

Audit Report

Maryland African American Museum Corporation

September 2010



OFFICE OF LEGISLATIVE AUDITS
DEPARTMENT OF LEGISLATIVE SERVICES
MARYLAND GENERAL ASSEMBLY

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DEPARTMENT OF LEGISLATIVE SERVICES
OFFICE OF LEGISLATIVE AUDITS
MARYLAND GENERAL ASSEMBLY

Karl S. Aro
Executive Director

September 1, 2010

Bruce A. Myers, CPA
Legislative Auditor

Senator Verna L. Jones, Co-Chair, Joint Audit Committee
Delegate Steven J. DeBoy Sr., Co-Chair, Joint Audit Committee
Members of Joint Audit Committee
Annapolis, Maryland

Ladies and Gentlemen:

We have audited the Maryland African American Museum Corporation (MAAMC) for the period beginning April 2, 2007 and ending February 23, 2010. MAAMC oversees the programs of the Reginald F. Lewis Museum of Maryland African American History and Culture.

Our audit disclosed that MAAMC did not comply with certain provisions of its endowment fund investment policy. For example, MAAMC could not provide documentation to support certain significant decisions of its Finance and Audit Committee, which was established to monitor and direct the investments, and it did not obtain required conflict of interest statements from its financial managers. MAAMC also could not provide documentation to substantiate that its Board of Directors authorized the opening of a \$1 million line of credit, and the subsequent withdrawal of \$900,000 of those funds, that was needed to cover funding shortfalls. Furthermore, adequate procedures and controls were not established over MAAMC's art collection, cash receipts, and procurements.

MAAMC's response is included as an appendix to this report. We wish to acknowledge the cooperation extended to us by MAAMC during the course of this audit.

Respectfully submitted,

Bruce A. Myers, CPA
Legislative Auditor

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Background Information

Agency Responsibilities

The Maryland African American Museum Corporation (MAAMC) was created by State law in 1998 to oversee the development and future programs of the Reginald F. Lewis Museum of Maryland African American History and Culture located in Baltimore City, which opened to the public in June 2005. MAAMC is constituted as a public instrumentality and an independent unit in the Executive Branch. A Board of Directors manages the affairs of MAAMC, which appoints an Executive Director to direct and supervise the administrative and technical affairs of MAAMC.

According to the State's records, during fiscal year 2009, MAAMC's operating expenditures totaled approximately \$4.2 million, which consisted of \$2.1 million in general fund expenditures and \$2.1 million in privately funded expenditures.

Financial Statement Audits

MAAMC engaged an independent accounting firm to perform audits of its financial statements for the fiscal years ended June 30, 2009, 2008, and 2007. In the related audit reports, the firm stated that MAAMC's financial statements were presented fairly in conformity with accounting principles generally accepted in the United States of America.

Findings and Recommendations

Endowment Fund

Finding 1

The Maryland African American Museum Corporation (MAAMC) did not comply with certain provisions of its endowment fund investment policy related to the oversight of investment decisions and disclosure requirements intended to prevent conflicts of interest.

Analysis

MAAMC did not comply with certain provisions of its endowment fund investment policy. Specifically, our review disclosed the following conditions:

- MAAMC could not provide documentation (such as in its Board minutes) to support certain significant activities of its Finance and Audit Committee (FAC),¹ which was established to monitor and direct its endowment investments. Specifically, MAAMC could not document that the FAC obtained monthly reports on the investment performance, reviewed the policy annually, and met with the financial managers at least once a year—all required by the endowment fund investment policy. This is significant because the investments incurred significant losses during fiscal years 2008 and 2009. Although the investment values have subsequently recovered, the failure to comply with the policy could adversely impact the disposition of the funds.
- MAAMC could not provide documentation to support the methods used to select the financial managers, such as solicitations, proposals, or any other criteria used in the selection process. While MAAMC management advised that financial advisory services were solicited from several vendors by phone, they were unable to provide us with documentation to support that assertion. Furthermore, the MAAMC procurement policy requires at least two written bids for procurements of services greater than \$10,000. In this regard, one of the managers was paid approximately \$32,000 during the period from January through April 2009.
- MAAMC did not receive conflict of interest statements from the financial managers. The policy requires the financial managers to certify, at least annually, that neither the firm nor any of its partners, members, or employees

¹ Per MAAMC management, the FAC comprises two members of the Board of Directors and is staffed by the chief financial officer.

has any relationship with MAAMC or its directors that could appear to impair the good faith judgment of the firm to act in the best interests of MAAMC, with respect to MAAMC's accounts, or the good faith judgment of MAAMC, with respect to the investments and choice of managers.

