

City of Miami

THEODORE P. GUBA, CPA, CIA, CFE
INDEPENDENT AUDITOR GENERAL



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May 22, 2019

Honorable Members of the City Commission
City of Miami
3500 Pan American Drive
Coconut Grove, FL 33133-5504

Re: Audit of Biscayne Bay Restaurant Corporation d/b/a Rusty Pelican Restaurant (BBRC), for the period July 1, 2013 through June 30, 2018
Report No. 19-10

Executive Summary

We have completed an audit of records and selected financial transactions of Biscayne Bay Restaurant Corporation d/b/a Rusty Pelican Restaurant (BBRC), primarily for the period July 1, 2013 through June 30, 2018. The audit was performed to determine whether BBRC complied with the applicable sections of its Lease Agreement (Lease) with the City of Miami (City). During the lease years 2013 through 2018, BBRC made base rent payments totaling \$360,000 per year, in addition to percentage rent payments. During the most recent lease years (2017 and 2018), BBRC made percentage rent payments totaling \$1,251,475 and \$1,241,076, respectively, while reporting total gross revenue of approximately \$16.1 million and \$16 million, respectively.

It should be noted that the prior report (Audit No.15-003) issued in September 2015, indicated that BBRC was unable to provide us with dedicated bank deposit transactions since deposits were comingled with those from its other restaurant operations. BBRC established a separate bank account specifically for Rusty Pelican operations; however, deposits were at times made to the comingled account during the scope period of this audit.

Overall, we concluded that except for certain controls over gross revenue reporting and insurance coverage that required strengthening, procedures and compliance with the Lease were generally adequate and being adhered to. This should include complete and accurate bank deposit transactions that are dedicated to the operations of this restaurant, rather than being comingled with deposits from other restaurants. Improvement is needed to ensure that BBRC's gross revenue, which is the basis for the percentage rent is reported accurately and that it procures adequate insurance coverage based on the appraised replacement cost of the property. As a result of the audit, **BBRC owes the City \$27,453 in additional rent** (See Schedule 1, page 4).

We wish to express our appreciation for the cooperation and courtesies extended to us by the BBRC management and accounting staff as well as the City's Department of Real Estate and Asset Management while conducting the audit.

Sincerely,



Theodore P. Guba, CPA, CIA, CFE
Independent Auditor General
Office of the Independent Auditor General

cc: The Honorable Mayor Francis Suarez
Emilio T. Gonzalez, City Manager
Victoria Mendez, City Attorney
Todd Hannon, City Clerk
Joseph Napoli, Deputy City Manager
Sandra Bridgeman, Assistant City Manager/Chief Financial Officer
Nzeribe Ihekweba, Assistant City Manager/Chief of Operations
Fernando Casamayor, Assistant City Manager
Daniel Rotenberg, Director, DREAM (Department of Real Estate and Asset Management)
Mark Burns, Lease Manager, DREAM (Department of Real Estate and Asset Management)
Erica T. Paschal, Director, Finance Department
Ann-Marie Sharpe, Director, Risk Management Department
Demetrio Constantiny, Accounts Receivable Supervisor, Finance Department
John Tallichet, Chief Executive Officer, Specialty Restaurants Corporation
Mary Carter, Interim Chief Financial Officer, Specialty Restaurants Corporation
Members of the Audit Advisory Committee
Audit Documentation File

Audit conducted by: Wesley Laurent, MBA, CPA, CIA, Senior Auditor

Audit reviewed by: Mala Khilnani, CPA, CISA, Assistant to the Auditor General

**AUDIT OF BISCAYNE BAY RESTAURANT CORPORATION
JULY 1, 2013 THROUGH JUNE 30, 2018
REPORT NO. 19-10**

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SCOPE, OBJECTIVES AND METHODOLOGY

The scope of the audit was to determine Biscayne Bay Restaurant Corporation's (BBRC) compliance with the rental payment and insurance provisions of its Lease Agreement (Lease) with the City of Miami (City). The audit primarily covered the period July 1, 2013 through June 30, 2018 and focused on the following objectives:

- To determine whether BBRC complied with the terms of the Lease to the extent that their rental payments to the City were consistent with: gross revenues periodically reported to the City; sales and use tax returns reported to the State of Florida; and, bank deposits.
- To determine whether BBRC rental payments were accurate and remitted in a timely manner.
- To determine whether insurance policies were adequate and in compliance with Lease terms.
- To determine whether adequate internal controls were maintained.
- Other audit procedures as deemed necessary.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The audit methodology included the following:

- Interviews and inquiries of appropriate personnel.
- Reviews of written policies and procedures in order to gain an understanding of the internal controls.
- Observations of current practices and processing techniques.
- Tests of applicable transactions and records.
- Other audit procedures as deemed necessary.

