
Performance Audit of the Mission Bay Improvement Fund

OPPORTUNITIES FOR IMPROVEMENT EXIST TO DOCUMENT
INTERNAL CONTROLS

MARCH 2012

Audit Report
Office of the City Auditor
City of San Diego



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THE CITY OF SAN DIEGO

March 16, 2012

Honorable Mayor, City Council, and Audit Committee Members
City of San Diego, California

Transmitted herewith is an audit report on the Mission Bay Park Improvement Fund and the San Diego Regional Parks Fund. This report is in accordance with City Charter Section 39.2. The Results in Brief is presented on page 1. The Administration's response to our audit recommendations can be found after page 27 of the report.

If you need any further information please let me know. We would like to thank the City Comptroller's staff, as well as representatives from other City departments for their assistance and cooperation during this audit. All of their valuable time and efforts spent on providing us information is greatly appreciated. The audit staff responsible for this audit report is Danielle Knighten, Kyle Elser, and Chris Constantin.

Respectfully submitted,

Eduardo Luna
City Auditor

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Results in Brief

With the passage of proposition C in 2008, the City Charter requires the City Auditor to conduct an annual audit of the Mission Bay lease revenue distributed to, and expended from, the San Diego Regional Parks Fund and the Mission Bay Improvement Fund beginning with fiscal year 2010. The new City Charter requirements replaced a previous City Council Ordinance¹ that originally established these Funds.

The Mission Bay lease revenues collected for fiscal year 2010, after adjustments, totaled \$23,984,104. Per the City Charter, any revenue in excess of the \$23 million threshold is to be distributed between the San Diego Regional Parks Fund and the Mission Bay Improvement Fund. As a result, the San Diego Regional Parks Fund received a distribution totaling \$984,104, and there was not enough lease revenue to distribute any monies to the Mission Bay Improvement Fund. Additionally, there were no fiscal year 2010 expenditures approved by the new Oversight Committees established by the City Charter. All the expenditures related to San Diego Regional Parks Fund or Mission Bay Improvement Fund were for projects approved prior to the beginning of fiscal year 2010.

Although the San Diego Regional Parks Fund only received a distribution of \$984,104 in fiscal year 2010, the actual amount that should be available to the new Oversight Committee is \$1,623,777. The \$639,673 difference is from an overestimated prior year accrual that reduced the fiscal year 2010 distribution amount.

While the new Oversight Committee should have \$1,623,777 available in the San Diego Regional Parks Fund for projects, in actuality, this Fund has overcommitted projects totaling (\$2,080,923), and the Mission Bay Improvement Fund has overcommitted projects totaling (\$2,420,604) as of June 30, 2010. Overcommitted projects means that the approved budgeted expenditures for projects exceed the current funds

¹ San Diego Municipal Code 22.0229

available. We found that the amount of funds overcommitted for projects is primarily due to prior years' inaccurate revenue budgeting estimates.

City Officials advised the Funds will remain overcommitted until Financial Management (FM) releases the unfunded or abandoned projects. As the overcommitted funding issues are being resolved, we found that the City Comptroller should establish a methodology to separately account for the \$1,623,777 that should be allocated to the San Diego Regional Parks as required by the City Charter.

We also found that the Office of the City Comptroller does not have documented policies and procedures for the Mission Bay lease revenues, and the existing procedures and process flow diagrams are broad in nature for the department as a whole and not specific to these unique transactions.

We provide three recommendations to improve the accounting process related to the Mission Bay lease revenue. The City Comptroller and Financial Management agreed with all three recommendations; the Administration's written response to the audit can be found after page 27 of this report.

Introduction

In accordance with the City Auditor's Fiscal Year 2012 Audit Work Plan, we conducted an audit of the Mission Bay Improvement Fund and Regional Parks Fund. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

We would like to thank management and staff from the Office of the City Comptroller, Financial Management, Office of the City Treasurer, Development Services Department's Facilities Financing and Real Estate Assets Department, as well as representatives from other departments for their assistance and cooperation during this audit. All of their valuable time and efforts spent on providing us information is greatly appreciated.

Background

Mission Bay Park Mission Bay Park is the largest man-made aquatic park in the country, consisting of 4,235 acres, approximately 46 percent land and 54 percent water.² In 1945, Mission Bay Park was transferred to the City of San Diego (City) with several restrictions, some of which were adopted by the citizens of the City into the City Charter and others implemented as part of the California Coastal Commission's oversight of local planning and land use decisions. These limitations include:

- a ban on permanent residential development or any private ownership of land within the tidelands; and,
- a limit on commercial development of leaseholds of no more than 25 percent of the land area and 6.5 percent of the water area for private purposes.

These limitations assure that most of the acres in Mission Bay Park are available for public recreational use.

Mission Bay Park Lease Revenues The City collects Mission Bay Park lease revenues (lease revenues) from commercial and non-profit sources within Mission Bay Park, including, but not limited to, funds received under leases of City-owned property within Mission Bay Park, revenues collected from contracts for concessions, and other revenues collected for the use of City-owned property within Mission Bay Park.³ The City Treasurer's Revenue Audit Division audits the percentage-based leases to ensure rent owed to the City is properly remitted.

