METROPOLITAN GOVERNMENT OF NASHVILLE AND DAVIDSON COUNTY

Management Letter

June 30, 2003

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

October 31, 2003

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

Ladies and Gentlemen:

We have audited the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Metropolitan Government of Nashville and Davidson County, Tennessee (the Government) as of and for the year ended June 30, 2003, which collectively comprise the Government's basic financial statements and have issued our report thereon dated October 31, 2003. We also have audited the Sports Authority, General Hospital, and Bordeaux Hospital, discretely presented component units of the Government, as of and for the year ended June 30, 2003 as displayed in the Government's basic financial statements. We also have audited the financial statements of each of the Government's nonmajor governmental, nonmajor enterprise, internal service, and fiduciary funds presented as supplementary information in the accompanying combining financial statements as of and for the year ended June 30, 2003.

In planning and performing our audit of the aforementioned financial statements, 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 a certain 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.

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, 2003.

These conditions were considered in determining the nature, timing, and extent of the audit tests applied in our audit of the 2003 financial statements, and this report does not affect our report on these financial statements dated October 31, 2003. 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

Appendix I

REPORTABLE CONDITION

METROPOLITAN NASHVILLE PUBLIC SCHOOLS
CASH MANAGEMENT ACTIVITIES

Observation

Significant deficiencies were noted in Metropolitan Nashville Public Schools (MNPS) cash management procedures. MNPS does not have adequate cash reconciliation procedures in place to effectively monitor cash activities and balances. The following deficiencies were noted:

- Cash reconciliations are not prepared in a timely manner. There is approximately a three-month lag between receipt of bank statements and preparation of reconciliations.

- Reconciliations are not organized in a manner conducive to cash management. Cash transactions and balances are not recorded directly to the general ledger. Therefore, cash balances cannot be reconciled to general ledger balances. The reconciliations performed are not organized in a way that would prevent or identify errors or reconciling items.

- Cash reconciliations consist of an excessive number of outstanding and reconciling items. KPMG noted outstanding items up to five years old. There are no procedures in place to investigate and resolve outstanding checks. As a result, if a check clears the bank for an amount different than that recorded on the check register, the original check will remain on the outstanding check list indefinitely. It is likely that many checks listed as reconciling items have actually been voided, canceled, or paid.

- Certain reconciling items represented checks that were paid twice by MNPS. The lack of formal review and approval procedures prior to re-issuance of a check allow a second check to be issued and clear before a stop payment order is processed.

- Unauthorized charges were incurred for an America Online internet account as the result of poor cash controls. An undisclosed party provided MNPS' bank account number to pay for an internet account, and these charges were paid approximately three times due to poor cash management controls. Timely reconciliations would have detected this misappropriation immediately and allowed management to prevent additional unauthorized payments.

- Reconciliations are prepared by the MNPS Internal Auditor, and are not subject to review by management. Segregation of duties and management review of reconciliations increase the control over cash activities and increase the likelihood that errors or misstatements are detected.

Recommendation

Formal reconciliation procedures should be documented and implemented in order to maximize the usefulness of cash reconciliations. The responsible party should prepare concise reconciliations and resolve reconciling items in a timely manner, including ensuring posting of adjusting entries to the general ledger where necessary. Reconciling items should be reviewed on a regular basis and be reinstated to cash or remitted to the state as required by law for unclaimed property. Cash reconciliations should be reviewed and approved by a qualified individual independent of cash management and reconciliation.

Management Response

We concur. MNPS has implemented a team to assist with bringing the monthly reconciliation current, addressing the issues of old outstanding items by June 30, 2004 and setting up procedures to maintain an adequate level of internal control effective immediately.

OTHER RECOMMENDATIONS

METROPOLITAN NASHVILLE PUBLIC SCHOOLS
COORDINATION OF ACCOUNTING AND CONTROL ACTIVITIES

Observation

The management and control structure of MNPS is highly decentralized between various operating units, such as accounting, payroll, benefits, pension, information services, employee relations, construction, warehouse, etc. Each area has responsibility for maintaining its own supporting information, and for forwarding information to the accounting department, which is responsible for recording transactions. To effectively manage, record and report the activities of this large organization, close coordination between the operational units is required. However, the culture and resource constraints of the organization currently inhibit timely and successful coordination between operating units. In addition, following implementation of FASTNET in February 2003, the need for strong coordination between operating units has increased. However, MNPS relies upon Metro Government personnel to perform various MNPS accounting functions. MNPS has not utilized FASTnet to the extent necessary to effectively record or process general ledger activity. As discussed in earlier observations, KPMG noted several instances where lack of effective coordination between units resulted in internal control weaknesses.

