



Memorandum from the Office of the Inspector General

August 7, 2008

Anda A. Ray, WT 11A-K

**FINAL REPORT – INSPECTION 2007-11428-03 – REVIEW OF SKULL ISLAND
CAMPGROUND LICENSE AGREEMENT**

At the request of the Chief Financial Officer's (CFO) office, we initiated reviews 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 regarding Skull Island Campground (SIC).¹ The Vice President (VP) of Environmental Stewardship and Policy (ES&P) specifically requested SIC be included as one of the marinas/campgrounds reviewed. Under the terms of the license agreement, SIC was provided use of the TVA land, adjoining shore land, and associated equipment and facilities for commercial recreation purposes and the benefit 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 payments were (1) calculated in accordance with payment terms, (2) generally received in a timely manner, and (3) supported by required documentation. 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 nothing to indicate SIC was not in compliance with other key provisions of the license agreement pertaining to (1) installation of improvements, permanent structures, and equipment; and (2) commercial general liability insurance.

BACKGROUND

On October 1, 1997, TVA entered into Contract RLR-64230 licensing the use of SIC.

¹ TVA entered into a license agreement for the operation of SIC. The Licensee will be referred to throughout this report as SIC.

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

The contract is an open-ended agreement with either TVA or the Licensee having the right to terminate the agreement with a 30-day notice. The licensed premises located on Chickamauga Lake is owned by TVA, Tract No. XCR-36PT, and includes all existing campground facilities, the boat launching ramp and parking area, and the dump station as well as the adjacent shore lands. The Licensee is permitted use of the land, adjoining shore land, and associated equipment and facilities for commercial recreation purposes and the benefit of the general public.

Per the agreement, the SIC Licensee:

- Is to pay TVA a license payment equal to three percent of gross income. SIC was required to make the payment no later than January 20th for the previous operating year ending December 31st.
- Must support the January 20th payment with a report of gross income for the previous annual period which, at a minimum, contained a breakdown of revenue for campsite rental, day use fees, and miscellaneous income.
- Is to operate and maintain, at a minimum, the campground and day use area from May 1st through September 30th.
- Has the right to make improvements, erect structures, and install equipment on the premises upon receipt of advanced written approval from TVA. The Licensee was not to install or permit the installation of porches, equipment storage sheds, appliances, or similar structures. In addition, SIC could not use or permit the use of mobile homes or campers for residences. However, upon TVA's advanced written approval, one residence could be established for a resident manager along with appropriate equipment storage facilities.
- Is to maintain commercial general liability insurance.
- Could allow seasonal campsite rentals with durations up to eight months. However:
 - Seasonal campsite rentals could not occupy more than 75 percent of the campsites.
 - TVA's advanced written approval of detailed operational guidelines was required.
 - 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.

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.

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 license and (2) interviewing key TVA personnel.
- Interviewed applicable TVA ES&P employees to (1) determine whether payments have been made to TVA under the license agreement, (2) determine whether TVA granted written approval for any modifications to the property, (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 license.
- Obtained supporting documentation for license payments to determine whether license 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 SIC operations, (2) review documentation applicable to the key contract provisions, and (3) visually observe structures and equipment. An ES&P employee escorted us on our walkdown of SIC.

The scope of the inspection included payments to TVA from SIC and other license 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 nothing to indicate SIC was not in compliance with the payment terms and other key license agreement provisions we selected for review. Additionally, 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 the invoicing and receiving of lease and license payments. However, 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. While not reflected in the agreements, ES&P has implemented new payment control activities requiring supporting documentation for revenues.

ACCURACY AND TIMELINESS OF PAYMENTS

We reviewed SIC revenue and payment documentation for the 2005 and 2006 operating seasons. At the time of our review, the information for 2007 was not available. ES&P personnel provided gross revenue calculation reports, a copy of the check received by TVA, a handwritten breakdown of revenue, Tennessee Sales Tax Returns, and receipts for ice and drinks.

During our walkdown of the facilities, we reviewed SIC's State Sales Tax Returns, spreadsheets of monthly revenue, and copies of cleared checks sent to TVA for payment which agreed with the information provided by ES&P. We compared the income reported to TVA to that reported on the Sales Tax Returns. For 2005, Sales Tax Returns were not provided for March, November, or December. However, during these months the campground should have been closed and not received any revenue. For 2006, all of the Sales Tax Returns were available for review, and the returns for March, November, and December showed no revenue. For both 2005 and 2006, the amount reported to TVA for camping matched the total revenue reported on the Sales Tax Returns provided for our review. In addition, SIC reported additional revenue related to picnics, swimming, drinks, and ice on the gross revenue calculation reports. While the payment amounts were calculated correctly based on the reported revenue for 2005, the 2006 payment amount was overstated by an immaterial amount. Both the 2005 and 2006 payments were received after the January 20th due date stated in the contract. However, we did not identify these as noncompliances since they were received within 30 days of the due date.

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 SIC and found no (1) permanent residences, with the exception of a manager's residence which is allowed under the contract; (2) buildings or structures on the premises that violate contract provisions; (3) improvements or modifications had been made that were not approved in advance by TVA. In addition, the campground appeared well maintained and clean as shown in the pictures on page 5 of this report. Per ES&P personnel, (1) there have been no problems with the campground or contract, and (2) SIC has not requested any improvements to the campground and no modifications to the property were noted during our visit.

The campground was closed during our visit in the offseason, and we found no campers present. According to the ES&P personnel, the campground and day use area usually open for operation on May 1st and close on September 30th, the minimum required by the contract. The Sales Tax Returns we reviewed showed revenue for April through September for both 2005 and 2006 and a small amount of revenue for October in 2005. These observations indicated that SIC appeared to be in compliance with the length-of- stay provisions in the contract. The contract also requires SIC to maintain commercial general liability insurance with specified coverage limit requirements for personal and property damage. The insurance policy reviewed appeared to be in compliance with the contract requirements.



RECOMMENDATIONS

We recommend the VP, ES&P:

- Implement written guidance, as deemed necessary, regarding the management of recreational facilities' "percentage of gross" contracts.
- 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.

These recommendations also apply 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.

Gregory C. Jaynes

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cc: See page 6

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