

AUDIT REPORT

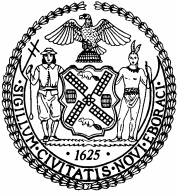


CITY OF NEW YORK
OFFICE OF THE COMPTROLLER
BUREAU OF FINANCIAL AUDIT
WILLIAM C. THOMPSON, JR., COMPTROLLER

Audit Report on the License Fees Due from Central Park Boathouse, LLC, And Compliance with Certain Provisions Of Its License Agreement

FP05-128A

March 28, 2007



THE CITY OF NEW YORK
OFFICE OF THE COMPTROLLER
1 CENTRE STREET
NEW YORK, N.Y. 10007-2341

WILLIAM C. THOMPSON, JR.
COMPTROLLER

To the Citizens of the City of New York

Ladies and Gentlemen:

In accordance with the Comptroller's responsibilities contained in Chapter 5, §93, of the New York City Charter, my office has audited the compliance of the Central Park Boathouse, LLC with its license agreement.

We audit concessions such as this to ensure that private concerns under contract with the City comply with the terms of their agreements, properly report revenue, and pay all fees due the City.

The results of this audit, which are presented in this report, have been discussed with officials from the Department of Parks and Recreation and the Central Park Boathouse, LLC, and their comments have been considered in preparing this report. Their complete written responses are attached to this report.

I trust that this report contains information that is of interest to you. If you have any questions concerning this report, please e-mail my audit bureau at audit@Comptroller.nyc.gov or telephone my office at 212-669-3747.

Very truly yours,

A handwritten signature in cursive script that reads 'William C. Thompson, Jr.'.

William C. Thompson, Jr.

WCT/fh

Report: FP05-128A
Filed: March 28, 2007

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*The City of New York
Office of the Comptroller
Bureau of Financial Audit*

**Audit Report on the License Fees Due from
Central Park Boathouse, LLC, and Compliance with
Certain Provisions of Its License Agreement**

FP05-128A

AUDIT REPORT IN BRIEF

The Department of Parks and Recreation (Parks) has a license agreement with the Central Park Boathouse, LLC, (the Boathouse) to renovate, operate, and maintain the Boathouse restaurant, café, catering facility, outdoor bar, snack bar, boat and bicycle rentals, a Park Activity and Resource Center, and a shuttle service at the licensed premises in Central Park, for the accommodation, enjoyment, and convenience of the public.

This audit determined whether the Boathouse accurately reported its total gross receipts, properly calculated the license fees due Parks, paid the license fees on a timely basis, and complied with certain other non-revenue-related requirements of the license agreement.

Audit Findings and Conclusions

The Boathouse generally complied with the non-revenue requirements of the license agreement. We verified that the Boathouse remitted a letter of credit to cover the security deposit to Parks, paid all its utility bills, paid late fees assessed by Parks, operated a shuttle service to and from the Boathouse, had the certificates of occupancy and incorporation on file, provided 24-hour security, supplied 100 new rowboats and bicycles for rental, maintained required insurance coverage, and named the City as an additional insured.

However, the Boathouse did not accurately report a total of \$2,392,669 in gross receipts. As a result, it owes Parks \$381,070 in license fees, plus late charges. Specifically, that amount includes:

- \$412,012 in gross receipts from catering, film shoots, and bicycle-rental sales was underreported by the Boathouse. Accordingly, the Boathouse owes \$65,922 in license fees, plus late charges. It should be noted that an additional \$190,611 of bicycle-rental sales may have been underreported based on non-projectable estimates. These could result in an additional \$30,498 in license fees, plus late charges.

- \$1,513,950 was improperly deducted from reported gross receipts. Accordingly, the Boathouse owes \$241,911 in additional fees, plus late charges.
- \$255,302 for the value of employee meals and complimentary meals was not reported in gross receipts. Accordingly, the Boathouse owes \$40,798 in additional fees, plus late charges.
- \$185,988 in gross receipts was recorded on Boathouse records but not posted to the monthly gross receipt report submitted to Parks. This includes \$47,214 in catering revenue that was unreported for three months in 2005 and \$138,774 in revenue between December 2001 and February 2002 and for the month of December 2003. Accordingly, the Boathouse owes \$28,372 in additional fees, plus late charges.
- \$25,417 from gift certificate sales that was not reported in gross receipts. Accordingly, the Boathouse owes \$4,067 in license fees plus late charges.

Further, the Boathouse lacks adequate controls over gondola-ride sales, and does not have sufficient safeguards over password access to its computerized point-of-sale system.

Audit Recommendations

We made 36 recommendations, 22 to the Boathouse and 14 to Parks, concerning the operation of the Boathouse and the oversight of this concession by Parks. Compliance with these recommendations will ensure that Parks collects from the Boathouse all license fees that are due; controls over the operations of the Boathouse are adequate to ensure that all gross receipts collected by the Boathouse are reported to Parks; and the Boathouse deducts from gross receipts only those amounts from items specified in the license agreement.

INTRODUCTION

Background

On June 12, 2000, the Department of Parks and Recreation entered into a license agreement with the Central Park Boathouse, LLC, to renovate, operate, and maintain the Boathouse restaurant, café, catering facility, outdoor bar, snack bar, boat and bicycle rentals, a Park Activity and Resource Center, and a shuttle service at the licensed premises in Central Park, for the accommodation, enjoyment, and convenience of the public. The term of the agreement is from March 1, 2001 to January 16, 2016.

The license agreement requires the Boathouse to pay Parks the greater of either a minimum annual fee, or a percentage of its gross receipts, as noted in Table I, below.

Table I
License Fees Payable by the Boathouse to Parks

Period	Minimum Fee	Percentage of Gross Receipts
March 1, 2001 to February 28, 2004	\$1,000,000	15%
March 1, 2004 to February 28, 2005	\$1,100,000	16%
Transition Period		
March 1, 2005 to June 30, 2005	\$330,000	16%
July 1, 2005 to June 30, 2007	\$1,100,000	16%
July 1, 2007 to June 30, 2010	\$1,212,200	17%
July 1, 2010 to June 30, 2013	\$1,337,060	17%
July 1, 2013 to June 30, 2015	\$1,473,440	17%
July 1, 2015 to January 16, 2016	\$1,473,440	17%

According to the license agreement, gross receipts consist of all revenue excluding collected sales taxes and gratuities paid directly or indirectly to employees and staff in addition to their regular salaries. The agreement also allows the licensee (provided that it does not obtain any monetary or financial benefit) to exclude from gross receipts “pass-throughs” such as entertainment or florists hired by a concession patron directly.

Additionally, the license agreement requires the Boathouse to spend a minimum of \$1,750,000 on capital improvements, post a \$370,000 security deposit with Parks, maintain certain types and amounts of insurance coverage, submit statements of gross receipts to Parks, and pay all required taxes and utility charges related to the facility.

For the 2004 and 2005 operating years (March 1, 2003, through June 30, 2005) the Boathouse reported a total of \$29,882,088 in gross receipts and paid Parks \$4,469,935 in fees.

Objectives

Our audit objectives were to determine whether the Boathouse:

- Accurately reported its total gross receipts, properly calculated the license fees due Parks, and paid the license fees on a timely basis; and
- Complied with certain other non-revenue-related requirements of the license agreement.

Scope and Methodology

The audit covered the period January 1, 2004, through December 31, 2005. To achieve our audit objectives, we reviewed the license agreement between Parks and the Boathouse and examined the agreement's requirements. We reviewed Parks correspondence, revenue reports, and other relevant documents. We analyzed the Parks concessionaire ledger for the gross receipts reported and paid to Parks, and determined whether payments were received on time.

To obtain an understanding of the Boathouse's control procedures for recording gross receipts, auditors interviewed management personnel. To determine if those controls were functioning as prescribed by management, we conducted a walk-through and unannounced observations of the Boathouse operations.

