City of New York

OFFICE OF THE COMPTROLLER

Scott M. Stringer
COMPTROLLER

FINANCIAL AUDIT

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Deputy Comptroller for Audit

Audit Report on the Compliance of Manhattan River Group, L.L.C. with Its License Agreements with the City

FN17-089A

June 28, 2017

http://comptroller.nyc.gov

THE CITY OF NEW YORK
OFFICE OF THE COMPTROLLER
SCOTT M. STRINGER

June 28, 2017

To the Residents of the City of New York:

My office has audited Manhattan River Group, L.L.C.'s (MRG's) operation of a restaurant and lounge (the Restaurant) and a marina (the Marina) located at the Dyckman Marina in Manhattan in order to determine whether MRG accurately reported its gross revenues, made appropriate and timely payments to the City and complied with other major requirements of the two license agreements, such as making required capital improvements, maintaining insurance coverage, and keeping adequate books and records.

The audit found that although MRG's payments to the Department of Parks and Recreation (Parks) under both agreements were timely, and capital improvements on the Restaurant were completed, MRG underreported its gross receipts from the Restaurant by at least $488,874 and consequently owes the City at least $39,110 in additional license fees and $17,842 in late charges. The audit also found inadequate internal controls and inconsistent practices in MRG's recordkeeping procedures, including a failure to maintain sufficient documentation related to its operation of the Marina. Moreover, the records produced by MRG were insufficient to show that it completed 8 of the 18 capital improvement items that were required for the Marina. Finally, MRG failed to maintain certain required insurance coverage for both the Restaurant and the Marina for each business's 2016 operating year. That omission potentially exposed the public and the City to unwarranted financial risk in violation of MRG's express obligations under its agreements.

Based on the audit findings, the audit made nine recommendations to MRG, including that MRG remit $56,952 in additional license fees and late charges owed to the City; accurately report all gross receipts to Parks; ensure that all gross receipts are accurate and consistent in and across all financial records; provide all capital improvement documentation to Parks for review; and ensure that the Marina and the Restaurant are properly insured at all times. The audit also made seven recommendations to Parks, including that Parks ensure that all promotional and complimentary management discounts are reported by MRG as gross receipts; ensure that MRG has the required insurance coverage at all times; and ensure that MRG implements the audit report recommendations.

The results of the audit have been discussed with MRG and Parks officials, and their comments have been considered in preparing this report. Their complete written responses are attached to this report. If you have any questions concerning this report, please e-mail my Audit Bureau at audit@comptroller.nyc.gov.

Sincerely,

Scott M. Stringer

TABLE OF CONTENTS

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EXECUTIVE SUMMARY

On June 25, 2009, the City of New York (the City) through its Department of Parks and Recreation (Parks) entered into two separate 15-year license agreements with Manhattan River Group, L.L.C. (MRG), one for the operation of a restaurant and lounge (the Restaurant), and a second for the operation of a marina (the Marina) at the Dyckman Marina, located at 348 Dyckman Street in Manhattan. Pursuant to the license agreement for the Restaurant (the Restaurant Agreement), MRG was required to pay the City the higher of $78,604 (the minimum annual fee) or eight percent of the Restaurant's gross receipts from the period of April 1, 2015 through March 31, 2016. Under the Marina's agreement (the Marina Agreement), MRG was required to pay the City the higher of $15,073 or five percent of the Marina's gross receipts for the period of November 1, 2015 through October 31, 2016. In addition, each of the two license agreements requires MRG to make and complete specific capital improvements by the end of the second operating year after the agreement was signed.

In this audit, we examined whether MRG accurately reported gross revenues; made the appropriate and timely payments to the City; and complied with other major requirements of the two license agreements, such as making capital improvements, maintaining insurance coverage, and keeping adequate books and records.

Audit Findings and Conclusions

Our audit found that although MRG's payments to Parks under both agreements were timely, and capital improvements on the Restaurant were completed, MRG underreported its gross receipts from the Restaurant by at least $488,874 and consequently owes the City at least $39,110 in additional license fees and $17,842 in late charges. We also found inadequate internal controls and inconsistent practices in MRG's recordkeeping procedures, including a failure to maintain sufficient documentation related to its operation of the Marina. Moreover, the records produced by MRG were insufficient to show that it completed 8 of the 18 capital improvement items that were required for the Marina. Finally, we found that MRG failed to maintain certain required insurance coverage for both the Restaurant and the Marina for each business's 2016 operating

year. That omission potentially exposed the public and the City to unwarranted financial risk in violation of MRG's express obligations under its agreements.

Audit Recommendations

To address these issues, we make nine recommendations to MRG and seven recommendations to Parks, including:

To MRG:

- Remit to Parks $56,952 in additional license fees and late charges owed to the City due to MRG's having underreported the Restaurant's gross receipts;
- Accurately report all gross receipts to Parks by including:
    - All complimentary meals, beverages, and discounts provided by the Restaurant;
    - All catering service charges;
    - Advance deposit and gift cards sales when proceeds are received;
    - Overpayments received from patrons;
- Ensure that all gross receipts are recorded accurately and with consistency in and across all financial records, including but not limited to the income journal, general ledger, and certified statement of gross receipts reported to Parks;
- Ensure that all deposits and revenue from special events are recorded and reported in a separate, appropriately named revenue category for purposes of accountability and to enable reconciliation with contracts generated for special events;
- Provide all documentation for capital improvements to Parks for review; and
- Ensure the Restaurant and the Marina are properly insured at all times.

To Parks:

- Ensure that MRG remits all additional fees due with applicable late fee charges;
- Ensure that all promotional and complimentary management discounts utilized by MRG for customer relationships are recorded as gross receipts and included in the calculation for fees due to the City;
- Ensure that MRG provides documentation to show that capital improvements at the Marina are completed as required by the agreement;
- Enhance Parks oversight to enable it to ensure that MRG maintains all required insurance coverage for the Restaurant and Marina operations and all times; and
- Ensure MRG implements the recommendations in this report.

MRG's Response

In its written response, MRG generally disputed the findings but agreed with seven of the nine recommendations. MRG stated that "the Audit Team has not undertaken an adequate legal review of the License Agreements between Manhattan River Group, LLC ('MRG') and the City of New York (the 'License Agreement'), and has failed to take into consideration best practices in the food and beverage industry." In particular, MRG contends that the audit report misinterprets the meaning of "gross receipts" as defined in the Restaurant Agreement. MRG also claims that “[t]he Comptroller has also exaggerated minor lapses in record keeping and focused in on software issues that were corrected well before the commencement of this audit.”

Despite MRG’s general and specific criticisms of the audit findings, the Restaurant Agreement clearly dictates that complimentary meals and drinks (comps) and discounts must be included in reportable gross receipts. As discussed in the audit report, the Restaurant Agreement specifically provides that the definition of “gross receipts” includes all sales, whether payment is received or not. Further, the Restaurant Agreement specifically provides that the only allowable deductions from gross receipts are sales tax, government grants, loans and supplemental funding, gratuities, and uncollected sales known as bad debts. No exclusion exists for orders placed or made at the Restaurant for which MRG chooses to forgo collection or accept lesser payment in exchange for the promotional value, good will or whatever other benefit it seeks to obtain. MRG’s decision to comp or discount Restaurant transactions does not relieve MRG of its obligation under the Restaurant Agreement to report all orders placed or made at the Restaurant as gross receipts.

Further, we disagree with MRG’s characterization of the problems the audit identified with data reliability as mere “minor” issues. To the contrary, because of the problems found with MRG’s method of record keeping and software, we did not receive sufficient adequate and consistent information to determine that the revenue reported was reliable.

Parks Response

Parks agreed with five of the seven recommendations. Parks neither agreed nor disagreed with the remaining two recommendations stating, “[w]ith regard to the potential fees owed on complimentary meals and beverages, and service charges, there is a difference in interpretation of the license agreement between the Comptroller’s Office and MRG. Parks is reviewing this matter with our General Counsel and the City’s Law Department.”

AUDIT REPORT

Background

On June 25, 2009, the City through Parks entered into two separate 15-year license agreements with Manhattan River Group, L.L.C., one agreement for the operation of the Restaurant, and the other agreement to operate the Marina at the Dyckman Marina, located at 348 Dyckman Street in Manhattan.[1] Under the license agreements, the Restaurant's operating year is April 1 through March 31 and the Marina's operating year is November 1 through October 31.[2] Each agreement requires MRG to pay the City the higher of the minimum annual license fee or a percentage of each operation's gross receipts.

Pursuant to the Restaurant Agreement, MRG was required to pay the City the higher of $78,604 (the minimum annual fee) or eight percent of the Restaurant's gross receipts from the period of April 1, 2015 through March 31, 2016.[3] For the Marina, MRG was required to pay the City the higher of $15,073 or five percent of the Marina's gross receipts for the period November 1, 2015 through October 31, 2016.

For operating year 2016, MRG reported gross receipts of $5,778,022 from the Restaurant operation and paid license fees to the City in the amount of $462,240. MRG reported $15,135 in gross receipts from operation of the Marina for the operating year ended October 31, 2016 and paid the minimum annual fee of $15,073 to the City. The license agreements require MRG to classify revenue according to specific categories within each operation and to maintain separate books and records for, respectively, the Restaurant and for the Marina.

In addition, each of the two license agreements requires MRG to make and complete specific capital improvements by the end of the second operating year after the agreement was signed. Specifically, MRG was required to invest $454,000 in the Marina for 18 specified capital improvements, including the repair and renovation of a Quonset hut on the property, the repair and stabilization of a cement bulkhead leading to the floating docks, and to rebuild and extend the walkway and floating pier. For the Restaurant, the license agreement required MRG to expend $850,000 for the demolition of the existing café and restaurant and the construction of a new restaurant, and for the construction of railings, decking, gates and fences.

In addition, MRG is required to comply with other provisions of the agreements, including:

- Maintaining a revenue control system to ensure the accurate and complete recording of all revenue received from the operation;
- Maintaining a separate and dedicated bank account in New York City;
- Maintaining adequate insurance, including commercial general liability, workers' compensation and disability benefits insurance;

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[1] The commencement dates of the Restaurant Agreement and Marina Agreement were April 1, 2012 and May 1, 2013, respectively. The Restaurant Agreement expires on March 31, 2027 and the Marina Agreement expires on October 31, 2028.

[2] The Restaurant's catering service is open year round, although the Restaurant itself is only open from April to September. The Marina is open in the summer months only, May through October.

[3] According the Restaurant Agreement, gross receipts "shall include all funds or receipts of any kind received by Licensee, without deduction or set-off of any kind, from the operation of the Licensed Premises, from the sales of merchandise, food and beverages at the Licensed Premises, from the licensing of the Licensed Premised for private functions, and from any related services of any kind. . . ." The Marina Agreement includes an identical definition of gross receipts.

