

November 8, 2000

Mr. Thomas L. Wagner, Jr., CPA
State Auditor
Office of the State Auditor
1401 Main Street, Suite 1200
Columbia, SC 29201

Dear Mr. Wagner:

My staff has completed our review of the agreed-upon procedures report for the year ending June 30, 1999 and authorizes the release of this report. I am enclosing our response to your comments, which will be added to your report.

We have made many improvements and will continue to implement your recommendations. Although you will not find all these matters corrected during your next review of fiscal year 2000, it is our goal to have all recommendations implemented by the end of fiscal year 2001.

Please accept our thanks for minimizing the disruption to our staff. I believe it was an efficient use of resources of both of our staffs to mainly follow-up on the 1998 report. It allowed us more time to make the needed improvements.

Sincerely,

Stanhope S. Spears
Major General, SCARNG
The Adjutant General

Internal Control

We have developed an internal control program and are working to ensure that it is implemented and that controls in all areas are improved. In May, 2000, we hired a certified public accountant who has considerable state experience. We are working to increase overall state knowledge through internal and external training and by hiring new employees with state experience. We are focusing our hiring efforts on permanent (not temporary) employees with a focus on long-term solutions as well as some short-term, highly experienced employees with a short-term focus of catching up areas that have fallen behind. To improve compliance with laws, rules, and regulations, we have obtained current reference materials, such as the STARS Manual. We are taking steps to correct the findings noted in the last several years' audit reports. However, it will take time to correct some of these weaknesses that existed for several years.

For fiscal year 2000, we revised our account structure to maximize the use of all components of an account number: department, fund, and object. By doing so, we can now report in a manner usable by both the federal and state government. This has eliminated the need for separate records to be maintained for federal reporting purposes and has also increased the working relationship between budget and finance and the Agency's program managers.

We have informed the United States Property and Fiscal Officer (USPFO) that we have accounts from 1997 through 1999 that are not closed on our books. In September, 2000, we worked with the USPFO to close the 1999 Army National Guard accounts and are presently working with Air National Guard staff to close its accounts for 1997 through 1999.

Bringing the reconciliation process up to date is our biggest challenge. We have made significant improvements in this process and corrected many of our prior years' errors. We expect that this will be the longest process in our corrective action plan.

We no longer maintain the resource manager position. Instead, we are using a team-based management approach whereby a group of team leaders work together to manage an area. The chief of staff for state operations coordinates the resource management area. The intent of this change is to ensure that the group is working together and staying in touch with the day-to-day operations.

We are continuing to improve the quality assurance (referenced in your report as internal review) process. Beginning with federal fiscal year 2001, we are transferring an employee with a bachelors degree in accounting to the quality assurance area. She is developing an annual audit plan and will report to a newly formed audit committee that is chaired by the Adjutant General.

Revenues

Deposits and Supporting Information. In December, 1998, the revenue and reconciliation accountant resigned and was not replaced for several months. During this time, the Agency did not properly record and account for its revenues as noted in your report. We have made numerous journal entries in fiscal years 2001 and 2000 to correct these errors, omissions, and double counting as we detected them in our “catch-up” reconciliation process. We have reissued guidance to the armories and other receipting locations regarding the required controls and procedures.

Coding of Revenue. We are properly using object code 2805 – federal grant subcontract state to distinguish federal revenues received from other state agencies from those received directly from the federal government. (The majority of our federal revenues are received directly from the federal government.)

Transaction Numbering. The problem with transaction numbering continued through fiscal year 2000. However, we recorded and filed the hard copy documents using the SABAR transaction number. For fiscal year 2001, we are not using our separate numbering system that proved unmanageable and intend to use only the SABAR recorded number.

Expenditures

Procurement Code. Our procedure is to record that the price is fair and reasonable on the purchase requisition because this is the place in the process where this determination is made. (Because of the decentralization of the procurement and accounts payable process, the purchaser usually will not receive the invoice. The requisitioner and the appropriate approvers are the ones who should make this determination not the accounts payable clerks.) We have determined that this procedure would not cover direct payments, i.e., vouchers paid without a purchase order. Beginning in fiscal year 2001 for these vouchers, we will ensure that the invoices are evaluated and noted as “fair and reasonable”.