The Boathouse uses the GCS (Rpower) System for point-of-sale transactions for the restaurant, fast food, bar sales, rowboat rentals and gondola-ride sales. The Comptroller's Office Information Technology unit evaluated the GCS (Rpower) System to determine its accuracy and reliability. To assess the controls over restaurant, fast food, and bar sales, we made purchases at various points-of-sale; dined at the restaurant on three separate occasions—lunch on August 9, 2005, Sunday brunch on August 14, 2005, and dinner on August 22, 2005; and purchased items from the fast-food café on August 17 and 18, 2005, and September 1 and 10, 2005.

To assess the controls over rowboat rentals, we rented boats on August 9 and 18, 2005. On each occasion the boat rental was for one hour, and a point-of-sale receipt was issued. To determine the controls over gondola-ride sales, we purchased a gondola ride on August 14, 2005, were given a point-of-sale receipt and then attempted to trace the receipt to the daily-close report. Bicycle rentals are recorded using bicycle-rental lease agreements. To assess the controls over bicycle rentals, we performed observations on September 1 and 10, 2005. The bicycle-rental operation was observed from opening to closing and recorded the time of day each bicycle was rented, the return time, and the type and number of bicycles rented. The results of our observations was compared with the Boathouse's bicycle-rental lease agreements. We also rented two bicycles on August 18, 2005, and were given a handwritten receipt.

To determine the accuracy of reported gross receipts, we compared daily receipt totals from the restaurant, fast food, bicycle and rowboat rentals, and gondola ride sales for August 2005 to the monthly profit-and-loss statements.

To determine whether the Boathouse accurately reported to Parks its gross receipts from banquet contracts, we traced those reported gross receipts to Boathouse profit-and-loss statements and subsidiary ledgers. We requested all banquet contracts and invoices from January 2004 through December 2005. All banquet contracts and invoices provided by the Boathouse were reviewed, and charges were compared to the amounts recorded on the profit-and-loss statements and subsidiary ledgers. The profit-and-loss statements listed 245 contracts for 2004 and 318 for 2005. We then traced the individual contract and invoice amounts to the general ledger and sales journal.

To determine whether the deductions from gross receipts for gratuities were correct under the terms of the license agreement, we traced the deducted amounts from the profit-and-loss statements to Boathouse banquet contracts. To determine whether those amounts paid to Boathouse staff through its payroll were actually gratuities, we reviewed the catering wait-staff payroll records for 2004 and 2005, including the employee data sheets, payroll registers, and W-2 forms. The amounts paid to catering wait staff on days when banquet events were held and the banquet contract included gratuities were compared to amounts paid to those same employees on days when there was no event, or when the banquet contract for the event did not include gratuities. We reviewed the payroll registers for two months in 2004 and two months in 2005 to ascertain whether the gratuities paid were in addition to the staff's regular salary.

To determine whether the Boathouse accurately reported its gross receipts from film shoots held at the Boathouse, we reviewed film-shoot invoices and traced them to the profit-and-loss statements. The statements listed eight film shoots for 2004 and nine film shoots for 2005.

We examined file documentation at Parks to confirm whether the Boathouse remitted to Parks the required \$370,000 security deposit. We reviewed Boathouse records to determine whether the Boathouse complied with the insurance requirements of this agreement, paid all of its utility bills, and has the certificates of occupancy and incorporation on file.

We determined whether the Boathouse contract was registered with the Comptroller's Office, as required by Chapter 14 of the City Charter. We determined whether license fee payments were remitted on time, and whether late charges were assessed and paid. We also tested the Boathouse's compliance with certain other provisions of the contract, such as whether it operated a Park Activity and Resource Center and a shuttle service to and from the Boathouse. Finally, we determined whether the Boathouse provided 24-hour security, supplied 100 new rowboats and bicycles for rent, and displayed a sign indicating hours of operations.

We did not assess whether the Boathouse renovated the restaurant, bathrooms, and catering hall as required by the license agreement since a previous audit, Audit report #EW03-136A (*Audit Report on Department of Parks and Recreation Oversight of Capital Improvements by Concessionaires*), issued January 20, 2004, confirmed that this work was substantially completed.

At the exit conference the Boathouse's Certified Public Accountant and its controller provided us with additional information related to our preliminary findings. We attempted to

follow up on the newly provided documentation but the Boathouse refused to respond to our written requests for clarification.

This audit was conducted in accordance with generally accepted government auditing standards (GAGAS) and included tests of the records and other auditing procedures considered necessary. This audit was performed in accordance with the audit responsibilities of the Comptroller, as set forth in Chapter 5, §93, of the New York City Charter.

Discussion of Audit Results

The matters covered in this report were discussed with Parks and Boathouse officials during and at the conclusion of this audit. A preliminary draft report was sent to Parks and Boathouse officials and was discussed at an exit conference held on October 17, 2006. On January 2, 2007, we submitted a draft report to Parks and Boathouse officials with a request for comments. We received written responses from Parks on January 12, 2007, and from the Boathouse's attorney, LePatner & Associates, on January 17, 2007.

In its response, Parks agreed with 27 of the 36 audit recommendations, partially agreed with four recommendations, disagreed with one recommendation, and has forwarded to the City's Law Department issues concerning the four remaining recommendations. Parks officials advised us that a Notice to Cure has been issued requiring the Boathouse to pay \$113,854 in additional fees and interest and has required the Boathouse to implement the report's recommendations.

Parks officials decided not to pursue the additional estimated fees of \$30,498 from underreported bike-rental sales for the two years that we identified, claiming that our estimate was based on a "limited observation period." Parks officials also did not agree with our assessment of \$31,359 for the value of complimentary meals that was not included in gross receipts. Parks officials stated that they consider these meals as "a cost to the Boathouse to conduct and promote its business."

The four recommendations that are pending a decision from the City's Law Department concern the deduction from gross receipts of charges to customers of catered affairs to pay for wait-staff gratuities. We questioned the propriety of the deduction from gross receipts because these receipts were not used to pay gratuities, but instead to pay for the salaries of the wait-staff and the maitre d' and a commission to the catering sales managers. Payment of salaries and commissions are not deductible from gross receipts under the terms of the license agreement and its amendment. The total assessment concerning these four recommendations is \$480,179.

In his response, the Boathouse's attorney agreed that his client underreported gross receipts to Parks concerning catering receipts and receipts from film shoots held on the property and as a result owed additional license fees of \$61,880. However, he disagreed with our largest assessment that the deduction of \$1,513,950 from gross receipts reported to Parks to pay for wages to catering staff was improper and that the value of employee and complimentary meals should not have been excluded from gross receipts reported to Parks.

In his response, the Boathouse attorney attempted to obfuscate a number of valid concerns raised by the auditors in this report by taking advantage of the most convenient, unsupported interpretations of the terms of the license agreement and its amendment, and by questioning widely accepted audit methodologies and practices.

Concerning the interpretation of the deduction of gratuities from gross receipts that were charged and collected from customers of catered events, the attorney has misconstrued the terms of the license agreement and its amendment. As previously stated, the Boathouse used the receipts earned from gratuity charges to pay for salaries and other expenses. The terms of the license agreement and its amendment clearly preclude deduction from gross receipts of money distributed to employees as salary, in that it states “Licensee shall provide documentation satisfactory to Parks that such gratuities were paid to employees and staff in addition to their regular salaries.” (Emphasis in original.) However, the Boathouse was unable to provide the auditors with the required documentation to justify its contention that the deductions were used to pay staff gratuities in addition to their regular salaries. In fact, contrary to Boathouse’s contention, our own review indicated that Boathouse staff were not paid gratuities in addition to their regular salaries; rather the gratuities were used to fund a portion of the promised hourly salary rate.

