by Sand Canyon and is reported in the pro-shop category on the monthly rent report to the County and 5% rent is paid.
- Environmental Fee: During May 2002 only, Sand Canyon indicated that it "charged" this fee to cover expenses related to maintaining the environmentally sensitive areas of the golf course. The item was reported as miscellaneous income on the monthly rent report to the County and 5% rent was paid.

Based on our review of the above items and the Agreement, all of these items should be reported in the green fees category since they are just a lessee-determined subcomponent/allocation of the amount charged for a round of golf. According to RDMD (formerly PFRD), Sand Canyon did not notify the County of these items or request approval to charge or reclassify these items.

Per Clause 6.B(2)a of the Agreement, percentage rent for the green fee category is as follows:

Year	Rent % of Gross Receipts
1 & 2 (November 1997 – October 1999)	5.0%
3 & 4 (November 1999 – October 2001)	7.5%
5 & 6 (November 2001 – October 2003)	10.0%

Properly classifying the above items as green fees would result in the following amounts due:

Category/Period	Gross Receipts Reported	Rent Paid (5%)	Rent Should Have Paid (7.5%)	Rent Should Have Paid (10%)	Difference (Rent Owed)
Advance Reservations:					
11/99 - 10/01	$ 615,820	$ 30,791	$ 46,187		$ 15,396
11/01 - 3/03	$ 815,401	$ 40,770		$ 81,540	$ 40,770
Pro-Shop Fee:					
5/02 – 3/03	$ 652,056	$ 32,603		$ 65,206	$ 32,603
Environmental Fee:					
May 2002	$ 12,170	$ 609		$ 1,217	$ 609
Tee Pack Fee	(See * below)				
Total Rent Owed					$ 89,378

* We did not calculate an amount due for the tee pack fee. The amount allocated from each round of golf for the tee pack is approximately $3. Rent owed as a result of the reallocation of the tee pack can be easily estimated by Sand Canyon.

Recommendation No. 1A: We recommend that RDMD collect rent owed of $89,378, plus late charges, for the advance reservation, pro-shop, and environmental fee reallocations. We also recommend that RDMD require Sand Canyon to calculate and pay rent owed, plus late charges, for these items for the period after March 2003.

RDMD Response: RDMD agrees with Recommendation No. 1A that all these fees should be properly reported in the green fees category and Sand Canyon has complied with the recommendation. On February 12, 2004, Sand Canyon paid to the County $173,044 to resolve all items included in the audit report. This includes the $89,378 as identified above and an additional $57,531 for the period after March 2003 for advance reservation fees, pro-shop fees and tee pack fees. Additionally the green fees category on the gross receipts form has been modified to include a reference that green fees include advance reservation fees, pro-shop fees and tee pack fees. In the course of resolving all outstanding audit issues, RDMD waived the late fees.

Recommendation No. 1B: We recommend that RDMD require Sand Canyon to calculate and pay rent owed, plus late charges, for the tee pack reallocations.

RDMD Response: RDMD agrees with Recommendation No. 1B and Sand Canyon has complied with the recommendation. On February 12, 2004, Sand Canyon paid to the County $173,044 to resolve all items included in the audit report which included $5,427 for additional rent for tee pack sales during the audit period. Subsequent amounts owed are included in the $57,531 amount as described above.

Recommendation No. 1C: We recommend that RDMD require Sand Canyon to revise the monthly rent report to the County so that it only includes approved categories as contained in the Agreement, or as subsequently approved by RDMD Director.

RDMD Response: RDMD agrees with Recommendation No. 1C and Sand Canyon has complied with the recommendation. RDMD staff prepared and delivered to Sand Canyon, a revised Gross Receipts form that only includes approved categories as contained in the Agreement. Sand Canyon has agreed to use the revised form and only add categories as approved by the RDMD Director. Description for the categories are also included in the form to further clarify items that are to be specifically included in that category.

2. Banquet/Event Equipment Rentals

A. Banquet/Event Equipment Rentals by Outside Vendor (Reporting Net vs. Gross)

Sand Canyon charges a fee for providing equipment used in banquets and other events. In some cases, the necessary equipment must be obtained from an outside vendor. When utilizing an outside vendor, Sand Canyon reports as gross receipts only the difference between the equipment fees charged to the customer and the amount paid by Sand Canyon to the outside vendor.

