

MIAMI BEACH

INTERNAL AUDIT REPORT

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TO: Jimmy L. Morales, City Manager *Am*
VIA: Mark D. Coolidge, Interim Internal Auditor *MDC*
FROM: Coral Vivolo, Auditor *av*

DATE: April 26, 2018
AUDIT: Fifth and Alton Parking Garage Financial Review
PERIOD: January 1, 2016 to December 31, 2017

This report is the result of a request made by the City's Parking Department to review the financial records of the Fifth and Alton Parking Garage, in which the City owns a portion (46%) of the parking spaces. This audit primarily focused on determining (1) whether operating expenses were properly allocated to the Garage as there are separate retail businesses on the property; (2) whether the annual Contributions due from the use of the parking spaces by the retail businesses were properly remitted, and (3) whether any excess monies in the operating account were properly distributed between the designated parties.

INTRODUCTION

In May 2005, the Mayor and City Commission adopted Resolution No. 2005-25899, approving a Development Agreement between the City of Miami Beach and AR&J Sobe, LLC (Developer) for the development of the project referred to as "Fifth and Alton," a public-private project whereby the City owns a portion of the parking spaces (46% of the approximately 1,100 parking spaces) of the multi-level commercial building used for supermarket/retail/restaurant space.

On December 30th, 2009, a Declaration of Condominium was recorded with the Miami-Dade County Clerks of Courts in which the terms of the Development Agreement were detailed. As per Section 10.4 of said Declaration, the Developer is responsible for operating, maintaining, and replacing all portions of the property in a first class manner; and the City is responsible for operating access, validation and collection systems for the Garage in a first class manner (subject to other provisions of the Declaration). In addition, the City and the Developer agreed on allocating all Garage related expenditures in proportion to the number of City owned spaces (500 or 46%) and Developer owned spaces (587 or 54%). Thus, as per Section 10.5 an operating bank account, accessible to both the Developer and the City, was created for all revenues to be deposited and all related operating expenses to be paid from.

In December 2012, AR&J Sobe, Inc. sold their beneficial ownership interests in the Garage to Edens Limited Partnership (Edens). As a result, Edens, in partnership with the City, became responsible for the operations of the Garage while the terms of the Declaration remained unchanged.

On a monthly basis, Edens is responsible for providing copies of the Garage's financial statements to the City's Finance Department who subsequently performs a cursory review searching for any non-Garage transactions, verifies the 46% vs. 54% allocation between the

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City and the Developer, and completes the bank reconciliation. Afterwards, the Finance Department prepares a summary financial sheet that is forwarded to the Parking Department to be used to determine Edens' financial position in relation to the approved budget and whether any monies need to be contributed to help meet operating expenses. The summary financial sheet is included as part of the department's monthly Parking Status Report.

OVERALL OPINION

Based on the results of our audit, it has been concluded that the Garage is essentially being operated in accordance with the terms of the Declaration of Condominium. However, it was noted that certain internal controls require enhancements due to the following deficiencies:

- Edens Limited Partnership (Edens) improperly allocated \$66,262 in expenses to the Garage operations.
- Excess funds totaling \$258,693 as of December 31, 2017 in the operating account were not distributed to either the City or the Developer. In addition, no actions were taken on any disbursements due from prior calendar years in accordance with the Declaration of Condominium's terms.
- Annual Retail Contributions were not properly calculated by Edens resulting in a \$50,947 overpayment to the City.

SCOPE, OBJECTIVES, AND METHODOLOGY

The scope of this audit was to determine compliance with selected provisions of the Declaration of Condominium of 5th & Alton Condominium, recorded in Official Records Book 27133, at Page 4420, of the Public Records of Miami-Dade County, Florida. The audit covered the period January 1, 2016 through December 31, 2017, and various transactions as needed made prior and subsequent to this period. This audit focused primarily on the following objectives:

- to determine whether operating expenses were properly allocated;
- to determine whether the annual Retail Contributions were calculated in accordance with Section 10.3 (d) of the Declaration; and
- to determine whether disbursements/deficiencies were properly distributed between the City and Edens.

We conducted this performance audit in accordance with the Standard Operating Procedures of the City of Miami Beach Office of Internal Audit as well as internal audit best practices. Those 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:

- Reviewed applicable provisions within the City Charter and Code of Ordinances, and City policies and procedures;

- Interviewed and made inquiries of City and external companies' personnel in order to gain an understanding of the internal controls (relative to the operations of the garage), assess control risk, and plan audit procedures;
- Performed substantive testing consistent with the audit objectives, including but not limited to examination, on a sample basis, of applicable transactions and records;
- Drew conclusions based on the results of testing, made corresponding recommendations, and obtained auditee responses and corrective action plans; and,
- Performed other audit procedures as deemed necessary.

