



CITY OF SAN ANTONIO

P.O. BOX 839966
SAN ANTONIO, TEXAS 78283-3966

June 13, 2005

Roger Flores
Councilman, District 1

Sheila D. McNeil
Councilman, District 2

Roland Gutierrez
Councilman, District 3

Patti Radle
Councilwoman, District 5

Enrique Barrera
Councilman, District 6

Chip Haass
Councilman, District 10

Ladies and Gentlemen:

RE: Final Audit Report - The Downtown San Antonio River Boats and Barges Concession Contract

This audit report was distributed to the Governance Committee over the weekend. Attached for your review and information are the transmittal letter and final report. An executive summary of the audit results has been developed as the transmittal letter to the Committee. The final report provides an overview about the audit and the high level conclusions, pages 3 through 10. A table of contents, page 2, serves as a guide for the report and provides summary captions for the audit issues identified.

The audit team wants the Mayor and City Council to know that City Management and Staff as well as the Contractor, Rio San Antonio Cruises, cooperated fully on this project. The report includes their responses which were viewed as positive commitments to implement process changes and improvements. Some follow up is required by City Staff to obtain required recoveries as well as a release from claims from the Contractor.

The Internal Audit Department is available to discuss the details of this report with you at your individual convenience. This project involved reviewing processes that are critical financially and publicly to the City. We appreciated being able to perform this audit and to offer recommendations that can make a difference in the future.

Sincerely,

Patricia M. Major CPA, CIA, CTP, CGFM
City Internal Auditor
(210) 207-2853 office; (210) 215-9455 cell

cc: J Rolando Bono, Interim City Manager
Martha Sepeda, Interim City Attorney
Leticia Vacek, City Clerk
Christopher Brady, Assistant City Manager
Melissa Byrne Vossmer, Assistant City Manager
Erik Walsh, Assistant to the City Manager
Rio San Antonio Cruises, Mrs. JoAnn Boone, President
Central Library Branch



CITY OF SAN ANTONIO
INTERNAL AUDIT DEPARTMENT

Parks & Recreation Department

**Audit of Downtown San Antonio River Boats
and Barges Concession Contract**

Project No. AU005-003

Report Date: December 23, 2004
(Fieldwork Completion Date)

Release Date: June 10, 2005

Patricia M. Major CPA, CIA, CTP, CGFM
Mike Ketterman, CPA
Stephanie Garza

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Background

An audit of the Boats and Barges Concession Contract was included in the Fiscal Year 2005 Audit Plan due to the significance of the overall revenue to the Contractor, concession commissions to the City, and the significant audit findings by the Office of Internal Review in 2000 and 2001. Total 2003 revenue of the Contractor was approximately \$7.4 million per its external auditor's attestation. The revenue was primarily comprised of cruise tickets with a lesser amount relating to photography. The City's commissions according to the same report were \$3.2 million. The primary finding from the Office of Internal Review in 2000 was that the City did not receive commissions on photography revenue. Various audit findings amounted to approximately \$1.3 million over a number of years.

The public's access to boat tours of the San Antonio River has been a significant aspect of the City's visitor market. The City has utilized a contracted concessionaire to be responsible for the provision of boats, staff and services since the river tours began. The City in turn has received substantial revenue for this public service contract.

From 1968 (HemisFair '68) to 1985, Paseo Del Rio Boats (Casa Rio Restaurant) operated a barge concession through agreements with the Parks and Recreation Department. In 1985, the City issued a RFP, and the City Council selected Paseo Del Rio Boats as concessionaire for a 10-year term. In late 1994, the City issued another RFP for the Boats and Barges Concession. In March 1995, the City Council selected Yanaguana Cruises, Inc. for a 10-year term. The Contract with Yanaguana Cruises, Inc. (YCI) was effective from September 1, 1995 to August 31, 2005. The agreement has been amended twice:

- ✚ Amendment No. 1: October 1, 1997. Increased cruise fees, revised the guaranteed minimum to City and established a merchandise commission to City of 15 percent.
- ✚ Amendment No. 2: November 9, 2000. Resolved litigation between YCI and the City regarding audit findings about photography sales revenue, and a libel claim by YCI. It also:
 - Increased the City's commission from 49 to 51 percent exclusive of merchandise and photography.
 - Allowed YCI to control all photography, and to remit commissions to the City on a sliding scale beginning at 12.5 and ending at 16.5 percent.
 - Established photography operating procedures, including customers' acquiescence.
 - Maintained a 15 percent commission to the City on merchandise sales.
 - Established \$300,000 in scholarships during remainder of the contract to be administered at City's discretion.
 - Clarified other operating conditions: Defined Adjusted Gross Sales, Addressed Assignment and Sub-letting, Repairs at the Nueva St. Marina, Emergency Relocation of Ticket Locations.

YCI changed ownership in November 2002. YCI now has one principle owner, who actively participates in the daily operations. YCI changed its operating name to Rio San Antonio Cruises, though the corporation remained Yanaguana Cruises, Inc.

Other City Council Actions were as follows:

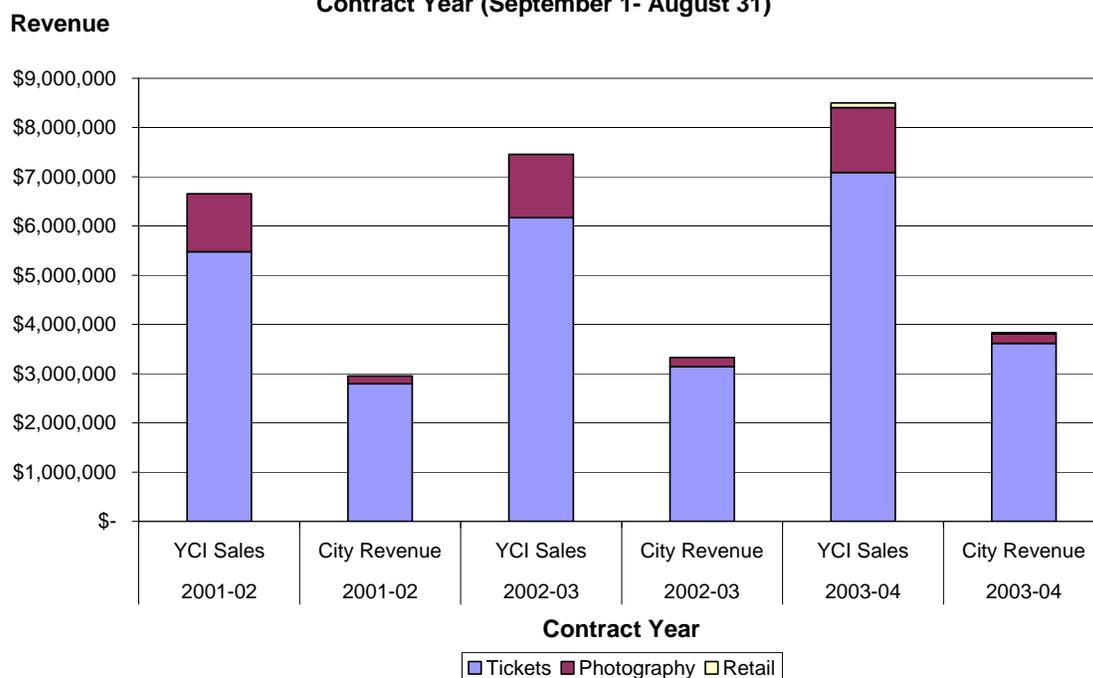
- ✚ Approval of Presidio Plaza Ticket Station - June 6, 2002, City Council authorized an additional ticket and boarding location.
- ✚ YCI Pricing Adjustments - April 3, 2003 City Council approved YCI request to moderately increase ticket prices in two phases: (1) Phase I Effective April 15, 2003; (2) Phase II Effective March 1, 2004.
- ✚ Approved River Taxi Locations.

