AUDIT REPORT
OF THE
NEBRASKA DEPARTMENT OF
ADMINISTRATIVE SERVICES - PROGRAM 173
DIVISION OF COMMUNICATIONS

JULY 1, 2001 THROUGH JUNE 30, 2002

NEBRASKA DEPARTMENT OF ADMINISTRATIVE SERVICES
PROGRAM 173 - DIVISION OF COMMUNICATIONS

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NEBRASKA DEPARTMENT OF ADMINISTRATIVE SERVICES
PROGRAM 173 - DIVISION OF COMMUNICATIONS

BACKGROUND

The Department of Administrative Services (DAS) Division of Communications was established by the 1975 Legislature. By this act, the Legislature expanded the scope and the authority of the Telecommunications Bureau, which had functioned as the Telecommunications Coordinating Agency since 1967.

The Division reviews the communications operations of all State agencies and helps design new or improved systems. Equipment utilization is reviewed and the Division coordinates the lease and purchase of communications equipment by all agencies. The Division coordinates and assists all State agencies and local political subdivisions in obtaining radio frequencies, manages the State telephone and data networks, and provides mutual communications support for emergency management agencies and local governments. The Division's statutory duties are administered by five operating sections, each run by a manager.

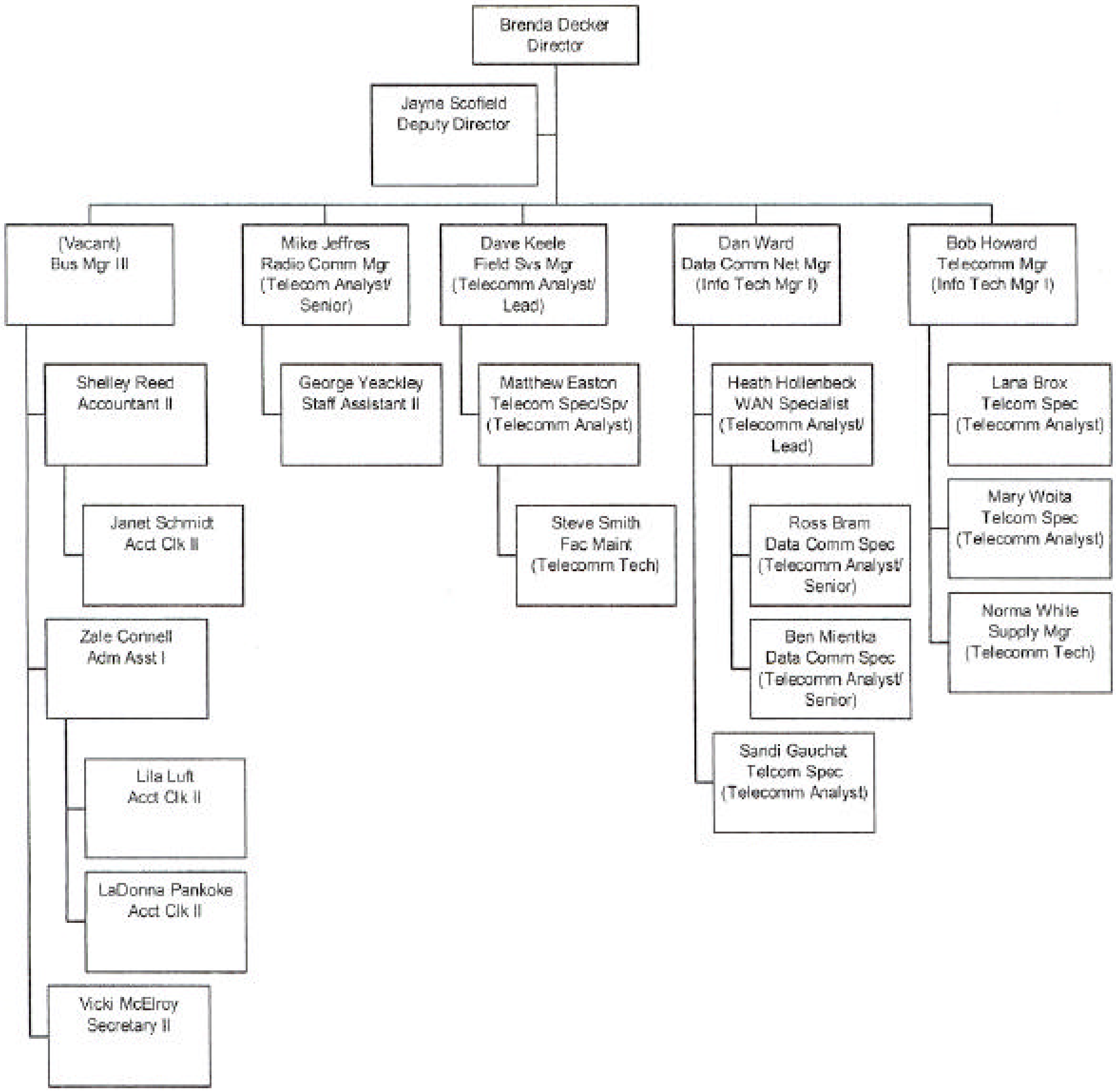
The Division also publishes and distributes the Nebraska State Government Directory. The manual provides names and telephone numbers of State agencies and employees, and agencies' addresses.