Special Park Funds Created in 2002 In October 2002, the City Council passed an ordinance that established two special funds entitled Mission Bay Improvement Fund and Regional Park Improvement Fund. These newly-created funds received revenue from the Mission Bay leases in excess of \$20 million.

² See Appendix B for a detailed map of Mission Bay Park, including permit sites identified by the Real Estate Assets Department (READ).

³ Lease revenues exclude items such as Mission Bay golf course, unless privately leased; mooring fees; any revenues from taxes including but not limited to Transient Occupancy Taxes, sales taxes, possessory interest taxes and property taxes. These revenues also exclude permit fees such as park and recreation fees or special event fees to the extent that those fees are levied to recover actual costs incurred by the City.

The Mission Bay Improvement and Regional Park Funds were each funded with an amount equal to 25 percent of the annual excess Mission Bay lease revenues, but not to exceed \$2.5 million. However, if anticipated revenues were insufficient to maintain existing City services, the City Manager had the option to ask the City Council to suspend the allocation distribution for the upcoming fiscal year.

The intent of the Mission Bay Improvement Fund was for permanent public capital improvements and deferred maintenance. The Regional Park Fund was intended for permanent public capital improvements, planning, deferred maintenance, and land acquisitions.

**2008 City Charter
Revisions to Park Funds**

In November 2008, Proposition C passed and resulted in changes to the Mission Bay Park and Regional Parks Improvement Funds. Effective July 1, 2009, the major changes included (1) an increase to the threshold amount, (2) different allocation percentages, (3) the formation of oversight committees for each of the funds, (4) the prioritization of projects and (5) a mandatory distribution of lease revenue above the threshold amounts.

Under the new Charter section, the Regional Park Fund is funded first before the money is available for the Mission Bay Improvement Fund. In order for the Mission Bay Improvement Fund to be funded, there must be more than \$2.5 million available in excess Mission Bay lease revenue. The Mission Bay percentage allocation increased from 25 percent to 75 percent.

This charter change also created and established the Mission Bay Improvement Fund Oversight Committee and the San Diego Regional Parks Improvement Fund Oversight Committee. The Oversight committees are charged with acting in an advisory capacity to the City Council, which includes recommending the priorities for expenditures and capital improvements in accordance with the Mission Bay Park Master Plan and verifying appropriate funds are collected, segregated, retained and allocated and spent as prioritized.

**San Diego Regional
Parks Improvement
Fund**

The San Diego Regional Parks Improvement Fund is a separate interest-bearing monetary fund maintained by the City to receive and spend Mission Bay Park lease revenues as previously identified for the benefit of the San Diego Regional Parks (Regional Parks). The City's Regional Parks are those parks that serve regional residents and/or visitor populations, as determined by City Council ordinance, including: Balboa Park, Chollas Lake Park, Mission Trails Regional Park, Otay River Valley Park, Presidio Park, San Diego River Park, open space parks, and coastal beaches and contiguous coastal parks. The Regional Parks specifically exclude Mission Bay Park and the Improvement Zone.

Effective July 1, 2009, funding for the San Diego Regional Parks Fund is derived based on allocations included in the City Charter that require 25 percent or \$2.5 million, whichever is greater, of all lease revenues collected from Mission Bay Park rents and concessions in excess of \$23 million be allocated to the San Diego Regional Parks Improvement Fund to solely benefit the Regional Parks.⁴

Funds in the San Diego Regional Parks Improvement Fund may be expended only for non-commercial public capital improvements for the Regional Parks and only for park uses. Funds in the San Diego Regional Parks Improvement Fund may not be expended for any of the following:

- commercial enterprises or improvements of leasehold interests;
- any costs associated with utilities, including, but not limited to, water and sewage;
- roads, vehicle bridges, or vehicular ramps; and
- daily, weekly, monthly, or annual upkeep of the Regional Parks.

**Mission Bay Park
Improvement Fund**

The Mission Bay Park Improvement Fund is a separate interest-bearing monetary fund maintained by the City to receive and spend Mission Bay Park lease revenues as identified above for the benefit of the Improvement Zone.

⁴ San Diego City Charter, Article V, Section 55.2(b).

Like the San Diego Regional Parks Improvement Fund, funding is also derived based on allocations included in the City Charter effective July 1, 2009.⁵ The City Charter requires that 75 percent of all Mission Bay lease revenues in excess of \$23 million be allocated to the Mission Bay Park Improvement Fund. However, if less than 75 percent is available, any revenue in excess of SDRPF's allocation of 25 percent or \$2.5 million shall be allocated to the Mission Bay Park Improvement Fund. For example, for MBIF to receive any allocation, the City would need to collect over \$25.5 million in net lease revenue (\$23 million threshold and \$2.5 million SDRPF allocation).

Funds in the Mission Bay Park Improvement Fund may be expended only in the Improvement Zone with the following goals:

- restore wetlands, wildlife habitat, and other environmental assets within the Improvement Zone;
- preserve the beneficial uses of the Improvement Zone including, but not limited to, water quality, boating, swimming, fishing, and picnicking by maintaining navigable waters and eliminating navigational hazards;
- restore embankments and other erosion control features; and
- improve the conditions of the Improvement Zone for the benefit and enjoyment of residents and visitors, consistent with the Master Plan.

