

City of Detroit

OFFICE OF THE AUDITOR GENERAL




**Audit Of
The Recreation Department's
Contracts and Partners Fund**

July 2009 – December 2012

MEMORANDUM

DATE: June 20, 2014

TO: Honorable City Council
Mayor Michael E. Duggan

FROM: Mark W. Lockridge, CPA 
Auditor General

RE: Audit of the Recreation Department's Contracts and Partners Fund

C: Alicia Minter, Director, Recreation Department
Kevyn Orr, Emergency Manager

Attached for your review is our report on the audit of the Recreation Department.

This report contains our audit purpose, scope, objectives, methodology, and conclusions; status of prior audit findings; background; audit findings and recommendations; the Recreation Department responses.

This report contains recommendations to strengthen the Recreation Department's internal control structure over its financial transactions. While the recommendations are not intended to be all-inclusive, the correction of all or any number of conditions as recommended would strengthen the controls in effect. The responsibility for the installation and maintenance of a system of internal control that minimizes errors and provides reasonable safeguards rests entirely with the Recreation Department. Responsibility for monitoring the implementation of recommendations is set forth in Section 7.5-105(4) of the City Charter, which states in part:

Recommendations which are not put into effect by the agency shall be reviewed by the Finance Director, who shall advise the Auditor General and the City Council of action being taken with respect to the recommendations.

We appreciate the cooperation and assistance that we received from the employees of the Recreation Department.

Copies of all of the Auditor General's reports can be found on our website at www.detroitmi.gov/CityCouncil/LegislativeAgencies/AuditorGeneral/tabid/2517/Default.aspx .

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AUDIT PURPOSE, SCOPE, OBJECTIVES, METHODOLOGY, AND CONCLUSIONS

Audit Purpose

The Office of the Auditor General's (OAG) performed the audit of the Recreation Department (Recreation) in accordance with the OAG's Charter mandate to audit the financial transactions, performance and operations of city agencies based on an annual risk-based audit plan prepared by the Auditor General, or as directed by the City Council and make a full report to the City Council of each individual audit and file a copy with the Mayor.

Audit Scope

The OAG performed an assessment of the Recreation's internal controls related to cemeteries, golf courses, and the Partners Fund for the period from July 2009 through December 2012 and determined that there are certain weaknesses in the system of internal controls. We focused our audit on the weaknesses discovered during the assessment and the status of the prior audit findings.

Our audit was conducted in accordance with Government Auditing Standards issued by the Comptroller General of the United States, except for the completion of an external peer review of the Office of the Auditor General within the last three years.

Audit Objectives

The objectives of the audit were:

- Determine if the Recreation is complying with applicable Finance Directives, policies, plans, procedures, laws and regulations regarding the Partners Fund and professional and contractual services; and
- Determine if the Recreation has resolved the prior audit findings.

Audit Methodology

To accomplish the audit objectives, our audit work included:

- Review of prior audit reports, applicable Finance Directives, City ordinances, laws, policies and procedures and other pertinent information related to Recreation;
- Interviews with appropriate Recreation management and personnel to gain an understanding of the department's internal control structure;
- An evaluation of the Recreation's internal controls over its major financial systems;
- An examination of a sample of transactions that we considered satisfactory to achieve our objectives; and
- Determination of the status of the findings cited in the prior audit report.

Conclusions

Based on our audit, we have concluded the following:

- The Recreation Department has resolved three of the four prior audit findings with one finding repeated.
- The Recreation Department is not complying with the Partners Fund Resolution.
- The Recreation Department is not complying with its Gethsemane concession contract with New Calvary Baptist Church.

BACKGROUND

The Detroit Recreation Department's (Recreation) origins go back to 1806, when the governor and judges of Michigan laid out Detroit with several public spaces and parks such as Grand Circus Park, Campus Martius and others. Belle Isle was purchased in 1879. Several other large parks, Palmer, Clark and Rackham Golf Course, were developed on land donated by citizens. The Recreation Department is a charter-mandated department of the City of Detroit. According to Section 7-1001 of the City Charter, "The Recreation Department shall operate recreation facilities, offer and carry on organized programs of recreational activities in the city, and, to the extent possible, coordinate all recreational programs and facilities being offered in the City."

