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South County Tourism Council

Special Review of

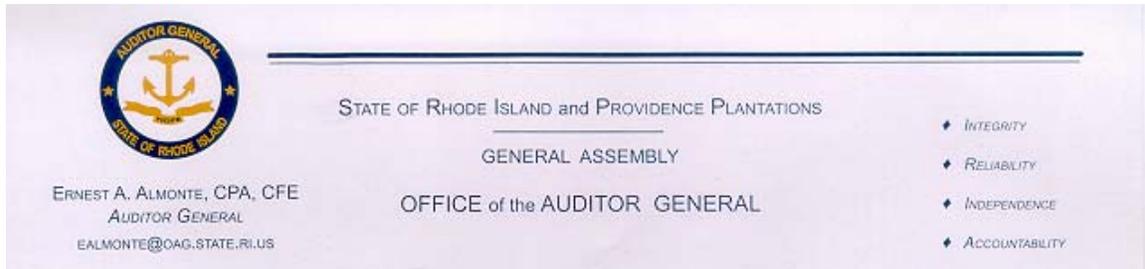
Polices and Procedures

February 2005

Ernest A. Almonte, CPA, CFE  
Auditor General

State of Rhode Island and Providence Plantations  
General Assembly  
Office of the Auditor General

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February 15, 2005

JOINT COMMITTEE ON LEGISLATIVE SERVICES

SPEAKER William J. Murphy

Senator Joseph A. Montalbano  
Senator Dennis L. Algieri  
Representative Gordon D. Fox  
Representative Robert A. Watson

We have completed a special review of policies and procedures at the South County Tourism Council. Our report is included herein.

Sincerely,

Ernest A. Almonte, CPA, CFE  
Auditor General

**SOUTH COUNTY TOURISM COUNCIL**

SPECIAL REVIEW OF POLICIES AND PROCEDURES

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## **I. INTRODUCTION**

### **OBJECTIVES, SCOPE AND METHODOLOGY**

We conducted a special review of policies and procedures at the South County Tourism Council. Our review primarily covered the period from July 1, 2002 to June 30, 2004. Where relevant, we extended our review to the current fiscal year.

Our objective was to identify practices and procedures that could be improved or made more efficient. We reviewed relevant policies and procedures, interviewed responsible personnel, and performed tests and other procedures as considered necessary in the circumstances.

### **BACKGROUND**

The South County Tourism Council was formed in 1986 to coordinate and promote the development and growth of tourism in the southern area of Rhode Island. The communities included in the Council consist of Charlestown, Coventry, East Greenwich, Exeter, Hopkinton, Narragansett, North Kingstown, Richmond, South Kingstown, Westerly, and West Greenwich. The Council operates as a not-for-profit corporation and is not an agency or department of the State of Rhode Island.

The Council is governed by a 22-member Board of Directors (two from each of the 11 communities listed above). The Council presently has three full-time employees: the President, who is responsible for management and direction of the Council, daily operations, and attendance at tourism events; the Director of Marketing; and the Marketing/Promotion Coordinator. In addition, the Council has a part-time tourism counselor, and seasonal volunteers. The current President was appointed in September 2004.

The Council derives the bulk of its revenues from the State hotel room tax. In fiscal 2004, approximately 85% of its total revenue of \$590,502 was from this source. The remainder of the Council's revenues is from advertising and other income. Total operating expenses in fiscal 2004 were \$605,412. Unrestricted net assets at June 30, 2004 totaled \$284,723.

The Council leases space in a state-owned facility in Wakefield.

## **II. FINDINGS AND RECOMMENDATIONS**

### **HOTEL INVESTMENT**

Our review disclosed that the South County Tourism Council invested \$97,500 in a private enterprise without exercising due diligence; failed to properly monitor the investment; and used hotel tax revenue in noncompliance with state economic development guidelines. The Council and its independent outside auditor now consider the investment worthless.

On August 12, 2002, the Council held a special meeting to discuss the possibility of becoming a participating partner in the purchase of the Lighthouse Inn, a hotel in the Galilee area of Narragansett, which was being purchased for \$4.1 million. We were informed that the developers of the hotel project needed the additional investment in order to close their purchase of the property. The Council's interest in hotel development in South County had been prompted by an outside consultant's report in 2001, which called for development of year-round hotel facilities in the area. The Council had not established any policy at that time for supporting a loan or investment in a private business.

On August 15, 2002, the Board voted at another special meeting to invest \$84,500 as a capital contribution for a 6.5% equity interest in the hotel project; an additional \$13,000 was loaned to the ownership of the hotel. Five members of the Board voted in favor of the investment; one member was opposed and three abstained (the Board has 22 members but only seven members are needed to be present for a quorum).

#### **Compliance with Special Meeting Notice Requirements**

We noted that the Board's own bylaws require a five-day notice to board members before a special meeting is held; this meeting was held only three days after the previous meeting. Due to the significant nature of this project, we believe the Council should have observed its own five-day rule and rescheduled the meeting until such time as at least a majority of the Board membership would have been available to vote on this proposal.

#### **Due Diligence**

We found that the Council did not obtain timely independent information concerning the property or the investors prior to voting to approve the loan. For example, financial projections provided to the Council by the investors had not been updated since March 2002. The projections were based on a 30% increase in room and food/beverage revenue, and an 8% increase in room rates. Further, the investors had secured long and

short-term bank financing in April 2002 but were still seeking additional financing four months later. In addition, the Chair of the Council at that time informed us that no independent appraisal of the property was obtained.

