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Audit Report

AUDIT OF SOUTH DALLAS FAIR PARK TRUST FUND

October 1, 2006 to May 31, 2008

(Report No. A09-004)

November 21, 2008

City Auditor

Craig D. Kinton

Table of Contents

	Page
Executive Summary	1
Audit Results	
Underwriting Guidelines Do Not Provide Sufficient Loan Evaluation Criteria	5
Trust Fund Loan Delinquency Management / Reserve Guidelines Are Not Consistently Followed	9
Special Collections Unit Did Not Deposit and Record the Loan Payments Timely	11
Trust Fund Reimbursed Grantee's Expenditure Requests Without Sufficient Documentation and Analysis	13
Appendices	
Appendix I – Background, Objective, Scope and Methodology	15
Appendix II – Summary Tables	18
Appendix III – Major Contributors to This Report	24
Appendix IV - Management's Response	25

Executive Summary

South Dallas Fair Park Trust Fund (Trust Fund) has continued to make improvements. The Trust Fund authorized fewer new loans and concentrated on the collection of loans currently in default. The Trust Fund collected the full amount of \$125,000 associated with three of the fifteen loans originally in default status. These three loans were originally issued between Fiscal Years 2000 and 2003.

Furthermore, in response to prior year audit recommendations, the Trust Fund:

- Revised grant policies and procedures to require grantees to use service delivery methods that allow the Trust fund to verify that the grant funds are used appropriately
- Developed conflict of interest statements
- Required grantees to provide contracts when other parties are used to deliver services
- Reimbursed expenditures to grantees with fully executed contracts

Background Summary

Trust Fund is administered by the Office of Economic Development (ECO). Since 1992, the Trust Fund has authorized 43 loans totaling \$1,076,739 and 261 grants totaling \$3,177,098.

Trust Fund Revenue and Sources (10/01/2006 to 05/31/2008)

General Fund Transfers	\$ 200,000
Smirnoff Ticket Sales	45,574
Flea Market/Antique Show Rentals	31,693
Gifts and Donations	50,000
Loan Payments	172,424
Other	126,154
Total Revenue	\$ 625,845

(Unaudited)

Trust Fund Program Areas

The Trust Fund facilitates economic and community development in the South Dallas Fair Park community through:

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

The Trust Fund, however, needs to improve underwriting guidelines, loan delinquency management, and accounting procedures to address the following:

- Underwriting guidelines do not provide sufficient criteria to help Trust Fund personnel evaluate an applicant's ability to repay the loan. As a result, the Trust Fund approved two \$25,000 loans without adequately reviewing the applicants' financial information.
- Trust Fund Loan Delinquency Management / Reserve Guidelines (Guidelines) are not consistently followed. As a result, the Trust Fund's accounting records still include loans that should have been written off as uncollectible. In addition, Trust Fund personnel did not make adequate collection efforts when a loan became delinquent.
- The Office of Financial Services Special Collections Unit did not deposit and record Trust Fund borrower payments timely as required by Administrative Directive (AD) 4-13, *Cash and Debt Management Policies and Procedures*,

**An Audit Report on –
South Dallas Fair Park Trust Fund**

Trust Fund Policies and Guidelines, and the Economic Development Department's (ECO) Accounting Procedures. As a result, the accounting system did not properly reflect that the loan principal, interest, and associated late fees had been paid and that the borrower's obligation to the Trust Fund was reduced.

- Trust Fund reimbursed grantee expenditure requests without sufficient documentation and analysis. As a result, the Trust Fund reimbursed two grantees for expenses totaling \$8,671 which were not incurred during the contract year. The Trust Fund also reimbursed \$4,980 to one grantee for contract personnel costs without sufficient documentation to ensure that the costs were incurred during the contract year. The Trust Fund reimbursed one grantee \$594 for a food purchase made by a related party without verifying that the purchase was for the grant program.

Summary of Recommendations

We recommend the Director of the Economic Development Department (ECO):

- 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
- 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
- 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
- Require grantees to provide more detailed documentation to enhance the review of the grant reimbursement process and ensure Trust Fund personnel more thoroughly analyze reimbursement requests before approval

Summary of Management's Response

Of the four recommendations contained within the report, management agreed with two recommendations, partially agreed with one recommendation, and disagreed with one recommendation. For the complete management response, please see Appendix IV.

Summary of Objectives, Scope and Methodology

The objective of the audit was to determine whether the Trust Fund adequately reviewed grant and loan applicants' information to determine eligibility, exerted sufficient collection efforts for current and delinquent loan accounts, accurately and timely recorded financial transactions in the City's accounting system, and properly reimbursed grantees expenditures.

The audit covered Trust Fund transactions from October 1, 2006 to May 31, 2008. We interviewed Trust Fund and other City staff, reviewed current Trust Fund policies and procedures, City Council Resolutions 06-1833 and 07-2962, various Administrative Directives, grants, loans, and associated documents, and analyzed certain financial transactions.