Concerning the fact that the Boathouse did not report in its gross receipts \$196,308, the value of complimentary meals that were provided to customers in 2004 and 2005, the attorney asserts “that such complimentary meals are not only common in the restaurant industry, but are integral to the restaurant’s business development and financial growth, which, of course, only serves to benefit Parks as well.” Although this practice may be common in the restaurant industry the Boathouse presented no documentation to prove that the complimentary meals were, in fact, provided to potential customers and ultimately contributed to the restaurant’s business development and financial growth. Without the required documentation we cannot ascertain the validity of the claim by the Boathouse’s attorney.

Concerning our observations and estimate of underreported bike-rental sales for the 2004 and 2005 operating years, the attorney questioned our audit methodology and audit protocol used in reaching our conclusions. In fact, the methodology we used to determine underreported bike-rental sales was prudent and an established auditing practice used by the New York State Department of Taxation and Finance to project underreported sale taxes. Moreover, the Boathouse has refused to establish any controls that would prevent further underreporting of receipts to Parks, such as the installation of a point-of-sale terminal.

The specific comments raised by Parks and by Boathouse’s attorney are contained in the relevant sections of this report. The full texts of their comments are included as addenda to this report.

FINDINGS AND RECOMMENDATIONS

The Boathouse generally complied with the non-revenue requirements of the license agreement. We verified that the Boathouse remitted a letter of credit to cover the security deposit to Parks, paid all its utility bills, paid late fees assessed by Parks, operated a shuttle service to and from the Boathouse, had the certificates of occupancy and incorporation on file, provided 24-hour security, supplied 100 new rowboats and bicycles for rental, maintained required insurance coverage, and named the City as an additional insured.

However, the Boathouse did not accurately report a total of \$2,392,669 in gross receipts. As a result, it owes Parks \$381,070 in license fees, plus late charges. Specifically, that amount includes:

- \$412,012 in gross receipts from catering, film shoots, and bicycle-rental sales that was underreported by the Boathouse. Accordingly, the Boathouse owes \$65,922 in license fees, plus late charges. It should be noted that an additional \$190,611 of bicycle-rental sales may have been underreported based on non-projectable estimates. These could result in an additional \$30,498 in license fees, plus late charges.
- \$1,513,950 that was improperly deducted from reported gross receipts. Accordingly, the Boathouse owes \$241,911 in additional fees, plus late charges.
- \$255,302 for the value of employee meals and complimentary meals that was not reported in gross receipts. Accordingly, the Boathouse owes \$40,798 in additional fees, plus late charges.
- \$185,988 in gross receipts that was recorded on Boathouse records but not posted to the monthly gross receipt report submitted to Parks. This includes \$47,214 in catering revenue that was unreported for three months in 2005 and \$138,774 in revenue between December 2001 and February 2002 and for the month of December 2003. Accordingly, the Boathouse owes \$28,372 in additional fees, plus late charges.
- \$25,417 from gift certificate sales that was not reported in gross receipts. Accordingly, the Boathouse owes \$4,067 in license fees plus late charges.

Further, the Boathouse lacks adequate controls over gondola-ride sales, and does not have sufficient safeguards over password access to its computerized point-of-sale system.

These findings are discussed in detail in the following sections of this report.

\$412,012 in Revenue Not Reported in Gross Receipts

The Boathouse underreported \$412,012 in gross receipts from catering, film shoots, and bicycle-rental sales. Of this amount, \$400,344 was for underreported catering revenue, \$10,598 was for underreported film-shoot revenue, and \$1,070 was for underreported bicycle sale rentals.

As a result of underreporting this revenue, the Boathouse owes Parks \$65,922 in license fees, plus late charges. We note that an additional \$190,611 of bicycle-rental sales may have been underreported based on non-projectable estimates. These could result in an additional \$30,498 in license fees.

Underreported Catering Revenue

The Boathouse underreported \$400,344 in catering-event revenue for 2004 and 2005 because it failed to report 35 catered events, did not accurately report revenue from 11 events, and did not include revenue from events that were canceled but for which patron deposits were non-refundable. As a result, the Boathouse owes Parks \$64,055 in license-fee payments, plus interest and penalties. During this two year period the Boathouse reported 563 catered events at its facility.

Of the 35 unreported events, we identified 13 in 2004 and 22 in 2005 for which the Boathouse collected \$302,964 in revenue that was not included in its profit-and-loss statements and in the monthly report of gross receipts submitted to Parks. Consequently, the Boathouse underpaid \$48,474 in license fees. The Boathouse controller agreed that these events were not reported. The Boathouse does not have adequate controls to ensure that each catered event contract can be accounted for. Our review of the Boathouse files found that the contracts are not sequentially numbered. Therefore, we were unable to determine whether all gross receipts from catered events were reported to Parks.

Of the 11 catered events for which revenue was not accurately reported on profit-and-loss statements and on the monthly report of gross receipts, revenue was understated for eight events and overstated for three events. This resulted in a net underreporting of \$26,762 in revenue. Consequently, the Boathouse underpaid \$4,282 in license fees.

Finally, the Boathouse collected \$70,618 in deposits for one catered event in 2004 and nine events in 2005 that were canceled, although this revenue was not included in Boathouse gross receipts. Boathouse officials stated that revenue was not included in the gross receipts because of the licensee's practice of recognizing revenue only at the time an event is held. However, according to the Boathouse contract with its patrons, deposits are non-refundable. Therefore, the revenue should have been included in the profit-and-loss gross receipts and been subject to the license fee. Consequently, the Boathouse underpaid \$11,299 in license fees.

Recommendations

The Boathouse should:

1. Pay Parks license fees totaling \$64,055, plus interest and penalties, for underreporting catering event revenue.
2. Implement a system of internal controls to ensure that all events are accurately reported, including reconciling its catered event spreadsheets to the catering receipts and deposits.

3. Use prenumbered contracts when booking catered events. This will improve controls over each contract and will improve accountability over the catered events.
4. Include all payments when they are received from patrons in its monthly report of gross receipts submitted to Parks. The Boathouse should not wait until the date of the event to record revenue received.

Parks should:

5. Ensure that the Boathouse pays the City \$64,055, plus interest and penalties, for underreporting catering event revenue.
6. Ensure that the above business process recommendations are implemented.

Parks Response: In its response, Parks agreed with our assessment and stated that it issued a Notice to Cure requiring the Boathouse to comply with the above recommendations.

Boathouse Response: In his response, the Boathouse's attorney stated:

“The Boathouse will agree to pay Parks license fees totaling \$52,756, which corresponds to the missed/underreported revenues the Boathouse has confirmed are owed based upon its internal review of the audited documents.

“The Boathouse has established internal controls via Excel spreadsheets that cross-reference party contracts with posted revenues and deposits, and which can then be reconciled to financial records of deposits and receivables on a monthly basis.

“Contracts are being numbered via a new software program, *Catermate*.

“The Boathouse cannot in good faith include patron payments (deposits) as part of its Gross Receipts submitted to Parks. Such practice would be contrary to GAAP [Generally Accepted Accounting Principles] standards, which provides under the accrual method of accounting, that revenues should not be reported until goods and/or services are actually provided. The Boathouse proposes to continue as it has such that all deposits are to be recorded as liabilities and reconciled monthly. Then, in the month the event occurs, the deposit will be re-classified as revenue in accordance with GAAP.”

Auditor Comment: It is clearly the intent of the license agreement that the Boathouse must recognize patron payments, including deposits, upon receipt. As previously stated, the Boathouse accepted deposits for ten events that were subsequently canceled before the

scheduled event dates. These deposits were not refunded and were never included in gross receipts reported to Parks. The Boathouse response stating that the accrual method of accounting precludes reporting of deposits as revenue until the “event occurs,” fails to acknowledge that a deposit not refunded for a canceled event becomes revenue when the event is canceled.

