



Mayor Jim Newberry

LEXINGTON-FAYETTE URBAN COUNTY GOVERNMENT
Division of Internal Audit

INTERNAL AUDIT REVIEW

DATE: May 31, 2007

TO: Jim Newberry, Mayor

CC: Charlie Boland, Chief Administrative Officer
Kimra Cole, Commissioner of General Services
William Carman, Deputy Director of Parks & Recreation
Evelyn Bologna, Parks & Recreation Superintendent
Urban County Council Members
Internal Audit Board Members

FROM: Bruce Sahli, Director of Internal Audit

RE: Extended School Program Collections and Disbursements Review

Background

On January 18, 2005 the Division of Internal Audit issued an audit report on the Extended School Program (ESP) Collections & Disbursement Controls. The report contained several significant findings related to the collection and depositing of funds and the disbursement of those funds. This review was conducted to evaluate controls put in place by management to address those specific findings from the January 18, 2005 report as summarized below:

- ESP Accounting System was inaccurate and underutilized
- Written procedures needed to be established
- Collection, recording, and depositing duties were not sufficiently segregated
- Late deposits were noted
- Significant unresolved variances were noted in the reported collection activity
- ESP collections were used to make various purchases
- Inappropriate expense allocations were noted
- Questionable bad debt write-offs were noted
- Account activity was not properly monitored

H O R S E C A P I T A L O F T H E W O R L D

200 East Main Street

Lexington, KY 40507

(859)258-3286

www.lfucg.com

- Customer account activity was not being updated in the accounting records
- There were significant past due inactive accounts
- Weekly deposit ledgers were not consistently provided to management for review
- Unsecured collections were held for an extended time at the school locations
- Voucher activity was not consistently supported
- Controls for approval of LFUCG Scholarships needed enhancement
- Child Care Council payments were not reconciled to billing detail

Scope and Objectives

We reviewed ESP Program collection and disbursement procedures and tested a sample of collection and disbursement transactions to determine that effective collection and disbursement controls were in place as indicated by management. Depending on the implementation dates of corrective actions taken by the Division of Parks and Recreation, our test samples included transactions within the period FY 2006 and FY 2007 through February, 2007.

Statement of Auditing Standards

We conducted our review in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the review to afford a reasonable basis for our judgments and conclusions regarding the organization, program, activity, or function under review. A review also includes limited assessments of applicable internal controls and compliance with requirements of laws and regulations when necessary to satisfy the review objectives. We believe that our review provides a reasonable basis for our conclusions.

Scope Limitations

Accounts Receivables Testing & Review

We were unable to test the accuracy of the Accounts Receivable balances for the ESP customer accounts, to review the appropriateness of Bad Debt Write-offs, to review for significant past due accounts, or to review for significant account variances. Beginning in July 2006, ESP management ceased the use of the ProCare System which had previously been used to manage the ESP accounts and adopted a program called Rectrac as part of a Parks & Recreation Division wide conversion to a newer software system. After a few months of use, it was determined by ESP management that Rectrac did not provide the financial reporting capabilities necessary to properly manage the ESP Program and that it was necessary to convert back to the ProCare System. In order to transfer back, ESP management deemed it necessary to zero out existing account balances or close accounts in order to have reliable data in the ProCare System. As a result, we were unable to confirm the accuracy or reasonableness of FY 2007 ESP customer account balances or activity.

Deposit Activity Testing & Review

We attempted to trace a random sample of FY 2007 ESP deposits through the ESP accounting system to the related STARS General Ledger and related bank statements without success. The transfer of accounts from Rectrac back to ProCare as described above resulted in an inability to effectively trace FY 2007 deposit activity. It was therefore necessary to limit our deposit review to FY 2006 activity, resulting in a more dated review of deposit activity than that preferred by the Division of Internal Audit.

