



THE SCHOOL DISTRICT OF PALM BEACH COUNTY, FLORIDA

Management Letter

June 30, 2005



KPMG LLP
450 East Las Olas Boulevard
Fort Lauderdale, FL 33301

**Management Letter in Accordance With the
*Rules of the Auditor General of the State of Florida***

The Honorable Chairperson and Members of
The School District of Palm Beach County, Florida:

We have audited the financial statements of the School District of Palm Beach County, Florida (the School District), as of and for the fiscal year ended June 30, 2005, and have issued our report thereon dated November 18, 2005, which was modified to refer to our reliance on the reports of other auditors as it relates to the aggregate discretely presented component units.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States and with the provisions of Chapter 10.800, *Rules of Auditor General*. We have issued our Independent Auditors' Report on Internal Control over Financial Reporting and on Compliance and Other Matters which is dated November 18, 2005, and should be considered in conjunction with this management letter.

The *Rules of the Auditor General* (Section 10.804(1)(d)1.) require that we address in the management letter, if not already addressed in the auditors' reports on compliance and internal controls, whether or not recommendations made in the preceding annual financial audit report have been followed. The recommendations made in the preceding annual financial audit report have been corrected, except for those reported under the Status of Prior Years' Observations, Recommendations, and Management's Responses (Appendix B).

As required by the *Rules of the Auditor General* (Section 10.804(1)(d)4.), the scope of our audit included a review of the provisions of Section 218.415, Florida Statutes, regarding the investment of public funds. In connection with our audit, we determined that the School District complied with Section 218.415, Florida Statutes.

The *Rules of Auditor General* (Sections 10.804(1)(d)3. and 5.) require disclosure in the management letter of the following matters if not already addressed in the auditors' reports on compliance and internal controls: (1) violations of laws, rules, regulations, and contractual provisions that have occurred, or are likely to have occurred; (2) improper or illegal expenditures; (3) improper or inadequate accounting procedures; and (4) failures to properly record financial transactions. Our audit disclosed the matters required to be disclosed by the *Rules of the Auditor General* in Current Year's Observations, Recommendations, and Management's Responses (Appendix A).

As required by the *Rules of the Auditor General* (Section 10.804(1)(d)2.), the scope of our audit included a review of the provisions of Section 218.503(1), Florida Statutes, regarding financial emergencies. In connection with our audit, we determined that the School District is not in a state of financial emergency as a consequence of the conditions described in Section 218.503(1), Florida Statutes.



This management letter is intended solely for the information of the chairperson and board members, the audit committee, and management of the School District and the State of Florida Office of the Auditor General, and is not intended to be and should not be used by anyone other than these specified parties.

November 18, 2005

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Current Year's Observations, Recommendations, and Management's Responses

Summary

No.	Current year's observations
2005-1	Completeness of Information obtained from the Real Estate Department
2005-2	Accuracy of Schedules provided by Capital
2005-3	Reconciliation of Capital Outlay
2005-4	Disposition of Capital Assets

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Current Year's Observations, Recommendations, and Management's Responses

2005-1 Completeness of information obtained from the Real Estate Department

Observation

During the course of the audit, we noted that the District does not maintain adequate and complete records of historical land purchases. Upon further discussion with management, we learned that the Capital Asset Section is notified of real estate transactions through the use of "notice of site acquisition" or "notice of sale or transfer of real property" and that the capital asset section did not receive a particular notice and has no procedures in place other than inquiry to ensure all notices are received.

Recommendation

The real estate department should use pre-numbered forms and keep a control log of all forms used. The capital asset section can then perform a review to ensure they have received all of the notices for the current fiscal year. Such a reconciliation process will help to ensure the completeness of data and may enhance the financial reporting process.

Management's Response

Management concurs. Real Estate will develop a control log and use a sequential numbering series for all transactions (purchases, swaps, donations, and retirements). The control log will be provided periodically to the Accounting Department for Capital Assets to assure that all land transactions are properly recorded.

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2005-2 Accuracy of schedules provided by Capital Asset Department

Observation

During the course of the audit, we observed the land transaction schedule provided by the Capital Asset Section was not correct. Although the schedule included all land transactions, the Capital Assets Section only included the effect on the capital assets and did not reflect all relevant information, such as proceeds. In addition, the schedule did not provide an adequate description of the transactions. As a result, the GASB 34 entry that was record to account for the land transactions on the government-wide financial statements required adjustment.

Recommendation

The transaction summary should be expanded to include all information regarding transactions including proceeds, cost, gain/loss. The Capital Asset Section should develop a checklist to ensure that they have obtained all of the relevant information from the real estate department. In addition, the capital asset transactions should be discussed with capital asset section prior to recording the GASB 34 entry. This will ensure that the Accountant is properly accounting for the transactions.

Management's Response

Management concurs. Upon notification via control log prepared by the Real Estate Department, the Capital Assets Section will expand the land transaction schedule to include proceeds, gain or loss, and any additional information needed from Real Estate to help properly record the transactions on the District's books. The PeopleSoft ERP System has the capability to track proceeds, gains, and losses on individual land parcels, and the District intends to take full advantage of this feature.

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2005-3 Reconciliation of Capital Outlay

Observation

During the course of the audit, it came to our attention that a timely reconciliation is not performed between capitalized capital outlay and noncapital capital outlay. A detail of capital outlay expenditures is manually reviewed to determine capital versus noncapital expenditures. The final schedule of capitalized software did not include \$6 million in capitalizable software costs relating to the Peoplesoft acquisition. The current process results in a manual and time-consuming effort to compile the information at year-end with opportunity for human error.

