NEBRASKA AUDITOR OF PUBLIC ACCOUNTS

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Kara Valentine, Director
Nebraska Department of Environment and Energy
245 Fallbrook Blvd, Suite 100
Lincoln, Nebraska 68521

Dear Ms. Valentine:

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 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, 2024, and the related notes to the financial statements, which collectively comprise the State's basic financial statements, and have issued our report thereon dated December 18, 2024. In planning and performing our audit of the financial statements, we considered the State's system of 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, 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 Environment and Energy (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 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 (Accounting Errors) to be a significant deficiency.

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 management 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 management letter. *Government Auditing Standards* require the auditor to perform limited procedures on the responses. The responses were not subjected to the other auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it. 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, 2024.

1. <u>Accounting Errors</u>

The Department is responsible for accurate reporting of accrual information to the Department of Administrative Services – State Accounting Division (State Accounting) for proper financial statement and footnote presentation. The following errors were identified in the Department's accrual reporting for the Clean Water State Revolving Fund (CWSRF) and Drinking Water State Revolving Fund (DWSRF) programs that required adjustments to the financial statements:

Issue	Affected Accounts	Amount
Federal Fund	We identified errors affecting the following accounts: Beginning Balance, Transfers Out, Expenditures, Federal Grants, and Contracts Revenue.	$ 6,871,860
Environmental Quality Fund	We identified errors affecting the following accounts: Transfers In, Beginning Balance, and Expenditures.	$ 1,380,420
	Total Adjusted	**$ 8,252,280**

A description of the issues requiring such adjustments is provided below:

- During previous audits, the Department failed to properly accrue for loan payments from the CWSRF and DWSRF programs when the reimbursement request was received prior to fiscal year end, but the payment was made after fiscal year end. A portion of the payments was paid from the Federal Fund, and the loans receivable was recorded in the Environmental Quality Fund, a non-major Special Revenue Fund. This required an adjustment to the beginning fund balance for both funds. An adjustment was also required to the transfer accounts for each fund to offset the current year entries.

- The Department also failed to accrue for loan forgiveness and grant expenditures during the fiscal year 2023 audit. This error resulted in the beginning fund balance and related expenses for fiscal year 2024 being overstated in both the Federal Fund and Environmental Quality Fund.

- The Department failed to record a Due from Federal Government receivable for Federal expenditures incurred during fiscal year 2023, for which the Federal revenue was not received until fiscal year 2024. This error resulted in the beginning fund balance being understated and the related revenue being overstated in the Federal Fund for fiscal year 2024.

Other significant errors were also identified by the APA. The State's accounting system allows users to identify transactions applicable to the prior fiscal year by applying a certain code to the transaction. When transactions are identified with this code, State Accounting records an entry to remove the expense from the current year activity and to adjust the beginning fund balance. The APA reviewed a sample of prior and current year expenditures to determine whether the transactions were reported in the proper fiscal year. The following table identifies a summary of issues related to the recording of these expenditures and other transactions.

Fund	Issue	Amount
Federal Fund	Overstatement of Accounts Payable	$ 16,912,092
Environmental Quality Fund	Overstatement of Accounts Payable	$ 10,084,505
Both Funds	Misstated expenses, loans receivable, due from Federal Government receivable, revenues, and transfers	$ 6,970,779

The APA proposed, and State Accounting posted, these adjustments to the financial statements.

A proper system of internal control requires procedures to ensure that accruals are properly reported to State Accounting. Without such procedures, there is an increased risk of material misstatements to the financial statements, which could remain undetected.

> We recommend the Department strengthen procedures for reviewing and identifying accrual activity to ensure that financial information is properly reported.

Department Response: We agree with the audit finding. The accrual entries noted in this finding were recorded in a methodology that is no longer used by the agency. Going forward, the agency has improved the method of identifying, reviewing, and reporting accruals. Internal controls were adjusted to reflect the new method. We will also work with DAS throughout the accrual reporting timeframe to ensure accruals are more accurately reported.

2. Pollution Remediation Accrual

According to a July 2022 press release on the Department's website, thousands of contaminated sites exist nationally due to improper management of hazardous waste. The Comprehensive Response, Compensation and Liability Act (CRCLA) from 1980 created what is known as a Superfund to clean up the sites. Once the U.S. Environmental Protection Agency (EPA) identifies a site as a Superfund site, the Department begins to provide assistance through the Superfund Management Assistance Program. Nebraska has 18 active Superfund sites – 13 in the cleanup phase and 5 in the study phase.

For financial statement purposes, a pollution remediation obligation (liability) is an obligation to address the current or potential detrimental effects of existing pollution by participating in pollution remediation activities. For example, obligations to clean up spills of hazardous wastes or hazardous substances and obligations to remove contamination such as asbestos are pollution remediation obligations. For fiscal year 2024, the Department reported a $40 million pollution remediation liability for future obligations.

The APA identified various errors in the Department's calculation of the liabilities reported to State Accounting for three sites due to the use of outdated expected cost amounts and not adjusting for future cost increases. Such errors resulted in the variances as presented below:

Site Name	NDEE Reported Liability	APA Calculated Liability	Variance
Cleburn Street Well Site	$ 1,154,000	$ 2,113,000	$ 959,000
Garvey Elevator Site	$ 6,635,000	$ 3,868,133	$ (2,766,867)
Parkview Well Site	$ 4,500,000	$ 5,790,177	$ 1,290,177
		Total	**$ (517,690)**

The Department provided the APA with updated documentation for its liability calculations, which was different than the documentation provided to State Accounting for its accrual. Although the revised documentation was not included in the accrual for the fiscal year 2024 financial statements, the APA reviewed the revised information to ensure the calculations were proper going forward. For one of the sites included in the revised documentation, the APA identified issues with the new projections due to the inaccurate calculation of expected cost increases, resulting in the variance shown below:

Site Name	NDEE Reported Liability	APA Calculated Liability	Variance
Parkview Well Site	$ 5,841,930	$ 5,932,990	$ 91,060

A proper system of internal control requires procedures to ensure that all liabilities are calculated correctly and updated timely upon the receipt of new information. Without such controls, there is an increased risk of material reporting errors in the State's Annual Comprehensive Financial Report (ACFR).

> We recommend the Department implement procedures to ensure that all liability amounts reported to State Accounting for inclusion in the ACFR are accurate and supported by adequate documentation and the estimates are updated in a timely manner upon receipt of new information.

Department Response: We agree with the audit finding. During the initial reporting and review of this accrual, personnel responsible for summarizing and reporting the ACFR item encountered many questions, considered approaches, and summarized the accrual to the best of their ability. The agency has reviewed its approach to estimating and documenting the accrual. The agency will use a slightly different method of estimation for SFY25 accruals related to this item. The new method will include Federal provided estimation details as well as updated actual-to-projection estimations.

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

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. 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.

The purpose of this letter is solely to describe the scope of our testing of internal control over financial reporting and compliance and the result of that testing, and not to provide an opinion on the effectiveness of State's internal control over financial reporting or compliance.

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 suitable for any other purposes. However, this communication is a matter of public record, and its distribution is not limited.

Kris Kucera

Kris Kucera, CPA, CFE
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