Recommendation

In an effort to address the need for a higher level of ownership and accountability for coordinating internal control and oversight processes KPMG recommends identification of resources within MNPS to correct many of the internal control weaknesses noted and instill a greater sense of ownership and accountability within MNPS.

Management Response

We concur. Under the direction of the Director of Business Services, MNPS' Accounting department staff is currently working with Metro Government personnel to bring a higher level of ownership and accountability for internal control and oversight into the MNPS' accounting department for the Fiscal Year 2004 audit.

METROPOLITAN NASHVILLE PUBLIC SCHOOLS
BUDGET MONITORING

Observation

There has been no documented review of actual performance in comparison to the approved budget during fiscal year 2003. Operational budgets must be prepared and approved prior to each fiscal year, and budget monitoring is essential to achieve fiscal accountability.

Recommendation

The MNPS Accounting Department should prepare monthly budget-to-actual comparisons in order to measure progress. FASTnet provides various reports that can be used to facilitate this process. Budget monitoring and review by management are effective controls to detect errors or misstatements in actual financial statements. A formal review should be performed on a regular basis, and significant variances should be investigated. The reasons for such variances should be documented and reviewed by management in a timely manner.

Management Response

We concur. Effective November 2003, Budget to Actual reports for the General Purpose Fund are prepared monthly for the Assistant Superintendent of Business Services. The Assistant Superintendent reviews these reports and provides copies to the MNPS Board of Education and Cabinet members.

METROPOLITAN NASHVILLE PUBLIC SCHOOLS
IMPROVE FIXED ASSETS RECORDS AND CONTROLS

Observation

During fiscal year 2003, MNPS implemented the fixed asset module of FASTnet, which required significant effort to ensure accurate carryover of balances from the prior system, and to ensure accurate information flow from various input sources. While these reconciliation processes were completed by a combination of MNPS and Metro personnel, the timeliness of reconciliation processes should be improved. In addition, there still exist certain weaknesses in the system of accountability for fixed assets, primarily in the area of physical identification and tracking of assets

Ongoing deficiencies noted include:

- Periodic physical inventories of fixed assets have not been performed. Capital assets are simply deleted from inventory without investigation when a school reports that it no longer has an asset in its inventory.

- Assets are not subject to a consistent central tagging process. Major purchases are tagged centrally; however, items purchased directly by schools (primarily from school activity funds) are not tracked or capitalized. Individual schools may engrave their name on the asset, but there is no system wide policy regarding this type of activity.

Recommendation

KPMG recommends that management continue to improve the coordination between affected operating units, particularly with regard to performing a physical inventory and to ensure that complete reconciliations are prepared on a timely basis. We encourage continued oversight by Metro Nashville personnel in order to ensure consistency in classification and presentation of information in the FASTnet fixed assets module. In addition, we suggest strengthening the authority of the central point of responsibility for all aspects of capital assets accounting, including financial statement disclosure and risk management.

Management Response

We concur. MNPS is adding a position to assist with performing a physical inventory and ensure that complete reconciliations are prepared on a timely basis.

METROPOLITAN NASHVILLE PUBLIC SCHOOLS
IMPROVE ORGANIZATION AND FILING OF PAYROLL DEDUCTION AUTHORIZATIONS

Observation

MNPS' payroll department is responsible for maintaining original supporting documentation of employees' payroll deductions for garnishments such as child support payment and Chapter 13 bankruptcy payments, as well as employee optional deductions for 12 month option pay, union dues, charitable contributions, credit union deductions, etc. There is currently no central location or documented procedures for filing such documentation, and as a result, it is not well organized to facilitate verification of information. In addition, personnel records are de-centralized, with several separate files for each employee. Separate files are maintained for payroll related documents, benefit documents, and personnel documents. Personnel records are maintained in several different locations within the human resources department, and there is a lack of consistency between files. As a result, audit requests are delayed and sometimes not completed because of the inability of MNPS staff to locate the appropriate documentation. KPMG noted two payroll deduction forms that could not be located, and one personnel file with incomplete salary authorization documentation.

