MANAGEMENT LETTER
OF THE
NEBRASKA STATE COLLEGE SYSTEM

For the Year Ended June 30, 2022

Issued on January 9, 2023

NEBRASKA AUDITOR OF PUBLIC ACCOUNTS

Mike Foley
State Auditor

Mike.Foley@nebraska.gov
PO Box 98917
State Capitol, Suite 2303
Lincoln, Nebraska 68509
402-471-2111, FAX 402-471-3301
auditors.nebraska.gov

December 13, 2022

Mr. Paul Turman, Chancellor
Board of Trustees
Nebraska State College System
1327 H Street, Suite 200
Lincoln, Nebraska 68508-3751

Dear Mr. Turman:

We have audited the financial statements of the Nebraska State College System (NSCS) (a component unit of the State of Nebraska) for the year ended June 30, 2022, and have issued our report thereon dated December 13, 2022.

Our audit procedures were designed primarily to enable us to form an opinion on the Basic Financial Statements. Our audit procedures were also designed to enable us to report on internal control over financial reporting and on compliance and other matters based on an audit of financial statements performed in accordance with government auditing standards and, therefore, may not bring to light all weaknesses in policies or procedures that may exist. We aim, however, to use our knowledge of the NSCS's organization gained during our work, and we make the following comments and recommendations that we hope will be useful to you.

The following is a summary of our Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*. Our complete report can be found with our report on the financial statements of the Nebraska State College System dated December 13, 2022.

We have audited 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, the financial statements of the business type activities, fiduciary activities, and the discretely presented component units of the NSCS, as of and for the year ended June 30, 2022, and the related notes to the financial statements, which collectively comprise the NSCS's basic financial statements, and have issued our report thereon dated December 13, 2022. Our report includes a reference to other auditors who audited the financial statements of the Nebraska State College System Foundations, the Nebraska State Colleges Facilities Corporation, and the activity of the Nebraska State College System Revenue and Refunding Bond Program, as described in our report on the NSCS's financial statements. The financial statements of these entities and program were not audited in accordance with *Government Auditing Standards*; accordingly, this report does not include the results of the other auditors' testing of internal control over financial reporting or compliance and other matters that are reported on separately by those auditors.

Report on Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the NSCS's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the NSCS's internal control. Accordingly, we do not express an opinion on the effectiveness of the NSCS's internal control.

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 NSCS's financial statements will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency* is a deficiency or 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.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Report on Compliance and Other Matters

As part of obtaining reasonable assurance about whether the NSCS's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards.*

Nebraska State College System's Response to Findings

We did note certain other matters that we reported to management of the NSCS, which are included below. The NSCS's responses to our findings are described below. The NSCS's responses were not subjected to the auditing procedures applied in the audit of the financial statements; accordingly, we express no opinion on them.

Comment No. 2022-001: Financial Statement Errors

During our audit of the financial statements of the Nebraska State College System (NSCS), we noted errors that resulted in significant misstatements. We proposed the NSCS adjust its financial statements to correct the identified misstatements. The NSCS did adjust the financial statements for all proposed adjustments.

The following are the significant misstatements the NSCS corrected:

- Additions for Scholarship Receipts and Deductions for Scholarship Expense on the Statement of Changes in Fiduciary Net Position were understated by $136,981. Students received scholarships from outside organizations that were awarded to the student with the funds provided to their college and applied to the student's account. These outside scholarships were considered a fiduciary activity for the NSCS under Governmental Accounting Standards Board (GASB) Statement No. 84, *Fiduciary Activities*, and should have been reported on the Statement of Changes in Fiduciary Net Position; however, an error was made when determining the Chadron State College outside scholarship amount.

- Due to errors made in recording 309 Task Force activity, Peru State College (PSC) understated State Grants and Contracts – Operating revenue by $126,399; Supplies, Services, and Other expense by $66,398; and overstated Accounts Payable by $60,000. The NSCS received funding from the State of Nebraska through the 309 Task Force to fund various facility projects. As the 309 Task Force expenditures were paid directly by the State, for the benefit of the NSCS, the NSCS makes an entry on their accounting system, SAP, to record revenues and expenditures for amounts paid by the 309 Task Force. PSC did not make two entries necessary to reflect the 309 Task Force activity.

