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**From:** McGuire, Kristen [kristen.mcguire@sfgov.org] on behalf of Reports, Controller [controller.reports@sfgov.org]  
**Sent:** Thursday, January 09, 2014 1:32 PM  
**To:** Calvillo, Angela; BOS-Supervisors; BOS-Legislative Aides; Kawa, Steve; Howard, Kate; Falvey, Christine; Elliott, Jason; Campbell, Severin; Steeves, Asja; Newman, Debra; Rose, Harvey; sfdocs@sfpl.info; gmetcalf@spur.org; Petrucione, Katharine; Kinsey, Nicholas; Hart, Tom; Commission, Recpark; CON-EVERYONE; CON-CCSF Dept Heads; CON-Finance Officers  
**Subject:** Report Issued: Recreation and Park Commission: The Beach Chalet, L.P., Owes the City \$53,208 for Paying Its Rent Late in 2009 Through 2011

The Office of the Controller's City Services Auditor Division (CSA) today issued a report on its audit of the rental payments and financial reporting of Beach Chalet, L.P., (Beach Chalet) to the Recreation and Park Department (Rec & Park) under their lease agreement. The audit found that:

- Beach Chalet owes Rec & Park \$53,208 for late rental payments.
- Rec & Park and Beach Chalet share the cost of water used at the building based on an estimate that may be incorrect. Beach Chalet deducted \$97,632 from its rent for the audit period based on this estimate.
- Beach Chalet deducted the cost of some janitorial supplies that are not listed as deductible items in the lease. Rec & Park did not review or maintain janitorial supply invoices submitted by Beach Chalet.
- Beach Chalet did not comply with lease requirements to provide Rec & Park with statements of gross sales, statements certifying the correctness of its annual percentage rent, or copies of its tax returns. Also, because the lease is vague, it is unclear if Beach Chalet complied with the requirement to submit year-end financial statements.

After receiving the draft audit report, Rec & Park invoiced Beach Chalet for the \$53,208 in late fees and interest charges, and Beach Chalet has paid Rec & Park the amount in full.

To view the full report, please visit our Web site at:  
<http://openbook.sfgov.org/webreports/details3.aspx?id=1654>

This is a send-only e-mail address.

For questions about the report, please contact Director of City Audits Tonia Lediju at [tonia.lediju@sfgov.org](mailto:tonia.lediju@sfgov.org) or 415-554-5393 or the CSA Audits Unit at 415-554-7469.

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**Document is available  
at the Clerk's Office  
Room 244, City Hall**

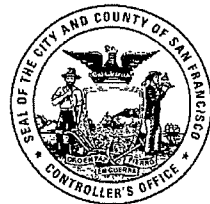


# City and County of San Francisco

Office of the Controller – City Services Auditor

## RECREATION AND PARK COMMISSION:

**The Beach Chalet, L.P., Owes the  
City \$53,208 for Paying Its Rent Late  
in 2009 Through 2011**



*January 9, 2014*



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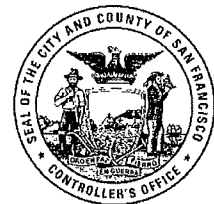


# City and County of San Francisco

Office of the Controller – City Services Auditor

## **RECREATION AND PARK COMMISSION:**

**The Beach Chalet, L.P., Owes the  
City \$53,208 for Paying Its Rent Late  
in 2009 Through 2011**



*January 9, 2014*

**OFFICE OF THE CONTROLLER  
CITY SERVICES AUDITOR**

The City Services Auditor Division (CSA) was created in the Office of the Controller through an amendment to the Charter of the City and County of San Francisco (City) that was approved by voters in November 2003. Charter Appendix F grants CSA broad authority to:

- Report on the level and effectiveness of San Francisco's public services and benchmark the City to other public agencies and jurisdictions.
- Conduct financial and performance audits of city departments, contractors, and functions to assess efficiency and effectiveness of processes and services.
- Operate a whistleblower hotline and website and investigate reports of waste, fraud, and abuse of city resources.
- Ensure the financial integrity and improve the overall performance and efficiency of city government.

CSA may conduct financial audits, attestation engagements, and performance audits. Financial audits address the financial integrity of both city departments and contractors and provide reasonable assurance about whether financial statements are presented fairly in all material aspects in conformity with generally accepted accounting principles. Attestation engagements examine, review, or perform procedures on a broad range of subjects such as internal controls; compliance with requirements of specified laws, regulations, rules, contracts, or grants; and the reliability of performance measures. Performance audits focus primarily on assessment of city services and processes, providing recommendations to improve department operations.

CSA conducts its audits in accordance with the Government Auditing Standards published by the U.S. Government Accountability Office. These standards require:

- Independence of audit staff and the audit organization.
- Objectivity of the auditors performing the work.
- Competent staff, including continuing professional education.
- Quality control procedures to provide reasonable assurance of compliance with the auditing standards.

For questions about the report, please contact Director of City Audits Tonia Lediju at [Tonia.Lediju@sfgov.org](mailto:Tonia.Lediju@sfgov.org) or 415-554-5393, or CSA at 415-554-7469.

