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CITY OF LOS ANGELES
DEPARTMENT OF RECREATION AND PARKS

July 14, 2010

TO: BOARD OF RECREATION AND PARK COMMISSIONERS

FROM: JON KIRK MUKRI
General Manager

SUBJECT: REVIEW OF PROPOSED BUDGET FOR GOLF COURSE OPERATIONS

During the Fiscal Year 2010-2011 budget development and approval process, the Mayor and Council approved the reorganization of the Department of Recreation and Parks' (RAP) Golf Division into a self-sustaining organization (i.e. the Golf Division would receive no General Fund assistance). During the May 17, 2010 RAP Board meeting, the Board directed staff to engage an independent consultant to review the budget (revenue and expenditure plans per Board Report 10-128, as amended) for the Golf Division to determine if the Division could be self-sustaining for the next three years.

Staff engaged the services of the Mayer Hoffman McCann P.C., an independent auditor to review the Golf Division adopted budget. The auditor was assigned a work scope with the following objectives:

- To determine if the Golf Division's proposed revenue and expenditure plan was reasonable;
- To determine if the assumptions used in the development of the proposed revenues and expenses were reasonable; and,
- To determine if golf course operations can be financially self-sustaining for the next three fiscal years beginning July 1, 2010.

The auditor found that the Golf Division can be a financially self-sustaining organization for the next three fiscal years beginning July 1, 2010. However, they did highlight some concerns as detailed below:

- The analysis of green fee revenues collected should be updated through May 31, 2010 (original projections used December 31, 2010) to determine if a decline of 3% in revenue for the current fiscal year is optimistic.

- The increase in revenue estimates for the latter two fiscal years (2011-12 and 2012-13) may be too optimistic and the auditor suggested using a 2% growth factor instead of a 3% growth factor.

- The financial success of the Golf Division is affected by some expenses that are not within the span of control of the Division (primarily those expenses reimbursable under the Cost Allocation Plan-CAP rate).

- The revenue and expense projections should be revisited every quarter in order to carefully monitor the Golf Division's performance.

A full copy of the auditor's report is attached for your review.

This report was prepared by Noel Williams, Chief Management Analyst, Finance Division.

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July 7, 2010

Board of Commissioners
Department of Recreation and Parks
221 N. Figueroa, Suite 1510
Los Angeles, California 90012

RE: REVIEW OF PROPOSED BUDGET FOR GOLF COURSE OPERATIONS

Dear Board of Commissioners:

Mayer Hoffman McCann P.C. (MHM) was engaged by the City of Los Angeles, Department of Recreation and Parks (RAP) to review the proposed budget for the golf course operations for the next three years. This letter documents the results of our review.

Executive Summary

Our review focused on the main objective of determining whether the golf course operations of RAP can be self-sustaining on a go-forward basis beginning July 1, 2010. We were presented with a Staff Report to the Board of Recreation and Park Commissioners, as well as supporting schedules of revenue and expense projections for fiscal years (FYs) 2010-11, 2011-12 and 2012-13. During the course of our review, we requested additional documentation from RAP detailing their calculations and assumptions for the three-year budget.

As detailed in the results section of this report, our review and analysis focused on the reasonableness and accuracy of revenue and expense projections for the three fiscal years beginning July 1, 2010. Based upon the results of our review, we have concluded that the projections appear reasonable, except as detailed below.

1) The analysis of green fee revenues collected should be updated through May 31, 2010. This updated revenue analysis can then be utilized to determine whether the decline in revenues during the third quarter of FY 2009-10 was entirely due to rainy weather.

   The current assumptions utilize revenues received through December 31, 2009 (decline of 3%), rather than more current information. We believe that utilizing a decrease of only 3% for current economic conditions is optimistic, as revenues have continued to decline since December 2009. After analyzing green fee revenues received through May 31, 2010, an adjustment may be appropriate.

