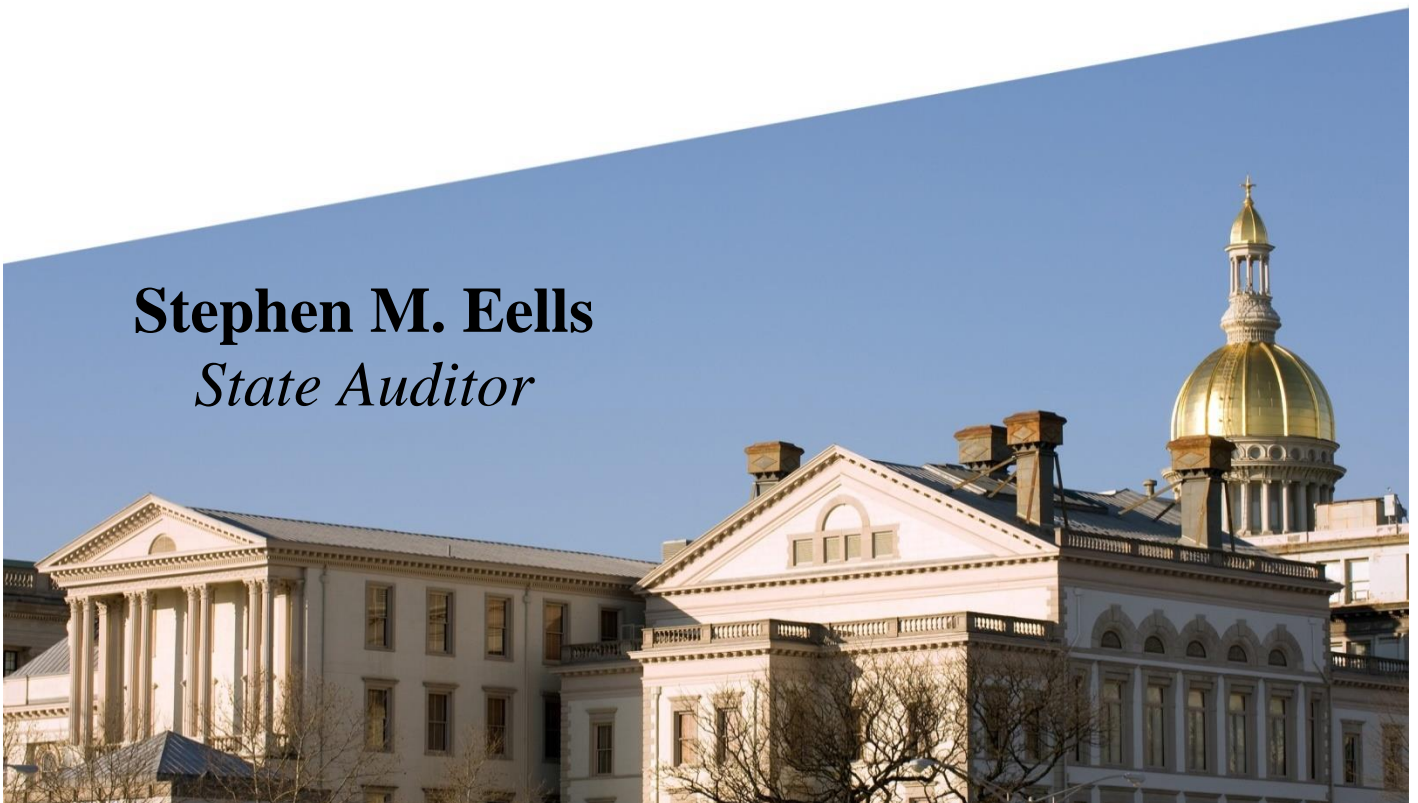


New Jersey Legislature
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OFFICE OF THE STATE AUDITOR

Casino Reinvestment Development Authority

January 1, 2014 to December 31, 2017

Stephen M. Eells
State Auditor



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Enclosed is our report on the audit of the Casino Reinvestment Development Authority for the period of January 1, 2014 to December 31, 2017. If you would like a personal briefing, please call me at (609) 847-3470.

A handwritten signature in dark ink, appearing to read "Stephen M. Eells".

Stephen M. Eells
State Auditor
September 11, 2018

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Scope

We have completed an audit of the Casino Reinvestment Development Authority (CRDA or authority), for the period January 1, 2014 to December 31, 2017. Our audit included financial activities accounted for in the CRDA's accounting systems. The CRDA is a component unit of the state. It is organizationally considered in, but not of, the Department of the Treasury.

Between 2014 and 2016, total annual expenditures for governmental and business-type activities ranged from \$94 million to \$151.8 million. During the same time period, total annual revenues for these activities ranged from \$104 million to \$135.5 million. Governmental activities include authority operations and programs, including the administration of community and economic development projects. Business-type activities include the financing and operation of a garage and the operations of the Convention Center Division and the Special Improvement District Division. Major components of revenue were luxury tax, grant revenue, parking fees, marketing fees, hotel room fees, and entertainment retail district grants. The authority is also the fiduciary for Investment Alternative Tax obligations paid by casino licensees. The year-end available fund balances totaled \$125.8 million, \$78.8 million and \$46.7 million in years 2014, 2015, and 2016, respectively.

The authority limited access to original documentation for our transaction and contract testing by requiring that documents requested initially pass through administration prior to our access. Many of our requests were then fulfilled with photocopied documents. In addition, the authority limited our ability to audit legal expenses by redacting invoices.

Objectives

The objectives of our audit were to determine whether financial transactions were related to the authority's programs, were reasonable, and were recorded properly in the accounting systems. Additional objectives were to determine if there was a coordinated effort by management to effectively merge the Atlantic City Convention and Visitors Authority (ACCVA) and the Atlantic City Special Improvement District (ACSID) with the CRDA and to determine whether the CRDA ensured the efficient and effective use of authority funds.

This audit was conducted pursuant to the State Auditor's responsibilities as set forth in Article VII, Section I, Paragraph 6 of the State Constitution and Title 52 of the New Jersey Statutes.

Methodology

Our audit was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. 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.

In preparation for our testing, we studied legislation, the administrative code, executive orders, and policies and procedures of the CRDA. Provisions we considered significant were documented and compliance with those requirements was verified by interview, observation, and through our review of the CRDA's records. We also read CRDA board agendas and minutes, reviewed financial trends, and interviewed personnel to obtain an understanding of the various functions, the internal control structure, and monitoring procedures. In addition, we reviewed annual audit reports issued by public accountants.

A nonstatistical sampling approach was used. Our samples were designed to provide conclusions on our audit objectives as well as internal controls and compliance. Sample populations were sorted and transactions were judgmentally selected for testing.

Conclusions

We found that the financial transactions included in our testing were related to the authority's programs. However, we did note certain transactions were not always reasonable or properly recorded in the accounting systems. We also found the CRDA did not always ensure an effective and efficient use of its funds. The authority lacked a process to monitor compliance with contract terms resulting in overpayments, lost revenue, and potentially lost deliverables, as well as not being able to use measurable results in future contract negotiations. We also found that the authority materially modified certain contracts with terms not consistent with authorizing board resolutions which resulted in unauthorized payments. In addition, we found improper uses of emergency procurement resulting in contracts being awarded to the highest bidder, improper approval of a direct investment project, improper calculation of sponsorship fees, and payment for board members' waived compensation; all resulting in potential overpayments.

We found the CRDA did not effectively streamline operations upon the completed merger with the ACCVA and ACSID in 2013. The authority did not formally evaluate the resulting functions in conjunction with the former responsibilities of the increased workforce, nor did it communicate new employee responsibilities through job descriptions or assess employee performance through periodic evaluations. Additionally, the authority continued to maintain separate accounting systems and processes for the acquired divisions without apparent consideration to unify the processes until 2016, nor did it have controls in place to effectively transition the finance operations when the former Chief Financial Officer retired in 2015.

Furthermore, the authority has not properly evaluated employee space needs in conjunction with the potential use of authority-owned buildings in addition to other cost savings opportunities. We also noted internal control weaknesses in the recording of revenue, procurement, and accrual processes.

Background

The CRDA was established in 1984 under Title 5, Chapter 12 of the New Jersey Statutes Annotated, to provide capital investment funds for economic development and community development projects in Atlantic City and the State of New Jersey primarily through Investment Alternative Tax (IAT) funds paid to the state from casino licensees. The CRDA is governed by a board of directors whose members include the Attorney General, the State Treasurer, the Mayor of Atlantic City, all ex officio; plus ten public members and two casino representatives, all appointed by the Governor. In addition, one member is appointed by the Governor to serve ex officio, who shall be either the Commissioner of the Department of Community Affairs or an additional member of the Casino Control Commission. Board minutes of every meeting of the CRDA are delivered to the Governor who has a 10-day period, excluding weekends and holidays, to veto any actions taken by the authority or any member thereof at such meeting.

In February 2011, Senate, No. 11 (S11) was enacted expanding the scope of the CRDA's responsibilities with the creation of the Atlantic City Tourism District which encompasses all casino hotels, the boardwalk, all major commercial districts, CRDA-owned properties, and Bader Field (a former general aviation airport). The district's purpose is to facilitate a clean, safe, and marketable city in order to attract tourists and investors. This law designated that all available assets and revenues of the authority shall be devoted to the purposes of the tourism district and community development in Atlantic City. The law also transferred all functions, powers, and duties of the ACCVA to the CRDA and directed, as appropriate, for the authority to assume all functions, powers, and duties of Atlantic City, and of any agency or instrumentality, thereof, with respect to the ACSID. As a result, the authority increased its workforce from 29 to approximately 135 employees by the end of 2013. New responsibilities included, maintaining Historic Boardwalk Hall and the Atlantic City Convention Center; attracting visitors to Atlantic City by promoting the convention, resort, and tourist industries of Atlantic City; facilitating maintenance and safe initiatives within the tourism district; and overseeing land use planning. In 2014, the CRDA approved the restructuring and outsourcing of the sales function of its Convention Center Division through the creation of a separate not-for-profit entity (Meet AC) and entered into a public-private partnership agreement to primarily fund that entity.

In May 2016, the Casino Property Taxation Stabilization Act was signed into law which redirected the moneys received by the State Treasurer from the payment of the IAT to the City of Atlantic City for the purposes of paying debt service on bonds. Without these funds, the CRDA's role in development will be limited until the end of 2026, when the funds may be redirected back to the CRDA.

During our audit period, the authority had two Executives Directors. The new Executive Director started on January 1, 2017.

Boardwalk Hall Roof Projects

The continuous and inconsistent application of emergency procurement resulted in additional costs.

Boardwalk Hall is a multi-purpose facility located on the Atlantic City Boardwalk. It was constructed in 1929 as the country's original convention center, underwent a major restoration in 2001, and was transferred to the CRDA in 2013 through S11. Boardwalk Hall is comprised of East Hall and West Hall. East Hall houses the main event hall, ballroom hall, and various ancillary spaces. West Hall is a two-story warehouse primarily used for parking of support vehicles for events at East Hall. The CRDA contracts with a facilities manager to serve as the authority's agent to manage and operate Boardwalk Hall. In October 2014, a five-year maintenance plan was prepared, identifying the need for repairs and replacement of the East Hall and West Hall roofs. Our review noted that the lapse in time between identifying the need for roof repair and replacement, and the questionable application of multiple emergency procurements, resulted in all roof work being awarded to one vendor at an additional cost to the authority of up to \$2.1 million.

Timeline

November 2014 – RFP for East and West Hall Roofs

A Request for Proposal (RFP) was released in November 2014 for the repair and replacement of the East and West Hall roofs. A contract was awarded but was cancelled. At that time, the authority evaluated the use of and costs associated with repurposing and/or demolishing West Hall and determined that the associated costs would be prohibitive compared to the budgeted costs to repair and/or replace the roofing system.

March 2015 – As-Needed Roofing Contract

In March 2015, the authority issued an RFP and subsequently awarded a two-year contract, not to exceed \$500,000, for an as-needed roofing contractor to the sole respondent of the RFP and immediately identified three projects, totaling \$455,000 to be completed under this contract. This vendor would eventually receive all additional Boardwalk Hall roof-related work over the next three years.

June 2015 – West Hall Emergency

In June 2015, a water leak was identified at West Hall. The authority determined that emergency work was required and sought a competitive process by releasing roof designs to replace a portion of the West Hall roof to four contractors who had participated in the original 2014 public bid. Two of the contractors responded at the July bid opening. A \$1.4 million contract was awarded in August to the vendor who was recently awarded the as-needed roofing contract and was the lower of the two bids.

