

# **Attachment C**

Audit Report Dated March 2, 2020

**INDEPENDENT ACCOUNTANT'S REPORT  
ON APPLYING AGREED-UPON PROCEDURES**

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City of Newport Beach  
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We have performed the procedures enumerated below, which were agreed to by the City of Newport Beach ("City"), solely to assist the City in reviewing American Legion Newport Harbor Post 291's ("Lessee") compliance with the American Legion Newport Harbor Post 291 Lease Agreement ("Lease") dated December 6, 2002, for the period January 1, 2016 through December 31, 2018. The Lessee's management is responsible for maintaining their accounting records and other documentation to support the information reported on the Lease Payment Analysis ("Annual Statements"). The sufficiency of these procedures is solely the responsibility of the management of the City. Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purpose for which the report has been requested or for any other purpose.

The procedures were performed, and the results of those procedures are as follows:

1. We obtained an understanding of the internal controls over collection and recording of Lessee revenues, including the specific system reports used to generate reporting to the City. We evaluated adjustments made, if any, to the system reports when reporting the information to the City.

We compared Gross Sales information reported to the City to Gross Sales information reported quarterly to the State of California, Board of Equalization.

**Results:**

The Lessee uses QuickBooks software to record all accounting transactions. The Lessee performs monthly bank reconciliations to ensure the accuracy of revenues recorded in the accounting system. The Lessee records revenue in defined revenue accounts (marina rentals, marina waitlist, dry storage, hall rentals, banquet sales, alcohol sales). The Lessee pays monthly Base Rent, and on an annual basis, the Lessee uses revenue reports to calculate additional Percentage Rent due to the City, if any.

No exceptions were noted as a result of our procedures.

2. We reviewed the date payments were remitted to the City for the period January 1, 2016 through December 31, 2018 to determine if they were submitted within the due date specified by the Lease.

**Results:**

No exceptions were noted as a result of our procedures.

- We traced information from the monthly reports provided to the City to the Lessee's reports supporting the amounts reported. We reconciled the information in these reports to the accounting system reports showing all revenues collected by the Lessee.

**Results:**

We noted three exceptions, summarized as follows, further elaborated below and detailed in Attachment A:

<u>Exception</u>	<u>Period</u>	<u>Net Effect On Percentage Rent</u>
Under-paid Base Rent	January-March 2018	\$ -
Overstated Base Rent	March 2018	1,039
Under-paid Percentage Rent	2016-2018	222,757
	<b>Total</b>	<u>\$ 223,796</u>

**Under-paid Base Rent**

In accordance with the Lease, section 4.1(b), Base Rent increases after the end of every fifth Lease Year and the increase shall be effective and paid to the City as of the first Rent Due Date after the calculation of the Periodic Adjustment goes into effect. Based on the initial Rent Commencement Date we noted the Lease Year runs on a calendar year basis. There was a rent increase that went into effect on January 1, 2018. We reviewed the City's calculation of the Periodic Adjustment to Base Rent and noted the calculation appeared to be performed in accordance with the Lease.

We noted the Lessee did not start paying the new Base Rent rate until April 2018. Per inquiry, the Lessee indicated they do not start paying the new Base Rent rate until the City informs them of the new monthly rate. The City informed the Lessee in March 2018. No retroactive payments were made by the Lessee. This is a timing issue; the Base Rent shortage was ultimately reconciled in the Lease Year true-up prepared by the Lessee. However, the short-paid amounts of \$1,038.79 per month for January through March 2018 would be subject to 5% late fee and 10% per annum interest totaling \$156 and \$300, respectively.

**Overstated Base Rent**

For March 2018, the Lessee reported paying \$11,426.67 for Base Rent on the Annual Statement but they actually paid \$10,387.88. This resulted in a Percentage Rent underpayment of \$1,038.79 in the Lease Year-end calculation for 2018.

**Under-paid Percentage Rent**

In accordance with Lease sections 1.2 and 4.2(a), the Lessee was required to include in their Percentage Rent calculations all Gross Sales from Hall Rental Revenues, Marina Revenues, Storage Revenues and Parking Lot. For Hall Rental Revenues, the Lessee only included the hall rental fee and improperly excluded banquet food revenue, banquet alcohol revenue and other banquet rental revenue. Further, for Marina Revenues, the Lessee only included marina slip rental revenues and improperly excluded marina waitlist revenue. See procedure 5 and Attachment A for additional details.

**Recommendations:**

For the next fifth year Base Rent increase, effective January 1, 2023, we recommend the City require the Lessee to pay the new Base Rent rate retroactive to the beginning of the 2023 Lease Year.