Audit Team: Mark Tipton, Audit Manager  
Irene Chiu, Associate Auditor





**CITY AND COUNTY OF SAN FRANCISCO**  
**OFFICE OF THE CONTROLLER**

**Ben Rosenfield**  
**Controller**

**Monique Zmuda**  
**Deputy Controller**

January 9, 2014

Recreation and Park Commission  
McLaren Lodge, Golden Gate Park  
501 Stanyan Street  
San Francisco, CA 94117

Mr. Phil Ginsburg  
General Manager  
Recreation and Park Department  
McLaren Lodge, Golden Gate Park  
501 Stanyan Street  
San Francisco, CA 94117

Dear Commission President, Commissioners, and Mr. Ginsburg:

The Office of the Controller's City Services Auditor Division (CSA) presents its report concerning the audit of Beach Chalet, L.P. (Beach Chalet). Beach Chalet has a lease agreement (lease) with the City and County of San Francisco (City), through its Recreation and Park Commission, to operate a restaurant and brewery in the Beach Chalet Building (building). The 20-year lease term began on December 31, 1996, and will expire in December 2016.

**Reporting Period:** January 1, 2009, through December 31, 2011

**Rent Paid:** \$1,562,997

**Results:**

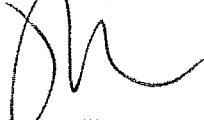
- Beach Chalet owes the Recreation and Park Department (Rec & Park) \$53,208, consisting of \$53,175 in late payment fees and \$33 in interest charges for late rental payments. Rec & Park did not assess or bill these fees.
- Rec & Park and Beach Chalet share the cost of water used at the building based on an estimate that may be incorrect. If it is incorrect, it results in inaccurate monthly deductions from Beach Chalet's rent for the City's portion of the water usage. The undocumented estimate that the City is responsible for 40 percent of the water used on the premises allowed Beach Chalet to deduct \$97,632 from its rent for the audit period.
- Beach Chalet deducted the cost of some janitorial supplies that are not listed as deductible items in the lease. For six months tested, the deductions were an average of \$236 per month.
- Rec & Park did not review or maintain janitorial supply invoices submitted by Beach Chalet to ensure that rent deductions were accurate and complied with lease requirements.

- Beach Chalet did not comply with lease requirements regarding providing Rec & Park with statements of gross sales, statements certifying the correctness of its annual percentage rent, or copies of its tax returns. Also, because the lease is vague, it is unclear if Beach Chalet complied with the requirement to submit year-end financial statements.

The responses of Rec & Park and Beach Chalet are attached to this report as appendices A and B, respectively. CSA's comments on Beach Chalet's response are attached as Appendix C. CSA will work with Rec & Park to follow up on the status of the recommendations made in this report.

CSA appreciates the assistance and cooperation of Rec & Park and Beach Chalet staff during the audit. For questions about the report, please contact me at [Tonia.Lediju@sfgov.org](mailto:Tonia.Lediju@sfgov.org) or 415-554-5393.

Respectfully,



Tonia Lediju  
Director of City Audits

cc: Mayor  
Board of Supervisors  
Budget Analyst  
Citizens Audit Review Board  
City Attorney  
Civil Grand Jury  
Public Library

## INTRODUCTION

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### **Audit Authority**

The Office of the Controller (Controller) of the City and County of San Francisco (City) has authority under the San Francisco Administrative Code, Chapter 10, Article 1, Section 10.6-2, to audit, at regular intervals, all leases of city-owned real property where rent of \$100,000 or more a year is to be paid to the City. Also, the city charter provides the Controller's City Services Auditor Division (CSA) with broad authority to conduct audits. The CSA Audits Unit conducted this audit under that authority and pursuant to an audit plan agreed to by the Controller and the Recreation and Park Department (Rec & Park).

### **Background**

The Beach Chalet, L.P., (Beach Chalet) has a lease agreement (lease) with the City and County of San Francisco (City), acting through the Recreation and Park Commission. The lease provides for Beach Chalet to establish and operate the Beach Chalet Restaurant and Brewery at the Beach Chalet Building (building), which the City owns. The lease has an effective date of June 19, 1995. The lease term is for 20 years, beginning on the first day of business operations by Beach Chalet, which was December 31, 1996.

The lease requires that Beach Chalet pay the greater of the minimum monthly rent of \$6,000 per month (\$72,000 per year) or an amount equal to the total specified percentages of Beach Chalet's gross receipts for its different sales categories. These categories and percentages are as follows:

- 10 percent of sales of alcoholic beverages
- 6 percent of sales of food, nonalcoholic beverages, and retail goods
- 4 percent of all other gross receipts

### **Scope and Methodology**

The purpose of this audit was to determine whether:

- The monthly statements and the deposits of gross receipts submitted by Beach Chalet to Rec & Park were correct and timely.
- Beach Chalet's monthly statements accurately

Office of the Controller, City Services Auditor  
Beach Chalet Owes the City \$53,208 for Paying Its Rent Late in 2009 Through 2011

reported its gross receipts and deductions for janitorial supplies expenditures based on monthly and daily records.

- Beach Chalet has no overdue payments payable to Rec & Park for the audit period.
- Beach Chalet reported its microbrewery's revenue and expenditures to Rec & Park.

The audit covered the period January 1, 2009, through December 31, 2011.

