



Frederick County
Internal Audit Department

TO: Paul Dial, Parks and Recreation, Department Head
Frederick County Parks and Recreation Commission

FROM: Bert Evans, Senior Auditor

SUBJECT: Parks and Recreation Enterprise Fund Study

DATE: September 8, 2004

CC: Martin T. Standel, Director, Internal Audit
Interagency Internal Audit Authority

Internal Audit has completed the Parks and Recreation Enterprise Fund Study that was requested. This study was conducted as a non-audit service and is to provide objective information without any conclusions, recommendations or opinions. The study was performed with the same professional due diligence employed in our customary audit work.

Attached to the enclosed study is a list of research/reference materials that is being conveyed to you for your use. Please feel free to contact me if you would like to discuss any of the enclosed materials or information contained in the study.

FREDERICK COUNTY
PARKS AND RECREATION DEPARTMENT
ENTERPRISE FUND STUDY

September 8, 2004

**FREDERICK COUNTY
INTERAGENCY INTERNAL AUDIT
AUTHORITY**

**SPECIAL STUDY FOR
FREDERICK COUNTY
PARKS AND RECREATION**

ENTERPRISE FUND



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Frederick County Parks and Recreation Department Enterprise Fund Study



Frederick County
Internal Audit Department

Part I – Introduction

Background

County Code
Chapter 1-12
Parks and Recreation

The Frederick County Parks and Recreation Commission (FCPRC) consist of eight persons appointed by the Board of County Commissioners, plus a member of the Board of County Commissioners, for a total of nine members.

The function of the FCPRC is to:

- Recommend general policy relating to parks and recreation for the county;
- Establish a park and open space system for the county, consistent with the county parks and open space plan, subject to budgetary policies and appropriations of the Board of County Commissioners of the county;
- Manage properties over which the Commission has jurisdiction; and,
- Direct a program of recreation for the county, subject to budgetary policies and appropriations of the Board of County Commissioners of the county. (1959 Code, § 30-10) (Ord. 80-11-163, 4-22-1980)

Request

The FCPRC is looking at other county park operations to determine the most effective and efficient way to operate the parks program for Frederick County. In a letter dated November 6, 2003 Chairman William H. Lukens, Esq. requested “Internal Audit consider taking on the task of investigating the establishment of an enterprise fund for the Frederick County Department of Parks and Recreation.” This request was also endorsed in a December 8, 2003 memo from Commissioner Cady. Since the FY2004 schedule was full, the Chairman was advised to submit the request in April 2004 for inclusion during the FY2005 Internal Audit work planning.

Commissioner Cady requested the study in response to the audit questionnaire for the FY 2005 work planning. Paul Dial, Director of Parks and Recreation Department, contacted Internal Audit in April requesting the enterprise fund review and Chairman Lukens contacted Martin Standel when he was appointed Director of Internal Audit in May. The request was present to and approved by the IIAA at the May IIAA meeting.

Parks & Recreation Department

Currently, Frederick County Parks and Recreation Department is responsible for 14 parks and 3 recreation centers. There are 41 full time employees and the number of part-time employees can range from 40 to 100 based on seasonal needs.

Park projects are funded through the County general fund, bonds, a portion of the recordation tax and the state Program Open Space (POS) grant program.

County Recordation Tax

Per Ordinance 00-06-248, 15 percent of the recordation tax revenue is earmarked for acquisition and development of recreational parks; the revenue is recorded as special revenue.

State Grant – POS

POS state grant funds are subject to allocation by the state. Fifty percent of Frederick County share is distributed to various county municipalities and the remaining balance is earmarked 50 percent for acquisition and 50 percent for development. Funds are distributed to Frederick County on a reimbursement basis.

Objectives

Internal Audit met with William Lukens, Chairman of FCPRC and Paul Dial, Parks and Recreation Department Head on June 1, 2004 to determine the scope of the work to be performed. Agreed upon objectives were to:

- Research and provide information relative to the legal ramifications of establishing an enterprise fund for the Frederick County Parks and Recreation Department.
- Research and provide information for alternative models for an enterprise fund.

Questions to be answered

- Are there any legal obstacles?
- What authorization is required?

