

MANAGEMENT LETTER

Nassau Health Care Corporation  
Year Ended December 31, 2008



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Management and the Board of Directors  
Nassau Health Care Corporation

In planning and performing our audit of the consolidated financial statements of Nassau Health Care Corporation (the "Corporation") as of and for the year ended December 31, 2008, in accordance with auditing standards generally accepted in the United States, we considered its internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Corporation's internal control. Accordingly, we do not express an opinion on the effectiveness of the Corporation's internal control.

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 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.

Our consideration of internal control was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control that we consider to be material weaknesses, as defined above.

During our audit, we noted the following control deficiencies (as described above) and other matters that we have included in the attached listing of comments to management.

This communication is intended solely for the information and use of management and the Board of Directors and is not intended to be and should not be used by anyone other than these specified parties.

We would be pleased to discuss the above matters or to respond to any questions, at your convenience.

*Ernst + Young LLP*

June 12, 2009

# Nassau Health Care Corporation

## Comments to Management

December 31, 2008

### **Postemployment Benefits Other Than Pensions (Comment Repeated from Prior Year)**

The Corporation provides its participant data listing to a consulting actuary, who prepares an annual actuarial valuation for its postemployment benefit plan. The annual actuarial valuation is used to determine the Corporation's annual postemployment benefit expense and the related liability and financial statement disclosures. The Corporation should consider implementing a process to formally document the compilation of information submitted to the actuary, challenge the information used by the actuary to develop the estimate and to formally document the reasonableness of assumptions (e.g., the discount rate) used by the actuary.

#### *Management's Response*

Management concurs and is currently challenging certain assumptions that are driving the annual required contribution ("ARC") to an amount in excess of \$40 million each year going forward.

### **Financial Statement Close Process and Significant Disclosures (Comment Repeated from Prior Year)**

The financial statement close process includes, among other things, the monthly process employed by the Corporation's finance department to update and maintain the general ledger, reconcile Corporation activity to the general ledger, perform detailed account analysis for management's review and produce financial statements. As the Corporation strengthens and enhances its human resources in the finance area, it is important for management to continue to strengthen the financial statement close processes by:

- Enhancing formal policies, procedures, roles, responsibilities, time-frames and financial statement closing goals into the monthly close process
- Enhancing formal procedures into the financial statement close process so that all appropriate account reconciliations are completed timely
- Codifying the formal procedures in the accounting policies and procedures manual.

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### Comments to Management (continued)

Additionally, the Corporation's controls over significant financial statement disclosures and the related sources of information that influence these disclosures should be evaluated by management. Controls related to the preparation, review and approval of the significant financial statement disclosures should be considered. Additionally, narratives or other explanatory information that document the flow of information from the Corporation's accounting records (including source inputs and required summarizations) to the disclosures in the financial statements should be maintained.

#### *Management's Response*

Management will continue to enhance its formal policies and procedures and reconciliation processes regarding its monthly close process to further ensure timely and accurate interim financial reporting.

#### **Journal Entry Process (Comment Repeated from Prior Year)**

The Corporation's processes and control procedures regarding recording journal entries should be strengthened. The Corporation should update policies related to adjusting journal entries. Specifically, policies should address the protocol for recording all types of journal entries, whether they are recurring, manual, pre-closing or post-closing.

Written documentation should include the parameters for initiating journal entries and a matrix for approving and authorizing journal entries. The policies should distinguish between recurring and non-recurring journal entries and pre- and post-closing journal entries and the varying controls over each type. Further, written policies should establish standard guidelines for the written approval of all journal entries by someone senior to the preparer, in addition to written documentation by the preparer.

#### *Management's Response*

Management will continue to enhance and further formalize its policies and procedures related to the monthly and year-end journal entry process.

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### Comments to Management (continued)

#### **Credit Balances (Comment Repeated from Prior Year)**

The complexity of billing arrangements, inconsistent patient information and the level of sophistication of payors are among the sources of credit balances. Credit balances have the potential to distort the periodic analysis of accounts receivable and the estimation of related allowances. It is important for the Corporation to ensure timely reconciliation and disposition of these accounts. Management should continue to review credit balance accounts to determine their cause and to document whether accounts should be adjusted, reclassified or refunded.