To conduct the audit, CSA:

- Examined the applicable terms of the lease and the adequacy of Beach Chalet's procedures for collecting, recording, summarizing, and reporting its gross revenues to Rec & Park.
- Reviewed the calculations in documents that Beach Chalet submitted to Rec & Park following each of the audit period's three years.
- Tested on a sample basis Beach Chalet's reported monthly sales to general ledger reports of sales.
- Tested on a sample basis Beach Chalet's daily sales reports with the sales receipts.
- Reviewed invoices to determine whether Beach Chalet's minimum monthly rent payments properly deducted janitorial expenses.
- Reviewed Beach Chalet's monthly and annual rent payments and any late fees paid to assess whether Beach Chalet owes any overdue payments for the audit period.
- Interviewed Beach Chalet's proprietor and observed use of Beach Chalet's point-of-sale system regarding how sales are recorded.

**Statement of Auditing Standards**

This performance audit was conducted in accordance with generally accepted government auditing standards. These standards require planning and performing the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for the findings and conclusions based on the audit objectives. We believe that the evidence obtained provides a reasonable basis for the findings and conclusions based on the audit objectives.

## AUDIT RESULTS

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*Beach Chalet Correctly Reported Its Gross Sales, but Paid Some Rent Late, Made Unallowed and Unsupported Deductions from Its Rent, and Did Not Comply With Certain Other Lease Provisions*

From January 1, 2009, through December 31, 2011, Beach Chalet, L.P. (Beach Chalet) reported gross sales of \$25,377,237 and paid \$1,562,997 in percentage rent to the Recreation & Park Department (Rec & Park). Exhibit 1 presents Beach Chalet's reported gross sales and the rents paid during the audit period.

<b>EXHIBIT 1</b>	<b>Gross Revenues Reported and Rents Paid January 1, 2009, Through December 31, 2011</b>	
<b>Period</b>	<b>Gross Sales Reported</b>	<b>Rent Paid</b>
January 1, 2009 – December 31, 2009	\$8,920,485	\$548,065
January 1, 2010 – December 31, 2010	\$8,403,215	\$521,819
January 1, 2011 – December 31, 2011	\$8,053,537	\$493,113
<b>Total</b>	<b>\$25,377,237</b>	<b>\$1,562,997</b>

Source: Rec & Park's Revenue Tracking System (RTS)

The percentage rent, paid yearly for the preceding year, is in addition to the \$72,000 per lease year in minimum monthly due from Beach Chalet to Rec & Park. However, Beach Chalet paid far less than \$72,000 per year in net monthly rent due to deductions and may have received unallowable or incorrect deductions to its minimum monthly rent payments. Also, Beach Chalet submitted some rental payments after their due dates, entitling Rec & Park to assess and collect late fees and interest charges, which Rec & Park did not do. Rec & Park also did not enforce lease provisions requiring Beach Chalet to submit annual tax returns, year-end financial statements, and statements of its gross sales and statements certifying the correctness of the percentage rents payable to Rec & Park. These findings are presented in detail below.

**Finding 1**

**Beach Chalet owes \$53,175 in late payment fees and \$33 in interest charges for late rental payments, totaling \$53,208.**

Beach Chalet paid both its annual percentage rent and

minimum monthly rent late on some occasions but, contrary to the lease, Rec & Park did not assess or collect late fees or interest charges. Beach Chalet owes Rec & Park \$53,208, consisting of late fees of \$52,059 for annual percentage rent paid late, \$1,116 for monthly minimum rent paid late, and \$33 for interest charges on late rental payments.

The lease, Section 5.4, states that if the minimum monthly rental is not delivered by the tenth day of the month, or the percentage rent, if any, and required accompanying documents are not delivered within 90 days after the end of each lease year, Rec & Park shall assess a late charge. This charge is to be 5 percent of the total outstanding balance due, including all delinquent charges and accruals. Also, any unpaid balance carried forward to a subsequent period is to be charged interest at 1 percent per month for each month or fraction of a month the payment remains delinquent.

According to Rec & Park, it agreed with Beach Chalet that the postmark date on the envelopes of Beach Chalet's rent payment would be considered the delivery date and, if a postmark date was not present, the check date would be recorded as the delivery date. Rec & Park could not provide this agreement to CSA in writing, and it appears that the agreement was never documented. Nonetheless, even by this unwritten agreement, Beach Chalet's 2009 and 2011 annual percentage rent payments to Rec & Park were late. That is, both of these payments were dated more than 90 days after the end of each of the lease years, resulting in a total of \$52,059 in late fees due. Beach Chalet also delivered some of its monthly rent payments to Rec & Park after the tenth of the month, resulting in a total of \$1,116 in late fees due and \$33 in interest charges due, but Rec & Park did not assess any of these fees.

Exhibit 2 displays Beach Chalet's minimum monthly rent and percentage rent paid late, the corresponding late fees, which do not include interest charges, and the number of days the percentage rent was late.

