

**METROPOLITAN GOVERNMENT OF NASHVILLE AND DAVIDSON COUNTY
METROPOLITAN AUDIT COMMITTEE MEETING**

September 25, 2012

On Tuesday, September 25, 2012, at 4:00 p.m., the Metropolitan Nashville Audit Committee met in the Metropolitan Courthouse, 2nd Floor, Committee Room 4. The following people attended the meeting:

Committee Members

Bob Brannon, Chairman
Brack Reed, Vice Chairman
Richard Riebeling, Director of Finance
Jacobia Dowell, Council Member
Diane Neighbors, Vice-Mayor

Others

Mark Swann, Metropolitan Auditor
Carlos Holt, Internal Audit Manager
Jack Henry, Internal Auditor
Albert U. Tiede, Administrator of Elections
J. Dell Crosslin, Crosslin & Associates, P.C.
Rich Lockwood, Crosslin & Associates, P.C.
Rachelle Gallimore-Scruggs, Department of Law

Committee Member Absent

Steve Glover, Metro Council

Quorum present? Yes

Call Meeting to Order

Bob Brannon, Committee Chairman, called the meeting to order.

Approval of Minutes

The minutes of the meeting on July 10, 2012, were approved.

New Business

Discussion on Council members' request dated September 4, 2012, for an audit of Davidson County Election Commission Use of Electronic Polling Books (Mark Swann – Metropolitan Auditor)

The Metropolitan Auditor met with the Davidson County Administrator of Elections, Albert Tiede two weeks ago and discussed the issue leading up to this request. Subsequent to this meeting, Mr. Tiede had a meeting with Metropolitan Nashville Council members to explain the events that created the problem at the August 2, 2012, election concerning the use of electronic poll books from Election Systems and Software. Mr. Tiede's internal review revealed that three voting precincts were problematic with the voter history tally and the voting machine tally. He indicated this was a result of poll worker operator error and changes made to the electronic poll book software to facilitate a process improvement request for users of the software in closed primary states. This resulted in the party in order of precedence, in this case the Republican party, being used on the voter application when one was not declared by the voter or poll administrator.

Mr. Swann stated all parties believe an independent internal audit is warranted of the events that occurred at the August 2, 2012, election. However, the Davidson County Administrator of Elections, Mr. Tieche, has requested that due to November presidential pre-election processing requirements, this audit be delayed until after the election. Additionally, the Metropolitan Auditor recommended the audit's scope consist of the entire election process, including manual and automated computer controls relied upon to ensure election integrity.

Ms. Neighbors said that she thinks that everyone was in agreement that the audit should be after the election in November. Ms. Dowell added that she thought everyone was comfortable with doing the audit after the election. Mr. Swann said that several council members had told him that they were concerned about the whole process. The audit should be a good independent objective review of the controls that Metro places reliance on to ensure the integrity of the election process. Just like any process there is a risk of something going wrong, so the goal is to minimize risk to the greatest extent possible.

Ms. Neighbors said that she thought it was the whole acquisition process of the books, the procedures for purchasing and then also anything that happened during the day of the primary. Ms. Neighbors then made the motion and it was seconded that the Office of Internal Audit revise the Office of Internal Audit 2012 Work Plan to include one more audit to facilitate this request and a response be made to the Metropolitan Nashville Council. The motion carried.

Ms. Dowell inquired about using the electronic poll books for this upcoming election because she knows that part of the concerns were around the process and procedures for using the electronic poll books. This was one of the reasons for the request for the audit. It was her understanding that this upcoming election was not using the electronic poll books other than maybe to look up something.

Mr. Riebeling said that was correct and they will be using traditional paper poll books. The Election Commission will still have one electronic poll book in every poll to look up voters that have had a change of address. There were no additional questions by the committee.

Discussion on Juvenile Court Clerk's Office audit report issued August 9, 2012 (Mark Swann – Metropolitan Auditor)

The Juvenile Court Clerk's Office budget for FY2011 was \$1.5 million which allowed the Office to process records related to 46,649 cases; collect fees and fines of \$675,000; process child support of \$2.0 million; and manage a \$1.9 million victims' compensation trust fund portfolio. The audit period included fiscal year 2010, 2011, and the first half of 2012.

The Office of Internal Audit was unable to render an opinion on the completeness of revenue collections for fines and fees along with receipts for child support due to documentation not being available for several months of activity. It was presumed that the documentation was destroyed as a result of the May 2010 flood. Seventy-seven percent of respondents to a survey strongly agreed that service received at the Juvenile Court Clerk's Office was effective.

