

OPERATIONAL AUDIT

J.M. DAVIS MEMORIAL COMMISSION

For the period January 1, 2008 through January 31, 2012



*Independently serving the citizens of
Oklahoma by promoting the
accountability and fiscal integrity of
governmental funds.*



Oklahoma State
Auditor & Inspector
Gary A. Jones, CPA, CFE

**Audit Report of the
J.M. Davis Memorial Commission**

**For the Period
January 1, 2008 through January 31, 2012**



Oklahoma State Auditor & Inspector

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March 25, 2013

TO THE J.M. DAVIS MEMORIAL COMMISSION

This is the audit report of the J.M. Davis Memorial Commission for the period January 1, 2008 through January 31, 2012. The goal of the State Auditor and Inspector is to promote accountability and fiscal integrity in state and local government. Maintaining our independence as we provide this service to the taxpayers of Oklahoma is of utmost importance.

We wish to take this opportunity to express our appreciation for the assistance and cooperation extended to our office during our engagement.

Sincerely,

A handwritten signature in blue ink, appearing to read "Gary A. Jones".

GARY A. JONES, CPA, CFE
OKLAHOMA STATE AUDITOR & INSPECTOR

J.M. Davis Memorial Commission Operational Audit

Background

The duty of the J.M. Davis Memorial Commission (Agency) is to house, preserve, and display the J.M. Davis Gun Collection and other artifacts. Oversight is provided by a five-member Commission (Commission) appointed by the Governor with the advice and consent of the Senate. The Commission pays for its operations through state appropriations, gift shop revenue, and donations.

Commission members are:

William Higgins Chair
 Jack Mayberry..... Vice-Chair
 Denny Haddox.....Member
 Chris SutherlandMember
 Donald HillMember

Table 1 summarizes the Agency's sources and uses of funds for fiscal years 2011 and 2010 (July 1, 2009 through June 30, 2011).

Table 1 - Sources and Uses of Funds for FY 2011 and FY 2010

	2011	2010
Sources:		
State Appropriations	\$ 306,671	\$ 332,013
Merchandise Sales	22,609	24,806
Private Grants & Donat. For Opns	21,155	-
Contributions/Other	11,865	29,127
Total Sources	<u>\$ 362,300</u>	<u>\$ 385,946</u>
Uses:		
Personnel Services	\$ 330,632	\$ 334,440
Professional Services	21,712	10,081
Miscellaneous Administrative	50,654	61,423
Maintenance and Repair Expense	7,406	5,716
Production, Safety, Security Expense	561	2,615
Office Furniture and Equipment	5,636	13,829
Merchandise for Resale	9,244	12,335
Other	5,679	5,229
Total Uses	<u>\$ 431,524</u>	<u>\$ 445,668</u>

Source: Oklahoma PeopleSoft Accounting System (unaudited, for informational purposes only)

J.M. Davis Memorial Commission Operational Audit

Purpose, Scope, and Sample Methodology

This audit was conducted in response to 74 O.S. § 212, which requires the State Auditor and Inspector's Office to audit the books and accounts of all state agencies whose duty it is to collect, disburse or manage funds of the state.

The audit period covered was January 1, 2008 through January 31, 2012.

Sample methodologies can vary and are selected based on the audit objective and whether the total population of data was available. Random sampling is the preferred method; however, we may also use haphazard sampling (a methodology that produces a representative selection for non-statistical sampling), or judgmental selection when data limitation prevents the use of the other two methods. We selected our samples in such a way that whenever possible, the samples are representative of the populations and provide sufficient evidential matter. We identified specific attributes for testing each of the samples. When appropriate, we projected our results to that population.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. This report is a public document pursuant to the Oklahoma Open Records Act (51 O.S. § 24A.1 et seq.), and shall be open to any person for inspection and copying.

Objective – Determine whether the Agency's internal controls provide reasonable assurance that revenues, expenditures (including payroll), and inventory were accurately reported in the accounting records.

Conclusion

The Agency's internal controls generally provide reasonable assurance that miscellaneous expenditures were accurately reported in the accounting records, but not that revenues (manually processed), payroll expenditures, or inventory were accurately reported.

Methodology

To accomplish our objective, we performed the following:

- Obtained an understanding of internal controls related to the revenue, expenditure, payroll, and inventory processes through discussions with Agency personnel, observation, and review of documents.
- Tested internal controls using the following procedures:
 - Reviewing expenditure documentation from 60 randomly selected payments to ensure they were independently and properly reviewed and approved.

