

**SOUTH CAROLINA  
OFFICE OF THE ADJUTANT GENERAL  
COLUMBIA, SOUTH CAROLINA**

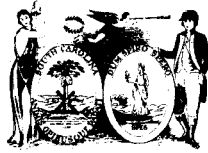
**STATE AUDITOR'S REPORT**

**JUNE 30, 2002**

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# State of South Carolina



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### INDEPENDENT ACCOUNTANT'S REPORT ON APPLYING AGREED-UPON PROCEDURES

July 14, 2003

Major General Stanhope S. Spears  
Adjutant General  
State of South Carolina  
Columbia, South Carolina

We have performed the procedures described below, which were agreed to by the management of the South Carolina Office of the Adjutant General (the Agency), solely to assist you in evaluating the performance of the Agency for the fiscal year ended June 30, 2002, in the areas addressed. The Agency's management is responsible for its financial records, internal controls and compliance with State laws and regulations. This agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. The sufficiency of these procedures is solely the responsibility of the specified parties in this report. Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

The procedures and the associated findings are as follows:

1. We tested selected recorded receipts to determine if these receipts were properly described and classified in the accounting records and internal controls over the tested receipt transactions were adequate. We also tested selected recorded receipts to determine if these receipts were recorded in the proper fiscal year. We compared amounts recorded in the general ledger and subsidiary ledgers to those in the State's accounting system (STARS) as reflected on the Comptroller General's reports to determine if recorded revenues were in agreement. We made inquiries and performed substantive procedures to determine if revenue collection and retention or remittance were supported by law. We compared current year recorded revenues from sources other than State General Fund appropriations to those of the prior year to determine the reasonableness of collected and recorded amounts by revenue account. The individual transactions selected for testing were chosen randomly. Our findings as a result of these procedures are presented in Deposits, Reconciliations and Data Translation to the State in the Accountant's Comments section of this report.

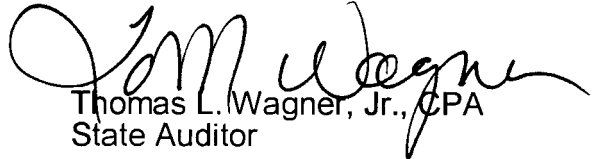
2. We tested selected recorded non-payroll disbursements to determine if these disbursements were properly described and classified in the accounting records, were bona fide disbursements of the Agency, and were paid in conformity with State laws and regulations; if the acquired goods and/or services were procured in accordance with applicable laws and regulations; and if internal controls over the tested disbursement transactions were adequate. We also tested selected recorded non-payroll disbursements to determine if these disbursements were recorded in the proper fiscal year. We compared amounts recorded in the general ledger and subsidiary ledgers to those in various STARS reports to determine if recorded expenditures were in agreement. The individual transactions selected for testing were chosen randomly. Our findings as a result of these procedures are presented in Reconciliations and Data Translation to the State in the Accountant's Comments section of this report.
3. We tested selected recorded payroll disbursements to determine if the tested payroll transactions were properly described, classified, and distributed in the accounting records; persons on the payroll were bona fide employees; payroll transactions, including employee payroll deductions, were properly authorized and were in accordance with existing legal requirements; and internal controls over the tested payroll transactions were adequate. We tested selected payroll vouchers to determine if the vouchers were properly approved and if the gross payroll agreed to amounts recorded in the general ledger and in STARS. We also tested payroll transactions for selected new employees and those who terminated employment to determine if internal controls over these transactions were adequate. The individual transactions selected for testing were chosen randomly. Our findings as a result of these procedures are presented in Reconciliations and Initial Pay in the Accountant's Comments section of this report.
4. We tested selected recorded journal entries and all operating and appropriation transfers to determine if these transactions were properly described and classified in the accounting records; they agreed with the supporting documentation, were adequately documented and explained, were properly approved, and were mathematically correct; and the internal controls over these transactions were adequate. The individual transactions selected for testing were chosen randomly. We found no exceptions as a result of the procedures.
5. We tested selected entries and monthly totals in the subsidiary records of the Agency to determine if the amounts were mathematically accurate; the numerical sequences of selected document series were complete; the selected monthly totals were accurately posted to the general ledger; and the internal controls over the tested transactions were adequate. The transactions selected for testing were chosen randomly. Our findings as a result of these procedures are presented in Reconciliations in the Accountant's Comments section of this report.

