NEBRASKA AUDITOR OF PUBLIC ACCOUNTS

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February 17, 2009

Catherine Lang, Commissioner
Nebraska Department of Labor
550 South 16th Street
Lincoln, NE 68509-4600

Dear Ms. Lang:

We have audited the basic financial statements of the State of Nebraska (the State) for the year ended June 30, 2008, and have issued our report thereon dated December 19, 2008. We have also audited the State's compliance with requirements applicable to major Federal award programs and have issued our report thereon dated February 10, 2009. 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 opinions on the basic financial statements of the State and on the State's compliance with requirements applicable to major programs, and to report on internal control in accordance with the Federal Office of Management and Budget (OMB) Circular A-l33 (the Single Audit) and not to 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 or compliance matters related to the activities of the Nebraska Department of Labor (the Agency) or other operational matters that are presented below for your consideration. These comments and recommendations, which have been discussed with the appropriate members of the Agency's 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 (if applicable) have been satisfactorily resolved.

Comment Number 1 (Bank Reconciliations) is considered a significant deficiency. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Agency's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the financial statements that is more than inconsequential will not be prevented or detected by the Agency's internal control. This comment will also be reported in the State of Nebraska's Statewide Single Audit Report Schedule of Findings and Questioned Costs.

Draft copies of this letter were furnished to the Agency 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. Responses have been objectively evaluated and recognized, as appropriate, in the letter. Responses that indicate corrective action has been taken were not verified at this time, but will be verified in the next audit.

The following are our comments and recommendations for the year ended June 30, 2008.

COMMENTS RELATED TO THE AUDIT OF THE BASIC FINANCIAL STATEMENTS

1. Bank Reconciliations

Good internal control requires a plan of organization, procedures, and records designed to safeguard assets and provide reliable financial information. Sound accounting practice and good internal control also require regular, detailed reconciliations of monies on deposit to the Agency's records to ensure errors, omissions, or irregularities that might occur are detected and resolved in a timely manner.

As part of its bank reconciliation process, the Agency tracked outstanding Unemployment Compensation checks using a manually prepared excel spreadsheet and their Benefits Payment System (BPS). Although the Agency performed monthly reconciliations of outstanding checks between these two records, unexplained variances remained in each month's outstanding checks total. During our audit, we noted many problems with the Agency's reconciliation process. As a result of our testing, we determined the total amount of outstanding checks used in the reconciliation was not accurate. The total amount of outstanding checks on the June 30, 2008, bank reconciliation was $1,258,100.

Subsequent to our testing, Administrative Services State Accounting Division (State Accounting) began working with the Agency on their reconciliation process. As of October 31, 2008, the Agency had identified and reconciled bank activity to book activity; however, the Agency's bank reconciliation was incomplete and showed an unknown variance of $5,288 between the Agency's bank balance and their manually prepared spreadsheets. Due to this information, we could not determine if the bank reconciliations performed by the Agency during the fiscal year ended June 30, 2008, were reliable. The last reliable reconciliation was performed in January 2003.

A similar comment was noted in our prior audit.

When variances between the Agency's bank balance and book balance are not sufficiently itemized to ensure their accuracy, there is an increased risk errors, omissions, or irregularities might occur and go undetected or unresolved.

> We strongly recommend the Agency review its reconciliation procedures and develop a method to account for, in detail, all variances and reconciling items. We also recommend, for errors that have been identified, a subsequent adjustment be made in the

> Agency's accounting records. Furthermore, we recommend the Agency continue to work with State Accounting to resolve these issues.

Management Response: The Agency's Treasury Management team has been working closely with State Accounting to formally adopt a reconciliation process and has already identified and corrected variances found to date. The team will continue to enforce this formal policy and research and document any variances found during the daily reconciliation process. Formal coordination is ongoing with both the State Accounting Team as well as the Agency's information technology staff on a daily basis to correct errors found in the reconciliation process.

2. Pledged Collateral

Neb. Rev. Stat. § 77-2395 (1) (Reissue 2003) states, "If a bank…furnishes securities pursuant to Section 77-2389, 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 one hundred two percent of the amount on deposit which is in excess of the amount so insured."

The Agency did not have sufficient pledged collateral to cover bank balances for a total of four days during the months of January and April 2008. Additional pledged collateral was obtained the next day. Uninsured deposit amounts on these four days were $2,098,337, $199,173, $679,848, and $28,665,326.

Without adequate pledged security to cover bank balances, there is an increased risk of loss of State funds.

> We recommend the Agency ensure sufficient pledged collateral exists for all bank deposits in order to remain in compliance with State Statute. Furthermore, we recommend the Agency obtain additional pledged collateral in advance of peak deposit time periods especially when those peak deposit periods may cause the Agency's funds to be under-insured.

Management Response: The Agency understands that a management response is not required for this finding but has chosen to formally agree with the findings of the audit team and provide a brief explanation of their corrective action plan.

Corrective Action Plan: The agency's treasury management team and financial management staff have met with bank representatives and discussed the issue of pledged collateral. As noted in the finding above this issue arises during peak periods of activity within the treasury program. The treasury program and financial management staff have identified methods to project peak periods and will work with bank representatives to ensure that pledged collateral is adequate to meet demands during these periods.

Contact: Tammy Williams, Treasury Supervisor

Anticipated Completion Date: Complete and ongoing.