- Submitting a certified statement of gross receipts to Parks within 30 days after the end of each operating year;
- Obtaining prior approval from Parks for all special events and rentals;
- Paying required security deposits;
- Paying all utility costs associated with the operation of the premises; and
- Providing 24-hour security of the licensed premises at its own cost.

Parks is responsible for monitoring the operation of the Restaurant and Marina to ensure that MRG complies with its license agreements.

Objectives

The audit objectives are to determine whether MRG: 1) accurately reported gross revenues; 2) made appropriate payments to the City in a timely manner; and 3) complied with other major requirements of the Parks license agreements, such as capital improvements, insurance, and adequate maintenance of books and records.

Scope and Methodology Statement

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. This audit was conducted in accordance with the audit responsibilities of the City Comptroller as set forth in Chapter 5, §93, of the New York City Charter.

The scope of this audit covered MRG's operating year 2016, including specifically April 1, 2015 through March 31, 2016 for the Restaurant and November 1, 2015 through October 31, 2016 for the Marina. Please refer to the Detailed Scope and Methodology at the end of this report for the specific procedures and tests that were conducted.

Discussion of Audit Results

The matters covered in this report were discussed with MRG and Parks officials during and at the conclusion of this audit. A preliminary draft report was sent to MRG and Parks and was discussed at an exit conference held on May 24, 2017. On June 5, 2017, we submitted a draft report to MRG and Parks with a request for comments. We received written responses from MRG and Parks on June 19, 2017.

In its written response, MRG generally disputed the findings but agreed with seven of the nine recommendations. MRG stated that "the Audit Team has not undertaken an adequate legal review of the License Agreements between Manhattan River Group, LLC ('MRG') and the City of New York (the 'License Agreement'),[4] and has failed to take into consideration best practices in the food and beverage industry." In particular, MRG contends that the audit report misinterprets the meaning of "gross receipts" as defined in the Restaurant Agreement. MRG also claims that

[4] Throughout MRG's response, it refers to its agreement with the City for the operation of the Restaurant as the "License Agreement." This is the same agreement that the audit report refers to as the Restaurant Agreement.

“[t]he Comptroller has also exaggerated minor lapses in record keeping and focused in on software issues that were corrected well before the commencement of this audit.”

Despite MRG’s general and specific criticisms of the audit findings, the Restaurant Agreement clearly dictates that complimentary meals and drinks and discounts must be included in reportable gross receipts. As discussed in the audit report, the Restaurant Agreement specifically provides that the definition of “gross receipts” includes all sales, whether payment is received or not. Further the Restaurant Agreement specifically provides that the only allowable deductions from gross receipts are sales tax, government grants, loans and supplemental funding, gratuities, and uncollected sales known as bad debts. No exclusion exists for orders placed or made at the Restaurant for which MRG chooses to forgo collection or accept lesser payment in exchange for the promotional value, good will or whatever other benefit it seeks to obtain. MRG’s decision to comp or discount Restaurant transactions does not relieve MRG of its obligation under the Restaurant Agreement to report all orders placed or made at the Restaurant as gross receipts.

Further, we disagree with MRG’s characterization of the problems the audit identified with data reliability as mere “minor” issues. To the contrary, because of the problems found with MRG’s method of record keeping and software, we did not receive sufficient adequate and consistent information to determine that the revenue reported was reliable.

In its response, Park agreed with five of the seven recommendations. In addition, Parks took no position on the remaining two recommendations, but rather stated that, “[w]ith regard to the potential fees owed on complimentary meals and beverages, and service charges, there is a difference in interpretation of the license agreement between the Comptroller’s Office and MRG. Parks is reviewing this matter with our General Counsel and the City’s Law Department.”

The full text of MRG’s and Parks’ responses are included as addenda to this report.

FINDINGS

Our audit found that although the payments MRG made to Parks were timely and the required capital improvements on the Restaurant were completed, MRG underreported its gross receipts from the Restaurant by at least $488,874 and consequently owes the City at least $39,110 in additional license fees and $17,842 in late charges. We also found inadequate internal controls and inconsistent practices in MRG's recordkeeping, including a failure to maintain sufficient documentation related to its operation of the Marina.

Moreover, the records produced by MRG were insufficient to show that it completed 8 of the 18 capital improvement items that were required for the Marina. Finally, MRG failed to maintain certain required insurance coverage for both the Restaurant and the Marina for each business's 2016 operating year. That omission potentially exposed the public and the City to unwarranted financial risk in violation of MRG's express obligations under its agreements.

MRG Owes the City at least $56,952 in Additional License Fees and Late Charges

MRG failed to ensure that all gross receipts were properly reported to the City in accordance with the Restaurant Agreement. Our review of MRG's records found that MRG underreported its gross receipts from the Restaurant by at least $488,874 and consequently owes the City $39,110 in additional license fees and $17,842 in late charges for a total of $56,952. (See Appendix for the calculation of the late charges[5].) Specifically, as discussed below, MRG improperly excluded the following sums from the gross receipts reported to the City for operating year 2016:

- $257,294 worth of complimentary meals and beverages and discounts on meals and beverages served at the Restaurant;
- $187,998 in service charges MRG collected for catered events;
- $42,536 in payments MRG received on deposit for special events; and
- $1,046 from an overpayment MRG received for a special event.

MRG's Response: "In its Audit Report, the Comptroller incorrectly concludes that MRG did not report more than $450,000 in gross revenue from comps, discounts, service charges and advance deposits. Our own analysis demonstrates that the Comptroller's audit team . . . has based its conclusions on a number of fundamental errors: (a) in the case of complimentary items and discounts, the License Agreement does <u>not</u> require MRG to pay the license fee on revenue that was never actually received due to legitimately issued comps and discounts; (b) in the case of advance deposits, the amounts were all reported to the City of New York; and (c) in the case of service charges, amounts paid to front of house staff were correctly deemed gratuities and thus exempt from inclusion in MRG's statement of Gross Receipts."

Auditor Comment: We address each of MRG's responses in the sections that follow. Briefly, (a) we disagree with MRG's assertions that the value of the forgone charges—booked as complimentary and discounted sales—for orders placed and served at the Restaurant, for reasons we explain below; (b) regarding the advance deposits, Parks has informed us that MRG delayed reporting the sums collected because of an erroneous

[5] Late payment charges were calculated up to May 11, 2017. A 2 percent late charge is assessed when any payment is overdue for more than ten days. The late charges are compounded on a monthly basis.

interpretation of when those sums were reportable and has paid the fees it owed on those deposits, except for the applicable late charges; and (c) with respect to service charges, the documentation MRG provided did not substantiate its claim that the amounts in question constituted gratuities as defined in the Restaurant Agreement.

MRG Excluded Complimentary Meals and Beverages and Discounts from Reported Gross Receipts

MRG excluded at least $257,294 worth of complimentary meals and beverages and manager-discounts from the Restaurant's gross receipts of $5.78 million that MRG reported to the City and consequently underpaid the City by at least $20,584. Examples of the excluded items include:

- A meal and beverages that according to the guest check totaled $622, which was initially discounted by 75 percent to a reduced total of $155 and then discounted to zero by the Restaurant manager; and
- Bottles of liquor provided to promoters as complimentary beverages during special events with a sales value of $215 each, according to the guest checks.

Article 2.1(i) and (iv) of the Restaurant Agreement, in pertinent part, state,

> Gross Receipts shall include *any orders placed or made* at Licensed Premises [and]. . . . Gross Receipts shall include sales made for cash or credit (credit sales shall be included in gross receipts as of the date of the sale) *regardless of whether the sales are paid or uncollected*. [Emphasis added.]

Further, no provision in the Restaurant Agreement allows MRG to exclude from gross receipts the revenue value of any meals or beverages ordered and served at the Restaurant, regardless of whether MRG collected payment for them. Thus, the full value of meals and beverages, without regard to the amounts charged, should have been reported as part of gross receipts.

> ***MRG's Response:*** "For purposes of this response, 'comps' are food and beverage items that are given to potential new customers, repeat customers, and guests who are dissatisfied with their experience. A typical example is a spilt beverage, which MRG replaces at no cost to the customer. In this example, the replacement beverage order will be entered into our point of sale system; the item will then be produced and comped. The inventory will have been depleted, but no revenue will be received. In another example, MRG may invite a potential private event client for brunch in order to close an event.
>
> The *comp* function in MRG's point of sale system is also frequently used for other purposes having nothing to do with customer experience. For example, a comp will be issued to track a reduction in inventory where income is to be imminently, but not immediately, received (for example, a declined payment when the guest is already known to MRG). The comp function is also used to track actual consumption where products are paid for in advance – for example, prepaid open bar for a private event. No revenue is collected for items that are *comped*, but the comped items are still indicated in the company's point of sale system at full value for purposes of inventory tracking.
>
> 'Discounts', on the other hand, are typically given as an incentive. Common discounts include *happy hour* discounts and percentage reductions given to customers who have demonstrated loyalty or who have accumulated a large bill (akin to a *bulk discount* or *volume discount* in other industries). Discounts might also be given for certain items or for a particular occurrence to drive sales (a rainy day discount of 10% when there is a high probability of rain). Similar to comps, if an item is discounted, the uncollected portion is not reported as Gross Receipts."

MRG's License Agreement with the City of New York defines 'Gross Receipts' as including 'funds or receipts of any of kind ***received*** by the Licensee. . . .' [Emphasis added by MRG.] Sections 2.1(j)(i)-(v)) [sic] of the License Agreement goes on to allow and disallow certain exclusions from Gross Receipts. . . . Nothing in the License Agreement requires MRG to pay the percentage license fee on revenue that it never received when items are properly comped or discounted in accordance with food and beverage industry best practice."

Auditor Comment: MRG analyzes its agreement with the City, together with what it asserts as "industry best practice" to define Gross Receipts as essentially cash received. However, the plain language of the agreement does not support its analysis. "Gross Receipts" are clearly defined in Article 2.1(i)(i)-(v) of the Restaurant Agreement. In particular, Article 2.1(i)(i) states in part that

> "Gross Receipts" shall include all funds or receipts of any kind received by Licensee, without deduction or set-off of any kind, from the operation of the Licensed Premises, from the sale of goods and beverages, merchandise and services of any kind at the Licensed Premises. . . .

Subsections (ii), (iii) and (iv) specify further items that "shall" be included as gross receipts, including specifically subsection (iv), which states that

> Gross Receipts shall include sales made for ***cash or credit*** (credit sales shall be included in gross receipts as of the date of the sale) ***regardless of whether the sales are paid or uncollected it being the distinct intention and agreement of the parties that all sums due to be received by Licensee from all sources from the operation of this License shall be included in Gross Receipts***, provided however, that any gratuities transmitted by Licensee directly or indirectly to employees and staff shall not be included within Gross Receipts. [Emphasis added.]

