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The Office of Internal Audit provides independent, objective assurance and consulting services that adds value to and improves Louisville Metro Government.

# Office of Internal Audit

Metro Finance Department

Community Foundation of  
Louisville Accounts



# Audit Report

Office of Internal Audit

## Metro Finance Department Community Foundation of Louisville Accounts

December 2006



Metro Finance Department

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Community Foundation of  
Louisville Accounts

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LOUISVILLE, KENTUCKY  
OFFICE OF INTERNAL AUDIT

MICHAEL S. NORMAN, CIA  
CHIEF AUDIT EXECUTIVE

## Transmittal Letter

December 22, 2006

The Honorable Jerry E. Abramson  
**Mayor of Louisville Metro**  
Louisville Metro Hall  
Louisville, KY 40202

**Re: Audit of Louisville Metro's Community Foundation of Louisville Accounts**

### Introduction

The operating records and procedures of Louisville Metro accounts at the Community Foundation of Louisville (CFL) were examined. The Metro Finance Department is responsible for the administration of the CFL accounts. The primary focus of the audit was the operational and fiscal administration of the activity. This included how Metro CFL accounts are processed, recorded, and monitored.

The examination was conducted in accordance with Government Auditing Standards issued by the Comptroller General of the United States and with the International Standards for the Professional Practice of Internal Auditing issued by the Institute of Internal Auditors.

As a part of the review, the internal control structure was evaluated. The objective of internal control is to provide reasonable, but not absolute, assurance regarding the achievement of objectives in the following categories:

- Achievement of business objectives and goals
- Effectiveness and efficiency of operations
- Reliability of financial reporting
- Compliance with applicable laws and regulations
- Safeguarding of assets

There are inherent limitations in any system of internal control. Errors may result from misunderstanding of instructions, mistakes of judgment, carelessness, or other personnel factors. Some controls may be circumvented by collusion. Similarly, management may circumvent control procedures by administrative oversight.

## Scope

The operating procedures for administering CFL account activity were reviewed through interviews with key personnel. The focus of the review was the operational and fiscal administration of the activity. Tests of sample data were performed for transactions from July 1, 2005 to May 31, 2006. Activity reviewed included supporting documentation for individual transactions, internal activity ledgers, CFL account statements and the Louisville Metro financial system.

The review included assessing whether activity was processed, recorded, and monitored accurately and appropriately. The details of the scope and methodology of the review will be addressed in the Observations and Recommendations section of this report. The examination would not identify all weaknesses because it was based on selective review of procedures and data.

## Opinion

It is our opinion that the administration of Metro CFL account activity is satisfactory. The internal control rating is on page 5 of this report. This rating quantifies our opinion regarding the internal controls, and identifies areas requiring corrective action.

While the overall opinion is satisfactory, opportunities to strengthen the administration of CFL account activity were noted. Examples of these include the following.

- **CFL Account Administration.** None of the fund agreements between Louisville Metro and the CFL could be located. This information is necessary to enable monitoring of the account to ensure it's used for intended purposes. The lack of fund agreements is a major issue that weakens the effectiveness of the control structure. The risk is somewhat mitigated by the small volume of transactions.
- **Policies and Procedures.** The Metro Finance policies and procedures do not include information pertaining to use of the Community Foundation of Louisville. Finance does have desktop procedures that document the departmental processing of CFL activity. The lack of enterprise policies and procedures increases the risk of improper use by Metro departments.
- **Monitoring and Reconciliation.** Monitoring and reconciliation of CFL account activity could be strengthened. The timeliness of reconciliation preparation, as well as, the documentation of the preparation and review of this activity could be enhanced. This would help ensure reconciliations are properly performed, and ultimately help verify the accuracy and completeness of the related records.

Metro Finance should be commended for corrective actions taken to address weaknesses noted in the prior review issued in July 2002. Several major risks appear to have been mitigated. The implementation of the recommendations in this report will help improve the internal control structure and effectiveness of the administration of CFL account activity.

**Corrective Action Plan**

Representatives from Metro Finance have reviewed the audit results. Metro Finance's corrective action plans are included in this report in the Observations and Recommendations section.

Sincerely,

A handwritten signature in blue ink that reads "Michael S. Norman". The signature is written in a cursive style and is positioned above a horizontal line.

