



INTERNAL AUDIT DEPARTMENT
COUNTY OF ORANGE

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**LIMITED REVIEW OF
LEASE REVENUE
SHIP TO SHORE INSURANCE AGENCY**

**For the Period
June 1, 2004 through May 31, 2005**

AUDIT NUMBER: 2560

REPORT DATE: MAY 9, 2006

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

**LIMITED REVIEW OF LEASE REVENUE
SHIP TO SHORE INSURANCE AGENCY**

**For the Period
June 1, 2004 through May 31, 2005**

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Transmittal Letter

Audit No. 2560

May 9, 2006

TO: George Carvalho, Director
Dana Point Harbor Department (DPHD)

FROM: Peter Hughes, Ph.D., CPA, Director
Internal Audit Department

SUBJECT: Limited Review of Lease Revenue for Ship to Shore Insurance Agency,
Sublease of T.B.W. Company, dba Dana West Marina
Parcel HA78H-24-20, 22

We have completed our limited review of Ship to Shore Insurance Agency, a sublease of the lease agreement with T.B.W. Company, dba Dana West Marina, for the period June 1, 2004 through May 31, 2005. The final report is attached along with your responses to our recommendations.

Please note, beginning in January 2005, we implemented a more structured and rigorous Follow-Up Audit process in response to recommendations and suggestions made by the Audit Oversight Committee (AOC) and the Board of Supervisors (BOS). **In the past, we followed-up on lease audit recommendations during a subsequent lease audit, which could be several years later.** As a matter of policy, our first Follow-Up Audit will now begin at six months upon the official release of the report. The AOC and BOS expect that audit recommendations will typically be implemented within six months and often sooner for significant and higher risk issues. Our second Follow-Up Audit will now begin at 12 months from the release of the original report by which time all audit recommendations are expected to be addressed or implemented.

At the request of the AOC, we are to bring to their attention any audit recommendations we find still not implemented or mitigated after the second Follow-Up Audit. The AOC requests that such open issues appear on the agenda at their next scheduled meeting for discussion.

We have attached a Follow-Up Audit Report Form. The Dana Point Harbor Department should complete this template as our audit recommendations are implemented. When we perform our Follow-Up Audit approximately six months from the date of this report, we will need to obtain the completed document to facilitate our review.

As the Director of Internal Audit, I now submit a monthly audit status report to the Board of Supervisors (BOS) where I detail any material and significant audit findings released in reports

*George Carvalho, Director
Dana Point Harbor Department
May 9, 2006
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during the prior month and the implementation status of audit recommendations as disclosed by our Follow-Up Audits. Accordingly, the results of this audit will be included in a future status report to the BOS.

As always, the Internal Audit Department is available to partner with the Dana Point Harbor Department so they can successfully implement or mitigate difficult audit recommendations. Please feel free to call me should you wish to discuss any aspect of our audit report or recommendations.

Additionally, we will be forwarding to the Dana Point Harbor Department a Customer Survey of Audit Services for completion. The Dana Point Harbor Department will receive the survey shortly after the distribution of this report.

Attachment

Other recipients of this report:

Members, Board of Supervisors
Members, Audit Oversight Committee
Thomas G. Mauk, County Executive Officer
Paul Lawrence, Manager, DPHD/Leasing & Revitalization
Bryan Speegle, Director, RDMD
Mary Fitzgerald, Manager, RDMD/Accounting Services
Betsy Estrada, Chief, RDMD/Accounting Services/External Claims/HB&P Programs
Foreperson, Grand Jury
Darlene J. Bloom, Clerk of the Board of Supervisors



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INTERNAL AUDITOR'S REPORT

Audit No. 2560

May 9, 2006

TO: George Carvalho, Director
Dana Point Harbor Department (DPHD)

SUBJECT: Limited Review of Lease Revenue for Ship to Shore Insurance Agency,
Sublease of T.B.W. Company, dba Dana West Marina
Parcel HA78H-24-20, 22

We have performed a limited review of certain records and documents of Ship to Shore Insurance Agency (SSI) for the year ended May 31, 2005. SSI is a sub lessee under the lease agreement (Lease Agreement) between the County of Orange (County) and T.B.W. Company, dba Dana West Marina (TBW), dated October 21, 1975, as amended. The Lease Agreement is primarily for the operation of the Dana Point West Marina located at Dana Point Harbor. SSI, through a sublease with TBW dated June 15, 1994, operates a boat insurance brokerage agency at the marina.