COMMENTS RELATED TO THE SINGLE AUDIT

Finding #08-23-02

Program: CFDA 17.258, 17.259, & 17.260 – Workforce Investment Act (WIA) Cluster; due to the cross–cutting nature of this finding, all Agency CFDA's are also impacted – Cash Management & Reporting

Grant Number & Year: Various

Federal Grantor Agency: U.S. Department of Labor

Criteria: OMB Circular A-133 § 300 states, "The auditee shall: (a) Identify, in its accounts, all Federal awards received and expended and the Federal programs under which they were received. . . . (b) Maintain internal control over Federal programs that provides reasonable assurance that the auditee is managing Federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements that could have a material effect on each of its Federal programs. (c) Comply with laws, regulations, and the provisions of contracts or grant agreements related to each of its Federal programs." Title 29 CFR § 97.21(b) (July 1, 2007) states, "Methods and procedures for payment shall minimize the time elapsing between the transfer of funds and disbursement by the grantee or subgrantee…" Good internal control requires procedures to ensure expenditures are properly reported and reconciled to Federal funds received.

Condition: There have been variances between Federal reported expenditures, actual expenditures, and Federal receipts drawn for the past several years. Although these variances may not have been significant for any particular grant for a particular year, the cumulative effect has risen to approximately $4 - 6 million variance between reported expenditures and drawdowns received. The Agency is currently working with Federal program officials to resolve this issue; however, we noted several issues with the procedures used.

Questioned Costs: Unknown

Context: Due to concerns by Federal program officials and the Agency, the Auditor of Public Accounts (APA) evaluated the accounting records and other information regarding variances between Federal reported expenditures, Federal expenditures per the State accounting system, and funds received from the Federal government from January 2003 to March 2008. Nebraska Information System (NIS) is the State accounting system implemented in 2003. Financial Accounting and Reporting System (FARS) was the system used for Federal reporting through December 2006 and was the approved system for cost allocations. The Agency did not reconcile FARS reported expenditures to NIS actual expenditures, or to drawdowns received.

Several concerns were noted and the Agency began work to attempt to resolve the issues and to determine the amount needed to repay the Federal government. The Agency performed procedures for the period from July 1, 2003, through June 30, 2008. This work included (1) the use of spreadsheets accumulating adjusted expenses and Payment Management System (PMS) drawdowns, and (2) a comparison of NIS general ledger expenses to NIS general ledger receipts.

The first method involved comparing adjusted NIS expenses to PMS draws. Adjusted NIS expenses were NIS general ledger expenses plus or minus adjustments identified by the APA necessary to correct improper cost allocations.

We noted the following regarding the first method:

- The Agency did not have written approval from the U.S. Department of Labor (U.S. DOL) for the time frame analyzed. The Agency indicated they had discussed the timeframe with U.S. DOL representatives. The Agency used from July 1, 2003, through June 30, 2008. The APA had noted variances from January 1, 2003, through June 30, 2003, in the amount of $1,929,137.

- The Agency focused on Workforce Investment Act, Employment Services and Unemployment Insurance grants, but the Agency did not consider all the projects in each of these programs. Also, the Agency did not consider other Federal programs which appeared to have discrepancies. The Agency did not have approval from the U.S. DOL to exclude any projects or programs.

- We could not trace all PMS draw amounts to PMS. We could not trace 8 of 15 Workforce Investment Act draws tested with variances ranging from ($169,357) to $959,962; 7 of 30 Employment Services draws tested ranging from ($629,588) to $352,054, and 13 of 20 Unemployment Insurance draws tested ranging from ($3,858,787) to $24,903.

- Amounts that were supposed to carryover from one spreadsheet to the next were not always properly carried forward. We noted errors ranging from ($931,809) to $598,624 for various projects tested. In addition, the APA noted many other clerical errors in the Agency's analysis.

- The purpose of the first method was to determine if any grant was overdrawn for a particular year; however, the results were not carried forward to a final determination of adjustments or repayments needed.

The second method compared NIS general ledger expenses and NIS general ledger receipts for only the specific grants originally identified by the Federal government as being overdrawn. The Agency's analysis resulted in a variance of $4,368,453. As noted in finding #08-23-03 our testing of unallowable transfers shows $5,589,779 has not been repaid.

We noted the following regarding the second method:

- The Agency did not evaluate all grants.

- The second method is based on the NIS general ledger and does not include adjustments needed due to cost allocation problems and other issues.

- The analysis used NIS receipts and not PMS draws. Since the Agency was not consistently depositing grant money from PMS into the correct grant business units in NIS, using NIS receipts would not accurately reflect which grants the dollars originated from. Also, the Agency did not consistently use the NIS receipt amount when determining the variance. If NIS receipts exceeded obligation authority, the Agency only recorded the amount they were authorized to spend.

We determined this work was not sufficient to adequately determine the amount needed to repay the Federal government.

Cause: The Agency was not performing adequate periodic reconciliations. Procedures within the Agency's finance area were not adequately documented. Supervisory reviews of cash management and reporting were ineffective.

Effect: WIA Federal funds were used for non-WIA purposes.