Michael S. Norman, CIA, CGAP  
Chief Audit Executive

cc: Louisville Metro Council Audit Committee  
Louisville Metro Council Members  
Deputy Mayors  
Secretary of the Cabinet for Finance and Administration  
Chief Financial Officer

**Internal Control Rating**



<u>Legend</u>			
<u>Criteria</u>	<u>Satisfactory</u>	<u>Weak</u>	<u>Inadequate</u>
<i>Issues</i>	Not likely to impact operations.	Impact on operations likely contained.	Impact on operations likely widespread or compounding.
<i>Controls</i>	Effective.	Opportunity exists to improve effectiveness.	Do not exist or are not reliable.
<i>Policy Compliance</i>	Non-compliance issues are minor.	Non-compliance issues may be systemic.	Non-compliance issues are pervasive, significant, or have severe consequences.
<i>Image</i>	No, or low, level of risk.	Potential for damage.	Severe risk of damage.
<i>Corrective Action</i>	May be necessary.	Prompt.	Immediate.

## **Background**

Louisville Metro has several accounts with the Community Foundation of Louisville (CFL). The accounts are not intended to circumvent any of Metro's policies and procedures. They are primarily for activities that are not part of Metro's normal operating business, and thus may be more effectively administered through the CFL. As of the review date, Metro had five accounts with the CFL. A complete list of accounts is included as the appendix of this report. Since these accounts are not administered using the Metro financial system, with its inherent controls, there is greater risk associated with the activity.

The Community Foundation of Louisville is a community-based, independent, nonprofit organization. The CFL does not have any legal connection to Louisville Metro. The CFL's primary purpose is to accumulate and manage permanent endowed funds. Permanent endowed funds are those in which an amount is deposited into a fund where the earnings are used for charitable activities or projects, while retaining the principal.

The Community Foundation of Louisville is comprised of three separate entities:

- The Community Foundation of Louisville
- The Community Foundation of Louisville Depository, Inc
- The Community Foundation of Louisville Corporate Depository, Inc.

The Community Foundation of Louisville Corporate Depository acts as a fiscal agent for nonprofit organizations or assists for-profit organizations with charitable giving. Funds are accumulated by way of donations for a nonprofit or charitable event/purpose. Distributions for expenditures relating to the event or purpose are then made through these accounts. The corporate depository is similar to a bank account.

As of March 31, 2006, the balance of the five Metro accounts at the Community Foundation of Louisville totaled approximately \$285,600.

This was a scheduled audit.

## **Summary of Audit Results**

### **I. Current Audit Results**

See Observations and Recommendations section of this report.

### **II. Prior Audit Issues**

The Office of Internal Audit previously audited the former City of Louisville CFL account activity in July 2002. Unless otherwise noted, all prior weaknesses have been satisfactorily addressed. Metro Finance should be commended for corrective actions taken to address weaknesses noted in the prior review. Several major risks appear to have been mitigated.

### **III. Statement of Auditing Standards**

The audit was performed in accordance with Government Auditing Standards issued by the Comptroller General of the United States and with the International Standards for the Professional Practice of Internal Auditing issued by the Institute of Internal Auditors.

### **IV. Statement of Internal Control**

A formal study of the internal control structure was conducted in order to obtain a sufficient understanding to support the final opinion.

### **V. Statement of Irregularities, Illegal Acts, and Other Noncompliance**

The examination did not disclose any instances of irregularities, any indications of illegal acts, and nothing was detected during the examination that would indicate evidence of such. Any significant instances of noncompliance with laws and regulations are reported in the Observations and Recommendations section of this report.

### **VI. Views of Responsible Officials/Action Plan**

A draft report was issued to the Metro Finance Department on October 27, 2006. An exit conference was held at the Metro Finance Department on December 4, 2006. Attending were Jane Driskell and Kim Statts representing Metro Finance; Scott Miller and Michael Norman representing Internal Audit. Final audit results were discussed.

The views of Metro Finance officials were received on December 18, 2006 and are included as corrective action plans in the Observations and Recommendations section of the report.

LMCO §30.36(B) requires Louisville Metro Agencies to respond to draft audit reports in a timely manner. It specifically states that

*“The response must be forwarded to the Office of Internal Audit within 15 days of the exit conference, or no longer than 30 days of receipt of the draft report.”*

Due to a misunderstanding of the timeframe requirements, the Department of Finance’s response was not provided within the required timeframe.

## Observations and Recommendations

### Scope

The operating procedures for administering Metro accounts at the Community Foundation of Louisville (CFL) were reviewed. The focus of the review was the operational and fiscal administration of the activity. This included how activity was processed, recorded, and monitored. Applicable personnel were interviewed in order to gain a thorough understanding of the various processes. A sample of Metro CFL account activity was judgmentally selected for the audit period July 1, 2005 through May 31, 2006. Metro CFL accounts were identified using the following methods.

#### Community Foundation of Louisville Confirmation

A confirmation response was received from the CFL identifying Louisville Metro accounts. This request was based on the federal tax identification numbers for the Louisville Metro Government, as well as, the former City of Louisville and Jefferson County.

