

**STATE OF SOUTH CAROLINA
OFFICE OF THE COMPTROLLER GENERAL**

GAAP CLOSING PROCEDURES MANUAL

CLAIMS CLOSING PACKAGE	REFERENCE	3.15
	ISSUE DATE	6-30-2002
	PAGE	1

PURPOSE AND OBJECTIVES

The State is subject to many types of claims. For this closing package, a claim is an application for payment of damages or a policy benefit resulting from the occurrence of an event, such as destruction of, or damage to, an asset. A claim may be paid by an insurance company, a State claim-paying program, or by the agency itself if that agency self-insures its risk.

State claim-paying programs accept risks instead of paying insurance companies to accept these risks. Claim-paying programs either:

- o Contract with private insurance carriers to process and/or pay claims.
- o Pay claims directly.

Examples of claim-paying programs in State government include:

- o State Health and Dental Insurance Plans.
- o Insurance Reserve Fund.
- o State Accident Fund.
- o Patients' Compensation Fund.

There may be others. The State Unemployment Compensation Program and the Victims' Compensation Fund, however, are not claim-paying programs for closing package purposes.

Instead of paying an insurance company or a State claim-paying program to accept its risks, an agency may choose to self-insure all or certain of its risks. An agency may intentionally self-insure against risk by setting aside cash and other resources deemed sufficient to pay the costs of losses when they occur. An agency may also unintentionally self-insure by under-insuring a risk of loss. Regardless, self-insurance is, in reality, no insurance because the risk of loss has not been transferred to a third party.

This closing package affects only State claim-paying programs and State agencies that self-insure any type of risk. It does not affect situations where the State pays insurance premiums to private insurers.

STATE OF SOUTH CAROLINA
OFFICE OF THE COMPTROLLER GENERAL

GAAP CLOSING PROCEDURES MANUAL

CLAIMS CLOSING PACKAGE	REFERENCE	3.15
	ISSUE DATE	6-30-2002
	PAGE	2

This closing package does not apply to:

- o Public Entity Risk Pools under the Governmental Accounting Standards Board's Statement No. 10, "Accounting and Financial Reporting for Risk Financing and Related Insurance Issues."
- o Lawsuits filed against the State. Agencies report lawsuits in the Litigation Closing Package.
- o Leases.

The State prepares its financial statements in accordance with Generally Accepted Accounting Principles (GAAP). GAAP requires that the State record liabilities for the estimated future costs of all events that occurred on or before June 30 if it is probable that an asset has been impaired or a liability has been incurred as of that date and the loss amount can be reasonably estimated. GAAP further requires the State to disclose events that may materially affect future claims costs.

AGENCY ACTION REQUIRED

- o Complete the Claims Closing Package if your agency's claims liabilities at the end of the fiscal year (June 30) total \$100,000 or more.
 - Complete a Claims Summary Form (GAAP Form 3.15.1) for each claim-paying program and for each type of risk your agency self-insures.
 - Complete the Additional Claims Information Form (GAAP Form 3.15.2) as of June 30 for each Claims Summary Form (GAAP Form 3.15.1) completed.
 - Return these Forms to the Comptroller General's Office no later than September 30. If you can return them earlier, please do so.
- o If something happens during the six months after June 30 (July 1 through December 31) that may materially change future claim costs:
 - Complete an updated Additional Claims Information Form (GAAP Form 3.15.2).
 - Submit it to the Comptroller General's Office as soon as possible.

STATE OF SOUTH CAROLINA
OFFICE OF THE COMPTROLLER GENERAL

GAAP CLOSING PROCEDURES MANUAL

CLAIMS CLOSING PACKAGE	REFERENCE	3.15
	ISSUE DATE	6-30-2002
	PAGE	3

Examples of such events are:

- New legislation.
- New agency policies.
- External events (such as natural or man-made disasters, epidemics, etc.).

that will materially change:

- The dollar amount per valid claim.
 - The number of valid claims.
- o Complete the Claims Closing Package Reviewer Checklist (GAAP Form 3.15.3) before submitting either the Claims Summary Form (GAAP Form 3.15.1) or the Additional Claims Information Form (GAAP Form 3.15.2). Retain the checklist with your working papers, but do not return it to the Comptroller General's Office.