Key recommendations related to: segregation of duties in the cash collections and recording of cash receipts process; posting cash receipts accounting transactions within two business days; retaining adequate documentation; limiting individual employees' abilities to make changes to accounting sub-systems without adequate approval; and documenting the victims' trust fund investment policy. Management of the Juvenile Court Clerk's Office was responsive to all Office of Internal Audit recommendations. There were no questions by the committee.

Discussion on Metropolitan Transit Authority Procure-to-Pay Process audit report issued August 10, 2012 (Mark Swann – Metropolitan Auditor)

This was a review of the Metropolitan Transit Authority (MTA) procurement process. Between FY 2010 and FY 2011 MTA processed over 18,000 payment vouchers totaling \$60.8 million, \$23 million was for bus purchases and \$6.8 million for fuel. Purchase Orders were managed through the Ron Truly fleet management systems and invoices were paid after a successful two-way or three-way match was completed using MTA's Sage ACCPAC accounting system.

Emerging internal control risks observed included a significant number of purchase orders being created after the invoice for goods or services was received. This was true for 46 percent of our sample. One explanation provided was that most of these purchases could be related to the emergency purchases for the May 2010 flood. However, documentation was lacking on these orders to confirm this claim. Approval of purchase requisitions was not discernible or was missing for 15 of 85 sampled items (17 percent). Also, a significant number of invoices were not paid on time per the invoice due date, which resulted in 197 of 208 (95 percent) invoices with payment discount terms being missed. Also, the temporary Accounts Payable Manager was using the computer user account of the recently retired Accounts Payable Manager, thus diminishing individual accountability of accounts payable computer activity. MTA management was responsive to all Office of Internal Audit recommendations.

There were no questions by the committee.

Discussion on Metro Public Health Department Drug Inventory Management audit report issued August 10, 2012 (Mark Swann – Metropolitan Auditor)

The Metro Public Health Department Pharmacy Services holds a retail and wholesale pharmacy license. The retail pharmacy is located at Metro's Lentz Public Health Center. Indigent patients can fill prescriptions for free or a \$7 co-payment. The wholesale license serves the distribution of medications to the three Metro Nashville public health clinics (*only Schedule IV and V drugs, no "controlled" substances*). Additionally, the Metro Animal Care and Control veterinarian orders and dispenses medicine (*includes Schedule II and III controlled substances*) to animals. For fiscal year 2012, drug expenditures were \$270,000 for pharmacy services and \$44,000 for animal care or a total of \$314,000.

The audit found that Metro Public Health needed to improve its management of drug on-hand inventory. Records were maintained of medications as they were being dispensed. However, periodic reconciliations of drugs on-hand with purchases and dispensations were not performed. Existing computer system functionality was not used to record purchased inventory. Improvement in documenting the disposal of expired drugs was also needed as drugs were properly disposed of but no records were kept as to precisely what was disposed of (including controlled drugs).

Management of the Metro Public Health Department was responsive to all Office of Internal Audit recommendations.

Mr. Riebeling asked if the Office of Internal Audit will follow-up with the Metro Public Health Department Drug Inventory Management to determine their progress on the corrective action.

Mr. Swann said that the Office of Internal Audit will follow-up through a self-reporting system that asks audit clients about the progress of their corrective action plan and the issue stays

open until they indicate they have completed the job. In the annual report, there's a chart of how many recommendations are still open. As audits are performed, like the Juvenile Court Clerk audit, verification of corrective action is performed. There are some shops that do make it their policy to verify after 90 days. The Office of Internal Audit resources are limited, so when the audit client indicates they did take corrective action, they are taken at their worded statement that they actually completed the action.

There were no additional questions by the committee.

Discussion on Music City Convention Center Construction Project interim audit report issued August 14, 2012 (Mark Swann – Metropolitan Auditor)

This was the fifth interim report for the Music City Convention Center Construction project. As of July 11, 2012, 82 percent of the \$585.8 million budget had been paid or \$480.5 million paid out. This audit focused on reviewing the administrative controls over the Owner Controlled Insurance Program (OCIP) which provides project specific insurance coverage including commercial general liability, umbrella/excess liability, builder's risk, employer's liability, and workers' compensation.

The OCIP budgeted cost was \$5.7 million based on initial total labor costs of \$68 million. Recently it was determined that the labor costs estimate will come up short. However, current budget contingency should absorb additional OCIP expenditures. Also, the Hartford Insurance Company has started auditing submitted payrolls for closed contractors and sub-contractors.

It was the Office of Internal Audit's opinion that OCIP was effectively managed by the Convention Center Authority Project Management staff and the OCIP Administrator. Contractor and subcontractor records, totaling \$47.5 million in contract value, were reviewed for 28 OCIP participants to determine the level of compliance with program requirements. No exceptions were observed. Management of the Convention Center Authority Project Management Office was responsive to all Office of Internal Audit recommendations.

