

**AUDIT REPORT
OF THE
NEBRASKA DEPARTMENT OF
CORRECTIONAL SERVICES
CORNHUSKER STATE INDUSTRIES**

JULY 1, 2000 THROUGH JUNE 30, 2001

NEBRASKA DEPARTMENT OF CORRECTIONAL SERVICES
CORNHUSKER STATE INDUSTRIES

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NEBRASKA DEPARTMENT OF CORRECTIONAL SERVICES
CORNHUSKER STATE INDUSTRIES

BACKGROUND

In 1967, the Division of Corrections was created within the Department of Public Institutions. The Department of Correctional Services (Department) was established as a separate agency of State government in 1973. The Department has responsibility for custody, control, study, correctional treatment, training, and rehabilitation of persons committed to it so they may be prepared for lawful and productive community living.

To further this goal, the Department operates Cornhusker State Industries (CSI), which enables the Department Director to make available to inmates participation in productive work in traditional industries and private venture projects. The first prison industry shop opened in 1886 and operated the following shops: shoes, furniture, laundry, paint, and canning. In 1935, the Legislature passed an act providing for what is commonly called the "State Use System of Prison Industries" and in 1969 passed the law that authorizes CSI to exist.

CSI locates its various operations in a majority of the department's secure adult institutions. Inmate on-the-job training is currently available in the areas of painting, printing, sheet metal, furniture manufacturing, signs, soaps and detergents, garments, mattresses, word processing, and Braille materials. Tax-supported agencies, political subdivisions, public schools and colleges, and charitable, fraternal, or registered non-profit organizations may purchase the items produced by CSI's traditional industries. Braille materials may be sold to individuals and firms.

Private venture projects, which operate under the sponsorship of the Private Sector/Prison Industry Enhancement Certification Program of the U.S. Department of Justice, started in 1988. Inmates work for a private company within the institution while fulfilling a variety of requirements imposed by the federal government. CSI also provides inmate labor for road and park crews and delivery services.

MISSION STATEMENT

The mission of the Department of Correctional Services is to serve and protect the public by providing control, humane care and program opportunities for those individuals placed in its custody and supervision, thereby facilitating their return to society as responsible persons.

NEBRASKA DEPARTMENT OF CORRECTIONAL SERVICES
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SUMMARY OF COMMENTS

During our audit of the Nebraska Department of Correctional Services - Cornhusker State Industries (CSI), we noted certain matters involving the internal control over financial reporting and other operational matters that are presented here. Comments and recommendations are intended to improve the internal control over financial reporting, ensure compliance, or result in operational efficiencies.

The four items below were brought forward from our fiscal year ended June 30, 2000 audit of CSI. These items were brought forward in summary form, as CSI had not corrected them as of the date of this report. The fiscal year ended June 30, 2000 report was issued in September 2001 and the Department has not had sufficient time to correct these deficiencies. In addition, item number 1, **Segregation of Duties Over Receipts**; the third bullet of item number 2, **Some bonuses are not equitably distributed**; item number 3, **Audit Delays**; and item number 4, **Late Payments**, were also noted in our fiscal year ended June 30, 2001 audit of CSI.

1. **Segregation of Duties Over Receipts:** We noted one individual opened the mail, prepared deposits, posted payments to the receivable accounts, and prepared the general document to deposit the payments to the Department's bank account.

We also noted no reconciliation of accounts receivable was being performed. A lack of segregation of duties increases the possibility of loss or misuse of state funds.

2. **Inmate Pay:** During our testing of inmate wage and bonus payments we noted:
 - Bonuses were overpaid in 8 shops by a total of \$5,061.
 - Twelve workers in one shop did not receive eligible bonuses of \$130 each.
 - Some bonuses are not equitably distributed.
3. **Audit Delays:** The availability of the Department of Corrections staff and records to complete the audit in a timely manner was not made available to us. For this reason the audit completion was delayed several months.
4. **Late Payments:** Twenty-eight of 199 invoices tested were not paid within 45 days as required by State Statute.

