

**THE METROPOLITAN GOVERNMENT OF NASHVILLE
AND DAVIDSON COUNTY, TENNESSEE**

Letter of Recommendations to Management

June 30, 2012



October 31, 2012

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

Ladies and Gentlemen:

We have audited the basic 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, 2012, which collectively comprise the Government's basic financial statements. We have also audited the financial statements of the Sports Authority Fund and the Industrial Development Board Fund, which are discretely presented component units of the Government, and the financial statements of each of the Government's nonmajor governmental, nonmajor enterprise, internal service and fiduciary funds, and have issued our report thereon dated October 31, 2012. Under professional standards, we are providing you with the accompanying information related to the conduct of our audit. We have also audited and reported on separately the financial statements of the following discretely presented component units: Metropolitan Nashville General Hospital and Bordeaux Long-Term Care and Knowles Home (funds of the Hospital Authority), the Metropolitan Transit Authority, and the Metropolitan Nashville Airport Authority. We did not audit the financial statements of the following discretely presented component units: the Nashville District Management Corporation, the Gulch Business Improvement District, Inc., the Metropolitan Development and Housing Agency, the Electric Power Board, the Emergency Communications District, and the Convention Center Authority. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion, insofar as it relates to the amounts included for those entities, is based on the reports of the other auditors.

Management of the Government is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit of the aforementioned financial statements, in accordance with auditing standards generally accepted in the United States of America, we considered the Government's internal control over financial reporting ("internal control") as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Government's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Government's internal control over financial reporting.



Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses and, therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as discussed below, we identified certain deficiencies in internal control that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

We consider the following deficiencies in internal control to be material weaknesses:

CLERK AND MASTER, COUNTY REGISTER, AND CIRCUIT COURT

Lack of Segregation of Duties with Financial Transactions

Observation

During our audit procedures over cash receipts and cash disbursements at these offices, we noted either one or several clerks are responsible for multiple duties which involve financial transactions, such as handling incoming cash receipts, processing these cash receipts, making physical deposits to the bank, maintaining check stock, processing cash disbursements, signing checks, including checks written to themselves for deputy clerk fees, and posting transactions to the Access database. There was no documentation that these functions were reviewed by another employee. These incompatible accounting functions constitute deficiencies in internal control which could lead to undetected misappropriation of funds as well as undetected material misstatements of the offices' financial information.

Recommendation

We recommend that management design and implement procedures that would more effectively segregate certain duties between employees that handle cash and those that record cash transactions. The following are suggestions for improving controls and segregation of duties:

- (1) An employee independent of posting transactions to the accounting records should be responsible for opening the mail/receiving cash and checks over the counter and making copies of checks received. This person should also prepare a daily cash receipts log indicating the dollar amount, nature of cash receipt, and court case. This person should also prepare and make the daily deposit to the bank.



- (2) The employee responsible for preparing the daily cash receipts log and making the daily deposit should submit the daily cash receipts log, bank deposit slip and copies of the checks to an independent employee for timely posting the daily cash receipts to the accounting records.
- (3) An employee independent of posting transactions to the accounting records and with no check signing authority should maintain the physical check stock for all bank accounts. In addition, this employee should maintain a check log for issuing check stock to the employee responsible for processing cash disbursements. This check log should list the sequence of checks issued, the number of checks issued and be signed and dated by both the employee maintaining the check stock and the employee requesting and receiving issued checks. Any unused or voided checks should be logged back into the check log.
- (4) An employee independent of the duties described in (1)-(3) above should be responsible for posting daily cash receipts and cash disbursement transactions as well as preparing the checks for cash disbursements.