Mr. Riebeling asked if the Office of Internal Audit will do some audit work after the fact when the Convention Center opens on May 1. Mr. Swann said that the Office of Internal Audit will have some funds for consulting work that needs to be directed and it might be good to have a close out audit.

There were no additional questions by the committee.

Discussion on Metropolitan Nashville Public Schools Custodial Outsourcing audit report issued August 15, 2012 (Mark Swann – Metropolitan Auditor)

The Metropolitan Nashville Public Schools (MNPS) custodial and grounds keeping outsourcing contract and financial savings projections were reviewed as part of this audit. The contract with GCA Services Group for \$22.7 million per year represents 3.6 percent of MNPS' fiscal year 2011 budget. As a result of this contract, 586 custodial and grounds keeping employees resigned, retired, or were laid off.

The audit identified 209 (36 percent) former MNPS employees who were hired by GCA Services Group. Additionally, using Bureau of Labor Statistics and GCA payroll records, the audit found that GCA Services Group pays more in hourly wages and benefits than the private sector pays

but less than the government sector. This will normally hold true for most hourly labored classified job categories in the Metro Nashville Government.

The Office of Internal Audit was able to verify that projected annual budgeted cost savings of at least \$6.5 million were realized through this outsourcing arrangement. Performance report card grades prepared by MNPS principals were "A" or "B" 94 percent of the time. An audit survey of 15 principals provided an overall average grade of "B".

The audit recommended that MNPS formalize a monitoring plan for this contract to document how the specific contract terms and pricing would be monitored. Subsequent to the release of the audit report, a written contract monitoring plan was developed.

Ms. Dowell stated there is more cost associated than just savings; there are some other intrinsic costs. Personally with the outsourcing, the schools in Ms. Dowell's district are not as clean. When she goes in them they're not as tidy as they were when whoever else was doing it. Ms. Dowell said she wasn't here when they had the big discussion about outsourcing. Mr. Swann stated again that 94 percent of the time the MNPS own internal staff and the Office of Internal Audit small survey of 15 principals gave an overall average grade of "B" and above. Ms. Dowell suggested the community needs to drive by the schools and go in there. She said she would take some pictures and send them to the Office of Internal Audit. She also said that people are not always going to answer honestly when employees are working in your building. They will be biased. Ms. Dowell said that she was anti-outsourcing and it causes a lot of problems.

There were no additional questions or comments by the committee.

Discussion on Hotel Occupancy Tax Audit Approach (Mark Swann – Metropolitan Auditor)

The Office of Internal Audit has completed a pilot audit of three hotels. The hotels included Brentwood Suites (56 rooms), Quality Inn & Suites (173 rooms), and Embassy Suites – Vanderbilt (208 rooms). A review of ten months indicated potential underreporting of hotel property revenue due to calculation errors, missing documentation or application of exemptions to room tax.

Initial results showed that large hotels had sophisticated software for hotel operations with little paper documentation to support rented room nights. This results in an audit skewed more to the surrounding general and application computer controls to place reliance on reports produced by the software. Medium and small hotels are more likely to have a manual system and employees with less knowledge of documentation required to be maintained for hotel occupancy tax audits.

Based on these three initial hotel audits we estimate that it would require 7,800 work hours to audit all 298 hotels (properties in the three year audit scope) in one year. If 2,200 hours were allocated annually, approximately 75 properties could be reviewed resulting in a four year cycle to audit all hotel properties. This briefing is for information purposes only and no motion is required. We still have half of the 800 hours available to continue this project for the remainder of this year.

Mr. Lockwood said if he understands the law, that you only get a three year look back so it might be in the governments best interest to concentrate on high risk hotels that are approaching that three year window before it closes; otherwise, if it closes you can't capture that revenue.

Mr. Reed asked if that statute applied to all situations. If it's fraud or intentional, he thinks, it wouldn't apply. Mr. Swann said the Department of Law was requested for an interpretation whether it was for three years or 36 rolling months.

The Office of Internal Audit is trying to see if the hotel operator is making a good faith effort going backward in time and hope to repair any leakage going forward. To do all the hotels would be time consuming and would take all of the Office of Internal Audit resources to do all of them in one year. As we learn more we will come back and re-visit this subject.

There were no additional questions or comments by the committee.

Discussion on Annual Metro-Wide Audit Risk Priority Assessment (Mark Swann – Metropolitan Auditor)

The committee was asked to review Attachment D, 2012 Risk Prioritization Service Delivery Objectives and associated risk. The 2013 annual work plan preparation will be starting up next month and it will be beneficial to have the committee members review the risk and the impact assumptions used in the annual assessment.

