

May 24, 1999

The Honorable James H. Hodges, Governor  
and  
Mr. Charles S. Way, Jr., Secretary of Commerce  
South Carolina Department of Commerce  
Columbia, South Carolina

This report on the audit of the financial statements of the East Cooper and Berkeley Railroad, a division of the South Carolina Department of Commerce - Division of Public Railways, for the fiscal year ended December 31, 1998, was issued by Wilkes & Company, Certified Public Accountants, under contract with the South Carolina Office of the State Auditor.

If you have any questions regarding this report, please let us know.

Respectfully submitted,

Thomas L. Wagner, Jr., CPA  
State Auditor

TLW/sj

**SOUTH CAROLINA DEPARTMENT OF COMMERCE -  
DIVISION OF PUBLIC RAILWAYS**

**EAST COOPER AND BERKELEY RAILROAD**

**FINANCIAL STATEMENTS**

**YEAR ENDED DECEMBER 31, 1998**

SOUTH CAROLINA DEPARTMENT OF COMMERCE -  
DIVISION OF PUBLIC RAILWAYS  
EAST COOPER AND BERKELEY RAILROAD

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YEAR ENDED DECEMBER 31, 1998

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## INDEPENDENT AUDITOR'S REPORT

Mr. Thomas L. Wagner, Jr., CPA  
State Auditor  
South Carolina Office of the State Auditor  
Columbia, South Carolina

We have audited the accompanying financial statements of the East Cooper and Berkeley Railroad, a division of the South Carolina Department of Commerce - Division of Public Railways, as of December 31, 1998, and for the year then ended as listed in the table of contents. These financial statements are the responsibility of the Railroad's management. Our responsibility is to express an opinion on these financial statements based on our audit.

Except as discussed in the following paragraph, we conducted our audit in accordance with generally accepted auditing standards. 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 component unit 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.

Governmental Accounting Standards Board Technical Bulletin 98-1, *Disclosures about Year 2000 Issues*, requires disclosure of certain matters regarding the Year 2000 Issue. East Cooper and Berkeley Railroads has included such disclosures in Note 14. Because of the unprecedented nature of the Year 2000 Issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Accordingly, insufficient audit evidence exists to support East Cooper and Berkeley Railroads disclosures with respect to the Year 2000 Issue made in Note 14. Further, we do not provide assurance that East Cooper and Berkeley Railroads is or will be year 2000 ready, that East Cooper and Berkeley Railroads year 2000 remediation efforts will be successful in whole or in part, or that parties with which East Cooper and Berkeley Railroads does business will be year 2000 ready.

As described in Note 1, the financial statements of the East Cooper and Berkeley Railroad are intended to present the financial position, results of operations, and the cash flows of only that portion of the funds of the State of South Carolina that is attributable to the transactions of the East Cooper and Berkeley Railroad, an enterprise fund of the State. These financial

Mr. Thomas L. Wagner, Jr., CPA  
State Auditor  
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Columbia, South Carolina  
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statements do not include other funds or enterprises of the Division of Public Railways, Department of Commerce, or the State or any component units of the State. These financial statements are not intended to present fairly the financial position of the State of South Carolina primary government or financial reporting entity of the South Carolina Department of Commerce - Division of Public Railways and the results of their operations and cash flows in conformity with generally accepted accounting principles.

The Railroad's financial statements do not adequately classify certain transactions and do not contain certain material disclosures. Also the notes to the financial statements do not disclose material information and accounting policies. These disclosures and information are not in the financial statements because it is exempted from public disclosure pursuant to the South Carolina Freedom of Information Act. Reporting of such information is essential for a fair presentation in conformity with generally accepted accounting principles.

In our opinion, because of the incomplete presentation and omission of note disclosures discussed in the preceding paragraph, the financial statements referred to in the first paragraph do not present fairly, in conformity with generally accepted accounting principles, in all material respects, the financial position of the East Cooper and Berkeley Railroad as of December 31, 1998, and the results of its operations and its cash flows for the year then ended.

Columbia, South Carolina  
April 2, 1999

## **FINANCIAL STATEMENTS**

SOUTH CAROLINA DEPARTMENT OF COMMERCE -  
 DIVISION OF PUBLIC RAILWAYS,  
 EAST COOPER AND BERKELEY RAILROAD

**BALANCE SHEET**  
 DECEMBER 31, 1998

ASSETS

Current Assets:	
Cash and cash equivalents	\$ 5,110,738
Accounts receivable	1,849,705
Interest receivable	18,202
Inventories	61,949
Prepayments	<u>2,165</u>
Total Current Assets	<u>7,042,759</u>
Property, Plant, and Equipment, Net of Accumulated Depreciation of \$1,266,635	
	<u>5,291,985</u>
Other Asset:	
Servicing rights	2,300,000
Less, accumulated amortization	<u>(460,000)</u>
Total Other Asset	<u>1,840,000</u>
Total Assets	<u>\$ 14,174,744</u>

