

Internal Audit Department

O R A N G E C O U N T Y
6th Largest County in the USA

Revenue Generating Lease Audit: OC DANA POINT HARBOR/ DANA POINT FUEL DOCK

For the Period
January 1, 2013 through December 31, 2013

**\$2.17M REPORTED GROSS RECEIPTS
FOR TWELVE-MONTH AUDIT PERIOD
\$70,800 RENT PAID TO THE COUNTY**

KDL Services, Inc., a California corporation, dba Dana Point Fuel Dock, operates a full service marine fueling facility at Dana Point Harbor.

We audited the underlying books and records to ensure reported gross receipts are supported and rent is properly paid as defined by the lease agreement. During the twelve-month audit period of January 1, 2013 through December 31, 2013, Dana Point Fuel Dock reported approximately \$2.17M in gross receipts and paid \$70,800 in total rent.

The Internal Audit Department found that Dana Point Fuel Dock's records adequately supported reported gross receipts and rent owed to the County was properly paid. We identified **four (4) Control Findings** related to recordkeeping for fuel throughput service and gift certificates, and reporting gift certificate sales.

AUDIT NO: 1344
REPORT DATE: JULY 21, 2014

Director: Dr. Peter Hughes, MBA, CPA, CIA
Senior Audit Manager: Alan Marcum, CPA, CIA
Audit Manager: Lily Chin, CPA, CGMA

RISK BASED AUDITING

GAO & IIA Peer Review Compliant – 2001, 2004, 2007, 2010, 2013



American Institute of Certified Public Accountants Award to Dr. Peter Hughes as 2010 Outstanding CPA of the Year for Local Government

GRC (Government, Risk & Compliance) Group 2010 Award to IAD as MVP in Risk Management



2009 Association of Certified Fraud Examiners' Hubbard Award to Dr. Peter Hughes for the Most Outstanding Article of the Year – Ethics Pays



2008 Association of Local Government Auditors' Bronze Website Award



2005 Institute of Internal Auditors' Award to IAD for Recognition of Commitment to Professional Excellence, Quality, and Outreach



ORANGE COUNTY BOARD OF SUPERVISORS'
Internal Audit Department

GAO & IIA Peer Review Compliant - 2001, 2004, 2007, 2010, 2013

Providing Facts and Perspectives Countywide

RISK BASED AUDITING

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Director

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OC Fraud Hotline (714) 834-3608



Transmittal Letter



Audit No. 1344 July 21, 2014

TO: Brad Gross, Director
OC Dana Point Harbor

FROM: Dr. Peter Hughes, CPA, Director
Internal Audit Department

SUBJECT: Revenue Generating Lease Audit of
OC Dana Point Harbor/Dana Point Fuel Dock
HA78H-24-1.01

We have completed our revenue generating lease audit of Dana Point Fuel Dock for the period January 1, 2013 through December 31, 2013. We performed this audit in accordance with our *FY 2013-14 Audit Plan and Risk Assessment* approved by the Audit Oversight Committee and the Board of Supervisors. Our final report is attached for your review.

Please note we have a 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). Our **First Follow-Up Audit** will begin at six months from the official release of the report. A copy of all our Follow-Up Audit reports is provided to the BOS as well as to all those individuals indicated on our standard routing distribution list.

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 begin at six months from the release of the first Follow-Up Audit report, by which time **all** audit recommendations are expected to be addressed and 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**. Your department should complete this template as our audit recommendations are implemented. When we perform our first Follow-Up Audit approximately six months from the date of this report, we will need to obtain the completed form to facilitate our review.

Each month I submit an **Audit Status Report** to the BOS where I detail any material and significant audit findings released in reports 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 your staff so that 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 request your department complete a **Customer Survey** of Audit Services. You will receive the survey shortly after the distribution of our final report.

ATTACHMENTS

Other recipients of this report are listed on the **OC Internal Auditor's Report** on page 3.

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OC Dana Point Harbor/Dana Point Fuel Dock
Audit No. 1344*

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OC Internal Auditor's Report



Audit No. 1344

July 21, 2014

TO: Brad Gross, Director
OC Dana Point Harbor

FROM: Dr. Peter Hughes, CPA, Director
Internal Audit Department

SUBJECT: Revenue Generating Lease Audit of
OC Dana Point Harbor/Dana Point Fuel Dock
HA78H-24-1.01

Audit Highlight

KDL Services, Inc. dba Dana Point Fuel Dock operates a full service marine fueling facility at Dana Point Harbor.