The primary purpose of our review is to determine whether SSI's records adequately supported gross receipts remitted to the County. We also reviewed compliance with certain other provisions of the Lease Agreement, such as accounting methods and payment procedures.

Based on our limited review, we find that SSI has retained sufficient documentation to adequately support monthly gross receipts remitted to the County but improvements in recordkeeping are needed. **No material weaknesses or significant issues were identified.** However, we identified that SSI owes the County additional rent of \$36,712 for the years 2001 through 2004. We also identified five control findings related to compliance with the Lease Agreement that are noted in the Detailed Observations, Recommendations and Management Responses section of this report. See Attachment A for a description of report item classifications.

We appreciate the courtesy and cooperation extended to us by the personnel at SSI, TBW, DPHD, and RDMD/Accounting Services. If you have any questions regarding our limited review, please contact Eli Littner, Deputy Director, at (714) 834-5899 or Autumn McKinney, Audit Manager, at (714) 834-6106.

*George Carvalho, Director
Dana Point Harbor Department
May 9, 2006
Page ii*



Peter Hughes, Ph.D., CPA
Director, Internal Audit

Attachment A – Report Item Classifications
Attachment B – DPHD Management Response

Distribution Pursuant to Audit Oversight Committee Procedure No. 1:

- Members, Board of Supervisors
- Members, Audit Oversight Committee
- Thomas G. Mauk, County Executive Officer
- Paul Lawrence, Manager, DPHD/Leasing & Revitalization
- Bryan Speegle, Director, RDMD
- Mary Fitzgerald, Manager, RDMD/Accounting Services
- Betsy Estrada, Chief, RDMD/Accounting Services/External Claims/HB&P Programs
- Foreperson, Grand Jury
- Darlene J. Bloom, Clerk of the Board of Supervisors

EXECUTIVE SUMMARY

OBJECTIVES

The Internal Audit Department conducted a limited review of lease revenue pertinent to the lease agreement with T.B.W. Company, dba Dana West Marina (TBW), for the primary purpose of determining whether the records of Ship to Shore Insurance Agency (SSI), a sublease of TBW, adequately supported gross receipts remitted to the County.

BACKGROUND

The County of Orange entered into a 30-year lease agreement (Lease Agreement) with T.B.W. Company dba Dana West Marina (TBW), dated October 21, 1975, for the operation of the Dana Point West Marina and other boat-related services located at Dana Point Harbor. TBW subsequently entered into a sublease with SSI, dated June 15, 1994, for the operation of a boat insurance brokerage agency in accordance with the Agreement. In 2004, SSI reported over \$26,000 in gross receipts and the County received approximately \$2,600 in rent payments.

The Lease Agreement with TBW expired October 31, 2005. The County has entered into a management agreement with TBW for the continued operation of the West Marina commencing on November 1, 2005. During the transition period, the County has entered into month-to-month leases with TBW's former sublessees including SSI.

SCOPE

Our review was limited to certain records and documents that support SSI's gross receipts reported to TBW and remitted to the County for the period from June 1, 2004 to May 31, 2005. We also reviewed compliance with certain other provisions of the Lease Agreement, such as accounting methods and payment procedures. Our review included inquiry, auditor observation, and limited testing for assessing the adequacy of documentation and ensuring completeness of reported gross receipts.

