



GARLAND

INTERNAL AUDIT

Hawaiian Falls Agreement

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Authorization

Internal Audit (IA) conducted an audit of the Hawaiian Falls Adventure Park (Hawaiian Falls) Agreement. This audit was conducted under the authority of Article VII, Section 5 of the Garland City Charter and in accordance with the Annual Audit Plan approved by the Garland City Council.

Objective

The objectives of this audit are to determine contract compliance regarding the following:

1. Receipt of revenue and the reporting of that revenue to the City (Section 10 – Rent and Section 11 – Records, Reports and Audits).
2. Insurance requirements and specifications (Section 13 – Insurance).
3. Maintenance (Section 14) and Texas State requirements regarding Amusement inspections.
4. Utilization of City services and payments (Section 15 – Utilities and Services).

Scope and Methodology

IA conducted this performance audit in accordance with Generally Accepted Government Auditing Standards. Those standards require that IA plan and perform the audit to obtain sufficient and appropriate evidence to provide a reasonable basis for the findings and conclusions based on the audit objectives. IA believes that the evidence obtained provides a reasonable basis for the findings and conclusions based on the audit objectives.

The scope of the audit was annual rental payments made by Hawaiian Falls from operating seasons 2008 thru 2013.

In order to meet the audit objectives and to describe the scope of our work on internal controls, IA performed the following:

- Obtained and reviewed the Waterpark Groundlease and Operating Agreement (agreement) between Hawaiian Falls and the City of Garland to determine compliance requirements (Obj. 1, 2, 3 and 4).
- Obtained and reviewed annual reports from Hawaiian Falls to determine accuracy of previously reported gross revenues (Obj. 1).
- Obtained and reviewed the general ledger for each of the audited operating seasons to determine daily revenue (Obj. 1).
- Obtained and reconciled register receipts for a sample of days (See Exhibit A) to reconcile with the general ledger and determine the reliability of gross revenues reported by Hawaiian Falls (Obj. 1).
- Performed a gap analysis on the dates listed in each general ledgers provided to determine if gaps were present (Obj. 1).

- Recalculated annual rental payments and late fees to ensure the accuracy of the payments provided (Obj. 1).
- Determined through calculations if any overpayments or underpayments existed during the audited period to ensure that funds were appropriately refunded and/or collected (Obj. 1).
- Requested and obtained a list of fees, rates and prices to ensure compliance with the Agreement in Section 14 - Maintenance (Obj. 1).
- Compared the current Certificate of Insurance on file to requirements listed in the Agreement to ensure compliance with Section 13 - Insurance (Obj. 2).
- Determined communication from Hawaiian Falls regarding annual maintenance to ensure compliance with the Agreement in Section 14 - Maintenance (Obj. 3).
- Compared Material Safety Data Sheets (MSDS) on file with MSDS provided by Hawaiian Falls to ensure compliance with the Agreement as outlined in Section 8.6.3 (Obj. 3).
- Performed a walkthrough of Hawaiian Falls located in Garland to gain an understanding of operations and obtain pictures of current inspections of the park rides (Obj. 3).
- Obtained a listing of current amusement park inspections from the State of Texas to ensure all Hawaiian Falls rides were included and properly listed (Obj. 3).
- Reviewed utility bills to ensure Hawaiian Falls subscribed to all City utility services as outlined in the Agreement (Section 15 - Utilities and Services) (Obj. 4).
- Recalculated and compared utility bills with payments made by Hawaiian Falls to ensure that all fees were collected appropriately (Obj. 4).

To assess the reliability of gross revenues reported by Hawaiian Falls, IA performed the following: (1) Reviewed the general ledgers for each of the operating seasons in the audit period, (2) Interviewed Hawaiian Falls Vice President of Finance and Accounting along with other organization officials, and (3) Traced a sample of receipts to the general ledger for operating seasons 2009, 2012 and 2013 (See Exhibit A). Hawaiian Falls could not provide the general ledger for its 2011 operating season. As a result of our testing, IA could not determine that the data was sufficiently reliable for the purposes of this report (See Finding #1).