Audit Results

Overall Conclusion

South Dallas Fair Park Trust Fund (Trust Fund) has continued to make improvements. The Trust Fund authorized fewer new loans and concentrated on the collection of loans currently in default. The Trust Fund revised certain grant policies and procedures and only reimbursed expenditures to grantees with fully executed contracts. The Trust Fund, however, needs additional improvements for loan underwriting procedures, loan delinquency management, loan accounting, and grant reimbursements.

In response to prior year audit recommendations, the Trust Fund continued to make improvements to its policies and procedures. See Appendix II, Table I, *Summary of Prior Year Audit Recommendations*, for a summary of those improvements.

Underwriting Guidelines Do Not Provide Sufficient Loan Evaluation Criteria

The Trust Fund's Underwriting Guidelines (Guidelines) do not provide sufficient criteria to help Trust Fund personnel:

- Evaluate an applicant's ability to repay the loan
- Document the analysis that supports the loan approval

As a result, the Trust Fund approved two \$25,000 loans without adequately reviewing the applicants' financial information. A \$25,000 loan check was issued to Applicant 1; however, due to concerns raised during the audit, Trust Fund personnel are in the process of reevaluating the financial status of Applicant 2.

The Guidelines are written broadly to allow the Trust Fund to approve loans for applicants that would not generally qualify for traditional loans. For example, the guidelines state:

- "Projections of Revenue and/or Net Income Increases Greater than 20% will Require SOUND Rational"
- "Review Financial Statements and Tax Returns thoroughly"

While broadly written guidelines offer the Trust Fund maximum flexibility to approve loans, they do not define what constitutes a sound rational nor do they specify the procedures, analysis techniques, or documentation needed to ensure compliance. For example, Trust Fund personnel evaluate the adequacy of the

**An Audit Report on –
South Dallas Fair Park Trust Fund**

applicant's business plan, projected revenue and net income, or pledged collateral without set expectations that the applicant must meet or exceed certain pre-specified criteria, such as financial ratios, before a loan is approved.

The loan applicants are required to provide insured collateral to secure the loan. Although the collateral requirement is intended to minimize the risk that the loan will not be repaid, the City has experienced difficulty liquidating certain types of collateral, such as equipment, when a borrower defaults on a loan.

The following are additional examples of issues noted due to the lack of sufficient underwriting and documentation criteria:

- Loan Applicant 2's projected net income increased 76 percent between 2007 and 2008 and projected income increased 29 percent between 2008 and 2009. Trust Fund personnel did not obtain an explanation from Applicant 2 to determine whether these projections were reasonable and the rationale for approving the loan was not documented.
- The applicant's income to payment ratio (net income plus interest plus depreciation equals 1.2 percent of the estimated loan payment) was not documented by Trust Fund personnel.

As a result, the adequacy of existing Trust Fund guidelines could not be determined.

If the Trust Fund used additional criteria to evaluate loan applicants, such as calculating short-term and long-term solvency ratios, it would have more complete information to assess the risk to the Trust Fund that the loan might not be repaid.

The ability of the two applicants to repay Trust Fund loans was low, as shown in Table 1 on the next page. The short-term solvency ratio for Applicant 1 was less than one for all three years reviewed. The short-term solvency ratio for Applicant 2 was significantly below one until 2007 when the ratio increased to 2.20. The long-term solvency ratios also did not confirm that the applicants had sufficient equity to repay the loans.

Solvency Ratios

Short-term – (Current Assets/Current Liabilities) Used to evaluate a loan applicant's ability to meet current obligations from current assets. (Greater than or equal to one is considered reasonable because a borrower has adequate assets to cover the loan).

Long-term – (Total Liabilities/Total Equity) Used to measure the relative amount of resources an applicant can provide for the loan repayment. (Greater equity results in a lower ratio which means the applicant has adequate equity to pay the loan.)

**An Audit Report on –
South Dallas Fair Park Trust Fund**

Table I: Financial Ratios

Solvency Ratios	Applicant 1			Applicant 2		
	2004	2005	2006	2005	2006	2007
Short-term	0.76 ^(a)	0.30	0.60	-0.14 ^(b)	0.21	2.20
Long-term	9.66%	39.20%	23.64%	-772.00% ^(c)	-3143.00% ^(d)	396.00%

(a) Negative current assets and negative current liabilities are reported on the balance sheet.

(b) The ratio is negative due to the negative cash balance.

(c), (d) The ratios are negative due to negative total equity.

Without more specific underwriting guidelines Trust Fund personnel do not have the information needed to ensure that they consistently and fairly evaluate loan applicants and that the applicant is likely to repay the loan.

Recommendation:

We recommend the Director of the Economic Development Department (ECO) 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.