2) For the latter two years, FY 2011-12 and FY 2012-13, we believe that the revenue estimates may be optimistic during this time of slow economic recovery. The UCLA Anderson Forecast April 2010 update is projecting that unemployment will continue to be in excess of 10% through 2012 and that any recovery will be very slow. Given this recent forecast, we believe it would be more conservative to project an increase in the second year of 2%, which also corresponds with the projected increase in controllable expenses. A projected increase of 3% for FY 2011-12 and FY 2012-13 is reasonable, but should be reviewed again in the future as new economic information is released.

3) It is important to note that the success of the Golf Special Fund in its ability to be self-sustaining will be affected by the expenses that are not within the span of control of the RAP, such as the reimbursement of General Fund costs. However, as stated below, our review did not extend to the reasonableness of the allocation of costs from the General Fund (i.e., the cost allocation plan (CAP rate), labor cost increases due to contractual obligations, etc.).

4) And finally, we recommend that the revenue and expense projections be revisited on at least a quarterly basis beginning with the first quarter of FY 2010-11. Frequent updates to these projections may be necessary as the first year progresses and the economy begins to recover. This frequent budgetary monitoring will assist in the newly established Golf Special Fund's success.

With the exception of the recommendations above, we believe that the Golf Special Fund can be self-sustaining for the three-year period covered in our review.

Objectives

The primary objectives of our review are as follows:

1) To determine whether the proposed revenues and expenses are reasonable;

2) To determine whether the assumptions used in the development of the proposed revenues and expenses are reasonable; and

3) To determine whether the golf course operations can be self-sustaining on a go-forward basis beginning July 1, 2010.

Scope

The scope of this project included a review of the proposed revenues and expenses, as well as the associated assumptions, for the fiscal years ending June 30, 2011, 2012 and 2013.

Methodology

We performed this review through inquiry of Departmental staff, review and analysis of proposed revenue and expense schedules, and verification of calculations as to accuracy of amounts presented.

Results

Utilizing all reports and schedules provided, including additional backup documentation requested, the following narrative details the results of our review.

We reviewed the Staff Report to the Board of Recreation and Park Commissioners to provide background information on the project. We also verified that all necessary schedules were attached for the Commissioners to make an informed decision regarding the proposed recommendations. All references to supporting documentation were verified for accuracy.

Attachment 2 of the staff report was reviewed for accuracy and supported the amounts referenced in the Staff Report. This Attachment consists of the projected balances of golf operations currently existing within the RAP's Special Fund. This Attachment also contains the proposed transfers to the newly established Golf Special Fund at July 1, 2010.

Attachment 3 of the Staff Report contains a detailed schedule of the proposed increases to golf fees beginning July 1, 2010. We did not independently survey neighboring golf courses, privately or publicly operated, but did review the survey results conducted by RAP's staff. All proposed increases appear reasonable when compared to the survey results. We also used Attachment 3 to ensure that the appropriate rates were used when calculating green fee projected revenues for the three-year period.

Attachment 4 of the Staff Report is a summary of all proposed green fee increases and the resulting increase in revenue at each of the City's golf courses. We used this Attachment to verify the calculations of total revenues expected to be received from green fees.

The majority of the work performed focused on Attachment 1. This Attachment is a three-year projection of revenues and expenses for golf course operations beginning in fiscal year (FY) 2010-11 and ending in FY 2012-13. In reviewing this schedule, additional backup documentation was requested from RAP staff. It proved important that the assumptions and calculations utilized for the numbers summarized on this report be analyzed. The verification of calculations was aided by telephone conversations and via e-mail with RAP staff with regard to golf course revenues.

Revenues

The following details the focused verification of revenue calculations and assumptions concerning each of the revenue worksheets. Assumptions and calculations that follow provide the basis for the three-year budgetary projections.

- *Green Fees* – Green fees represent 82.8% of golf course operational revenues for FY 2010-11. We reviewed actual revenues from FY 2007-08, FY 2008-09, actual revenues for FY 2009-10 through December 31, 2009; and actual revenues for FY 2009-10 through April 30, 2010.

  Green fee revenues increased 7.3% for FY 2008-09 as compared to the prior year (due to an increase in fees). However, during the first half of FY 2009-10, green fee revenues decreased 3% as compared to the six-month period ended December 31, 2008. Because rounds of golf played remained approximately the same, this decrease in revenue indicates that more golfers played during the discount times.