Recommendation: We recommend the Agency continue to work with Federal program officials to resolve this issue and repay funds as necessary. Specifically, we recommend the Agency: 1) Obtain the U.S. DOL's approval for the parameters of the evaluation, including approval for any dates or projects excluded, 2) The evaluation should be based on NIS general ledger expenditures adjusted for cost allocation errors and PMS drawdowns received, and 3) Adequate supporting documentation should be maintained for all adjustments and repayments.

Management Response: The Agency accepts the findings and recommendations of the State audit team.

Corrective Action Plan: The Agency will continue to work with federal administrators in the Region V office on the validation controls to be used to determine the amount of the actual shortfall and will ensure that any agreements on parameters is obtained in writing. Evaluation will include adjusted NIS expenses as well as a comparison to current GL and reported numbers compared with actual draw downs from the federal payment management system.

Contact: Mike Smith, Director of Finance/Controller

Anticipated Completion Date: July 2009

<u>Finding #08-23-03</u>

Program: CFDA 17.258, 17.259, & 17.260 – Workforce Investment Act (WIA) Cluster – Allowability & Cash Management

Grant Number & Year: #AA154910655, FFY 2007; #AA160420755A31, FFY 2008; #AA171350855A31, FFY 2009

Federal Grantor Agency: U.S. Department of Labor

Criteria: Per 31 C.F.R. 205.33(a) (July 1, 2007), "A State must minimize the time between the drawdown of Federal funds from the Federal government and their disbursement for Federal program purposes." Per OMB Circular A-87, "To be allowable under Federal awards, costs must meet the following general criteria: a. Be necessary and reasonable for proper and efficient performance and administration of Federal awards." Per 29 C.F.R. 97.20(a) (July 1, 2007), "Fiscal control and accounting procedures of the State, as well as its sub-grantees and cost-type contractors must be sufficient to… (2) Permit the tracing of funds to a level of expenditures adequate to establish that such funds have not been used in violation of the restrictions and prohibitions of applicable statutes." Good internal control requires procedures be in place to ensure draws are accurate.

Condition: The Agency drew funds from the WIA Cluster and then performed a journal entry to transfer the funds to another Federal program. In addition, we tested three cash draws and noted all three draws did not comply with Federal regulations.

Questioned Costs: $5,589,779

Context: On May 2, 2007, a U.S. DOL employee sent the Agency an email showing the Employment Services and Unemployment Insurance Administration grants were overdrawn by $8,190,181. To cover these grant overdrafts, the Agency drew funds from WIA. We determined the Agency made three journal entries transferring $7,522,047 from WIA to cover the other grants. Of this amount, one transaction occurred in fiscal year 2008 for $827,010 and transferred funds from WIA to Unemployment Insurance CFDA 17.225. The transactions for the other $6,695,037 occurred in June 2007. First, the Agency drew the funds from WIA, and then they performed a journal entry to transfer the funds to the other grants. At the end of fiscal year 2008, the Agency repaid $1,932,268 as follows: $1,612,351 was drawn from Unemployment Insurance and repaid to WIA and $319,917 was transferred from Employment Services to WIA, leaving $5,589,779 that had not been repaid.

During testing of cash draws, we also noted the following:

- Throughout the fiscal year the Agency drew funds from WIA and deposited them directly into non-WIA grants. Funds were deposited into Food Stamps and Workfare, which were programs the Nebraska Department of Health and Human Services (DHHS) contracted with the Agency to perform. The Agency was effectively borrowing from WIA to cover these program expenses until reimbursed by DHHS. For the three draws tested, the Agency drew $8,025 for Food Stamps and $18,116 for Workfare.

- The Agency overdrew $11,780 due to a data entry error.

- The Agency was unable to locate supporting spreadsheets for two of three draws tested.

- For the first six months of the fiscal year, the Agency deposited many of the WIA draws into a few business units instead of using all of the actual business units the expenditures were paid from. Therefore, we were unable to determine the actual source of funds used for each expenditure.

Cause: Inadequate reconciliation procedures in current and prior years. The Agency drew funds from WIA to pay expenses for other grants. In addition, the Agency used combining spreadsheets to accumulate draw information. Dollar amounts were entered into multiple spreadsheets numerous times, making data entry errors more likely.

Effect: The Agency misused WIA Federal funds. Funds are due to the Federal government.

Recommendation: We recommend the Agency reverse the unallowable transfer. We further recommend all accounting entries be adequately supported and documented. The Agency should not prepare journal entries to transfer funds between grants; nor should they directly deposit WIA funds into other grants. If corrections are needed, each grant should have separate accounting entries with proper documentation to support each transaction. We recommend the Agency implement procedures to ensure cash draws are accurate. Finally, we recommend the Agency comply with all Federal regulations.

Management Response: The Agency accepts the findings and recommendations of the State audit team with comment. As noted in the finding above the Agency is working with its federal partners to gain agreement on the amount of Federal funds owed to the WIA program and is further working with the state legislature on obtaining the funds required to reverse this unallowable transfer.

Corrective Action Plan: The Agency will continue to work with its Federal partners to gain agreement on the parameters to be used to determine the amount of the shortfall within the Federal program and thus the exact amount to be repaid to the WIA program. To date a total of approximately $1.9M has already been repaid. In additional the Agency will continue to work with the state legislature to gain agreement and approval on the method to be used to repay these federal funds. Corrective actions will be taken to return the funds and correct the inappropriate journal entries once funds have been provided.

