

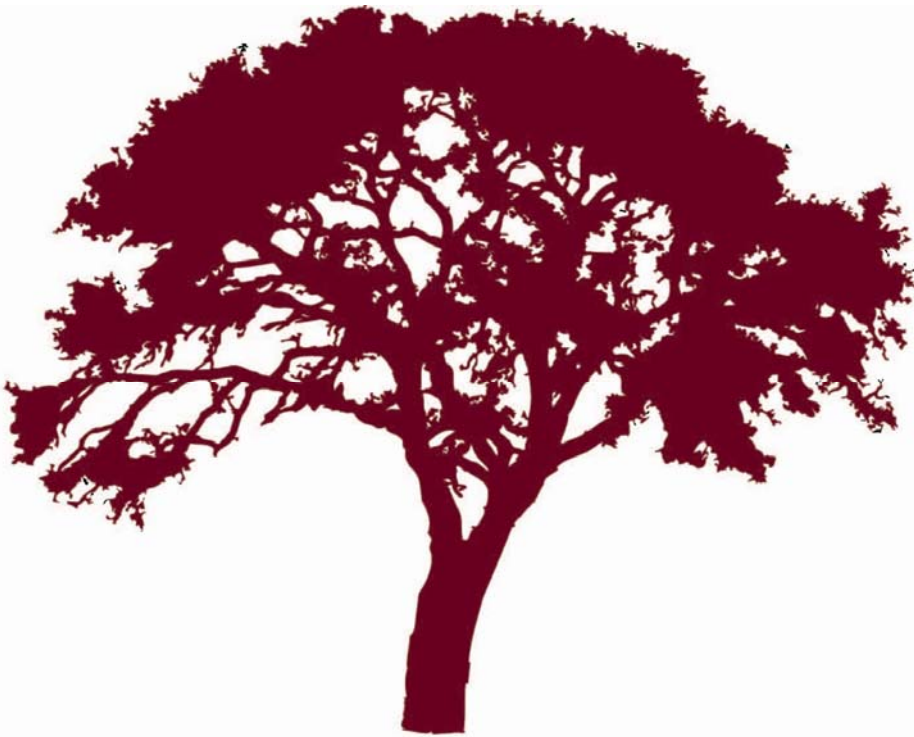
# City of Oakland Office of the City Auditor

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November 18, 2010

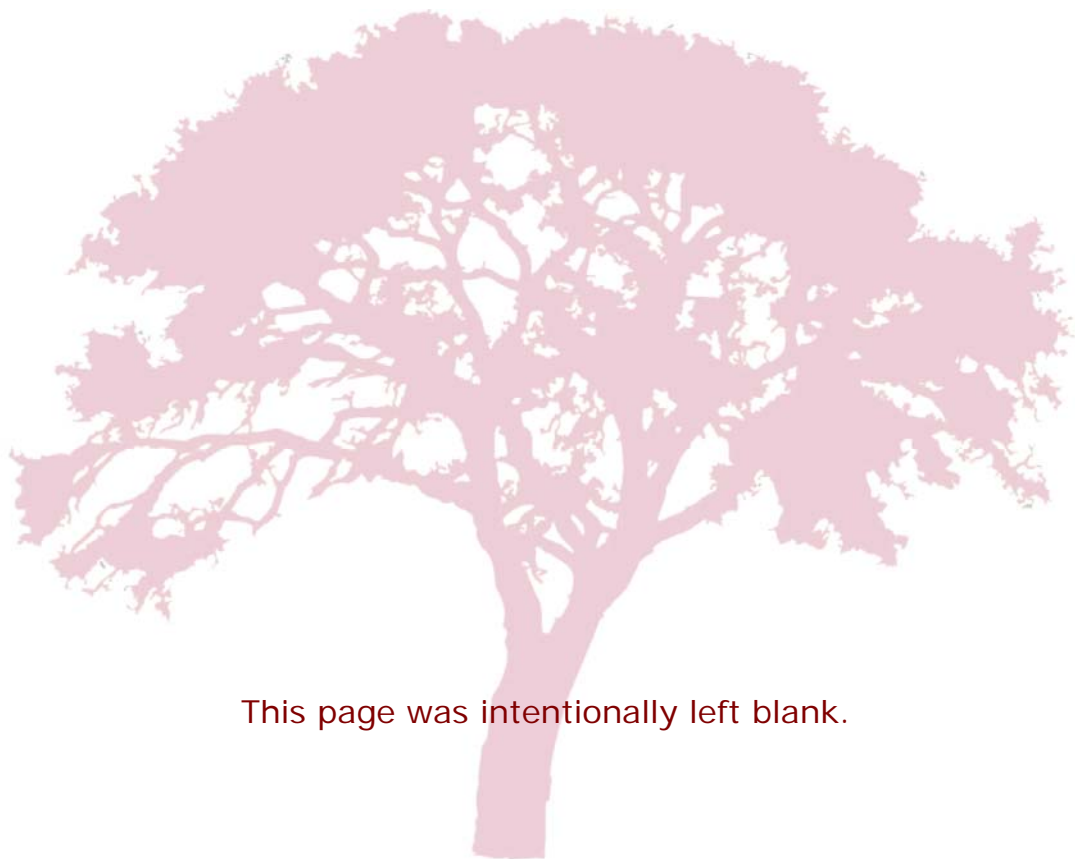
## CEDA Loan Receivables Performance Audit

*Millions of inaccurately recorded  
dollars arose from weak  
internal controls*



City Auditor  
Courtney A. Ruby, CPA, CFE

# PERFORMANCE AUDIT



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November 18, 2010

OFFICE OF THE MAYOR  
HONORABLE CITY COUNCIL  
OAKLAND CITIZENS  
OAKLAND, CALIFORNIA

**RE: CEDA LOAN RECEIVABLES PERFORMANCE AUDIT**

Attached is the Community and Economic Development Agency (CEDA) Loan Receivables Performance Audit, which focuses on loans issued by the City with outstanding receivable balances during fiscal years 2006-2009. The audit focused solely on loans funded by local taxpayer dollars through the Redevelopment Agency's Tax Increment Fund, as well as the General Fund.

The audit's objectives were to:

- Analyze and evaluate loan receivables policies and procedures
- Determine if there are adequate internal controls in place to accurately account for outstanding loans, defaulted loans, and loan payments

The importance of looking at receivables is to determine whether or not the City's revenue will be realized as has been previously expected. Citizens and the City Council must know that the Administration is properly accounting for residents' tax dollars, especially during these challenging economic times when every dollar counts.

Unfortunately, this audit revealed that the Administration had lost track of \$14 million dollars in loan receivables, failed to properly record loans that had been authorized to be converted to grants more than 10 years ago, and operates a flawed system to record homebuyer loans.

Inadequate oversight and weak internal controls masked these issues until they were revealed by this audit. Disconcertingly, the audit showed that the Administration was unaware it had \$14 million in loan receivables, as well as the corresponding deferred revenue that was on the books, which we now know will never be realized and must be written off. Illustrating the magnitude of these deficiencies, \$14 million constitutes approximately 35% of CEDA's locally funded loan portfolio.

The greater issue is what else is the Administration unaware of on the City's books. This audit calls into question larger concerns regarding the dependability of the City's financial system to produce relevant and reliable information that decision makers absolutely require. Additionally, this audit recommends that the City's financial statement auditors increase their internal controls testing in the receivables area.

In its response to the audit, the Administration skirts its responsibilities by alleging that the audit exaggerates its findings and by falsely asserting that there is no correlation between historic loans and current loan practices. The Administration's dismissal of the issues raised in this audit is more alarming than the audit's findings themselves. Only as a result of this audit are we now aware that \$14 million dollars the City was counting on will not be realized, yet the Administration calls this irrelevant. In a time when we are laying off personnel and cutting back on valuable residential services, how can \$14 million be irrelevant?

Quite simply, the Administration's response is appalling. I ask the City Council and the citizenry to join me in demanding absolute accountability without equivocation or excuse.

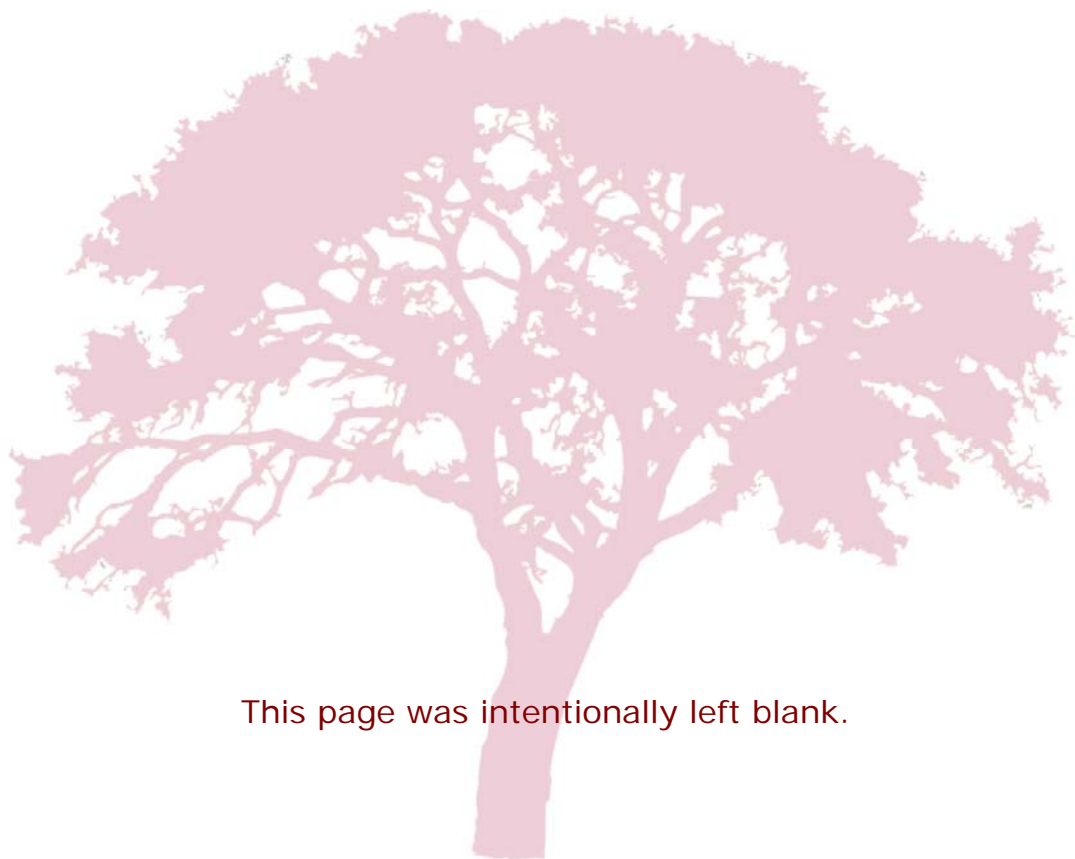
Respectfully submitted,

A handwritten signature in dark ink, reading "Courtney A. Ruby". The signature is fluid and cursive, with the first name "Courtney" being larger and more prominent than the last name "Ruby".

COURTNEY A. RUBY, CPA, CFE  
City Auditor

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## CEDA LOAN RECEIVABLES PERFORMANCE AUDIT REPORT SUMMARY

### Inadequate Internal Controls

**Inadequate Internal Controls:** *CEDA Management and FMA Management's inadequate internal controls resulted in approximately \$14 million in loan receivables on the books that should have been written off and more than \$450,000 in errors from inaccurate or unrecorded loans.*

### Overview

The Office of the City Auditor conducted a performance audit of the Community and Economic Development Agency's (CEDA) loan receivables for City-funded loans. The scope of the audit focused on loans funded through the City's General Fund (Fund 1010) and CEDA Property Tax Increment Fund (Fund 2185) with outstanding receivable balances during fiscal years 2006-2009. The objectives of the audit were a) to analyze and evaluate loan policies and procedures related to loan receivables, and b) to determine if there are adequate internal controls in place to accurately account for outstanding loans, defaulted loans and loan payments.

### Key Findings

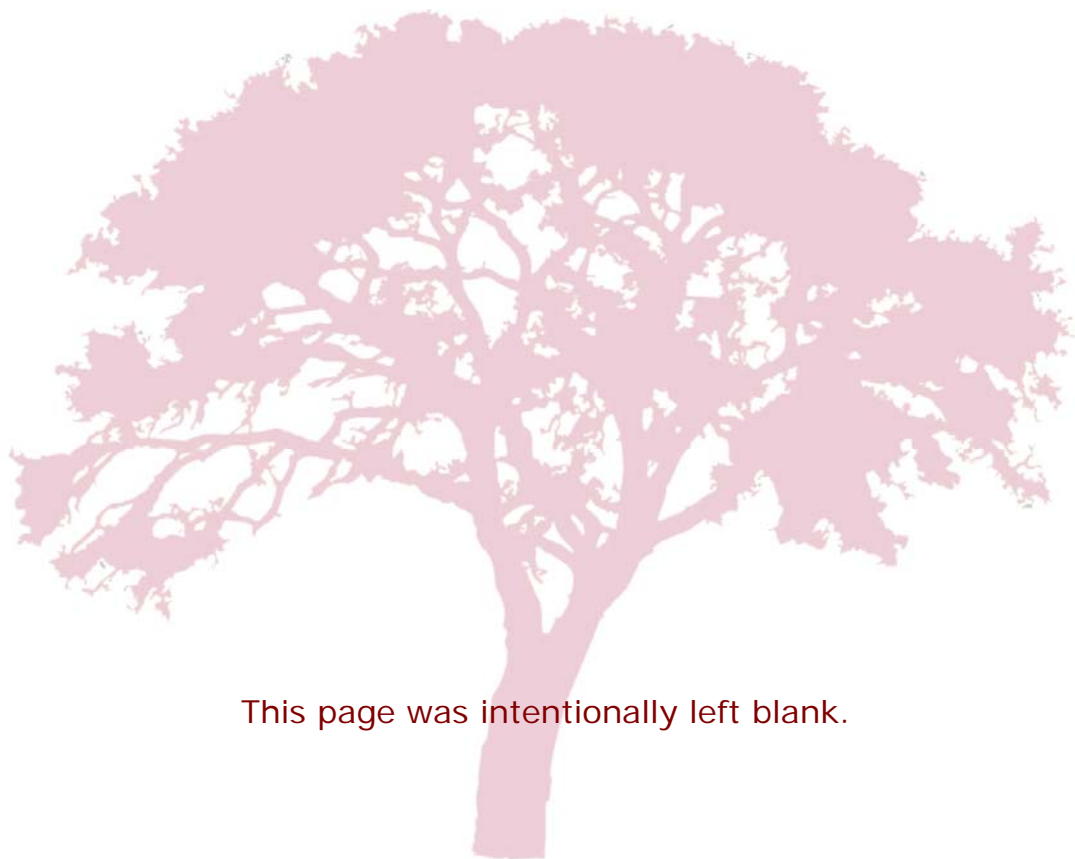
The following are key findings from the audit:

- FMA and CEDA Management cannot justify carrying approximately \$14 million in loan receivables on the books that should have been written off.
- FMA and CEDA Management did not accurately record approximately \$220,000 in loan receivables that had been converted to grants by City Council.
- CEDA Management did not maintain any documentation for deeming approximately \$100,000 in loan receivables as uncollectible.
- Subsidiary ledgers used to maintain homebuyer loan information and Oracle are inaccurate therefore the process is flawed and errors exceed \$450,000.

### Key Recommendations

To address the audit's findings, the report includes several key recommendations. Overall, we recommend that FMA and CEDA Management:

- Evaluate the design and operation of their internal controls over loan receivables.
- Implement best practices and prepare detailed loan policies and procedures to ensure all loan receivable records are complete and accurate.
- Conduct an annual review of all loans, to ensure that all loan receivable records in the sub-ledger and in Oracle are complete and accurate.
- Research and evaluate systems that would have the capability to automatically interface with Oracle to update loan data.



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## Introduction

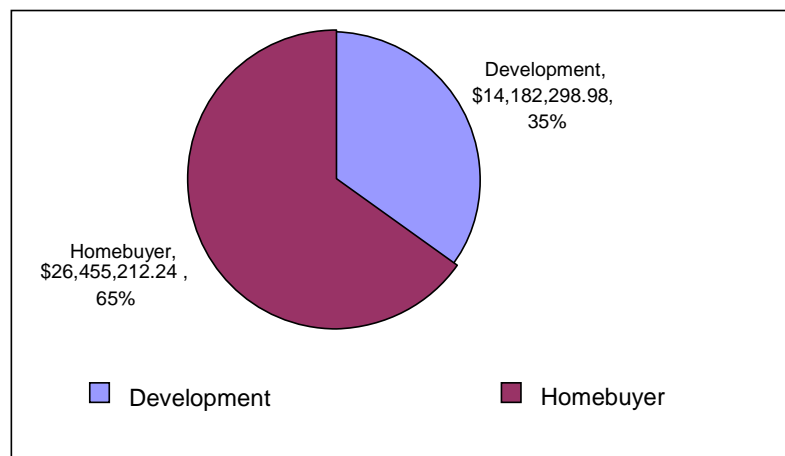
The City of Oakland (City) has been operating in an environment of severe budget deficits since fiscal year (FY) 2007-08. Deficits have gripped municipalities and state governments across the country since the onset of the current recession. As revenue streams shrink, cash management is critical and it is essential that accuracy, internal controls, and tracking in receivables remain at the forefront of the City Administration's efforts to track, properly account for, and collect all loans due to the City. The Office of the City Auditor (Office) conducted a loan receivables audit of the Community and Economic Development Agency's (CEDA) City-funded loans to evaluate the efficiency and effectiveness of the CEDA loan receivables system.

## Background

CEDA administers both federally and City-funded loans. The audit reviewed City-funded loans. These loans are financed through the General Fund (Fund 1010) and the Property Tax Increment Fund (Fund 2185) and include two types of loans:

- Development loans
- Homebuyer loans

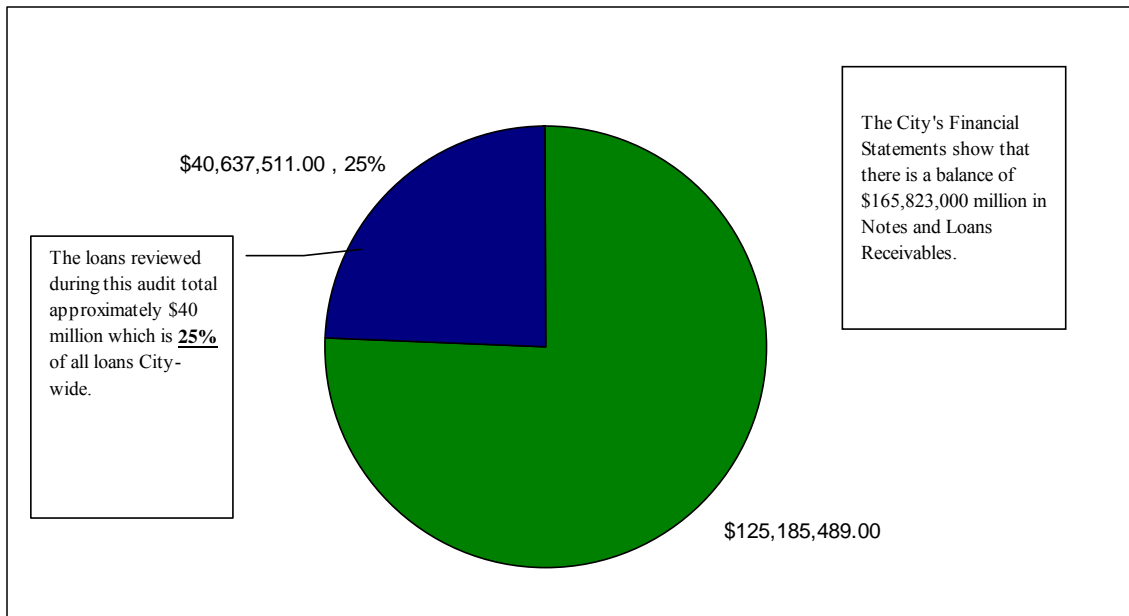
### Exhibit 1: APPROXIMATELY \$40 MILLION IN CITY-FUNDED LOANS<sup>1</sup>



These loans make up approximately 25% of the total loan receivables for the City's General Fund and Redevelopment Fund for FY 2008-09, as shown in Exhibit 2.