J.M. Davis Memorial Commission Operational Audit

- Ensuring vendor warrants are handled by someone independent of the expenditure posting process.

Observation

Control Environment Risks Are High

An effective internal control system has in place policies and procedures that reduce the risk of errors, fraud, and professional misconduct within the organization. A key factor in this system is the environment established by management. Management's ethics, integrity, attitude, and operating style become the foundation of all other internal control components.

As part of our control risk assessment, we surveyed and interviewed the three Agency employees other than the executive director. We noted the following general concerns:

- Employees are not satisfied with the ethical tone at the Agency.
- An atmosphere of mistrust and poor communication exists.

In addition, the Agency does not have a written code of ethics.

Employees' concerns, whether they are factual or perceived, have a negative impact on the Agency's control environment. This increases the risk of errors and misappropriation of assets.

Recommendation

We recommend the Commission and the executive director recognize the risks associated with this type of environment and begin working towards evaluating and addressing the situation to ensure the mission of the Agency is accomplished in the most efficient manner possible.

This may include developing a written code of ethics and ensuring employees have a trusted method to report suspected improper activity.

Views of Responsible Officials

Since October of 2012, employees have held a weekly meeting with the director to discuss museum projects and their status. Employees are encouraged to bring up any concern or idea they may have about the projects. Employees agree to the timetable assigned to each project.

Employees are working with the executive director to write a written code of ethics that will be reviewed by the museum's board of commissioners.

Observation

Inadequate Controls over Revenues

To protect against possible errors or irregularities, an effective internal control system should provide reasonable assurance that assets are adequately safeguarded.

The Agency receives its manually processed revenues through gift shop sales and donations in four locked boxes throughout the museum. While receiving cash in this manner is inherently risky, the Agency has designed controls to lessen the risk by having multiple employees perform cash-related duties and having review processes in place. For example, the Agency's policy is for two employees to collect cash donations together and initial a log of the amount collected, which is later compared to the bank deposit.

However, during our visit to the museum we observed the executive director collecting cash from the donation boxes unassisted, thus circumventing the safeguards discussed. It appears these controls, while properly designed, are not being effectively implemented.

This lack of implementation could allow funds to be misappropriated without detection.

Recommendation

Employees should adhere to the Agency policy of collecting cash donations only in groups of two, properly documenting and reviewing the amount collected. If at all possible, the executive director, who is responsible for the bank deposit review, should not be one of the collecting parties.

In addition, management should be responsible for ensuring the Agency's key controls are properly implemented, and should set an example of proper conduct for the other employees.

Views of Responsible Officials

Two employees should be present when all cash is collected and counted at the end of the day. This process is understood and carried out on a daily basis by all employees. Both employees will be at the front desk donation box when the money is collected.

Observation

Failure to Retain Key Expenditure Documentation

An effective internal control system provides for accurate and reliable records and adequate review of supporting documentation.

J.M. Davis Memorial Commission Operational Audit

During our procedures related to miscellaneous and payroll expenditures, we encountered multiple instances in which the Agency was unable to provide the supporting documentation requested. Of the 60 randomly selected expenditure claims included in our sample (totaling \$26,386), the Agency was unable to provide invoices to support three of the payments, totaling \$947¹.

During our payroll procedures, we attempted to review payroll claims and related documents for 25 randomly selected months of the audit period. The Agency was unable to provide us with supporting documentation of payroll costs for the following:

- Five of 25 months for full-time employees
- 19 of 25 months for part-time employees

Overall, the Agency was able to provide full payroll documentation for only two of the 25 months selected. Because of this lack of documentation, we were unable to determine whether the Agency truly has adequate safeguards in place over its payroll process.

Without adequate support for its expenditures, the Agency cannot document exactly what transactions took place, or whether they were reasonable and properly reviewed. Lack of documentation also impedes the ability of entities with oversight responsibility – such as the Commission – to perform their duties.

Recommendation

Management should review and retain detailed documentation to support all financial transactions, including miscellaneous and payroll expenditures. These records should be maintained for at least the minimum length of time required by relevant laws (such as 21 O.S. § 590.A²) and organized in such fashion that they can be made available to the Commission and other appropriate parties as needed.