Management’s Response:

Disagree. The South Dallas Fair Park Trust Fund was established to bring greater access to capital to a defined market where credit needs were historically underserved. Because the market was underserved, borrowers resorted to obtaining credit from sources that charged exorbitant interest under untenable terms. Such terms of credit left many borrowers with challenging credit histories that made borrowing from conventional lenders under conventional criteria difficult, if not impossible. 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.

The Trust Fund Commercial Loan and Underwriting Guidelines require:

- Collateral (advance ratios included in policies and procedures)
- Personal Guarantee
- Cash Flow sufficient to meet payment coverage of 1.2
- Business and personal credit accounts current for most recent 12 months
- Acceptable written explanation of any derogatory credit accounts (prior to 12 months)

**An Audit Report on –
South Dallas Fair Park Trust Fund**

- Positive monthly balances on bank statements for 12 months

ECO believes the above criteria establish a definitive basis for Trust Fund loan decisions. ECO appreciates that there are other meaningful criteria used to evaluate credit worthiness, including the recommended ratios. Established norms for the use of such ratios are not useful for the Trust Fund market. Establishing arbitrary minimum ratios would not be meaningful. The Trust Fund is a collateral based lender and requires that exceptions to underwriting guidelines are supported by exceptional collateral.

ECO will institute a Loan Summary Write Up that documents the loan evaluation and spells out the rationale for loan decisions and the basis of high probability of repayment.

Implementation Date: November 1, 2008

Responsible Manager: Assistant Director and Trust Fund Manager

Auditor's Follow-Up Comment

We understand that the purpose of the Trust Fund is to provide access to capital for a market that creates unique underwriting challenges; however, vague evaluation guidelines are of limited benefit for ensuring that loan applications are evaluated consistently and fairly against pre-established criteria. We continue to encourage management to develop sufficient criteria to help Trust Fund personnel consistently evaluate an applicant's ability to repay the loan.

Trust Fund Loan Delinquency Management / Reserve Guidelines Are Not Consistently Followed

The Trust Fund can improve loan collection efforts by consistently following the Trust Fund's Loan Delinquency Management / Reserve Guidelines (Guidelines). For example:

- Trust Fund personnel did not follow-up with the City Attorney's Office (CAO) to determine the Uniform Commercial Code (UCC) Filing Status of 12 loans totaling \$354,022 submitted for legal intervention between 2005 and 2008. As a result, the Trust Fund's accounting records still include loans that are uncollectible. See Appendix II, Table II, *Summary of the Status of the Loans Referred to City Attorney's Office*.

Loan Portfolio Overview (1992 - 07/31/2008)		
<u>Total Loans Principal</u>		
Principal –	43 loans	\$1,076,740
Paid-off –	22 loans	\$524,373
Referred to legal –	16 loans *	\$354,022
* Subsequent to referral, one loan was charged off		
<u>Balance Unpaid</u>		
Charged-off ⁽¹⁾ –	4 loans	\$ 38,885
	2 loans	(Charge-off Amount Unavailable)
Current –	4 loans	\$ 52,648.90 ⁽²⁾
(1) Amounts may include principal, interest, and late fees		
(2) Principal balance as of May 31, 2008		
<u>Loan Default Rate</u>		
17 out of 43 loans –		40%
Source: Trust Fund data (Unaudited)		

- Trust Fund personnel also did not consistently follow the Guidelines for one borrower. The payment history for this borrower showed that when the loan account became delinquent Trust Fund personnel limited collection efforts to the following:
 - Visited the borrower one time and made two telephone calls
 - Sent the payment history to the borrower for 5 of 14 delinquent payments

One payment for this borrower was 83 days past due. Although the Guidelines provide Trust Fund personnel with specific steps to escalate collection efforts, these steps were not followed. For example, Trust Fund personnel did not call the borrower, send the borrower a payment history and written requests for payment, or refer the loan to the CAO for legal intervention.

Without sufficient collection efforts, including periodic requests on the status of delinquent loans referred to the CAO, the Trust Fund cannot reduce the number of delinquent loans in its loan portfolio.

Recommendation:

We recommend the Director of the ECO ensure that Trust Fund personnel follow the Loan Delinquency Management / Reserve Guidelines, including routine follow-ups with the CAO to determine when legal intervention has been exhausted so that the accounting records are properly updated to reflect loan collectability.

Management Response:

Agree. Delinquency management and follow-up has been inconsistent. Trust Fund staff will review Policies and Procedures for delinquency management. Each loan file of borrowers not transferred to CAO and currently making payments will include a delinquency follow-up log for documenting collection efforts. Trust Fund Manager will review files monthly for compliance with delinquency management policies and procedures.