<sup>1</sup> The audit included testing of random and judgmental samples of the Homebuyer loans and all of the Development loans.

## Exhibit 2: TOTAL GENERAL FUND AND REDEVELOPMENT FUND NOTES AND LOANS RECEIVABLES AS OF FY 2008-09



### CEDA Structure for Loan Oversight

Prior to FY 1998-99, there were two divisions in CEDA, the Office of Housing and Neighborhood Development (OHND) and the Office of Economic Development and Employment (OEDE). In FY 1999-00, OHND and OEDE were consolidated to create CEDA. After the two offices were consolidated, CEDA Fiscal was developed as a subdivision in CEDA and given the responsibility to consolidate and account for all CEDA loans. Prior to this consolidation, Finance and Management Agency (FMA) managed all CEDA loans. The loans reviewed in this audit originated in various departments, but with the transfer of the loans from FMA to CEDA, the loans became the responsibility of CEDA Management.

## Objectives, Scope & Methodology

### Audit Objectives

The objectives of the CEDA loan receivables audit were:

- To analyze and evaluate loan policies and procedures related to loan receivables
- To determine if there are adequate internal controls<sup>2</sup> in place to accurately account for outstanding loans, defaulted loans and loan repayments

### Audit Scope

During the entrance conference and the first few weeks of the audit, the Office clarified that the focus of the audit would be on loans funded by local Oakland's tax dollars rather than federal or state dollars. Specifically, the scope of the audit focused on loans funded through the City's General Fund (Fund 1010) and CEDA Property Tax Increment Fund (Fund 2185) with outstanding receivable balances during fiscal years 2006-2009. The audit scope encompassed 16 Development loans, approximately 700<sup>3</sup> homebuyer loans from the Mortgage Assistance Program (MAP) and 23 Public Safety Employees-Downpayment Assistance Program (PSE-DAP) loans.

The audit reviewed all 16 Development loans and a judgmental sample of ten MAP loans was selected to identify the areas of potential internal control weaknesses. In addition, all of the foreclosed MAP loans were reviewed to ensure they were accurately recorded in Oracle. All PSE-DAP loans were reviewed for foreclosures and to verify that the loans were accurately recorded in Oracle.

### Audit Methodology

This section describes the methodologies used to complete the audit objectives.

To analyze and evaluate loan receivable policies and procedures we:

- Reviewed the CEDA/HCD Loan Payment Processing Instructions and Residential Lending Loan Servicing Policies and Procedures provided by CEDA Management
- Interviewed CEDA Management to determine the procedures in place for recording loans, tracking receivables, processing repayments and detecting and preventing fraud

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<sup>2</sup> Internal controls consist of plans, methods, policies and procedures used to meet management's mission, goals and objectives.

<sup>3</sup> 700 MAP City-funded MAP loans include approximately 500 outstanding loans and 200 paid, cancelled or foreclosed loans as of June 30, 2009.

To determine if there were adequate internal controls in place to accurately account for outstanding loans, defaulted loans and loan repayments, we:

- Interviewed FMA Management to understand the background regarding Development loans
- Reviewed FMA's financial reporting system used by the City to track loan receivables
- Reviewed CEDA's internal controls over processing loan receivables
- Reviewed the first time homebuyer approval process

We also reviewed:

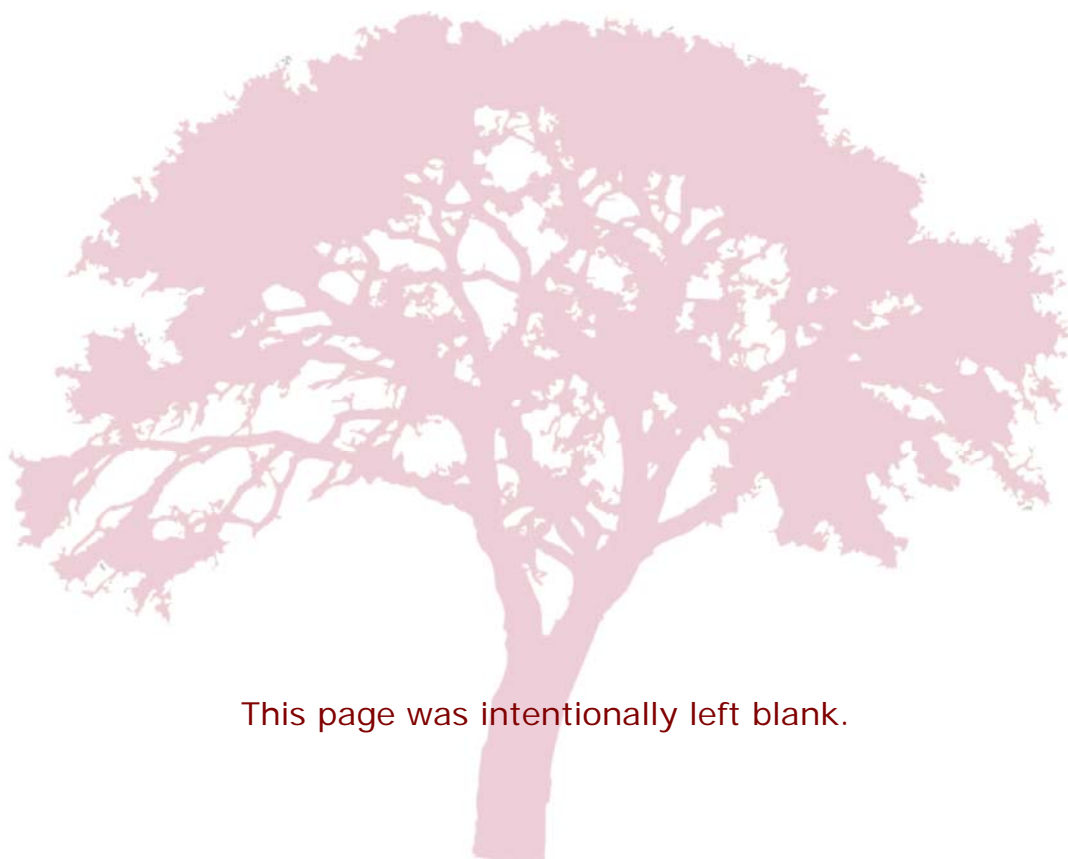
- Administrative Instructions, City Council Resolutions, state-level legislation pertaining to redevelopment agencies and projects, and Oakland Redevelopment Agency's Budget
- General and subsidiary ledgers (sub-ledgers) and the City's centralized accounting and financial reporting system, Oracle

We performed this performance audit in accordance with the 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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.



# **SECTION ONE**

## **DEVELOPMENT LOANS**



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Based upon our criteria of loans funded from the General Fund or the Property Tax Increment Fund, we identified 16 Development loans with loan receivable balances totaling approximately \$14 million at the end of FY 2008-09.

- Eleven of the 16 loans were economic development loans from the previous OEDE department.
- Three of the 16 loans were housing development loans from the previous OHND department.
- One of the 16 loans was from the Department of Human Services.
- One of the 16 loans, neither FMA nor CEDA Management could provide any documentation that specified the department from which the loan originated.

For the purposes of this audit, these 16 loans will be referred to as Development loans. Three of the 16 loans were short term loans and the remaining 13 loans were deferred loans, which means the repayment of loans are due upon sale or transfer of property. These loans were originally tracked in the previous financial system and were transferred to Oracle in FY 1998-99. The specific loans reviewed are listed in Appendix 1 of this report.

The audit found that neither FMA nor CEDA Management could provide sufficient supporting documentation for 14 out of the 16 Development loans, totaling approximately \$14 million of inappropriately accounted for loan receivables on the City's books. Furthermore, FMA Management did not accurately account for three loans that City Council approved to be converted to grants, totaling approximately \$220,000. FMA Management was also not able to provide supporting documentation for deeming three loans, totaling approximately \$100,000, as uncollectible. Lastly, the audit found inaccurate due dates and payment terms were recorded in Oracle for these loans.

These findings are indicative of larger internal control design and operational deficiencies. According to Government Auditing Standards, a deficiency in internal controls exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, detect, or correct misstatements in financial or performance information.

As a result of these findings, the City's accounting system failed to properly reflect the City's current assets and liabilities. The City's maintaining inaccurate financial records highlights the lack of a properly designed and implemented system of internal controls over loan receivables. Internal controls provide a reasonable basis for financial officers to assert that the information may be relied upon. This system failed to provide that assurance.

We recommend that FMA and CEDA Management immediately review their internal controls over loans including the establishment of policies and procedures to ensure:

1. Accurate loan values, dates and payment terms are recorded.
2. Loan receivable aging analysis is prepared and reviewed monthly by management and for deferred loans a tracking system should be established.
3. An allowance for doubtful accounts policy is established that includes preparing periodic estimates of uncollectible loan balances for review and authorization by management.
4. All loan write-offs, grant conversions or forgiveness of delinquent loans have a clear audit trail that documents the justification for writing off, forgiving or converting the loan including all authorizing signatures and City Council resolutions if applicable.

In addition, CEDA and FMA Management should jointly conduct an annual review of all loans to ensure all loan receivable records are accurate and updated.

#### Loan Receivables Subsidiary Ledgers to Oracle Process

To clearly understand the findings reported in this audit report, it is helpful to understand the process of how loan data is input into Oracle. All CEDA loan data is maintained by CEDA Fiscal in various loan subsidiary ledgers. For example, the Mortgage Assistance Program (MAP)<sup>4</sup> sub-ledger records each of the MAP loans with information such as the borrowers name, loan origination date, title company, principal payments made, interest payments made and the loan balance. Loans are monitored by CEDA Fiscal using the data in the subsidiary ledgers.

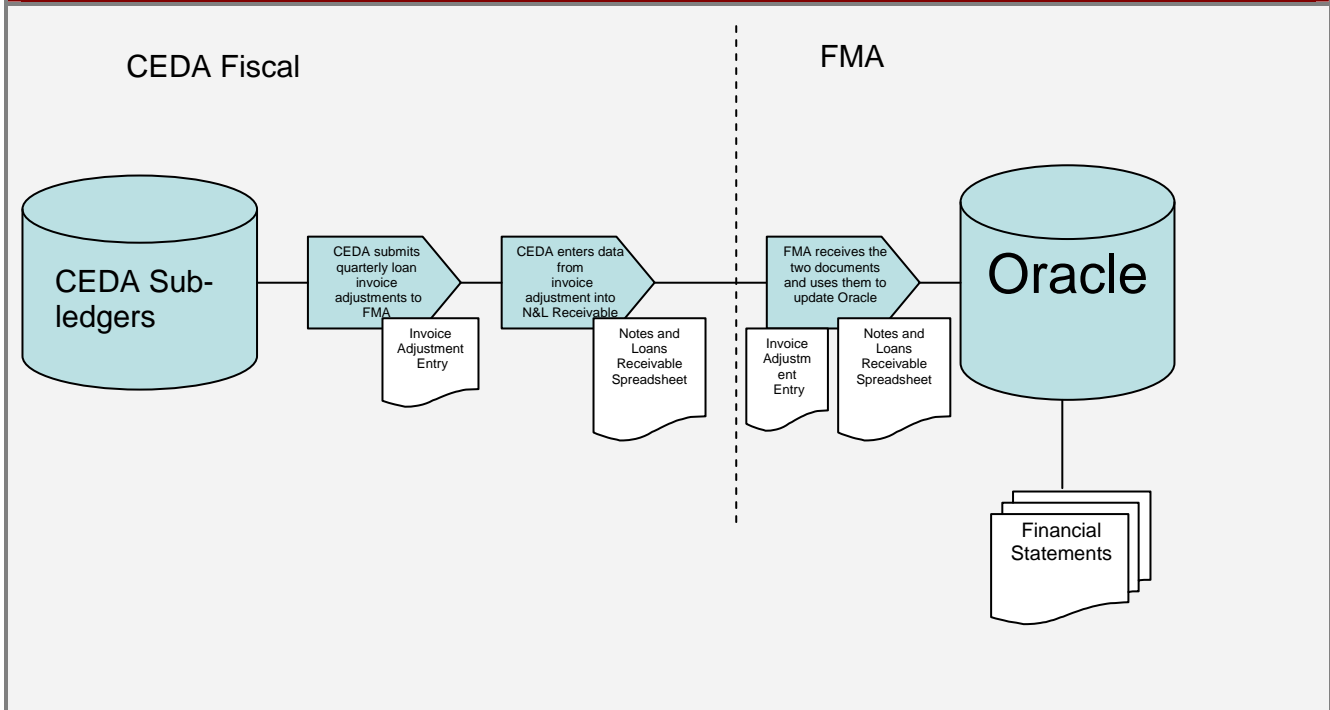
Before Oracle is updated, CEDA Fiscal uses invoice adjustment entries, completed on a quarterly basis, to update the Notes and Loans Receivables sub-ledger, which is a spreadsheet used to record all of the loans City-wide. The loan program or debtor's name is listed in the spreadsheet, along with the account number and payments made on the loan for the fiscal year. Quarterly, FMA receives the invoice adjustments and Notes and Loans Receivable sub-ledger, then updates Oracle and prepares the City's financial statements. Oracle only maintains the debtor name or loan program, loan amount, loan type, due date and payment terms. Exhibit 3 describes this process.

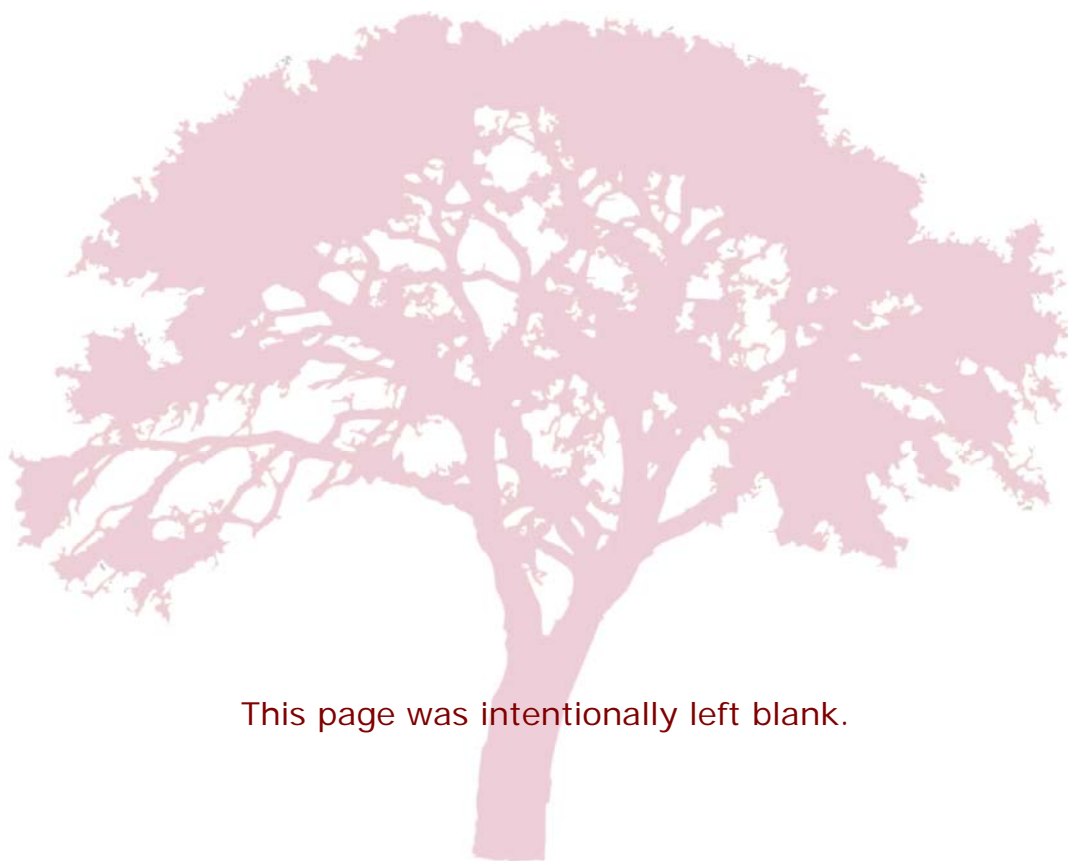
The audit found that there are no internal control procedures in place to detect and rectify accounting errors after quarterly inputs and reconciliations have occurred. The audit noted that maintenance of sub-ledgers is currently a manual process.

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<sup>4</sup> Additional information about MAP is in Section Two of this audit report.

### Exhibit 3: MANUAL INPUT FROM SUB-LEDGER TO ORACLE PROCESS





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# CHAPTER 1

## FMA & CEDA MANAGEMENT CANNOT JUSTIFY APPROXIMATELY \$14 MILLION IN LOAN RECEIVABLES, RESULTING IN A MISSTATEMENT OF ASSEST & LIABILITIES.

FMA and CEDA Management could not provide sufficient supporting documentation for 14 out of 16 Development loans, equaling 99% of the outstanding Development loan balance

According to best practices from the State of Illinois Office of the Comptroller, there should be prompt and accurate recording of all receivables. In addition, periodic estimates of uncollectible loan balances should be reported in a timely manner to management. These practices ensure that receivables are complete and accurate and ultimately that financial statements are reliable. According to the Government Finance Officers Association (GFOA), a sound framework of internal controls is necessary to afford a reasonable basis for financial officers to assert that the information provided can be relied upon. Without proper supporting documentation for loans, CEDA Management cannot verify that the loans were accurately recorded.

FMA and CEDA Management provided insufficient supporting documentation for 14 out of 16 Development loans, with no supporting documentation provided for four of the loans. These 14 loans are shown in Exhibit 4 and total approximately \$14 million. Additional details about each of the loans are in Appendix 1 of this report.