Recommendation

The District should implement a process to reconcile capital and noncapital capital outlay. All schedules should be reviewed and agreed to supporting documentation prior to input into the financial statements. A process over reconciling capital outlay will help improve capital project's control over the School District's assets, and enhance management financial reporting process.

Management's Response

Management concurs. The reconciliation of capital versus non-capital expenditures is an improvement the District will realize from the implementation of the PeopleSoft ERP System. With regard to the specific PeopleSoft expenditures, the value of the PeopleSoft asset includes the software purchase plus the consulting fees for the implementation costs. The \$6 million represents implementation costs, which have been manually added to the software costs. Future consulting fees will be properly tracked and added to the value of the asset for fiscal year 2006 and until the PeopleSoft ERP System implementation is finalized.

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Current Year's Observations, Recommendations, and Management's Responses

2005-4 Disposition of Capital Assets

Observation

During the course of the audit, it came to our attention that fixed asset disposals are not being recorded in the correct period. The current procedure is to identify all assets to be disposed on a quarterly basis. This report is then presented to the audit committee at the first meeting subsequent to quarter end and then submitted to the Board for approval. The disposal is not recorded until Board approval is received. Therefore asset writeoffs for the quarter ended June 30, 2005 were not recorded until fiscal year 2006.

Recommendation

The District should develop a policy and procedure to prepare the disposal listing for the year ended June 30, on a timely basis and should accrue for the loss on disposal of assets during that fiscal year to ensure that the government wide financial statements are correct and reflect all known information.

Management's Response

Management concurs. The District intends to modify the current accounting practice with the implementation of the PeopleSoft ERP System. The current process has been in place for many years, and it has been consistently followed from year-to-year. Assets are batched for disposal and are retired from the fixed assets system after the Quarterly Disposal Report has been presented to the School Board for approval. However, with the implementation of the PeopleSoft ERP System, the District will modify the timing of the current procedure to record the asset retirements to the District's financial records as they occur. Asset disposals will be reported to the School Board subsequently.

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Status of Prior Years' Observations, Recommendations, and Management's Responses

Summary

<u>No.</u>	<u>Prior year's observations</u>	<u>Observation is still relevant</u>	<u>Observation addressed or no longer relevant</u>
1999-6	Maintaining General and Subsidiary Ledgers	X	
2001-6	Maximo – Operational Budget Monitoring	X	
2001-7	Direct Journal Entries into the TERMS System	X	
2001-8	Budgeting	X	
2001-9	Vendor Master Files	X	
2001-15	IT Operations	X	
2001-16	IT Security Controls	X	
2003-2	Access to Vendor Master File	X	
2004-1	Preparing Bank Reconciliations in a Timely Basis	X	
2004-2	Detail of Debt and Supporting Schedules	X	
2004-3	Market Value Adjustment	X	
2004-4	Reconciliation of Capital outlay	X	
2004-5	Review and Authorization of On-Line Time Records	X	

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1999-6 Maintaining General and Subsidiary Ledgers

Prior Year's Observation

During our review of the controls over the fixed assets of the School District, we noted that all subsidiary records are PC-based. The PC-based files cannot be interfaced with the School District's general ledger thereby necessitating a series of manual reconciliations when accounting for additions and deletions between the general ledger and the PC-based files. The manual process could result in a series of errors that if not detected could misstate the School District's financial statements.

Prior Year's Recommendation

We recommend the School District develop an automated interface between the subsidiary and the general ledger records to eliminate the potential for human error.

Prior Year's Status

This observation is still applicable in the current year. The fixed assets subsidiary records are still PC-based. See prior year's recommendation above.

Prior Year's Management's Response

We concur. The School District has completed a yearlong business system and functional process review that deals with the deficiencies noted. We are in the process of completing the readiness activities that are intended to lead to the issuance of a request for proposal (RFP), which will facilitate the acquisition of enterprise resource planning (ERP) software designed to address the limitations of the current system. Until a fully integrated system is implemented, this comment will continue to be relevant. Compensating controls include a manual reconciliation at year-end to adjust any differences.

2004 Status

This observation is still applicable in the current year. The capital assets subsidiary records are still PC-based.

2004 Management's Response

The School District's effort towards replacing its business systems and transforming our processes continues to move forward.

1. The District continues to make progress on several hundred specific enterprise resource planning (ERP) readiness items; the completion of which will strongly position the District for successful implementation of ERP software.
2. The District has undergone a thorough process to select ERP software. The District selected and the Board approved the acquisition of PeopleSoft software.

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3. The District is in the middle of a process to select an implementer to install and configure PeopleSoft software. We look forward to a winter 2005 implementation start date.
4. The District has established a new ERP Department where a dedicated project team has been assigned and works on an ongoing basis with functional areas to identify process change and define business rules.

We continue to believe the vast majority of findings/deficiencies related to process and/or systems issues will be addressed and corrected with the successful implementation of the new ERP software.

2005 Management's Response

The School District has contracted with the eVerge Group as the implementers of the PeopleSoft Enterprise Resource Planning System (ERP). To date, more than 120 processes have been identified and documented, covering the current way they are performed. In addition, new processes have been developed to address systemic and process issues, this one included. The new ERP system is planned to go-live on July 1, 2006 and will address the majority of these findings/deficiencies.