While MRG seeks to dismiss the language of subsection (iv) as only relating to "credit sales," it is clear from the actual language of that subsection that it applies equally to *all sales*, both cash and credit.

It is notable that where the Restaurant Agreement intends to exclude items from the definition of gross receipts, those exclusions are clearly identified. Thus, as a matter of contract construction, it would be improper to impute an exclusion where none is expressly stated. Specifically, the Restaurant Agreement provides for four exclusions from the gross receipts:

1. sales tax [Article 2.1(i)(i)];
2. government grants, loans, and supplemental funding [Article 2.1(i)(i)];
3. gratuities as specifically defined in the Restaurant Agreement [Article 2.1(iv)]; and
4. uncollected sales debts known to be bad, subject to documentation of MRG's collection efforts, if requested by Parks [Article 2.1(v)].

No express exclusion exists for sales for which MRG chooses to forgo collection. As MRG indicates in its response, "comps" and discounts are given at times for promotional reasons and to engender good will (e.g., "food and beverage items . . . given to potential new customers, repeat customers and guests who are dissatisfied with their experience"). Thus, by its own admission, MRG gets value from these transactions. That value, as measured by the sales price, must be reported under the Restaurant Agreement as part of the Restaurant's gross receipts.

MRG Excluded $187,998 in Service Charges from Gross Receipts Reported to the City

Our review of MRG's income journal found that a total of $187,998 in revenue from service charges was excluded from the gross receipts it reported to the City. Consequently, MRG owes $15,040 in license fees on that revenue. Specifically, our detailed review of MRG's catered-event records for July and August 2015 found that service charges of 22 percent were collected for 23 of the 28 special events held at the licensed premises during that two-month period. Although MRG was allowed to deduct "gratuities" from its gross receipts, the service charges collected from those events were not considered gratuities under the license agreement's definition. Rather, according to the Restaurant Agreement, Article 2.1(i)(iv)(b),

> With respect to catered events, a "Gratuity" shall be an amount *no greater than 20%* of the catering food and beverage sales for the event, provided that such Gratuity is a charge that: (i) is separately stated on the bill or invoice given to Licensee's customer, (ii) *is specifically designated as a gratuity*, or purports to be a gratuity, and (iii) is paid over by Licensee in total to its employees who actually provide services at the event, and who are primarily engaged in the serving of food or beverages to guests, patrons or customers, including, but not limited to, wait staff, bartenders, captains, bussing personnel, and similar staff. "Regular Salary" for purposes of this subsection shall mean the set hourly wage for the applicable employee. Licensee shall provide documentation reasonably satisfactory to Parks to prove that Gratuities were paid to employees *in addition* to their regular salaries, and were otherwise in accordance with the forgoing provisions. Such documentation shall be signed and verified by an officer of Licensee. [Emphasis added.]

Contrary to this contract definition of gratuities, the service charges MRG collected for the abovementioned catered events: (1) exceeded 20 percent; (2) were clearly differentiated from the gratuities in MRG's contracts with its catered-event customers, which also served as MRG's bills; and (3) were not documented by MRG as gratuities in addition to regular compensation to its employees who worked at the events. Moreover, in the payment for one of the 23 catered events, auditors noted that MRG received separate sums for service and for gratuities, a further indication that MRG's service charges did not constitute gratuities under the Restaurant Agreement.

As noted previously, Article 2.1(i)(i) of the Restaurant Agreement states that gross receipts "shall include *all funds or receipts of any kind received by Licensee*, without deduction or set-off of any kind, from the operation of the Licensed Premises, from the licensing of the Licensed Premises *for private functions, and from any related services* of any kind." [Emphasis added.] Accordingly, MRG should have reported and failed to the abovementioned services charges as gross receipts. Consequently, MRG owes the City $15,040 in additional license fees for operating year 2016.

> ***MRG's Response:*** "The Audit Team determined that any amounts listed as *service charges* on catering contracts should be included in Gross Receipts even when those amounts were paid in full to front of house staff. [Footnote omitted.] The license [sic] Agreement states in relevant part, 'any gratuities transmitted by Licensee directly or indirectly to employees and staff shall not be included within Gross Receipts.' Subsection (iv)(b) goes on to explain that gratuities must meet the following requirements: (i) the amount must be separately stated on the bill or invoice, (ii) it must be 'specifically

designated as a gratuity, or purport… to be a gratuity', and (iii) it must [sic] paid in total to front of house staff providing services at the event.

In its analysis, the Audit Team determined that $187,998 in service charges are not gratuities and must be reported as Gross Receipts, at a potential cost to our business of $15,040 in license fees. However, we believe that a large percentage of these service charges meet the definition of gratuities. MRG considers service charges paid in full to front of house staff to be gratuities under the License Agreement and thus exempt from inclusion in the calculation of Gross Receipts. Any amounts paid to non-service staff (i.e. kitchen and support) should have been included in MRG's calculation of Gross Receipts.

Based on our further analysis of the information compiled for the Audit Team, we have determined that some *service charges* should not have been classified as *gratuities*. MRG will provide further analysis and remit additional License Fee on recalculated Gross Receipts."

Auditor Comment: Our determination that MRG had inappropriately excluded $187,998 in service charges from the gross receipts it reported to the City is based on the terms of the Restaurant Agreement and our review of MRG's catered-event documentation. The documentation provided to us contradicts MRG's claim that the service charges were for gratuities, in part, because every special event contract that we reviewed showed that service charges were itemized charges identified separately from gratuities. In addition, MRG did not provide us with any evidence that the payments made to the staff out of the service charges MRG collected were made in addition to those staff members' regular salaries, as it would be required to prove under the Restaurant Agreement. Notably, even now, MRG does not assert nor does it provide any records to show that the service charges it claims to have remitted to its serving staff were made in addition to their regular salaries for working at the catered events.

MRG Omitted $42,536 in Advance Deposits in Reporting Its Gross Receipts to the City

MRG did not accurately report its receipt of advance deposits and gift card sales in accordance with the Restaurant Agreement. According to Article 2.1(i)(i) of that agreement, gross receipts "shall include all receipts of Licensee for services *to be rendered*." [Emphasis added.] However, our review of MRG's monthly statements of gross receipts submitted to the City found that MRG did not include payments it received as advance deposits, which MRG records in the Advance Deposit account in its general ledger. As of March 31, 2016, that account showed a balance of $42,536, which MRG failed to report to the City and on which it failed to pay the applicable license fee. Therefore, MRG owes the City $3,403 in additional license fees on that unreported revenue.

MRG's Response: "The Audit Team determined that 'MRG Omitted $42,536 in Advance Deposits in Reporting Its Gross Receipts to the City'. However, that statement leaves out the relevant fact that MRG did include the full amount of those advance deposits in its Gross Receipts calculation, and further, paid the city $3,403 in license fee that the Audit Team stated remains unpaid."

Auditor Comment: Parks confirmed that MRG paid the sum mentioned in MRG's response—after the period covered by our audit. Parks concurred with our finding that the amounts should have been reported previously, that is, when MRG received the payments. Accordingly, MRG should pay the applicable late charges as calculated in the Appendix of this report.

MRG Failed to Include a $1,046 Overpayment in the Gross Receipts It Reported to the City

Our review of MRG's general ledger found that MRG failed to include an overpayment collected from a catered event in the gross receipts it reported to the City. The overpayment was recorded as a credit in the "Over/Short" account, which is an expense account in the general ledger that is generally used to record an overage or shortage of cash collected by wait-staff identified in the "close-out" summary at the end of the business day. According to Article 2.1(i)(i) of the Restaurant Agreement, gross receipts "shall include all funds or receipts of any kind received by Licensee, without deduction or set-off of any kind, from the operation of the Licensed Premises . . . from the licensing of the Licensed Premises for private functions, and from any related services of any kind." By failing to include this payment, MRG understated Restaurant gross receipts by $1,046 and consequently owes the City $84 in additional fees.

> ***MRG's Response:*** "The Audit Team uncovered $1,046.00 that was not included in MRG's calculation of Gross Receipts. This appears to have been a bookkeeping error. Concurrent with this letter, MRG has remitted payment $84 to the New York City Department of Parks and Recreation. We note that this shortcoming amounts to 0.00018% of Gross Receipts during the audit period."
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> ***Auditor Comment:*** Although the sum in question is not a material amount, the fact that it was misclassified and excluded from gross receipts reflects a control weakness in MRG's recordkeeping procedures, of which numerous examples were found during the audit, including several described in detail in the following sections of this report.

Control Weaknesses in MRG's Recordkeeping

We identified several internal control weaknesses in MRG's recordkeeping. Specifically, we found unexplained gaps in the sequential transaction numbers and contract numbers recorded, respectively, in MRG's point-of-sale system and its event planning software. Sequential numbering serves as a basic control to help ensure that all transactions are accounted for in an entity's books and records.[6] Accordingly, as discussed in below, MRG's failure to maintain sequential numbers on its transactions and contracts eliminates a basic tool designed to help ensure that there are no omissions in its records.

In addition, we found inconsistencies in MRG's recording of its gross receipts in its books and records, as is also discussed in more detail below. Article 4.7 of the Restaurant Agreement states that

> [MRG] shall maintain adequate systems of internal controls and shall keep complete and accurate records, books of account and data, including daily sales and receipts records, which shall show in detail the total business transacted by Licensee and the Gross Receipts therefrom.

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[6] See, e.g., New York State Department of Taxation and Finance, *Recordkeeping Requirements for Sales Tax Vendors*: "Users of POS systems must maintain auditable internal controls to ensure the accuracy and completeness of the transactions recorded in the POS system. . . . Audit trail details include, but are not limited to: *internal sequential transaction numbers*; . . . and *procedures to account for voids, cancellations, or other discrepancies in sequential numbering.*" [Emphasis added.] https://www.tax.ny.gov/pubs_and_bulls/tg_bulletins/st/record-keeping_requirements_for_sales_tax_vendors.htm, downloaded April 2017. For our audit scope period, MRG used the Pixelpoint system for all transactions at the Restaurant and Caterease for recording all catering events

Inadequate internal controls and inconsistent practices in recordkeeping will hinder the City's ability to determine whether MRG properly reported its gross receipts to the City.

Missing Sequential Sales Numbers in Point-of-Sale System and Event Planning Software

We were unable to determine whether all gross receipts from the operation of the Restaurant were accounted for and reported to the City because of deficiencies in the point-of-sale system and MRG's inability to retrieve certain catering contract information from its event planning software.[7] Specifically, in our review of the Restaurant's guest checks issued for our sampled period (July 5–11, 2015), we found that 44 sequential transaction numbers out of approximately 6,000 transactions were missing and not accounted for. Although the number of missing transactions was small in comparison with the population of transactions, their existence is of concern because it indicates an incomplete recording and reporting of the transactions conducted by MRG at the Restaurant.