ECO has spent the past year on efforts to accurately adjust and reflect the Trust Fund loan portfolio. We have attempted to follow Administrative Directive 4-10 concerning loans believed to be uncollectible and to make appropriate accounting entries. It is our interpretation that loans can only be removed from the accountings records with written documentation from CAO that the loan is uncollectible. To follow-up on uncollectible loans transferred to CAO, the Trust Fund will begin a quarterly written follow-up with CAO to ascertain the status of loans transferred in accordance with Administrative Directive 4-10. Written responses will be requested with copies to the file and ECO Budget / Finance for appropriate accounting entries.

Implementation Date: November 1, 2008

Responsible Manager: Trust Fund Manager

Special Collections Unit Did Not Deposit and Record the Loan Payments Timely

The Office of Financial Services Special Collections Unit (Special Collections) neither deposited loan payments in the City's Treasury nor recorded payments in the City's financial system timely as required by Administrative Directive 4-13, *Cash and Debt Management Policies and Procedures*, the Trust Fund Policies and Guidelines, and ECO's *Accounting Procedures*.

One borrower made a total of ten loan payments. Deposits for eight of the ten payments were late (one to six business days) and all ten deposits were not recorded in the accounting system timely (two to sixteen business days). Three of five loan payments were recorded late (one to three months). As a result, the accounting system did not properly reflect that the loan principal, interest, and associated late fees had been paid and that the borrower's obligation to Trust Fund was reduced.

Sections 2.1 and 5.1.2 of Administrative Directive 4-13 requires the Office of Financial Services (OFS) to deposit cash collections into the City Treasury on the day of receipt, if possible, or within one business day of receipt. Section III A of the Trust Fund Policies and Guidelines requires Special Collections to record payments as they are received. Appendix III of the Trust Fund Accounting Procedures, *Accounting Entries for SDFPTF Business Loan documented by ECO*, requires Special Collections to monthly record the interest, principal, and late fees associated with the loan. These accounting procedures also require Special Collections to reduce the balance sheet control accounts (Account Receivable and Deferred Revenue Account) to match the loan sub-ledger at the end of each month.

Recommendation:

We recommend 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.

Management's Response:

Partially Agree. The audit finding of timeliness of deposits and postings (accounting transactions) per Administrative Directive 4-13 is an OFS Special Collections Unit non-compliance issue and is outside of the authority and control of ECO. ECO cannot respond and take corrective action to address the timeliness of deposits. To address the impact of untimely posting to Trust Fund accounts, ECO will continue to review, on a monthly basis, the Monthly Payments Log of Trust Fund Payments received from OFS Special Collections

**An Audit Report on –
South Dallas Fair Park Trust Fund**

Unit. When the Trust Fund monthly payments and posting do not reconcile, ECO Budget / Finance will work with Special Collections to determine the reason and make the necessary adjustments. Adjustments to Trust Fund postings will be made as quickly as correcting information can be determined. Payment adjustments will revert to the effective date of the payment to accurately reflect date payment was received and impact to balances owed and interest paid.

Implementation Date: Already in place

Responsible Manager: ECO Budget / Finance

Auditor's Follow-Up Comment

While management partially agrees with this recommendation, their response indicates that they have implemented additional monitoring procedures. It is our understanding that ECO's ability to monitor the timeliness of deposits and accounting transactions will be improved with the implementation of Pay1.

Trust Fund Reimbursed Grantees' Expenditure Requests Without Sufficient Documentation and Analysis

Grantees' expenditure requests were reimbursed without sufficient documentation and analysis. For example, the Trust Fund:

- Reimbursed two grantees for administrative costs totaling \$8,671 incurred before the grant agreements were signed
- Reimbursed \$4,980 to one grantee for contract personnel costs without sufficient documentation to ensure that the costs were incurred during the contract year. The grantee contracted with individuals to officiate basketball games. The grantee provided an invoice detailing the number of games worked by each official and the amount paid to each official. The Trust Fund verified that the personnel costs were within the scope of the contract; however, the Trust Fund did not obtain documentation, such as a game schedule, to determine whether the games were held during the contract year.
- One grantee requested reimbursement for a food purchase totaling \$594. The grantee's executive director purchased food with a personal check. The Trust Fund obtained and reviewed the itemized receipt; however, Trust Fund personnel did not obtain any additional information to verify that the food purchase was actually used for the grant program.

Section IE (Grant Procedures) of South Dallas Fair Park Trust Fund Policies and Guidelines state that invoices should evidence expenditures are within the scope of services and the contract year.

Recommendation:

We recommend the Director of ECO improve the grantee reimbursement process by requiring the grantees to provide more detailed documentation to support the reimbursement request. We also recommend the Director of ECO ensure that Trust Fund personnel more thoroughly analyze reimbursement requests before the requests are approved.

Management Response:

Agree. Trust Fund has developed a Certification to be signed by the Grantees that certifies that the Grantee is in compliance with all of the requirements of the Grant. In addition, the Trust Fund will include, where available, other evidence of

**An Audit Report on –
South Dallas Fair Park Trust Fund**

grant activity compliance, such as schedules of events, posters, brochures, and other announcements of the funded activity.