- ✚ Rio San Antonio Cruises was authorized to provide:
 - Barges and Taxis (up to 40 boats) with ticket sales at up to four approved locations: (1) Historia (Hilton), (2) Clearwater (Rivercenter), (3) Presidio Plaza (no longer utilized), and (4) Holiday Inn (North Channel).
 - Dining and Cocktail Charters (minimum 10 barges).
 - River Taxi Service (minimum 2 barges).
 - Photography Sales at ticket locations.
 - Merchandise at ticket locations.

River barges are generally operated from the Nueva Street Marina (Marina); and the International Center Marina provided additional, but limited, storage capacity. Compressed natural gas (CNG) powers the river barges. The City has provided fuel at cost to the Contractor's river barge fleet from the City-owned CNG compressor station at the Marina. In addition to slips for river barge storage, the Marina includes a paint booth, space for maintenance and repair, and office space that has been provided to the Contractor in consideration of the annual payment to the City. Office utility expenses are shared on a prorated basis.

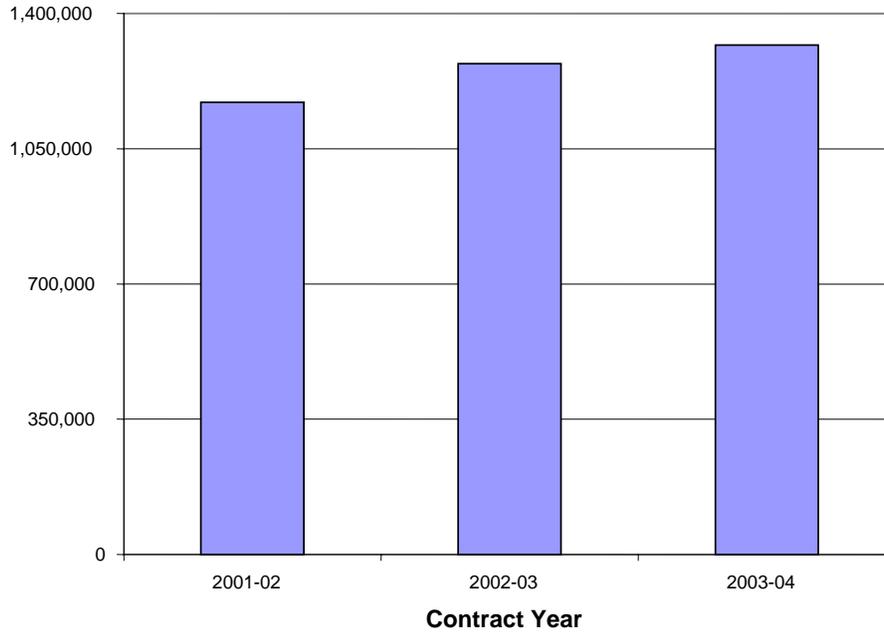
Revenue to the City from the boats and barges concession contract has generally increased over the past three years, as shown below. The last two contract years represent City revenue since YCI changed ownership. Revenue increases in 2002-2003 and 2003-2004 were partially attributable to ticket price increases included in Ordinance 97413 which became effective April 15, 2003 (Phase 1) and March 1, 2004 (Phase 2). Greater photography commissions to the City were partially attributable to escalators beginning January 1, 2002 to 13.5 percent and continuing through 2005 by 1 percent on January 1 per Amendment No. 2 to the original contract (effective December 2000). The photography commission rate as of January 1, 2005 is 16.5 percent.

Financial Summary
YCI Sales and City Revenue
Contract Year (September 1- August 31)

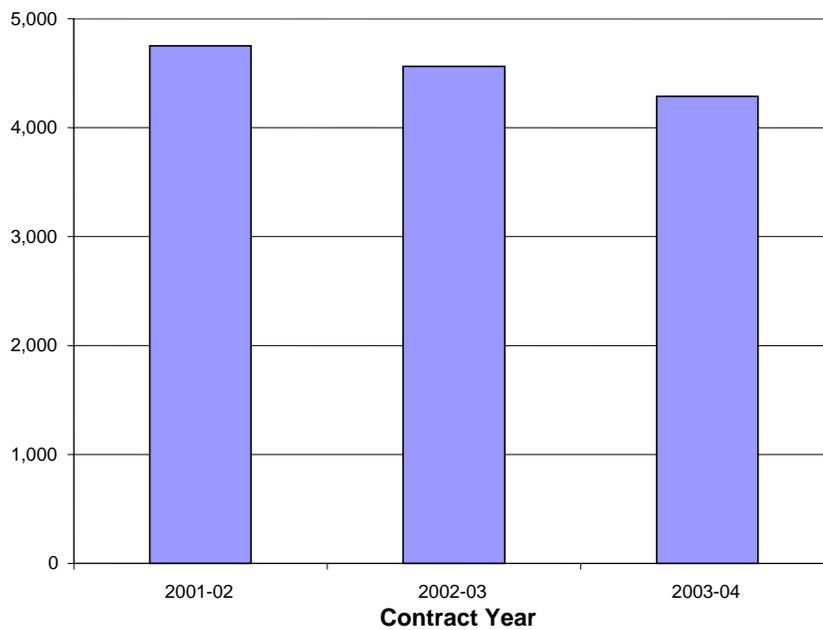


The number of tickets sold each year for boat and barge cruises has generally increased while the number of charter and dinner cruises has slightly decreased over the past three years as shown below:

Tickets Sold for Boat and Barge Cruises

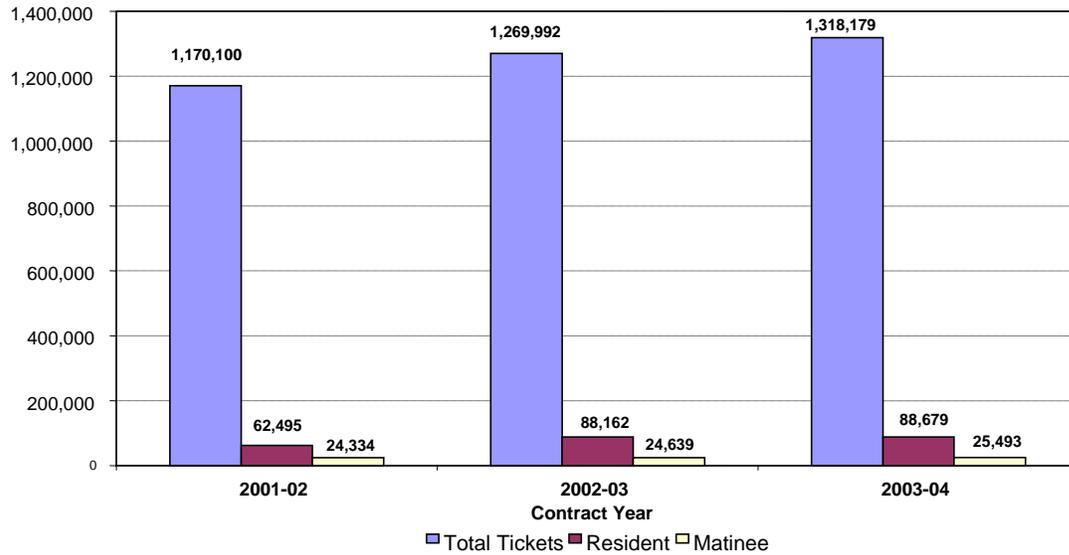


Number of Charter and Dinner Cruises

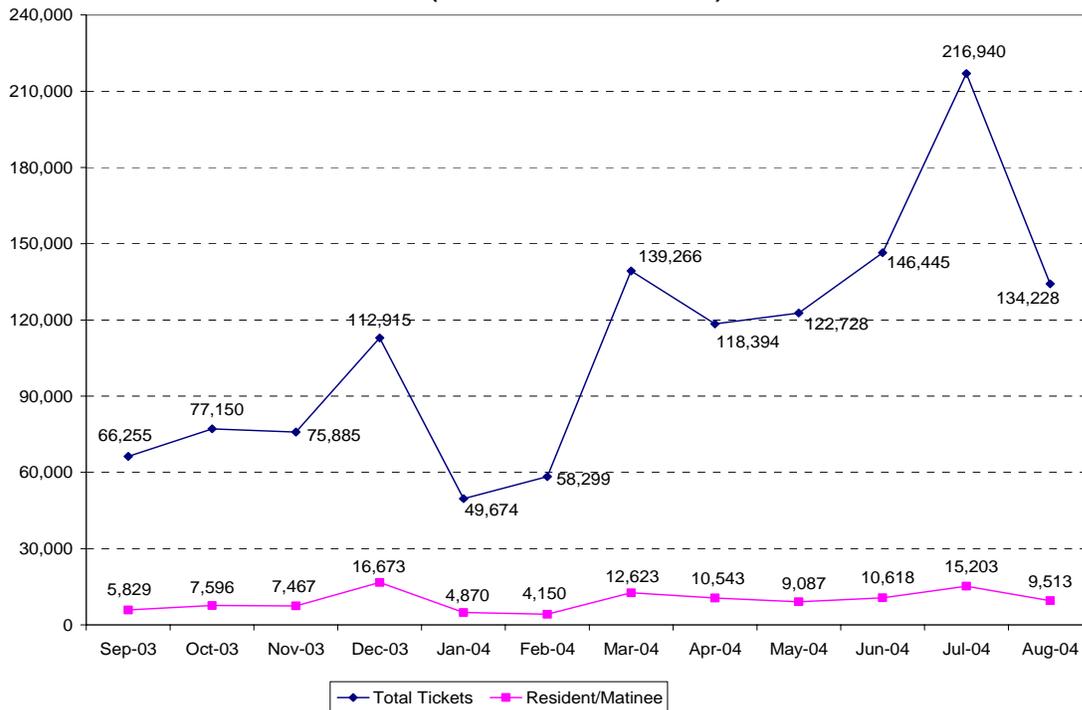


The graphs that follow show the tickets sold for resident and matinee categories as compared to total tickets sold. The audit team observed that tickets sales for resident and matinee boat rides were low compared to total sales. Refer to finding 7, Resident Ticket Sales for more detailed information.

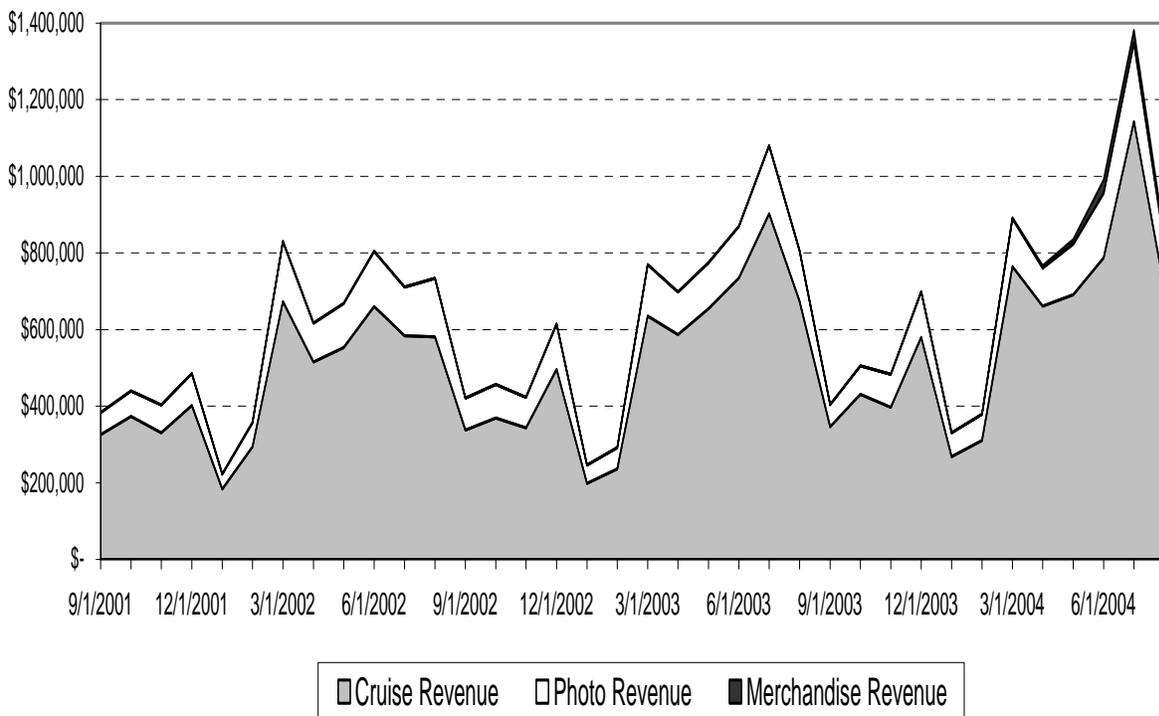
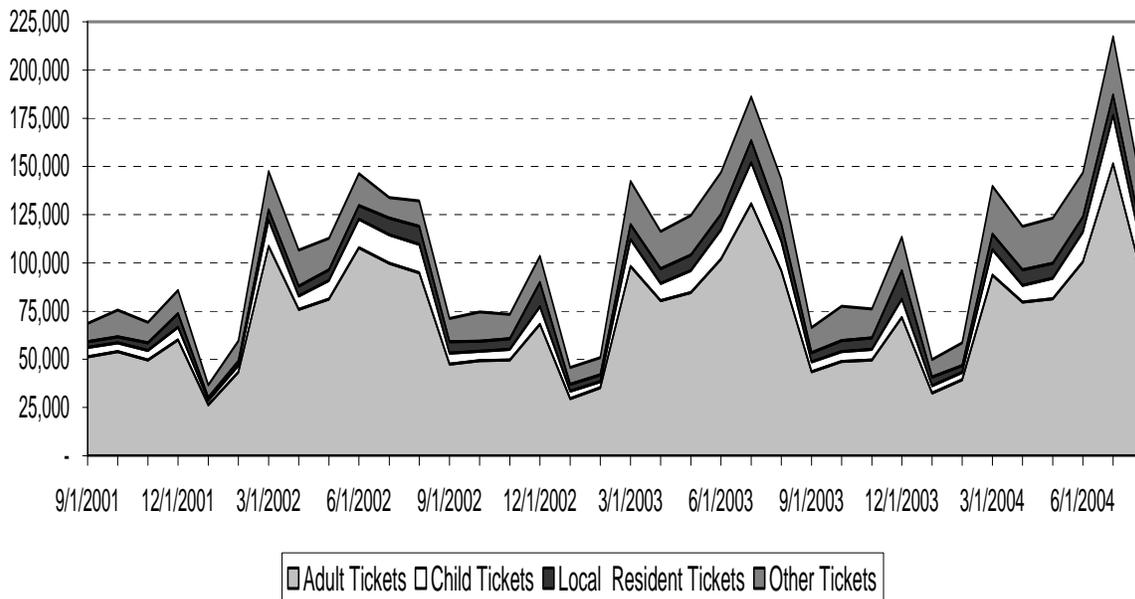
**Total Tickets Sold
 Compared To
 Resident And Matinee
 (Excludes Child and Senior)**



**Total Tickets Sold
 Compared To
 Resident and Matinee
 (Excludes Child and Senior)**



Ticket Sales Transactions and Revenue



On June 14, 2004, a Request for Proposal (RFP) was released to select an operator for a new concession contract since the current license agreement expires on August 31, 2005. On September 20, 2004, the RFP closed and responses were received from the following five companies:

- ✚ Fiesta Del Rio
- ✚ Yanaganua Cruises, Inc., dba Rio San Antonio Cruises
- ✚ Ripley Entertainment
- ✚ River Walk Cruises
- ✚ Selrico Services Inc.