### Exhibit 4: TOTAL INAPPROPRIATELY ACCOUNTED FOR LOAN RECEIVABLES AT THE END OF FY 2008-09

| Debtor   | Total Loan(s) Amount | Number of Loans | Documentation Provided              |
|--|----------------------|-----------------|-------------------------------------|
| Oakland Hotel Association (OHA)                      | \$12,038,314         | 6               | Insufficient documentation provided |
| Oakland Renaissance Association (ORA)                | \$1,769,693          | 2               | Insufficient documentation provided |
| Oakland Business Development Corporation (OBDC)      | \$52,444             | 1               | No documentation provided           |
| Bananas Inc.   | \$50,000             | 1               | Insufficient documentation provided |
| Oakland Citizens Community for Urban Renewal (OCCUR) | \$36,671             | 1               | Insufficient documentation provided |
| Bank of America Commercial Revitalization Loan       | \$25,575             | 1               | No documentation provided           |
| Secondary Loans Housing Revitalization               | \$22,000             | 1               | No documentation provided           |
| Crossroads Family Center                             | \$2,600              | 1               | No documentation provided           |
| <b>TOTAL</b>   | <b>\$13,997,297</b>  | <b>14</b>       |                                     |

Source: Oracle Financial System and FMA and CEDA Management

Appropriate supporting documentation to validate a loan's existence, terms, payment history and aging analysis would have included:

- Background documentation explaining the purpose of the loan
- Promissory note showing approval of the loan terms by the City and the debtor
- Documentation showing whether or not any payments had been made on the loan
- Accounting records to demonstrate that the accounts had been reviewed on a periodic basis, aging analyses were prepared at proper intervals, and if necessary, estimates were prepared if the loan was considered at risk of not being collected

For the six OHA and two ORA loans, which are related to the Hyatt and subsequently Marriott Hotel, FMA provided background documentation about the reasoning for the loans.

**However, there were no promissory notes, documentation about payments made, or up to date accounting records that provided information about the current status of the loans. According to the City Auditor's Office's 1995 report of Active Loans Receivables, the loans to OHA and ORA were to be paid off from the positive cash flow of the sale of the hotel. The sale of the Marriott Hotel occurred in 2007.**

From the information provided, CEDA and FMA Management could not explain why the sale did not liquidate the loans.

On September 30, 2010, at the conclusion of this audit, CEDA Management provided a memo to FMA Management stating that the approximately \$13.8 million in OHA and ORA loans were erroneously kept on the books and should have been removed with the sale of the Marriott Hotel in 2007. The memo directs FMA to remove these loans from the books.

For the Bananas, Inc. loan, only a "Customer Master File History" document was provided detailing the loan due date and amount. No additional documentation was provided.

For the OCCUR loan, minimal documentation was provided. A promissory note was provided, however a report from the City Auditor's Office in 1995 shows that the City Attorney's Office was tasked to follow up on the OCCUR loan to identify the process to convert the loan to a grant. Neither CEDA nor FMA Management provided any documentation stating that the loan was approved to be converted to a grant.

For the remaining four loans, no documentation was provided. According to CEDA Management, in FY 1998-99, the management of loan receivables was transferred from FMA to CEDA Fiscal. Adequate documentation and knowledge of the loan histories were not maintained after the transfer.

Due to inadequate internal controls over loan receivables, the City could not determine whether or not it was owed approximately \$14 million in loan repayments

Due to the status of these loans being unknown until this audit, with the status of some still unknown, the City could have been owed approximately \$14 million in loan repayments if these loans were due. The audit found at least approximately \$13.8 million of the \$14 million in loan receivables should have been written off. The remaining balance potentially should already have been collected. Furthermore, there was the potential that interest revenue had not been collected if interest should have been applied to these loans. Consequently, FMA Management was maintaining inaccurate financial records. During the audit, FMA Management required a retired accounts receivables specialist to return to the City to track down and review loan documentation. If FMA and CEDA Management had accurate and updated documentation available, they would have been knowledgeable of the status of the loans rather than relying on retired staff to return to the City.

We recommend that FMA and CEDA Management evaluate the design and operation of their internal controls over loan receivables. Specifically, we recommend that CEDA and FMA Management immediately review its loan receivables system to implement best practices and prepare detailed Development loan policies and procedures to ensure all loan receivable records are complete and accurate. In addition, we recommend that FMA and CEDA Management coordinate to conduct an annual review of all loans, to ensure that all loan receivable records in the sub-ledger and in Oracle are complete and accurate. Lastly, we recommend that CEDA and FMA Management find the supporting documentation for the remaining Development loans, and determine if the loans are still collectible or if they should be written off.

## Conclusion

The audit found that CEDA Management did not have adequate supporting documentation and with several loans no supporting documentation for approximately \$14 million in loan receivables. Specifically, best practices were not in place to ensure sufficient internal controls were operating so that financial data could be relied upon. The City's accounting records were inaccurate and the system failed to properly reflect the City's current assets and liabilities. The audit found at least approximately \$13.8 million of the \$14 million in loan receivables should have been written off. The remaining approximately \$200,000 potentially should already have been collected. Furthermore, there was the potential that interest revenue had not been collected if interest should have been applied to these loans. Consequently, FMA was maintaining inaccurate financial records.

## RECOMMENDATIONS

### We recommend that the FMA and CEDA Management:

|  |  |
|--|--|
| Recommendation #1  | <p>Evaluate the design and operation of their internal controls over loan receivables including the establishment of policies and procedures to ensure:</p> <ol style="list-style-type: none"> <li>1. Accurate loan values, dates and payment terms are recorded</li> <li>2. Loan receivable aging analysis is prepared and reviewed monthly by management and for deferred loans a tracking system should be established.</li> <li>3. An allowance for doubtful accounts policy is established that includes preparing periodic estimates of uncollectible loan balances for review and authorization by management</li> <li>4. All loan write-offs, grant conversions or forgiveness of delinquent loans have a clear audit trail that documents the justification for writing off, forgiving or converting the loan including all authorizing signatures and City Council resolutions if applicable.</li> </ol> |
| Recommendation #2  | <p>Conduct an annual review of all loans to ensure that all loan receivable records in the sub-ledger and in Oracle are complete and accurate.</p>   |
| Recommendation #3  | <p>Find the supporting documentation for the remaining Development loans where the write off process has not yet been initiated and determine if the loans are still collectible, including interest revenue or if they should be written off.</p>   |
| <b>We recommend that the City's external financial statement auditors:</b> |  |
| Recommendation #4  | <p>Increase their internal control testing of receivables during the next financial statement audit.</p>   |

## CHAPTER 2

### FMA AND CEDA MANAGEMENT DID NOT ACCURATELY RECORD APPROXIMATELY \$220,000 IN LOAN RECEIVABLES THAT HAD BEEN CONVERTED TO GRANTS BY CITY COUNCIL OVER 10 YEARS AGO

Best practices recommend that there be sufficient internal controls in place so that financial data can be relied upon

The audit found three approved loans that were incorrectly accounted for in Oracle, which totaled approximately \$220,000 as shown in Exhibit 5. City Council approved a loan to the Organized People of Elmhurst Neighborhood (OPEN) and a loan to Pro Arts to be converted to grants. However, these loans were still recorded in Oracle as loan receivables as of the end of FY 2008-09.

The audit also found that according to CEDA Management, the loan to OCCUR was also approved to be a grant. However, CEDA Management did not provide any documentation to show that City Council approved the loan to be converted to a grant.

Consequently, the City's financial records inaccurately reflected these grants as outstanding loans in Oracle for more than ten years. As a result, the audit found the City's internal controls over loan conversions are insufficient to provide reasonable assurance that the financial information is accurate and reliable.

#### Exhibit 5: GRANTS OR POTENTIAL GRANTS INACCURATELY RECORDED AS LOANS IN ORACLE

| Debtor   | Amount           | Resolution No. & Date              | Status in Oracle Fiscal Year End 2009 |
|--|------------------|------------------------------------|---------------------------------------|
| Organized People of Elmhurst Neighborhood (OPEN)                 | \$165,000        | Res. 72442 C.M.S.<br>February 1996 | Open Loan                             |
| Pro Arts   | \$20,000         | Res. 66471 C.M.S.<br>July 1989     | Open Loan                             |
| Oakland Citizen Community for Urban Renewal (OCCUR) <sup>5</sup> | \$36,671         | Not provided                       | Open Loan                             |
| <b>TOTAL</b>   | <b>\$221,671</b> |                                    |                                       |

Source: Oracle Financial System, FMA and CEDA Management and Office of the City Clerk

<sup>5</sup> According to CEDA Management, the OCCUR loan was approved to be a grant. Without a City Council Resolution, this loan conversion cannot be confirmed.

CEDA Management has inadequate internal controls in place to ensure outstanding loan balances are accurate

CEDA Management lacks the proper controls to ensure that all loan balances are accurate and that relevant documentation for the loans is maintained by staff. CEDA Management stated that it submits quarterly loan invoice adjustment entries to FMA Management documenting updates that have been made to loans. Although this control is in place, the control is not designed to detect loans that were authorized to be converted into grants. As a result of this significant control gap in the loan receivables process, the grants remained inaccurately recorded as loans for over a ten year period.

We recommend that CEDA Management establish effective internal controls over loan conversions. Additionally, we recommend CEDA and FMA Management coordinate to conduct jointly an annual review of all outstanding loans to ensure all loan records include supporting documentation and are complete and accurate. We also recommend that CEDA Management should create a system of internal controls that tracks, links, and monitors loans to City Council actions. Lastly, we recommend that CEDA Management accurately account for the OPEN and Pro Art loans as grants, and determine if the OCCUR loan is indeed a grant, and if so, accurately account for the conversion, which would include conducting the loan write off process.

## Conclusion

The audit found that two of the 16 Development loans identified in the audit were approved to be converted to grants by City Council. For over ten years, these loan receivables were not updated in Oracle to show that these loans were grants. CEDA Management stated that one additional loan was approved to be converted to a grant; however, CEDA Management did not provide any documentation to support this claim. CEDA Management lacks the proper controls to ensure that all loans balances are accurate and that relevant supporting documentation is maintained by staff.

## RECOMMENDATIONS

### We recommend that CEDA Management:

|                   |   |
|-------------------|---|
| Recommendation #5 | Establish effective internal controls over loan conversions by developing appropriate procedures to record loans as grants and make the necessary updates to the loans which were approved to be converted to grants.   |
| Recommendation #6 | Perform an annual review of all loan receivables that would ensure that all loans that have been approved to be accounted for as grants by City Council Resolution are recorded accurately, and create a system of internal controls that tracks, links, and monitors loans to actions taken by City Council. |
| Recommendation #7 | Accurately account for the OPEN and Pro Art loans as grants, and determine if the OCCUR loan is indeed a grant, and if so, accurately account for the conversion, including conducting the loan write off process.  |

## CHAPTER 3

### **CEDA MANAGEMENT DID NOT MAINTAIN ANY DOCUMENTATION FOR DEEMING APPROXIMATELY \$100,000 IN LOAN RECEIVABLES AS UNCOLLECTIBLE**

FMA Management relies on CEDA Management to direct their staff on when to classify a loan receivable as uncollectible. The three short-term loans listed in Exhibit 6 were issued by the previous OEDE office; therefore, neither FMA nor CEDA Management knew what procedures were applied to these loans. CEDA Management did not provide any documentation to show why these three loans were deemed uncollectible.

Best practices recommend that there be sufficient internal controls in place so that financial data can be relied upon

As stated in Chapter I, GFOA best practices state a sound framework of internal controls is necessary to afford a reasonable basis for finance officers to assert that the information they provide can be relied upon. Without proper supporting documentation for loans where an allowance for doubtful accounts has been established, CEDA Management cannot verify that the loans were accurately determined to be uncollectible.

CEDA Management should establish a clear allowance for doubtful accounts policy to ensure that the financial records properly reflect the amount of the loan receivables that management estimates will be uncollectible. The method of establishing an allowance for doubtful accounts should be left to management's discretion. However, the estimated allowance should be based upon historical data or other pertinent information, and the rationale should be clearly documented. Neither CEDA nor FMA Management provided documentation to demonstrate the rationale for establishing a doubtful allowance account for the three loans shown in Exhibit 6.

CEDA Management should have documentation that shows how each of these loans meets the criteria to be deemed uncollectible. It should also maintain documentation that shows approval for the establishment of a doubtful allowance account for these loans. Lastly, it should establish a policy regarding the length of time the receivable and the allowance account will remain on the books before being removed completely.

### **Exhibit 6: AMOUNT RECORDED IN ALLOWANCE FOR DOUBTFUL ACCOUNTS**

| <b>Debtor</b>                                      | <b>Allowance Amount</b> |
|--|-------------------------|
| Bananas Inc.                                       | \$50,000                |
| Pro Arts   | \$20,000                |
| OCCUR  | \$36,672                |
| <b>TOTAL</b>                                       | <b>\$106,672</b>        |
| Source: Oracle Financial System and FMA Management |                         |

#### The City's accounting records inaccurately reflected grants as loans

With no supporting documentation to show why these loans were treated as uncollectible and no effective tracking of these loans, the City continues to maintain these assets in its accounts. The accounting system failed to document why the allowance was created and failed to set a time limit when the receivable would be removed from the City's assets. As discussed in Chapter 2, two of the three loans were converted to grants and their corresponding allowances should have been removed from the accounts when the loan was converted to a grant. Carrying the approximately \$100,000 allowance for doubtful accounts in the City's financial records has no financial impact because the allowance netted against the receivable balance equals zero. However, the City's maintaining financial records that are inaccurate highlights the lack of a properly designed and implemented system of internal controls over loan receivables.

We recommend that CEDA and FMA Management establish a policy and procedure for loan receivables allowance of doubtful accounts. Furthermore, we recommend CEDA Management ensure that all loans tracked in the allowance for doubtful accounts have proper supporting documentation and approval.

## **Conclusion**

CEDA Management did not maintain any evidence to document the rationale for establishing an allowance for doubtful accounts for approximately \$100,000 in loan receivables. Without proper supporting documentation for loans where an allowance for doubtful accounts has been established, CEDA Management cannot verify that the loans were accurately determined to be uncollectible. CEDA Management should have documentation that shows how each of these loans meets the criteria to be deemed uncollectible. CEDA Management should have also provided documentation that shows approval for the establishment of a doubtful allowance account for these loans. The impact is that the City is maintaining financial records that are inaccurate and it is incumbent upon management to design and then operate a system of internal controls that provide a reasonable basis for financial officers to assert that the information may be relied upon.

## RECOMMENDATIONS

### We recommend that CEDA and FMA Management:

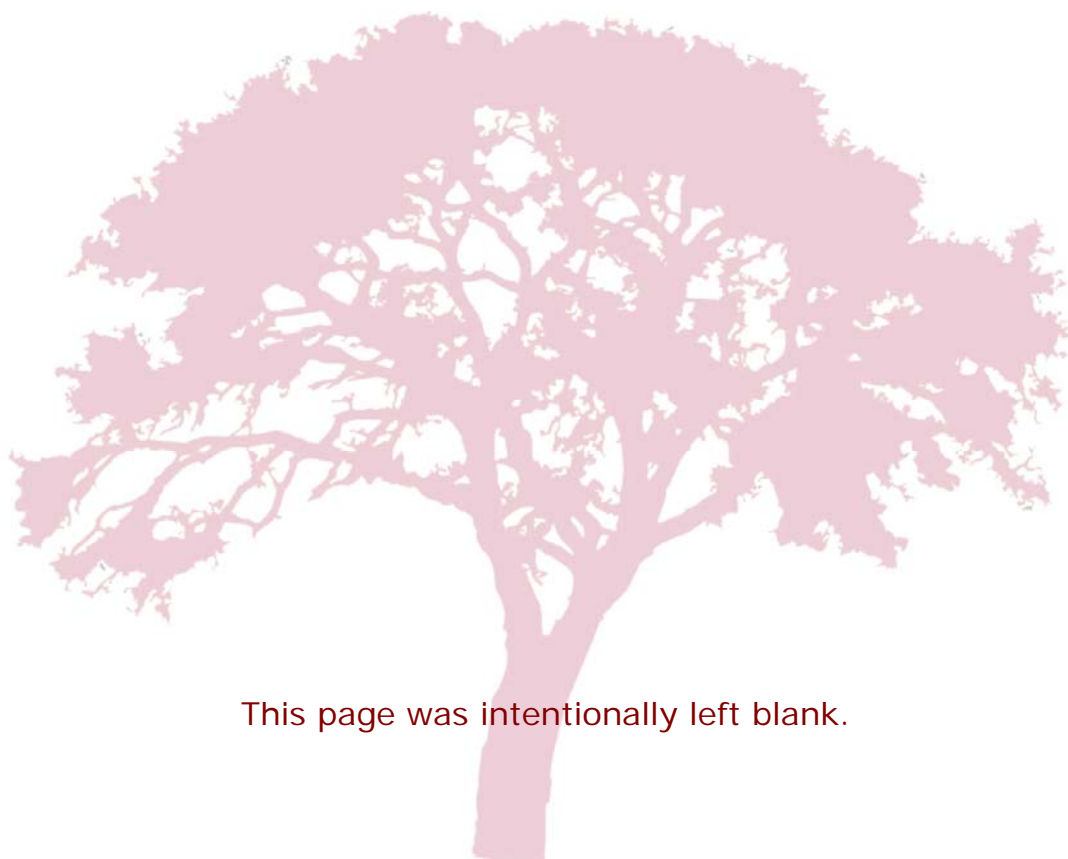
#### Recommendation #8

Establish a loan receivables policy and procedure for allowance for doubtful accounts, which should detail the criteria for when an account is doubtful and the specific process for accurately establishing an allowance for doubtful account.

### We recommend that CEDA Management:

#### Recommendation #9

Ensure that all loans that are tracked in the “allowance for doubtful accounts” have the appropriate approvals and supporting documentation stating why the loans may not be collectible.



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## CHAPTER 4

### FMA MANAGEMENT INACCURATELY RECORDED ALL DEVELOPMENT LOANS' DUE DATES AND LOAN PAYMENTS TERMS IN ORACLE

For all of the 16 CEDA Development loans reviewed during the audit, the due dates and the payment terms were inaccurate. All of the long term loans are deferred and are due upon sale or transfer of the property, thus any specific due date in Oracle for the loan would be inaccurate. Furthermore, CEDA and FMA Management were not able to determine actual payment terms for these loans listed in Oracle because insufficient loan documentation was located to provide this information.

Although Oracle is inaccurate, it is not the main record keeping system for loan receivables. The sub-ledgers maintained by CEDA Fiscal track the various loans. However, the audit found the data transfer from the sub-ledger to the general ledger in Oracle was a manual process, as shown in Exhibit 3 in the Background section of this report. Without a robust tracking system, including regular review of loan documentation between CEDA and FMA Management, Oracle records cannot be accurately maintained.