LIABILITIES AND FUND EQUITY

Current Liabilities:	
Other customer payables	\$ 2,718,320
Accounts payable, CSX Transportation, Inc.	1,988,953
Accounts payable, PUC-PTR	44,970
Accounts payable - other	521
Payroll taxes withheld and accrued employee benefits - payable to PUC-PTR	18,433
Accrued payroll	25,331
Accrued annual leave and related benefits	85,256
Other liability - current portion	<u>652,940</u>
Total Current Liabilities	<u>5,534,724</u>
Long Term Liabilities:	
Advance payable to PUC-PTR	1,387,869
Other liability	<u>895,582</u>
Total Long Term Liabilities	<u>2,283,451</u>
Total Liabilities	<u>7,818,175</u>
Fund Equity:	
Retained earnings:	
Unreserved and unappropriated	<u>6,356,569</u>
Total Liabilities and Fund Equity	<u>\$ 14,174,744</u>

THE ACCOMPANYING NOTES  
 ARE AN INTEGRAL PART OF THIS FINANCIAL STATEMENT

SOUTH CAROLINA DEPARTMENT OF COMMERCE -  
DIVISION OF PUBLIC RAILWAYS,  
EAST COOPER AND BERKELEY RAILROAD

**STATEMENT OF REVENUES, EXPENSES AND CHANGES  
IN RETAINED EARNINGS  
FOR THE YEAR ENDED DECEMBER 31, 1998**

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Operating Revenues:	
Freight charges, net	\$ 2,327,026
Use of engine	<u>32,308</u>
Total Operating Revenues	<u>2,359,334</u>
Operating Expenses:	
Railway operating expenses:	
Maintenance of way and structures	
Superintendence	25,834
Depreciation	42,184
Other maintenance of way expenses	<u>181,587</u>
Total Maintenance of Way and Structures	<u>249,605</u>
Maintenance of equipment:	
Superintendence	27,436
Depreciation	33,183
Other equipment expenses	<u>63,578</u>
Total Maintenance of Equipment	<u>124,197</u>
Transportation:	
Superintendence	76,037
Yard employees	192,030
Other transportation expenses	<u>185,371</u>
Total Transportation	<u>453,438</u>
General:	
Administration	365,487
Insurance	22,676
Depreciation	13,963
Amortization of servicing rights	<u>115,000</u>
Total General	<u>517,126</u>
Total Railway Operating Expenses	<u>1,344,366</u>

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SOUTH CAROLINA DEPARTMENT OF COMMERCE -  
 DIVISION OF PUBLIC RAILWAYS,  
 EAST COOPER AND BERKELEY RAILROAD

**STATEMENT OF REVENUES, EXPENSES AND CHANGES  
 IN RETAINED EARNINGS  
 FOR THE YEAR ENDED DECEMBER 31, 1998**

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Other General Operating Expenses:	
Rent expense for leased road and equipment	17,698
Hire of freight cars	<u>6,975</u>
Total Other General Operating Expenses	<u>24,673</u>
Total Operating Expenses	<u>1,369,039</u>
Operating Income	<u>990,295</u>
Nonoperating Revenues (Expenses):	
Interest income	206,855
Interest expense	(24,757)
Other	<u>486</u>
Total Nonoperating Revenues (Expenses)	<u>182,584</u>
Net Income	1,172,879
Retained Earnings, Unreserved, Unappropriated:	
Beginning of year	<u>5,183,690</u>
End of year	<u>\$ 6,356,569</u>

THE ACCOMPANYING NOTES  
 ARE AN INTEGRAL PART OF THIS FINANCIAL STATEMENT

SOUTH CAROLINA DEPARTMENT OF COMMERCE -  
DIVISION OF PUBLIC RAILWAYS,  
EAST COOPER AND BERKELEY RAILROAD

**STATEMENT OF CASH FLOWS**  
FOR THE YEAR ENDED DECEMBER 31, 1998

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Cash Flows From Operating Activities:	
Operating income	\$ 990,295
Adjustments to reconcile operating income to net cash used for operating activities:	
Depreciation	89,330
Depreciation charged from related entity	(13,963)
Amortization	115,000
Other nonoperating revenues, net	486
(Increase) decrease in assets:	
Accounts receivable	(936,440)
Inventories	(858)
Prepayments	(1,729)
Increase (decrease) in liabilities:	
Other customer payables	2,159,895
Accounts payable, CSX	536,435
Accounts payable, PUC-PTR	4,091
Accounts payable, other	(2,458)
Payroll taxes withheld and accrued employee benefits payable to PUC-PTR	3,142
Accrued payroll	25,331
Accrued annual leave and benefits	<u>47</u>
Net Cash Provided by Operating Activities	<u>2,968,604</u>
Cash Flows From Noncapital Financing Activities:	
Principal paid on other liability	<u>(462,457)</u>
Net Cash Used by Noncapital Financing Activities	<u>(462,457)</u>
Cash Flows From Capital and Related Financing Activities:	
Purchase of fixed assets	(165,991)
Interest paid on notes payable	<u>(24,757)</u>
Net Cash Used for Capital and Related Financing Activities	<u>(190,748)</u>