Contact: Mike Smith, Director of Finance/Controller

Anticipated Completion Date: August 2009

<u>Finding #08-23-04</u>

Program: CFDA 17.258, 17.259, & 17.260 – Workforce Investment Act (WIA) Cluster; due to the cross–cutting nature of this finding, all Agency CFDA's are also impacted – Allowable Costs/Cost Principles

Grant Number & Year: Various

Federal Grantor Agency: U. S. Department of Labor

Criteria: Per OMB Circular A-87 all activities which benefit from the governmental unit's indirect cost, including unallowable activities and services donated to the governmental unit by third parties, will receive an appropriate allocation of indirect costs. Any cost allocable to a particular Federal award or cost objective under the principles provided for in this Circular may not be charged to other Federal awards to overcome fund deficiencies, to avoid restrictions imposed by law or terms of the Federal awards, or for other reasons. Also per A-87 fringe benefits must be equitably allocated to all related activities, therefore, the Agency must allocate to State programs using the same method as Federal projects. All projects, both State and Federal must use the same allocation method. Also, per A-87 a "cost is allocable to a particular cost objective if the goods or services involved are chargeable or assignable to such cost objective in accordance with relative benefits received." Per written correspondence from the U.S. Department of Labor Division of Cost Determination (DCD) dated April 29, 2005, "The cost allocation methodology to be utilized in the centralized State of Nebraska Information System (NIS) should be submitted to the DCD, for written acceptance/approval, before the transfer is implemented." Good internal control requires procedures to ensure the Agency has an approved Cost Allocation Plan.

Condition: The Agency was not properly allocating costs in accordance with OMB Circular A-87. Additionally, we noted the Agency did not have a Federally-approved Cost Allocation Plan for the fiscal year ended June 30, 2008.

Questioned Costs: Unknown

Context: Implemented in 2003, NIS is the State's official accounting system and is used to record all State expenditures and revenues. The Agency enters all accounting transactions into the NIS General Ledger in order to record and make payments from Federal funds received. From 2003 through December 2006, the Agency also entered its accounting information into the Financial Accounting and Reporting System (FARS) to allocate indirect costs and report expenditures to the Federal government. The Federal government approved this use of FARS through June 30, 2006, with the understanding that NIS could take over the allocation process once written acceptance/approval was received from the Federal government.

In January 2007, the Agency switched from using FARS to using NIS to allocate indirect costs and report expenditures to the Federal government. However, the Agency did not have authorization from the Federal government to change from FARS to NIS. In fact, the Agency did not obtain approval for any cost allocation plan, NIS or FARS, until August 25, 2008, when the Federal government provisionally accepted NIS to replicate the previously approved FARS cost allocation methodologies.

In addition, the Agency was not properly allocating overhead costs to State Safety projects. These State projects were charged a flat rate which was less than allocated costs, as a result Federal programs were charged for Safety costs. The Agency continued to misallocate Safety costs through fiscal year 2008. There are also business units that are accumulated and allocated to other projects. One of these is project code 500. At the end of the month, this code is allocated out to programs within Greater Nebraska WIA. Per the Agency, this allocation was based on the percentage of Federal authorization for each CFDA within the WIA Cluster. Project codes 160, 165, 200, and 800 were also allocated to various Federal programs based on available funds or estimates. This is not an acceptable allocation method per OMB Circular A-87.

Cause: The Agency indicated that Safety projects did not have enough funds to pay for all costs allocated based on hours and so they were charged a set percentage of 7.5%.

Effect: Noncompliance with regulations could result in Federal sanctions.

Recommendation: We recommend the Agency have procedures to ensure costs are allocated in accordance with an approved Cost Allocation Plan and Circular A-87.

> **Management Response:** The Agency accepts the findings and recommendations of the State audit team.
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> **Corrective Action Plan:** This corrective action has been implemented. An approved cost allocation plan, developed in accordance with OMB Circular A-87 and approved by the US Department of Labor is currently in place and will be updated annually as appropriate.
>
> **Contact:** Mike Smith, Director of Finance/Controller
>
> **Anticipated Completion Date:** Completed August 2008

<u>Finding #08-23-05</u>

Program: CFDA 17.002 – Labor Force Statistics; CFDA 17.207 – Employment Service/Wagner-Peyser Funded Activities; CFDA 17.225 – Unemployment Insurance; CFDA 17.245 – Trade Adjustment Assistance; CFDA 17.258 – WIA Adult Program; CFDA 17.259 – WIA Youth Activities; CFDA 17.260 – WIA Dislocated Workers – Reporting

Grant Number & Year: All open grants

Federal Grantor Agency: U.S. Department of Labor

Criteria: OMB Circular A-133 § 300 requires the State to identify, in its accounts, all Federal awards received and expended and the Federal programs under which they were received. The State shall also prepare the Schedule of Expenditures of Federal Awards (SEFA) in accordance with section 310 including total Federal awards expended for each individual Federal program and the CFDA number. Good internal control requires procedures to ensure the SEFA is properly presented.

Condition: The Agency did not accurately report Federal expenditures by CFDA. We informed Administrative Services and the Agency of the error and the SEFA was subsequently adjusted.