KEY TERMS

Claim. A claim is an application for payment of damages or a policy benefit resulting from the occurrence of an event, such as the destruction of, or damage to, an asset.

Claim-Paying Program. State claim-paying programs accept risks instead of paying insurance companies to accept these risks. Claim-paying programs do one or both of the following:

- o Contract with private insurance carriers to process and/or pay claims.
- o Pay claims directly.

The State Unemployment Compensation Program and the Victims' Compensation Fund, however, are not claim-paying programs for closing package purposes.

Claims Known But Not Paid. These are claims that satisfy both of the following conditions:

- o The State is aware that a covered event occurred on or before June 30. Example: a covered party filed a claim on or before June 30.

STATE OF SOUTH CAROLINA
OFFICE OF THE COMPTROLLER GENERAL

GAAP CLOSING PROCEDURES MANUAL

CLAIMS CLOSING PACKAGE	REFERENCE	3.15
	ISSUE DATE	6-30-2002
	PAGE	4

- o As of June 30, your agency either has made no payment or only partial payment on the claim.

The amount for claims known but not paid includes both:

- o The known amount that the State must pay in the future for claims settled on or before June 30.
- o An estimate of amounts the State will pay in the future for claims in process (if any) at June 30.

Current Liability. Current liabilities at June 30 are liabilities an agency expects to pay before June 30 of the next fiscal year.

Incurred But Not Reported (IBNR). Incurred but not reported is the estimated cost of covered events that:

- o Occurred on or before June 30.
- o Will result in valid claims against the State.
- o Are unknown to the State at June 30 (the covered party has not yet filed a claim).

Actuaries and accountants refer to this estimated cost as IBNR.

Liability. A liability is an obligation resulting from past events that will (or is likely to) result in future payments and/or reductions in future revenues.

Long-Term Liability. Long-term liabilities at June 30 are liabilities that an agency expects to pay after June 30 of the next fiscal year (i.e., beyond one year).

Probable. A future event is probable if the event is likely to occur.

Risk Financing. Risk financing is an element of risk management that involves implementation of plans for paying the costs of losses when they occur. Some risk financing options available to organizations are to:

- o Insure risk by paying premiums to an insurance company or to a State claim-paying program (see definition above), such as the Insurance Reserve Fund, which accepts the risk and agrees to pay the premium-paying organization in the event of a covered loss.
- o "Self-insure" risk (see definition of Self-Insurance).

STATE OF SOUTH CAROLINA
OFFICE OF THE COMPTROLLER GENERAL

GAAP CLOSING PROCEDURES MANUAL

CLAIMS CLOSING PACKAGE	REFERENCE	3.15
	ISSUE DATE	6-30-2002
	PAGE	5

Risk Management. Risk management is the process of managing an organization's activities to minimize the adverse effects of certain losses. Organizations are subject to risks of loss arising from events such as:

- o Damages to, or destruction of, assets from causes such as fire, natural disasters, theft, vandalism, etc.
- o Injuries to employees.
- o Torts (wrongful acts, injuries, or damage, not involving a breach of contract, for which civil actions can be brought).

Self-Insurance. Self-insurance is the retention of risk of loss by an entity rather than transferring that risk to a third party through the purchase of an insurance policy. Self-insurance is sometimes accompanied by the setting aside of assets to pay the costs of losses when they arise. In reality, self-insurance is no insurance.

Subsequent Event. Subsequent events are events or transactions that:

- o Occur after June 30 but before the State issues its financial statements.
- o Have a material effect on the statements and/or the auditor's report.

Governments must disclose subsequent events in their financial statements.

Subsequent Period. The subsequent period is the time after June 30 but before the State issues its financial statements. The State plans to issue its financial statements by December 31. For practical purposes, therefore, the subsequent period is between July 1 and December 31. Governments must disclose on their financial statements any material events that occur during the subsequent period.