Underreported Film-Shoot Revenue

The Boathouse did not report \$10,598 in revenue it obtained from 15 film shoots held in 2004 and 2005. As a result, the Boathouse underpaid its license fee by \$1,696. Additionally, invoices totaling \$1,500 for three film shoots were not on file; however, the film shoots were reported on the profit-and-loss statements.

Recommendations

The Boathouse should:

7. Pay Parks license fees totaling \$1,696, plus interest and penalties, for underreporting film-shoot revenue.
8. Issue sequentially numbered receipts for film shoots.
9. Reconcile its film-shoot invoices to the film-shoot receipts, deposits, profit-and-loss statements, and the monthly report of gross receipts submitted to Parks.

Parks should:

10. Ensure that the Boathouse pays the City \$1,696, plus interest and penalties, for underreporting film-shoot revenue.

Parks Response: In its response, Parks agreed with our assessment and stated that it issued a Notice to Cure requiring the Boathouse comply with the above recommendations.

Boathouse Response: In his response, the Boathouse’s attorney stated:

“The Boathouse will agree to pay Parks license fees totaling \$1,696, which corresponds to the missed/underreported revenues Boathouse has confirmed are owed based upon its internal review of the audited documents.

“On a going forward basis, film shoots will be handled in the same manner as a catered event, thus being subject to the same cross-referencing,

reconciling and balancing with each month's close as indicated above for catered events."

Underreported Bike-Rental Sales

The Boathouse underreported bike-rental fees totaling \$1,070. As a result the Boathouse owes Parks an additional \$171 in license fees, plus late charges. The underreported amount is based on unannounced observations conducted for two-days in September 2005.

The results of our unannounced visits cannot be projected for the purposes of calculating additional license fees due Parks based upon underreported revenue. However, for illustrative purposes we estimated that bike rentals could have been underreported by an additional \$190,611, and this could result in an additional \$30,498 in license fees.

Our estimates are based on our unannounced observations for a two-day period in September 2005, in which the Boathouse underreported its bike-rental sales and understated the corresponding revenue by \$1,070.¹ (See Table II below.) Based on these observations, we determined that approximately 39 percent of total bike-rental receipts collected were not reported. Accordingly, we applied the underreported percentage of rental receipts to the Boathouse's reported bike-rental sales for 2004 (\$139,621) and 2005 (\$160,187), and estimated that the total underreported bike-rental sales could have been \$191,681. (The estimated \$191,681, less the actual underreported fees totaling \$1,070, results in \$190,611 of additional revenue that we estimate could have been underreported.)

Table II
Summary of Bike Rentals Reported vs. Observed

Date of observation	Number of bike rentals observed	Number of bike rentals reported	Difference	Total fees based on bike rentals observed	Total fees reported	Underreporting of bike revenue
September 1, 2005	86	54	32	\$874	\$541	\$333
September 10, 2005	167	109	58	\$1,851	\$1,114	\$737
Totals	253	163	90	\$2,725	\$1,655	\$1,070

¹ We stationed two auditors near the bike-rental booth and in full view of the rentals and found on September 1, 2005, (Thursday) that of the 86 bike rentals, 32 were not reported by the Boathouse. On September 10, 2005, (Saturday) we performed another observation and found that of the 167 bike rentals, 58 were not reported by the Boathouse.

The Boathouse lacks controls to ensure that all revenue generated from bike rentals is reported in gross receipts. We therefore conducted unannounced observations to assess potential revenue that may have been underreported due to the inadequate controls. The Boathouse rents bikes to the public and charges patrons an hourly rental fee. Four types of bikes are rented: cruisers at \$9 for the first hour; 21-speed bikes at \$15 for the first hour; tandem bikes (two-seaters) at \$20 for the first hour; and children's bikes at \$6 for the first hour. (For each type of bike, there is a prorated charge for each additional half-hour.) The Boathouse has one employee who handles all rentals and collects cash payments. The bike-rental kiosk uses a stand-alone register that is not connected to the Boathouse point-of-sale system. Moreover, there is no oversight of the bike attendant to ensure that the amount he collects daily is deposited and properly recorded.

Recommendations

The Boathouse should:

11. Pay Parks license fees totaling \$171, plus interest and penalties, for underreported bicycle-rental sales.
12. Install a register that is linked to the point-of-sale system used for restaurant sales and row boat rentals.

Parks should:

13. Ensure that the Boathouse pays the City \$171, plus interest and penalties, for underreporting bicycle-rental sales.
14. Ensure that the Boathouse bike-rental sales register is linked to the point-of-sale system so that subsequent bike revenues may be accurately recorded and reported.
15. Follow up on the estimated \$190,611 that may have been underreported and consider whether additional revenues of \$30,498 may be due.

Parks Response: In its response, Parks agreed with our assessment and stated that it issued a Notice to Cure requiring the Boathouse pay an additional \$174, inclusive of interest charges to Parks. However, it further stated:

“Subject to the Boathouse’s full implementation of the required actions noted . . . for recommendation 12, Parks will not pursue the collection of this additional sum considering that this additional assessment is based on a limited observation period.

“The audit observations . . . illustrate a serious deficiency in controlling the collection and reporting of revenue for bicycle rentals. The Boathouse must implement this recommendation (recommendation 12) to alleviate the problem of underreporting. Boathouse officials believed that an

internal audit program to randomly test the rental operation would provide a better monitor to ensure that all revenue is recorded. This additional action together with the point-of-sale link required under recommendation 12 should provide the necessary level of control over these ancillary sources of income.”

Boathouse Response: In his response, the Boathouse’s attorney stated:

“Notwithstanding the nominal amount purported to be due, the method of calculating such revenue and license fees is both unreasonable and unreliable. First, the Auditor’s review of the Boathouse’s bicycle-rental operations is solely based upon observations, without documentary support, conducted on 2 isolated days during one month of an Audit Period covering 2 years. The potential and likelihood for errors relating to speculation, conjecture and lack of documentary support are immeasurable.

“Based upon the Boathouse’s position on this issue, it is submitted that no additional fees are due and owing to Parks for bicycle-rental sales. Notwithstanding the recommendation in the Draft Report based on a two day observation, the Boathouse does not believe the installation of a point-of-sale terminal is likely to result in greater control of bike-rental sales.”

Auditor Comment: The methodology used in testing the accuracy of the reporting of the bicycle-rental sales is sound and an established auditing practice. New York State Department of Taxation and Finance auditors use this same methodology to project underreported sale taxes. The State auditors’ project underreported sales based on sample observations when testing the accuracy of reported sales. The State auditors have used observations of one day’s sales to estimate an entity’s sales tax liability for as many as four years. Moreover, in cases before the New York State Division of Tax Appeals, Administrative Law Judges have upheld the use of this methodology to determine sales tax liability when an entity’s sales records were insufficient to rely on.

The Boathouse response presents no explanation for the sales observed by our auditors that were not reported in gross receipts to Parks. The Boathouse notes a lack of “documentary support” without providing any books or records to dispute that the receipts based on the transactions we observed were reported to Parks. Additionally, the Boathouse fails to describe any controls that were in place to verify the accuracy of the bicycle-rental sales that were reported to Parks. As previously noted, the cash register at the bicycle-rental kiosk was not linked to the point-of-sale system. Moreover, the same person is responsible for collecting, recording and reconciling the daily sales activity, a clear violation of the basic tenet of sound internal controls. The duties of collecting, recording and reconciling sales should be separate to ensure that all revenues are collected, properly accounted for, recorded, and deposited in the bank.

Our estimate of \$190,611 in underreported bike-rental sales for 2004 and 2005 was formulated using the same methodology used by the New York State Department of Taxation and Finance for identifying unreported revenue. The Boathouse's attorney failed to provide any substantive evidence to support the claim in his response that the amount we identified was based on "speculation and conjecture." The Boathouse has refused to establish any controls that would prevent further underreporting of receipts to Parks, such as the installation of a point-of-sale terminal. The Boathouse's assertion that they do "not believe the installation of a point-of-sale terminal is likely to result in greater control of bike-rental sales" is without merit given our observations and the lack of basic controls. As the agency responsible for monitoring this concession, Parks must require the Boathouse to take the necessary measures to ensure that all the income earned by the Boathouse is accurately reported in gross receipts.