#### *Management's Response*

Management reviews credit balance reports on a monthly basis. We will continue to further enhance and formalize this process on a monthly basis.

#### **Accounts Receivable and Revenue (Comment Repeated from Prior Year)**

Based on the results of our tests of transactions and our inquiries of finance management, we noted that the billing system does not reflect the most current third party reimbursement rates for several payors. Although the billing departments have back-end procedures in place to adjust for differences, a process should be implemented to help ensure that billings to third party payors reflect the latest rates.

#### *Management's Response*

Management concurs and will further formalize its periodic updating procedures to ensure the latest rates are incorporated into the billing system on a timely basis.

#### **Documented Cost Reporting Policies and Procedures (Industry Comment)**

The Corporation has a number of policies and procedures designed to help ensure compliance with the myriad of regulations related to the preparation of its regulatory cost reports. Some of the policies and procedures have developed from established business practices, management oversight, job responsibilities, etc. and are not documented in writing. Given the importance of documenting compliance with rules and regulations, the Corporation should consider documenting in writing the policies and procedures involved in the development of cost report data, including those that help ensure that:

- Costs are not claimed unless based on appropriate and accurate documentation
- Allocation of costs to various cost centers are accurate and supported by verifiable and auditable data

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Comments to Management (continued)

- Unallowable costs are not claimed for reimbursement
- Costs are properly classified
- Prior year cost report adjustments are incorporated into future filings
- Related party charges are reflected at cost
- Procedures for reporting bad debts are in accordance with federal statutes, regulations, guidelines and policies.

This comment continues to be important in light of widespread heightened emphasis on documented internal controls and the desire of organizations to demonstrate the effectiveness of established controls.

**Information Technology**

In connection with the 2008 audit of the financial statements, we performed an evaluation of the effectiveness of the information technology (“IT”) general controls (“ITGCs”) environment. Our objectives were to:

- Update our understanding of the IT processes that support the business (financial statement relevance) and to consider business risks identified
- Validate the key controls related to the IT processes (change control, logical access security and technology operations) that affect the reliability of electronic audit evidence and financial reporting
- Evaluate the design effectiveness of the ITGCs through appropriate audit procedures
- Assess remediation of the issues communicated during the 2007 financial statement audit.

We focused on applications that have a direct effect on financial reporting. Our 2008 audit procedures related to ITGCs for the following applications:

- Eagle
- Lawson

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### Comments to Management (continued)

*Section 1* of this information technology section of our comments includes observations and recommendations based on our 2008 financial statement audit procedures.

*Section 2* provides summary information for the follow-up of the prior year's comments.

#### **Section 1**

##### **Change Management Process – Documentation of Controls in Change Management Process**

Management has implemented a limited set of program change policies and procedures to control changes made to the Eagle and Lawson applications. Although the Corporation does not own the source code of these applications and changes are limited to vendor initiated upgrades and report changes, management does not regularly perform and document testing, approval or monitoring of these changes. Evidence of key controls, such as authorization to develop, test, and user acceptance approvals are not consistently prepared or retained for each change.

Without formal program change policies and procedures, management cannot be assured that all changes are documented, tested and properly approved. Moreover, management cannot confirm that changes are made according to management's specifications and that only authorized programs are migrated into production. Programs moved to the production environment without appropriate testing have the potential to corrupt production data.

The lack of formal, written policies and procedures weakens the control environment and increases the risk that informal controls may not be followed. Additionally, as employees are not aware of the controls management has implemented, the risk that controls will not operate is increased.

The Corporation should strengthen its program change controls to require that all program change requests be documented, tested, approved and migrated to production by personnel independent of the application development function. Management should enhance the change management policies and procedures to better define and formalize the process of requesting, authorizing, testing and approving program changes. Appropriate evidence of this review should be retained for a period of twelve rolling months.