Any deficiencies in internal control that are significant within the context of the audit objectives and based upon the audit work performed are stated in the Opportunities for Improvement section starting on page 4.

Overall Conclusion

IA's review of the objectives regarding compliance with the agreement found that Hawaiian Falls was in compliance with Objectives 2 and 4; and partially compliant with Objective 3. However, IA could not determine compliance with Section 10 and 11 of the agreement because the accuracy of the gross revenues reported could not be verified for the audit period (Objective 1).

In addition, improvements could be made in the following areas:

- Gross revenues reported with the annual rental payments should be accompanied by an officer certification as outlined in Section 10.2 (Obj. 1).
- Late fees should be recalculated to ensure accuracy and compliance with the methodology outlined in Section 10.6 (Obj. 1).
- Appropriate MSDS should be obtained annually as outlined in Section 8.6.3 (Obj. 3).

Background

Horizon Amusement South, L.L.C. is an independent contractor which operates Hawaiian Falls located at 4550 North Garland Avenue in Garland. The City of Garland entered into an operating agreement with Horizon Amusement South, L.L.C. to provide for development, operations and management of the water playground that was initially proposed for W. Cecil Winters Park in 2002. The current contract is scheduled to expire in November 2042. In accordance with the agreement the operating season for Hawaiian Falls begins no earlier than May 1 and ends no later than September 30 each year.⁽¹⁾

The agreement between the City and Hawaiian Falls stipulates that the annual rental payment is 5% of the gross revenues during its previous operating season ⁽¹⁾. Gross revenues are reported annually with the rental payment submitted by Hawaiian Falls ⁽¹⁾. Gross revenues and rental payments for the audit period were as follows:

Operating Season	Reported Gross Revenues⁽¹⁾⁽²⁾⁽³⁾	Rental Payment Amount (Gross Revenues*5%)⁽¹⁾⁽²⁾⁽³⁾
2008	\$2,354,436	\$117,658
2009	\$2,562,649	\$128,132
2010	\$2,825,628	\$141,281
2011	\$3,076,915	\$153,846
2012	\$3,565,757	\$178,288
2013	\$3,472,855	\$173,643

The Parks, Recreation and Cultural Arts Department (PRCAD) manages the agreement between the City and Hawaiian Falls.

Because Hawaiian Falls is a contractor, only the items necessary to verify the terms of the contract were examined, not an examination of the entire corporate operation. This examination included information from the inception of the contract. The report will focus on areas of noncompliance with the contract. Recommendations were made to resolve the variances from contract terms.

- (1) The agreement.
- (2) Gross revenue amounts were obtained from documentation provided by PRCAD.
- (3) Amounts listed are rounded to the nearest dollar.

Opportunities for Improvement

During our audit IA identified certain areas for improvement. This audit was not designed or intended to be a detailed study of every relevant system, procedure, and transaction. Accordingly, the Opportunities for Improvement section presented in this report may not be all-inclusive of areas where improvement might be needed.

Finding #1 (Obj. 1)

Condition (The way it is)

Hawaiian Falls sells admission tickets at the front gate and online via their website. Some sales include season passes, group sales, and parties. In addition, food and beverage and retail items are sold inside the park. At the end of the day, each register is totaled and reported to the Hawaiian Falls office located in Irving. Annual gross revenues for the operating season are compiled and reported along with Hawaiian Falls' annual rental payment.

- A. As part of the review regarding reliability of the gross revenues reported, IA obtained the general ledgers from Hawaiian Falls and compared them to register receipts for a sample of operating days (see Exhibit A) to verify if the data reported was accurate. The register receipts included sales from admissions, some season passes, some online sales, parties, food and beverage, and retail.

IA's review found the following:

- Hawaiian Falls could not provide the 2011 operating season general ledger.
 - IA could not reconcile the daily register receipts to the general ledger.
 - Hawaiian Falls could not provide source documentation for group ticket sales, group food and beverage sales, season pass sales and online ticket sales.
 - Some register receipts did not list the correct date from the operating days sampled.
- B. In addition, gross revenues provided by Hawaiian Falls were not always certified by an officer of the organization.