MISSION STATEMENT

The mission of the Department of Administrative Services - Division of Communications is to provide efficient, economical, and reliable telecommunications services for State government.

ORGANIZATIONAL CHART

(July 15, 2002)



COMMENT AND RECOMMENDATION

During our audit of the Nebraska Department of Administrative Services - Program 173 - Division of Communications, we noted certain matters involving the internal control over financial reporting and other operational matters which are presented here. Comments and recommendations are intended to improve the internal control over financial reporting, ensure compliance, or result in operational efficiencies.

Reporting Lease Obligations

The Division of Communications (Division) did not have documentation to support lease disclosure requirements in accordance with Generally Accepted Accounting Principles (GAAP). The Division had an estimated 600 leases, both capital and operating. We noted the following:

- The Division had not analyzed which leases were capital leases or which were operating leases.
- The Division did not maintain records, such as amortization schedules, to support principal and interest amounts that were required to be disclosed for capital leases in accordance with GAAP.
- The Division did not always add capital items for certain capital leased equipment on the State's capital fixed asset records, the StateWide Inventory System (SWIS). The reason given by management for this equipment not being included on SWIS was the equipment, even though being purchased on a capital lease agreement, may not have been equipment that would have been needed for the term of the lease. In those cases, the equipment was returned to the vendor and a new lease was entered into for new equipment. However, the Division had no documented policy to identify to which leases this applied.

A similar comment was noted in our fiscal year 2000 audit report of the Department of Administrative Services.

Without documentation to support lease disclosure requirements in accordance with GAAP, information required for financial statement disclosure is not readily available. In addition, when there is no policy to identify capital leases in which the Division is to own the equipment, capital assets will be understated and appropriate controls over those capital assets is lost.

> We recommend the Division of Communications review the records and determine whether the leases are capital or operating leases. Once that determination has been made, records should be kept to support the accounting for all leases in accordance with GAAP. In addition, all

COMMENT AND RECOMMENDATION

Reporting Lease Obligations (Concluded)

equipment purchased through a capital lease, in accordance with GAAP and the Division's policy, should be added to SWIS upon entering into the lease agreement, as it is an asset of the State at that time.

Division's Response: When the Division of Communications enters into the leases in question, it is not our intent to finalize the purchase of the equipment. Therefore, we do not believe that the affect of non-capitalization of these leases on our financial statements is material, particularly since we do not intend to take ownership. Additionally, the record keeping to add and remove these assets from the Statewide Inventory System at the beginning and end of the lease is cost prohibitive to the Division in relation to the immateriality of non-capitalization of the assets on the financial statements.

It should be noted this report is critical in nature since it contains only our comment and recommendation on the area noted for improvement.

Draft copies of this report were furnished to the Division to provide them an opportunity to review the report and to respond to the comment and recommendation included in this report. 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 ADMINISTRATIVE SERVICES
PROGRAM 173 - DIVISION OF COMMUNICATIONS

INDEPENDENT AUDITORS' REPORT

We have audited the accompanying fund financial statements of the Nebraska Department of Administrative Services - Program 173 - Division of Communications (Division), as of and for the year ended June 30, 2002, as listed in the Table of Contents. These financial statements are the responsibility of the Division's management. Our responsibility is to express an opinion on these 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 our audit provides a reasonable basis for our opinions.

As discussed in Note 1, these financial statements were prepared on the basis of cash receipts and disbursements, which is a comprehensive basis of accounting other than generally accepted accounting principles.