FINDINGS, RECOMMENDATIONS AND MANAGEMENT RESPONSES

1. Finding: Edens Limited Partnership (Edens) Improperly Allocated \$66,262 in Expenses to the Garage Operations

As per Section 10.5 (c) of the Declaration of Condominium, the cost of maintaining, repairing, insuring, and, when necessary, replacing those portions of the property (or components thereof), including the Garage, as enumerated on Schedule 1, in the percentages noted on said Schedule, whether or not technically a part of the Retail Space (the "Operating Expenses"), shall be allocated to the Garage and shall ultimately be payable by the City and Developer {Edens Limited Partnership or Edens} in proportion to the number of City Spaces and Retail Spaces owned by each from time to time (i.e. City 46% and Edens 54%).

In order to determine whether expenses paid were properly allocated to the Garage, the financial statements and supporting documentation (i.e. invoices/receipts) for selected expenses such as painting and maintenance personnel, were requested, obtained and reviewed. During calendar years 2016 and 2017, the painting expense allocated to the Garage totaled \$195,878 as per the financial statements. However, after reviewing the corresponding invoices in the amount of \$200,266 (prior to any allocations), it was noted that the allocation of six (6) invoices totaling \$156,387 were incorrectly done, as 100% of the cost was allocated to the Garage. As per Schedule 1 of the Declaration, only 90% of the cost (or \$180,240) should have been allocated to the Garage, and the remaining 10% to the Retail Space. As a result, \$15,638 (\$156,387 x 10%) was over allocated to the Garage.

Furthermore, the Maintenance Personnel expenses were also reviewed whereby it was noted that \$50,624 of "Total Other Non-Direct Expenses" was allocated to the Garage under the maintenance personnel category for allocation of the Miami office, human resources, technology and corporate accounting resources during calendar years 2016 and 2017. However, after reviewing the Declaration, it is unclear why these fees are being charged to the Garage as a total of \$50,000 in management fees are paid annually for the management services of the Garage operations. Several documented requests were sent to the Edens asking for clarification but no satisfactory responses were received to date.

Per discussions with the Parking Department, this agreement was monitored by the City's Economic Development Division Director until his December 28, 2012 termination date. Afterwards, it was apparently not re-assigned to another City department as no one was knowingly tasked with monitoring its terms. As a result, the City's Office of Real

Estate was assigned in January 2018 the responsibility of monitoring and enforcing the agreement's terms going forward.

Recommendation(s):

It is recommended that additional monies incorrectly allocated to the Garage for painting expense (\$15,638) be reimbursed by the Retail Space and deposited into the operating bank account. In addition, it is recommended that the additional \$50,624 charged to the Garage operations for "Total Other Non-Direct Expenses" be reimbursed by Edens and deposited into the operating bank account.

Management's Response (Edens):

Edens is reviewing the invoices associated with the painting expense and will respond based on its findings and will discuss with the City. Related to the "Total Other Non-Direct Expenses", Edens agrees with the findings that there is an allocation of costs such as office rents, technology costs, etc, but Edens would like to further discuss with the City on re-evaluating whether the costs to manage the garage is at market rate prior to Edens reimbursing for the "Total Other Non-Direct Expenses".

Implementation Date: July 2018

Management's Response (City's Parking Department):

The Parking Department agrees with the recommendation made by the Office of Internal Audit and will work together with the City's Office of Real Estate and the Finance Department to ensure that the overpayment of painting expense from the operating account be reimbursed.

Implementation Date: July 2018

Management's Response (City's Office of Real Estate):

The Office of Real Estate also agrees with the recommendation made by Internal Audit. We will work together with the City's Parking and Finance Departments and will discuss this issue with Edens to ensure that overpayment of painting expense from the operating account be reimbursed.

Implementation Date: July 2018

2. Finding: *Excess Funds Totaling \$258,693 as of December 31, 2017 in the Operating Account were Not Distributed to Either the City or the Developer*
As per Section 10.5 (d) of the Declaration, Developer shall consult and coordinate with City in preparing an annual budget for Revenue and Operating Expenses, which budget shall be prepared and finalized at least 60 days before the year end for the prior budget. In addition, as per Section 10.5 (g) of the Declaration of Condominium, following each annual reconciliation, and subject to any audit adjustments, any amounts in the operating account in excess of three months of projected operating expenses¹ shall be distributed to the City (46%) and Edens (54%). Similarly, Section 10.5 (b) indicates that if

¹ Although, the Declaration does not contain any wording to define how three months of projected Operating Expenses is to be calculated, the monthly average for each calendar year was used as the basis for each calculation as it was determined to be the most equitable method.

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at any time the Operating Account has insufficient sums to cover Operating Expenses, the City and Edens shall deposit the deficiency within three (3) business days after notice in the same aforementioned percentages.