Furthermore, FMA Management stated that it could not update the loan due dates and payment terms in Oracle because the fields are not updatable. The loan due dates and payment terms were automatically entered into the system during the last system conversion to Oracle in FY 1998-99. Instead of using the due dates and payment terms, FMA Management can identify the loans as deferred by the transaction type. They can also update the "Reference" field with additional notes about the loan. To change the due date, FMA Management would need to void the loan and recreate the loan transaction in Oracle. Currently, for new loans originated in Oracle, FMA Management has the ability to specify whether or not a loan is deferred in the "Payment Term" and "Due Date" fields. Exhibit 7 below highlights the "Reference" field and "Payment Term" and "Due Date" fields in Oracle.

## Exhibit 7: ORACLE SCREENSHOT SHOWING UPDATABLE FIELDS

This field is updatable.

These fields are not updatable.

The City is at risk of not being able to rely upon its financial data to ensure timely collection of loan receivables.

CEDA Management does not have adequate internal controls in place to monitor the outstanding loans in Oracle and to ensure that the information in Oracle is accurate. As stated earlier, internal controls provide reasonable assurance that financial reporting can be relied upon. If financial data is inaccurate, appropriate recording of loans will not occur.

With inaccurate loan due dates and payment terms in Oracle, the City does not know when a loan or specific loan payment is actually due. Oracle records should reflect the most current data from the sub-ledgers to provide reliable loan receivable reporting. We recommend that FMA and CEDA Management update the "Reference" field to include the accurate due dates and payment terms for the remaining<sup>6</sup> Development loans in Oracle in order to establish a reliable reporting system.

## Conclusion

For the 16 CEDA Development loans selected in our sample the due dates and the payment terms were inaccurate. The CEDA sub-ledgers are the primary system used to actively monitor the loans. Oracle needs to reflect the relevant data from the sub-ledgers to ensure accurate financial reporting. We recommend that FMA Management address the inaccurate due dates and payment terms in Oracle in the "Reference" field to ensure a reliable reporting system.

<sup>6</sup> As stated in Chapter 1, at the conclusion of the audit CEDA Management determined that 8 of the 16 loans should be written off.

## RECOMMENDATIONS

### We recommend that CEDA and FMA Management:

#### Recommendation #10

Update the "Reference" field for each of the remaining Development loans that are not being written off to reflect the accurate due date and payment term for the loan. In addition, as part of the annual review in recommendation #2, review the loan due dates and payment terms to ensure accuracy of the recording of the loans.

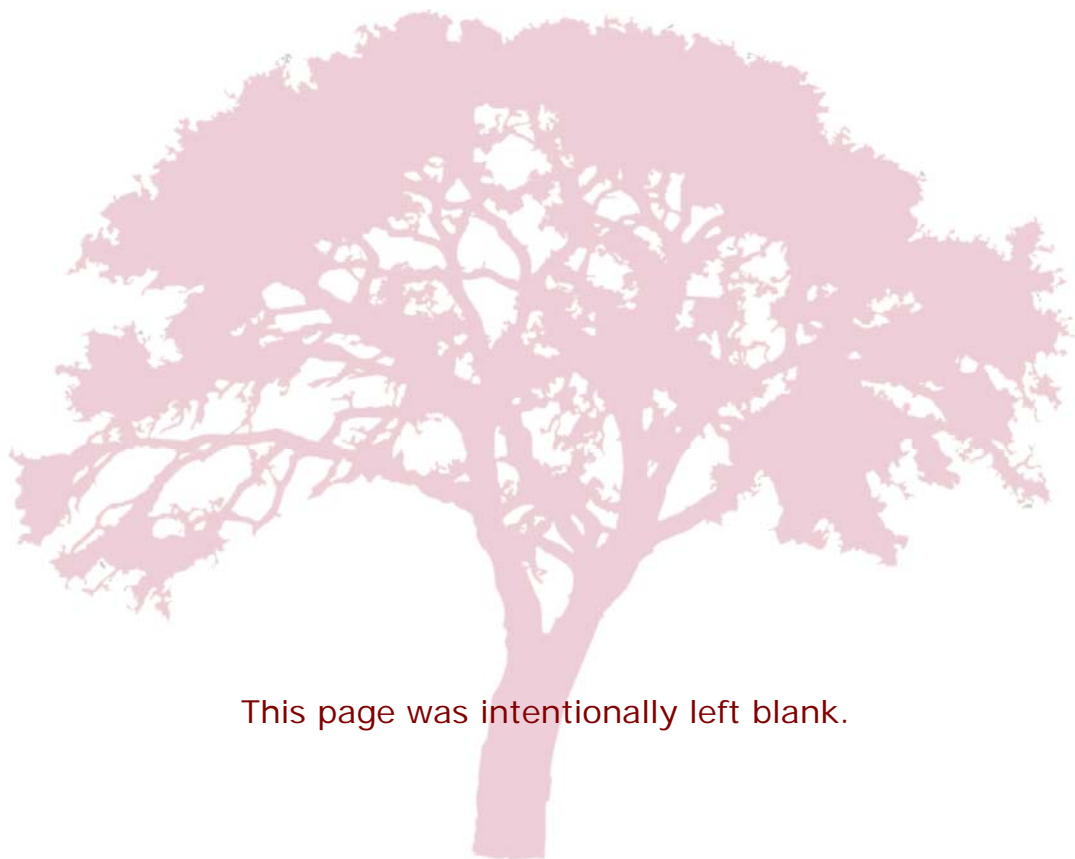
## SECTION ONE SUMMARY MATRIX

| Item No. | Organization Name                                       | Loan Amount  | Chapter One<br>No Documentation<br>Provided | Chapter One<br>Insufficient<br>Documentation<br>Provided | Chapter Two<br>Loans that should<br>have been accounted<br>for as Grants | Chapter Three<br>Loans were<br>Deemed<br>Uncollectible | Chapter Four<br>Inaccurate Due<br>dates and<br>payment terms |
|----------|---|--------------|---|--|--|--|--|
| 1        | OCCUR   | \$36,671.64  |   | X  | X  | X  | X  |
| 2        | BANANAS INC   | 50,000.00    |   | X  |  | X  | X  |
| 3        | PRO ART   | 20,000.00    |   |  | X  | X  | X  |
| 4        | OAKLAND HOTEL<br>ASSOC. LTD                             | 6,229,798.23 |   | X  |  |  | X  |
| 5        | OAKLAND HOTEL<br>ASSOC. LTD                             | 1,756,585.87 |   | X  |  |  | X  |
| 6        | OAKLAND HOTEL<br>ASSOC. LTD                             | 3,000,000.00 |   | X  |  |  | X  |
| 7        | OAKLAND HOTEL<br>ASSOC. LTD                             | 379,140.54   |   | X  |  |  | X  |
| 8        | OAKLAND<br>RENAISSANCE ASS.,<br>LTD                     | 1,414,809.30 |   | X  |  |  | X  |
| 9        | OAKLAND<br>RENAISSANCE ASS.,<br>LTD                     | 354,884.51   |   | X  |  |  | X  |
| 10       | OAKLAND HOTEL<br>ASS. LTD                               | 98,241.00    |   | X  |  |  | X  |
| 11       | OAKLAND HOTEL<br>ASS. LTD                               | 574,548.52   |   | X  |  |  | X  |
| 12       | OAKLAND<br>BUSINESS DEV.<br>CORP.                       | 52,444.00    | X   |  |  |  | X  |
| 13       | CROSSROAD<br>FAMILY CENTER,<br>INC.                     | 2,600.00     | X   |  |  |  | X  |
| 14       | BANK OF AMERICA<br>COMMERCIAL<br>INDUSTRY<br>REVITALIZ. | 25,575.37    | X   |  |  |  | X  |
| 15       | THE ORGANIZES<br>PEOPLE OF ELMH.                        | 165,000.00   |   |  | X  |  | X  |
| 16       | SECONDARY LOANS<br>HOUSING REV.<br>LOAN PROGRAM         | 22,000.00    | X   |  |  |  | X  |
| TOTAL    |   | \$14,182,299 |   |  |  |  |  |



## **SECTION TWO**

## **HOMEBUYER LOAN PROGRAMS**



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Among the various residential programs administered by the CEDA Housing and Community Development (HCD) Division, the audit identified two residential homebuyer programs that are City-funded through the Property Tax Increment Fund (Fund 2185).

First Time Home Buyer Program- Mortgage Assistance Program (MAP)

The purpose of MAP is to assist low-income, first time homebuyers with the purchase of homes in the City of Oakland. MAP loans may not exceed \$75,000 for borrowers with income less than 80% average median income (AMI ), or \$50,000 for borrowers with income between 81% and 100% of AMI<sup>7</sup>. At the end of FY 2008-09, these loan receivables totaled approximately \$26.2 million.

Public Safety Employees & Teachers Downpayment Assistance Program (PSE-DAP)

The purpose of PSE-DAP is to loan funds to public safety employees and teachers for down payment and/or closing costs for the purchase of owner occupied, single family homes in the City of Oakland. The maximum loan amount is \$20,000. The majority of public safety employees and teachers qualify for larger loans under MAP, thus this loan program is underutilized compared to MAP. At the end of FY 2008-09, these loan receivables totaled approximately \$300,000.

The audit reviewed PSE-DAP to determine if there were documented policies and procedures for the loan receivables process, and to evaluate whether or not the policies and procedures in place assure proper management and oversight of outstanding loans, defaulted loans and loan payments.

The audit found CEDA Management has:

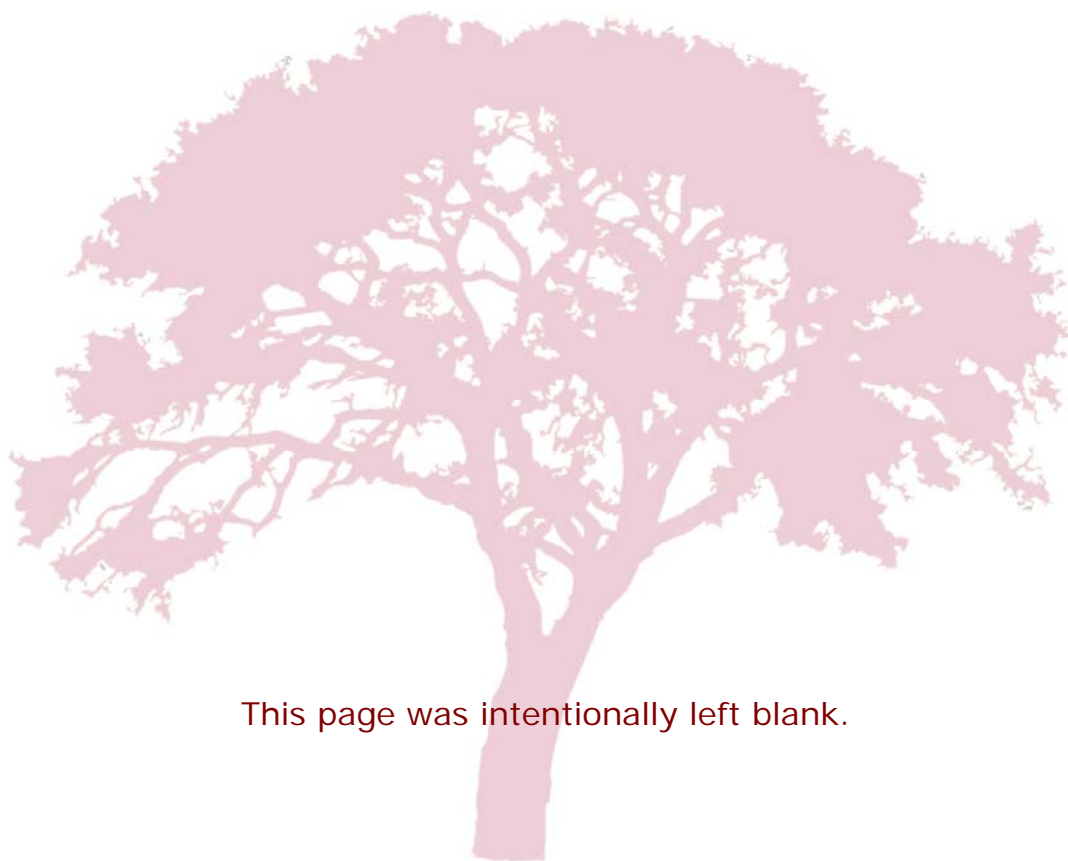
- Inadequate policies and procedures
- No fraud assessment training for staff
- Inaccurately recorded loan data in the subsidiary ledgers

**We recommend that CEDA Management comprehensively document all loan receivables policies and procedures and develop a formal fraud assessment training to ensure all staff are able to prevent and detect fraud. We also recommend that CEDA Management coordinate with FMA Management to conduct an annual reconciliation of all homebuyer loans to ensure:**

- Oracle and the subsidiary ledgers are complete and accurate
- All supporting loan documentation is maintained

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<sup>7</sup> Area Median Income is calculated by the federal government that sets a maximum income limit for a household to be eligible for certain programs. AMI varies by geographic region with adjustments for family size.



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## CHAPTER 5

### **CEDA MANAGEMENT DOES NOT HAVE COMPREHENSIVE AND UPDATED POLICIES AND PROCEDURES FOR THE HOMEBUYER LOAN RECEIVABLES, NOR DO THEY HAVE ADEQUATE AND FORMALIZED FRAUD TRAINING**

Best practices recommend accounting policies and procedures should be comprehensive and made available to employees.

According to Government Finance Officers Association (GFOA), the documentation of accounting policies should be readily available to all employees who need it. It should delineate the authority and responsibility of all employees, especially the authority to authorize transactions and the responsibility for safekeeping of assets and records. Additionally, the documentation of accounting policies and procedures should explain the design and purpose of control-related procedures to increase employee understanding of and support for controls. Up to date policies and procedures are necessary to provide staff with the appropriate practices necessary to accurately and completely record loan transactions. Furthermore, GFOA recommends that every government establish policies and procedures to encourage and facilitate the report of fraud or abuse and questionable accounting or auditing practices.

Clearly documented policies and procedures ensure that staff knows its responsibilities. Furthermore, if new staff arrives, staff should be able to rely on the documented policies and procedures to inform them of the steps necessary to perform daily tasks. To ensure accuracy, policies and procedures should be reviewed on a periodic basis, signed as reviewed by management and dated.

CEDA Management did not have comprehensive and up to date homebuyer loan processing policies and procedures.

CEDA Management provided the Office with the following documents:

- CEDA/HCD Loan Payment Processing Instructions
- Residential Lending Loan Servicing Policies and Procedures

The CEDA/HCD Loan Payment Processing Instructions included a flowchart of the process, roles and responsibilities, procedures for new loans, adjustments, payments, schedules and reconciliation. The Residential Lending Loan Servicing policies and procedures included details regarding roles and responsibilities, loan review and booking, collections, delinquency prevention, foreclosure and deeds of reconveyance. Although the policies and procedures outlined the internal controls in the loan receivables process, the following was not included in the policies and procedures:

- Specific procedures for prevention or detection of fraud
- Procedures for cancelled loans

Additionally, the documented policies and procedures CEDA provided were outdated, meaning that policies and procedures were not reflective of the current loan receivable processing environment. Furthermore, CEDA Management did not provide evidence that the policies and procedures were communicated to staff. By not having comprehensive and updated policies and procedures, the City is at risk of inaccurately recording loan transactions. We recommend that CEDA Management review and continue to periodically review policies and procedures to ensure that they are updated to reflect the current industry standards and the current operating environment. Specifically, CEDA Management should ensure that all key processes are addressed, including the loan cancellation process.

CEDA Management should develop formal fraud assessment training and a guideline.

According to CEDA Management, the loan receivable process has internal controls built within the system that successfully eliminate fraud. However, CEDA Management also acknowledged the absence of formal fraud training for staff. If staff is not trained or are not aware of how to prevent or detect fraud, then there is a greater risk that fraud may go undetected in the loan receivable process.

We recommend that CEDA Management develop formal fraud training and policies and procedures for staff.

## Conclusion

Although CEDA Management does have informal homebuyer policies and procedures that outline the internal controls in the loan receivables process, the following were not included in the policies and procedures:

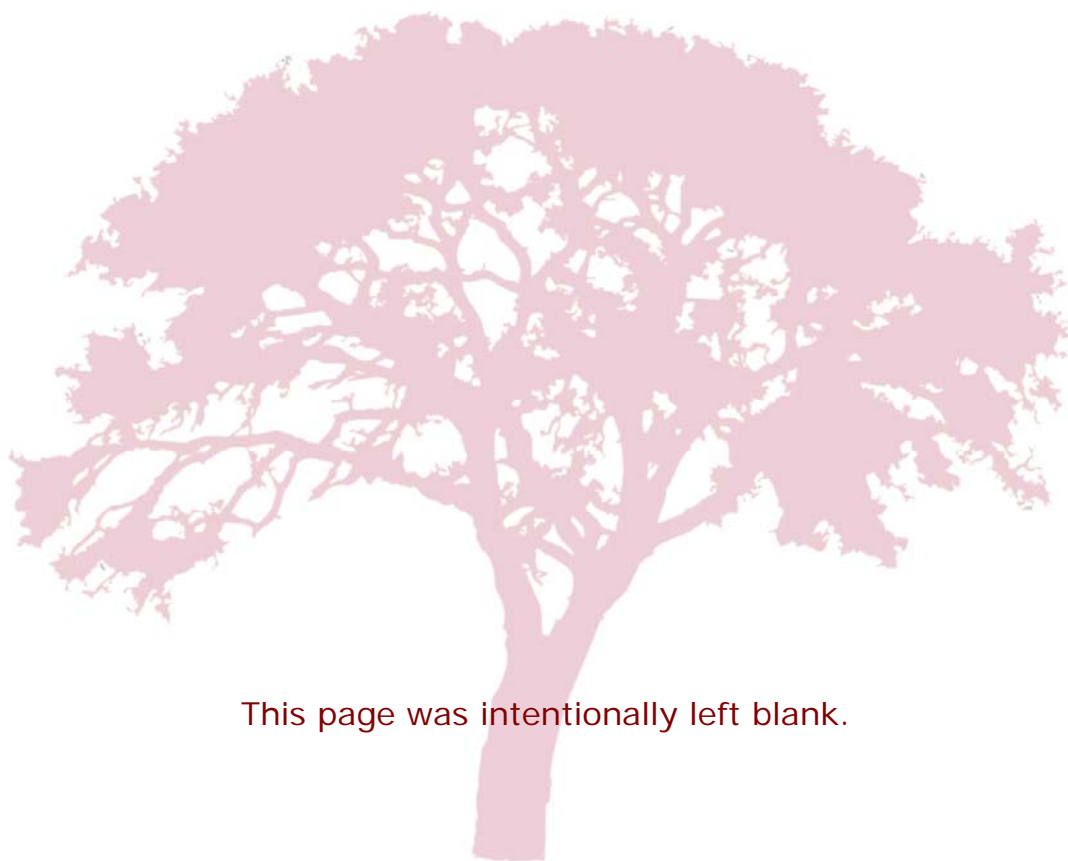
- Specific procedures for prevention or detection of fraud
- Procedures for cancelled loans

Additionally, the policies and procedures in existence were both outdated and had not been communicated to staff. Specifically related to fraud, if staff are not trained on how to prevent or detect fraud, then there is a greater risk that fraud will go undetected. We recommend that CEDA Management develop formal fraud training and comprehensive policies and procedures for staff.

