

**SOUTH CAROLINA DEPARTMENT OF COMMERCE
COLUMBIA, SOUTH CAROLINA**

FINANCIAL STATEMENTS

YEAR ENDED JUNE 30, 2004

State of South Carolina



Office of the State Auditor

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May 16, 2005

The Honorable Mark Sanford, Governor
and
Mr. Robert Faith, Secretary
South Carolina Department of Commerce
Columbia, South Carolina

This report on the audit of the financial statements of the South Carolina Department of Commerce for the fiscal year ended June 30, 2004, was issued by Rogers & Laban, PA, 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,

A handwritten signature in black ink, appearing to read "Tom Wagner".

Thomas L. Wagner, Jr., CPA
State Auditor

TLWjr/sag

SOUTH CAROLINA DEPARTMENT OF COMMERCE

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CERTIFIED PUBLIC ACCOUNTANTS AND FINANCIAL CONSULTANTS

INDEPENDENT AUDITOR'S REPORT

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

We have audited the accompanying financial statements of the governmental activities, each major fund and the aggregate remaining fund information of the South Carolina Department of Commerce (the "Department") as of and for the year ended June 30, 2004, as listed in the table of contents. These financial statements are the responsibility of the Department'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 auditing standards generally accepted in the United States of America and Government Auditing Standards, issued by the Comptroller General of the United States. 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 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.

The financial statements referred to above do not include the Department's enterprise funds, which are comprised of the Division of Public Railways and Division of Savannah Valley Development, which should be included in order to conform with accounting principles generally accepted in the United States of America. The omitted funds have assets, liabilities, revenues, and expenses as follows as of and for the years ended:

	December 31, 2003 Public Railways	June 30, 2004 Savannah Valley
Assets	\$37,288,106	\$19,945,337
Liabilities	1,158,499	15,574,899
Revenues	7,582,772	1,376,555
Expenses and Transfers	4,900,818	1,114,584

As described in Note 1 to the financial statements, the financial statements of the Department are intended to present the financial position and results of operations of only that portion of the financial reporting entity of the State of South Carolina that is attributable to the transactions of the Department, excluding its enterprise funds noted in the above paragraph. They do not purport to and do not present the financial position of the State of South Carolina as of June 30, 2004, and changes in its financial position, for the year then ended in conformity with accounting principles generally accepted in the United States of America, and do not include, other agencies, divisions or component units of the State of South Carolina.



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In our opinion, except for the effect on the financial statements of the omissions described in the third paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of the governmental fund activities, each major fund and the aggregate remaining fund information of the South Carolina Department of Commerce as of June 30, 2004, and the results of its operations for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on pages 3 through 8 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was performed for the purpose of forming an opinion on the financial statements of the Department taken as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, and is not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

In accordance with Government Auditing Standards, we have also issued our report dated March 23, 2005 on our consideration of the Department's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Governmental Auditing Standards and should be considered in assessing the results of our audit.

Rogers & Lalan, PA

March 23, 2005

SOUTH CAROLINA DEPARTMENT OF COMMERCE MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of the South Carolina Department of Commerce ("the Department"), we provide this *Management's Discussion and Analysis* of the South Carolina Department of Commerce's Financial Statements for the fiscal year ended June 30, 2004 as a narrative overview and analysis. We encourage readers to consider this information in conjunction with the Department's financial statements, which follow.

A requirement of the *Management's Discussion and Analysis* is that it should discuss the current year results in comparison with prior year, with emphasis on the current year. This fact-based analysis should discuss the positive and negative aspects of the comparison with the prior year.

This report consists of a series of financial statements, prepared in accordance with the Governmental Standards Board in Statement 34, Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments. These financial statements differ significantly, in both the form and accounting principles utilized, from prior financial statements presented.

The Financial Statements and the *Management's Discussion and Analysis* do not include the Public Railways Division or the Savannah Valley Development Division of the Department of Commerce as these activities are covered by separate audit reports.

FINANCIAL HIGHLIGHTS

Department-Wide

Net Assets – The assets of the Department exceeded its liabilities at fiscal year ending June 30, 2004 by \$60.5 million (presented as "net assets"). Of this amount there was a deficit of \$6.3 million was reported as "unrestricted net assets". Unrestricted net assets represent the amount to be used to meet the Department's ongoing obligations to citizens and creditors.

Changes in Net Assets – The Department's total net assets decreased by \$21.5 million (a 26% decrease) in fiscal year 2004. The decrease is attributed to a decrease in Water and Wastewater Grants funds received in prior year and expensed in a current year.

DEPARTMENT-WIDE FINANCIAL ANALYSIS

Net Assets

The Statement of Net Assets presents information reflecting the Department's assets, liabilities and net assets as of the end of the fiscal year. This statement provides the reader with a fiscal snapshot of the Department. The Statement of Net Assets presents

end of year data concerning Assets (current and non-current), Liabilities (current and non-current), and Net Assets (Assets minus Liabilities). Current assets and liabilities are those with immediate liquidity or which are collectible or due within twelve months of the statement date. The Statement of Net Assets is prepared under the accrual basis of accounting, whereby revenues and assets are recognized when the service is provided and expenses and liabilities are recognized when others provide the service, regardless of when cash is exchanged.

The assets of the Department exceeded its liabilities at fiscal year ending June 30, 2004 by \$60.5 million. The Department reported \$6.3 million as a deficit in unrestricted net assets.

**Condensed Statement of Net Assets
Comparison June 30, 2003 and June 30, 2004**

	June 30, 2003	June 30, 2004
ASSETS		
Current assets	\$ 18,040,930	\$ 12,954,140
Restricted cash and investments	76,865,225	56,600,613
Capital Assets, net of related depreciation	<u>6,221,339</u>	<u>4,585,959</u>
Total Assets	<u>\$101,127,494</u>	<u>\$ 74,140,712</u>
LIABILITIES		
Current liabilities	\$ 13,125,095	\$ 9,926,125
Long-term liabilities	<u>5,983,174</u>	<u>3,660,807</u>
Total liabilities	<u>\$ 19,108,269</u>	<u>\$ 13,586,932</u>
NET ASSETS		
Invested in capital assets, net of related debt	\$ 6,221,339	\$ 4,585,959
Restricted	81,708,978	62,378,590
Unrestricted (deficit)	<u>(5,911,092)</u>	<u>(6,350,769)</u>
Total net assets	<u>\$ 82,019,225</u>	<u>\$ 60,553,780</u>
Total liabilities and net assets	<u>\$101,127,494</u>	<u>\$ 74,140,712</u>

The year ended June 30, 2003 had a reported \$5.9 million deficit in unrestricted net assets with the year ended June 30, 2004 having a reported \$6.3 million deficit in unrestricted net assets. These deficits were primarily attributable to notes for Spartanburg Renaissance Project issued in prior years and other account payables and annual leave accruals.

The Department has various airport and economic development projects. The outstanding commitments for the Department as of June 30, 2004 as compared to June 30, 2003 are as follows:

Outstanding Commitments

	June 30, 2003	June 30, 2004
Water and Wastewater Infrastructure Grants	\$ 45,387,899	\$ 3,786,666
State Rural Infrastructure	2,486,955	10,719,679
Community Development Block Grants	16,637,227	14,323,842
State Economic Dev Program (Hwy Set Aside)	21,373,274	18,209,691
Capital Improvement Bond Funds	513,627	165,982
Aviation Fuel Tax (Earmarked Funds)	323,686	491,434
State Aviation Fund (State Funds)	453,563	877,627
Union County Airport (Earmarked Funds)	<u>12,757</u>	<u>0</u>
 Total Commitments	 <u>\$ 87,188,988</u>	 <u>\$ 48,574,921</u>

Statement of Activities

This statement represents the program revenues and expenses, as well as any general revenue that the agency receives. The purpose of this statement is to present the reader with information relating to revenues received and expenses incurred during the fiscal year.

Program revenues for the Department are classified in two categories; Charges for Services, Operating Grants and Contributions. Charges for services are received for providing services to the various customers and constituencies of the agency. Operating grants are primarily made up of grants from various activities that are mandated legislatively, for which there are no appropriated funds to carry out the activities.

Because many of the individual grants are for projects that take several years to complete, the timing of the expenses in any given year can greatly affect the agency's increase and decrease in net assets. This accounts for substantially all of the decrease in net assets.

General revenues are revenues received for which services are not provided. State appropriations are considered general revenue because they are provided by the State without directly receiving commensurate services. The other items of general revenue included investment income and contributions from such funds as the State Admissions Tax, State Rural Infrastructure Fund, State Aviation fund and State Economic Development Gasoline Tax made available to the agency. Total general revenue for the agency was \$33.9 million in fiscal year 2004 as compared to \$32.2 in fiscal year 2003. This is a increase of \$1.7 million, which is primarily attributable to a increase in general obligation economic development bond revenue of \$2.6 million along with a decrease in state appropriations of \$1.2 million.

Expenses for the agency are shown under the category of Economic Development and are classified as personal services; other operating costs, including grants; and interest and depreciation. Personal service costs were \$8.3 million (8.8%) for the fiscal year 2004 as compared to \$9.1 (8.4%) for fiscal year 2003. Other operating costs, including grants totaling \$84.6 (89.7%) million for fiscal year 2004 as compared to \$98.5 million (90.9%) for fiscal year 2003. Interest costs, depreciation expense and loss on disposal of capital assets totaled \$1.2 million (1.5%) for fiscal year 2004 as compared to \$.7 (.1%) million for fiscal year 2003.