We also found other discrepancies, such as a transaction number that was assigned out of sequence, as well as another transaction that was closed out three business days after it was initiated and had a transaction number that was more than 2,000 numbers above the first transaction number generated for that day's transactions. MRG was unable to explain any of these anomalies. As a consequence, MRG's numbering discrepancies for Restaurant transactions reflect deficiencies in MRG's system of internal controls, which could render the business and the City vulnerable to errors, omissions, and manipulation, such as incomplete recording of sales, payments, and other transactions that could result in the underreporting of gross receipts.

In addition, our review of records maintained in MRG's catering-planning system for the 12-month period of April 1, 2015 through March 30, 2016 found that records corresponding to seven of MRG's sequential catering-contract numbers were missing and unaccounted for. MRG was unable to provide an explanation for that anomaly.

In the absence of procedures and controls sufficient to produce complete, reliable business records of all financial transactions, including auditable "procedures to account for voids, cancellations, or other discrepancies in sequential numbering," there is no assurance that MRG has accurately reported its gross receipts to the City, or paid the correct license fees in accordance with the agreements.[8]

> ***MRG's Response:*** "MRG uses point of sale software to record retail sales transactions. Event sales transactions are recorded in specialized software designed to build catering and event quotes, contracts and invoices. At the time of Comptroller's audit, MRG used Pixelpoint as its point of sale system provider and Caterease for events. On or around May, 2016, prior to the commencement of this audit, MRG moved to a new point of sale platform, and, on the recommendation of its events staff, switched events management software. Data stored in both systems was retained and provided to the Audit Team. [Footnote omitted.]
>
> During the course of this audit, it was brought to the attention of MRG that the point of sale system report showed gaps in the sequential record. Specifically 44 transaction numbers were missing. While we were able to verify with our merchant processor that no credit

[7] Both the relevant point-of-sale and event planning systems were no longer in use at the time of our audit field work.

[8] New York State Department of Taxation and Finance, *Recordkeeping Requirements for Sales Tax Vendors*, op. cit.

card transactions were associated with the sequential record gaps, we cannot explain the missing transactions. It remains our understanding that the point of sale system we used at the time does not permit deletion of transactions or tampering with the transaction record. Our attempts to verify this with the US sales agent for the software were inconclusive; and we did not receive a call back from the company headquarters in Canada.

As for the incomplete transaction record in the events software, we were able to determine that the gaps represented preliminary intake information for potential events, which was not preserved by the vendor. However, MRG was able to recreate a complete record of all event proposals and final contracts, all of which was provided to the Audit Team."

Auditor Comment: The fundamental premise and purpose of an automated numbering system is to account for *every* transaction processed within the system. MRG's failure to account for missing transaction numbers reflects a deficiency in its internal control system. Furthermore, MRG's claim that it provided "a *complete* record of all events" is misleading. During the course of this audit, MRG was unable to "explain the missing transactions" in its system. As noted, that reflects a control weakness, even where MRG claims to have been able to "recreate a complete record of all event proposals and final contracts."

Inconsistencies in MRG's Recordkeeping

MRG did not consistently follow its recordkeeping procedures and did not adequately ensure the accuracy of its recorded and reported gross receipts to the City. According to the Restaurant Agreement section 4.7(a),

> Licensee shall maintain adequate systems of internal control and shall keep complete and accurate records, books of account and data, including daily sales and receipts records, which shall show in detail the total business transacted by Licensee and the Gross Receipts therefrom.

Contrary to the contractual requirement of complete and accurate records, books of account and data supported by adequate systems of internal control, we found various discrepancies and deficiencies in MRG's financial records. Specifically, we found that:

- MRG did not always record all business activities in its income journal. MRG used Excel spreadsheets as income journals to record the Restaurant's daily gross receipts, payment information, and the payment of certain miscellaneous expenses using cash collected during the day. However, our comparison of the bank deposits with the income journal for our audit scope period identified 10 discrepancies of amounts $500 or more, totaling $45,700, where MRG did not record all cash collected in its income journal. In addition, for the audit scope period, our comparison of the gross receipts recorded in the income journal and the general ledger found that the income journal recorded $75,746 more than the general ledger.
- MRG inappropriately used the "Over/Short" account as a receivables account to record amounts owed by customers for catered events. According to MRG's chart of accounts, "Over/Short" is an expense account, not an asset account, and as such should be used only to record an overage or shortage of cash collected by wait-staff. Since MRG's general ledger entries relating to this account were sometimes unexplained, we were unable to differentiate the actual overages and shortages verses the receivables owed to MRG by customers.
- Hard copies of the guest checks did not always match the sales information in the electronic back up file. Specifically, during our sampled period (July 5, 2015 to July 11,

2015), MRG was able to provide only 2,406 hardcopy guest checks out of approximately 6,000 guest checks for our review. Although MRG maintained an electronic back-up file for the guest checks, we were not able to match all the sales amounts on hardcopy guest checks with the sales amounts recorded in the back-up file. We found 79 instances where sales amounts on the hard copies of the guest checks did not match the electronic data. Some of the hardcopy guest checks showed larger sales amounts than were shown in the electronic data, while other hardcopy checks showed less. For example, the hardcopy of the guest check for July 10, 2015, transaction # 329286, showed a total amount of $143.93, while the electronic back-up file showed $0. In another instance, transaction # 331289 for July 11, 2015 showed a total of $357.06 on the hardcopy guest check, while the electronic file showed $1,000.

- MRG often did not have all the hardcopy transaction payments included in its package provided to us. We found a net discrepancy of $5,689 between the total sum of MRG's 2,406 hardcopy checks and the higher total sum of the corresponding 2,406 entries in electronic file.
- MRG did not properly classify revenue in its general ledger. Although the general ledger has separate accounts designated for catering events, MRG did not use them or otherwise identify catering revenue as a specific category of gross receipts in its general ledger. In addition, MRG recorded rental income in the miscellaneous income account instead of in the "space rental" account that was already set up in the general ledger. Since MRG did not properly categorize its gross receipts in its general ledger, we were unable to determine whether MRG accurately recorded its catering revenue in the general ledger.
- MRG inappropriately recorded *revenue*—catering service charges collected from its customers—in an *expense* account captioned "Professional Fee – Other," an account that was also used to record expenses, without explanatory notes in the memo section of the general ledger. Given the commingling of expense and revenue entries and the absence of documentation specifying the types of professional fees recorded, we were unable to determine the total amount of service charge revenues recorded in this account.
- MRG's gross receipts recorded in its general ledger cannot be reconciled to the statements of gross receipts submitted to the City. MRG's revenue categories reported to the City do not all match those recorded on its general ledger, thereby requiring additional adjustments of accounts to perform a reconciliation. In addition, MRG's general ledger does not include certain revenue categories such as "catering food," "merchandise sales" and "valet parking." As a result, even though the amount reported to the City exceeds the amount in the general ledger by over $14,000 we are unable to attest to the accuracy of either of the reported amounts.
- MRG did not record all gift card sales in its general ledger. Specifically, there was a credit balance of $1,916 in the Gift Card liability account indicating that gift cards redeemed exceeded gift cards sold by $1,916, a clear indication that MRG did not correctly record all its gift card sales.
- MRG did not always record its gross receipts timely. For example, we found that MRG received an advance deposit on July 15, 2015, for an event to be held on August 1, 2015. However, MRG did not record the payment of $2,789 until August 2, 2015, more than two weeks after the payment was received.

MRG's lack of consistency in recordkeeping prevents Parks from reconciling the gross receipts received and reported to the City. In addition, the lack of proper procedures for recording and reporting gross receipts can be perceived as lack of transparency in reporting that revenue.

MRG's Response: "MRG record keeping practices fulfill the requirements of the License Agreement: the company's full time financial controller maintains a complex system of internal controls to ensure that all income is properly documented, and records maintained. The Comptroller's own findings, identifying only $1,046 in unreported revenue out of more than $5,778,022 in Gross Receipts validates MRG's position that it maintains effective internal controls. Despite conducting the audit while our financial controller was out of the country visiting his family in the Philippines, the Audit Team was able to reconcile every penny of income with deposits and payments, with a shortfall of only 0.00018%. We believe that it is inaccurate and unfair for the Comptroller to suggest that MRG's internal controls are materially flawed.

It appears from the Audit Team's lengthy discussion in this section of the Audit Report that they incorrectly focused on the financial controller's income journal instead of focusing on the company general ledger which contains the internally audited sales and income figures used to report Gross Receipts to the City of New York. [Footnote omitted.] MRG regularly evaluates and audits its own procedures to ensure that all sales are recorded and that all Gross Receipts are accurately identified and reported. To support this assertion, our financial controller provided documentation to demonstrate that a number of the Audit Team's specific recommendations were implemented prior to commencement of this audit."

Auditor Comment: Contrary to MRG's position, our audit focused on all aspects of MRG's recordkeeping, not simply the controller's income journal, and found numerous discrepancies within MRG's various books and records, including daily gross receipts, reconciled bank statements, general ledger, and the income journal, as reported above. Therefore, MRG's contention that it is recording and reporting all its gross receipts accurately is questionable and we continue to urge MRG to strengthen its internal controls.

MRG's Records Show Partial Compliance with Capital Improvement Requirements for the Marina

MRG was unable to provide sufficient documentation to demonstrate that it completed all the capital improvements outlined in Exhibit D of the Marina Agreement. Specifically, although MRG, following the audit exit conference, provided invoices to support its statement that it had expended more than $800,000 in capital improvements, as of May 26, 2017, it still has not provided invoices to support the claimed completion of 8 of the 18 required capital improvement items for the Marina. In addition, MRG did not provide a completed copy of a Capital Verification Sheet, as required by Parks.[9]

According to the Marina Agreement, MRG was required to expend at least $454,000 to complete 18 specific capital improvements to the Marina by end of the second operating year after the commencement of the agreement. At MRG's request, Parks, by letter dated May 13, 2013, extended the commencement date to May 1, 2013.[10] Accordingly, the capital improvements should have been completed by the end of the second full operating year following the commencement date, i.e., October 31, 2015.

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[9] A Capital Verification Sheet is a document that a licensee is required to submit to Parks upon substantial completion of all capital improvements required by their agreement.

[10] Parks' letter of May 13, 2013 states that the agreement shall terminate October 31, 2028, which is the end of the 15th *full* operating year following May 1, 2013.

