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## **Internal Auditor's Report**

The County Council and County Executive of Wicomico County, Maryland:

Pursuant to Section 305(D) of the Wicomico County Code and Council Resolution No. 106-2017, the Office of the Internal Auditor (IA) conducted a review of Airport Fuel Flowage Fees program. A report is submitted herewith. The purpose of the consultation was to gain an understanding of the Airport Fuel policies and procedures.

At the request of the Airport Management and County Administration, IA conducted the consultation with due professional care, and we planned and performed the consultation to obtain an understanding of the current practices, analyze financial considerations, and perform risk assessment for the Airport Fuel program.

IA extends our appreciation to management and staff from the Salisbury Airport and hangar lessees for their assistance.

Respectfully submitted,

*J. Stephen Roser, CPA*

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Internal Auditor

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## Consultation Report

### Background

The purpose of this exercise was to perform an audit of the Fuel Flowage Fees paid by hangar lessees to Salisbury Airport. Four lessees have agreements that are subject to these fees. Lessees provide reports and payments to the Airport monthly from each hangar. The Airport's former accountant had been working on evaluating this program and provided us with a spreadsheet spanning from July 2012 through June 2017 that detailed fees paid by month over that period. One point of focus for this consultation was to evaluate internal controls and methods of fuel usage verification in order to ensure the accuracy of the monthly reports provided by the fuel users.

### Objectives

The objectives of the project were to:

1. Gain an understanding of the aviation fuel system for SBY Airport
  - a. Determine the nature and substance of the systems in place
2. Evaluate internal control over required payments to the Airport from fuel users and distributors
3. Evaluate adherence to internal controls
4. Make recommendations (if appropriate)

### Scope

Objectives and methodology were adjusted as information was gathered. The audit period that was examined on a test basis was FY2013 to date. The Scope was open ended. Observations, interviews, and Inquiries with appropriate personnel (including selected vendors) were conducted. The auditors performed inspections of selected documentation including any working papers provided by the Airport accountant, billing records, accounting records, contracts in force, and vendor records.

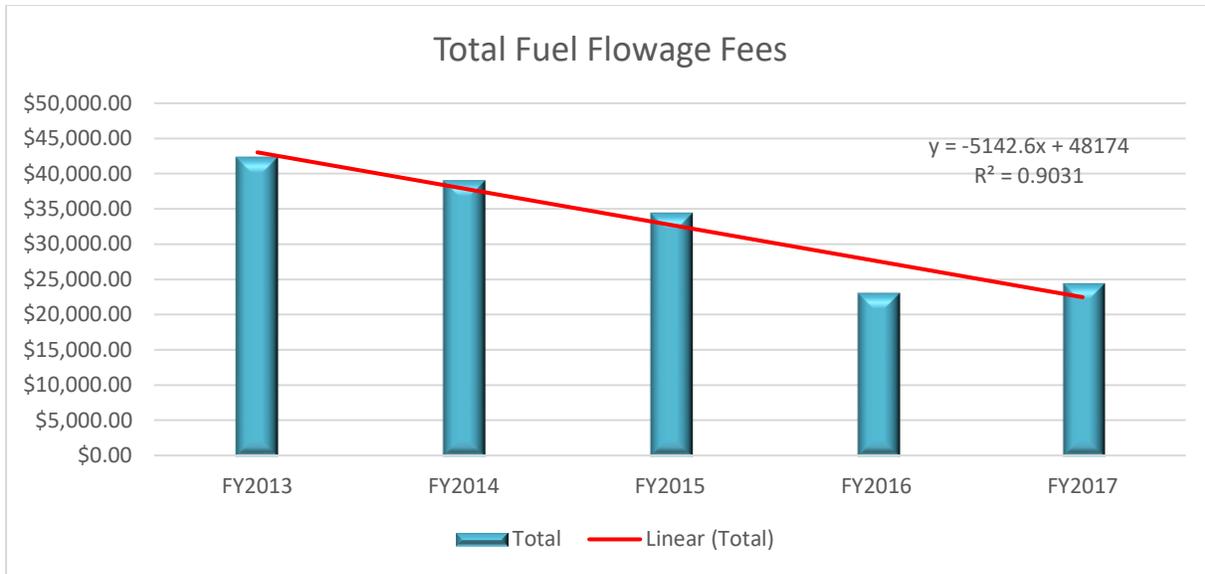
### Fuel Flowage Fee Rate

The County charges the lessees two rates for fuel usage, depending on whether the fuel was used internally or sold at retail (externally). Currently, only one hangar sells fuel externally, the other three only use fuel for their own purposes. The agreed-upon rates between the Airport and the hangar lessees are as follows:

- 1.25% of wholesale price per gallon dispensed for internal aircraft
- 2.00% of retail price per gallon sold at retail

Using a percentage fee structure ties the revenue of the flowage fees directly to the market price (wholesale or retail) for fuel. This in turn creates volatility. As illustrated in the following chart, revenue over the past five years has declined significantly:

*(Continued)*



The total fees collected in 2013 were \$42,359. In 2017, the fees dropped to \$24,556. According to vendor interviews, fuel usage did not change significantly during the same period. The drop in revenue therefore may be attributed (in part) to the decrease in fuel costs. Using data from one hangar that reported both price and gallons, fuel costs per gallon dropped from \$3.45 in 2012 to \$1.66 in 2017. Associated usage increased slightly by 1.75% and the Airport fee collections dropped 51%.