On November 18, 2004 the City Council approved Ordinance 99974, unanimously selecting Rio San Antonio Cruises to operate the San Antonio River Boat and Barge Concession upon expiration of the current license agreement in Summer 2005. The Ordinance also gave authorization for the Interim City Manager or his designee to enter into contract negotiations with Rio San Antonio Cruises. The resulting negotiated contract shall be brought back to the City Council for final approval in early 2005

Objective

The audit was designed to address the following objectives:

- ✚ Determine if the City of San Antonio received commissions from Yanaguana, now known as Rio San Antonio Cruises, in accordance with the agreement.
- ✚ Evaluate whether Rio San Antonio Cruises complied with significant non-financial requirements of the current agreement, and that the Parks and Recreation Department monitored these.
- ✚ Determine that adequate internal controls were in place and functioning as intended for both Rio San Antonio Cruises and the City with regard to accumulating, calculating, and reviewing sales underlying the monthly commission payments.
- ✚ A high level comparison of State sales tax data with revenue reported to the City.

Criteria

This audit was performed in compliance with generally accepted government auditing standards (GAGAS) by the U.S. Government Accountability Office (GAO) and other criteria to conform with The Institute of Internal Auditors' "International Standards for the Professional Practice of Internal Auditing." The program and procedures used for this review would provide City Executive Management with reasonable but not absolute assurance about the Contractor's compliance with the agreement, and the effectiveness of internal controls employed by the City and by the Contractor for this concession.

Government Auditing Standards "Quality Control and Assurance" Section 3.52, issued by the Comptroller General of the U.S., states: "Audit organizations performing audits and attestation engagements in accordance with GAGAS should have an external peer review of their auditing and attestation engagement practices at least once every three years by reviewers independent of the audit organization being reviewed". The City Internal Audit Department (CIAD) had its last external peer review in July 2001. CIAD is scheduled for the next peer review in Summer 2005.

Scope and Methodology

The authority for this review and access to YCI's records was contained in Amendment No. 2 to the Downtown San Antonio Boats and Barges Concession Contract, Article XXIX, Section 29.5 of the contract which states, "All applicable records and accounts of CONTRACTOR, together with all supporting documentation, shall be preserved in Bexar County, Texas, by CONTRACTOR for thirty-six (36) months after the termination of this CONTRACT. CITY, if it elects, may require that any or all of such records and accounts be submitted for audit. If so, CITY shall notify CONTRACTOR, who shall either agree that such audit be conducted by the CITY's Office of Internal Review, or, at its sole discretion, require that such audit be conducted by an independent auditor."

The audit included the period of September 1, 2003 through October 31, 2004. This was a normal contract year of September 1, 2003 through August 31, 2004 in addition to the most recent period of activity. In the event that there were significant financial findings, controls were not deemed adequate, or analytical procedures suggested questionable matters, the audit could have extended back to September 2001. Only significant financial and non-financial contractual requirements as determined by the Office of the City Auditor were considered. Methods used in this project included:

- # Examine the concession agreement and related documents.
- # Perform and document a walkthrough of significant Rio San Antonio Cruises operations and perform a risk assessment to determine the required audit procedures.
- # Perform analytical procedures of revenue, ticket data, sales tax returns, bank statement activity, and related items over the past three years.
- # Perform an observation of Rio's ticket count at the end of October and agree it to the monthly statement.
- # Perform a rollback of ticket transactions and examine activity on a test basis.
- # Select a sample of days to verify that revenue were properly deposited and reported on the City statement.
- # Review missing photography prints and analyze merchandise sales compared to purchases.
- # Review monthly revenue and Adjusted Gross Sales (AGS) reports and determine their completeness and correctness.
- # Review the annual "statement of attestation" of commission revenue paid to the City by Rio San Antonio's external CPA and the work performed to support their attestation.
- # Consider the results of prior procedures performed by the prior Office of Internal Review.
- # Generate suggestions for a stronger control environment as applicable based upon the risk assessment and other audit procedures.
- # Inquiries/interviews with Rio San Antonio Cruises and the Parks and Recreation Department.

Conclusion

Generally, the Boats and Barges Concession Contract requirements were being fulfilled. The current management of Rio San Antonio Cruises actively participates in the daily operations of the company. It was noted that since the last audit of this contract in February 2000 and a review in April 2001, significant improvements have been made in the area of ticket inventory controls and reporting methods to the City. In addition, overall concession commissions have increased over the past three years. Internal controls have been established to provide reasonable assurance that contract requirements are met; however, it was noted some of these controls are not functioning as intended.

CONTRACTOR

- ✚ Rio Cruises has limited staffing which can create difficulty in establishing proper segregation of duties. Some duties are performed by the Director of Management Information Systems, which should be distributed to other personnel or reviewed by management. A summary of the Director's conflicting duties included:
 - Overall access to the information system including transaction data and report generation.
 - Issuing taxi tickets to supervisors for distribution to cashiers.
 - Reconciling ticket usage at month-end.
 - Making reservations/selling tickets.
 - Collecting payments.

- ✚ During the past four years, \$23.392 million in proceeds have been collected; this amount includes sales tax. Rio San Antonio Cruises does not state the amount of sales tax for each transaction on its receipts or tickets; nor is a statement made such as "all sales tax included" on its tickets/receipts. Rio San Antonio Cruises began implementing ticket/receipt and signage changes regarding this issue in November 2004 based on audit discussion.

As a matter of public policy, audit staff recommends that Rio continue to implement a process where all receipts for tickets, merchandise, or photographs either state separately the amount of sales tax collected or a statement including "all sales tax included." This would provide appropriate notification to all customers of sales tax amounts.

It is recommended that the City of San Antonio obtain a formal claim release for any commission refunds that might result from future audits by the State Comptroller's Office relating to sales tax pertaining to this audit issue for this contract.

PARKS AND RECREATION DEPARTMENT

- ✚ No formalized City monitoring plan is in place for the current contract. A plan should be created identifying specific financial and non-financial contract terms. This was consistent with the 2000 audit recommendation. Formal monitoring can ensure that the Contractor is performing as expected, and that the City is meeting its requirements as well. Contract monitoring should be documented, and the results given to the City Management Executive Team and the Finance Department at least quarterly for review due to the high profile nature of this contract.

RIO SAN ANTONIO CRUISES (Rio)

1. State Sales Tax Separately On Tickets And Receipts

For the audit period, Rio did not state the amount of sales tax on its tickets or on its receipts for photography or merchandise. Nor did the customer copy include a statement such as "all sales tax included." Audit staff observed and documented signage at the two ticket booths which included the "sales tax included" statement. During the audit, a comparison was made of the revenue reported to the State for gross receipts and taxable revenue purposes.

Observation

The Contract with Rio required that the City Council consider and approve all ticket price increases prior to implementation. As a general rule, the Contractor works with City Parks Department Management to present a schedule of ticket pricing that has been easy to understand and administer with the public. Part of this strategy, was to use pricing with increments of twenty-five cents beginning in spring 2003. On April 3, 2003, City Council approved revised rate changes in two phases for the Contractor. Exhibits 1 and 2 submitted by City Staff provided the current and recommended ticket pricing and the impact on commissions to the City based upon the prospective ticket prices.

Ordinance 97413 dated April 3, 2003 did not grant the Contractor authority to charge customers sales tax above the scheduled ticket prices. Exhibit 2 of the agenda item documentation presented the Parks Department methodology for determining the commissionable revenue per ticket transaction. City Staff's calculations appeared consistent with the Texas Tax Code Section 151.416 "Commingled Receipts And Tax" and Title 34 of the Texas Administrative Code, Rule 3.286 (d) (3), "Seller's And Purchaser's Responsibilities."

The Contractor was uncertain about practices used prior to 2003 for tickets, receipts and signage. It appeared that Rio had been paying its sales tax based upon daily aggregation of receipts. It paid sales tax based upon the net amount rather than the face value of the ticket prices.