ACCOUNTING PRINCIPLES AND POLICIES

Accounting Standards

Settled claims that require the State to make future payments or suffer other future losses are liabilities. GAAP requires the State to record

**STATE OF SOUTH CAROLINA
OFFICE OF THE COMPTROLLER GENERAL**

GAAP CLOSING PROCEDURES MANUAL

CLAIMS CLOSING PACKAGE	REFERENCE	3.15
	ISSUE DATE	6-30-2002
	PAGE	6

material liabilities existing at June 30 on its financial statements. Therefore, if your agency has claims against it at June 30 of \$100,000 or more, you should complete the Claims Summary Form (GAAP Form 3.15.1).

Other GAAP requirements relating to claims appear in:

- o *Governmental Accounting Standards Board (GASB) Codification Sections 1500.101 through .108, 1600.129, and C50.101 through .149.*
- o *AICPA's Audits of State and Local Government Units.*
- o *Financial Accounting Standards Board (FASB) Statement 5, Accounting For Contingencies as revised and interpreted.*
- o *GASB Statement No. 10, Accounting and Financial Reporting for Risk Financing and Related Insurance Issues as amended by GASB Statement No. 34.*
- o *GASB Statement No. 34, Basic Financial Statements - and Management's Discussion and Analysis-for State and Local Governments.*

Governmental Accounting Standards Board (GASB) Codification Section 2200.116 requires that liabilities of Governmental, Enterprise, and Internal Service Funds with maturities greater than one year be reported in two components in the government-wide financial statements—"the amount due within one year and the amount due in more than one year." Enterprise, Internal Service, and Trust Funds are reported in a similar manner within the fund financial statements.

The reporting of Governmental funds in the fund financial statements, however, is governed by Codification Section 1600.129, which defines Governmental fund current liabilities as "the amount left unpaid at the end of the reporting period that normally would be liquidated with expendable available financial resources." Long-term liabilities of Governmental Funds are recorded only in the government-wide financial statements, not in the fund financial statements.

Liabilities of Trust and Agency Funds are recorded only in the fund financial statements, not in the government-wide financial statements.

GAAP requires that the State record liabilities for the estimated future costs of insured events that occurred on or before June 30 if it is probable that an asset has been impaired or a liability has been

STATE OF SOUTH CAROLINA
OFFICE OF THE COMPTROLLER GENERAL

GAAP CLOSING PROCEDURES MANUAL

CLAIMS CLOSING PACKAGE	REFERENCE	3.15
	ISSUE DATE	6-30-2002
	PAGE	7

incurred as of that date and the loss amount can be reasonably estimated. GAAP further requires the State to report two components of this estimated cost:

- o Cost of claims known but not paid at June 30.
- o Estimate of claims incurred but not reported at June 30.

GASB Codification Section C50.114 states:

Expenditures/expenses and liabilities may be estimated through a case-by-case review of all claims, the application of historical experience to the outstanding claims, or a combination of these methods. Estimates of IBNR losses should be based on historical experience. When historical experience is used, the outstanding claims should be stratified by amount and type of claim, and the strata should be sufficiently refined to ensure that the estimation is reasonable.

Events that will materially change future claims costs may occur after June 30 but before the State issues its financial statements. Such events are subsequent events. GAAP for subsequent events appears in:

- o GASB Codification Sections 2300.106 and C50.145.
- o Various Statements on Auditing Standards (SAS's) and related interpretations issued by the American Institute of Certified Public Accountants.

State Policies--General

It is the State's policy to record claims liabilities on its financial statements if it is probable that an asset has been impaired or a liability has been incurred as of June 30 and the loss amount can be reasonably estimated. These liabilities will include the estimated future costs of all covered events that occurred on or before June 30. The State's claims liabilities include:

- o Claims known but not paid.
- o Incurred but not reported.

STATE OF SOUTH CAROLINA
OFFICE OF THE COMPTROLLER GENERAL

GAAP CLOSING PROCEDURES MANUAL

CLAIMS CLOSING PACKAGE	REFERENCE	3.15
	ISSUE DATE	6-30-2002
	PAGE	8

These liabilities are estimates. Agencies may estimate liabilities through:

- o A case-by-case review of all claims.
- o The application of historical experience to the outstanding claims.
- o A combination of these methods.

