MANAGEMENT LETTER
OF THE
NEBRASKA STATE COLLEGE SYSTEM

JULY 1, 2006 THROUGH JUNE 30, 2007

Issued on December 11, 2007

NEBRASKA AUDITOR OF PUBLIC ACCOUNTS

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State Auditor

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December 10, 2007

Mr. Stanley Carpenter, Chancellor
Nebraska State College System
Board of Trustees
P.O. Box 94605
Lincoln, NE 68509-4605

Dear Mr. Carpenter:

We have audited the basic financial statements of the Nebraska State College System (NSCS) for the fiscal year ended June 30, 2007, and have issued our report thereon dated December 10, 2007. We have also audited the NSCS's compliance with requirements applicable to major federal award programs and have issued our report thereon dated December 10, 2007. In planning and performing our audit, we considered the NSCS's internal controls in order to determine our auditing procedures for the purpose of expressing our opinions on the basic financial statements of the NSCS and to report on internal control in accordance with Office of Management and Budget (OMB) Circular A-133 and not to provide assurance on internal control. Internal control and compliance matters required by *Government Auditing Standards* and OMB Circular A-133 were reported in the above reports. The matters disclosed in this letter are not required to be reported in the above reports but are matters for NSCS's consideration. We have not considered internal control since the date of our reports.

As noted above, in connection with our audit, we noted certain matters involving the internal control over financial reporting and other operational matters which are presented below for your consideration. These comments and recommendations, which have been discussed with appropriate individuals at the NSCS Office, Chadron State College (CSC), Peru State College (PSC), and Wayne State College (WSC), are intended to improve the internal control over financial reporting, ensure compliance, or result in increased operational efficiencies.

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

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

Also included in this letter is a listing of Governmental Accounting Standards Board (GASB) Statements which may have an effect on future financial statements of the NSCS. These GASB Statements are provided for the NSCS's future consideration.

1. Academic Competitiveness Grant (ACG) Eligibility - Chadron State College

34 CFR Section 691.15 states that to be eligible for an Academic Competitiveness Grant (ACG) a student must be in their first or second academic year of an eligible program. In addition, 34 CFR Section 691.62 establishes the maximum ACG award as up to $750 for the first academic year of a student's eligible program, and up to $1,300 for the second academic year of a student's eligible program. Lastly, good internal control requires adequate training, education, and oversight of student financial aid packaging to ensure compliance with aid requirements.

Two of three students tested who received an ACG award were ineligible for such awards. In both instances, CSC had posted $1,300 second-year ACG grant awards ($650 for the Fall 2006 semester and $650 for the Spring 2007 semester) to the students' accounts despite the students having entered their third academic year at the start of the Spring 2007 semester; a point at which they would no longer have been eligible for a second-year ACG grant award. Subsequent to audit identification of these exceptions, CSC's Financial Aid staff promptly adjusted both students' 2006-2007 financial aid packages so that neither student would be over-awarded aid.

Following this issue being brought to their attention by the auditors, the CSC's Financial Aid staff reviewed all 26 second-year Spring 2007 ACG grant awards and determined a total of 15, or approximately 58% of students who had received ACG awards were ineligible based on their academic year completion. The CSC's Financial Aid staff indicated the involved students' 2006-2007 financial aid packages were promptly adjusted so no students would be over-awarded aid.

When the CSC does not award student financial aid in compliance with Federal grant requirements there is an increased risk of aid disbursements to ineligible students as well as aid over-award.

> We recommend CSC strictly enforce financial aid eligibility criteria as set forth in Federal regulations. We further recommend when implementing new student financial programs CSC have more than one individual involved in the process to ensure compliance with Federal student financial aid requirements.

NSCS's Response: Chadron State College agrees with the APA that further training and oversight of this grant is necessary. The College has already implemented additional procedures to insure that this problem does not occur again.

