

**SOUTH CAROLINA
DEPARTMENT OF AGRICULTURE
COLUMBIA, SOUTH CAROLINA**

STATE AUDITOR'S REPORT

JUNE 30, 2002

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State of South Carolina



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INDEPENDENT ACCOUNTANT'S REPORT ON APPLYING AGREED-UPON PROCEDURES

January 24, 2003

The Honorable Charles R. Sharpe, Commissioner
South Carolina Department of Agriculture
Columbia, South Carolina

We have performed the procedures described below, which were agreed to by the Commissioner and management of the South Carolina Department of Agriculture (the Department), solely to assist you in evaluating the performance of the Department for the fiscal year ended June 30, 2002, in the areas addressed. The Department's management is responsible for its financial records, internal controls and compliance with State laws and regulations. This agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. The sufficiency of these procedures is solely the responsibility of the specified parties in this report. Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

The procedures and the associated findings are as follows:

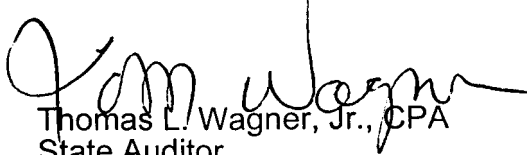
1. We tested selected recorded receipts to determine if these receipts were properly described and classified in the accounting records and internal controls over the tested receipt transactions were adequate. We also tested selected recorded receipts to determine if these receipts were recorded in the proper fiscal year. We compared amounts recorded in the general ledger and subsidiary ledgers to those in the State's accounting system (STARS) as reflected on the Comptroller General's reports to determine if recorded revenues were in agreement. We made inquiries and performed substantive procedures to determine if revenue collection and retention or remittance were supported by law. We compared current year recorded revenues from sources other than State General Fund appropriations to those of the prior year to determine the reasonableness of collected and recorded amounts by revenue account. The individual transactions selected for testing were chosen randomly. We found no exceptions as a result of the procedures.

2. We tested selected recorded non-payroll disbursements to determine if these disbursements were properly described and classified in the accounting records, were bona fide disbursements of the Department, and were paid in conformity with State laws and regulations; if the acquired goods and/or services were procured in accordance with applicable laws and regulations; and if internal controls over the tested disbursement transactions were adequate. We also tested selected recorded non-payroll disbursements to determine if these disbursements were recorded in the proper fiscal year. We compared amounts recorded in the general ledger and subsidiary ledgers to those in various STARS reports to determine if recorded expenditures were in agreement. We compared current year expenditures to those of the prior year to determine the reasonableness of amounts paid and recorded by expenditure account. The individual transactions selected for testing were chosen randomly. We found no exceptions as a result of the procedures.
3. We tested selected recorded payroll disbursements to determine if the tested payroll transactions were properly described, classified, and distributed in the accounting records; persons on the payroll were bona fide employees; payroll transactions, including employee payroll deductions, were properly authorized and were in accordance with existing legal requirements; and internal controls over the tested payroll transactions were adequate. We tested selected payroll vouchers to determine if the vouchers were properly approved and if the gross payroll agreed to amounts recorded in the general ledger and in STARS. We also tested payroll transactions for selected new employees and those who terminated employment to determine if internal controls over these transactions were adequate. We compared amounts recorded in the general ledger and subsidiary ledgers to those in various STARS reports to determine if recorded payroll and fringe benefit expenditures were in agreement. We performed other procedures such as comparing current year recorded payroll expenditures to those of the prior year; comparing the percentage change in recorded personal service expenditures to the percentage change in employer contributions; and computing the percentage distribution of recorded fringe benefit expenditures by fund source and comparing the computed distribution to the actual distribution of recorded payroll expenditures by fund source to determine if recorded payroll and fringe benefit expenditures were reasonable by expenditure account. The individual transactions selected for testing were chosen randomly. We found no exceptions as a result of the procedures.
4. We tested selected recorded journal entries and all operating and appropriation transfers to determine if these transactions were properly described and classified in the accounting records; they agreed with the supporting documentation, were adequately documented and explained, were properly approved, and were mathematically correct; and the internal controls over these transactions were adequate. The journal entries selected for testing were chosen randomly. We found no exceptions as a result of the procedures.
5. We tested selected entries and monthly totals in the subsidiary records of the Department to determine if the amounts were mathematically accurate; the numerical sequences of selected document series were complete; the selected monthly totals were accurately posted to the general ledger; and the internal controls over the tested transactions were adequate. The transactions selected for testing were chosen randomly. We found no exceptions as a result of the procedures.