Management's Response

Clerk and Master

This recommendation was addressed in January 2012 and noted previously in Management's Response to the June 2011 audit. The Office hired an additional bookkeeper increasing the bookkeeping staff from two to three. Management continues to consult with Metro Finance, EBS and other departments to develop processes that will improve controls and segregate duties. The following processes have been implemented:

- 1. An employee independent of posting transactions to the accounting records opens all the mail and makes copies of all checks. A daily mail check log is kept and reviewed against daily deposits by an employee independent of posting transactions to the accounting records. The daily deposit is also made by an employee independent of posting transactions to the accounting records.*
- 2. A sign has been posted at the accounting desk stating, "If you fail to receive a receipt ask to speak to the Clerk and Master."*
- 3. Employees with check writing authority no longer are signatory on checks made to themselves for special officer fees. This practice ceased prior to receipt of the June 2011 audit.*
- 4. An employee independent of posting transactions to the accounting records and who is without check signing authority maintains the physical check stock and a check log for issuing checks for cash disbursements.*

As previously stated, Management will continue to explore and implement options to address noted concerns.



County Register

1. *At this time the Register of Deeds Office does not have ample staff to accomplish this process. Furthermore, it does seem that we would be duplicating to some degree the process we are currently using.*
2. *We agree that an independent employee should timely post the daily cash receipts to the accounting records. We do have an independent employee performing this process.*
3. *Steve Moore, Chief Deputy of Information Technology, maintains all check stock. Checks are locked in the safe in the Information Technology department. Steve maintains a spreadsheet for each checking account that includes the date, check numbers, signature of employee requesting check and signature of employee releasing checks.*
4. *Currently, Charles Snyder, Chief Deputy of Finance, is responsible for posting daily cash receipts and cash disbursement transactions as well as preparing checks for cash disbursement. He will continue to do so. He has no involvement in opening and dispersing mail. Also, a second employee verifies bank deposits on the bank statement against daily accounting reports from our document recording/retrieval system.*

Circuit Court

Management is in agreement with the recommendation made regarding the receipting and disbursement of Minor Trust Funds. We will start implementing the change where the Chief Clerk or Team Leaders will receipt the funds from the savings accounts for minors. The Internal Auditor will follow up on the checks that are issued for these Minor Trust Accounts to verify the information is correct as it was Court Ordered.

* * * * *

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the following deficiencies in internal control to be significant deficiencies:

CIRCUIT COURT

Bank Reconciliations – Cancelled Checks

Observation

During our audit procedures over bank reconciliations at this office, we noted that cancelled checks returned by the bank with bank statements are not inspected as part of the bank reconciliation process. As a result, any improper changes made after printing and signing the checks may not be identified timely.



Recommendation

We recommend that the preparers and reviewers of bank reconciliations inspect cancelled checks to identify improper changes made after printing and signing the checks, including comparing all information on the checks to the information in the accounting system.

Management's Response

Since we no longer receive the canceled checks with our bank statements, the Internal Auditor will do a random sampling of checks being processed in particular Checks issued for Minor Trust Accounts, Judgments, Tender and Attorney Fees to compare to the canceled check images on Bank of America Online system to verify no changes have been made.

* * * * *

In addition, during our audit, we noted certain matters involving the internal control and other operational matters that are presented for your consideration. This letter does not affect our report dated October 31, 2012, on the aforementioned financial statements. We will review the status of these comments during our next audit engagement. Our comments and recommendations, all of which have been discussed with appropriate members of management, are intended to improve the internal control or result in other operating efficiencies. We will be pleased to discuss these comments in further detail at your convenience, perform any additional study of these matters, or assist you in implementing the recommendations. Our comments are summarized as follows:

CENTRAL GOVERNMENT

Timely Preparation of Bank Reconciliations

Observation

In testing the Government's internal controls over bank reconciliations, we identified certain bank accounts that were not reconciled timely. Specifically, the Water and Sewer customer refunds and Trustee's imprest checking accounts and the Trustee's unapplied property taxes account were not reconciled timely for several months of the fiscal year. The Government does have certain compensating controls in place to timely detect significant misstatements in the financial statements. However, the risk of not identifying cash errors and possible fraud related to cash increases greatly when bank accounts are not reconciled timely.