THE ACCOMPANYING NOTES ARE AN  
INTEGRAL PART OF THIS FINANCIAL STATEMENT

SOUTH CAROLINA DEPARTMENT OF COMMERCE -  
DIVISION OF PUBLIC RAILWAYS,  
EAST COOPER AND BERKELEY RAILROAD

**STATEMENT OF CASH FLOWS**  
**FOR THE YEAR ENDED DECEMBER 31, 1998**

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Cash Flows from Investing Activities:	
Interest received on deposits with the State Treasurer	<u>188,662</u>
Net Cash Provided by Investing Activities	<u>188,662</u>
Net Increase in Cash and Cash Equivalents	2,504,061
Cash and Cash Equivalents, Beginning of Year	<u>2,606,677</u>
Cash and Cash Equivalents, End of Year	<u>\$ 5,110,738</u>

THE ACCOMPANYING NOTES ARE AN  
INTEGRAL PART OF THIS FINANCIAL STATEMENT

SOUTH CAROLINA DEPARTMENT OF COMMERCE -  
DIVISION OF PUBLIC RAILWAYS,  
EAST COOPER AND BERKELEY RAILROAD

**NOTES TO FINANCIAL STATEMENTS**  
DECEMBER 31, 1998

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**NOTE 1 - REPORTING ENTITY**

The core of the financial reporting entity is the primary government which has a separately elected governing body. As required by generally accepted accounting principles, the financial reporting entity includes both the primary government and all its component units. Component units are legally separate organizations for which the elected officials or the primary government are financially accountable. In turn, component units may have component units.

An organization other than a primary government may serve as a nucleus for a reporting entity when it issues separate financial statements. That organization is identified herein as a primary entity.

The primary entity is financially accountable if it appoints a voting majority of the organization's governing body including situations in which the voting majority consists of the primary entity's officials serving as required by law (e.g., employees who serve in an ex officio capacity on the component unit's board are considered appointments by the primary entity) and (1) it is able to impose its will on that organization or (2) there is a potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the primary entity. The primary entity also may be financially accountable if an organization is fiscally dependent on it even if it does not appoint a voting majority of the board. An organization is fiscally dependent on the primary entity that holds one or more of the following powers:

- (1) Determine its budget without another government's having the authority to approve and modify that budget.
- (2) Levy taxes or set rates or charges without approval by another government.
- (3) Issue bonded debt without approval by another government.

Based on the application of the above criteria, no component units are included in the reporting entity.

East Cooper and Berkeley Railroad (ECBR) is part of the State of South Carolina Primary Government. ECBR is reported within the Public Railways Divisions enterprise fund in the State's Comprehensive Annual Financial Report.

Effective July 1, 1993, as part of the Government Restructuring Act of 1993 Code Section 13-1-1310 created the Division of Public Railways within the Department of Commerce which is governed by the Secretary of the Department of Commerce.

The Department of Commerce is a cabinet agency operating under the governor and is subject to state laws and regulations. The Division however is not subject to the State Procurement Code or Appropriation Act. Also, the Division is not subject to State Human Resource Regulations. The Secretary of the Department of Commerce is responsible for oversight of the Division. The Division has powers of a body corporate including,

1. The power to sue or be sued, and make contracts.
2. To acquire by purchase or donation and to own, rent, lease, mortgage and dispose of real or personal property.
3. To operate, acquire, construct, maintain and control the tracks and equipment of the Division and be governed by rules and regulations of the Interstate Commerce Commission and its successor, the Surface Transportation Board.
4. To employ and dismiss the employees of the Division and to fix and to pay the compensation thereof.
5. To issue revenue bonds and other obligations, subject to approval by the State Budget and Control Board, to defray the cost of acquisition of other railroads.

The South Carolina Department of Commerce - Division of Public Railways consists of three separate divisions: the Port Utilities Commission and Port Terminal Railroad (PUC-PTR), the East Cooper and Berkeley Railroad (ECBR), and the Tangent Transportation Company (TTC). The functions of each of the divisions are different and are outlined in the report on the combined financial statements of the South Carolina Department of Commerce - Division of Public Railways which are presented under separate cover. The function of East Cooper and Berkeley Railroad is as follows:

Operation and maintenance of the railroad line constructed by the Division and located in Berkeley County, South Carolina, is the primary responsibility of the East Cooper and Berkeley Railroad (ECBR). The railroad was constructed with financing by Amoco Chemicals Corporation, its major customer. This came after requests from the Division and the State Budget and Control Board to service the east side of the Cooper River north of Charleston, South Carolina were denied by the common carrier railroads operating in South Carolina.

The accompanying financial statements present the financial position, results of operations, and the cash flows solely of the East Cooper and Berkeley Railroad, a division of the South Carolina Department of Commerce - Division of Public Railways and do not include any other funds of the State of South Carolina, or other divisions of the Division of Public Railways.