When agencies use historical experience, they should stratify the outstanding claims by amount and type of claim. Agencies should refine these strata enough to ensure that the estimation is reasonable.

The State will disclose events occurring during the subsequent period that will materially affect future claims costs.

State Policies--Claims Known But Not Paid

The amount for Claims Known But Not Paid includes both:

- o Known amounts the State must pay in future years for claims settled on or before June 30.
- o An estimate of amounts the State will pay in future years for claims in process (if any) at June 30.

There are many ways to estimate the amount the State will pay in future years for claims in process at June 30. For example, the agency might compute:

- o Total cost resulting from claims filed during some previous fiscal year.
- o Divided by the number of claims filed during that year.
- o Times the total number of claims in process at June 30 this year.

Or the agency may compute:

- o Average cost per valid claim over a recent period of time.
- o Times the number of claims in process at June 30 this year estimated to be valid.

STATE OF SOUTH CAROLINA
OFFICE OF THE COMPTROLLER GENERAL

GAAP CLOSING PROCEDURES MANUAL

CLAIMS CLOSING PACKAGE	REFERENCE	3.15
	ISSUE DATE	6-30-2002
	PAGE	9

The exact computation will depend on data available to the agency when it completes the Claims Summary Form (GAAP Form 3.15.1).

State Policies--Incurred But Not Reported (IBNR)

Agencies should report IBNR only if it is probable that claims will be asserted and the loss can be reasonably estimated. The exact computation of IBNR will depend on data available. Computation of IBNR can be complex. The Comptroller General's Office prefers to use estimates of IBNR that independent consulting actuaries have prepared. If this is not practical, the agency's staff should estimate IBNR.

State Policies--Current and Long-Term Claims Liabilities

The State's policy is to use a one-year availability period for purposes of reporting its Governmental funds. Accordingly, for all practical purposes, the definitions of current and long-term liabilities contained in *Governmental Accounting Standards Board (GASB) Codification* Section 2200.116 apply across all fund types and activities. Specifically, current liabilities are those "due within one year," and long-term liabilities are those "due in more than one year."

Components of long-term liabilities include:

- o Claims known but not paid that the agency expects to pay from future financial resources.
- o Claims incurred but not reported.

WORKING PAPERS

All working papers may be subject to audit. The agency should keep copies of the completed Claims Summary Form (GAAP Form 3.15.1). In addition, the agency should keep any documents that support data that appears on that Form. Such documents may include:

- o Actuarial reports.
- o Computations supporting estimates with full description of:
 - Any assumptions made.
 - Mathematical, actuarial, and/or statistical methods used.

STATE OF SOUTH CAROLINA
OFFICE OF THE COMPTROLLER GENERAL

GAAP CLOSING PROCEDURES MANUAL

CLAIMS CLOSING PACKAGE	REFERENCE	3.15
	ISSUE DATE	6-30-2002
	PAGE	10

-- Each component figure in the computation and any supporting source documents (such as claim forms).

Appropriate documentation and the level of detail will vary according to circumstances.

STATE OF SOUTH CAROLINA
OFFICE OF THE COMPTROLLER GENERAL

GAAP CLOSING PROCEDURES MANUAL

CLAIMS CLOSING PACKAGE

REFERENCE	3.15
ISSUE DATE	6-30-2002
PAGE	11

GENERAL INSTRUCTIONS--CLAIMS SUMMARY FORM (GAAP FORM 3.15.1)

- o All State agencies that either administer claim-paying programs or self-insure any type of risk with claims liabilities at June 30 totaling \$100,000 or more must complete the Claims Summary Form (GAAP Form 3.15.1).
- o Use separate Claims Summary Forms (GAAP Form 3.15.1) for separate claim-paying programs and for each type of self-insured risk (e.g., vehicle collision, tort liability, etc.).
- o Return the Form to the Comptroller General's Office no later than September 30.
- o Round all dollar amounts to the nearest whole dollar.
- o The person who completes and signs the Form should keep a copy. The Comptroller General's Office will telephone this person if there are any questions.
- o Exhibit 3.15 (A) shows a sample completed Claims Summary Form (GAAP Form 3.15.1). Detailed instructions for completing the Form follow the Exhibit.

