

**SOUTH CAROLINA
STATE DEPARTMENT OF EDUCATION**

COLUMBIA, SOUTH CAROLINA

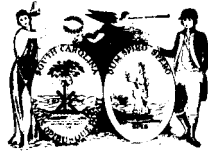
STATE AUDITOR'S REPORT

JUNE 30, 2001

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State of South Carolina



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INDEPENDENT ACCOUNTANT'S REPORT ON APPLYING AGREED-UPON PROCEDURES

June 18, 2002

The Honorable Inez M. Tenenbaum
State Superintendent of Education
South Carolina State Department of Education
Columbia, South Carolina

We have performed the procedures described below, which were agreed to by the management of the South Carolina State Department of Education (the Department), solely to assist you in evaluating the performance of the Department for the fiscal year ended June 30, 2001, in the areas addressed. This engagement to apply agreed-upon procedures was performed in accordance with standards established by the American Institute of Certified Public Accountants. The sufficiency of the procedures is solely the responsibility of the specified users of the 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, and we used estimations and other procedures to determine the reasonableness of collected and recorded amounts by revenue account. We also tested the accountability and security over documents issued for money. The individual transactions selected for testing were chosen randomly. We found no exceptions as a result of the procedures.

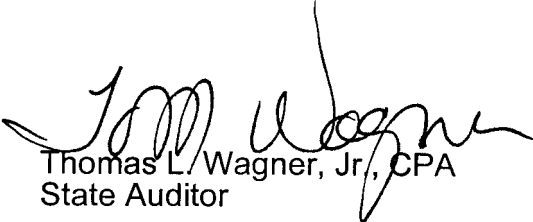
2. We tested selected recorded non-payroll disbursements to determine if these disbursements were properly described and classified in the accounting records, were bona fide disbursements of the Department, and were paid in conformity with State laws and regulations and if internal controls over the 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. We compared current year expenditures to those of the prior year to determine the reasonableness of amounts paid and recorded by expenditure account. The individual transactions selected for testing were chosen randomly. We found no exceptions as a result of the procedures.
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. We compared amounts recorded in the general ledger and subsidiary ledgers to those in various STARS reports to determine if recorded payroll and fringe benefit expenditures were in agreement. We performed other procedures such as comparing current year recorded payroll expenditures to those of the prior year; comparing the percentage change in recorded personal service expenditures to the percentage change in employer contributions; and computing the percentage distribution of recorded fringe benefit expenditures by fund source and comparing the computed distribution to the actual distribution of recorded payroll expenditures by fund source to determine if recorded payroll and fringe benefit expenditures were reasonable by expenditure account. The individual transactions selected for testing were chosen randomly. Our finding as a result of these procedures is presented in Payroll Transaction in the Accountant's Comments section of this report.
4. We tested selected recorded journal entries and all recorded operating and interagency 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 journal entry 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 Department 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. We found no exceptions as a result of the procedures.
6. We obtained all monthly reconciliations prepared by the Department for the year ended June 30, 2001, and tested selected reconciliations of balances in the Department'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 recalculated the amounts, agreed the applicable amounts to the Department'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 Department's accounting records and/or in STARS. The reconciliations selected for testing were chosen randomly. We found no exceptions as a result of the procedures.
7. We tested the Department'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 2001. Our findings as a result of these procedures are presented in Blanket Bond and Legal Services in the Accountant's Comments section of this report.
8. We obtained copies of all closing packages as of and for the year ended June 30, 2001, prepared by the Department 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 Closing Packages in the Accountant's Comments section of this report.
9. We obtained a copy of the schedule of federal financial assistance for the year ended June 30, 2001, prepared by the Department 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. We found no exceptions as a result of the procedures.

We were not engaged to, and did not, perform an audit, the objective of which would be the expression of an opinion on the specified areas, accounts, or items. Further, we were not engaged to express an opinion on the effectiveness of the internal control over financial reporting. Accordingly, we do not express such opinions. Had we performed additional procedures or had we conducted an audit or review of the Department's financial statements or any part thereof, other matters might have come to our attention that would have been reported to you.

The Honorable Inez M. Tenenbaum
State Superintendent of Education
South Carolina State Department of Education
June 18, 2002

This report is intended solely for the information and use of the State Superintendent of Education and of the management of the South Carolina State Department of Education 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.

