

Memorandum



CITY OF DALLAS
(Report No. A11-006)

DATE: February 11, 2011

TO: Honorable Mayor and Members of the City Council

SUBJECT: Audit of South Dallas Fair Park Trust Fund ¹

The South Dallas Fair Park Trust Fund (Trust Fund) continues to experience difficulties in managing grant and loan programs according to Trust Fund Policies and Guidelines. Specifically:

Loan Guidelines Not Followed

The Trust Fund made exceptions to the Trust Fund Loan Underwriting Guidelines (Guidelines) for all three loans issued during the audit period. Instead of following the Guidelines, the Trust Fund qualified the three borrowers for higher loan amounts by increasing the value of the borrowers' pledged collateral to 110 percent of the Dallas County Appraisal District (DCAD) value. The Guidelines state the Trust Fund should use the lesser of 90 percent of real estate cost or 80 percent of the DCAD appraised value with improvements minus any outstanding encumbrances.

Background

The Trust Fund is administered by the Department of Economic Development (ECO). The Trust Fund facilitates economic and community development in the South Dallas Fair Park community through grants and loans that support:

- Business and economic development initiatives
- Housing and community development
- Community service programs

The Trust Fund authorized 18 grants totaling \$267,926 and three loans totaling \$169,484 during the audit period. (October 1, 2009 through July 31, 2010).

Source: ECO

Granting exceptions to loan applicants may result in additional monetary losses to the City of Dallas. (As of July 31, 2010, nine Trust Fund loans with pay-off amounts totaling

¹ The audit was conducted under the authority of the City Charter, Chapter IX, Section 3 and in accordance with the Fiscal Year 2010 Audit Plan approved by the City Council. The audit objectives were to determine whether the Trust Fund adequately reviewed grant and loan applicants' information to determine eligibility, exerted sufficient oversight and collection efforts for current and delinquent loan accounts, properly reimbursed grantees' expenditures, and accurately and timely recorded financial transactions in the City's accounting system. The audit scope included Trust Fund grants and loans from October 1, 2009 to July 31, 2010. This performance audit was conducted in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based upon our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. We interviewed ECO personnel, reviewed Trust Fund policies and guidelines, City Council Resolutions 06-1833 and 07-2962, grants, loans, and the associated documents, and analyzed certain transactions.

approximately \$254,103 were in default. According to Trust Fund management, these loans were made prior to revisions of the Trust Fund Policies and Guidelines related to loan underwriting.) Previous Trust Fund audits noted that the Trust Fund did not have adequate Loan Underwriting Guidelines to help Trust Fund personnel evaluate a loan applicant's ability to repay the loan and to document the analysis that supports the loan approval.

Recommendation I

We recommend the Director of ECO ensure that Trust Fund Guidelines are followed to support loan approval decisions.

Loan Payments Not Accurately Monitored

The ECO did not accurately monitor the timeliness of loan payments. As a result, ECO assumed the first loan payment from a borrower was paid early and incorrectly recorded the entire loan payment to principal. The promissory note signed by the borrower indicated that the first loan payment was due on May 1, 2010 and not June 1, 2010 as shown on the ECO loan amortization schedule.

In addition, ECO was not aware that this borrower had made four loan payments that were 29 to 33 days late and \$333.50 in late fees were due. The promissory note stated:

"If any payment of principal or interest hereon is not paid within ten (10) days of the date when the same is due, there shall be due and payable, at the option of the Lender, in addition to such installment and interest thereon, a late charge equal to five percent (5%) of the amount of such defaulted installment."

Trust Fund Policies and Guidelines also state: *"Late fees for loan payments will be \$25 per occurrence. A late fee will be assessed after a payment is 10 days past due."* This does not appear to align with the provisions of the promissory note.

Recommendation II

We recommend the Director of ECO ensure that the Trust Fund monitors the timeliness of loan payments. We also recommend the Director of ECO ensure late fees are collected from the delinquent borrower and that promissory note provisions for late fees align with Trust Fund Policies and Guidelines.

Applications Approved Without Required Documents

Five of the 18 judgmentally sampled grant applications received grants without submitting all of the required application documents. For example, the Trust Fund signed a contract for a \$5,000 Challenge grant with the South Dallas Cultural Association without obtaining the following required documents: (1) Budget Form B; (2) Unaudited financial statements; (3) Articles of Incorporation; (4) Tax certificates; (5) Organizational chart; (6) Contract

signing authority; and (7) a Conflict of Interest Statement. According to ECO, the Trust Fund Policies and Guidelines do not currently reflect the actual grant and loan operational requirements.

