June 11, 2004

Mr. Ron D. Ross, Treasurer  
State of Nebraska  
P.O. Box 94788  
Lincoln, Nebraska 68509-4788

Dear Mr. Ross:

We have audited the basic financial statements of the state of Nebraska (the State) for the year ended June 30, 2003, and have issued our report thereon dated June 11, 2004. In planning and performing our audit, we considered the State’s internal controls in order to determine our auditing procedures for the purpose of expressing our opinion on the basic financial statements. An audit does not include examining the effectiveness of internal control and does not provide assurance on internal control. We have not considered internal control since the date of our report.

In connection with our audit described above, we noted certain internal control matters related to the activities of the Treasurers’ Office (the Agency) and other operational matters that are presented below for your consideration. These comments and recommendations, which have been discussed with the appropriate members of Agency management, are intended to improve internal control or result in other operating efficiencies.

Our consideration of internal control included a review of prior year comments and recommendations. To the extent the situations that prompted the recommendations in the prior year still exist, they have been incorporated in the comments presented for the current year. All other prior year comments and recommendations have been satisfactorily resolved.

Our comments and recommendations for the year ended June 30, 2003 are shown on the following pages.
1. **Cash in Bank Not on the State’s Accounting System**

   At year end, the Department of Administrative Services (DAS) posts an adjustment to record cash and investments not recorded on the State’s accounting system by the Nebraska Brand Committee. Although there are exceptions, State statutes require all cash be processed through the Treasurer’s Office. To reduce the risk of error, misappropriation of assets, and to ensure compliance with State statutes, we recommend the State develop procedures to ensure all cash is properly processed by the Treasurer’s Office and recorded on the State’s accounting system. We encourage both agencies to work together to develop procedures that address this risk; for example, send confirmations to banks to verify all accounts are on the State’s accounting system.

2. **Pledged Collateral**

   In accordance with LB1274, section 9, if a bank or capital stock financial institution designated as a depository furnishes securities pursuant to the Public Funds Deposit Security Act, the custodial official shall not have on deposit in such depository any public money or public funds in excess of the amount insured by the Federal Deposit Insurance Corporation, unless and until the depository has furnished to the custodial official securities, the market value of which are in an amount not less than 102 percent of the amount on deposit that is in excess of the amount so insured. On March 25, 2003, $18,086,775 of deposits at a financial institution were not collateralized as required by the above statute. The Agency has monitoring procedures in place; however, the procedures do not ensure compliance with these statutes on a daily basis.

   Cash balances can fluctuate significantly from day to day, requiring more frequent monitoring than is currently being performed by the Agency. The Agency is not consistently in compliance with this statute. We encourage the Agency to implement procedures necessary to ensure consistent compliance with this statute.

3. **Cash Reconciliation**

   The preparation of reconciliations between the actual bank statements and the accounting records (NAS) and the related disposition of reconciling items is an essential element of control in safeguarding cash and providing accurate interim and annual financial information.

   The State has an established reconciliation process in place; however, the following areas need to be addressed:

   - The variance shifts from month to month, which still indicates unknown reconciling items continue to exist. As of June 30, 2003, the unreconciled variance between the bank balances and the State’s accounting records was $3,654,783, which indicates that the cash balance per the State’s accounting records is overstated.

   - No adjustment has been made for the portion of the variance that is due to prior errors.
- No adjustments have been made for the carryover reconciling items related to the Investment Council.

- Although a reconciliation is being performed, some reconciling items are not posted to the general ledger at year end.

- The reconciliations are not being performed or reviewed in a timely manner.

- Monitoring and developing procedures to capture reconciling activity from new systems. The SDU also has an unreconciled amount in addition to the above of approximately $1.9 million.

- Developing an automated daily reconciliation process.

Unknown reconciling items continue to exist which increases the risk of future variance increases. Interim cash reports produced by NIS and annual financial statements may not accurately reflect the State’s cash balance, which may lead to errors in the managerial decision-making process.

We encourage the Agency to work with DAS to help investigate the shift in the variance caused by the implementation of a new system at the Agency. In addition, we encourage the Agency to provide other reconciling information in a timely manner to help reduce the amount of time required to complete the reconciliation process. We recommend the State continue to investigate the shift in the variance to determine the cause and establish policies and procedures related to posting adjustments in a timely manner to ensure cash is accurately reported. We also recommend that the reconciliations be prepared in a timely manner and someone other than the preparer review them shortly after completion. Finally, we recommend the State investigate and begin the implementation of a systematic on-line reconciliation process by utilizing the capabilities of the new accounting system. The implementation of an on-line reconciliation process would further require that the Treasurer’s current manual ledger be maintained on-line.

4. **Formalization of Policies and Procedures**

We recommend the Agency develop a formalized policies and procedures manual to ensure consistency of accounting applications, training of accounting and program personnel, and to ensure all personnel are aware of their respective responsibilities and duties.

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Our audit procedures are designed primarily on a test basis and, therefore, may not bring to light all weaknesses in policies or procedures that may exist. Our objective is, however, to use our knowledge of the Agency and its interaction with other State agencies and administrative departments gained during our work to make comments and suggestions that we hope will be useful to you.
We would be pleased to discuss these comments and recommendations with you at any time.

This report is intended solely for the information and use of the Auditor of Public Accounts, the Governor and members of the Legislature, Treasurer’s Office, and management of the state of Nebraska, and is not intended to be, and should not be used by anyone other than these specified parties.

We appreciate and thank all of the Treasurer’s Office employees for the courtesy and cooperation extended to us during our audit.

Very truly yours,

KPMG LLP