In accordance with the April 2007 Joint Chairmen's Report (JCR), \$250,000 of MAAMC's fiscal year 2008 general fund appropriation was withheld until MAAMC submitted a report to the budget committees that it had selected an investment manager, outlined a long-term investment plan, invested its endowment funds according to the long-term investment plan, and completed an endowment draw policy. The required report was submitted to the budget committees and the \$250,000 was released for MAAMC's use. Further, in accordance with the JCR recommendations, MAAMC developed an investment plan and, beginning in fiscal year 2008, invested \$4 million of the endowment funds in a combination of investments, including cash and equivalents, mutual funds, government bonds, corporate bonds, stocks, and foreign assets. According to its records, the value of these investments at February 26, 2010 was approximately \$4.1 million.

Recommendation 1

We recommend that MAAMC

- a. ensure that the FAC properly monitors and directs investments in accordance with the policy and retains documentation to support these efforts,**
- b. document the process for selecting financial managers, and**
- c. obtain the required conflict of interest documentation from the financial managers and properly address any conflicts.**

Line of Credit

Finding 2

MAAMC could not document that its Board of Directors authorized the opening of a \$1 million line of credit and the subsequent withdrawal of \$900,000 to cover funding shortfalls.

Analysis

MAAMC could not provide documentation (such as in Board minutes) that its Board authorized the opening of a line of credit and subsequent withdrawals. Because of funding shortfalls, MAAMC opened a line of credit, secured by \$1 million in endowment funds, and withdrew \$900,000 during fiscal years 2008

through 2010.² While not documented, MAAMC management advised us that the Board of Directors approved the line of credit and related withdrawals to cover operating expenses and to comply with the State matching requirements. Consistent with State law, MAAMC enters into a memorandum of understanding each year with the Department of Budget and Management requiring it to match each dollar of State grant funds with other non-State funds. For fiscal years 2008 to 2010, MAAMC received a State grant to cover 50 percent of its operating costs.

State law also provides that the Board shall manage the affairs of MAAMC and shall exercise all of its corporate powers. Given the significance of the line of credit and the related funding shortfall, we believe that Board approval was warranted for the line of credit and related withdrawals.

Recommendation 2

We recommend that MAAMC document Board approval for critical financial decisions.

Art Collection

Finding 3

MAAMC had not established comprehensive procedures and adequate controls over its art collection.

Analysis

MAAMC lacked adequate controls over its art collection. Specifically, MAAMC maintained listings of its collection inventory; however, the listings did not include certain critical information, such as the location of each item and a tag number for identification and control purposes. Furthermore, the listings did not always include an approximate value of the items. In addition, our test of 10 items physically sighted at MAAMC disclosed that 2 were not listed on the aforementioned listings. Finally, we noted that MAAMC did not maintain an independent control account and did not conduct any physical inventories during our audit period. As a result, there was a lack of assurance that all art collection inventory was properly accounted for.

² While MAAMC has a substantial endowment fund, the endowment policy limits annual withdrawals.

This condition was caused, in part, by the lack of comprehensive written procedures and controls over the art collection, which should address, at a minimum, recordation of items, periodic physical inventories, an independent control account, and disposal procedures. According to its records, as of September 2009, the value of the MAAMC art collection inventory totaled approximately \$1.3 million; however, as previously noted, MAAMC had not recorded a value for numerous items included on these records.

Recommendation 3

We recommend that MAAMC

- a. develop comprehensive written procedures and controls for its art collection;**
- b. develop comprehensive detail inventory records (which include critical information, such as the location and value of the assets) and an independent control account, and periodically reconcile the control account balance to the related detail records; and**
- c. conduct periodic inventories and investigate any missing items.**

Cash Receipts

Finding 4

Procedures and controls were not established to ensure all cash receipts were deposited.

Analysis

MAAMC lacked adequate procedures and controls over cash receipts, which according to its records, totaled approximately \$1.3 million during fiscal year 2009. For example, while the employee who received monetary donations (which totaled approximately \$1.1 million in fiscal year 2009) recorded them on a check log, MAAMC procedures did not require that this log be used as the source for preparing letters from MAAMC to the donors to acknowledge receipt of such donations. Rather, this employee forwarded copies of the checks to the employees responsible for issuing the letters. Since the check log was used in the deposit verification process, the employee receiving these collections could direct that acknowledgment letters be prepared and misappropriate related collections without timely detection.

Recommendation 4

We recommend that

- a. MAAMC develop comprehensive procedures and controls for cash receipts, and**
- b. the check log used in the deposit verification process serve as the source for preparing donor acknowledgment letters.**

Procurements

Finding 5

MAAMC's procurement policies were not sufficiently comprehensive.

Analysis

MAAMC's procurement policies were not sufficiently comprehensive. For example, the policies did not address publicly advertising bid solicitations and awards, and the related procedures for ensuring that the bidding process was properly safeguarded. In addition, the procurement policies for sole source procurements did not require any written justification to support the propriety of the awards. In this regard, our test of eight procurements, with payments totaling \$221,510 that were awarded as sole source procurements (each over \$10,000), disclosed that the solicitations and awards were not publicized for any of the procurements. Furthermore, written justifications were not on file for six of these procurements.

