



**METROPOLITAN GOVERNMENT OF NASHVILLE  
AND DAVIDSON COUNTY**

Management Letter

June 30, 2001



**KPMG LLP**

1900 Nashville City Center  
511 Union Street  
Nashville, TN 37219-1735

October 31, 2001

The Honorable Mayor and Members of Council  
The Metropolitan Government of Nashville and Davidson County  
Nashville, Tennessee

Ladies and Gentlemen:

We have audited the general purpose financial statements and the combining and individual fund and account group financial statements and schedules of The Metropolitan Government of Nashville and Davidson County, Tennessee (the Government) for the period ended June 30, 2001, and have issued our report thereon dated October 31, 2001. In planning and performing our audit of the general purpose financial statements and the combining and individual fund and account group financial statements and schedules of the Government, we considered internal control in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements. An audit does not include examining the effectiveness of internal control and does not provide assurance on internal control. The maintenance of adequate control designed to fulfill control objectives is the responsibility of management. Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, controls found to be functioning at a point in time may later be found deficient because of the performance of those responsible for applying them, and there can be no assurance that controls currently in existence will prove to be adequate in the future as changes take place in the organization. Furthermore, reportable conditions do not include potential future internal control problems; that is, control problems coming to our attention that do not affect the preparation of financial statements for the period under audit.

However, we noted one matter involving internal control and its operation that we consider to be a reportable condition under standards established by the American Institute of Certified Public Accountants. Reportable conditions are matters coming to our attention that, in our judgment, relate to significant deficiencies in the design or operation of internal control and could adversely affect the organization's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. Our consideration of internal control would not necessarily disclose all matters in internal control that might be reportable conditions. The reportable condition noted during our audit, which has been discussed with the appropriate members of management, is summarized in Appendix I.

A material weakness is a reportable condition in which the design or operation of one or more internal control components does not reduce to a relatively low level the risk that errors or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.





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October 31, 2001  
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Our consideration of internal control would not necessarily disclose all matters in internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. However, the reportable condition described above is not believed to be a material weakness.

Although not considered to be reportable conditions, we also noted other certain matters involving internal control and other operational matters that are presented for your consideration in Appendix II.

We also noted matters involving the Government's internal control and its operation used to administer federal financial assistance programs which we will report to management of the Government in a separate report dated October 31, 2001.

These conditions were considered in determining the nature, timing, and extent of the audit tests applied in our audit of the 2001 financial statements, and this report does not affect our report on these financial statements dated October 31, 2001. We have not considered internal control since the date of our report.

This report is intended solely for the information and use of the audit committee, management, and others within the organization and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

**KPMG LLP**

## REPORTABLE CONDITION

### METROPOLITAN BOARD OF EDUCATION IMPROVE FIXED ASSETS RECORDS AND CONTROLS

#### Observation

There is no central accountability for the Metropolitan Board of Education's (MBOE's) fixed asset records, and the existing central fixed asset records are generally deficient. While the Fixed Asset Department adds and deletes purchases and disposals of furniture and equipment, the Construction Office appears to have primary responsibility for accounting tasks related to any land transactions or building construction. The result is that building additions do not go through the proper channels in transitioning from construction in progress to fixed assets and do not appear on the additions report at year-end. While the Construction Office submits invoices and requisitions to the Accounting Department for purchasing approval and payment process, it is the individual in the Construction Office who is the primary source of information regarding these expenditures - the Accounting Department typically only records the information they are given. These construction related expenditures account for millions of dollars annually and should be primarily the responsibility of MBOE's Accounting Department. The result of these issues is that there is no central point of responsibility for all aspects of fixed assets accounting nor is there any uniformity in the treatment of the classes of fixed assets.

As indicated above, the Fixed Asset Department, the Construction Office and the Accounting Department function independently of each other when tracking and recording fixed assets. While the Fixed Asset Ledger, the MICS Tracking System and the General Ledger all contain information regarding the fixed assets maintained by MBOE, these records are not reconciled. Due to the large volume and dollar amount of activity in these accounts, a formal reconciliation process should be developed. Lack of such reconciliation's results in untimely recording of finished projects on the Fixed Asset Ledger and the untimely identification of discrepancies between these systems. Furthermore, with the implementation of GASB 34, which is required for fiscal year 2002, the current situation could result in inaccurate depreciation expense.