Based on the documentation provided to us by Parks, as of March 21, 2017, MRG had provided documentation—consisting only of canceled checks—for $66,273 for capital expenditures, which constituted less than 15 percent of the required $454,000 and could not be matched with individual capital improvements required by the agreement.[11] When we discussed this topic with MRG during the audit, MRG informed us in substance that it had completed all capital improvements on the Marina as required by the agreement and had submitted the relevant documentation to Parks. Our review, however, found that MRG had failed to submit documentation of the completed work to Parks in response to Parks' written requests. Specifically, the documentation requested by Parks included invoices, canceled checks, and a Capital Verification Sheet—which would constitute MRG's representation to Parks that the specific capital improvements listed thereon had been substantially completed in accordance with the agreement. In a third notice to MRG, dated January 26, 2015, Parks requested that the required documentation be submitted by February 20, 2015.

Notwithstanding Parks' written request, and our requests during the audit, MRG did not submit any of the above-described documentation to Parks until after our May 24, 2017, exit conference. Based on the invoices and payment records that MRG provided to Parks after that exit conference, we were able to verify that MRG had procured and paid for work related to 10 of the 18 required capital improvement items. However, the additional documentation was insufficient to establish whether the remaining eight items were completed.

According to Article 6.4 of the Marina Agreement, "[i]n the event Licensee fails to finally complete a particular improvement by the date specified for completion in Exhibit D, Licensee may be required to pay the City liquidated damages of $100 per day until the outstanding improvement is completed." Should Parks determine that MRG has not completed any of the required capital improvements to the Marina, Parks would have a right to assesses liquidated damages, provided it gave MRG the requisite "notice to cure" and an opportunity to do so, in accordance with the Marina Agreement.

> ***MRG Response:*** "MRG expended approximately $881,619.00 to restore the Dyckman Landing Marina and facilities. This is far more than the $454,000 required under the License Agreement. While MRG acknowledges that the Capital Verification Sheet may not have been provided to the Department of Parks and Recreation, when the Audit Team requested documentation to demonstrate that all of the required capital improvements were timely completed, MRG promptly complied."
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> ***Auditor Comment:*** Despite our repeated requests as well as repeated requests from Parks dating back more than two years, MRG waited until the end of our audit to submit its documentation of capital improvements, after having stated that it had lost that same documentation in 2012 during Superstorm Sandy. Even now, MRG acknowledges that it failed to provide the written representation for completion of work required by the Marina Agreement and repeatedly requested by Parks—the Capital Verification Sheet. Moreover, it was not until *after* the May 24, 2017, exit conference for this audit that MRG provided us and including Parks with the required invoices for work MRG was required to have completed nearly two years earlier. At this point, because of MRG's dilatory and inconsistent responses to basic record requests, the question of whether MRG completed all required capital improvements remains to be determined by Parks.

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[11] Capital improvement documents were obtained from Parks because MRG officials said that their records were destroyed during Hurricane Sandy, which struck New York City in October 2012.

MRG Failed to Execute a Written Seasonal Docking Contract

Although MRG stated it had just one seasonal docking client for operating year 2016, it was unable to provide a contract with that client. According to MRG officials, no written contract was executed for the seasonal slip rental.

According to MRG's Marina Agreement with Parks, section 4.7, (a), "[l]licensee shall maintain adequate systems of internal control and shall keep complete and accurate records, books of account and data, including daily sales and receipts records, which shall show in detail the total business transacted by Licensee and the Gross Receipts thereof."

MRG stated that it had an understanding with the client for the seasonal docking and that no written contract was executed. MRG further stated that the gross receipts earned from the entire Marina business were less than the threshold amount that would have triggered its obligation to pay a percentage to the City under the Marina Agreement. However, without a written docking contract outlining payment terms, we were unable to determine whether MRG had accurately reported all gross receipts from the operation of the Marina.

> ***MRG's Response:*** "Seasonal dockage income was included in the calculation of Gross Receipts provided to the City. Invoice and proof of payment were provided to the Audit Team both early in the audit and then again at the close-out meeting. The assertion that MRG 'had an understanding' with the seasonal dockage customer misquotes a verbal exchange. MRG acknowledges that it did not enter into a contract with the seasonal docking customer, though disputes that the License Agreement requires contracts for seasonal docking."
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> ***Auditor Comment:*** We are not questioning whether the dockage income reported by MRG was included in the calculation of gross receipts, but rather are noting that without a written agreement stating the price and signed by both parties, MRG's documentation was insufficient to demonstrate that the sum MRG collected from its seasonal docking client and reported to the City reflected the actual value of the docking facility as agreed between the two parties. The Marina Agreement requires MRG to "keep complete and accurate records . . . , which show in detail the total business transacted by Licensee and the Gross Receipts thereof." In the absence of a written contract or equivalent memorialization of the agreed price and terms there is no way to determine whether the invoiced amount reported by MRG constitutes, with respect to the seasonal dockage transaction, "the total business transacted by Licensee and the Gross Receipts thereof."

MRG Failed to Maintain, or Provide Documentation to Show it Maintained, Required Insurance Coverage

Our review of MRG's 2016 insurance records found that MRG failed to provide records to show it maintained certain categories of required insurance coverage that it was obligated to secure, at its own cost and expense, for the Restaurant and the Marina. Missing from the insurance records that were produced in connection with the audit were records reflecting certain insurance in the required coverage amounts and for necessary coverage dates. MRG's failure to honor its contractual obligation to maintain proper insurance—or to demonstrate that it honored that obligation—may have left the City and the public exposed to risk of loss for injuries and events that might have occurred as a result of MRG's occupancy and operations on City property.

According to the terms of the Restaurant Agreement, Section 20.1:

> Licensee shall, at its own cost and expense, procure and maintain such insurance for the Interim Period and the Term of the License as will: a) protect Licensee from Worker's Compensation, Disability, and Employer's Liability claims; b) insure Licensee, its agents and sublicensees, the City, Parks, DEP and their agents against any and all loss, liability, obligations, fines, damages, penalties, claims, charges, costs, or expenses.

Furthermore, Section 20.2 states that

> [T]he policy shall provide the amounts of insurance hereafter mentioned, and . . . Each certificate shall be marked "Premium Paid" and shall have endorsed thereon: "No cancellation of or change in this policy shall become effective until after thirty days' notice by Certified Mail to Asst. Commissioner for Revenue, Department of Parks and Recreation. . . .

We found that, for the Restaurant operation, MRG did not have or did not provide records to show it had coverage for two categories of required insurance, as reflected in Table I(a), which follows.

Table I(a)

Insufficient Insurance Coverage– Restaurant
for the Period April 1, 2015 through March 31, 2016

Type of Insurance Required Per Agreement 20.6	Amount Required on Insurance	Amount Covered	Insufficient Amount	Policy Effective Date	Policy Expiration Date	Period Not Covered
Any Auto, Hired Auto, and Non-Owned Auto for any one occurrence	$ 1,000,000	Not Provided				4/1/2015 to 3/31/2016
Fire and Extended Coverage for any one occurrence	Replacement value of the buildings; reassessed every year	Not Provided				4/1/2015 to 3/31/2016

Similarly, MRG did not have or did not provide records of sufficient insurance for the Marina during the 2016 operating year. Table I(b), which follows, shows that the Marina did not have sufficient insurance coverage for two categories of required insurance.

Table I(b)

Uninsured Periods – Marina
for the Period November 1, 2015 through October 31, 2016

Description of Insurance Required	Amount Required	Amount Covered	Insuffient Amount	Effective Date	Expiration Date	Period Not Covered
Any Auto, Hired Auto, and Non-Owned Auto for any one occurrence	$ 1,000,000	Not Provided				11/1/2015 to 10/31/2016
Fire and Extended Coverage for any one occurrence	Replacement value of the buildings; reassessed every year	Not Provided				11/1/2015 to 10/31/2016

MRG's failure to maintain the insurance required by its agreements with the City improperly exposed the public and the City to unnecessary risk of loss and/or harm in the event of an accident or other disastrous event.

MRG's Response: "The audit team identified two apparent lapses in MRG's insurance coverage, and MRG provided explanations to both.

a) Hired Auto Coverage. This coverage covers liabilities arising from the use of private and hired vehicles for company purposes. In most cases, this coverage is included with general liability coverage without extra cost. However, in the course of the audit, it came to our attention that the Certificate of Insurance provided to the Audit Team did not expressly list this coverage as being included in MRG's general liability policy. We have not been able to verify if this coverage was in place at the time, but can confirm that there have been no claims have been raised for occurrences within the audit period for which this coverage would have been triggered. MRG currently has hired auto coverage as part of its general liability insurance policy."

b) Reassessment of Value of Buildings. It should be clarified that MRG maintains a valid and binding insurance policy on the replacement value of the buildings; however, we neglected to have the value of the buildings reassessed on an annual basis. Notwithstanding this omission, we continue to believe that MRG maintains suitable coverage on the value of the buildings, and that the City of New York is not improperly exposed to a loss event.

The above explanations apply to both Marina and Restaurant License Agreements."

Auditor Comment: The absence of contractually-required insurance coverage—including any lapse in existing coverage—poses a significant risk to the public and the City. Therefore, MRG should ensure that it timely procures all required insurance and obtains reassessments of the replacement values each year.

RECOMMENDATIONS

MRG should:

1. Remit to Parks $56,952 in additional license fees and late charges owed to the City due to MRG's having underreported the Restaurant's gross receipts;

   MRG's Response: "MRG disputes this recommendation, but acknowledges (a) a shortfall of $84, plus late fees as a result of its failure to report $1,046; and that (b) MRG will work with parks to include service fees not paid to front of house staff in the recalculation of gross receipts."

   Auditor Comment: The bulk of the additional license fees and late charges MRG currently owes to the City result from MRG's exclusion of two types of transactions from gross receipts it reported to the City: (1) $257,294 worth of complimentary meals and beverages and discounts on meals and beverages served at the Restaurant; and (2) $187,998 in service charges MRG collected for catered events. We found that under the Restaurant Agreement, both sums should have been reported to the City, and that MRG should therefore pay the City its share of those sums.

   As to the complimentary meals and discounts, MRG has disputed our interpretation of the Restaurant Agreement, and Parks reports that it is reviewing the matter with its General Counsel and the City's Law Department. Pending that review, we continue to recommend that MRG remit the sum owed, which we calculate as at least $20,584, plus late charges.

   As to the unreported service charges, MRG has provided no additional documentation and has otherwise failed to support its contention that some portion of the excluded amount constituted gratuities rather than service charges. Accordingly, we reiterate our recommendation to MRG that it remit to Parks the sum MRG owes the City for that revenue, which we calculate at $15,040 plus applicable late fees, and we recommend that Parks collect the full amount owed by MRG.