Also, as discussed in Note 1, the financial statements present only the fund financial statements of the State attributable to the transactions of the Nebraska Department of Administrative Services - Program 173 - Division of Communications. They do not purport to, and do not, present fairly the cash balances of the State of Nebraska as of June 30, 2002, and its changes in cash balances for the year then ended in conformity with the cash receipts and disbursements basis of accounting.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective cash balances of the internal service funds of the Nebraska Department of Administrative Services - Program 173 - Division of Communications, as of June 30, 2002, and the respective changes in cash balances thereof for the year then ended in conformity with the basis of accounting described in Note 1.

In accordance with Government Auditing Standards, we have also issued our report dated July 25, 2002, on our consideration of the Nebraska Department of Administrative Services - Program 173 - Division of Communication's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. 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.

Our audit was conducted for the purpose of forming an opinion on the financial statements that comprise the Program's fund financial statements. The accompanying combining statements and schedules are presented for purposes of additional analysis and are not a required part of the fund financial statements of the Nebraska Department of Administrative Services - Program 173 - Division of Communications. Such information, except for that portion marked "unaudited," on which we express no opinion, has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated in all material respects in relation to the financial statements taken as a whole.

Pat Reding, CPA

July 25, 2002 Assistant Deputy Auditor

NEBRASKA DEPARTMENT OF ADMINISTRATIVE SERVICES
PROGRAM 173 - DIVISION OF COMMUNICATIONS
STATEMENT OF ASSETS AND FUND BALANCES
ARISING FROM CASH TRANSACTIONS
PROPRIETARY FUNDS - INTERNAL SERVICE FUNDS
June 30, 2002

	Total Internal Service Funds (Memorandum Only)
Assets	
Cash in State Treasury	$ 2,634,004
Deposit with Vendors	1,984
Total Assets	$ 2,635,988
Fund Balances	
Reserved for Postage	$ 1,984
Unreserved, Undesignated	2,634,004
Total Fund Balances	$ 2,635,988

The accompanying notes are an integral part of the financial statements.

NEBRASKA DEPARTMENT OF ADMINISTRATIVE SERVICES
PROGRAM 173 - DIVISION OF COMMUNICATIONS
STATEMENT OF RECEIPTS, DISBURSEMENTS,
AND CHANGES IN FUND BALANCES
PROPRIETARY FUNDS - INTERNAL SERVICE FUNDS
For the Fiscal Year Ended June 30, 2002

	Total Internal Service Funds (Memorandum Only)
RECEIPTS:	
Sales & Charges	$ 19,804,706
Miscellaneous:	
Investment Interest	173,105
Other Miscellaneous	2,500
TOTAL RECEIPTS	19,980,311
DISBURSEMENTS BY FUNCTION:	
General Government	20,907,341
TOTAL DISBURSEMENTS	20,907,341
Excess of Receipts Over (Under) Disbursements	(927,030)
OTHER FINANCING SOURCES:	
Sales of Assets	1,883
Net Change in Fund Balances	(925,147)
FUND BALANCE, JULY 1, 2001	3,561,135
FUND BALANCE, JUNE 30, 2002	$ 2,635,988

The accompanying notes are an integral part of the financial statements.

NOTES TO FINANCIAL STATEMENTS

For the Fiscal Year Ended June 30, 2002

1. Summary of Significant Accounting Policies

The accounting policies of the Nebraska Department of Administrative Services - Program 173 - Division of Communications are on the basis of accounting as described in the Nebraska Accounting System Manual.

A. Reporting Entity

The Nebraska Department of Administrative Services - Program 173 - Division of Communications (Program) is a program within the Nebraska Department of Administrative Services. The Nebraska Department of Administrative Services is a State agency established under and governed by the laws of the State of Nebraska. As such, the Program is exempt from State and Federal income taxes. The financial statements include all funds of the Program.

The Nebraska Department of Administrative Services - Program 173 - Division of Communications is part of the primary government for the State of Nebraska's reporting entity.

B. Basis of Presentation

Fund Financial Statements. The Statement of Assets and Fund Balances Arising From Cash Transactions and the Statement of Receipts, Disbursements, and Changes in Fund Balances provide information about the Program's funds. Governmental generally accepted accounting principles (GAAP) requires separate statements by fund category - governmental, proprietary, and fiduciary. The Program uses only the proprietary fund category. The proprietary fund category includes two fund types, enterprise and internal service funds. The Program uses only the internal service fund type. In accordance with GAAP all internal service funds are reported in the aggregate.