#### Louisville Metro Departmental Confirmations

A confirmation request was sent to Louisville Metro Departments requesting they report any CFL accounts being used for Metro business purposes.

#### Louisville Metro Financial System Account Review

A cursory review of the account used to record CFL activity on the Louisville Metro financial system was performed. This review was intended to identify CFL deposit and disbursement transactions processed through the Louisville Metro financial system.

#### Louisville Metro Financial System Supplier Payment Report Review

The Louisville Metro financial system supplier payment history report was reviewed to identify Metro supplier payments to the CFL. The activity for each payment was reviewed to identify the nature of the transaction.

The review consisted of examining the sample of Metro CFL account activity. The review focused on information recorded on supporting documentation for individual transactions, internal activity ledgers, CFL account statements and the Louisville Metro financial system. An assessment of the internal controls and procedures for the administration of CFL account activities was performed.

This information was reviewed to ensure that activity was processed accurately and appropriately. The review would not reveal all weaknesses because it was based on selective review of data.

### Observations

The internal control structure for the administration of Metro accounts at the Community Foundation of Louisville is satisfactory. There were some opportunities noted to strengthen the control structure. The observations are as follows:

- #1 CFL Account Administration
- #2 Monitoring and Reconciliation

Details of these begin on the following page.

## #1 - CFL Account Administration

The Community Foundation of Louisville (CFL) processes all disbursements approved by authorized Metro employees and ultimately receives all revenue deposits. The CFL also provides investment management services for applicable accounts and prepares periodic statements for each individual account.

The Metro Finance department provides oversight for all Louisville Metro accounts at the CFL. This includes providing deposit and payment processing support. In addition, Finance is responsible for reconciling supporting documentation with CFL account statements for all activity. The following issues were noted regarding Metro's administration of CFL accounts.

### Account Documentation

- None of the fund agreements between Louisville Metro and the CFL could be located. These documents detail the establishment of each account and the intended purpose. This information is necessary to properly ensure all disbursements and receipts are managed in accordance with the account requirements. Since Metro Finance provides the authorizing signature for payment distributions and performs the account reconciliations, an understanding of each account is imperative.
  - For example, two of the Metro accounts are charged investment manager fees and CFL administrative fees. The fee structure applied (e.g., percentage of fund, charge per individual transactions) to the two funds is not documented. This may increase the risk of improper fees being assessed to the funds.
- Metro Finance indicated that a request was made for the Undesignated Art Fund (Monument Fund #1) to be merged with another and was unaware that this had not been done. The account is used for various short-term public art projects. Any remaining funds are transferred to the Public Art Trust Endowment Fund at the conclusion of each project. The account had a zero balance for the review period and it appears that the last transaction was processed in November 2002.

*The lack of fund agreements is a major issue that impairs the effectiveness of the internal control structure. It is somewhat mitigated by the small volume of transactions. Regardless, it needs to be addressed. Also, similar problems were noted during the previous review.*

### Policies and Procedures

- The Metro Finance policies and procedures do not include information pertaining to the use of the Community Foundation of Louisville. While the Metro Cash Management policy does address bank accounts, CFL account establishment and use is not addressed. This does not provide guidance for Metro's use or potential uses of the CFL. While use of CFL accounts should be tightly controlled and limited, the lack of enterprise policies and procedures increases the risk of improper use by Metro departments.

Finance does have desktop procedures that document the departmental processing of CFL activity. This documentation is useful to help Finance staff process CFL activity as intended and to help monitoring of the accounts.

### Recommendations

Appropriate personnel should take corrective action to address the concerns noted. Specific recommendations include the following.

- ✓ Metro Finance should maintain copies of the fund agreements documenting the establishment and intended purpose of the CFL accounts. This information should be available to individuals processing and monitoring activity to ensure the appropriateness of transactions.
- ✓ Appropriate Metro Finance personnel should verify that they have been properly notified of all Louisville Metro accounts at the CFL. This should also include verifying accounts that may have been established under the former City of Louisville and Jefferson County Governments.
- ✓ Finance should continue the practice of periodically assessing the need for all of the accounts at the CFL. When possible, accounts with limited activity and monetary balances should be combined. Closing accounts with limited activity or a terminated purpose is strongly recommended.
- ✓ The Metro Finance policies and procedures should include guidelines for Metro's use of CFL accounts. This includes the establishment of accounts, along with processing and monitoring responsibilities. Since the use of the CFL should be extremely limited, no accounts should be authorized by any department other than Metro Finance. These policies and procedures should be disseminated to all Metro departments.