Other significant deficiencies noted include:

- Periodic physical inventories of fixed assets have not been performed. Often, the Fixed Asset Department simply deletes assets from inventory without investigation when a school reports that they no longer have an asset in their inventory.
- Assets are not subject to a central tagging process. Each school or department is responsible for engraving their name on the asset and there is no verification as to whether this is done.

#### Recommendation

Sound financial administration in safeguarding the MBOE's investment in fixed assets is of utmost importance in the exercise of stewardship responsibilities. These responsibilities can be effectively discharged only through adequate systems and coordination between affected operating units. Establishing accurate fixed asset records can be a difficult and time-consuming task. Several recommendations in this regard follow:

- Establish a central point of responsibility for all aspects of fixed assets accounting, including financial statement disclosure and risk management.

- Develop a formal reconciliation process between the MICS Tracking System and the Fixed Asset Ledger, which will be performed quarterly. Once reconciled with the MICS Tracking System, the Fixed Asset Ledger should be reconciled to the General Ledger.
- Establish written procedures to control the proper input into the records for all fixed asset additions, sales, abandonment's, and transfers.
- Develop written procedures to ensure that donations from Parent/Teacher Organizations, businesses, fundraisers, and other sources are reported to the Fixed Asset Department for inventory and/or depreciation purposes.
- Clearly define the location of physical assets and accounting control over fixed assets.
- Plan and perform a complete inventory of all fixed assets. In adding assets to the inventory records, obtain the needed information such as asset description, location, vendor or manufacturer, acquisition date, and cost. Any missing fixed assets identification tags should be affixed at the time the physical inventory is taken.
- Once the complete inventory of fixed assets has been performed, follow-up with periodic inventories of fixed assets by location, with appropriate investigation of discrepancies.
- Implement a central tagging process whereby all assets are identified by number.
- Assign values to each asset according to generally accepted accounting principles. Fixed Assets should be recorded at historical cost. If the original cost is not available, use estimated historical cost, or, in the case of gifts or contributions, use the fair market value at the date received.

By maintaining accurate fixed asset records, the MBOE will realize several benefits:

- Responsibility for custody and effective use of fixed assets will be clearly established;
- Fixed assets can be inventoried periodically to ensure that they are properly controlled;
- Information regarding sources of supply, prices, and useful lives will be readily available; and
- Records will be readily available to substantiate the amount of grants used to finance expenditures for fixed assets, and, furthermore, the determination of costs for building or equipment use would be facilitated.

### **Management Response**

We concur. A process is underway to reorganize the management of fixed assets. Revised job descriptions are pending approval for two fixed asset positions to conduct tagging as noted above. Procedures have been written concerning management of fixed assets and are pending approval. An additional accounting position has been budgeted and the hiring process commenced to enable the accounting staff to reconcile fixed asset matters. A central tagging process does exist. We are aware of deficiencies in timely accomplishing the tagging, but feel the reorganization will improve this deficiency. We are likewise hopeful that when additional staff are in place, a process which is being done now, those resources will be brought to bear on the reconciliation among fixed assets, accounting, and construction.

## OTHER RECOMMENDATIONS

### EMPLOYEE BENEFIT BOARD RECONCILIATIONS

#### **Observation**

Prior to June 30, 2001, the Government had not implemented a formal reconciliation process between deductions for medical insurance withheld from employees to amounts submitted to insurance carriers. As of September 2001, the reconciliation of the deductions for medical insurance withheld from employees to amounts submitted to insurance carriers was completed for the year ended June 30, 2001. The large volume of activity and the high dollar amount of withholdings should require formal reconciliation processes for this function throughout the year. Lack of such reconciliation processes creates the opportunity for overpayments to vendors.