## **NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

### **Basis of Accounting**

ECBR adheres to generally accepted accounting principles as promulgated by the Governmental Accounting Standards Board.

The South Carolina Department of Commerce - Division of Public Railways is required by State Law (58-19-110) to maintain separate accounting of its three divisions: the Port Utilities Commission and Port Terminal Railroad, the East Cooper and Berkeley Railroad, and the Tangent Transportation Company. Presented here are the financial statements of the East Cooper and Berkeley Railroad division of the Division of Public Railways.

ECBR utilizes the accrual basis of accounting. Under the accrual basis of governmental accounting for enterprise funds, revenues are recognized in the accounting period in which they are earned and become measurable. Expenses are recognized in the period incurred, if measurable. Fund equity is segregated into contributed capital and retained earnings components. The operating statement presents increases (e.g., revenues) and decreases (e.g., expenses) in net total assets. The accounting principles utilized by the South Carolina Department of Commerce - Division of Public Railways and ECBR are in conformity with the uniform system of accounts for railroad companies prescribed by the Surface Transportation Board and generally accepted accounting principles. ECBR has elected to apply all Financial Accounting Standards Board statements and interpretations issued prior to December 31, 1989, unless they conflict with GASB pronouncements.

### **Fund Accounting**

ECBR uses funds to report its financial position and the results of its operations. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

A fund is a separate fiscal and accounting entity with a self-balancing set of accounts recording cash and other financial resources, together with related liabilities and residual equities or balances and changes therein which are segregated to carry on specific activities or attain certain objectives in accordance with applicable regulations, restrictions or limitations. Separate accounts are maintained for each fund. Accordingly, all financial transactions have been reported by fund type.

Funds are classified into three categories: governmental, proprietary, and fiduciary. Each category, in turn, is divided into separate "fund types." ECBR reports activities by the enterprise "fund type" under the proprietary fund category.

Proprietary funds are used to account for activities similar to those found in the private sector, where the determination of net income is necessary or useful to sound financial administration. Goods or services for such activities can be provided either to outside parties (enterprise funds) or to other departments or agencies primarily within the government (internal service funds).

Enterprise funds account for activities that are self sustaining, primarily through user charges or are used when management wants to control or measure costs of services.

### **Property, Plant, and Equipment**

Except on track and roadway, fixed assets with a unit acquisition cost in excess of \$2,000 are capitalized and depreciated over the estimated useful lives of the assets using the straight-line method of depreciation. Estimated useful lives are as follows: buildings, 20 years; equipment, 3-25 years. Assets valued at less than \$2,000 are expensed when purchased.

Track and roadway are capitalized at cost and depreciation is not recognized. Replacements and repairs are expensed in the period that costs are incurred. Betterments to track and roadway are capitalized.

### **Servicing Rights**

The servicing rights asset is being amortized.

### **Inventories**

Inventories consisting of materials and supplies are stated at the lower of cost or market using the weighted average method.

### **Policy for Uncollectible Accounts**

At year end management reviews past due accounts receivable and recognizes bad debt expense for those accounts determined to be uncollectible. This method is not in conformity with generally accepted accounting principles which requires accounts receivable to be reported at net realizable value using an allowance for uncollectible accounts. However based on ECBR's collection history, the results from using the direct write-off method are not materially different from the allowance method.

### **Statement of Cash Flows**

For purposes of this statement ECBR considers deposits with State of South Carolina cash management pool to be cash equivalents because they are readily convertible to cash with an insignificant risk of loss in value.

### **Cash and Cash Equivalents**

The amounts shown in the financial statements as "cash and cash equivalents" represent cash on hand with the State Treasurer, and cash invested in various instruments by the State Treasurer as part of the State's cash management pool.

Because the cash management pool operates as a demand deposit account, amounts invested in the pool are classified as cash and cash equivalents. The pool includes some long-term investments such as obligations of the United States and certain agencies of the United States, obligations of the State of South Carolina and certain of its political subdivisions, certificates of deposit, collateralized repurchase agreements, and certain corporate bonds. Most State agencies participate in the cash management pool; however, some agency accounts are not included in the pool because of restrictions on the use of funds. For those accounts, cash equivalents included investments in short-term, highly liquid securities having a maturity of three months or less.

The State's cash management pool consists of a general deposit account and several special deposit accounts. The State records an agency's equity interest in the general deposit account, however all earnings on that account are credited to the State General Fund. ECBR, however only has special deposit accounts. Investments in the pool are recorded at fair value. Interest earned by the agencies' special deposit accounts is posted to the agency's account at the end of each month and is retained by the agency. Interest earnings are allocated based on the percentage of an agency's accumulated daily interest receivable to the total undistributed interest received by the pool. Reported non-operating interest income includes interest earnings, realized gains/losses and unrealized gains/losses on investments in the pool.

Although the cash management pool includes some long-term investments, it operates as a demand deposit account; therefore, for credit risk information pertaining to the cash management pool, see the deposits disclosures in Note 3.