## **#2 - Monitoring and Reconciliation**

Metro Finance internal policies and procedures require that quarterly reconciliations of CFL accounts be performed. The following problems were noted with the reconciliation of this activity.

- For one account, a documented reconciliation was not retained with the quarterly statements for two periods. It's uncertain whether reconciliations for this account were performed during these periods. Timely reconciliations are an imperative control to provide for the proper oversight of CFL account activity.
- For one account, Metro Finance's internal ledger was not updated in a timely manner. A single posting of approximately \$46,000 was recorded for five quarters. The ledger should be updated as part of the quarterly reconciliation process. Untimely updates decrease the usefulness of the internal ledger as a management and monitoring tool.
- None of the reconciliations examined were signed / dated by the preparer or a reviewer. This does not adequately document the timeliness of preparation or review. The review of reconciliations helps ensure their accuracy and completeness. This is an important part of the process.

*Issues with reconciliations and monitoring were noted during the previous review.*

## **Recommendations**

Appropriate personnel should take corrective action to address the concerns noted. Specific recommendations include the following.

- ✓ A major component of any reporting system is proper reconciliation and monitoring. It is imperative that administrative staff reviews the information on a regular basis. This includes reviewing individual transactions for appropriateness, completeness and adherence to requirements, along with monitoring of Community Foundation of Louisville account statements. Also, transactions that might be processed by Louisville Metro (e.g., revenue receipts) should be reconciled to the Metro financial statements to ensure the accurate and timely reflection of activity. In order to promote proper segregation of duties, an administrator independent of the actual processing of activity should perform this function.
- ✓ A formal, documented reconciliation process should be practiced. The detailed activity reports should be compared to some type of source documentation, such as disbursement requests. Discrepancies should be properly noted and researched. This helps ensure the transactions were processed as intended and properly recorded. This also helps to verify the accuracy of and strengthen the reliability of the related financial records.
- ✓ Reconciliations should be signed and dated by the preparer, as well as the reviewer. This will help ensure that all activity appears appropriate, complete, and adheres to requirements.

### **Department of Finance's Corrective Action Plan**

Since the previous review of the Community Foundation of Louisville (CFL) Accounts, several corrective actions have been taken and implemented to improve controls over these accounts.

- The Finance department has divided administration and monitoring of the accounts between the Business Office and the Accounting Division, to ensure appropriate segregation of duties.
- A review of accounts was conducted in 2005 to consolidate, eliminate and confirm accounts. Seven accounts were eliminated or consolidated, with five (technically four) CFL accounts remaining for Metro.
- Regular account reconciliations are performed and reviewed for all CFL accounts.
- Operating procedures have been developed and implemented over the administration of the CFL accounts.

#### **#1: CFL Account Administration**

The Finance department has contacted the Community Foundation and requested copies of the account agreements for our records. Once received, copies of these agreements will be maintained by Finance.

#### **#2: Policies and Procedures**

The Finance Department maintains policies and procedures for the administration of CFL accounts. This policy addresses the processing of payments, donations, and reconciliations. CFL accounts are not available to all departments in the Metro Government and therefore no other policy is considered necessary as accounts are only opened based upon the Administration's request and all accounts are monitored by the Finance Department.

#### **#3: Monitoring and Reconciliation**

Due to personnel changes over the past year, the responsibility for monitoring and reconciling the CFL accounts has transitioned to new employees in both the Finance Business Office and General Accounting. The employees now monitoring the CFL accounts are working to ensure all transactions are recorded and accounts are reconciled on a timely basis.

## Appendix - Metro Community Foundation of Louisville Accounts

Agency	Account Name	Purpose	Balance as of 3/31/06
<b>Endowment</b>			
1	Finance Belle of Louisville	This fund was established to support the maintenance of the Belle of Louisville Steamboat.	\$138,113.49
2	Finance Public Art Trust	Fund to purchase new pieces of public art, including land and other support needs, and to repair and maintain existing public art. Any groups supporting public art can request a grant from this fund.	\$116,975.50
<b>Depository</b>			
3	Finance Flock of Finns (Monument Fund #8)	This fund collects gifts from various sources to support the Flock of Finns that is placed around Louisville.	\$26,230.65
4	Finance Warheim Park Fund	This fund was established by a Foundation donor to pay the expenses of Warheim Park, which is owned by Metro Parks.	\$4,276.73
5	Finance Undesignated Art Fund (Monument Fund #1)	This fund is used for various short-term public art projects. When a special project is concluded, any remaining funds are transferred to the Public Art Trust Endowment Fund.	\$0.00
<b>Total</b>			<b>\$285,596.37</b>