**Statement of Activities
Comparison June 30, 2003 and June 30, 2004**

	June 30, 2003	June 30, 2004
Revenues:		
Program Revenues		
Charges for Services	\$ 765,691	\$ 455,753
Operating Grants and Contributions	44,355,458	38,533,214
General Revenues		
State Appropriation	12,783,206	11,548,375
State General Obligation Economic Development Bonds		2,632,894
State Capital Improvements Bond	290,836	425,368
State Economic Development Programs	19,052,730	19,269,954
Contributions and Other	41,762	
Gain on Sale of Assets and Sale of Surplus		70,090
Less Amounts Transferred to State General Fund	(611,277)	(71,488)
Total Revenues	<u>\$76,678,406</u>	<u>\$ 72,864,160</u>
Expenses:		
Economic Development	<u>\$107,969,051</u>	<u>\$ 94,329,605</u>
Increase (decrease) in Net Assets	(\$31,290,645)	(\$21,465,445)
Net Assets, Beginning of Year	<u>\$113,309,870</u>	<u>\$ 82,019,225</u>
Net Assets, End of Year	<u>\$ 82,019,225</u>	<u>\$ 60,553,780</u>

FINANCIAL ANALYSIS OF THE DEPARTMENT'S INDIVIDUAL FUNDS

Governmental Funds

The focus of the Department's governmental funds is to provide information on near-term inflows, outflows and balances of spendable resources. As of the end of the current

fiscal year, the Department's governmental funds reported ending fund balances of \$62.7 million, a decrease of \$20.5 million in comparison with the prior year. \$386,167 of these total fund balances constitutes unreserved fund balances, which are available for spending in the coming year. The remainder of the balance is reserved to indicate that it is not available for new spending because it has already been committed. The Department's fund balance in governmental funds decrease can be attributable to the 1) Water and Wastewater Infrastructure Fund expenditures exceeding the revenue by \$38.2 million, 2) State Rural Infrastructure revenue exceeding the expenditures by \$7.9 million and State Economic Development revenue exceeding the expenditures by \$9.2 million.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The Department's Capital Assets net of depreciation were \$4.5 million at June 30, 2004. This was a decrease of \$1,635,379. This decrease in Capital Assets is due to the sale and disposal of assets including the investment in a share of a Hawker Aircraft. This investment in capital assets includes aircraft and leasehold improvements, as well as computer and presentation systems.

**Capital Assets
Comparison June 30, 2003 and June 30, 2004**

	June 30, 2003	June 30, 2004
Building Improvements	\$ 4,035,982	\$ 4,035,982
Furniture, Fixtures and Equipment	1,342,648	1,357,248
Aircraft and Vehicles	<u>4,699,631</u>	<u>2,692,134</u>
Total Cost	\$10,048,261	\$ 8,085,364
Less Accumulated Depreciation	<u>3,826,922</u>	<u>3,499,405</u>
Net Capital Assets	<u>\$ 6,221,339</u>	<u>\$ 4,585,959</u>

*The Department's buildings are located on long term-leased land at Columbia Metropolitan Airport. The Department owns no land.

Debt Administration

The Department did not incur new debt during the fiscal year 2004. An unsecured note for \$3 million, with a maturity of March 1, 2003 is still being reported. This note was delayed until fiscal year 2004-2005 for payment by a proviso in the Appropriations Act for fiscal year 2003-2004. A second note of \$3.5 million is to be paid in 4 equal installments over the next four years with the first payment being made in July of Fiscal Year 2003-2004.

Economic Outlook

Downturns in the U.S. economy that began in March 2001 had a similar impact on the State of South Carolina's general fund revenue sources. As a result, the Department has undergone midyear and base budgets reductions to our State Appropriated funds. Even with these reductions during the fiscal year, the Department carried out its mission and managed these shortfalls through attrition and reduced workloads. The Department has also restructured and had a reduction in force to help attain the funding levels that we currently have. The Department has streamlined most of its processes and look for accountability in all aspects of our mission.

In Fiscal Year 2003-2004 the Department has taken a mid year reduction of 1% which is \$110,000. The Department has worked to absorb this cut as well as future cuts by restructuring. The Outlook is good for the Department as businesses are expanding and looking for a new home in South Carolina. We are at 42% of our goal in business recruitment and job creation in Calendar Year 2005 in the first four months. We believe that this is a good indicator for a good solid year at the Department.

Request for Information

This financial report is designed to provide a general overview of the Department of Commerce finances for all of the Department's taxpayers, customers and creditors. This financial report seeks to demonstrate the Department's accountability for the funds it receives. Questions concerning any of the information provided in this report or requests for additional information should be addressed to:

South Carolina Department of Commerce
Director of Administration
1201 Main Street, Suite 1600
Columbia, South Carolina 29201

SOUTH CAROLINA DEPARTMENT OF COMMERCE

STATEMENT OF NET ASSETS
JUNE 30, 2004

	Governmental Activities
ASSETS	
Current assets:	
Cash and cash equivalents	\$ 5,212,254
Accounts receivable	24,176
Intergovernmental receivables:	
Federal government	1,388,672
General Fund of the State	410,299
State agencies	5,843,695
State capital improvement bonds	41,890
Prepaid expenses	11,947
Inventories	21,207
Total current assets	12,954,140
Noncurrent assets:	
Restricted cash and cash equivalents	56,600,613
Capital assets	4,585,959
Total assets	\$ 74,140,712
 LIABILITIES AND NET ASSETS	
Liabilities:	
Current liabilities:	
Accounts payable	\$ 6,226,230
Accrued salaries and related benefits	559,446
Accrued interest payable	407,282
Deferred revenue	31,167
Current portion of notes payable	2,250,000
Current portion of accrued compensated absences and related benefits	452,000
Total current liabilities	9,926,125
Noncurrent liabilities:	
Notes payable, net of current portion	3,500,000
Accrued compensated absences and related benefits, net of current portion	160,807
Total noncurrent liabilities	3,660,807
Total liabilities	13,586,932
Net assets:	
Invested in capital assets, net of related debt	4,585,959
Restricted for:	
Water and wastewater infrastructure grants and administrative costs	7,840,970
State economic development projects	27,791,810
Admission tax projects	2,338,397
Aviation fuel tax projects	1,435,030
State rural infrastructure fund training and projects	17,564,870
State General Obligation Economic Development Bonds Act projects	842
State General Fund appropriations	2,662,295
General fund restricted purpose funds	2,684,376
Unrestricted (deficit)	(6,350,769)
Total net assets	60,553,780
Total liabilities and net assets	\$ 74,140,712

See accompanying Notes to Financial Statements.

SOUTH CAROLINA DEPARTMENT OF COMMERCE

STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2004

	Governmental Activities
Expenses:	
Economic development:	
Personal services	\$ 8,384,351
Other operating costs, including grants	84,683,468
Interest expense	372,282
Depreciation	616,521
Loss on sale of capital assets	272,983
	94,329,605
Total program expenses	94,329,605
Program revenues:	
Charges for services	455,753
Operating grants and contributions	38,533,214
	38,988,967
Net program expenses	55,340,638
General revenues:	
State appropriations	11,548,375
State General Obligation Economic Development Bond Act funds	2,632,894
State capital improvement bond revenue	425,368
State admissions tax	1,269,954
State economic development gasoline tax	18,000,000
Gain on sale of capital assets	27,625
Sale of surplus noncapitalized equipment	42,465
	33,946,681
Total general revenues	33,946,681
Transfers:	
Transfers to General Fund of the State	(8,463)
Indirect costs remitted to General Fund of the State	(63,025)
	(71,488)
Total transfers	(71,488)
Increase (decrease) in net assets	(21,465,445)
Net assets - beginning of year, as restated	82,019,225
	60,553,780
Net assets - end of year	\$ 60,553,780

See accompanying Notes to Financial Statements.

**SOUTH CAROLINA DEPARTMENT OF COMMERCE
BALANCE SHEET - GOVERNMENTAL FUNDS
JUNE 30, 2004**

ASSETS	General	Federal	Water and Wastewater Infrastructure		State Economic Development	State Rural Infrastructure	Other Governmental	Total Governmental Funds
			Infrastructure	Development				
Cash and cash equivalents	\$ 654,327		\$ 1,282,696	\$ 7,840,970	\$ 2,499,217	\$ 456,282	\$ 319,732	\$ 5,212,254
Cash and cash equivalents - restricted	5,346,671		7,840,970	27,791,810	12,299,041	3,322,121	2,077	56,600,613
Accounts receivable	22,099							24,176
Due from other State agencies	127,795						450,071	5,843,695
Due from General Fund of the State	410,299							410,299
Due from Federal government		1,388,672						1,388,672
Due from other funds	295,322							295,322
State capital improvement bonds receivable	41,890							41,890
Prepaid expenses	11,947							11,947
Inventories	21,207							21,207
Total assets	\$ 6,931,557	\$ 1,388,672	\$ 9,123,666	\$ 30,291,027	\$ 18,021,152	\$ 4,094,001	\$ 69,850,075	

LIABILITIES AND FUND EQUITY

LIABILITIES:								
Accounts payable	\$ 732,527	\$ 999,884	\$ 1,282,696	\$ 2,475,853	\$ 415,638	\$ 319,732	\$ 6,226,230	
Accrued salaries and related benefits	425,676	69,662	23,364	40,744			559,446	
Due to other funds		295,322					295,322	
Deferred revenue	7,363	23,804					31,167	
Total liabilities	1,165,566	1,388,672	1,282,696	2,499,217	456,282	319,732	7,112,165	

FUND EQUITY:

Fund balances:								
Reserved for inventories	21,207							21,207
Reserved for prepaid expenses	11,947							11,947
Reserved for restricted purpose funds carried forward	2,684,376							2,684,376
Reserved for State General Fund appropriations carried forward	2,662,295							2,662,295
Reserved for State economic development projects				27,791,810				27,791,810
Reserved for admissions tax projects						2,338,397		2,338,397
Reserved for aviation fuel tax projects						1,435,030		1,435,030
Reserved for State General Obligation Economic Development Bond Act projects						842		842
Reserved for State rural infrastructure fund training and projects					17,564,870			17,564,870
Reserved for water and wastewater infrastructure grants and administrative costs			7,840,970					7,840,970
Unreserved:								
Undesignated	386,166							386,166
Total fund equity	5,765,991		7,840,970	27,791,810	17,564,870	3,774,269	62,737,910	
Total liabilities and fund equity	\$ 6,931,557	\$ 1,388,672	\$ 9,123,666	\$ 30,291,027	\$ 18,021,152	\$ 4,094,001	\$ 69,850,075	

See accompanying Notes to Financial Statements.