  At April 30, 2010, revenues had continued to decline, with a total decline in revenues for all golf courses of 4.4%. For ease of analysis, if total revenues are straight lined for the remainder of the fiscal year, the total decline in green fee revenues for FY 2009-10 will be 4.6%.

  We reviewed the methodology utilized for calculating green fee revenues for FY 2010-11, which included a reduction based upon revenues at December 31, 2009, and a corresponding increase based upon the proposed adjustments to green fees. We concur with the methodology utilized for the green fee calculation, including the anticipated 3% reduction to rounds of golf played as a result of the proposed fee increase.

  We inquired as to utilizing December 31, 2009 revenue declines rather than the additional declines experienced through April 30, 2010. RAP staff indicated that the first four months of 2010 had been exceptionally rainy. It was her opinion that the wet weather was the leading indicator for the continued decline in revenues during FY 2009-10. It is impossible to ascertain from the information provided how much of the additional 1.4% decrease in total revenues was due to weather and how much was due to the overall economic conditions affecting discretionary spending. Other than this uncertainty, the assumptions used in developing the estimated green fee revenue appear reasonable. We recommend that RAP update the green fee revenue analysis through May 31, 2010 to determine whether revenue projections should be adjusted further.

- *Other Golf Course Revenue* – Other golf course revenues represent 1.4% of total revenues for FY 2010-11. These revenues were included in the information reviewed for FY 2007-08 and FY 2008-09. This revenue category decreased 11.7% from June 30, 2008 to June 30, 2009 mainly due to increased fees on July 1, 2008. No updated revenues for FY 2009-10 were provided, but our review confirmed that FY 2008-09 totals were used as a starting point for FY 2010-11. This assumption appears reasonable.

- *Reservation Office Revenue* – This revenue category represents 1.6% of total revenues for FY 2010-11. Actual revenues collected in FY 2008-09 is the starting point for FY 2010-11 estimated revenues. FY 2008-09 revenues were adjusted, allowing for a 32.7% decrease for FY 2010-11. This estimated drop in revenue is due to the fact that reservation card memberships are purchased on a three-year cycle. This assumption appears reasonable.

- *Interest Income* – Interest income represents 2.2% of total revenues for FY 2010-11. The $575,000 projected for FY 2010-11 is an increase of 1.3% over FY 2008-09 actual revenue received. This revenue estimate appears reasonable in the current economic environment.

- *Concession, Tregnan Junior Golf Academy and Armand Hammer Trust Revenues* – Revenues received from all concessions, the Tregnan Junior Golf Academy and the Armand Hammer Trust represent 12.0% of revenues for FY 2010-11. With the exception of the golf cart concession, all revenues included in this category for FY 2010-11 are estimated at the level of FY 2008-09 actual revenues. All concessionaires, except the golf cart concessionaire, collect the revenues and pay a rental fee to the City of Los Angeles. For ease of operations, a change was made to revenue collections for the golf cart concession in March 2010. For the month of March 2010 and thereafter, all revenues are collected by the City of Los Angeles and a percentage is forwarded to the concessionaire. Since this change was implemented, golf cart revenues increased by approximately 15%. This increase in revenues was utilized as justification for increasing golf cart revenues by 6.9% for FY 2010-11 from the actual revenues received for FY 2008-09. This assumption appears reasonable.

After verifying the beginning revenue projections for FY 2010-11, we calculated the increases to revenue projections for FY 2011-12 and FY 2012-13. With the exception of interest income, an increase of 3% was utilized for each of the two additional years in the projection. A 3.5% increase for each of the fiscal years was projected for interest income. As documented above, certain historical information was utilized for FY 2010-11. The rationale utilized for the increases projected for FY 2011-12 and FY 2012-13 includes 1) an assumption that the economy will begin to improve; 2) increased marketing of RAP's golf courses; and 3) if necessary, additional increases to green fees. These projections may still be optimistic considering that economists are projecting that California unemployment will continue in the double digits through 2012 and normal growth rates are not expected in the State until mid-2011. In addition, the beginning revenue estimates for FY 2010-11 appear somewhat optimistic considering that revenues have continued to decline through April 2010.