In its response, Parks notes that "Boathouse officials believed that an internal audit program to randomly test the rental operation would provide a better monitor to ensure that all revenue is recorded." However, to date no internal audit program or random test procedures have been implemented, identified, or even suggested by officials of the Boathouse. As noted above, the Boathouse response accepts no suggestion for an acceptable level of internal controls. Furthermore, we doubt the sincerity of the Boathouse acknowledgement of the benefit of random tests of the rental operations. The Boathouse was notified of our auditors' bike rental observation results on February 22, 2006, well before the start of the 2006 bike rental season. Yet the Boathouse acknowledged at the exit conference on October 17, 2006 that it did not perform its own observations or other random testing of the bike rental operations during the 2006 season.

As stated in the response, the Boathouse still has not established adequate internal controls over bike-rental sales. The methodology we used to determine unreported bike-rental sales was prudent and is identical to that used by the New York State Department of Taxation and Finance. In that regard, we believe that Parks should reconsider its position and require the Boathouse to pay the \$30,498 plus interest and penalties that we identified. In addition, Parks must require the Boathouse to establish an adequate system of internal controls over bike-rental sales to ensure that all sales are reported and all fees are paid.

Improper Deductions from Gross Receipts Relating to Catered Affairs

For 2004 and 2005, the Boathouse improperly deducted \$1,513,950 from its gross receipts when calculating the monthly franchise fee due Parks. According to Boathouse representatives, the deductions were used to pay gratuities to catering wait-staff and consisted of a mandatory 11.5 percent charge to customers for gratuities, a charge for maitre d' services, and an additional staff fee for each catered affair. While the September 10, 2001 amendment to the agreement permits gratuities to be deducted from gross receipts, our review of Boathouse records indicated that those deductions were actually used to pay the salaries of the maitre d', a commission to the catering sales managers, and approximately 80 percent of the hourly wages of

the catering wait-staff. The license agreement clearly does not allow these types of expenses to be deducted from the gross receipts. Thus, as a result of these improper deductions, the Boathouse owes Parks additional license fees totaling \$241,911, plus interest and penalties (\$112,490 in 2004 and \$129,421 in 2005).

The September 10, 2001 amendment requires that the *“Licensee shall provide documentation satisfactory to Parks that such gratuities were paid to employees and staff in addition to their regular salaries.”* (Emphasis in original.) However, the Boathouse was unable to provide the required documentation to justify its contention that the deductions were used to pay staff gratuities. In fact, contrary to Boathouse’s contention, our own review indicated that Boathouse staff were not paid gratuities.

The maitre d’ and the sales managers are paid fixed weekly salaries, regardless of the number of affairs held. The maitre d’s salary is funded from a \$300-\$350 charge that the Boathouse assesses customers for catered affairs, and a portion of the sales managers’ salaries are funded from 1.5 percent of catered-affair sales. Payroll records indicate that neither the maitre d’ nor the sales managers is paid any gratuities.

As indicated by the following Boathouse documentation, payments to the catering wait-staff were composed entirely of salary:

1) *Employee data sheets (employment agreements), signed by the employee and a Boathouse manager, stating the hourly salary for the job title.* For example, the job title of “Catering Waiter” lists the salary as \$17 per hour. This is a fixed hourly rate, and the employees do not receive gratuities in addition to the \$17.

2) *Payroll Registers showing two pay categories for catering wait-staff regular salary and “party pay.”* Regular salary is minimum wage. Party pay is the difference between the employees’ hourly hire rate and the minimum wage. For example, a catering waiter in 2004 earned \$17 per hour, consisting of a regular salary of \$3.30 and party pay of \$13.70 per hour. In 2005 and 2006, as the regular salary (minimum wage) increased to \$3.85 and \$4.35, the party-pay rate decreased to \$13.15 and \$12.65. If indeed the party pay was a gratuity payment, its amount should not decrease because the minimum wage increased.

3) *Boathouse payroll records in 2004 and 2005 indicating that catering wait-staff were paid \$66,541 in party pay for working 4,915 hours on days when there was either no catering event or there was an event at which no gratuities were collected from the patron hosting the event.* If indeed the party pay was a gratuity payment, it would not be paid on days that there was no catering event or when no gratuities were collected. Specifically, there were:

- 35 instances in which there was no record of an event held on the day indicated;

- 20 instances in which the event was not reported on the Boathouse profit-and-loss statements (both the revenue and the gratuities charged for these events were not reported to Parks as gross receipts);
- 15 instances in which the entire cost of the event was free-of-charge to the patron and a gratuity was not collected;
- 14 instances in which gratuities were not added to the invoice (a gratuity is listed as a separate line item on the invoice); and
- 2 instances, on Thanksgiving Day in 2004 and 2005, in which the catering hall was used to accommodate the overflow of patrons from the restaurant and a total of 16 catering wait-staff were paid \$17 per hour (\$13.70 “party pay” plus \$3.30 minimum wage). This was not a catered event for which the Boathouse charged gratuities.

4) *Boathouse payroll records indicating that a waiter was paid \$548 in party pay for one week’s vacation.* Obviously, if party pay was a gratuity payment, it would not have been used for vacation pay.

The results of our review belie the Boathouse contention that the gratuities it collects from customers for catered affairs should be deductible from gross receipts. In fact, documentation clearly indicates that the Boathouse has established a pattern of using customer gratuities to fund salaries for catering wait-staff, the maitre d’, and sales managers. Gratuities charged to patrons are deductible only if such gratuities were paid to employees and staff *in addition to their regular salaries*, which these gratuities clearly were not.

At the exit conference, the Boathouse stated that it was in compliance with the intent of the contract since it distributed the gratuities collected to its catering wait-staff even though the funds were paid as wages. However, the Boathouse could not offer any evidence to support its position. In fact, the Boathouse agreed that on the W-2 forms for the catering wait-staff, it records the total dollar amount of compensation as wages (box 1), not as tips (box 8). As stated above, the contract requires that if gratuities are to be deductible from gross receipts, they have to be paid *in addition* to regular salaries. Our analysis clearly shows that the \$1.5 million that the Boathouse deducted from gross receipts were used to pay the employees’ regular salaries and not paid as additions to their regular salaries. Thus, the Boathouse’s practice does not comply with the deductibility requirement in the September 10, 2001 amendment to the agreement.

Please note that from October 2001 to December 2003 and from January to June 2006, the Boathouse deducted from its gross receipts an additional \$1,503,620 for gratuities and additional staff. Although these periods were beyond the scope of our audit, we are concerned that these deductions have been used to pay the salaries of catering staff as reported above. Therefore, Parks should determine whether these deductions were in fact legitimate gratuity payments that could have been deducted from gross receipts. However, if Parks determines that these deductions were actually used to pay salaries, it should compel the Boathouse to pay an additional \$228,853 in license fees, plus interest and penalties.

Recommendations

The Boathouse should:

16. Pay Parks license fees totaling \$241,911, plus interest and penalties, for improper deductions from gross receipts.
17. Include all revenue received from its operations in its gross receipts without deducting for gratuities used to fund salaries. Gratuities should only be deducted to the extent that they are distributed to employees for services rendered for a specific event and when the distribution is in addition to their regular salaries. Commissions paid to sales managers should never be deducted from gross receipts.

Parks should:

18. Ensure that the Boathouse pays the City \$241,911, plus interest and penalties, for incorrectly deducting from gross receipts gratuities used to pay salaries and commissions.
19. Determine whether \$1,503,620 in deductions from Boathouse gross receipts from October 2001 to December 2003 and from January to June 2006 were used to pay salaries of its catering wait-staff. If so, Parks should collect from the Boathouse \$228,853 in additional license fees, plus interest and penalties.