SOUTH CAROLINA DEPARTMENT OF COMMERCE
BALANCE SHEET - GOVERNMENTAL FUNDS (CONTINUED)
JUNE 30, 2004

Reconciliation to the statement of net assets:

Fund balances - governmental funds		\$ 62,737,910
Amounts reported for governmental activities in the statement of net assets are different because:		
Liabilities are not due and payable in the current period, therefore, are not reported in the fund:		
Notes payable	\$ (5,750,000)	
Accrued compensated absences and related benefits	(612,807)	
Accrued interest payable	(407,282)	(6,770,089)
		<u>4,585,959</u>
Assets capitalized and depreciated in statement of net assets are charged to expenditures in the governmental fund:		
Capital assets, net of accumulated depreciation		<u>4,585,959</u>
Net assets - governmental activities		<u>\$ 60,553,780</u>

See accompanying Notes to Financial Statements.

SOUTH CAROLINA DEPARTMENT OF COMMERCE
STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCES - GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2004

	General	Federal	Water and Wastewater Infrastructure	State Economic Development	State Rural Infrastructure	Other Governmental	Total Governmental Funds
REVENUES:							
State appropriations	\$ 11,548,375						\$ 11,548,375
Gasoline and fuel taxes for State economic development				18,000,000			18,000,000
Federal grants		25,097,449					25,097,449
Allocations from other State agencies	220,000						220,000
Enterprise Zone Act fees	343,000						343,000
Admissions taxes					1,269,953		1,269,953
Aircraft rental	13,843						13,843
Sales of goods and services	127,726						127,726
Special events registration fees	167,015						167,015
Sponsorships of special events	71,250						71,250
Investment income	2,359		497,812			841	501,012
State Aviation Fund fees/taxes						651,229	651,229
Capital improvement bond revenue	425,368						425,368
State General Obligation Economic Development Bond Act funds	117,865			550,000			667,865
Miscellaneous revenue						2,632,894	2,632,894
Refunds from grantees							117,865
State Rural Infrastructure Fund job development fees					11,099,273		11,099,273
TOTAL REVENUES	13,036,801	25,097,449	497,812	18,550,000	11,099,273	4,554,917	72,836,252

EXPENDITURES:

Administration and Support:							
Office of the Secretary	837,150						837,150
Financial services	1,828,572						1,828,572
Information technology	897,460						897,460
Programs and Services:							
Appalachian Regional Commission Grant funds	16,919	17,927					34,846
Export services	1,159,743						1,159,743
Business recruitment	2,582,031						2,582,031
Marketing	550,944						550,944
Film office	324,798						324,798
Research administration	152,800						152,800
Legal services and communications	772,661						772,661
Rural and community development	582,185						582,185
Economic development set-aside administrative costs, projects and grants				9,327,459			9,327,459
Enterprise zone administrative and other costs	225,084						225,084
Community grants	429,239	25,011,231				751,440	25,440,470
Admission tax infrastructure grants							751,440
Flight operations	1,449,557						1,450,153
Recycling Market Development Advisory Council	158,075	4,670					162,745

SOUTH CAROLINA DEPARTMENT OF COMMERCE

STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCES - GOVERNMENTAL FUNDS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2004

	General	Federal	Water and Wastewater Infrastructure	State Economic Development	State Rural Infrastructure	Other Governmental	Total Governmental Funds
State Rural Infrastructure Fund training and projects			38,698,232		3,100,686		3,100,686
Water and Wastewater Infrastructure grants and administrative costs	383,477						38,698,232
Allocation to other entities for airport capital improvements							383,477
State General Obligation Economic Development Bond Act funds						2,632,894	2,632,894
Savannah Valley Authority	10,308						10,308
Special items:							
Coordinating Council for Economic Development	714,447						714,447
Union County Airport Improvements	12,757						12,757
State Aviation Fund airport improvement projects and grants	122,394				639,090		761,484
Hartsville Airport	9,000						9,000
Debt service:							
Principal	750,000						750,000
TOTAL EXPENDITURES	13,969,601	25,034,424	38,698,232	9,327,459	3,100,686	4,023,424	94,153,826
EXCESS OF REVENUES OVER (UNDER) EXPENDITURES	(932,800)	63,025	(38,200,420)	9,222,541	7,998,587	531,493	(21,317,574)
OTHER FINANCING SOURCES (USES):							
Transfers between funds	(75,699)			(13,803)		89,502	-
Remitted to the General Fund of the State	(8,463)						(8,463)
Proceeds from sale of capital assets	959,912						959,912
Indirect cost recovery remitted to General Fund of the State		(63,025)					(63,025)
TOTAL OTHER FINANCING SOURCES (USES)	875,750	(63,025)	-	(13,803)	-	89,502	888,424
EXCESS OF REVENUES AND OTHER FINANCING SOURCES OVER (UNDER) EXPENDITURES AND OTHER FINANCING SOURCES (USES)	(57,050)	-	(38,200,420)	9,208,738	7,998,587	620,995	(20,429,150)
FUND BALANCES - BEGINNING OF YEAR	5,823,041	-	46,041,390	18,583,072	9,566,283	3,153,274	83,167,060
FUND BALANCES - END OF YEAR	\$ 5,765,991	\$ -	\$ 7,840,970	\$ 27,791,810	\$ 17,564,870	\$ 3,774,269	\$ 62,737,910

See accompanying Notes to Financial Statements.

SOUTH CAROLINA DEPARTMENT OF COMMERCE

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCE - GOVERNMENTAL FUNDS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2004

RECONCILIATION TO THE STATEMENT OF ACTIVITIES:

Revenues and other financing sources over (under) expenditures and other financing uses for the governmental funds	\$ (20,429,150)
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Amounts reported in the statement of revenues, expenditures and changes in fund balances - governmental funds are different from those reported in the statement of activities for the following reasons:

Increases in accrued interest payable are reported as an expense in the statement of activities	(372,282)
Purchases of capital assets are treated as an expenditure in the governmental funds and as an increase in assets in the statement of net assets	186,411
Depreciation of capital assets is reported as an expense in the statement of activities	(616,521)
Repayments of notes payable are reported as expenditures in the governmental funds and as a reduction of liabilities in the statement of net assets	750,000
Decrease in accrued compensated absences is reported as a decrease of expense in the statement of activities	221,367
Proceeds from the sales of capital assets are reported as revenues in the governmental funds but as part of the loss on sales of assets on the statement of activities	(959,912)
Gains on sales of capital assets are reported as general revenue in the statement of activities	27,625
Losses on disposals of capital assets are reported as an expense in the statement of activities	<u>(272,983)</u>

INCREASE (DECREASE) IN NET ASSETS	<u>\$ (21,465,445)</u>
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See accompanying Notes to Financial Statements.

SOUTH CAROLINA DEPARTMENT OF COMMERCE

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2004**

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

The financial statements of South Carolina Department of Commerce (the Department) were prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to governmental entities. The Government Accounting Standards Board (GASB) is the accepted standard-setting body in the United States of America for establishing governmental accounting and financial reporting principles. The more significant of the Department's accounting policies are described below.

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 of its component units. Component units are legally separate organizations for which the elected officials of 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 government/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 government/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 government/entity. The primary government/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 independent if it holds all three of the following powers:

1. Determines its budget without another government's having the authority to approve and modify that budget.
2. Levies taxes or set rates or charges without approval by another government.
3. Issues bonded debt without approval by another government.

Otherwise, the organization is fiscally dependent on the primary government/entity that holds one or more of these powers.

The Department is responsible for the stimulation of economic development activity, management of business affairs of the Division of Savannah Valley Development, development of public airports and air transportation systems, and development of public railways systems. The Department is an agency of the State of South Carolina established by Section 1-30-10 and 1-30-25 of the Code of Laws of South Carolina.

The Department was created by the Government Restructuring Act of 1993 which became effective on July 1, 1993. The Governor appoints the director of this cabinet level department. The agency consists of a combination of the former agencies of the State Development Board, Aeronautics Commission, Coordinating Council for Economic Development (Coordinating Council), Savannah Valley Authority, and the South Carolina Public Railways Commission. Management has elected to exclude its enterprise funds, the Division of Public Railways and the Division of Savannah Valley Development from this reporting entity. Separate audited financial statements are available for each of the excluded divisions. The funds and account groups of the Department, including the two divisions excluded from this report, are included in the Comprehensive Annual Financial Report of the State of South Carolina, the primary government. Copies of the reports for the two excluded divisions can be obtained from the Department at P.O. Box 927, Columbia, South Carolina, 29202.

SOUTH CAROLINA DEPARTMENT OF COMMERCE

NOTES TO FINANCIAL STATEMENTS JUNE 30, 2004

The accompanying financial statements present the financial position and results of operations and note disclosures of only those transactions of the State of South Carolina that are attributable to the Department reporting entity defined above.