**EXHIBIT 2 Beach Chalet's Minimum Monthly Rent and Percentage Rent Paid Late, Late Fees, and Number of Days Percentage Rent Was Paid Late January 1, 2009, Through December 31, 2011**

Period	Minimum Monthly Rent Paid Late	Minimum Monthly Rent Late Fees	Annual Percentage Rent Paid Late	Annual Percentage Rent Late Fees	Days Percentage Rent Paid Late
January 1, 2009 – December 31, 2009	\$4,762	\$238	\$548,065	\$27,403	1
January 1, 2010 – December 31, 2010	8,485	424	-	-	-
January 1, 2011 – December 31, 2011	9,086	454	493,113	24,656	2
<b>Total</b>	<b>\$22,333</b>	<b>\$1,116</b>	<b>\$1,041,178</b>	<b>\$52,059</b>	

**Recommendations**

The Recreation and Park Department should:

1. Collect \$53,175 in late fees and \$33 in interest charges, totaling \$53,208, owed by Beach Chalet for paying its rent late.
2. Develop and implement a process for identifying late rental payments from Beach Chalet and for assessing, billing, and collecting late fees and interest charges from Beach Chalet for late rent payments.

**Finding 2**

**Beach Chalet received \$97,632 in rent deductions for estimated city water usage based on a formula that is not in the lease and that may not accurately reflect actual water usage by the parties.**

Beach Chalet receives from Rec & Park a 40 percent discount on the billed cost of the building's water usage despite there being no basis in fact for this estimate. The discount, in the form of a rent deduction, is intended to compensate Beach Chalet for the estimated water usage and wastewater charges at the building attributable to the City. However, the formula for determining relative water usage by Beach Chalet and the City is not in the lease. Moreover, neither Rec & Park nor Beach Chalet could provide evidence to CSA that the formula is documented or reasonable.

Based on this formula, Beach Chalet deducted \$97,632 from its rent during the audit period. The monthly water charges at the building average \$6,780, so Beach Chalet received an average monthly rent deduction of \$2,712 for water usage

during the audit period.

The first amendment to the lease, Section 22.1, states that the City will install “deduct meters” to measure water usage in the building. The San Francisco Water Department was to then bill Beach Chalet for its water usage and associated sewer charges measured by the meters. However, although the City did install water meters, they do not capture only Beach Chalet’s water usage as anticipated, but also include usage by the City. Because the meters fail to distinguish the water usage of the two parties, Beach Chalet may be receiving incorrect rent deductions, causing incorrect rent payments to Rec & Park.

### Recommendations

The Recreation and Park Department should:

3. Document the agreement to allocate 40 percent of the building’s metered water usage to the City and deduct the cost of that usage from Beach Chalet’s rent.
4. Until and unless meters can be installed that will separate the water usage of the City and Beach Chalet at the building, reevaluate—in consultation with Beach Chalet—the formula for estimating the parties’ respective water usage and document any changes to the formula in the written agreement.

### Finding 3

**Beach Chalet underpaid its rent by an average of \$236 per month for six tested months because it deducted the cost of janitorial supplies not listed in the lease as a joint expense.**

The lease allows Beach Chalet to deduct from its rent half of the costs it incurs for specified restroom janitorial supplies. For six selected months tested, the invoices for janitorial supplies that Beach Chalet provided to Rec & Park contained items not listed in the lease, including gloves, mats, baby table service, and sani-services, totaling \$2,831. Beach Chalet received rent deductions for half of the costs, which totaled \$1,415, or an average of \$236 per month.

The lease, Section 25.2(c), states that Beach Chalet and Rec & Park are jointly responsible for supplying the following restroom janitorial supplies: toilet seat covers and disposable sanitary napkin bags, roll towels and/or flat fold towels, large



roll toilet tissue and/or flat fold toilet tissue, hand soap, bleach, toilet bowl cleaner and disinfectant, cleansers, rags, mops, garbage bag liners, brooms, hand brushes, and sponges.

Beach Chalet is to furnish all necessary listed supplies and bill Rec & Park for 50 percent of the costs by submitting copies of the original invoices for the supplies to Rec & Park. Rec & Park is then to reimburse Beach Chalet through a credit against its minimum monthly rent. The lease also provides that these specifications are subject to review and revision from time to time by mutual agreement between the parties.

#### Recommendations

The Recreation and Park Department should:

5. Review the lease, Section 25.2(c), and the janitorial invoices submitted by Beach Chalet for the audit period and determine whether the department and Beach Chalet agreed to revise the list of jointly responsible restroom janitorial supplies.
6. Record any revisions that it made with Beach Chalet to the list of restroom janitorial supplies in the lease, Section 25.2(c).
7. Recover from Beach Chalet the value of any improperly deducted janitorial supplies for the audit period.
8. Document any future agreements with Beach Chalet to revise the list of jointly responsible restroom janitorial supplies.

#### Finding 4

**Some of Beach Chalet's expense claims for janitorial supplies differ slightly from the vendor invoices Beach Chalet submitted or are not addressed by the lease, resulting in incorrect or unallowable rent deductions.**

Some janitorial supplies expense claims, which result in rent deductions that Beach Chalet submitted to Rec & Park, show small inconsistencies with the vendor invoices on which they were based. Although the differences are very small, were in Rec & Park's favor, and are based only on six test months, this is a problem because larger differences in other months, including ones that could be in Beach Chalet's favor, may

have gone undetected by Rec & Park. Examples of the inconsistencies include:

- Beach Chalet's janitorial supplies invoice for July 27, 2009, through August 23, 2009 did not include its expenses for scrub pads in the amount of \$22.60, which Beach Chalet should have deducted from its rent.
- Beach Chalet recorded 25 percent of the total \$478.48 purchase price for trash liners to be \$94.92 on its janitorial supplies invoice for August 22, 2011, through September 25, 2011, but the actual amount is \$119.62, so Beach Chalet should have deducted an additional \$24.70 from its rent.