- What will be the disposition of revenue in excess of operating expenses?
- Who will be responsible for the administration of enterprise fund financial accountability?
- How should the enterprise fund be structured?

Methodology

Yellow Book 2.14
Nonaudit Services Provided by
Audit Organizations

Originally Internal Audit agreed to perform the work as an attestation engagement; however, upon our review of the *Government Auditing Standards* it was determined that the work performed is more appropriately classified as a *nonaudit service*.

“Audit organizations may also provide nonaudit services that are not covered by GAGAS¹. Nonaudit services generally differ from financial audits, attestation engagements and performance audits in that auditors may . . . (2) provide information or data to a requesting party without providing verification, analysis, or evaluation of the information or data, and, therefore, the work does not usually provide a basis for conclusions, recommendations, or opinions on the information or data. These services may or may not result in the issuance of a report”

The intent of our study is to provide the Parks and Recreation Department with objective information only. Internal Audit does not endorse or recommend any specific solution or model.

Internal Audit researched the issue using an *Audit List* inquiry, internet search, and interviews with accountants, park directors and others.



¹ If audit organizations provide nonaudit services, audit organizations need to consider whether providing these services creates a personal impairment either in fact or appearance that adversely affects their independence for conducting audits.

Frederick County Parks and Recreation Department Enterprise Fund Study



Frederick County
Internal Audit Department

Part II – Research

Enterprise Funds

Guidelines

Generally accepted accounting principles (GAAP) *mandate* the use of an enterprise fund when legal requirements or management policy requires that the full cost of providing services (including capital costs), be recovered through fees and charges. GAAP also *permit* the use of an enterprise fund “to report any activity for which a fee is charged to external users for goods or services¹,” regardless of whether the government intends to fully recover the cost of the goods or services provided.

Enterprise funds are used to account for services provided to the general public on a user charge basis. Additionally, enterprise funds may be used to account for any operations “where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriated for capital maintenance, public policy, management control, accountability, or other purposes.”²

When Required

GAAP also *require* the use of an enterprise fund for any activity whose principal revenue sources meet any of the following criteria:²

- **Debt backed solely by fees and charges.** If issued debt is backed *solely* by fees and charges, an enterprise fund must be used to account for the activity. This sole backing criterion encompasses debt secured, in part, by a portion of the debt proceeds themselves (reserved funds), but *not* debt that is also secondarily secured by the full faith and credit of the government.

¹ GASB Statement No. 34, paragraph 67

² GASB Codification Sec 1100.103b(1)

- **Legal requirement to recover cost.**³ An enterprise fund must be used if the cost of providing services for an activity (including capital costs such as depreciation or debt service) must legally be recovered through fees or charges.
- **Policy decision to recover cost.**⁴

Characteristics

The use of an enterprise fund as an accounting/budgeting tool does not grant additional powers to the department providing the services. The department operating the enterprise service must follow financial and managerial requirements like every other department. However, it does provide the mechanism to report clearly the portion of total costs of services recovered through user fees and the portion that is subsidized by tax dollars and grants.

Enterprise funds are financed and operated in a manner similar to private business. It is often the intent of the governing body that the cost (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed and recovered primarily through user charges; however, this is not required and it is common to encounter enterprise funds that are used to account for services where the government intends to recover only a portion of its costs through fees or user charges.

Under enterprise accounting, the revenues and expenditures of the service are segregated into a separate fund with its own financial statements, rather than commingled with the revenues and expenses of all other governmental activities. Financial transactions are reported using standards similar to private sector accounting. Revenues are recognized when earned and expenses are recognized when incurred, under a full accrual basis of accounting.

An enterprise fund provides management and taxpayers with information to:

- Measure performance
- Analyze the impact of financial decisions
- Determine the cost of providing a service(s)

³ Cost for this purpose means *all direct costs*. Thus a *legal* requirement to recover a specified percentage of costs does *not* require the use of an enterprise fund. Likewise, the exclusion of *any* direct cost (e.g., pension contributions) nullifies this requirement.

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- Identify any subsidy from the general fund in providing a service

Basic Financial Statements

Enterprise funds require three basic financial statements.

1. Statement of net assets (balance sheet) - represents the basic position of the enterprise fund.
2. Statement of revenues, expenses and change in fund net assets/equity
3. Statement of cash flows

Parks will need to work with Accounting to set up accounts and prepare the needed reports.