2. Accurately report all gross receipts to Parks by including:

   - All complimentary meals, beverages, and discounts provided by the Restaurant;

     MRG's Response: "MRG will work with Parks to determine what comps and discount categories may be excluded from gross receipts, subject at all times to proper documentation and support."

   - All catering service charges;

     MRG's Response: *"*Based on the audit findings, we will make this change.*"*

   - Advance deposit and gift cards sales when proceeds are received;

     MRG's Response: "Based on the audit findings, we will make this change."

   - Overpayments received from patrons;

     MRG's Response: "Overpayments received from patrons are recorded as gross receipts."

3. Ensure that its point-of-sale system properly account for all sequential transaction numbers issued, and that all sales and revenue-transactions are included in gross receipts reported to Parks;

MRG's Response: *"*To the best of our knowledge, MRG's current POS system (installed in May 2016) properly accounts for all transactions on a sequentially numbered basis. MRG will include all revenue transactions in gross receipts reported to Parks."

4. Ensure that all gross receipts are recorded accurately and with consistency in and across all financial records, including but not limited to the income journal, general ledger, and certified statement of gross receipts reported to Parks;

   MRG's Response: "MRG has and will continue to maintain consistent and accurate financial controls and reporting."

   Auditor Comment: Apart from the unwarranted exclusions of certain transactions from gross receipts addressed in Recommendations 1 and 2, MRG's financial records contained numerous discrepancies and inconsistencies, some of which were noted in the audit report. We recommend that MRG review the specific examples cited in this report and change its procedures as needed to achieve consistency in its financial records.

5. Ensure that all deposits and revenue from special events are recorded and reported in a separate, appropriately named revenue category for purposes of accountability and to enable reconciliation with contracts generated for special events;

   MRG's Response: "MRG now maintains a separate revenue category for events."

6. Utilize the "Over/Short" account only for actual daily cash shortages or overages and not for any other purpose;

   MRG's Response: "The over/short account is used for daily cash accounting only."

7. Establish a Catering Receivables account in its general ledger to properly account for the catering receivables.

   MRG's Response: "A catering receivables account has been established in the General Ledger."

8. Provide all documentation for capital improvements to Parks for review; and

   MRG's Response: "Work has been completed and documentation has been provided."

9. Ensure the Restaurant and the Marina are properly insured at all times.

   MRG's Response: "The Restaurant and Marina have been, and remain, properly insured. MRG has requested a reassessment of the property value for policies now in effect."

Parks should:

1. Ensure that MRG remits all additional fees due with applicable late fee charges;

   Parks' Response: "With regard to potential fees owed on complimentary meals and beverages, and service charges, there is a difference in interpretation of the license agreement between the Comptroller's Office and MRG. Parks is reviewing this matter with our General Counsel and the City's Law Department. With regard to advance deposits, while we concur that advance deposits and gift card purchases should be reported at the time of its sale, the amounts cited in the Report were purchased in late 2015/early 2016 and were later redeemed and reported in their gross receipts after the March 31, 2016, end of this audit period. We are also following up with MRG to ensure receipt of the amount cited in the Report related to their not including an overpayment they collected in their reported gross receipts."

Auditor Comment: As to the complimentary meals and discounts, MRG has disputed our interpretation of the Restaurant Agreement, and Parks reports that it is reviewing the matter with its General Counsel and the City's Law Department. Pending that review, we continue to recommend that MRG remit the sum owed, which we calculate as at least $20,584, plus late charges.

As to the unreported service charges, MRG has provided no additional documentation and has otherwise failed to support its contention that some portion of the excluded amount constituted gratuities rather than service charges. Accordingly, we reiterate our recommendation to MRG that it remit to Parks the sum MRG owes the City for that revenue, which we calculate at $15,040 plus applicable late fees, and we recommend that Parks collect the full amount owed by MRG.

As to the advanced deposits and overpayment by client on catered event, we recommend that Parks collect late charges.

2. Ensure that all promotional and complimentary management discounts utilized by MRG for customer relationships are recorded as gross receipts and included in the calculation for fees due to the City;

   Parks' Response: "Due to the difference in interpretation of the license agreement between the Comptroller's Office and MRG, Parks is reviewing this matter with our General Counsel and the City's Law Department."

3. Ensure that MRG provides documentation to show that capital improvements at the Marina are completed as required by the agreement;

   Parks' Response: Parks combined its response to this recommendation with recommedaton # 4 below.

4. Assign or retain an engineer to observe and evaluate the capital improvements performed at the Marina;

   Parks' Response: "Parks is in receipt of documentation from MRG related to capital improvements they made at the Marina and we are currently in the process of verifying them to ensure that it complies with the requirements of the agreement. After review, if we believe any improvements necessitate further evaluation, we will consider assigning an engineer."

5. Determine whether it should provide the requisite notice and opportunity to cure and assess the liquidated damages for the unfinished capital improvements at the Marina;

   Parks' Response: **"**We are currently in the process of verifying the capital documentation that MRG submitted for the Marina. If it is determined that any required items under the agreement remain unfinished, Parks will follow up with MRG accordingly."

6. Enhance Parks oversight to enable it to ensure that MRG maintains all required insurance coverage for the Restaurant and Marina operations and all times; and

   Parks' Response: "We will follow up regularly with MRG to ensure that all required insurance coverage is maintained."

7. Ensure MRG implements the recommendations in this report.

   Parks' Response: "Parks has discussed the recommendations in this Report with MRG and, where appropriate, will work with MRG to implement recommended improvements, or otherwise address the concerns raised by the Report."

DETAILED SCOPE AND METHODOLOGY

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. This audit was conducted in accordance with the audit responsibilities of the City Comptroller as set forth in Chapter 5, §93, of the New York City Charter.

The scope of this audit covered the operating year 2016, including April 1, 2015 through March 31, 2016 for the Restaurant and November 1, 2015 through October 31, 2016 for the Marina.

To gain an understating of MRG's responsibilities and requirements with relation to the operation of the Restaurant and the Marina, we reviewed its license agreement with Parks, which formed the basis of our audit criteria.

To obtain an understanding of the operation of the Restaurant and the Marina by MRG, we performed an observation of the Restaurant and the Marina, conducted walk-throughs of the operation, interviewed officials at MRG and Parks to understand their roles and responsibilities, and requested and reviewed financial documents received from MRG and Parks related to the operation of the Restaurant and the Marina. We documented our understanding of the operation in memoranda.

To determine whether revenues at the Restaurant and Marina were reported to Parks, we reconciled MRG's monthly income journals to the QuickBooks general ledgers and then to the monthly gross receipts statements submitted to Parks and the annual gross receipts summary report for all gross receipts generated for operating year 2016.

To determine whether the Restaurant operation utilized a sequential numbering system for its sales and payments, we obtained and analyzed the Restaurant guest checks for the highest grossing week of July 5 through July 11, 2015 for the operating year 2016. To determine the accuracy and completeness of the recording of gross receipts, we compared the daily amounts recorded on the guest checks to the Daily Summary Report generated from the Restaurant's point-of-sale system and to the daily income journal, an Excel spreadsheet that MRG officials updated manually using the daily Income Summary Report. We also obtained and reviewed the exception reports generated by MRG's point-of-sale system.[12] In addition, we judgmentally reviewed the event folders for all special events held in July and August 2015 and traced the special event gross receipts to the income journal and/or general ledger.[13]

For the Marina operation, we requested MRG to provide all contracts related to seasonal docking at the Marina. We then traced the rental revenue to MRG's general ledger.

To determine whether MRG maintained segregated bank accounts and made proper daily deposits of revenue received from operations of the Restaurant and the Marina, we reconciled the monthly income recorded in MRG's income journal to the credit card statements and to MRG's two bank statements. We also compared the credit card payments recorded on the income journal to the settlement amounts on the credit card statements.

[12] Exception reports contain information of the voided transactions, complimentary transactions, promotions and discount information.

[13] July and August 2015 were selected because they represented the months with the highest gross revenue during the operating year 2015-2016.

To determine whether MRG accurately paid all fees to Parks, we reviewed Parks' Lease Ledger for the Restaurant and the Marina and compared them with the gross receipts reported by MRG. In addition, we determined whether MRG made timely payments to Parks by conducting a comparison of the payment dates to the due dates for each installment of the minimal seasonal fee and percentage fees.

To determine whether MRG maintained the required insurance coverage, we reviewed the insurance certificates and ensured the City was listed as the additional insured on the policy. In addition, to determine whether MRG complied with the security deposit requirement, we reviewed MRG's letter-of-credit to ascertain Parks was the benefactor.

Finally, to determine whether MRG expended the required amounts for capital improvements, of the Restaurant and the Marina, we reviewed invoices, contracts, Parks' checklist and other documents associated with capital improvements.

The results of our test, while not projectable, provided sufficient, appropriate evidence to support our conclusions regarding MRG's compliance with the City's license agreements.

Month	Discounts and Manager's Promos	Overpayment by Client for Event recorded in GL	Service Charges for Events	Advance Deposits*	Total Underreported	# of Months Late as of 05/11/2017	8% of Fees Due	Compounded Late Fees at 2% on Fees Due as of 5/11/2017	Total Due Plus Late Charges
Apr-15	$385	$1,046	$11,462		$12,893	22	$1,031	$563	$1,595
May-15	$41,180		$8,176		$49,356	22	$3,948	$2,156	$6,104
Jun-15	$42,805		$20,767		$63,572	22	$5,086	$2,777	$7,863
Jul-15	$71,313		$12,633		$83,946	21	$6,716	$3,463	$10,179
Aug-15	$65,581		$11,785		$77,366	20	$6,189	$3,008	$9,197
Sep-15	$35,990		$40,863		$76,853	19	$6,148	$2,809	$8,957
Oct-15	$40		$25,200		$25,240	18	$2,019	$865	$2,884
				$28,000	$28,000	6	$2,240	$283	$2,523
Nov-15			$16,277		$16,277	17	$1,302	$521	$1,823
Dec-15			$19,061		$19,061	16	$1,525	$568	$2,093
Jan-16			$14,387		$14,387	15	$1,151	$398	$1,549
Feb-16			$1,373		$1,373	14	$110	$35	$145
Mar-16			$6,014	$5,386	$11,400	13	$912	$268	$1,180
				$3,375	$3,375	1	$270	$5	$275
				$5,775	$5,775	12	$462	$124	$586
TOTAL	**$257,294**	**$1,046**	**$187,998**	**$42,536**	**$488,874**		**$39,110**	**$17,842**	**$56,952**

* Late fees were calculated up to the month MRG recognized the advance deposits as revenue.