Recommendation

Sound establishment of an organized and safeguarded document filing system is critical to maintaining sufficient supporting documentation for employee deductions. To improve this function, KPMG recommends establishment of a central location for filing supporting documentation for employee payroll deductions. The files should be organized by type of deduction or by employee ID. In addition, supporting documentation should be filed immediately after entry into the computer system, keeping most recent documents on top. In addition, personnel files should be kept current and include authorized documentation of the most recent salary and position information.

Management Response

We concur. The Payroll Manager will take the responsibility of organizing the record keeping for the payroll section of MNPS. The Assistant Superintendent for Human Resources will be responsible for oversight to ensure that Human Resources employees work with the payroll section regarding documentation filing and retention as part of the EBS implementation.

METROPOLITAN NASHVILLE PUBLIC SCHOOLS
RECONCILIATION OF ACTUARIAL VALUATION

Observation

Under existing procedures, MNPS does not reconcile its payroll census data to the actuarial valuation report provided by the consulting actuary to ensure the accuracy of the data, which is used as the basis for computing the pension obligation and related information. This limits MNPS' ability to prevent, detect and correct potential errors in the calculation of the pension obligation. The Benefits Office was unable to provide a copy of or re-create the payroll census data that is provided to the consulting actuary.

Recommendation

The Benefits Office should coordinate with the payroll and human resources offices to develop a procedure to ensure the accuracy of the census data provided to the consulting actuary. Such a control would better ensure accuracy in the calculation of the pension obligation.

Management Response

We concur. The Benefits Office will coordinate with payroll, Information Technology, and human resources offices to develop a procedure to ensure the accuracy of the census data provided to the consulting actuary for the next evaluation.

METROPOLITAN NASHVILLE PUBLIC SCHOOLS
AUTHORIZATION OF PROCUREMENT CARDS

Observation

MNPS has formal procedures in place surrounding issuance of procurement cards to individuals, including proper counseling and authorization by the Department Heads and the Purchasing Agent. KPMG noted several instances where these procedures were not followed, resulting in procurement cards being issued with no documentation of proper authorization.

Recommendation

KPMG recommends that there be controls in place that do not allow procurement cards to be issued without both required levels of authorization. The Purchasing Agent should be the only party allowed to issue procurement cards, and should be responsible for ensuring that all required criteria have been met. We do acknowledge that there are certain mitigating controls that reduce the risk of loss associated with procurement cards, including embedded credit limits and review of purchases by Department Heads. However, KPMG suggests that preventative controls be implemented, in order to reduce the risk of loss in the event that a detective control fails.

Management Response

We concur. MNPS issued new procurement cards in fiscal year 2004. With the issuance of new cards, MNPS reviewed documentation to make sure it was current and accurate. A training session was given to all control clerks, and emphasis was made on proper procedure for the procurement card. A new operating procedure will be issued within the next two months and distributed to all managers and cardholders.

METROPOLITAN NASHVILLE PUBLIC SCHOOLS
RECONCILIATION OF THE SCHOOL PROFESSIONAL EMPLOYEE INSURANCE FUND

Observation

Reconciliations for the School Professional Employee Insurance Fund are not prepared in a timely manner. KPMG noted an average lag of three months between month-end and preparation of reconciliations. Furthermore, there is no evidence of review of the reconciliations by anyone other than the preparer. The records and reconciliations are maintained on a cash basis, using actual claims paid, requiring adjustment by the auditors to the accrual basis used for financial reporting.

Recommendation

KPMG recommends that an individual with sufficient knowledge and training prepare a reconciliation of insurance statements to the general ledger. MNPS should be responsible for making any adjustments necessary to report balances and activity in the School Professional Employee Insurance Fund on the accrual basis.

Management Response

We concur. MNPS will assign the function of reconciliation of the insurance statements to the general ledger to an employee with the skills and knowledge to complete the task in a timely manner. MNPS' Accounting Department will work with the Benefits Office to see that necessary adjustments are made to report balances and activities on an accrual basis by June 30, 2004.

GENERAL GOVERNMENT INFORMATION SYSTEMS
DOCUMENTATION OF SYSTEM CHANGE

Observation

KPMG Information Risk Management noted that for a sample of changes implemented for the Tax Accounting system, three out of ten move forms did not contain documented approvals from the Development group manager.

Recommendation

We recommend management enforce current procedures so that changes are only implemented in the production environment if documented approval of the change has been obtained from the Development group manager. We also recommend that details of the change (i.e. change request, testing, etc) be retained for application changes to the system. This will help ensure that the integrity of the system is maintained and that changes implemented are properly authorized.