June to September 2016 – RFP for the East Hall Roof and Remainder of the West Hall Roof; Rejection of Bids; Increase As-Needed Contract

It was not until June 2016, when the CRDA released an RFP to repair and replace the East Hall roof areas and the remainder of the West Hall roof. There were six respondents, four of whom submitted a bid for both projects. The highest and lowest combined bids were approximately \$5.4 million and \$3.46 million, respectively. The architect evaluated all submitted bids and concluded that the lowest bid proposal contained all prerequisites required by the RFP and the respondent was prepared to contract. The CRDA's management and the facilities manager recommended the board award a contract for both projects to the lowest combined bid. A draft resolution was prepared for the September 2016 board meeting to reflect these recommendations; however, the board chose to reject all bids on the basis of examining the scope of work for the proposed construction and, once again, to further examine potential options related to the repair and/or replacement of the roofing system. At that same board meeting, the board immediately presented and approved a resolution to increase the as-needed roofing contract by \$2 million (from \$500,000 to \$2.5 million), to effectuate certain limited emergency repairs to a portion of the East Hall roofing system, even though the vendor holding the as-needed contract had just submitted the highest bid for the East Hall and West Hall roof projects.

November 2016 – East Hall Roof Emergency

Less than two months after the board's rejection of the competitive bids, the authority requested a proposal for an emergency roof replacement at East Hall. The as-needed contract vendor submitted a proposal for \$1.4 million to replace specific East Hall roof areas "as per original bid documents" that mirrored its previous bid, which was the highest bid. The CRDA issued a purchase order for the work under the as-needed roofing contract with no consideration of a competitive process, even though the specifications used were those from the very recent June 2016 bid solicitation and could have been re-released, as in past practice. The vendor was paid based on percentage of completion, and the project was for roof replacement, not repair, which was not in accordance with the as-needed roofing contract.

January 2017 – West Hall Roof Emergency

Over a year and a half after the first West Hall roof emergency, and two months after the East Hall roof emergency, another emergency was identified at West Hall. On January 24, 2017 there was a power outage caused by the electrical switchgear being "flushed over due to water intrusion from a leaking roof." The power was restored to the hall, the affected area was fenced off, and the room was locked making it inaccessible to unauthorized personnel. A proposal was requested from only the as-needed contractor to complete the roof repair and replacement of the remaining roof areas of West Hall as identified in the June 2016 RFP.

On March 1, 2017, the as-needed contractor submitted a proposal with a base cost of \$2,350,000. In this emergency, the CRDA management recommended the Executive Director waive the authority's public bidding process based on exigencies requiring the immediate

delivery of the services and award a contract to this vendor. Management drafted a memo citing public exigencies existed which required immediate delivery of services under N.J.S.A. 52:34-10(b) (statute) as justification to waive the public bidding process. This statute, however, is not specific to state authorities. The authority's procurement protocol was developed in accordance with a 2006 executive order (EO 37), which specifically addresses the procurement process for state authorities, includes limited circumstances in which exception to public advertising and a competitive process shall apply, and additionally requires specific documentation and procedures when an exception is invoked. The CRDA opted to rely on the statutory provision which appears to have circumvented the additional requirements of the executive order process.

- Similar to the statute, EO 37 removes the requirement of a competitive process in the case of unforeseen life or safety emergencies where the public exigency requires that the services be purchased immediately, however, EO 37 requires this to be demonstrated by the memorialized concurrence of three authority officials. We were not provided with this required memorialized concurrence of three authority officials. Based on the lapse in time between the emergency and authorization to commence work and documentation presented, we question whether a public exigency existed. We calculated that 77 calendar days lapsed from the incident date to April 11, 2017, when the Executive Director authorized the commencement of work, which is not an immediate response. Since roof designs were already prepared from the 2016 RFP it appears there was ample time for a competitive bidding process. The electrical contractor, who restored power, did not state a public exigency existed, but that repair and/or replacement of the roof must be completed prior to any additional electrical work performed and recommended that the roof be addressed as soon as possible to eliminate further additional problems and unsafe conditions. Additionally, our walkthrough of the West Hall area identified that the affected switchgear room was out of public view and only accessible by authorized personnel.
- When an exception to competitive purchasing is invoked under EO 37, a proposed resolution concerning the contract shall set forth the justification for invoking the exception, and the authority's Executive Director shall certify the circumstances that warrant application of the exception. The CRDA did not prepare a resolution or formally receive board approval, nor did the Executive Director certify that circumstances warranted application of the exception. The Executive Director simply sent an email to authorize emergency work in an amount not to exceed \$3,052,500, including a 25% contingency.
- Per EO 37, the emergency contract must be limited to purchasing those services or products necessary to mitigate the emergency situation. The as-needed contractor was authorized to complete the replacement of all West Hall roof areas, as identified in the June 2016 RFP, which appears more than necessary to mitigate an emergency.
- The lowest base bid submitted and rejected in 2016 for these West Hall roof areas was \$1,381,500. The authority ultimately paid the \$2,350,000 base bid plus a contingency for this project; \$968,500 more than the lowest base bid.

August 2017 – RFP for remaining East Hall Roof Areas

By the summer of 2017, repair and replacement of all of West Hall and a portion of East Hall roof areas had been procured through some form of an emergency process. In August 2017, the CRDA issued an RFP to repair and replace the remaining roof areas of the East Hall, as outlined in the June 2016 RFP, along with the addition of gutter work. The only bid submitted was from the as-needed contract vendor that was granted all work on the Boardwalk Hall roofs, mostly through non-competitive processes. The CRDA management could have authorized a re-bid prior to opening the one bid, to ensure a competitive process, but chose not to do so and instead awarded a base contract for \$1.8 million plus a contingency. The architect's recommendation stated that the bid was within the expected range for said work, however the authority could not provide support of any such range dated prior to the bid opening. This base contract, in addition to the November 2016 East Hall roof emergency base contract, totaled approximately \$3.2 million and exceeded the lowest bid that was submitted and rejected in the 2016 East Hall RFP by approximately \$1.1 million.

At the conclusion of all Boardwalk Hall roof repair and replacement projects, the vendor with the highest base bid of \$5.4 million in the 2016 competitive process received base contracts totaling \$5.53 million plus contingencies. Upon completion of all work, we estimate the authority will expend approximately \$2.1 million more than if the board had awarded the projects to the contractor with the lowest base bid of \$3.46 million in 2016.

Recommendation

We recommend the authority ensure compliance with its own procurement guidelines and EO 37. The authority should follow its maintenance plan to minimize emergency situations. When applying emergency procurement procedures, the authority should limit the purchase to those services or products necessary to mitigate the emergency and ensure proper application and approval of the exception to competitive procurement. The authority should consider a rebid when there is only one response to an RFP. Finally, the deficiencies identified in the procurement of the Boardwalk Hall roof projects should be examined and the appropriate controls implemented to ensure a proper procurement process and commitment to efficient fiscal management and transparency.

**Beach and Boardwalk Hall Events**

Amendments and non-compliance with the beach and Boardwalk Hall events contract resulted in \$1.75 million in unauthorized payments and overpayments.

The authority contracted with a national events promoter (promoter) to book, present, and produce beach concerts and Boardwalk Hall events. We found that certain contract terms were amended by authority management in a manner not consistent with the board's authorizing

resolution and another contract term was not followed resulting in a total of \$1.75 million in unauthorized payments and overpayments.

In March 2016, the board authorized a resolution to reserve funds not to exceed \$9 million for the promoter for beach concert events (\$6 million) and Boardwalk Hall events (\$3 million). The resolution authorized the Executive Director to negotiate and execute agreements upon the following provisions and such other terms and conditions the Executive Director deemed appropriate and consistent with the resolution.

- The promoter will book and perform a minimum of six beach events annually between May and September of 2016 through 2018. The authority will allocate up to \$2.0 million per year, with a maximum per event subsidy of \$333,333.
- The promoter will book and perform a minimum number of events held at Boardwalk Hall as determined by, and subject to, the authority's approval. The authority will allocate up to \$1 million per year, of which \$500,000 will serve as an annual event subsidy and \$500,000 will serve as an event loss mitigation fund.

The Boardwalk Hall agreement replaced a 2014 agreement having similar terms.

Beach Concert Events

In April 2016, the CRDA entered into a three-year contract for the promoter to annually produce at least six beach concerts with total payments not to exceed \$2.0 million per year. The parties acknowledged and agreed that due to the unique nature of the beach concerts, the promoter did not guarantee that it would be able to book six beach concerts in each contract year. The authority agreed to pay the promoter \$333,333 for each beach concert other than those occurring on a Saturday and/or holiday weekend. In the first contract year, the promoter was eligible to receive payment of \$166,666 per beach concert for a maximum of two Saturday beach concerts. After the first contract year, the promoter was not eligible for any payment for beach concerts scheduled on a Saturday and/or holiday weekend.

In the summer of 2016, five concerts were booked, however, only three were performed due to cancellations resulting from inclement weather. We found that one of these concerts was performed on a Saturday and the authority paid \$333,333; a payment of \$166,667 more than the contracted amount. It was not until more than four months after the concert date that authority management amended the original agreement and authorized a payment of \$333,333 to the promoter for this Saturday beach concert. While the original contract sets the payment amounts "unless otherwise specifically agreed by the parties," it is questionable practice to amend a contract four months after the delivery date, especially since the authority was unable to support that the \$333,333 amended compensation was agreed upon prior to this Saturday beach concert.

In July 2017, the Executive Director amended the beach concert agreement and materially modified the financial terms specified in the board's authorizing resolution by providing a

maximum financial assistance package of \$2.5 million for the 2017 contract year in return for a minimum of three beach concerts and mutually agreeable assistance and logistical support to the authority for other authority-approved entertainment events. During the 2017 contract year, the promoter only produced three weekday beach concerts, provided no additional assistance and logistical support since there were no additional events, and was paid the full \$2.5 million, a payment of \$1.5 million in excess of the board's authorization for three beach concert events, and also exceeding the board's authorization of a \$2 million annual subsidy.

Boardwalk Hall Events

The September 2014 Boardwalk Hall agreement was subsequently replaced by the March 2016 Boardwalk Hall agreement. Under both agreements, the authority agreed to pay the promoter a sponsorship fee based on the number of events as follows: no fee for up to five events, \$270,000 for six or seven events, \$350,000 for eight or nine events, \$460,000 for ten or eleven events, and \$500,000 for twelve or more events. We found that during the 2015-2016 contract year, the promoter produced seven events, however, the authority calculated the sponsorship fee based on eight events, one of which was not identified as the promoter's event. The authority was unable to provide any support substantiating the inclusion of this event in the calculation. As a result, the authority overpaid the promoter \$80,000 in sponsorship fees.

Recommendation

The authority should implement controls to ensure that contracts are executed in accordance with the financial provisions authorized by board resolution. Contract terms and subsequent amended terms that are not consistent with the authorizing resolution should be presented to the board for approval and transparency. The board should evaluate the propriety of payments to the promoter and ensure management recovers any overpayments. Additionally, management should ensure accuracy of any sponsorship fee payments and seek recovery of the \$80,000 overpayment.



Miss America Organization Contract

The CRDA did not monitor actual costs, contract deliverables, and economic impact when negotiating a second contract with the Miss America Organization.

Pageant Contract Expenditures

In May 2013, after a nine-year absence, the CRDA entered into a three-year contract with the Miss America Organization (MAO) to return the iconic pageant to Boardwalk Hall. This initial contract covered the 2014, 2015, and 2016 competitions. The CRDA agreed to pay 50 percent of the pageant's production costs and 50 percent of the annual building operations costs associated with the pageant, up to a total maximum annual payment of \$2,267,000. The MAO

was responsible for the remaining 50 percent and any amount in excess of \$4,534,000. The CRDA was also responsible for other costs such as meals and transportation for the contestants and chaperones, a welcoming ceremony, and security at Boardwalk Hall. At the conclusion of this contract, the CRDA had paid \$6,801,000 (the maximum for all three years).

The CRDA was unable to provide documentation to support any efforts on their part to monitor the actual costs related to the Miss America Competition. In addition, under the 2013 contract terms, the MAO was to provide written reports every 90 days supporting the production costs incurred. The CRDA was unable to provide us any of these required cost reports. It was only able to provide us a copy of the 2015 year-end settlement statement; however, it provided no evidence that the expenses were verified for accuracy. This statement reflected a \$61,650 credit balance which was never received by the authority.

In February 2016, the CRDA entered into a second contract with the MAO that guarantees payments of \$12,536,000 over a three-year period representing an 80 percent increase from the prior contract cost. The CRDA agreed to pay \$3,500,000, \$3,750,000 and \$4,000,000 for the 2017, 2018 and 2019 pageants, respectively. The second contract eliminated the requirement for the MAO to provide written reports supporting the production costs. Additionally, this contract provides annual payments of \$325,000 to the MAO towards the cost of other competition expenses, such as contestant and chaperone meals, hotel related fees, transportation and security for the contestants, and a VIP after-party. By comparison, the CRDA paid a total of \$176,000 over three years for similarly related costs under the prior contract. Furthermore, the authority agreed to pay \$311,000 for prior year costs, but was unable to provide any documentation or rationale for these expenses.