STATE OF SOUTH CAROLINA
OFFICE OF THE COMPTROLLER GENERAL

GAAP CLOSING PROCEDURES MANUAL

CLAIMS CLOSING PACKAGE

REFERENCE	3.15
ISSUE DATE	6-30-2002
PAGE	12

STATE OF SOUTH CAROLINA
CLAIMS SUMMARY FORM
At June 30, 2002 (1)

EXHIBIT
3.15 (A)

Agency:	(2)	<u>A99</u>	<u>Sample Agency</u>		
		Code	Name		
Prepared:	(3)	<u>7/15/02</u>	By: <u>J. P. Junior</u>	Title: <u>Accountant I</u>	Phone: <u>734-1234</u>
		Date	Employee Name		
Approved:	(3)	<u>7/18/02</u>	By: <u>I. M. Senior</u>	Title: <u>Dir. of Accounting</u>	Phone: <u>734-2345</u>
		Date	Employee Name		
Name of Claim-Paying Program/Type of Self-Insured Risk: (4) <u>Vehicle Collision/Comprehensive</u>					
GAAP Fund Code:		<u>2005</u> (5)	GAAP Fund Name: <u>Departmental General Operating—Earmarked</u> (6)		
Description					Dollar Amount
Liability for Claims that the agency paid or plans to pay during STARS FM 13 of the current fiscal year					(7) \$ 25,000
Liability for Claims that the agency plans to pay during STARS FM 01 – FM 12 of the next fiscal year					(8) \$ 65,000
Liability for Claims that the agency plans to pay <i>after</i> June 30 of <i>next</i> fiscal year					(9) \$ 20,000
GAAP Fund Total					(10) \$ 110,000

**STATE OF SOUTH CAROLINA
OFFICE OF THE COMPTROLLER GENERAL**

GAAP CLOSING PROCEDURES MANUAL

CLAIMS CLOSING PACKAGE	REFERENCE	3.15
	ISSUE DATE	6-30-2002
	PAGE	13

COMPLETING THE CLAIMS SUMMARY FORM (GAAP FORM 3.15.1)

REF	EXPLANATION
(1)	Enter the fiscal year for which this Form applies.
(2)	Enter the agency name and three-character STARS agency code.
(3)	Complete all information regarding preparation of this Form. The Finance Director or Executive Director should approve the Form before sending it to the Comptroller General's Office. The agency should retain a copy of the completed Form.
(4)	Enter the name of the claim-paying program or type of self-insured risk (e.g., vehicle collision, tort liability, etc.).
(5)	Enter the four-digit GAAP fund code of the fund responsible for payment of the claims. (See Appendix A.)
(6)	Enter the name of the GAAP fund responsible for payment of claims. (See Appendix A.)
(7)	Enter the portion of the current claims liability at June 30 that the agency will pay (or has already paid) <i>during STARS FM 13</i> of the current fiscal year. (The Comptroller General's staff will reclassify this amount from Accounts Payable to Claims Payable.)
(8)	Enter the portion of the current claims liability at June 30 that the agency plans to pay during STARS FM 01 through FM 12 of the next fiscal year.
(9)	Enter the long-term portion of the claims liability at June 30 (i.e., the portion that the agency plans to pay in years beyond the next fiscal year).
(10)	Enter the total claims liability at June 30. Amount entered must equal the sum of items (7), (8) and (9).

STATE OF SOUTH CAROLINA
OFFICE OF THE COMPTROLLER GENERAL

GAAP CLOSING PROCEDURES MANUAL

CLAIMS CLOSING PACKAGE	REFERENCE	3.15
	ISSUE DATE	6-30-2002
	PAGE	14

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STATE OF SOUTH CAROLINA
OFFICE OF THE COMPTROLLER GENERAL

GAAP CLOSING PROCEDURES MANUAL

CLAIMS CLOSING PACKAGE	REFERENCE	3.15
	ISSUE DATE	6-30-2002
	PAGE	15

GENERAL INSTRUCTIONS--ADDITIONAL CLAIMS INFORMATION FORM (GAAP FORM 3.15.2)

- o Complete an Additional Claims Information Form (GAAP Form 3.15.2) as of June 30 for each Claims Summary Form (GAAP Form 3.15.1) completed. Return these Forms to the Comptroller General's Office no later than September 30.
- o If anything happens during the six months after June 30 that could materially change future claims costs:
 - Complete an updated Additional Claims Information Form (GAAP Form 3.15.2).
 - Submit it to the Comptroller General's Office as soon as possible.