Management Response

We concur. We will ensure that this policy is complied with going forward.

GENERAL GOVERNMENT INFORMATION SYSTEMS
MONITORING OF SECURITY VIOLATIONS

Observation

Monitoring of security violations and powerful user activity is not currently performed by the Assessor's information systems group for the AssessPro application or for the Windows 2000 server on which AssessPro runs.

Recommendation

We recommend that management implement procedures to monitor significant security violations and powerful user activity to increase the assurance that unauthorized access is not obtained to the AssessPro system.

Management Response

We concur. Currently, the AssessPro software does not have the capability to monitor security violations and powerful user activity. The software vendor is upgrading the software with new security options that the Office of the Assessor will implement when available. The new security options will enhance security monitoring capabilities and allow the Assessor's office to monitor security violations and powerful user activity.

GENERAL GOVERNMENT INFORMATION SYSTEMS
MAINFRAME USER ACCESS

Observation

KPMG Information Risk Management noted that although a request for mainframe user access must be authorized by a user's supervisor before the access is granted by the system administrator, these documented authorizations are only retained for one year. Periodic reviews or reauthorization of users are also not performed by management on a regular basis.

Recommendation

We recommend that management consider implementing periodic management reviews (i.e., annual, semi-annual, quarterly, etc) to help ensure that users are authorized for their access. Documentation from these reviews should be retained as evidence that all current users' access has been properly authorized.

Management Response

We concur. We have implemented periodic reviews of all access authorizations.

GENERAL GOVERNMENT INFORMATION SYSTEMS
DELINQUENT TAX ACCOUNT RECONCILIATIONS

Observation

Payments for delinquent tax accounts are reconciled at the detailed level only once annually at the time the new tax roll is updated in the Trustee system. Discrepancies usually arise between the summary and detailed delinquent data due to adjustments made in the system.

Recommendation

We recommend a reconciliation of delinquent tax years be completed on a quarterly basis to help increase the accuracy of both the detail and summary accounts on an interim basis. Also, if new software is selected to replace the mainframe Assessor and Trustee systems, we recommend the new system have the functionality to account for special exceptions (i.e. bounced checks, update past delinquent accounts, etc) that currently require IS and the Trustee's office to make manual adjustments to the system. This could help minimize discrepancies discovered in the delinquent tax accounts during the year-end reconciliation process.

Management Response

We concur. The Tax Accounting system will be replaced soon and will address the functionality outlined in this recommendation.

GENERAL GOVERNMENT INFORMATION SYSTEMS
CHANGE MANAGEMENT DOCUMENTATION

Observation

Although documented approvals are required from development managers before ITS application or operating system changes are moved into the production environment, documentation and testing of application changes are the responsibility of the individual development groups. We also noted that documentation of requests, testing and final requestor approvals are not retained in most cases for application and operating system changes.

Recommendation

For Departments without change management procedures, management should consider establishing procedures for all changes implemented. These procedures may include the following criteria:

- Change requests should be documented and submitted to the IT department by authorized individuals within the related user or IT groups.
- The assignment of resources should be documented for each request
- Development resolutions should be documented
- Test scripts and test results should be documented and approved by the appropriate personnel (i.e., IT supervisors, users, etc)
- Changes should be reviewed and approved by a development supervisor independent of the individual responsible for coding the change, before the change can be moved to the production environment.

The requestor should be responsible for approving the change (i.e., "closing the change ticket") after the change has been implemented in production.

Management Response

We concur. Current procedures address these issues. Efforts will be made to be sure that current procedures are being followed.

GENERAL GOVERNMENT INFORMATION SYSTEMS
ACCESS TO PRODUCTION AND DEVELOPMENT ENVIRONMENTS

Observation

Developers in the ITS Web Applications group have access to the development and production environments. Management has currently segregated duties so that the Web Applications manager is migrating changes to production. The Web Applications manager does not have access to the development environment, but there are still Web Applications programmers that have access to make changes and move them to production.

Recommendation

We recommend that management should restrict the migration of Web Applications changes to the production environment to an independent group outside of the Web Applications group and programmers should not have access to the production environment.

Management Response

We concur. It is sometimes difficult with a small staff to have a complete segregation of duties but we agree that this would be the best approach. An effort will be made to implement this recommendation.

