



NEBRASKA AUDITOR OF PUBLIC ACCOUNTS

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Kyle Schneweis, Director
Nebraska Department of Transportation
1500 Nebraska Hwy 2
Lincoln, Nebraska 68502

Dear Mr. Schneweis:

In planning and performing our audit of the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Nebraska (State), as of and for the year ended June 30, 2017, in accordance with auditing standards generally accepted in the United States of America and standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, we have issued our report thereon dated December 14, 2017. In planning and performing our audit, we considered the State's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements of the State, but not for the purpose of expressing an opinion on the effectiveness of the State's internal control. Accordingly, we do not express an opinion on the effectiveness of the State's internal control.

In connection with our audit described above, we noted certain internal control or compliance matters related to the activities of the Nebraska Department of Transportation (Department) 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 Department'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.

Our consideration of internal control was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as discussed below, we identified a certain deficiency in internal control that we consider to be a significant deficiency.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. We did not identify any deficiencies in internal control that we consider to be material weaknesses.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider Comment Number 1 (Federal Activity Adjustment) to be a significant deficiency.

That comment will also be reported in the State of Nebraska's Statewide Single Audit Report Schedule of Findings and Questioned Costs.

In addition, we noted other matters involving internal control and its operation that we have reported to management of the Department, pursuant to AICPA Auditing Standards AU-C Section 265.A17, in separate early communication letters dated January 24, 2017, October 2, 2017, and November 27, 2017.

Draft copies of this letter were furnished to the Department to provide management with an opportunity to review and to respond to the comments and recommendations contained herein. 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 they will be verified in the next audit.

The following are our comments and recommendations for the year ended June 30, 2017.

1. Federal Activity Adjustment

Prior to July 2017, the Department was two separate agencies, the Department of Roads and the Department of Aeronautics (Aeronautics). Aeronautics did not account for all of its Federal activity in Federal funds. Aeronautics recorded \$16,456,169 in revenues and expenditures in its Airport Development Fund, which is a Cash fund on the State's accounting system. The inaccurate activity was adjusted on the State's financial statements for the fiscal year ending June 30, 2017, to reflect accurately the Federal activity in accordance with the Department of Administrative Services (DAS) policies.

According to the DAS "State Accounting Manual," Application of Principles – Section AM-003, the fund types used in the State accounting system include the following:

- *40000 - Federal Funds - accounts for all federal grants and contracts received by the State.*
- *20000 - Cash Funds - accounts for revenues generated by specific activities from sources outside of state government and the expenditures directly related to the generation of the revenues.*

- 10000 - General Fund - accounts for all financial resources not required to be accounted for in another fund. Revenue generally comes from state taxes.

A good internal control plan requires the Department to record Federal financial activity related to Aeronautics in a Federal fund type, as prescribed in the “State Accounting Manual.”

Additionally, sound accounting practices require procedures to ensure activity on the financial statements is properly reflected.

When Federal financial activity is not recorded as prescribed in the “State Accounting Manual,” the financial activity of those funds can be misleading to the users of the financial information.

We recommend the Department work with the DAS Accounting Administrator to develop a plan for recording all Aeronautics Federal activity in the Federal funds, as prescribed by the “State Accounting Manual.”

Department Response: The Division of Aeronautics does record the receipt of these Federal funds as a federal receipt. However, this is a reimbursable federal program, there are no federal funds expended. Aeronautics must first expend the funds out of its Cash Fund. Then a request is made for a reimbursement of those cash expenditures. Aeronautics has been accounting for these federal grant funds in its Cash Fund for decades as directed by the Nebraska Department of Administrative Services Accounting Division in compliance with that Accounting Division’s interpretation of its own accounting manual.

APA Response: The majority of Federal funds expended by the State are on a reimbursement basis. The APA proposed an adjustment to the Department of Administrative Services (DAS), the State agency responsible for preparing the CAFR financial statements. DAS agreed the funds would be more accurately reported in the Federal Fund, and posted an adjusting entry.

2. Inventory Balances

The Department of Administrative Services, State Accounting Division (DAS), prepares the State of Nebraska Comprehensive Annual Financial Report (CAFR) and requires all State agencies to determine and report accurate amounts for financial reporting.