Department's Response: As you have noted in the Summary of Comments our response to the points noted can be found in the FY2000 audit. We do however feel it important to note that efforts will be undertaken to avoid audit delays in the future.

Draft copies of this report were furnished to the Department of Corrections and to CSI to provide them an opportunity to review the report and to respond. The Departments response to the summary comments noted above can be found in the fiscal year ending June 30, 2000 audit of CSI. This report can be obtained from the Auditor of Public Accounts. All formal responses received have been incorporated into this report. Responses have been objectively evaluated and recognized, as appropriate, in the report. Responses that indicate corrective action has been taken were not verified at this time but will be verified in the next audit.

We appreciate the cooperation and courtesy extended to our auditors during the course of the audit.

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NEBRASKA DEPARTMENT OF CORRECTIONAL SERVICES CORNHUSKER STATE INDUSTRIES

INDEPENDENT AUDITORS' REPORT

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We have audited the accompanying general purpose financial statements of the Nebraska Department of Correctional Services - Cornhusker State Industries as of and for the fiscal year ended June 30, 2001, as listed in the Table of Contents. These general purpose financial statements are the responsibility of the Department's management. Our responsibility is to express an opinion on these general purpose financial statements based on our audit.

We conducted our audit 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1, the general purpose financial statements present only the Nebraska Department of Correctional Services - Cornhusker State Industries and are not intended to present fairly the financial position and results of operations of the State of Nebraska, in conformity with generally accepted accounting principles.

In our opinion, the general purpose financial statements referred to above present fairly, in all material respects, the financial position of the Nebraska Department of Correctional Services - Cornhusker State Industries, as of June 30, 2001, and the results of its operations and cash flows of its proprietary fund for the year then ended in conformity with generally accepted accounting principles.

In accordance with Government Auditing Standards, we have also issued our report dated October 3, 2001, on our consideration of the Nebraska Department of Correctional Services - Cornhusker State Industries' internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, and contracts. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

October 3, 2001


Manager

NEBRASKA DEPARTMENT OF CORRECTIONAL SERVICES
 CORNHUSKER STATE INDUSTRIES
BALANCE SHEET
INTERNAL SERVICE FUND 5251
 June 30, 2001

	Cornhusker State Industries Fund 5251
ASSETS	
<hr/>	
CURRENT ASSETS:	
Cash in State Treasury	\$ 2,849,669
Deposit with Vendors	275
Petty Cash	6,000
Receivables, net of allowance:	
Accounts	1,183,200
Private Venture	11,103
Interest	11,510
Merchandise Inventory	2,560,598
TOTAL CURRENT ASSETS	<hr/> 6,622,355 <hr/>
Property, Plant and Equipment, Net	5,640,827
TOTAL ASSETS	<hr/> \$ 12,263,182 <hr/> <hr/>
 LIABILITIES AND FUND EQUITY	
<hr/>	
CURRENT LIABILITIES:	
Accounts Payable	\$ 405,206
Accrued Payroll	94,584
TOTAL LIABILITIES	<hr/> 499,790 <hr/>
NONCURRENT LIABILITIES,	
Accrued Compensated Absences	249,512
TOTAL NONCURRENT LIABILITIES	<hr/> 249,512 <hr/>
TOTAL LIABILITIES	<hr/> 749,302 <hr/>
FUND EQUITY,	
Retained Earnings	11,513,880
TOTAL FUND EQUITY	<hr/> 11,513,880 <hr/>
TOTAL LIABILITIES AND FUND EQUITY	<hr/> \$ 12,263,182 <hr/> <hr/>

See Notes to General Purpose Financial Statements.