## RECOMMENDATIONS

We recommend that CEDA Management for the Homebuyer Loan Programs:

|                    |   |
|--------------------|---|
| Recommendation #11 | Update all homebuyer loan processing policies and procedures to ensure all key loan receivables processes are documented. |
| Recommendation #12 | Ensure the revised homebuyer loan receivables policies and procedures are communicated to staff.                          |
| Recommendation #13 | Include specific guidelines on how to prevent and detect fraud in homebuyer loan receivables process procedures.          |
| Recommendation #14 | Implement homebuyer loan program fraud training for staff.  |



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## CHAPTER 6

### SUBSIDIARY LEDGERS USED TO MAINTAIN ORACLE ARE INACCURATE THEREFORE THE PROCESS IS FLAWED AND ERRORS EXCEEDED \$450,000

#### MAP Loans Testing

As a part of the audit, a judgmental sample of 10 MAP loans was selected. The audit found that each loan was properly approved according to the CEDA/HCD Loan Payment Processing Instructions and the loan repayments were accurately recorded in Oracle. Furthermore, the audit found MAP to be successful in preventing foreclosures, with less than 1% of approximately 700 MAP loans in default since the program began in 1994 and no foreclosures occurring since 2005. However, the audit also identified areas for improvement based on inaccurate accounting of loans where the MAP subsidiary ledger and Notes and Loan Receivables subsidiary ledger did not agree with Oracle.

#### PSE-DAP Loans Testing

The audit found that neither CEDA nor FMA Management accounted for approximately \$300,000 in PSE-DAP loans in FY 2008-09 Notes and Loans Receivables. Specifically, FY 2008-09 PSE-DAP loans were not entered into Oracle until FY 2009-10.

**FMA has  
inaccurately  
recorded loan data  
in two financial  
subsidiary ledgers**

#### Subsidiary Ledgers

As shown in Exhibit 3 (page 11) in the Background section of this report, the MAP subsidiary ledger includes loan information such as the borrowers name, loan origination date, title company, principal payments made, interest payments made and the loan balance. The Notes and Loans Receivables sub-ledger is used to record all of the loans City-wide and includes the loan program or debtor's name, along with the account number and payments made on the loan for the fiscal year. Exhibit 8 summarizes the inaccuracies the audit found in the MAP subsidiary ledger and Notes and Loan Receivables sub-ledger. It also specifies the impact of those inaccuracies.

## Exhibit 8: SUBSIDIARY LEDGER INACCURACIES

| Subsidiary Ledger                    | Inaccuracies   | Impact   |
|--------------------------------------|--|--|
| MAP Sub-Ledger                       | One loan for approximately \$95,000 was inaccurately recorded as cancelled.  | Oracle was accurate; however the MAP sub-ledger is used to update Notes and Loans Receivable spreadsheet, which is then used to update Oracle. The fact that the error was not reflected in Oracle means the two systems were not reconciled and the system failed to work as designed and therefore is unreliable |
| MAP Sub-Ledger                       | One loan payment was inaccurately recorded in sub-ledger as \$59,277.58 while it was accurately recorded in Oracle as \$59,461.88. The sub-ledger was off by \$184.30. | Oracle was accurate; however the MAP sub-ledger is used to update Notes and Loans Receivable spreadsheet, which is then used to update Oracle. The fact that the error was not reflected in Oracle means the two systems were not reconciled and the system failed to work as designed and therefore is unreliable |
| Notes & Loans Receivables Sub-ledger | Approximately \$150,000 in doubtful loans receivables were recorded to the wrong fund.   | The City overstated the MAP loans receivables in the Property Tax Increment fund by approximately \$150,000 and understated Housing and Urban Development (HUD) loans receivables fund by approximately \$150,000 in Oracle.   |
| Notes & Loans Receivables Sub-ledger | Approximately \$300,000 in PSE-DAP loans were not accounted for in FY 2008-09 in the Property Tax Increment Fund (Fund 2185).  | Oracle was inaccurate, the loans receivables in Fund 2185 were understated by approximately \$300,000 in PSE-DAP loans.<br><br>PSE-DAP loans were not entered into Oracle until April 19, 2010.  |
| Source: FMA and CEDA Management      |  |  |

The City overstated the Property Tax Increment Fund by approximately \$150,000 and understated HUD loans receivables fund by approximately \$150,000

CEDA Management does not have adequate internal controls in place to ensure that the outstanding loans in Oracle are monitored and that the information in Oracle is accurate. As a result, the City overstated the Property Tax Increment Fund by approximately \$150,000 in default loans and subsequently understated the HUD loan receivables fund by approximately \$150,000 in default loans.

The City understated loan receivables in the Property Tax Increment Fund overall by approximately \$300,000.

PSE-DAP loan receivables were not included in the FY 2008-09 Notes and Loans Receivable sub-ledger, which is used to complete the City's financial statements. Since PSE-DAP loans were not included in the spreadsheet, loan receivables were understated by approximately \$300,000. Furthermore, PSE-DAP loans were not entered into Oracle until April 19, 2010, meaning that for a majority of FY 2009-10 the PSE-DAP were not accounted for as well.

Without proper recording of loans in the sub-ledger or Oracle, the system of internal controls failed to operate as designed and inaccurate financial data was recorded in three different systems that are not properly reconciled.

We recommend that CEDA Management correct the inaccuracies to the MAP subsidiary ledger and Notes and Loans Receivables spreadsheet. We also recommend that CEDA Management evaluate its internal controls over loan receivable subsidiary systems to ensure that there are controls in place that are designed to prevent and detect loan data inaccuracies. Lastly, we recommend that CEDA Management research and evaluate systems that would have the capability to automatically interface with Oracle to update loan data.

## Conclusion

The audit found that the City has several inaccuracies between Oracle, the Notes and Loans Receivable sub-ledger and the MAP sub-ledger. These inaccuracies resulted in overstating the MAP loan receivables by approximately \$150,000 and understating PSE-DAP loans by approximately \$300,000 in the Property Tax Increment Fund. We recommend that CEDA Management evaluate their internal controls over loan receivables to ensure that there are controls in place that are designed to prevent and detect loan data inaccuracies. We also recommend that CEDA Management research and evaluate systems that would have the capability to automatically interface with Oracle to update loan data.

## RECOMMENDATIONS

### We recommend that CEDA Management:

|                    |  |
|--------------------|--|
| Recommendation #15 | Correct the inaccuracies to the MAP sub-ledger and Notes and Loans Receivables sub-ledger.   |
| Recommendation #16 | Improve internal controls over loan receivable subsidiary systems to ensure that there are controls in place that are designed to prevent and detect loan data inaccuracies including appropriate reconciliations. Specifically, ensure that all loans in CEDA's sub-ledgers are reviewed and reconciled to each loan in Oracle as part of the quarterly invoice adjustment process. |
| Recommendation #17 | Research and evaluate systems available that would allow for automatic system integration with Oracle.   |

## Appendix 1: DEVELOPMENT LOANS REVIEWED

| Item No. | Organization Name   | Loan Balance    | Origination Date in Oracle | Due Date in Oracle | Status in Oracle |
|----------|---|-----------------|----------------------------|--------------------|------------------|
| 1        | Oakland Citizens Community for Urban Renewal                    | \$36,671.64     | 26-Feb-88                  | 2/27/1992          | Open             |
| 2        | Bananas Inc.  | \$50,000.00     | 30-Aug-89                  | 8/31/1993          | Open             |
| 3        | Pro Arts  | \$ 20,000.00    | 13-Jul-86                  | 7/15/1990          | Open             |
| 4        | Oakland Hotel Association                                       | \$6,229,798.23  | 4-Nov-86                   | 11/5/1990          | Open             |
| 5        | Oakland Hotel Association                                       | \$1,756,585.87  | 4-Nov-86                   | 11/5/1990          | Open             |
| 6        | Oakland Hotel Association                                       | \$3,000,000.00  | 4-Nov-86                   | 11/5/1990          | Open             |
| 7        | Oakland Hotel Association                                       | \$379,140.54    | 4-Nov-86                   | 11/5/1990          | Open             |
| 8        | Oakland Renaissance Association                                 | \$1,414,809.30  | 29-Apr-93                  | 4/30/1997          | Open             |
| 9        | Oakland Renaissance Association                                 | \$354,884.51    | 29-Apr-93                  | 4/30/1997          | Open             |
| 10       | Oakland Hotel Association                                       | \$98,241.00     | 29-Apr-93                  | 4/30/1997          | Open             |
| 11       | Oakland Hotel Association                                       | \$574,548.52    | 29-Apr-93                  | 4/30/1997          | Open             |
| 12       | Oakland Business Development Corp.                              | \$52,444.00     | 13-Jun-94                  | 6/14/1998          | Open             |
| 13       | Crossroads Family Center  | \$2,600.00      | 29-Apr-93                  | 3/1/1997           | Open             |
| 14       | Bank of America Commercial Industry Revitalization Loan Program | \$25,575.37     | 17-Jun-88                  | 6/18/1992          | Open             |
| 15       | The Organized People of Elmhurst Neighborhood                   | \$165,000.00    | 4-Nov-86                   | 11/5/1990          | Open             |
| 16       | Secondary Loans Housing Revitalization Program                  | \$22,000.00     | 31-Mar-89                  | 4/1/1993           | Open             |
| TOTAL    |   | \$14,182,298.98 |                            |                    |                  |

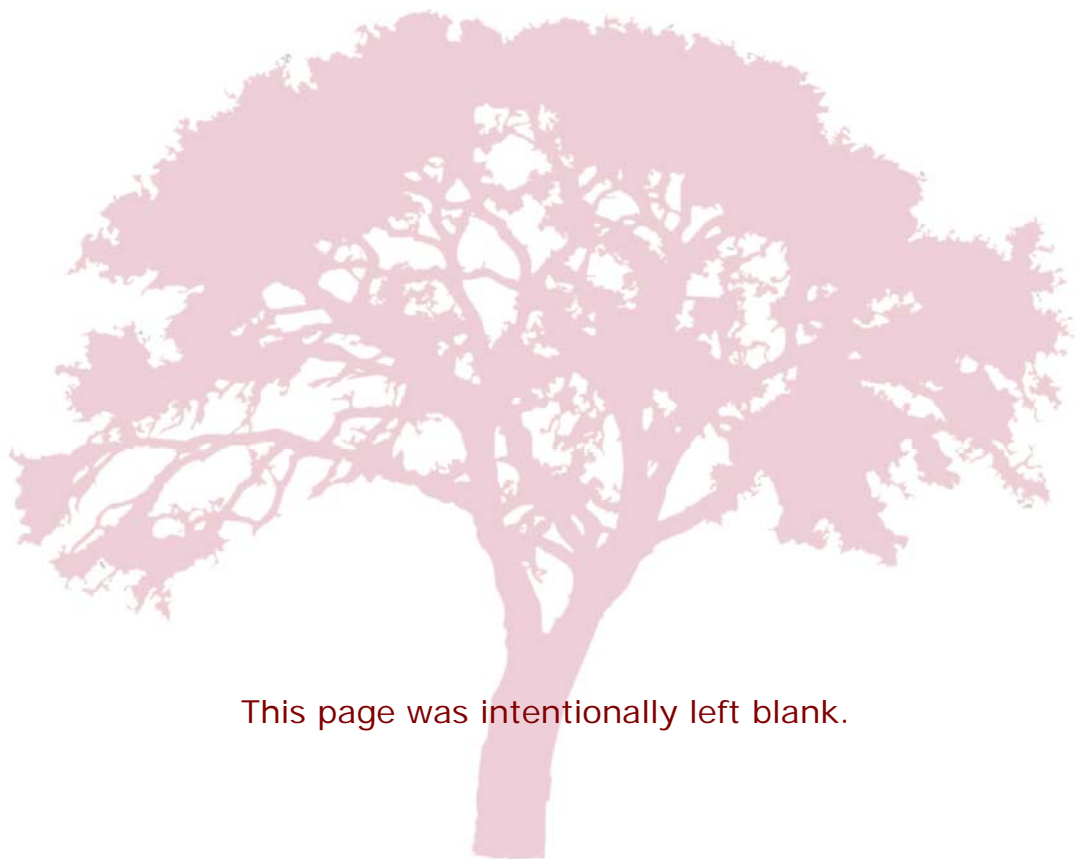
## Appendix 2: HOMEBUYER LOANS REVIEWED

| Item No.   | Invoice Number               | Loan Balance                  | Title Company           | Status of the Loan            |
|--|------------------------------|-------------------------------|-------------------------|-------------------------------|
| First Time Homebuyer Program – Mortgage Assistance Program (MAP)<br>(Judgmental sample of 10 loans – includes outstanding, paid, cancelled and foreclosed) |                              |                               |                         |                               |
| 1  | 06-1099-10M                  | \$75,000.00                   | Old Republic            | Partially Paid                |
| 2  | 07-1141-10M                  | \$47,519.43                   | Placer                  | Partially Paid                |
| 3  | 07-1154-01A                  | \$75,000.00                   | Commonwealth Land       | Open                          |
| 4  | 09-1266-10M                  | \$75,000.00                   | Chicago Title           | Open                          |
| 5  | 98-584-01M                   | \$0.00                        | Old Republic            | Paid in Full, Equity Stake    |
| 6  | 98-649-09M                   | \$0.00                        | Old Republic            | Paid in Full, Equity Stake    |
| 7  | 01-737-09M                   | \$0.00                        | Old Republic            | Paid in Full, Simple Interest |
| 8  | 08-1201-10M                  | \$0.00                        | Financial National      | Cancelled                     |
| 9  | 04-924-01M                   | <i>doubtful (\$50,000.00)</i> | Chicago Title           | Foreclosed                    |
| 10   | 96-355-03M                   | <i>doubtful (\$23,980.00)</i> | Old Republic            | Foreclosed                    |
|  | <b>Outstanding MAP Total</b> | <b>\$272,519.43</b>           |                         |                               |
| <b>Foreclosed MAP Loans Reviewed<sup>8</sup></b>   |                              |                               |                         |                               |
| 1  | 95-215-03M                   | <i>doubtful (\$12,232.89)</i> | Fidelity National Title | Foreclosed                    |
| 2  | 04-924-01M                   | <i>doubtful (\$50,000.00)</i> | Chicago Title           | Foreclosed                    |
| 3  | 96-355-03M                   | <i>doubtful (\$23,980.00)</i> | Old Republic            | Foreclosed                    |
| 4  | 96-292-03M                   | <i>doubtful (\$6,830.86)</i>  | American Title          | Foreclosed                    |
| 5  | 96-332-03C                   | <i>doubtful (\$4,509.59)</i>  | American Title          | Foreclosed                    |
| 6  | 05-1018-10M                  | <i>doubtful (\$50,000.00)</i> | Chicago Title           | Foreclosed                    |
|  | <b>Doubtful MAP Total</b>    | <b>(\$147,553.34)</b>         |                         |                               |
| CONTINUED ON NEXT PAGE<br>(Appendix 2: HOMEBUYER LOANS REVIEWED)   |                              |                               |                         |                               |

<sup>8</sup> The six foreclosed loans represent the total population of City-funded MAP foreclosed loans. The six foreclosed loans were reviewed to ensure that they were accurately recorded in Oracle. In addition, supporting documentation was reviewed for two of the foreclosed MAP loans included in the judgmental sample.

## Appendix 2: HOMEBUYER LOANS REVIEWED

| Item No.  | Invoice Number                   | Loan Amount         | Title Company | Status of the Loan |
|---|----------------------------------|---------------------|---------------|--------------------|
| Public Safety Employees & Teachers Downpayment Assistance Program (PSE-DAP) |                                  |                     |               |                    |
| 1   | 2002-842-08D                     | \$ 4,967.87         | N/A           | Partially Paid     |
| 2   | 2003-892-10D                     | \$13,877.19         | N/A           | Partially Paid     |
| 3   | 2003-900-10D                     | \$13,877.45         | N/A           | Partially Paid     |
| 4   | 2003-903-03D                     | \$14,838.80         | N/A           | Partially Paid     |
| 5   | 2003-909-03D                     | \$20,000.00         | N/A           | Open               |
| 6   | 2004-918-10D                     | \$9,045.73          | N/A           | Partially Paid     |
| 7   | 2004-952-10D                     | \$17,775.50         | N/A           | Partially Paid     |
| 8   | 2004-956-10D                     | \$20,000.00         | N/A           | Open               |
| 9   | 2004-958-08D                     | \$20,000.00         | N/A           | Open               |
| 10  | 2004-967-10D                     | \$19,898.49         | N/A           | Partially Paid     |
| 11  | 2004-970-10D                     | \$18,733.21         | N/A           | Partially Paid     |
| 12  | 2004-986-08D                     | \$20,000.00         | N/A           | Open               |
| 13  | 2005-1024-06D                    | \$20,000.00         | N/A           | Open               |
| 14  | 2007-1136-01D                    | \$20,000.00         | N/A           | Open               |
| 15  | 2007-1156-01D                    | \$20,000.00         | N/A           | Open               |
| 16  | 2009-1283-15D                    | \$20,000.00         | N/A           | Open               |
| 17  | 2009-1317-10D                    | \$20,000.00         | N/A           | Open               |
| 18  | 2000-723-08D                     | \$0.00              | N/A           | Paid Off           |
| 19  | 2001-760-08D                     | \$0.00              | N/A           | Paid Off           |
| 20  | 2002-794-03D                     | \$0.00              | N/A           | Paid Off           |
| 21  | 2002-853-03D                     | \$0.00              | N/A           | Paid Off           |
| 22  | 2004-955-03D                     | \$0.00              | N/A           | Paid Off           |
| 23  | 2004-929-10D                     | \$0.00              | N/A           | Loan cancelled     |
|   | <b>Outstanding PSE-DAP Total</b> | <b>\$293,014.24</b> |               |                    |



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## RECOMMENDATIONS

### We recommend that the FMA and CEDA Management:

|                   |  |
|-------------------|--|
| Recommendation #1 | <p>Evaluate the design and operation of their internal controls over loan receivables including the establishment of policies and procedures to ensure:</p> <ol style="list-style-type: none"> <li>1. Accurate loan values, dates and payment terms are recorded</li> <li>2. Loan receivable aging analysis is prepared and reviewed monthly by management and for deferred loans a tracking system should be established.</li> <li>3. An allowance for doubtful accounts policy is established that includes preparing periodic estimates of uncollectible loan balances for review and authorization by management</li> <li>4. All loan write-offs, grant conversions or forgiveness of delinquent loans have a clear audit trail that documents the justification for writing off, forgiving or converting the loan including all authorizing signatures and City Council resolutions if applicable.</li> </ol> |
| Recommendation #2 | <p>Conduct an annual review of all loans to ensure that all loan receivable records in the sub-ledger and in Oracle are complete and accurate.</p>   |
| Recommendation #3 | <p>Find the supporting documentation for the remaining Development loans where the write off process has not yet been initiated and determine if the loans are still collectible, including interest revenue or if they should be written off.</p>   |