Clause 10.B of the Agreement states that "gross receipts shall include the charges made by the Tenant for the sale or rendition on or from the Premises of services of any nature or kind … whether the services are actually performed or not." Sand Canyon should report the full amount charged to the customer for equipment rentals.

We found that gross receipts for equipment rentals provided by an outside vendor were underreported by $237,469 for the period January 2000 through March 2003, resulting in rent owed of $17,810 (7.5%). Because the necessary detail records for this item were not available for periods prior to January 2000, we did not determine the amounts owed prior to January 2000.

Recommendation No. 2A: We recommend that RDMD collect rent owed of $17,810, plus late charges, for the banquet/event equipment rentals reported at net amounts. We also recommend that RDMD require Sand Canyon to calculate and pay rent owed, plus late charges, for the periods before January 2000 and after March 2003.

RDMD Response: RDMD agrees with Recommendation No. 2A and Sand Canyon has complied with the recommendation. On February 12, 2004, Sand Canyon paid to the County $173,044 to resolve all items included in the audit report which included $17,810 for additional rent owed for banquet/event equipment rentals reported at net amounts and an additional $1,773 for any prior or subsequent periods. By letter dated February 23, 2004, RDMD also approved a very limited approval of excluding third party equipment rentals provided certain criteria are met.

B. Incorrect Category for Banquet/Event Equipment Rentals (5% vs. 7.5%)

The amount that was reported for banquet/event equipment rentals by Sand Canyon was reported as miscellaneous income and rent of 5% was paid. Clause 6.B(2)b of the Agreement indicates that banquet/meeting sales should be reported in the food and beverage category, which has a 7.5% rent percentage. Therefore, rent of $603 ($24,137 x 2.5%) was underpaid for the period January 2001 to March 2003.

Recommendation No. 2B: We recommend that RDMD collect rent owed of $603 for the banquet/event equipment rentals reported in the incorrect rent category. We also recommend that RDMD require Sand Canyon to calculate and pay rent owed for the period after March 2003.

RDMD Response: RDMD agrees with Recommendation No. 2B and Sand Canyon has complied with the recommendation. On February 12, 2004, Sand Canyon paid to the County $173,044 to resolve all items included in the audit report which included $603 for additional rent owed for the misclassification of banquet/event equipment rentals. Sand Canyon has also corrected its accounting records to eliminate this issue for subsequent periods. Additionally the food and beverage category on the gross receipts form has been modified to include a reference that banquet/event equipment rentals are to be reported in this category.

3. Incorrect Category for Other Site Fees (5% vs. 7.5%)

Sand Canyon charges fees to customers for providing certain décor, equipment, and other services for banquets/events, in addition to the standard banquet site fee. These additional site fees are currently being reported on the monthly rent report to the County as miscellaneous income and rent of 5% is paid.

Clause 6.B(2)b of the Agreement indicates that banquet/meeting sales should be reported in the food and beverage category, which has a 7.5% rent percentage. Therefore, rent of $522 ($20,891 x 2.5%) was underpaid for the period December 2001 to March 2003.

Sand Canyon does properly include the standard banquet site fee in the 7.5% rent category.

Recommendation No. 3: We recommend that RDMD collect rent owed of $522 for the other site fees reported in the incorrect rent category. We also recommend that RDMD require Sand Canyon to calculate and pay rent owed for the period after March 2003.

RDMD Response: RDMD agrees with Recommendation No. 3 and Sand Canyon has complied with the recommendation. On February 12, 2004, Sand Canyon paid to the County $173,044 to resolve all items included in the audit report which included $522 for the other site fees reported in the incorrect rent category. Sand Canyon also has corrected its accounting records to eliminate this issue for subsequent periods. Additionally, the food and beverage category on the gross receipts form has been modified to include a reference that site fees are to be reported in this category.

4. Handicap & Membership Services Activities Require Approval

Sand Canyon offers the following services and charges a related fee:

- Handicap Fee: Scorekeeping and handicap calculations provided by an outside vendor. For calendar year 2002, these fees were approximately $16,820.

- Membership Fee: Becoming a member of the golf course and as such, receiving certain benefits including discounted green fees, lessons, and merchandise. For calendar year 2002, these membership fees were approximately $47,645.