Economic Benefits

The MAO had a partner relationship with an entertainment production company (company). The 2016 contract included a provision to help promote the City of Atlantic City through the company's other productions. The company was required to air a live remote performance occurring in Atlantic City to be incorporated in the 2017, 2018, and 2019 New Year's Eve telecasts. The CRDA was required to cover all costs related to the performance but did not sign a performer for the 2017 event and was unable to provide us documentation of a search effort. We requested any cost-benefit analysis prepared prior to adding this term to the contract and were provided none. In late 2017, the company severed its ties with the MAO, effectively removing this contract provision. We subsequently noted that the authority did not adjust its funding to the MAO as a result of this change.

The authority's initial and second contract with the MAO included non-financial obligations by the MAO to promote Atlantic City. We requested documentation demonstrating that the CRDA verified compliance with these terms but were provided none.

After the initial contract was signed, an economic impact study was performed prior to the 2014 competition. The study estimated \$60.4 million in economic benefits from the pageant to the Atlantic City area through a combination of local jobs created for the pageant, consumer

spending, and state and local tax revenues. There was no estimate of the value of Atlantic City's exposure on television.

No follow-up study was performed to measure if expected benefits were achieved. The only other economic impact study performed was after the 2017 competition, which was after the CRDA negotiated the second contract and significantly increased the payments to the MAO. The second economic impact study identified only \$23.2 million in economic benefits to the Atlantic City area including the value of Atlantic City's exposure on television and was significantly less than the benefit estimated in 2013.

Without documentation to support the actual competition related costs, assurance that all promotional deliverables were received, planning for and utilizing the New Year's Eve broadcast and ultimately losing the provisions related to the entertainment production company, or using any measure of economic impact in contract negotiations and overall monitoring, it appears that the CRDA did not effectively manage these contracts nor have the ability to determine if the funds were spent in an efficient manner.

Recommendation

We recommend the authority develop and institute monitoring controls to determine if all parties perform in accordance with contract terms and deliverables. Performance should be measured, when applicable, and reviewed to determine whether funds were spent in an efficient and effective manner and used as a basis for future contracts.



Agreement Modifications

CRDA management materially modified an agreement, resulting in significant additional payments.

In 2000, the CRDA partnered with a company to develop, lease, and manage The Walk, which is the shopping district located at the foot of the Atlantic City Expressway. The land is owned by the CRDA. Development of The Walk was planned in phases and multiple stages and included a plan to eventually develop the facility of an agreed-upon large retailer which ultimately opened in 2015. We found that authority management so materially modified an agreement related to the final project phase which included the large retailer, that the agreement is no longer consistent with the board resolution. Project financing originally approved as a \$12 million loan, and annual grants totaling \$10 million have been modified to a degree that will now require the authority to pay the developer up to \$18.7 million in excess of the board authorized terms over the course of the modified agreement.

In August 2012, the board authorized, through resolution, financial assistance in the form of a \$12 million loan, funded through the issuance of casino licensee bonds, to the developer for the

construction of this large retail store. The board subsequently adopted a bond resolution authorizing the issuance of bonds in an aggregate principal amount not to exceed \$12 million to fund the loan. In addition to the loan, the board authorized the developer to receive an additional \$1 million per annum of the authority's annual grant under the Casino Reinvestment Development Authority Urban Revitalization Act until 2024. The developer was previously authorized to receive up to \$1.25 million per annum of this grant related to the development of prior stages of The Walk. This addition increased the board authorized grant total to up to \$2.25 million per annum.

The Executive Director was authorized to negotiate and execute necessary and desirable agreements with the developer, including loan agreements and related documents, amendments to the Phase Two Master Development Agreement, if any, and the stage development agreement, all consistent with the resolution, and subject to the CRDA Act, rules and policy. The Executive Director entered into a stage development agreement with the developer for the project in May 2013. The developer separately executed its lease with the retailer which included payment of a base rent amount plus a percentage of retail sales. We found that the Executive Director subsequently amended the agreement with the developer with material changes that no longer appeared consistent with the board's authorizing resolutions resulting in the following outcomes and analyses.

- A debt service and sharing of percentage rent clause was added to the developer's agreement where, for any calendar year in which the gross sales under the lease between the retailer and the developer did not exceed \$29,999,999.99, the CRDA shall reimburse the developer 100 percent of the regularly scheduled principal and interest payments on the CRDA loan. The CRDA was unable to provide any documentation to substantiate sales projections of \$30 million.
- The retailer actually made less than 57 percent of the gross sales benchmark, and the CRDA reimbursed the developer the full principal and interest payments received on its loan, totaling \$300,916 and \$857,761 for 2015 (partial year) and 2016, respectively.
- We calculated the developer received payment of approximately \$1.5 million in rent from the retailer and reimbursement of principal and interest from the authority for 2016. If sales had equaled \$30 million, the developer would have only received an estimated \$927,000 in rent and no CRDA reimbursement.
- The modified agreement contained an additional clause that specified when the retailer's gross sales meet or exceed \$40 million, 50 percent of the percentage rent paid to the developer shall be remitted to the authority. We calculated that for the developer to receive the same \$1.5 million with no reimbursement of principal and interest from the CRDA, the retailer would have to generate gross sales of approximately \$80 million, which appears unlikely based on recent sales data.

- The Executive Director increased the entertainment retail district grants from \$2,250,000 to \$2,500,000 per year, resulting in additional payments of \$750,000 for 2015 through 2017 and potentially \$1,750,000 in additional payments over the remaining term of the agreement. These payments were not included in any board resolution.
- Additionally, the authority sold bonds to the casinos and issued a loan to the developer for \$330,000 in excess of the amount authorized by board resolution for the project and the bond resolution. This amount accounted for CRDA's 2.75 percent project processing fee and is also now subject to reimbursement to the developer under the amended agreement.

Per the bond resolution, revenues defined as all payment received by the authority derived from any repayments of the loan (by the developer) are pledged to the payment of principal and redemption price of any interest on the bond. The developer continues to make timely monthly payments on the loan and the authority reduces the note receivable. However, since the Executive Director agreed to reimburse 100 percent of these payments if sales do not exceed \$30 million, the casinos are not receiving any interest payments or redemption of principal on its bonds. The CRDA continues to record interest expense and accrue interest payable to the casinos and record the refund of principal and interest to the developer, all under the debt service fund. If sales of the retailer continue to be less than \$30 million, the debt service fund will continue in a negative direction, and the CRDA could potentially default on the bonds, thereby resulting in the casinos and the authority subsidizing the developer. This would amount to approximately \$18.7 million, consisting of the \$12 million loan, a \$330,000 project processing fee, \$3.83 million in amortized interest, and the potential \$2.5 million excess payment of entertainment retail grants.

Recommendation

We recommend that the board evaluate the propriety of terms added to the amended stage development agreement and payments issued to the developer, and the authority should seek a return of any unauthorized payments. All contracts should be executed in accordance with board resolutions. Any terms recommended by the Executive Director that are not in accordance with board resolutions should be placed on the board agenda to ensure a public session vote and the required board approval, which would be memorialized in the board minutes and subject to review by the Governor. Additionally, when applicable, the authority should consider tiered financing terms instead of a 100 percent reimbursement based on a set amount.



Direct Investment Project

The board approved an additional \$2 million direct investment project for a casino licensee without supporting documentation.

In accordance with N.J.S.A. 5:12-144.1, and prior to legislative changes in 2016, each casino was required to either pay 2.5 percent of its gaming revenue to the state or reinvest 1.25 percent of its gaming revenues, through the CRDA, in community and economic development projects in Atlantic City or throughout the state. These 1.25 percent payments, known as Investment Alternative Tax (IAT), are held in an escrow account by the CRDA and used to purchase bonds (to fund CRDA projects), as direct investments (reimbursed back to a casino licensee for its CRDA approved project), or as donations. Under the donation credit policy, a casino licensee is eligible to donate IAT funds to the authority in order to receive access to its IAT funds for non-gaming amenity projects. Through legislation passed in 2011, the IAT funds were redirected to only be used within Atlantic City's Tourism District. Subsequently, in May 2016, legislation redirected future IAT funds to the city of Atlantic City for its debt service obligations.

During our review of IAT donations, we identified one resolution where the board amended a casino licensee's project approval from almost two years earlier, to provide that licensee with an additional \$8 million IAT direct investment and simultaneously approved the licensee to donate \$7,067,600 of its IAT funds to the CRDA.

- On January 25, 2016, the casino licensee submitted a letter to the authority requesting to amend its original \$18.8 million funding application submitted in 2014. The licensee requested increased funding for additional redevelopment of approximately 15,000 square feet of space that was to be utilized as three food and beverage outlets at the property for an additional cost of \$6 million. The casino submitted a market study which outlined, that in the opinion of their advisors, the \$6 million project complied with a direct investment requirement of N.J.S.A. 5:12-178 in that the project did not directly and exclusively benefit, improve or increase the assessed value of a casino hotel or related facility, and approximately 30 percent of the direct and indirect incremental revenues associated with the project would be realized at other Atlantic City establishments outside the casino.
- In April 2016, the casino licensee submitted another letter "to clarify" the previous request dated January 25, 2016 requesting an amendment to permit the direct investment of \$8 million, instead of \$6 million, of currently available IAT obligations for the proposed project. The letter stated that in addition to the redevelopment of restaurant space, the licensee would also renovate its ballroom, meeting rooms, and retail corridor and lobby. Only the casino licensee commissioned market study in support of the \$6 million project was attached. In this letter, the casino licensee also requested to donate \$7,067,600 of its IAT obligations to the authority at a 1:1 ratio, which in accordance with the donation policy means the authority receives the full donation and the licensee received "goodwill". However, this donation request was in conjunction with the direct investment increase, which does not appear to be goodwill and therefore is a unique arrangement.

In response to our request, the authority was unable to provide a subsequent study or any documentation to demonstrate the potential impact of the additional \$2 million investment and compliance with the statute in that the project did not directly and exclusively benefit, improve or increase the assessed value of the casino hotel or related facility. We were unable to determine how the board made the determination to approve the investment without support of compliance.

Recommendation

The authority should obtain independent assurance that the \$2 million investment was in compliance with the N.J.S.A. 5:12-178 and if determined noncompliant, it should seek return of the \$2 million from the licensee. For future projects, the authority should obtain sufficient documentation to ensure compliance with this statute.



Space Utilization

Building assets of the CRDA should be reevaluated for employee occupancy utilization.

The CRDA has not adequately evaluated space requirements for its employees and potential usage of the building assets acquired as a result of S11. In December 2011, after S11 was signed, the CRDA paid \$3.1 million for a two-floor office building and parking lot located next to a previously owned CRDA parking lot. The authority also entered into a lease in a neighboring building for office space previously occupied by the ACSID. Additionally, in 2013, the CRDA acquired Boardwalk Hall and the Atlantic City Convention Center (Convention Center), which both include office space.

As of October 2017, the CRDA had 70 full-time employees assigned to the various locations. We performed a walkthrough of each area, reviewed floor plans where available, and found that space was not being efficiently utilized.

- The office building measures 12,260 square feet and contains 25 offices, 21 cubicles, 4 conference rooms, and the board room. Only 29 employees are assigned to this building.
- There are no floor plans for the office space located at the back of Boardwalk East Hall. The CRDA provides office space to Meet AC in this area for \$5,000 per month, however, there is no formal agreement for this lease arrangement. Additionally, one division of the CRDA is assigned to the space. We performed a walkthrough and identified 54 workspaces, of which 24 were vacant.
- The Convention Center also contains office space. The management company for Boardwalk Hall and the Convention Center occupies 33 spaces. We obtained floor plans, which have not been updated, toured the facility, and identified significant underutilized

space, which we estimate could accommodate at least 22 more employees, if efficiently configured.

- Although there appears to be ample space within the other CRDA properties, the authority is paying \$87,000 annually for leased office space for eight employees and three contracted individuals.

We noted that the Convention Center has 45 meeting rooms available for rent. The planning guide produced by Meet AC identifies each space and a corresponding rental price. Based on event data obtained for the Convention Center, we noted a decrease in the number of smaller sized events. We requested the booking data for these meeting rooms in order to evaluate usage and found that neither Meet AC nor the management company for the Convention Center track the usage of these event rooms in the booking software. If the usage was properly recorded and evaluated, underutilized rooms could potentially be repurposed for office space to accommodate all of the authority's professional operations.

Recommendation

We recommend the CRDA evaluate usable office space throughout authority-owned properties and determine where efficiencies could be achieved by consolidating operations into fewer buildings, ending a lease of excess office space, and potentially disposing of excess administration properties. Additionally, the authority should ensure the use of Convention Center meeting rooms is recorded to properly analyze usage.