To achieve these goals, the City Charter identifies improvement priorities intended to be authorized, funded, and completed in the order provided.⁶ Once those priority projects have been fully budgeted or completed, additional projects can be prioritized and funded only for capital improvements as identified in the Master Plan, recommended by the Mission Bay Park Improvement Fund Oversight Committee, and approved by the City Council.

⁵ San Diego City Charter, Article V, Section 55.2(b).

⁶ San Diego City Charter, Article V, Section 55.2(c)(1) as approved by the voters.

Aside from the above, funds in the Mission Bay Park Improvement Fund may not be expended for commercial enterprises or improvements of leasehold interests; for any costs associated with utilities, including, but not limited to, water and sewage; or for roads, vehicle bridges, or vehicular ramps; or on costs that cannot be capitalized; or on daily, weekly, monthly, or annual upkeep of the Improvement Zone. Also, there shall be no expenditure for contracted labor or services or for City employee salaries, pensions or benefits unless those expenses can be capitalized, and only then at the then-standard rates used by the City for all other capital improvement projects.

The Improvement Funds' Budgets Have Decreased in Recent Periods

Per the adopted budgets for fiscal years 2010 through 2012, the funds have no budgeted employees or departmental expenses. Total revenue for the two funds combined has significantly decreased from approximately \$5,036,208 in fiscal year 2010 to \$2,281,433 in fiscal year 2012.

Exhibit 1 below provides the detailed budgeted revenue for each improvement fund between fiscal year 2010 and 2012:

Exhibit 1

Overview of Budgeted Revenue for the Mission Bay Park and San Diego Regional Park Improvement Funds for Fiscal Years 2010 through 2012

| Fund Title | FY 2010 | FY 2011 | FY 2012 |
|----------------|---------------------------|---------------------------|---------------------------|
| Mission Bay | \$2,536,208 | \$872,678 | \$0 |
| Regional Parks | <u>\$2,500,000</u> | <u>\$2,500,000</u> | <u>\$2,281,433</u> |
| Total | <u>\$5,036,208</u> | <u>\$3,372,678</u> | <u>\$2,281,433</u> |

Source: OCA generated based on information from the City of San Diego adopted budgets for fiscal years 2010 through 2012.

The City's Contracting for and Administration of Mission Bay Park Leases

The Real Estate Assets Department's (READ) Asset Management Group administers the City's lease portfolio. This includes negotiating, developing and administering lease agreements for use of City-owned property by both profit and non-profit organizations City-wide, including Mission Bay Park. The majority of the lease contracts relate to hotel, campsite, amusement park, fishing and other forms of recreational activities, with a wide range of related percentage rates applied to various forms of revenue.

Improvement Fund Oversight Committees The Mission Bay Park Improvement Fund Oversight Committee and the San Diego Regional Parks Improvement Fund Oversight Committee provide oversight and monitoring of the two respective Mission Bay related improvement funds. According to the City Charter, effective July 1, 2009, these committees are required to meet at least quarterly to do the following:

- audit and review the implementation of the City Charter;
- recommend priorities for expenditures and capital improvements consistent with the master plans for each of the Mission Bay Improvement Zone and the San Diego Regional Parks, with the Master Plan or within the priorities identified in the City Charter, as applicable; and,
- verify that the appropriate funds are collected, segregated, retained and allocated according to the intent of—and spent as prioritized in—the City Charter.

According to their bylaws, to carry out these stated purposes, the committees shall perform the following duties:

- *Inform the Public.* Inform the public concerning the City's expenditure of bond proceeds;
- *Review Expenditures.* Provide oversight, including reviewing specific reports, produced by the City, to ensure that proceeds are expended only for the purposes set forth in the City Charter;
- *Annual Report.* The committees shall present to the Park and Recreation Board, in public session, an annual written report, which shall include the following:
 - a. Complete accounting of all revenues received;
 - b. The amount and nature of all expenditures;
 - c. A report as to whether in the respective committee's view, the expenditures have been consistent with the priorities and provisions of the City Charter.

Objectives, Scope, and Methodology

The City Charter requires that the City Auditor perform an annual audit of the distribution of Mission Bay lease revenues. Specifically, we are required to establish and oversee a mechanism to ensure public accountability by effectively reporting and communicating the extent and nature of revenues, expenses and improvements generated and in compliance with City Charter requirements. This shall include, at a minimum, an annual audit report to the Mayor, City Council and public. Each annual report shall, at a minimum, contain the following: 1) a complete accounting of all revenues received; 2) the amount and nature of all expenditures; and, 3) a report as to whether in each committee's view the expenditures have been consistent and compliant City Charter requirements. This performance audit report is intended to satisfy the first item listed immediately above for fiscal year 2010, since these City Charter provisions went into effect July 1, 2009. However, since no fiscal year 2010 funds have been expended to date, the second and third items above are not currently considered applicable.

The audit's objectives were to verify that fiscal year 2010 collection, allocation, and use of Mission Bay Park lease revenues are in compliance with City Charter requirements. After analyzing financial and oversight information gathered during the audit, we expanded our audit scope to address two risk areas that the City faces:

The accuracy and appropriateness of the amount and nature and proper accounting of all Mission Bay Park lease-related revenues and expenditures.

The Mission Bay Park and San Diego Regional Parks Oversight Committees provide appropriate and timely

oversight of Mission Bay Park lease revenues and expenditures including consistency with the priorities and provisions of the City Charter.