### We recommend that the City's external financial statement auditors:

|                   |  |
|-------------------|--|
| Recommendation #4 | <p>Increase their internal control testing of receivables during the next financial statement audit.</p> |
|-------------------|--|

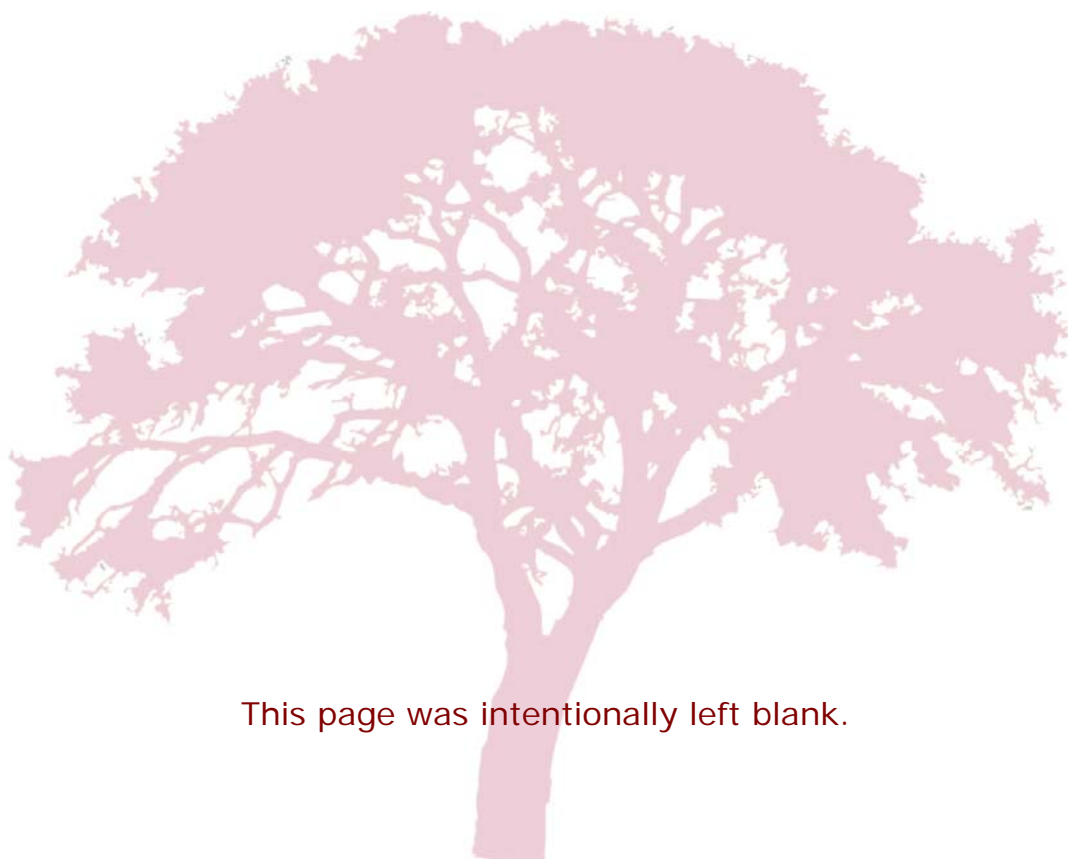
### We recommend that CEDA Management:

|                   |  |
|-------------------|--|
| Recommendation #5 | <p>Establish effective internal controls over loan conversions by developing appropriate procedures to record loans as grants and make the necessary updates to the loans which were approved to be converted to grants.</p>   |
| Recommendation #6 | <p>Perform an annual review of all loan receivables that would ensure that all loans that have been approved to be accounted for as grants by City Council Resolution are recorded accurately, and create a system of internal controls that tracks, links, and monitors loans to actions taken by City Council.</p> |

|   |  |
|---|--|
| Recommendation #7   | Accurately account for the OPEN and Pro Art loans as grants, and determine if the OCCUR loan is indeed a grant, and if so, accurately account for the conversion, including conducting the loan write off process.   |
| <b>We recommend that CEDA and FMA Management:</b>                         |  |
| Recommendation #8   | Establish a loan receivables policy and procedure for allowance for doubtful accounts, which should detail the criteria for when an account is doubtful and the specific process for accurately establishing an allowance for doubtful account.  |
| <b>We recommend that CEDA Management:</b>                                 |  |
| Recommendation #9   | Ensure that all loans that are tracked in the “allowance for doubtful accounts” have the appropriate approvals and supporting documentation stating why the loans may not be collectible.  |
| <b>We recommend that CEDA and FMA Management:</b>                         |  |
| Recommendation #10  | Update the “Reference” field for each of the remaining Development loans that are not being written off to reflect the accurate due date and payment term for the loan. In addition, as part of the annual review in recommendation # 2, review the loan due dates and payment terms to ensure accuracy of the recording of the loans.   |
| <b>We recommend that CEDA Management for the Homebuyer Loan Programs:</b> |  |
| Recommendation #11  | Update all homebuyer loan processing policies and procedures to ensure all key loan receivables processes are documented.  |
| Recommendation #12  | Ensure the revised homebuyer loan receivables policies and procedures are communicated to staff.   |
| Recommendation #13  | Include specific guidelines on how to prevent and detect fraud in homebuyer loan receivables process procedures.   |
| Recommendation #14  | Implement homebuyer loan program fraud training for staff.   |
| <b>We recommend that CEDA Management:</b>                                 |  |
| Recommendation #15  | Correct the inaccuracies to the MAP sub-ledger and Notes and Loans Receivables sub-ledger.   |
| Recommendation #16  | Improve internal controls over loan receivable subsidiary systems to ensure that there are controls in place that are designed to prevent and detect loan data inaccuracies including appropriate reconciliations. Specifically, ensure that all loans in CEDA's sub-ledgers are reviewed and reconciled to each loan in Oracle as part of the quarterly invoice adjustment process. |

**Recommendation #17**

Research and evaluate systems available that would allow for automatic system integration with Oracle.



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October 21, 2010

Ms. Courtney Ruby  
City Auditor  
City of Oakland, California  
Frank Ogawa Plaza, 4<sup>th</sup> Floor  
Oakland, California 94612

*RE: Response to Performance Audit of CEDA Loan Receivables*

Dear Auditor Ruby:

Attached please find the City's response to the CEDA Loan Receivables audit.

2

We welcome performance audits conducted in a fair and impartial manner. Generally Accepted Government Auditing Standards (GAGAS) section 7.58 states: "*The audit report should be fair and not misleading, and should place the audit results in perspective. This means presenting the audit results impartially and guarding against the tendency to exaggerate or overemphasize deficient performance...*"

We find the draft CEDA Loan Receivables audit report does not meet that standard: it is **misleading** and shows a **clear tendency to exaggerate**. Specifically:

3

- This audit found no substantial performance deficiencies and **absolutely no** cases of fraud, illegal acts or noncompliance issues.

1

- A majority of the findings and recommendations relate directly to a few loans that date back to the 1980's and early 1990's. Despite implications to the contrary, **these historic loans' financials are accurately accounted for** in the Oracle system.

**Note:** The reference numbers in the left margin correspond to the reference numbers in the next section of the audit report: City Auditor's Analysis and Summary of Actions Necessary to Close the Report.

1

7

- Whatever the practices of 25 or 30 years ago, there is **no correlation** between these historic loans and current loan program practices, policies, and performance. Unfortunately, this audit tries to make that illogical leap – which results in an audit that is misleading and inappropriate.

2

- According to GAGAS section 6.9, “auditors should obtain an understanding of the program to be audited to help assess, among other matters, the significance of possible audit objectives and the feasibility of achieving them.” **The Auditor’s report clearly shows a lack of understanding of the City’s financial system and the reporting of its assets.**

Attached to this cover letter is the City’s detailed response. The first section of the City’s response presents general concerns regarding the audit process and findings. This is followed by specific comments for each chapter and associated recommendations.

We sincerely hope that the City Auditor’s Office will correct the tone and specific conclusions of the above audit before it is issued. Staff are prepared to meet with your office once again to discuss major issues with the draft report.

Sincerely,



Dan Lindheim  
City Administrator

## Audit Response

8

This is a response to the City of Oakland CEDA loan receivables audit conducted by the City Auditor. **The City is not in agreement with many of the comments, assumptions, conclusions and recommendations** in the report. The audit found no substantial performance deficiencies and **absolutely no cases of fraud, illegal acts or noncompliance issues**. The following are general concerns regarding the audit process and findings:

1

- **Audit Scope and Planning:** According to generally accepted government auditing standards (GAGAS) 4.6.3, auditors should “communicate to the auditee the nature and extent of the planned testing and reporting in compliance with laws and regulations and internal control over financial reporting.” The original scope of the audit was stated to cover revenue collection in CEDA’s Housing and Community Development Division (HCD), with a particular focus on outstanding *housing* loans dating back to FY 2006-07. The initial audit meeting was only with housing staff and made no mention of non-residential lending activity.

The City Auditor expanded the scope to include commercial loans and loans to non-profits that date back to the 1980s and early 1990s without formally notifying any appropriate City staff. The additional scope reviewed loans that pre-date current departmental structures and staff. Therefore, **to characterize the status of these loans that date back to the 1980s and 1990s as failure of CEDA and FMA is misplaced and undeserved.**

2

- **Mortgage Assistance Program (MAP):** Auditors are required under GAGAS (7.43 and 7.44) to report noteworthy accomplishments. The audit mentions that the loans under the MAP were properly approved and recorded in Oracle and includes one sentence regarding the program’s successes in limiting the foreclosure rate. **These successes should be highlighted and commended** – not buried in the report or mentioned in passing. The current CEDA Housing loan programs should not be included in the same category as audit findings for loans that originated decades ago under completely different programs.

5

- **HCD Loan Programs:** **HCD recently received recognition for best practices** from HUD on its Affordable Housing Development (HOME Partnership) loan program, which recognized the completeness of files maintained for all the housing development projects and the monitoring of the programs. All of HCD’s loan programs employ the same policies and procedures for this nationally recognized program.

4

Findings related to the original scope of the audit (i.e. residential loans, including HCD’s Homebuyer program) are limited to less than one percent of the value of all outstanding loans totaling \$356 million, which is **below the quantitative and qualitative materiality thresholds of government accounting practices**. The findings included:

- 1) MAP sub-ledger inaccurately recorded a \$95,000 loan as cancelled, and another loan differed from Oracle by \$184. However, **Oracle – containing the City’s official fiscal records - was accurate in both cases.**

- 2) \$150,000 in doubtful loan receivables was recorded in the wrong fund. However, both funds are within the same fund group, which means year-end reporting would not be impacted.
- 3) A minor delay in the recording of a \$300,000 PSE-DAP loan in Oracle. However, it was accurately recorded prior to the commencement of this audit.

Oracle and the CEDA sub-ledger **have already been corrected** where necessary.

- 2 • 1980's and Early 1990's Notes & Loan Receivables: According to GAGAS section 6.9, "auditors should obtain an understanding of the program to be audited to help assess, among other matters, the significance of possible audit objectives and the feasibility of achieving them." **The Auditor's report clearly shows a lack of understanding of the City's financial system and the reporting of its assets.** This reflects poor field work standards for financial and performance audits, which is required for achieving proper audit objectives.

1 7 All the findings in Section One for the "Development Loans" address loans that date back to the 1980's and early 1990's and not to current loan programs. **This means that the audit's claim that the City (and particularly CEDA) lacks proper internal control over loan receivables is in error**, because it addresses loans from 20 and 30 years ago. The audit does not take into consideration **current** policies, procedures and practices.

1 The audit also fails to acknowledge the current existence of built-in internal controls in the City's financial system (Oracle). **The audit's claim that the "City's accounting system failed to properly reflect the City's current assets" is simply not true.** Each loan questioned in the audit was properly recorded in Oracle as a loan receivable (asset) and deferred revenue (liability), which has been confirmed by the City's outside financial auditors.

6 Additionally, **CEDA and FMA staff identified adequate documentation to address 98 percent of the development loan balances discussed in the Auditor's report.** The remaining loans that the audit says require clean-up or close-out documentation (approximately \$190,000) will be brought to Council for action before the end of the calendar year.

- Policies and Procedures: Policies and procedures for current HCD loan programs are regularly audited by HUD and the City's external financial auditors in the single audit. To review loans dating back to the 1980's and 1990's to measure the effectiveness of management of current loan programs, as this audit does, is unjustified.

8 General comments to each of the report's chapters, and detailed responses to each of the report's 17 recommendations follows.

Chapter I – FMA and CEDA Management cannot justify approximately \$14 million in loan receivables.

7

This audit finding is untrue. **All of these loans were recorded in Oracle accurately as a loan receivable (asset) and deferred revenue (liability), which nets to zero, and therefore had no bearing on the City's financial status or position.**

The City has documentation for \$13.8 million of the identified \$14 million in loan receivables. The bulk of the \$14 million in loan receivables relate to a \$12 million loan to the Oakland Hotel Association (OHA) and \$1.77 million loan to the Oakland Renaissance Association (ORA). The OHA loan was restructured in 1986 following the Hyatt bankruptcy, and should have been forgiven or subordinated to the new ORA loan at that time. The \$1.77 million in ORA receivables, which were from ballroom fees and ground lease rent, should have also been tied to the ORA loan in the 1997 restructuring. Both of these receivables should therefore have been written off with the 2007 ORA loan restructuring. CEDA staff was not aware of any monitoring that was required after the actions in 2007. A memo has been submitted to FMA including copies of applicable resolutions that provide the appropriate documentation to adjust the loan receivable and deferred revenue to eliminate the remaining ORA and OHA debt. **FMA has already taken this action.**

FMA will bring the remaining loans identified by the audit to Council for action before the end of the calendar year.

*Recommendation #1: Evaluate the design and operation of their internal controls over loan receivables including the establishment of policies and procedures to ensure:*

1. *Accurate loan values, dates and payment terms are recorded*
2. *Loan receivable aging analysis is prepared and reviewed monthly by management*
3. *An allowance for doubtful accounts policy is established that includes preparing periodic estimates of uncollectible loan balances for review and authorization by management*
4. *All loan write-offs, grant conversions or forgiveness of delinquent loans have a clear audit trail that documents the justification for writing off, forgiving or converting the loan including all authorizing signatures and City Council resolutions if applicable.*

**Response #1:** The recommendation is irrelevant. Except for monthly aging analysis meetings (#2), which are neither required or appropriate for these type of loans, policies and procedures are already in place that address each sub-point in recommendation #1. CEDA Housing loans are deferred loans due upon the earlier of: (a) sale or transfer of the Property; or (b) the end of the term of the loan and, therefore, are long-term and not current receivables. According to generally accepted accounting principles (GAAP) *"if assets are recognized in connection with a transaction before the earnings process is complete, those assets must be offset by a corresponding liability for deferred revenue (commonly referred to as unearned revenue in the private sector): As such, regular aging analysis is not a relevant exercise for deferred housing loans.*

In 2008, enhancements were implemented to reflect accurate loan values, dates and payment terms in the financial system. Loans made prior to this date were booked so that

pertinent information, such as payment terms, is included in the reference field. It should also be noted that the City has an allowance for doubtful accounts policy, which was established by FMA and adopted by CEDA. It is reviewed by the City's external financial auditors on an annual basis as they conduct the City financial audit.

***Recommendation #2:** Conduct an annual review of all loans to ensure that all loan receivable records in the sub-ledger and in Oracle are complete and accurate.*

**Response #2:** The recommendation is irrelevant. FMA **already reviews outstanding loans on a quarterly basis** to ensure that all loans in the subsidiary ledger (maintained by CEDA) are reconciled with the Oracle. In addition, the City's external financial auditors conduct on a test basis, evidence supporting the amounts and disclosures in the financial statements, and this includes a test of the loan receivables portfolio. The external auditors issued "unqualified" opinion or "clean" opinion on the City financial statements.

***Recommendation #3:** Find the supporting documentation for the remaining Development loans where the write off process has not yet been initiated and determine if the loans are still collectible, including interest revenue, or if they should be written off.*

**Response #3:** As previously stated, 98 percent of the loan receivables identified in Chapter I (for OHA and ORA) have been addressed and already adjusted in Oracle. When Oakland Renaissance Associates, Ltd. took over the Hyatt and converted it to a Marriott, the OHA loan totaling \$12 million was authorized to be restructured, and therefore should have been eliminated from the City's books, per Resolutions No. 63455 C.M.S. and No. 64122 C.M.S. The ORA loan, totaling \$1.77 million (included unpaid ground lease rent (\$0.3 million) and unpaid ball room fees (\$1.4 million)), should have been capitalized into the 1997 restructuring of the Marriott debt, and therefore eliminated following the 2007 sale of the Marriott (Resolution No. 80446 C.M.S.).

City staff continues to research files and archives for additional documentation on the six remaining historic loans identified by the audit. These six loans will be brought to Council for action before the end of the calendar year.

*We recommend that the City's external financial statement auditors:*

***Recommendation #4:** Increase their internal control testing of receivables during the next financial statement audit.*

**Response #4:** The City's external financial auditors, Macias, Gini & O'Connell, LLP, are independent auditors who follow the highest auditing standards and are qualified to conduct impartial audits of the City's financials and internal controls. While staff has shared the City Auditor's recommendation with this independent outside audit firm, we do not expect them to take direction from an elected official. Their direction comes from relevant auditing regulations, and no one – City staff or elected officials – are supposed to influence their work.

*Chapter II – FMA and CEDA Management did not accurately record approximately \$220,000 in loan receivables that had been converted to grants by City Council.*

This chapter cites problems with the status of loans in Oracle that date back to the 1980's. These loans pre-date current departmental structures and staff, and were transferred from an antiquated financial system to Oracle. The audit acknowledges that the City currently has internal controls in place, in which CEDA sends FMA quarterly loan invoice adjustment entries. **The City maintains that these existing controls are sufficient, and designed to capture loans authorized to become grants**

*Recommendation #5: Establish effective internal controls over loan conversions by developing appropriate procedures to record loans as grants and make the necessary updates to the three loans which were approved to be converted to grants.*

Response #5: This recommendation is not relevant. No problems were identified with recent activity in which loans were converted to grants. City management believes that appropriate procedures and sufficient internal controls are in place to convert current loans to grants in a timely manner upon approval by Council. The audit identifies two loans that date back to 1986 that were authorized to be converted to grants per Council resolution. These two (OPEN and Pro Arts) have been adjusted in Oracle. The third loan identified, to OCCUR dating back to 1988, will be forwarded to Council for action before the end of the calendar year.

*Recommendation #6: Perform an annual review of all loan receivables that would ensure that all loans that have been approved to be accounted for as grants by City Council Resolution are recorded accurately, and create a system of internal controls that tracks, links, and monitors loans to actions taken by City Council.*

Response #6: This recommendation is not relevant. As previously discussed, a quarterly review of loan receivables is already performed by City staff. In addition, the City's external financial auditors conduct an annual review of the loan receivables, which has consistently resulted in a clean opinion. The quarterly review by City staff includes the monitoring of loans and implementing the actions taken by City Council. CEDA subsidiary ledgers are reviewed and reconciled to each loan in the Oracle system by preparing adjusting entries to reconcile the loan receivables balances in Oracle to CEDA's subsidiary ledger.