The reimbursement of the YMCA expense of \$8,671 and \$100 for A Sister's Gift (ASG) outside of the contract period was in error due to Trust Fund management's failure to recognize that the dates of receipts for expenses incurred were outside of the contract period. The proper period expenses have been submitted for the YMCA. Proper period reimbursement receipts have been requested from ASG.

Trust Fund staff has been instructed to follow the second review process before submitting reimbursement request for payment in an effort to insure that documentation errors are eliminated. Trust Fund manager and administrative support will review and jointly sign and/or initial all request for payment prior to signature by ECO executives as evidence that the request has been reviewed twice for correctness.

Implementation Date: November 1, 2008
Responsible Manager: Trust Fund Manager

Appendix I

Background, Objective, Scope and Methodology

Background

The South Dallas Fair Park Trust Fund (Trust Fund) was initially recommended by the South Dallas Fair Park Neighborhood Preservation and Economic Development Plan (Plan), which was adopted by the City Council in 1987.

The Trust Fund receives funding from the following revenue sources:

- Annual \$200,000 contribution from the General Fund reduced by \$100,000 Community Development funding allocated to South Dallas Fair Park Minor Home Repair Program
- Revenue from the Visitor's Formula – The Visitor's Formula is based on the estimated hotel, sales tax, and expenditures collected from Dallas visitors that have Fair Park as their primary destination
- Smirnoff ticket sales (\$0.15/ticket sold)
- Flea market and antique show rentals (50 percent of the rental revenue)
- Trust Fund loan repayment (both principal and interest)
- Interest earnings from Trust Fund account balances

The Trust Fund funds three program areas through grants and business loan programs.

Grant Program – Includes challenge grants, public safety grants, community based non-profit organization grants, and special grants.

- Business and economic development initiatives to promote local economic development, improve and stimulate business and commercial activities / opportunities, create and retain jobs, and encourage affordable housing development

**An Audit Report on –
South Dallas Fair Park Trust Fund**

- Housing and neighborhood improvement projects to provide assistance for low cost repairs of owner-occupied residences and provide needed community improvements
- Community service programs to provide job-related and human services assistance

During the current audit period, Trust Fund authorized seventeen grants totaling \$256,500. As of May 31, 2008, the Fiscal Year 2007-2008 grant applications were still in the review process and, thus, they were excluded from the audit.

Loan Program – One loan in the amount of \$25,000 was approved in April 2008; however, the Trust Fund is re-evaluating the borrower’s loan qualifications. Consequently, this loan was not included in the evaluation of accuracy and timeliness of loan related account posting.

The Trust Fund collected the full amount of \$125,000 associated with three of the fifteen loans originally in default. These three loans were originally issued between Fiscal Years 2000 and 2003.

Status of Prior Year Audit Recommendations – Of the eight prior year audit recommendations, the Trust Fund Management fully implemented five, partially implemented one, and did not implement two. See Appendix II, Table 1, *Summary of Prior Year Audit Recommendations*.

Objective, Scope and Methodology

The objective of the audit was 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 covered Trust Fund transactions from October 1, 2006 to May 31, 2008. We interviewed Trust Fund and other City staff, reviewed current Trust Fund policies and procedures, City Council Resolutions 06-1833 and 07-2962, various grants, loans, and associated documents, and analyzed various financial transactions.

We conducted this audit 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

**An Audit Report on –
South Dallas Fair Park Trust Fund**

based on our audit objective. The audit of the Trust Fund was also conducted under authority of City Charter, Chapter IX, Section 3.

To achieve the audit objective the City Auditor's Office:

1. Interviewed Trust Fund and Economic Development Department (ECO) personnel to gain an understanding of grant and loan administration and accounting procedures
2. Reviewed *South Dallas Fair Park Trust Fund (SDFPTF) Policies and Guidelines*, ECO's *Accounting Procedures for SDFPTF Business Loans*, Council Resolutions (06-1833 and 07-2962) and Administrative Directives (AD) 4-10, *Delinquent and Uncollectible Accounts Receivable* and AD 4-13, *Cash and Debt Management Policies and Procedures*, to identify the criteria for the audit
3. Selected samples for testing
4. Examined the selected grants and loans in order to determine whether ECO is in compliance with departmental policies and guidelines and City's provisions