6. We obtained all monthly reconciliations prepared by the Agency for the year ended June 30, 2002, and tested selected reconciliations of balances in the Agency's accounting records to those in STARS as reflected on the Comptroller General's reports to determine if they were accurate and complete. For the selected reconciliations, we determined if they were timely performed and properly documented in accordance with State regulations, recalculated the amounts, agreed the applicable amounts to the Agency's general ledger, agreed the applicable amounts to the STARS reports, determined if reconciling differences were adequately explained and properly resolved, and determined if necessary adjusting entries were made in the Agency's accounting records and/or in STARS. Our findings as a result of these procedures are presented in Reconciliations and Data Translation to the State in the Accountant's Comments section of this report.
7. We tested the Agency's compliance with all applicable financial provisions of the South Carolina Code of Laws, Appropriation Act, and other laws, rules, and regulations for fiscal year 2002. Our findings as a result of these procedures are presented in Deposits, Reconciliations, Capital Assets Closing Package, Initial Pay and Data Translation to the State in the Accountant's Comments section of this report.
8. We reviewed the status of the deficiencies described in the findings reported in the Accountant's Comments section of the State Auditor's Report on the Agency resulting from our engagement for the fiscal year ended June 30, 2001 to determine if adequate corrective action has been taken. Our findings as a result of these procedures are presented in various comments in Section A of the Accountant's Comments as described in Section B - Status of Prior Findings in the Accountant's Comments section of this report.
9. We obtained copies of all closing packages as of and for the year ended June 30, 2002, prepared by the Agency and submitted to the State Comptroller General. We reviewed them to determine if they were prepared in accordance with the Comptroller General's GAAP Closing Procedures Manual requirements; if the amounts were reasonable; and if they agreed with the supporting workpapers and accounting records. Our findings as a result of these procedures are presented in Capital Assets Closing Package in the Accountant's Comments section of this report.
10. We obtained a copy of the schedule of federal financial assistance for the year ended June 30, 2002, prepared by the Agency and submitted to the State Auditor. We reviewed it to determine if it was prepared in accordance with the State Auditor's letter of instructions; if the amounts were reasonable; and if they agreed with the supporting workpapers and accounting records. Our findings as a result of these procedures are presented in Reconciliations and Data Translation to the State in the Accountant's Comments section of this report.

Major General Stanhope S. Spears  
Adjutant General  
State of South Carolina  
July 14, 2003

We were not engaged to and did not conduct an audit, the objective of which would be the expression of an opinion on the specified areas, accounts, or items. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the information and use of the Adjutant General and of the management of the South Carolina Office of the Adjutant General and is not intended to be and should not be used by anyone other than these specified parties.



Thomas L. Wagner, Jr., CPA  
State Auditor

**ACCOUNTANT'S COMMENTS**

## **SECTION A - MATERIAL WEAKNESSES AND/OR VIOLATIONS OF STATE LAWS, RULES OR REGULATIONS**

The procedures agreed to by the agency require that we plan and perform the engagement to obtain reasonable assurance about whether noncompliance with the requirements of State Laws, Rules, or Regulations occurred and whether internal accounting controls over certain transactions were adequate. Management of the entity is responsible for establishing and maintaining internal controls. A material weakness is a condition in which the design or operation of one or more of the specific internal control components does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Therefore, the presence of a material weakness or violation will preclude management from asserting that the entity has effective internal controls.

The conditions described in this section have been identified as material weaknesses or violations of State Laws, Rules, or Regulations.