During the 12-month audit period from January 1, 2013 to December 31, 2013, Dana Point Fuel Dock generated approximately **\$2.17 million** in gross receipts and paid the County **\$70,800** in rent.

We found that Dana Point Fuel Dock's records adequately supported reported gross receipts and rent paid. We identified **four (4) Control Findings** related to recordkeeping for fuel throughput services and gift certificates and reporting gift certificate sales.

OBJECTIVES

We have performed an audit of certain records and documents for the period from January 1, 2013 through December 31, 2013, pertinent to the lease agreement (Agreement) between the County of Orange (County) and KDL Services, Inc. dba Dana Point Fuel Dock, dated December 8, 1994. The Agreement is for the operation of a marine fueling facility on Parcel 1 at Dana Point Harbor. Our audit objectives were:

1. The primary objective of our audit is to determine whether Dana Point Fuel Dock's records adequately supported their monthly gross receipts reported to the County and rent owed is properly paid.
2. The secondary objective of our audit is to determine whether Dana Point Fuel Dock complies with certain other financial provisions of the Agreement, such as monthly gross receipts statement format and annual financial statement requirements.

In addition, while performing the audit we may identify internal control weaknesses for which we will identify suggestions for improvement.

RESULTS

Objective #1: We found that Dana Point Fuel Dock's records adequately supported gross receipts reported to the County and rent owed was properly paid. We identified **four (4) Control Findings** related to recordkeeping for fuel throughput service and gift certificates and reporting gift certificate sales.

Objective #2: We found that Dana Point Fuel Dock complied with certain other financial provisions of the Lease Agreement such as the monthly gross receipts statement format and annual financial statement requirements.

OC Internal Auditor's Report



The following *Summary of Findings and Recommendations* shows our findings and recommendations for this audit. See further discussion in the *Detailed Findings, Recommendations and Management Responses* section of this report. See *Attachment A* for a description of Report Item Classifications.

Finding No.	Finding Classification - See Attachment A	Finding Description	Recommendation	Agreement by Management?	Page No. in Audit Report
1.	Control Finding	A copy of the record documenting gallons of fuel dispensed to one of the fuel throughput service client was not retained.	DPFD retain the supporting document for recording fuel dispensed for the throughput service.	Yes	4
2.	Control Finding	Agreement for the throughput service is not formally established in writing.	DPFD should establish the fuel throughput service agreement in writing.	Yes	4
3.	Control Finding	The date of sale is used as the Gift Certificate number rather than using a sequential number.	DPFD should use numerical sequence for gift certificate numbers to ensure certificates are accounted for.	Yes	5
4.	Control Finding	Gift Certificate sales are not reported as gross receipts when sold. They are reported when redeemed.	DPFD should report gift certificate sales as gross receipts when sold.	Yes	5

BACKGROUND

The County of Orange (County) entered into a 20-year lease agreement with KDL Services, Inc., a California corporation, dba Dana Point Fuel Dock, dated December 8, 1994, for the operation of a marine fueling facility on Parcel 1 at Dana Point Harbor. Dana Point Fuel Dock sells gasoline and diesel fuel, food, beverages, and sundry items, and provides limited vessel services and throughput services. During the 12-month audit period ending December 31, 2013, Dana Point Fuel Dock generated approximately **\$2.17** million in gross receipts and paid the County **\$70,800** in rent.

SCOPE

Our audit was limited to certain records and documents that support Dana Point Fuel Dock's gross receipts reported to the County for the twelve-month audit period from January 1, 2013 through December 31, 2013. Our audit included inquiry, auditor observation, and limited testing for assessing the adequacy of documentation and ensuring completeness of reported gross receipts.

Acknowledgment

We appreciate the courtesy extended to us by the personnel at Dana Point Fuel Dock, OC Dana Point Harbor, and OC Public Works/Dana Point Accounting Services during our audit. If you have any questions regarding our revenue generating lease audit, please contact me directly at (714) 834-5475, or Alan Marcum, Senior Audit Manager at 834-4119.