Table I: Summary of Prior Year Audit Recommendations

No.	Audit Issue(s)	Audit Recommendation(s)	Audit Follow Up Result(s)
1.	The Trust Fund received excess General Fund contributions.	We recommended the Director of Economic Development Department (ECO) to work with the City Attorney's Office (CAO) and the Director of the Housing Department to clarify the General Fund contribution provisions of Resolution 99-3439 and adjust funding accordingly.	Partially Implemented. In October 2007, the CAO was contacted for the interpretation of Council Resolution 99-3439, Section 2 (C) (4). The interpretation from the CAO is not conclusive, and General Fund funding has not been adjusted at the time this report was written.
2.	The Trust Fund did not reimburse the General Fund for fiscal year 2006 administrative expenditures.	Ensure the Trust Fund reimburses the General Fund for administrative expenditures for fiscal year 2006.	Implemented. In October 2007, ECO reimbursed the General Fund \$142,638 for its share of budgeted administrative expenses for Fiscal Year 2005-2006.
3.	Loan related balance sheet accounts remain incorrect.	We recommend the Director of ECO ensure the Trust Fund analyzes the prior loan related accounting entries to correct the Trust Fund's loan related accounts and develop appropriate accounting methodologies to record future loan transactions.	Implemented. ECO analyzed prior loan related accounting entries to record the allowance for doubtful accounts. ECO implemented "SDFPTF Accounting Procedures – Entries for SDFPTF Business Loans" to record loan transactions in December 2007. The procedures were officially adopted in April 2008.

**An Audit Report on –
South Dallas Fair Park Trust Fund**

No.	Audit Issue(s)	Audit Recommendation(s)	Audit Follow Up Result(s)
4.	Grant policies and procedures do not require grantees to use service delivery methods that Trust Fund staff can verify.	We recommend the Director of ECO ensure the Trust Fund's grant policies and procedures are revised to require grantees to use service delivery methods that allow the Trust Fund to verify that grant funds were used appropriately.	Implemented. The Trust Fund reimbursed a grantee \$2,440.75 for Wal-Mart and Target gift cards without obtaining the information necessary to verify that the gift cards were used for eligible grant activities. In the current audit period, ECO denied the same grantee's reimbursement request for \$2,340 for Wal-Mart and Kroger gift cards. On the grant agreement, ECO also limited the scope of expenses that it can reimburse to the grantee.
5.	A grant reimbursement was made without a fully executed contract.	We recommend the Director of ECO ensure the Trust Fund's policies and procedures are revised to require that a fully executed contract is in place prior to approving any reimbursement requests. The Trust Fund should also work with the CAO and City management to streamline the contract execution and approval processes.	Implemented. We reviewed eight of seventeen grants approved in Fiscal Year 2006-2007. ECO reimbursed four grantees whose contracts have been fully executed.
6.	Grantees are not required to sign conflict of interest statements or provide formal agreements or contracts when using other parties to deliver services.	<p>We recommend the Director of ECO ensure the Trust Fund's grant application process is amended to:</p> <ul style="list-style-type: none"> • Include a requirement that grant applicants must complete conflict of interest statements • Notify grantees that the Trust Fund will not reimburse grantees for services provided by related parties • Require grantees to obtain formal agreements or contracts when grantees use subcontractors to provide service delivery. The Trust Fund should include copies of these contracts in its files. 	Implemented. ECO developed a conflict of interest statement and a scope of services reimbursement certification. ECO also obtains the contracts between grantees and subcontractors when grantees use subcontractors to provide service delivery.

**An Audit Report on –
South Dallas Fair Park Trust Fund**

No.	Audit Issue(s)	Audit Recommendation(s)	Audit Follow Up Result(s)
7.	Fifty-seven percent of the Trust Funds' authorized loans are in default.	We recommend the Director of ECO ensure the Trust Fund enforces its revised loan policies and procedures that require thorough credit and financial reviews are conducted prior to authorizing a loan.	Not Implemented. Three loans, which were reported in the prior audit report, are still in default.
8.	Encumbrances for expired grants are not closed timely.	We recommend the Director of ECO ensure the Trust Fund notifies the grantees associated with the expired grant encumbrances that reimbursement requests should be made within a specified time period. After that time period passes, the Trust Fund should close the expired encumbrances. For existing and future grants, the Trust Fund should revise its policies and procedures to require grantees to file reimbursement requests within a specified time after the grant closes.	Not Implemented. The prior audit reported that encumbrances for several expired grants that were authorized prior to Fiscal Year 2004 were open. As of May 2008, these encumbrances prior to Fiscal Year 2004 are still outstanding. The Trust Fund current policies and procedures require Trust Fund personnel to review prior year outstanding (unpaid) grants ninety days after the awarded grants expire. Trust Fund personnel are required to send letters to recipients to notify the grantees that the grants are expiring and that extensions can be requested; however, the policies and procedures do not specify the required time frame for grantees to respond to the letters.