Recommendation

All bank accounts should be reconciled timely on a monthly basis by the Government and all unusual reconciling items should be promptly investigated, adjusted and documented with adequate explanations. This will reduce the likelihood of cash errors and fraud, provide for more timely and accurate financial information, and assist in the effective management of cash flow.



Management's Response

Metro Water Services

Metro Water Services goal is to have the Customer Refund Account reconciled according to the guidelines of Metro Finance Department. These guidelines are to have the Customer Refund Account reconciled no later than two to three months after the close of the current month. During the past year the reconciliation was not completed on time due to being under staffed in the CSC-Cash section. MWS is in the process of hiring a Finance Officer II for the CSC-Cash section and this will be one of their main responsibilities.

Trustee's Office

We are happy to report that we are caught up on the monthly reconciliations. This task has been reassigned to a new employee who has been doing them in a timely manner for the past several months. We do not foresee any problems with keeping up to date on these reconciliations from this point forward.

Old Outstanding Items on Bank Reconciliations

Observation

Reconciliations for the Trustee's imprest checking account and the Water and Sewer customer refunds account include excessive quantities of reconciling items that have been outstanding in excess of one year.

Recommendation

Though none of the items identified are significant individually or in the aggregate for the respective bank accounts, the Government should evaluate the propriety of reconciling items over a year old periodically (at least annually) and include adequate explanations for any resultant adjustments.

Management's Response

Trustee's Office

Every effort has been made to begin evaluating the reconciling items at least once a year. Since this task is tedious, two employees have been working on evaluating outstanding items. We believe we will make significant progress in this area over the next several months after which, we will work to maintain these improvements.



Metro Water Services

Metro Water Services has begun to reconcile the outstanding items that are over a year old. This has been incorporated into the monthly reconciliation of the Customer Refund Account to evaluate the outstanding items.

Deposit Timing for Cash Collections

Observation

During our testing of cash receipts of the Fire Department, we noted several receipts in September 2011 and April 2012 totaling \$2,475 that were not deposited within three days of physical receipt. The State of Tennessee mandates in the Audit Manual that cash collections should be deposited within three days.

Recommendation

The Fire Department should implement procedures that assure that it abides by the State of Tennessee Audit Manual requirement for depositing checks and cash within three days of receipt.

Management's Response

The Nashville Fire Department is restructuring the organization and recently hired a new Finance Manager. Since then, the Fire Department is utilizing the Metro Government Cash Policy which requires deposits within one business day of receipt. We will continue working on compliance with this policy.

Documenting Approvals for Cash Disbursements

Observation

During our testing of cash disbursements, we noted seven credit card disbursements for which there was no written evidence of approvals by the respective department heads, as follows:

General Sessions Court	\$ 17.61
Registrar of Deeds	10.00
State Fair Board	127.84
State Fair Board	35.07
State Trial Court	606.00
Historical Commission	4.14
Fire Department	856.16



Recommendation

Though none of the items identified are significant individually or in the aggregate, the Government should ensure that department head approvals for credit card disbursements are obtained timely and documented.

Management's Response

We agree with the observation and recommendation. The Finance Director recently sent a letter to all department heads reminding them of their responsibilities for all credit card payments. A copy of the policy was attached and department heads were encouraged to review the policy with staff.

Deficit Balances in Internal Service Funds

Observation

The Government reported three internal service funds with deficit net asset balances at year-end. The School Professional Employees' Insurance fund made progress during the year in funding its prior year deficit. However, the School Self Insurance and Injured on Duty funds increased their prior year deficit balances by incurring additional current year losses.

Recommendation

We recommend that charges to other funds be routinely monitored and adjusted to eliminate the deficits over a reasonable period. Otherwise, transfers will be required from the General and/or General Purpose School funds over the next two to three years until the deficit balances are alleviated.

Management's Response

We agree with the observation and recommendation. The fiscal year 2012-2013 budgets for all three internal service funds that had deficit fund balances at June 30, 2012 included additional amounts to fund those deficits over approximately a three year period.