Attachments

Distribution Pursuant to Audit Oversight Committee Procedure No. 1:

Members, Board of Supervisors
Members, Audit Oversight Committee
Michael B. Giancola, County Executive Officer
Mark Denny, Chief Operating Officer
Jessica O'Hare, Assistant to the Chief Operating Officer
Lisa Smith, Deputy Director, OC Dana Point Harbor
Paul Lawrence, Operations Manager, OC Dana Point Harbor
Howard Thomas, Section Manager, OCPW/Accounting Services
Anne Tran, Senior Accountant, OCPW Accounting/Dana Point Accounting Services
Foreperson, Grand Jury
Susan Novak, Clerk of the Board of Supervisors
Macias Gini & O'Connell LLP, County External Auditor



Finding 1 – Supporting Documentation Not Retained for Fuel Throughput Service Client (Control Finding)

Clause 14.A of the Agreement requires Dana Point Fuel Dock (DPFD) at all times keep or cause to be kept true and complete books, records, and accounts of all financial transactions in the operation of all business activities. The records must be supported by source documents such as sales slips, cash register tapes, purchase invoices, or other pertinent documents.

Dana Point Fuel Dock provides fuel throughput service to Dana Wharf Sportfishing and Catalina Express by storing and dispensing the fuel purchased by Dana Wharf Sportfishing (Dana Wharf) and Catalina Express (Catalina). DPFDD charges an agreed upon rate per gallon based on the number of gallons dispensed to the vessels. When the fuel is dispensed, DPFDD maintains a record documenting the date, number of gallons, type of fuel, name of vessel, and obtains the captain's signature. A weekly billing statement is issued to Dana Wharf and Catalina for the throughput service.

Finding No. 1: While Dana Point Fuel Dock retains a copy of the supporting document for fuel dispensed to Catalina, a copy of the supporting documents was not retained for Dana Wharf. DPFDD uses a two-part slip for Dana Wharf. One copy is given to the captain and the second copy is retained until the weekly billing statement is issued. Dana Point Fuel Dock gives the second copy along with the weekly billing statement to Dana Wharf to support the amount billed. Since a copy is already given to Dana Wharf when the fuel was dispensed, DPFDD should retain the second copy for its own recordkeeping.

Recommendation No. 1: We recommend OC Dana Point Harbor require DPFDD to retain the fuel throughput tickets for fuel dispensed to Dana Wharf Sportfishing.

OC Dana Point Harbor Management Response: Concur.

OC Dana Point Harbor will provide written direction to the tenant to retain all fuel throughput tickets for fuel dispensed to Dana Wharf Sportfishing and Catalina Express.

Finding 2 – Written Agreement Not Established for Fuel Throughput Service (Control Finding)

Clause 14.A of the Agreement requires DPFDD keep or cause to be kept true and complete books, records and accounts of all financial transactions in the operation of all business activities. Good internal controls require services performed be established in writing to ensure duties are clearly defined.

Dana Point Fuel Dock has a verbal agreement with Dana Wharf and Catalina on the service charge for the fuel throughput service.

Finding No. 2: Dana Point Fuel Dock did not have a written agreement with Dana Wharf and Catalina for the fuel throughput service.

Recommendation No. 2: We recommend OC Dana Point Harbor require DPFDD establish a written agreement for the fuel throughput service to ensure terms and conditions and rates are clearly defined in writing.

OC Dana Point Harbor Management Response: Concur.

The County will provide written direction to the tenant to document this business arrangement between the tenant and Dana Wharf Sport Fishing/Catalina Express.



Finding 3 – Gift Certificates Not Pre-Numbered (Control Finding)

Clause 14.A of the Agreement requires DPF to issue serially numbered tickets and shall keep an adequate record of said tickets, both issued and unissued. Gift certificates should be serially numbered to ensure to ensure completeness of the certificates.

Finding No. 3: During our review of the gift certificate log, we found that Dana Point Fuel Dock uses the date of sale as the certificate number.

Recommendation No. 3: We recommend OC Dana Point Harbor require DPF to use a serially numbered sequence for gift certificate numbers.

OC Dana Point Harbor Management Response: Concur.

OC Dana Point Harbor will provide written direction to the tenant to require tenant to serially number gift certificates.

Finding 4 – Sale of Gift Certificates Reported as Gross Receipts when Redeemed, Rather than when Sold (Control Finding)

Clause 11 of the Agreement requires DPF to include in gross receipts the sale price of all goods, wares, merchandise, and products sold on or from the premise, and all charges made by DPF whether services are actually performed or not.

Finding No. 4: Dana Point Fuel Dock sells gift certificates periodically and reports the gross receipts when they are redeemed, not when sold. DPF informed us that due to different percentage rent categories which the gift certificates can be redeemed for and the low activity volume, reporting gross receipts at redemption is more accurate and more efficient. For the audit period, DPF sold six certificates for a total amount of \$750.