Accounting Practices

We noted internal control weaknesses over the recording of revenue, procurement, and accruals.

Revenue Recording

The CRDA maintains a number of funds within its financial reporting system. In addition to accounting for direct revenue sources, a significant number of interfund transactions were processed through journal entries and issuance of checks payable to the CRDA. We found limited approval and untimely recording of revenue-related transactions, including journal entries, contributed to errors. The CRDA accounting manual requires that a copy of each check and additional support be retained for each entry, however, we found that this was not the actual practice, as complete support was not routinely retained.

The authority has written policy and procedures to ensure all cash receipts are properly documented, independently verified, and promptly deposited. These procedures include a policy that all cash and checks should be logged into a cash receipts journal. For the 25 transactions

we tested, no cash receipts journal was maintained nor were deposits made timely. In the absence of a cash receipts journal, we used the check date and compared it to the deposit date and noted delays ranging from 4 to 85 days, with the median delay of 20 days. One check for \$3.2 million was deposited 85 days after the check date. We noted another check for \$529,000 was sent to an attorney in error, where it remained for 24 days before the attorney sent a check to the CRDA and was not deposited for an additional 14 days. Also, the CRDA did not record accounts receivables for other revenue, which could allow for receivables to go undetected and therefore uncollected.

At the completion of our field work, the authority indicated that the deficiencies in recording cash receipts had been addressed with updated procedures. We tested these updated processes and found controls were still inadequate. The authority now uses an Excel spreadsheet to log cash receipts; however, the same Excel file is updated daily and accessible by anyone in the finance department. We performed an additional review and found it still took an average of 19 days from the time a check was received until deposit. Furthermore, the authority does not have a control structure in place to prevent checks from being misappropriated or unaccounted for, since it does not reconcile cash receipts to deposits.

Some transactions we tested were not routinely recorded timely in the accounting system which is necessary for accurate financial reporting and the ability for management to make informed decisions. We identified the following.

- A \$301,000 check dated, and for 2015, was held and recorded in 2016.
- 2015 interest income of \$43,146 was recorded in 2016.
- 2015 project processing fees totaling \$33,382 were recorded in June 2016.

The authority's practice of utilizing interfund transactions allowed payable and receivable accounts to grow without an efficient process to reconcile the activity. These accounts should be zeroed-out to provide an accurate cash perspective in each fund.

Special Improvement District Assessment

A Special Improvement District (SID) assessment is charged to businesses within the Tourism District. Separate accounting software is utilized to track these assessments which are due quarterly and payable to the CRDA. The authority's Special Improvement Division is responsible for the collection efforts. The authority's Finance division prepares a multi-step calculation to arrive at year-end amounts related to this revenue source which are recorded in the accounting system. Our review identified the following.

- Through a verbal request, the Finance division directed the Special Improvement Division to credit \$153,635 in receivables in the assessment software. This transaction was not simultaneously accounted for in the accounting system. The omission was not identified

until after the year-end calculation was complete. The authority improperly addressed the omission by increasing the allowance for doubtful accounts by \$153,635 and stated it was “to increase the allowance to 100% of the current year outstanding assessments.” Since current year outstanding assessments were less than that amount, the accounts receivable was understated by \$31,540. The lack of written documentation for this transaction allowed for the resulting error and revealed a control weakness in the recording of transactions.

- A journal entry for \$71,480 was credited to SID assessments in error, thereby overstating revenue and assets for 2016.
- A bad debt expense is not utilized. Additionally, there is no formal policy on what is deemed uncollectible. Bad debt is recorded as a direct reduction of revenue resulting in an understatement of current revenues when used for analysis.

Procurement and Accruals – Convention Center Division

We found the Convention Center Division’s actual purchasing practices did not follow the authority’s accounting manual and needed improvement. Our sample of 76 transactions identified control weaknesses that could result in overspending or misappropriation of assets.

- Of the 49 applicable transactions tested, we noted 34 purchases totaling \$349,520 were ordered without proper authorization prior to the purchase, as required by the accounting manual.
- Supporting documentation, including shipping and receiving reports, was inadequate for 12 of 76 invoices we tested totaling \$235,727.
- Competitive price quotations were not documented for 24 of the 34 applicable transactions between \$5,000 and \$36,000, as required by the authority’s accounting manual.
- A two-year contract entered into by the ACCVA in December 2012 and assumed by the CRDA through the merger authorized payments totaling \$110,950 for 2014. The contract allowed for a one-year extension at the discretion of the authority. Actual payments to this vendor totaled \$234,300 for 2014 and \$228,000 for 2015. There was no CRDA board approval for the additional \$351,350 expended over the original contract terms and as required for this level of spending.

The Convention Center Division of the authority accrues expenses for various types of transactions. We found certain accounts continue to increase in an excessive and unsupported manner.

- There was no rationale for accruing audit fees totaling \$241,500 between 2014 and 2016. The authority subsequently recorded year-end adjustments to transfer \$113,400 of this accrued amount to the CRDA general fund. The CRDA actually paid \$145,500 for the 2014

through 2016 audits and it appears disproportionate that the Convention Center Division was responsible for 78 percent of this overall expense.

- The authority continues to record a monthly liability to New Jersey Transit “in an abundance of caution.” From January 2014 through September 2017, the authority has expensed \$712,500. The monthly expense was previously paid by the ACCVA under a stated agreement until it merged with the CRDA in 2013. We reviewed the agreement and could not determine that a \$190,000 annual payment is due. While authority management states that it is involved in ongoing discussions regarding this matter, after four years the issue has not been resolved and the amount of reserved funds continues to increase.

Recommendation

We recommend the authority improve their internal controls over accounting for revenue. Transaction support should be retained in the Finance division, and the authority should implement levels of approval for each type of accounting entry and formally document and approve all adjustments. State of New Jersey, Department of the Treasury Circular 12-02-OMB states that funds must be deposited on the same day they are received. While state authorities do not have to comply with the circular, the guidelines are a measure of best practice. A secure process to record cash receipts on a daily basis should be implemented. A reconciliation between cash receipts and the actual deposit should be performed to reduce the risk of lost funds and unrecorded transactions. The authority should also implement procedures to timely zero-out interfund transactions. In addition, it should develop a policy regarding write-off of uncollectible accounts. Since the Special Improvement Division is responsible for the accounting of SID assessments, it should be included in the year-end close process to ensure accuracy. The authority should ensure that all its divisions follow the same procurement policies and procedures. Accrued expenses should be properly supported and proportionately allocated to applicable divisions. Finally, the authority should resolve the \$190,000 payment issue with New Jersey Transit.



Marketing and Communications

Resources related to the Marketing and Communications division are not being used in an efficient and effective manner.

The CRDA maintains a Marketing and Communications division (division), which is one of the larger authority divisions with an employee count of 19, annual salaries and benefits of \$833,000, and a spending budget of \$1.1 million in 2017. The division’s primary responsibilities include overseeing visitor information centers, a call center, and some CRDA events in addition to maintaining the CRDA websites and a marketing partnership program. We noted the division’s role appears limited, and resources are not being used in an efficient and effective manner.

Prior to S11, the ACCVA was responsible for advertising and promoting the tourist, resort, convention, and casino gaming industries. The Atlantic City Alliance (ACA), a public-private partnership, was created in late 2011 with \$30 million in annual funding from the casinos to develop a brand identity for Atlantic City and market the city as a destination resort. The ACCVA continued some of the consumer marketing after the ACA began operations, however, upon the completed merger with the CRDA in 2013, the ACCVA employees were absorbed, but their consumer marketing responsibilities ceased. In 2014, Meet AC was established to sell and market conventions in Atlantic City, effectively removing this responsibility from the division as well. As part of the Casino Property Tax Stabilization Act signed into law in May 2016, the marketing partnership required under the Tourism District Act was repealed. As a result, the ACA disbanded and its remaining funds were directed to the City of Atlantic City for debt service. Assets of the ACA were transferred to the CRDA; however, it was unclear during our audit if the authority will be responsible for consumer marketing.

Software

After joining the CRDA and being subsequently stripped of any consumer marketing and convention sales responsibilities, the division contracted for a new customer relationship management computer application without board approval. On December 22, 2014, the division signed a contract which included a one-time fee of \$41,125 plus annual charges of \$37,600 for four years. The CRDA paid \$78,725 on December 30, 2014, although only the deposit of \$20,562.50 was required upon contract execution, with the remaining balance due upon program launch, which did not occur for four months. After our review of the services and modules provided under the contract, it appears, and was confirmed by management, that the software capabilities are underutilized and not necessary for the limited functions of this division.

Visitor Welcome Center

The Atlantic City Expressway Visitor Welcome Center appears underutilized. In 1998, the CRDA constructed the 2,500-square-foot center. Upon completion, ownership of the center was transferred to the South Jersey Transportation Authority, which agreed to a ten-year lease for \$1 with the ACCVA. This lease has continued past the termination date. Once ACCVA merged with the CRDA, the Visitor Welcome Center became the responsibility of the CRDA. The center is open Wednesday through Sunday from 9am to 5pm. The CRDA is responsible for staffing, utilities, and interior maintenance of the facility. We noted that minimal visitor traffic, combined with building overhead costs, may not substantiate the functionality of the facility.

Analytics

Employees of the Visitor Welcome Center and Boardwalk Information Center are instructed to request visitors' zip codes, which are then entered into the marketing program along with the number of visitors in the group. A manual tally of visitors to each center is also maintained on a daily basis. These manually recorded counts are summarized and published to the CRDA website, but appear to be inflated based on our review.

We obtained a download of the data entered into the marketing program and the manual tally sheets. We calculated that on average 50 groups stopped at the welcome center per day from May 1, 2015 to April 30, 2016 and that number decreased to 48 groups per day from May 1, 2016 to April 30, 2017. It appears a group can include an entire bus, although it is not clear how many individuals, if any, requested information or entered the facility. Bus passes, restaurant week gift certificates, and restroom facilities are also available at the welcome center. Per CRDA management, the database of zip codes was not used for anything since the CRDA does not perform any destination marketing for the city.

Utilities

Utility expenses at the Visitor Welcome Center appear excessive for a 2,500-square-foot building. Electricity averaged \$2,800 per month from 2014 through 2016, and water bills totaled approximately \$11,000 in 2014 and peaked at \$18,000 in 2015 before an apparent leak was fixed, decreasing the 2016 total to \$1,400.

Visitor Welcome Counselors

Three employees answer phone calls and respond to emails and online chat requests Monday through Friday from 9am to 5pm. Annual salaries and benefits totaled approximately \$135,000. During off-hours and weekends, an operating service handles phone calls. The service directs callers to restaurants, hotels, casinos, and other areas of interest. We reviewed the volume of inquiries by phone to the center and noted the volume decreased by 7 percent in 2016, compared to 2015, totaling 10,129 calls and averaged 13 calls per employee per day. Based on this volume, the costs for this operation may not be the most effective use of authority funds.

Restaurant Week

The CRDA organizes a one-week event at which participating Atlantic City and Atlantic County restaurants offer fixed price, three-course meals at a reduced cost. Total restaurant week expenses, net of restaurant participation fees, averaged approximately \$146,000 for 2016 and 2017 and were primarily advertising and marketing related, in addition to a preview event and gift card-related fees. In 2017, the preview event featured 13 of the restaurants participating in restaurant week. Based on the information provided to us, it appears that approximately one-fourth of the 2017 attendees at the preview event were VIP guests, including media, restaurant owners, sponsors, and authority staff and board members. We were informed that registration is tracked on the evening of the event, but documentation is not retained. Tickets to the public were sold for \$35 each with reported proceeds of \$8,890 for 2017 which was deposited into a foundation account to fund scholarships. The authority's cost of the 2017 event was \$21,090 and included an open bar to VIP guests. The event is held at an outside venue even though the CRDA owns Boardwalk Hall and the Convention Center. The CRDA does not solicit proposals to hold the event at one of its buildings. The CRDA sets a budget for restaurant week but has not performed a formal analysis to substantiate if the overall level of spending resulted in increased patronage.

Recommendation

The authority should assess the responsibilities of the Marketing and Communications division in order to ensure an effective and efficient use of its resources. It should evaluate the customer relationship marketing software to determine if its capabilities are necessary and procure any future contracts properly. The authority should also evaluate the objectives of the Visitors Welcome Center and determine if the operational costs combined with the visitation numbers are an efficient use of its resources. Events should have clear objectives with performance metrics, and budgets should be adjusted accordingly. Additionally, the authority should seek outside clarification to determine any responsibility for consumer marketing of Atlantic City.



Legal Expenditures

Legal expense payments were not in accordance with contract terms.

The authority employs two attorneys and two paralegals and also engages outside counsel for various needs. Our review of legal expenditures identified the following.