## **INTRODUCTORY COMMENTS**

The entire operations under the South Carolina Adjutant General are very complex, including military operations at both the federal and state levels. Many employees under the Adjutant General's supervision are federal military and/or civilian employees and many of the federal military operations are funded and accounted for by federal agencies. The Adjutant General is also responsible for the South Carolina Office of the Adjutant General (the Agency), a State agency governed by the same State laws, rules, and regulations. The State Auditor's Office is responsible for any required audit functions for the Agency. These functions include an agreed-upon procedures engagement at the agency level as well as the inclusion of the State agency in the Statewide Single Audit and the audit of the State's financial statements.

For fiscal year 2002, the Agency had approximately \$8.2 million appropriations and 64 authorized full-time equivalent positions (FTEs) in general funds and approximately \$28.7 million appropriations and 163 FTEs in total funds. Most of the difference in general and total funds is federal funding for military operations, maintenance, and construction. In addition to the military operations, the Agency also has an emergency management division.

In our comments that follow we refer to the entity as "the Agency". As such, we are referring to the State agency, South Carolina Office of the Adjutant General and not to all operations under the supervision of the Adjutant General. As necessary, we will mention these other operations and attempt to denote that these areas are not part of the entity to which these engagements apply.

## **DEPOSITS**

We tested a sample of 50 deposits and noted that 14 contained receipts, totaling \$77,810, that were not deposited timely in accordance with State law and Adjutant General regulations.

Proviso 72.1. of the fiscal year 2002 Appropriation Act requires that receipts be remitted to the State Treasurer at least once each week, when practical. Also, Adjutant General Regulation (AGR) 37-2, Paragraph 1-13.c.(4) requires all funds received to be deposited by Tuesday of each week.

We again recommend that the Agency develop and implement control procedures to strengthen internal controls over cash receipts and revenues to ensure that receipts are deposited timely in accordance with the Agency's policies and State law.

## **RECONCILIATIONS**

As noted in State Auditor's reports for the five prior fiscal years, the Agency has not performed complete revenues, expenditures, cash, and CSA467 report (federal programs) reconciliations between its books and those of the State Comptroller General, who maintains the State's books (STARS), on a monthly basis. In fiscal year 2002, the Agency began reconciling the current year revenues and expenditures. We reviewed the procedures and noted that the revenue and expenditure reconciliations were properly performed, signed and dated by the preparer. However, none of the monthly reconciliations were signed and dated by the reviewer. In addition, Agency personnel told us that they have established new procedures for preparing reconciliations and are continuing to work on all unperformed reconciliations for the previous fiscal years including cash and federal reconciliations for fiscal year 2002. The Agency does not expect to have these reconciliations completed until the end of fiscal year 2004. Because these reconciliations were not performed, we were unable to

agree year-end cash balances and federal project component code amounts between the Agency's books and STARS. We were also unable to perform analytical reviews (i.e. – comparisons between current and prior year data) for revenues, expenditures, and fringe benefits because fiscal year 2001 reconciliations were not complete and the information in the Agency's books, STARS, or both may be erroneous.

The STARS Policies and Procedures Manual (STARS Manual) requires reconciliations to be performed at least monthly on a timely basis, be documented in writing in an easily understandable format with all supporting working papers maintained for audit purposes, be signed and dated by the preparer, and be reviewed and approved in writing by an appropriate agency official other than the preparer. Errors discovered through the reconciliation process must be promptly corrected in the agency's accounting records and/or in STARS as appropriate.

We recommend the Agency continue its process of completing reconciliations to ensure compliance with the STARS Manual requirements and to identify and correct errors in its accounting records and/or STARS as necessary. We also recommend that all reconciliations be reviewed and approved in writing by an appropriate official other than the preparer.