Questioned Costs: None

Context: The Agency reports expenditures for the SEFA to Administrative Services. Administrative Services compiles the information for all agencies and reports to the auditor. The amounts reported were as follows:

CFDA #	Amount Initially Reported	Corrected SEFA Amount	Variance
17.002	$ 931,143	$ 920,608	$ 10,535
17.207	$ 7,297,709	$ 7,441,185	$ (143,476)
17.225	$ 14,775,345	$ 15,666,720	$ (891,375)
17.245	$ 1,092,087	$ 1,165,532	$ (73,445)
17.258	$ 3,805,352	$ 3,958,657	$ (153,305)
17.259	$ 2,234,568	$ 2,221,851	$ 12,717
17.260	$ 1,561,531	$ 1,625,458	$ (63,927)

Cause: The Agency manually accumulated expenditures from NIS on a spreadsheet by month and by project number (multiple project numbers may combine into one CFDA) and the auditor noted input errors occurred. In addition, some NIS business units were not properly linked to the correct CFDA.

Effect: Noncompliance with Circular A-133.

Recommendation: We recommend procedures be implemented to ensure Federal expenditures are properly reported in accordance with Circular A-133.

Management Response: The Agency accepts the findings and recommendations of the State audit team.

Corrective Action Plan: The Agency has begun to phase out its use of the abbreviated GA-17 report to determine actual SEFA amounts and will use the summary grant reporting system contained with the NIS accounting reports. This system allows for the capture of actual draws and expenses by business unit and associated grant. To date all PY08 FY09 grants have been adapted into the system and approximately 85% of the agencies business units. Additional work is required on those business units contained within the WIA program which tie to multiple grants. This effort is being worked with the State Accounting office.

Contact: Mike Smith, Director of Finance/Controller

Anticipated Completion Date: July 2009

Finding #08-23-06

Program: CFDA 17.258, 17.259 & 17.260 – Workforce Investment Act Cluster – Reporting

Grant Number & Year: All open grants

Federal Grantor Agency: U.S. Department of Labor

Criteria: Title 29 CFR § 92.20 (July 1, 2007) requires fiscal control and accounting procedures of the State sufficient to permit preparation of required reports and permit the tracing of funds to expenditures adequate to establish the use of these funds were not in violation of applicable regulations. NIS is the official accounting system for the State of Nebraska and all expenditures are generated from NIS. Good internal control requires procedures to reconcile the accounting system to the submitted reports.

Title 29 CFR § 92.20 also requires subgrantees maintain records and adequately identify the source and application of funds provided for financially-assisted activities. The records must contain information pertaining to grant or subgrant awards and authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, and income. The regulations also require accurate, current, and complete disclosure of the financial results of financially-assisted activities must be made in accordance with the financial reporting requirements of the grant or subgrant and accounting records must be supported by such source documentation as cancelled checks, paid bills, payrolls, time and attendance records, contract and subgrant award documents, etc. Title 29 CFR § 97.40 (July 1, 2007) states, "Grantees are responsible for managing the day-to-day operations of grant and subgrant supported activities. Grantees must monitor grant and subgrant supported activities to assure compliance with applicable Federal requirements and that performance goals are being achieved. Grantee monitoring must cover each program, function or activity." Good internal control requires procedures to ensure amounts paid to subrecipients agree to amounts reported by the subrecipients.

Condition: We noted the Agency did not have adequate procedures to ensure amounts reported by subrecipients agreed to accounting records.

Questioned Costs: Unknown

Context: We tested six quarterly WIA reports submitted for the quarter ended June 30, 2008, and noted the amounts reported could not be traced to financial records. The quarterly reports were prepared from information included on monthly expenditure reports from the local areas. Two of the local areas were managed by the Agency and the monthly reports were prepared by the Agency. The Agency indicated the monthly reports were prepared utilizing financial information from the GA-17 reports from NIS. During testing, we were unable to trace the amounts from the monthly expenditure reports to the supporting information. The Agency staff member who prepared the reports was no longer employed by the Agency and other staff members were not aware of the process utilized to prepare the monthly expenditure reports so no explanation for the variances could be provided. In an attempt to reconcile the local area monthly reports to the NIS GA-17 reports we subtracted the cumulative amount for the June 30, 2007, local area reports from the cumulative amount for the June 30, 2008, local area reports for program years 2006 and 2007. The amount determined to be current expenditures from the process was $6,118,709. We also ran a General Ledger Detail from NIS for the business units which corresponded to the monthly reports. The amount of expenditures per NIS was $5,926,204. The variance between the two amounts was $192,505 which was included in the reports utilized to prepare the ETA-9130, but not supported by NIS expenditures.

The other local area was self-managed and prepared financial reports based on information from their own accounting system. The Agency received the reports from the local area on a monthly basis; however, we noted the local area did not include supporting documentation for the amounts reported. The Agency paid the local area $890,447 during the fiscal year according to the State accounting system.

Cause: Departure of the Agency staff member responsible for preparing the monthly expenditure reports for two local areas. The Agency did not feel they needed to complete additional procedures for the local area which prepared its own monthly expenditure report.

Effect: Without adequate procedures to ensure amounts reported reconcile to the accounting system there is a risk amounts reported are not correct and cannot be relied on. Failure to require subrecipients to send supporting documentation with reported amounts increases the risk the amounts are incorrect.