- The authority regularly utilizes three firms that were procured through Request for Qualifications proposals in 2014 and 2016. Contracts with these firms covered September 2014 through July 2018. We noted expenditure caps are not included in the contracts; however, there is an overall budget for legal expenses. Total annual payments averaged \$1.28 million from 2014 through 2017.
- We were unable to determine the accuracy or reasonableness of a \$52,136 legal payment to an additional law firm procured through an exception to competitive procurement. The documentation on file in the Finance Division to substantiate the payment for approximately one month of service was insufficient, so we requested the invoice. The authority redacted all activity descriptions, stating “attorney-client privilege,” thereby limiting our ability to properly audit this transaction. Up to that point, we reviewed legal invoices in full content, but we were informed that any additional legal invoices subject to our audit would be redacted.
- Of the remaining invoices that we were able to review in full content, we noted that the authority did not verify invoice charges to the applicable contract for compliance with contract terms.
 - We found that the authority was paying one firm a two percent administrative fee on professional fees which was not authorized by contract. We presented this issue to management, and as a result the firm refunded the authority \$21,300.
 - The authority paid invoices billed at a Counsel title but at a Partner title rate, the highest

rate allowable under the contract. A Counsel title is not authorized under this firm's contract with the authority. Of the \$42,800 in invoices we reviewed for this firm, \$23,000 was incorrectly billed at the Partner rate.

Recommendation

We recommend the authority ensure legal payments are made in accordance with contract terms and evaluate methods to reduce overall legal fees. We also recommend it recover any additional overpayments noted as a result of our review.



Parking Garage Revenue

Revenue generating activities are not properly monitored.

In 2012, the authority opened the Wave Parking Garage, a five-story structure with 1,180 parking spaces and retail space on the ground floor. Our review of revenues related to the garage found a lack of monitoring by the authority.

A feasibility analysis was completed prior to construction of the garage which estimated total annual revenues would average \$4.6 million for 2014, 2015, and 2016, representing the third, fourth and fifth year of the garage's operations. We noted that actual revenues for this time period averaged only \$755,000 (16 percent of the forecast). We requested, and the authority could not clearly identify, who has been responsible for monitoring the garage operations and the lease.

Retail space on the first floor of the garage consists of approximately 16,000 square feet. The space, which is leased to a university for one dollar per year, houses artist studios, galleries, shops, a café, and a flexible workshop/classroom and hosts special events throughout the year. Under the terms of the lease, the authority should receive additional rent from the university in the form of a pro-rata share of the garage's operating costs and 20 percent of net revenues generated from the leased space. We found that the Finance division was unaware of the lease terms and therefore issued no invoices until we presented the issue. This has resulted in the following.

- The authority determined that 3.8 percent of the garage is common space and agreed that operating costs should have been billed to the university. We calculated that approximately \$105,000 was due to the authority from November 19, 2013 through 2017.
- The university informed the authority that there has been no net revenue generated from the leased space and only provided an abbreviated financial statement for fiscal years 2014 through 2017 to substantiate this claim. The authority did not request additional support to verify the amounts for accuracy or evaluate them for reasonableness.

The roof of the garage maintains a 54,000-square-foot rooftop solar array consisting of 1,677 solar panels. A Solar Renewable Energy Credit (SREC) is generated for sale on the SREC market. After multiple requests for SREC data, we were finally provided with a report. We identified a decrease in SREC production for the 18 months between October 2015 and March 2017. When compared to October 2013 through March 2015, we found that production decreased (41 percent) from a monthly average of 41 SRECs to 24 SRECs. The authority was not monitoring the matter and did not address the underlying problem of two non-operational inverters until March 2017. We estimate that due to the lack of monitoring SREC production, approximately \$58,000 in SREC revenue was lost.

Recommendation

We recommend the authority monitor the terms of all contracts and consistently monitor and evaluate revenue producing assets to ensure revenues are collected and maximized. The authority should collect past due rent payments from the university and should ensure supporting documentation is received in order to evaluate the accuracy of amounts submitted by the lessee.



Human Resources and Payroll

The authority did not ensure proper communication regarding employee job responsibilities and performance, a standard procedure regarding waiver of board compensation, and compliance with employment contracts.

Job Descriptions and Performance Evaluations

When the authority absorbed the ACCVA and the ACSID, it appears there was little effort to effectively merge the employees' responsibilities. We found the authority did not maintain adequate communication with employees or implement a process to monitor their responsibilities and performance.

- Employees should be presented with, and provide acknowledgement of, valid job descriptions to ensure awareness of their job responsibilities. Job descriptions also provide the employer with a measurement of employee resources and performance. We requested job descriptions for all of the authority's employees with the exception of seasonal and on-call employees. Of the 77 full-time and regular part-time employees as of March 1, 2017, we identified 56 titles and found the authority did not have a job description for 23 of them. We also noted that 8 of the 33 job descriptions were outdated, and responsibilities, such as those of the ACCVA employees, were no longer valid. The authority was unable to provide any documentation that employees were actually presented with their job descriptions.
- The CRDA Policy and Procedure manual states that the authority endeavors to conduct an

annual written performance review of each employee. In addition, it shall be the policy of the authority to recognize meritorious performance through an increase in salary commensurate with the individual's contribution to the success of the organization. We found the authority did not conduct employee performance reviews during our audit period even though salary increases were given to some employees.

Reduction in Force

As of March 1, 2017 the authority had 108 employees of which 77 were full-time or regular part-time. In March 2017, the authority completed a reduction-in-force (RIF) in which 11 employees were terminated resulting in a reduction of \$715,000 in salary and benefit costs. Eighteen employees were simultaneously awarded salary increases ranging from \$2,000 to \$40,000, for a total of \$149,000, which decreased the RIF's cost savings. Fourteen of these employees were given a new title, of which there were no job descriptions for nine of them. We found the authority still had not prepared these job descriptions more than seven months after the RIF. Four employees who were given salary increases remained in their same title. The authority was unable to document how it most effectively reduced staff and awarded raises without having a complete assessment of employee responsibilities and performance. We noted by year-end the authority hired four new employees while three employees separated, resulting in a net increase of \$185,000 in salary and benefit costs, thereby further decreasing the cost savings from the RIF.

Board Compensation

In accordance with N.J.S.A. 5:12-156, each appointed and voting public member of the CRDA, with the exception of casino industry representatives, shall receive compensation of \$18,000 per annum; compensation of the Chairman is set to \$23,000 per annum. We found that board members who waived their compensation were retroactively paid a combined total of \$68,000. In January 2017, three board members submitted letters, all with similar language, to the authority stating that each had previously voluntarily waived their right to receive the annual stipend, and all three were requesting that the authority reinstate payment retroactively to January 1, 2016. The authority processed \$59,000 through payroll in 2017 for the 2016 waived compensation. On July 17, 2017, a fourth board member submitted a similar letter requesting reinstatement from and after January 1, 2016, but was only paid \$9,000 retroactively from January 1, 2017. The authority lacks a formal procedure on waiver of compensation. We question the propriety of retroactively reinstating compensation that was previously waived. Additionally, the approval and payment of these retroactive payments were not handled consistently.

Executive Director Severance

At the December 6, 2016 public meeting, the board announced that the Executive Director would be leaving the authority effective December 31, 2016, and consistent with his employment agreement he would receive a severance equal to one year of his \$225,000 base salary. Our review of the employment agreement identified that severance shall be paid for a

“Termination without Cause” or “Resignation for Good Reason” and any termination shall be communicated by a written Notice of Termination which indicates the specific termination provision relied upon. We requested the required written Notice of Termination and found that neither the authority nor the former Executive Director prepared this document. We also reviewed the Separation Agreement signed on December 31, 2016 and could not identify which party initiated the separation and under which circumstances. It appears the severance payment was released under conditions not consistent with the employment agreement and therefore was unauthorized without additional board action.

Potential Cost Savings

The authority maintained two separate payrolls, one primarily for former ACCVA employees and the other for the remaining employees. These two payrolls were processed on a weekly basis and direct deposit was not mandatory. We estimate that the authority could reduce payroll processing costs by an estimated \$15,000 per year if the two payrolls were consolidated into one, payroll was processed on a bi-weekly basis, and direct deposit was mandatory. Additionally, the elimination of weekly payroll would reduce administrative time spent on this function.

Recommendation

The authority should ensure employee job descriptions are prepared, updated, and presented to employees, and management should perform annual formal evaluations of staff. The authority should also develop a standard procedure for waivers of board compensation with any reinstatement effective prospectively from the date of request. The authority should adhere to all terms of employment contracts and the board should review the propriety of the former Executive Director’s severance payment. The authority should also evaluate payroll processing policies for cost and time efficiency.



Redevelopment Project

The authority should actively monitor redevelopment projects.

In 2003, the authority entered into an intergovernmental agreement with the Camden County Improvement Authority (CCIA) to provide \$24 million in funding towards a property redevelopment project. As part of the agreement, the authority is entitled to inspect and audit the records of the CCIA activities related to the project, but it was unable to substantiate to us any effort to do so. Additionally, the authority did not provide us with any documentation to demonstrate that the project was monitored. In 2004, the authority paid \$2.4 million, the first of ten installment payments to the CCIA, in accordance with the intergovernmental agreement. By 2005, when the CCIA’s proposed project failed to materialize, the authority did not remit the next installment payment. The CCIA modified the purpose of the project, citing economic

factors. The CRDA subsequently reduced the project funding to \$16.5 million and in July 2007 amended the intergovernmental agreement requiring the CCIA to enter into a development agreement for the property within three years, thereby extending the deadline to 2010. The CRDA funded the remaining \$14.1 balance in September 2007. Once again, the deadline was not met, an additional two years passed, and in 2012 the intergovernmental agreement was amended. This second amended agreement entitled the CRDA to one-half of the proceeds from the sale of the property when a development agreement was to be executed and extended the maximum project completion deadline to seven and one-half years after the signing of the development agreement, with the first phase of the project to be completed within the first two years.

The CCIA failed to secure a development agreement for more than 12 years but in 2016 finally executed an agreement including the sale of the property. The CRDA received \$3.2 million, as per the second amended agreement, and currently has a net investment of \$13.3 million in the project. The second amended development agreement requires that the first phase of the project (200 units) be completed by April 2018 and the entire project by October 2023. As of May 22, 2018 the audit team observed that the required 200 units were not completed. While it appears that the project is currently in progress, the authority allowed more than 12 years to pass without an apparent return on its investment.

Recommendation

The CRDA should develop controls to monitor projects through completion to ensure that deadlines are achieved, and its funds are utilized as intended and in an efficient and effective manner. In addition, the authority should establish criteria to recover funds in a timely manner when a project is not materializing as approved.



CRDA/ACCVA Foundation

The CRDA/ACCVA Foundation lacks a governing board necessary to expend the nearly \$120,000 fund balance that has been available for over three years.

The former Atlantic City Convention and Visitors Authority Foundation (foundation) was established in 2004 to support appropriate benevolent causes, with specific attention given to attracting greater diversity of visitors to and investment in the destination, fostering quality partnerships in and around the region, and identifying and assisting worthy individuals and organizations in the greater Atlantic City area. The CRDA assumed responsibility for the foundation in 2013 upon transfer of functions resulting from S11. It was then renamed the CRDA/ACCVA Foundation. The individuals who formed the governing body of the foundation, in addition to the authorized signatures on one of the two foundation bank accounts, are no longer active members of the foundation or associated with the CRDA. After four years, a process to appoint new board members has not been completed and, as a result, available

funds have not been utilized to support the foundation's mission. As of March 2017, which was the most recent available bank statement for the foundation during our audit, there was a balance of nearly \$120,000. The last deposit was made in June 2014 and the last distribution of funds was in October 2013 except for monthly service charges for accounting software that has not been utilized since January 2013.

Recommendation

We recommend a new board be appointed to the ACCVA/CRDA Foundation to ensure the remaining funds are utilized as originally intended. Additionally, the unused accounting software services should be cancelled if determined unnecessary.



Observations

Notes Receivable Allowance

The Authority does not have a policy to uniformly identify doubtful notes receivable.

As part of its redevelopment mission, the authority had provided assistance in the form of loans for various projects in Atlantic City and throughout the State of New Jersey. At the end of fiscal year 2016, the balance of notes receivable, which accounts for these loans, totaled approximately \$115 million, less an allowance of approximately \$40 million for loans deemed uncollectable. This allowance amount represents three projects approved in 1987, 1993, and 2001. We noted a fourth project, also approved in 1993, that has never remitted a principal or interest payment on its loan, but was not included in the allowance. The applicable notes receivable was \$10 million and the accrued interest balance was approximately \$9.8 million at the end of 2016. The authority does not accrue interest on the other three uncollectable project loans nor does it have a policy to uniformly identify which receivables should be written-off. We could not identify any collection efforts for the fourth project or why this \$10 million loan is accounted for differently than the other three that are in a similar default status. The authority should consider developing, implementing, and documenting a write-off policy to uniformly identify, document, and account for doubtful notes receivable and present a more accurate financial position.