However, since there were no expenditures approved by the Oversight Committee for the revenue collected during fiscal year 2010, and all expenditures were for projects approved prior to fiscal year 2010, the second and third items above are not applicable.

To accomplish our objectives we performed the following audit procedures:

- Reviewed pertinent laws, policies and regulations related to Mission Bay Park lease revenues;
- Gathered and analyzed agreements and information related to Mission Bay Park lease revenues;
- Identified, collected, analyzed financial information including transaction adjustments and management reports related to Mission Bay Park lease revenues;
- Evaluated current Mission Bay Park lease revenues processes and practices;
- Interviewed management and key staff in charge of managing and monitoring information related to Mission Bay Park lease revenues;
- Reviewed Mission Bay Park and San Diego Regional Park Improvement Fund Oversight Committee minutes, agendas and related bylaws; and,
- Analyzed the quality and effectiveness of the reporting related to Mission Bay Park lease revenues.

We reviewed data for fiscal year 2010. We performed data reliability testing of the financial data provided to us and which we relied on in this report.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Audit Results

Finding 1: Fiscal Year 2010 Mission Bay Lease Revenue, Distributions, Adjustments, and Accruals

Mission Bay Lease Revenue

We found that for fiscal year 2010, the adjusted Mission Bay lease revenue totaled \$23,984,104, the distribution to the San Diego Regional Parks Fund was \$984,104, and there was not enough lease revenue for a distribution to the Mission Bay Improvement Fund. However, we also found that the actual amount that should be available to the new Oversight Committee in the San Diego Regional Parks Fund is \$1,623,777. The additional \$639,673 is the result of an overestimated fiscal year 2009 accrual that reduced the 2010 distribution amount. The following sections will cover each of these issues.

Based on our review of City Comptroller records, the Mission Bay Park lease revenue, before adjustments, for fiscal year 2010 was \$24,988,570. For fiscal year 2010, approximately 89 percent of total lease revenues were generated by only seven of the 24 lessees, each with at least \$1 million in annual proceeds to the City. The single largest source was Sea World, with \$11.4 million, or 45 percent, of the total annual lease revenues for that same period. Exhibit 2 below summarizes the total unadjusted revenues by lessee from Mission Bay Park leases for fiscal year 2010.

Exhibit 2**Fiscal Year 2010 Mission Bay Park Unadjusted Lease Revenues, by Lessee**

| Lessee | Revenue Amount | Percentage of the Total Lease Revenue Collected |
|--|-------------------------|---|
| Sea World Inc | \$ 11,362,733.46 | 45.47% |
| Kecall Ownership, Inc | \$ 2,598,081.18 | 10.40% |
| LHO Mission Bay Hotel, L.P. | \$ 2,453,677.60 | 9.82% |
| LHO Mission Bay Rosie Hotel | \$ 1,870,768.92 | 7.49% |
| Campland, LLC | \$ 1,542,989.78 | 6.17% |
| Bartell Hotels | \$ 1,310,243.70 | 5.24% |
| BH Partnership | \$ 1,005,861.00 | 4.03% |
| Seaforth Sportfishing Corporation | \$ 779,003.21 | 3.12% |
| Retirement Fund Trust Of Plumbing | \$ 659,378.33 | 2.64% |
| Driscoll Mission Bay LLC | \$ 352,150.87 | 1.41% |
| Wesco Sales Corp | \$ 319,038.13 | 1.28% |
| Mission Bay Yacht Club | \$ 262,543.92 | 1.05% |
| San Diego Mission Bay Boat & Ski Club | \$ 94,505.16 | 0.38% |
| Bahia Sternwheelers Inc/02 | \$ 77,457.60 | 0.31% |
| SD Visitor Information Center | \$ 76,791.64 | 0.31% |
| Everingham Bros Bait Co | \$ 46,611.31 | 0.19% |
| Gleason, Richard And Debra | \$ 44,008.88 | 0.18% |
| Sportsmen's Seafood Co Inc | \$ 44,000.00 | 0.18% |
| Bahia Sternwheelers Inc/01 | \$ 33,452.34 | 0.13% |
| Braemar Partnership 9th & A LP | \$ 25,029.19 | 0.10% |
| Associated Students SDSU/Regents Of | \$ 14,622.25 | 0.06% |
| San Diego Rowing Club/Intercollegiate Rowing | \$ 11,833.04 | 0.05% |
| Hanohano Outrigger Canoe Club | \$ 3,288.00 | 0.01% |
| Braemar Partnership/02 | \$ 500.04 | 0.00% |
| Grand Total | \$ 24,988,569.55 | 100.00% |

Source: OCA generated based on information from the Office of the City Comptroller

Adjustments and Accruals The City Comptroller's Office adjusts the Mission Bay lease revenue account as needed. Adjustments can occur for different reasons, such as posting or reversing accruals or correcting system errors. At the end of each fiscal year, an accrual is needed to record lease revenue that is collected after the year end which is attributable to the current year. For example, lease payments for June that are paid in July are accrued. This accrual is then reversed the following year so that the payments are not counted twice. Exhibit 3 below provides the type and amount of adjustments made to the fiscal year 2010 Mission Bay lease revenue.