#### **Recommendation**

A formal reconciliation process between amounts paid to insurance carriers and amounts collected from employees should be performed on a timely basis (i.e., on a monthly or quarterly basis) with the appropriate review to ensure the accuracy and completeness of amounts paid and collected.

#### **Management Response**

We concur. Internal Audit has just entered into a contract to have the insurance rolls fully reconciled and to develop ongoing reconciliation procedures for the Department of Finance to implement once the initial reconciliation is completed. We expect this work to be done and the procedures to be in place and operational by June 30, 2002.

**GENERAL GOVERNMENT  
FIXED ASSET INVENTORY**

**Observation**

During fiscal 2000, in connection with the implementation of the fixed asset module of FASTnet, each department of the Government completed a review of all fixed assets for the purposes of ensuring accuracy of information input to FASTnet. Further, at the end of fiscal 2000, the responsibility for maintenance of the fixed asset records transferred to the Division of Accounts. During fiscal 2001, the Division of Accounts has drafted formal policies on the continuing review of capitalized/fixed assets. However, to date, the detailed procedures to implement the policies adopted have not been developed.

**Recommendation**

We recommend that the Division of Accounts formalize its procedures for implementing the recently adopted policies surrounding the record keeping and periodic physical inspection of fixed assets.

**Management Response**

We concur. Division of Accounts will have the procedures implemented by June 30, 2002.

**GENERAL GOVERNMENT  
INFORMATION TECHNOLOGY  
DISASTER RECOVERY AND BUSINESS CONTINUITY**

**Observation**

Although written procedures exist for recovering the operating system in the event of catastrophic system failure, there is no disaster recovery plan that addresses the possibility where the data center is rendered unusable. Furthermore, no testing has been performed, nor are contracts in place, for an external alternative processing site, and no written procedures have been developed to define a policy for back-up tape rotation, tape retention periods, and testing of back-up tapes, including those with annual financial information. The lack of disaster recovery and business continuity plans was also noted for the Metropolitan Board of Education and the Department of Water and Sewerage Services.

**Recommendation**

We recommend the following steps toward having effective disaster recovery and business continuity planning:

- Complete a business continuity and disaster recovery plan for all Departments which includes a business impact assessment which defines recovery time objectives and priorities for each system based upon operational requirements.
- The Department Water and Sewerage should communicate with the Metro IT department and study the benefits of moving their systems (AS/400) to Metro Central Information System facilities. Such a strategy can increase synergy by having multiple experienced employees familiar with each system and could contribute toward efforts to establish disaster recovery practices for the overall Metropolitan Government.
- Plan for periodic testing and modifications of the disaster recovery plan.
- Develop operational procedures for critical processes that can be used to capture and process data.

**Management Response**

We concur. The Finance and Information Systems Departments are currently in the process of developing a request for proposals (RFP) for information technology services that will address the observations and recommendations above. We expect the RFP to be issued in early January of 2002 and plan to have a contractor in place by March.

**GENERAL GOVERNMENT  
INFORMATION TECHNOLOGY  
SECURITY**

**Observation**

*FASTnet*

FASTnet security measures include requirements for password structure and tenure, and automatic disabling after a certain number of attempted log-on's. Currently, the system is set to automatically log off after 60 minutes of inactivity.

*Justice Information System (JIS)*

There is no formal procedure to ensure that terminated employees are communicated to JIS Security Administrators. This increases the risk that terminated user IDs may still be active in the system.

*Department of Water and Sewerage Services*

At the Department of Water and Sewerage Services we noted the there are no appropriate fire extinguishing systems installed in the computer room.

*MBOE*

Access to the computer room is not restricted to authorized personnel only.

**Recommendation**

*FASTnet*

To improve the security environment, we recommend considering automatic logoff from the FASTnet system after 30 minutes of inactivity by a user.

*JIS*

JIS should establish communication with the human resources department to ensure that terminated user IDs are disabled in a timely manner.

*Department of Water and Sewerage Services*

Appropriate fire extinguishing apparatus should be installed at the Department of Water and Sewerage Services' computer room.