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Status of Prior Years' Observations, Recommendations, and Management's Responses**2001-6 Maximo – Operational Budget Monitoring*****Prior Year's Observation***

The budget within the Maximo subsidiary ledger system is split between capital projects and an operational budget. Although Maximo does provide for system spending controls for the capital projects budget, these controls are inactive for the operational budget. As a result, the capital projects budget is systematically monitored and reviewed on a regular basis while the operational budget requires additional reports generated in conjunction with the budget department to determine their budget to actual status. Furthermore, operational budget expenditures are not uploaded into the TERMS financial system real-time, but on a weekly basis as a direct journal entry resulting in delayed budgetary information for decision-making purposes. The capital projects budget is uploaded into the TERMS financial system as an encumbrance.

The lack of spending control and monitoring capability within Maximo pertaining to the operational budget may cause funds to be exceeded and go unnoticed. Additionally, the School District may have to find funds from other sources after expenditures have been made and increase the amount of budget transfers and budget amendments that require approval throughout the year. When the budget was adopted for the FY '01 there was \$25 million budgeted for maintenance within the operational budget. However, for salaries and supplies, the expenditures were exceeded throughout the year by approximately \$7.9 million. The budget was balanced monthly throughout the fiscal year by transferring most of the necessary funds from capital projects.

Prior Year's Recommendation

Management should consider the feasibility of one budgetary system to help ensure consistent application of spending controls, monitoring procedures, and the availability of timely information for the entire School District.

Prior Year's Management's Response

Management concurs. A review of business processes and systems will look specifically at this issue.

Prior Year's Status

This status has not changed although the operational budget is being monitored by Maintenance Department in conjunction with the Budget Department based on reports generated by the system.

Operational budget expenditures will be uploaded into the TERMS financial system on a daily basis in a few weeks.

Prior Year's Management's Response

The business system and functional process review has been completed. A key deliverable for this project is re-designed business processes that feature best management practices and strong internal controls. Re-designed business processes will address the need for integration and automation of operational and capital budgets as well as strong front end controls to prevent processing errors. In addition, we are in the process of completing the

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readiness activities that are intended to lead to the issuance of a request for proposal (RFP), which will facilitate the acquisition of enterprise resource planning (ERP) software designed to address the limitations of the current system.

2004 Status

Operational budget expenditures from the Maximo subsidiary ledger are now being uploaded into the TERMS financial system on a daily basis. This results in more timely information that facilitates decision-making.

2004 Management's Response

The School District's effort towards replacing its business systems and transforming our processes continues to move forward.

1. The District continues to make progress on several hundred specific enterprise resource planning (ERP) readiness items; the completion of which will strongly position the District for successful implementation of ERP software.
2. The District has undergone a thorough process to select ERP software. The District selected and the Board approved the acquisition of PeopleSoft software.
3. The District is in the middle of a process to select an implementer to install and configure PeopleSoft software. We look forward to a winter 2005 implementation start date.
4. The District has established a new ERP Department where a dedicated project team has been assigned and works on an ongoing basis with functional areas to identify process change and define business rules.

We continue to believe the vast majority of findings/deficiencies related to process and/or systems issues will be addressed and corrected with the successful implementation of the new ERP software.

2005 Management's Response

The School District has contracted with the eVerge Group as the implementers of the PeopleSoft Enterprise Resource Planning System (ERP). To date, more than 120 processes have been identified and documented, covering the current way they are performed. In addition, new processes have been developed to address systemic and process issues, this one included. The new ERP system is planned to go-live on July 1, 2006 and will address the majority of these findings/deficiencies.

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2001-7 Direct Journal Entries into the TERMS System

Prior Year's Observation

Direct journal entries conducted by the Accounting Department are not subject to system spending and balancing controls. The system edit checks have been deactivated which would prevent the posting of an unbalanced journal entry; however, the Accounting Department utilizes the journal listing and trial balance on a daily basis in order to detect funds and accounts that are out of balance. The entry of journal entries directly into the TERMS system that are not subject to spending and balancing controls, may result in unbalanced budgetary information and increase the reliance placed on manual review procedures.

Prior Year's Recommendation

Management should consider developing preventative system controls to help ensure that journal entries cannot be posted unless they are balanced.

Prior Year's Management's Response

Management concurs.

Prior Year's Status

Although the School District does utilize the panel to verify out of balance journal entries and a warning message is generated within that panel, the School District does not utilize error, edit, or exception reports to verify the data input of these direct journal entries.

Prior Year's Management's Response

The system is capable of accepting out of balance journal entries. However, the Accounting Department reviews, on a daily basis, "journal reports" that display debits and credits for transactions processed the previous business day. Exceptions are resolved immediately. This procedure is documented with the appropriate journal entry before it is filed.

The business system and functional process review has been completed. A key deliverable for this project is re-designed business processes that feature best management practices and strong internal controls. Online, real-time edits for spending controls and balancing controls will be addressed during the re-design of business processes that will be conducted during this review. In addition, we are in the process of completing the readiness activities that are intended to lead to the issuance of a request for proposal (RFP), which will facilitate the acquisition of enterprise resource planning (ERP) software designed to address the limitations of the current system.

2005 Status

This observation is still applicable in the current year.

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2004 Management's Response

The School District's effort towards replacing its business systems and transforming our processes continues to move forward.