Ms. Dowell asked about item #2 on page 36 of the agenda workbook regarding the risk of "Favoritism in employment selection or promotion process." She asked Mr. Swann how that is measured looking at equality. Mr. Swann said that the metric used to measure the impact was the number of employees. If an entity has more than 500 employees, the entity will receive a high score. If between 50 and 500 full-time equivalent (FTE) employees, it will get a medium score, and if less than 50 FTE it will get a low score. If there are more employees there is more opportunity for favoritism. Ms. Dowell asked if any measurement was done looking at employee promotions for example how many women are in managerial positions. Mr. Swann said we are not doing that for the risk assessment process but the number of positions posted department wide might be something to add to the assessment.

Ms. Dowell said it would be interesting to know how many people are related to someone. She said she hears it all the time about nepotism and situations where there is not equality and maybe all of the managers are related. Ms. Dowell was curious if there was a way of measuring that to find out if there is any truth to these concerns. Mr. Swann said that we can bring that up to the human resources department who has likely had the question before. Mr. Swann said Ms. Dowell had brought up some good points for the annual risk assessment and he could add the number of promotions for an entity as a better measurement than number of employees. There were no additional questions or comments by the committee.

Annual confirmation of responsibilities outlined in the Metropolitan Audit Committee Bylaws. (Bob Brannon – Committee Chairman)

Mr. Swann said he believed all requirements had been fulfilled with the exception of the annual review of the committee and Office of Internal Audit Bylaws. The annual review is an agenda item later in this meeting.

Motion made and carried to concur with the assessment.

Annual assessment of Metropolitan Auditor's performance (Bob Brannon – Committee Chairman)

The Metropolitan Nashville Council approved budget included a two percent salary increase or \$2,600 for the Metropolitan Auditor position. Also, the Metropolitan Auditor has requested his leave time for vacation be increased one week upon completion of five years of service and that his sick time accrue at twelve days annually to align with other civil service employees in the Office of Internal Audit.

Motion made and carried to approve all requests.

Bylaws annual review (Bob Brannon – Committee Chairman)

No recommendations were made for revisions. New Department of Law representatives have been requested to review and make recommendations if needed.

Motion made to approve bylaws as adopted subject to any recommendations by Department of Law.

Motion carried.

Old Business

Audit of Nashville Electric Services by State Comptroller's County Audit Division (Mark Swann – Metropolitan Auditor)

Mr. Swann had discussed the status of this audit with Jim Arnette, State of Tennessee Comptroller, Director of Local Government Audit. Mr. Arnette stated the project is drawing toward a completion with the draft report being reviewed in the next few weeks.

Follow-up on external auditor presentation FY 2011 Management Letter and Single Audit (Bob Brannon – Committee Chairman)

Mr. Brannon said to hold up discussing this item until next meeting.

Metro Hotline Status and Investigation Reports (Carlos Holt – Internal Audit Manager)

Mr. Holt reported that the Office of Internal Audit is still averaging about two calls a month on the Metro Nashville IntegrityLine, 22 items have been closed. One alert was closed that was sent to the State of Tennessee Comptroller recently.

Mr. Brannon asked Mr. Holt if he thought it was worthwhile to have a hotline. Mr. Holt said that if you have an active 24-hour hotline cuts the risk of fraud. There is a requirement for a hotline on certain funds, such as federal and ARRA funds, so the hotline acts as a safety net and is a value added service.

Internal Audit Project Status (Mark Swann – Metropolitan Auditor)

Nine audit reports of the 16 planned for CY 2012 have been issued, two additional audit reports, General Sessions Court Probation Department Agreed-Upon procedure and State Fair / Nashville Expo Center Computer Acceptable Use should be issued this week.

Other Administrative Matters (Mark Swann – Metropolitan Auditor)

FY 2013 Budget

The FY 2013 Budget is approximately \$1.3 million with \$290,000 spent-to-date. An audit of ITS Telecommunications for an estimated \$60,000 will be started next month.

Staffing

One Senior Auditor position is currently open due to resignation because of her spouse being re-posted to Washington D.C. She has recently accepted employment with the U.S. Department of Treasury Inspector General Office for TARP. The Office of Internal Audit is reviewing the timing to facilitate recruitment efforts to fill this position.

Consideration of Items for Future Meetings (Bob Brannon - Committee Chair)

No items were discussed.

Meeting adjourned after 65 minutes.

The next meeting is scheduled for Tuesday, December 11, 2012.