The Program reports the following funds:

Internal Service Funds. Reflect transactions used to account for centrally operated services 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.

NOTES TO FINANCIAL STATEMENTS
(Continued)

1. Summary of Significant Accounting Policies (Continued)

C. Measurement Focus, Basis of Accounting

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus and basis of accounting. The accounting records of the Program are maintained and the fund financial statements were reported on the basis of cash receipts and disbursements. As such, the measurement focus includes only those assets and fund balances arising from cash transactions. Revenues are recognized when received and expenditures are recognized when paid for all funds of the Program. This differs from GAAP, which requires proprietary fund financial statements to be reported using the economic resources measurement focus and the accrual basis of accounting. Under this measurement focus and basis of accounting revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

D. Assets

Cash in State Treasury. Cash in the State Treasury represents the cash balance of a fund as reflected on the Nebraska Accounting System. Investment of all available cash is made by the State Investment Officer, on a daily basis, based on total bank balances. Investment income is distributed based on the average daily book cash balance of funds designated for investment. Determination of whether a fund is considered designated for investment is done on an individual fund basis. All of the funds of the Program were designated for investment during fiscal year 2002.

Inventories. Disbursements for items of an inventory nature are considered expended at the time of purchase rather than at the time of consumption.

Capital Assets. Under the cash receipts and disbursements basis of accounting, capital assets are not capitalized in the funds used to acquire or construct them. Instead, capital acquisitions are reflected as disbursements in proprietary funds. GAAP requires capital assets, which would include property, plant, equipment, and infrastructure assets (e.g., roads, bridges, sidewalks, and similar items) to be reported in the applicable governmental activities columns in the government-wide financial statements.

Depreciation expenses on capital assets were not recorded on the cash basis financial statements. Under GAAP, depreciation expenses would be recorded in the Statement of Activities. The cost of normal maintenance and repairs that does not add to the value of the asset or extend asset life is not capitalized.

NOTES TO FINANCIAL STATEMENTS
(Continued)

1. Summary of Significant Accounting Policies (Concluded)

Compensated Absences. All permanent employees working for the Program 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. Under the receipts and disbursements basis of accounting, the liabilities for compensated absences are not reported since they do not represent liabilities arising from cash transactions. Under GAAP, the compensated absences liability would be reported in the government-wide and proprietary financial statements, and would be recorded in accordance with the State of Nebraska policy which is to 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.

E. Fund Balance Reservations

Reservations of fund balances are established to identify the existence of assets that have been legally segregated for specific purposes. Reservations of fund balances are also established for assets which are not current in nature, such as postage.

2. Totals

The Totals "Memorandum Only" column represents an aggregation of individual account balances. The column is presented for overview informational purposes and does not present consolidated financial information because interfund balances and transactions have not been eliminated.

3. Contingencies and Commitments

Risk Management. The Program is exposed to various risks of loss related to torts, theft of, damage to, or destruction of assets, errors or omissions, injuries to employees, and natural disasters. The Program, 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:

A. 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. State agencies have the option to purchase coverage for physical damage to vehicles.

NOTES TO FINANCIAL STATEMENTS
(Continued)

3. Contingencies and Commitments (Concluded)

B. The DAS-Personnel Division maintains health care and life insurance for eligible employees.

C. Crime coverage, with a limit of $1 million for each loss, and a $10,000 retention per incident.

D. Real and personal property on a blanket basis for losses up to $250,000,000, with a self-insured retention of $200,000 per loss occurrence. 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. The perils of flood and earthquake are covered up to $10,000,000.

E. State agencies have the option to purchase building contents and inland marine coverage.

No settlements exceeded commercial insurance coverage in any of the past three fiscal years. Health care insurance is funded in the Compensation Insurance Trust Fund through a combination of employee and State contributions. Workers' compensation is funded in the Workers' Compensation 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 Administrative Services - Program 173 - Division of Communication's financial statements.