Governmental Funds

Governmental funds are those through which most governmental functions typically are financed and used to account for the government's general government activities including the collection and disbursement of earmarked funds. Expendable assets are assigned to the various governmental funds according to the purposes for which they may or must be used; current liabilities are assigned to the fund from which they are to be paid; and the differences between the assets and liabilities is the fund balance.

The Department reports the following major funds:

The general fund accounts for all activities except those required to be accounted for in another fund. Major revenue sources include the annual state appropriation as approved by the General Assembly, donations and contributions for special marketing events, State Capital Improvement Bond proceeds for grants to municipalities for airport improvements, allocations from other State agencies, and charges for goods and services. The revenues are used for general ongoing governmental services such as administration, maintenance, aeronautics and economic program development and service. Also included are operating transfers from the special revenue fund for Coordinating Council administrative costs and expenditures and for the South Carolina Infrastructure – Economic Development Planning Project expenditures. The general fund also includes application fees not to exceed \$2,000 from qualifying businesses applying for the tax incentives allowed under the Enterprise Zone Act of 1995. The application fees collected by the Coordinating Council must be expended for administrative, data collection, credit analysis, cost/benefits analysis, reporting and any other obligations pursuant to the Act. The Act allows for the carryforward of unexpended funds collected under the Act to the next fiscal year to be expended for the same purpose.

Federal funds consist primarily of Community Development Block Grant funds and are used primarily for water and sewage infrastructure grants and community housing grants.

The Water and Wastewater Infrastructure Fund was established by an act of the legislature in the fiscal year ended June 30, 2001. The fund received a portion of the proceeds (approximately \$78,000,000) from bonds that were sold by the South Carolina Tobacco Settlement Revenue Management Authority. The Department is not required to repay these funds. These funds along with any investment earnings are used to make grants to governmental units and private entities for constructing and improving water and wastewater facilities that are necessary for public purposes, including economic development and for technology related infrastructure grants for local units of government. The Department charged each applicant 2% of the grants awarded to be used for administrative expenses of operating the program.

The State Economic Development account established by South Carolina Code of Law Section 12-28-2910. This account accumulates the first \$18 million generated from the tax levied in Section 12-28-310. The proceeds are to be used for economic development projects approved through the Coordinating Council. The Coordinating Council establishes project priorities and authorizes all project expenditures. The economic development set-aside expenditures are primarily expended for infrastructure grants for roads when needed to complete negotiations with an economic development prospect.

SOUTH CAROLINA DEPARTMENT OF COMMERCE

NOTES TO FINANCIAL STATEMENTS JUNE 30, 2004

The State Rural Infrastructure Fund was authorized by Section 12-10-85 to provide financial assistance to local government for training cost and facilities; improvements to regionally planned public and private water and sewer systems; improvements to both public and private electricity, natural gas, and telecommunications systems; and fixed transportation facilities. These funds are received from the South Carolina Department of Revenue and represent funds collect pursuant to SC Code 12-10-80.

Other non-major governmental funds include admissions tax revenue authorized by Section 12-21-6510. Section 12-21-6540 provides that amount equal to one-fourth of the license tax on admissions to major tourism facilities collected by the Department of Revenue is remitted to the Department. The Coordinating Council approves expenditures of these funds specifically for infrastructure development grants. Other governmental funds also include the Aviation Fuel tax authorized by Section 55-5-280 which provides for "all monies received from the licensing of airports, landing fields and air schools, the tax on aviation gasoline and fees and other licenses under this chapter to be credited to the "State Aviation Fund" to be used for airport improvements and job development fees paid by various companies received by the Department. Also included in other governmental funds is funds available from the State General Obligation Economic Development Bond Act authorized by Chapter 41 of the South Carolina Code of Laws. These funds are received by the Department from the State of South Carolina from the sale of general obligation bonds to fund infrastructure for economic development within the State.

Government-wide and Fund Financial Statements

The financial statements of the Department are presented in accordance with accounting principles generally accepted in the United States of America applicable to state and local governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body in the United States of America for establishing governmental accounting and financial reporting principles.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenues include 1) charges to customers or applicants who purchase, use or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Other items not properly included among program revenues are reported instead as general revenues.

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis method of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis method of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Department considers revenues to be available if they are collected within one year of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting.

SOUTH CAROLINA DEPARTMENT OF COMMERCE

NOTES TO FINANCIAL STATEMENTS JUNE 30, 2004

Revenues – Exchange and Non-Exchange Transactions

Revenue resulting from exchange transactions, in which each party gives and receives essentially equal value, is recorded on the accrual basis when the exchange takes place. On a modified accrual basis, revenues are recorded in the fiscal year in which the resources are measurable and become available. Available means that the resources will be collected within the current fiscal year or are expected to be collected soon enough thereafter to be used to pay liabilities of the current fiscal year. For the Department, available means expected to be received within one year of the fiscal year-end.

Nonexchange transactions, in which the Department receives value without directly giving value in return, include grants and donations. On an accrual basis, revenue from grants and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied. Eligibility requirements include timing requirements, which specify the year when the resources are required to be used or the fiscal year when use is first permitted, matching requirements, in which the Department must provide local resources to be used for a specific purpose, and expenditure requirements, in which the resources are provided to the Commission on a reimbursement basis. On a modified accrual basis, revenue from nonexchange transactions must be available before it can be recognized.

Capital Assets

Capital assets are recorded at cost at the date of acquisition or fair market value at the date of donation in the case of gifts. The Department follows capitalization guidelines established by the State of South Carolina. All land is capitalized, regardless of cost. Qualifying improvements that rest in or on the land itself are recorded as depreciable land improvements. Major additions and renovations and other improvements costing \$100,000 or more that add to the usable space, prepare existing buildings for new uses, or extend the useful life of an existing building are capitalized. The Department capitalized movable personal property with a unit value in excess of \$5,000 and a useful life in excess of one year and buildings and improvements and intangible assets costing in excess of \$100,000. Routine repairs and maintenance and library materials are charged to operating expenses in the year in which the expense was incurred.

Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally 15 to 50 years for buildings and improvements and land improvements and 2 to 25 years for machinery, equipment, and vehicles.

Budget Policy

The Department is granted an annual appropriation for operating purposes by the General Assembly. The appropriation as enacted becomes the legal operating budget for the Department. The Appropriation Act authorizes expenditures from funds appropriated from the General Fund of the State and authorizes expenditures of total funds. The Total Funds column in the Appropriation Act for each individual budgetary unit authorizes expenditures from all budgeted resources. A revenue budget is not adopted for individual budgetary units. The General Assembly enacts the budget through passage of line-item appropriations by program within budgetary unit within budgetary fund category, State General Fund or other budgeted funds. Budgetary control is maintained at the line-item level of the budgetary entity. Agencies may process disbursement vouchers in the State's budgetary accounting system only if enough cash and appropriation authorization exist.

A budget versus actual comparison is not presented as required supplementary information for any of the funds since not all revenues or expenditures are legally budgeted in any of the funds.

SOUTH CAROLINA DEPARTMENT OF COMMERCE

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2004**

Cash and cash equivalents with State Treasurer

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

Most State agencies including the Department participate in the State's internal cash management pool. The State Treasurer administers the cash management pool. 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. For credit risk information pertinent to the cash management pool, see the deposits disclosure in Note 3.

The State's internal cash management pool consists of a general deposit account and several special deposit accounts. The State records each fund's equity interest in the general deposit account; however, all earnings on that account are credited to the General Fund of the State. The Department records and reports its deposits in the general deposit account at cost and reports its deposits in the special deposit accounts at fair value. Investments held by the pool are recorded at fair value. Interest earned by the Department's special deposit accounts is posted to the Department's account at the end of each month and is retained. Interest earnings are allocated based on the percentage of the Department's accumulated daily interest receivable to the total income receivable of the pool. Reported interest income includes interest earnings at the stated interest rate, realized gains/losses and unrealized gains/losses arising from changes in the fair value of investments in the pool. Realized gains and losses are allocated daily and are included in the accumulated income receivable. Unrealized gains and losses are allocated at year-end based on the percentage ownership in the pool.

Compensated Absences

State 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 State 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. The compensated absences liability includes accrued annual leave and compensatory holiday leave earned for which the employees are entitled to paid time off or payment at termination. In the governmental funds, expenditures for compensated absences are recorded when payment is made. Since no funds are budgeted for compensated absences in excess of the actual amount incurred during the year, no additional expenditures are accrued as a current liability of the governmental funds. The Department calculates the gross compensated absence liability based on recorded balances of unused leave. The entire unpaid liability, inventoried at current fiscal year-end salary costs and the cost of the salary related benefit payments, is recorded as a liability in the statement of net assets.

Indirect Cost Recoveries

The receipt of indirect cost recoveries on government-sponsored programs have been included in the special revenue fund as federal grants revenue and payments of certain of these recoveries to the State's General Fund have been recorded as other financing uses. State law requires the Department to remit to the General Fund of the State recoveries from federal grants and awards whose annual award is in excess of \$200,000. The Department retains and expends other recoveries.

SOUTH CAROLINA DEPARTMENT OF COMMERCE

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2004**

Net Assets / Fund Balances

The Department records reservations for portions of its fund equity which are legally segregated for specific future uses or which do not represent available expendable resources and therefore, are not available for expenditures in the governmental fund balance sheet. Unreserved fund balance indicates that portion of fund equity, which is available for appropriations, in future periods. If restricted and unrestricted assets are available for the same purpose, then restricted assets will be used before unrestricted assets.