Also, for five of the six test months, Beach Chalet claimed 25 percent of its total trash liner costs of \$1,086.48, or \$272, as a shared janitorial expense. However, the lease does not provide for this (or any) method for determining the parties' shares of trash liner costs. Also, Beach Chalet did not appear to have followed this method in its janitorial supplies invoice for December 27, 2010, through January 23, 2011, to Rec & Park, which included the total trash liner costs of \$157.32, rather than only 25 percent of the costs, as a shared expense.

The lease, Section 25.2 (c), states that Beach Chalet will submit with its janitorial supply invoices to Rec & Park, copies of the original invoices for the cost of the supplies. Rec & Park stated that Beach Chalet probably submitted the invoices, but due to a change in Rec & Park personnel and an office move, the documents may have been misplaced or accidentally discarded. Because Rec & Park could not provide to CSA Beach Chalet's janitorial supply invoices for the six test months, the audit tested invoices provided to CSA by Beach Chalet.

## Recommendations

The Recreation and Park Department should:

9. Before authorizing rent credits, develop and implement a process for documenting its review of Beach Chalet's janitorial supply invoices and for verifying amounts against the original vendor invoices.

10. Establish a system for maintaining janitorial supply invoices submitted by Beach Chalet.
11. Obtain and compare janitorial supply invoices to vendor invoices submitted by Beach Chalet for the audit period and correct any incorrect minimum monthly rent deductions.

**Finding 5**

**Beach Chalet did not fulfill lease requirements to submit—and Rec & Park did not request—annual statements of gross sales or annual statements certifying the correctness of the percentage rent payable.**

Beach Chalet did not meet the requirements of the lease regarding submittal of a statement of its gross sales for each year or a certified statement of the correctness of its annual percentage rent payment. The lease, Section 5.3(a)(i), requires that within 30 days following the end of each lease year, Beach Chalet must provide Rec & Park a statement of Beach Chalet's gross sales for the preceding lease year. Within 90 days following the end of each lease year, Beach Chalet must provide Rec & Park a statement certified as correct by Beach Chalet of the percentage rent payable for the lease year just ended. The lease specifies that the latter statement should set forth Beach Chalet's gross receipts for the lease year and the manner in which the percentage rent, if any, was calculated.

Beach Chalet sends Rec & Park only one annual statement each year. Sent approximately 90 days following the end of each lease year, it is a spreadsheet of Beach Chalet's percentage rent calculation that accompanies the percentage rent payment to Rec & Park. This spreadsheet includes the amount of gross sales for the preceding year, but it is not provided within 30 days of the end of the lease year. Beach Chalet's proprietor stated that the lease provision requiring year-end statements probably refers to the spreadsheet of gross sales with percentage rent calculations that Beach Chalet submits to Rec & Park after each lease year. He also stated that Rec & Park has not asked Beach Chalet to comply with these lease requirements.

**Recommendations**

The Recreation and Park Department should:

12. Review and clarify with Beach Chalet what the lease, Section 5.3, requires of Beach Chalet regarding a statement setting forth its gross sales for the preceding year and a certified statement of the correctness of its annual percentage rent.
13. Document in writing the clarification of the statement requirements in the lease, Section 5.3.
14. Ensure that Beach Chalet complies with the statement requirements in the lease, Section 5.3

**Finding 6**

**Beach Chalet does not submit tax returns to Rec & Park and it is unclear if Beach Chalet submits year-end financial statements.**

Rec & Park could not provide CSA copies of Beach Chalet's tax returns or year-end financial statements. The lease, Section 16.3, states that Beach Chalet was to submit to Rec & Park at the end of Beach Chalet's 2009, 2010, and 2011 fiscal years, copies of its "operations tax returns," which refer to annual tax returns, according to Rec & Park, and year-end financial statements. Rec & Park's property management office is to keep these copies in its permanent records.

According to its proprietor, Beach Chalet has not submitted tax returns to Rec & Park. He believes that the lease requirement for year-end financial statements may be met by the spreadsheets that Beach Chalet prepares and submits to Rec & Park following each lease year to report Beach Chalet's gross sales and calculation of its percentage rent. He further stated that Rec & Park has not requested these documents from Beach Chalet.

**Recommendations**

The Recreation and Park Department should:

15. Review and clarify with Beach Chalet what the lease, Section 16.3, requires regarding submission of Beach Chalet's tax returns and year-end financial statements.
16. Document the clarification of the requirement in the lease, Section 16.3, regarding tax returns and year-end financial statements.

**Office of the Controller, City Services Auditor  
Beach Chalet Owes the City \$53,208 for Paying Its Rent Late in 2009 Through 2011**

17. Use the documentation that is to be submitted by Beach Chalet to verify the accuracy and completeness of its reported gross sales.
  
18. Maintain at its offices the tax returns and year-end financial statements submitted by Beach Chalet.

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## APPENDIX A: DEPARTMENT RESPONSE

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Edwin M. Lee, Mayor  
Philip A. Ginsburg, General Manager

November 12, 2013

Tonia Lediju  
Director of City Audits  
City Hall, Room 476  
1 Dr. Carlton B. Goodlett Place  
San Francisco, CA 94102

Dear Ms. Lediju:

The Recreation and Park Department would like to thank you and your staff for the diligent work on the recently completed audit on the lease between The Beach Chalet, LP and the City and County of San Francisco.