NEBRASKA DEPARTMENT OF CORRECTIONAL SERVICES
 CORNHUSKER STATE INDUSTRIES
**STATEMENT OF REVENUES, EXPENSES,
 AND CHANGES IN RETAINED EARNINGS**
INTERNAL SERVICE FUND 5251
 For the Year Ended June 30, 2001

	Cornhusker State Industries <u>Fund 5251</u>
OPERATING REVENUES:	
Charges for Services	\$ 7,377,526
Other	7,015
Private Venture Revenues	<u>401,616</u>
TOTAL OPERATING REVENUES	<u>7,786,157</u>
 OPERATING EXPENSES:	
Personal Services	2,270,217
Operating Expenses	4,528,845
Travel Expenses	86,205
Depreciation Expense	<u>253,163</u>
TOTAL OPERATING EXPENSES (Note 6)	<u>7,138,430</u>
OPERATING INCOME	<u>647,727</u>
 NONOPERATING REVENUES:	
Interest Income	177,469
Gain on Sale of Fixed Asset	<u>2,523</u>
TOTAL NONOPERATING REVENUES	<u>179,992</u>
NET INCOME	827,719
RETAINED EARNINGS, JULY 1, 2000	<u>10,686,161</u>
RETAINED EARNINGS, JUNE 30, 2001	<u>\$ 11,513,880</u>

See Notes to General Purpose Financial Statements.

NEBRASKA DEPARTMENT OF CORRECTIONAL SERVICES
 CORNHUSKER STATE INDUSTRIES
STATEMENT OF CASH FLOWS
INTERNAL SERVICE FUND 5251
 For the Year Ended June 30, 2001

	Cornhusker State Industries <u>Fund 5251</u>
CASH FLOWS FROM OPERATING ACTIVITIES:	
Cash Received from Sales & Charges	\$ 7,457,316
Cash Paid to Employees	(2,258,241)
Cash Paid to Suppliers	<u>(5,570,875)</u>
NET CASH FLOWS FROM OPERATING ACTIVITIES	<u>(371,800)</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:	
Acquisition and Construction of Capital Assets	(861,431)
Proceeds from Sale of Fixed Assets	<u>2,523</u>
NET CASH FLOWS FROM CAPITAL AND RELATED ACTIVITIES	<u>(858,908)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:	
Interest Income	<u>182,029</u>
NET CASH FLOWS FROM INVESTING ACTIVITIES	<u>182,029</u>
NET INCREASE IN CASH	(1,048,679)
CASH AND CASH EQUIVALENTS, JULY 1	3,904,623
CASH AND CASH EQUIVALENTS, JUNE 30	<u>\$ 2,855,944</u>
RECONCILIATION OF OPERATING INCOME TO NET CASH FLOWS FROM OPERATING ACTIVITIES:	
Operating Income	<u>\$ 647,727</u>
Adjustments to reconcile operating income to net cash flows from operating activities:	
Depreciation	253,163
Non-Cash Operating Expenses	10,143
Change in Assets and Liabilities:	
(Increase) in Accounts Receivable	(592,209)
Decrease in Private Venture Receivable	263,568
(Increase) in Inventories	(1,179,395)
Increase in Accounts Payable	213,227
Increase in Accrued Payroll	10,372
Increase in Accrued Compensating Absences	<u>1,604</u>
Total Adjustments	<u>(1,019,527)</u>
NET CASH FLOWS FROM OPERATING ACTIVITIES	<u>\$ (371,800)</u>

See Notes to General Purpose Financial Statements.

NEBRASKA DEPARTMENT OF CORRECTIONAL SERVICES
 CORNHUSKER STATE INDUSTRIES
**STATEMENT OF RECEIPTS, DISBURSEMENTS,
 AND CHANGES IN FUND BALANCE - FUND 5251**
 BUDGET AND ACTUAL (Budgetary Basis)
 For the Year Ended June 30, 2001