As part of the agreement with the Lighthouse Inn owners, the Council was to receive quarterly financial reports on the status of its investment, and was to attend ownership meetings at the hotel. We found no evidence of the Board receiving financial reports. We noted that the investor group sustained a calendar year 2002 operating loss in excess of \$250,000; the Council's share of this loss was \$16,317. The former Chair of the Council informed us that he attended only one ownership meeting at the hotel.

Our review revealed that the Council was informed through a certified letter dated March 4, 2003 from the attorney for the prime lender on the hotel project that the owners of the hotel had defaulted on its loan, and that the owners would no longer be permitted to make payments on the Council's loan. We found no evidence in minutes of Council meetings that the Council took any action following receipt of this notice; the former Chair of the Council informed us that he was unaware of this notice.

#### Use of Hotel Tax Revenues

The Council had been informally advised in August 2002 by the state Director of Tourism to "only commit monies generated from areas other than the hotel tax." for this proposed investment. Although several board members and others we interviewed believed the investment was drawn from monies generated through advertising and other revenues of the Council that were maintained in a separate restricted fund, we found that the Council commingled its sources of revenue into a single operating account. Since the hotel tax distribution represents 85% of the Council's revenues, we believe it is appropriate to conclude that the major share of the hotel investment came from this source.

#### Policies and Procedures - Tourism Projects

The Council chose to provide substantial funding to a single enterprise without sufficient safeguards to ensure the safety of its investment and without policies and procedures regarding this type of investment.

We noted that development of a separate fund was discussed at the August 15, 2002 special board meeting. Also, in a letter to the state Director of Tourism the next day, the Council President stated, "a committee will be formed to structure a policy for revolving loans and investments for future tourism development projects." We were informed that the Council did not establish this committee.

We believe the Council should have adopted terms and conditions similar to those required for tourism loans issued by the state's Division of Tourism (part of the Rhode Island Economic Development Corporation). The RIEDC had established a \$500,000 hospitality/tourism fund at that time; however, the maximum loan amount for working

capital was set at \$10,000 and required the borrowers to personally guarantee the loan. The Council's loan exceeded this maximum and did not include a personal guarantee of repayment.

### RECOMMENDATION

1. Utilize the hotel room tax revenue solely for tourism marketing and promotion.

### Auditee Views:

*The South County Tourism Council concurs with this recommendation.*

### **EXPENSE DOCUMENTATION AND TIMELY PAYMENTS**

Our review of Council expenses for fiscal 2004 noted that several payments were remitted late, including premiums for worker's compensation and healthcare insurance for the Council's employees.

Payment to the worker's compensation insurance provider was remitted subsequent to the Council's receipt of the provider's notice of expiration. In addition, several of the payments made for healthcare coverage could not be traced to single invoices. The Council's accountant informed us that several invoices were combined into a single payment because the remittance was late. However, we could not verify the amount remitted to individual supporting invoices.

Payments made for expenses incurred on a corporate credit card were also late; the Council had to process an electronic funds transfer in June 2004 to satisfy the outstanding credit card balance. Lastly, we noted that two payments made to a vendor whose terms are net 15 days, exceeded 30 days.

We were unable to trace four of the fifty-two expenses examined to supporting documentation, including two receipts for deposits made at the local Post Office for future bulk mailings.

The Council should remit payments to insurance providers and vendors on a timely basis to ensure continuity of coverage and business relations. Also, the Council should secure and retain all supporting documentation for expenses incurred.

### RECOMMENDATIONS

2. Ensure timely payment of expenses.
3. Obtain sufficient documentation for purchases and deposits.

4. Establish appropriate procedures for the retention and filing of invoices for expenses incurred.

Auditee Views:

*The South County Tourism Council concurs. In September 2004, the Council hired an outside accountant for one day weekly to ensure that standard accounting procedures are being followed. The Council has also implemented an official accounting procedures manual.*

## **BIDDING PRACTICES AND CONTRACTS**

During our review, we noted that the Council did not obtain formal bids for major services rendered on behalf of the Council including accounting, auditing, legal representation, advertising/public relations, and printing services. We were informed that the Board generally approved cost proposals informally obtained by the former Council President for these services.

The Council did not consistently enter into contracts for these services. We noted signed agreements only for the current independent audit, and a similar letter for legal services dated July 2004.

The Council should procure bids for major services, select the lowest responsible bidder, and enter into formal contracts to ensure reasonable cost, continuity, and completion of service, and protection from increases in price. The Board of Directors should directly secure the services of an independent auditor and legal counsel in order to ensure independence from Council management. The Council should also form an audit committee to whom the independent auditors will report.

## **RECOMMENDATIONS**

5. Establish guidelines for bidding procedures.
6. Obtain signed contracts for major services provided to the Council.
7. Form an audit committee from Board members to whom the independent outside auditors will report.

Auditee Views:

*The South County Tourism Council concurs, and these recommendations have been implemented.*

## **MINUTES OF BOARD OF DIRECTORS MEETINGS**

Minutes of Board meetings during the period of the Council's investment in the Lighthouse Inn did not include evidence of discussions concerning the status of the hotel project. Several members of the Board recalled brief updates on the investment; however, none of these are reflected in the minutes.

The Council should ensure that the minutes are complete. All items listed on the agendas for the meetings should be addressed in the minutes, regardless of the brevity of the discussions. In the latter part of the summer 2004, the Council approved a measure to electronically record the meetings, and retain the recordings.

### **RECOMMENDATIONS**

8. Continue to record all meetings of the Board of Directors electronically, and retain the electronic version of the proceedings.
9. Review the minutes prior to issuance to ensure completeness and accuracy.

#### **Auditee Views:**

*The South County Tourism Council concurs and has been using an electronic recording device.*