1. The District continues to make progress on several hundred specific enterprise resource planning (ERP) readiness items; the completion of which will strongly position the District for successful implementation of ERP software.
2. The District has undergone a thorough process to select ERP software. The District selected and the Board approved the acquisition of PeopleSoft software.
3. The District is in the middle of a process to select an implementer to install and configure PeopleSoft software. We look forward to a winter 2005 implementation start date.
4. The District has established a new ERP Department where a dedicated project team has been assigned and works on an ongoing basis with functional areas to identify process change and define business rules.

We continue to believe the vast majority of findings/deficiencies related to process and/or systems issues will be addressed and corrected with the successful implementation of the new ERP software.

2005 Management's Response

The School District has contracted with the eVerge Group as the implementers of the PeopleSoft Enterprise Resource Planning System (ERP). To date, more than 120 processes have been identified and documented, covering the current way they are performed. In addition, new processes have been developed to address systemic and process issues, this one included. The new ERP system is planned to go-live on July 1, 2006 and will address the majority of these findings/deficiencies.

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2001-8 Budgeting

Prior Year's Observation

The School District utilizes three budgeting programs for the budgeting process:

- Resource allocation program for the schools
- Budget system for the remainder of the departments in the School District
- Capital projects reporting

Resource allocation formulas for the schools are approved by the School District's Board prior to entry by the IT Department into the system. Based on these formulas, the system calculates the resources for each school. The department allocation program is used to create a "snapshot" of the current year's budget for each of the School District's departments to use as the basis for next year's budget. A budget file is created and sent via batch job to the budget system. A variance report is generated that is reviewed by the schools and departments. Any subsequent changes have to be submitted in writing and are entered into the budget system manually by the Budget Department.

The Capital Projects Department utilizes a separate database to create, maintain and track their budget on a daily basis. Once the Capital Projects Department has established their budget for the new fiscal year, a hard copy is given to the Budget Department for manual entry into the budget system of the School District. When the budget has been approved it is converted into journal entries and uploaded into the TERMS financial system. Manual reviews are conducted throughout the entire process.

Maintaining two separate budget programs may result in incomplete or inaccurate data being transferred from these systems into the TERMS financial system. Extensive manual review procedures are required to minimize this risk and may result in additional budget processing support costs.

Prior Year's Recommendation

Management should consider integrating the capital project's budget program into the budget system in order to minimize the risk of incomplete or inaccurate data from being transferred into the financial system. In addition, management should evaluate options to automate the process for the schools and departments to enable the submission of budget requests and changes online and reduce the manual entry of changes and the extensive manual review currently being performed.

Prior Year's Management's Response

Management concurs. This issue will be specifically addressed as part of the business process and systems review that will begin as soon as a consultant to assist is selected.

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Prior Year's Status

This observation is still applicable in the current year. There has been no change pending the completion of the business process and systems review which started in fiscal year 2003.

Prior Year's Management's Response

The business system and functional process review has been completed. A key deliverable for this project is re-designed business processes that feature best management practices and strong internal controls. The budget development process is within the scope of this project. The re-design will address the integration, data integrity and automation issues discussed in this management comment. In addition, we are in the process of completing the readiness activities that are intended to lead to the issuance of a request for proposal (RFP), which will facilitate the acquisition of enterprise resource planning (ERP) software designed to address the limitations of the current system.

2004 Status

This observation is still applicable in the current year.

2004 Management's Response

The School District's effort towards replacing its business systems and transforming our processes continues to move forward.

1. The District continues to make progress on several hundred specific enterprise resource planning (ERP) readiness items; the completion of which will strongly position the District for successful implementation of ERP software.
2. The District has undergone a thorough process to select ERP software. The District selected and the Board approved the acquisition of PeopleSoft software.
3. The District is in the middle of a process to select an implementer to install and configure PeopleSoft software. We look forward to a winter 2005 implementation start date.
4. The District has established a new ERP Department where a dedicated project team has been assigned and works on an ongoing basis with functional areas to identify process change and define business rules.

We continue to believe the vast majority of findings/deficiencies related to process and/or systems issues will be addressed and corrected with the successful implementation of the new ERP software.

2005 Management's Response

The School District has contracted with the eVerge Group as the implementers of the PeopleSoft Enterprise Resource Planning System (ERP). To date, more than 120 processes have been identified and documented, covering the current way they are performed. In addition, new processes have been developed to address

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systemic and process issues, this one included. The new ERP system is planned to go-live on July 1, 2006 and will address the majority of these findings/deficiencies.

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2001-9 Vendor Master Files

Prior Year's Observation

There are three vendor master files currently being used by the School District: one is updated and maintained by the Accounts Payable Department in the TERMS financial system, another is a database in the Procurement Department utilized for electronically notifying vendors of bid opportunities, and the third is maintained by the Office of Diversity in Business Practices that works closely with the Procurement Department in certifying and promoting minority vendors. The TERMS Vendor Master File and the Office of Diversity Vendor Master file are currently synchronized through a real-time programming interface for vendor creation. Data fields unique to each file may not be synchronized. A decision to maintain a separate vendor master file for procurement and minority reporting purposes drove the development for two of these additional databases. Maintaining vendor master data in three separate files may result in incomplete or inaccurate data being utilized by the School District.

Prior Year's Recommendation

Management should implement procedures to help ensure that only one vendor master file is utilized and updated on a regular basis in order to avoid inaccurate data from being utilized and help ensure that all the data is centrally accessible.

Prior Year's Management's Response

Management concurs. This issue will be reviewed as part of the business process and systems review. The review will begin as soon as a consultant is selected to assist in conducting these reviews.