BACKGROUND

The City of Miami (City) owns a twenty-one (21) acre waterfront site on Rickenbacker Causeway, which is part of the City's Miami Marine Stadium complex. Subsequent to issuing a request for proposal (RFP) to develop and operate a high class restaurant at the Marine Stadium complex, the City executed a Lease Agreement (Lease), dated February 13, 1970, with Biscayne Bay Restaurant Corporation (BBRC), (a Florida Corporation and a wholly owned subsidiary of Specialty Restaurants Corporation [SRC], a California corporation) d/b/a Rusty Pelican.

In accordance with the terms of the Lease, BBRC constructed a pedestrian walkway (the "Baywalk") and an outdoor deck (the "Vista Point") in consideration for the extension of the term of the lease to October 1, 2027.

BBRC is required to pay the City stipulated base rent payments of \$360,000 per year or \$30,000 per month. Based on revenues generated by the restaurant (Rusty Pelican), BBRC is required to pay "Percentage Rent" as outlined in the Lease. During the most recent lease years (2017 and 2018), BBRC made percentage rent payments totaling \$1,251,475 and \$1,241,076, respectively, while reporting total gross revenue of approximately \$16.1 million and \$16 million, respectively.

AUDIT FINDINGS AND RECOMMENDATIONS

CONCLUSION: Overall, we concluded that except for certain controls over gross revenue reporting and insurance coverage that required strengthening, procedures and compliance with the Lease were generally adequate and being adhered to. Improvements should include complete and accurate bank deposit transactions that are dedicated to the operations of this restaurant, rather than being comingled with deposits from other restaurants. They should ensure that BBRC's gross revenue, which is the basis for the percentage rent, is reported accurately. Also, they should procure adequate insurance coverage based on the appraised replacement cost of the property. As a result of the audit, **BBRC owes the City \$27,453 in additional rent.**

Details of our findings and recommendations follow:

FINDING 1: UNDERSTATED GROSS REVENUES REPORTED TO THE CITY RESULTED IN UNDERPAYMENTS OF PERCENTAGE RENT TOTALING \$27,453

The Lease stipulates that BBRC must pay a variable percentage of Lessee's Gross Revenues, if any, in excess of the Base Rent. During the period audited (July 2013 to June 2018), we noted that Base Rent was \$360,000 (or \$30,000 monthly) and the applicable Percentage Rent was as follows:

- 7% of Gross Revenues from \$0 to \$ 12 million annually and
- 8% of Gross Revenues over \$12,000,000 annually

In order to determine whether BBRC paid the correct amount of percentage rent during the audit period, we performed reconciliations of gross revenue (GR) reported to the City to all cash deposited by BBRC into bank accounts. Accordingly, we obtained all bank deposits and made adjustments for various items that should have been excluded from Gross Receipts including sales and use taxes collected, advance deposits, service charges (gratuities/tips) and banquet charges. When performing the reconciliation, we calculated a reporting shortage of \$344,541 between the total reconciled Gross Revenues and the Gross Revenues that BBRC reported to the City. Accordingly, BBRC owes the City \$27,453 in additional rent (See Schedule 1, page 4).