MANHATTAN RIVER GROUP, LLC
348 DYCKMAN STREET NEW YORK NY 10034

MANHATTAN RIVER GROUP, LLC
RESPONSE TO AUDIT REPORT
ISSUED BY
CITY OF NEW YORK
OFFICE OF THE COMPTROLLER,
SCOTT M. STRINGER

June 19, 2017

This response addresses the findings of the Office of the Comptroller's June 5, 2017 Audit Report (the "Audit Report"). In the paragraphs below, we carefully evaluate the Comptroller's arguments and attempt to respond to specific issues raised. We conclude that the Audit Team has not undertaken an adequate legal review of the License Agreements between Manhattan River Group, LLC ("MRG") and the City of New York (the "License Agreement"), and has failed to take into consideration best practices in the food and beverage industry. Specifically, the Comptroller's findings attempt to rework the definition of Gross Receipts set forth in the License Agreement to include large swaths of foregone income that were properly documented and excluded. The Comptroller has also exaggerated minor lapses in record keeping and focused in on software issues that were corrected well before the commencement of this audit.

Find below our responses to each item listed in the Comptroller's Audit Report. Unless otherwise indicated, capitalized terms have the meanings set forth in the License Agreement.

I. *REPORTING OF GROSS RECEIPTS*

In its Audit Report, the Comptroller incorrectly concludes that MRG did not report more than $450,000 in gross revenue from comps, discounts, service charges and advance deposits. Our own analysis demonstrates that the Comptroller's audit team (the "Audit Team") has based its conclusions on a number of fundamental errors: (a) in the case of complimentary items and discounts, the License Agreement does <u>not</u> require MRG to pay the license fee on revenue that was never actually received due to legitimately issued comps and discounts; (b) in the case of advance deposits, the amounts were all reported to the City of New York; and (c) in the case of service charges, amounts paid to front of house staff were correctly deemed gratuities and thus exempt from inclusion in MRG's statement of Gross Receipts.

A. Comps and Discounts

For purposes of this response, "comps" are food and beverage items that are given to potential new customers, repeat customers, and guests who are dissatisfied with their experience. A typical example is a spilt beverage, which MRG replaces at no cost to the customer. In this example, the replacement beverage order will be entered into our point of sale system; the item will then be produced and comped. The inventory will have been depleted, but no revenue will be received. In another example, MRG may invite a potential private event client for brunch in order to close an event.

The *comp* function in MRG's point of sale system is also frequently used for other purposes having nothing to do with customer experience. For example, a comp will be issued to track a reduction in inventory where income is to be imminently, but not immediately, received (for example, a declined payment when the guest is already known to MRG). The comp function is also be used to track actual consumption where products are paid for in advance – for example, prepaid open bar for a private event. No revenue is collected for items that are *comped*, but the comped items are still indicated in the company's point of sale system at full value for purposes of inventory tracking.

"Discounts", on the other hand, are typically given as an incentive. Common discounts include *happy hour* discounts and percentage reductions given to customers who have demonstrated loyalty or who have accumulated a large bill (akin to a *bulk discount* or *volume discount* in other industries). Discounts might also be given for certain items or for a particular occurrence to drive sales (a rainy day discount of 10% when there is a high probability of rain). Similar to comps, if an item is discounted, the uncollected portion is not reported as Gross Receipts.

MRG's License Agreement with the City of New York defines "Gross Receipts" as including "funds or receipts of any kind ***received*** by Licensee…." Sections 2.1(j)(i)-(v) of the License Agreement goes on to allow and disallow certain exclusions from Gross Receipts. For example, Paragraph (i) states that MRG may not exclude revenue even if the order is "placed or made at Licensed Premises, *although delivery of merchandise or services may be made outside*…." Paragraph (iv) clarifies that it is the intention of the License Agreement "…that all sums *due to be received* by Licensee from all sources from the operation of this License shall be included in Gross Receipts" - in other words, even if payment is deferred, such deferred payment shall be included in Gross Receipts, unless and until it is deemed a bad debt, in which case it would be specifically excluded from Gross Receipts pursuant to Paragraph (v).[1]

The Comptroller's Audit Report concludes otherwise. Instead of paying a fee on *revenue received*, or even on *sums due to be received*, the Audit Team hypothesizes that MRG should be responsible for paying the License Fee for "any orders placed or made at Licensed Premises [and]…Gross Receipts shall include sales made for cash or credit (credit sales shall be included in gross receipts as of the date of the sale) regardless of whether the sales are paid or uncollected (sic)." To create this definition, the Audit Team combined a clause from Paragraph (i), discussing revenues from off premises catering, with a clause from Paragraph (iv), which deals with credit sales.

Under the Comptroller's revised definition of Gross Receipts, MRG underpaid the City of New York by $39,110 despite the fact that the revenue on which this additional fee would be calculated was never charged to any customer or received by MRG. The Audit Team appears to be most troubled by particular comps and discounts that it considers unjustified; however the Audit Report refuses to address the well documented business purpose behind comps and discounts, MRG's extensive tracking and reporting, or industry best practices.

In fact, MRG's comp rate (the total comps and discounts divided by gross revenue) for the audit period was approximately 4.4%, in line with industry norms. According to a 2014 report by analysts at Breadcrumb POS, the average comp rate for New York restaurants is 3.59%, a difference of less than 1%.[2] Considering that MRG's business faces operational challenges such as enormous volume over just a few months, unpredictable weather, and a high number of seasonal staff, its comp rate suggests that MRG comp and discount practices are not out of the ordinary. Furthermore, the Comptroller's findings disregard that comps and discounts were systematically documented in MRG's point of sale system and accurately

[1] Emphasis added throughout this paragraph.

[2] See https://blogdotbreadcrumbposdotcom.wordpress.com/tag/new-york/ Breadcrumb was previously owned by Groupon and purchased in 2016 by Upserve, a highly regarded restaurant software company. Breadcrumb at the time of this analysis was used in thousands of food and beverage businesses in major metropolitan areas across the United States.

reported to the City of New York pursuant to this audit and previously in disclosures to the Department of Parks and Recreation.

Nothing in the License Agreement requires MRG to pay the percentage license fee on revenue that it never received when items are properly comped or discounted in accordance with food and beverage industry best practices. It would be contrary to the plain language of the License Agreement to require MRG to pay a fee on revenue that it would have been unable to collect, or on amounts that would have been collectible only in complete disregard for its customers. Despite the basic proposition of the License Agreement that Gross Receipts include "funds or receipts of any kind *received by Licensee*", the Audit Report concocts a new, much broader definition that was never agreed by MRG.

B. Service Charges

The Audit Team determined that any amounts listed as *service charges* on catering contracts should be included in Gross Receipts even when those amounts were paid in full to front of house staff.[3] The license Agreement states in relevant part, "any gratuities transmitted by Licensee directly or indirectly to employees and staff shall not be included within Gross Receipts." Subsection (iv)(b) goes on to explain that gratuities must meet the following requirements: (i) the amount must be separately stated on the bill or invoice, (ii) it must be "specifically designated as a gratuity, or purport… to be a gratuity", and (iii) it must paid in total to front of house staff providing services at the event.

In its analysis, the Audit Team determined that $187,998 in service charges are not gratuities and must be reported as Gross Receipts, at a potential cost to our business of $15,040 in license fees. However, we believe that a large percentage of these service charges meet the definition of gratuities. MRG considers service charges paid in full to front of house staff to be gratuities under the License Agreement and thus exempt from inclusion in the calculation of Gross Receipts. Any amounts paid to non-service staff (i.e. kitchen and support) should have been included in MRG's calculation of Gross Receipts.

Based on our further analysis of the information compiled for the Audit Team, we have determined that some *service charges* should not have been classified as *gratuities*. MRG will provide further analysis and remit additional License Fee on recalculated Gross Receipts.

C. Advance Deposits

The Audit Team determined that "MRG Omitted $42,536 in Advance Deposits in Reporting Its Gross Receipts to the City". However, that statement leaves out the relevant fact that MRG did include the full amount of those advance deposits in its Gross Receipts calculation, and further, paid the city $3,403 in license fee that the Audit Team stated remains unpaid. Amounts and payment dates are as follows:

1)	$5,744.79	Event cancelled; deposit returned
2)	$5,417.25	Event held on 4/16/16; License Fee paid in April 2016 statement of Gross Receipts
3)	$18,000.00	Event held on 4/16/16; License Fee paid in April 2016 statement of Gross Receipts
4)	$10,000.00	Event held on 4/19/16; License Fee paid in April 2016 statement

[3] The Audit Team correctly quotes the relevant portion of the Gross Receipts definition, which it notably failed to include in its discussion of comps and discounts: "'Gross Receipts' shall include all funds or receipts of any kind ***received*** by Licensee without deduction or set-off of any kind…" (emphasis added).

		of Gross Receipts
5)	$3,375.00	Event held on 6/13/16; License Fee paid in June 2016 statement of Gross Receipts

It has come to our attention through this audit that the City of New York expects event deposits to be booked as income on the date they are received, rather than on the date they become non-refundable, a system that is contrary to accounting best practices. MRG has agreed to adjust its calculation methodology to include date hold, gift cards and other event deposits on the date income is received. If for any reason, a deposit is returned, we have been instructed to credit the amount of License Fee paid on such amount.

D. Failure to Report $1,046

The Audit Team uncovered $1,046.00 that was not included in MRG's calculation of Gross Receipts. This appears to have been a bookkeeping error. Concurrent with this letter, MRG has remitted payment $84 to the New York City Department of Parks and Recreation. We note that this shortcoming amounts to 0.00018% of Gross Receipts during the audit period.

II. *RECORDKEEPING AND REPORTING*

E. Alleged Control Weakness

This is addressed in MRG's response to the concrete finding discussed below.

F. Missing Sequential Sales Numbers

MRG uses point of sale software to record retail sales transactions. Event sales transactions are recorded in specialized software designed to build catering and event quotes, contracts and invoices. At the time of Comptroller's audit, MRG used Pixelpoint as its point of sale system provider and Caterease for events. On or around May, 2016, prior to the commencement of this audit, MRG moved to a new point of sale platform, and, on the recommendation of its events staff, switched events management software. Data stored in both systems was retained and provided to the Audit Team.[4]

During the course of this audit, it was brought to the attention of MRG that the point of sale system report showed gaps in the sequential record. Specifically 44 transaction numbers were missing. While we were able to verify with our merchant processor that no credit card transactions were associated with the sequential record gaps, we cannot explain the missing transactions. It remains our understanding that the point of sale system we used at the time does not permit deletion of transactions or tampering with the transaction record. Our attempts to verify this with the US sales agent for the software were inconclusive; and we did not receive a call back from the company headquarters in Canada.

As for the incomplete transaction record in the events software, we were able to determine that the gaps represented preliminary intake information for potential events, which was not preserved by the vendor. However, MRG was able to recreate a complete record of all event proposals and final contracts, all of which was provided to the Audit Team.