Responses to your recommendations are attached along with estimated dates for completion, where appropriate.

The professionalism and patience displayed by your staff throughout this process has been greatly appreciated.

Sincerely,

A handwritten signature in black ink that reads "Katharine E. Petrucione".

Katharine E. Petrucione  
Director of Administration and Finance

cc: Nicholas Kinsey, Director of Property  
Mark A. Tipton  
Irene Chiu

For each recommendation, the responsible agency should indicate whether it concurs, does not concur, or partially concurs. If it concurs with the recommendation, it should indicate the expected implementation date and implementation plan. If the responsible agency does not concur or partially concurs, it should provide an explanation and an alternate plan of action to address the identified issue.

## RECOMMENDATIONS AND RESPONSES

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Recommendation	Response
The Recreation and Park Department should:	
1. Collect \$53,175 in late fees and \$33 in interest charges, totaling \$53,208, owed by Beach Chalet for paying its rent late.	The Department concurs. RPD has issued an invoice for payment of past due amounts.
2. Develop and implement a process for identifying late rental payments from Beach Chalet and for assessing, billing, and collecting late fees and interest charges from Beach Chalet for late rent payments.	The Department concurs. The Department has already issued an RFP to procure lease management software to assist in managing all leases. The Department has selected Yardi as responsive to that RFP and is negotiating a contract for such software. The Department anticipates beginning implementation within the next six months and for implementation to be completed within 12 months.
3. Document the agreement to allocate 40 percent of the building's metered water usage to the City and deduct the cost of that usage from Beach Chalet's rent.	The Department concurs. RPD will formally document the 40 percent usage by the City until Recommendation 4 is implemented. This documentation will be completed by December 2, 2013.



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Recommendation	Response
<p>4. Until and unless meters can be installed that will separate the water usage of the City and Beach Chalet at the building, reevaluate—in consultation with Beach Chalet—the formula for estimating the parties' respective water usage and document any changes to the formula in the written agreement.</p>	<p>The Department concurs. Analysis will be conducted on the various water uses in the building to arrive at a more accurate allocation of this expense. This should be done and implemented no later than March 31, 2014. RPD feels retrofitting meters at the various points of use is not feasible.</p>
<p>5. Review the lease, Section 25.2(c), and the janitorial invoices submitted by Beach Chalet for the audit period and determine whether the department and Beach Chalet agreed to revise the list of jointly responsible restroom janitorial supplies.</p>	<p>The Department concurs. It is expected for this to be accomplished by December 31, 2013.</p>
<p>6. Record any revisions that it made with Beach Chalet to the list of restroom janitorial supplies in the lease, Section 25.2(c).</p>	<p>The Department concurs. This will be accomplished along with Recommendation #5.</p>
<p>7. Recover from Beach Chalet the value of any improperly deducted janitorial supplies for the audit period.</p>	<p>The Department concurs. We will review the documentation prior to December 31, 2013 and submit any outstanding charges to the concessionaire.</p>
<p>8. Document any future agreements with Beach Chalet to revise the list of jointly responsible restroom janitorial supplies.</p>	<p>The Department concurs.</p>

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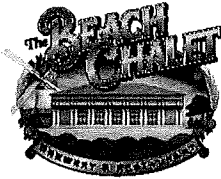
Recommendation	Response
9. Before authorizing rent credits, develop and implement a process for documenting its review of Beach Chalet's janitorial supply invoices and for verifying amounts against the original vendor invoices.	The Department concurs. RPD staff will meet with Lessee to review schedule and expenses for all janitorial services provided for the Visitor Center and public restrooms. That meeting will be held and the process formulated by December 31, 2013. The Department anticipates that this process will be streamlined with the implementation of the Yardi software in 2014.
10. Establish a system for maintaining janitorial supply invoices submitted by Beach Chalet.	The Department concurs. This will be done by December 2, 2013. The Department anticipates that this process will be streamlined with the implementation of the Yardi software in 2014.
11. Obtain and compare janitorial supply invoices to vendor invoices submitted by Beach Chalet for the audit period and correct any incorrect minimum monthly rent deductions.	The Department concurs. Notification will be sent to the Lessee to submit original vendor invoices for reimbursement. This will be done by December 2, 2013.
12. Review and clarify with Beach Chalet what the lease, Section 5.3, requires of Beach Chalet regarding a statement setting forth its gross sales for the preceding year and a certified statement of the correctness of its annual percentage rent.	The Department concurs. RPD will review and clarify the terms in Section 5.3 of the lease with the Lessee, will document the findings and send notification to the Lessee no later than December 2, 2013.
13. Document in writing the clarification of the statement requirements in the lease, Section 5.3.	The Department concurs. RPD will review and clarify the terms in Section 5.3 of the lease with the Lessee, will document the findings and send notification to the Lessee no later than December 2, 2013.