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### Comments to Management (continued)

#### *Management's Response*

We concur with the recommendation. Meetings will be scheduled with the appropriate vendor representatives to ensure that appropriate change controls and documentation are in effect and that the change control functions are performed by those not directly involved in the application development process.

#### **Change Management Process – Outsourced Function Not Monitored and Review of Changes Implemented in Production**

Eagle and Lawson upgrades and patches are developed and implemented by the vendors. Both vendors are able to continuously access the production environment and a review of changes promoted into the application production environment is not in place to verify that only authorized changes are migrated into the Eagle and Lawson Financials environments. Additionally, extensive/administrator privileges (ability to add/modify/delete user access) has been granted to two administrative accounts which the Eagle vendor (Siemens) uses.

Unsupervised application access increases the risk of unauthorized or unintentional changes to programs and resources, improper segregation of duties and unauthorized access to data files, which affects the data integrity of the master data files and the completeness and accuracy of the reports generated and used for financial purposes.

While organizations typically exercise little direct control over support service organizations, the services provided by these service organizations and their related internal controls are ultimately the responsibility of the Corporation's management. Without adequate IT management review of the vendor's support activities, application system changes can be made without express approval of management or the user. This issue makes the financial system vulnerable to undocumented changes, whether intentional or accidental, that can affect the data integrity of the applications.

Management should review vendor access to confirm that personnel can detect unauthorized or unapproved access to the Eagle and Lawson applications, and that sufficient security is in place over the organization's information assets. This review should be documented and maintained for a period of twelve rolling months. Access to the Eagle and Lawson applications should be reviewed as follows:

- Initiate a supervisory review of the application logs to confirm that no changes were made by the vendor that were unauthorized or unapproved

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### Comments to Management (continued)

- Confirm that the vendor's personnel use unique user IDs and passwords when accessing the network and applications
- Routinely evaluate the Eagle and Lawson contracts and security agreements for compliance

#### *Management's Response*

We agree and will work in cooperation with our vendors to implement the suggested reviews.

#### **Logical Access Process – Administrative Users' Access**

We reviewed the access granted to specific accounts and access allowing extensive/administrator privileges (ability to add/modify/delete user access) and noted that the Director of Finance has inappropriate administrative access to the Lawson application, as he is also responsible for approving user access.

Administrative functions for the Eagle application are performed substantially by Siemens, the third party hosting the application. Siemens maintains constant access to the Corporation's production environment with administrative access into the application. However, we believe the number of user IDs with privileged '9' access into the Eagle application is excessive; a total of 61 accounts are owned by employees associated with the Corporation or Siemens. Further, a single employee is often granted multiple user accounts.

Inappropriate administrative access to the Lawson and Eagle application increases the risk of improper segregation of duties and unauthorized access to data files. This could affect the data integrity of the master data files and the completeness and accuracy of the reports generated and used for financial purposes.

Administrative user access should be limited to appropriate individuals on Lawson and Eagle applications. Further, logging of administrators access should be implemented, reviewed timely by an employee independent of the privileged access and maintained indefinitely.

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### Comments to Management (continued)

#### *Management's Response*

The Corporation's system security personnel will be instructed to perform a review of all Lawson and Eagle administrative access. Upon review access will be limited to those with a demonstrated need and whose other system functions do not present a security exception.

#### **Logical Access Process - User Access Requests /Mirroring of Current Users**

A formal process to request user access to the Eagle application is in place. A form is initially created, approved and routed to IT when access rights are requested for a new user, although the specific application-level authorities required for the user are not specified on this form. Rather, the administrator mirrors the user after another user with a similar job function.

Users possessing access privileges that are not needed for their job responsibilities could result in improper segregation of duties or unauthorized access to data files. Mirroring a user's access based on a current user, as opposed to a pre-defined (role based) user profile, allows the potential for additional or inappropriate access to be granted for a new user. Request documentation should be saved for future reference such that these requests can be referenced and reviewed, if necessary.

We recommend expanding the formal user access request process to include application-level authorities. IT should be provided with an "approver list" so that the IT function is not responsible for granting or modification of user access without proper approval from both the application administrator and the user's manager.