Exhibit 3

Adjustments to Mission Bay Lease Revenue

| | |
|---------------------------------------|---------------|
| Beginning Balance as of June 30, 2010 | \$24,988,570 |
| FY 09 Year End Accrual Reversal | (\$3,449,831) |
| Accounts Receivable Revenue Reversals | \$4,000 |
| FY 10 Year End Accrual | \$2,441,365 |
| Ending Balance for FY 10 Per SAP | \$23,984,104 |

Source: OCA generated based on SAP data and Comptroller’s supporting documentation

Funds Allocation in Excess of The Threshold Amount

According to the Office of the City Comptroller (City Comptroller) records, the Mission Bay lease revenue collected for fiscal year 2010, after adjustments, totaled \$23,984,104. In accordance with the City Charter, any revenue in excess of the \$23 million threshold is distributed to the San Diego Regional Parks Fund and the Mission Bay Improvement Fund using a predetermined formula. As a result, the San Diego Regional Parks Fund received a distribution in fiscal year 2010 totaling \$984,104; however, there was not enough lease revenue to distribute any monies to the Mission Bay Improvement Fund. The allocations for San Diego Regional Parks Fund and the Mission Bay Improvement Fund are displayed in Exhibit 4 below:

Exhibit 4

Mission Bay Lease Revenue Allocation to Funds

| Fund Name | Allocation Breakdown in excess of the threshold | FY 2010 Allocation Amounts |
|-----------------------------------|---|----------------------------|
| San Diego Regional Parks Fund | 25% or \$2.5 million, whichever is greater, in excess of the \$23 million threshold | \$984,104 |
| Mission Bay Park Improvement Fund | 75% of the excess over the \$23 million threshold, if less than the 75% then, the remainder after the San Diego Regional Parks allocation | \$0 |

Source: San Diego City Charter, Article V, Section 55.2(b)

Since the amount in excess of the \$23 million threshold was less than \$2.5 million, San Diego Regional Parks Fund received all excess funds, which totaled \$984,104 with no funds available for transfer to the Mission Bay Park Fund. However, the actual amount that should be available to the new Oversight Committee in the San Diego Regional Parks Fund is \$1,623,777.

Funds Totaling \$1,623,777 Should Be Available to The New Oversight Committee

As reported, we found that after adjustments, for the City collected \$23,984,104 in Mission Bay lease revenue for fiscal year 2010, and distributed \$984,104 to the San Diego Regional Parks Fund. However, the actual amount that that should have been distributed and available to the new Oversight Committee is \$1,623,777. The additional \$639,673 is the result of an overestimated fiscal year 2009 accrual that reduced the 2010 distribution amount.

The \$639,673 overestimated accrual overstated the fiscal year 2009 distribution of \$1,987,013 (pre-charter change), and understated the fiscal year 2010 distribution by this amount. Exhibit 5 below reflects the corrected distribution amounts for fiscal year 2009 and 2010 for the San Diego Regional Parks Fund. We also verified that the fiscal year 2010 year end accrual was accurate.

Exhibit 5

San Diego Regional Parks Fund Distribution for Fiscal Years 2009 and 2010

| Distributions | FY 2009 | FY 2010 |
|--|--------------|--------------|
| Actual Distribution Amounts to San Diego Regional Parks Fund | \$ 1,987,013 | \$ 984,104 |
| Over Distributed to Fund | (639,673) | |
| Under Distributed to Fund | | 639,673 |
| Corrected Distribution Amount to San Diego Regional Parks Fund | \$ 1,347,340 | \$ 1,623,777 |

Source: OCA generated based on information from the City of San Diego SAP system

There were no fiscal year 2010 expenditures approved by the new Oversight Committees established by the City Charter. All the expenditures related to San Diego Regional Parks Fund or Mission Bay Improvement Fund were for projects approved prior to the beginning of fiscal year 2010.

Although the new Oversight Committee should have \$1,623,777 available in the San Diego Regional Parks Fund for projects, this Fund has overcommitted projects totaling (\$2,080,923) as of June 30, 2010, due to prior years' activities and inaccurate budgeting estimates, which is addressed in Finding #2.

Finding 2: Due to Inaccurate Budgeting Estimates, Both Funds Have Overcommitted Projects in Excess of (\$2) Million

We found that the San Diego Regional Parks and Mission Bay Improvement Funds both have overcommitted projects totaling over (\$2) million due primarily to prior years' inaccurate budgeting estimates. We also, found that a method has not yet been established to separately account for the financial activities after the City Charter change.

As of June 30, 2010 the San Diego Regional Parks Fund and Mission Bay Improvement Fund have overcommitted projects totaling (\$2,080,923) and (\$2,420,604) respectively. This means that the approved budgeted expenditures for projects exceed the current funds available. The amount of funds overcommitted for projects is due primarily to inaccurate revenue budgeting estimates in prior years. The budgeted revenue for the Mission Bay Improvement Fund and San Diego Regional Parks Fund (SDRPF) are based on Real Estate Asset Department's calculated revenue amounts rather than actual distributions. As a result, the Mission Bay Improvement Fund and the San Diego Regional Parks Fund are both overcommitted on projects because the distributions received were less than anticipated.

For example, as shown in Exhibit 6 below, the Mission Bay Improvement Fund and San Diego Regional Parks Fund each had revenue allocations (pre charter change) that were lower than the budgeted amounts by \$(586,770) and \$(479,789) in fiscal years 2008 and 2009 for a cumulative total of \$(1,066,559) for each fund respectively.