We recommend the City collect the under-paid Percentage Rent of \$1,038.79 from the Lessee for Lease Year 2018 which resulted from overstated total payments made by the Lessee. Going forward, we recommend the City compare all Base Rent payments

actually received from the Lessee to Base Rent payments reported by the Lessee on the Annual Statement to ensure the Lessee’s worksheet is properly stated.

We recommend the City evaluate the Lessee’s under-reporting of revenue and under-payment of Percentage Rent and consider collecting Percentage Rent underpayments, as further described in procedure 5.

We noted the Annual Statements provided by the Lessee to the City do not include “reasonable detail” in that they do not show the actual Gross Sales Revenue by category, they only show calculated Percentage Rent by category. In accordance with Lease section 4.2(c) “Annual Statement/Payment of Percentage Rent,” the Lessee shall within sixty days following the end of each Lease Year provide the City with a statement, in reasonable detail, of the amount of the Lessee’s Gross Sales Revenue for each Revenue Category. The Statement shall also calculate the Percentage Rent due based on Gross Sales Revenue in each category multiplied by the corresponding Percentage Rent Rates prescribed by the Lease. We recommend the City require the Lessee to provide Annual Statements showing the full calculation of Percentage Rent, including Gross Sales for each month for each revenue category.

4. We tested the monthly reports for mathematical accuracy and proper calculation of amounts owed to the City.

**Results:**

No exceptions were noted as a result of our procedures.

5. We evaluated the reasonableness of revenues considered exempt from taxable revenue reported to the City.

**Results:**

In accordance with Lease sections 1.2 and 4.2(a), the Lessee was required to include in their Percentage Rent calculations all Gross Sales from Hall Rental Revenues, Marina Revenues, Storage Revenues and Parking Lot. However, per review of the Lessee’s accounting reports and inquiry of Lessee, for Hall Rental Revenues, the Lessee only included the hall rental fee and improperly excluded banquet food revenue, banquet alcohol revenue and other banquet rental revenue. Further, for Marina Revenues, the Lessee only included marina slip rental revenues and improperly excluded marina waitlist revenue.

The following is a recap, by revenue category, of under-reported revenue which resulted in under-paid Percentage Rent for all years in the review period:

	<b>Revenue by Category</b>				
	<b>Hall Rental</b>	<b>Marina</b>	<b>Storage</b>	<b>Parking Lot</b>	<b>Total</b>
<b>2016</b>					
Revenue per Auditor	\$ 505,910	253,992	29,880	-	789,782
Revenue per Lessee	119,714	251,693	29,730	-	401,137
Total Revenue Difference	386,196	2,299	150	-	388,645
Percentage Rent Difference	77,239	920	75	-	78,234
<b>2017</b>					
Revenue per Auditor	533,071	249,986	30,243	-	813,300
Revenue per Lessee	148,395	246,936	29,943	-	425,274
Total Revenue Difference	384,676	3,050	300	-	388,026
Percentage Rent Difference	76,935	1,220	150	-	78,305

**Revenue by Category**

	<u>Hall Rental</u>	<u>Marina</u>	<u>Storage</u>	<u>Parking Lot</u>	<u>Total</u>
<b><u>2018</u></b>					
Revenue per Auditor	457,767	248,457	30,421	-	736,645
Revenue per Lessee	<u>134,228</u>	<u>244,682</u>	<u>30,421</u>	-	<u>409,331</u>
Total Revenue Difference	<u>323,540</u>	<u>3,775</u>	-	-	<u>327,315</u>
Percentage Rent Difference	<u>64,708</u>	<u>1,510</u>	-	-	<u>66,218</u>
Total Percentage Rent Difference, by category	<u>\$ 218,882</u>	<u>3,650</u>	<u>225</u>	-	<u>222,757</u>
Base Rent payment overstated (March 2018)					<u>1,039</u>
Total Lessee Underpayment, before late fees and interest					<u>\$ 223,796</u>

5% late fees and 10% per annum interest on unpaid balances, pertaining to the Lessee under-reporting revenue and under-paying Percentage Rent amounts, could be charged by the City. Following is a recap of such fees, where interest is calculated per annum through February 29, 2020:

	<u>2016</u>	<u>2017</u>	<u>2018</u>	<u>Total</u>
Late fees	\$ 3,912	3,915	3,311	11,138
Interest	<u>27,327</u>	<u>17,390</u>	<u>7,048</u>	<u>51,765</u>
Total	<u>\$ 31,239</u>	<u>21,305</u>	<u>10,359</u>	<u>62,903</u>

**Recommendations:**

We recommend the Lessee report all subject revenues, by category, in accordance with the Lease, and calculate Percentage Rent on all-inclusive Gross Revenue figures. Lessee should include all revenues from Hall Rental including banquet food, banquet alcohol, and other banquet rental items. Further, Marina Revenue should include marina waitlist revenue received by the Lessee. We further recommend the City consider collecting under-paid Percentage Rent of \$223,796 for January 1, 2016 through December 31, 2018. The City may further consider assessing late fees and interest totaling \$62,903 for the unpaid amounts.