### **NOTE 3 - DEPOSITS**

All deposits of the agency are under the control of the State Treasurer who, by law, has sole authority for investing State funds.

State law requires full collateralization of all State Treasurer bank balances. The State Treasurer must correct any deficiencies in collateral within seven days. At December 31, 1998, all State Treasurer bank balances were fully insured or collateralized with securities held by the State or by its agents in the State's name.

With respect to investments in the State's cash management pool, all of the State Treasurer's investments are insured or registered or are investments for which the securities are held by the State or its agent in the State's name. Information pertaining to the reported amounts, fair values, and credit risk of the State Treasurer's investments is disclosed in the Comprehensive Annual Financial Report of the State of South Carolina.

**NOTE 4 - PROPERTY, PLANT, AND EQUIPMENT**

Property, plant, and equipment is stated at original cost and is depreciated on the straight-line method. Property, plant and equipment is summarized as follows:

<u>ASSETS</u>	<u>Estimated Useful Life(years)</u>	
Land and improvements	-	\$ 2,133,006
Buildings	20	703,303
Road and equipment	3 - 25	1,488,670
Non-depreciable road	-	<u>2,233,641</u>
		6,558,620
Less accumulated depreciation		<u>1,266,635</u>
		<u>\$ 5,291,985</u>

Depreciation expense for the period ended December 31, 1998, from East Cooper and Berkeley Railroad's operations was \$89,330, of which \$13,963 was charged to ECBR by the PUC-PTR Division in relation to the overhead cost sharing between ECBR and PUC-PTR as explained in Note 10.

**NOTE 5 - ACCOUNTS PAYABLE, CSX TRANSPORTATION, INC.**

East Cooper and Berkeley Railroad has a reciprocal agreement with CSX Transportation, Inc., whereby freight charges to customers are billed by the railroad line that originated the rail carrier order. Therefore, East Cooper and Berkeley Railroad may bill a customer for the entire freight charge even though both East Cooper-Berkeley Railroad and railroad lines owned by CSX Transportation, Inc. were used. East Cooper and Berkeley Railroad then remits to CSX their portion of the freight revenue due them. As of December 31, 1998, \$1,988,953 had not yet been remitted to CSX Transportation, Inc.

**NOTE 6 - ACCRUED ANNUAL LEAVE**

Non-union ECBR employees are entitled to accrue and carry forward at calendar year end a maximum of 180 days sick leave and 45 days annual vacation leave. Upon termination of employment, employees are entitled to be paid for accumulated unused annual vacation leave up to the maximum of 45 days, but are not entitled to any payment for unused sick leave. Employees do not accrue or carry forward holiday leave, compensatory time or overtime.

Union employees can earn up to 25 days annual vacation leave per year, but do not earn any sick leave. Union employees do not carry forward any unused vacation leave. Upon termination of employment, union employees are entitled to be paid for accumulated unused annual vacation leave up to 25 days. Union employees do not accrue or carry forward holiday leave, compensatory time or overtime.

ECBR calculates the gross compensated absences liability based on recorded balances of unused leave. The entire unpaid liability for which the employer expects to compensate employees through paid time off or cash payments, inventoried at fiscal year-end current salary costs and the cost of the salary related benefit payments is recorded as a current liability. The net change in the liability is recorded in the current year in the applicable operating departments.

**NOTE 7 - ADVANCE PAYABLE TO PUC-PTR**

The advance from PUC-PTR on May 31, 1995 of \$1,387,869 was to assist ECBR in paying a note payable to Amoco in 1995. The advance is non-interest bearing and has no definite repayment terms, although it is the intent of management that the advance will eventually be repaid.

**NOTE 8 - PENSION PLANS AND EMPLOYEE BENEFIT PLANS**

The Retirement Division of the State Budget and Control Board maintains four independent defined benefit plans and issues its own publicly available Comprehensive Annual Financial Report (CAFR) which includes financial statements and required supplementary information. A copy of the separately issued CAFR may be obtained by writing to the Retirement Division, 202 Arbor Lake Drive, Columbia, South Carolina, 29223. Furthermore, the Division and the four pension plans are included in the CAFR of the State of South Carolina.

The majority of employees of the Division are covered by a pension plan through the South Carolina Retirement System (SCRS), a cost-sharing multiple-employer defined benefit pension plan administered by the Retirement Division, a

public employee retirement system. Generally all State employees are required to participate in and contribute to the SCRS as a condition of employment unless exempted by law as provided in Section 9-1-480 of the South Carolina Code of Laws. This plan provides retirement annuity benefits as well as disability, cost of living adjustment, death, and group-life insurance benefits to eligible employees and retirees.

Under SCRS, employees are eligible for a full service retirement annuity upon reaching age 65 or completion of 30 years credited service regardless of age. The benefit formula for full benefits effective since July 1, 1989, for the SCRS is 1.82 percent of an employee's average final compensation multiplied by the number of years of credited service. Early retirement options with reduced benefits are available as early as age 55. Employees are vested for a deferred annuity after five years service and qualify for a survivor's benefit upon completion of 15 years credited service. Disability annuity benefits are payable to employees totally and permanently disabled provided they have a minimum of five years credited service. A group-life insurance benefit equal to an employee's annual rate of compensation is payable upon the death of an active employee with a minimum of one year of credited service.