	REVOLVING FUND		
	BUDGET	ACTUAL (BUDGETARY BASIS)	VARIANCE FAVORABLE (UNFAVORABLE)
RECEIPTS:			
Sales and Charges		\$ 7,055,287	
Miscellaneous		<u>590,660</u>	
TOTAL RECEIPTS		<u><u>7,645,947</u></u>	
DISBURSEMENTS:			
Personal Services	\$ 2,241,218	2,258,241	\$ (17,023)
Operating	7,566,922	5,484,670	2,082,252
Travel	113,500	86,205	27,295
Capital Outlay	<u>166,500</u>	<u>861,431</u>	<u>(694,931)</u>
Total Budgeted	10,088,140	8,690,547	1,397,593
Under Budgeted	<u>459,263</u>		<u>459,263</u>
TOTAL DISBURSEMENTS	<u><u>10,547,403</u></u>	<u><u>8,690,547</u></u>	<u><u>1,856,856</u></u>
Excess of Receipts Over Disbursements		<u>(1,044,600)</u>	
OTHER FINANCING SOURCES (USES):			
Sale of Assets		2,523	
Net Distributive Activity		<u>(200)</u>	
TOTAL OTHER FINANCING SOURCES (USES)		<u><u>2,323</u></u>	
Excess of Receipts and Other Financing Sources Over Disbursements and Other Financing (Uses)		(1,042,277)	
FUND BALANCES, JULY 1, 2000		<u>3,894,323</u>	
FUND BALANCES, JUNE 30, 2001		<u><u>\$ 2,852,046</u></u>	

See Notes to General Purpose Financial Statements.

NEBRASKA DEPARTMENT OF CORRECTIONAL SERVICES
CORNHUSKER STATE INDUSTRIES

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS
For the Fiscal Year Ended June 30, 2000

1. Summary of Significant Accounting Policies

- A. Basis of Presentation.** The accompanying general purpose financial statements of the Nebraska Department of Correctional Services (Department) - Cornhusker State Industries (CSI) have been prepared in conformance with generally accepted accounting principles (GAAP) as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

The general purpose financial statements have been prepared primarily from accounts maintained by the State Accounting Administrator of the Department of Administrative Services.

- B. Reporting Entity.** The Department is a State agency established under and governed by the laws of the State of Nebraska. As such, the Department is exempt from State and federal income taxes. The financial statements include all funds of CSI. CSI has also considered all potential component units for which it is financially accountable, and other organizations which are fiscally dependent on CSI, or the significance of their relationship with CSI are such that exclusion would be misleading or incomplete. The GASB has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of CSI to impose its will on that organization, or (2) the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on CSI.

As required by generally accepted accounting principles, these financial statements present the Nebraska Department of Correctional Services - Cornhusker State Industries. No component units were identified. The Nebraska Department of Correctional Services - Cornhusker State Industries is part of the primary government for the State of Nebraska's reporting entity.

- C. Fund Structure.** The Department's accounts are maintained in accordance with the principles of fund accounting to ensure compliance with limitations and restrictions placed on the use of resources available to it. Under fund accounting, individual funds are established for the purpose of carrying on activities or attaining objectives in accordance with specific regulations, restrictions, or limitations. Each individual fund is a self-balancing set of accounts recording cash and other financial resources, together with liabilities and residual equities or

NEBRASKA DEPARTMENT OF CORRECTIONAL SERVICES
CORNHUSKER STATE INDUSTRIES

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS
(Continued)

1. **Summary of Significant Accounting Policies (Continued)**

balances, and changes therein. These generic fund types differ from the Department's budgetary funds which are described later in Note 2. A brief description of the fund type as used in the Department and the category into which it is grouped follows:

Proprietary Funds. Transactions related to activities similar to those found in the private sector. Proprietary funds include:

Internal Service Funds. Reflect transactions used to account for centrally operated services and centrally procured commodities which are provided to other State departments and agencies and other governmental units of the State. The services and commodities are charged to recipient agencies on a cost-reimbursement basis.

D. Basis of Accounting. The accounting and financial reporting treatment applied to a fund is determined by its measurement focus.

All proprietary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operation of these funds are included on the balance sheet. Fund equity (i.e., net total assets) is segregated into contributed capital and retained earnings components. Proprietary fund-type operating statements present increases (e.g., revenues) and decreases (e.g., expenses) in net total assets.