Expenditure Cutoff. We significantly improved in this area at the end of fiscal year 2000. Both accounts payable and procurement worked to ensure that open purchase orders were closed as either paid or cancelled and that all voucher information (invoice, receiving report, etc.) was received timely to permit payment before the cutoff of month thirteen. We corresponded with all program areas to remind them of the cutoff requirements and to encourage their support.

Reconciliations

As previously stated, the reconciliation process is our biggest challenge. Because we did not properly prepare reconciliations and numerous differences exist between SABAR and

STARS, we are experiencing a long, difficult process to correct the errors and bring the reconciliations up to date. We are trying to identify a temporary employee familiar with the state system and reconciliation experience to prepare the older reconciliations. Our existing staff should be able to perform the reconciliation process on a current basis.

Accounting Transactions

Journal Entries. The same process that caused the numerical sequence finding for revenues caused this finding. See that response for the corrective action taken.

Appropriation Transfers. We have developed controls to ensure that all documents, including appropriation transfers, are properly prepared and approved. The document referenced in your report was properly recorded in “current transactions” for revenue and cash. We did not use SABAR for budget monitoring in fiscal year 1999; therefore, we did not post this document to budgetary expenditure accounts.

Closing Packages

We made significant improvements in the closing packages prepared for fiscal year 2000. For fiscal year 2000, we prepared a loans receivable package. Lease closing packages need improvement, as we did not have proper source data available to prepare these packages. For accounts payable, we documented our review of potential vouchers and listed our accounts payable. Also, we estimated our future payments on disaster assistance accounts payable. For the 2000 closing package, we did not include payroll in our accounts payable.

Our grants and entitlements package is supported by the schedule of federal financial assistance and the accounts payable closing package. Although our fixed assets accounting system supports the 2000 closing package, we still need to improve our fixed assets accounting system. The SABAR module for compensated absences does not properly separate holiday and overtime-compensatory leave when balances are brought forward. We manually calculated the separate amounts for the closing package. However, we are in the process of modifying our compensated absences accounting system in order to monitor the use of compensatory leave (with the 90-day rule). Overall, we have significantly improved the closing package process.

Deferred Revenues

The Agency’s deferred revenues are minimal, mainly for armory rental deposits collected in advance. Due to employee turnover and the new employee being unaware of the requirement, we did not capture deferred revenues at the end of fiscal year 2000. We will include this requirement in budget and finance’s policies and procedures manual and ensure that the revenue accountant captures this information at the end of fiscal year 2001.

Petty Cash Checking Accounts

Currently, each of the approximately 85 units has a petty cash bank account. The Agency recently revised Adjutant General Regulation 37-4 to require that the unit maintenance funds be maintained at the battalion level with each unit in a battalion receiving \$500 once per year. As we determine which accounts to maintain and which to close, we intend to obtain the proper internal and external approvals for the remaining accounts. We currently anticipate maintaining approximately 16 accounts with a total of \$42,500. Also, we intend to audit the accounts as we close them.

Workers' Compensation

We used our past credits and resumed paying premiums in fiscal year 2000. We allocated the premiums to each fund based on the proportionate share of payroll.

The employee who negotiated the prior credits is no longer employed by the Agency and the Agency does not have the records to determine if any prior year corrections are required. In the future, we will ensure that premiums, credits, and refunds are applied proportionate to payroll and to the applicable periods.

Tuition Assistance Program

As previously stated we completed the loans receivable closing package for 2000, including only receivables that had not exceeded the three-year statute of limitations. Based on the advice of the Judge Advocate General, we still have not contracted with the South Carolina Department of Revenue (DOR) for debt collection pending the outcome of legal cases against the DOR program.

The Agency has new legislation requiring the restructuring of the tuition assistance program. The new program will be associated with the South Carolina Student Loan Corporation and will take the Agency out of the debt collection process. The program is currently being developed and will probably be effective beginning in fiscal year 2002.