Since July 1, 1988, employees participating in the SCRS have been required to contribute 6.0% of all compensation. Effective July 1, 1998, the employer contribution rate became 9.58% which included a 2.03% surcharge to fund retiree health and dental insurance coverage. The rate for the State's fiscal year (effective July 1, 1997) was 9.466% which included a 1.916% surcharge. The Division's actual contributions to the SCRS for the fiscal year ended December 31, 1998 were \$41,387, and equaled the required contributions of 7.55% (excluding the surcharge) for the year. Employer contributions for 1997 were \$36,098, and for 1996 were \$31,995. Also, the Division paid employer group-life insurance contributions of \$795 in the current fiscal year at the rate of .15% of compensation.

The amounts paid by the East Cooper and Berkeley Railroad for pension and group-life benefits are recorded in the appropriate operating department corresponding to the employee for whom contributions are made.

Article X, Section 16, of the South Carolina Constitution requires that all State operated retirement systems be funded on a sound actuarial basis. Title 9 of the South Carolina Code of Laws of 1976, as amended, prescribes requirements relating to membership, benefits, and employee/employer contributions for each pension plan. Employee and employer contribution rates to SCRS are actuarially determined. The surcharges to fund retiree health and dental insurance are not part of the actuarially established rates. Annual benefits, payable monthly for life, are based on length of service and on average final compensation (an annualized average of the employee's highest 12 consecutive quarters of compensation).

The System does not make separate measurements of assets and pension liabilities for individual employers. Under Title 9 of the South Carolina Code of Laws, the Division's liability under the plan is limited to the amounts of contributions (stated as a percentage of covered payroll) established by the State Budget and Control Board. Therefore, the Division's liability under the pension plan is limited to the contribution requirements for the applicable year from amounts appropriated therefor in the South Carolina Appropriation Act and amounts from other applicable revenue sources. Accordingly, the Division recognizes no contingent liability for unfunded costs associated with participation in the plan.

At retirement, employees participating in the SCRS receive additional service credit (at a rate of 20 days equals one month of service) for up to 90 days for accumulated unused sick leave.

The East Cooper and Berkeley Railroad contributed \$138,517 this year to the U.S. Railroad Retirement System, which covers all employees. Participation is mandatory. This program is a two-tier system which is funded based on each employee's gross annual wages. Effective January 1, 1998, wages up to \$68,400 were funded at 6.2% by ECBR to meet Tier 1 funding requirements and all wages were funded at 1.45% by ECBR to meet Tier I Medicare Funding requirements. ECBR funded wages up to \$50,700 at 16.1% to meet Tier II funding requirements. Employees matched the Division's Tier 1 contribution, but paid only 4.9% versus ECBR's 16.1% Tier II rate on wages up to \$50,700 for the maximum Tier II employee liability of \$2,484. In addition, there is a supplemental charge based on hours worked in a given month. The rate is 35 cents per hour. The cost is borne by ECBR.

This plan is administered by the U. S. Railroad Retirement Board, in accordance with the Railroad Retirement Acts.

Data concerning the actuarial status of the U.S. Railroad Retirement System as related to ECBR is not available. ECBR is not liable for any unfunded costs associated with the plan and recognized no contingent liability for such cost.

### **Post-Retirement and Other Employee Benefits**

In accordance with the South Carolina Code of Laws and the annual Appropriation Act, the State of South Carolina provides certain health care, dental, and life insurance benefits to active and certain retired State employees and certain surviving dependents of retirees. All permanent full-time employees of East Cooper and Berkeley Railroad are eligible to receive these benefits. The State provides post employment health and dental benefits to employees who retire from State service or who terminated with at least 20 years of State service who meet one or more of the

eligibility requirement, such as age, length of service, and hire date. Generally those who retire must have at least 10 years of retirement service credit to qualify for State-funded benefits. Benefits are effective at date of retirement when the employee is eligible for retirement benefits. These benefits are provided through applicable revenue sources for its active employees and to the State Budget and Control Board for all participating State retirees except the portion funded through the pension surcharge and provided from other applicable division revenue sources of the East Cooper and Berkeley Railroad for its active employees who are not funded by State General Fund appropriations. The State finances health and dental plan benefits on a pay-as-you-go basis. Currently, approximately 18,500 State retirees meet these eligibility requirements.

The East Cooper and Berkeley Railroad recorded employer contributions expenses for these insurance benefits for active employees in the amount of \$66,254 for the year ended December 31, 1998. As discussed above, the East Cooper and Berkeley Railroad paid \$11,119 applicable to the surcharge included with the employer contributions for retirement benefits. These amounts were remitted to the South Carolina Retirement Systems for distribution to the Office of Insurance Services for retiree health and dental insurance benefits.