Host Awards

The Authority should evaluate the spending on the awards gala.

The CRDA facilitates the annual Atlantic City Host Awards to honor employees in the tourism and hospitality industry who enhance the experience for Atlantic City visitors. It hosts a gala to honor the nominees and award recipients. Complimentary tickets are given to each nominee and a guest in addition to CRDA staff and board members. Additional tickets for the event are sold

but do not cover the cost of the event, resulting in an average net expense of \$61,000 to the authority. The authority should consider examining the program to determine if the level of spending on the gala to present the host awards is an effective use of CRDA funds.





Philip D. Murphy
Governor

August 21, 2018

Robert E. Mulcahy, III
Chair

BY OVERNIGHT MAIL AND EMAIL: jtermyna@njleg.org

Elizabeth M. Muoio
State Treasurer

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Mayor Frank M. Gilliam, Jr.
City of Atlantic City

Debra P. DiLorenzo

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Michael I. Hanley

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Matthew J. Doherty
Executive Director

Mr. John J. Termyna
Assistant State Auditor
Office of Legislative Services
Office of the State Auditor
125 South Warren Street
PO Box 067
Trenton NJ 08625-0067

RE: Response of the Casino Reinvestment Development Authority to the
Office of Legislative Services Audit Report dated August 2, 2018

Dear Mr. Termyna:

On behalf of the Casino Reinvestment Development Authority (the "Authority"), its members and staff, I am delivering the Authority's response to the audit report prepared by the Office of Legislative Services (the "OLS").

The OLS audit staff spent twenty-four months examining the Authority operations and financial statements. The Authority reviewed and evaluated each of the audit findings in the report, and indicated its agreement or disagreement, as set forth in our response. Where the Authority agreed with the audit finding, we described appropriate corrective and preventative action(s) to address the matter. In some of the cases where the auditors identified the need to corrective action, the Authority, through self-examination of its operations, was implementing a corrective and preventative action plan prior to completion of the audit. Where the Authority disagreed with the audit finding, we endeavored to state with specificity the factual basis for our disagreement.

The OLS audit covered a period of unprecedented challenge for the Authority as the State twice significantly changed the Authority's focus and finances with major legislation in 2011 and 2016. Additional major challenges included: a change in its executive leadership, ongoing assimilation of the former Atlantic City Convention and Visitors Authority, a streamlining of personnel and structure, a complete overhaul of

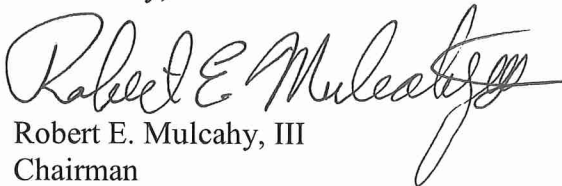
Mr. John J. Termyna
August 21, 2018
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its legacy information technology platform and systems, the upgrade of its accounting and financial management systems and accounting policies and procedures, promulgation of new land development regulations to advance the Legislature's goals and objectives for the Atlantic City Tourism District, a redefining of its mission due to the diversion of nearly two-thirds of its revenues to support the State's efforts to address the City's fiscal crisis, and the dissolution of the Atlantic City Alliance, the Authority's private-sector partner for marketing and promoting the City.

Despite these challenges, the Authority redoubled its efforts to achieve the Legislature's mission for Atlantic City, by utilizing its existing resources to invest in capital maintenance projects at Jim Whelan Boardwalk Hall and the Atlantic City Convention Center, to support the construction and expansion of non-gaming amenities at nearly all of the major casino properties, to finance construction of the first new rental housing stock in nearly 50 years in the City, to help fund development of Stockton University's new Atlantic City campus and academic facilities, to advance programs and world-class entertainment events for the convention, meeting and leisure tourism industries, and to invest in public safety infrastructure and personnel to foster a clean and safe Atlantic City.

I note that during this period of significant change, the Authority continued to receive unmodified opinions from its independent financial auditors, who prepare the Authority's annual audited public financial statements. We welcome the OLS's examination and critique of our operations and financial status, and the Authority will continue to seek opportunities to improve our processes so that we may better serve our stakeholders.

Yours truly,


Robert E. Mulcahy, III
Chairman

Enclosure

c: Stephen M. Eells, State Auditor w/encl.



Casino Reinvestment Development Authority Response to OLS Audit Report of August 2, 2018

The detail below sets forth the Authority's reply to the Office of Legislative Services' audit report dated August 2, 2018. As necessary, relevant text of the audit report are referenced in *italics* prior to each Authority response.

I. SCOPE: *The authority limited access to original documentation for our transaction and contract testing by requiring that documents requested initially pass through administration prior to access. Many of our requests were then fulfilled with photocopied documents. In addition, the authority limited our ability to audit legal expenses by redacting invoices.*

See
Auditor's
Follow-up
Response
Page #47

Response: The authority disagrees that it limited access to original documentation or limited the auditors' ability to audit legal expenses by redacting invoices.

The audit scope spanned three years of authority activities, thousands of pages of records, and the interview of numerous staff personnel. In order to keep track of the voluminous information requests from the auditors, the authority assigned a member of its senior staff to coordinate and compile document requests. At the kick-off meeting, the auditors were introduced to this staff person, and made aware of the authority's intent to coordinate the audit through this individual. During the course of the audit, this staff person fielded document requests to ensure that requests were tracked and responded to by authority staff. Copies of requested records and a list thereof were retained by the authority so that it could efficiently respond to numerous follow-up queries from the auditors. The auditors were provided with originals, copies of originals and scanned copies of archival documents.

Nothing in the Government Auditing Standards 2011 Revision, GAO-12-331G (issued December 2011) (the "2011 GAGAS"), which is the audit standard applicable to the Audit Report, precludes or restricts the authority's ability to coordinate its responses to the auditors through administrative staff. The authority's process for managing the auditors' inquiries for records is consistent with the 2011 GAGAS, which contemplates and allows for the production of originals and copies of original records (See Chapter 6, Field Work Standards for Performance Audits). Best practice guidance for managing external audits requires that the entity being audited coordinate the audit through a liaison, review document requests prior to submission to the auditor to ensure completeness, and either maintain a list of requested documents and/or retain a copy thereof.

As to the redaction of legal invoices, upon the advice of legal counsel, the authority redacted the substantive written description of its communication with its special legal counsel to protect its attorney-client privilege. The authority did not redact cost and expense detail from its invoices.

Section 6.70 of the 2011 GAGAS states: "Sufficiency and appropriateness of evidence are relative concepts, which may be thought of in terms of a continuum rather than as absolutes.



Casino Reinvestment Development Authority Response to OLS Audit Report of August 2, 2018

Sufficiency and appropriateness are evaluated in the context of the related findings and conclusions. For example, even though the auditors may have some limitations or uncertainties about the sufficiency or appropriateness of some of the evidence, they may nonetheless determine that in total there is sufficient, appropriate evidence to support the findings and conclusions.”

The auditors’ characterization that their review was limited by the authority’s actions is inappropriate given the thousands of pages of documents reviewed, the unfettered access to staff, and the standards set forth in the 2011 GAGAS.

II. CONCLUSIONS: See *italicized auditor statements* in the body of the authority’s responses below.

Response: A. *[C]ertain transactions were not always reasonable... We also found that the CRDA did not always ensure an effective and efficient use of its funds.* As an entity established in but not of the Department of the Treasury, the use of authority funds is principally driven by the policy goals and objectives of the State of New Jersey, as set by the executive branch. As an economic and community development entity, the authority typically participates as a junior funder with private sector senior lenders and equity investors in approved projects. As such, unlike a private commercial bank, the authority has and will likely continue to be, an at-risk funder, sometimes of last resort, for important economic and community development endeavors. As such, like all public redevelopment entities, the authority is, in many instances, required to be a “patient” investor, focusing on achieving important policy goals and objectives over financial metrics.

Pursuant to its enabling legislation (as amended), the authority makes project investment decisions based on a number of criteria grounded principally in policy goals and objectives, and secondarily in financial return on investment. When the authority makes an investment in a project, it relies on its analysis of the facts and policy direction at the time, in the exercise of its business judgment, without the benefit of knowing whether its investment decision will ultimately result in a successful project. To suggest that the authority is ineffectively and inefficiently using its funds or that such use is unreasonable, applies a subjective hindsight bias to authority decision-making, rather than the objective analysis and understanding of the authority’s purpose and goals, and related outcomes, as required under the standards promulgated in the 2011 GAGAS (See e.g., Sections 2.10, 6.15b, 6.15e, 6.15g).

B. *The authority lacked a process to monitor compliance with contract terms resulting in overpayments, lost revenue and potentially lost deliverables, as well as not being able to use measurable results in future contract negotiations.* The authority assigns project officers and senior project officers to monitor and manage its contractual and project relationships. These individuals, principally in the Project Implementation and Management Unit, are charged with managing projects from board approval to completion. With minor exception, the authority does not agree that overpayments, lost revenues or lost deliverables resulted from any perceived



Casino Reinvestment Development Authority Response to OLS Audit Report of August 2, 2018

deficiency in its monitoring of contractual relationships through its Project Implementation and Management Unit. As part of a corrective and preventative action plan, the authority intends to redouble its effort to provide additional training to the project management staff to ensure they are equipped with current project and contract management best practices.

C. *[T]he authority materially modified certain contracts with terms not consistent with authorizing board resolutions which resulted in unauthorized payments.* As more fully set forth in this memorandum response, the authority does not agree that unauthorized payments were made contrary to board approval. As a general matter, the authority's governing body delegates the power to negotiate and execute agreements to the executive director. The authority's governing body is involved in all instances where material contractual terms are being amended, subsequent to the original delegation of authority and approval of a project. These discussions concerning contract terms and conditions take place in closed, executive, sessions of the board, where the governing body provides direction to authority staff, which direction is then incorporated into amendment(s) to the contractual relationship. Executive session meeting minutes generally summarize the subject matter of these discussions. As part of a corrective and preventative action plan, as appropriate, the authority will provide more specificity in its closed session meeting minutes to reflect the board's involvement in material modifications to its contractual relationships.

D. *[W]e found improper use of emergency procurement resulting in contracts being awarded to the highest bidder, improper approval of a direct investment project, improper calculation of sponsorship fees and payment for board members' waived compensation; all resulting in potential overpayments.* As more fully set forth in this memorandum response, the authority disagrees with this conclusion.

E. *We found the CRDA did not effectively streamline operations upon the completed merger with the ACCVA and ACSID in 2013. The authority did not formally evaluate the resulting functions in conjunction with the former responsibilities of the increased workforce, nor did it communicate new employee responsibilities through job descriptions or assess employee performance through periodic evaluations. Additionally, the authority continued to maintain separate accounting systems and processes for the acquired divisions without apparent consideration to unify the processes until 2016, nor did it have controls in place to effectively transition the finance operations when the former Chief Financial Officer retired in 2015.*

The authority agrees, in part, to the auditors' conclusion.

The authority did not "merge" with the ACSID or ACCVA. In furtherance of the Tourism District Act, P.L. 2011, c.18, as amended, upon the city of Atlantic City's repeal of its special improvement district ordinance, the authority, in the second quarter of 2011 established a new, separate special improvement district, an area over four times the geography of the City's former district. The authority reviewed the duties of all City ACSID staff and made employment decisions



Casino Reinvestment Development Authority Response to OLS Audit Report of August 2, 2018

based upon this review, retaining some personnel and laying off others. After further evaluation of its new responsibilities since 2011, the authority added personnel, including the funding of "Class 2" police officers as part of an intergovernmental agreement with the city of Atlantic City. The authority also assessed the assets utilized by the former City ACSID and over the following three year period, dedicated significant resources to upgrading and adding to the equipment and rolling stock necessary to meet its mission in the new district.

Subsequently from the second quarter of 2013 through the fourth quarter of 2014, the authority initiated and substantially advanced the transfer of ACCVA operations into a new division known as the "convention center division," along with rights and obligations of the New Jersey Sports and Exposition Authority, including the ownership and operational responsibilities appurtenant to Historic Boardwalk Hall and the Atlantic City Convention Center.

From 2011 through 2015, the authority's focus for both its new special improvement district and convention center division was to ensure a seamless transition from a customer, conventioneer and tourist perspective, with recognition that process upgrades and complete assimilation of the differing operating entities would necessarily follow.