Parks Response: In its response, Parks stated “**Recommendations 16, 17, 18, and 19** cover alleged improper deductions from gross receipts by the Boathouse that were used to pay employees’ regular salaries rather than as gratuities in addition to their regular salaries. Parks will refer this issue to the City’s Law Department to obtain a legal opinion on whether the Boathouse’s methodology to account for the gratuities it collects and then deducts from gross receipts complies with the license agreement language that allows for their exclusion from reportable sales. Parks will render a determination covering this issue after the Law Department has replied. The total assessments concerning this finding, \$480,179 (\$470,764 plus \$9,415) is pending a final ruling.”

Boathouse Response: In his response, Boathouse’s attorney stated:

“It is customary practice in the restaurant and food service industry to charge the customer a service charge/auto gratuity and then redistribute the payments as wages to the catering and related service staff. Such practice is consistent with the gratuity deduction permitted by in the Amendment to the Lease Agreement.

“The Boathouse submits that no fees are due relative to the gratuity issue detailed above. It is the Boathouse’s position that it is in full compliance with all Labor Law and License Agreement obligations as they relate to the receipt, handling and recording of gratuities and their deductions from the Gross Receipts.”

Auditor Comment: The assertion that the Boathouse gratuity deduction is consistent with the amendment to the license agreement lacks any basis in fact or law. The lease amendment allows gratuities to be deducted only when gratuities are paid *in addition* to employees’ regular salaries. In fact Parks stated in a response to another audit report on a similar license agreement that the “gratuity exclusion provision was never intended to serve as a means for a licensee to write-off its payroll expense against reportable gross revenue to the City.”²

The Boathouse’s attorney states that the Boathouse is “in full compliance with all Labor Law . . . obligations as they relate to the receipt, handling and recording of gratuities and their deductions from the Gross Receipts.” In regards to our audit assessment, this is irrelevant. The deductibility of gratuities from gross receipts in calculation of the license fee due is based not on Labor Law but on the terms stipulated in the license agreement and its amendment. As documented in our finding above, the terms of the license agreement and amendment clearly preclude deduction from gross receipts of money distributed to employees as salary.

Furthermore, the New York State Supreme Court (New York County) decision dated August 26, 1996, (Index No. 407578/93) determined that banquet service charges (including gratuity charges) in another City license agreement is not income to be included in gross receipts in those instances *in which 100 percent* of the banquet service charge is distributed to the banquet staff. The Court’s Order that was drafted by the Corporation Counsel of the City of New York was filed October 10, 1996, and finalizes this decision. As illustrated by our analysis, 100 percent of the banquet gratuities that was collected *was not* distributed to banquet staff working the affair. This is further exemplified by the fact that during the peak season period the Boathouse uses the services of a second maitre d’. The maitre d’ is paid a per shift fee of \$250, yet the Boathouse charges its patrons \$350 for maitre d’ services. Obviously, 100 percent of this maitre d’ charge deducted from gross receipts is not 100 percent disbursed to the maitre d’. Accordingly, the Boathouse is not adhering to the court’s criteria for gratuity deductibility.

Finally, if the gratuities were 100 percent distributed to meet deductibility of the test established by the court ruling, then the gratuity charges would be exempt from sales tax. The Boathouse has been charging its patrons sales tax on the gratuity charges. Therefore, the Boathouse has either been incorrectly charging New York State sales tax on the

² Audit Report FL03-102A, *Compliance of Crystal Ball Group, Inc., (Terrance on the Park) with Its License Agreement and Its Payment of License Fees Due the City April 1, 1999-March 31, 2002*, Addendum II, Page 4 of 6, issued February 26, 2004.

gratuity amount or the gratuity is not deductible from gross receipts. We believe the latter is true, and we accordingly assert that \$480,179 in additional license fees and interest is due Parks.

**Value of Employee Meals and Complimentary Meals
Not Included in Gross Receipts**

The Boathouse did not include in its gross receipts \$58,994 for the value of meals provided to its employees. As a result, the Boathouse underpaid Parks \$9,439 in license fees, plus late fees.

The Boathouse 2004 and 2005 payroll registers identified \$58,994 in meals provided to employees that employees were charged for in the form of a payroll deduction. As such, the payroll deduction for these meals are required to be treated as revenue and be included in the gross receipts.

Moreover, the Boathouse did not report in its gross receipts \$196,308, the value of complimentary meals that were provided to customers in 2004 and 2005. The value of those meals was recorded on the Boathouse point-of-sale system. As a result of not reporting this revenue, the Boathouse underpaid Parks \$31,359 in licensee fees, plus late fees.

According to §2.1 (l) (iv) of the license agreement:

Gross Receipts shall include sales made for cash or credit, (credit sales shall be included in gross receipts as of the date of the sale) regardless of whether the sales are paid or uncollected. It being the distinct intention and agreement of the parties that all sums due to be received by Licensee from all sources from the operation of this License shall be included in Gross Receipts. (Emphasis added)

The Boathouse claims that such complimentary meals promote its business and increase future sales by allowing patrons to sample its food before they either book a catered affair or dine with a large party. While we recognize that the Boathouse is permitted to forgo charging patrons or friends for meals, the agreement does not permit the Boathouse to similarly forgo paying license fees. Further, the Boathouse procedures do not document to whom the complimentary meals and drinks were given; therefore, we could not determine whether prospective clients were in fact the recipients of these complimentary meals, as claimed. Therefore, the value of complimentary meals must be included in the gross receipts reported to Parks.

Based upon documentation provided at the exit conference, we requested explanations for some of the larger complimentary meals and lost sales (deductions that ranged between \$800 and \$2,600 each) that were deducted from gross receipts reported to Parks. *The Boathouse would not provide us any further information.* Without an acceptable explanation and supporting documentation for these large deductions, we cannot assess their legitimacy and must disallow the complimentary meal deductions from gross receipts.

The documentation provided at the exit conference also showed that in many instances entire restaurant sales were deemed complimentary and excluded from gross receipts. In those cases, the Boathouse should pay either sales tax or compensating-use tax. Our review of sales tax returns revealed that the Boathouse submits sales tax based on its gross receipts (using the same dollar amount as reported to Parks for calculating the license fee); thus, the Boathouse does not pay either tax on the complimentary meals provided to patrons or the meals provided to employees. When the Boathouse purchases food and beverages it does so without paying sales tax because it is with the intention that these provisions will be resold and at that point sales tax will be charged. However, in the case of complimentary meals and employee meals, there is no sales tax charged when the meals are given to either patrons or employees. The Boathouse has the option to provide free meals but state tax law requires that compensating-use tax be paid on the cost of the provisions used to provide free meals. Based on the Boathouse's profit and loss statements the cost of the food and drink provided as complimentary would have resulted in \$4,523 compensating-use taxes for 2004 and 2005. Additional compensating-use tax is due on employee meals; however, we were unable to determine the cost of the provisions used to provide employee meals. The Boathouse should use a reasonable method to determine the tax due for employee meals under this contract.

We should also note that from October 2001 to December 2003 and from January to June 2006, the Boathouse did not report in its gross receipts \$249,638. That amount was the value of complimentary meals recorded on the Boathouse point-of-sale system. In addition, from January to June 2006, the Boathouse did not include in its gross receipts \$23,894 for meals that employees were charged through a payroll deduction. Although these periods were beyond the scope of our audit, we must point out that the value of complimentary and employee meals were similarly not included in gross receipts, as cited above. Therefore, Parks should determine whether the \$273,532 should have been included in reported Boathouse gross receipts. If Parks determines that the \$273,532 should have been included in gross receipts, then it should compel the Boathouse to pay an additional \$42,428 in license fees. In addition, the Boathouse did not pay compensatory-use tax on the \$249,638 for complimentary meals. It is estimated that the tax would be \$5,608.