Net assets are categorized as follows:

Invested in capital assets, net of related debt: This represents the Fund's total investment in capital assets, net of outstanding debt obligations, if any, related to those capital assets. To the extent debt has been incurred but not yet expended for capital assets, such amounts are not included as a component of invested in capital assets, net of related debt.

Restricted: Consists of assets with constraints placed on the use either by (1) external groups such as creditors, grantors, contributions, or laws or regulations of other governments; or (2) law through constitutional provisions or enabling legislation.

Unrestricted net assets: Consists of the remainder of the Department's assets in excess of liabilities excluding those net assets reported in other categories.

When both restricted and unrestricted resources are available for use, it is the Department's policy to use restricted resources first, then unrestricted resources as they are needed.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

NOTE 2. STATE APPROPRIATION:

The following represents a reconciliation of the Appropriation Act for the period ended June 30, 2004 as originally enacted by the General Assembly to appropriation revenue as reported in the general fund.

Original appropriation	\$ 11,818,206
Allocations by State Budget & Control Board for State budget mid-year reductions	<u>(110,682)</u>
Adjusted Appropriation, Budgetary Basis	11,707,524
Accrual adjustments:	
Funding for personal services and employer contributions	<u>(159,149)</u>
Accrual basis State appropriation revenue	<u>\$ 11,548,375</u>

SOUTH CAROLINA DEPARTMENT OF COMMERCE

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2004**

The Coordinating Council receives State General Fund appropriations for special purposes only. These appropriations do not cover operating costs. The Department allocates funds from its State appropriation to cover operating cost associated with management of these special purpose State General Fund appropriations.

The amount of the 2000 Capital Reserve Fund appropriation brought forward to fiscal year 2004 was \$48,476. \$12,757 of this amount was carried forward to fiscal year pursuant to the August 1999 Joint Resolution R201, H3697.

The amount of State funds brought forward to fiscal year 2004 was \$3,043,496. The Department brought forward to fiscal year 2004 \$9,000 for county airport improvements at Hartsville Airport and \$2,499,115 for allocation to the Coordinating Council for economic development as allowed by part VI of the 1997 Appropriations Act. In addition, \$535,351 of funds appropriated for Aviation grants was brought forward pursuant to Proviso 27.13 of the 2004 Appropriations Act.

The amount of State General Fund appropriations to be carried over to fiscal year 2005 is \$2,662,295. This carry forward is reported as reserved fund balance. The Department carried forward to fiscal year 2005 \$1,784,668 allocated to the Coordinating Council for economic development was carried forward as allowed by Part VI of the 1997 Appropriations Act. In addition, \$877,627 of funds appropriated for Aviation grants was carried forward pursuant to Proviso 27.13 of the 2005 Appropriations Act.

Proviso 72.30 of the 2004- Appropriations Act authorizes the Department to carry forward unspent fiscal year 2004 appropriations up to a maximum 10% of the original appropriation less any reduction to the 2004 fiscal year excluding amounts carried forward under separate carry forward authority. Unspent fiscal year 2004 appropriations amounted to \$16,916 as of June 30, 2004 that was carried over to fiscal year 2005.

NOTE 3. DEPOSITS AND INVESTMENTS:

Cash and cash equivalents consist of deposits under the control of the State Treasurer, who by law, has sole Fund for investing State funds and deposits under the control of the Department Fund. However, as authorized by the State Treasurer's office, certain funds for foreign office operation are invested and deposited with foreign financial institutions.

The following schedule reconciles deposits within the footnotes to the financial statement amounts:

Financial Statements		Footnotes	
Cash and cash equivalents	\$ 61,812,867	Deposits Held by State Treasurer	\$ 61,746,950
		Other Deposits	65,617
		Petty Cash	300
	\$ 61,812,867		\$ 61,812,867

The account classified as "Cash on deposit with the State Treasurer" in the financial statements consists of amounts in the general and special deposits accounts with the State Treasurer as part of the State's internal cash management pool. The special deposits are in a composite account that draws interest. The account classified as cash on hand consists of cash used for petty cash and change fund purposes. Cash held in foreign accounts consists of cash held by foreign banks for the Tokyo, Japan; Hong Kong; and Munich, Germany offices.

Deposits

State law requires full collateralization of all State Treasurer bank balances. The State Treasurer must correct any deficiencies in collateral within seven days

SOUTH CAROLINA DEPARTMENT OF COMMERCE

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2004**

With respect to investments in the State's internal 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 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.

The Entity's deposits which are not with the State Treasurer are categorized to indicate the level of risk assumed by the entity at year-end. The credit risk categories are concerned with custodial credit risk, which is the risk that a government will not be able to recover deposits if the depository financial institution fails or to recover the value of collateral securities that are in the possession of an outside party if the counterparty to the deposit transaction fails. Category 1 includes deposits insured or collateralized with securities held by the entity/entities. Category 2 includes deposits collateralized with securities held by the pledging financial institution trust department or agent in the entity's name. Category 3 includes uncollateralized deposits, including any bank balance that is collateralized with securities held by the pledging financial institution, or by its trust department or agent, but not in the entity's name.

All of the deposits with foreign banks are in Category 3 and the carrying amount and bank balance was \$65,617 as of June 30, 2004. The highest balance of deposits in Category 3 during the year was approximately \$335,000.

Investments

Legally authorized investments include obligations of the United States, obligations of the State of South Carolina and other states and certain of their political subdivisions, certificates of deposit, collateralized repurchase agreements, certain corporate bonds, and commercial paper.

All of the Department's investments are stated at fair value except those meeting certain specific requirements. Purchases and sales are accounted for on the trade date. Unrealized gains and losses on investments have been recorded. Realized gains and losses on securities transactions are recorded on the accrual basis. Earnings are recorded on the accrual basis.

The Department did not own any investments as of June 30, 2004. Investments held during the year consisted of state and local obligations.

NOTE 4. INVENTORIES:

The Department's Aeronautics Division had inventories at June 30, 2004 of \$21,207. The inventories consisted of jet and automotive fuels and are accounted for at the lower of cost or market on a first-in, first-out basis.

NOTE 5. STATE CAPITAL IMPROVEMENT BOND PROCEEDS:

In prior years, the State of South Carolina authorized funds for improvements and expansion of municipal airport facilities and various other projects within the State using the proceeds of state capital improvement bonds. As capital projects are authorized by the State Budget and Control Board, the bond proceeds are allocated to the municipal entity. The Department records the proceeds as revenue when the expenses/expenditures are incurred. These funds represent a type of pass-through grant to municipal entities, and are reported as allocations to other entities for airport capital improvements and special items. These authorized funds can be requested as needed once State authorities have given approval to begin specific projects. The Department is not obligated to repay state capital improvement bonds.

SOUTH CAROLINA DEPARTMENT OF COMMERCE

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2004**

A summary of the balances available from these authorizations as of June 30, 2004 follows:

Act	Total Authorized	Balance Undrawn June 31, 2004
R256 of 1991	\$ 3,861,687	\$ 3,628
111 of 1997	3,000,000	162,355
Totals	\$ 6,861,687	\$ 165,983

NOTE 6. CAPITAL ASSETS:

The following schedule summarizes capital assets activity for the Department for the fiscal year 2004:

	Beginning Balances June 30, 2003	Increases	Decreases	Ending Balances June 30, 2004
Capital assets:				
Buildings and improvements	\$ 4,035,982	\$ -	\$ -	\$ 4,035,982
Equipment and furniture	1,342,648	160,550	(145,950)	1,357,248
Vehicles	4,669,631	25,861	(2,003,358)	2,692,134
Total capital assets	10,048,261	186,411	(2,149,308)	8,085,364
Less accumulated depreciation for:				
Buildings and improvements	1,749,214	196,500		1,945,714
Equipment and furniture	782,522	154,195	(137,024)	799,693
Vehicles	1,295,186	265,826	(807,014)	753,998
Total accumulated depreciation	3,826,922	616,521	(944,038)	3,499,405
Total capital assets, net	\$ 6,221,339	\$ (430,110)	\$ (1,205,270)	\$ 4,585,959

NOTE 7. DUE FROM THE GENERAL FUND OF THE STATE:

The amount receivable represents funds due from the State General Fund for personal services and employer contributions of the Department consisting of salaries and the cost of related employee benefits funded by State appropriations accrued at June 30 but paid in July. By State law, these accruals are paid from funds appropriated for the next fiscal year.

NOTE 8. NOTES PAYABLE:

On March 1, 2002, the Department borrowed \$3,500,000 from the South Carolina State Budget and Control Board to be repaid on March 1, 2004 with simple interest at 3% per annum. These funds were utilized to fund \$3,500,000 grant for the Spartanburg Renaissance project. All revenue and funds of the Department are pledged to secure this loan. On July 1, 2002, the Department borrowed an additional \$3,000,000 from the South Carolina State Budget and Control Board for the same purpose, to be repaid on July 2, 2004 with interest at 3% per annum. The Department paid \$750,000 of principal on the \$3,000,000 note during the year and paid off the remaining balance of \$2,250,000 plus \$157,000 interest in August, 2004. A new repayment plan has been entered into on the \$3,500,000 loan requiring annual payments of \$750,000 including interest at 3% beginning in fiscal year 2006.

Total interest expense on the notes payable during the fiscal year was \$372,282.