Table II: Summary of the Status of the Loans Referred to City Attorney’s Office

Loans	Referral Date	Reasons of Referral	Status of Loan Referral
1	10/6/2005 4/4/2006	Misuse of public funds; breach of contract; Non performance	The borrower has not been located. Note: There is a deed of trust on non-exempt, residential rental property that was put up for security for the loan by an unrelated party. A demand collection letter may be effective to the owner of such property.
2 *	8/15/2006	Non performance	The CAO obtained a default judgment against the borrower on June 15, 2007 for \$49,999. An Abstract of Judgment was filed on April 1, 2008. A demand letter was sent to the borrower’s latest address on July 17, 2008.
3	Unknown	Non performance (Bankruptcy 09/16/2002)	The CAO obtained an Agreed Final Judgment on November 22, 2005. There also exists a Payment Agreement entered into by the borrower as part of the Agreed Final Judgment. CAO needs information on the current loan payment history regarding the borrower. The borrower, in the past, has responded to demand letters from the CAO.
4 *	Unknown	Non performance	The CAO obtained judgment on December 18, 2002. An Abstract of Judgment was filed on April 28, 2005 with a partial release on February 14, 2007 for the debtor’s homestead. No further collection activity is planned by the CAO.
5	12/13/2005	Non performance	The CAO has no record of having received this matter for legal action.
6	12/13/2005	Non performance; Breach of contract	In 2005, the CAO was asked for an opinion as to what to do in a situation where the borrower was serving on active duty in a foreign country. The Trust Fund Administrator was informed what it would take to pursue collection under the federal Soldier’s and Sailor’s Relief Act. CAO was later informed that the borrower’s relative was operating the business and had resumed payments. No other record of this matter being referred to the CAO for collection has been located.

**An Audit Report on –
South Dallas Fair Park Trust Fund**

Loans	Referral Date	Reasons of Referral	Status of Loan Referral
7 *	8/7/2007	Non performance	The CAO accepted this file for legal collection activity on or about August 9, 2007. CAO requested additional information of the Trust Fund Administrator on August 9, 2007 and sent a demand letter to the borrowers on September 19, 2007 (which was returned as undeliverable). Borrower has not been located as of this date. Note: ECO's loan history file shows that this borrower is current on payment.
8 *	Unknown	Judgment against the borrower	An Abstract of Judgment has been filed in Dallas County records. At the request of the borrower, there have been two attempts to settle the matter by payment to the City of a reduced settlement amount approved by the City Council in order to release the judgment lien on other real property owed by the borrower, but the borrower did not follow through. No further collection action is planned by the CAO.
9 *	Unknown	Unknown	The CAO has no record of this matter being referred for collection.
10	2/19/2008	Information not available	The CAO received this file on or about February 19, 2008. The CAO was informed that the borrower died in 2007. Demand has been made to the borrower's estate. Currently waiting for the estate to resolve Internal Revenue Service issues and then pay out to the creditors.
11	2/19/2008	Information not available	The CAO received this file on or about February 19, 2008. The borrower filed for bankruptcy protection in November 2004 and the City was duly noticed. The CAO file has been closed.
12	Information not available	Information not available	This matter was recalled by the Trust Fund Administrator in May 2008 as the borrower had submitted a payment.
13 **	Information not available	Information not available	The CAO has no record of receiving a collection referral on this matter.
14 **	Information not available	Information not available	The CAO has no record of receiving a collection referral on this matter.

**An Audit Report on –
South Dallas Fair Park Trust Fund**

Loans	Referral Date	Reasons of Referral	Status of Loan Referral
15 **	Information not available	Information not available.	The CAO has no record of receiving a collection referral on this matter.
16 **	Information not available	Information not available.	The CAO has no record of receiving a collection referral on this matter.

Note:

* Business closed.

** These loans were previously charged off to loss between 1994 and 1996. CAO has no record of receiving a collection referral for these loans.

Major Contributors to This Report

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Thandee Kywe, Project Manager
Reisha Hall, Auditor
Kimeca Jackson, Auditor
Theresa Hampden, CPA, Quality Control Manager

Management's Response

Memorandum

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CITY AUDITOR'S OFFICE

DATE: November 13, 2008

TO: Craig D. Kinton, City Auditor

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

The Office of Economic Development provides the following responses to the audit report recommendations:

Recommendation 1:

We recommend the Director of the Economic Development Department (ECO) 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.

Management Response / Corrective Action Plan

Agree Disagree X Partially Agree

The South Dallas/Fair Park Trust Fund was established to bring greater access to capital to a defined market where credit needs were historically underserved. Because the market was underserved, borrowers resorted to obtaining credit from sources that charged exorbitant interest under untenable terms. Such terms of credit left many borrowers with challenging credit histories that made borrowing from conventional lenders under conventional criteria difficult if not impossible. Underwriting Guidelines for the Trust Fund were established to create access to capital for borrowers who won't qualify under conventional guidelines while giving the Trust Fund a high probability of repayment.