#### *Management's Response*

The IT department is in the process of hiring a resource whose skill set and experience include the management of user application security. This person will be tasked with creating the appropriate security request forms for each application. These forms, which will be completed by the user's manager, reviewed and signed off by the application administrator and approved by an appropriate manager who, depending on the situation may or may not be the user's direct report.

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### Comments to Management (continued)

#### **Logical Access Process – Periodic Review of User Access**

A periodic review of user access to confirm that only current (active) employees have the appropriate user access (based on job function) is not being performed. Without a periodic review of users and their assigned privileges, the potential for unauthorized access to critical data is increased.

Management should work with business process owners and application custodians to review the list of active users and their access levels on a pre-determined, periodic basis (e.g. quarterly). This review will help ensure that user access (and perimeters of entities allowed) levels are appropriate, thereby minimizing any known segregation of duties conflicts. Any users with inappropriate access should be immediately addressed and their profiles should be updated accordingly. Appropriate evidence, including initial review of user access, suggestion of user profile changes, and business process owner/application custodian sign off, should be retained.

#### *Management's Response*

Procedures will be put into place to monitor changes in user function and status as it affects system access. The previously mentioned IT resource will be responsible for confirming that these changes have taken place and for the periodic auditing of user access.

**Section 2**

**Summary of the 2007 Recommendations and Status**

In connection with our audit of the 2007 financial statements, we provided our management letter that included recommendations related to the ITGC environment. As part of our 2008 audit, we performed a review of the implementation of remediation actions related to our recommendations. The recommendations and the status summary are detailed below. For each issue noted, we have indicated whether the remediation plan has been:

- **Implemented** – Controls have been implemented; however, we did not test such controls for fiscal year 2007.
- **Partially Implemented** – Improvements have been put in place, but controls have not yet been fully implemented.
- **Not Implemented** – Controls have not been implemented.

Summary of 2007 Recommendations	Current Status	EY Comments
<p><b><i>Change Management Process</i></b>  <i>Documentation of Controls in Change Management Process (Systems Affected: Eagle and Lawson)</i></p>	<p>Not Implemented</p>	<p>A change management procedure is in place whereby changes to the Eagle and Lawson application are authorized, tested and approved. However, documentation of these key controls is not retained.</p> <p>This comment is noted above as a current observation for the 2008 fiscal audit.</p>
<p><b><i>Change Management Process</i></b>  <i>Outsourced Function Not Monitored (Systems Affected: Eagle and Lawson)</i></p>	<p>Eagle–Partially Implemented</p> <p>Lawson–Not Implemented</p>	<p>Eagle - Although the audit log of program files access by the vendor is reviewed on a quarterly basis, no formal evidence of the review is retained.</p> <p>Lawson – a process to monitor vendor activity in the production environment is not in place.</p> <p>This comment is noted above as a current observation for the 2008 fiscal audit.</p>

Summary of 2007 Recommendations	Current Status	EY Comments
<p><b><i>Change Management Process</i></b>  <i>Review of Program Changes After Implementation</i>  <i>(Systems Affected: Eagle and Lawson)</i></p>	Not Implemented	<p>A process to review program changes made to the Lawson and Eagle applications is not in place to verify whether only authorized changes were implemented.</p> <p>This comment is noted above as a current observation for the 2008 fiscal audit.</p>
<p><b><i>Logical Access Process</i></b>  <i>Administrative Users' Access (Systems Affected: Eagle and Lawson)</i></p>	Not Implemented	<p>Eagle - The vendor has administrative access to the application.</p> <p>Lawson - The Director of Finance is responsible for approving user access, and also is granted conflicting duty of user administration.</p> <p>This comment is noted above as a current observation for the 2008 fiscal audit.</p>
<p><b><i>Logical Access Process</i></b>  <i>Periodic Review of User Access (Systems Affected: Eagle and Lawson)</i></p>	Not Implemented	<p>A user access recertification process is not in place to periodically verify whether users access commensurate with their job functions.</p> <p>This comment is noted above as a current observation for the 2008 fiscal audit.</p>