Audit staff believed that Rio may be required to pay sales tax on the face value of tickets, photographs, and merchandise sold where the customer's receipt does not have the printed "sales tax included". Ordinance exhibits appear to support this view. This determination is also based on Title 34, Texas Administrative Code, Rule 3.286 (d) (3), "Seller's and Purchaser's Responsibilities."

Once this matter was brought to the attention of Rio Management, they immediately took action, and in November of 2004 started printing on tickets that "all sales taxes are included". Management is also currently evaluating a plan to have taxes printed on Point of Sale System (POS) receipts for merchandise and photography. As of report date this was still pending completion. In addition, Rio Management spoke with the State Comptroller's Office to obtain clarification of this matter. The Tax Policy Division provided a response to Rio which it shared with the auditors.

Risk

The amount of revenue during the four years audited totaled \$23.3 million. The audit staff's interpretation of the tax and taxable revenue methodology equated to a difference of about two cents per ticket sold during the four year period. The risk to COSA would be the Contractor reclaiming commissions paid of roughly \$60,000 for the four-year period. This could potentially occur due to a State audit reporting sales and taxes.

The Contractor attempted to obtain clarification from the State Comptroller's Office. The Contractor feels comfortable about their communication with the State regarding the current reported and payment procedures. However, potential risk to the City may still exist since the State Comptroller has not performed an audit of the Contractor's records since 1996-97 and rendered an official audit opinion about this matter.

Recommendation

As a matter of public policy, audit staff recommends that Rio continue to implement a process where all receipts for tickets, merchandise, or photographs either state separately the amount of sales tax collected or a statement including "all sales tax included." This would provide appropriate notification to all facility users of sales tax amounts.

It is recommended that the City of San Antonio obtain a formal claim release for any commission refunds that might result from future audits by the State Comptroller's Office relating to sales tax pertaining to this audit issue for this contract.

Contractor - Rio San Antonio Cruises Response dated June 8, 2005

The Company has complied fully with all state reporting requirements. It is the opinion of Rio San Antonio Cruises, that the City's interpretation of state sales tax rule 3.286 is incorrect. Support for our position is supplied directly from the state of Texas Audit Policy Division. We have attached a copy (see next page) of the formal response from Joseph Mancuso from the Tax Policy Division of the State Comptroller's Office.

Management will continue to print the all sale tax included statement on the tickets, even though not required.

Rio San Antonio Cruises agrees to sign a formal claim release relating to this issue.

Responsible Party for Implementation

Ben Lira (Director of Finance)

Implementation Date

Currently implemented

Email Attachment

January 31, 2005

From: Joseph Mancuso, Tax Policy Division

To: Timothy D. Gilliam [Tim@gilliamcpapc.com]

Thank you for your follow-up to the original tax help inquiry (#04349594) dated January 14, 2005 (copy attached). This follow-up is in response to our request for more information dated January 18, 2005 (copy attached), whereby you have provided an amendment to the contract signed by the City Manager of San Antonio.

In connection with the above, there was a January 27th and 31st, 2005 telephone communication during which you refined your request to help expedite our response as follows: "You asked as a for profit Company operating as a direct (vs. reseller) provider of amusement services under a contract with the City of San Antonio with a Texas sales tax permit, if the phrase 'sales tax is included' is required to be stated on the face of the ticket in order for sales tax to be excluded from the amounts reported as gross sales and taxable sales."

Response:

Sales Tax Rule §3.286(d)(3) provides that the amount of the sales tax must be separately stated on the bill, contract, or invoice to the customer or there must be a written statement to the customer that the stated price includes sales or use taxes. Contracts, bills, or invoices that merely state that "all taxes" are included are not specific enough to relieve either party to the transaction of its sales and use tax responsibilities. The total amount that is shown on such documents is presumed to be the taxable item's sales price, without tax included. The seller or customer may overcome the presumption by using the seller's records to show that tax was included in the sales price.

You have provided a copy of the contract amendment signed by City Manager of San Antonio that lists the various prices for the amusement services that your company provides, and also contains the phrase "includes sales tax." You also represent that the sales tax collection and reporting is consistent with this contract, and that gross and taxable sales amounts were calculated and reported by reducing the gross receipts collected, only by the amount of the appropriate sales tax. Finally you have represented that a sign is displayed outside the ticket booth that states "sales tax is included."

Based on the facts presented, the requirement referenced above per Sales Tax Rule §3.286(d)(3), i.e. that the seller's records show that tax was included in the sales price, appears to be satisfied. Therefore, the phrase "sales tax is included" does not appear to be required to be stated on the face of the amusement tickets in order for you to exclude sales tax from the amounts reported as gross sales and taxable sales.

This opinion is based on the facts presented. Additional or different facts may yield different results.

If you need any additional information or have any questions my internet address is joseph.mancuso@cpa.state.tx.us, or you may call me at 1-800-531-5441, extension 54653.

Our goal is to provide you with prompt, professional service. Please take a moment to complete our on-line survey at <http://aixtcp.cpa.state.tx.us/surveys/tpsuvr/>.

Sincerely,

Joseph Mancuso
Tax Policy Division

2. Underpayment Of Commissions To The City

Observation

CIAD audit and review procedures noted the following instances where commissions to COSA were potentially underpaid.

2.1 Advertising Revenue Deductions

Rio deducted all ticket-printing costs from its advertising revenue for the purpose of calculating the City's commission rather than subtracting the costs of printing just the advertising on the tickets. The deduction was not made until the 2003-2004 contract year-end CPA attestation of the revenue. The effect was \$8,236 being deducted from the October 2004 commission paid to the City.

2.2 Unearned Revenue Adjustment

The August 2002 report to the City excluded an adjustment of \$2,178 to Rio's unearned revenue general ledger account. The unearned revenue account is generally used to track deposits or advance payments for future charter reservations. The adjustment was recorded to miscellaneous income, but was excluded from the report to COSA. Rio is unable to support the nature of the journal entry but it likely represents a balancing of the unearned revenue deposited with Rio for a cruise already taken but not otherwise recorded.

2.3 Mail Order Income

Mail order reprint income was not included as revenue in the COSA Monthly Photography Sales Report for eight months during the period September 2001 through September 2004. Revenue totaling \$1,965 was not reported with the COSA commission shortage amounting to \$245. Amendment #2 Section 45.1 to the contract states in part, "Photography Services consist of photographs of Contactor's passengers in the process of boarding, riding or immediately departing its tour boats, dining charters and charter tours and sell Paper Prints of those photographs." Mail order reprint income is deemed part of the photography services provided by Rio and is subject to commission.

2.4 Water Sales Tax Deductions

COSA is paid a commission on the sale of merchandise at the rate of 15 percent of the price less sales tax. Water is not a taxable item based on Texas Tax Publication 96-280, "What is Taxable at Grocery and Convenience Stores," January 2001. Sales tax, however, has been paid to the State of Texas, and deducted in the City's commission calculation.

2.5 Merchandise Sales Tracking

Rio uses a simple register for its merchandise sales. At times, reports run from the POS are inaccurate due to the wrong type of report being run by the supervisor to summarize daily sales. The daily sales reports are typically used to determine the commissionable revenue to the City. When the reports are incorrect, Rio utilizes hash marks recorded on a piece of paper by the cashier for sales throughout the day to determine what the sales report should reflect.

Risk

2.1 The 2003-2004 contract year is the first time that ticket-printing costs have been deducted from the advertising revenue. COSA is absorbing the full versus incremental costs which is de minimis.

2.2 Adjustments to the unearned revenue account could be the result of balancing the account for a cruise already taken but not otherwise recorded. The commissionable portion would be \$1,111, or 51 percent of \$2,178.