Results of Review

In our opinion, sufficient controls were not in place to provide reasonable assurance that funds collected were being accurately reported and deposited on a timely basis, and that expenditures were being accurately recorded and approved. This opinion is based to a significant extent on the scope limitations listed above. Opportunities to enhance controls are included in the Summary of Findings.

SUMMARY OF FINDINGS

ESP Account Reports Not Available to Management

Due to the changing of ESP Program software from ProCare to Rectrac then back to ProCare, ESP management was only receiving manually produced deposit ledgers from the ESP school sites. ESP management was not receiving any reports from the ProCare system as of the completion of field work as the system conversion had only been in place for about two months and the Administrative Specialist had not yet finished updating the ProCare system with any outstanding balances. System generated reports of account activity are an important tool in the management of an accounts receivable program such as ESP. It is recommended every effort be made to complete the ProCare update process and to begin utilizing the various management reports contained therein.

Division of Parks & Recreation Management Response: As the return to the ProCare Software is completed, the controls and reports that were originally in place to track and effectively balance revenue numbers shall be put back into place. Outstanding balance reports shall be distributed starting with the summer of 2007. Aging reports shall be created for past due accounts and the necessary actions will be taken including late payment assessments and collections with assistance from the Law Department.

Late Deposit Activity

Due to the scope limitation previously noted, we could not test deposit activity for FY 2007. In order to obtain some indication whether deposits were being made in a timely manner, we examined 136 randomly selected ESP deposits made during FY 2006. We noted that 10 deposits (7.4%) were made six or more business days after collection at the school site, while 33 deposits (24.3%) were made five or more business days after collection at the school site, including 16 deposits for \$1,000 or more. Assuming the deposits were held for two days at the school site as allowed by Parks & Recreation

policy (i.e. Monday collections would typically be delivered to Dunbar on Wednesday), this indicates these deposits were made at least three or four days after receipt at Dunbar.

ESP deposit procedures currently state that ESP funds collected at the school sites must be turned in to ESP management at the Dunbar Center twice per week for processing and deposit. Under this current policy, it is reasonable to expect that as many as four and possibly five business days may expire from the time funds are collected, processed, and deposited at the bank. It is recommended that Parks & Recreation management consider amending their ESP deposit procedures to require that collections exceeding a certain amount (e.g., \$750 or \$1,000) be delivered to ESP management at the Dunbar Center on the same or next day in order to deposit the funds in a more timely manner and reduce the risk associated with the security of ESP funds.

Division of Parks & Recreation Management Response: Policy has been amended to ensure that deposits are made on Tuesdays by all sites as Mondays are the largest collection day on site. Deposits will still be required twice a week with a mandatory deposit made on Tuesdays. Deposits are made to revenue at least 3 times weekly from the Dunbar Center and this procedure shall continue. Several options have been researched to help streamline the process including an automated check scanner that will deposit the funds electronically after scanning the checks at the Dunbar Center thereby negating the need to deposit checks to Revenue.

Expenditures Charged to the Wrong Site

We randomly selected 31 ESP expenditures and examined them for proper site and account coding, noting four instances where charges were either charged to the wrong site or the expenditures were not properly allocated among the benefited sites. A list of the misallocations noted during our review has been provided to management. It is recommended all ESP expenditures be applied against the appropriate site location on a consistent basis to ensure the cost of operations at those sites is accurately reflected in the financial records. This will ensure that management has the most accurate financial information available to evaluate the cost effectiveness of the ESP Program at the various program sites.

Division of Parks & Recreation Management Response: ESP Management has made every effort to apply expenditures to the sites that benefited most from the purchase. There are several expenses that must be distributed as mentioned in the previous audit. Transportation costs have been moved to the administration account to allow for the fact that busses may not serve just one site (as mentioned on the invoice), but rather make pick ups from several different sites in the course of a day.

Training costs are another difficult area as a staff may work at one site during the school year, but at another site on full days and yet another site in the summer. Training funds have been moved into the administrative budget as well as insurance and cell phone appropriations.