Recommendation: We recommend the Agency improve procedures utilized to prepare monthly reports for the local areas it manages in order to ensure the amounts can be traced to support and the correct amounts are reported. We also recommend the Agency implement procedures to ensure the amounts paid to the independent local area agree to amounts reported on the monthly expenditure reports.

Management Response: The Agency accepts the findings and recommendations of the State audit team.

Corrective Action Plan: Control practices have been put in place which ensures that at least three accounting staff review financial reports prior to their publication; the program manager, accountant, budget office or financial manager will review all reports and supporting documents to ensure that numbers reported are correct and auditable.

Contact: Mike Smith, Director of Finance/Controller

Anticipated Completion Date: Completed January 2009

Finding #08-23-07

Program: CFDA 17.258, 17.259, & 17.260 – Workforce Investment Act Cluster – Period of Availability

Grant Number & Year: All open grants

Federal Grantor Agency: U.S. Department of Labor

Criteria: According to 20 CFR § 667 107(a) (April 1, 2007), "Funds allotted to States under WIA sections 127(b) and 132(b) for any program year are available for expenditure by the State receiving the funds only during that program year and the two succeeding program years." Title 29 CFR 97.20(a) (July 1, 2007) states, "Fiscal control and accounting procedures of the State, as well as its sub-grantees and cost-type contractors must be sufficient to . . . Permit the tracing of funds to a level of expenditures adequate to establish that such funds have not been used in violation of the restrictions and prohibitions of applicable statutes." Good internal control requires the official accounting system to identify the source of funds expended.

Condition: The business units used to record the WIA expenditures were not tied to a particular grant number and year, thus expenditures could not be tied to which grant funds were expended.

Questioned Costs: Unknown

Context: NIS is the official accounting system for the State of Nebraska which utilizes business units to identify the source and expenditure of funds. In NIS, a business unit is a separate entity within a fund used to track revenues and expenditures. The Agency did not properly utilize the business units to identify the source of funds. Rather the business units reflected the fiscal year the expenditure was made. WIA grants are available 3 years. For all 26 expenditures tested, it appears the grant funds being used met the period of availability as the 2004 grant was closed. However, since the Agency did not utilize the business units to separately identify each grant year, we were unable to determine if these expenditures met the period of availability.

Cause: The business units reflect the fiscal year the expenditure was made rather than being tied to a particular grant.

Effect: Unable to determine compliance with the period of availability requirements.

Recommendation: We recommend the Agency set up NIS business units to properly identify the source and use of Federal funds. Each grant should have a separate and unique business unit.

> **Management Response:** The Agency accepts the findings and recommendations of the State audit team with comment. Because each grant can have multiple business units – e.g. the WIA grant can support multiple projects – the recommendation should read that each business unit should tie to only one grant. This philosophy has been confirmed with the State Accounting office and is currently in place with other state agencies which utilize Federal grant funds.
>
> **Corrective Action Plan:** This plan has been put in place for all Federal grants in PY08 and FY09 with the exception of those WIA administrative accounts which tie through necessity to multiple grants. The Agency financial officer will continue his work with the state accounting staff to establish parent-child business unit relationships to establish better control over these remaining accounts.
>
> **Contact:** Mike Smith, Director of Finance/Controller
>
> **Anticipated Completion Date:** July 2009

Finding #08-23-08

Program: CFDA 17.258, 17.259, & 17.260 – Workforce Investment Act Cluster – Earmarking

Grant Number & Year: All open grants

Federal Grantor Agency: U.S. Department of Labor

Criteria: Title 29 CFR § 92.20 (July 1, 2007) requires fiscal control and accounting procedures of the State sufficient to permit preparation of required reports and permit the tracing of funds to expenditures adequate to establish the use of these funds were not in violation of applicable regulations. NIS is the official accounting system for the State of Nebraska and all expenditures are generated from NIS. Good internal control requires that adequate supporting documentation be maintained to show expenditures.

Condition: We noted the Agency did not have adequate supporting documentation to ensure earmarking levels were met.

Questioned Costs: Unknown

Context: We tested the grants that were closed during State fiscal year 2008 and noted that several of the earmarks were not supported by adequate documentation. In reviewing the spreadsheets the Agency prepares and utilizes to show the earmarks, it appears the requirements have been met. However, the earmark requirements for 10% local area administrative costs and 30% out-of-school youth activity funds were supported by the local areas' monthly expenditure reports. Two of the local areas were managed by the Agency and the monthly reports were prepared by the Agency. The Agency indicated the monthly reports were prepared utilizing financial information from the GA-17 reports from NIS. During testing we were unable to trace the amounts from the monthly expenditure reports to the supporting information. Additionally, one local area prepares monthly expenditure reports which are sent to the Agency with no supporting documentation. The Agency does not have procedures in place to ensure these monthly reports are accurate. The earmark requirements for 15% State Reserve, 5% State administrative costs, and 25% rapid response were supported by expenditure reports from NIS. However, the Agency did not properly utilize the NIS business units to identify the source of funds. Rather the business units reflected the fiscal year the expenditure was made, and thus expenditures could not be tied to which grant funds were expended. Therefore, the tracking of these earmarking requirements by grant in NIS was not possible without Agency hand-written cumulative amounts. We were unable to trace these cumulative amounts to supporting information.