*Recommendation #7: Accurately account for the OPEN and Pro Art loans as grants, and determine if the OCCUR loan is indeed a grant, and if so, accurately account for the conversion, including conducting the loan write off process.*

Response #7: This recommendation is not relevant. Please refer to response #5 above.

*Chapter III – CEDA Management did not maintain any documentation for deeming approximately \$100,000 in loan receivables as uncollectible.*

Again, this chapter is misleading and misplaced. **CEDA does have a system and documentation to account for doubtful accounts for its current loan programs.** This

chapter identifies three loans dating back to the 1980's that were deemed uncollectible, and claims CEDA does not have a policy to address the allowance of doubtful accounts. These three loans - as stated in the audit - were established before CEDA existed, and appear to be authorized by completely separate departments. CEDA does have a policy regarding allowance of doubtful accounts, as detailed in response #8.

***Recommendation #8:** Establish a loan receivables policy and procedure for allowance for doubtful accounts, which should detail the criteria for when an account is doubtful and the specific process for accurately establishing an allowance for doubtful account.*

**Response #8:** The recommendation is irrelevant. **CEDA's current loan program already has an established policy and procedure for the allowance of doubtful accounts.** Loans are deemed as non-performing when the property securing the loan is foreclosed by the senior lien holder and there is insufficient equity to pay the City loan. A listing of non-performing loans is provided by CEDA to FMA, which becomes the basis of the allowance for doubtful accounts that is booked by FMA at the end of the fiscal year. The City does comply with the GAAP requirement to value the receivables base on the net realizable value. The City's external financial auditors review and audit the allowance for double accounts for notes and loan receivables on an annual basis, and have not raised any concerns with the City's records or practices.

***Recommendation #9:** Ensure that all loans that are tracked in the "allowance for doubtful accounts" have the appropriate approvals and supporting documentation stating why the loans may not be collectible.*

**Response #9:** CEDA already maintains supporting documentation and analysis to determine if the loan is collectible. Loans are deemed non-performing when the property securing the loan is foreclosed by the senior lien holder and there is insufficient equity in the property to pay the City loan. Uncollectible loans are added to the list of non-performing loans and provided to FMA to book the allowance for doubtful accounts.

***Chapter IV – FMA Management inaccurately recorded all Development loans' due dates and loan payments terms in Oracle.***

This is an artifact of the conversion process from the previous financial system (FMS) to Oracle. In many cases, the records were transferred from the financial system that pre-dated FMS. Since 1994/1995 the City has used third-party software (Universal) for the servicing requirements of the loans. Separate subsidiary ledgers for development, rehabilitation and homeownership loans are maintained by CEDA Loan Servicing Units. The subsidiary system records all loan information including the terms and conditions. Changes in the loan balances are recorded in Universal, which is then used to update Oracle Receivables.

During the 1999 systems conversion, the Oracle loan services module was not robust enough to handle the variety of payment terms offered by the City's housing programs. The City, therefore, continued to use Universal for loan tracking. The Oracle Receivable module is not a loan services module; it was not set up to accommodate the wide variety of terms offered by various housing programs.

The City has subsequently expanded the Receivable Payment Terms to accommodate more of the standard loan terms. To fully implement the Oracle loan services module, the Information Technology Department estimates the cost of implementation to be up to \$450,000.

The City acknowledges these historic loans do not have accurate due date and payment term information due to this conversion process. It is not possible to delete these records and re-enter them (as the Auditor suggests). Furthermore, **payment terms and due dates have no financial impact on the loans**, because they are deferred for several years. However, it is important to note current loans are accurately recorded in Oracle with appropriate due dates and payment terms and the loans are booked properly as deferred revenue. This practice is consistent with GAAP.

*Recommendation #10: Update the "Reference" field for each of the remaining development loans that have not been written off to reflect the accurate due date and payment term for the loan. In addition, as part of the annual review in recommendation # 2, review the loan due dates and payment terms to ensure accuracy of the recording of the loans.*

*Response #10: All remaining development loans have been or will be eliminated from the financial system. The City includes due dates and payment terms for current loans.*

*Chapter V – CEDA Management does not have comprehensive and updated policies and procedures for the homebuyer loan receivables, nor do they have adequate and formalized fraud training.*

**This finding is exaggerated** – CEDA does have policies and procedures with regard to its homebuyer loan program. For this particular program, the only items noted by the audit as not being included in the policies and procedures relate to detecting and preventing fraud, and cancelled loans. Current policies and procedures will be reviewed to determine what, if anything, should be added to specifically address these two components. Additionally, the policies and procedures can be posted to the City's intranet for easy access by all Housing staff for training and reference purposes.

Improving policies and procedures is a repeated finding in all City Auditor reports. The City believes its policies and procedures are adequate, but also acknowledges there is always room for improvement, but this work must be balanced with other priorities and its return on investment (i.e. it is impossible to achieve 100 percent accuracy solely through policies and procedures).

*Recommendation # 11: Update all homebuyer loan processing policies and procedures to ensure all key loan receivable processes are documented.*

*Recommendation # 12: Ensure the revised homebuyer loan receivables policies and procedures are communicated to staff.*

Recommendation # 13: Include specific guidelines on how to prevent and detect fraud in homebuyer loan receivables process procedures.

Responses #11, 12 & 13: The homebuyer loan policies and procedures will be reviewed and updated as necessary. The policies and procedures will be posted to the City's intranet for easy access and training for all Housing staff.

Recommendation #14: Implement homebuyer loan program fraud training for staff.

Response #14: First and foremost, **no fraud was identified** by the City Auditor. The current program already involves requirements for 3<sup>rd</sup> party documentation of income and other controls to independently verify information:

1. Loan files are submitted by participating lenders. As an example for Bank of America, their fraud procedures are implemented at the processing level. Their verification includes employment, social security numbers, and verifying signatures. If they detect possible discrepancies, the file is sent to their Fraud Department for immediate investigation.
2. City staff reviews loan files and documents to determine program eligibility that include property, occupancy, household size and income. Additional documentation is requested from the buyer through the lender to address any questions that, among other items, include deposits and withdrawals from bank statements to verify sources of income and patterns and anything that raises suspicion.
3. Staff is investigating training programs that may be provided to staff that provide loans.

*Chapter VI – Subsidiary ledgers used to maintain loan information are inaccurate and the process is flawed.*

Housing is implementing a system called the Grants & Loans Information Management System, which will automate lending functions from loan origination to underwriting, loan closing and construction loan management and loan servicing for both single-family and multi-family housing projects. Other features include compliance monitoring and loan asset management. The system will also serve as the subsidiary accounting ledger to record detail on loan receivables (for housing related loans) that will then be posted in summary form to the City's Oracle financial accounting system. Implementation of the system will improve efficiency and accuracy of the loan data while enhancing the capability of staff to manage the loan portfolio.

Recommendation # 15: Correct the inaccuracies to the MAP sub-ledger and Notes and Loans Receivables sub-ledger.

Response #15: The sub-ledgers have been corrected.

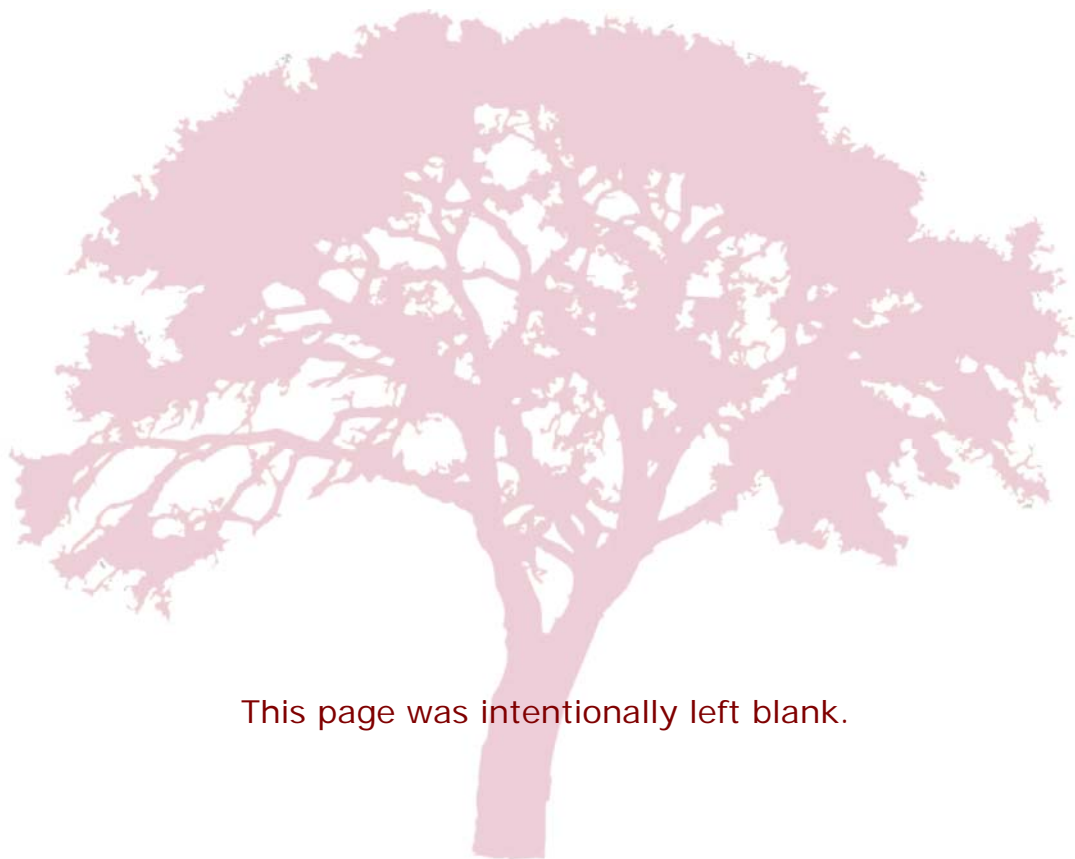
Recommendation # 16: Improve internal controls over loan receivable subsidiary systems to ensure that there are controls in place that are designed to prevent and detect loan data inaccuracies including appropriate reconciliations. Specifically, ensure that all

*loans in CEDA's sub-ledgers are reviewed and reconciled to each loan in Oracle as part of the quarterly invoice adjustment process.*

Response #16: Both CEDA and FMA staff will closely reconcile the sub-ledgers and Oracle on a quarterly basis to ensure both systems information matches.

Recommendation #17: *Research and evaluate systems available that would allow for automatic system integration with Oracle.*

Response #17: The City has entered into contract with Housing Development Software Inc., to purchase software, equipment, installation, customization and maintenance services for the implementation of the Grant and Loan Information Management System. Prior to approval of the contract, CEDA consulted with Information Technology staff regarding the ability to integrate automatically with Oracle and it was concluded that the City did not currently have the capability to facilitate this integration, and that doing so would cost up to \$450,000 in addition to the \$500,000 cost for the entire Grant and Loan Information Management System.



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## ANALYSIS & SUMMARY OF ACTIONS NECESSARY TO CLOSE THE REPORT

We provided a draft audit report to the City Administration (Administration) for review and comment in compliance with Generally Accepted Government Auditing Standards (GAGAS). The Administration's comments and details regarding the actions it has taken or plans to implement in response to the audit's recommendations have been included in the previous section of the report. Their comments comprise responses from the City Administrator's Office, CEDA Management, and FMA Management.

This section of the report provides clarification on the status of the report recommendations, including the follow-up actions needed to be completed to close the report. The reference numbers in the left margin below correspond directly to the reference numbers in the Administration's response.

Seven areas highlighted in the Administration's response require clarification. The areas needing further clarification are:

- |                            |                               |
|----------------------------|-------------------------------|
| (1) Audit Scope            | (5) HUD Recognition           |
| (2) References to GAGAS    | (6) Adequacy of Documentation |
| (3) References to Fraud    | (7) Responsibility for Loans  |
| (4) Homebuyer Loan Program |                               |

The remaining balance of the Office of the City Auditor's (Office) comments focuses on the disposition of each recommendation.

1

### Audit Scope

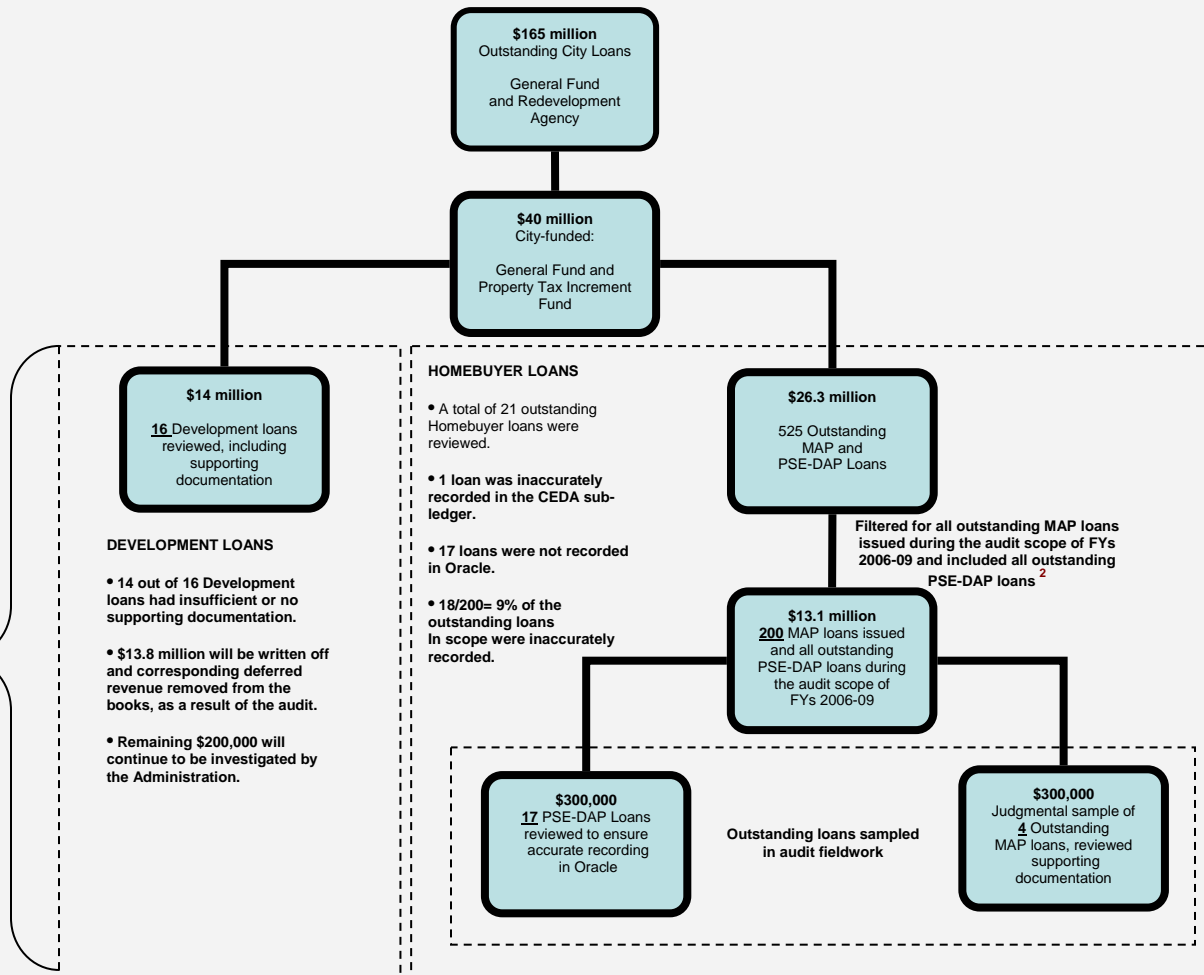
In its response, the Administration states that the Office changed the scope of the audit. This statement is inaccurate because during the entrance conference and preliminary meetings with CEDA Management and FMA Management in the audit's first few weeks, the Office clarified the scope to include any City funded loans, which were either funded through the City's General Fund or the Property Tax Increment Fund. The adjustment was in accordance with GAGAS 7.07, which states *"planning is a continuous process throughout the audit. Therefore, auditors may need to adjust the audit objectives, scope, and methodology as work is being completed."*

Furthermore, it is the City Auditor's charter mandated duties to review and appraise the soundness, adequacy and application of accounting, functional and operating controls, as well as the reliability and timeliness of accounting and other data generated within the organization.

The Administration states that the audit findings and recommendations relate to loans dating back to the 1980's and 1990's. his statement is misleading, as Exhibit 9 illustrates, the loan receivables for the General Fund and the Redevelopment Agency are clearly within the audit's scope and are reported in the City's financial statements for FY 2008-09. The audit found that the Administration was unaware of the status of these loans and still recorded them on the City's books all three years of the audit scope, from FY 2006-07 to FY 2008-09. In fact, these loans remained on the books at the conclusion of this audit in September 2010.

## EXHIBIT 9: GENERAL FUND & REDEVELOPMENT AGENCY LOAN RECEIVABLES INCLUDED IN THE CITY'S FY 2008-09 FINANCIAL STATEMENTS

**AUDIT SCOPE<sup>1</sup>**



<sup>1</sup> The scope of the audit focused on loans funded through the City's General Fund (Fund 1010) and CEDA Property Tax Increment Fund (Fund 2185) with outstanding receivable balances during FYs 2006-2009.

<sup>2</sup> Audit testing also included the judgmental sample of three paid, two foreclosed, and one cancelled MAP loans that was reviewed to identify areas of potential internal control weakness. In addition, one cancelled and five paid PSE-DAP loans were reviewed to ensure that the loan amounts were accurately recorded in Oracle. In all, audit fieldwork sampled 37 Homebuyer loans, 31 of which were inaccurately recorded either in the sub-ledger or in Oracle.

1

## Audit Scope (continued)

The Administration claims the loans were accurately accounted for, yet it could not answer whether the loans had been repaid, should have been repaid, or should have been written off. Only as a result of the audit did the Administration become aware of the loans' existence on the books and begin to track down supporting documentation to determine whether or not the loans were accurately recorded on the books. To determine the status of the loans, the Administration needed to bring back a retired employee to conduct the research. Ultimately, the audit found that these loans are not collectible, and that the deferred revenue will never be realized, but the City continued to record them on its books. While the Administration highlights a current quarterly review of loans process, the existence of these loans on the books and the overstatement of deferred revenue went unnoticed for years. Write off of assets should be made when Management becomes aware:

- Assets are legally without merit
- Assets cannot be substantiated by evidence
- Debtor cannot be located
- It is impossible to collect any substantial amount
- Statutory requirement exist to terminate asset recovery

Unfortunately, as the audit illustrates, the Administration was unclear who had oversight responsibility over the loans. Therefore, they were left on the books for years without anyone determining if the financial information was accurate or reliable.