### **CAPITAL ASSETS CLOSING PACKAGE**

Due to the State's implementation of GASB Statement 34 in fiscal year 2002, the requirements for reporting capital assets changed. The State Comptroller General's Office (CGO) began using a new capital assets closing package which categorized capital assets as non-depreciable and depreciable. Non-depreciable assets include land and non-depreciable improvements, construction in progress, works of art and historical treasures, and intangible assets that are considered to have infinite useful lives. Depreciable assets include depreciable land improvements, buildings and building improvements, vehicles, machinery, equipment, exhaustible collections of works of art and historical treasures, and intangible assets. The new

closing package requires agencies to reclassify assets to the appropriate categories. In addition, the CGO changed the capitalization thresholds. All land and non-depreciable land improvements are capitalized, regardless of the cost. Depreciable land improvements, building and building improvements, and intangible assets of at least \$100,000 are required to be capitalized. Vehicles, machinery, equipment and works of art and historical treasures have a capitalization threshold of \$5,000.

We reviewed and tested the capital assets additions reconciliation form and determined the amounts reported to be reasonable, except that the Agency included, in error, donated assets totaling \$314,055 with individual estimated fair market values less than the capitalization thresholds. Furthermore, the Agency understated asset expenditures not meeting the required capitalization criteria. This resulted in an overstatement of capital asset additions on the reconciliation form of \$192,426. In total, capital asset additions reported on the closing package was overstated by \$506,481.

We also reviewed the capital assets and accumulated depreciation summary forms to determine whether amounts were reasonable and adequately supported by Agency records. Other than current year capital asset additions and retirements for machinery and equipment, the Agency was not able to provide us with adequate supporting documentation for the amounts and ending balances of the assets reported in the summary forms. In addition, the ending balances on the summary form did not agree to the Agency's property inventory records. Agency personnel told us that an inventory of the Agency's capital assets had not been performed in several years. South Carolina Code of Laws Section 10-1-140 requires the head of each agency to make an inventory of all personal property under his supervision each fiscal year.

The State Comptroller General's Office obtains GAAP (generally accepted accounting principles) data from agency-prepared closing packages for the State's financial statements. Section 1.7 of the GAAP Closing Procedures Manual (GAAP Manual) states that each agency

is responsible for submitting accurate and complete closing package forms that are completed in accordance with instructions and further states that, "The accuracy of closing package data is extremely important." Section 1.8 states, "Agencies should keep working papers to support each amount they enter on each closing package form." In addition, the GAAP Manual recommends an effective review of each closing package and the underlying working papers to minimize closing package errors and omissions. To assist each agency in performing effective reviews, the State Comptroller General's Office requires a reviewer checklist to be completed for each closing package submitted.

Section 3.9 of the GAAP Manual requires agencies to maintain full documentation to support each number on the closing package. This section also states that in order to be considered a capital asset, the asset must meet the established capitalization criteria. Agencies are not to capitalize any assets that do not meet or exceed the thresholds stated above.

We recommend that the Agency develop and implement procedures to ensure that its financial information is properly identified and that its accumulated balances and transactions are reported in accordance with GAAP and GAAP Manual instructions. Such procedures should ensure that only assets meeting the appropriate capitalization criteria be reported as capital assets. Furthermore, the Agency should perform an inventory of all capital assets and adjust its accounting records to properly reflect those assets.

### **INITIAL PAY**

During our test of employee additions, we noted six instances in which employees were not paid in a timely manner. Late payments ranged from several weeks to three months after starting work. The employees were not paid timely because required payroll documentation (e.g., employee leave and attendance records, and personnel/payroll action requests) was not submitted by the armory supervisors to the payroll department at headquarters in a timely

manner. The Agency violated the STARS Policies and Procedures Manual (STARS Manual) which requires vouchers to be delivered to the Comptroller General within 30 days from the receipt of services. A similar comment was included in the State Auditor's reports for fiscal years 2000 and 2001.

We again recommend that the Agency implement procedures to ensure that proper documentation for adding new employees to the payroll be promptly completed and submitted to the Agency's payroll department.