*MBOE*

Restrict access to the MBOE computer room to authorized personnel only

**Management Response**

We concur. Each recommendation will be implemented by June 30, 2002.

**GENERAL GOVERNMENT  
INFORMATION SYSTEMS  
INTERFACES**

**Observation**

Revenues from several major revenue sources are manually posted to FASTnet , which makes the process prone to human error. For example, there is no automated interface between the Customer Information System at the Department of Water and Sewerage Services or the customer billing systems at Metro General/Bordeaux Hospitals and FASTnet that would enable automatic posting to the General Ledger.

**Recommendation**

A secure and tested interface should be established between all major revenue subsidiary systems and FASTnet so that postings to the G/L can be handled without human intervention.

**Management Response**

We concur. Finance will investigate and implement these interfaces by June 30, 2003.

**GENERAL GOVERNMENT  
PROPERTY TAX SYSTEM**

**Observation**

Three types of taxes exist: Real Property, Personal Property, and Public Utility. These revenues, which represent the Government's largest revenue stream, are maintained on a separate mainframe in an outdated software package. This is one of the last systems to be processed on the mainframe. As such, the expenses related to maintaining the mainframe for fewer and fewer purposes become relatively more expensive per application. Further, no interface exists between the Tax Accounting System and FASTnet. Rather, FASTnet is updated manually from reports generated by the Tax Accounting System.

**Recommendation**

In order to enhance the efficiency of the tax accounting process, reduce overall expenses (related to maintaining the mainframe), and to reduce the risk of errors, we recommend that the Government investigate the purchase of a complete tax compilation system which would interface with both the general ledger system and the other necessary systems (Land Information System, etc.) This will provide for more timely updates of financial reporting and reduce the risk of human error in the process. Once all applications have been transferred from the mainframe environment, the Government will achieve cost savings from discontinuance of the mainframe operations.

**Management Response**

We concur. Information Systems is performing a needs assessment for all applications on the mainframe and will then proceed to search for non-mainframe comprehensive integrated solutions. This will include the areas of land information, property tax assessment and billing and general ledger.

**GENERAL GOVERNMENT  
CONSTRUCTION WORK IN PROCESS FASTnet MODULE**

**Observation**

The Government currently maintains a mainframe system for processing of construction work in progress for the Department of Water and Sewerage Services. This is one of the last applications resident on the mainframe, and as such, the cost per application of maintaining the mainframe is increasingly expensive.

**Recommendation**

We recommend that the Government implement the Job Cost module of FASTnet, which will allow the Department of Water and Sewerage Services to convert their work-in-progress construction activity to FASTnet. Once all applications have been transferred from the mainframe environment, the Government will achieve cost savings from discontinuance of the mainframe operations.

**Management Response**

We concur. The Job Cost module will be implemented December 31, 2002.

**GENERAL GOVERNMENT  
GENERAL LEDGER ACCOUNTING SYSTEM**

**Observation**

Currently most operating units of the Government utilize the Primary Government's general ledger accounting system (FASTnet). However, MBOE and General Hospital do not use FASTnet as their Primary Accounting System. We recognize that 1) MBOE is currently investigating various general ledger system options and 2) General Hospital uses several modules of FASTnet. However, the duplication of effort and the inefficiencies resulting from having to "reconcile" two sets of general ledgers suggests that the full utilization of FASTnet by both entities may be appropriate.

**Recommendation**

We recommend that MBOE complete the needs assessment in progress related to its general ledger. Upon completion of this assessment, we suggest that MBOE move forward to implement its new system at the earliest possible date. If the decision is made to select FASTnet, MBOE can benefit from the implementation experience of other significant portions of the Government.

We recommend that General Hospital convert to the FASTnet, except for the use of its current accounts receivable/billing system. This will allow management to discontinue reconciling "two sets of general ledgers".

**Management Response**

MBOE concurs. This initiative is in progress. Subcommittees have developed needs assessments in areas including, payroll, accounting, human resources, fixed assets, and meeting have been held with Metro representatives to determine the ability of FASTnet to meet MBOE needs. This process is scheduled for completion in December 2001.

