

# Memorandum



CITY OF DALLAS  
(Report No. A10-006)

DATE: December 11, 2009

TO: Honorable Mayor and Members of the City Council

SUBJECT: Final Report – Follow-Up of Audit Recommendations, Office of Economic Development, South Dallas Fair Park Trust Fund (October 1, 2006 to May 31, 2008)

The Office of Economic Development (ECO) has responded to recommendations resulting from the *Audit of the South Dallas Fair Park Trust Fund* (SDFPTF). Attachment I provides detailed information for the four recommendations included in this audit<sup>1</sup> report.

The SDFPTF Loan Underwriting Guidelines were not revised to provide sufficient criteria to help Trust Fund personnel evaluate an applicant’s ability to repay the loan and to document the analysis that supports the loan approval. In addition, the Loan Delinquency Management/Reserve Guidelines (Guidelines) are still not consistently followed. These Guidelines are intended to ensure the SDFPTF makes sufficient collection efforts to reduce the number of delinquent loans in its loan portfolio. During the audit period, June 1, 2008 through May 31, 2009, there were two delinquent loans where the SDFPTF was still receiving reduced or sporadic payments. (Note: Since 1992, the SDFPTF has authorized 43 loans totaling \$1,076,739).

### Summary of Follow-up Audit Results

Fiscal Year Audit Report Issued	Number of Report Recommendations	Recommendations Implemented	Recommendations Partially Implemented	Recommendations Not Implemented	Did Not Evaluate
2008	4	1	0	2	1 *

The following prior year recommendation was not evaluated\* because the Special Collections Unit’s transition to Pay1 for SDFPTF transaction processing was not completed during the audit period:

- The Director of ECO work with the Office of Financial Services Special Collections Unit to obtain the information it needs to properly monitor the timeliness of deposits and accounting transactions.

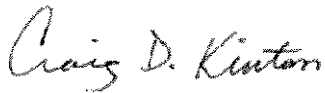
<sup>1</sup> This audit was conducted under the authority of the City Charter, Chapter IX, Section 3 and in accordance with the Fiscal Year 2009 Audit Plan approved by the City Council. The audit objective was to verify that management has taken corrective action(s), the corrective action(s) are achieving the desired results, or management has assumed the risk of not taking corrective action(s). 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 on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. We interviewed ECO department personnel, reviewed SDFPTF policies and procedures, City Council Resolutions 06-1833 and 07-2962, grants, loans, and the associated documents, and analyzed certain transactions.

The evaluation of this recommendation will be considered for subsequent audits of the SDFPTF.

Management has accepted the risks associated with not implementing two recommendations. The City Auditor's Office will not conduct any further follow-up on three of the four recommendations, but will consider the risks in determining future audit coverage as part of the annual audit plan. Although there were no new recommendations made, ECO management provided a written response to this follow-up audit (see Attachment II).

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

Attachments

- C: Mary K. Suhm, City Manager
- A.C. Gonzalez, Assistant City Manager
- Karl Zavitkovsky, Director – Office of Economic Development
- Lee McKinney, Southern Dallas Assistant Director
- Leo Hicks, Trust Fund Manager

**ATTACHMENT I**

Audit Report	Audit Issues	Audit Recommendations	Audit Follow-Up Results
<p><b>Audit of the South Dallas Fair Park Trust Fund (November 21, 2008)</b></p>	<p><b>Underwriting Guidelines Do Not Provide Sufficient Loan Evaluation Criteria</b></p>	<p>- Revise the loan underwriting guidelines to provide sufficient criteria for Trust Fund personnel to evaluate an applicant's ability to repay a loan and to establish a basis or sound rationale for the evaluation and ensure that the evaluation is documented.</p>	<p><b>Not Implemented.</b></p> <p>Management disagreed with this recommendation. According to management, Underwriting Guidelines for the Trust Fund were established to create access to capital for borrowers who will not qualify under conventional guidelines, while giving the Trust Fund a high probability of repayment.</p> <p>The Loan Underwriting Guidelines in the SDFPTF policies and procedures have not been revised. For example, the current Loan Underwriting Guidelines do not include clear and measurable criteria for consistent loan evaluation and file documentation. According to the Trust Fund Manager, he has revised certain loan evaluation procedures; however, these procedures were not included in the loan underwriting guidelines. Further, these new procedures were not evaluated because the SDFPTF did not issue any new loans during the audit period.</p>
	<p><b>Trust Fund Loan Delinquency Management/Reserve Guidelines Are Not Consistently Followed</b></p>	<p>- Ensure that Trust Fund personnel follow the Loan Delinquency Management/Reserve Guidelines, including routine follow-ups with the City Attorney's Office (CAO) to determine when legal intervention has been exhausted so that the accounting records are properly updated to reflect loan collectability.</p>	<p><b>Not Implemented.</b></p> <p>The Guidelines require SDFPTF personnel to:</p> <ul style="list-style-type: none"> <li>• Call each borrower that was more than 10 days past due on a payment</li> <li>• Send a written request for payment within 30 days of the first phone contact</li> <li>• Mail a certified letter requesting that the loan be brought current within 15 days from the date of the letter</li> </ul>