The Trust Fund application instructions for the Community Based, Challenge, Public Safety, and Special Development grants state: "*Applications must be full and complete for funding consideration. All applications must contain...*" Then, a specific document list is provided for each grant type.

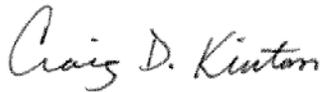
Recommendation III

We recommend the Director of ECO ensure that before the grant applications are considered by the Trust Fund Board and Trust Fund for final approval, all grant applications are complete, including all documents required by Trust Fund Policies and Guidelines. We also recommend the Director of ECO ensure that Trust Fund Policies and Guidelines are revised to align with current grant and loan operational requirements.

The ECO has responded to the recommendations resulting from the *Audit of the South Dallas Fair Park Trust Fund* (See Attachment I). We appreciate the cooperation and assistance we received from ECO, City management, and staff during this audit.

If you have any questions or need additional information, please contact me at 214-670-3222 or Carol Smith, Assistant City Auditor, at 214-670-4517.

Sincerely,



Craig D. Kinton
City Auditor

- C: Mary K. Suhm, City Manager
Thomas P. Perkins, City Attorney
A.C. Gonzalez, Assistant City Manager
Karl Zavitkovsky, Director – Office of Economic Development
Lee McKinney, Assistant Director – Office of Economic Development
Leo Hicks, Trust Fund Manager
Robert L. Perry, II, Trust Fund Board Chair

Management's Response

Memorandum

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FEB 09 2011

City Auditor's Office



DATE: February 9, 2011

TO: Craig D. Kinton, City Auditor

SUBJECT: Response to Audit Report: Audit of South Dallas Fair Park Trust Fund

Our responses to the audit report recommendations are as follows:

Recommendation I:

We recommend the Director of ECO ensure that Trust Fund Guidelines are followed to support loan approval decisions.

Management Response / Corrective Action Plan

Agree Disagree

- Trust Fund Policies and Guidelines have been modified and approved by the Trust Fund Advisory Board (1/8/11)
- ECO will follow loan guidelines. Exceptions will be communicated and fully documented.
- All loans made during the review period are paying as agreed
- Defaulted loans originated 1993 through 2007. \$240K transferred to CAO in 2007, deemed uncollectable. Referenced defaults are unrelated to the review period

Implementation Date

Immediately, upon CAO review of revised Policies and Guidelines

Responsible Manager

Trust Fund Manager, Leo Hicks
ECO AD, Lee McKinney

Recommendation II:

We recommend the Director of ECO ensure that the Trust Fund monitors the timeliness of loan payments. We also recommend the Director of ECO ensure late fees are collected from the delinquent borrower and that promissory note provisions for late fees align with Trust Fund Policies and Guidelines.

Management Response / Corrective Action Plan

Agree X Disagree

- Loan in question is current and paying as agreed. Delinquency resulted from a lost payment
- Past due payments resulted from internal City issues that resulted in late discovery of lost payment
- ECO takes responsibility for late discovery of a lost payment and exercised option to waive late fees
- Late fee amount in the Promissory Note has been aligned with revised Policies and Guidelines
- Trust Fund Manager will monitor loan payments monthly

Implementation Date

Immediately, upon CAO review of revised Policies and Guidelines

Responsible Manager

Trust Fund Manager, Leo Hicks

Recommendation III:

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Management Response / Corrective Action Plan

Agree X Disagree

- Trust Fund Policies and Guidelines have been revised (1-01-11) to identify and differentiate minimum documentation required for Board consideration for grant approval and necessary documentation required for funding disbursements.
- ECO will follow revised guidelines

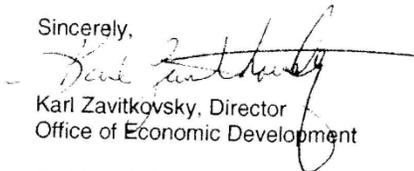
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Immediately, upon CAO review of revised Policies and Guidelines

Responsible Manager

Trust Fund Manager, Leo Hicks
ECO AD, Lee McKinney

Sincerely,


Karl Zavitkovsky, Director
Office of Economic Development

C: Mary Suhm, City Manager
A.C. Gonzalez, Assistant City Manager