2

## References to Generally Accepted Government Auditing Standard

In its response, the Administration made several references to Generally Accepted Government Auditing Standard (GAGAS) in an effort to imply that the audit was not performed in accordance to GAGAS. This implication is erroneous because this audit, as are all of the Performance Audits that are issued by the Office of the City Auditor, are performed in accordance to GAGAS. The following clarifies the GAGAS standards cited throughout the Administration's response.

- GAGAS 7.58 "the audit report should be fair and not misleading, and should place the audit results in perspective. This means presenting the audit results impartially and guarding against the tendency to exaggerate or overemphasize deficient performance."

The audit report is a fair representation of the Administration's failure to monitor and write-off loans in the amount of \$14 million. The Administration's lack of sufficient internal controls and documentation for over 35 percent of CEDA's loan portfolio presented a significant deficiency. According to GAGAS 7.21, in performance audits, a deficiency in internal controls exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, detect, or correct misstatement in financial or performance information.

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|                     | <ul style="list-style-type: none"> <li>• GAGAS 6.9 “auditors should obtain an understanding of the program to be audited to help assess, among other matters, the significance of possible audit objectives and the feasibility of achieving them.<br/><br/>The audit team fully obtained an understanding of the CEDA loan program as it relates to the audit objectives which were: 1) to analyze and evaluate loan policies and procedures related to loan receivables, and 2) to determine if there are adequate internal controls in place to accurately account for outstanding loans, defaulted loans and loan payments. In fact, it was the audit team that discovered the loans in the amount of \$14 million that were still on the books and should have been written off years ago. Neither CEDA Management nor the City Administrator’s Office was aware that these loans remained on the books until the audit. To further illustrate the Administration’s lack of understanding its own loan program, during the end of audit fieldwork the Administration enlisted a retired employee to research the status and find supporting documentation for the \$14 million in loans that were sampled as part of the audit.</li> <li>• GAGAS 4.6.3 which relates to communicating to the auditee the nature of the planned testing and reporting in compliance with laws and regulations and internal control over financial reporting.<br/><br/>As previously stated, the Office clarified the scope of the audit during the entrance conference and during several preliminary meetings with CEDA Management and FMA Management. The clarification stemmed from the objective to focus only on City-funded loans as was discussed at great length with the auditee. The adjustment to the scope was in accordance with GAGAS 7.07 which states “planning is a continuous process throughout the audit. Therefore, auditors may need to adjust the audit objectives, scope, and methodology as work is being completed.”</li> <li>• GAGAS 7.43 auditors are required to report noteworthy accomplishments.<br/><br/>The audit report clearly states, on page 35, that loan repayments under the MAP program were properly approved and recorded in Oracle, as the Administration acknowledges in its response. However, the audit found FMA inaccurately recorded other loan data in the subsidiary ledgers and Oracle.</li> </ul> |
| References to Fraud | <p>In its response, the Administration stated “this audit found no substantial performance deficiencies and absolutely no cases of fraud, illegal acts or noncompliance issues”. This statement is misleading. The audit found significant performance deficiencies including a) the failure to write off \$14 million in loans that have erroneously remained on the City’s books for years without notice of CEDA Management or FMA Management b) inaccurate recording of approximately \$220,000 in loan receivables that had been converted</p>  |

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|                        | <p>to grants over ten years ago, c) subsidiary ledgers used to maintain homebuyer loan information and Oracle were inaccurate by approximately \$450,000, and d) the lack of appropriate internal controls resulted in insufficient financial oversight of CEDA's loan portfolio. The audit report does not indicate any fraud related findings. However, GAGAS standard 7.30 requires that audit planning include an assessment of fraud within the context of the audit objectives. While the audit found no fraud or illegal acts, there are potential risks involved because of the flaws in the internal control systems. Therefore, there is a recommendation that CEDA Management include fraud awareness procedures in its policies and procedures, for which CEDA has agreed to implement.</p>   |
| Homebuyer Loan Program | <p>In its response, the Administration stated that the findings related to the Homebuyer Program <i>"are limited to less than one percent of the value of all outstanding loans totaling \$356 million, which is below the quantitative and qualitative materiality threshold of government accounting practices."</i></p> <p>This statement is misleading because \$356 million reflects all outstanding loans, including federal and state loans. As shown in Exhibit 9 in this response, the City's FY 2008-09 financial statements report \$165 million in outstanding Notes and Loans Receivables for City-funded loans (General Fund and Oakland Redevelopment Agency). The audit scope covered \$40 million in City-funded loans, of which \$14 million was in Development loans and \$26 million was in Homebuyer loans. Approximately 2% of the \$26 million dollar amount in loans was reviewed and 11% of the number of loans paid or issued during FYs 2006-09 were reviewed.</p> <p>The concept of quantitative and qualitative materiality applies to financial audits. A financial statement audit opines that the financial statements present fairly, in all material respects, the respective financial position of the City. The materiality concept used within financial auditing relates to the importance and or significance of an amount, transaction, or discrepancy.</p> <p>However, <b>the objectives of performance audit are very different</b> than the objectives of a financial statement audit. A performance audit scrutinizes City operations to determine whether management systems are reliable, assets are properly safeguarded; the City is in compliance with laws and regulations, and whether programs are being run efficiently and effectively while accomplishing their goals and objectives. Therefore, it is inappropriate for the Administration to apply the concept of materiality to performance audits conducted by the Office, which has the mandated responsibilities of reviewing and appraising the soundness, adequacy and application of accounting, functional and operating controls, as well as the reliability and timeliness of accounting and other data generated within the organization.</p> |

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HUD Recognition

In its response the Administration stated that CEDA had received recognition for best practices from HUD on its Affordable Housing Development loan program. While we commend CEDA for its recognition, the program for which it received recognition is not within the scope of this audit.

6

Adequacy of Documentation

In its response the Administration claimed that CEDA and FMA staff identified adequate documentation to address 98 percent of the development loan balances discussed in the Auditor's report. This statement is misleading. FMA provided background documentation about the loans.

**However, there were no promissory notes, documentation about payments made, or up to date accounting records that provided information about the current status of the loans.**

7

Management Responsibility for the Loans

Exhibit 9 reflects the loan receivables for the General Fund and the Redevelopment Agency reported in the City's financial statements for FY 2008-09. The audit reviewed the loans reported during this period and found that the Administration was unaware of the status of these loans and still recorded them on the City's books all three years of the audit scope, from FY 2006-07 to FY 2008-09.

In its response, the Administration claimed that it was unfair that the current Administration is held responsible for loans that were improperly managed in the 1980's and 1990's. However, the City Administrator's Office is fully aware of its responsibility for the loans. In fact, Administration Management acknowledged during the exit conference for this audit, current balances in the City's books are the responsibility of today's Administration. Accordingly, the Administration is responsible for deficiencies in the financial system that resulted in loans not being monitored and carried on the City's books for years. As stated in the report, the Administration is responsible for maintaining a sound framework of internal controls that affords a reasonable basis to assert that the City's financial information may be relied upon. As stated in Government Auditing Standards, internal controls must be designed to allow management or employees, in the normal course of performing their assigned functions, to prevent, detect, or correct misstatements in financial or performance information.

The lack of knowledge surrounding which department is responsible for the loans is indicative of a larger problem, which includes the lack of coordination and collaboration across City departments. Had appropriate internal controls been in place, CEDA Management should have identified \$14 million in loans that were on the books and insufficiently supported. Instead, these loans have erroneously remained on the City's books for years without notice of CEDA Management or FMA Management. The lack of appropriate internal controls for either department creates an environment that does not result in sufficient financial oversight of CEDA's loan portfolio and the corresponding deferred revenue.

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|            | <p>The Office agrees with the Administration when it states that the loan receivables combined with the deferred revenue recorded in Oracle had a net neutral effect on the City's financial status or position. However, at the time of the audit neither FMA Management nor CEDA Management could provide supporting documentation that clearly accounted for the \$14 million in loan receivables. The Administration could not readily determine whether or not the repayment of loans should occur, already occurred, or should have been written off. At the very end of the audit, only after it was determined that there was insufficient supporting documentation for the \$14 million in loan receivables did CEDA Management produce a memo dated September 30, 2010, to FMA Management stating that approximately \$14 million in loan receivables related to the sale of the Marriott should have been written off and requested that it proceed with the write-off process.</p> <p>The significance of this deficiency is that the City's books include deferred income that will never be realized. Unrealized deferred revenue impacts the City's ability to properly plan for the future. As this audit reveals, the City did not track \$14 million in loans, and as a result was unaware of the status of \$14 million in anticipated revenues. Analysis of the City's expected revenues plays a critical part in determining the City's financial position going forward. Given the current state of the City's finances – the write off of \$14 million dollars in expected revenues is unfortunate and significant, and had appropriate oversight been in place could have identified much sooner.</p> |
| Conclusion | <p>The Office would have hoped that the Administration would assess the results of the audit and recommendations as an opportunity to strengthen its internal control weaknesses regarding its loan receivables. However, it is evident from the response that the opportunity for improvement is overshadowed by a need to downplay the significance of the findings on the logic that these findings, which identify unreliable and inaccurate financial data for millions of dollars are exaggerated. Unfortunately, this kind of response to an audit emphasizes the Administration's position of defending errors and inaccuracies versus assuring the public that the underlying system failures will be fixed.</p>   |

## SUMMARY OF ACTIONS NECESSARY TO CLOSE THE REPORT

The "Analysis and Summary of Actions Necessary to Close the Report" provides our analysis of both the City Administrator's Office and CEDA Management's comments and proposed actions required to close the report. The status of each of the 17 recommendations at the time of publication for this report is unresolved, partially resolved, resolved or closed. The Administration disagrees with the audit report findings but has agreed to implement approximately 65% of the recommendations that were provided in the report.

### Recommendation #1

**Unresolved** – CEDA Management disagrees with this recommendation and stated it is irrelevant. However, these recommendations are based on best practices from the Office of the State Controller of Illinois and are recommended for the loan receivables process. If these policies and procedures were already in place, the Administration should have detected these outstanding loans that have been on the books for over 10 years and not monitored by any specific division within CEDA.

**To close this recommendation, CEDA Management should evaluate the design and operation of their internal controls over loan receivables including the establishment of policies and procedures to ensure:**

1. Accurate loan values, dates and payment terms are recorded.
2. Loan receivable aging analysis is prepared and reviewed monthly by management and for deferred loans a tracking system should be established.
3. An allowance for doubtful accounts policy is established that includes preparing periodic estimates of uncollectible loan balances for review and authorization by management
4. All loan write-offs, grant conversions or forgiveness of delinquent loans have a clear audit trail that documents the justification for writing off, forgiving or converting the loan including all authorizing signatures and City Council resolutions if applicable.

**CEDA Management should provide loan receivables policies and procedures with the attributes listed above to the Office of the City Auditor by January 31, 2011.**

**Unresolved** status indicates no agreement on the recommendation or the proposed corrective action. Implementation of proposed corrective action is directed in the City Auditor's Analysis and Summary of Actions Necessary to Close the Report.

**Partially Resolved** status indicates partial agreement on the recommendation or the proposed corrective action. Implementation of the proposed corrective action is clarified in the Analysis and Summary of Actions Necessary to Close the Report.

**Resolved** status indicates agreement on the recommendation and the proposed corrective action. Implementation of the proposed corrective action forthcoming from the auditee.

**Closed** status indicates the agreed upon corrective action is complete and the impact of the action will be reviewed during future audit recommendation follow-up.

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| Recommendation #2 | <p><b>Unresolved</b> – CEDA Management disagrees with this recommendation and states it is irrelevant. At the time of the audit, neither FMA Management nor CEDA Management had sufficient supporting documentation for the \$14 million in loan receivables. An annual review of all the loans would include a detailed review of all the supporting loan files to ensure supporting documentation is available. Based on the supporting documentation, CEDA Management should be able to determine if the sub-ledger and Oracle are accurate.</p> <p><b>To close this recommendation CEDA Management should provide documentation showing an annual review of supporting documentation for all loans. CEDA Management should also provide policies and procedures that document this annual review process. CEDA Management should provide this information to the Office of the City Auditor by January 31, 2011.</b></p> |
| Recommendation #3 | <p><b>Resolved</b> – The Administration agrees with the finding and has already begun the process to write off the approximately \$14 million in loans related to the sale of the Marriott Hotel as a result of the audit. Management continues to research and identify documentation for the remaining loans and plans to bring them to the City Council for appropriate action.</p> <p><b>To close this recommendation CEDA Management should provide documentation to show that the appropriate loans have been written off and that the loans that are not written off are accurately recorded in Oracle by providing supporting documentation. CEDA Management should provide this information to the Office of the City Auditor by January 31, 2011.</b></p>  |
| Recommendation #4 | <p><b>Closed</b> – FMA Management has shared the recommendation with the external auditors.</p> <p><b>No further action is necessary.</b></p>  |
| Recommendation #5 | <p><b>Unresolved</b> – CEDA Management states that the City maintains that there are sufficient controls currently in place to identify loans authorized to become grants. However, the audit concluded that since the audit found two loans authorized to be converted to grants that the CEDA Management did not properly account for, internal controls can be improved. Furthermore, CEDA Management acknowledges it still needs to bring one loan before City Council for appropriate action.</p> <p><b>To close this recommendation, CEDA Management should provide a copy of loan conversion policies and procedures to the Office of the City Auditor by January 31, 2011.</b></p>   |

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| Recommendation #6 | <p><b>Unresolved</b> – CEDA Management disagrees with this recommendation. CEDA Management stated that during the quarterly review all loans are reviewed and linked to actions taken by City Council. If this was the case, staff should have determined years ago that the two loans were authorized to be converted to grants and started the procedure to convert the loans as necessary. The audit found that the quarterly review focuses only on invoice adjustments from the sub-ledgers to the general ledger.</p> <p><b>To close this recommendation CEDA Management and FMA Management should provide a policy and procedure which documents the annual review of all the loans including the process that tracks, links and monitors loans to actions taken by City Council. CEDA Management should provide this information to the Office of the City Auditor by January 31, 2011.</b></p> |
| Recommendation #7 | <p><b>Partially Resolved</b> – CEDA Management disagrees with this recommendation, however it states that the OCCUR loan will be forwarded to City Council for action before the end of the year. CEDA Management also should initiate the process to accurately reflect the ProArts and OPEN loans as grants, including the write-off process for the loans.</p> <p><b>To close this recommendation, CEDA Management should provide documentation to show that the OCCUR loan was brought to the City Council for action. CEDA Management should also provide documentation to show that the ProArt and OPEN loans are accurately reflected in Oracle as grants. CEDA Management should provide this information to the Office of the City Auditor by January 31, 2011.</b></p>  |
| Recommendation #8 | <p><b>Unresolved</b> – The Administration claims that CEDA Management already has an established policy and procedure for the allowance of doubtful accounts. However, the doubtful allowance policy and procedure provided by FMA was only for short term accounts receivables, not loan receivables. Additionally, the loan receivables procedure provided by the Housing and Community Development Division did not clearly document the doubtful allowance procedure. If these policies and procedures are already in place, CEDA Management should provide the documentation.</p> <p><b>To close this recommendation CEDA Management should provide a documented doubtful allowance policy and procedure for loan receivables to the Office of the City Auditor by January 31, 2011.</b></p>   |

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| Recommendation #9  | <p><b>Unresolved</b> – CEDA Management claims that they already maintain supporting documentation for all loans in the “allowance for doubtful accounts.” However, when the Auditor’s Office asked for the documentation for the three short term loans identified during the audit, CEDA Management was not able to provide any supporting documentation that describes why these loans were considered doubtful.</p> <p><b>To close this recommendation CEDA Management should provide supporting documentation that the loans have been appropriately written off to the Office of the City Auditor by January 31, 2011.</b></p> |
| Recommendation #10 | <p><b>Resolved</b> – CEDA Management has stated that the all remaining Development loans have been or will be eliminated from the financial system. The Auditor’s Office should be provided documentation to show that has actually occurred.</p> <p><b>To close this recommendation CEDA Management should provide documentation to show that all the remaining Development loans have been written off, to the Office of the City Auditor by January 31, 2011.</b></p>  |
| Recommendation #11 | <p><b>Resolved</b> – CEDA Management agrees with this recommendation. CEDA Management stated that the homebuyer loan processing policies and procedures will be reviewed and updated as necessary. The policies and procedures will also be posted on the City’s Intranet for easy access and training for all Housing staff.</p> <p><b>To close the recommendation CEDA Management should provide updated copies of the homebuyer loan processing policies and procedures to the Office of the City Auditor by January 31, 2011.</b></p>   |
| Recommendation #12 | <p><b>Resolved</b> – CEDA Management agrees with this recommendation and stated that the policies and procedures will also be posted on the City’s Intranet for easy access and training for all Housing staff.</p> <p><b>To close the recommendation, CEDA Management should provide a print out of the policies and procedures available on the City’s Intranet to the Office of the City Auditor by January 31, 2011.</b></p>  |
| Recommendation #13 | <p><b>Resolved</b> – CEDA Management agrees with this recommendation and stated that the homebuyer policies and procedures will be updated as necessary to include fraud awareness procedures.</p> <p><b>To close the recommendation, CEDA Management should provide updated copies of the homebuyer policies and procedures that include fraud awareness procedures to the Office of the City Auditor by January 31, 2011.</b></p>   |

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| Recommendation #14 | <p><b>Resolved</b> – CEDA Management agrees with this recommendation. Although it already believes that there are good controls in place to detect fraud, CEDA Management stated it will investigate training programs for staff.</p> <p><b>To close the recommendation CEDA Management should provide documentation to show that fraud awareness training has occurred to the Office of the City Auditor by June 30, 2011.</b></p>  |
| Recommendation #15 | <p><b>Resolved</b> – CEDA Management agrees with this recommendation and stated that the sub-ledgers have already been corrected.</p> <p><b>To close this recommendation CEDA Management should provide a copy of the corrected sub-ledgers to the Office of the City Auditor by January 31, 2011.</b></p>   |
| Recommendation #16 | <p><b>Resolved</b> – CEDA Management agrees with this recommendation and stated that both CEDA Management and FMA Management will closely monitor and reconcile the sub-ledgers in Oracle on a quarterly basis to ensure both systems information matches. CEDA Management should review the quarterly adjustment process to ensure that it is operating effectively.</p> <p><b>To close this recommendation, CEDA Management should provide an example of the next quarterly invoice adjustment reconciliation to the Office of the City Auditor by January 31, 2011.</b></p> <p><b>CEDA Management should also document any changes made to the quarterly adjustment reconciliation process in the loan receivables policies and procedures. CEDA Management should provide the revised loan receivable policies and procedures to the Office of the City Auditor by January 31, 2011.</b></p> |
| Recommendation #17 | <p><b>Resolved</b> – CEDA Management agrees with this recommendation and already has begun the process of researching the possibility of automatic system integration with Oracle.</p> <p><b>To close this recommendation, CEDA Management should provide documentation showing the research conducted to evaluate automatic system integration with Oracle to the Office of the City Auditor by June 30, 2011.</b></p>  |