6. We obtained all monthly reconciliations prepared by the Department for the year ended June 30, 2002, and tested selected reconciliations of balances in the Department's accounting records to those in STARS as reflected on the Comptroller General's reports to determine if they were accurate and complete. For the selected reconciliations, we determined if they were timely performed and properly documented in accordance with State regulations, recalculated the amounts, agreed the applicable amounts to the Department's general ledger, agreed the applicable amounts to the STARS reports, determined if reconciling differences were adequately explained and properly resolved, and determined if necessary adjusting entries were made in the Department's accounting records and/or in STARS. The reconciliations selected for testing were chosen randomly. We found no exceptions as a result of the procedures.
7. We tested the Department's compliance with all applicable financial provisions of the South Carolina Code of Laws, Appropriation Act, and other laws, rules, and regulations for fiscal year 2002. Our findings as a result of these procedures are presented in Closing Packages in the Accountant's Comments section of this report.
8. We obtained copies of all closing packages as of and for the year ended June 30, 2002, prepared by the Department and submitted to the State Comptroller General. We reviewed them to determine if they were prepared in accordance with the Comptroller General's GAAP Closing Procedures Manual requirements; if the amounts were reasonable; and if they agreed with the supporting workpapers and accounting records. Our findings as a result of these procedures are presented in Closing Packages in the Accountant's Comments section of this report.
9. We obtained a copy of the schedule of federal financial assistance for the year ended June 30, 2002, prepared by the Department and submitted to the State Auditor. We reviewed it to determine if it was prepared in accordance with the State Auditor's letter of instructions; if the amounts were reasonable; and if they agreed with the supporting workpapers and accounting records. We found no exceptions as a result of the procedures.

We were not engaged to and did not conduct an audit, the objective of which would be the expression of an opinion on the specified areas, accounts, or items. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the information and use of the Governor, the Commissioner, and of the management of the Department and is not intended to be and should not be used by anyone other than these specified parties.


Thomas L. Wagner, Jr., CPA
State Auditor

ACCOUNTANT'S COMMENTS

MATERIAL WEAKNESSES AND VIOLATIONS OF STATE LAWS, RULES OR REGULATIONS

The procedures agreed to by the agency require that we plan and perform the engagement to obtain reasonable assurance about whether noncompliance with the requirements of State Laws, Rules, or Regulations occurred and whether internal accounting controls over certain transactions were adequate. Management of the entity is responsible for establishing and maintaining internal controls. A material weakness is a condition in which the design or operation of one or more of the specific internal control components does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Therefore, the presence of a material weakness or violation will preclude management from asserting that the entity has effective internal controls.

The conditions described in this section have been identified as material weaknesses or violations of State Laws, Rules, or Regulations.

CLOSING PACKAGES

Introduction

The State Comptroller General's Office obtains certain generally accepted accounting principles (GAAP) information from agency-prepared closing packages to prepare the State's financial statements. Section 1.8 of the GAAP Closing Procedures Manual (GAAP Manual) states that each agency is responsible for submitting accurate and complete closing package forms that are completed in accordance with instructions. Section 1.9 requires agencies to keep working papers to support each amount they enter on each closing package form. The GAAP Manual recommends an effective review of each closing package and the underlying working papers to minimize closing package errors and omissions. To assist in performing effective reviews, the GAAP Manual instructions require a reviewer checklist to be completed for each closing package submitted. Further, a strong control environment requires management to display and communicate an appropriate attitude regarding internal controls and the reporting process.

We noted numerous errors in our review of the Agency's year-end closing packages which we have described below. We determined that the errors occurred because Agency staff did not follow GAAP Manual instructions and failed to perform an effective review of each closing package (despite the fact that each reviewer's checklist was completed). Department personnel told us that they have not devoted appropriate time to required financial reporting because of budget and staff reductions experienced by the Agency during the year.

Grant/Contribution Receivables and Deferred Revenue

In our review of the grant/contribution receivables and deferred revenue closing package and the Department's schedule of federal financial assistance, we found that the Agency failed to report receivables and deferred revenue for all of its federal grants. The grant receivables and grant deferred revenue were understated \$644 and \$92,429, respectively.

Department personnel believed that they were only required to report those individual grants that had federal revenues greater than \$750,000. Section 3.3 of the GAAP Manual instructs agencies to complete the closing package if the *combined* grant and contribution revenue that an agency received during the fiscal year totaled \$750,000 or more. This section further states that “the final closing package amounts should reconcile to your Schedule of Expenditures of Federal Awards plus or minus accounts payable and accounts payable reversals and non-Federal grants/contributions.”