Given the foregoing, the authority agrees that the streamlining of processes and assimilation of personnel took longer than anticipated, and was interrupted by the unanticipated retirement of its former Chief Financial Officer in 2015. However, as the auditors were made aware during their examination of the authority, but what is not stated, at all or clearly, in the Report, the authority has already invested significant financial resources to: (i) replace its legacy information technology platform (including the investment into an off-premise data center to ensure uninterrupted functionality to its core IT systems), (ii) upgrade and replace its accounting and financial management system, including the preparation and dissemination of new accounting and financial management standard operating procedures, and (iii) add needed personnel in the areas of human resource management and in finance to address self-identified shortcomings in those areas of its operations. Moreover, as the auditors were made aware, but not clearly stated in the Report, the authority conducted a second assessment of its personnel, and reorganized its staff following changes to its enabling legislation that diverted significant financial resources of the authority to fund City debt service. The foregoing initiatives, some of which began prior to the audit, are part of a corrective and preventative action plan that resulted from the authority's self-assessment of its operations and need to made systematic and structural change.

F. [T]he authority has not properly evaluated employee space needs in conjunction with the potential use of authority-owned buildings in addition to other cost savings opportunities. The authority acknowledges the need to evaluate its office space requirements. The authority does not understand the reference to "other cost savings opportunities," based on its discussions with the auditors, and, therefore, reserves its right to respond to this audit finding.



Casino Reinvestment Development Authority Response to OLS Audit Report of August 2, 2018

G. *We also noted internal control weaknesses in the recording of revenue, procurement, and accrual processes. As more fully set forth in this memorandum response, the authority disagrees with this conclusion.*

III. BOARDWALK HALL ROOF PROJECTS: *[T]he lapse in time between identifying the need for roof repair and replacement, and the questionable application of multiple emergency procurements, resulted in all roof work being awarded to one vendor at an additional cost to the authority of up to \$2.1 million. While the authority agrees that the aggregate cost to repair and replace the roofing system over the entirety of Boardwalk Hall was \$5.5 million plus contingencies and that the initial base bid (without contingencies) was \$3.46 million, the authority disagrees that it incurred additional costs of up to \$2.1 million. The auditors finding as to aggregate cost assumes that the original base bid would have remained static without significant change orders. The magnitude of the roofing systems' deteriorated condition was not fully appreciated until work progressed over the course of several months, with the removal of various roofing structures revealing unanticipated structural problems. The auditors' finding as to additional costs is, at best, speculative, given the actual latent condition of the roof and nature of the work.*

The authority contracts the management and operation of Boardwalk Hall to a facilities manager, who procures goods, services and materials in accordance with a purchasing protocol developed by the authority in 2014. The repair and replacement of the Boardwalk Hall roofing system was complicated by extended discussion and analysis of the propriety of preserving West Hall and/or reducing its size and scope of operation. During the period of this debate, the authority approved certain emergency repairs to the roofing system in response to significant deterioration of the roof and resulting damage to interior infrastructure and systems. These emergency repairs were accomplished in accordance with the authority's purchasing protocol and applicable law. In one instance, water leaking into the facility shorted-out electrical switchgear causing a loss of electrical power, including lighting, to Boardwalk Hall.

As part of their finding that the authority did not need to procure emergency repair services, the auditors' state, "[O]ur walkthrough of the West Hall area identified that the affected switchgear room was out of public view and only accessible by authorized personnel." The fact that the switchgear was not in view of the public and only accessible to authorized personnel does not obviate the need to make emergency repairs so that lighting and electrical service to Boardwalk Hall was assured during the public's attendance at upcoming events. Additionally, the passage of time, by itself, in this instance does not negate the need for emergent action, given the public use of the facility. To dismiss the authority's legitimate, although admittedly protracted, examination of West Hall and to suggest that restoration of reliable, safe electrical power and lighting to a State-owned building, with public invitees, does not rise to the level of an emergency, demonstrates a lack of understanding for the public purpose and use of this facility, and applies a subjective hindsight bias to authority decision-making, rather than the objective analysis required under the standards promulgated in the 2011 GAGAS.



Casino Reinvestment Development Authority Response to OLS Audit Report of August 2, 2018

IV. BEACH AND BOARDWALK HALL EVENTS: *Amendments and non-compliance with the beach and Boardwalk Hall events contract resulted in \$1.75 million in unauthorized payments and overpayments.* For the reasons outlined below, the authority disagrees with this finding.

The authority has two contracts for promoting entertainment events – one contract for the City beach (the “Beach Agreement”) and another for inside Boardwalk Hall (the “HBH Agreement”).

Under the express terms of the Beach Agreement for 2017 (as amended by Letter Agreement dated December 22, 2016), unused funds from 2016 could be available for beach concerts in 2017, subject to the “mutual agreement” of the parties. Since two beach concerts were cancelled due to weather in 2016, approximately \$1.0 million was unused and available for 2017 beach concerts, subject to agreement by the parties. The authority agreed to carry over and make available the unused funds from 2016 to 2017. Under the express terms and conditions of the First Amended and Restated Agreement dated July 12, 2017 (which covers the 2017 and 2018 seasons, terminating in March of 2019), the authority and the promoter agreed to: (i) a “minimum of three Beach Concerts” for each of 2017 and 2018, (ii) \$2.5 million per Contract Year, and (iii) additional assistance and logistical support if the authority agreed to such assistance and support. The funds paid to the promoter are consistent with the board’s approval and direction and the contract.

Under the express terms of the HBH Agreement dated March 31, 2016, joint promotion arrangements are permitted, and the promoter is entitled to the compensation called for under the agreement. The promoter produced eight events, one jointly, and, as such was entitled to be paid under its contract with the authority.

V. MISS AMERICA ORGANIZATION CONTRACT: *The CRDA did not monitor actual costs, contract deliverables, and economic impact when negotiating a second contract with the Miss America Organization.* For the reasons set forth below, the authority disagrees with auditors’ finding.

Pageant Contract Expenditures and Economic Benefits: The nature of the authority’s negotiation of the second Miss America agreement and the eventual terms and conditions thereof provided that the authority pay a fixed sum for expected costs based, in part, on actual costs incurred under the first agreement. The authority acknowledges that the Miss America Organization did not provide reports with the frequency called for under the first agreement, but the authority was able to validate costs based on the event statements. The analysis of economic impact would not have affected the authority’s decision to renew the relationship. As stated elsewhere herein, the authority’s investments are driven by policy goals and objectives as well as expectation of a projected return on investment. During the negotiation of the second agreement, the authority’s support of the Miss America competition was considered in the context of the event’s status as an iconic Atlantic City function with positive public relations and media exposure,



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at a time when the City was struggling to chart a positive image as a destination resort. As such, the authority, in the exercise of its business judgment, decided to continue its financial support for the event through the 2019 pageant.

VI. AGREEMENT MODIFICATIONS: *CRDA management materially modified an agreement, resulting in significant additional payments.* For the reasons outlined below, the authority disagrees with the auditors' finding.

The authority approved the Walk Project in 2000 and through a series of resolutions beginning in 1999 through 2004, authorized the executive director to negotiate and execute agreements acceptable to authority counsel to advance the project, which ultimately came to fruition through a series of multiple development stages. As part of the financial incentives to spur developer investment in the corridor region of the City, the authority designated an entertainment-retail district for the entirety of the proposed project area, and subsequently through a series of negotiated agreements, agreed to share incentive payments with the developer.

In third quarter of 2012, for the last stage of the Walk development, to attract a major national retailer, the authority approved: (i) a floor for collection of debt service on a note payable from the landlord to the authority, based on the retailer's sales volume, (ii) participation in a percentage of the rent payable to the landlord from the retailer, if the retailer's annual sales reached a certain threshold, and (iii) an increase to the entertainment-retail rebates paid to the developer. To-date, the retailer's annual sales have not met the threshold that would require debt service payments or participation by the authority in percentage rental. Non-recourse IAT-based casino pool bond proceeds were the source of funds for the loan to the landlord.

During the conduct of the negotiations for this final stage of the Walk Project, the authority's governing body was involved in all instances where material contractual terms were being amended. These discussions of contract terms and conditions took place in closed, executive, sessions of the board, where the governing body provided direction to authority staff, which direction was then incorporated into amendment(s) to the contractual relationship.

In its recommendations, the auditor suggests that: (i) the governing body was not involved in the negotiation of the material terms of the relationship with the developer, (ii) unauthorized payments were made to the developer, and (iii) the authority should consider tiered financing terms instead of the agreement it negotiated with the developer. The authority's governing body was involved in the discussion of material contract terms in this transaction, and the agreements signed by the executive director reflect those discussions. As such, all payments were authorized and are being made in accordance with contractual provisions. As to the financial terms of the transaction, the auditor's approach to the transaction may be more appropriate, but this finding applies subjective hindsight to authority decision-making, rather than objective analysis. Had retail sales met projections, the authority would have received full payment of its loan and/or received half of the rental. While the anticipated financial return on investment has not realized its potential, the



Casino Reinvestment Development Authority Response to OLS Audit Report of August 2, 2018

authority's policy objective has been met by its financial support for this last stage of the Walk Project.

VII. DIRECT INVESTMENT PROJECT: *The board approved an additional \$2 million direct investment project for a casino licensee without supporting documentation.* For the reasons set forth below, the authority disagrees with this finding.

Pursuant to Resolution 16-39 adopted April 19, 2016, the authority approved an amendment to increase the direct investment request of a casino licensee for a previously approved project that met the requirements of N.J.S.A. 5:12-178 of the CRDA Act. Resolution 16-39 expressly states, in pertinent part:

[the licensee] has provided further independent written and oral testimony as set forth in the market study and assessment of nongaming development at [the licensee] and its impact on Atlantic City and State of New Jersey dated January 22, 2016 by Morowitz Gaming Advisors, LLC (the "Morowitz Market Study") that the Amended Project satisfies the requirements of Section 178 of the CRDA Act and will result in new, unique destination attractions with differentiated amenities;

The April 2016 meeting minutes expressly further state, in pertinent part:

Mr. Corey Morowitz identified the economic impacts of the proposed additional amenities, and presented testimony that these new non-gaming elements satisfied the CRDA Act, in particular Section 178 therein, and the Authority's adopted Master Plan.

Based on the foregoing, the authority does not agree with the auditors' finding.

VIII. SPACE UTILIZATION: *Building assets of the CRDA should be reevaluated for employee occupancy utilization.* The authority concurs that it should reexamine its utilization of space, and is currently assessing potential changes, in particular, the relocation of its special improvement district operations to consolidate and streamline this unit and the possible relocation of project management personnel.

IX. ACCOUNTING PRACTICES: *We noted internal control weaknesses over the recording of revenue, procurement, and accruals.* For the reasons stated below, the authority agrees, in part, with the findings. As noted elsewhere in the report the Authority's previous Chief Financial Officer had recently departed. This departure, the transfer of another finance staff member out of the department and other recent retirements left the finance department understaffed during a significant portion of the period under audit, a condition only recently corrected. Additionally, some of the facts outlined in the auditors' report require clarification and correction.



Casino Reinvestment Development Authority Response to OLS Audit Report of August 2, 2018

Revenue Recording: The Authority agrees with the recommendation to establish additional controls over its cash receipts journal and has done so, as part of the planned upgrade to its accounting and financial management system and revised policies and procedures. The journal is currently password protected and is reconciled each month. Users accessing the log to perform reconciliation or review may access the log on a “read-only” basis.

The finance department has begun to make more frequent deposits of received funds. While the audit report notes that State authorities are not required to follow State of New Jersey, Department of the Treasury Circular 12-02-OMB, the authority agrees daily deposits of receipts are considered a best practice and has begun making daily deposits of funds received when warranted. However, there are instances where the authority will intentionally not deposit a check if there are potential legal ramifications in doing so, two of the specific examples identified by the auditors fit this situation. In both cases the checks were purposely held until legal questions were resolved, at which time the checks were deposited.

The audit report also identifies two items that pertained to 2015 and states that these items were not recorded until 2016. This finding is incorrect as both of these items were properly accrued at year end and therefore recorded in 2015, even though payment was not received until 2016.

The authority agrees with the recommendation to zero out the applicable inter-fund accounts on a timelier basis and will do so as part of the planned upgrade to its accounting and financial management system and revised policies and procedures.

Special Improvement District: The authority does not agree with the auditors’ finding that the recording of the identified receivable transaction was improper. The finance department directed SID accounting staff to credit the accounts receivable account for the specified amount as an offset against amounts the authority owed to the obligor of the accounts receivable. The resultant transaction properly established the year-end balance for the allowance for doubtful accounts, the year-end balance of the accounts receivable, and was reviewed and found acceptable to the authority’s outside independent financial auditors.

The authority also does not agree that it lacks a formal documented policy on the calculation for the allowance for doubtful accounts. This written policy is part of the authority’s current accounting policies and procedures manual.

Procurement and Accruals – Convention Center Division: The authority agrees that in the past convention center division management was not routinely following authority purchasing and procurement policies. The authority has addressed and resolved this lapse with the implementation of the new accounting and financial management system, which requires that all authority purchasing units utilize the same procedures and approval process for procurement, unless covered by a separate agreement approved in accordance with authority rules. The authority



Casino Reinvestment Development Authority Response to OLS Audit Report of August 2, 2018

is also redoubling its efforts to train division personnel on proper procurement policy and procedures.