GENERAL GOVERNMENT INFORMATION SYSTEMS
CHANGE MANAGEMENT AND SYSTEMS DEVELOPMENT PROCEDURES

Observation

Currently there are several different Metro government IT departments that are responsible for their own change management and systems development procedures over the systems that they maintain. These departments include: Metro Nashville Police Department, Metro Nashville Fire Department, Metro Nashville Public Schools, FASTNET/Finance, Metro Water Service, Metro Solid Waste, Register of Deeds and the Justice Information Systems.

Recommendation

For IT departments without change management and systems development procedures, we recommend that management consider implementing such procedures to increase the assurance that all changes and development projects are properly documented, tested and approved before migrated to the production environment.

Management Response

We concur. This recommendation should be carefully considered by both the departments referenced and by Metro's Information Systems Council.

GENERAL GOVERNMENT
FASTNET ACCESS

Observation

One programmer and a systems analyst have administrator access to FASTNET, and two members of the payroll department have *ALL (full access rights with the exception of command line access) to the FASTNET system.

One programmer has been granted administrator and command line access to the system so that she has access to make programming changes and migrate her own changes to the production environment. Two members of the payroll department have been granted *ALL access to FASTNET so that they have access to all programs needed to run payroll processing each pay-period.

Recommendation

We recommend that management limit programmer access so that programmers do not have access to make changes to code in the production environment and do not have access to update production data. Management should also research the programs needed to run payroll each pay period and limit each individual's access to only the necessary programs that they need to complete their job responsibilities. If this is not feasible, then management should implement the appropriate controls (i.e., periodic review of exception reporting which covers all potential unauthorized activities) to monitor the activities of these payroll employees in FASTNET on a regular basis.

Management Response

We concur. We will research the programs needed to run payroll and limit payroll department users' access to only the necessary programs needed to carry out their job responsibilities. We will limit programmer access to production data by removing command line access and *ALL access rights by June 30, 2004.

GENERAL GOVERNMENT
AUTHORIZATION OF FASTNET USER ACCESS

Observation

A documented management approval is not required before a user is granted access to the FASTNET system. A user's manager is notified after a user has been granted access to the system, but no documented response from the manager is required to authorize the individual's access. Also, periodic management reviews have not been implemented to increase the assurance that terminated or unauthorized access has not been granted to FASTNET users.

Recommendation

We recommend that management implement procedures requiring managers to provide a documented authorization of user access before users are granted access to FASTNET by the security administrator, and that this documentation be retained for future reference. We also recommend that management implement a periodic review of access of the individuals that they supervise.

Management Response

We concur. We currently review user access and revoke access to users that have not accessed the system at least semi-annually. We currently revoke or modify user access for terminated or transferred employees on a weekly basis.

The PeopleSoft Enterprise One implementation, scheduled to go-live January, 2005, will provide additional security and approval capabilities. For example, system security will be granted by groups that have been approved by internal audit. These groups will not combine job functions that would jeopardize internal controls.

Also, beginning in January, 2005, user requests for training will require supervisor approval before additional system security is granted.

GENERAL GOVERNMENT
LINKAGE OF DEPRECIATION RECORDS

Observation

Currently, if an improvement or addition related to an existing fixed asset is recorded, the system computes depreciation expense based on the inception date of the existing asset, rather than the date the improvement or addition is completed. This results in a mismatch of depreciation expense and the useful life of the new asset.

Recommendation

We recommend that improvements or additions be depreciated based on their respective useful lives. This will properly reflect depreciation expense over the life of the new asset.

Management Response

We concur. New fixed asset master records, linked to the original asset in a parent/child relationship, are being set up for expenditures July 1, 2003 and forward for any improvements or additions to existing assets. Once completed and put into use, the improvement or addition is transferred from construction work in progress and depreciation calculations begin. This facilitates accurate depreciation calculations for both the original asset and its improvements and/or additions.

OFFICE OF TREASURY
MNPS RETIREMENT FUND TRUSTEE RECONCILIATIONS

Observation

MNPS 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) was recorded throughout the year, activity for funds held by the third party trustee was not recorded until adjustments were compiled 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 reconciliations could leave such assets at risk and potentially creates the opportunity for untimely identification of errors.

Subsequent to June 30, 2002, the Government's Office of Treasury assigned personnel to work with MNPS personnel to establish procedures for reconciliation of this information; however, no notable progress was made during fiscal year 2003. Treasury personnel did complete these reconciliations as of and for the year ended June 30, 2003, and adjusting entries were posted to the general ledger in November 2003.