Cause: Departure of the Agency staff member responsible for preparing the monthly expenditure reports for two local areas. The Agency did not feel they needed to complete additional procedures for the local area which prepared its own monthly expenditure report. The Agency uses a cumulative amount when calculating several monthly expenditures.

Effect: Without adequate supporting documentation we could not determine whether earmarking requirements were met.

Recommendation: We recommend the Agency maintain supporting documentation to ensure earmarking requirements were meet. We further recommend the Agency utilize separate business units for each grant year to track earmarking requirements.

Management Response: The Agency accepts the findings and recommendations of the State audit team.

Corrective Action Plan: Control practices have been put in place which ensures that at least three accounting staff review financial reports prior to their publication; the program manager, accountant, budget office or financial manager will review all reports and supporting documents to ensure that numbers reported are correct and auditable. In addition the financial management staff will work with the state accounting office and the Agency's program management office to establish better audit procedures related to the issuance and monitoring of funds for the Lincoln WIA program.

Contact: Mike Smith, Director of Finance/Controller

Anticipated Completion Date: August 2009

Finding #08-23-09

Program: CFDA 17.258, 17.259, & 17.260 – Workforce Investment Act Cluster – Reporting

Grant Number & Year: All open grants

Federal Grantor Agency: U.S. Department of Labor

Criteria: Good internal control requires procedures be in place to ensure information from the client database correctly transfers to the Workforce Investment Act Standardized Record Data (WIASRD) report.

Condition: We tested 25 lines of coding on the WIASRD for key line items and noted one inconsistency between the report and supporting documentation.

Questioned Costs: None

Context: Line item 619, "Type of Recognized Credential" had a value of "0" on the WIASRD, meaning no credential was received. However, information on the Agency's case management system, the Tracking and Reporting Exchange System (TREX) showed the client actually received an associate's degree. The data on the TREX did not match the WIASRD.

Cause: There was a programming error in the code to transfer data from the TREX to the WIASRD. The client was co-enrolled in the WIA Dislocated Worker (DLW) program and the National Emergency Grant (NEG) program. The client received the degree through the DLW program and did not receive a degree through the NEG program. However, the results of the NEG record inadvertently overrode the results of the DLW record.

Effect: Incorrect information reported could lead to sanctions.

Recommendation: We recommend the Agency correct the programming error and ensure data in the WIASRD properly reflects the actual information on the TREX.

Management Response: The Agency acknowledges the need for accurate reporting. The described programming error was fixed, tested and moved to production on December 22, 2008. The Agency does not feel any further corrective action is needed at this time.

It should be noted that this data was reflected correctly in the WIA Annual Report submitted September, 23, 2008. Per Training and Employment Guidance Letter (TEGL) 9-07, the Annual Report is the official submission that contains the data upon which incentive and sanction determinations are based.

Corrective Action Plan: As noted above

Contact: Joan Modrell, Director, Office of Employment and Training

Anticipated Completion Date: Completed

Finding #08-23-10

Program: CFDA 17.258, 17.259, & 17.260 – Workforce Investment Act Cluster – Subrecipient Monitoring

Grant Number & Year: All open grants

Federal Grantor Agency: U.S. Department of Labor

Criteria: OMB Circular A-133 § 400(d)(3) requires that pass-through entities "monitor the activities of subrecipients as necessary to ensure that Federal awards are used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved." Good internal control requires that a reconciliation be performed between a subrecipient's reported expenditures and Federal receipts to ensure Federal funds are being used properly. OMB Circular A-133 § 400 (d) states, "A pass-through entity shall perform the following for the Federal awards it makes: (1) Identify Federal awards made by informing each subrecipient of CFDA title and number, award name and number, award year, if the award is R&D, and name of Federal agency."

Condition: Monitoring of expenditures was inadequate for one subrecipient tested. Additionally, this subrecipient was not properly notified of Federal award information.

Questioned Costs: Unknown

Context: The Agency has three local areas. Two of these areas the programs are administered by the Agency. The other local area is administered by a subrecipient. The subrecipient reported expenditures monthly to the Agency and periodically submitted a request for funds. However, no supporting documentation was submitted with the request for funds and the Agency did not reconcile the amount of Federal funds given to the subrecipient to the monthly expenditure reports nor to the subrecipient's Single audit.

Additionally, award information provided to this subrecipient did not include the CFDA numbers or the Federal awarding agency. The amount of Federal funds paid to this subrecipient during State fiscal year 2008 was $890,448.

Cause: Unknown

Effect: Without adequate monitoring of subrecipients there is an increased risk of misuse of Federal funds. Without notification of award information there is increased risk for errors at the subrecipient level.

Recommendation: We recommend the Agency reconcile the Federal funds paid to the subrecipient to the expenditures the subrecipient reports. Additionally, we recommend the Agency include all required information on subrecipient award documents.

Management Response: The Agency accepts the findings and recommendations of the State audit team.

Corrective Action Plan: Control practices have been put in place which ensures that at least three accounting staff review financial reports prior to their publication; the program manager, accountant, budget office or financial manager will review all reports and supporting documents to ensure that numbers reported are correct and auditable. In addition the financial management staff will work with the state accounting office and the Agency's program management office to establish better audit procedures related to the issuance and monitoring of funds for the Lincoln WIA program.