6. We reconciled the monthly revenue reports to a sample of daily reports / support.

**Results:**

No exceptions were noted as a result of our procedures.

7. We selected a sample of daily reports/support and traced amounts to individual receipts supporting the daily report.

**Results:**

No exceptions were noted as a result of our procedures.

8. For any credits or exemptions allowed by the Lease, we verified documentation supporting the exemption.

**Results:**

No exceptions were noted as a result of our procedures.

The agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. We were not engaged to, and did not, conduct an examination or review, the objective of which would be the expression of an opinion or conclusion, respectively, on the Summary Annual Rental Reports. Accordingly, we do not express such an opinion or conclusion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the information and use of management of the City of Newport Beach and is not intended to be, and should not be, used by anyone other than those specified parties.



Irvine, California  
March 2, 2020

American Legion Newport Harbor Post 291  
 Monthly Activity - Auditor Recalculation  
 2016 - 2018

Schedule A

	2016				2017				2018				Total			
	Hall Rental Gross Revenue	Marina Gross Revenue	Storage Gross Revenue	Total	Hall Rental Gross Revenue	Marina Gross Revenue	Storage Gross Revenue	Total	Hall Rental Gross Revenue	Marina Gross Revenue	Storage Gross Revenue	Total	Hall Rental Gross Revenue	Marina Gross Revenue	Storage Gross Revenue	Total
January	\$ 54,124	22,113	2,028	78,265	38,614	22,584	2,534	63,732	40,692	22,187	2,608	65,487	133,430	66,884	7,170	207,484
February	28,920	20,838	2,137	51,895	49,932	21,484	2,534	73,950	22,742	19,720	2,493	44,955	101,594	62,042	7,164	170,800
March	45,510	20,854	2,137	68,501	54,669	21,159	2,534	78,362	28,304	20,425	2,557	51,286	128,483	62,438	7,228	198,149
April	32,188	21,429	2,687	56,304	26,528	21,109	2,551	50,188	25,432	20,600	2,557	48,589	84,148	63,138	7,795	155,081
May	70,993	20,369	2,687	94,049	52,650	21,162	2,595	76,407	29,406	20,500	2,607	52,513	153,049	62,031	7,889	222,969
June	42,780	20,244	2,687	65,711	46,915	21,262	2,408	70,585	57,609	20,400	2,607	80,616	147,304	61,906	7,702	216,912
July	47,304	21,074	2,687	71,065	36,719	20,511	2,408	59,638	35,843	20,400	2,557	58,800	119,866	61,985	7,652	189,503
August	35,838	21,409	2,626	59,873	53,447	19,746	2,472	75,665	39,574	20,775	2,557	62,906	128,859	61,930	7,655	198,444
September	21,853	21,635	2,551	46,039	35,478	19,986	2,558	58,022	40,789	20,875	2,457	64,121	98,120	62,496	7,566	168,182
October	34,555	21,409	2,551	58,515	51,281	20,548	2,558	74,387	36,376	20,925	2,507	59,808	122,212	62,882	7,616	192,710
November	24,113	21,309	2,551	47,973	31,096	20,548	2,508	54,152	20,070	20,875	2,457	43,402	75,279	62,732	7,516	145,527
December	67,732	21,309	2,551	91,592	55,742	19,887	2,583	78,212	80,930	20,775	2,457	104,162	204,404	61,971	7,591	273,966
Subtotal	\$ 505,910	253,992	29,880	789,782	533,071	249,986	30,243	813,300	457,767	248,457	30,421	736,645	1,496,748	752,435	90,544	2,339,727
Percentage Rent Rate	20%	40%	50%		20%	40%	50%		20%	40%	50%		20%	40%	50%	
Percentage Rent Recalculated by Auditor	\$ 101,182	101,597	14,940	217,719	106,614	99,994	15,122	221,730	91,553	99,383	15,211	206,147	299,350	300,974	45,272	645,596
Total Paid by Lessee				\$ 139,485				143,425				138,890				421,800
Difference - underpaid				78,234				78,305				67,257				223,796
Late Fees and Interest				\$ 31,239				21,305				10,359				62,903