Recommendations

The Boathouse should:

20. Pay Parks license fees totaling \$40,798, plus interest and penalties, for not reporting the value of employee meals and complimentary meals.
21. Include the value of meals employees are charged for and complimentary meals in its gross receipt reports to Parks.
22. Pay \$4,523 in additional compensating use tax owed to New York State as well as determine the compensating-use tax due for employee meals.

Parks should:

23. Ensure that the Boathouse pays the City \$40,798, plus interest and penalties, for not reporting the value of employee meals and complimentary customer meals.
24. Determine whether \$273,532, the value of complimentary and employee meals, should have been included in gross receipts reported to Parks. If so, Parks should collect from the Boathouse \$42,428 in additional license fees, plus interest and penalties. Parks should ensure that the Boathouse pay compensating use tax on the cost of the provisions used to provide the complimentary meals and employee meals.

Parks Response: In its response, Parks stated:

“Parks agreed with the portion of recommendation 20 that requires the Boathouse to report the value of meals provided to its employees and which the employees were charged for in the form of a payroll deduction. The Boathouse must pay \$9,628 (inclusive of interest) under recommendation 20, and another \$3,899 (inclusive of interest) for recommendation 24, representing the unreported amount of employee meals.

“Parks does not agree with the portion of recommendations 20 through 24 that represents an assessment for unreported complimentary meals that we consider to represent a cost to the Boathouse to conduct and promote its business.”

Boathouse Response: The Boathouse attorney disagreed with the auditors’ findings that the value of meals provided to its employees and the value of complimentary meals to customers are required to be included in the total Gross Receipts.

The Boathouse attorney stated in regards to employee meals, “Providing employees with meals is a standard practice throughout the restaurant and food service industry. Indeed, applicable Labor Law provisions permit restaurants to charge employees a nominal amount (up to \$2.00 per meal in 2006), which can be offset against labor costs. . . . Accordingly, the value of such meal is not deemed a sale in the normal course of business, but rather, a reduction of labor costs, and thus, should not be included in Gross Receipts. Meals provided as a courtesy to employees does not meet the defined criteria of ‘Gross Receipt’ under the terms of the License Agreement.”

In regards to complimentary meals, the attorney stated that “the Boathouse contends that such complimentary meals are not only common in the restaurant industry, but are integral to the restaurant’s business development and financial growth, which, of course, only serves to benefit Parks as well. Likewise, it is common that such meals are typically treated as a discounting of sales price.”

The Boathouse's attorney further stated that the Boathouse's position is supported by an Advisory Opinion of the New York State Commissioner of Finance, which notes that when a restaurant provides a beverage in conjunction with the sale of a meal or a beverage at no extra charge, the sales tax is to be computed on the actual amount paid by the customer.

In regards to recommendations 20 through 22, the Boathouse's attorney responded:

"The Boathouse disagrees with the Auditor's assessment of fees for employee meals and complimentary meals for the reasons discussed herein.

"The Boathouse similarly disagrees with the Auditor's position that employee and complimentary meals should be included in the calculation of Gross Receipts.

"Notwithstanding the inappropriate raising of the use tax issue in the Draft Report, and with reservation of rights and objections thereto, the Boathouse will confer with the J.H. Cohn Accounting and Consulting Firm for an opinion regarding the propriety of any use tax that may be applicable to the instant circumstance."

Auditor Comment: We are pleased that Parks agrees with our findings pertaining to including in gross receipts the value of meals the Boathouse provided and charged its employees in the form of a payroll deduction. In the Boathouse response, its attorney calls the charge for employee meals a reduction of payroll expense, but neglected to recognize the fact that the employee is actually paying for the meal.

With regard to complimentary meals, we continue to maintain the value of the complimentary meals should be included in gross receipts, especially due to the nature of some of the undocumented complimentary meals. On numerous occasions the Boathouse coded large dollar amounts as complimentary (between \$800 and \$2,600) without any explanation. Without documentation to substantiate the purpose for the deduction, we could not assess whether these deductions were truly for complimentary meals that would foster the restaurant's business development and financial growth, or simply a method to avoid reporting gross receipts. As stated previously, the Boathouse would not provide us with any additional information regarding these complimentary meals.

The complimentary meal amount deducted from gross receipts included deductions coded both as lost sales and complimentary meals on the daily close reports. For example, the daily close report for April 22, 2005, contained a deduction of \$2,475, coded as complimentary meals with the notation "open food." The daily close report for June 20, 2005, contained another deduction for \$2,601, coded as complimentary meals without a notation. The daily close report for August 17, 2005, contained a deduction of \$1,067, coded as a lost sale with a notation of "bike rentals." The last example is of particular

concern since for this summer day there were no bike-rental sales recorded on the daily closeout report to adjust. These are only three examples of what lead us to question the merit of the entire deduction for complimentary meals, and how this deduction relates to enhancing the business development and financial growth of the Boathouse.

The license agreement Article IV §4.7 (c) allows “the Comptroller to make reasonable projections of the amount of Gross Receipts which would have been disclosed had the required statements been furnished or the required records be maintained, based upon such extrinsic factors as the auditors deem appropriate in making such projections.” In regards to complimentary meals, the documentation the Boathouse has refused to furnish makes it reasonable for us to disallow the entire deduction and assess license fees due. We therefore maintain that the Boathouse should pay license fees on the value of complimentary meals and recommend that Parks reconsider its position on this matter.

Revenue Not Reported Accurately to Parks

The Boathouse underreported \$47,214 in catering revenue for three months on its profit-and-loss statement and its monthly report of gross receipts in 2005. The underreported revenue was incorrectly reported for the months of February, May, and June 2005. These amounts were not correctly transferred from the Boathouse computerized listing of catered events to the profit-and-loss statement and the monthly report of gross receipt submitted to Parks. As a result, the Boathouse understated gross receipts for those months and underpaid Parks a total of \$7,554 in license fees. The Boathouse controller agreed that Boathouse underreported catering revenue for the three months, but claimed that this underpayment was more than offset by a \$57,630 refund given to another patron that was also not posted to the profit-and-loss statement. We did not accept this as a compensating offset since the Boathouse could not provide adequate documentation that it had provided a refund to a patron.

At our request, the Boathouse provided prior-period documentation addressing the above issue. We identified similar errors for the three months between December 2001 and February 2002 and for the month of December 2003. During these periods, a total of \$138,774 in revenue that was reported on the profit-and-loss statement was not reported on the monthly report of gross receipts that was submitted to Parks. As a result of these errors, the Boathouse owes Parks an additional \$20,818 in license fees, plus late fees.

At the exit conference, the Boathouse provided an explanation and documentation for a \$1,500 revenue discrepancy that had been identified for May 2005. The Boathouse claimed the discrepancy resulted from a reversal of a discounted gift certificate sale that was incorrectly reported as a catering food sale. Although we agree that a gift certificate sale should not have been reflected as part of catering sales, we believe it should have been included in the monthly gross receipts report to Parks as a gift certificate sale, which it was not. As a result of this explanation, a larger issue was disclosed, namely that the Boathouse sells gift certificates and does not include the sale in the gross receipt report until the gift certificate is redeemed, which could be never. In fact, 28 of the 34 gift certificates sold in May 2005 had not been redeemed by mid-October 2006, 17 months after they were issued. These gift certificates are no longer

redeemable since according to Boathouse officials gift certificates are good for one year. Therefore, the sale of the 28 gift certificates will never be included in gross receipts.

A further analysis of the Boathouse's gift certificate schedule indicated a total of \$25,417 outstanding gift certificates issued since January 20, 2005. Of these, \$7,371 in gift certificates were not redeemed within the one-year redemption period and are no longer valid. Although these certificates generated revenue, under the current procedures, revenue associated with these gift certificates will never be included in gross receipts. The contract requires the Boathouse to include in gross receipts all sources of income realized from its operation of the licensed premises. Based on this requirement, the revenue from gift certificate sales should have been included when the gift certificates were sold.

