MITCHELL TITUS

July 24, 2020

To Management and Board of Directors of
Nassau Health Care Corporation:

In planning and performing our audit of the financial statements of Nassau Health Care Corporation (NHCC or Hospital) as of and for the year ended December 31, 2019, in accordance with auditing standards generally accepted in the United States of America, we considered NHCC's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we do not express an opinion on the effectiveness of NHCC's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be *material weaknesses or significant deficiencies* and, therefore, *material weaknesses or significant deficiencies* may exist that were not identified. However, as discussed below, we identified certain deficiencies in internal control 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 over financial reporting, 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. A *reasonable possibility* exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

- *Reasonably possible*. The chance of the future event or events occurring is more than remote but less than likely.
- *Probable*. The future event or events are likely to occur.

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 the entity's internal control to be significant deficiencies:

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Financial Statement Review and Close Process

During our audit, we noted the following:

- Detailed accounting policies and procedures were not written for some key accounting functions.
- Monthly bank reconciliations were not performed regularly. At year end, there was an unexplained reconciling difference of approximately $278,000.
- A reconciliation of payroll expense to Form 941 was not performed.
- Certain year-end accruals were not corrected prior to or during the audit.
- Certain financial statements presentation and footnotes weren't updated to reflect current pronouncements.
- The long-term debt was not properly classified on the face of the financial statements in accordance with GASB No. 1. Per GASB No. 1, if there are provisions that make debt "callable," the debt is required to be presented on the accelerated terms. While the footnote presentation was proper, the financial statement presentation between current and non-current debt was misclassified by $11,596,000.
- Management relies significantly on the analysis performed by Healthcare Management Solutions, LLC (HMS), and there was no evidence of review by the Hospital.

Accounting principles generally accepted in the United States require that management establish policies and procedures to ensure that proper internal controls exist to prevent, detect and deter misstatements in financial statements due to fraud or error. Common procedures should include written policies and procedures, periodic reconciliations of subsidiary ledgers and certain financial accounts, as well as review of accounts, reconciliations and financial statements by varying levels of management.

<u>Recommendation</u>

Management should review, update and consolidate existing narratives into detailed written policies and procedures, which would include preparing reconciliations and management reviews. Additionally, management should ensure they are up to date on new accounting guidance and pronouncements impacting the financial statements.

<u>Management's Response</u>

Management will review and formalize policies and procedures and include detailed controls including management review procedures. With respect to the $11 million reclassification of long-term debt, management had discussions with Nassau County officials (Nassau County guarantees this debt) and NHCC financial advisors relative to this debt, that the related remarketing agreement and letters of credit that expire on September 25, 2020 and were actively working on renewing or replacing these agreements prior to the issuance of the audited financial statements. When the debt is remarketed its presentation in the statement of net position will be consistent with the requirements of GASB No. 1. The long-term debt has been historically renewed/replaced annually. Management will review the accounting guidance and ensure proper presentation and disclosure in future financial statements.

Evaluation of Going Concern

U.S. GAAP requires management to evaluate the organizations ability to continue as a going concern. Specifically when relevant conditions or events, considered in the aggregate indicate that the organization will be unable to meet its obligations as they become due within one year after the issuance date of the financial statements, and therefore raise substantial doubt about the organizations ability to continue, management should discuss and prepare a plan to mitigate and address these conditions and events. Per our inquiry of management and review of Board minutes, we noted while management was aware of the risk, no formal plan was developed or discussed with the Board or the Audit Committee.

Recommendation

We recommend that management and the Board develop plans to mitigate and/or address the factors that contribute to its inability to continue as a going concern. The plan at a minimum should include cash flow projections and corrective actions (quantitative and qualitative) with responsibilities and a timeline. The plan should cover the period from the financial statement date through twelve months subsequent to the issuance date.

Management’s Response

Management agrees and is aware of the going concern issues facing NHCC. Management has prepared projected cash flows and has had discussions with the NYS Department of Health in an effort to obtain additional funding through various programs to support the operations of NHCC. The deficits, and corresponding financial condition, have resulted from the long-standing mission of NHCC to provide care to the indigent and people with limited financial resources. Further, NHCC’s fringe benefits were structured in the past to provide benefits, which are normally more comprehensive than those provided to employees of other hospitals. However, in a conscious effort to reduce operating costs, these benefits have recently been modified to be more in line with the current offerings by other hospitals. Unfortunately, the legacy cost of the previous arrangements will continue to impact NHCC over the next several decades (future health benefit liabilities at December 31, 2019 are $565 million). As such, NHCC will need to request additional support through programs of NYS to support operations, along with modification of operations to improve operating results.