SOUTH CAROLINA DEPARTMENT OF COMMERCE

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2004**

Details of annual debt service as of June 30, 2004, including interest, for each year are as follows:

Year ending June 30	Principal	Interest	Totals
2005	\$ 2,250,000	\$ 157,000	\$ 2,407,000
2006	358,239	391,761	750,000
2007	655,747	94,253	750,000
2008	675,420	74,580	750,000
2009	695,682	54,318	750,000
2010 and 2011	1,114,912	45,398	1,160,310
Total debt service obligations	\$ 5,750,000	\$ 817,310	\$ 6,567,310

NOTE 9. LONG-TERM LIABILITIES:

Long-term liability activity for the year ended June 30, 2004 was as follows:

	Balance, July 1, 2003	Additions	Reductions	Balance, June 30, 2004	Due Within One Year
Notes payable	\$ 6,500,000		\$ 750,000	\$ 5,750,000	\$ 2,250,000
Accrued compensated absences and related benefits	834,174	230,420	451,787	612,807	452,000
	<u>\$ 7,334,174</u>	<u>\$ 230,420</u>	<u>\$ 1,201,787</u>	<u>\$ 6,362,807</u>	<u>\$ 2,702,000</u>

NOTE 10. LEASE OBLIGATIONS:

OPERATING LEASES

The Department has entered into operating leases for non-state owned land, office space and some office equipment with external parties. All of the leases are non-cancelable leases with no purchase options and their terms are greater than one year. Payments are due on a monthly basis. Ending payment dates range from fiscal years from 2005 through 2029. Certain operating leases provide for renewal options for periods from one to five years at their fair rental value at the time of renewal. In the normal course of business, operating leases are generally renewed or replaced by other leases.

Rental expenditures for all operating leases aggregated approximately \$1,423,000 for the year ended June 30, 2004. The following is a schedule by fiscal year of future minimum rental payments at June 30, 2004 required under the noncancellable operating lease agreements.

Year	Amount
2005	\$ 584,113
2006	584,113
2007	584,094
2008	562,814
2009	560,477
2010-2014	287,204
2015-2019	287,204
2020-2024	287,204
2025-2029	244,123
Total	\$3,981,346

The Department paid the State Budget and Control Board approximately \$74,000 for vehicle rentals on year to year leases. These leases are generally renewed each year.

SOUTH CAROLINA DEPARTMENT OF COMMERCE

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2004**

NOTE 11. FUND BALANCE RESERVATIONS:

In addition to the General Fund reservations for restricted purpose State General Fund appropriations carried forward and disclosed in Note 2, other fund balance reservations in the general fund were for restricted purposes and equaled \$2,684,376 at fiscal year end 2004. Included in this amount are the following: \$200,765 carried forward for administrative, data collection, credit analysis, cost-benefit analysis and reporting expenditures under the enabling act for the enterprise zones; \$1,439,737 of proceeds from aircraft sales carried over to be used for purchase of replacement aircraft under Proviso 27.12 of the 2004 Appropriation Act; \$105,873 from the South Carolina Department of Health and Environmental Control to fund the activities of the Recycling Market Development Advisory Council and \$643,241 for the Coordinating councils administrative costs; and \$294,760 for other legally and contractually required purposes.

NOTE 12. TRANSACTIONS WITH STATE AGENCIES:

The Department has significant transactions with the State of South Carolina and various State agencies.

The Department remitted indirect cost recoveries received under various grants to the State General Fund. In addition, the Department remitted \$6,000 of hanger rental income pursuant to Proviso 27.8 of the 2004 Appropriations Act. Also, \$1,743 was refunded for a prior period expenditure and \$720 of miscellaneous revenues were remitted to the State.

Services received at no cost from State agencies include maintenance of certain accounting records and payroll and disbursement processing from the Comptroller General; check preparation and banking from the State Treasurer and legal services from the Attorney General; collection of highway taxes levied under South Carolina Code of Laws Section 12-28-2910 by the Department of Revenue; and records storage from the Department of Archives and History. Other services received at no cost from the various divisions of the State Budget and Control Board include retirement plan administration, insurance plan administration, procurement services, audit services, grant services, personnel management, assistance in the preparation of the State Budget, property management and record keeping review and approval of certain budget amendments and other centralized functions.

The Department had financial transactions with various State agencies during the fiscal year. Significant payments were made to divisions of the State Budget and Control Board for retirement and insurance plan contributions, vehicle rental, insurance coverage, office supplies, printing, telephone, and interagency mail. Significant payments were also made during the year to the State Accident Fund and the Employment Security Commission for workers compensation and unemployment insurance coverage, respectively.

The Department provided no material services free of charge to other State agencies during the fiscal year. Services provided for a fee include air transportation and sale of fuel and supplies. Revenues from other State agencies are recognized when goods or services are provided by the Department. Revenues from other State agencies are included in the "Aircraft rental" and "Sale of goods and services" revenue accounts. Significant revenues derived from other State agencies amounted to approximately \$66,000.

The Department received rental income of \$47,000 from the South Carolina Office of the Adjutant General for use of space at the Aeronautics Division during the year.

SOUTH CAROLINA DEPARTMENT OF COMMERCE

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2004**

State agency members of the Coordinating Council for Economic Development voted not to assess dues to its members beginning with the fiscal year ended June 30, 1995. The Council determined that it would be satisfactorily funded with "highway taxes for State Economic Development". The Coordinating Council for Economic Development administers and has responsibility for the State Economic Development account. The member agencies of the Council are the Department of Agriculture, the State Ports Authority, the Department of Revenue, the Department of Commerce – State Division of Development, the Department of Parks, Recreation and Tourism, Santee Cooper, the Jobs-Economic Development Authority, the State Board of Technical and Comprehensive Education, the State Budget and Control Board – Office of Research and Statistical Services, and the Employment Security Commission.

Pursuant to Sections 12-10-80 and 12-10-85 of the South Carolina Code of Laws, the Department received \$11,099,273 in job development fees from the State Department of Revenue to be retained in the State Rural Infrastructure Fund which included \$5,265,829 due to the Department from the State Department of Revenue as of June 30, 2004. The State Department of Revenue also collects and remits to the Department admissions, gasoline and aviation fuel taxes. The Department received \$1,269,954 and \$18,000,000 in admissions and gasoline taxes; respectively. \$450,071 of the \$1,269,954 was due from the Department of Revenue as of June 30, 2004. The Coordinating Council approves expenditures of these funds specifically for infrastructure development grants. The Department received \$651,229 in aviation fuel tax to be spent on airport improvements as directed by the Department's Aeronautics division.

The Department received the following allocations from other state agencies during the current year:

<u>Agency Transferred from</u>	<u>Purpose</u>	<u>Amount</u>
Department of Health and Environmental Control	Recycling Program	\$ 150,000
Department of Parks, Recreation and Tourism	Marketing	\$ 70,000

NOTE 13. PENSION PLAN:

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 Department are covered by a retirement 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 the SCRS, employees are eligible for a full service retirement annuity upon reaching age 65 or completion of 28 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 of service and qualify for a survivor's benefit upon completion of 15 years credited service (five years effective, January 1, 2001).

SOUTH CAROLINA DEPARTMENT OF COMMERCE

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2004**

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.

Effective January 1, 2001, Section 9-1-2210 of the South Carolina Code of laws allows employees eligible for service retirement to participate in the Teacher and Employee Retention Incentive (TERI) Program. TERI participants may retire and begin accumulating retirement benefits on a deferred basis without terminating employment for up to five years. Upon termination of employment or at the end of the TERI period, whichever is earlier, participants will begin receiving monthly service retirement benefits which will include any cost of living adjustments granted during the TERI period. Because participants are considered retired during the TERI period, they do not make SCRS contributions, do not earn service credit, and are ineligible to receive group life insurance benefits or disability retirement benefits.

Since July 1, 1988, employees participating in the SCRS have been required to contribute 6 percent of all compensation. Effective July 1, 2003 the employer contribution rate became 10.85 percent which included a 3.30 percent surcharge to fund retiree health and dental insurance coverage. The Department's actual contributions to the SCRS for the most recent fiscal years ended June 30, 2004, 2003 and 2002 were approximately \$661,000, \$526,000 and \$585,000, respectively, and equaled the required contributions of 7.55% (excluding the surcharge) for each year. Also, the Department paid employer group life insurance contributions of approximately \$9,100 for the current fiscal year at the rate of .15% of compensation. In connection with a reduction in force, the Department purchased additional years of service with the retirement system at a total costs of approximately \$672,000.

The amounts paid by the Department for pension and group-life benefits are expenditures reported as employer contribution within the applicable program.

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, benefit and employer/employee contributions for each retirement system. 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 twelve consecutive quarters of compensation).

The Systems do not make separate measurements of assets and pension benefit obligations for individual employers. Under Title 9 of the South Carolina Code of Laws, the Department's liability under the plan is limited to the amount of contributions (stated as a percentage of covered payroll) established by the State Budget and Control Board. Therefore, the Department's liability under the pension plan is limited to the contribution requirements for the applicable year from amounts appropriated therefore in the South Carolina Appropriation Act and amounts from other applicable revenue sources. Accordingly, the fund recognizes no contingent liability for unfunded costs associated with participation in the plan. At retirement, employees participating in SCRS may receive additional service credit (at a rate of 20 days equal to one month of service) for up to 90 days for accumulated unused sick leave.

Certain State employees may elect to participate in the Optional Retirement Program (ORP), a defined contribution plan. The ORP was established in 1987 under Title 9, Chapter 17, of the South Carolina Code of Laws. The ORP provides retirement and death benefits through the purchase of individual fixed or variable annuity contracts that are issued to, and become the property of, the participants. The State assumes no liability for this plan other than for payment of contributions to designated insurance companies.

To elect participation in the ORP, eligible employees must irrevocably waive SCRS membership within their first ninety days of employment.

SOUTH CAROLINA DEPARTMENT OF COMMERCE

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2004**

Under State law, contributions to the ORP are required at the same rates as for the SCRS, 7.55 percent plus the retiree surcharge of 3.30 percent from the employer in fiscal year 2004.