These fees are reported to the County as miscellaneous income and rent of 5% is paid. According to RDMD, Sand Canyon did not notify the County of these services or request approval for reporting these items in a 5% rent category. As this requires further clarification and the proper rent categories have not been established, we did not calculate additional rent owed for these activities.

Recommendation No. 4: We recommend that RDMD require Sand Canyon to submit a written request for approval of the handicap and membership activity and identification of the proper rent categories and rent percentages.

RDMD Response: RDMD agrees with Recommendation No. 4 and Sand Canyon has complied with the recommendation. At RDMD's request, Sand Canyon submitted a request for approval of handicap services and membership fees. The RDMD Director by letter dated October 9, 2003 approved the handicap services request and established the percentage rent at 5%. Subsequently, the RDMD Director of Harbors, Beaches and Parks by letter dated March 18, 2004 approved a membership fee category subject to certain limiting criteria and established the percentage rent at 5%. Rent for both of these uses was previously reported at the 5% level, so no additional rent is due.

5. Financial Statements Require Attestation & Audit by CPA

Clause 13.C of the Agreement requires Sand Canyon to submit to the County an annual balance sheet and income statement prepared by a Certified Public Accountant (CPA). Sand Canyon is required to have the CPA attest that the balance sheet and income statement are an accurate representation of Sand Canyon's records as reported to the United States of America for income tax purposes. Additionally, Sand Canyon is required to submit a statement of gross receipts audited by a CPA.

We noted that, for the years ended December 31, 2000, 2001, and 2002, Sand Canyon submitted a balance sheet and income statement, but they were not prepared by a CPA and did not include the required CPA attestation. Additionally, for the years ended December 31, 2000, 2001, and 2002, Sand Canyon submitted gross receipts statements that were reviewed by a CPA, but not audited by a CPA.

Recommendation No. 5: We recommend that RDMD require Sand Canyon to provide financial statements retroactively and prospectively that comply with the Agreement, most importantly an audited statement of gross receipts.

RDMD Response: RDMD agrees with Recommendation No. 5 and Sand Canyon will comply with the recommendation. Sand Canyon has agreed to resubmit financial statements with the required CPA attestation and gross receipt statements certified as to accuracy by a CPA. Sand Canyon has contracted with a CPA firm for this work and we anticipate receiving the statements by no later than June 30th.

6. Audit Costs Require Reimbursement

Clause 13.C.1 of the Agreement states that the full cost of the audit shall be borne by Tenant if "the audit reveals an underpayment of more than two percent (2%) between the rent due as reported and paid by Tenant in accordance with this Lease and the rent due as determined by said audit."

Due to the underpaid rent noted above in items 1. and 2. above, we determined that Sand Canyon underpaid rent by more than 2% and therefore, audit costs should be assessed to Sand Canyon.

Recommendation No. 6: We recommend that RDMD require Sand Canyon to reimburse the County for audit costs of $9,090.

RDMD Response: Although RDMD concurs with Recommendation No. 6, in the course of resolving all audit issues and in demand for prompt payment of all sums due, RDMD waived the audit costs.

IRWD was in concurrence with this approach and, as provided for in the Concession Management Agreement, IRWD subsequently reimbursed the County one-half of the audit costs.

7. Supervisory Review of Vending Cart Sales

Sand Canyon operates mobile vending carts on the golf course to provide food and beverages to golfers during play. The cart employee prepares a daily inventory sheet at the beginning and end of each day to document the change in inventory and calculate the amount of sales. A supervisor or manager reviews the sheet and observes the inventory count for accuracy. We noted that the daily inventory sheet for 6/1/02 that we sampled contained errors, was completed incorrectly, and was not signed by a supervisor or manager to indicate appropriate supervisory review and approval.

Clause 13.A of the Agreement states that the Tenant must keep "...true and complete books, records, and accounts of all financial transactions in the operation of all business activities...the records must be supported by source documents such as sales slips, cash register tapes ...or other pertinent documents."

Recommendation No. 7: To help ensure mobile vending cart gross receipts are accurate and complete, we recommend that RDMD require Sand Canyon to make sure its daily inventory sheets are reviewed and signed by a supervisor.

