

**MANAGEMENT LETTER
OF THE
NEBRASKA DEPARTMENT OF
ENVIRONMENTAL QUALITY
DRINKING WATER
STATE REVOLVING FUND PROGRAM
JULY 1, 2003 THROUGH JUNE 30, 2004**

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Issued on June 1, 2005

STATE OF NEBRASKA AUDITOR OF PUBLIC ACCOUNTS



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Dear Mr. Linder:

Pat Reding, CPA
Asst. Deputy Auditor
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We have audited the financial statements of the Nebraska Department of Environmental Quality (Department) – Drinking Water State Revolving Fund Program (Program) as of and for the year ended June 30, 2004, and have issued our report thereon dated April 25, 2005. We have also issued a Report on Compliance and on Internal Control Over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*, dated April 25, 2005 and a Report on Compliance and on Internal Control Over Compliance with Requirements Applicable to the Nebraska Department of Environmental Quality – Drinking Water State Revolving Fund Program in Accordance with *U.S. Environmental Protection Agency Audit Guide for Clean Water and Drinking Water State Revolving Fund Programs*.

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In planning and performing our audit, we considered the Program's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting, and on the Program's compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts.

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We noted certain matters involving the internal control over financial reporting and other operational matters that are presented here. Comments and recommendations are intended to improve the internal control over financial reporting, ensure compliance, or result in operational efficiencies.

Our Comments and Recommendations for the Program for the fiscal year ended June 30, 2004 are included on pages 4 and 5.

This letter is intended solely for the information and use of the Department, the appropriate Federal and regulatory agencies, and citizens of the State of Nebraska, and is not intended to be and should not be used by anyone other than these specified parties. However, this letter is a matter of public record and its distribution is not limited.

Sincerely,

Pat Reding, CPA

Pat Reding
Assistant Deputy Auditor

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY
DRINKING WATER STATE REVOLVING FUND PROGRAM

SUMMARY OF COMMENTS

During our audit of the Nebraska Department of Environmental Quality – Drinking Water State Revolving Fund Program, we noted certain matters involving the internal control over financial reporting and other operational matters which are presented here.

1. **Accounting Records:** Certain information on the Department's financial statements could not be reconciled to the Nebraska Information System (NIS) or agency records. Also, prior year adjustments were not corrected.
2. **Loan Records:** Loans were not properly accounted for on NIS. Loans receivable at June 30, 2004 per NIS were \$53,302,451, however, the Department's internal records showed loans receivable of \$47,253,732. The amount of loans overstated in NIS at June 30, 2004 was \$6,048,719.
3. **Financial Status Reports:** The financial status report for Grant #FS997805-02 for the Federal fiscal year ended September 30, 2004 did not agree to supporting documentation. The Federal share was understated and the State share was overstated by \$315,685.

More detailed information on the above items is provided hereafter. It should be noted this report is critical in nature since it contains only our comments and recommendations on the areas noted for improvement.

Draft copies of this letter were furnished to the Department to provide them an opportunity to review the letter and to respond to the comments and recommendations included in this letter. All formal responses received have been incorporated into this letter. Where no response has been included, the Department declined to respond.

We appreciate the cooperation and courtesy extended to our auditors during the course of the audit.

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY
DRINKING WATER STATE REVOLVING FUND PROGRAM

COMMENTS AND RECOMMENDATIONS

1. Accounting Records

NIS was established to be the official accounting system of the State of Nebraska. Sound accounting practices and good internal controls require information reported on the financial statements to reconcile to accounting records. Prior year adjustments should also be corrected. Good internal control requires procedures be established to ensure journal entries are properly recorded.

Loans receivable reported on the financial statements did not reconcile to the Department's records by \$70,689. Prior year financial statements included \$78,814 in cash and cash equivalents for transactions that were not corrected on NIS until the current fiscal year. The Department did not adjust the current year financial statements to correctly reflect the prior year transactions. It was noted during the fiscal year 2003 audit that the cash and cash equivalents on the accounting system were \$26,169 more than were reported on the balance sheet. This adjustment had still not been corrected on accounting records. We also noted transactions that increased or reduced cash when the transaction should not have affected the cash account. Journal entries which did not balance created an automatic entry to post against the cash account. The net effect was a reduction in cash by \$46,390. Similar findings have been noted in the three previous audits.

While variances are small in relation to the entire Program balance, it is important to reconcile Program activity as recorded on NIS in order to ensure all of the Program's activity was properly recorded and accounted for.

We recommend the Department reconcile the activity recorded on the financial statements to actual activity recorded on NIS and make any adjustments necessary. In addition, we recommend the Department correct prior year adjustments and reverse prior year entries.

2. Loan Records

Good internal controls require that all loan activity be recorded on NIS.

Loan activity was not properly accounted for on NIS. Loans receivable at June 30, 2004 per NIS were \$53,302,451, however, the Department's internal records showed loans receivable in the amount of \$47,253,732. The amount of loans overstated in NIS was \$6,048,719, which resulted in the accounting system showing incorrect financial information. A similar finding was noted in the prior report.

We recommend the Department record all loan activity on NIS.

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY
DRINKING WATER STATE REVOLVING FUND PROGRAM

COMMENTS AND RECOMMENDATIONS

(Continued)

3. Financial Status Reports

Sound accounting practice requires supporting documentation agree to the required Federal reports submitted.

One of two financial status reports tested did not agree to NIS and supporting documentation. The financial status report for grant #FS997805-02 for the Federal fiscal year ended September 30, 2004 did not agree to supporting documentation. The cumulative amount reported was accurate but the Federal share was understated and the State share was overstated by \$315,685. This resulted in inaccurate reporting on the financial status reports.

We recommend the Department ensure the amounts reported on the financial status reports agree to NIS and supporting documentation.