Recreation provides opportunities for the public to participate in organized activities in more than 308 parks, 13 recreation centers, outdoor basketball courts, tennis courts, and golf courses. Recreation also operates specialized facilities such as Historic Fort Wayne, Belle Isle and Henderson Marina; and provides a means for public involvement in cultural arts. In addition, Recreation is responsible for the operations of three city-owned cemeteries.

Recreation's core activities include conducting and overseeing recreational programs, as well as programming for adults, senior citizens, and citizens with physical and emotional disabilities.

The following table shows the budgeted appropriations, revenues, and number of staff of Recreation, a general fund agency, for the fiscal years 2009-2010 through 2012-2013:

	General Fund	General Grants	Block Grants	Total
2009-2010:				
Appropriations	\$ 24,399,058	\$ 464,294		\$ 24,863,352
Revenues	1,387,310	464,294		1,851,604
Net Tax Cost	<u>\$ 23,011,748</u>	<u>\$ 0</u>		<u>\$ 23,011,748</u>
Number of Staff	178	0		178
2010-2011:				
Appropriations	\$ 21,549,475	\$ 82,000	\$ 550,000	\$ 22,181,475
Revenues	1,318,444	82,000	550,000	1,950,444
Net Tax Cost	<u>\$ 20,231,031</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 20,231,031</u>
Number of Staff	143	0	0	143
2011-2012:				
Appropriations	\$ 19,161,755	\$ 54,300	\$ 480,000	\$ 19,696,055
Revenues	1,081,440	54,300	480,000	1,615,740
Net Tax Cost	<u>\$ 18,080,315</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 18,080,315</u>
Number of Staff	141	0	0	141

	<u>General Fund</u>	<u>General Grants</u>	<u>Block Grants</u>	<u>Total</u>
<u>2012-2013:</u>				
Appropriations	\$ 12,064,311	\$ 54,300	\$ 150,000	\$ 12,268,611
Revenues	685,962	54,300	150,000	890,262
Net Tax Cost	<u>\$ 11,378,349</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 11,378,349</u>
Number of Staff	87	0	0	87

The Director of Recreation during the audit period is Alicia Minter.

STATUS OF PRIOR AUDIT FINDINGS

The prior audit of the Recreation Department for the audit period July 2007 through June 2010, by the Office of the Auditor General, included the findings listed below. Of the four prior audit findings listed, one finding was not resolved and is repeated in this report. The other three findings were resolved.

Findings:

1. Detroit Recreation Department (Recreation) Intentionally Violated Purchasing Policies And Circumvented City Council Oversight
This finding has not been resolved and is included in Finding 1 on page 6 of this report.
2. Recreation Management Is Unable To Determine Whether Its Concession Vendor Is Operating Under The Terms Of An Approved Contract Amendment
This finding has been resolved.
3. Recreation Failed To Obtain Annual Audited Financial Statements From Contractors Employed To Manage City Owned Facilities
This finding has been resolved.
4. Recreation Lacks Adequate Controls Over Cash Receipts
This finding has been resolved.

AUDIT FINDINGS AND RECOMMENDATIONS

1. Issues Related To Cemetery Contract And Operations

Since November 1992, the Recreation Department and New Calvary Baptist Church have had a concession agreement (agreement) that allowed New Calvary Baptist Church to manage exclusively Gethsemane Cemetery for the Recreation Department. We reviewed the agreement and noted the following:

- New Calvary Baptist Church subcontracted the management of Gethsemane Cemetery to Necaba Management Group, Inc. This action occurred without the Recreation Department's written approval.
- City Council did not approve the renewal of the agreement. The agreement included two five-year extensions. New Calvary Baptist Church and the Recreation Department needed to exercise the last of these extensions before June 30, 2012. In letters dated January 31, 2013 and February 8, 2013 respectively, New Calvary Baptist Church and the Recreation Department agreed to exercise the final extension. However, the parties did not exercise the extension timely, and the extension was not submitted to the City Council for approval.
- The Recreation Department is responsible for managing two additional cemeteries – Forest Hills and Mount Hazel. According to a departmental representative, both cemeteries are "closed," meaning the cemeteries cannot sell any burial plots. However, individuals who have purchased plots before the cemeteries closed can be buried when the time comes. The Recreation Department does not have any staff assigned to either cemetery. If a body must be buried, the Recreation Department has Necaba Management Group, Inc., to perform the service. As previously stated, the agreement is exclusively for Gethsemane Cemetery.

