



NEBRASKA AUDITOR OF PUBLIC ACCOUNTS

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Ronnie D. Mitchell, Director
Nebraska Department of Aeronautics
3431 Aviation Road
Lincoln, NE 68524

Dear Mr. Mitchell:

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, 2016, in accordance with auditing standards generally accepted in the United States of America and standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, we have issued our report thereon dated December 15, 2016. 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 Department Aeronautics (Agency) or other operational matters that are presented below for your consideration. This comment and recommendation, which have been discussed with the appropriate members of the Agency's management, are intended to improve internal control or result in other operating efficiencies.

Our consideration of internal control included a review of prior year comments and recommendations. To the extent the situations that prompted the recommendations in the prior year still exist, they have been incorporated in the comment presented for the current year. All other prior year comments and recommendations (if applicable) have been satisfactorily resolved.

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

Draft copies of this letter were furnished to the Agency to provide management with an opportunity to review and to respond to the comment and recommendation contained herein. Any formal response received has been incorporated into this letter. Such response has been objectively evaluated and recognized, as appropriate, in the letter. A response that indicates corrective action has been taken was not verified at this time, but it will be verified in the next audit.

The following is our comment and recommendation for the year ended June 30, 2016.

1. Hanger Loan Receivable

The Department of Administrative Services, State Accounting Division (State Accounting), prepares the State of Nebraska Comprehensive Annual Financial Report (CAFR) and requires all State agencies to determine and report payable and receivable amounts at the end of the fiscal year on an accrual response form.

The Agency provides funding to public-use airports for the purpose of increasing or improving the hangar space. This funding is in the form of a loan that must be paid back to the Agency in the future. Any outstanding loans were reported as a receivable in the CAFR financial statements. At June 30, 2016, the hangar loan receivable balance for one airport was overstated by \$438,207.

The airport applied for a Federal grant to pay for an existing loan received from the Agency. The Federal grant was approved on June 2, 2016. The Agency did not receive the Federal monies to pay off the loan until after June 30, 2016. Since Federal funds were going to be used to pay off this loan, there should have been no receivable due from the airport. Rather, there should have been a receivable due from the Federal government. The Auditor of Public Accounts proposed adjustment was made by State Accounting to correct the CAFR financial statements for this error.

A good internal control plan requires agencies to have adequate procedures for the reporting of accurate and complete financial information to State Accounting.

When loan balances are not recorded properly at fiscal year end, there is an increased risk that the financial statements will be inaccurate.

We recommend the Agency implement procedures to ensure the accuracy of loan receivable balances and accrual information submitted to State Accounting for inclusion in the CAFR.

Agency Response: Several months after providing a hanger loan to the City of Valentine, they applied for a federal grant to cover the costs of the hanger. The federal grant was signed by the Federal Aviation Administration (FAA) on June 16, 2016.

The grant itself is a contract between the FFA and the airport, NOT between the department and the airport. The Hanger Loan Agreement, however, is the contract in question. Regardless of where the money originated to pay the loan back, the airport was responsible for the payment of the loan according to the loan agreement.

Aeronautics acts as agent on behalf of the airports in the state, and we channel the money from the FAA through to the airports. When that is done, we perform a netting function to recover any agency costs involved in performance of our duties as agent. Also, we would recover any other monies due from the airport to the department on this project. We recovered the loan funds in question in the netting function to pay off the loan for which the AIRPORT was obligated and as provided under the terms of the Hangar Loan Agreement.

APA Response: In July 2016, the Agency received the grant funds directly from the FAA, not from the City. FAA grant approval and congressional release of funds occurred prior to June 30, 2016, and the Agency was aware of the grant funds it was to receive from the FAA on behalf of the City. During our testing, the Agency agreed originally that the grant should be included as a receivable due from the federal government.

GASBS 24 – Accounting and Financial Reporting for Certain Grants and Other Financial Assistance, Pass-Through Grants (paragraph 34), states the following:

NCGA Statement 1, paragraph 18(3), states that agency funds are purely custodial. The Board believes that if a recipient government has administrative involvement in a pass-through grant, its responsibility in relation to the resources is more than custodial; the recipient government is essentially exercising operational responsibility. Research shows that the types of administrative involvement recipient governments have with pass-through grants include (a) monitoring secondary recipients for compliance with program-specific requirements, (b) determining eligible secondary recipients or projects, even if using grantor-established criteria, and (c) having the ability to exercise discretion in how the funds are allocated. A recipient government's administrative involvement with a pass-through grant usually takes place both before and after the grantor government makes the award. However, some pass-through grants may involve only pre-award administrative involvement by the recipient government. For example, in several states, federal Airport Improvement Program grants (CFDA program number 20.106) pass through the state government because of state legislation—called “channeling acts”—that requires airports that apply for the grants to coordinate their activities through a state aviation agency or board that controls the content and submission of the grant application. This grant meets this Statement's criteria for reporting as revenue and expenditures and expenses based on the state government's pre-award administrative involvement.

(Emphasis added.) Additionally, GASB Codification N50 – Nonexchange Transactions, Determining Fund Types for Reporting Pass-through Grants (paragraph 128), provides the following:

Governmental entities often receive grants and other financial assistance to transfer to or spend on behalf of a secondary recipient. These amounts are referred to as pass-through grants. All cash pass-through grants received by a governmental entity (referred to as a recipient government) should be reported in its financial statements. As a general rule, cash pass-through grants should be recognized as revenue and expenditures or expenses in the funds of the primary government and in the government-wide financial statements.

Finally, Neb. Rev. Stat. § 3-124 (Reissue 2012), authorized the Agency to administer pass-through funds for privately owned public use airports, as follows:

The department is authorized to accept federal and other money, either public or private, for and on behalf of this state, any municipality, or any person owning a privately owned public use airport, for the acquisition, construction, improvement, maintenance, and operation of airports and other air navigation facilities, whether such work is to be done by the state, by such municipalities, or by any person owning a privately owned public use airport, or jointly, aided by grants of aid from the United States, upon such terms and conditions as are or may be prescribed by the laws of the United States and any rules or

regulations made thereunder. The department may act as agent of any municipality of this state or any person owning a privately owned public use airport, upon the request of such municipality or person, in accepting such money in its behalf for airports or other air navigation facility purposes, and in contracting for the acquisition, construction, improvement, maintenance, or operation of airports or other air navigation facilities, financed either in whole or in part by federal money, and such person or the governing body of any such municipality is authorized to designate the department as its agent for such purposes and to enter into an agreement with it prescribing the terms and conditions of such agency in accordance with federal laws, rules, and regulations and with the State Aeronautics Department Act. Such money as is paid over by the United States Government shall be retained by the state or paid over to the municipalities or persons under such terms and conditions as may be imposed by the United States Government in making such grants.

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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 Agency 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 Agency.

This communication is intended solely for the information and use of the Agency, the Governor and State Legislature, others within the Agency, 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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