In order to determine whether there were any excess balances in the operating account to be distributed, the monthly bank statements as well as the financial statements from 01/01/15 through 12/31/17 were reviewed. While reviewing the financial statements, it was noted that a total of \$811,400 in "Other Liabilities" consisting of \$373,248 due to the City (\$137,526 + \$189,722 + \$46,000) and \$438,160 due to Edens for contributions made during 2009 and 2012 to cover operating expenses as required by Section 10.5 (b). Furthermore, an additional contribution in the amount of \$162,380 remitted by the City in September 2013 was not included for a total of \$535,628 (\$373,248 + 162,380) due to the City.

At the same time, it was determined that during calendar years 2015 through 2017, there were sufficient funds in the operating account to cover three (3) months of estimated expenses and to distribute these excess funds between the City and Edens as per Section 10.5 (g) of the Declaration. Exhibit A located at the end of this audit report provides a detailed analysis of the calculations performed. As of 12/31/17, there was a total excess in the operating account of \$258,693 (\$599,361 - \$340,668) of which 46% or \$118,999 should have been distributed to the City. However, no monies have been distributed to date which is most likely due to the City's lack of sufficient monitoring of the agreement's terms.

Recommendation(s):

The City's Parking Department and the Office of Real Estate as well as Edens should review the available funds in the operating account on a continuous basis so that any future disbursements could be promptly made as the money becomes available (i.e. taking into account the required three (3) months of estimated operating expenses balance to be maintained). Furthermore, all parties should reach a consensus as to the manner in which the three months of projected expenses will be consistently calculated going forward in the determination of the annual disbursements/deficiencies needed by the City and Edens.

Management's Response (Edens):

Edens agrees that excess cash in the Operating Account should be distributed between the City and Edens. It is important to note that monthly operations of the garage is currently yielding a loss of up to \$35,000/monthly as well as the garage will be making an insurance payment of approximately \$400,000 to \$420,000 in the second half of 2018. It is certainly reasonable for the Garage to distribute funds to both the City and Edens but it is likely that a cash contribution will have to be made by both parties to fund the insurance payment due in the second half of the calendar year.

Implementation Date: Year end 2018

Management's Response (City's Parking Department):

Taking into consideration the above statement made by Edens, the Parking Department believes it is best to not distribute any excess monies. Monthly reviews are on-going to determine if any monies need to be contributed. Meanwhile, a year end analysis will be

performed with the Finance Department and the Office of Real Estate to conclude whether any available monies can be disbursed.

Implementation Date: Year end 2018

Management's Response (City's Office of Real Estate):

The Office of Real Estate agrees with the recommendation made by Internal Audit. Going forward, we will work with the Parking and Finance Departments to help ensure that any excess available monies are distributed when due.

Implementation Date: Year end 2018

3. Finding: *Annual Retail Contributions were Incorrectly Calculated by Edens Resulting in a \$50,947 Overpayment*

As per Section 10.3 (g) of the Declaration of Condominium, employees and customers of the occupants of all of the Retail Space shall be entitled to park in the Garage free of charge, subject to the validation and decal provisions, and payment of the agreed upon annual expense contribution (the "Contribution") for parking spaces by the owner of the Retail Space. The amount of the Contribution shall be \$313,500 (based on a formula calculation in the Declaration) per annum (plus applicable sales tax) and shall be paid in 12 monthly installments on or before the fifth day of each month in advance commencing on the date the Garage first opens for normal business operations. The amount of the Contribution shall increase by 2.5% (over the prior year's Contribution) per year starting on the January 1 immediately following the third anniversary of Full Occupancy of the Retail Space (2013).

In order to determine whether the Contribution was properly remitted, the financial statements for calendar years 2015, 2016, and 2017 were reviewed. Testing found that during calendar years 2014 through 2017 the Contribution amounts were not properly calculated by Edens, thus resulting in an overpayment of \$50,947 as shown below.

Period	Applicable Increase	Annual Contribution	Monthly	Paid	(Over)/Under Payment
2010	First 3 Years- 2.5% increase per year does not apply	\$ 313,500	\$ 26,125	NOT REVIEWED	
2011		313,500	26,125		
2012		313,500	26,125		
2013	2.50%	321,338	26,778		
2014	2.50%	329,371	27,448	321,600	7,771
2015	2.50%	337,605	28,134	313,015	24,590
2016	2.50%	346,045	28,837	389,312	(43,267)
2017	2.50%	354,696	29,558	394,738	(40,042)
Total Overpayment				\$	(50,947)

This deficiency most likely occurred due to Edens' personnel changes and was not realized and corrected due to the City's lack of sufficient monitoring.