RDMD Response: RDMD agrees with Recommendation No. 7 and Sand Canyon has complied with the recommendation. RDMD discussed this finding with Sand Canyon, and Sand Canyon by letter dated September 9, 2003 agreed to have its daily inventory sheets reviewed and signed by a supervisor.

8. Documentation of Register Voids

For two of eight voided cash register transactions in the pro-shop that we reviewed, supporting documentation could not be located. Also, for one of the eight voided transactions, the original sales ticket was not attached to the voided ticket.

Clause 13.A of the Agreement states that the Tenant must keep "...true and complete books, records, and accounts of all financial transactions in the operation of all business activities...the records must be supported by source documents such as sales slips, cash register tapes ...or other pertinent documents."

Recommendation No. 8: We recommend that RDMD require Sand Canyon to maintain adequate supporting documentation of all voided transactions.

RDMD Response: RDMD agrees with Recommendation No. 8 and Sand Canyon has complied with the recommendation. RDMD discussed this finding with Sand Canyon, and Sand Canyon by letter dated September 12, 2003 agreed to maintain adequate supporting documentation of all voided transactions.

We appreciate the courtesy and cooperation extended to us by the personnel at Sand Canyon, RDMD/HBP/Lease Management, and RDMD/Accounting Services. If you have any questions regarding our limited review of lease revenue, please call Eli Littner, Deputy Director, at (714) 834-5899, or Autumn McKinney, Audit Manager, at (714) 834-6106.

Peter Hughes

Dr. Peter Hughes, CPA
Director of Internal Audit

Audit Team:
Eli Littner, Deputy Director, CPA, CIA
Autumn McKinney, Audit Manager, CPA, CIA
Carol Swe, Senior Auditor II, CPA, CIA
Moreland & Associates, Audit Staff

Attachment – RDMD Response

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Foreman, Grand Jury
Darlene J. Bloom, Clerk of the Board of Supervisors

Attachment – RDMD Response

COUNTY OF ORANGE

RESOURCES & DEVELOPMENT MANAGEMENT DEPARTMENT

Bryan Speegle, Director
300 N. Flower Street
Santa Ana, CA

P.O. Box 4048
Santa Ana, CA 92702-4048

Telephone: (714) 834-2300
Fax: (714) 834-5188

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INTERNAL AUDIT DEPARTMENT

DATE: June 29, 2004

TO: Peter Hughes, Director, Internal Audit Department

FROM: Bryan G. Speegle, Director
Resources and Development Management Department

SUBJECT: **Response to Limited Review Audit No. 2340 – Sand Canyon, LLC (Strawberry Farms Golf Club) PR48A-28**

The Resources and Development Management Department (RDMD), formerly the Public Facilities and Resources and the Planning and Development Services Departments, has reviewed the draft letter of the Internal Audit Department's Limited Review of the Strawberry Farms Golf Club lease with Sand Canyon, LLC, for the year ended March 31, 2003. During that period, Sand Canyon operated under the terms and conditions of a lease agreement dated November 8, 1996 ("the Agreement"). The Agreement is for operation and maintenance of an eighteen-hole golf course, driving range and pro-shop on properties owned by the County and Irvine Ranch Water District (IRWD).

We understand the primary purpose of Internal Audit's review was to determine whether Sand Canyon records adequately supported their computation of monthly gross receipts rental payments made to the County and IRWD. We understand that Internal Audit also reviewed compliance with certain other provisions of the Agreement, such as accounting methods and payment procedures. The County manages the Agreement on behalf of the County and IRWD based on a concession management agreement between the agencies dated August 22, 1995.

The audit concluded that Sand Canyon has retained sufficient documentation to adequately support monthly rent payments made to the County; however, the audit identified additional rent owed, areas of non-compliance with the Agreement and areas for improvements. The audit made a total of eight recommendations.

RDMD staff provided Sand Canyon with a copy of Audit No. 2340 and discussed with Sand Canyon the findings, RDMD's responses to the findings and any required actions.