### **DATA TRANSLATION TO THE STATE**

The following comment was included in the State Auditor's report for fiscal years 1998 and 1997 and repeated in the fiscal year 1999 through 2001 reports.

The State maintains two accounting systems: STARS which is its budgetary accounting system and Series Z which is its GAAP-basis accounting system. Agencies are required to submit all revenue and expenditure transactions to the State's Comptroller General to be processed in STARS and are required to reconcile their books to STARS. The Comptroller General translates STARS into Series Z and collects and processes other GAAP data on agency-prepared closing packages in order to produce its GAAP-basis financial statements. Both STARS and Series Z are table driven and for the financial statements to be accurate it is necessary that all the tables and translations be correct.

All federal grants and permanent improvement projects are assigned project numbers, which are four digit numbers. Recurring grants awarded by grant year maintain the same project number but retain their separate identity through the use of phase codes, which are two digit numbers that follow the project numbers. Together these six digit project/phase code numbers comprise the State's D38 table. When permanent improvement projects are funded by federal grants, the State uses a process to interrelate the grant and permanent improvement project/phase codes. This process is described in the STARS Manual in Section 2.1.2.50. For fiscal years 1998 and 1997, the Agency has not submitted accurate information in sufficient detail to the State to ensure that the project/phase codes are used properly. It has not interrelated its grants and permanent improvements as required by the State. Therefore, because the Comptroller General relied on this data, the State's financial statements are incorrect as they relate to the Agency. We could not determine the extent of the inaccuracies; however, we informed the auditors of the State's financial statements of the problem and also pointed out the significant size of the Agency.

The federal government assigns a catalog of federal domestic assistance (CFDA) number to most of its grants and cooperative agreements. The State requires each agency to provide the CFDA number for each grant when it obtains budgetary authority and approval for the grant. At this point, the State establishes the grant on the D38 table and also establishes a conversion table to relate D38 numbers and CFDA numbers. All documents submitted to the Comptroller General to be processed into STARS must include the project/phase code, if applicable.

Using the tables and the information provided on the transactions, the Comptroller General produces its CSA467 report which is a summary by project/phase code of cash, beginning fund balances, adjustment to beginning fund balances, revenues, and expenditures. The STARS Manual requires agencies to reconcile the CSA467 report to their books. See related findings in the comment, Reconciliations.

The State Treasurer is responsible for monitoring agencies' cash management and calculating interest receivable/payable under the federal Cash Management Improvement Act (CMIA). It uses data from STARS, including the project/phase codes and the translation to CFDA numbers to calculate cash balances by program. If these numbers and translations are inaccurate, then the interest calculations will also be inaccurate.

We noted that the Agency has significant errors in the translation of project/phase codes and CFDA numbers. Therefore, the State Treasurer's interest calculation is incorrect. Based on information provided by us, the State Treasurer requested the Agency to correct these errors in January 1999. On May 5, 1999, the Agency had not made the corrections.

Accounting personnel told us that steps have been taken toward correcting these issues by training its employees on the use of the Agency's accounting system (SABAR) and on the Comptroller General's STARS and Series Z requirements. While the training process is ongoing the Agency anticipates correcting the errors by the end of fiscal year 2004 as it catches up on its monthly reconciliations (see Reconciliation comment).

We recommend that the Agency continue in its efforts to train employees in the proper accounting of transactions and balances in SABAR, STARS, and GAAP-basis data provided to the Comptroller General. Also, we recommend that the Agency implement policies and procedures which ensure that all accounting data will be accurate, timely, and in compliance with all State and federal laws, rules, and regulations as well as with GAAP. The Agency should review the project/phase codes and CFDA numbers for each active grant and permanent improvement project and should make all the corrections needed. It should contact the Comptroller General and State Treasurer to determine what action is needed to correct errors that have already occurred.