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Recommendation(s):

It is recommended that the City's Office of Real Estate monitor future Contributions to help ensure that the correct annual contribution is remitted. In addition, we recommend that the City's Office of Real Estate discuss with Edens the preferred method to correct the \$50,947 Contribution overpayment.

Management's Response (Edens):

Edens agrees with the findings and attributes the deficiency to a change of personnel over the past several years. There have been three accountants responsible for the Garage accounting records during the period under Audit. Edens has documented the methodology for the Retail contribution as noted above and has addressed it in monthly Retail Contributions in 2018. Additionally, Edens suggests that the overpayment be addressed through a ratable reduction to the monthly Retailer contribution throughout the remaining months in 2018. Since the contribution was not increased on January 1st 2018 from \$29,513 to \$30,297 the current underpayment as of March 2018 is \$2,351 (i.e. $(\$30,297 - \$29,513) \times 3$ months). The remaining overpayment of \$48,596 will reduce Edens monthly Retail contribution throughout the remaining 9 months of 2018 (i.e. $(\$50,947 - \$2,351) / 9$ months = \$5,400 monthly reduction).

Implementation Date: June 2018

Management's Response (City's Office of Real Estate):

The Office of Real Estate agrees with the recommendations made by Internal Audit. The Office of Real Estate will monitor the Contribution to help ensure its accuracy. Additionally, the Office of Real Estate will provide a Contribution schedule to the Finance Department to ensure accuracy of the payments upon receipt.

Implementation Date: June 2018

EXIT CONFERENCE

An exit conference was held in the Parking Department's Small Conference Room. Participants included Saul Frances (Parking Department Director), Laura Franco-Rubines (Assistant Parking Department Director), Rocio Alba (Administrative Services Manager), Charles Dike (Senior Management Analyst), Mark Milisits (Asset Manager), Coral Vivolo (Auditor) and Mark Coolidge (Interim Internal Auditor). Afterwards, a draft copy of this audit report was sent to Edens Limited Partnership and AR&J Sobe, LLC for their review. All parties were in agreement as to the contents of this report. Management responses were solicited and included in our report.

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cc: Kathie G. Brooks, Assistant City Manager
John Woodruff, Chief Finance Officer
Saul Frances, Parking Department Director
Mark Milisits, Asset Manager
Nicole Shiman, Vice President-Investments, Edens Limited Partnership
Elias Droubi, Director of Property Operations, Edens Limited Partnership

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Exhibit 1

Period	Total Deposits per Bank Statement	Total Payments per Bank Statement
Beginning Bal.	\$464,702	
Jan-15	112,368	-88,532
Feb-15	155,284	-88,581
Mar-15	193,542	-84,028
Apr-15	141,541	-79,526
May-15	148,616	-75,533
Jun-15	100,972	-92,608
Jul-15	125,702	-98,177
Aug-15	131,568	-65,276
Sep-15	78,672	-452,466
Oct-15	162,068	-62,468
Nov-15	106,156	-60,247
Dec-15	147,201	-85,363
Total	\$2,068,391	(\$1,332,804)
Ending Bal. 12/31/15		
\$735,587		

Period	Total Deposits per Bank Statement	Total Payments per Bank Statement
Beginning Bal.	\$735,587	
Jan-16	178,525	-95,278
Feb-16	116,124	-70,646
Mar-16	160,146	-59,821
Apr-16	141,399	-99,308
May-16	114,183	-77,697
Jun-16	198,169	-76,927
Jul-16	109,921	-419,608
Aug-16	112,161	-52,870
Sep-16	107,110	-100,815
Oct-16	112,588	-65,545
Nov-16	83,179	-126,111
Dec-16	113,674	-74,254
Totals	\$2,282,764	(\$1,318,880)
Ending Bal. 12/31/16		
\$963,884		

Period	Total Deposits per Bank Statement	Total Payments per Bank Statement
Beginning Bal.	\$963,884	
Jan-17	105,617	-139,582
Feb-17	119,814	-69,814
Mar-17	125,257	-160,181
Apr-17	95,687	-204,126
May-17	129,660	-98,686
Jun-17	103,991	-74,612
Jul-17	119,123	-98,393
Aug-17	97,856	-117,425
Sep-17	59,018	-71,747
Oct-17	121,603	-115,088
Nov-17	90,489	-55,476
Dec-17	101,311	-428,819
Totals	\$2,233,310	(\$1,633,949)
Ending Bal. 12/31/17		
\$599,361		

	(1)	(2) (1)/12 Monthly Average	(2)*3 months Three Months of Operating Estimated Expenses
Total Operating Expenses 2015	\$1,270,825	\$105,902	\$317,706
Total Operating Expenses 2016	1,382,958	115,247	345,740
Total Operating Expenses 2017	1,362,671	113,556	340,668