Prior Year's Status

Management has contracted CHAMPS software for minority vendors and is in the implementation process. Management contracted with Dunn & Bradstreet to match NAICS codes to School District vendors. IT staff has consolidated vendor information from the bid opportunities file (Purchasing) and the minority vendors file (ODBP) into one unique database in a client server environment.

Prior Year's Management's Response

Management concurs with the exception of NAICS codes that, upon further evaluation, were replaced with NIGP codes. NIGP codes align better with commodity definitions and are compatible with the CHAMPS software.

Prior Year's Status

Management has implemented the CHAMPS software for minority vendors. Management contracted with Dunn & Bradstreet to integrate the purchasing vendor master file with the Office of Business Diversity vendor master file into an Access database that only is accessible to authorized personnel within the Procurement Department and the Office of Business Diversity. This would incorporate approximately 6,000 vendors into one Access 2000 database file. Currently, there is no plan to integrate the vendors maintained within the TERMS system.

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Prior Year's Management's Response

Management concurs. A comprehensive database file currently exists and is utilized by the Purchasing and the Diversity In Business Practices Departments. This data is generated from the TERMS vendor file, which is downloaded into the CHAMPS system on a regular basis. In addition, the School District has completed a yearlong business system and functional process review that deals with the deficiencies noted. We are in the process of completing the readiness activities that are intended to lead to the issuance of a request for proposal (RFP), which will facilitate the acquisition of enterprise resource planning (ERP) software designed to address the limitations of the current system.

2004 Status

This observation is still applicable in the current year.

2004 Management's Response

The District is in the process of acquiring ERP software that will address the integration, data integrity and automation issues discussed in this management comment.

2005 Management's Response

The School District has contracted with the eVerge Group as the implementers of the PeopleSoft Enterprise Resource Planning System (ERP). To date, more than 120 processes have been identified and documented, covering the current way they are performed. In addition, new processes have been developed to address systemic and process issues, this one included. The new ERP system is planned to go-live on July 1, 2006 and will address the majority of these findings/deficiencies.

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2001-15 IT Operations

Prior Year's Observation

Security Policy and Procedures

- Documents outlining security procedures have been drafted for several systems including the financial, payroll, and personnel systems. Although some of the departments have developed security policies, a comprehensive School Districtwide policy that addresses security matters from a strategic perspective for the entire enterprise has not been created. The lack of an enterprisewide security policy allows for inconsistent procedures to be developed and potentially conflict with each other.

Security Awareness Program

- There is a limited security awareness program to educate employees on how to meet information security goals set by management. Employees and administrators are not regularly informed on security issues and procedures to make an efficient and effective response.

Security Strategy

- The current approach to security does not allow management to determine the proper response to incidents ahead of time, which would allow for appropriate and effective action.

Specific security measures and policies are rendered less effective because procedures are applied inconsistently throughout the School District. A strong security measure in one department or system can be rendered ineffective because of a weak control in a seemingly disparate or underlying area.

An inconsistent approach to implementing a security program may result in the treatment of controls on an independent basis, implementing incongruent controls, which are not interoperable with each other, and ultimately creating an unstable technology foundation. In addition, staff is constantly having to be re-trained on the disparate and new tools being introduced to the network.

Prior Year's Recommendation

- Management should consider creating a School Districtwide security policy to provide a benchmark for implementing enterprisewide controls and procedures, which effectively and consistently restrict and monitor system access.
- A more thorough and regularly scheduled School Districtwide security awareness program should be developed that leverages the security policy in order to effectively raise alertness on information asset safeguarding.
- Incident response procedures should be developed into a comprehensive. School Districtwide security program.

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Prior Year's Management's Response

Management concurs. Current security policies should be integrated into an enterprisewide security policy. Schools and departments are notified through School District bulletins, the official channel for communication of the School District.

Prior Year's Status

Partially resolved. Security Awareness is accomplished through the regular distribution of printed and emailed bulletins and "Awareness Reports" to the School District directors and school principals. All School District employees are required to sign an employment agreement that includes sections on drug free workplace, conviction affidavit, and computer acceptable use sections as part of their reappointment agreement. Comprehensive, School Districtwide incident response procedures still need to be developed.

Prior Year's Management's Response

Enterprisewide security procedures – Partially complete (ongoing). Current security policies will be integrated into enterprisewide security procedures for fiscal year 2003. Due to technology advancements this will be an ongoing process.

Prior Year's Status

Continued resource restraints have challenged the resolution to this issue. However, the School District is in the process of recruiting a Chief Technology Officer (CTO) for the purpose of leading in the forming of a framework to address IT infrastructure, resource and security needs. The goals of the newly formed position will include incorporating more effectively the existing dispersed security policy and awareness programs into an enterprisewide security policy and awareness program.

The recent virus outbreak which impacted the School District network for more than 24 hours highlights the need for a robust and focused security awareness and incident response program that educates the School District population on how to identify and effectively respond to security threats. The CTO will also be tasked with helping to ensure that the incident response procedures are aligned into an effective security program to adequately address risks to the School District IT infrastructure in a timely manner.

Resource and budget constraints have not been in line with the additional requirements imposed by the introduction of new schools and IT demands to the IT and network departments. These resource limitations do not allow for the alerting and response to incidents across the organization in a consistent, timely, and effective manner.