Certain of the Department's employees have elected to be covered under optional retirement plans. For the fiscal year, total contributions requirements to the ORP were approximately \$21,800 (excluding the surcharge) from the Commission as employer and approximately \$17,300 from its employees as plan members. 5.7 percent of the total contributions were remitted to the Retirement Division of the State Budget and Control Board. Also, the Commission paid employer group life insurance contributions of approximately \$430 in the current fiscal year at the rate of .15 percent of compensation. The balance was remitted directly to the respective annuity policy providers. The obligation for payment of benefits resides with the insurance companies.

NOTE 14. POST-EMPLOYMENT AND OTHER EMPLOYEE BENEFITS:

In accordance with the South Carolina Code of Laws and the Annual Appropriations Act, the State of South Carolina provides certain health care, dental, and life insurance benefits to certain active and retired State employees and certain surviving dependents of retirees. All permanent full-time employees and certain permanent part-time employees of the Department 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 requirements, 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 annual appropriations by the General Assembly to the Department for its active employees and to the State Budget & Control Board for all participating State retirees, except the portion funded through the pension surcharge, and provided from other applicable fund sources of the Department 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. Approximately 26,400 State retirees met these eligibility requirements as of June 30, 2004.

The Department recorded employer contribution expenditures applicable to these insurance benefits for active employees in the amount of approximately \$362,000 for active employees for the year ended June 30, 2004. As discussed in Note 13, the Department paid approximately \$211,000 applicable to the 3.30% 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 the Department retirees is not available. By State law, the Department 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 South Carolina 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 South Carolina General Fund annually.

NOTE 15. DEFERRED COMPENSATION PLANS:

Several optional deferred compensation plans are available to State employees and employers of its political subdivisions. Certain employees of the Department have elected to participate. The multiple-employer plans, created under Internal Revenue Code Section 457, 401(k), and 403(b), are administered by third parties and are not included in the Comprehensive Annual Financial Report of the State of South Carolina. Compensation deferred under the plans is placed in trust for the contributing employee.

SOUTH CAROLINA DEPARTMENT OF COMMERCE

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2004**

The State has no liability for losses under the plans. Employees may withdraw the current value of their contributions when they terminate State employment. Employees may also withdraw contributions prior to termination if they meet requirements specified by the applicable plan.

NOTE 16. RISK MANAGEMENT:

The Department is exposed to various risks of loss and maintains State or commercial insurance coverage for each of those risks. Management believes such coverage is sufficient to preclude any significant uninsured losses for the covered risks. There were no significant reductions in insurance coverage from coverage in the prior year except that the Department did not renew their fidelity bond coverage when it expired in October 2003. Settled claims have not exceeded this coverage in any of the past three years. The Department 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 economic losses sustained during the policy period in accord with insurance policy and benefit program limits except for the deductibles.

State management believes it is more economical to manage certain risks internally and to 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 State employees for unemployment compensation benefits (Employment Security Commission);
2. Claims of covered employees for workers' compensation benefits for job-related illnesses or injuries (State Accident Fund);
3. Claims of covered public employees for health and dental insurance benefits (Office of Insurance Services); and
4. 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 State's self-insured plan. All of the other coverages listed above are through the applicable State self-insurance plan except dependent and optional life premiums which are remitted to commercial carriers.

The Department and other entities pay premiums to the State's Insurance Reserve Fund (IRF) which issues policies, accumulates assets to cover the risks of loss, and pays claims incurred for covered losses related to the following assets, activities, and/or events:

1. Theft of, damage to, or destruction of assets;
2. Real property, its contents, and other equipment;
3. Motor vehicles;
4. Torts; and
5. Natural disasters.

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.

The Department also purchases insurance through a commercial insurer for aircraft coverage, including bodily injury and property damage insurance up to \$10 million per occurrence and aircraft physical damage insurance based on the insured value of each aircraft maintained by the Department.

The Department has recorded insurance premium expenditures in the applicable program expenditure categories of the general fund.

SOUTH CAROLINA DEPARTMENT OF COMMERCE

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2004**

The Department has not transferred the portion of risk of loss related to insurance policy deductibles, and policy limits to a State or commercial insurer. The Department reported no expenditures in the current year for actual claims payment and costs related to such retained risks of loss.

In management's opinion, claims losses in excess of insurance coverage are unlikely, and if incurred, would be insignificant to the Department's financial position. Furthermore, there is no evidence of asset impairment or other information to indicate that a loss expenditure and liability should be recorded at year-end. Therefore, no loss accrual has been recorded.

NOTE 17. CONTINGENT LIABILITIES:

The various federal programs administered by the Department for the fiscal year 2004 and prior years are subject to examination by the federal grantor agencies. At the present time, amounts, if any, which may be due federal grantors have not been determined but the Department believes that any such amount in the aggregate would not have a material adverse effect on the financial position of the Department. Furthermore, there is no information to indicate that a liability should be recorded at fiscal year-end.

NOTE 19. COMMITMENTS:

The Department engages in a variety of development projects. All project commitments are to local government entities which are responsible for contracting with specific vendors to achieve the project objectives. Outstanding commitments as of June 30, 2004 are as follows:

Water and Wastewater Infrastructure Grants	\$	3,786,666
State Rural Infrastructure Grants		10,719,679
Community Development Block Grants		14,323,842
State Economic Development Programs		18,209,691
Airport Improvement and Expense Projects - funded by State Capital Improvement Bonds		165,982
State Aviation Fuel Tax Grants		1,369,061
Totals	\$	<u>48,574,921</u>

SOUTH CAROLINA DEPARTMENT OF COMMERCE
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2004

<u>Federal Grantor/Pass-Through Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Total Expenditures</u>	<u>Pass-Through Expenditures Subrecipients</u>
U.S. Department of Housing and Urban Development			
Direct Program:			
Community Development Block Grants/State's Program	14.228	\$ 24,399,658	\$ 23,538,651
U.S. Department of Transportation			
Direct Program:			
Federal Aviation Administration Airport Improvement Program	20.106	596	
Appalachian Regional Commission			
Direct Programs:			
Appalachian State Research, Technical Assistance and Demonstration Project	23.011	17,594	
Appalachian Area Development	23.002	904,158	904,158
U.S. Environmental Protection Agency			
Direct Programs:			
Solid Waste Management Assistance	66.808	4,690	
TOTALS		<u>\$ 25,326,696</u>	<u>\$ 24,442,809</u>

The Schedule of Expenditures of Federal Awards includes the federal grant activity of the South Carolina Department of Commerce and has been prepared on the cash basis method of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments and Non-Profit Organizations. Therefore some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the financial statements.



CERTIFIED PUBLIC ACCOUNTANTS AND FINANCIAL CONSULTANTS

**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT
OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE
WITH GOVERNMENT AUDITING STANDARDS**

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

We have audited the financial statements of South Carolina Department of Commerce (the Department) as of and for the year ended June 30, 2004, and have issued our report thereon dated March 23, 2005 which was qualified because of the omission of the Department's enterprise funds. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Department's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Department's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. The reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as items 04-1 through 04-7.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe the reportable conditions described on the accompanying Schedule of Findings and Questioned Costs as items 04-1 through 04-5 are material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Department's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under Government Auditing Standards.



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This report is intended solely for the information and use of the Governor, the Secretary of Commerce, management of the Department and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Roger Lalan, PA

March 23, 2005



CERTIFIED PUBLIC ACCOUNTANTS AND FINANCIAL CONSULTANTS

**REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE
TO ITS MAJOR PROGRAM AND INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**

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

Compliance

We have audited the compliance of South Carolina Department of Commerce (the Department) with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to its major federal program for the year ended June 30, 2004. The Department's major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to its major federal program is the responsibility of the Department's management. Our responsibility is to express an opinion on the Department's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Department's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the Department's compliance with those requirements.

As described in item 04-8 in the accompanying schedule of findings and questioned costs, the Department did not comply with requirements regarding monitoring that is applicable to its major federal program. Compliance with such requirements is necessary, in our opinion, for the Department to comply with the requirements applicable to that program.

In our opinion, except for the noncompliance described in the preceding paragraph, the Department complied, in all material respects, with the requirements referred to above that are applicable to its major federal program for the year ended June 30, 2004.

Internal Control Over Compliance

The management of the Department is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the Department's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.



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Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the Governor, the Secretary of Commerce, management of the Department and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Roger A. Lalan, PA

March 23, 2005

SOUTH CAROLINA DEPARTMENT OF COMMERCE
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004

SUMMARY OF AUDITOR'S RESULTS

Financial statements:

1. A qualified opinion dated March 23, 2005 on the financial statements of the Department for the year ended June 30, 2004 was issued.
2. Reportable conditions relating to the internal control over financial reporting were noted during our audit of the financial statements. These conditions are reported as material weaknesses.
3. No instances of noncompliance which were material to the financial statements were disclosed during the audit.

Federal Awards:

4. No reportable conditions in internal control over major programs were noted.
5. A qualified opinion on compliance for the major program dated March 23, 2005 was issued.
6. One finding was disclosed during the audit that is required to be reported under Section .510(a) of OMB Circular A-133.
7. The major program of the Department is the Community Development Block Grant – CFDA #14.228
8. The dollar threshold used to distinguish between Type A and Type B programs was \$759,801.
9. The Auditee was not determined to be a low risk auditee.

FINDINGS – FINANCIAL STATEMENT AUDIT

FINDINGS RELATED TO THE FINANCIAL STATEMENTS

The following reportable conditions are material weaknesses, are related to the Department's financial statements and are required to be reported in accordance with government auditing standards generally accepted in the United States of America.