- During testing of Federal Grants and Contracts revenue at PSC, the Auditor of Public Accounts noted the following four errors: 1) direct loans are a pass-through activity and were eliminated on the Statement of Revenues, Expenses, and Changes in Net Position; however, when completing this entry, the amount eliminated was understated by $161,418; 2) Federal Grants and Contracts revenue was recorded as Operating Revenue on the financial statements initially, and an adjustment made to reclass from Operating to Non-Operating was overstated by $130,965; 3) Federal revenue for indirect costs of $24,226 was incorrectly recorded as Other Operating Revenue but should be Federal Grants & Contracts – Operating; and 4) when reconciling the Federal expenditures and revenues, it was noted that $71,666 of expenditures were incurred during fiscal year 2022, but the revenue was recorded to fiscal year 2023, and an entry should have been recorded to accrue an Accounts Receivable and Federal Grants & Contracts – Operating revenue for this amount. These errors had the following effect in total:

Line Item	Over (Under) Stated Amount
Federal Grants & Contracts – Operating	$ (65,439)
Other Operating Revenue	$ 24,226
Federal Grants & Contracts – Non-Operating	$ 130,965
Scholarships & Fellowships Expense	$ 161,418
Accounts Receivable	$ (71,666)

- PSC and Chadron State College (CSC) used Higher Education Emergency Relief Funds (HEERF) to discharge student account balances. These expenses were recorded initially as Scholarships and Fellowships expense but should have been included in Supplies, Services, and Other expense. As a result, Scholarships and Fellowships expense was overstated, and Supplies, Services, and Other expense was understated by $293,332 at CSC and $422,081 at PSC. Additionally, the HEERF receipts used to discharge balances were improperly included in the scholarship allowance to reduce Scholarship and Fellowship expense, Tuition and Fee revenue, and Auxiliary Enterprises revenue. This caused Tuition and Fees revenue to be understated by $137,847 at CSC and $61,982 at PSC, and Auxiliary Enterprises revenue to be understated by $45,949 at CSC and $36,533 at PSC.

- PSC did not capitalize $505,185 in expenditures for its Geothermal Utilities Project. As a result, Capital Assets, Net was understated by $505,185, and Supplies, Services, and Other expense was overstated by $505,185.

- Two PSC expenditures, totaling $297,691, were recorded as fiscal year 2023 expenditures; however, the expenditures were for services provided during fiscal year 2022 and should have been recorded in fiscal year 2022. This caused Accounts Payable and Supplies, Services, and Other expense to be understated by $297,691.

- In preparing its financial statements, PSC did not eliminate alternative loan activity, which resulted in Private Grants and Contracts revenue and Scholarships and Fellowships expense to be overstated by $221,094. PSC records expenditures and revenues related to processing alternative loan activity. An alternative loan is a private loan obtained by a student through a financial institution, which verifies the student's status with the college and remits the loan funds to the college for application to the student's account. Because the college does not have an administrative role in such process, this would be considered pass-through activity and should be eliminated from the financial statements.

- PSC overstated State Grants and Contracts – Non-Operating revenue and understated Unearned Revenue by $234,353 in fiscal year 2022 and $108,785 in fiscal year 2021 for revenue received but not expended on the Corrections Workforce Development Program (CWDP). Per an agreement between the two entities, the Department of Corrections provides funding to PSC at the start of each semester to operate the CWDP and provide Corrections Leadership Scholarships to students enrolled in this program. Because revenue received for this program exceeded the expenditures thereof, such excess revenue should be reported as unearned revenue.

- CSC's net position classifications did not agree to documentation provided by CSC. The documentation to support net position classifications was correct, except for the calculation of Restricted for Plant net position. This caused the following misstatements, in total:

Line Item	Over (Under) Stated Amount
Restricted for Plant	$ 141,595
Restricted for Other	$ 900,217
Unrestricted	$ (1,041,812)

- During fiscal year 2022, the NSCS implemented GASB Statement No. 87, *Leases*, for improved accounting and financial reporting for leases. When preparing the Statement of Cash Flows, information was not presented in the schedule of noncash transactions for Acquisitions of Right to Use Assets through Lease Obligations. The NSCS had $27,706 and $635,217 of Acquisitions of Right to Use Assets through Lease Obligations for fiscal years 2022 and 2021, respectively.

A good internal control plan and sound accounting practices require financial information to be complete and accurate. This includes procedures to ensure the financial statements are correct, and adjustments are made.

Without such procedures, there is an increased risk that material misstatements may occur and remain undetected.

A similar finding has been noted since the fiscal year 2016 audit.

> While the NSCS has improved procedures related to the preparation of its financial statements, we recommend the NSCS continue to strengthen procedures to ensure internally prepared information is complete and accurate upon submission to the auditors.