Recommendations

The Boathouse should:

25. Pay Parks license fees totaling \$28,372 plus interest and penalties for incorrectly reporting revenue.
26. Ensure that the profit-and-loss statements and the monthly report of gross receipts accurately report gross receipts.
27. Pay Parks license fees totaling \$4,067 plus interest and penalties on the \$25,417 in gift certificate sales not previously reported.
28. Ensure that all revenue the Boathouse realized from its operation of the leased premises such as gift certificate sales be included in gross receipts when the payment is received.

Parks should:

29. Ensure that the Boathouse pays the City \$28,372, plus interest and penalties, for incorrectly reporting revenue and the \$4,067 plus interest and penalties on the \$25,417 in gift certificate sales not previously reported.
30. Require the Boathouse to provide a list of outstanding gift certificates and ensure that the Boathouse pays the City the license fees due on the unreported gift certificate sales.

Parks Response: In its response, Parks agreed with our assessment and stated that it issued a Notice to Cure requiring the Boathouse comply with the above recommendations.

Boathouse Response: In his response, the Boathouse’s attorney stated that the Boathouse agrees that it misreported catering sales totaling \$45,714. However, he did not agree that gift certificate sales should be included in gross receipts and that a prior period year-end adjustment totaling \$138,774 by the outside accounting firm should be included in gross receipts. Accordingly, the attorney’s response to the recommendations stated:

“The Boathouse will agree to pay Parks \$7,428 in licensing fees, in accordance with the terms of the License Agreement.

“The Boathouse has implemented procedures to ensure correct and accurate profit-and-loss statements and monthly reports of Gross Receipts. Proper steps will be taken to finalize the catering sales reconciliations prior to any submission to Parks.

“Based on the foregoing, the Boathouse submits that revenue is not generated by gift certificate sales, and thus, no licensing fees are due as a result thereof.

“It should be noted that gift certificate sales are not the *operation of a leased premise* as presented in the Draft Report, rather, in accordance with GAAP, they are a liability maintained on the balance sheet and not a revenue-generating item.”

Auditor Comment: The Boathouse’s refusal to include the cash received for gift certificates in gross receipts is a violation of the license agreement. The license agreement Article II §2.1 (l) (iv) states that “Gross Receipts shall include sales made for cash or credit, (credit sales shall be included in gross receipts as of the date of the sale) regardless of whether the sales are paid or uncollected.” Furthermore, it should be noted that the license agreement, not GAAP, defines what is included in gross receipts. Accordingly, we are satisfied that Parks has issued a Notice to Cure for license fees due on the sale of gift certificates in the amount assessed by the auditors.

In addition, the Boathouse was unable to provide any documentation in regards to an alleged prior period adjustment totaling \$138,774. The only information that is currently available is that the Boathouse generated \$138,774 more in revenue than was reported to Parks. Therefore, the license fees should be paid on the \$138,774 additional revenue as indicated in the Parks Notice to Cure.

Poor Controls over Gondola-Ride Sales

The Boathouse has poor controls over its gondola-ride sales. As a result, not all revenue from gondola-ride sales was included in the gross receipts.

The Boathouse operates a gondola ride on the lake adjacent to the Boathouse restaurant. Patrons generally make an advance reservation that is recorded in the gondola reservation book. On August 14, 2005, two auditors reserved a gondola ride. Prior to their ride, they observed two

separate gondola rides. Afterwards, they went on the gondola ride for a half hour. At the conclusion of their ride, the auditors paid the \$30 fee and requested a receipt. They were given a computerized receipt from the Boathouse point-of-sale system.

We then traced the August 14, 2005 gondola sales to the daily-close report and found only two gondola rides had been reported for the entire day, despite the three rides that the auditors had either observed or taken. We attempted to trace the entire month of August 2005 gondola-ride sales to the reservation book, but were told that the gondolier took the 2005 reservation book with him at the end of the season and could not find it. As a result, we were unable to review the reservation book and reconcile it to the reported gondola sales.

The Boathouse does not have controls in place to ensure that all revenue generated from gondola-ride sales are reported in the gross receipts. By allowing the gondolier to take official records home, the licensee eliminated the checks and balances that were in place that could ensure that all sales have been recorded and deposited.

Recommendations

The Boathouse should:

31. Ensure that there are adequate controls to ensure that all gondola-ride sales are recorded and reconciled to the reservations made. This would include ensuring that the reservation book remains at the Boathouse at all times.
32. Reconcile the reservation book to the daily gondola receipts detailed in the daily-close reports to ensure that all gondola rides are accounted for.

Parks should:

33. Ensure that the Boathouse has adequate controls over its gondola-ride sales.

Parks Response: In its response, Parks agreed with our assessment and stated that it issued a Notice to Cure requiring the Boathouse comply with the above recommendations.

Boathouse Response: In his response, the Boathouse's attorney stated: "The Boathouse will take appropriate measures to properly secure the reservation book, and will establish a written protocol governing the reservations, the recording and sales of the gondola rides, and providing for the proper reconciliation of the reservation book to sales posted. It is anticipated that such protocol will be in force prior to the start of the 2007 season."

Noncompliance with Miscellaneous Contract Provisions

The Boathouse did not adhere to certain contract provisions. Specifically, the Boathouse did not operate a Park Activity and Resource Center and did not display a sign posting operating days and hours. The only sign we observed that was posted in the front of the restaurant was the menu that listed lunch, dinner, and brunch prices.

According to contract agreement Article IX, Operations, §9.1 (g), the Boathouse must “operate a Park Activity & Resource Center that will house information and materials pertaining to Loeb Boathouse and Central Park as well as serve as an informal meeting space for groups and organizations that frequently hold events in Central Park.” Further, §9.5 states that “Licensee shall, at its sole cost and expense, print, frame, and prominently display in a place and manner designated by Commissioner, the current approved schedule of operating days, hours, fees and rates.”

Recommendations

34. The Boathouse should comply with the contract provisions that require it to operate a Park Activity and Resource Center and display the operating days and hours.
35. Parks should ensure that the Boathouse complies with all contract provisions.

Parks Response: In its response, Parks stated that “the Boathouse already provides an informal meeting area for groups and organizations and is in the process of implementing a computerized information center about the Loeb Boathouse and Central Park.”

Boathouse Response: In his response, the Boathouse’s attorney stated: “The Boathouse will continue, as it has in the past, to take all steps necessary to comply with the License Agreement.”

Other Issues

Password Access to Point-of-Sale System Not Adequately Safeguarded

Our Information Technology unit reviewed the Boathouse computerized point-of-sale system and found that “the software package possesses adequate controls, if utilized properly, to ensure complete, accurate, and reliable information as needed for the Boathouse Restaurant operation.” However, the Boathouse needs to improve its password controls over access to the point-of-sale system. Specifically, the Boathouse did not implement a procedure to change employee passwords periodically; did not delete from its point-of-sale system password accounts for inactive and terminated employees; and did not maintain a written policy for its employees to protect the integrity of their passwords.

Changing passwords periodically and deleting inactive password accounts are important safeguards to prevent any unauthorized access.

Recommendation

36. The Boathouse should implement a procedure to periodically change employee passwords and delete inactive user accounts from the system as well as maintain a written policy for its employees to protect the integrity of their passwords.

Parks Response: In its response, Parks stated: “The Boathouse should implement the procedures suggested in recommendation 36 to provide important safeguards to prevent any unauthorized access.”

Boathouse Response: In his response, the Boathouse’s attorney stated: “The Boathouse will investigate and research the current software and R-Power system with its technology consultant to ensure that adequate account controls and safeguards are established.”