Schedule of Federal Financial Assistance

The schedule for 2000 was prepared from and reconciled to federal funds in SABAR. We improved the controls over the process and do not anticipate significant findings in this area.

Public Assistance

Due to changes in the way we handle this grant, the finding is no longer valid as written. However, we will comply with federal and state requirements for disaster assistance funds.

In fiscal year 2000, we assumed responsibility and accountability for federal disaster funds, regardless of whether the funds were expended by the Agency (activation of military) or passed through to other governments. Therefore, we changed the subfund accounting for disaster assistance. Most pass-through transactions will flow through the 5511 subfund and be treated as special revenue funds. Beginning with fiscal year 2001 in accordance with Comptroller General requirements, we are accounting for activity passed through to other state agencies in the 5544 pass-through subfund that is classified in STARS as an **agency** fund.

Regarding reimbursed funds, we have expended the \$339,412 and \$5,506 of the \$657,000. The Agency did not realize that administrative costs should be remitted to the State General Fund. Currently, we do not have funds available to remit \$344,918. We will pursue this matter with State authorities to resolve this matter as soon as possible.

Cost Allocation Plan

For fiscal years 1997 through 1999, the Agency had a “cost allocation plan” (CAP). Then the National Guard determined that the MCA does not allow indirect costs, specifically statewide-centralized costs. Therefore, it allowed a “centralized personnel plan” (CPP) to cover a state military department’s centralized costs. For fiscal year 2000, the Agency had a CPP. In this CPP as recommended in your report, we adjusted for the differences in estimated vs. actual based on the estimates used in the 99 CAP.

In the development of all future CPPs, we will ensure that we apply all applicable cost principles and not repeat the errors listed in your report. Although we did not provide sufficient information for the state’s auditors for the 1997 through 1999 plans, the USPFO did approve these plans and has closed the MCA for fiscal years 1997 through 1999. Therefore, we consider these plans closed.

Because the National Guard Bureau does not consider these plans to be indirect costs, we do not believe that these funds should be remitted to the State General Fund. Beginning with fiscal year 2000, our centralized costs recoveries were used only for the intended purposes. With the implementation of the CPP for fiscal year 2001, we intend to eliminate all temporary grant positions in the centralized cost departments. (We will only have temporary grant and time-limited positions in other departments that are funded by earmarked and federal funds.)

Permanent Improvement Project Accounting

Effective July 1, 2000, we reorganized our permanent improvement project accounting. In doing so, procurement’s role in this area will be limited solely to approving procurements and issuing purchase orders. Facilities management and budget and finance will handle SPIRS accounting and reporting. We are in the process of developing controls and procedures to ensure that we are in federal and state compliance with permanent improvement project accounting. Also, we are in the process of closing completed SPIRS projects on the SPIRS and STARS systems as well as our SABAR

system. We are reviewing CIB balances with the state and federal military construction balances with the USPFO to determine if we have unused funds for permanent improvement projects and what the proper disposition of such funds should be.

Regarding errors in specific projects, we will review and correct errors as appropriate. The Hawk projects (Pickens, Ware Shoals, and Fountain Inn) are in mediation but should be settled soon. As soon as we learn the outcome and finalize the costs, we will ensure that all three projects are properly charged and capitalized.

Accounting System

We have made significant progress in using SABAR to monitor budgets. As mentioned previously, the full use of department numbers has made our accounting system more useful to our internal users and the USPFO. We continue to encourage program managers to discuss their needs with budget and finance so that they will not see the necessity to maintain separate systems.

SABAR did not have an automatic rollover option as noted in your report. We agreed that this option was needed and contracted with the software developer to have this option. When we opened fiscal year 2001 on SABAR, we successfully used this option. It saved an enormous amount of time and eliminated errors that can easily occur in such a large, manual process. Also, we currently prepare all federal reports directly from SABAR.

Data Translation to the State

We have improved our understanding of how STARS and Series Z interrelate to each other and to SABAR. We are working to correct all such deficiencies in SABAR and in the information we provide to STARS and Series Z. We are working the State Treasurer to ensure that we properly comply with cash management.