It is recommended that the new CTO position have sufficient involvement in the budgetary planning process to allocate sufficient resources to address vulnerabilities that place the School District network and systems at risk.

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Prior Year's Management's Response

The departments within the division will work closely with the CTO to develop a strategic security plan with appropriate funding and resources to help ensure that the risk of intrusion will be mitigated.

In addition, the School District has completed a yearlong business system and functional process review that deals with the deficiencies noted. We are in the process of completing the readiness activities that are intended to lead to the issuance of a request for proposal (RFP), which will facilitate the acquisition of enterprise resource planning (ERP) software designed to address the limitations of the current system.

2004 Status

The new Chief Technology Officer (CTO) for the Division of Information Technology has restructured the organization to place more emphasis on enterprise security.

2004 Management's Response

The Board approved the job description for the Director of Security on July 19, 2004. Once resources are in place, the security issues will be addressed.

2005 Management's Response

The District recruited a Director of Security. A strategic security plan was implemented and a Policy and Procedures manual prepared and presented to the Audit Committee on August 12, 2005. Security incidents are now handled and coordinated by the Information Security Department.

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Status of Prior Years' Observations, Recommendations, and Management's Responses

2001-16 IT Security Controls

Prior Year's Observation

Our review of the IT security controls indicated that:

- Management is redesigning the current network perimeter—the access points between the School District network and the Internet—in order to reduce the current risks to the School District network associated with externally initiated connections being answered by internal servers. Servers such as the email, web and domain name servers, should be located in a “buffer zone,” also known as a “demilitarized zone,” to reduce the exposure to internal network. With this design of the network perimeter, no traffic originating from the Internet or other untrusted networks would enter the internal School District network. Servers exposed to the Internet are contained in a separate logical network.
- Currently, the School District is utilizing the intrusion detection feature of the existing firewall (Microsoft Internet Accelerator server) to analyze suspected attacks. However, this is not considered an adequate intrusion detection system (IDS) solution as there are numerous types of attacks that the firewall is not designed to recognize. A separate IDS has not been deployed to assist management in discovering violations of the network perimeter. An IDS is a device (or application that runs on a server) that analyzes network traffic in “real time” and responds via alerts or other methods to possible breaches of the network perimeter.

Under the current network perimeter and firewall design, untrusted and unknown traffic is entering the School District network, increasing the risk of attacks to internal systems and decreasing the ability to detect them. Traffic to the network is not being monitored, and it is not possible to determine if or how frequently it is being attacked.

Prior Year's Recommendation

- Deploy the updated design of the perimeter network and the “demilitarized zone or DMZ.”
- Conduct an information security and risk assessment to determine the types of risk to the network. Specific recommendations to reduce the exposure can be evaluated from the results of such an assessment.
- Regular scans of both perimeter and internal systems should be performed using vulnerability assessment tools to confirm the effectiveness of the firewall and intrusion detection system.

Prior Year's Management's Response

Management concurs with the need for improved perimeter security as indicated by our pre-audit redesign and its deployment that is currently underway.

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Management concurs that conducting an information security and risk assessment would determine the types of risk to the network. However, the perimeter redesign and the recent overhaul of the McAfee Deployment Server mitigate the risk of exposure significantly. Specific recommendations to further reduce the exposure could be evaluated from the results of such an assessment. Therefore, this assessment will be conducted as resources (personnel and budget) become available.

Management concurs that regular scans of both perimeter and internal systems should be performed using vulnerability assessment tools to confirm the effectiveness of the firewall and intrusion detection system. This procedure will be developed and implemented subject to budget and manpower limitations.

Prior Year's Status

Partially resolved. The School District has purchased a second Microsoft ISA firewall to provide redundancy to its network perimeter control. The network perimeter design has been updated to include a DMZ where all public or Internet facing servers are placed. Additional steps toward network security will be taken which will include the installation of an IDS and regular network vulnerability scans.

Prior Year's Management's Response

Partially resolved. The School District has purchased a second Microsoft ISA firewall to provide redundancy to its network perimeter control. The School District is investigating more robust security firewall devices (currently piloting Netscreen's 500cs) and will deploy based on budget and resources. The network perimeter design has been updated to include a DMZ where all public or Internet facing servers are placed.

Additional steps toward network security will be taken which will include the installation of an IDS and regular network vulnerability scans.

Prior Year's Status

The School District has purchased a set of redundant firewall and content filtering appliances and implemented an architecture to address the weak network perimeter configuration from previous years.

As evidenced by strains placed on the majority of the School District by the recent virus, there is a need to create and adequately fund a program to assess the risks and to regularly test the security program and controls protecting the School District infrastructure.

Prior Year's Management's Response

The departments within the division will work closely with the Chief Technology Officer to develop a strategic security plan with appropriate funding and resources to assure risk of intrusion will be mitigated.

2004 Status

For two years the District has utilized Netscreen 500 which is an intrusion detection system (IDS) for the network perimeter.

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The new CTO for the Division of Information Technology has restructured the organization to place more emphasis on enterprise security.

2004 Management's Response

The Board approved the job description for the Director of Security on July 19, 2004. Once resources are in place, the security program and controls for protecting the School District's infrastructure will be enhanced. Trial systems being used for IDS & IPS include ENTERSYS-Dragon device and SNORT.

2005 Management's Response

The Information Security Department has successfully tested, implemented, and currently uses 24x7, a Cisco advanced Intrusion Prevention system at the gateway of our network. All attempt incidents are monitored and investigated.