Views of Responsible Officials

The failure to find some of the records payroll costs is partly due to inadequate record keeping on the museum's part. The next week after the auditor's visit to the museum employees began to correct this problem. Records have been

¹ Auditors were able to obtain two of the three expenditure claims through the Department of Libraries.

² 21 O.S. § 590.A states in part, "A. Every state governmental entity shall, for a period of two (2) years, maintain accurate and complete records, as defined in Section 203 of Title 67 of the Oklahoma Statutes, reflecting all financial and business transactions, which records shall include support documentation for each transaction. No such records shall be disposed of for three (3) years thereafter, except upon a unanimous vote of the members of the Archives and Records Commission..."

correctly filed and prepared for storage that will allow a prompt response for these records in the future. OMES has been handling the museum's payroll records since 2010.

Observation

Inadequate Controls Related to Inventory

To protect against potential errors and misappropriation, an effective internal control system provides reasonable assurance that assets are adequately safeguarded.

Museum Inventory

All responsibilities related to museum inventory belong to the curator. In addition to handling museum inventory items, he is solely responsible for updating electronic inventory records (including additions, changes, and removals) and is the only employee with access to the museum inventory system. He performs the annual inventory count with another employee.

Without proper segregation of duties, the curator has the opportunity to make changes to the electronic inventory system without detection, which increases the risk of misappropriation of museum assets.

Gift Shop Inventory

During our procedures related to revenues, it was brought to our attention that the Agency does not have a system in place to track the items for sale in the museum gift shop. Without an inventory tracking system, it would appear difficult for management to properly track sales, restock sold items, and monitor to ensure gift shop inventory is not being stolen or damaged.

Recommendation

We recommend management improve the safeguarding of its museum assets by properly segregating inventory duties. Handling of items such as guns which are susceptible to theft is an inherently risky situation, and the Agency's small staff size amplifies this risk. Management should ensure at least one additional employee is involved in the museum inventory process, and the employee responsible for recordkeeping should not be involved in the inventory count.

Steps should also be taken to ensure management could access the electronic inventory records if the curator were no longer present.

We further recommend that management develop an inventory system to track the items purchased for the gift shop, to enable them to track available inventory and monitor for potential theft or other shrinkage. Inventory could be tracked in a

J.M. Davis Memorial Commission Operational Audit

variety of manners, from use of spreadsheets that are later compared to cash register records, to implementation of a barcode and scanner system. Periodic inventory counts of gift shop inventory would further allow management to track and monitor the items present.

Views of Responsible Officials

The recommendations by the auditor will be implemented with the next inventory count in 2014. The curator is in the process of amending the collection management policies and procedures and will seek approval by the museum commissioners at the March, 2013 commission meeting. Employees other than the curator and executive director will conduct the actual annual inventory.

A Gift Shop Manger was hired by the agency on March 8, 2013. As part of their job duties, they will begin a process for better inventory controls.

Other Items Noted

Although not considered significant to the audit objective, we feel the following issue should be communicated to management and the Commission.

Observation

Questionable Consignment Inventory in Museum Gift Shop

Through discussions with staff and review of documentation we learned that an acquaintance of the executive director has been permitted to place items for sale in the museum gift shop on a consignment basis since the close of our audit period. The Agency also made regular inventory purchases from the same vendor. The Agency paid \$941 to this vendor during the audit period, as well as \$762 since the audit period (\$448 on a consignment basis).

We did not encounter any Agency policies specifically addressing consignment sales. The Commission chairman indicated that the Commission has recently been made aware of this situation and has asked that consignment sales cease in the gift shop.

Because these sales benefitted a private business, they may have violated Article X, Section 15.A of the Oklahoma Constitution, which states:

Except as provided by this section, the credit of the State shall not be given, pledged, or loaned to any individual, company, corporation, or association, municipality, or political subdivision of the State, nor shall the State become an owner or stockholder in, nor make donation by gift, subscription to stock, by tax, or otherwise, to any company, association, or corporation.

J.M. Davis Memorial Commission Operational Audit

Recommendation We recommend the Commission visit with its Attorney General liaison regarding the potential Constitutional conflict and as applicable, develop and implement policy addressing this situation.

Views of Responsible Officials The consignment agreement with the vendor that was discussed with the auditor in the gift shop has been terminated.



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