Criteria (The way it should be)

- A. Section 11.1 states "Contractor shall keep true and accurate books and records showing all of its business transactions concerning its operations on the Premises in separate records of account in a manner acceptable to Garland and Garland shall have the right through its representative, and at all reasonable times, to inspect such books and records including sales tax returns and other amusement and/or admissions tax records. Contractor hereby agrees that all such records and instruments are available to

Garland."

- B. Section 10.2 - Annual Payment states "Contractor shall make its rent payment on or before December 31 of each year and shall provide to Garland, in addition to such payments, a statement certified by an officer or agent of the Contractor of the gross revenues for the preceding year."

Effect (So what?)

- A. IA could not ensure the accuracy of the gross revenues reported to the City annually.
- B. Hawaiian Falls is not in compliance with Section 10.2 of the agreement.

Cause (Difference between condition & criteria)

- A. Hawaiian Falls' entire accounting Department was replaced in August of 2013 and accounting records were not maintained properly.
- B. Hawaiian Falls was unaware of the criteria.

Recommendation

Management should:

- A. 1. Conduct a ticket sales operations review and audit records of receipts to verify accuracy during the 2014 operating season.
2. Obtain the generals ledgers and supporting evidence (at least for the major items) on an annual basis.
3. Conduct random testing to verify the accuracy of the gross revenues reported to the City.
- A. A statement of gross revenues is certified by an officer of the organization and is included with the annual payment.

Management Response

- We concur with IA on the recommendations.

Action Plan

- Department sent a letter to Hawaiian Falls outlining the major deficiencies and immediate steps to correct the deficiencies.
 - Hawaiian Falls shall provide a "statement certified by an officer or agent...of the Gross Revenues for the preceding year".
 - Per the following paragraphs of the operating agreement, 7.4. Control of Ticket Sales, 11.1. Maintenance and Disclosure of Records, and 11.3. Cash Register Equipment, the City's representative shall this summer review and audit records of receipts and inspect records for all business transactions at the park.
- We will inform Hawaiian Falls that we will require a copy of the general

ledgers and supporting evidence on an annual basis.

- We will revise our current checklist to include Internal Audit recommendations and develop procedures.

Implementation Date

- Summer 2014 / Fall 2014 / Winter 2015

Finding #2 (Obj. 1)

Condition (The way it is)

IA reviewed payments received from Hawaiian Falls for operating seasons 2008 through 2013 and found that payments for three of the six operating seasons were made late. IA's review of late payments revealed the following:

A. Late fees were not accurately calculated by Hawaiian Falls as follows:

Operating Season	Late Fees Paid	Late Fees Should have been paid	Amount (Over)/Under
2009	\$11,677.06	\$4,910.46	(\$6,766.60)
2011	\$1,211.53	\$1,788.45	\$576.92
2012	\$4,323.24	\$4,272.05	(\$51.19)

B. Overpayments for 2009 & 2012 were not refunded to Hawaiian Falls and underpayments for 2011 were not collected by the City.

Criteria (The way it should be)

A. & B. According to Section 10.6 – Late Payments of the agreement states, "in the event a rental payment is not made on or before the due date herein provided, Contractor shall pay to Garland a late charge on unpaid rental payments at the rate of .75 percent per month from and after the due date thereof until the date of payment." Also, according to the agreement Garland can waive the late charge at its discretion.

Effect (So what?)

- A. The City may not receive all applicable late fees if fees are not accurately calculated.
- B. Overpayments and underpayments were not appropriately applied in 2009, 2011 and 2012.

Cause (Difference between condition & criteria)

- A. Hawaiian falls did not use the correct number of months to calculate the late fees
- B. The City did not verify payments made by Hawaiian Falls to ensure accuracy of Late Payments calculated (See Exhibit B).

Recommendation

Management should:

- A. Recalculate Late Fees to ensure accuracy of fees collected.

B. Ensure Late Fees are appropriately refunded or collected in a timely manner.

Management Response

- We concur with IA on the recommendations.

Action Plan

- We will base our calculation on this audit and submit to Finance Department for verification.
- We will ensure all fees are paid in a timely manner.