Information regarding the cost of insurance benefits applicable to East Cooper and Berkeley Railroad retirees is not available. By State law, East Cooper and Berkeley Railroad has no liability for retirement benefits. Accordingly, the cost of providing these benefits for retirees is not included in the accompanying financial statements.

In addition, the State General Assembly periodically directs the Retirement Systems to pay supplemental (cost of living) increases to retirees. Such increases are primarily funded from System's earnings; however, a portion of the required amount is appropriated from the State General Fund annually for the SCRS benefits.

### **Deferred Compensation Plans**

Several optional deferred compensation plans are available to State employees and employers of its political subdivisions. Certain employees of ECBR have elected to participate. The multiple-employer plans, created under Internal Revenue Service code sections 457, 401(k), and 403(b) are accounted for as agency funds of the State and included in the Comprehensive Annual Financial Report of the State of South Carolina. Employees may withdraw the current value of their contributions prior to termination if they meet requirements specified by the applicable plan.

Compensation deferred under the Section 401(k) and 403(b) plans is placed in trust for the contributing employee. The State has no liability for losses under the plans. Under the Section 457 plan, all deferred compensation plan amounts and

earnings remain assets of the employer (the State) subject to the claims of the employer's general creditors, one of whom is the employee participant. It is unlikely, however, that the State would ever use plan assets to satisfy claims of the State's general creditors. The portion of assets of the Section 457 plan to which the State has access is disclosed in its financial report.

On August 20, 1996, the provisions of Internal Revenue Service Code Section 457 were amended by adding subsection (g). That subsection provides that new plans will not be considered eligible plans unless all assets and income of the plans are held in trust for the exclusive benefit of the participants and their beneficiaries. Existing plans also must comply with this requirement by January 1, 1999. South Carolina's plan adopted this change effective July 24, 1998.

#### **NOTE 9 - OPERATING LEASES**

The only operating lease obligations was a yearly payment to the U. S. Department of Agriculture for right of way for the railroad on National Forest Land in the amount of \$1,498 per year until such time as the right of way is abandoned by East Cooper and Berkeley Railroad and the lease of equipment from ECBR's sister division PUC-PTR. There is a month to month lease of a backhoe at \$1,350 a month and a bushcutter is leased on a month to month basis at \$688 per month. \$16,200 was paid to PUC-PTR during 1998 for the lease of a backhoe and \$8,250 for the bushcutter lease.

#### **NOTE 10 - TRANSACTIONS WITH STATE ENTITIES AND SISTER DIVISION**

East Cooper and Berkeley Railroad has certain transactions with the State of South Carolina, various State agencies and it's two sister divisions, Port Utilities Commission and Port Terminal Railroad, and Tangent Transportation Company. Services received at no cost from State agencies include banking and investment functions from the State Treasurer, legal services from the Attorney General, and retirement and insurance plan administration and audit services from various divisions of the State Budget and Control Board. East Cooper and Berkeley Railroad had financial transactions with various State agencies during the year. Payments were made to the State Budget and Control Board for insurance coverage. The amounts of 1998 expenses applicable to related party transactions are not readily available. East Cooper and Berkeley Railroad provided no services free of charge to other State agencies during the year.

At December 31, 1998 East Cooper and Berkeley Railroad owed the PUC-PTR Division \$44,970 for various services provided by PUC-PTR on behalf of East

Cooper and Berkeley Railroad and \$18,433 of accrued payroll taxes payable by the PUC-PTR division on behalf of East Cooper and Berkeley Railroad. The total payable to PUC-PTR was \$63,403.

East Cooper and Berkeley Railroad incurred \$16,200 in expenses for rental of a backhoe and \$8,250 for use of a bushcutter to clear right of ways. These amounts were paid to PUC-PTR division.

Overhead expense of the PUC-PTR and ECBR divisions are split 56% to ECBR and 44% to PUC-PTR. Overhead expenses include superintendence, general administration, insurance, and consulting fees.

#### **NOTE 11 - RISK MANAGEMENT**

ECBR is exposed to various risks of loss and maintains State or commercial insurance coverage for certain risks. Management believes such coverage is sufficient to preclude any significant uninsured losses to the Railroad. Settled claims have not exceeded this coverage in any of the past three years. There were no significant reductions in insurance coverage from coverage in the prior year. The Railroad pays insurance premiums to certain other State agencies and commercial insurers to cover risks that may occur in normal operations. The insurers promise to pay to or on behalf of the insured for covered premium losses sustained during the policy period in accord with the insurance policy and benefit program limits. State management believes it is more economical to manage certain risks internally and set aside assets for claim settlement. Several State funds accumulate assets and the State itself assumes substantially all risks for the following:

1. Claims of covered public employees for health and dental insurance benefits (Office of Insurance Services); and
2. Claims of covered public employees for long-term disability and group-life insurance benefits (Office of Insurance Services).

Employees elect health coverage through either a health maintenance organization or through the states self-insured plan. All of the other coverages listed above are through the applicable state self-insured plan except dependent and optional life premiums which are remitted to commercial carriers.

