



Memorandum from the Office of the Inspector General

August 7, 2008

Anda A. Ray, WT 11A-K

FINAL REPORT – INSPECTION 2007-11428-08 – REVIEW OF NORMANDY CEDAR POINT PUBLIC USE AREA 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 lease agreement were complied with. This report presents the results of our work regarding Cedar Point Public Use Area (Cedar Point).¹ Under the terms of the lease agreement, Cedar Point was provided 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, based on a scope limitation, we were unable to determine Cedar Point's compliance with certain requirements of the contract (e.g., length-of-stay provision, payment calculations, and documentation). At the time of our review, Cedar Point could not provide documentation from operations. We found Cedar Point's 2005 and 2006 payments to TVA were accompanied by required documentation; however, payments were not consistently received by the required contract payment date. 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 campground and marinas, ES&P has implemented new payment control activities requiring supporting documentation for revenues. We also found nothing to indicate Cedar Point was not in compliance with other key provisions of the lease agreement pertaining to (1) permanent residences, (2) installation of buildings or structures on the premises, and (3) commercial general liability insurance. However, we noted Cedar Point does not maintain a performance bond as required by contract provisions, and Environmental Stewardship and Policy (ES&P) did not have documentation for the required investment in the property by Cedar Point. It was also

¹ TVA entered into a lease agreement for the operation of Cedar Point public use area. The Lessee will be referred to throughout this report as Cedar Point.

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

noted that seasonal guests are given preference to return to their site each year and are allowed to leave camping vehicles and equipment on site while the campground is closed for the winter months.

BACKGROUND

On January 31, 2000, TVA entered into License Agreement RLR-69896 with Cedar Point for the use of TVA-owned land, Tract No. XNRMR-6L. The lease term is for 19 years. The Lessee is permitted use of the property for public commercial recreation purposes and for the construction, maintenance, development, and operation thereon and therein of public campground facilities and associated improvements and recreational facilities as authorized in advance and in writing by TVA. The campground has approximately 52 campsites.

Per the agreement, Cedar Point is required to:

- Pay TVA an annual lease payment in the amount of the greater of five percent of all gross revenue or the guaranteed minimum rent of \$2,600 on or before January 31st of the following year.
- Deliver to TVA a certified statement showing the gross revenue for the preceding lease year.
- Keep records and books of accounts based on generally accepted accounting practices covering business operations and shall, whenever requested, transmit operating statements and other reports to TVA.
- Invest a minimum of \$50,000, not including the cost of the lease, for development of the leased premises within two years of the effective date of this lease.
- 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.
- Keep the premises and all improvements thereon in a safe condition and in good order and, in accordance with applicable laws/regulations and with sufficient frequency, shall collect and dispose of all trash, garbage, and other solid waste accumulated or left to keep premises in an orderly and sanitary condition.
- 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.

Additionally, Cedar Point may allow seasonal campsite rentals with durations up to eight months. However:

- 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 880 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 lease 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 Cedar Point 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 we were unable to determine Cedar Point's compliance with certain requirements of the contract (e.g., length-of-stay provision, payment calculations, and documentation) due to a scope limitation. Documentation could not be obtained from Cedar Point at the time of our review. From our review of documentation maintained by

TVA, we found lease payments were accompanied by the required gross revenue statements. However, payments were not consistently received by the required contract payment date. In addition, 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. 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. With regard to the other lease provisions we reviewed, we found Cedar Point (1) did not maintain a required performance bond and (2) could not provide documentation to support a required \$50,000 investment in the property. It was also noted that seasonal guests are given preference to return to their site each year and are allowed to leave camping vehicles and equipment on site while the campground is closed for the winter months.

ACCURACY AND TIMELINESS OF PAYMENTS

At the time of our review, no documentation could be obtained from Cedar Point. According to campground management, the accountant for Cedar Point had passed away at the beginning of the year and Cedar Point has been denied access to the records. The accountant maintained all documentation and no copies were kept at the campground.

Cedar Point was to submit supporting documentation along with the lease payment by January 31st for the previous operating season. ES&P personnel provided invoices and payment documentation submitted by Cedar Point to TVA for the 2005 and 2006 operating seasons. During our review of TVA documentation, it was noted that payments were accompanied by handwritten and signed breakdowns of revenue but were not consistently received in a timely manner. Payment for the 2005 operating season was received by TVA in January 2006, and payment for the 2006 operating season was received by TVA in August 2007.

Payment for the 2007 operating season had not been remitted at the time of our review due to the difficulties of obtaining records, according to campground management. Additionally, 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 based on that information. Therefore, the January 31st payment due date may no longer be applicable, and Business Services is working with Cedar Point to implement the new control requirements.

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 Cedar Point and found (1) no permanent residences, (2) no buildings or structures on the premises that violate contract provisions, and (3) the campground appeared well maintained and clean as noted in the pictures on page 6 of this report. During the site visit, we obtained and reviewed copies of the required commercial general liability insurance policies. The insurance policies reviewed appear to be in compliance with the contract requirements. However, Cedar Point does not maintain the performance bond as required by the contract. We were also unable to verify that Cedar Point fulfilled an investment lease provision because records could not be provided by TVA or Cedar Point. Specifically, according to the contract terms, a \$50,000 investment for development of the leased premises was to be fulfilled within two years of the effective date of this lease.

The contract also requires that the seasonal rental be for a maximum duration of eight months and that only 75 percent of the sites may be rented for the full season. According to campground management, the campground is closed from mid-November through the end of March indicating compliance with the length-of-stay provision. At the time of the site visit, campground management stated that the guests and recreational vehicles on the property were all seasonal campers. Auditors noted that the number of guests and recreational vehicles on the property appeared to be less than the 75 percent maximum of seasonal camping.

According to campground management, some camping vehicles and equipment are allowed to remain on the campsites while the campground is closed for the winter months and certain guests are allowed to occupy the same campsite year after year. While not specifically disallowed in the lease agreement, the contract language does state the premises and any public facilities constructed thereon shall at all times be made available for use by all members of the general public without distinction or discrimination. 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 Vice President, ES&P:

- Require Cedar Point comply with the documentation requirements of the lease agreement including obtaining documentation to support the fulfillment of the investment provision.
- 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.

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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.

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Page 7
August 7, 2008

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



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