MNGH Concur. MNGH places a premium value on monthly detailed departmental financial statements including current month and YTD comparison to both budget and prior year. We will continue to assess FASTnet's ability to meet the Hospital Authority's reporting needs both currently and in the future. Until that occurs, management believes the value added to the organization of having detailed departmental financial statements far exceeds the cost of reconciling two general ledgers.

**GENERAL GOVERNMENT  
RISK MANAGEMENT**

**Observation**

During fiscal 2001, Metro made significant improvements in the area of risk management through implementation of a new claims system which tracks available historical information for claims as well as litigation support purposes. We are aware Metro has issued a request for proposal for consulting services related to comprehensive risk management and that the deliverable for these services will include a written risk management plan.

**Recommendation**

We support the efforts of the Government to develop a formal risk management function. We recommend that the plan inventory all the traditional risk management duties such as loss control and safety, hazard identification mitigation, work rules, exposure identification, risk transfer, cost and funding analysis, claims handling and reporting, regulatory, and management reporting. To ensure its effectiveness, we suggest the execution of the plan should be the responsibility of a dedicated risk manager reporting to a high level within the Government. Appropriate budgetary authority should exist to gain compliance.

In order to more effectively manage known risks, the Government should consider issuing a Government-wide formal policy which requires reporting of liability claims to ICD within a specified timeframe. The Government currently has an informal policy that all unasserted liability claims be reported to the Insurance and Claims Division (ICD) immediately. However, in practice this generally does not occur on a timely basis. Rather, the Departments typically turn in unasserted claims only when the information is specifically sought by ICD or legal. As a result, ICD may not know about the incident until the claim is filed, reducing the Government's ability to effectively manage the potential loss.

**Management Response**

Management concurs with the recommendations for the scope of the risk management analysis.

Management concurs with the recommendation that the reporting of known potential claims be required by a Government wide policy within a short period. This would allow disciplinary actions in many cases for failure to comply with the policy and help assure that risks are corrected or minimized promptly.

**GENERAL GOVERNMENT  
PAYROLL DEDUCTION INPUT**

**Observation**

Payroll receives a variety of forms for all new employees who are selecting medical, dental, and other benefits. They also receive information for non-voluntary deductions. Currently, there are several individuals who enter these voluntary and non-voluntary options into FASTnet for payroll deductions. However, there does not appear to be a review of the entered information to ensure that the options were entered correctly. The mitigating control is that the employee should complain if the wrong options were entered. However, this reliance on a detective control may cause a customer service issue.

**Recommendation**

We recommend that voluntary and non-voluntary deductions input into FASTnet be reviewed by a supervisor or third party at least on a test basis.

**Management Response**

We concur. This recommendation will implemented by June 30, 2002.

**GENERAL GOVERNMENT  
NEW ACCOUNTING PRONOUNCEMENT**

**Observation**

The Governmental Accounting Standards Board (“GASB”) has issued Statement No. 34 *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments*, which will be effective for the fiscal year ending June 30, 2002. This Statement establishes financial reporting standards for state and local governments. It establishes that the basic financial statements and required supplementary information (RSI) for general purpose governments should consist of:

- 1) *Management’s discussion and analysis (MD&A)* - MD&A should introduce the basic financial statements and provide an analytical overview of the government’s financial activities. Although it is required supplemental information (RSI), governments are required to present MD&A before the basic financial statements.
- 2) *Basic financial statements* - The basic financial statements should include:
  - i) Government-wide financial statements, consisting of a statement of net assets and a statement of activities. Prepared using the economic resources measurement focus and the accrual basis of accounting, these statements should report all of the assets, liabilities, revenues, expenses, and gains and losses of the government. Each statement should distinguish between the governmental and business-type activities of the primary government and between the total primary government and its discretely presented component units by reporting each in separate columns. Fiduciary activities, whose resources are not available to finance the government’s programs, should be excluded from the government-wide statements.
  - ii) Fund financial statements consist of a series of statements that focus on information about the government’s major governmental and enterprise funds, including its blended component units. Fund financial statements also should report information about a government’s fiduciary funds and component units that are fiduciary in nature. Governmental fund financial statements (including financial data for the general fund and special revenue, capital projects, debt service, and permanent funds) should be prepared using the current financial resources measurement focus and the modified accrual basis of accounting. Proprietary fund financial statements (including financial data for enterprise and internal service funds) and fiduciary fund financial statements (including financial data for fiduciary funds and similar component units) should be prepared using the economic resources measurement focus and the accrual basis of accounting.
  - iii) Notes to the financial statements consist of notes that provide information that is essential to a user’s understanding of the basic financial statements.
- 3) *Required supplementary information - (RSI)*. In addition to MD&A, this Statement requires budgetary comparison schedules to be presented as RSI along with other types of data as required by previous GASB pronouncements. This Statement also requires RSI for governments that use the modified approach for reporting infrastructure assets.

The Government has been proactive in ensuring readiness to implement this new statement and has made significant progress toward effective compliance.

**Recommendation**

We recommend the Government continue to be proactive in ensuring compliance with this new statement through its current process and consider communicating with all other applicable departments and component units in an effort to ensure their compliance.

**Management's Response**

The Government will implement GASB Statement No. 34 for June 30, 2002. The appropriate communications with departments and component units will be completed by June 30, 2002.

**GENERAL GOVERNMENT  
HEALTH INSURANCE PORTABILITY AND ACCOUNTABILITY ACT OF 1996**

**Observation**

The Health Insurance Portability and Accountability Act of 1996 (HIPAA) has established stringent standards for the privacy and security of individually identifiable health information and requires the use of specific transactions and code sets for all providers that choose to submit business information electronically. The final HIPAA Transactions and Code Sets Rule was published in the August 17, 2000 Federal Register. The first required compliance date is in October 2002, with additional requirements regarding security, privacy and identifiers phasing in through 2004. Noncompliance with these regulations could result in monetary and/or criminal penalties being assessed against the Government and/or their employees. Privacy breaches could also serve as the basis for civil litigation against the Government should the confidentiality of an individual's health information be compromised.

We noted the Government is at different levels of understanding of the requirements, planning for compliance with the requirements, and implementing the plan for compliance across various departments. Further, different departments may create duplication of efforts because of the lack of coordination.

**Recommendation**

The Government should consider assigning one individual responsible for ensuring compliance with HIPAA. This individual should create a task force to compel a risk assessment, derive a plan for compliance, and implement and monitor the completion of this plan. We believe that these steps are both prudent and cost effective over the long term and that the implementation of the electronic data interchange (EDI) aspects of HIPAA present an opportunity to reduce operating costs and accounts receivable in the future.

**Management Response**

We concur. The Department of Finance, Office of Support Services is responsible for the HIPAA compliance function. At this time an RFP is being drafted to seek a qualified entity to: perform an assessment of Metro's readiness for HIPAA, identify priority areas to be addressed immediately, develop a compliance model, create an implementation timeline, and provide consultation around implementation. A system for monitoring HIPAA standards will be developed.

**METROPOLITAN BOARD OF EDUCATION  
RETIREMENT FUND TRUSTEE RECONCILIATIONS**

**Observation**

MBOE maintains a significant volume and dollar amount of investments for three retirement funds. While investment activity for funds invested in the Metropolitan Investment Pool (MIP) were recorded throughout the year, activity for funds held by the third party trustee were not recorded until adjustments were proposed as a result of the annual audit. The large volume of activity and high dollar amount of investments indicate a need for a formal monthly reconciliation process. Lack of such reconciliation's leaves such assets at risk and potentially creates the opportunity for untimely identification of errors.

Under current practices, there is no assigned oversight of the accounting information maintained in the Pension Department by a responsible official within the accounting office or The Government's Office of Treasury. This results in a lack of coordination of information between the two offices during the year.