[4] As of May, 2016, MRG no longer uses Pixelpoint or Caterease software, and has verified that sequential integrity cannot be compromised in the point of sale and events management software currently in use.

G. Alleged Inconsistencies in Record Keeping

MRG record keeping practices fulfill the requirements of the License Agreement: the company's full time financial controller maintains a complex system of internal controls to ensure that all income is properly documented, and records maintained. The Comptroller's own findings, identifying only $1,046 in unreported revenue out of more than $5,778,022 in Gross Receipts validates MRG's position that it maintains effective internal controls. Despite conducting the audit while our financial controller was out of the country visiting his family in the Philippines, the Audit Team was able to reconcile every penny of income with deposits and payments, with a shortfall of only 0.00018%. We believe that it is inaccurate and unfair for the Comptroller to suggest that MRG's internal controls are materially flawed.

It appears from the Audit Team's lengthy discussion in this section of the Audit Report that they incorrectly focused on the financial controller's *income journal* instead of focusing on the company *general ledger* which contains the internally audited sales and income figures used to report Gross Receipts to the City of New York.[5] MRG regularly evaluates and audits its own procedures to ensure that all sales are recorded and that all Gross Receipts are accurately identified and reported. To support this assertion, our financial controller provided documentation to demonstrate that a number of the Audit Team's specific recommendations were implemented prior to commencement of this audit.

H. <u>Partial Compliance with Capital Requirements</u>

MRG expended approximately $881,619.00 to restore the Dyckman Marina and facilities. This is far more than the $454,000 required under the License Agreement. While MRG acknowledges that the Capital Verification Sheet may not have been provided to the Department of Parks and Recreation, when the Audit Team requested documentation to demonstrate that all of the required capital improvements were timely completed, MRG promptly complied.

III. *MISCELLANEOUS*

I. Docking Contract

Seasonal dockage income was included in the calculation of Gross Receipts provided to the City. Invoice and proof of payment were provided to the Audit Team both early in the audit and then again at the close-out meeting. The assertion that MRG "had an understanding" with the seasonal dockage customer misquotes a verbal exchange. MRG acknowledges that it did not enter into a contract with the seasonal docking customer, though disputes that the License Agreement requires contracts for seasonal docking.

J. Insurance

The audit team identified two apparent lapses in MRG's insurance coverage, and MRG has provided explanations to both.

a) Hired Auto Coverage. This coverage covers liabilities arising from the use of private and hired vehicles for company purposes. In most cases, this coverage is included with general liability coverage without extra cost. However, in the course of the audit, it came to our attention that the Certificate of

[5] MRG's general ledger does not include certain items of revenue that are reported to the Department of Parks and Recreation as income, but which are not actually received by MRG. Such items are included in MRG's calculation of Gross Receipts, but not listed in the general ledger.

Insurance provided to the Audit Team did not expressly list this coverage as being included in MRG's general liability policy. We have not been able to verify if this coverage was in place at the time, but can confirm that there have been no claims have been raised for occurrences within the audit period for which this coverage would have been triggered. MRG currently has hired auto coverage as part of its general liability insurance policy.

b) Reassessment of Value of Buildings. It should be clarified that MRG maintains a valid and binding insurance policy on the replacement value of the buildings; however, we neglected to have the value of the buildings reassessed on an annual basis. Notwithstanding this omission, we continue to believe that MRG maintains suitable coverage on the value of the buildings, and that the City of New York is not improperly exposed to a loss event.

The above explanations apply to both Marina and Restaurant License Agreements.

IV. *RECOMMENDATIONS FOR MRG:*

1. Remit to parks $56,952 in additional license fees and late charges owed to the City due to MRG's having underreported the Restaurants gross receipts:

MRG DISPUTES THIS RECOMMENDATION, BUT ACKNOWLEDGES (A) A SHORTFALL OF $84, PLUS LATE FEES AS A RESULT OF ITS FAILURE TO REPORT $1,046; AND THAT (B) MRG WILL WORK WITH PARKS TO INCLUDE SERVICE FEES NOT PAID TO FRONT OF HOUSE STAFF IN THE RECALCULATION OF GROSS RECEIPTS.

2. Accurately report all gross receipts to Parks by including:

- All complimentary meals, beverages, and discounts provided by the Restaurant;

MRG WILL WORK WITH PARKS TO DETERMINE WHAT COMPS AND DISCOUNT CATEGORIES MAY BE EXCLUDED FROM GROSS RECEIPTS, SUBJECT AT ALL TIMES TO PROPER DOCUMENTATION AND SUPPORT.

- All catering service charges;

BASED ON THE AUDIT FINDINGS, WE WILL MAKE THIS CHANGE.

- Advance deposit and gift card sales when proceeds are received;

BASED ON THE AUDIT FINDINGS, WE WILL MAKE THIS CHANGE.

- Overpayments received from patrons;

OVERPAYMENTS RECEIVED FROM PATRONS ARE RECORDED AS GROSS RECEIPTS.

3. Ensure that its point-of-sales system properly account for all sequential transaction numbers issued, and that all sales and revenue-transactions are included in gross receipts reported to Parks *(sic);*

TO THE BEST OF OUR KNOWLEDGE, MRG'S CURRENT POS SYSTEM (INSTALLED IN MAY 2016) PROPERLY ACCOUNTS FOR ALL TRANSACTIONS ON A SEQUENTIALLY NUMBERED BASIS. MRG WILL INCLUDE ALL REVENUE TRANSACTIONS IN GROSS RECEIPTS REPORTED TO PARKS.

4. Ensure that all gross receipts are recorded accurately and with consistency and across all financial records, including but not limited to the income journal, general ledger, and certified statement of gross receipts reported to Parks;

MRG HAS AND WILL CONTINUE TO MAINTAIN CONSISTENT AND ACCURATE FINANCIAL CONTROLS AND REPORTING.

5. Ensure that all deposits and revenue from special events are recorded and reported in separate, appropriately named revenue category for purposes of accountability and to enable reconciliation with contracts generated for special events;

MRG NOW MAINTAINS A SEPARATE REVENUE CATEGORY FOR EVENTS.

6. Utilize the "Over/Short" account only for actual daily cash shortages or overages and not for any other purpose;

THE OVER/SHORT ACCOUNT IS USED FOR DAILY CASH ACCOUNTING ONLY.

7. Establish a Catering Receivables account in its general ledger to properly account for the catering receivables;

A CATERING RECEIVABLES ACCOUNT HAS BEEN ESTABLISHED IN THE GENERAL LEDGER.

8. Provide all documentation for capital improvements to Parks for review; and

WORK HAS BEEN COMPLETED AND DOCUMENTATION HAS BEEN PROVIDED.

9. Ensure the Restaurant and the Marina are properly insured at all times.

THE RESTAURANT AND MARINA HAVE BEEN, AND REMAIN, PROPERLY INSURED. MRG HAS REQUESTED A REASSESSMENT OF THE PROPERTY VALUE FOR POLICIES NOW IN EFFECT.

Based on the foregoing, MRG submits this response to the Comptroller's Audit Report as of the date first set forth above.

Manhattan River Group, LLC

By: ______________________________
Joshua Rosen, Managing Member

Mitchell J. Silver, FAICP
Commissioner

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Parks & Recreation

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June 19, 2017

Marjorie Landa
Deputy Comptroller for Audit
City of New York Office of the Comptroller
1 Centre Street, Room 1100
New York, NY 10007

Re: Audit Report on the Compliance of Manhattan River Group, LLC with its License Agreements with the City; FN17-089A

Dear Deputy Comptroller Landa:

This letter addresses the findings and recommendations contained in the New York City Comptroller's ("Comptroller") Draft Audit Report ("Report"), dated June 5, 2017, on the above subject matter.

The City of New York entered into two separate 15-year license agreements with Manhattan River Group, LLC ("MRG"), one for the operation of a restaurant and lounge, and a second for the operation of a marina at the Dyckman Marina, in Manhattan. Prior to the opening of these concessions, this area along the Hudson River waterfront in northern Manhattan was largely undeveloped and subject to dumping and other illegal activities. Since that time, the area – including the restaurant, lounge and marina – has proved a popular amenity for New Yorkers and visitors. We are pleased that this Report found that MRG's payments to Parks under both agreements were timely and that capital improvements on the restaurant were completed.

This Report includes nine recommendations to MRG and seven recommendations to Parks. In reference to the Report's recommendations directed to Parks:

Recommendation 1 – Ensure that MRG remits all additional fees due with applicable late charges.
With regard to the potential fees owed on complimentary meals and beverages, and service charges, there is a difference in interpretation of the license agreement between the Comptroller's Office and MRG. Parks is reviewing this matter with our General Counsel and the City's Law Department. With regard to advance deposits, while we concur that advance deposits and gift card purchases should be reported at the time of its sale, the amounts cited in the Report were purchased in late 2015/early 2016 and were later redeemed and reported in their gross receipts after the March 31, 2016 end of this audit period. We are also following up with MRG to ensure receipt of the amount cited in the Report related to their not including an overpayment they collected in their reported gross receipts.

Recommendation 2 – Ensure that all promotional and complimentary management discounts utilized by MRG for customer relationships are recorded as gross receipts and included in the calculation for fees due to the City.
Due to the difference in interpretation of the license agreement between the Comptroller's Office and MRG, Parks is reviewing this matter with our General Counsel and the City's Law Department.

Recommendation 3 – Ensure that MRG provides documentation to show that capital improvements at the Marina are completed and required by the agreement.
Recommendation 4 – Assign or retain an engineer to observe and evaluate the capital improvements performed at the Marina.
Parks is in receipt of documentation from MRG related to capital improvements they made at the Marina and we are currently in the process of verifying them to ensure that it complies with the requirements of the agreement. After review, if we believe any improvements necessitate further evaluation, we will consider assigning an engineer.

Recommendation 5 – Determine whether it should provide the requisite notice and opportunity to cure and assess the liquidated damages for the unfinished capital improvements at the Marina.
We are currently in the process of verifying the capital documentation that MRG submitted for the Marina. If it is determined that any required items under the agreement remain unfinished, Parks will follow up with MRG accordingly.

Recommendation 6 – Enhance Parks' oversight to enable it to ensure that MRG maintain all required insurance coverage for the Restaurant and Marina operations and all times.
We will follow up regularly with MRG to ensure that all required insurance coverage is maintained.

Recommendation 7 – Ensure MRG implements the recommendations of this report.
Parks has discussed the recommendations in this Report with MRG and, where appropriate, will work with MRG to implement recommended improvements, or otherwise address the concerns raised by the Report.

Finally, Parks wishes to thank you and your audit staff for the time and effort devoted to completing this report.

Sincerely,

David Cerron
Chief of Revenue, Concessions & Controls Oversight