Examples of such events are:

- New legislation.
- New agency policies.
- An external event (such as a natural or man-made disaster, epidemic, etc.).

that will materially change:

- The amount of future valid claims.
- The number of claims filed in the future.

- o Use separate Additional Claims Information Forms (GAAP Form 3.15.2) for separate claim-paying programs and for different types of self-insured risk (e.g., vehicle collision, tort liability, etc.).
- o The person who completes and signs the Form should keep a copy. The Comptroller General's Office will telephone this person if there are any questions.
- o Exhibit 3.15 (B) shows a sample completed Additional Claims Information Form (GAAP Form 3.15.2). Detailed instructions for completing the Form follow the Exhibit.

**STATE OF SOUTH CAROLINA
OFFICE OF THE COMPTROLLER GENERAL**

GAAP CLOSING PROCEDURES MANUAL

CLAIMS CLOSING PACKAGE

REFERENCE	3.15
ISSUE DATE	6-30-2002
PAGE	16

STATE OF SOUTH CAROLINA
ADDITIONAL CLAIMS INFORMATION FORM

EXHIBIT
3.15 (B)

Agency:	(1)	<u>A99</u>		<u>Sample Agency</u>	
		Code		Name	
Prepared:	(2)	<u>9/15/02</u>	By:	<u>J. P. Junior</u>	Title: <u>Accountant I</u> Phone: <u>734-1234</u>
		Date		Employee Name	
Approved:	(2)	<u>9/18/02</u>	By:	<u>I. M. Senior</u>	Title: <u>Dir. of Accounting</u> Phone: <u>734-2345</u>
		Date		Employee Name	

Name of Claim – Paying Program/Type of Self-Insured Risk: **(3)** Vehicle Collision/Comprehensive

(4) Information as of: 6 / 30 / 02 / / (between 7/1 and 12/31)

(5) Please briefly explain how you compute claims known but not paid for claims in process at June 30.
Case by case review of all claims in process.

(6) Please briefly explain how you compute claims incurred but not reported (IBNR) at June 30.
Actuarial study.

If an actuary computes the IBNR figure for you, please attach a copy of the actuary's report.

(7) Since the last Additional Claims Information Form you submitted, has anything happened that may materially change future claims costs? Yes No

(8) If "Yes," please explain

**STATE OF SOUTH CAROLINA
OFFICE OF THE COMPTROLLER GENERAL**

GAAP CLOSING PROCEDURES MANUAL

CLAIMS CLOSING PACKAGE	REFERENCE	3.15
	ISSUE DATE	6-30-2002
	PAGE	17

COMPLETING THE ADDITIONAL CLAIMS INFORMATION FORM (GAAP FORM 3.15.2)

- | REF | EXPLANATION |
|-----|--|
| (1) | Enter the agency name and three-character STARS agency code. |
| (2) | Complete all information regarding preparation of this Form. The Finance Director or Executive Director should approve the Form before sending it to the Comptroller General's Office. The agency should retain a copy of the completed Form. |
| (3) | Enter the name of the claim-paying program or type of self-insured risk (e.g., vehicle collision, tort liability, etc.). |
| (4) | Check one block to indicate whether the data is year-end data or subsequent period data. For year-end data, fill in the year. If the Form describes major changes that occurred between July 1 and December 31, enter the date that the change occurred. |
| (5) | Briefly describe the way you estimate the liability for claims in process at June 30. |
| (6) | Briefly describe the way you estimate the liability for Incurred But Not Reported. |
| (7) | Sometimes things happen that materially change: <ul style="list-style-type: none"> o The cost per valid claim. o The number of valid claims filed in future periods. <p>For example, new legislation or new agency policies may affect the cost per valid claim. Likewise, the number of valid claims filed in future periods may increase if natural or man-made disasters or epidemics occur. State whether any such events occurred since the last time you submitted an Additional Claims Information Form (GAAP Form 3.15.2).</p> |
| (8) | Describe the nature of the event(s). Attach copies of new laws or policies if applicable. If possible, please estimate the dollar effect of the event(s) on future claims costs. |