RDMD hereby provides the following "Responses" and "Actions" to the Internal Audit Department's "Findings" and "Recommendations":

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Attachment – RDMD Response (cont'd)

INTERNAL AUDIT FINDING NO. 1

Reallocation of Advance Reservation Fee, Pro-Shop Fee, Tee Pack Fee and Environmental Fee

The Agreement provides for different rent percentages based on the categories of gross receipts, i.e., green fees (includes driving range and cart rentals), pro-shop activities (merchandise, repairs, and lessons) and food and beverage (includes banquets). Green fees are the highest percentage rent category.

When a customer is charged for a round of golf, the amount paid is shown as a flat amount on the customer receipt, but is typically allocated within Sand Canyon's point of sale cashiering system to more specific revenue accounts as shown below:

- Green Fee
- Tee Pack
- Pro Shop Fee (began May 2002)
- Advance Reservation Fee
- Environmental Fee (only for month of May 2002)

Of the above five bulleted items, only green fees were included in the green fee category (currently 10%). The other items were reported in other categories for which the percentage rent is lower (5%). Specific details are:

- Advance Reservation Fee: Sand Canyon indicated that it "charges" this fee for the service of making advance golf reservations. According to Sand Canyon, most customers make reservations in advance. This item is reported as a separate line item on the monthly rent report to the County and 5% rent is paid.

- "Premium" or Pro-Shop Fee: Beginning in May 2002, Sand Canyon indicated that it "charges" this fee to cover the "extra service and ambience" provided by the golf course that is typically not found at a publicly-leased golf course. This item is reported as miscellaneous income on the monthly rent report to the County and 5% rent is paid.

- Tee Pack Fee: Sand Canyon indicated that it "charges" this fee to cover the cost of complimentary tees provided to the customer when playing a round of golf. This item is considered to be merchandise by Sand Canyon and is reported in the pro-shop category on the monthly rent report to the County and 5% rent is paid.

- Environmental Fee: During May 2002 only, Sand Canyon indicated that it "charged" this fee to cover expenses related to maintaining the environmentally sensitive areas of the golf course. The item was reported as miscellaneous income on the monthly rent report to the County and 5% rent was paid.

Based on our review of the above items and the Agreement, all of these items should be reported in the green fees category since they are just a lessee-determined subcomponent/allocation of the amount charged for a round of golf. According to RDMD (formerly PFRD), Sand Canyon did not notify the County of these items or request approval to charge or reclassify these items.

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Attachment – RDMD Response (cont'd)

Per Clause 6.B(2)a of the Agreement, percentage rent for the green fee category is as follows:

Year	Rent % of Gross Receipts
1 & 2 (November 1997 – October 1999)	5.0%
3 & 4 (November 1999 – October 2001)	7.5%
5 & 6 (November 2001 – October 2003)	10.0%

Properly classifying the above items as green fees would result in the following amounts due:

Category/Period	Gross Receipts Reported	Rent Paid (5%)	Rent Should Have Paid (7.5%)	Rent Should Have Paid (10%)	Difference (Rent Owed)
Advance Reservations:					
11/99 - 10/01	$ 615,820	$ 30,791	$ 46,187		$ 15,396
11/01 - 3/03	$ 815,401	$ 40,770		$ 81,540	$ 40,770
Pro-Shop Fee:					
5/02 – 3/03	$ 652,056	$ 32,603		$ 65,206	$ 32,603
Environmental Fee:					
May 2002	$ 12,170	$ 609		$ 1,217	$ 609
Tee Pack Fee	(See * below)				
Total Rent Owed					$ 89,378

* We did not calculate an amount due for the tee pack fee. The amount allocated from each round of golf for the tee pack is approximately $3. Rent owed as a result of the reallocation of the tee pack can be easily estimated by Sand Canyon.

Internal Audit Recommendation No. 1A: We recommend that RDMD collect rent owed of $89,378, plus late charges, for the advance reservation, pro-shop, and environmental fee reallocations. We also recommend that RDMD require Sand Canyon to calculate and pay rent owed, plus late charges, for these items for the period after March 2003.

RDMD Response: RDMD agrees with Recommendation No. 1A that all these fees should be properly reported in the green fees category and Sand Canyon has complied with the recommendation. On February 12, 2004, Sand Canyon paid to the County $173,044 to resolve all items included in the audit report. This includes the $89,378 as identified above and an additional $57,531 for the period after March 2003 for advance reservation fees, pro-shop fees and tee pack fees. Additionally the green fees category on the gross receipts form has been modified to include a reference that green fees include advance reservation fees, pro-shop fees and tee pack fees. In the course of resolving all outstanding audit issues, RDMD waived the late fees.