The Trust Fund Commercial Loan and Underwriting Guidelines require:

- Collateral (advance ratios included in policies and procedures)
- Personal Guarantee
- Cash Flow sufficient to meet payment coverage of 1.2
- Business and personal credit accounts current for most recent 12 months
- Acceptable written explanation of any derogatory credit accounts (prior to 12 months)
- Positive monthly balances on bank statements for 12 months

ECO believes the above criteria establishes a definitive basis for Trust Fund loan decisions. ECO appreciates that there are other meaningful criteria used to evaluate credit worthiness, including the recommended ratios. Established norms for the use of such ratios are not useful for the Trust Fund market. Establishing arbitrary minimum ratios would not be meaningful. The Trust Fund is a collateral based lender

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**An Audit Report on –
South Dallas Fair Park Trust Fund**

and requires that exceptions to underwriting guidelines are supported by exceptional collateral.

ECO will institute a Loan Summary Write Up that documents the loan evaluation and spells out the rationale for loan decisions and the basis of high probability of repayment.

Implementation Date

November 1, 2008

Responsible Manager

Assistant Director and Trust Fund Manager

Recommendation 2:

We recommend the Director of the ECO 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.

Management Response / Corrective Action Plan

Agree Disagree Partially Agree

Delinquency management and follow up has been inconsistent. Trust Fund staff will review Policies and Procedures for delinquency management. Each loan file of borrowers not transferred to CAO and currently making payments will include a delinquency follow up log for documenting collection efforts. Trust Fund Manager will review files monthly for compliance with delinquency management policies and procedures.

ECO has spent the past year on efforts to accurately adjust and reflect the Trust Fund loan portfolio. We have attempted to follow Administrative Directive 4 – 10 concerning loans believed to be uncollectable and to make appropriate accounting entries. It is our interpretation that loans can only be removed from the accounting records with written documentation from CAO that the loan is uncollectable. To follow up on uncollectable loans transferred to CAO, the Trust Fund will begin a quarterly written follow up with CAO to ascertain the status of loans transferred in accordance with Administrative Directive 4 – 10. Written responses will be requested with copies to the file and ECO Budget/Finance for appropriate accounting entries.

Implementation Date

November 1, 2008

Responsible Manager

Trust Fund Manager

Recommendation 3:

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

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**An Audit Report on –
South Dallas Fair Park Trust Fund**

Management Response / Corrective Action Plan

Agree Disagree Partially Agree X

The audit finding of timeliness of deposits and postings (accounting transactions) per Administrative Directive 4- 13 is an OFS Special Collections unit non compliance issue and is outside of the authority and control of ECO. ECO cannot respond are take corrective action to address the timeliness of deposits. To address the impact of untimely posting to Trust Fund accounts, ECO will continue to review on a monthly basis, the Monthly Payments Log of Trust Fund Payments received from OFS Special Collections unit. When the Trust Fund monthly payments and postings don't reconcile, ECO Budget/Finance will work with Special Collections to determine the reason and make the necessary adjustments. Adjustments to Trust Fund postings will be made as quickly as correcting information can be determined. Payment adjustments will revert to the effective date of the payment to accurately reflect date payment was received and impact to balances owed and interest paid.

Implementation Date

Already in Place

Responsible Manager

ECO Budget/ Finance

Recommendation 4:

We recommend the Director of ECO improve the grantee reimbursement process by requiring the grantees to provide more detailed documentation to support the reimbursement request. We also recommend the Director of ECO ensure that Trust Fund personnel more thoroughly analyze reimbursement requests before the requests are approved.

Management Response / Corrective Action Plan

Agree X Disagree Partially Agree

Trust Fund has developed a Certification to be signed by all Grantees that certifies that the Grantee is in compliance with all of the requirements of the Grant. In addition, the Trust Fund will include where available, other evidence of grant activity compliance such as, schedules of events, posters, brochures and other announcements of the funded activity.

The reimbursement of the YMCA expense of \$8,671 and \$100 for A Sisters Gift (ASG) outside of the contract period was in error due to Trust Fund management's failure to recognize that the dates of receipts for expenses incurred were outside of the contract period. The proper period expenses have been submitted for the YMCA. Proper period reimbursement receipts have been requested from ASG.

Trust Fund staff has been instructed to follow the 2nd review process before submitting reimbursement request for payment in an effort to insure that documentation errors are eliminated. Trust Fund manager and administrative support will review and jointly sign and/or initial all request for payment prior to signature by ECO executive as evidence that the request has been reviewed twice for correctness.

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**An Audit Report on –
South Dallas Fair Park Trust Fund**

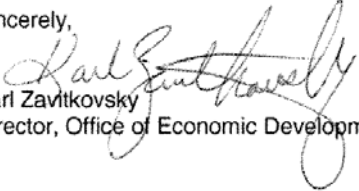
Implementation Date

November 1, 2008

Responsible Manager

Trust Fund Manager

Sincerely,


Karl Zavitkovsky
Director, Office of Economic Development

C: Lee McKinney
Sheri Price
Leo Barron hicks

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