ECBR and other entities pay premiums to the States Insurance Reserve Fund (IRF) which issues policies, accumulate assets to cover the risks of loss and pays claims incurred for covered losses related to the following Railroad assets, activities, and/or events.

1. Real property, its contents and other equipment - Coverage per loss of real property is based on current valuation with a \$250 deductible. Eighty percent of each loss is covered by the IRF. Equipment losses are subject to a \$500, or two percent deductible, whichever is less.
2. Motor vehicles - Coverage is up to \$1,000,000 per loss with a \$200 deductible for comprehensive and \$500 for collision.
3. Torts

The IRF is a self insurer and purchases reinsurance to obtain certain services and specialized coverage and to limit losses in the areas of property, boiler and machinery, and automobile liability. The IRF's rates are determined actuarially.

State agencies are the primary participants in the State's Health and Disability Insurance Fund and in IRF.

The Division purchases insurance, which covers all divisions, through private carriers for liability and property loss on road and locomotive assets, and employee fidelity bond insurance coverage for all employees to cover losses of up to \$100,000 arising from theft or misappropriations. Management believes based on exposure and likelihood of loss that this coverage is sufficient.

The Division has purchased insurance, which covers all divisions, from a private carrier for liability under the Federal Employers Liability Act (FELA) which is similar to workmans compensation insurance and covers all employees. The Division has elected to retain the risk of loss on this coverage for up to the first \$25,000 of costs per claim. Management has elected to retain this amount of risk because it feels that it is more economical than paying additional premiums for increased coverage. In the current year, no expenses were incurred on claims under the policy. Also a tax is paid to the U.S. Railroad Retirement System to cover the Railroad employees for unemployment benefits.

ECBR has recorded insurance premium expenses in the applicable operating department corresponding to the employees for whom contributions are made or in insurance expense under administrative costs.

ECBR's management believes risk of loss from business interruption is a remote likelihood and does not maintain insurance for this risk.

ECBR did not incur any significant losses in 1998 for self insured risks. Also, no reserves have been established for potential losses for self insured risks. ECBR reports such expenses if information prior to issuance of the financial statement

indicates that it is probable that an asset has been impaired or a liability has been incurred on or before fiscal year end and the amount is reasonably estimable. The recorded expense is valued at an estimate of the ultimate cost of settling the claim or of the asset loss.

**NOTE 12 - CONTINGENCIES**

There are currently several cases in litigation concerning Workmans Compensation (FELA) Claims. The outcome or potential liability to the Division or ECBR is not known at this time and cannot be reasonably estimated, therefore no liability or reserve has been established at this time. Also management believes any aggregate liability, if any, would not have a material adverse effect on the financial statements. The Division has insurance in force that effectively limits their exposure to \$25,000 per claim. Losses, if any on the above, would be split between PUC-PTR and ECBR in the same ratio as their overhead cost sharing percentage as explained in Note 10.

**NOTE 13 - ACCOUNTING CHANGES AND PRIOR PERIOD ADJUSTMENTS**

Effective January 1, 1998, ECBR adopted Governmental Accounting Standards Board (GASB) Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. This statement requires that most investments of governmental entities be stated at fair value rather than at cost. For internal (and external) investment pools, this statement requires the equity position of each fund that sponsors the pool to be reported as assets in those funds. The effect of this change on the beginning balances at January 1, 1998, was not material and therefore no prior period adjustments were necessary. The unrealized gains included in cash and cash equivalents at December 31, 1998, was \$8,449 for ECBR.

**NOTE 14 - THE YEAR 2000 ISSUE**

The year 2000 issue arises because most computer software programs allocate two digits to the year date field on the assumption that the first two digits will be 19. Without reprogramming, such programs will interpret, for example, the year 2000 as the year 1900. Also, some programs may be unable to recognize that the year 2000 is a leap year.

The year 2000 issue may affect electronic equipment containing computer chips that have date recognition features - such as environmental systems, elevators, and vehicles - as well as computer software programs. In addition, the year 2000 issue

affects not only computer applications and equipment under the South Carolina Department of Commerce - Division of Public Railways's (Division) control but also the systems of other entities with which the Division transacts business. Some of the Division's systems/equipment affected by the year 2000 issue are critical to the continued and uninterrupted operations of the Division.

Because of the unprecedented nature of the year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Management cannot assure that the Division is or will be year 2000 ready, that the Division's remediation efforts will be successful in whole or in part, or that parties with whom the Division does business will be year 2000 ready.

The Y2K problem is an issue the Division's management is fully aware of and has been upgrading all hardware. The last system was installed in January 1999, making all hardware Year 2000 compliant.

All software used in house meets Year 2000 requirements. The ISS and IRCS programs that interface with the other railroads are or will be compliant before the end of 1999. The Divisions banks, Wachovia and NationsBank, have replied to written requests as to compliance. Wachovia has stated that they plan to be compliant by the end of March 1999. NationsBank has stated they will be compliant by the end of June 1999.