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Recommendation	Response
14. Ensure that Beach Chalet complies with the statement requirements in the lease, Section 5.3.	The Department concurs. RPD will review and clarify the terms in Section 5.3 of the lease with the Lessee, will document the findings and send notification to the Lessee no later than December 2, 2013.
15. Review and clarify with Beach Chalet what the lease, Section 16.3, requires regarding submission of Beach Chalet's tax returns and year-end financial statements.	The Department concurs. RPD will issue a statement clarifying the requirement for tax returns and year-end statements as stipulated in Section 16.3. A statement will be sent to the Lessee not later than December 2, 2013.
16. Document the clarification of the requirement in the lease, Section 16.3, regarding tax returns and year-end financial statements.	The Department concurs. RPD will track receipt of any documentation due.
17. Use the documentation that is to be submitted by Beach Chalet to verify the accuracy and completeness of its reported gross sales.	The Department concurs. RPD will cross-check the annual statement of gross earnings against both the annual tax returns and the payments of percentage rent each year.
18. Maintain at its offices the tax returns and year-end financial statements submitted by Beach Chalet.	The Department concurs. Going forward, RPD will maintain clear and accessible records of such financial documents.

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## APPENDIX B: TENANT RESPONSE



Tonia Lediju  
Director of City Audits  
City Hall, Room 476  
1 Dr. Carlton B. Goodlett Place  
San Francisco, CA 94102

Dear Ms. Lediju,

This letter is in response to the draft audit document report concerning the lease agreement between the Beach Chalet, L.P. and the City and County of San Francisco, through the Recreation and Parks Commission.

The Beach Chalet has the following comments regarding your audit findings:

- We do not agree with Finding 1.
  - We do not agree with the finding that the payments were late based on Rec & Parks systems of acceptance.
  - The Beach Chalet, L.P. has never received notice of late payments.
  - The Beach Chalet, L.P. is not aware of the Departments statement regarding recording of the payments based on delivery date or check date.
  - Payments have been regularly hand delivered by the Proprietor to the Rec & Park Department Property Management staff based on a scheduled meeting time agreed to by the Rec & Park Staff. Rec & Park staff have always been aware of delivery dates.
  
- We do not agree with Finding 2.
  - Utility meters ARE installed in the building and accurate meter counts and water billing have been used to determine the past usage numbers. These calculations have been sent to the Recreation and Park Department to determine the water usage.
  - The Water deduct meters are located in difficult to access locations, which make regular monthly monitoring a challenge.

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- Current usage and monitoring should be determined and verified to date.
- We do not agree with Finding 3.
  - There has been a verbal agreement between the Beach Chalet, L.P. and the Rec & Park Department regarding the items mentioned and usage. It was understood between both parties that the lease list of items was incomplete and actual supplies would be used.
  - All janitorial invoices have been sent to the Department, reviewed by Department Staff, and the Beach Chalet, L.P. received written approved prior to any credits taken.
- We do not agree with Finding 5.
  - Each year the Beach Chalet L.P. provides the Rec & Park Department with a statement of Gross Receipts.
  - We do not agree with the statement as documented by the auditor: “Beach Chalet’s proprietor stated that the Beach Chalet does not submit a statement of its annual gross sales for the preceding year or a certified statement of the correctness of its annual percentage rent. He stated that the lease provision probably refers to the spreadsheets of gross sales with percentage rent calculations that Beach Chalet submits to Rec & Park after each lease year. He also stated that Rec & Park has not asked Beach Chalet to comply with these lease requirements.”

The proprietor actually stated:  
The gross sales statement that is sent to the City is provided to the Beach Chalet, L.P. and certified for accuracy by their CPA firm Burr Pilger Mayer and is in line with all tax filings.

The Proprietor actually stated:  
Rec & Park has not asked us to comply with “the auditors” opinion of what she thought was an annual statement certifying the correctness of the percentage rent payable.  
It was explained that the spreadsheet that was provided to the Rec & Part Department was the document. Proprietor agrees to modify the cover letter to define this in future years. Also, proprietor states that the Rec & Park Department has never asked the Beach Chalet, L.P. to provide anything other than the statement spreadsheet that has been provided for years. This

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comment has nothing to do with "not complying with lease requirements."

- We do not agree with a portion of Finding 6.
  - The Beach Chalet, L.P. has provided appropriate year-end financial statements.

Should you have any questions, please feel free to contact me.

Sincerely,

Greg Gar Truppelli  
President

Beach Chalet Brewery & Restaurant 1000 Great Highway, San Francisco, CA 94121

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## **APPENDIX C: AUDITOR COMMENTS ON BEACH CHALET'S RESPONSE**

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To provide clarity and perspective, CSA is commenting on Beach Chalet's response to the audit report. Beach Chalet disagrees with findings 1, 2, 3, 5 and a portion of 6.

### Finding 1: Late Fees and Interest Charges

In its response, Beach Chalet states that it disagrees with the finding that its rent payments were late based on Rec & Park's system of accepting rent payments. Beach Chalet states that it was unaware of Rec & Park's willingness to consider the check date or postmark date as the date paid, and notes that Rec & Park did not notify Beach Chalet that the payments were late. However, the requirements of Beach Chalet's lease clearly indicate that the payments were late and that Rec & Park is entitled to late charges.

The lease, Section 5.4, states the required due dates of the rent payments and how late fees and interest charges are to be assessed. Rec & Park has a copy of each of Beach Chalet's rent checks for the audit period and the envelope in which it was delivered (stamped with the U.S. Mail postmark date). The payments noted as late in the audit report were late based on the deadline in the lease, even accounting for the fact that the unwritten agreement to use the check date or envelope postmark date as the date paid may have given Beach Chalet more time to provide the rent payments than the lease allows. Dates on checks and postmarks may precede or be the same as the dates Rec & Park received the checks, so the payments in Finding 1 were late by any measure.