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

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

NOTES TO FINANCIAL STATEMENTS
(Continued)

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

depend on total contributions, investment earnings, and the investment options selected. Prior to April 18, 2002, membership in the Plan was mandatory for all permanent full-time employees on reaching the age of thirty and completion of twenty-four months of continuous service. Full time employee is defined as an employee who is employed to work one-half or more of the regularly scheduled hours during each pay period. Voluntary membership is permitted for all permanent full-time or permanent part-time employees upon reaching age twenty and completion of twelve months of permanent service within a five-year period. Any individual appointed by the Governor may elect to not become a member of the Plan. Legislative Bill 687 (2002), effective April 18, 2002, stated all permanent full-time employees shall begin participation in the plan upon completion of twelve continuous months of service.

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 pay a sum equal to 4.8% of their monthly compensation for the remainder of such calendar year. The Division matches the employee's contribution at a rate of 156%.

The employee's account is fully vested. The employer's account is vested 100% after five years participation in the system (prior to April 18, 2002) or at retirement. Legislative Bill 687 (2002), effective April 18, 2002, changed the vesting requirement to a total of three years of participation in the system, which includes the 12-month eligibility period or credit for participation in another governmental plan prior to actual contribution to the Plan.

For the fiscal year ended June 30, 2002, employees contributed $33,561 and the Division contributed $52,355.

5. Leases

The Division of Communications leases equipment and communication lines. These leases vary in length, terms, and requirements. The Division has approximately 600 leases. They provide most of the equipment and communication lines services for State agencies and political subdivisions. When an agency's service needs have changed or because of changes in technology, the equipment may become obsolete. The equipment may be returned to the vendor and a new lease agreement signed for the new equipment before the old lease expires. The Division's operating leases are primarily for communication lines.

For the fiscal year ended June 30, 2002, the Division disbursed $900,000, which includes operating leases, and principal and interest payments for capital leases. The Division expects this obligation to continue in the future with increases for inflation.

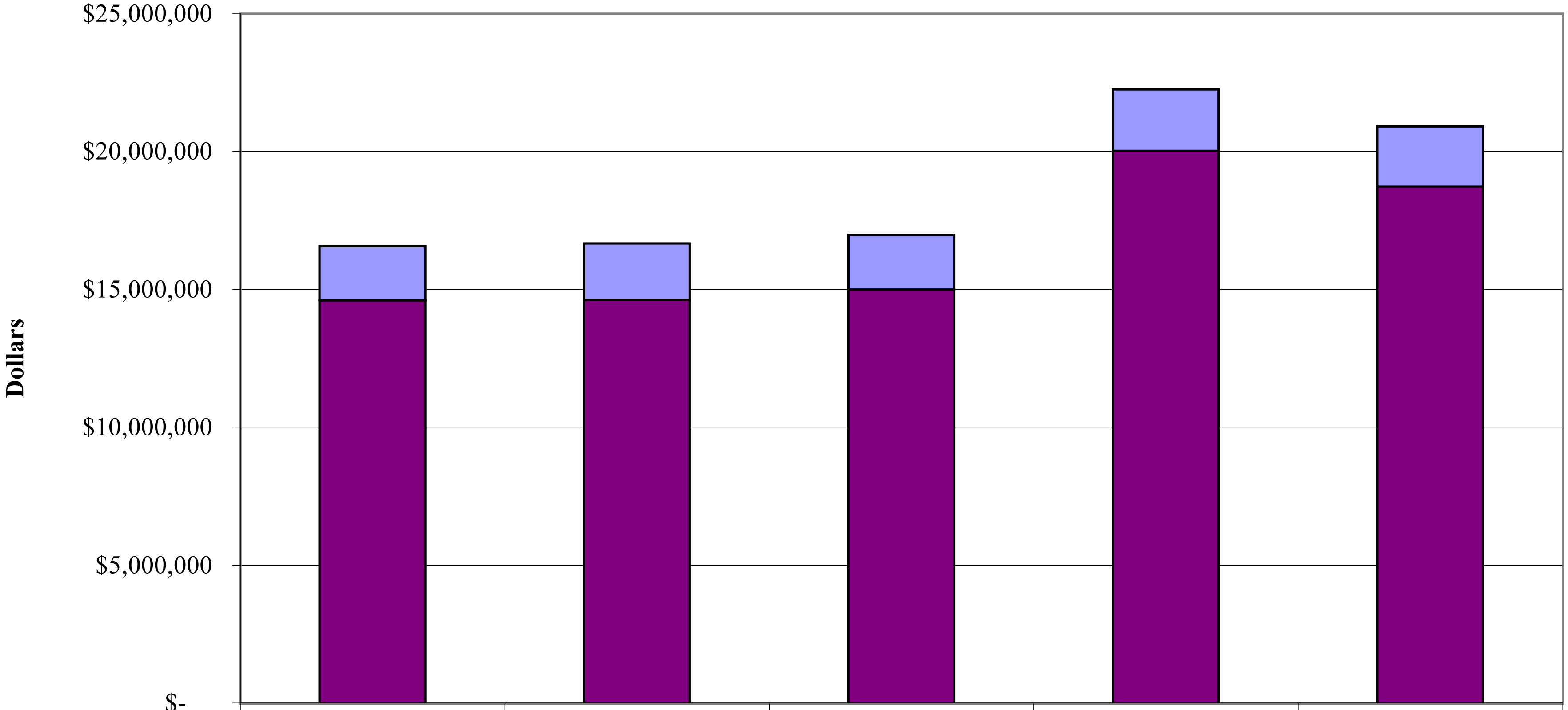
NEBRASKA DEPARTMENT OF ADMINISTRATIVE SERVICES
PROGRAM 173 - DIVISION OF COMMUNICATIONS
COMBINING STATEMENT OF ASSETS AND FUND BALANCES
ARISING FROM CASH TRANSACTIONS
INTERNAL SERVICE FUNDS
June 30, 2002