Recommendation

The coordinated effort between the MNPS Accounting Department, the MNPS Pension Department and the Office of Treasury that was established late in 2003 should be continued, and focus should be placed on timely preparation of reconciliations and resolution of differences.

Management Response

We concur. Written procedures will be put in place in the Office of the Treasurer detailing the process and deadlines for completion. The entries and reconciliations for January 2004 and forward will be completed on a monthly basis.

OFFICE OF TREASURY
COORDINATION BETWEEN THE DEPARTMENT OF WATER AND SEWERAGE SERVICES AND TREASURY

Observation

KPMG noted that a market adjustment entry had not been posted to some investment accounts on a timely basis. The Treasury Department receives the statements related to this investment account but was unaware that they were responsible for the entry.

Recommendation

KPMG recommends that coordination and communication between the Department of Water and Sewerage Services (W&S) and Treasury be improved so all investment entries are posted on a timely basis.

Management's Response

We concur. The adjusting entry to record to market will be completed on a monthly basis going forward.

DEPARTMENT OF WATER & SEWERAGE SERVICES
COORDINATION OF ACCOUNTING FUNCTIONS

Observation

During our accounts receivable reconciliation testwork, it was noted that an accrual for revenue had been recorded twice on the general ledger. This occurred because W&S and Division of Accounts each recorded the entry. This duplicate entry was also noted in the prior year audit.

Recommendation

We recommend that W&S and Division of Accounts more closely coordinate their efforts in order to avoid duplicate entries. A well-defined outline of entries for which each W&S and Division of Accounts is responsible would facilitate this process, as well as allow W&S to take more ownership of the accounting function.

Management Response

We concur. W&S will coordinate with Metro Finance in future year-end wrap-ups to avoid duplicating a portion of the accrual and to reconcile differences.

DEPARTMENT OF WATER AND SEWERAGE SERVICES
WATER CUT-OFF AND COLLECTION ACTIVITIES

Observation

The Department's current policies state that water services will be cut off after 30 days of delinquent non-payment. It is the responsibility of the meter readers to perform the cut-off procedure. Due to a shortage in meter reading personnel, management has instructed the readers to place priority on the meter readings, and to defer cut-off procedures. In 2003, the Department incurred bad debt expense of approximately $1.7M, which is partially attributable to inadequate cut-off procedures.

Recommendation

We recommend that W&S follow its approved cut-off and collection procedures in order to minimize write-off of uncollectible amounts from customers.

Management's Response

We concur. W&S adheres to rules set forth by the Tennessee Public Service Commission regarding collection of unpaid services (T.C.A., 65-32-104)

WS secured a third party contractor to work field collections in Fiscal Year 2004. This will ensure that delinquent accounts are addressed more quickly.

DEPARTMENT OF WATER AND SEWERAGE SERVICES
REVIEW OF ADJUSTMENTS TO CUSTOMER ACCOUNTS

Observation

There was an unreconciled amount of approximately $1.3M between the H.T.E. system and FASTnet primarily because customer service staff may make adjustments to customers' accounts without supervisor review. As a result, entries may not be correct or properly authorized.

Recommendation

We recommend that W&S implement a management review and documented approval for adjustments made to customers' accounts. This would help ensure that entries are proper and are posted correctly to both H.T.E. and FASTnet, which will in turn, facilitate the reconciliation process between the two systems.

Management's Response

We concur. W&S expects to improve account reliability in subsequent fiscal years, we are partnering with Eisner Technologies to develop an interface to FASTnet from H.T.E. The interface will allow the Point of Sale system to pass all cash transactions to FASTnet and for the H.T.E. system to pass all revenue transactions to FASTnet.

COURTS
CENTRALIZED GENERAL LEDGER SYSTEM

Observation

KPMG notes that the Juvenile Court, the County Clerk, the County Register, the Trustee, the Criminal Court, the Clerk & Master, and the Circuit Court each use different General Ledger systems, generally in the form of a combination of software packages and manual ledger books. These systems lack some of the basic controls of a centralized general ledger system. Additionally, a lack of a centralized general ledger allows greater possibility of human error or fraud compared with a centralized general ledger system.

Recommendation

KPMG recommends the Courts & Constitutional Officers use FASTnet for general ledger purposes. This will promote uniformity of recording and reporting among the Courts & Constitutional Officers and with other Metro agencies.