Audit Report	Audit Issues	Audit Recommendations	Audit Follow-Up Results
			<ul style="list-style-type: none"><li>• Document all collection activity in the borrower's file</li><li>• After 60 days of delinquency with no response and/or plan to bring the loan current, notify the City Attorney (CAO) and request that legal action be taken</li></ul> <p>According to SDFPTF personnel, these procedures were not followed because the borrowers have been in a delinquent status for an extended period of time. (Note: The SDFPTF works with the borrowers that are making payments even if the payments are late or for amounts that are less than the original monthly loan payment).</p> <p>However, the Loan Delinquency Management/Reserve Guidelines were not updated to show that the SDFPTF personnel could follow alternative collection procedures when the borrowers are already delinquent.</p> <p>The Guidelines also require the Trust Fund to follow-up with the CAO quarterly to determine the collection status of defaulted loans. The Trust Fund Manager provided support that this procedure was completed in only one of the four quarters tested. Additionally, the Trust Fund Manager did not include a delinquency follow-up log (as stated in SDFPTF response to the prior year audit recommendation) in either of the two borrower's files to document that the Trust Fund monitored the collection status of the loans monthly.</p>

Audit Report	Audit Issues	Audit Recommendations	Audit Follow-Up Results
	<p><b>Special Collections Unit Did Not Deposit and Record the Loan Payments Timely</b></p>	<p>- Work with the Office of Financial Services Special Collections Unit to obtain the information it needs to properly monitor the timeliness of deposits and accounting transactions.</p>	<p><b>* Did not Evaluate</b></p> <p>The Special Collections Unit's transition to Pay1 for SDFPTF transaction processing was not completed during the audit period, June 1, 2008 to May 31, 2009. As a result, this recommendation was not evaluated. However, it will be considered for evaluation in subsequent audits.</p>
	<p><b>Trust Fund Reimbursed Grantees' Expenditure Requests Without Sufficient Documentation and Analysis</b></p>	<p>- Improve the grantee reimbursement process by requiring the grantees to provide more detailed documentation to support the reimbursement request. Also ensure that Trust Fund personnel more thoroughly analyze reimbursement requests before the request are approved.</p>	<p><b>Implemented</b></p> <p>The grantee reimbursement process has improved. The grantee reimbursement requests are supported by detailed documentation and reviewed by more than one person. Additional process improvements can be made by consistently filing relevant documents in each grantee's file.</p>

**Memorandum**

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CITY OF DALLAS

DATE December 2, 2009  
TO Craig D. Kinton, City Auditor  
SUBJECT Response to Audit Recommendations, South Dallas /Fair Park Trust Fund

I have reviewed the draft report regarding the Follow Up of Audit Recommendations, Office of Economic Development, South Dallas Fair Park Trust Fund (October 1, 2006 to May 31, 2008).

Management takes no exception to the audit recommendations for loan underwriting as prudent and meaningful and believes that in a conventional lending environment they are most appropriate. However, the South Dallas Fair Park Trust Fund was established to meet the needs of a unique service area with unique issues that impede access to capital and require alternative underwriting guidelines.

It is management's belief that underwriting guidelines in effect for the South Dallas Fair Park Trust Fund are considerate of repayment risk and that non compliance with the Delinquency Policy relative to the two (2) loans mentioned are with consideration for the circumstances. It should be noted that the Trust Fund has improved operations significantly over the past two (2) years. The one loan criticized in the November 21, 2008 Audit Report has been paid in full and six (6) additional loans have also been paid since the audit.

Guidelines spelled out in the March 2006 Policies and Procedures are intended to validate capability and willingness to repay debt. Heavy reliance is placed on collateral with advance guidelines designed to provide a secondary source of loan repayment. Management believes the following underwriting guidelines are sufficient measures of ability and willingness to repay debt.

Financial

- Annual Business Net Income must cover Annual Loan Payments 1.20X's
- Personal Guarantee of Business owner(s)
- Adhere strictly to Collateral Advance guidelines
- Total monthly payments on personal debt less than 50% of monthly income

Other

- All business and personal accounts current
- All accounts paid as agreed for past 12 months
- No City of Dallas judgments or delinquent debt
- Business bank statements should have positive balances for preceding 12 months

Financial Statements (business and personal), Tax Returns, Bank Statements and Credit Reports are thoroughly reviewed to determine that underwriting guidelines are met. Derogatory and/or other negative information must be explained, documented and depending upon the issue, mitigated.

Management acknowledges that the template (Fact Sheet) developed to document analysis to support loan decisions as recommended by the November 2008 audit is inadequate. It does not address the underwriting criteria listed above and/or whether or not the criteria were assessed in making the loan decision. The loan summary document (Fact Sheet) will be modified to fully address and document all of the underwriting guidelines that support loan approval. No new loans have been made since the loan analysis document was recommended.

**Response to Audit Recommendations South Dallas/ Fair Park Trust Fund**  
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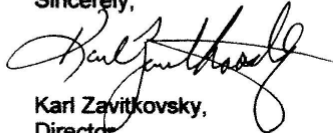
The Delinquency Management process, for the two (2) loans cited, while non compliant, was by passed for cause, and management believes that non compliance has no impact on the collectability of the loans. The Co op Supply borrower has paid \$200.00 each month, "all he can afford" since 2004 when his business failed. The loan balance at the time of the business failure was \$35,163.00. The current loan balance is \$13, 495. The borrower is retired and disabled but insist on "meeting his obligation". Management is accepting the monthly payment and has chosen not to send delinquency notices.

Owens Fast Food owner is in the Trust Fund office 2 to 3 times per month. She repeats that she will do everything she can to pay the loan and will bring in whatever she has as often as she can even though her business has closed. Delinquent notices won't change her situation.

Trust Fund management continues to implement practices and guidelines to strengthen its loan operation, manage risk and maximize debt repayment.

If you have further questions or require additional information, please contact me at 214 670 5140.

Sincerely,



Karl Zavitkovsky,  
Director  
Office of Economic Development

C: Mary K. Suhm, City Manager  
A. C. Gonzalez, Assistant City Manager  
Lee McKinney, Assistant Director, Office of Economic Development  
Leo B. Hicks, Trust Fund Manager