2. Perkins Exit Interviews and Repayment Plan - Chadron State College

34 CFR Section 674.42 (a) requires colleges to disclose to borrowers a repayment schedule for their Perkins loans including the date the first installment is due and the number, amount, and frequency of required payments. In addition, 34 CFR Section 674.42 (b), regarding exit interviews, requires schools to conduct exit counseling with each borrower in person, by audiovisual presentation or by interactive electronic means. If borrowers withdraw from school without the school's prior knowledge or fail to complete an exit counseling session as required, the school must provide exit counseling through either interactive electronic means or by mailing

counseling materials to the borrower at their last known address. Lastly, 34 CFR Section 674.42 (b) requires colleges to maintain documentation substantiating their compliance with these exit requirements for each borrower.

Testing of 13 Perkins loan borrowers in default and 11 Perkins loan borrowers entering repayment status noted the following:

- Three Perkins loan borrowers in default did not have adequate documentation of CSC having conducted or attempted to conduct borrower exit interviews; and

- One borrower had signed a $2,400 repayment plan when the amount actually owed totaled $2,700.

Noncompliance with the many aspects of Perkins loan due diligence, including adequate documentation of borrower exit interviews as well as signing of complete and accurate repayment plans by borrowers, increases the risk of delinquent loan amounts.

> We recommend CSC adequately document exit interviews, including those attempted by electronic means or mailing, for all Perkins borrowers. We also recommend CSC implement procedures to ensure all Perkins loan repayment plans signed by borrowers are complete and accurate.

NSCS's Response: Federal guidelines do require the College to maintain documentation substantiating contact of a student for an exit interview; however, there is no guidance as to what constitutes adequate documentation. The College will continue to work with the APA to satisfy concerns on this topic. Additional review of repayment plans will be conducted to reduce the chance of repeating the signing of incorrect documents.

3. NIS Leave Balances - Chadron State College, System Office

Nebraska State Accounting Manual, AM-005, Unused Leave Recorded in NIS Policy, Section 34 states, "State Accounting has adopted the Nebraska Information System (NIS) to record all earned but not used sick and vacation leave and compensatory time …." State Accounting needs this data in the NIS system in order to verify the dollar amount of earned but unpaid days when employees leave State employment. If an agency does not input leave data into NIS, it is the State of Nebraska's policy to consider such liability not to exist. As a result, when any employee leaves State government, no payment is to be allowed for claimed unused vacation, sick, or compensatory leave time until proper accounting for such leave is provided.

While employee vacation, sick, and compensatory leave activity for both the NSCS Office and CSC employees was recorded on NIS, it was not complete and accurate. Instead of using NIS as the system of origination for maintaining true employee leave balances, both the NSCS Office and CSC maintained their own separate, comprehensive leave records which were used for financial reporting purposes. Management of the NSCS Office and CSC indicated these separate leave records were necessary due to technical issues with NIS not recording leave activity completely or accurately for their employees.

The use of dual employee leave records increases the risk of errors and/or omissions. In addition, inaccurate NIS balances could lead to employee confusion when reviewing their pay stubs on which the NIS leave balances are reported.

> We recommend the NSCS Office and CSC work with the Nebraska Department of Administrative Services to resolve any technical issues they may have with being able to completely and accurately record employee leave activity on NIS.

NSCS's Response: The accrual of leave balances is accomplished by maintaining a set of records separate from the NIS System. Employees are informed that the balances reflected on their pay stubs are not correct. Leave reports are generated from the separate system and are provided to employees periodically. The accruals recorded in the audit are done from the separate system. The System Office has requested the establishment of a new leave table that will allow all System Office employees to accurately accrue leave in NIS. Currently, however, NIS does not properly accrue leave balances for certain groups of employees at the Colleges and the manual override of incorrect data is time-intensive. It is very likely that this issue will be resolved with the implementation of new human resources/payroll software by December 31, 2011.

4. <u>NIS Security - Chadron State College</u>

Good internal control requires functional accounting system access only be assigned to employees with a logical, work-related need for such access. For example, fixed asset or accounts payable functionality should be limited to employees whose work responsibilities include those functions.