Internal Audit Recommendation No. 1B: We recommend that RDMD require Sand Canyon to calculate and pay rent owed, plus late charges, for the tee pack reallocations.

RDMD Response: RDMD agrees with Recommendation No. 1B and Sand Canyon has complied with the recommendation. On February 12, 2004, Sand Canyon paid to the County $173,044 to resolve all items included in the audit report which included $5,427 for

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Attachment – RDMD Response (cont'd)

additional rent for tee pack sales during the audit period. Subsequent amounts owed are included in the $57,531 amount as described above.

Recommendation No. 1C: We recommend that RDMD require Sand Canyon to revise the monthly rent report to the County so that it only includes approved categories as contained in the Agreement, or as subsequently approved by the RDMD Director.

RDMD Response: RDMD agrees with Recommendation No. 1C and Sand Canyon has complied with the recommendation. RDMD staff prepared and delivered to Sand Canyon, a revised Gross Receipts form that only includes approved categories as contained in the Agreement. Sand Canyon has agreed to use the revised form and only add categories as approved by the RDMD Director. Description for the categories are also included in the form to further clarify items that are to be specifically included in that category.

INTERNAL AUDIT FINDING NO. 2

Banquet/Event Equipment Rentals

A. Banquet/Event Equipment Rentals by Outside Vendor (Reporting Net vs. Gross)

Sand Canyon charges a fee for providing equipment used in banquets and other events. In some cases, the necessary equipment must be obtained from an outside vendor. When utilizing an outside vendor, Sand Canyon reports as gross receipts only the difference between the equipment fees charged to the customer and the amount paid by Sand Canyon to the outside vendor.

Clause 10.B of the Agreement states that "gross receipts shall include the charges made by the Tenant for the sale or rendition on or from the Premises of services of any nature or kind ... whether the services are actually performed or not." Sand Canyon should report the full amount charged to the customer for equipment rentals.

We found that gross receipts for equipment rentals provided by an outside vendor were underreported by $237,469 for the period January 2000 through March 2003, resulting in rent owed of $17,810 (7.5%). Because the necessary detail records for this item were not available for periods prior to January 2000, we did not determine the amounts owed prior to January 2000.

Internal Audit Recommendation No. 2A: We recommend that RDMD collect rent owed of $17,810, plus late charges, for the banquet/event equipment rentals reported at net amounts. We also recommend that RDMD require Sand Canyon to calculate and pay rent owed, plus late charges, for the periods before January 2000 and after March 2003.

RDMD Response: RDMD agrees with Recommendation No. 2A and Sand Canyon has complied with the recommendation. On February 12, 2004, Sand Canyon paid to the County $173,044 to resolve all items included in the audit report which included $17,810 for additional rent owed for banquet/event equipment rentals reported at net amounts and an additional $1,773 for any prior or subsequent periods. By letter dated February 23, 2004, RDMD also approved a very limited approval of excluding third party equipment rentals provided certain criteria are met.

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Attachment – RDMD Response (cont'd)

B. Incorrect Category for Banquet/Event Equipment Rentals (5% vs. 7.5%)

The amount that was reported for banquet/event equipment rentals by Sand Canyon was reported as miscellaneous income and rent of 5% was paid. Clause 6.B(2)b of the Agreement indicates that banquet/meeting sales should be reported in the food and beverage category, which has a 7.5% rent percentage. Therefore, rent of $603 ($24,137 x 2.5%) was underpaid for the period January 2001 to March 2003.

Internal Audit Recommendation No. 2B: We recommend that RDMD collect rent owed of $603 for the banquet/event equipment rentals reported in the incorrect rent category. We also recommend that RDMD require Sand Canyon to calculate and pay rent owed for the period after March 2003.

RDMD Response: RDMD agrees with Recommendation No. 2B and Sand Canyon has complied with the recommendation. On February 12, 2004, Sand Canyon paid to the County $173,044 to resolve all items included in the audit report which included $603 for additional rent owed for the misclassification of banquet/event equipment rentals. Sand Canyon has also corrected its accounting records to eliminate this issue for subsequent periods. Additionally the food and beverage category on the gross receipts form has been modified to include a reference that banquet/event equipment rentals are to be reported in this category.