Advantages

1. Present the total cost of service(s) with all the direct, indirect and capital costs of providing services in a consolidated fund. This provides a mechanism whereby the general public will be able to readily identify the true cost of providing services.
2. Provide useful management information – With the consolidation of revenues and costs of the service and information on the operating performance (positive or negative) of the fund, management will be able to analyze how much user fees and charges support the service and to what extent general fund revenues are need to subsidize the enterprise fund.
3. Investment income and surplus are retained by the fund rather than closing to the general fund. The surplus, *if not appropriated*, may be used to fund operating, capital or debt service costs associated with the enterprise.

Considerations

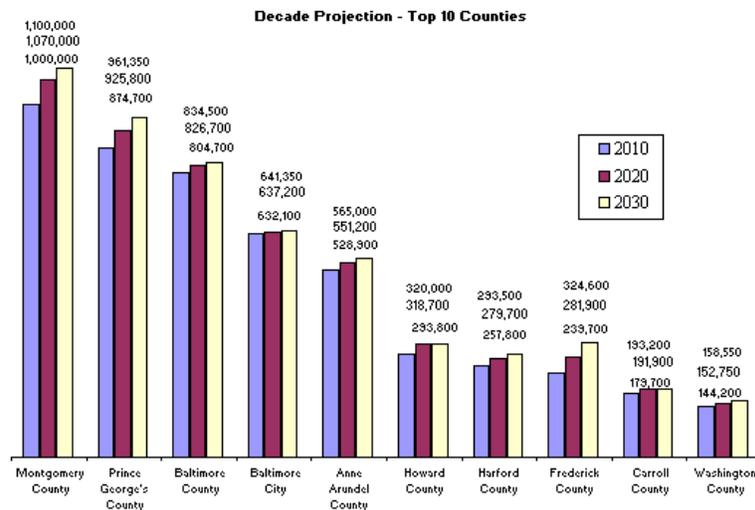
1. Philosophical Orientation - To be successful an enterprise fund requires a transition from a public service perspective to promotion for-a-profit mindset.
2. Unrealistic Expectations – The quest for total self-sustainability may never happen. Our research disclosed reduction of general fund contributions but no conclusive self-sustainability was found.

3. Analytical Skill Set – Business oriented planning and marketing skills will be needed. Special training for staff may be required. Management responsibilities will have to include aggressively seeking out resources that will generate revenue and require assertive evaluation of what is and what is not profitable.
4. Strategic Plan – To be successful a well developed business plan that includes objectives and goals both short and long term should be in place.

Frederick County

Size/Population

Frederick is the largest county in Maryland with 663 square miles and currently ranks eighth in population. State projections indicate that by 2030 Frederick County will rank sixth in population.



[figure 1]

Maryland Department of Planning

Statistics

Per US Census Bureau figures there were 70,060 households in 2000 with a 1999 median income of \$60,276. In 2000 there were 294.6 persons per square mile; in 2003 the number was 322.7. Using Maryland state population projections the number of persons per square mile will increase to 489.6 by 2030.

Population Shifts

The migration flow statistics for Frederick County for the period 1995 to 2000 [figure 2] indicate a significant inflow from Montgomery and Prince George's counties. These counties have a robust Parks and Recreation program through the Maryland-National Capital Parks and Planning Commission (MNPPC). It is reasonable to conclude that there will be an increase in the expectation of services available to citizens.

1995 – 2000
Migrations Pattern

	In-Migration From:	Out-Migration To:	Net Migration
Maryland Counties			
Montgomery	11,165	3,248	7,917
Prince George's	1,994	847	1,147
Howard	1,302	793	509
Anne Arundel	959	511	448
Baltimore City	866	485	381
Carroll	1,627	1,275	352
Baltimore County	984	691	293
Washington	1,402	3,118	-1,716
Wicomico	20	260	-240
Allegany	131	251	-120
Cecil	29	142	-113
Other MD Counties	1,014	694	320

[figure 2]

Source: US Census Bureau and Maryland Department of Planning

MNPPC

Montgomery and
Prince George Counties

The Maryland - National Capital Park and Planning Commission is a bi-county agency empowered by the State of Maryland in 1927 to acquire, develop, maintain and administer a regional system of parks within Montgomery and Prince George's Counties, and to prepare and administer a general plan for the physical development of the two counties. In addition, the Commission gained responsibility for the public recreation program in Prince George's County in 1970.