	Telecom Cash Fund 2653	Telecom Revolving Fund 5653	**Total Internal Service Funds**
Assets			
Cash in State Treasury	$ 231,478	$ 2,402,526	$ 2,634,004
Deposit with Vendors	438	1,546	1,984
Total Assets	$ 231,916	$ 2,404,072	$ 2,635,988
Fund Balances			
Reserved for:			
Postage	$ 438	$ 1,546	$ 1,984
Unreserved, Undesignated	231,478	2,402,526	2,634,004
Total Fund Balances	$ 231,916	$ 2,404,072	$ 2,635,988

NEBRASKA DEPARTMENT OF ADMINISTRATIVE SERVICES
PROGRAM 173 - DIVISION OF COMMUNICATIONS
COMBINING STATEMENT OF RECEIPTS, DISBURSEMENTS, AND CHANGES IN FUND BALANCES
INTERNAL SERVICE FUNDS
For the Fiscal Year Ended June 30, 2002

	Telecom Cash Fund 2653	Telecom Revolving Fund 5653	**Total Internal Service Funds**
RECEIPTS:			
Sales & Charges	$ 1,308,819	$ 18,495,887	$ 19,804,706
Miscellaneous:			
Investment Interest	14,181	158,924	173,105
Other Miscellaneous	2,500	-	2,500
TOTAL RECEIPTS	1,325,500	18,654,811	19,980,311
DISBURSEMENTS BY FUNCTION:			
General Government	1,376,066	19,531,275	20,907,341
TOTAL DISBURSEMENTS	1,376,066	19,531,275	20,907,341
Excess of Receipts Over (Under) Disbursements	(50,566)	(876,464)	(927,030)
OTHER FINANCING SOURCES:			
Sales of Assets	-	1,883	1,883
Net Change in Fund Balances	(50,566)	(874,581)	(925,147)
FUND BALANCES, JULY 1, 2001	282,482	3,278,653	3,561,135
FUND BALANCES, JUNE 30, 2002	$ 231,916	$ 2,404,072	$ 2,635,988

NEBRASKA DEPARTMENT OF ADMINISTRATIVE SERVICES
PROGRAM 173 - DIVISION OF COMMUNICATIONS
TOTAL DISBURSEMENTS - OVERHEAD AND DIRECT COSTS
Fiscal Years Ended June 30, 1998 through June 30, 2002
UNAUDITED



	1998	1999	2000	2001	2002
Overhead Costs	$1,968,926	$2,034,478	$1,965,376	$2,224,898	$2,187,848
Direct Costs	$14,597,194	$14,622,654	$15,002,986	$20,034,120	$18,719,492