INTERNAL AUDIT FINDING NO. 3

Incorrect Category for Other Site Fees (5% vs. 7.5%)

Sand Canyon charges fees to customers for providing certain décor, equipment and other services for banquets/events, in addition to the standard banquet site fee. These additional site fees are currently being reported on the monthly rent report to the County as miscellaneous income and rent of 5% is paid. Clause 6.B(2)b of the Agreement indicates that banquet/meeting sales should be reported in the food and beverage category, which has a 7.5% rent percentage. Therefore, rent of $522 ($20,891 x 2.5%) was underpaid for the period December 2001 to March 2003. Sand Canyon does properly include the standard banquet site fee in the 7.5% rent category.

Internal Audit Recommendation No. 3: We recommend that RDMD collect rent owed of $522 for the other site fees reported in the incorrect rent category. We also recommend that RDMD require Sand Canyon to calculate and pay rent owed for the period after March 2003.

RDMD Response: RDMD agrees with Recommendation No. 3 and Sand Canyon has complied with the recommendation. On February 12, 2004, Sand Canyon paid to the County $173,044 to resolve all items included in the audit report which included $522 for the other site fees reported in the incorrect rent category. Sand Canyon also has corrected its accounting records to eliminate this issue for subsequent periods. Additionally, the food and beverage category on the gross receipts form has been modified to include a reference that site fees are to be reported in this category.

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Attachment – RDMD Response (cont'd)

INTERNAL AUDIT FINDING NO. 4

Handicap & Membership Services Activities Require Approval

Sand Canyon offers the following services and charges a related fee:

- Handicap Fee: Scorekeeping and handicap calculations provided by an outside vendor. For calendar year 2002, these fees were approximately $16,820.
- Membership Fee: Becoming a member of the golf course and as such, receiving certain benefits including discounted green fees, lessons and merchandise. For calendar year 2002, these membership fees were approximately $47,645.

These fees are reported to the County as miscellaneous income and rent of 5% is paid. According to RDMD, Sand Canyon did not notify the County of these services or request approval for reporting these items in a 5% rent category. As this requires further clarification and the proper rent categories have not been established, we did not calculate additional rent owed for these activities.

Internal Audit Recommendation No. 4: We recommend that RDMD require Sand Canyon to submit a written request for approval of the handicap and membership activity and identification of the proper rent categories and rent percentages.

RDMD Response: RDMD agrees with Recommendation No. 4 and Sand Canyon has complied with the recommendation. At RDMD's request, Sand Canyon submitted a request for approval of handicap services and membership fees. The RDMD Director by letter dated October 9, 2003 approved the handicap services request and established the percentage rent at 5%. Subsequently, the RDMD Director of Harbors, Beaches and Parks by letter dated March 18, 2004 approved a membership fee category subject to certain limiting criteria and established the percentage rent at 5%. Rent for both of these uses was previously reported at the 5% level, so no additional rent is due.

INTERNAL AUDIT FINDING NO. 5

Financial Statements Require Attestation & Audit by CPA

Clause 13.C of the Agreement requires Sand Canyon to submit to the County an annual balance sheet and income statement prepared by a Certified Public Accountant (CPA). Sand Canyon is required to have the CPA attest that the balance sheet and income statement are an accurate representation of Sand Canyon's records as reported to the United States of America for income tax purposes. Additionally, Sand Canyon is required to submit a statement of gross receipts audited by a CPA.

We noted that, for the years ended December 31, 2000, 2001, and 2002, Sand Canyon submitted a balance sheet and income statement, but they were not prepared by a CPA and did not include the required CPA attestation. Additionally, for the years ended December 31, 2000, 2001, and 2002, Sand Canyon submitted gross receipts statements that were reviewed by a CPA, but not audited by a CPA.

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Attachment – RDMD Response (cont'd)

Internal Audit Recommendation No. 5: We recommend that RDMD require Sand Canyon to provide financial statements retroactively and prospectively that comply with the Agreement, most importantly an audited statement of gross receipts.