Montgomery County Recreation offers hundreds of classes, clinics, workshops for all ages and interests, ranging from arts, crafts, exercise, fitness, dance, music, tiny tots, and special interests such as bridge, dog obedience, photography, sailing, and many more.

Challenges

Frederick County's Parks and Recreation Department faces significant challenges in the next 25 years that include:

- The changing demographic make up of the County (figure 2)
- Escalating land prices that make purchases of opens spaces for parks ever more difficult and costly
- Increase cost of goods and construction and as a result the development of new facilities for parks and recreation are more expensive to develop and maintain.

Future for Park and Recreation Programs

The biggest hurdle to building a new facility or enhancing existing resources is money. Traditional funding may no longer be able to completely support current and future needs of the Parks and Recreation Department. Alternative funding will likely be a primary revenue generator for parks and recreation agencies in the future.

Internal Audit's research disclosed a variety of funding alternatives and some are included for consideration.

Trends and Alternative Funding Methods**Fees vs Taxes**

Appendix A

Clearly amenities like parks and recreation programs benefit property owners due to rise in property value whether or not they make use of these services. Therefore, a mix of tax financing and user fees is appropriate when some of the benefits accrue to particular individuals, while other benefits are for the community as a whole.

By and large taxes (e.g. income, sales, property) are clearly a payment for general government services unrelated to how much of the services the taxpayer may use. In the case of fees, on the other hand, many are clearly a *quid pro quo* with the citizen paying a fee for a particular service.

The problem of relying solely on tax financing for services is that those services may benefit non-taxpayers or a special interest group(s) who will demand more and better services because they do not have to pay for the services. If everything is paid for with taxes, those who are vocal or organized or persistent will compel others to pay for services to benefit their special interest.

Analysts have defined two criteria by which to judge when a public service is a good candidate for user-charge funding.

- Service must have readily identifiable users who must benefit substantially more for the service than nonusers.
- It must be possible to ensure that nonusers can be excluded from the benefits of the service.

Where it is possible to clearly identify those who benefit, those individuals should pay an appropriate share of the cost, even though it is not always easy to determine exactly what that share should be. Therefore, when benefits are confined to an identifiable group, the larger share of the cost should be borne by that group rather than the taxpayers as a whole. Fees and user charges provide a mechanism to target actual users of services.

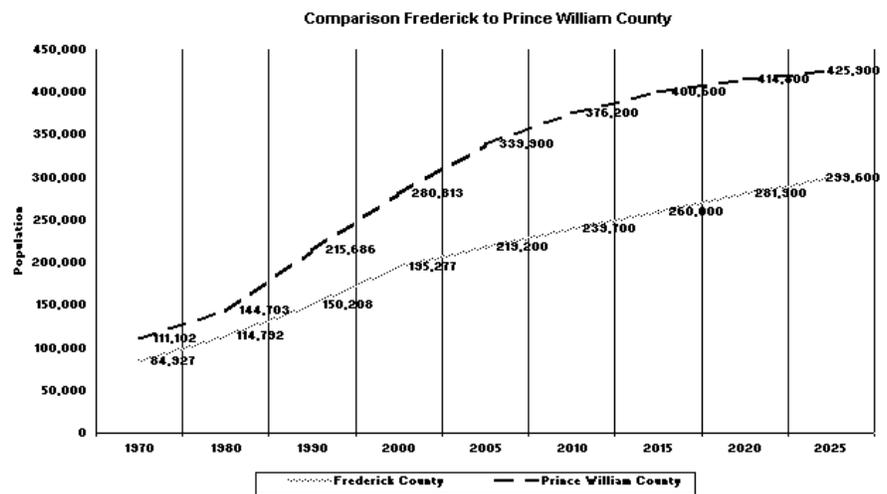
User fees can also serve as a source of feedback to park and recreation districts as they try to determine which facilities and services are truly in demand. User fees should reduce a facilities reliance on tax dollars.