The Department applies all applicable GASB pronouncements, as well as the requirements of FASB Statements and Interpretations, APB Opinions, and ARBs, issued on or before November 30, 1989, unless they conflict with or contradict GASB pronouncements. In addition, the Department applies all FASB Statements and Interpretations issued after November 30, 1989, except those that conflict with or contradict GASB pronouncements in accounting and reporting for its operations.

The accrual basis of accounting is utilized by proprietary fund types. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

E. Cash. Cash reported on the balance sheet is under the control of the State Treasurer or other administrative bodies as determined by law. All cash deposited with the State Treasurer is maintained by the Treasurer in an investment pool.

NEBRASKA DEPARTMENT OF CORRECTIONAL SERVICES
CORNHUSKER STATE INDUSTRIES

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS
(Continued)

1. **Summary of Significant Accounting Policies (Continued)**

The State Investment Officer invests the deposited cash in short-term securities and other investments. Interest revenue is allocated to CSI's Proprietary fund 5251 based on average balances of all invested funds.

- F. Receivables.** Receivables are stated net of estimated allowances for uncollectible amounts, which are determined based upon past collection experience and current economic conditions. The receivables in the proprietary funds are amounts that have arisen in the normal course of business.
- G. Inventories.** Inventories of materials and supplies are determined by both physical counts and through perpetual inventory systems. Proprietary funds valuation method is primarily at the lower of cost (first in, first out) or market.
- H. Fixed Assets.** All purchased fixed assets are valued at cost, where historical records are available, and at estimated historical cost, where no historical records exist. Donated fixed assets are valued at their estimated fair market value on the date received.

Fixed assets do not include infrastructure such as highways, bridges, and lighting systems, as these assets are immovable and of value only to the government. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend asset life are not capitalized.

For the period July 1, 2000 through December 31, 2000, equipment which had a cost in excess of \$300 at the date of acquisition and had an expected useful life of two or more years was capitalized. For the period January 1, 2001 through June 30, 2001, equipment which had a cost in excess of \$1000 at the date of acquisition and had an expected useful life of two or more years was capitalized. Initial building costs, land, land improvements, building improvements, and renovations are capitalized case by case based on management review.

Depreciation of machinery, equipment, and buildings in the proprietary fund types is recorded using the straight-line method.

- I. Compensated Employee Absences.** All permanent employees working for the Department earn sick and annual leave and are allowed to accumulate compensatory leave rather than being paid overtime. Temporary and intermittent employees are not eligible for paid leave.

NEBRASKA DEPARTMENT OF CORRECTIONAL SERVICES
CORNHUSKER STATE INDUSTRIES

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS
(Continued)

1. **Summary of Significant Accounting Policies (Continued)**

Department employees accrue vested annual leave at a variable rate based on years of service. Generally, accrued annual leave cannot exceed 35 days at the end of a calendar year.

Employees accrue sick leave at a variable rate based on years of service. In general, accrued sick leave cannot exceed 180 days for employees under the Nebraska Classified System Personnel Rules and Regulations. In general, there is no maximum limit on the accumulation of sick days for employees under a labor contract. Sick leave is not vested, except upon death or upon reaching the retirement eligibility age of 55, at which time the State is liable for 25 percent of the employee's accumulated sick leave. Employees under labor contracts can be paid a maximum of 50 days. It is the Department's policy to liquidate unpaid annual leave, vested sick leave, and compensatory leave from future sources rather than from currently available expendable resources.

All internal service funds recognize the expense and accrued liability when vacation and compensatory leave is earned or when sick leave is expected to be paid as termination payments.

J. Revenues. The major account titles and descriptions as used by the Department are:

Operating Revenues/Sales and Charges. Income is derived from sales of merchandise and commodities, and compensation for services rendered.

Non-Operating Revenues/Miscellaneous Receipts. Revenues from sources not covered by other major categories, which consists primarily of interest income on the Statement of Revenues, Expenses, and Changes in Retained Earnings. Miscellaneous receipts on the Statement of Receipts, Expenditures, and Changes in Fund Balance, Budget and Actual consists of interest income, and receipts primarily from Private Venture operations.