The audit report states that an allocation of expense to the convention center division, "appears disproportionate". The authority disagrees with this audit finding. The allocation in question was derived by calculating a percentage based on the financial transactions created by the convention center division versus the total of all authority financial transaction for a given period. This fraction multiplied by 100 fairly represents the proportionate allocation.

As to the auditors' finding concerning the New Jersey Transit matter, the authority will continue to reserve, as a contingent liability, the purported obligation pending final confirmation of the obligation and legal review.

X. MARKETING AND COMMUNICATIONS: *Resources related to the Marketing and Communications division are not being used in an efficient and effective manner.* For the reasons stated below, the authority agrees, in part, with the finding. Additionally, some of the facts outlined in the auditors' report require clarification.

Presently, the authority's marketing and communications unit employs mostly part-time staff who work in the Visitor Welcome Centers at Boardwalk Hall and at the Atlantic City Expressway location and a small contingent of full-time personnel. With the enactment of the tourism district amendments to the CRDA Act in 2011, the principal marketing and communications activities of the former ACCVA (which was consolidated into the authority as the convention center division) were vested in the Atlantic City Alliance, a private entity supported by its member casino-licensees (the "ACA"). With an annual budget of \$30 million, the ACA developed and implemented a sophisticated campaign for the leisure tourist market, which centered around the "DO AC" theme.

In an effort to grow the stagnant convention and meeting business, in 2014, the authority outsourced its convention sales and marketing activities to MeetAC, Inc, a not-for profit organization. MeetAC absorbed some of the convention and meeting sales staff of the former ACCVA, and has been responsible for managing the authority's convention and meeting business at Boardwalk Hall and the Atlantic City Convention Center. The authority took the step to outsource convention and meeting sales and marketing after researching nationwide best practices of similarly situated public entities.

In 2016, the legislature further amended the CRDA Act, which, among other things, resulted in ACA terminating its public-private partnership with the authority to market and promote Atlantic City. By statute, ACA assets and any remaining revenues would be transferred to the authority to support the tourism district. With the casino licensees no longer funding the ACA marketing campaign, the authority is examining ways to augment its resources to reinvigorate a leisure tourism marketing effort.



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Software: The authority agrees with the auditors' finding. The procurement of the software by the convention center division marketing management and communication staff was contrary to authority procurement policy. The authority has retrained staff involved in the transaction to reinforce proper procurement procedures, and has augmented its procurement process, as part of the upgrade to its accounting and financial management system to prevent future lapses.

Visitor Welcome Center, Analytics, Utilities, Visitor Welcome Counselors: The authority concurs with the auditors' findings. The authority recognizes the need to further assess the entirety of the Visitor Welcome Center operations to determine whether this activity and its related costs are an effective and efficient use of limited authority resources. The authority notes that prior to and during the audit engagement, it has investigated consolidating the Atlantic City Expressway Visitor Center with the sister center at Boardwalk Hall, and, in conjunction with the South Jersey Transportation Authority, the owner of the AC Expressway Center, sought to solicit proposals to repurpose this center for a higher and better use. These efforts have not been successful to-date.

Restaurant Week: As part of its future support of this event, the authority will endeavor to assess whether restaurant week results in increased patronage at local Atlantic City eateries. The authority has held the kick-off gathering for this event at different venues throughout the City to promote the event and the businesses that support it.

XI. LEGAL EXPENDITURES: *Legal expense payments are not in accordance with contract terms.* For the reasons set forth below, the authority agrees, in part, with the auditors' finding.

The authority asserts its attorney-client privilege for all of its communications to and from its special legal counsel and other engaged external legal counsel. The authority has provided to the auditors all authority costs and expenses for its engagements of special legal counsel and other external legal counsel.

The authority agrees that the payment of an administrative fee was contrary to the contract with special counsel, and when identified by the auditors, promptly corrected, as noted in the auditors' report. The firm involved in this instance provided a full accounting of all cost and expenses, which was validated by the authority's finance staff, and resulted in a refund payment to the authority. As a preventative step, the authority legal and finance staff have redoubled their examination of this firm's costs and fees to validate on-going compliance with the contract.

The authority disagrees that the payment of attorneys titled as "Counsel" at the partner rate is inappropriate, or that the authority was incorrectly billed by its special counsel. As a corrective and preventative step, the authority is amending its nomenclature in its professional services



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agreements with all special counsel to include the designation of "Counsel" and establish the partner rate as the compensation rate for attorneys with such designation.

XII. PARKING GARAGE REVENUE: *Revenue generating activities are not properly monitored.* For the reasons set forth below, the authority agrees, in part, with the auditors' finding.

As a general matter, the authority recognizes the need to retrain project implementation and management personnel in their responsibilities of overall contract management, in particular, as it pertains to oversight of the revenue generating activities in the parking garage. As to the authority's lease with the university, the authority has reviewed the university's documentation in accordance with the terms and conditions thereof.

XIII. HUMAN RESOURCES AND PAYROLL: *The authority did not ensure proper communication regarding employee job responsibilities and performance, a standard procedure regarding waiver of board compensation, and compliance with employment contracts.* For the reasons set forth below, the authority agrees, in part, with the auditors' finding.

Job Descriptions and Performance Evaluations: The authority concurs with the finding, and as the auditors are aware, prior to the completion of the audit, as part of the authority's corrective and preventative action plan for human resources, the authority hired a human resources professional to lead the human resources function and to proactively address plan goals and objectives, including, upgrading of job descriptions, identifying training needs, and instituting performance evaluations.

Reduction in Force: In the first quarter of 2017, the authority took action to reorganize its workforce and consolidate certain areas of its operations. This action, taken in response to changes to the CRDA Act and the authority's mission, involved more than a reduction in force. The authority also hired skilled finance, human resources and information technology personnel, and made significant investment in its information technology platform and software systems. The authority agrees with the auditors' finding that the authority is still realizing cost savings as a result of the reorganization of its workforce.

Board Compensation: The authority agrees, in part, that a formal procedure would be helpful to address situations where a board member seeks to waive or reinstate his or her statutory compensation. As the auditors note in their finding, board member compensation is mandated by statute. During the period identified in the auditors' report certain board members waived their right to compensation, and subsequently notified the authority of their desire to reinstate their statutory compensation. The authority responded to these requests based on the timing thereof. The authority does not agree that any of the payments were improper given the statutory framework requiring such payment.



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Executive Director Severance: The authority disagrees that the payment of severance pursuant to the employment agreement with the former executive director was unauthorized without additional board action.

In accordance with the authority's bylaws, the authority's personnel and administration committee is charged with oversight of the executive director. The relevant bylaw provision, provides that the duties of the committee shall include, "(c) [t]he appointment, review, promotion, termination, suspension, discipline and supervision of the Executive Director." Moreover, the committee's decision to abide by the terms of the employment agreement and pay the severance required thereunder was reviewed with the authority's board in a closed, executive session on December 6, 2016. As reflected in the public meeting minutes of December 6, 2016, the authority board did, in fact, vote to support the committee's decision to pay the severance required under the employment agreement.

The public meeting minutes state, in pertinent part:

The Acting Chair then announced that Mr. John Palmieri would be leaving the Authority effective December 31, 2016, and that consistent with his employment agreement dated October 3, 2011, Mr. Palmieri would receive a severance equal to one-year of base salary, but without continuation of benefits. The Acting Chair shared with the Board and the public the Authority's press statement that would be released after the meeting, and further stated that action by the members was not required given the prior Board approval of an employment agreement. The members expressed support for execution of a separation and release agreement, which was part of the previously approved employment agreement signed by the Authority when Mr. Palmieri was hired in 2011. A motion in response to the Chair's request for support was made by Mr. Hill and seconded by Mr. Tolson. The Acting Chair's request for support was approved by unanimous vote of the members.

Potential Cost Savings: The authority agrees with the finding, and has already taken steps to significantly reduce payroll administration costs by engaging a new payroll vendor.

XIV. REDEVELOPMENT PROJECT: *The authority should actively monitor redevelopment projects.* For the reasons set forth below, the authority believes that it does actively monitor redevelopment projects.

The auditors identify one project, where the authority invested with the Camden County Improvement Authority ("CCIA"), a sister redevelopment agency, in the revitalization of the former Pennsauken Mart. The authority was briefed by CCIA representatives and their developers throughout the extended period of development, which spanned several years due to the several challenges faced by the CCIA, including environmental areas of concern, changing economic



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factors, and changing developer commitments. As such, the CCIA was required to rethink the ultimate uses for the site, which led to several modifications to the originally proposed project. The CCIA reviewed each of these proposed changes with the authority, and, as the auditors' report states, the project is progressing.

The authority's original investment in the project took the form of a grant, but given the passage of time, the authority and the CCIA agreed to modify the terms of the authority's investment to allow for repayment of proceeds from the sale of real estate for the project. As a result, the authority received \$3.2 million for use in the Atlantic City tourism district. Since enactment of the tourism district legislation, the authority limits its investments to projects and initiatives that support its mission in the district.

The auditors' characterization that the authority waited for an extended period for, "an apparent return on its investment," fails to recognize the authority's overarching policy objective of supporting worthy development projects, as (in many cases) an investor of last resort. Like all other redevelopment authorities, the authority is required, at times, to be a "patient" investor focused on larger policy goals and objectives rather than on the commercially reasonable return on investment expected by a private-sector creditor or equity participant.

XV. CRDA/ACCVA FOUNDATION: *The CRDA/ACCVA Foundation lacks a governing board necessary to expend the nearly \$120,000 fund balance that has been available for over three years.* For the reasons set forth below, the authority agrees, in part, to the auditors' finding.

The authority has not taken any action to rename the foundation, but has taken steps to rectify the dormant bank account, including, documenting for the bank, its right of access to account information, contacting prior foundation trustees to obtain their cooperation with transitioning governance to the authority, drafting necessary resolutions to effectuate the transfer, and working with special counsel to facilitate the authority's corrective action plan to address this finding. The authority is evaluating the accounting software, and concurs with the auditors' finding.

XVI. OBSERVATIONS

Notes Receivable Allowance: *The Authority does not have a policy to uniformly identify doubtful notes receivable.* The authority disagrees with this observation. The authority reviews notes receivable on an annual basis as part of its annual financial audit. The authority's independent financial auditors send confirmations to each note holder in accordance with their audit plan and review. The authority and its independent auditors then work together to determine the classification of all notes receivable.

Host Awards: *The Authority should evaluate the spending on the awards gala.* As set forth below, the authority agrees, in part, with the auditors' finding.



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The host awards ceremony is the one occasion when the authority and other organizations in the hospitality and tourism industry can demonstrate their appreciation for the work of dedicated service employees throughout the City. The authority, while willing to examine the efficacy of its expenditure for this event, believes that its support of the host awards is an important aspect of its mission in the tourism district.

Auditor's Follow-up Response

The Office of the State Auditor is required by generally accepted government auditing standards (GAGAS) to provide additional explanation when an agency's response could potentially cloud an issue, mislead the reader, or inappropriately minimize the importance of the auditors' findings.

Comments Related to Audit Scope

The Authority disagreed that it limited access to original documentation by using administrative staff to coordinate its responses to the auditors and that *Government Auditing Standards* 2011 Revision (the 2011 GAGAS) does not preclude such assistance. In accordance with Chapter 6, Field Work Standards for Performance Audits, Section 6.61(b) and (c) of the 2011 GAGAS, evidence obtained through the auditors' *direct* physical examination, observation, computation, and inspection is generally more reliable than evidence obtained indirectly and examination of *original* documents is generally more reliable than examination of copies. Thus, because the auditors dealt with a *significant* number of copies of original documentation and that much of this information was passed through the inspection of management representatives before being given to the auditors, we felt it necessary, in our judgement, and in accordance with Section 6.72 of the 2011 GAGAS which states that if an auditor identifies limitations or uncertainties in evidence that is significant to the audit findings and conclusions, they should apply additional procedures, as appropriate, which includes "presenting the findings and conclusions so that the supporting evidence is sufficient and appropriate and *describing in the report* the limitations or uncertainties with the validity or reliability of the evidence, if such disclosure is necessary to avoid misleading the report users about the findings or conclusions." The issue of sufficient and appropriate evidence is a matter of professional judgement by the auditor in accordance with Section 6.07 of the 2011 GAGAS. Therefore, based upon these auditing standards, it is neither a "best practice" nor deemed optimally acceptable to have audit evidence pass through management review prior to receipt by the requesting auditor. In accordance with the standards, it clearly lessens evidential matter reliability.

In addition, many attempts were made by the auditors to express the significant difference between the performance audit for which we were engaged and the annual financial audit of the Authority by its independent auditors. The scope and objectives are very different and thus the conclusions can vary significantly.