CLOSING PACKAGES

Introduction

The Office of the Comptroller General (OCG) obtains certain generally accepted accounting principles (GAAP) data for the State's financial statements from agency-prepared closing packages because the State's accounting system (STARS) is on a budgetary basis. We determined that the Department submitted to the OCG certain incorrectly prepared and/or misstated fiscal year-end 2001 closing packages.

To accurately report the Department's and the State's assets, liabilities, and current year operations, the GAAP closing packages must be complete and accurate. Furthermore, Section 1.8 of the Comptroller General's GAAP Closing Procedures Manual (GAAP Manual) states, "Each agency's executive director and finance director are responsible for submitting. . . closing package forms . . . that are: Accurate and completed in accordance with instructions. Complete. Timely." Also, Section 1.8 requires an effective, independent supervisory review of each completed closing package and the underlying working papers and accounting records and completion of the reviewer checklist and lists the minimum review steps to be performed. In addition, Section 1.9 directs agencies to keep working papers to support each amount and other information they enter on each closing package form.

The following outlines the errors noted on certain 2001 closing packages.

Fixed Assets

The fiscal year 2001 ending balance of \$247,672,572 for machinery, equipment and other reported on the General Fixed Assets Summary Form differed from the ending balance of \$248,659,211 recorded in the Department's General Ledger Summary. In response to our inquiries about the difference, Department personnel could only assume the difference to be a result of errors from prior years because a reconciliation of these two amounts has never been performed. In addition, the fiscal year 2001 ending balance of \$231,956,048 for vehicles

included in the Department's fixed assets supporting worksheet did not agree to the ending balance of \$231,768,448 included in the amount reported for machinery, equipment and other on the Department's Book Value Report. According to Department personnel, the difference of \$187,600 is due to an incorrect adjustment made to adjust for items not meeting the Department's capitalization limit. The Department had not corrected this error as of June 2002.

The Department does not currently record Construction in Progress (CIP) on its General Ledger; therefore, we could not agree the fiscal year 2001 CIP ending balance reported on the closing package to the Department's books. Department personnel stated that the Department has never reported CIP on its books.

GAAP Manual Section 3.8 provides guidance for preparation of the Fixed Assets Overview Questionnaire. In addition, those instructions require retention of working papers supporting all information entered on the summary.

Accounts Payable

The Department reported \$78,261,493 of intergovernmental expenditures and \$194,479 of other current expenditures as federal payables (GAAP fund 4005) as of June 30, 2001 on the accounts payable summary form. According to the "Detail Budget Report by Project Component" and the Department's supporting worksheet, the correct amounts of intergovernmental and other current expenditures were \$78,506,551 and \$202,741, respectively. Amounts for subfund 5055 reported on the Department's supporting worksheet for the accounts payable closing package did not foot. These totals were included in the total federal payables amount recorded on the accounts payable summary form. Despite evidence of supervisory review of the closing package and the applicable supporting documentation and completion of the reviewer checklist, the reviewer did not detect this error. Therefore, federal payables reported on the accounts payable summary form were understated by \$253,321.

An effective internal control system requires that adequate supporting documentation be prepared and retained and financial and related information be properly recorded in the accounting and other agency records and be properly summarized in reports prepared therefrom.

Operating Leases

One of five Lease Registers tested during our review of the operating leases closing package did not include a determination of whether the lease was operating or capital (item 11). The lease was for rental of property beginning on July 1, 2000. According to Department personnel, the determination that the lease was operating was made at the inception of the lease but was not documented on the Lease Register.

Section 3.19 of the GAAP Manual requires that, for audit purposes, each agency must retain a completed Lease Register, including item 11, for each lease the agency has entered into.

Recommendations

We recommend that the Department implement procedures to ensure that all future closing packages contain accurate and complete information in accordance with the GAAP Manual instructions. As required by the GAAP Manual, the Department's closing package procedures should include an effective independent review before submitting the forms to the OCG. Each closing package review at a minimum should include the following steps: determine the accuracy and adequacy of documentation prepared, retained and cross-referenced to support each closing package response (monetary and other); determine the reasonableness of each closing package response; agree each response to the closing package worksheets and other supporting documentation and to the accounting and other source records; verify the methodology and formulas used in the supporting documentation and the computations in the working papers and on the closing package; and complete the applicable Closing Package Reviewer Checklist.

