



Memorandum from the Office of the Inspector General

August 7, 2008

Anda A. Ray, WT 11A-K

FINAL REPORT – INSPECTION 2007-11428-02 – REVIEW OF RILEY CREEK
CAMPGROUND LEASE AGREEMENT

At the request of the Chief Financial Officer's (CFO) office, we initiated a review of selected marina and campground contracts to determine whether (1) payments to TVA were accurate and timely and (2) key provisions of the license agreement were complied with. This report presents the results of our work at Riley Creek Campground (Riley Creek).¹ The Vice President (VP) of Environmental Stewardship and Policy (ES&P) specifically requested Riley Creek be included as one of the marinas/campgrounds reviewed. Under the terms of the lease agreement, Riley Creek was permitted use of the TVA land and adjoining shore land for commercial recreation purposes and the benefit and enjoyment of the general public. TVA was to be paid a fee for the use of the property based on a percentage of gross revenue. TVA refers to these contracts as "percentage of gross" contracts.

In summary, we found Riley Creek was not in compliance with some of the lease terms we reviewed. Specifically, lease payments were not made in a timely manner, required supporting documentation was not submitted, and records were not maintained in accordance with generally accepted accounting practices. In addition, while TVA accounting practices² provide guidance on the invoicing and receiving of lease and license payments, they contain no documented guidance on the management of the "percentage of gross" contracts (i.e., licenses and leases) including the verification of the accuracy of Licensee and Lessee payments. While not reflected in license and lease agreements for campgrounds and marinas, ES&P has implemented new payment control activities requiring supporting documentation for revenues. We also found lease provision violations such as (1) recent unapproved land clearing activities, (2) unapproved additions to campsites, (3) an approved new campsite being built outside of approved specifications, (4) debris and trash piles maintained on the premises, and (5) failure to maintain a performance bond.

BACKGROUND

On April 16, 2003, TVA entered into License Agreement RLR-126019 with Riley Creek Campground for the use of TVA-owned land, Tract No. XWBR-714L. The lease term is for

¹ TVA entered into a lease agreement for the operation of Riley Creek Campground. The Lessee will be referred to throughout this report as Riley Creek.

² The applicable TVA accounting practices were External Billing (Standard Principles and Practices [SPP] 13.7) and Accounts Receivable (SPP 13.15).

19 years. The Lessee is permitted use of the property for public commercial recreation purposes. The Lessee may perform construction, maintenance, development, and improvement activities of public campground and recreational facilities as authorized in advance and in writing by TVA. As of March 2008, the campground had approximately 43 campsites.

Per the agreement, Riley Creek is required to:

- Pay TVA an annual lease payment in the amount of the greater of five percent of all gross revenues or the guaranteed minimum rent of \$1,000 with an annual cost of living adjustment of three percent on or before January 31st of the following year.
- Deliver to TVA a certified statement showing the gross revenues for the preceding lease year.
- Keep records and books of accounts based on generally accepted accounting practices covering business operations and, whenever requested, transmit operating statements and other reports to TVA.
- Rehabilitate the existing septic system in accordance with a plan as submitted to and approved by TVA and install electric and water service to the existing 34 campsites. Work shall be completed within three years from the effective date of this lease unless otherwise approved in advance and in writing by TVA.
- Obtain prior written approval to (1) construct, maintain, or operate buildings/facilities/structures; (2) place equipment on; (3) conduct any dredging activities; or (4) place any fill material on the premises. In addition, the Lessee shall not make any modifications to any wetlands or shoreline vegetation except in accordance with plans and specifications which shall first have been approved in writing by TVA.
- Notify TVA's Cultural Resources Staff and obtain TVA's written approval prior to conducting any land-disturbing activities on the leased premises.
- Minimize removal of vegetation, particularly woody vegetation, and maintain the premises to prevent erosion.
- Keep the premises and all improvements thereon in a safe condition and in good order and shall collect and dispose of all trash, garbage, and other solid waste accumulated or left in accordance with applicable laws/regulations and, with sufficient frequency, keep premises in an orderly and sanitary condition.
- Operate and maintain, at a minimum, (1) the campground and day use area from May 1st through September 30th and (2) the boat ramp year-round.
- Prohibit the use of mobile homes, recreational vehicles, campers, or on-site facilities as residences. However, upon TVA's advanced written approval, one residence could be established for a resident manager along with appropriate equipment storage facilities.
- Maintain commercial general liability insurance and a performance bond.

In addition, Riley Creek may allow seasonal campsite rentals with durations up to eight months. However:

- TVA's advanced written approval of detailed operational guidelines was required.