**Recommendation**

A coordinated effort between the Accounting Department, the Pension Department and the Office of Treasury should be established. A formal monthly reconciliation and review process should be implemented to ensure that amounts reported by investment custodians are accurate and the underlying activity is recorded on the general ledger of MBOE.

**Management Response**

We concur. The Accounting Department, the Pension Department and the Office of Treasury will develop and implement a process to review and reconcile the Master Custodian monthly reports.

**METROPOLITAN BOARD OF EDUCATION  
INFORMATION SYSTEMS  
PAYROLL PROCESSING**

**Observation**

During the year ended June 30, 2001, MBOE took several steps to address the information technology (IT) deficiencies that currently exist. These steps include the establishment of a Board appointed Technology Committee and a Chief Technology Officer position which was filled in November 2001. In addition to these new internal resources, MBOE retained an outside consultant to develop a strategic plan and roadmap for IT expenditures which are estimated to be \$15 million over the next 3 to 5 years.

MBOE's payroll system has been in existence for more than 20 years and processes checks for approximately 9,800 employees bi-weekly. The payroll application is a highly customized system which requires a specialized skill set to maintain. Currently, the payroll department has only one individual who is completely familiar with the payroll system and process.

Group ID's are issued to all staff with access to the payroll system, which results in minimal accountability for changes made to the system and the payroll application. Additionally, Operator ID's are only 3 digits, require no password, and are not required to change periodically. Thus, it is possible that someone can execute a transaction using someone else's ID with little monitoring of the user activity in the payroll system.

The payroll system also does not prevent any users from looking at specific employee information, only from unauthorized changes. The information technology (IT) department has initiated some discussion with Human Resources regarding efforts to prevent users from viewing employee data unless authorized.

**Recommendation**

To improve the control environment surrounding the operation of the payroll system, we strongly recommend consideration of replacement of the current payroll system with the system used centrally to process payroll for all other departments of the Government, FASTnet. In the event FASTnet is not selected and implemented in the near future, MBOE should develop a secondary resource that is fully capable of processing payroll in order to ensure functionality of the system in the case of employee absence. One advantage of using FASTnet would be having knowledgeable back-up personnel within the Government in the event of primary payroll system personnel being unavailable. Using FASTnet would also provide the opportunity for MBOE to automate its time entry processes, thus significantly increasing the efficiency of the payroll process and reducing the risk of human errors. Even if FASTnet is not adopted by MBOE, methods for automation of the time entry process should be investigated.

To improve the access controls over the payroll processing system, IT should produce and review audit trails and reports that show all activity on the system. Logical security controls should be enhanced by use of individual ID's, with stronger authentication controls, and user access levels should be periodically reviewed and old accounts eliminated. We also recommend that the IT department continue its efforts with Human Resources to limit access to employee information to authorized personnel.

**Management Response**

We concur. This will be accomplished in concert with the initiatives examining FASTnet as our software system noted above. IT will be asked to determine interim solutions as proposed above to improve security pending changes in the software system.

**METROPOLITAN BOARD OF EDUCATION  
CODE OF ETHICS AND CONFLICT OF INTEREST POLICY**

**Observation**

MBOE has made progress toward the establishment of a formal code of ethics and conflict of interest policy. Currently, the proposed code and policy have been developed and are awaiting final approval prior to implementation.

**Recommendation**

We recommend that MBOE move forward to complete the approval process as soon as possible so that implementation of the Code of Ethics and Conflict of Interest Policy can proceed. Obtaining statements from employees who agree to engage in ethical practices will enhance the communication to employees regarding management's philosophy of integrity and ethical conduct. In addition, signed code of ethics/conduct statements would assist in possible litigation of employees who commit fraudulent activities.

**Management Response**

We concur. We will complete this process and implement by July 1, 2002.