In Section 15.02 of the agreement, it states, "None of the Services covered by this Agreement shall be subcontracted without the prior written approval of the City."

Section 4-122 of the City Charter states, "The City may not purchase or in any way procure property or the services of independent contractors without approval by resolution of the City Council except as provided by ordinance." In addition, Section 18-5-21(a) of the City Code states, "City council approval of a contract or amendment shall not be deemed an approval of any renewal or extension sought to be entered into pursuant to such contract. Such renewals or extensions of contracts or the exercise of an option to renew or extend a contract shall require separate city council approval."

By the vendor subcontracting services with a third party without the proper due diligence and approvals, the department does not know whether the third party has the ability or is the best vendor to perform the contracted services.

By not obtaining City Council approval of the contract extension, the Recreation Department is making unauthorized payments for unapproved services. In addition, the City is liable for any damages and/or mistakes made by the third party.

By requesting and compensating for services outside of the contract, the Recreation Department is exposing the City to liability for any damages, injuries and/or mistakes by the vendor.

We recommend the Recreation Department:

- Obtain City Council approval for all applicable contracts and contract extensions in accordance with City Charter Section 4-122 and City Code Section 18-5-21(a).
- Perform a due diligence review of Necaba Management Group, Inc., before agreeing in writing to the subcontracting of services from New Calvary Baptist Church to Necaba Management Group, Inc. The Recreation Department should have assurance that Necaba Management Group, Inc., can perform the services.
- The Recreation Department should issue a Request for Proposal (RFP) and rebid the contract due to the expiration of the contract.

2. The Partners Fund Is Not In Compliance With Its Governing Resolution

A July 1981 City Council resolution established the Recreation Department's Partners Fund (Partners Fund). According to the resolution, the Recreation Department instituted a Gift Catalog Program. Businesses and/or individuals donated funds to the Recreation Department for recreational activities contained in the Gift Catalog. The Recreation Department made expenditures from the Partners Fund consistent with the wishes of the donor without using the normal bid procedure in accordance with the resolution.

The Partners Fund does not operate in accordance with the original resolution that established it. The Recreation Department no longer prepares a Gift Catalog; therefore, donors can donate funds to the Recreation Department that can use the funds, as it chooses. We were unable to determine when the Partners Fund no longer prepared and used the Gift Catalog.

Section 4-114 of the City Charter states, "... a resolution shall be adopted to express a determination, to direct a particular action, or to approve a singular event."

By operating the Partners Fund outside of the parameters of its original resolution, the Recreation Department is creating a fund that it can use for any purpose the Department deems necessary.

We recommend the Recreation Department revise the Partners Fund resolution to stipulate the purpose of the Partners Fund, the programs associated with the Partners Fund, how donations are to be made to the Partners Fund, and how the Recreation Department will spend the funds.

ISSUES AND CONCERNS

The Recreation Department is responsible for four golf courses – Chandler Park, Palmer Park, Rouge Park, and Rackham. The Recreation Department has a five-year concession contract with Vargo Golf Company (Vargo) to operate, manage, and maintain the golf courses. The contract includes an extension for an additional five years. The initial contract period is from December 2010 through November 2015. The extension, if exercised, will continue the contract through November 2020.

Vargo will pay the Recreation Department an annual base payment of \$125,000. According to the contract, Vargo will pay the annual base payment in six monthly installments of \$20,833.33 beginning June 15 through November 15 each year. In addition to the annual base payment, the Recreation Department will receive performance payments from Vargo based on annual gross golf course receipts. The performance payments are as follows:

- If the gross receipts are less than \$3,599,999.99, the Recreation Department does not receive a performance payment.
- If the gross receipts range from \$3,600,000.00 to \$4,000,000.00, the Recreation Department will receive a performance payment of 1% of the gross receipts.
- If the gross receipts range from \$4,000,000.01 to \$4,500,000.00, the Recreation Department will receive a performance payment of 2.5% of the gross receipts.
- If the gross receipts range from \$4,500,000.01 to \$5,000,000.00, the Recreation Department will receive a performance payment of 3.5% of the gross receipts.
- If the gross receipts exceed \$5,000,000.01, the Recreation Department will receive a performance payment of 5% of the gross receipts.