We also recommend the Department record CIP on its general ledger and record adjustments in its detail fixed assets records and on its fixed assets closing packages as necessary. In addition, we recommend the Department implement procedures to ensure the accuracy of its fixed assets records. We further recommend that the Department properly complete Lease Registers for all leases it enters into in order to ensure that the Department has properly classified each lease as a capital or operating lease in accordance with GAAP.

BLANKET BOND

The Department did not obtain approvals from the Attorney General and the State Auditor for the blanket bond it purchased in September 1999. This deficiency was discussed with departmental personnel during the fiscal year 2000 Agreed Upon Procedures engagement. In its response to the prior year discussion with management, personnel at the Department stated that the procurement officer was unaware of these requirements. The individual stated that the Department would, however, comply with the law.

Section 1-11-180 of the 1976 South Carolina Code of Laws states, in part, the following:

(A) In addition to the powers granted the Budget and Control Board under this chapter or any other provision of law, the board may: ... (4) approve blanket bonds for a state department, agency, or institution including bonds for state officials or personnel. However, the form and execution of blanket bonds must be approved by the Attorney General.

The Budget and Control Board has delegated the approval for the bonds to the State Auditor.

We recommend the Department obtain the required approvals of the Attorney General and the State Auditor for its employee dishonesty bond.

LEGAL SERVICES

The Department paid for certain legal services that were not properly authorized by the South Carolina Attorney General's Office (AGO). The Department submitted the "South Carolina Attorney General Request for Authorization to Employ Associate Council" form to the AGO on July 3, 2000, for the required approval of attorney services to be provided from July 3, 2000, through June 30, 2001. The Attorney General approved the maximum requested compensation of \$5,000 on July 10, 2000. However, the Department paid a total of \$8,100 to the attorney during the stated dates of service.

Proviso 32.3. of Part IB of the 2000-2001 Appropriation Act states the following:

No department or agency of the State Government shall engage on a fee basis any attorney at law except upon the written approval of the Attorney General and upon such fee as shall be approved by him ...

We recommend the Department establish and implement procedures to ensure that it obtains approval from the South Carolina Attorney General's Office prior to engaging an attorney on a fee basis, to monitor services and cumulative costs under each approved procurement, and to obtain advance approval for expansion of services and/or increased fees.

SECTION B - OTHER WEAKNESS NOT CONSIDERED MATERIAL

The condition described in this section has been identified as a weakness subject to correction or improvement but it is not considered a material weakness or violation of State Laws, Rules, or Regulations.

PAYROLL TRANSACTION

The Department paid an individual \$3,984 from earmarked funds on July 1, 2001, as part of a grievance settlement through the Equal Employment Opportunity Commission (EEOC). Although the Department developed and maintained both a payroll and a personnel file for the person, departmental personnel could not locate a copy of the settlement agreement nor any documentation showing the amount the Department agreed to pay the individual. As a result, we were unable to verify that the Department paid the individual the appropriate amount.

Based on discussions with personnel in the Human Resources and Legal departments, each thought the other was retaining and maintaining documentation to support the amount of the payment.

Proper internal controls require that all expenditures have adequate supporting documentation. Also, the General Records Retention Schedules Administrative and Personnel Records of State Agencies, developed by the Archives and Records Management Division of the State Archives was prepared to provide general retention and disposition schedules for state agencies. It gives state agencies the legal authorization to retain and dispose of administrative and personnel records. These guidelines were established to ensure that agencies retain administrative, legal, fiscal, and other records for as long as necessary and also ensure that records are retained in accordance with state and federal laws, regulations, policies, and procedures.

We recommend that the Department maintain the appropriate supporting documentation for all transactions. Procedures should be established to ensure that supporting documents are properly filed and organized in a logical manner to facilitate retrieval. Proper communication should be established and maintained between departments

within the agency to ensure that records are properly retained and maintained. We further recommend that employees responsible for maintaining the Department's records be informed of the approved record retention policy.

MANAGEMENT'S RESPONSE

MANAGEMENT'S RESPONSE

The management of the South Carolina State Department of Education did not respond to the findings identified in the Accountant's Comments Section of this report by the due date specified in our transmittal letter accompanying the preliminary draft for the agency's review dated August 6, 2002.

5 copies of this document were published at an estimated printing cost of \$1.58 each, and a total printing cost of \$7.90. The FY 2001-02 Appropriation Act requires that this information on printing costs be added to the document.