State law provides that MAAMC shall adopt a system of financial accounting, controls, audits, and reports. Since MAAMC receives half of its funding from a general fund appropriation, it is critical that the policies and procedures related to procurements are sufficiently comprehensive to ensure the integrity of the procurement process. According to its records, during fiscal year 2009, MAAMC procured goods and services totaling approximately \$1.9 million.

Recommendation 5

We recommend that MAAMC ensure that its procurement policies and procedures are sufficiently comprehensive to ensure the integrity of the procurement process.

Audit Scope, Objectives, and Methodology

We have audited the Maryland African American Museum Corporation (MAAMC) for the period beginning April 2, 2007 and ending February 23, 2010. The audit was conducted in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

As prescribed by the State Government Article, Section 2-1221 of the Annotated Code of Maryland, the objectives of this audit were to examine MAAMC's financial transactions, records and internal control, and to evaluate its compliance with applicable State laws, rules, and regulations.

In planning and conducting our audit, we focused on the major financial-related areas of operations based on assessments of materiality and risk. The areas addressed by the audit included endowment investments, purchases and disbursements, cash receipts, payroll, and art collection inventories. Our audit procedures included inquiries of appropriate personnel, inspections of documents and records, and observations of MAAMC's operations. We also tested transactions and performed other auditing procedures that we considered necessary to achieve our objectives. Data provided in this report for background or informational purposes were deemed reasonable, but were not independently verified.

MAAMC's management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that objectives pertaining to the reliability of financial records, effectiveness and efficiency of operations including safeguarding of assets, and compliance with applicable laws, rules, and regulations are achieved.

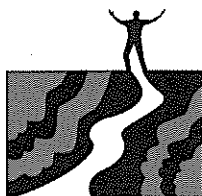
Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or compliance with policies and procedures may deteriorate.

Our reports are designed to assist the Maryland General Assembly in exercising its legislative oversight function and to provide constructive recommendations for improving State operations. As a result, our reports generally do not address activities we reviewed that are functioning properly.

This report includes findings relating to conditions that we consider to be significant deficiencies in the design or operation of internal control that could adversely affect MAAMC's ability to maintain reliable financial records, operate effectively and efficiently, and/or comply with applicable laws, rules, and regulations. Our report also includes findings regarding significant instances of noncompliance with applicable laws, rules, or regulations. Other less significant findings were communicated to MAAMC that did not warrant inclusion in this report.

MAAMC's response to our findings and recommendations is included as an appendix to this report. As prescribed in the State Government Article, Section 2-1224 of the Annotated Code of Maryland, we will advise MAAMC regarding the results of our review of its response.

APPENDIX



REGINALD F. LEWIS MUSEUM
of Maryland African American
History & Culture

August 26, 2010

Bruce A. Myers, CPA
Legislative Auditor
Office of Legislative Audits
301 West Preston Street – Room 1202
Baltimore, MD 21201

Mr. Myers:

Our responses to the audit findings for the Maryland African American Museum Corporation (MAAMC) are as follows:

Finding 1

MAAMC's Finance and Audit Committee (FAC) does monitor and direct the investments in its endowment fund. Currently the FAC has two members and is staffed by MAAMC's chief financial officer. Being such a small group, most business is conducted via telephone and electronic mail. In the future MAAMC will ensure that formal meetings are documented and that said documentation is retained.

MAAMC did receive a conflict of interest statement from its financial manager. However, that statement did not speak to all of the required disclosures as stated in MAAMC's endowment investment policy. MAAMC will ensure that future conflict of interest statements include all of the required disclosures.

Finding 2

Board approval of the line of credit was received. However, this approval and the related discussions concerning the line were not adequately documented in Board minutes. MAAMC will make certain that future critical decisions are documented in Board minutes.

Finding 3

For clarification purposes only please note that MAAMC's collection includes not only art but, historical artifacts. MAAMC does have a written Collections Management Policy (CMP). The CMP is a working document and speaks more to the collections review

process (i.e., what types of items we will acquire and why) and not to the cataloguing process. It also includes a section on deaccessioning (disposal) of collection items.

MAAMC will assess its current CMP for any deficiencies in the recommended areas and revise that policy accordingly.

Finding 4

MAAMC does maintain a written controls policy for its cash receipts. We will review this policy and make revisions as necessary.

MAAMC will use the check log used in the deposit verification process, along with copies of the check and other documentation received, as the source for preparing donor acknowledgment letters.

Finding 5

MAAMC will review its procurement policies and make revisions as necessary to ensure the integrity of the procurement process.

Respectfully,



David T. Terry, Ph.D.
Executive Director

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