### Fee Structure Compliance

The two hangars that used/sold more fuel had dramatic decreases likely caused by fuel pricing declines. Perdue and AG Atlantic, however, stayed mostly flat. Upon analyzing a sample monthly reports and a spreadsheet provided by the Airport, it seems that those two hangars are not paying 1.25% of the wholesale price per gallon, they are instead paying 1.25 cents per gallon (regardless of the cost). The auditors verified this practice via interviews with the lessees. Please see Appendix I Fuel Flowage Fees by Hanger for more information.

### Report Data & Structure

A matrix containing some of the auditor’s findings follows:

	Is the contract language clear as to pricing?	Reporting Detail	Data Source	Rate Calculation
AG Atlantic	No	Gallons	Pilot Records	Per Gallon
Bayland	Yes	None	QuickBooks	Percentage of price per gallon
Perdue	Yes	Gallons	Pilot Records	Per Gallon
Piedmont	No	Gallons/Cost	N/A	Percentage of price per gallon

The contracts that we reviewed were not uniform and, in one example, most of the language was contained in an original draft from 1978. In the documentation provided to the Auditors, two contracts had sufficient language to support the fee structure and two did not. This does not mean that documentation does not exist elsewhere. For

example, the Piedmont contract reviewed lacks the supporting language, but the company follows the prescribed percentage fee structure.

Reporting detail varies greatly among the four hangars. AG and Perdue provide information on how many gallons they used, Bayland does not provide any information, and Piedmont provides both the cost of the fuel and the amount of gallons they used. The system for calculating the usage is based on the honor system, internal controls are pilot records and QuickBooks records, but no tangible or independent meters or invoices are available.

## Conclusion and Suggestion

There is some confusion among the hangars concerning the fee structure, as well as, how much information should be submitted to the Airport. The hangars have been following different perceived understandings of the fee structure for at least five years and Airport Management should review the contracts with the lessees to clarify any misperceptions about the fees or rates that are expected. Further, management could explore the recommendations and findings below to strengthen and improve the program for both the Airport and the hangar lessees.

## Findings and Recommendations

We present these findings and recommendations to highlight topics with the Airport Fuel program as a possible course to make the program more controlled and efficient.

### Price-based Fee Rate Structure Internal Control Concerns

The implemented program allows the hangar tenants to calculate and pay required fees to the Airport. We found no mention of how the price of fuel is accounted for (FIFO, LIFO, average). The two hangars that pay with the percentage method simply report a price and pay and their percentage based upon that price. If the Airport were to adopt a system that validated usage by reading a meter, it would prove quite difficult because fuel is transferred to tank trucks to deliver fuel to the runway and the truck may not be emptied on that trip. In addition, trucks are subject to monthly recirculation testing. Fuel is run back through the system, which also changes the meters. Tracking these events would be cumbersome on all parties involved. With that in mind, if the Airport stays with the price-based fee rates, then the auditors recommend establishing internal controls to validate the hangars usage and not to rely on the current honor system.

### Gallon-based Fee Rate Structure

Currently, the fees paid to the Airport are based on the cost of fuel and as illustrated above have negatively impacted the revenue from the program. The Airport could consider charging a flat rate per gallon instead of tying it to the market price of fuel. This structure could prove to have several benefits:

- Revenue to the airport is more stable, tied to usage instead of price of fuel
- Fees could be assessed based on fuel delivery instead of usage
- The Airport could potentially use third-party invoices as an internal control measure
- Billing process would be easier and more transparent for all stakeholders

### Historical Reports

One concern presented to us was underpayment from the hangars over the past several years. It is likely that AG Atlantic and Perdue have been underpaying because they are only paying 1.25 cents per gallon. That would equate the cost of the fuel to only \$1.00/gallon if they were using the proper formula. With that in mind, they paid a combined \$5,403 over a 5-year period. Even if (hypothetically) they underpaid by 60%, they would owe \$8,104 to the County. Our office would not recommend putting forth the resources to try to recoup this relatively small

amount. Instead, we would encourage management to work with the hangar tenants to better understand their contracts and ensure the proper calculation of future payments using consistent methodology.

### **Management Response**

*As it is draft, I am assuming you have not completed the audit. One of the main requirements of this audit was to determine the fuel flowage and price at Bay Land and if they had calculated the resale fuel cost to the public and our fuel flowage rates properly. Will that still be accomplished - since this is our highest fuel-flow vendor and we have the most to lose, and it is resale, we need to know how much we have lost or gained?*

*I do agree with your recommendation of a price per gallon. The industry as a whole has gone to the .04-.08 cents per gallon. We pump a million+ gallons a year at SBY so getting a proper accounting system is imperative. We do not have a standardized or systematic method of collection.*

### **Auditor's Reply**

The requirements of the audit, as stated in the scope and objectives, were to understand the protocols, weigh in on internal controls, and make recommendations. The auditors tested the Bay Land billing submission against Bay Land QuickBooks records from December 2017. We recalculated all the numbers and found no variation. The scope of annual Bay Land payments to the county for fuel tax (according to spreadsheets provided by management) ranged from \$23,901 in FY2013 to \$15,014 in FY2017. The auditors are of the opinion that the possible return of funds to the county based on a project of the magnitude described does not warrant the cost of the project. Additionally, given the subjective component of determining fuel pricing, the auditors recommend that Airport management apply future efforts toward the creation of a more accountable system as described in our findings and recommendations.

### **Auditor's Closing Remark**

The Wicomico County Office of the Internal Auditor would like to thank the Airport staff and the hangar lessees for their candid assistance with this project.

### Appendix I - Fuel Flowage Fees by Hangar