Contact: Mike Smith, Director of Finance/Controller

Anticipated Completion Date: August 2009

<u>Finding #08-23-11</u>

Program: CFDA 17.258, 17.259, & 17.260 – Workforce Investment Act Cluster – Allowability

Grant Number & Year: All open grants

Federal Grantor Agency: U.S. Department of Labor

Criteria: OMB Circular A-87 states, "To be allowable under Federal awards, costs must…Be necessary and reasonable for proper and efficient performance and administration of Federal awards…Be adequately documented." The Student Orientation Agreement all WIA participants sign before they receive training states, "I understand that any books, tools, uniforms, or any other material purchased by WIA will remain the property of WIA during the training period. If I discontinue training, or if I am terminated before completion, I agree to return these items to the WIA office no later than seven (7) days after the date of termination." The agreement goes on to state, "I agree to pay the cost of all classes that are dropped after the school's identified drop/add time frame. I may either repay Nebraska Workforce Development the appropriate amount or pay the training provider directly. If I return to WIA for additional training services, I will repay the training provider directly for all future training costs until the amount I have paid equals the amount I owed from previous dropped classes."

Condition: For 2 of 16 aid expenditures tested, the participant dropped the classes and did not reimburse WIA the tuition nor did they return to WIA the textbooks, tools, or other supplies purchased with WIA funds.

Questioned Costs: $1,472 known

Context: One WIA client dropped three classes in the spring of 2008, each at a charge to WIA. There was no documentation showing the case manager informed the participant he would have to reimburse WIA for the tuition of the dropped classes. Case notes state WIA paid for summer 2008 classes that were also dropped. After the summer classes were dropped the case manager informed the client that WIA would not pay for the next few classes for fall 2008, but there was no attempt to collect the tuition from the participant. The textbooks and tools purchased with WIA funds for the dropped classes were not returned to WIA. The total cost of dropped classes for spring 2008 was $270. The tools and textbooks cost $345.

Another WIA client dropped three classes in the fall of 2007, each at a charge to WIA. The case manager informed the client she would have to pay for these classes if she would need to take them again, but there was no attempt to collect tuition from the participant. Additionally, the textbooks and calculator for the dropped classes were purchased with WIA funds and were not returned to WIA. The tuition for the dropped classes totaled $575. The textbooks and calculator cost $282.

Federal payment errors noted were $1,472. The total Federal sample tested was $20,320 and total WIA Federal aid payments for fiscal year 2008 were $3,400,843. Based on the sample tested, the case error rate was 12.5% (2/16). The dollar error rate for the sample was 7.24% ($1,472/$20,320) which estimates the potential dollars at risk for fiscal year 2008 to be $246,221 (dollar error rate multiplied by population).

Cause: Unknown

Effect: By not following WIA policies there is an increased risk for misuse of Federal funds.

Recommendation: We recommend the Agency collect supplies, textbooks, and tuition from clients who discontinue training by following current policies.

Management Response: The Agency acknowledges the need to follow its own prescribed policies, especially in the absence of federal WIA guidance for recouping client training costs as outlined in items #3 and #9 the Student Orientation Agreement (noted under Criteria).

Corrective Action Plan:

Corrective Action Steps	**Accountable Person**	**Due Date**
Revise Student Orientation Agreement	Administrative Entity	01/23/2009
Draft client Request for Repayment and/or Return of Materials letter	Administrative Entity	01/23/2009
Develop Guidance letter to staff concerning seeking repayment of tuition and/or return of materials	Administrative Entity	02/28/2009
Complete Training with staff concerning Guidance Letter and use of the Request of Repayment letter via the monthly WIA conference call.	WIA Program Coordinators	03/15/2008

Upon review, the Agency feels the need to further clarify the statements contained within the Student Orientation Agreement:

For item #3, a client's "training period" should be defined as the overall training program, not one particular component of the training. IE: One class.

For item #9, the statement was revised to highlight the client's ability to satisfy tuition costs incurred by classes previously dropped after the school's indentified drop/add time frame by paying "equal" to the amount owed as well as better define the Agency's right to pursue payment. The revised statement below:

> I agree to pay the cost of all classes that are dropped after the schools identified drop/add time frame. I understand that if I return to WIA for additional training services, WIA has the right to demand that I pay the training provider directly for all future training costs until the amount I have paid equals the amount I owed from the previous dropped classes. Additionally, I understand that if no additional training is completed Nebraska Workforce Development can seek payment of training costs incurred for the dropped classes.

Additionally, a formal letter of request is being developed that will seek payment of tuition and/or materials. When appropriate to do so, this letter will be sent via certified mail by staff and will serve as documentation of collection attempts.

Finally, all staff and management will be trained on these new procedures and the need for proper documentation of all activities.

Contact: Cecilia Coatney, Administrator, Office of Employment and Training

Anticipated Completion Date: All steps completed by April, 2009

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.

This letter is intended solely for the information and use of the Agency, the Governor and State Legislature, others within the Agency, Federal awarding agencies, pass-through entities, and management of the State of Nebraska. However, this letter is a matter of public record and its distribution is not limited.

We appreciate and thank all of the Agency employees for the courtesy and cooperation extended to us during our audit.

Signed Original on File	Signed Original on File
Pat Reding	Don Dunlap
Assistant Deputy Auditor	Assistant Deputy Auditor