With proper administration of the funds transferred, remaining costs will be allocated to the proper site according to ESP policy. Every effort will be made to track these expenditures in house to determine if the correct charge outs are occurring.

Controls for Approval of LFUCG Scholarships Need Enhanced

Certain participants in the ESP Program can qualify for a weekly rate discount from the LFUCG, referred to as the Scholarship Program. Eligibility is based upon total family income, and an application process is used to determine eligibility. Applicants must submit a signed application, provide a 1040 tax form as proof of income, and meet income eligibility guidelines. Scholarships are awarded to eligible applicants on a first come, first serve basis, and there are a limited number of Scholarships available at each school.

We examined 61 Scholarship applications and supporting documentation provided to us by ESP management. We noted the approval of 54 scholarships, of which 42 (77.8%) did not indicate approval by the ESP Manager or his designee (it is understood that these 42 recipients were qualified to receive the scholarship). We also noted eight instances (14.8%) where the amount of the scholarship was incorrectly entered into ProCare, and five instances (9.3%) where eligibility information was not verified before rewarding the scholarship.

It is recommended that senior ESP management sign off on the application to denote their approval and acknowledgment of the award. Care should be exercised to correctly enter scholarship data into the ProCare accounts, and the requirement that eligibility be confirmed before scholarships are awarded should be consistently adhered to.

Division of Parks & Recreation Management Response: As a result of the previous audit, control of the scholarship approval process was shifted to the District Directors to administer the scholarship applications within their respective districts. This shift explains the lack of approval by the ESP Manager. It may be necessary to review the policies of approval with these designees as we move forward. A formal review shall take place at the ESP staff meeting scheduled for June.

The ProCare system does not allow for rate fluctuation within the Scholarship fee codes. Once a student is identified as a scholarship recipient, there are only two rates that can be applied; Full Time and Part time. There may be some confusion here with other discounted rates available to the families. As a licensed program, ESP accepts all forms of assistance including CCAP funds (State Assistance), Foster Care Reimbursement, Employer Funded Assistance, and several other individualized plans of childcare reimbursement and assistance. For this reason, there are an infinite number of rates that can be charged within the ProCare system to accommodate individualized plans that set the family's co-pay amount based on what the family can afford. There are, however, only two rates associated with the Parks and Recreation funded scholarship program. A detailed review of the ProCare procedures associated with scholarships will be included in the review planned for the June ESP staff meeting.

Collections Taken Home

ESP procedures require site collections be taken to the Dunbar Center for processing and subsequent deposit twice per week. Site Directors at two of the three locations we visited during our review stated that they take the daily collections (mostly checks) home with them for the night, rather than

leaving them at the school site, and then deliver the collections to Dunbar the following day. It is a violation of Parks & Recreation Cash Management Procedures for employees to take collections home.

It is recommended that ESP Management comply with Division of Parks & Recreation Cash Management Procedures.

Division of Parks & Recreation Management Response: ESP management is very concerned about this development as this procedure is completely against ESP policy and must stop immediately. To that end, a memo was sent immediately by ESP Management to all Site Directors and Bookkeepers demanding a stop to this practice immediately. Very clear wording has been added to the ESP Revenue Management Procedures to state in no uncertain terms that this is not ESP policy and failure to adhere to the policy shall be met with disciplinary action. Copies of this revised policy were distributed to all Site Directors and Bookkeepers with a verification of Receipt and Understanding that was to be signed and returned to the office to be included in the employee's file. All verifications have been received back in the office and personal meetings were held to make sure that each Site Director understood.

Deposits are to be made every Tuesday and again sometime during the week. This should cut down on the bulk of the revenue being kept on site as Tuesday deposits should be the bulk of the collections for the week. Otherwise deposits are to be secured on site to the best of the staff's ability and to the extent that the host facility will allow. ESP will make every effort to put an end to this unsafe practice and is very grateful to the Audit team for bringing this to our attention.