The Department did not accurately reflect all inventory balances on its accrual response form. The Department reported no fuel inventory balance at June 30, 2017, when the correct balance was \$319,798. The Department subsequently adjusted the response form to include the fuel inventory balance.

A good internal control plan requires the Department to have procedures for the reporting of accurate and complete financial information to DAS.

Without adequate processes and procedures in place to ensure the accuracy of financial reporting, there is a greater risk material misstatements may occur and remain undetected.

We recommend the Department strengthen procedures to ensure information is complete and accurate.

Department Response: NDOT concurs and will review processes.

3. Timely Payment

The Department received a vendor invoice that was dated October 21, 2016, for a total amount due of \$3,041. Payment by the Department was not made to the vendor until January 9, 2017, more than 45 calendar days after the invoice date, which is not in compliance with State statute.

Neb. Rev. Stat. § 81-2403(1) (Reissue 2014) states, in relevant part, the following:

[E]ach agency shall make payment in full for all goods delivered or services rendered on or before the forty-fifth calendar day after (a) the date of receipt by agency of the goods or services or (b) the date of receipt by the agency of the bill for the goods or services, whichever is later, unless other provisions for payment are agreed to in writing by the creditor and the agency.

When the Department does not make payment within 45 days of the purchase date for goods and services, it is not in compliance with State statute.

We recommend the Department implement procedures to ensure payments are made timely and in compliance with State statute.

Department Response: NDOT concurs and will review procedures already in place to comply to the prompt payment statute.

4. Risk Assessment

The Department was in the process of developing an Information Technology (IT) Security Plan to include an IT risk assessment; however, it lacked application-specific risk information.

Nebraska Information Technology Commission (NITC) Standards and Guidelines, Information Security Policy 8-101 (December 10, 2013), Section 4.5.1, Physical Security Perimeter, states, in relevant part, the following:

Agencies will perform a periodic threat and risk assessment to determine the security risks to facilities that contain State information

NITC Standards and Guidelines, Information Security Policy 8-101 (December 10, 2013), Section 4.9.3, Risk Assessment, states, in relevant part, the following:

Security requirements and controls must reflect the value of the information involved, and the potential damage that might result from a failure or absence of security measures The framework for analyzing the security requirements and identifying controls to meet them is associated with a risk assessment, which must be performed by the data owner(s) and Agency management. A process must be established and implemented for each application to:

- *address the business risks and develop a data classification profile to help to understand the risks;*
- *identify security measures based on the criticality and data sensitivity and protection requirements;*

- *identify and implement specific controls based on security requirements and technical architecture;*
- *implement a method to test the effectiveness of the security controls; and*
- *identify processes and standards to support changes, ongoing management and to measure compliance.*

A good internal control plan requires procedures to ensure that an IT risk assessment is completed and updated periodically. Those procedures should require the assessment to address application-specific risk information.

Without adequate risk assessment procedures, there is an increased risk that an application's threats will not be identified. This increases the risk of preventable security vulnerability and threat exploitation, causing such issues as downtime, loss of productivity, unauthorized access, compromise of confidential information or data integrity, or interference with other State or Federal systems.

A similar finding was noted during the previous audit.

We recommend the Department continue developing its IT Security Plan and implement procedures to ensure the periodic performance of an IT risk assessment that addresses application-specific risk information.

Department Response: BTSD is continuing to work toward completion of an application-specific risk assessment for NDOT. BTSD had delayed completion of its specific IT Security Plan until revisions to the NITC Security Policy were complete. This would allow NDOT to include those revisions/recommendations in its IT Security Plan. BTSD continues to address and implement appropriate changes to applications to mitigate security vulnerability risk for NDOT.

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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 Department 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 the Department.

This communication is intended solely for the information and use of the Department, the Governor and State Legislature, others within the Department, Federal awarding agencies, pass-through entities, and management of the State of Nebraska and is not intended to be, and should not be, used by anyone other than the specified parties. However, this communication is a matter of public record, and its distribution is not limited.



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