Implementation Date

- Summer / Fall 2014 / Winter 2015

Finding #3 (Obj. 3)

Condition (The way it is)

Hawaiian Falls purchases chemicals and cleaning products for use at its facility in Garland and provides MSDS sheets for our records. MSDS sheets contain information about the chemical or product regarding first aid instructions, emergency details, composition and storing recommendations, as well as important handling guidelines.

As part of the audit, IA compared MSDS sheets on file with PRCAD with MSDS sheets obtained from Hawaiian Falls. IA's comparison 23 MSDS sheets revealed that only one matched the MSDS sheets on file with PRCAD.

Criteria (The way it should be)

Section 8.6.3 of the agreement stipulates that Hawaiian Falls should provide the City with copies of MSDS sheets prior to application of chemicals on the premises.

Effect (So what?)

The City of Garland cannot know the types of chemicals used unless MSDS sheets are provided. Chemicals that pose a danger to people or the environment could be used without the City's knowledge.

Cause (Difference between condition & criteria)

Hawaiian Falls changed vendors and PRCAD did not obtain new MSDS sheets that should have been provided each year.

Recommendation

Management should ensure that appropriate copies of MSDS are obtained each year.

Management Response

- We concur with IA on the recommendation.

Action Plan

- The Aquatic/Athletic Manager received a hard copies of the MSDS sheets for 2014 and will request a new copies of the MSDS sheets annually.

Implementation Date

- June 2014

Exhibit A

Sampling Methodology

IA obtained the general ledgers for each of the years audited and compared the gross revenues listed in the general ledger with those reported in each of the audited years. Hawaiian Falls was unable to provide the general ledger for the 2011 operating season.

Recalculations revealed that the late payments paid by Hawaiian Falls were not accurately calculated for operating seasons 2009 and 2012. Therefore, IA judgmentally selected these years as well as 2013 for additional testing then IA calculated the number of operating days listed for each operating season:

Year	No. of Operating Days	No. of Sampled Days
2013	109	4
2012	110	7
2009	114	6

IA judgmentally selected days based on the amount of revenue recorded in the general ledger and varied our selections by high and low dollar amounts collected as well as chose days that were spread over the operating season. This sampling methodology was chosen to review areas in the population that could be considered high risk.

IA obtained register receipts for each of the days in the sample and traced the receipts to the general ledgers. Some register receipts did not list the correct date. In addition, IA found that receipts could not be reconciled with the general ledger. Hawaiian Falls reconciled the data; however, their accounting department could not provide documentation to validate admission ticket, group, season pass and online sales.

As a result of our testing, IA could not determine the reliability of the information provided by Hawaiian Falls.

Exhibit B

Hawaiian Falls Payment Review

2009 Operating Season	
Gross Revenue	\$2,562,649.00
Rent (Gross Revenue * 5%)	\$128,132.45
Payment #1 - 4/21/2010	(\$25,000.00)
Late Fee	\$3,363.48
Payment #2 - 6/25/2010	(\$114,809.51)
Late Fee	\$1,546.99
Over Payment Made (Rent+Late Fees-Payments)	(\$6,766.60)

2011 Operating Season	
Gross Revenue	\$3,076,914.99
Rent (Gross Revenue * 5%)	\$153,845.75
Payment #1 - 1/14/12	(\$100,000.00)
Late Fee	\$576.92
Payment #2 - 4/15/12	(\$55,057.28)
Late Fee	\$1,211.53
Under Payment Made (Rent+Late Fees-Payments)	\$576.92

2012 Operating Season	
Gross Revenue	\$3,565,757.42
Rent (Gross Revenue * 5%)	\$178,287.87
Payment #1 - 1/1/2013	(\$35,657.57)
Late Fee	\$1,604.59
Payment #2 - 2/15/2013	(\$36,727.30)
Late Fee	\$2,382.82
Payment #3 - 5/15/2013	(\$30,000.00)
Late Fee	\$284.64
Payment #4 - 5/31/2013	(\$80,226.24)
Over Payment Made (Rent+Late Fees-Payments)	(\$51.19)