Vargo is responsible for paying all expenses related to golf course operations, including utilities. The contract requires Vargo to submit to the Recreation Department monthly revenue and expense reports and annual audited financial reports.

The Office of the Auditor General (OAG) received from the Recreation Department monthly reports and annual reports for the 2011 and 2012 seasons. The following revenue and expense information was included in the reports:

2011 Season – January 1 through December 31

	Chandler Park	Palmer Park	Rackham	Rouge Park	Total
Income	\$ 566,482.71	\$ 265,983.03	\$ 1,168,572.86	\$ 530,831.38	\$ 2,531,869.98
Expense	645,770.29	439,215.48	940,092.41	605,524.76	2,630,602.94
Profit/(Loss)	\$ (79,287.58)	\$ (173,232.45)	\$ 228,480.45	\$ (74,693.38)	\$ (98,732.96)

2012 Season – January 1 through December 31

	Chandler Park	Palmer Park	Rackham	Rouge Park	Total
Income	\$ 600,187.92	\$ 299,333.08	\$ 1,346,600.02	\$ 684,952.73	\$ 2,931,073.75
Expense	681,458.85	414,395.37	1,169,157.22	647,507.27	2,912,518.71
Profit/(Loss)	\$ (81,270.93)	\$ (115,062.29)	\$ 177,442.80	\$ 37,445.46	\$ 18,555.04

A Recreation Department representative stated that Vargo indicated that Chandler Park, Rackham, and Rouge Park could be profitable by the end of the contract, but Palmer Park would not. The main impediment to Palmer Park's success is the water and sewerage billing problem. The other golf courses have separate water and sewerage lines. Their water and sewerage billings are based on actual usage by that specific golf course. The Palmer Park Golf Course's water and sewerage lines are connected to the rest of Palmer Park's water and sewerage lines. Palmer Park Golf Course water and sewerage billings are based on a percentage estimate related to the entire park. According to the Recreation Department representative, the cost of segregating the water and sewerage lines between the golf course and the rest of the park were very high. As such, neither Vargo nor the Recreation Department would take on that expense.

The main reason for starting a business is to make a profit. The Palmer Park Golf Course water and sewerage billing problem precludes Vargo or an other vendor from maximizing profits. In addition, the Recreation Department will not realize any performance revenue.

We recommend the Recreation Department close the Palmer Park Golf Course consider another use for the property.



CITY OF DETROIT
RECREATION DEPARTMENT
ADMINISTRATION OFFICE

18100 MEYERS
DETROIT, MICHIGAN 48235
PHONE 313•224•1100
FAX 313•224•3544
WWW.DETROITMI.GOV

ATTACHMENT A

July 17, 2014

Mark W. Lockridge, Auditor General
Office of the Auditor General
2 Woodward Avenue
Room 216, Coleman A. Young Municipal Center
Detroit, Michigan 48226

Dear Mr. Lockridge:

The following presents the Recreation Department's responses for the indicated findings and recommendations for the Audit of the Recreation Department's Contracts and Partners Fund report as prepared by the Office of the Auditor General.

Finding No.: 1 Issues Related to Cemetery Contract and Operations

Department's Response:

The Recreation Department is reviewing the recommendations regarding the management contract at Gethsemane Cemetery with the Law Department to receive advisement on the agreement. New Calvary Baptist Church sub-contracted the management agreement to NECABA, a division of the church and NECABA has managed Gethsemane Cemetery for 22 years. A contract extension will be re-submitted for approval.

Finding NO.2: The Partners Fund is not in compliance with the Governing Resolution.

Department's Response:

The Recreation Partners Fund is being utilized in accordance to the July 1981 City Council resolution with the exception of a gift catalog. The Recreation Partners Fund is a restricted general fund account utilized as specified by the donor donation as support for various projects and programs and is designated as such for expenditure purposes. The department started revisions to the Gift Catalog earlier this year and will continue to utilize the account in accordance to all Finance and Accounting procedures.

Sincerely,

Alicia C. Minter
Director, Recreation Department

cc: Charlie Beckham, Group Executive –DON
Kevyn Orr, Emergency Manager