K. Expenses. The major account titles and descriptions used by the Department on the Statement of Revenues, Expenses, and Changes in Retained Earnings are:

Personal Services. Salaries, wages, and related employee benefits provided for all persons employed by a government.

Operating. Expenses directly related to a program's primary service activities.

NEBRASKA DEPARTMENT OF CORRECTIONAL SERVICES
CORNHUSKER STATE INDUSTRIES

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS
(Continued)

1. **Summary of Significant Accounting Policies (Concluded)**

Travel. All travel expenses for any state officer, employee, or member of any commission, council, committee, or board of the State.

Depreciation Expense. An annual expense of using capital assets.

L. **Disbursements.** The major account titles and descriptions used by the Department on the Statement of Receipts, Disbursements, and Changes in Fund Balance, Budget and Actual are:

Personal Services. Salaries, wages, and related employee benefits provided for all persons employed by a government.

Operating. Expenses directly related to a program's primary service activities.

Travel. All travel expenses for any state officer, employee, or member of any commission, council, committee, or board of the State.

Capital Outlay. Disbursements which result in the acquisition of or an addition to fixed assets. Fixed assets are resources of a long-term character, owned or held by the government.

2. **Budgetary Process**

The Department's biennial budget cycle ends on June 30 of the odd-numbered years. By September 15, prior to a biennium, the Department must submit its budget request for the biennium beginning the following July 1. The requests are submitted on forms that show estimated funding requirements by programs, sub-programs, and activities. The Executive Branch reviews the requests, establishes priorities, and balances the budget within the estimated resources available during the upcoming biennium.

The Governor's budget bill is submitted to the Legislature in January. The Legislature considers revisions to the bill and submits the revised appropriations bill to the Governor for signature. The Governor may: a) approve the appropriations bill in its entirety, b) veto the bill, or c) line item veto certain sections of the bill. Any vetoed bill or line item can be overridden by a three-fifths vote of the Legislature.

The appropriations that are approved will generally set spending limits for a particular program within the agency. Within the agency or program, the Legislature may provide funding from one to five budgetary fund types. Thus, the control is by fund type, within a

NEBRASKA DEPARTMENT OF CORRECTIONAL SERVICES
CORNHUSKER STATE INDUSTRIES

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS
(Continued)

2. Budgetary Process (Continued)

program, within an agency. The central accounting system maintains this control. A separate publication entitled "Annual Budgetary Report" shows the detail of this level of control. This publication is available from the Department of Administrative Services, Accounting Division.

Appropriations are usually made for each year of the biennium with unexpended balances being reappropriated at the end of the first year of the biennium. For most appropriations, balances lapse at the end of the biennium.

The budgetary fund type used by the Department differs from the fund type presented in the financial statements. In the Statement of Receipts, Expenditures, and Changes in Fund Balance – Budget to Actual the Department's Fund is identified as a Revolving Fund. A Revolving Fund accounts for the financing of goods or services provided by one State agency to another State agency on a cost-reimbursement basis.

The accompanying financial statements were prepared by classifying budgetary fund data into the fund format required by GAAP. The cash basis of accounting is used for all budgetary fund types.

All State budgetary expenditures for the revolving fund type are made pursuant to the appropriations which may be amended by the Legislature, upon approval by the Governor. State agencies may allocate the appropriations between major object of expenditure accounts, Increases in total revolving fund appropriations must also be approved by the Legislature as a deficit appropriations bill.

The Department utilizes encumbrance accounting to account for purchase orders, contracts, and other expenditure commitments. However, State law does not require that all encumbrances be recorded in the State's centralized accounting system, and, as a result, the encumbrances that were recorded in the accounting system have not been included in the accompanying financial statements, except for the impact as described below.