RDMD Response: RDMD agrees with Recommendation No. 5 and Sand Canyon will comply with the recommendation. Sand Canyon has agreed to resubmit financial statements with the required CPA attestation and gross receipt statements certified as to accuracy by a CPA. Sand Canyon has contracted with a CPA firm for this work and we anticipate receiving the statements by no later than June 30th.

INTERNAL AUDIT FINDING NO. 6

Audit Costs Require Reimbursement

Clause 13.C.1 of the Agreement states that the full cost of the audit shall be borne by Tenant if "the audit reveals an underpayment of more than two percent (2%) between the rent due as reported and paid by Tenant in accordance with this Agreement and the rent due as determined by said audit."

Due to the underpaid rent noted above in items 1. and 2. above, we determined that Sand Canyon underpaid rent by more than 2% and therefore, audit costs should be assessed to Sand Canyon.

RDMD Response:

Internal Audit Recommendation No. 6: We recommend that RDMD require Sand Canyon to reimburse the County for audit costs of $9,090. Although RDMD concurs with Recommendation No. 6, in the course of resolving all audit issues and in demand for prompt payment of all sums due, RDMD waived the audit costs. IRWD was in concurrence with this approach and, as provided for in the Concession Management Agreement, IRWD subsequently reimbursed the County one-half of the audit costs.

INTERNAL AUDIT FINDING NO. 7

Supervisory Review of Vending Cart Sales

Sand Canyon operates mobile vending carts on the golf course to provide food and beverages to golfers during play. The cart employee prepares a daily inventory sheet at the beginning and end of each day to document the change in inventory and calculate the amount of sales. A supervisor or manager reviews the sheet and observes the inventory count for accuracy. We noted that the daily inventory sheet for 6/1/02 that we sampled contained errors, was completed incorrectly and was not signed by a supervisor or manager to indicate appropriate supervisory review and approval.

Clause 13.A of the Agreement states that the Tenant must keep "...true and complete books, records, and accounts of all financial transactions in the operation of all business activities...the records must be supported by source documents such as sales slips, cash register tapes ...or other pertinent documents."

Internal Audit Recommendation No. 7: To help ensure mobile vending cart gross receipts are accurate and complete, we recommend that RDMD require Sand Canyon to make sure its daily inventory sheets are reviewed and signed by a supervisor.

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Attachment – RDMD Response (cont'd)

RDMD Response: RDMD agrees with Recommendation No. 7 and Sand Canyon has complied with the recommendation. RDMD discussed this finding with Sand Canyon, and Sand Canyon by letter dated September 9, 2003 agreed to have its daily inventory sheets reviewed and signed by a supervisor.

INTERNAL AUDIT FINDING NO. 8

Documentation of Register Voids

For two of eight voided cash register transactions in the pro-shop that we reviewed, supporting documentation could not be located. Also, for one of the eight voided transactions, the original sales ticket was not attached to the voided ticket.

Clause 13.A of the Agreement states that the Tenant must keep "...true and complete books, records, and accounts of all financial transactions in the operation of all business activities...the records must be supported by source documents such as sales slips, cash register tapes ...or other pertinent documents."

Internal Audit Recommendation No. 8: We recommend that RDMD require Sand Canyon to maintain adequate supporting documentation of all voided transactions.

RDMD Response: RDMD agrees with Recommendation No. 8 and Sand Canyon has complied with the recommendation. RDMD discussed this finding with Sand Canyon, and Sand Canyon by letter dated September 12, 2003 agreed to maintain adequate supporting documentation of all voided transactions.

Thank you for allowing us the opportunity to respond to your draft letter. If you have any questions or need additional information, please feel free to contact Mike Hentzen of my staff at (714) 834-6286.

Bryan Speegle

cc: James D. Ruth, County Executive Officer
Vicki Wilson, Deputy County Executive Officer
Steve Danley, Director, RDMD/Management Services
Kevin Thomas, Director, RDMD/Harbors, Beaches & Parks
Bob Hamilton, Manager, RDMD/HBP/Program Management
Rich Adler, Chief, RDMD/HBP/Lease Management
Mike Hentzen, Leasing Coordinator, RDMD/HBP/Lease Management
Mary Fitzgerald, Manager, RDMD/Accounting Services
Brian P. Murphy, Chief, Central Quality Assurance

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