Exhibit 6**Fiscal Year 2008 and 2009 Budgeted to Actual Revenues Received For Mission Bay Improvement Fund and San Diego Regional Parks Fund**

| Mission Bay Improvement Fund | | | San Diego Regional Parks Fund | | | |
|--------------------------------|--------------------|--------------------|-------------------------------|--------------------|--------------------|----------------------|
| | FY 2008 | FY 2009 | Total | FY 2008 | FY 2009 | Total |
| Actual Revenue Transfer Amount | \$1,913,230 | \$1,987,013 | \$3,900,243 | \$1,913,230 | \$1,987,013 | \$3,900,243 |
| Budgeted Amount | \$2,500,000 | \$2,466,802 | \$4,966,802 | \$2,500,000 | \$2,466,802 | \$4,966,802 |
| Difference (Deficit) | \$(586,770) | \$(479,789) | \$(1,066,559) | \$(586,770) | \$(479,789) | \$(1,066,559) |

Source: OCA Generated based on City of San Diego Adopted Budgets and Simpler Financial Reports for fiscal years 2008 and 2009

Departments responsible for oversight of the projects stated the over estimated revenue provides a false picture of available funding. City staff that work on the projects see the budget amounts in the City's financial system and believe the funds are available to spend, but in actuality, they are just numbers that are not supported by actual dollars.

City Officials advised that new post charter budgeting practices for San Diego Regional Parks and Mission Bay Improvement Funds will eliminate the risk of over-committing budgeted expenditures in the future. The budgeted expenditures will be based on prior year's actual distributions and not on estimated revenue as in past years. This new budgeting practice will provide "real" dollars available for projects. Although this budgeting practice was discussed at both Oversight Committee meetings, it should be documented in the policies and procedures for these funds to ensure it is followed in the future.

City Officials advised the funds will remain overcommitted until the Financial Management Department releases the unfunded or abandoned projects. As the overcommitted funding issues are being resolved, the City Comptroller should establish a methodology to separately account for the \$1,623,777 that should be allocated to the San Diego Regional Parks as required by the City Charter, as described in Finding #1.

If any of the de-appropriated unfunded or abandoned projects are going to be funded with post-charter dollars, FM, Development Services Facilities Financing Division, and the Park and Recreation Department should include the appropriate Oversight Committee to ensure proper approval and full disclosure.

An accounting mechanism within the City's financial system SAP has not yet been established by the City Comptroller to separately track the actives subsequent to the City Charter change. All the financial activities that occurred before and after the City Charter change should be accounted for separately to ensure all City Charter requirements for these monies are met. This could be accomplished by accounting for these transactions as separate cost unit within the Funds.

Recommendation #1

In conjunction with the Park and Recreation Department and Development Services Facilities Financing Division, the Financial Management Department should continue to de-appropriate the unfunded and abandoned projects in the Mission Bay Improvement Fund and San Diego Regional Parks Fund to eliminate the negative balances. The appropriate Oversight Committee should approve any projects using funding received subsequent to fiscal year 2010. (Priority 2)

Recommendation #2

The City Comptroller should establish a methodology to separately account for the financial transactions within the Mission Bay Improvement Fund and San Diego Regional Parks Fund that are required by the City Charter effective July 1, 2009. (Priority 2)

Finding 3: The City Lacks Documented Financial Internal Controls Specific to the Mission Bay Revenue Fund

According to City Comptroller records, the Mission Bay Park lease revenues for fiscal year 2010 were \$24,988,570 before adjustments. During our review, we found that the City Comptroller does not have documented policies and procedures for the Mission Bay Park lease revenues. The City Comptroller's written policies and procedures are contained in existing process narrative procedures and process flow diagrams which are broad in nature for the department as a whole and not specific to these unique transactions. City Comptroller, Real Estate Assets Department (READ), Office of the City Treasurer, and Financial Management Department (FM) staff could benefit from comprehensive policies and procedures related to the lease revenues due to their statutory requirements and inherent complexities.

In conjunction with the aforementioned lack of policies and procedures, we noted that there are no formalized and documented procedures to reconcile the amounts recorded by the Real Estate Assets Department (in REportfolio) and those accounted for by the City Comptroller (in SAP). As a result, we noted differences of approximately \$257,000 between the amounts reported by the respective departments as shown below in Exhibit 7.