- 2.3 Commissions of \$245 are owed to COSA for the months where mail order reprint income was not included in the City statement.
- 2.4 The commission on water has historically had sales tax deducted from it resulting in lower commissions paid to COSA. The effect from audit date is estimated to be \$120 as merchandise sales began in March 2004 and have gradually increased in volume. The effect in future reporting periods could be more significant.
- 2.5 As the POS reports are run correctly the vast majority of the time, the effect of this condition is not that significant. The effect for the six months of the 2003-2004 contract year that merchandise was sold is estimated to be \$100. As merchandise sales increase this could become more significant. This practice was also noted during the CPA attestation of revenue. The October 2004 commission statement from Rio has been adjusted to reflect this and other differences noted from the attestation.

Recommendation

In summary, Rio should pay COSA \$9,256 as noted below, and otherwise change its practices to ensure proper calculation of revenue and commissions in the future.

- 2.1 The incremental cost of printing advertisements on the back of tickets is very small, therefore, commissions of \$8,236 should be returned to the City.
- 2.2 As neither Rio nor CIAD is able to determine the exact nature of the transaction, splitting of the amount is deemed appropriate; therefore \$555 or fifty percent of \$1,111 would be the amount due to the City.
- 2.3 Rio should pay COSA the commission due from mail order reprint income in the amount of \$245. No recommendations are made relating to the reporting process as Rio has made timely commission payments for mail order reprint income for the past year.
- 2.4 Rio should immediately cease collecting tax on water and ensure that COSA is receiving commission based on the gross price of water. An estimate of commissions for this issue was calculated at \$120.
- 2.5 When POS reports cannot be used, rely on daily deposit information. Additional training of supervisors could reduce the number of days that POS reports are run incorrectly. Testing indicated that COSA may be due \$100 for this issue.

Contractor - Rio San Antonio Cruises Response dated June 8, 2005

- 2.1 The Company believes it followed the language in Amendment No.2 paragraph 44.4 and correctly reduced advertising revenues by the cost to produce said tickets. Amendment 44.4 does not refer to an incremental cost and as such the Company believes it has fully complied with the contract.
- 2.2 This transaction occurred before the change of ownership, as such it is impossible to determine the exact nature of this adjustment.
- 2.3 This transaction occurred before the change of ownership, as such it is impossible to determine the exact nature of this adjustment.
- 2.4 The Company is in agreement with City recommendations.
- 2.5 The Company is in agreement with City recommendations

Responsible Party for Implementation

Ben Lira (Director of Finance)

Implementation Date

Immediate

Auditor's Response dated June 8, 2005

- 2.1 The cost to print advertising on the back of tickets is a de minimis incremental expense. The contract language was unclear and clarification of this was another audit issue, (See page 30).

The audit team believed that there is an issue of consistent practices. In prior years, ticket-printing costs were not deducted from advertising revenue. It appeared that this was a new interpretation that was implemented in 2004.
- 2.2 and 2.3 An unearned revenue adjustment and mail order photo reprint income that occurred before the change of ownership are potential commission liabilities that are assumed by new owners. Ownership change does not affect contract compliance.

3. Process Improvements

Observation

CIAD noted instances where Rio could improve its revenue control processes.

3.1 Merchandise Inventory Variances

Rio began selling merchandise in March 2004. Merchandise sales have expanded to both ticket locations, and they are expected to increase in the future. At the time of the audit, Rio required that each cashier count the merchandise inventory at the beginning and end of a shift and reconcile the change in inventory to the Point of Sale System (POS). Variances, however, do not appear to be investigated or documented by Rio.

3.2 Photography Print Variances

Rio tracks the number of prints/packages developed versus the number of packages sold or returned unsold to reconcile daily activity. Photography print variances exist when the machine meter reading does not match the total number of prints reportedly sent to the sales gallery. During review, it was noted that several months had high print variances, including some greater than 200, and were not easily explained by Rio Management. No documentation was noted on Rio's reconciliation to document variances. Improvements have been made in recent months with new personnel and more accurate documentation.

3.3 Dinner And Charter Cruise Refunds

For certain cancellations, such as inclement weather, Rio will issue refunds for cruises. There were instances where the check request form initiated by the reservations agent was not approved by Rio Management before payment. Refunds should be approved to prevent unauthorized or inappropriate refunds.

Risk

3.1 Inventory variances can be an indication of unrecorded sales and/or employee theft. Either situation could result in lost commissions for the City.

3.2 Unexplained photography print variances could be an indicator of lost revenue to Rio and lost commissions to COSA. It could also be an indicator of machine errors, personal use, etc. It is noteworthy; however, that Rio has other controls in place to mitigate the risk of lost revenue.

3.3 Refunds could be made inappropriately which could result in COSA not receiving commission on services that were actually performed or on deposits forfeited.

Recommendation

3.1 Inventory counts should be verified and variances explained by supervisors. Employees should be held accountable for merchandise variances.

3.2 Wasted photography prints and office printing should be documented and included in the variance calculation. Daily variances should be investigated and documented.

3.3 All check requests should be reviewed by an appropriate member of Rio Management. The nature and amount of the refund should be reviewed to ensure that the refund is appropriate and that the correct amount is being refunded to the customer.

Contractor - Rio San Antonio Cruises Response dated June 8, 2005

3.1 The Company has adopted the City recommendation as of November 2004.

3.2 The Company has adopted the City recommendation as of November 2004.

3.3 The Company has adopted the City recommendation as of November 2004.

Responsible Party for Implementation

Ben Lira (Director of Finance)

Implementation Date

Immediate

4. Segregation Of Duties

Observation

Some duties are performed by the Director of Management Information Systems which should be distributed to other personnel or reviewed by Rio Management. A summary of the Director's conflicting duties includes: overall access to the information system including transaction data and report generation, issuing taxi tickets to supervisors for distribution to cashiers, reconciling ticket usage at month end, making reservations/selling tickets, and collecting payments.

A strong control system should include, at a minimum, segregation between the authorization of transactions, recording of transactions, and custody of related assets.

Risk

Based upon the various responsibilities of the Director, a control weakness exists whereby services or money could be stolen and covered up by the Director.

Recommendation

Additional staffing, a reallocation of responsibilities, or closer supervision is recommended to ensure that a segregation exists between the IT function and control of assets (ticket stock, reservations, payments received), between report creation and control of assets, and between ticket issuance and reconciliation.

Contractor - Rio San Antonio Cruises Response dated June 8, 2005

The Company has taken action to implement additional segregation of duties as per the City recommendation.

Responsible Party for Implementation

Ben Lira (Director of Finance) / JoAnn Boone (President)

Implementation Date

Immediate

5. Point Of Sale (POS) System Issues

Observation

Through inquiry of Rio personnel, CIAD noted potential weaknesses in the current POS for charter and dinner cruise reservations. When a customer cancels a reservation close to the date of the event, a forfeiture of the deposit or other amounts paid up to that date usually occur. Commissions are paid to the City on forfeitures. When a forfeiture is recorded in the POS, the name of the customer is changed to "DEPOSIT F" so that at the end of the day, the forfeitures can be identified and formally transacted as a forfeiture in the POS.

Weaknesses noted are as follows:

- It is possible for a reservations employee to just rename the forfeiture to another customer name and apply the forfeiture to that customer.
- When a customer cancels a reservation, the reservations employee can incorrectly call a forfeiture a refund and pocket the refund.
- The determination of the percent forfeited versus refunded is solely determined by the reservations employee and not the POS system leaving room for manipulation or error.
- The system does not prevent changes to past reservations. This could enable an employee to cancel a reservation from years ago and use the credit for that reservation for current services. The POS System should include sufficient application controls to ensure that revenue and proceeds are recorded for all services performed.

Risk

All of these instances could potentially result in lost revenue from a reservations employee giving away services to another customer; by a reservations employee keeping a payment received for their own use and applying forfeitures/cancellations/refunds in its place; or by human error. Employees generally seemed unaware of their ability to perform these transactions. Very limited cash is received for payment at the main office where reservations are made; however, checks and credit card payments are received.

Recommendation

All cancellations, forfeitures and refunds recorded in the system should be flagged for Rio Management review or override. Rio should perform a study to more fully understand the risks inherent in the current POS System and make changes as needed.