- Seasonal campsite rentals could occupy no more than 75 percent of the campsites.
- The remaining 25 percent of the campsites could not be rented for more than 21 consecutive days.
- Campsites below the maximum shoreline contour (elevation 750 mean sea level) may not be rented between November 1st and March 31st for more than 14 consecutive days.
- All camping units will remain truly mobile year-round. Recreational vehicles must be mobile and ready for highway use (on wheels or a jacking system and attached to the site only by quick disconnect-type utilities and security devices).

OBJECTIVES, SCOPE, AND METHODOLOGY

The objectives of our review were to determine whether (1) payments to TVA were accurate and timely and (2) key provisions of the license agreement were complied with. To achieve our objectives, we:

- Identified and documented key agreement provisions by (1) reviewing the lease and (2) interviewing key TVA personnel.
- Interviewed applicable TVA ES&P employees to (1) determine whether payments have been made to TVA under the lease agreement; (2) determine whether TVA granted written approval for any improvements, new structures, or equipment on the premises; (3) identify key control activities; (4) ascertain whether any opportunities exist to improve contract language and controls; and (5) identify any other potential issues pertaining to the lease.
- Obtained supporting documentation for lease payments to determine whether lease payments have been made in accordance with the contract provisions.
- Obtained and reviewed documentation to ensure commercial general liability insurance was maintained as required by the agreement.
- Performed a site visit and walkdown of the property to (1) document Riley Creek operations, (2) review documentation applicable to the key contract provisions, and (3) visually observe structures and equipment.

The scope of the inspection included payments to TVA from the Lessee and other lease provisions from January 1, 2005, through December 31, 2007. This inspection was conducted in accordance with the "Quality Standards for Inspections."

FINDINGS

Our review found Riley Creek was not in compliance with some of the lease terms we reviewed. Lease payments were not submitted in accordance with lease provisions, and Riley Creek did not maintain records and books of accounts based on generally accepted accounting practices as required by the lease. Our review of TVA policies and procedures found TVA Accounting Practices External Billing (SPP 13.7) and Accounts Receivable (SPP 13.15) provide guidance on invoicing and receiving of lease and license payments. The accounting practices do not, however, provide guidance on verification of the accuracy of Licensee and Lessee payments. We found no formal TVA policies and procedures

regarding management of "percentage of gross" licenses and leases. During the site visit, it was noted that Riley Creek was not in compliance with other key provisions of the lease and did not maintain a performance bond as required.

ACCURACY AND TIMELINESS OF PAYMENTS

We reviewed Riley Creek revenue and payment documentation for the 2005, 2006, and 2007 operating seasons. ES&P personnel provided invoices, payment records, and correspondence regarding Riley Creek lease payments. During our walkdown of the facilities, we reviewed limited documentation provided by Riley Creek.

As previously mentioned, Riley Creek was to submit a certified gross revenues statement along with the five percent payment by January 31st for the previous operating season. We found that payments were not accompanied by the required supporting documentation and were not always submitted in accordance with the payment dates outlined in the agreement. Specifically, the 2005 payment was received in February 2006 and was not supported by a certified gross revenues statement. The 2006 payment was not submitted until December 2007 after four letters had been addressed to Riley Creek regarding the late payment. Also, a certified gross revenues statement was not submitted for the 2006 payment.

The lease payment for the 2007 operating season had not been remitted at the time of our review. While the contract had not been modified and states that payments should be made by January 31st, during 2007 TVA Business Services requested all "percentage of gross" entities to send supporting documentation along with their revenue report. Business Services would then invoice the Lessee based on that information. Therefore, the January 31st payment due date may no longer be applicable, and Business Services is working with Riley Creek to implement the new control requirements.

Our review also found the Lessee was not in compliance with the lease requirement to keep records and books of accounts based on generally accepted accounting practices covering business operations. The Lessee could not provide documentation of revenue for the 2005 and 2007 operating season. Additionally, the documentation provided for the 2006 operating season was not sufficient to confirm revenue totals or calculations.

Policies and Procedures

TVA Accounting Practices External Billing (SPP 13.7) and Accounts Receivable (SPP 13.15) provide guidance on the invoicing and receiving of lease and license payments. We found no documented guidance on the management of the "percentage of gross" licenses and leases including the verification of the accuracy of Licensee and Lessee payments. TVA Operations' Business Services personnel recently took over the invoicing and payment process for the "percentage of gross" licenses and leases from the individual watershed teams. According to Operations' Business Services personnel, key control activities relating to the payment process were implemented in 2007 including requiring Licensees and Lessees to provide gross revenue documentation prior to being invoiced by TVA. These new activities appear to address certain invoicing and payment controls. However, the licenses and leases have not been amended to reflect these changes.