Under State budgetary procedures, appropriation balances related to outstanding encumbrances at the end of the biennium are lapsed and reappropriated in the first year of the next biennium. The effect of the Department's current procedure is to include in the budget columns, Total Expenditure line, of the Statement of Revenues, Expenditures, and Changes in Fund Balances - Budget and Actual the current year's appropriations plus the amounts reappropriated for encumbrances outstanding at the end of the prior biennium. This procedure indicates the Department's intention to honor the encumbrances at the end

NEBRASKA DEPARTMENT OF CORRECTIONAL SERVICES
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NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS
(Continued)

2. Budgetary Process (Concluded)

of a biennium. The expenditures columns of the Statement include cash payments related to the appropriated and reappropriated amounts. For the year ended June 30, 2001, there were no budgetary funds in which expenditures exceeded appropriations.

Budgets for object of expenditure accounts are included in the Nebraska Department of Administrative Services Budget Status Report. However, as noted on the Statement of Revenues, Expenditures, and Changes in Fund Balances - Budget and Actual the Department did not budget \$459,263 of the amount appropriated to the Department for CSI fund 5251.

The Revenues are not budgeted. Therefore, there are no budgeted amounts shown on the Budget and Actual Statement.

A reconciliation of the budgetary versus the financial statements funds as of June 30, 2001 follows:

	BUDGETARY FUND EQUITIES	FINANCIAL STATEMENT FUND EQUITIES
		PRIMARY GOVERNMENT
		Internal Service
	Total	
PERSPECTIVE DIFFERENCES:		
Classifications of budgetary fund equities into Financial Statement fund structure:		
Revolving	\$ 2,852,655	\$ 2,852,655
Budgetary fund equities classified into Financial Statement fund structure	\$ 2,852,655	
BASIS DIFFERENCES:		
Record fixed assets		5,640,827
Record net accrued receivables, liabilities, and inventories		3,020,398
Financial Statement Fund Equities, June 30, 2001		\$ 11,513,880

NEBRASKA DEPARTMENT OF CORRECTIONAL SERVICES
CORNHUSKER STATE INDUSTRIES

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS
(Continued)

3. **Fixed Assets**

The following is a summary of proprietary fund-type fixed assets at June 30, 2001:

Machinery and equipment	\$	2,312,062
Buildings		5,598,783
Land		315,000
Total		<u>8,225,845</u>
Less: Accumulated Depreciation		<u>(2,585,018)</u>
Net Fixed Assets	\$	<u><u>5,640,827</u></u>

In the proprietary fund the following estimated useful lives are used to compute depreciation:

Buildings	20-40 years
Equipment	5-20 years

4. **State Employees Retirement Plan (Plan)**

The Plan is a single-employer defined contribution plan administered by the Public Employees Retirement Board in accordance with the provisions of the State Employees Retirement Act and may be amended by Legislative action. In the defined contribution plan, retirement benefits depend on total contributions, investment earnings, and the investment options selected. Membership in the Plan is required of all permanent full-time employees on reaching the age of thirty and completion of twenty-four months of continuous service, and voluntary participation is permitted for all permanent full-time or part-time employees upon reaching age twenty and completion of twelve months of service within a five-year period, except any individual appointed by the Governor may elect to not become a member of the Plan.

Employees contribute 4.33% of their monthly compensation until such time as they have paid during any calendar year a total of eight hundred sixty four dollars, after which time they shall pay a sum equal to 4.8% of their monthly compensation for the remainder of such calendar year. The Department matches the employee's contribution at a rate of 156% of the employee's contribution.

The employee's account is fully vested. The employer's account is vested 100% after five years participation in the plan or at retirement.

For the Fiscal Year Ended June 30, 2001, the Department's employees contributed \$70,264 and the Department contributed \$109,612.

NEBRASKA DEPARTMENT OF CORRECTIONAL SERVICES
CORNHUSKER STATE INDUSTRIES

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS
(Continued)

5. **Contingencies and Commitments**

Risk Management. The Department is exposed to various risks of loss related to torts, theft of, damage to, and destruction of assets, errors and omissions, injuries to employees, natural disasters, and health care insurance. The Department, as part of the primary government for the State, participates in the State's risk management program. The Nebraska Department of Administrative Services (DAS) Division of Risk Management is responsible for maintaining the insurance and self-insurance programs for the State. The State generally self-insures for general liability and workers compensation. The State has chosen to purchase insurance for:

1. Motor vehicle liability, which is insured for the first \$5 million of exposure per accident. Insurance is also purchased for medical payments, physical damage, and uninsured and underinsured motorists with various limits and deductibles.
2. Health care insurance for employees selecting certain coverage options. All health care insurance was purchased.
3. Crime coverage, with a limit of \$1 million for each loss, and a \$10,000 retention per incident.
4. Real and personal property on a blanket basis for losses up to \$250,000,000, with a self-insured retention of \$100,000 per loss occurrence. The perils of flood and earthquake are covered up to \$9,000,000. Newly-acquired properties are covered up to \$1,000,000 for 60 days or until the value of the property is reported to the insurance company.

No settlements exceeded commercial insurance coverage in any of the past three fiscal years. Health care insurance is funded in the Risk Management Internal Service Fund through a combination of employee and State contributions. Worker's compensation is also funded in the Risk Management Internal Service Fund through assessments on each agency based on total agency payroll and past experience. Tort claims, theft of, damage to, or destruction of assets, errors or omissions, and natural disasters would be funded through the State General Fund or by individual agency assessments as directed by the Legislature, unless covered by purchased insurance. No amounts for estimated claims have been reported in the Nebraska Department of Correctional Services - Cornhusker State Industry's financial statements.

NEBRASKA DEPARTMENT OF CORRECTIONAL SERVICES
CORNHUSKER STATE INDUSTRIES

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS
(Continued)

5. Contingencies and Commitments (Concluded)

Litigation. The potential amount of liability involved in litigation pending against the Department, if any, could not be determined at this time. However, it is the Department's opinion that final settlement of those matters should not have an adverse effect on the Department's ability to administer current programs. Any judgement against the Department would have to be processed through the State Claims Board and be approved by the Legislature.

6. Total Operating Expenses

Total Operating Expenses include only those costs charged directly to CSI. The Department incurs other costs related to CSI that are not included in the financial statement. These other Department costs could include Accounting and Finance, Director and Director of Administrative Services, Budget, Engineering, Legal Training, and Human Resources. These other costs are budgeted in the General Fund.

7. GASB 34

In June 1999, the Governmental Accounting Standards Board (GASB) issued Statement No. 34, Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments. The State of Nebraska is planning to implement the Statement for the fiscal year ending June 30, 2002. The new accounting and reporting standards will impact the State's revenue and expenditure recognition and assets, liabilities, and fund equity reporting. The financial statements will be reformatted to reflect the new standards.

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NEBRASKA DEPARTMENT OF CORRECTIONAL SERVICES
CORNHUSKER STATE INDUSTRIES
**REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER
FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL
STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

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We have audited the general purpose financial statements of the Nebraska Department of Correctional Services - Cornhusker State Industries as of and for the year ended June 30, 2001, and have issued our report thereon dated October 3, 2001. The report was modified to emphasize that the financial statements present only the funds of the Nebraska Department of Correctional Services - Cornhusker State Industries. We conducted our audit 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.

Compliance

As part of obtaining reasonable assurance about whether the Nebraska Department of Correctional Services - Cornhusker State Industries' general purpose financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contracts, 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 that are required to be reported under Government Auditing Standards. We noted certain immaterial instances of noncompliance that we have reported to management of the Nebraska Department of Correctional Services - Cornhusker State Industries in the Comments Section of the fiscal year ending June 30, 2000 report (see Summary of Comments section of the report) for comments identified as Inmate Pay and Late Payments.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Nebraska Department of Correctional Services - Cornhusker State Industries's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting that we have reported to management of Nebraska Department of Correctional Services – Cornhusker State Industries in the Comments Section of the fiscal year ending June 30, 2000 report (see Summary of Comments section of the report) for the comment identified as Segregation of Duties Over Receipts.

This report is intended solely for the information and use of the agency, the appropriate Federal and regulatory agencies, and citizens of the State of Nebraska, and is not intended to be and should not be used by anyone other than these specified parties.

October 3, 2001



Manager