Furthermore, Rec & Park can assess late charges regardless of whether it immediately notifies Beach Chalet that its rent payments were late, and acceptance of late charges does not release Beach Chalet from paying overdue rent amounts. The lease, Section 5.5, provides that: "Acceptance of any late charges(s) shall not constitute a waiver of Lessee's default with respect to the overdue amount, or prevent the Lessor from exercising any of the other rights and remedies available to Lessor." By accepting Beach Chalet's rental payments, Rec & Park did not waive its rights to assess and collect late payment fees and interest charges under the lease.

### Finding 2: Rent Deductions for Estimated City Water Usage

In its response, Beach Chalet states that it disagrees with the finding that Beach Chalet received rent deductions for estimated city water usage based on a formula that is not in the lease and may not accurately reflect actual water usage by the parties. Beach Chalet's response states that utility meters were installed in the building and accurate meter counts and water billing have been used to determine the past usage numbers. The response also notes that the regular monthly monitoring of the water deduct meters is a challenge due to

their difficult-to-access locations, and that current usage and monitoring should be determined and verified to date.

The report states that deduct meters were installed on Beach Chalet's premises, just as Beach Chalet's response notes. The issue, however, is that these meters do not only measure Beach Chalet's water usage—as intended by the lease, Section 22.1(a)—but also capture some of the City's water usage on the premises. If the meters functioned as intended by the lease, there would be no issue as to how much water Beach Chalet uses and should pay for. (Section 22.1 (a) states that deduct meters will be installed to measure Beach Chalet's water usage, and the San Francisco Water Department will bill Beach Chalet for all water usage and associated sewer charges as measured by the meters.) Because the meters cannot precisely measure the water used by Beach Chalet or the water used by the City on the premises, deduct meter readings were used to arrive at an estimated percentage, agreed to by the parties, that is used as the basis of Beach Chalet's rent discount for water usage. As the report notes, this percentage is an estimate that is not documented in the lease or elsewhere. Because neither Beach Chalet nor Rec & Park could provide CSA with documentation of the basis of the percentage used, the audit could not assess whether the percentage and resulting rent discounts are reasonable.

### Finding 3: Janitorial Supplies

In its response, Beach Chalet states that it disagrees with the finding that it underpaid its rent due to deducting—as a joint expense with Rec & Park—the cost of janitorial supplies not listed in the lease. The response refers to a verbal agreement that Beach Chalet had with Rec & Park that the list of items in the lease was incomplete, that all actual supplies purchased by Beach Chalet would be used instead, and that Rec & Park approved the credits taken by Beach Chalet. However, the audit found no evidence of such an agreement, verbal or written, so must consider the lease binding.

The lease, Section 25.2(c), lists specific types of janitorial supplies, the cost of which will be expenses shared by Beach Chalet and Rec & Park. The lease further states that the specifications are subject to review and revision from time to time if the parties agree. The lease, Section 50.0, states that “no alteration or variation of the terms of this Lease shall be valid unless made in writing and signed by the parties hereto, and that no oral understandings or agreements incorporated herein, and no alteration or variations of the terms hereof, unless made in writing between the parties hereto, shall be binding on any of the parties hereto.”

### Finding 5: Annual Statements

In its response, Beach Chalet states that it disagrees with the finding that it does not submit annual statements of its gross sales or annual statements certifying the correctness of the percentage rent payable to Rec & Park. Its response states that each year Beach Chalet submits a statement of its gross receipts to Rec & Park in the form of the spreadsheet of its

gross sales. The response also states that its gross sales statement is certified for accuracy by Beach Chalet's CPA firm and is Beach Chalet's annual statement certifying the correctness of the percentage rent payable. However, Beach Chalet does not fulfill what is required by the lease in regard to annual statements.

As the report states, the lease, Section 5.3(a)(i), requires annual statements of Beach Chalet's gross sales for the preceding lease year within 30 days following the end of each lease year. Thus, the spreadsheet that Beach Chalet submits approximately 90 days after each lease year, along with the percentage rent check, does not meet this lease requirement. Moreover, the spreadsheets do not meet the lease requirement that the annual statements due 90 days after each lease year must be certified as correct by Beach Chalet. Although these spreadsheets may be prepared by (or based on work by) Beach Chalet's CPA firm, they do not indicate that either Beach Chalet or anyone else certifies the correctness of the percentage rent payable for the lease year ended. Thus, Beach Chalet did not comply with the requirements of the lease, Section 5.3(a)(i).

#### Finding 6: Tax Returns and Year-End Financial Statements

In its response, Beach Chalet states that it disagrees with the portion of the finding that it does not submit year-end statements. As the report states, the lease, Section 16.3, does not describe the required year-end financial statements. Thus, it is unclear whether the spreadsheets that Beach Chalet submits with its annual percentage rent payments qualify as year-end financial statements. As a result, Recommendation 15 states that Rec & Park should review and clarify with Beach Chalet the requirements of the lease, Section 16.3. Finding 6 has been changed to reflect that it is unclear whether what Beach Chalet submits meets the lease requirement for year-end financial statements.