Example of Fees vs. Taxes

Prince William County, VA

Appendix B – 7

Frederick County’s position is similar to that of Prince William County, Virginia. In the 1970s, the population was approximately 111,000 and the park authority had two parks, a few wooded areas and ball fields, and some arts and craft programs. By 1996 the population had more than doubled and with the resulting growth, the demand for facilities had grown dramatically. [figure 3]



Source - US Census

[figure 3]

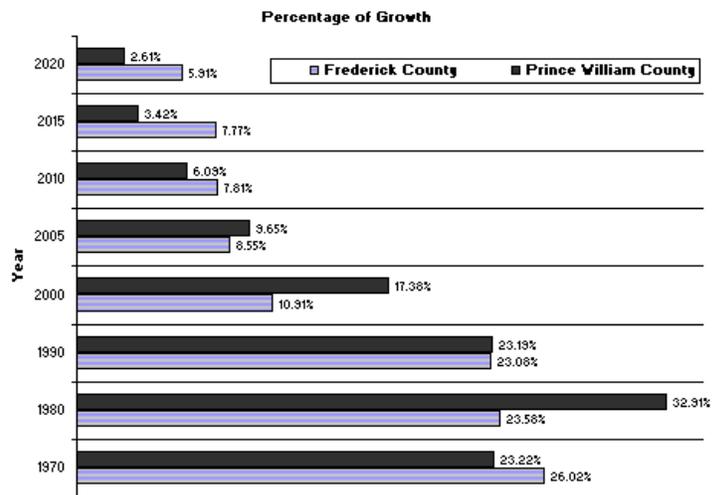
Solution

In the 1990s Prince William County was faced with population growth, an increased demand for facilities and political pressure to keep property taxes from rising. To answer these challenges Prince William County began to implement a fee for service system.

www.pwcparks.org

In 1993 taxpayers funded 68% of the parks and recreation budget and today less than 50 percent is funded by the general fund. In spite of the reduction in general fund contributions the park and recreational options for citizens of Prince William County have expanded significantly. Services in Prince William County include golf courses, water parks, fitness resources, recreation facilities and parks.

Frederick County’s population is projected to reach 300,000 in the next twenty years and during that time Frederick County’s percentage of growth will exceed that of Prince William’s county by 2010 [figure 4].



[figure 4]

Source - US Census

Partnerships

Partnership is a method whereby two or more organizations working together can accomplish something that either party alone is unable or unwilling to do. Many park districts are now beginning to see the possibility of offering outdoor recreation within their program without assuming the responsibility for organization or staffing. There is a definite advantage of a partnership in that the partners share risk, operational costs, responsibilities and asset management based on the strengths and weaknesses of each partner.

Partnerships come in many shapes and forms, i.e., institutional, corporate, non-profit, developer partnerships, community partnerships, etc.

Partnership can range from informal agreements about shared resources to complex legal agreements involving significant or in-kind resources. Each is unique and most change over time. Partnerships allow for expanded services while controlling cost to the governmental general fund.

<http://www.pgparcs.com>

Prince George's County, Maryland offers three partnerships:

The 94th Aero Squadron Restaurant

Located adjacent to College Park Airport and College Park Aviation Museum, the 94th Aero Squadron Restaurant is an aviation theme restaurant which offers great views of the airport's runway to diners, a fine selection of good food, and a fun dining atmosphere.

Prince George's Stadium

Home to the Bowie Baysox, Class AA affiliate of the Baltimore Orioles this minor league baseball stadium is the result of a cooperative venture between Maryland Baseball Limited Partnership and The Maryland-National Capital Park and Planning Commission.

The Garden's Ice House

Opened in 1996 on land owned by The Maryland-National Capital Park and Planning Commission, The Gardens Ice House is owned and managed by Top Shelf Development Company. This cooperative venture between the public and private sectors has resulted in the construction and operation of this year-round ice-skating complex within Fairland Regional Park.

Example of Partnerships

Jackson County, OR Gerry Douglas, Assistant Director, Jackson County Roads, Parks and Planning provided information on what they view as a successful enterprise fund operation.