CONCLUSION

Based on our limited review, we find that SSI has retained sufficient documentation to adequately support monthly gross receipts remitted to the County but improvements in recordkeeping are needed. **No material weaknesses or significant issues were identified.** However, we identified that SSI owes the County additional rent of \$36,712 for the years 2001 through 2004. We also identified five control findings related to compliance with the Lease Agreement that are noted in the Detailed Observations, Recommendations and Management Responses section of this report. See Attachment A for a description of report item classifications.



DETAILED OBSERVATIONS, RECOMMENDATIONS AND MANAGEMENT RESPONSES

Rent Owed to the County

Clause 12.B of the Lease Agreement states that gross receipts shall include all charges made on or from the leased premises of services of any nature or kind whatsoever, whether payment is actually made or not.

Findings No. 1 & No. 2: SSI provides insurance brokerage services and receives commissions for new and renewed policies. Also, other insurance brokerage companies may utilize SSI to obtain insurance for their clients, for which SSI receives a portion of the commission. According to Clause 10 of the Lease Agreement, SSI must report all insurance brokerage commissions as gross receipts to the County. However, SSI did not report as gross receipts the commissions earned on policies sold from the leased premises to clients residing outside of Orange County and its portions of commissions earned on policies sold by “sub-brokers.” As a result, during the years 2000 through 2004, SSI underreported gross receipts by \$367,124 and owes rent of \$36,712 to the County. See schedule below:

Year	Income Per SSI's Tax Return	Gross Receipts Reported to County	Underreported Gross Receipts	Additional Rent Due the County (10%)
2000	\$112,491.00	\$30,534.50	\$81,956.50	\$8,195.65
2001	\$96,417.00	\$33,446.25	\$62,970.75	\$6,297.08
2002	\$94,448.00	\$29,622.70	\$64,825.30	\$6,482.53
2003	\$109,942.00	\$35,529.24	\$74,412.76	\$7,441.28
2004	\$109,291.00	\$26,332.58	\$82,958.42	\$8,295.84
Totals	\$522,589.00	\$155,465.27	\$367,123.73	\$36,712.37

Recommendation No. 1: We recommend that DPHD require TBW and SSI to pay \$36,712 in additional rent owed for commissions earned but not reported as gross receipts for the years 2000 through 2004.

DPHD Response: DPHD concurs; estimated completion date is July 28, 2006 (this completion is dependent upon negotiations between TBW and a former sub-tenant).

Recommendation No. 2: We recommend that DPHD require TBW and SSI to calculate and pay additional rent owed for commissions earned but not reported as gross receipts for the period beginning January 1, 2005 through the date of correction.

DPHD Response: DPHD concurs; estimated completion date is April 28, 2006.



Adequacy of Supporting Records – Serially Numbered Forms

Clause 14 of the Lease Agreement requires that SSI maintain 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 invoices or other pertinent documents.

Finding No. 3: SSI does not issue serially numbered source documents, such as invoices or quote forms, to help ensure completeness of reported gross receipts. Based on discussions with SSI, there are standard forms issued to new clients, such as a binder or ACORD (a government-required form), which could be serially numbered and accounted for.

Recommendation No. 3: We recommend that DPHD require TBW and SSI to ensure serially numbered forms are prepared for each new client, and that the numerical sequence of the forms is accounted for.

DPHD Response: DPHD concurs; estimated completion date is April 21, 2006.

Adequacy of Supporting Records – Incomplete or Missing Documents

Clause 14 of the Lease Agreement requires that SSI maintain true and complete books, records, and accounts of all financial transactions in the operation of all business activities. The records must be supported by pertinent source documents.

Finding No. 4: SSI was unable to generate certain financial reports (such as the general ledger by account) or reprint certain financial reports due to computer system limitations. Some documents (such as the profit and loss statement for March 2005) were illegible. According to SSI, its computer system is outdated, has limited functionality, and is no longer supported by the vendor. SSI informed us it is considering replacing the current computer system with one that can provide the financial records required by the Lease Agreement.

Recommendation No. 4: We recommend that DPHD require TBW and SSI to ensure the computer system utilized is capable of generating the financial records required by the Lease Agreement.

DPHD Response: DPHD concurs; estimated completion date is May 5, 2006.