Contractor - Rio San Antonio Cruises Response dated June 8, 2005

The Company is in agreement with City recommendations.

Responsible Party for Implementation

Ben Lira (Director of Finance) / JoAnn Boone (President)

Implementation Date

During 2005

6. Operational Concerns

Observation

During the course of the audit, CIAD staff became aware of operational matters which could result in the loss of business, and possibly a loss of commissions to the City.

6.1 Credit Card Acceptance During Peak Times

To reduce line waiting times, credit cards may not be taken at ticket booths at busy times. Credit card transactions take longer than cash or check transactions. Using credit cards is less risky than cash, and with proper equipment, should be encouraged.

6.2 Rio Trans Taxi Location Signage

Rio utilizes 39 taxi areas; however, only nine have signage. The signage present states that taxi boat drivers do not take cash, and tickets can be purchased at surrounding Riverwalk restaurants. This is not consistent with current Rio Trans operations as taxi drivers do take cash, and surrounding restaurants generally do not sell tickets.

6.3 Cancellation Policies For Dinner And Charter Cruises

Rio charter cancellation policies are more restrictive than the contract allows. Rio's 2003 cancellation policy provides only a 25 to 75 percent refund of the sales amount if a cancellation is made more than 30 days prior to the event. The 2004 policy states that cancellations made more than 30 days prior to the event result in a 100 percent lost deposit. A deposit is normally 25 percent of the sales amount.

Amendment 1 to the contract (Sec. 12.2) states that "Contractor is authorized to collect a full fee advance deposit on barge charter reservations. Contractor is authorized to retain such deposits on charters if the person, firm or organization booking such charter fails to release unwanted or unneeded barges at least thirty (30) days prior to the charter event. Contractor is authorized to establish deposit policies no more restrictive than those permitted under this paragraph."

Risk

6.1 During periods when credit cards are not taken, persons without cash or checks would not be able to ride. Thus, Rio and the City could lose revenue. Additionally, if customers are not informed that credit cards are not accepted prior to waiting in line, customers could be angry and leave with a bad impression of the cruise/Riverwalk/City. Less handling of cash is a better general practice for the City and Rio.

6.2 If proper signs are not presented at taxi stops, customers will not know how to use the service. Current signage would cause customers to leave the taxi stop in search of a ticket sales location which could result in lost revenue.

6.3 Rio's cancellation policy varies from the contract requirements. With the existing cancellation policy, COSA could earn higher commissions due to there being more forfeited payments. The policy could also result in lost revenue if customers see it as being too restrictive to book in advance.

Recommendation

- 6.1 Additional staffing for registers during peak times would reduce customer wait times. Optionally, having faster credit card machines could reduce wait times.
- 6.2 Taxi stops should be clearly labeled. Signage should reflect where the pickup areas are, and correct ticket purchase, and price information for the various types of taxi services available.
- 6.3 For all reservations made for the 2005 calendar year, Rio's policy will be consistent with that required by the Contract. Rio should refer to the contract requirements when implementing future operational changes. It is recommended that Rio, at least annually, review all contract requirements to ensure continued compliance.

Contractor - Rio San Antonio Cruises Response dated June 8, 2005

- 6.1 The Company has adopted the City recommendation as of November 2004.
- 6.2 The Company is in the process of adopting this recommendation.
- 6.3 The Company is in agreement with City recommendation.

Responsible Party for Implementation

Ben Lira (Director of Finance) / JoAnn Boone (President)

Implementation Date

ASAP

7. Resident Ticket Sales

Observation

During the course of the audit, CIAD staff became aware of operational matters which could result in the loss of business and thus loss of commissions to the City.

Displaying of Ticket Prices

Local resident prices are listed as "Bexar Co." and "Bexar Co. Res." at the ticket booths. Non-local resident adult prices are listed as "Regular." When any customer asks the ticket prices, the answer is usually \$6.50, the "Regular" fare. The communication of ticket prices may be unclear to customers. In addition, discounted matinee prices are not displayed, nor are they located on printed information. From September 2001 to August 2004, resident and matinee tickets combined for a total of 8.4 percent of total tickets sold. This low percentage suggests that: (1) resident customers may be paying full price for tickets; or (2) residents are not informed concerning resident prices; or (3) the utilization of this activity by resident customers is extremely low and should be promoted.

Risk

By not having all ticket options available to them, customers may be overcharged when purchasing their tickets. If customers are aware of all the prices available to them, there may be an increase in those wishing to take advantage of Rio's services, especially outside of the peak season. Resident patronage could be a source of revenue to Rio, and, in turn, greater commissions to the City.

Recommendation

Ticket prices should be displayed clearly and in a logical order. Matinee times and prices should be added to all printed and displayed material, including ticket boards, website, and brochures. The size of ticket boards might need to be increased. Contractor should look for ideas on promoting resident and matinee tickets during non-peak seasons.

Contractor - Rio San Antonio Cruises Response dated June 8, 2005

The Company is in the process of adopting this City recommendation.

Responsible Party for Implementation

Ben Lira (Director of Finance) / JoAnn Boone (President)

Implementation Date

ASAP

8. Compliance With ADA Requirements

Observation

Rio is to provide access to disabled persons and be compliant with the requirements of ADA (Americans with Disabilities Act) under Section XVI of the Contract. Additionally, as Rio is considered a public accommodation, it has compliance requirements directly with the ADA as well. CIAD performed procedures relating to ADA compliance, which were supplemented with procedures performed by the City Disability Access Office (DAO). The more significant recommendations from DAO's review are noted below.

- * Installation of wheelchair locks in addition to seatbelts on boats
- * Provide more signage / brochure information on accessible taxi stops
- * Create more taxi stops that are accessible
- * Advise customers of service limitations on dining barges
- * Tour boats should be redesigned for more inclusion of people with disabilities within general seating area

Risk

Limitations on access for disabled persons can create compliance issues with the ADA and could result in lost revenue. Additionally, if Rio were to have a publicized complaint regarding disabled access, it could negatively affect the City's image.

Recommendation

Rio should continue working with the DAO to implement its recommendations. Rio should perform and document its own study of disability access issues to demonstrate their efforts to comply with ADA requirements.

Contractor - Rio San Antonio Cruises Response dated June 8, 2005

The Company agrees to continue working with the DAO and will consider conducting additional disability access studies.

Responsible Party for Implementation

JoAnn Boone (President)

Implementation Date

During the 2005-2006 business year.

9. Trash Disposal Requirements

Observation

Rio currently disposes of ticket booth trash in the City cans at the Riverwalk, and City trash trucks near the Marina. Section 10.3 of the contract requires that "all costs of garbage and refuse collection at ticket sales stations shall be at Contractor's sole cost and expense."

Risk

The City is not collecting revenue for services provided.

Recommendation

Rio should begin paying the City for garbage disposal for ticket booths and the Marinas. The Department of Parks and Recreation could be asked to approve the current method of trash disposal.

Contractor - Rio San Antonio Cruises Response dated June 8, 2005

The Department of Parks & Recreation has approved the current method of trash disposal.

Responsible Party for Implementation

JoAnn Boone (President)

Implementation Date

Currently implemented

10. Advertising Revenue Reported As Taxable

Observation

CIAD reviewed Texas Sales and Use Tax Returns filed by Rio San Antonio Cruises. It was noted that in December 2003 Rio San Antonio Cruises included \$10,000 advertising income in its Sales and Use Tax Return. CIAD staff spoke with a Tax Analyst Specialist of the Texas State Comptroller's Office. He stated that advertising is not subject to sales and use tax. Per the Texas Tax Code, §151.0101. "Taxable Services," advertising is not listed as a taxable item.

Rio San Antonio Cruises inadvertently overstated revenue by \$10,000 for December 2003 on its monthly filing of the Texas Sales and Use Tax Returns to the Comptroller of Public Accounts.