COMPLIANCE WITH KEY CONTRACT PROVISIONS

We performed a walkdown of Riley Creek and found (1) recent land clearing activities that did not receive prior TVA approval as required; (2) additions to campsites which did not receive prior TVA approval as required; (3) a new, approved campsite being built outside of approved specifications; and (4) debris and trash piles on the premises in violation of lease provisions. ES&P personnel attended the site visit at Riley Creek. (Some of the noncompliance conditions are noted in the pictures included on page 6 of this report.)

According to ES&P personnel, Riley Creek has been in violation of the lease agreement for over a year and a half, and they have previously recommended that the lease be terminated. A review of correspondence from TVA to Riley Creek found Riley Creek was notified of 22 compliance issues in June 2006. As of January 2007, Riley Creek had corrected 3 of the 22 compliance issues and were notified that the remaining compliance issues must be corrected by March 1, 2007. According to ES&P personnel, Riley Creek had not corrected all 22 of the compliance issues at the time of our site visit in March 2008.

Furthermore:

- During our review, we requested copies of the required commercial general liability insurance policy and performance bond from TVA and Riley Creek. We found Riley Creek does not maintain a performance bond as required by the agreement. Riley Creek has provided TVA with a current certificate of commercial general liability insurance; however, ES&P personnel have asked for additional information to determine compliance with requirements.
- Due to the lack of auditable records at Riley Creek, we were not able to determine if Riley Creek was in compliance with the length-of-stay and seasonal rental provisions. Specifically, the lease requires that (1) the campground and day use area be open from May 1st through September 30th and the boat ramp be open year-round, (2) seasonal rentals be for a maximum duration of eight months, and (3) only 75 percent of the sites may be rented for the full season. According to campground management, the campground and day use area remain open year-round which indicates Riley Creek is in compliance with the minimum operating season requirement.³
- Riley Creek was required to rehabilitate the existing septic system in accordance with a plan as submitted to and approved by TVA and install electric and water service to the existing 34 campsites by May 2006. According to Riley Creek, the septic system did not require rehabilitation and no inspection of the system had been completed. According to ES&P personnel, the campsite improvements and septic system are not considered complete due to a lack of supporting documentation.

TVA has developed a campground compliance committee with the objective of developing a consistent campground contract compliance process. According to TVA personnel, issues being discussed include a methodology of ensuring campsites at licensed/leased campgrounds are available for use to the general public.

³ TVA has developed a campground compliance committee with the objective of developing a consistent campground contract compliance process. According to TVA personnel, issues being discussed include a methodology of ensuring campsites at licensed/leased campgrounds are available to the general public for use.



RECOMMENDATIONS

We recommend the VP, ES&P:

- Implement necessary actions to ensure Riley Creek's compliance with lease terms or consider termination options.
- Implement written guidance, as deemed necessary, regarding the management of recreational facilities' "percentage of gross" contracts. This recommendation also applies to the other six "percentage of gross" contracts in which separate reports were issued.
- Determine whether licenses and leases should be amended based on the implementation of payment control activities. ES&P personnel also plan to consider any opportunities for improvement identified by the campground compliance committee. This recommendation also applies to the other six "percentage of gross" contracts in which separate reports were issued.

- - - - -

This final report is for your review and final action. Please advise us of your planned actions (i.e., management decision) in response to our findings within 60 days of the date of this report.

Information contained in this report may be subject to public disclosure. Please advise us of any sensitive information in this report that you recommend be withheld.

If you have any questions, please contact Michael A. Driver, Project Manager, at (423) 751-8158 or Gregory C. Jaynes, Deputy Assistant Inspector General, Inspections, at (423) 751-7821.

We appreciate the courtesy and cooperation received from your staff during this review.

A handwritten signature in cursive script that reads "Gregory C. Jaynes".

(for) Robert E. Martin
Assistant Inspector General
(Audits and Inspections)
ET 3C-K

SLO:BKA

cc: Bridgette K. Ellis, WT 11A-K
Peyton T. Hairston, Jr., WT 7B-K
Tom D. Kilgore, WT 7B-K
John E. Long, Jr., WT 7B-K
Richard W. Moore, ET 4C-K
Emily J. Reynolds, OCP 1L-NST
Stephen B. Summers, WT 4B-K
OIG File No. 2007-11428-02