



## NEBRASKA AUDITOR OF PUBLIC ACCOUNTS

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December 17, 2020

John Albin, Commissioner  
Nebraska Department of Labor  
550 South 16<sup>th</sup> St.  
Lincoln, Nebraska 68509

Dear Commissioner Albin:

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, 2020, in accordance with auditing standards generally accepted in the United States of America and the 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 17, 2020. 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 Labor (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 Department management, are intended to improve internal control or result in other operating efficiencies.

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 material weakness.

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 consider Comment Number 1 (Unemployment Insurance Fund Issues) to be a material weakness.

These comments 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 265B.A17, in a separate early communication letter dated December 16, 2020.

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, 2020.

**1. Unemployment Insurance Fund Issues**

The Department did not have procedures to ensure the Unemployment Insurance (UI) Proprietary Fund financial statements were presented accurately for the Comprehensive Annual Financial Report (CAFR) audit. The Department performed entries within the accounting system, which were used by the Department of Administrative Services (DAS) to generate the financial statements. The financial statements required material adjustments due to duplicate or incorrect journal entries, overstated accruals, and a lack of adequate procedures to reconcile the Department’s separate tax system (TMS) and benefit system (GUS) to the State’s accounting system to ensure the activity was reflected properly.

For the errors detailed in the table below, the Auditor of Public Accounts (APA) proposed adjustments to ensure that the financial statements would be reflected properly.

Description	Misstatement Amount	Reason
Benefits Payable	\$ 296,242,317	The Department’s benefits payable was not calculated accurately. Assumptions using the last three months of claims paid in the fiscal year were used to calculate the estimate. However, this inflated the payable, as only \$12 million had been paid through November 18, 2020, and the Department indicated it had caught up in the payments to individuals. The Department did not identify the issue until it was raised by the APA and corrected at that time.
Benefits Payable / Receivables	\$ 93,242,673	The Department entered a payable and receivable twice in the accounting system, creating negative balances in both of \$93 million. The Department did not perform procedures to identify the issue in the trial balance. DAS corrected the error after the APA proposed an adjusting entry.
EUISAA (Emergency Unemployment Insurance Stabilization and Access Act) Revenue / Payable	\$ 12,145,290	Revenue of \$6,072,645 and a payable to the Federal government for \$4,128,834 were recorded in the UI fund, instead of the Federal fund. Furthermore, transfers of \$1,943,811 between the funds should have been eliminated. The APA proposed an adjustment, but DAS did not record the correcting entry.
Payable / Receivable Eliminations	\$ 11,436,600	The Department recorded a payable to and receivable from the UI fund requiring the activity to be eliminated. Neither the Department nor DAS had procedures to eliminate the activity for the financial statements. During this review, we also noted \$889,941 in unrecorded revenue that required adjustment. DAS corrected the error after the APA proposed an adjusting entry.

Description	Misstatement Amount	Reason
Expenditures / Benefits Payable	\$ 7,739,509	The Department did not ensure transfers in and out agreed between funding sources at fiscal year-end. DAS reclassified a portion of the difference as an expenditure for \$6.2 million inappropriately. The proper entry should have reduced benefits payable for \$7.8 million, as the payable established by the Department on June 30 should have been eliminated due to timing differences in the general ledger. The difference of \$1.6 million was to correct a payable that DAS reversed inappropriately. DAS corrected the error after the APA proposed an adjusting entry.
CWC Receivable	\$ 3,022,038	The Department failed to record the Combined Wage Claim receivable for fiscal year 2020, for \$3,022,038. DAS corrected the error after the APA proposed an adjusting entry.
Accounts Receivable / Revenue	\$ 1,540,313	The Department tripled an entry in the accounting system when attempting to correct an erroneous entry. DAS corrected the error after the APA proposed an adjusting entry.
Transfers / Due to Funds	\$ 130,853	DAS eliminated a transfer out, as the corresponding transfer in was not recorded until the following fiscal year by the Department. The timing issue had been discussed with both DAS and the Department for several years, but no corrections have been performed to categorize the activity correctly.
<b>Total Misstatement</b>	<b>\$ 425,499,593</b>	

We also noted the following issues during testing:

- The Department calculated a benefit overpayment receivable based on a report from its benefit system. The report was for established overpayments as of June 30, 2020, for \$8.6 million. The APA performed testing of the underlying details and determined that the report was not accurately accumulating balances, as 2 of 19 claims tested reflected inaccurate balances for payments made after fiscal year end. The Department was unable to provide an accurate report. Furthermore, due to the COVID-19 pandemic, the Department paid over 10 times the annual benefits for unemployed individuals as in a normal year. As noted in the separate early communication letter to the Department dated December 16, 2020, it was behind in its review and research of potential fraudulent claims, of which totaled nearly \$37 million. The Department and DAS did not consider further receivables and subsequent payables necessary for the financial statements until questioned by the APA. It could only be assumed that there would be other unrecorded receivables and subsequent payables not yet accounted for in the benefit system. Neither the Department nor DAS could come up with a reasonable estimate due to unknown factors, including a lack of research performed to identify further fraudulent claims. Therefore, no further receivable or payable was recorded in the financial statements, requiring a disclaimer of opinion to be issued by the APA.
- The Department did not ensure the Federal Trust fund balance agreed to the accounting system at the fiscal year ended June 30, 2020. An additional entry for \$4,128,834 was necessary to correct the error. The Department also had a variance of \$5,819 in the benefit bank account reconciliation that was not researched and resolved at fiscal year-end.

Good internal controls and sound accounting practice require procedures to ensure that documentation used to prepare the financial statements is accurate and complete.

Without such procedures, there is an increased risk for material misstatement of the financial statements.

We recommend the Department work closely with DAS to establish procedures sufficient for calculating and reporting the UI fund for the CAFR. Furthermore, we recommend the Department establish procedures for its staff to review documentation, including the trial balance, and reconcile the separate TMS and GUS systems to the accounting system to identify issues that need to be rectified.

*Department Response: NDOL and DAS administrations experienced unprecedented challenges brought about by the COVID-19 pandemic. Those challenges, coupled with the implementation of a new unemployment benefits system, hindered the reporting process.*

*NDOL will work with State Accounting to refine existing procedures for reporting Unemployment Insurance CAFR numbers. NDOL has already implemented new reporting elements in the unemployment benefits system specific to CAFR reporting.*

## **2. CCF/MMF Tool Access – TMS**

The Department uses the Change Control Facility/Migration Management Facility (CCF/MMF) tool to track changes made to its mainframe application, TMS. The CCF/MMF tool is a mainframe application that maintains prior code versions in order to revert to the previous code.

During a review of Department users with access to the CCF/MMF tool, we noted a lack of segregation of duties for a user with access to the TMS system. In addition to having the ability to promote his or her own changes to production, one individual could use his or her own ID to check out and edit code.

Nebraska Information Technology Commission (NITC) Standards and Guidelines, Information Security Policy 8-202 (July 2017), “Change control management,” contains the following:

*To protect information systems and services, a formal change management system must be established to enforce strict controls over changes to all information processing facilities, systems, software, or procedures. Agency management must formally authorize all changes before implementation and ensure that accurate documentation is maintained.*

NITC Standards and Guidelines, Information Security Policy 8-303 (July 2017), “Identification and authorization,” states, in relevant part, the following:

*(4) To reduce the risk of accidental or deliberate system misuse, separation of duties must be implemented where practical. Whenever separation of duties is impractical, other compensatory controls such as monitoring of activities, increased auditing and management supervision must be implemented. At a minimum, the audit of security must remain independent and segregated from the security function.*

A good internal control plan requires an adequate segregation of duties, so no individual has the ability to edit program code unilaterally or promote his or her own changes to production.

Without an adequate segregation of duties, there is an increased risk that a malicious change or a change not in line with management’s intentions could be developed and moved into production.

We recommend the Department implement procedures to ensure an adequate segregation of duties is in place to prevent a user from developing an unauthorized change and moving that change into production.

*Department Response: NDOL experienced unprecedented challenges brought about by the COVID-19 pandemic. NDOL previously planned to launch a new tax system to replace TMS in 2020, due to the challenges of the pandemic the launch has not happened. NDOL plans to launch the new system in 2021 and therefore any corrective action to existing processes in TMS are unnecessary.*

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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 management, 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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