04-1 ACCOUNTS PAYABLE UNDERSTATED

Condition:

Our audit disclosed that the Department underreported payables on the accounts payable closing package by approximately \$507,000. The same finding was cited in the prior year's report.

Cause:

The Department did not perform a careful review of vouchers processed subsequent to fiscal year-end to ensure that all liabilities attributable to the fiscal year were recorded.

Effect:

Liabilities and expenses/expenditures were understated. Audit adjustments were made to the Department's financial statements to correct these understatements.

Criteria:

Good business practices and GAAP require the Department to record all liabilities existing at fiscal year-end.

Recommendation:

The procedures being used to identify an invoice as a payable need to adhere more closely with GAAP. The Department should carefully review all vouchers processed subsequent to each fiscal year-end to ensure that all liabilities attributable to the fiscal year are recorded.

04-2 ERROR IN CAPITAL ASSETS CLOSING PACKAGE

Condition:

The Department did not adjust the beginning reported depreciation for vehicles based on adjustments made during the prior year's audit which resulted in the current year's depreciation expense and accumulated depreciation for vehicles being reported incorrectly on the capital assets closing package. A similar finding was cited in the prior year's management letter.

Cause:

Department personnel did not reconcile their capital asset depreciation schedule to the prior year's adjusted schedule. A detailed review by someone independent of the preparer should be performed.

Effect:

Misstatements resulted in current year depreciation expense and accumulated depreciation. Audit adjustments were made to the Department's financial statements to correct these misstatements.

Criteria:

Good business practices require that all schedules be reconciled and that they be independently reviewed for reasonableness.

Recommendation:

We recommend that the Department implement adequate review procedures to ensure that all schedules and reports that it prepares are accurate.

04-3 ERRORS IN GRANTS RECEIVABLE AND DEFERRED REVENUE CLOSING PACKAGE

Condition:

Our audit disclosed the following errors in the grants receivable and deferred revenue closing package:

1. The Department reported deferred revenue of \$93,771 as shown on their grant analysis worksheet as grants receivable and reported the grants receivable of \$3,158 as deferred revenue on the closing package.
2. The Department did not make the necessary adjustments to record the effect of approximately \$144,000 of accounts payable reported on the accounts payable closing package which would have caused the deferred revenue amount to become a grant receivable.

Cause:

Failure to carefully prepare and review the closing package before submission to the Comptroller General's Office.

Effect:

Misstatements resulted in grants receivable, deferred revenue and federal revenues.

Criteria:

The Comptroller General's GAAP Closing Procedures Manual contains instructions on the proper completion of the closing package.

Recommendation:

We recommend that additional care be taken in the preparation and review of the closing packages to ensure that they are prepared correctly and include all required elements.

04-4 ERROR IN OPERATING LEASE CLOSING PACKAGE

Condition:

Our audit disclosed that the Department included a cancelable lease in the operating lease closing package as a future minimum lease payment commitment in error. The lease agreement allowed the Department to cancel the lease upon payment of six months rent.

Cause:

Department personnel apparently did not perform an adequate review of all terms of the lease agreement.

Effect:

The Department closing package was in error.

Criteria:

The Comptroller General's GAAP Closing Procedures Manual contains instructions on the proper preparation of the closing package.

Recommendation:

We recommend that additional care be taken to ensure that the future minimum lease payments schedule is accurate.

04-5 OUTSTANDING COMMITMENTS OVERSTATED

Condition:

The Department did not reduce the amount of outstanding commitments for various grants by the amount reported as accounts payable as required which resulted in an overstatement of approximately \$4,500,000 in the amount of outstanding commitments.

Cause:

Failure to adequately follow the instructions contained in the Comptroller General's GAAP Closing Procedures Manual.

Effect:

The Department overstated the amount shown as outstanding commitments.

Criteria:

Generally accepted accounting principles require that outstanding commitments be reduced by any amounts reported as a liability.

Recommendation:

We recommend that the Department ensure that all amounts reported for outstanding commitments are adjusted for accounts payable.

04-6 SUPPORT NOT RECEIVED FOR CAPITAL ASSET DELETIONS

Condition:

In testing five capital asset deletions, we determined that the Department did not have the proper turn-in documents to support the deletions for two of the assets.

Cause:

Unknown

Effect:

The Department could lose control over capital assets by removing them from the capital asset listing without the required documentation.

Criteria:

Departmental policy required the receipt of certain documents before the assets are deleted from the listing.

Recommendation:

We recommend that the Department follow its procedures to ensure that all required documentation is received prior to the deletion of any capital asset.

04-7 GRANT PAYMENTS MADE PRIOR TO CONTRACT EXTENSION

Condition:

Our audit disclosed five instances where the Department made reimbursements to sub-recipients under contracts that had expired. All of the agreements were subsequently amended to extend the contract period but only after the payments had already been made by the Department.

Cause:

Unknown

Effect:

The Department spent funds for which a sub-grant agreement was not executed which could lead to a loss of control over the funds.

Criteria:

Good internal controls require the existence of a valid grant agreement that covers the period to be reimbursed before reimbursements are made.

Recommendation:

We recommend that the Department revise its procedures to ensure that all parties sign valid extensions before reimbursements are processed.

FINDINGS AND QUESTIONED COSTS FOR FEDERAL AWARDS

04-8 INADEQUATE MONITORING PROCEDURES – COMMUNITY DEVELOPMENT BLOCK GRANTS / STATE'S PROGRAM – CFDA # 14.228

Condition:

The Department has not adequately followed up on the audit findings for one of its sub-recipients. The June 30, 2003 report was received by the Department on June 7, 2004 and the Department had not completed its review of the report as of February 8, 2005. The same finding was cited in the report for the year ended June 30, 2003 was also cited for the prior two years for the sub-recipient and the Department did not ensure that adequate corrective action was taken.

Cause:

Department personnel apparently did not perform adequate and timely reviews of the audit reports received.

Effect:

The Department is at risk that the sub-recipient is not properly following the required guidelines.

Criteria:

The A-133 Compliance Supplement requires the Department to issue a management decision on audit findings within six months of receipt and to ensure that the sub-recipient takes timely and appropriate action on all audit findings.

Questioned Costs:

None

Recommendation:

We recommend that the Department ensure that all audit findings are followed up on in a timely manner and also ensure that their sub-recipients take the required corrective action.

CORRECTIVE ACTION PLAN

APPENDIX A



Mark Sanford
Governor

SOUTH CAROLINA
DEPARTMENT OF COMMERCE

Robert A. Faith
Secretary

May 13, 2005

Rogers and Laban, PA
Certified Public Accountants and Financial Consultants
Mr. Barry Laban
PO Box 124
Columbia, SC 29202

Dear Mr. Laban:

This letter is in response to the Management Letter Findings and Comments for the audit period ending June 30, 2004 for the South Carolina Department of Commerce.

GAAP Packages:

04-1 Accounts Payable Closing Package

Management agrees with the Accounts Payable finding. The Department did begin correction of this process as soon as it was noted in the 2003 audit (March 2004). We do agree that grant recipients should submit reimbursements in a timely manner and that we should review all grant payments closer for possible accounts payables. The Department made tremendous improvements in reporting accounts payables and even reported estimates as was suggested in last years audit. The Department has implemented a new procedure for reviewing Accounts Payables at year end and management will ensure that all accounts payables are being reported to the best of our knowledge.

04-2 Capital Assets Closing Package and 04-06 Capital Assets Deletions

Management agrees with the Capital Assets finding. A new Capital Asset system was implemented beginning July 1, 2004 (Fiscal Year 2004-2005) as a follow up the 2003 audit (March 2004). This new system will ensure that all capital assets are being reconciled and reported correctly with appropriate depreciation. Management will review all schedules and reports to ensure that procedures are being followed and that proper documentation is being kept.

04-3 Grants Receivable and Deferred Revenue Closing Package

Management agrees with the Grants Receivable and Deferred Revenue finding. The Department did not properly review and cross reference to ensure that deferred revenue and grants receivables were being properly reported. Management will review all schedules and reports to ensure that procedures are being followed and that proper documentation is being kept and that all numbers are reported properly.

04-4 Operating Lease Closing Package

Management agrees with the Operating Lease finding. All terms of each lease will be reviewed more thoroughly. A process was put into place following the 2003 audit (March 2004) to ensure that all leases were reviewed by the Finance Department. Management will review all leases more thoroughly to ensure proper recording of leases.

04-5 Commitments Closing Package

Management agrees with the Commitment finding. This package was first submitted by Commerce beginning in the 2003 audit (March 2004) and proper training on the GAAP Package did not occur until 2005. Management understands that all commitments must be net of any accounts payable and will ensure that staff is reporting the commitments correctly on future closing packages.

Other Findings:

04-6 Asset Turn In Documents

Management agrees that all asset turn in documents should be maintained with asset file and will ensure that all documentation will be maintained upon deletion or disposal of capital assets.

04-7 Grant Payments Made Prior to Contract Extension

Management agrees that all grant payments should be made under a current contract. A system of checks and balances has been implemented immediately to ensure that only current contracts that have not expired can receive grant payments. The Grants and Incentives Division was notified of the new procedure and will work with Administration Division to receive the proper contract extension in a timely manner.

04-8 Monitoring Procedures for CDBG Audits

Management agrees with the finding and had developed a revised audit process in January 2005. This new audit process would have corrected the situation which was cited in this audit. It should be noted that there was no process in place prior to this and that no previous audits (federal or state) had noted any problems with the monitoring of audits. Management believes that the new audit process has addressed this finding and should have been noted in the audit.

The Department of Commerce has made tremendous strides in correcting previous audit findings and will continue to address the findings in this audit.

Sincerely,



Mandy M. Kibler
Director of Administration
South Carolina Department of Commerce