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2003-2 Access to Vendor Master File

Prior Year's Observation

We noted that five employees have been granted access to change and update vendor master data within TERMS. Of those, four employees also have been granted access to enter invoices and issue checks within TERMS. In addition, changes to the vendor master file are not reviewed or monitored.

Lack of systemic controls to segregate setup and validation of payee information from payment execution may lead to unauthorized posting of transactions to the general ledger, unauthorized payments, unauthorized changes to master data, and limited ability to authenticate which employee performed or approved a transaction.

Prior Year's Recommendation

Staff should not be able to setup a new vendor or change existing vendor (payee) information and also make a payment to that vendor, without appropriate review by a second party to verify that the vendor is valid and the payment amount is correct based upon a valid invoice. Management should undergo an assessment of job roles and responsibilities and redefine existing user profiles to separate the role of validating vendor and payee information from that of executing disbursements within TERMS.

Prior Year's Management's Response

Management concurs. This recommendation has been addressed by eliminating the Supervisor of Accounts Payable and the Manager of Financial Services access to the Vendor Master File (VMF). There are only two employees with access to modify the VMF when granted and the system keeps track of the changes performed by each employee, including date and time. We requested a biweekly report of all changes performed by each of these employees to the VMF. This report is provided to the Supervisor of Accounts Payable on the following Monday to verify if changes were granted. Also, before any payment is performed, there is an audit process in place to verify correctness of disbursements. Please contact us if you need additional information or details.

In addition, the District has completed a yearlong business system and functional process review that deals with the deficiencies noted. We are in the process of completing the readiness activities that are intended to lead to the issuance of a request for proposal (RFP), which will facilitate the acquisition of enterprise resource planning (ERP) software designed to address the limitations of the current system.

2004 Status

There are only three employees with access to modify the VMF when granted and the system keeps track of the changes performed by each employee, including date and time. The Supervisor of Accounts Payable verifies if changes were granted on the Monday following the change.

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2004 Management's Response

The School District's effort towards replacing its business systems and transforming our processes continues to move forward.

1. The District continues to make progress on several hundred specific enterprise resource planning (ERP) readiness items; the completion of which will strongly position the District for successful implementation of ERP software.
2. The District has undergone a thorough process to select ERP software. The District selected and the Board approved the acquisition of PeopleSoft software.
3. The District is in the middle of a process to select an implementer to install and configure PeopleSoft software. We look forward to a winter 2005 implementation start date.
4. The District has established a new ERP Department where a dedicated project team has been assigned and works on an ongoing basis with functional areas to identify process change and define business rules.

We continue to believe the vast majority of findings/deficiencies related to process and/or systems issues will be addressed and corrected with the successful implementation of the new ERP software.

2005 Management's Response

The School District has contracted with the eVerge Group as the implementers of the PeopleSoft Enterprise Resource Planning System (ERP). To date, more than 120 processes have been identified and documented, covering the current way they are performed. In addition, new processes have been developed to address systemic and process issues, this one included. The new ERP system is planned to go-live on July 1, 2006 and will address the majority of these findings/deficiencies.

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Current Year's Observations, Recommendations, and Management's Responses

2004-1 Preparing Bank Reconciliations on a Timely Basis

Observation

During the course of the audit, we observed that bank reconciliations were not reconciled on a timely basis. As a result, a time-consuming effort was necessary to reconcile this account at year-end.

Recommendation

Reconciliations between the bank statements and the general ledger should be performed monthly. Reconciliations should be prepared in a standardized format, and all reconciling items should be fully explained and supported. The financial services supervisor should review the reconciliations and any adjusting journal entries and document approval by initialing the reconciliation. Timely and accurate bank reconciliations will improve accounting control over the School District's cash accounts, which will enhance the School District's financial reporting process.

2004 Management's Response

Management concurs. This fiscal year, the usual course of timely bank reconciliations was interrupted with the untimely departures of several key accounting personnel including the manager and the accountant in charge of the bank reconciliation process. Management recognizes the need for timely bank reconciliations as a control over the School District's cash accounts and agrees with all recommendations made. In order to grant that all reconciliations are prepared on a timely basis, the following steps have been taken:

1. The cross-training of accounting personnel to minimize the impact of personnel turnover on processes and procedures.
2. A review of current bank reconciliation procedures to identify opportunities and deficiencies within the process.
3. We are working in coordination with information technology in the implementation of automated bank reconciliation process to improve its accuracy and timeliness, following a standardized format.

2005 Management's Response

Some automation to the bank reconciliation process has been achieved through the use of direct data downloads from the Human Resources (CHIPS) system to Excel, eliminating the need for large paper reports and manual data input, which saved considerable time and increased the efficiency while researching differences. The School District has contracted with the eVerge Group as the implementers of the PeopleSoft Enterprise Resource Planning System (ERP). To date, more than 120 processes have been identified and documented, covering the current way they are performed. In addition, new processes have been developed to address systemic and process issues, this one included. The new ERP system is planned to go-live on July 1, 2006 and will address the majority of these findings/deficiencies.

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2004-2 Detail of Debt and Supporting Schedules

Observation

The Treasury Department tracks debt and related accounts (such as, accrued interest payable, cost of issuance, and derivatives) through the use of Excel spreadsheets. During the course of the audit, we observed several mistakes (such as, mathematical and calculation errors) related to the debt calculations on these spreadsheets. This current process is a manual and time-consuming effort to compile the information at year-end and exposes the District to human error.