During our review of NIS Security, we noted the following:

- Two individuals involved in the payroll process have functional NIS Accounts Payable access despite not being involved in the accounts payable process;
- Six individuals have functional NIS Fixed Asset access despite only one CSC employee being directly involved in the fixed asset process; and
- Eight individuals have functional NIS Accounts Receivable access despite only four individuals being directly involved in the accounts receivable process.

When individuals are assigned functional accounting system access without a logical, work-related need for such access, there is an increased risk of error.

> We recommend CSC periodically review its NIS security to ensure functional accounting system access is only assigned to individuals with a logical, work-related need for such access.

NSCS's Response: Through Chadron State College's Pandemic Flu planning process, recommendations are made to increase cross training and access to deal with the expected high rate of illness (expect up to 40% absenteeism). The flexibility needs to remain at the college level to determine what constitutes sufficient cross training and backup for any position. However, per this recommendation, Chadron State will review NIS Security periodically.

In addition to the above comments and recommendations we also noted two other internal control and compliance matters, Perkins Loan Grace Period Contacts and IT Segregation of Duties, which were reported in the audit reports Schedule of Findings and Questioned Costs.

GASB Standards for the NSCS's Future Consideration

The NSCS should review and determine the applicability of the following GASB Statements which may have an effect on the financial statements of the NSCS for the year ending June 30, 2008.

GASB has issued Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, effective for fiscal years beginning after December 15, 2006. This Statement establishes uniform financial reporting standards for other postemployment benefits (OPEB) plans and supersedes the interim guidance included in Statement No. 26, *Financial Reporting for Postemployment Healthcare Plans Administered by Defined Benefit Pension Plans.* The approach followed in this Statement generally is consistent with the approach adopted in Statement No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*, with modifications to reflect differences between pension plans and OPEB plans.

GASB has issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions,* effective for fiscal years beginning after December 15, 2007. This Statement provides standards for the measurement, recognition, and display of other postemployment benefit expenditures, assets, and liabilities, including applicable note disclosures and required supplementary information.

GASB has issued Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues,* effective for fiscal years beginning after December 15, 2006. This Statement established criteria that governments will use to ascertain whether the proceeds received should be reported as revenue or as a liability. The criteria should be used to determine the extent to which a transferor government either retains or relinquishes control over the receivables or future revenues through its continuing involvement with those receivables or future revenues.

GASB has issued Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations,* effective for fiscal years beginning after December 15, 2007. This Statement establishes standards for accounting and financial reporting for pollution remediation obligations, which are obligations to address the current or potential detrimental effects of existing pollution by participating in pollution remediation activities such as site assessments and cleanups.

GASB has issued Statement No. 50, *Pension Disclosures an amendment of GASB Statements No. 25 and No. 27*, effective for fiscal years beginning after June 15, 2007, except for requirements related to the use of the entry age actuarial cost method for the purpose of reporting a surrogate funded status and funding progress of plans that use the aggregate actuarial cost method, which are effective for periods for which the financial statements and required supplementary information (RSI) contain information resulting from actuarial valuations as of June 15, 2007, or later. This Statement more closely aligns the financial reporting requirements for pensions with those for OPEB and, in doing so, enhances information disclosed in notes to financial statements or presented as RSI by pension plans and by employers that provide pension benefits.

GASB has also issued Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*, effective for fiscal years beginning after June 15, 2009, with provisions for this statement generally required to be applied retroactively. The objective of this Statement is to establish accounting and financial reporting requirements for intangible assets to reduce inconsistencies in the accounting and financial reporting of intangible assets among state and local governments, particularly in the areas of recognition, initial measurement, and amortization and thereby enhance the comparability of the accounting and financial reporting of intangible assets among state and local governments.

This letter is intended solely for the information and use of management, the Board of Trustees, others within the Nebraska State College System, the appropriate Federal and regulatory awarding agencies, and pass-through entities 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 Nebraska State College System employees for the cooperation and courtesy extended to us during the course of the audit.

Sincerely,

Don Dunlap CPA

Don Dunlap
Assistant State Auditor