NSCS's Response: The NSCS understands that accuracy of the financial statements is important. The NSCS remains committed to finding ways to continue to improve on existing procedures for the financial statement preparation and review process prior to submission to reduce financial statement errors. To address some of the findings noted above:

- *There was a change in staff responsible for preparing the financial statement at PSC for the audit period. It is now evident that additional support is needed for new staff and that better documentation on how to handle various adjustments and entries related to the items identified to be put into place. NSCS will work to document common financial preparation entries in the accounting manual to provide additional guidance for new employees. Additional support from the System Office will be offered to the Colleges when we have staff turnover.*

- *The HEERF funding used for the discharge of student account balances was a unique situation with limited guidance available. We will ensure that any future expenditures of HEERF related to discharging student account balances are recorded using NACUBO's guidance if no additional guidance becomes available.*

- *For future GASB implementation, the NSCS will continue to work towards ensuring all financial reporting requirements are met.*

NSCS concurs with the statement that improved procedures are necessary to ensure accurate and complete financial statements, and we plan to work on improving our procedures and documentation this coming year by focusing on areas where errors and omissions were made this past year.

INFORMATION TECHNOLOGY (IT) COMMENTS

Comment No. 2022-002: Password Settings

The NSCS's Identity Management system, is used for setting a global password policy. In addition, the NSCS also establishes password settings and authenticates to the Nebraska Student Information System (NeSIS) and to SAP, the NSCS accounting system, through various active directories.

During our review of the NSCS password settings, we noted that all authenticators used to access NeSIS and SAP were not salted and hashed as required by the National Institute of Standards and Technology (NIST) Digital Identity Guidelines.

Additionally, during testing of reauthentication settings it was noted that not all users were required to reauthenticate to SAP and NeSIS, within the time limits established by NIST guidelines.

University of Nebraska (University) staff manage the SAP and NeSIS applications on behalf of both the University and State Colleges. The University's Password Policy, Version 1.1 (Revised March 4, 2014), states the following:

> *Any credential which identifies a subject or service account should follow recommendations outlined in National Institute of Standards (NIST) 800-63-2 [2], [3] using a token method and the level of entropy or randomness as outlined in §§ 6.1.2 and 6.3.*

NIST has since issued Special Publication (SP) 800-63-3 in June 2017, which supersedes NIST SP 800-63-2. This more recent publication, along with SP 800-63A, SP 800-63B, and SP 800-63C, provides technical guidance to agencies for the implementation of digital authentication standards.

NIST SP 800-63B (June 2017), § 5.1.1.2, states, in relevant part, the following:

> *Verifiers SHALL store memorized secrets in a form that is resistant to offline attacks. Memorized secrets SHALL be salted and hashed using a suitable one-way key derivation function. Key derivation functions take a password, a salt, and a cost factor as inputs then generate a password hash. Their purpose is to make each password guessing trial by an attacker who has obtained a password hash file expensive and therefore the cost of a guessing attack high or prohibitive.*

NIST SP 800-63B (June 2017), § 4.2.3, states, in relevant part, the following:

> *Reauthentication of the subscriber SHALL be repeated following any period of inactivity lasting 30 minutes or longer. The session SHALL be terminated (i.e., logged out) when either of these time limits is reached.*

Good internal control includes system-enforced password parameters to ensure users meet minimum password standards.

Inadequate password settings increase the risk of unauthorized users gaining access to sensitive information contained in both the NeSIS and SAP applications.

A similar finding has been noted since the fiscal year 2011 audit.

> We recommend the NSCS work with the University to strengthen its password parameters to achieve compliance with NIST standards.

NSCS's Response: The University of Nebraska and Nebraska State College System continue to work together to align password settings, policies, and procedures to the NIST 800-63-3 standards. The reauthentication settings have been updated to align with NIST guidelines.

Comment No. 2022-003: General Ledger Transactions in SAP

The workflow in the SAP system does not require separate preparers and posters of General Ledger (GL) type transactions, primarily journal entries that do not result in vendor payments. As a result, certain individuals throughout the NSCS could complete GL transactions from beginning to end without a documented secondary review and approval in SAP. Each NSCS location (the three Colleges and the System Office) developed its own unique compensating controls to address this inherent system weakness. However, in general, the compensating controls put in place at all NSCS locations included a manual documentation of the preparer and poster of the GL transactions.

During our audit of the GL security roles in SAP, we identified 25 users with the ability to prepare and post GL entries in SAP without a secondary, system-required review or approval. The 25 users are noted by location below, along with the GL document types they could prepare and post:

Location	# of Users
Chadron State College (CSC)	6
Peru State College (PSC)	7
Wayne State College (WSC)	7
NSCS System Office	4
UNOP (University)	1

(Document Types: JE – Journal Entry, IB – Internal Charges Batch, IC – Internal Charges Online)

A secondary role allowed 24 of those 25 users to prepare and post additional GL document types. The 24 users capable of preparing and posting additional GL document types without a secondary, system-required review or approval are noted by location below, along with the GL document types they could prepare and post:

Location	# of Users
CSC	6
PSC	6
WSC	7
NSCS System Office	4
UNOP (University)	1

(Document Types: CN – ACH Receipt, ND – NIS Journal Entry*, UU – University Only Journal Entry**, UA – Accrual Journal Entry, PJ – Payroll Journal Entry, TC – Interstate Billing Transaction)

**NIS refers to the State's EnterpriseOne accounting system.*
***Role is used for College Only Journal Entries; however, the document type is also used by the University of Nebraska, which shares the SAP environment with the State Colleges.*

A good internal control plan requires a proper segregation of duties to ensure that no one individual can process a transaction from beginning to end. A good internal control plan also includes adequate security controls, through the design, creation, approval, and assignment of user roles, to prevent users from performing functions that do not allow for a proper segregation of duties.

When individuals are able to complete GL transactions without a system-required, documented, secondary review and approval prior to posting the transaction to the GL, there is a greater risk for error and for inappropriate GL transactions to occur and remain undetected. Additionally, in the absence of an adequate segregation of duties, there is an increased risk of loss, theft, or misuse of funds.

A similar finding has been noted since the fiscal year 2014 audit.

> We recognize that the NSCS has worked to implement compensating controls to mitigate the risks related to the SAP system's lack of an established workflow, which would automatically require a segregation of duties in the preparation and posting of GL entries. Nevertheless, we continue to recommend that the NSCS work on a system-based SAP solution as well.

NSCS's Response: The Colleges review the users' access annually and determines if current access is necessary based on how the roles are defined within SAP. As noted above by the auditors, the NSCS has compensating controls in place.

Comment No. 2022-004: Accounts Payable (A/P) Transactions

During our audit of the A/P security roles in SAP, the NSCS's accounting system, we noted that seven users had the ability to prepare an invoice, post it in SAP, and also approve and post it in EnterpriseOne (E1), the State's accounting system. Additionally, two of the seven users had the ability to create a purchase order, prepare the invoice related thereto, and post the transaction in both SAP and E1. Finally, six of the seven users could set up a vendor in SAP.

The seven users who could prepare invoices and post them in SAP and E1 are noted by location below:

Location	# of Users
Chadron State College (CSC)	2
Peru State College (PSC)	3
Wayne State College (WSC)	0
NSCS System Office	2

Two of the seven users identified above could also prepare a purchase order, as noted by location below:

Location	# of Users
CSC	0
PSC	0
WSC	0
NSCS System Office	2

Six of the seven users identified above could also set up a vendor in SAP, as noted by location below:

Location	# of Users
CSC	2
PSC	2
WSC	0
NSCS System Office	2

The A/P roles in SAP did not restrict users from posting their own transactions. Those transactions were entered into E1 through an interface process. The users above had the ability to approve and post transactions that flowed through the interface process in E1.

A good internal control plan requires a proper segregation of duties to ensure that no one individual can process a transaction from beginning to end. A good internal control plan also includes adequate security controls, through the design, creation, approval, and assignment of user roles, to prevent users from performing functions that do not allow for a proper segregation of duties.

A lack of segregation of duties in the A/P process allows a single individual to make purchases and pay vendors without a secondary review or approval. Additionally, some of those users had the ability to create new vendor records in SAP. This risk allows for the possible theft and misuse of State funds.

A similar finding has been noted since the fiscal year 2014 audit.

> We recommend the NSCS review the security design of the A/P roles in SAP and implement controls that require separate individuals to prepare and post A/P transaction types. We also recommend reviewing users with the ability to create vendors in SAP to ensure a proper segregation of duties exists.

NSCS's Response: The Colleges review the SAP and EnterpriseOne users' access for all accounting staff annually and make changes as necessary to ensure adequate daily operations while still striving to meet best practices for internal control. The NSCS agrees that this deserves continued efforts and will continue to seek solutions that will further diminish risk and take into account the NSCS's small operating staff.

* * * * * *

It should be noted that this letter is critical in nature, as it contains only our comments and recommendations on the areas noted for improvement and does not include our observations of any strengths of the NSCS.

Draft copies of the comments and recommendations included in this management letter were furnished to the NSCS administrators to provide them with an opportunity to review and respond to them. All formal responses received have been incorporated into this management letter. Responses have been objectively evaluated and recognized, as appropriate, in the management letter. Responses that indicate corrective action has been taken were not verified at this time, but they will be verified in the next audit.

This letter is intended solely for the information and use of management, the Board of Trustees, others within the NSCS, and the appropriate Federal and regulatory awarding agencies and pass-through entities, and it is not intended to be, and should not be, used by anyone other than these specified parties.

Sincerely,

Zachary Wells

Zachary Wells, CPA, CISA
Assistant Deputy Auditor