Recommendation

The debt schedules should be reviewed, agreed to supporting documentation, and the calculations verified prior to input into the financial statements. The schedules should be prepared in a standardized format and a check figure should be added to help ensure all schedules are mathematically correct. A standardized schedule will improve the treasury's control over the School District's debt, which will enhance management's ability to make informed decisions.

2004 Management's Response

Management concurs. The Treasury Department plans to replace the current investment management program, Evare, with a more robust program that will also handle debt issues. The new program will provide standard reports for all debt and investments.

2005 Management's Response

During Fiscal Year 2005, the Treasury Department entered into a lease contract for Sympro, an investment and debt management program. The program was successfully installed and is currently used to track all investment and debt issues. The program eliminated much of the manual tracking related to debt issues and has greatly improved the reporting capabilities of the District.

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2004-3 Market Value Adjustment

Observation

During the course of the audit, we noted that the fair market value adjustment computed by the Treasury Department staff was not in accordance with Government Accounting Standards Board (GASB) No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. During the current year, the Treasury Department staff calculated the fair market value adjustment manually and it contained an error. The error resulted in an understatement of investments which the District deemed to be insignificant.

Recommendation

The District should develop and establish a process and procedures to help ensure the fair market value adjustment is properly recorded. Such a process over recording the fair market value adjustment will improve the Treasury Department's internal control over the School District's investment accounts, which will enhance the financial reporting process.

2004 Management's Response

Management concurs. The Treasury Department did utilize the investment management program, Evare, to prepare the GASB 31 report. However, the software calculates the adjustment based on purchased price rather than the amortized cost. As the District is recording investments based on the amortized cost, the calculation of the investment management program is no longer accurate and cannot be easily modified resulting in the manual calculation. The Treasury Department plans to install a more robust investment management program that will allow the calculation to be modified based on current reporting procedures.

2005 Management's Response

During Fiscal Year 2005, the Treasury Department entered into a lease contract for Sympro, an investment and debt management program. The program was successfully installed and is currently used to track all investment and debt issues. Additionally, it was determined that the best method to calculate market value adjustments was to compare carrying cost of the investments to the current market value.

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Current Year's Observations, Recommendations, and Management's Responses**2004-4 Reconciliation of Capital Outlay*****Observation***

During the course of the audit, it came to our attention that a timely reconciliation is not performed between capitalized capital outlay and noncapital capital outlay. A detail of capital outlay expenditures is manually reviewed to determine capital versus noncapital expenditures. The final schedule of capitalized construction in progress did not include \$29 million in capitalizable construction costs for a school put into service in August 2004. The current process results in a manual and time-consuming effort to compile the information at year-end with opportunity for human error.

Recommendation

The District should implement a process to reconcile capital and noncapital capital outlay. All schedules should be reviewed and agreed to supporting documentation prior to input into the financial statements. A process over reconciling capital outlay will help improve capital project's control over the School District's assets, and enhance management financial reporting process.

2004 Management's Response

Management concurs. At the close of each fiscal year, the detailed capital outlay expenditures are manually reviewed by the staff in Treasury/Capital Projects to determine capital versus noncapital expenditures. This manual and time-consuming process is fraught with the possibility of human error. Consequently, the final schedule of capitalized construction in progress did not include approximately \$29 million in capitalizable construction costs for a school put into service in August 2004. The implementation of the newly acquired software for the ERP system should eliminate the manual process currently utilized to categorize expenditures within the capital budget. In the meantime, the Treasury/Capital Projects staff will incorporate a reconciliation between capitalized capital outlay and noncapitalized capital outlay into the current manual process, and the capitalizable costs will be reclassified in the financial statements and added to the schedule of construction in progress.

2005 Management's Response

The School District has contracted with the eVerge Group as the implementers of the PeopleSoft Enterprise Resource Planning System (ERP). To date, more than 120 processes have been identified and documented, covering the current way they are performed. In addition, new processes have been developed to address systemic and process issues, this one included. The new ERP system is planned to go-live on July 1, 2006 and will address the majority of these findings/deficiencies. The reconciliation of capital versus non-capital expenditures is an improvement the District will realize from the implementation of the PeopleSoft ERP System.

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2004-5 Review and Authorization of On-line Time Records

Observation

During the course of the audit, we observed that Principals do not always document their review and authorization of the online employee time record.

Recommendation

We recommend Principals explicitly evidence their review in the payroll system. The documentation of the review and authorization of the online employee time record will provide evidence that employee is compensated for the correct number of hours worked and that labor hours are being allocated to proper jobs.

2004 Management's Response

Management concurs. The majority of the Principals do approve their payroll timely, however, we could have some that do not meet this deadline. We are going to reactivate the procedure of sending notice to the locations that do not approve their payroll timely, with a copy to the Area Offices. The notice will also request the Principal to send an email to the Payroll Manager, certifying that they have reviewed the payroll and approved it.

2005 Management's Response

The reactivation of our procedure of sending notices to locations that do not approve their payroll timely, with copy to the Area Offices, was very successful. The number of instances of delayed or non-approvals have reduced drastically. In addition the School District has contracted with the eVerge Group as the implementers of the PeopleSoft Enterprise Resource Planning System (ERP). To date, more than 120 processes have been identified and documented, covering the current way they are performed. In addition, new processes have been developed to address systemic and process issues, this one included. The new ERP system is planned to go-live on July 1, 2006 and will address the majority of these findings/deficiencies.