Gerry has provided us with copies of several lease and concession agreements they use and these are included in the research materials. Also included are the emails with more details on the program and analysis spreadsheets, program materials and brochures. [Appendix E]

History

Originally several parks operated under an enterprise fund and the balance were under the general fund. The mixing of funds resulted in problems in record keeping and in 1992 the decision was made to place all the parks under an enterprise fund.

Jackson County's management has elected to operate each park as a separate business and at the end of each fiscal year an analysis is performed to determine whether or not each park has made or lost money. The overhead is allocated based on a percentage of total expenditures. Revenues are recorded where earned and any shared revenues are allocated based on total expenditures per park. They have found this to be the best management tool for trying to manage and ensure that parks pay for themselves.⁵

Although not entirely successful – some parks generate big surplus due to exceptional revenue generating capacity and some parks lose money every year – they feel that a certain level of success has been reached. They report that prior to the reorganization the parks program received about \$1.5 million in general fund support for a \$2.5 million program. Today the parks program receives about \$193,000 in general fund support in a budget of about 2.3 million dollars.

Privatization

Jackson County had also privatized operations of several parks using leases or concession agreements. The county is paid a percentage based on the **gross income**. To be successful partnership policies must be carefully prepared and should address the specifics of each partnership. In many cases the success or failure may be determined by the way contracts are worded. Care must be taken to cover as many contingencies as possible.

Sponsorships

Sponsorships can also be used to augment revenues for parks and recreations. Sponsorships can take a number of forms from corporate to private.

Corporate Sponsorships – Business can pay a fee for access to Parks markets, e.g. scoreboard advertising, exclusive soft drink 'pouring rights', etc.

Sponsorships are often used for special programs or events.

⁵ Excel spread sheets on disk with support materials

Park Trust or Foundation

Money is raised from tax-exempt, non-profit organizations established with private donations in promotion of specific causes, activities or issues.

Private companies and community organizations contribute funds or in-kind donations as long-term commitments to the community – gifts or planned giving could be directly funneled into a “Parks Trust”

Mandatory Parkland Dedication Ordinances

Mechanism whereby residential developers are required to provide land or a fee per lot for parkland. Non-residential developers pay a fee per commercial acre that is developed.

Landscape Maintenance Districts

Basically a tax these are special assessment districts that established a fund for a specific area. These are established via citizen vote and use of the funding is restricted to and for that district.

Revenue Bonds

Pay as you go may not be suitable with the increase cost to acquire, develop and build new facilities, and/or improve existing parks. This type of bond can be used for capital projects that will generate revenue for debt service where fees can be set aside to support repayment of the bond.



Frederick County Parks and Recreation Department Enterprise Fund Study



Frederick County
Internal Audit Department

Part III Summary

QUESTIONS TO BE ANSWERED:

1. **What is the legal feasibility for establishing an enterprise fund in Frederick County?**

There is no legal restriction for establishing an enterprise fund; however, at this point in time, Frederick County Parks and Recreation Department does not have any facility or program that would require an enterprise fund.

Funding has been approved for a consultant to research and prepare a proposal for the development of a revenue generating facility in the future. If such a facility is developed and policy requires its cost to be recovered by fees then it will require an enterprise fund for accountability.

2. **What authorization is required?**

Approval of the Board of County Commissioners will be required and the Parks Department and the Accounting department will have to set up the accounting requirements.

Current County Code requires that funds generated by Parks and Recreation become general fund revenue. Currently, the Parks Director and the County Attorney are evaluating revisions to the County Code for Parks. Internal Audit has discussed with Parks and the County Attorney issues pertaining to general revenue and debt financing.

3. **What will be the disposition of revenue in excess of operating expenses?**

Enterprise fund revenues in excess of operating expenses are retained by the enterprise fund. Management will assess what will be required as reserve for maintenance of the facility. Excess revenue can be transferred to other funds.

4. **Who will be responsible for the administration of enterprise fund financial accountability?**

Parks Department with assistance from Accounting will be responsible for reporting.

5. **How should the enterprise fund be structured?**

A park, charging fees to users, generating revenue and, expected to be self-sufficient will have to be set up as an enterprise fund. Over time, if more than one facility is developed with these characteristics, management will probably set up each facility as separate enterprise fund. However, Parks may at that time decide to bring the entire Parks and Recreation Department under one enterprise fund and perform analysis of each facility.