Management will work with the Board of Directors to develop plans to address NHCC’s going concern.

Receivable and Subsequent Cash Analysis

During our analysis of in- and out-patient receivables and subsequent cash collections, we noted management completes its analysis on a combined basis. Due to the different risks and collectability of the in-patient versus out-patient receivables, we believe that the two should be evaluated separately. Combining the evaluation can result in the individual accounts being over/under reserved even if the aggregate reserves are reasonable.

Recommendation

We recommend that management review its subsequent cash collections separately for in- and out-patient receivables.

Management's Response

Management accumulates in- and out-patient subsequent cash receipts and compares them to overall accounts receivable balances since these are combined as one balance on the balance sheet. We will evaluate the analysis to determine the benefit of separating this analysis into both components.

Grant Requirements

During our review of grant revenue and receivables, we noted that a significant State grant required NHCC's audit be performed in accordance with *Government Auditing Standards*. Management did inquire with the State agency which confirmed acceptance of an audit completed in accordance with U.S. GAAP. However, noncompliance with grant requirements can result in penalties and/or repayments of a grant.

Recommendation

We recommend that management review all grant agreements to ensure NHCC is in compliance with the terms and conditions of the grant.

Management's Response

Management will establish procedures to ensure compliance with grant requirements.

Documentation for Fixed Asset Projects

During our testing of fixed assets and transfers from construction in progress, we noted detailed policies and procedures regarding the accumulation of budget and/or costs by project were not written. Per our inquiry, management informed us that their procedures include the request and receipt of individual emails from the applicable departments, noting a project has been completed. We were not provided with the appropriate documentation for completed projects during testing.

Recommendation

We recommend that management document its policies and procedures to record and track project costs from inception to completion.

Management's Response

In accordance with prior-year audit recommendations, management was successful in implementing improved policies and procedures regarding the recording of CIP transactions and transfers. However, management agrees that these policies and procedures need to be more formally documented and as such will do so as deemed necessary.

Journal Entries

During our review of journal entries, we noted that supporting documentation for two entries did not exist. In addition, while the journal entries were properly supported and appeared reasonable, there was not consistent evidence of supervisory approval. Good accounting practices suggest that there is an adequate system of review established by management.

Recommendation

We recommend that management establish policies and procedures to ensure adequate documentation is maintained for all journal entries and that they are reviewed and authorized prior to posting in the general ledger.

Management's Response

Management agrees with the recommendation and will implement a more formalized journal entry authorization and review process.

Cash Testing

We noted during our standard bank confirmation testing that a former employee, who we were informed was a consultant, is still an authorized signer on certain accounts. This could present a significant risk to the organization.

Recommendation

We recommend that management immediately and periodically review all authorized signors to ensure only appropriate individuals are approved as signatures on cash or other accounts.

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Management's Response

Management notes that the consultant referenced is not a consultant. He is a part time salaried employee and was the trusted full-time Comptroller before retiring and returning on a part time basis in February 2020. However, management agrees that bank signatories should be periodically reviewed and will ensure that this is done more routinely throughout the year.

We have also identified the following as an area for improvement:

Internal Audit Function

During our audit, we noted that NHCC does not have an Internal Auditor or similar position. Due to the size and complexity of NHCC, we believe it would be beneficial for the corporation to establish an Internal Audit function. The position should report directly to the Board or Audit Committee and would be responsible for developing an annual audit plan to address the financial, operational and compliance objectives of NHCC.

Recommendation

We recommend that management consider establishing an Internal Auditor Position along with a detailed written job description, including objectives and responsibilities of the position. The Internal Auditor, in conjunction with the Audit Committee, can develop an annual and three-year audit plan.

Management's Response

Management agrees and has issued a request for proposal for this function.

The purpose of this communication, which is an integral part of our audit, is to describe for management and those charged with governance the scope of our testing of internal control and the results of that testing. Accordingly, this communication is not intended to be and should not be used for any other purpose.

Mitchell & Titus, LLP