

April 5, 2023

Board of Directors and Management of
The Southeastern District, LCMS

In planning and performing our audit of the financial statements of the Southeastern District as of and for the year ended December 31, 2022, in accordance with auditing standards generally accepted in the United States of America, we considered the District's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we do not express an opinion on the effectiveness of the Southeastern District's internal control.

A deficiency in internal control 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 or detect and correct misstatements on a timely basis. A material weakness is a deficiency or combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses. In addition, because of inherent limitations in internal control, including the possibility of management override of controls, misstatements due to error or fraud may occur and not be detected by such controls. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses.

During our audit, we became aware of the following matters, which we believe represent opportunities for strengthening internal controls and operating efficiency:

BANK RECONCILIATION PROCESS

Segregation of duties is a fundamental requirement for a strong system of internal controls. The fundamental concept of segregation of duties is that no one individual should have total control over any transaction or perform more than one function of authorizing transactions, recording transactions, or maintaining custody of an organization's assets. Designing a system of internal controls with adequate segregation of duties is inherently difficult for small organizations with limited staff, such as the Southeastern District. For these types of organizations, designing strong controls over the bank reconciliation process is a critical component of internal control.

Through our audit procedures we were pleased to note the District is reconciling its bank accounts on a monthly basis. Currently, the District Director of Business and Finance obtains the bank statements directly via the bank's online system. Once the bank statements are obtained, the Director of Business and Finance reviews it for unusual activity (i.e. unusual deposits, unusual payees), and then performs the reconciliation. Further discussions with District management confirmed that, upon their completion, the reconciliations are not reviewed and approved another member of the District staff who is independent of the cash receipting and disbursing functions.

BANK RECONCILIATION PROCESS – Continued

To strengthen controls over the District's bank reconciliation process, we recommend that someone independent of the cash receipting and disbursing function (e.g., District President or Treasurer) directly obtain the bank statements via the bank's online system. This person should review the account activity and all canceled checks for authorized signatures, unusual payees, irregular endorsements, and possible alterations in payees or dollar amounts. The Director of Business and Finance can also obtain the bank statements via the bank's online system in order to prepare the monthly reconciliation of the cash account balances. Once completed, the reconciliations should be reviewed and approved by the District President or Treasurer. By separating these duties and implementing a review and approval process for bank reconciliations, internal controls over cash will improve thereby reducing the District's risk of errors and/or fraud.

DONOR-RESTRICTED ENDOWMENT POLICIES

The District's donor-restricted endowment currently consists of two individual funds (Anna Hoffmeister and Spillman Memorial Funds) established by donors to provide annual funding for preparing church workers. Since these funds were received by the District, substantial changes have occurred in the management of endowments by not-for-profit organizations. These changes can be attributed to the following:

1. The Council of The District of Columbia enacted the Uniform Prudent Management of Institutional Funds Act (UPMIFA) with an effective date of January 23, 2008. UPMIFA focuses on managing donor-restricted endowment funds as a whole (the original gift and net appreciation) and as a prudent investor would. It eliminates the prior concept of historical value in favor of a more robust set of guidelines about what constitutes prudent spending, explicitly requiring consideration of the duration and preservation of the fund.
2. In response to the UPMIFA legislation, the Financial Accounting Standards Board (FASB) issued new accounting rules for the net asset classification of donor-restricted endowment funds and enhanced the disclosure requirements for a not-for-profit's endowment funds (both donor-restricted and board-designated endowments). This guidance from the FASB enabled users of financial statements to understand the net asset classification, net asset composition, changes in net asset composition, spending policies, and related investment policies for all endowment funds.

The District previously invested these funds various certificates with LCEF and Wells Fargo and used the yearly income for scholarship purposes. Since these investments didn't provide substantial earnings or preservation of the funds, the District's Finance Committee decided to move the funds into a larger LCEF certificate and use 50% of the earnings to increase the value of the endowment funds and use the remaining 50% for the endowments' purpose.

DONOR-RESTRICTED ENDOWMENT POLICIES – Continued

We recommend the Board of Directors and management review all existing endowment investment and spending policies and consult with your legal counsel to ensure they are in compliance with any and all applicable statutes of The District of Columbia or elsewhere. We also recommend all endowment policies be formalized and adopted by the Board as these policies are required by Accounting Principles Generally Accepted in the United States to be disclosed in your audited financial statements (see Note L of your 2022 audited financial statements).

SOUTHEASTERN DISTRICT ENDOWMENT

The District established the Southeastern District (SED) Endowment with a Declaration of Rules and Policies in September 2011. The fund was to be used for expenses outside normal operating budget of the District. The endowment remained unfunded until May 2014 when the District Board of Directors added \$750,000 of the proceeds from the sale of Raven Rock Camp. No additional contributions in the form of Board-designations or donor-restricted gifts have been added since 2014.

Based on the policies of the fund, the District should distribute at least 85% of the income each year; however, any undistributed income is to be added to the principal of the fund. The fund hasn't distributed any income since its inception; therefore, all interest and dividend income from the linked investment has been added to the principal each year. As of December 31, 2022, the SED Endowment has a corpus of \$962,754.

Given the limited activity, current investment market, and lack of donor giving, we suggest management and the Board of Directors review the SED Endowment's purpose to determine if future uses exists. We also suggest reviewing the related policies for clarification of proper accounting for investment activity (i.e. interest, dividend, and gains/losses).

This communication is intended solely for the information and use of the Board of Directors, management, and others within the Organization, and is not intended to be, and should not be, used by anyone other than these specified parties.

We appreciate the opportunity to provide audit services to the Southeastern District and would like to thank Sidney Heetland and Donald Tucker for the cooperation and courtesy extended to us during the audit process. Should you have any questions regarding this letter or the audited financial statements, or if we can be of further assistance in the current fiscal year, please do not hesitate to call.

Sincerely,



Christopher Wood, CPA, CFE
Executive Director, LCMS Accounting and Financial Services