Infrastructure Reported Using the Modified Approach

Observation

The Government has adopted the alternative to recording depreciation expense on selected infrastructure assets. Under this method, referred to as the modified approach, the Government expenses certain maintenance and preservation costs and does not report depreciation expense. Roads and bridges are accounted for using the modified approach. The Government's Condition Rating of Transportation Network showed that the percentage of lane miles in fair or better condition declined significantly in 2011. During fiscal 2012, the actual amount spent on roadway paving and surface treatment was again lower than the needed amount.

Recommendation

In order to continue using the modified approach for selected infrastructure assets, we recommend that the Government maintain its roads and streets in accordance with its established policy of at least 70 percent of its road and street system at a fair or better condition.

Management's Response

The numbers reported in the CAFR do not reflect the improved road conditions for flood damaged roads that have been repaired. Those roads will be assessed prior to the next CAFR report and management fully expects that assessment will demonstrate that the actual road conditions are in line with the policy.

Other Postemployment Benefit Plans Funding

Observation

The Government is currently funding its other postemployment benefit ("OPEB") plans on a pay-as-you-go basis, which has resulted in an escalating OPEB liability in its Governmental Activities financial statements. If the current funding trend continues, the Governmental Activities will report a net deficit as early as 2015 in the government-wide statement of net assets.

Recommendation

We understand that the Government is not unique in the challenges it faces in funding its OPEB obligations, neither within the state of Tennessee nor across the United States. Further, we understand that the Government assembled a committee tasked with arriving at best practices for postemployment medical benefits strategy and made significant changes. However, we believe it is important to highlight the matter due to the significance of the exposure and, as such, recommend that the Government continue its efforts to aggressively pursue available means to fund its OPEB obligations.



Management's Response

The Study and Formulating Committee appointed by the Mayor made several recommendations to reduce the cost of postemployment benefits that were adopted by the Metropolitan Council. As a result, the unfunded actuarial accrued liability decreased by nearly \$300 million for June 30, 2012 and the annual required contribution decreased by \$24 million.

COUNTY REGISTER

Deposit Timing for Cash Collections

Observation

During our testing of cash receipts of the County Register office, we noted cash collections for escrow monies are not routinely deposited within three days of physical receipt. The State of Tennessee mandates in the Audit Manual that cash collections should be deposited within three days.

Recommendation

The County Register office should implement procedures that assure that the office abides by the State of Tennessee Audit Manual requirement for depositing escrow monies within three days of receipt.

Management's Response

The Register of Deeds office will make a concerted effort to deposit all escrow monies within three days of receipt.

SHERIFF WORK RELEASE AND INMATE TRUST

Old Outstanding Items on Bank Reconciliations

Observation

Reconciliations for the Sheriff Work Release and Inmate Trust office checking account include several reconciling items that have been outstanding in excess of one year.

Recommendation

Though none of the items identified are significant individually or in the aggregate for the respective bank accounts, the Sheriff Work Release and Inmate Trust office should evaluate the propriety of reconciling items over a year old periodically (at least annually) and include adequate explanations for any resultant adjustments.



Management's Response

The outstanding checks from the 2007-08 timeframe, payable to other Metro government agencies equaling approximately \$20,000, need to be and are in the process of being voided. The other outstanding items consist mainly of Inmate checks that are less than \$5. These checks are too costly to have voided and also would be too labor intensive to eliminate in the Aramark system. The checks that are greater than \$5 are payable to inmates who were determined to be illegal. These checks were cut and forwarded to the location of deportation. The State will not allow these items to be included on the Unclaimed Property list at the end of each fiscal year.

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Management's responses to the material weaknesses, significant deficiencies, and comments identified in our audit have not been subjected to the audit procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the audit committee, management, and others within the Government, and federal and state awarding agencies and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

Crosslin & Associates, P.C.

CROSSLIN & ASSOCIATES, P.C.