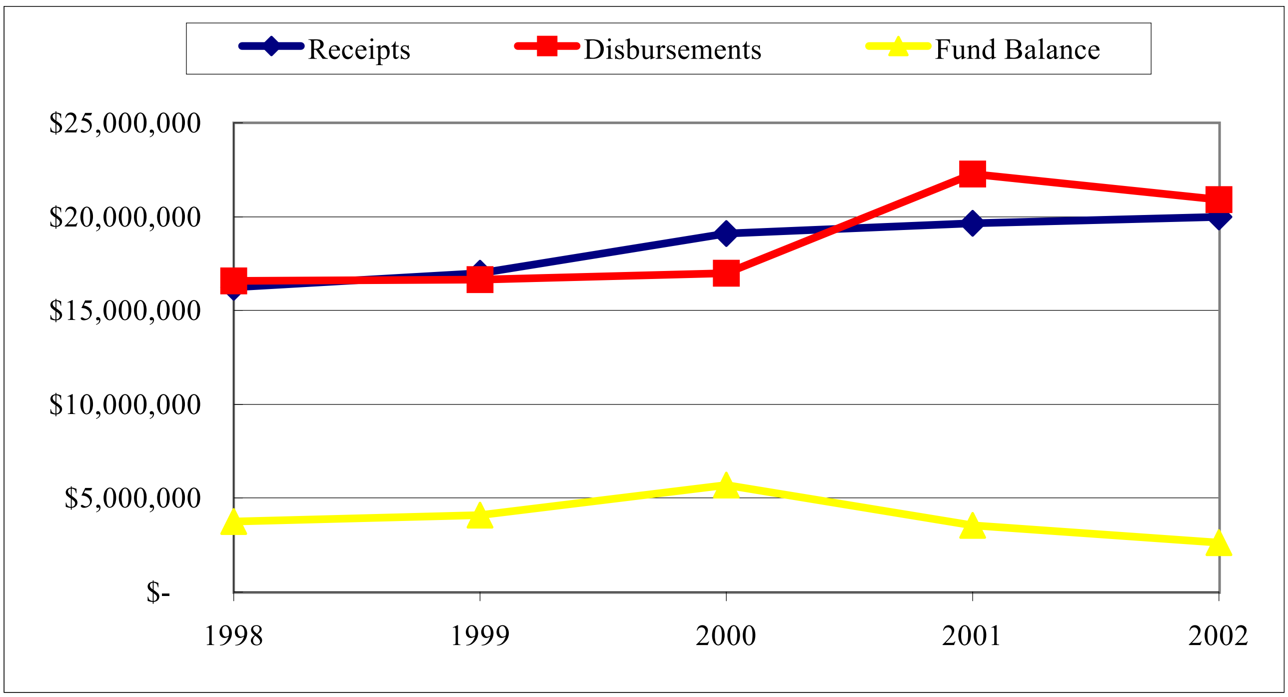
Fiscal Year

Note: Overhead includes Division administration costs such as personnel, rent, and travel. Direct costs are charges from telephone companies which are billed to user agencies.

NEBRASKA DEPARTMENT OF ADMINISTRATIVE SERVICES
PROGRAM 173 - DIVISION OF COMMUNICATIONS
FIVE-YEAR SCHEDULE OF INTERNAL SERVICE FUNDS RECEIPTS, DISBURSEMENTS, AND ENDING FUND BALANCE
Fiscal Years Ended June 30, 1998 through June 30, 2002

	Fiscal Year Ended June 30				
	1998 (Unaudited)	1999	2000	2001 (Unaudited)	2002
Receipts	$ 16,247,239	$ 17,001,789	$ 19,093,660	$ 19,633,964	$ 19,982,194
Disbursements	$ 16,566,119	$ 16,657,132	$ 16,991,561	$ 22,259,018	$ 20,907,341
Fund Balance	$ 3,739,432	$ 4,084,089	$ 5,686,188	$ 3,561,134	$ 2,635,988

Note: Receipts and Disbursements include other financing sources and uses.



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NEBRASKA DEPARTMENT OF ADMINISTRATIVE SERVICES
PROGRAM 173 - DIVISION OF COMMUNICATIONS

REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

We have audited the fund financial statements of the Nebraska Department of Administrative Services - Program 173 - Division of Communications as of and for the year ended June 30, 2002, and have issued our report thereon dated July 25, 2002. The report notes the financial statements were prepared on the basis of cash receipts and disbursements and was modified to emphasize that the financial statements present only the funds of the Nebraska Department of Administrative Services - Program 173 - Division of Communications. 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 Administrative Services - Program 173 - Division of Communication's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Nebraska Department of Administrative Services - Program 173 - Division of Communication'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.

This report is intended solely for the information and use of the Division, 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.

Pat Reding, CPA

July 25, 2002 Assistant Deputy Auditor