Management's Response

We concur. Finance will work with the Courts and other Constitutional Officers toward a solution and complete a plan of action by June 30, 2004.

COURTS
CLERK AND MASTER – SEGREGATION OF DUTIES

Observation

KPMG notes that there is little segregation of duties among personnel in the Clerk and Master office. The same individual prepares disbursements, signs checks (although a dual signature is required), prepares deposits, reconciles bank accounts, and maintains the ledger. Additionally, bank reconciliations do not appear to be prepared on a timely basis. With lack of segregation of duties, the risk of misstatement due to fraud increases. Also, there are few review processes in place, so unintentional errors may go unnoticed.

Recommendation

The Clerk and Master office is small, so it is understandable that complete segregation of duties may not be a possibility due to the limited number of personnel. However, a review process of the ledger maintenance may mitigate the risk of misstatement due to error and fraud. KPMG suggests that a trial balance be prepared on a monthly basis, and a supervisor should review this trial balance and all bank reconciliations for the month. Because of the lack of segregation of dutues, it is crucial that bank reconciliations be prepard on a timely basis, in order to quickly identify potential errors or fraudulent transactions.

Management's Response

We concur. Bank reconciliations will be prepared on a timely basis going forward and a supervisor will review the trial balance and bank reconciliations.

COURTS
CRIMINAL COURT – CASH PROCEDURES

Observation

KPMG noted the following weaknesses in controls over the cash process and potential effects in the Criminal Court Clerk's office:

- Cashiers can alter the receipt date when receiving cash into CJIS (Criminal Justice Information System). This allows cashiers to backdate receipts so that they do not show up on the daily balancing report; thus, the cashier may misappropriate the cash received without being detected by the daily balancing report.

- Cashiers balance money received with receipts entered into CJIS each day using a report that details receipts received on the current day. This allows the accountants to balance the daily cash received with the receipts in CJIS, but they may not be aware of any receipts that were physically received and entered on the current date, but backdated.

- All receipts are not accounted for using a report that identifies and highlights any skips in sequence. Cashiers are therefore in a position to receipt a payment but misappropriate the money received. Under surrent procedures, the accountants would not recognize this as they would not know if there was a skip in receipt sequence.

- Receipts entered into CJIS are not reconciled with the cash receipts in the general ledger. Cashiers may give a manual receipt to a defendant, but not record the receipt in CJIS; thus, the money may be misappropriated, and the revenue would not be recorded.

- Manual receipt books are not reviewed on a regular basis to ensure all manual receipts are properly entered into CJIS.

The overall effect of these weaknesses is that fraud and errors could occur without being detected, thus, revenue and cash may be understated on the financial statements.

Recommendation

KPMG suggests the following procedures for resolution of the above weaknesses. Those items marked with "*" have already being implemented by the court as of September 2003; however, these procedures were not in effect for the year ended 6/30/03:

- Limit the ability to alter the receipt date in CJIS only to supervisors. This capability is necessary to correct errors on receipts, but should be limited to individuals who do not ordinarily receive cash. Individuals should have unique login ID's and passwords for access to CJIS, and the computer should automatically log the individual out after 10 minutes of inactivity. This will mitigate the ability of an unauthorized user to access secure areas of the information system.

- The daily cash balancing report should list all receipts created on the current date, and should highlight any discrepancies between receipt date and the date receipt was created.*

- In addition to the daily cash balancing report, a report should be run daily that lists the receipts for the day in numerical order. Any skips in receipt sequence should be highlighted and investigated.

- Cash receipts per CJIS should be reconciled on at least a monthly basis with cash received per the general ledger. Any discrepancies should be investigated on a timely basis.

Manual receipt books should be reviewed on a weekly or monthly basis to ensure that all receipts are accounted for, and all receipts have been entered into CJIS.*

Management's Response

We concur. We are investigating the first recommendation of limiting access to the ability to change a date in the payment receipting screen to supervisors and its Director. A system change will be required. We have determined that JIS has the expertise in house to make this change and have requested the change be made.

Although the system does not automatically log out users after a period of inactivity, we now have implemented a policy making it mandatory for each employee to log out when they leave their desk. We have evaluated the effectiveness of this policy and are confident that employees are in compliance with this policy.

We have created reports that list all receipts in numerical order. We have one report for all receipts, one for only Criminal Receipts and one for only the G/S receipts in numerical order. Each bookkeeper will review the report and investigate any discrepancies.