Expenses

The following details our analysis of the budgeted expenses for the upcoming three years.

- *Salaries, General and Salaries, As Needed* – Salary expenses represent 40.3% of all golf course expenses for FY 2010-11. All salary calculations for full-time and part-time employees by golf course and administrative functions were sampled for accuracy on the spreadsheet provided. The starting point for FY 2010-11 salary expenses is actual salary schedules for FY 2009-10 with an anticipated cost of living adjustment (COLA) of 4.1%. The anticipated COLA increase was provided by the City Administrative Officer. Salary calculations are accurate and in line with the information provided by the City of Los Angeles. Golf course administration has no control over the anticipated increases to salaries, as all employees are represented by collective bargaining units.

- *Maintenance, Materials and Supplies/Contractual Services/Concession Improvements* – Other expenses, i.e. maintenance, materials and supplies; contractual services; and concession improvements represent 9.1% of total expenses for FY 2010-11. Verification of other golf course expenses was conducted through telephone conversations with RAP staff. The projections for FY 2010-11 were based upon projections provided by the Golf Manager, which were calculated utilizing current expenses for FY 2009-10. These projected expenses appear reasonable.

- *Utilities* – This expense line item represents 5.8% of total expenses for FY 2010-11. The estimated expense for this line item is provided from the Administrative Office of the Recreation and Parks Department. It is based on a percentage of all departmental utility costs. This allocation method is used because many of the utilities are not separately metered for golf course operations. The projected expense for FY 2010-11 appears reasonable.

- *Reimbursement of General Fund Costs* – Reimbursement of General Fund costs represents 44.8% of all golf course expenses for FY 2010-11. This line item includes calculations for fringe benefits, central services, and departmental administration and support. The total percentage is referred to as the Cost Allocation Plan (CAP) rate and is calculated based upon total salary expenses for both full-time and part-time employees. The full-time employees' rate for FY 2010-11 is 85.99% and the part-time employees' rate for FY 2010-11 is 64.92%. All calculations were verified as a percentage of both full-time and part-time employee salaries. The $11.5 million in reimbursement of General Fund costs was budgeted based upon historical costs; however, only actual related costs will be reimbursed from golf course operations. For FY 2010-11, it is expected that the expenses will be $2.6 million less than the budgeted amount. This $2.6 million could be used to offset any unforeseen future contingencies, such as potential revenue shortfalls (identified in previous paragraphs). In addition, the Golf Division is budgeted to contribute $500,000 to the General Fund for RAP operations. Our review did not extend to the reasonableness of the allocation of costs from the General Fund.

After verifying the beginning expense projections for FY 2010-11, we calculated the increases to expense projections for FY 2011-12 and FY 2012-13. For full-time and part-time salaries, anticipated COLA's were provided by the City Administrative Officer in the amount of 4.1% and 3.0% respectively, for each of the two additional years in the projection. Except for a few golf course administrative employees, all employees are covered by Memorandums of Understanding (MOU's) between Coalition Unions and the City of Los Angeles. Although these COLA's appear somewhat high given the current economic conditions, these expenses are not controllable at the RAP level. For each of the "other expenses" listed above, an increase of 2% was added for each of the two additional years. This appears to be in line with a conservative estimate for a slow economic recovery.

Utilities and reimbursement of General Fund costs remain static for FY 2011-12 and FY 2012-13. Although the General Fund costs appear high, these expenses are not under the direct control of the golf course staff.

With the exception of the recommendations above, we believe that the Golf Special Fund can be self-sustaining for the three year period covered in our review.

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We are available to discuss the results of our analysis at RAP's convenience. Should you have any questions or need additional information, please email me at mddavis@cbiz.com, or call me at (949) 474-2020, extension 244.

Sincerely,

MAYER HOFFMAN McCANN P.C.

Marcus D. Davis, CPA
Shareholder