SCHEDULE 1 - RECONCILIATION OF GROSS REVENUES - BISCAYNE BAY RESTAURANT CORP. (BBRC)						
	Year Ended 6/30/2014	Year Ended 6/30/2015	Year Ended 6/30/2016	Year Ended 6/30/2017	Year Ended 6/30/2018	Total
Bank Deposits:	\$ 14,746,688	\$ 16,930,892	\$ 18,861,327	\$ 18,936,090	\$ 19,275,836	\$ 88,750,832
Plus:						
AMEX Fees (A)	145,263	150,357	166,593	152,093	131,229	745,536
Less:						
Credit Card Refunds (B)	-	-	-	-	(307,431)	(307,431)
Banquet Surcharges (C)	(1,022,091)	(999,633)	(1,028,380)	(955,322)	(977,655)	(4,983,080)
Total Sales & Use Tax Collected (D)	(932,346)	(1,055,918)	(766,990)	(1,144,725)	(1,138,626)	(5,038,604)
Credit Card Gratuities (E)	(411,635)	(462,083)	(648,533)	(666,029)	(743,628)	(2,931,909)
Advance Deposits (F)	-	-	-	-	(125,434)	(125,434)
Reconciled Gross Revenue	12,525,879	14,563,616	16,584,017	16,322,107	16,114,292	76,109,911
Gross Revenue Reported to the City	12,790,702	14,624,457	16,231,629	16,120,034	15,998,548	75,765,370
Over/(Under) Reporting	264,823	60,841	(352,387)	(202,073)	(115,744)	\$ (344,541)
Percentage Rent Due per Audit	943,815	1,118,246	1,291,192	1,268,772	1,250,983	5,873,008
Percentage Rent Paid	968,524	1,123,454	1,261,027	1,251,475	1,241,076	5,845,555
Percentage Rent over(under)	\$ 24,709	\$ 5,208	\$ (30,164)	\$ (17,297)	\$ (9,907)	\$ (27,453)
<p>(A)= AMEX charges are deposited net of AMEX fees. (B)= Point of Sale system duplicated sales in 2018. A refund was issued to the customers. (C)= Banquet Service Surcharge charged for events. 82% of the service charges are distributed to the employees and excluded from Gross Revenue. (D)= According to the lease, Sales & Use taxes collected are excluded from Gross Revenue. (E)= According to the lease, gratuities paid to employees are excluded from Gross Revenue. (F)= Advance deposit balance for events as of 6/30/18.</p>						

As noted earlier, for part of the audit period, bank deposits were comingled with deposits from other restaurants rather than using the dedicated bank account.

RECOMMENDATION 1.1: BISCAYNE BAY RESTAURANT CORPORATION (BBRC)

We recommend that BBRC enhance their internal control procedures to ensure that all “Monthly Gross Revenue Statements” and percentage rent payments to the City are accurately calculated consistent with the Lease. In addition, we recommend that BBRC remit the additional percentage rent of \$27,453 due to the City.

We recommend that a separate bank account and statements be used at all times to account for the restaurant operations.

- **Auditee Response:** BBRC will remit the additional percentage rent of \$27,453 due to the City. Also, Rusty Pelican deposits are now deposited into a dedicated bank account, and not comingled with deposits from other restaurants.
- **Implementation Date:** Immediately.

RECOMMENDATION 1.2: FINANCE DEPARTMENT

We recommend that the City's Finance Department bill and collect the percentage rent due to the City from BBRC in the amount of \$27,453.

- **Auditee Response:** The Finance Department will bill BBRC the percentage rent due in the amount of \$27,453.
- **Implementation Date:** Immediately

FINDING 2: INSURANCE COVERAGE WAS NOT IN COMPLIANCE WITH LEASE TERMS

In accordance with Paragraph 21 (vii) of the Lease Agreement (Lease) between the City of Miami (City) and BBRC:

“...commencing on September 1, 2013 and every four years thereafter, the replacement cost of the Insured Property shall be adjusted pursuant to an appraisal conducted by an insurance appraiser, selected and paid for by the Lessee, provided that the Lessee shall obtain Lessor's approval (which approval shall not be unreasonably withheld, conditioned or delayed) of the appraiser before the commencement of the appraisal. The appraiser selected by the Lessee shall submit a written report of the appraised replacement cost to the Lessor and Lessee by July 15th in the year of the adjustment.”

Based on our review of the Lease and supporting documentation, we noted that BBRC did not obtain an appraisal commencing on September 1, 2013, or four (4) years thereafter in 2017, in order to determine the current replacement cost of the property. We reported this finding in Audit No. 15-003 in September 2015. Not obtaining such an appraisal and ascertaining the property's current replacement cost could cause the property to be underinsured and increase the City's risk of sustaining a material financial loss in the event of a major catastrophe.

RECOMMENDATION 2.1: (BISCAYNE BAY RESTAURANT CORPORATION)

We recommend that BBRC obtain the necessary appraisal as required in the Lease in order to adjust the replacement cost and insurance coverage of the City's property.

- **Auditee Response:** The Company has obtained the appraisal but are waiting issuance of the updated insurance.
- **Implementation Date:** May 2019.

RECOMMENDATION 2.2: (REAL ESTATE AND ASSET MANAGEMENT DEPARTMENT)

We recommend that the Department of Real Estate and Asset Management (DREAM) periodically monitor insurance provisions of City lease agreements in order to ensure lessee adherence to all insurance requirements.

- **Auditee Response:** BBRC has obtained the appraisal. Once the updated insurance policy is obtained, Risk Management will review the policy.
- **Implementation Date:** May 2019.