Findings No. 5: SSI receives periodic statements from insurance companies showing the amount of commissions paid to SSI. We found that SSI does not consistently retain and/or receive statements from all of the insurance companies it does business with.

Recommendation No. 5: We recommend that DPHD require TBW and SSI to ensure commission statements are obtained and retained from all insurance companies that SSI does business with.

DPHD Response: DPHD concurs; estimated completion date is April 21, 2006.



ATTACHMENT A: Report Item Classifications

For purposes of reporting our audit observations and recommendations, we have classified audit report items into three distinct categories:

Material Weaknesses:

Audit findings or a combination of Significant Issues that can result in financial liability and exposure to a department/agency and to the County as a whole. Management is expected to immediately address “Material Weaknesses” brought to their attention.

Significant Issues:

Audit findings or a combination of Control Findings that represent a significant deficiency in the design or operation of processes or internal controls. Significant Issues do not present a material exposure throughout the County. They generally will require prompt corrective actions.

Control Findings:

Audit findings that require management’s corrective action to implement or enhance processes and internal controls. Control Findings are expected to be addressed within our follow-up process of six months, but no later than twelve months.





COUNTY OF ORANGE
DANA POINT HARBOR DEPARTMENT

George A. Carvalho, Director
24650 Dana Point Harbor Drive
Dana Point, CA 92629

Telephone: (949) 923-3798
Fax: (949) 496-1225

DATE: May 3, 2006
TO: Peter Hughes, Ph.D., CPA, Director Internal Audit Department
FROM: George A. Carvalho, Director Dana Point Harbor Department
SUBJECT: Draft Report on Limited Review for Ship to Shore Insurance Agency, Sublease of T.B.W. Company, dba Dana West Marina, Parcel HA78H-24-20, 22; Audit 2560.
CC:

Attached are responses to the findings and recommendations of your audit: Draft Report on Limited Review for Ship to Shore Insurance Agency, Sublease of T.B.W. Company, dba Dana West Marina, Parcel HA78H-24-20, 22; Audit 2560. We concur with your recommendations.

I would like to express my appreciation for your department's work regarding the audit of the Ship to Shore Insurance Agency.

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INTERNAL AUDIT DEPARTMENT
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ATTACHMENT B: DPHD Management Responses (cont.)

Dana Point Harbor Department Response

DETAILED OBSERVATIONS, RECOMMENDATIONS AND MANAGEMENT RESPONSES

Rent Owed to the County

Clause 12.B of the Lease Agreement states that gross receipts shall include all charges made on or from the leased premises of services of any nature or kind whatsoever, whether payment is actually made or not.

Findings No. 1 & No. 2: SSI provides insurance brokerage services and receives commissions for new and renewed policies. Also, other insurance brokerage companies may utilize SSI to obtain insurance for their clients, for which SSI receives a portion of the commission. According to Clause 10 of the Lease Agreement, SSI must report all insurance brokerage commissions as gross receipts to the County. However, SSI did not report as gross receipts the commissions earned on policies sold from the leased premises to clients residing outside of Orange County and its portions of commissions earned on policies sold by "sub-brokers." As a result, during the years 2000 through 2004, SSI underreported gross receipts by \$367,124 and owes rent of \$36,712 to the County. See schedule below:

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Recommendation No. 1: We recommend that DPHD require TBW and SSI to pay \$36,712 in additional rent owed for commissions earned but not reported as gross receipts for the years 2000 through 2004.

DPHD Response: DPHD concurs; estimated completion date is July 28, 2006 (this completion is dependent upon negotiations between TBW and a former sub-tenant).

Audit No. 2560



Dana Point Harbor Department Response

Recommendation No. 2: We recommend that DPHD require TBW and SSI to calculate and pay additional rent owed for commissions earned but not reported as gross receipts for the period beginning January 1, 2005 through the date of correction.

DPHD Response: DPHD concurs; estimated completion date is April 28, 2006.

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Dana Point Harbor Department Response

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