Exhibit 7**Mission Bay Lease Revenue Recorded by The City Comptroller and READ**

| LESSEE | COMPTROLLER TOTALS | READ RePORTFOLIO TOTALS | DIFFERENCES |
|---|------------------------|-------------------------------|----------------------|
| SEA WORLD INC | \$ 11,362,733.46 | \$ 11,362,733.46 | \$ - |
| KECALL OWNERSHIP, INC | 2,598,081.18 | 2,426,308.63 | 171,772.55 |
| LHO MISSION BAY HOTEL, L.P. | 2,453,677.60 | 2,453,677.90 | (0.30) |
| LHO MISSION BAY ROSIE HOTEL | 1,870,768.92 | 1,870,768.92 | 0.00 |
| CAMPLAND, LLC | 1,542,989.78 | 1,542,989.78 | 0.00 |
| BARTELL HOTELS | 1,005,861.00 | 1,005,861.00 | 0.00 |
| BH PARTNERSHIP | 1,310,243.70 | 1,310,243.70 | 0.00 |
| SEAFORTH SPORTFISHING CORPORATION | 779,003.21 | 728,198.13 | 50,805.08 |
| RETIREMENT FUND TRUST OF PLUMBING | 659,378.33 | 659,378.33 | 0.00 |
| DRISCOLL MISSION BAY LLC | 352,150.87 | 352,150.87 | 0.00 |
| WESCO SALES CORP | 319,038.13 | 293,637.23 | 25,400.90 |
| MISSION BAY YACHT CLUB | 262,543.92 | 262,543.92 | 0.00 |
| SAN DIEGO MISSION BAY BOAT & SKI CLUB | 94,505.16 | 94,505.16 | 0.00 |
| BAHIA STERNWHEELERS INC/02 | 77,457.60 | 77,457.60 | 0.00 |
| SD VISITOR INFORMATION CENTER | 76,791.64 | 70,551.92 | 6,239.72 |
| SPORTSMEN'S SEAFOOD CO INC | 46,611.31 | 39,432.17 | 7,179.14 |
| GLEASON, RICHARD AND DEBRA | 44,008.88 | 44,008.88 | 0.00 |
| EVERINGHAM BROS BAIT CO | 44,000.00 | 48,000.00 | (4,000.00) |
| BAHIA STERNWHEELERS INC/01 | 33,452.34 | 33,452.34 | 0.00 |
| BRAEMAR PARTNERSHIP 9th & A LP | 25,029.19 | 25,029.19 | 0.00 |
| ASSOCIATED STUDENTS SDSU/REGENTS OF | 14,622.25 | 14,622.25 | 0.00 |
| SAN DIEGO ROWING CLUB/INTERCOLLEGIATE ROWING | 11,833.04 | 11,833.04 | 0.00 |
| HANOHANO OUTRIGGER CANOE CLUB | 3,288.00 | 3,288.00 | 0.00 |
| BRAEMAR PARTNERSHIP/02 | 500.04 | 500.04 | 0.00 |
| Grand Total | \$24,988,569.55 | \$ 24,731,172.46 | \$ 257,397.09 |

Source: OCA generated based on information from the Office of the City Comptroller and Real Estate Assets Department for fiscal year 2010.

At our request, City Comptroller staff reconciled the difference and determined a majority of the differences were attributed to payments totaling \$261,397 received and recorded in SAP in July 2009. However, these payments were not recorded in REportfolio. The Comptroller should establish policies and procedures to review and reconcile any differences between REportfolio and SAP to verify revenue is properly recorded.

We also found that the accrual methodology used by the City Comptroller at the end of the fiscal year is not clearly documented or well communicated to READ. Prior to fiscal year 2010, the City Comptroller's Office used estimates to accrue Mission Bay lease revenue that was due toward the end of the fiscal year, but not collect until the following fiscal year.⁷ As discussed in Finding #1, in fiscal year 2009 (pre-charter), the accruals were overestimated, and as a result, the fiscal year 2010 (post charter) accrual reversal reduced the post charter allocation by \$639,673. For the fiscal year 2010, the accrual was accurate because it was based on an analysis of actual lease payments collected after the year end rather than an estimate. Neither of these methodologies are formally documented.

To ensure the accuracy of the Mission Bay revenue recorded, the City Comptroller should base year end accruals on an analysis of actual payment received after year end instead of estimating the amounts. This methodology should be documented in written policies and procedures that will be used for future year end accruals related to the Mission Bay lease revenue.

According to the Government Finance Officers Association (GFOA), an essential component of internal control is the design, implementation, and maintenance of specific, control-related policies and procedures. In addition, a key element of a comprehensive framework of internal control is the effective and efficient communication of information through a

⁷ The City used a modified accrual basis of accounting for revenue recognition Modified accrual accounting standards are established by the Government Accounting Standards Board (GASB), the official source of generally accepted accounting principles (GAAP) for state and local governments Modified accrual accounting combines accrual-basis accounting with cash-basis accounting, for this reason modified accrual accounting recognizes revenues when they become available and measurable. Mission Bay Lease Revenue historical data was used in determining the estimated amounts.

comprehensive formal documentation of policies and procedures that encompasses the accounting and internal controls of the organization. Finally, according to the GFOA, management is responsible to monitor and update policies and procedures to ensure that they continue to function properly.

Management must also verify that policies and procedures have, in fact, been created and updated and that they address new or recent changes. Without a comprehensive set of policies and procedures related to the Mission Bay lease revenues, there is no certainty that City staff understand or adhere to the policies and procedures. This increases the risk that monies may be improperly recorded or expended.

City Comptroller staff informed us that the lack of policies and procedures for the administration and management of lease revenues is due in part to the relatively recent implementation of the City Charter requirements effective July 1, 2009.