**DEPARTMENT OF WATER AND SEWERAGE SERVICES  
REVENUE OPPORTUNITIES**

**Observation**

The Department's policy in the past has been to have a minimum of 100% excess capacity to ensure that the customers would continue to receive water and sewerage services in case of an emergency. As a result, the Department has operated under an approach where there is no assumption of the risk of not being able to provide these services. This practice is not consistent with other water and sewerage providers. This policy also incurs significant costs to maintain the unused "reserve" capacity, a cost which could be utilized for other priorities of the Department in an environment where significant pressure exists to keep customer rates stable.

**Recommendation**

The Department should review its current minimum excess capacity policy and consider taking on an acceptable level of risk of not being able to provide these services. Reducing the minimum excess capacity levels and taking on a certain level of risk will provide additional opportunities for volume selling. This in turn allows the cost of maintaining the current capacity to be allocated over a greater number of customers and postpones future rate increases to the current customers.

**Management Response**

We concur. The Department will monitor its capacity availability and will seek additional opportunities to increase revenue. It will actively seek opportunities to sell services to other entities or to expanded customers bases in the current service area, where it is beneficial to the current customers to do so.

**GENERAL HOSPITAL  
INTERIM ESTIMATION OF THIRD-PARTY SETTLEMENTS**

**Observation**

Metropolitan Nashville General Hospital (General Hospital) has not routinely prepared interim analyses of expected third-party cost report settlements. In addition, the Hospital does not routinely prepare and reconcile third-party payor log information to Provider Statistical and Reimbursement Reports (PS&R). Maintenance of accurate and complete logs for Medicare is important in determining the current year estimated settlement.

**Recommendation**

The Hospital should develop and implement procedures to estimate current year retroactive settlements at least once each quarter. Templates can be developed and utilized to provide reasonable estimates. Also, to improve the documentation and estimation process, we recommend that third-party logs be reconciled to the PS&Rs on a regular basis. Implementation will ensure that interim financial information used by management to make operating and financial decisions is more accurate and can help identify potential Medicare interim overpayments and underpayments at a time when management may be able to take corrective action by requesting payment changes from Medicare.

**Management Response**

Management agrees that the ability to estimate current year settlement could only have a positive effect on operations and decision-making. The Medicare payer logs are 90% functional and we expect to start reconciling the logs to Medicare PS&R by March 31, 2002 pending the vendor fixing their problem which has led to the PS&R not being available since early 2001.

**GENERAL HOSPITAL  
THIRD PARTY ACCOUNTING AND BILLING PROCEDURES**

**Observation**

In 2000, General Hospital's average time for bills to drop significantly improved to approximately 15 days. The Hospital's average time for bills to drop during fiscal 2001 remained fairly consistent. However, we noted that the billing department does not have an automated contract management system to load fee schedules and approved amounts for each payor. Currently, when a payment is posted, the Hospital does not have automated controls in place to identify underpayments. Furthermore, the Hospital is in the process of obtaining a provider number for Medicare Part A due to a change in ownership as a result of the creation of the Hospital Authority. Additionally, the Hospital is filing for a Medicare Part B professional provider number as professional charges have not historically been billed.

**Recommendation**

We recommend that the Hospital continue to train physicians and department personnel to decrease billing time to the industry standard of 5-7 days. Such improvements will enhance collections and cash flow and result in fewer rebills and denials. We also suggest that the Hospital install a contract management system to assist patient accounting in the collections process. A contract management system would allow underpayments to be identified quickly and increase the efficiency of the patient accounting department by eliminating the monthly manual review of each payor's payments. Furthermore, we suggest that the Hospital continue the process to obtain the requested provider numbers and coordinate these efforts closely under advisement of attorneys. Finally, the Hospital should carefully consider any financial impact resulting from obtaining these provider numbers to ensure that the impact is recorded in an appropriate time period.

**Management Response**

We concur. While we have made significant reductions in the bill drop timeframe, we can and will continue to improve. We anticipate getting below 10 days; however, the 5-7 day industry average will be a difficult target to achieve. With funding reduced, the contract management system had to be pushed back to FY 2003. At that time a contract management system will be selected. Finally, we are pressing ahead in obtaining all required provider number and, as recommended, have obtained the input of legal council as appropriate.