STATE OF SOUTH CAROLINA
OFFICE OF THE COMPTROLLER GENERAL

GAAP CLOSING PROCEDURES MANUAL

CLAIMS CLOSING PACKAGE	REFERENCE	3.15
	ISSUE DATE	6-30-2002
	PAGE	18

GENERAL INSTRUCTIONS--CLAIMS CLOSING PACKAGE, REVIEWER CHECKLIST (GAAP FORM 3.15.3)

- o The purpose of the Reviewer Checklist is to help your agency perform an effective review of the completed closing package forms **before** you submit them to the Comptroller General's Office. An effective review is essential to minimizing closing package errors. As such, it is an important internal control. **Completion of this Checklist is required.**
- o Retain the completed checklist for audit along with your other working papers; **do not** return it to the Comptroller General's Office.
- o Your agency's Finance Director, Executive Director, or another reviewer should complete the Reviewer Checklist. The reviewer **must** be someone other than the preparer.
- o Each question on the Reviewer Checklist is designed so that a "No" answer indicates a potential problem. Generally, when the reviewer responds "No," he/she should return the closing package form to the preparer to be corrected and resubmitted. If you believe that a "No" answer to a particular question is unavoidable or acceptable in your unique situation, however, attach an explanation to the completed checklist and retain it with the completed checklist.
- o This checklist is not all-inclusive. It is designed only to detect the most frequent types of errors. It may not identify all possible errors.
- o Exhibit 3.15 (C) shows a sample completed Reviewer Checklist (GAAP Form 3.15.3).

STATE OF SOUTH CAROLINA
OFFICE OF THE COMPTROLLER GENERAL

GAAP CLOSING PROCEDURES MANUAL

CLAIMS CLOSING PACKAGE	REFERENCE	3.15
	ISSUE DATE	6-30-2002
	PAGE	19

EXHIBIT
3.15 (C)

STATE OF SOUTH CAROLINA
CLAIMS CLOSING PACKAGE
REVIEWER CHECKLIST
FISCAL YEAR 2002

Reviewer's Signature:	<i>I. M. Senior</i>
Date Last Review Step Was Completed:	<i>9/20/02</i>

REVIEW STEP	YES/NO
Is the reviewer of all claims closing packages someone other than the person who prepared them?	<i>Yes</i>
Did the preparer and reviewer sign the closing packages (not just type or rubber-stamp their names)?	<i>Yes</i>
Did the preparer and reviewer show their titles and telephone numbers?	<i>Yes</i>
Can all amounts reported on the Claims Summary Form (GAAP Form 3.15.1) be traced back to official agency accounting records or to working papers?	<i>Yes</i>
Do the completed closing package forms reflect implementation of all changes in closing package instructions for this year, if any, that apply to your agency?	<i>Yes</i>
Are differences between the closing package amounts reported in the current-year and those reported last year either (1) small or (2) explained (as to reasons) in working papers retained for audit purposes?	<i>Yes</i>
Have GAAP fund codes and GAAP fund names been provided when requested?	<i>Yes</i>
On the Claims Summary Form (GAAP Form 3.15.1), has the claim-paying program or type of self-insured risk been identified?	<i>Yes</i>
On the Claims Summary Form (GAAP Form 3.15.1), has the current claims liability been split between amounts to be paid in STARS FM 13 of the current fiscal year and amounts to be paid during the next fiscal year?	<i>Yes</i>
Has an Additional Claims Information Form (GAAP Form 3.15.2) been completed for each completed Claims Summary Form (GAAP Form 3.15.1)?	<i>Yes</i>