## **SECTION B - STATUS OF PRIOR FINDINGS**

During the current engagement, we reviewed the status of corrective action taken on each of the findings reported in the Accountant's Comments section of the State Auditor's Report on the South Carolina Office of the Adjutant General for the fiscal year ended June 30, 2001, and dated May 17, 2002. We determined that the Agency has taken adequate corrective action on each of the findings except for the following which have been repeated in Section A of this report.

### **2001 Comment Title**

DEPOSITS

RECONCILIATIONS

FIXED ASSETS CLOSING PACKAGES

PAYROLL AND PERSONNEL

Initial Pay

DATA TRANSLATION TO THE STATE

### **2002 Comment Title**

DEPOSITS

RECONCILIATIONS

CAPITAL ASSETS CLOSING PACKAGE

INITIAL PAY

DATA TRANSLATION TO THE STATE



## **MANAGEMENT'S RESPONSE**

### **Deposits**

Although the Agency has improved its controls over revenues including the deposit process, it has not eliminated its problems with armory deposits. Military employees who turn over frequently do most of the Agency's deposits. Therefore, the Agency must continually train new people. The Agency has reissued guidance to the armories and other receipting locations regarding the required controls and procedures. Also, the general ledger accountant and the armory operations coordinator offer one-on-one training and group training.

### **Reconciliations**

The Agency has continued to make significant improvement in the reconciliation process in fiscal year 2003. It has reconciled all current year revenues and expenditures by subfund for fiscal years 2002 and 2003. By the end of fiscal year end 2003, it reconciled current year transactions by project. The Agency has reconciled some old year balances and closed approximately 50 old projects on STARS. Because the Agency did not properly reconcile for several years and numerous differences exist between SABAR and STARS, it is a long, difficult process to correct the errors and bring the reconciliations up to date. The Agency's goal is to have all old year reconciliations current by the end of fiscal year 2004.

### **Capital Assets Closing Package**

The Military Department of South Carolina has a complex capital assets structure. Some assets are purchased and owned by the military, some are purchased and owned by the (State) Agency, and some are a combination. The Agency determined that many of the capital projects done via the (State) Agency will not be assets of the Agency. (Such is the case with capital projects built on 100% federal property at McEntire and McCrady.)

During the implementation of GASB 34, the Agency and Comptroller General agreed to the proper reporting for such projects and assets. However, this will require large adjustments (in both numbers and dollars of assets) to our automated system. For closing package purposes, the Agency tried to make these adjustments "offline" and in the process made some closing package errors.

The Agency made organizational changes at the end of fiscal year 2002 to improve the capital assets process; however, war activations resulted in a setback in these changes that will last into fiscal year 2004. Therefore, the Agency will continue to lag in the improvement it understands is needed for its capital assets system and the related closing package.

### **Initial Pay**

The Agency has been unable to solve its timing problems with armory sitters who intermittently work armory rentals at a rate of \$10 per hour. Either the sitter or the armory supervisor does not timely submit the paperwork to notify the payroll department that the sitter has worked or is authorized to work. In December 2001, the Agency developed a separate form for armory sitters, which combines the timesheet and the

personnel action form. One of the purposes of this new form is to reduce the number of sitters who are not paid in accordance with all applicable rules.

Budget and Finance is unaware that a sitter has worked if the sitter does not submit a timesheet. During fiscal year 2003, the Agency also learned that some sitters were being paid for events for which the armory had not submitted rental contracts or revenue to Budget and Finance. The Agency has implemented a policy that sitters will be promptly paid when all the paperwork (rental and payroll) is received.

#### **Data Translation to the State**

The Agency has improved its understanding of how STARS and Series Z interrelate to each other and to SABAR. It is working to correct all such deficiencies in SABAR and in the information it provides to STARS and Series Z. It is working the State Treasurer to ensure that it properly complies with cash management requirements. Also, it is working with B&C Board – Budget Division, Grant Services to review the process and ensure the accuracy of its project/phase codes and CFDA number translation. Total implementation of this recommendation will not be complete until the reconciliations are current. (See related finding and response, Reconciliations.)

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