To develop, formalize, and implement standardized lease revenues processes, we recommend:

Recommendation #3

The City Comptroller should establish comprehensive process narrative procedures, process flow diagrams and departmental guidance to properly document the processes specific to the unique nature of Mission Bay Park lease revenues. These procedures should include but are not limited to:

- **How the requirements outlined in the City Charter will be administered**
- **Procedures to reconcile SAP and REportfolio records**
- **The methodology used for year-end accruals, which should be based on an analysis of actual payment received after year end**
- **The methodology used for budgeting revenue**
- **The methodology used by the Oversight Committees for budgeting specific projects based on prior year's distributions (Priority 2)**

Conclusion

The management of the City's Mission Bay Park lease revenues is an ongoing activity which impacts the revenue proceeds from businesses and other organizations located in Mission Bay Park. As a result, these funds should receive ongoing oversight from City management to ensure the effective and efficient use of these accounts.

The Mission Bay lease revenue collected for fiscal year 2010, after adjustments, totaled \$23,984,104. The City Charter requires any revenue in excess of \$23 million be allocated among the San Diego Regional Parks and Mission Bay Improvement Funds. As a result, the San Diego Regional Parks Fund received a distribution totaling \$984,104, and there was not enough lease revenue to distribute any monies to the Mission Bay Improvement Fund. Additionally, there were no fiscal year 2010 expenditures approved by the new Oversight Committees established by the City Charter.

Although the San Diego Regional Parks Fund only received a distribution of \$984,104 in fiscal year 2010, the actual amount that should be available to the new Oversight Committee is \$1,623,777. The \$639,673 difference is from an overestimated prior year accrual that reduced the fiscal year 2010 distribution amount.

While the new Oversight Committee should have \$1,623,777 available in the San Diego Regional Parks Fund for projects, in actuality, this Fund has overcommitted projects totaling (\$2,080,923), and the Mission Bay Improvement Fund has overcommitted projects totaling (\$2,420,604) as of June 30, 2010.

City Officials advised the Funds would remain overcommitted until Financial Management releases the unfunded or abandoned projects. As the overcommitted funding issues are being resolved, we found that the City Comptroller should establish a methodology to separately account for the \$1,623,777 that should be allocated to the San Diego Regional Parks as required by the City Charter.

The Office of the City Comptroller does not have documented policies and procedures for the Mission Bay lease revenues, and the existing procedures and process flow diagrams that are broad in nature for the department as a whole and not specific to these unique transactions.

By implementing comprehensive policies and procedures for administering the Mission Bay Park lease revenue in accordance with City Charter requirements, the City could improve its oversight in managing the funds. Making improvements will require collaboration and effort between the Office of the City Comptroller, Real Estate Assets Department, the Office of the City Treasurer, Development Services Department's Facilities Financing and Financial Management.

Recommendations

To ensure the accuracy, completeness and appropriateness of Mission revenues and expenses, we recommend that the City take the following actions:

- Recommendation #1** In conjunction with the Park and Recreation Department and Development Services Facilities Financing Division, the Financial Management Department should continue to de-appropriate the unfunded and abandoned projects in the Mission Bay Improvement Fund and San Diego Regional Parks Fund to eliminate the negative balances. The appropriate Oversight Committee should approve any projects using funding received subsequent to fiscal year 2010. (Priority 2)
- Recommendation #2** The City Comptroller should establish a methodology to separately account for the financial transactions within the Mission Bay Improvement Fund and San Diego Regional Parks Fund that are required by the City Charter effective July 1, 2009. (Priority 2)
- Recommendation #3** The City Comptroller should establish comprehensive process narrative procedures, process flow diagrams and departmental guidance to properly document the processes specific to the unique nature of Mission Bay Park lease revenues. These procedures should include but are not limited to:
- How the requirements outlined in the City Charter will be administered
 - Procedures to reconcile SAP and REportfolio records.
 - The methodology used for year-end accruals, which should be based on an analysis of actual payment received after year end
 - The methodology used for budgeting revenue
 - The methodology used by the Oversight Committees for budgeting specific projects based on prior year's distributions (Priority 2)

Appendix A: Definition of Audit Recommendation Priorities

DEFINITIONS OF PRIORITY 1, 2, AND 3 AUDIT RECOMMENDATIONS

The Office of the City Auditor maintains a classification scheme applicable to audit recommendations and the appropriate corrective actions as follows:

| Priority Class ⁸ | Description ⁹ | Implementation Action ¹⁰ |
|-----------------------------|--|-------------------------------------|
| 1 | Fraud or serious violations are being committed, significant fiscal or equivalent non-fiscal losses are occurring. | Immediate |
| 2 | A potential for incurring significant or equivalent fiscal and/or non-fiscal losses exist. | Six months |
| 3 | Operation or administrative process will be improved. | Six months to one year |

⁸ The City Auditor is responsible for assigning audit recommendation priority class numbers. A recommendation which clearly fits the description for more than one priority class shall be assigned the higher number.

⁹ For an audit recommendation to be considered related to a significant fiscal loss, it will usually be necessary for an actual loss of \$50,000 or more to be involved or for a potential loss (including unrealized revenue increases) of \$100,000 to be involved. Equivalent non-fiscal losses would include, but not be limited to, omission or commission of acts by or on behalf of the City which would be likely to expose the City to adverse criticism in the eyes of its residents.

¹⁰ The implementation time frame indicated for each priority class is intended as a guideline for establishing implementation target dates. While prioritizing recommendations is the responsibility of the City Auditor, determining implementation dates is the responsibility of the City Administration.

Appendix B: Map of Mission Bay Park, Including Permit Sites