Risk

Rio Management should ensure that staff has proper knowledge of sales tax reporting to detect errors and/or omissions, which could result in the City benefiting in the local sales tax portion. Such errors could potentially impact the City's commission if not detected by Rio Management. The effect of Rio San Antonio Cruises including advertising as an item on its Texas Sales and Use Tax Returns is an overpayment of taxes in the amount of \$788 to the State of Texas.

Recommendation

This specific error had no effect on the commissions or contract compliance. Training on sales tax regulations and Rio Management's review of monthly reporting is recommended to prevent and detect future errors.

Contractor - Rio San Antonio Cruises Response dated June 8, 2005

The Company agrees with the City's recommendation. Accounting staff will receive training on sales tax regulations.

Responsible Party for Implementation

JoAnn Boone (President)

Implementation Date

As soon as practical.

11. Timely Updates To Point Of Sale System (POS)

Observation

The POS includes the net sales price and tax for the total ticket/cruise price. Reports from the POS are used to report commissionable revenue net of sales tax to the City. The tax rate changed from 7.875 to 7.75 percent in July 2004; however, Rio did not fully change all rates in the POS. Tax rate changes should be entered timely and accurately.

Risk

The July 2004 tax rate change was partially updated in August 2004, and fully updated in October 2004. The August error was corrected on the September 2004 City Commission Statement. The September error was not corrected on the statement. The estimated effect is less than \$30. This illustrates that a systematic error such as this could continue without being detected.

Recommendation

Review of changes made to the POS System should be performed by Rio Management after events, such as tax rates, or ticket pricing.

Contractor - Rio San Antonio Cruises Response dated June 8, 2005

The Company agrees with the City's recommendations.

Responsible Party for Implementation

Ben Lira (Director of Finance)

Implementation Date

Currently implemented

Parks And Recreation Department

12. Contract Monitoring

Observation

12.1 Formalized Monitoring Plan

The Contract is considered “high risk” both financially and from the public interest point of view. A formalized monitoring plan does not exist for this Contract. The Department relies upon their knowledge of the Contract and their recollection of the timing of key changes. No documentation was noted demonstrating that any methodical review had been done other than a reconciliation of tickets performed in January 2004 for the prior 12 month period.

A formalized plan can help ensure that contractor is performing correctly. It can also demonstrate that Department is adequately monitoring the Contractor, and ensure that the City is performing its contractual obligations.

12.2 Performance Bond

Rio is contractually obligated to provide a performance bond in the amount of \$750,000. The bond can be called upon by the City if Rio fails to perform.

2003-2004 Contract year: Attached to the continuation certificate for the performance bond for the 2003-2004 contract year was a power of attorney by the president of the bond company authorizing his employees to sign bonds. The most recent power of attorney attached was for up to \$500,000 which is less than the bond required under contract. It is unclear whether the City had the proper protection from the performance bond for the 2003-2004 contract year.

2004-2005 Contract year: Parks and Recreation was unable to timely deliver the performance bond for the 2004-2005 contract year. An original certified copy was provided to Parks and Recreation on December 28, 2004, by Rio. The contract year started September 1, 2004. It is unclear whether the City had the proper protection from the performance bond for the four months of the 2004-2005 contract year.

Risk

12.1 Improper performance of financial or non-financial requirements may not be identified timely. This could result in lost revenue or public image issues.

12.2 Without ensuring that the performance bond is adequate or in the possession of the City, the City has additional financial risk.

Recommendation

12.1 A formal monitoring plan should be created and approved by the Department Director. The plan should identify the timing of the review of significant financial and non-financial compliance matters. Monthly financial expectations and performance indicators should be developed and compared to actual performance. Significant differences between expected and actual performance should be investigated and documented. Periodic reporting should be provided to the City Executive Management and the Finance Department due to the importance of the Contract. This recommendation is consistent with the February 15, 2000 audit report recommendation from the former Department of Internal Review.

Additionally, the City Manager may want to consider the cost benefit of a centralized monitoring process plan versus de-centralized monitoring for high-risk contracts.

- 12.2 The Parks and Recreation Department now possesses the 2004-2005 performance bond. Obtaining the bond annually should be included in the formal monitoring plan. The location of the original bond should be documented in the contract file. The performance bond should be reviewed as it relates to bond ratings and also verify the legality of the bond.

Management Response

- 12.1 The Parks and Recreation Department Contract Services Division is working on a formal monitoring plan for this and all "high risk" contracts monitored by the department as recommended in the audit. The plan will identify the timing of the review of significant financial and non-financial compliance matters, as well as the development of parameters for measuring monthly performance. We will continue to coordinate all high-risk contract issues with the Contract Services Department, to include periodic reporting to the City Manager's Office and the Finance Department.

- 12.2 As part of the monitoring plan, procedures are being established to ensure timely receipt and review for adequacy and legality of all Performance Bonds. Documentation will be placed in the contract file as to the location of the original bond.

Responsible Party for Implementation

Malcolm Matthews (Director of Parks & Recreation Department)

Implementation Date

No time given

13. Suggestions For Contract Changes

Observation

During the audit, CIAD staff evaluated current contract requirements and what might be appropriate to include in the new 2005-2015 contract. Suggestions are as follows:

- Rio currently makes monthly commission payments to the City; more frequent payments could improve City cash flow. The City can utilize cash flow to better serve its residents. More timely payments will also help ensure that commissions are not held in contractor accounts exceeding the FDIC insurance limits. During the 2003-04 contract period, the lowest commission paid to COSA was approximately \$137,000 (January) and the highest commission paid to COSA was approximately \$582,000 (July). Rio's highest average daily balance per their bank statement was approximately \$1,047,000 in August 2004.
- Establishing additional performance requirements of the Contractor could help ensure that the boats and barges service is run properly and that commissions are satisfactory for years to come. For the current contract, minimum commission revenue to COSA is the only performance measure required.
- Additional performance requirements could include:
 - ✚ Defined performance measures (required growth) to promote ticket sales for tourists, local residents, taxi service, and dinner cruises
 - ✚ Number of ticket and taxi locations
 - ✚ Number of available daily/nightly cruise barges, etc.
 - ✚ Required minimum merchandise revenue
- Require Contractor to post signage stating "if customer fails to obtain a receipt, please call Rio sales office or Parks & Recreation Department at *designated phone number*." This will provide additional assurance that City is receiving all revenue it may be entitled.
- Consider revising Article II, section 2.1 to add a clause for defined interest and penalties if payments are not received in a timely manner.
- Consider revising Article XXIX, section 29.5 to read "if the payments have been understated/overstated by more than two percent (2%) and City is entitled to an increase/decrease in payments due hereunder as a result of such under/overstatement, then Contractor shall pay the full cost of such audit.
- Consider revising Article XLIV, section 44.4 to include language clarifying that no expense deductions for advertising revenue will be allowed.
- Consider adding language to contract stating that vendor will supply COSA compressed natural gas (CNG) for use in police boats at no charge during the contract period. In turn, COSA will provide garbage and refuse collection at no charge to Contractor.
- Consider adding language restricting Rio San Antonio Cruises from being able to sell incentive tickets. These incentive tickets can be purchased in blocks of twenty five (25) by any customer. The customer receives a ten (10) percent discount per ticket. The customer is allowed to re-sell the tickets at full price, with COSA only receiving commissions on the discounted price of the ticket. On a \$6.50 ticket, Rio would sell the ticket for \$5.85. COSA is losing fifty-one (51) percent commission on the \$.65 discounted price. COSA may consider only allowing the sale of discounted tickets to educational and tax exempt groups.

Recommendation

The above suggestions should be considered in the development of the new contract.

Management Response

In the preparation of the new concession contract with Rio San Antonio Cruises, we will address contract performance issues observed in the audit. These include process and policy improvements, POS system management, cancellations and accurate sales tax calculations, and ADA accommodations. We will also negotiate for a more frequent than once-a-month payment schedule.

Responsible Party for Implementation

Malcolm Matthews (Director of Parks & Recreation Department)

Implementation Date

No time given; assumed to be early 2005