Recommendation No. 4: We recommend OC Dana Point Harbor require DPF report gift certificate sales as gross receipts when sold as required by the lease.

OC Dana Point Harbor Management Response: Concur.

Although OC Dana Point Harbor concurs, we recommend, based on the very low activity of gift certificate sales, allowing DPF to report gift certificate sales as gross receipts when redeemed due to differing percentage rent categories into which the actual sales may be categorized when redeemed (which is not known when gift certificate is purchased).



ATTACHMENT A: Report Item Classifications

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

▶ **Critical Control Weaknesses:**

These are Audit Findings or a combination of Auditing Findings that represent critical exceptions to the audit objective(s) and/or business goals. Such conditions may involve either actual or potential large dollar errors or be of such a nature as to compromise the Department's or County's reputation for integrity. Management is expected to address Critical Control Weaknesses brought to their attention immediately.

▶ **Significant Control Weaknesses:**

These are Audit Findings or a combination of Audit Findings that represent a significant deficiency in the design or operation of internal controls. Significant Control Weaknesses require prompt corrective actions.

▶ **Control Findings:**

These are Audit Findings concerning internal controls, compliance issues, or efficiency/effectiveness issues 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.



ATTACHMENT B: OC Dana Point Harbor Management Response



Brad Gross, Director
24650 Dana Point Harbor Drive
Dana Point, CA 92629
Telephone: (949) 923-2236
Fax: (949) 923-3792

July 14, 2014

Dr. Peter Hughes, CPA, Director
OC Internal Audit Department
12 Civic Center Plaza, Room 232
Santa Ana, CA 92701

Re: Draft Report on Revenue Generating Lease Audit No. 1344 of Dana Point Fuel Dock

Dear Peter:

OC Dana Point Harbor appreciates the support provided by Internal Audit and we concur with the Control Findings and Recommendations (1 through 4) as presented in the attached Draft Report on Revenue Generating Lease Audit of Dana Point Fuel Dock (DPFD), Audit No. 1344.

The Chief Operating Officer has reviewed OC Dana Point Harbor's responses to each recommendation, which responses are intended to ensure DPFD fully complies with all recommendations from the Internal Audit Department. A summary of Internal Audit's recommendations 1 through 4, along with OC Dana Point Harbor's responses, are as follows:

Recommendation No. 1: We recommend that OC Dana Point Harbor requires DPFD to retain the fuel throughput tickets for fuel dispensed to Dana Wharf Sportfishing (and Catalina Express).

OC Dana Point Harbor Response: Concur

OC Dana Point Harbor will provide written direction to the tenant to retain all fuel throughput tickets for fuel dispensed to Dana Wharf Sportfishing and Catalina Express.

Recommendation No. 2: We recommend that OC Dana Point Harbor require DPFD establish written agreement for the fuel throughput service to ensure terms and conditions and rates are clearly defined in writing.

OC Dana Point Harbor Response: Concur

The County will provide written direction to the tenant to document this business arrangement between the tenant and Dana Warf Sport Fishing/Catalina Express.

Recommendation No. 3: We recommend that OC Dana Point Harbor require DPFD use serially numbered sequence for gift certificates numbers.

OC Dana Point Harbor Response: Concur

OC Dana Point Harbor will provide written direction to the tenant to require tenant to serially number gift certificates.



ATTACHMENT B: OC Dana Point Harbor Management Responses (continued)

Recommendation No. 4: We recommend OC Dana Point Harbor require DPFID report gift certificates sales as gross receipts when sold as required by the lease.

OC Dana Point Harbor Response: Concur

Although OC Dana Point Harbor concurs, we recommend, based on the very low activity of gift certificate sales, allowing DPFID to report gift certificate sales as gross receipts when redeemed due to the differing percentage rent categories into which the actual sales may be categorized when redeemed (which is not known when the gift certificate is purchased).

Thank you and should you have any questions, please call me at 949-923-3798.

Sincerely,

Brad Gross
Director, OC Dana Point Harbor

Enclosures: Audit No. 1344
Letter from OC Dana Point Harbor to DPFID dated July 14, 2014

cc: Mark Denny, County of Orange COO
Susan Nestor, Senior Internal Auditor
Lily Chin, Audit Manager, OC Internal Audit Department
Paul Lawrence, Operations Manager, OC Dana Point Harbor