Operating Lease Lessor Summary Form

In our review of the Operating Lease Lessor Summary Form we found two clerical errors. First, the Agency reported \$7,611,393 on the closing package for land leased to others while supporting documentation shows the correct amount to be \$7,661,393. Second, the amount should have been reported as buildings leased to others rather than as land leased to others.

Section 3.20, page 9 of the GAAP Closing Procedures Manual provides guidance on the completion of the closing package and the reviewer’s checklist specifically stating “An effective review is essential to minimizing closing package errors. As such, it is an important internal control.”

Capital Assets Summary Form

In our testing of the Capital Assets Summary Form, we noted that the amount reported for “assets removed due to capitalization criteria change” for machinery and equipment could not be supported by Agency accounting records. In our discussions with Agency personnel, we discovered that the amount was determined by subtracting the prior year “end-of-year balance” from the current year “start-of-year balance”. For fiscal year 2002, the Agency used a new capital asset worksheet to determine the “start-of-year balance”. On the worksheet, this balance had already been adjusted for assets removed due to the change in capitalization

criteria but the Department did not maintain a record of those assets. Also, we found a formula error in the worksheet that overstated “assets removed due to capitalization criteria change” and understated the “end-of-year balance” by \$552,272.

Accumulated Depreciation Summary Form

In our testing of the Accumulated Depreciation Summary Form, we found that the Agency did not follow GAAP Manual instructions for determining the useful lives of its capital assets. The GAAP Closing Procedures Manual, Section 3.9, page 17 states the following: “The useful life you choose should fall within the range provided in Exhibit 3.9(A) for the particular type of asset and should be expressed in a whole number of years. If you disagree with the range of useful lives for a particular type of asset as listed on the useful lives schedule, please contact the Comptroller General’s Office so that we may agree on an appropriate useful life.” We found that the Department calculated depreciation and accumulated depreciation for its vehicles based on a twenty year useful life rather than using the lives shown on the Comptroller General’s schedule which are significantly less. Further, the Department did not contact the Comptroller General’s Office as stated in the requirement above.

Miscellaneous Receivables Closing Package

In our testing of the Miscellaneous Receivables Closing Package, we noted several errors in the preparation of the closing package as follows.

1. Amounts receivable at June 30, 2002 that were received before the closing package was prepared (September 4, 2002) were not included in the closing package receivable.
2. Some amounts were added twice when calculating the receivables total.
3. Prepaid rent was reported as revenue instead of deferred revenue.

The first two errors resulted in an understatement of miscellaneous accounts receivable and revenue of \$213,860. The third error resulted in an understatement of deferred revenues and an overstatement of revenues of \$27,733.

Upon further investigation, we found that a proper review of the closing package was not performed. The reviewer checklist was completed by the same individual who prepared the closing package. Also, the Agency responded yes to questions that should have been answered no. If these questions had been investigated and answered correctly, the errors noted above likely would have been detected. GAAP Manual section 3.4, page 4, defines Miscellaneous Accounts Receivable as “revenues that your agency has earned during the fiscal year for which your agency did not receive payment as of June 30”. Agencies are instructed to record deferred revenue if, at June 30, the State has collected cash or other assets but has not yet earned the related license, fee, and permit revenue or charges for services and commodities revenue. Section 3.4, page 19 of the GAAP Closing Procedures Manual provides guidance on the completion of the closing package and the reviewer’s checklist specifically stating “An effective review is essential to minimizing closing package errors. As such, it is an important internal control.” The cited section goes on to say that the reviewer must be someone other than the preparer.

Recommendation

We recommend that the Agency implement effective internal controls for the preparation and review of each closing package submitted to the Comptroller General’s Office. Such controls should address the control environment including management’s display and communication of an appropriate attitude toward financial reporting including both the completion and review of the closing packages. Staff should be thoroughly familiar with the GAAP Manual and the agency data required to be reported on each closing package. Further, the reviewer should be someone other than the person completing each closing package and should perform an effective review by using the required reviewer’s checklist.

MANAGEMENT'S RESPONSE

The management of the South Carolina Department of Agriculture did not respond to the findings identified in the Accountant's Comments Section of this report by the due date specified in our transmittal letter accompanying the preliminary draft for the agency's review dated February 20, 2003.

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