

# **Office of the State Auditor**

## **FY 2005-2006 Accountability Report**

### **Section I – Executive Summary**

#### **1. Mission and Values:**

The mission of the Office of the State Auditor is to bolster public confidence in state government finance by serving as a deterrent to fiscal mismanagement, fraud, and misuse of assets by state agencies and providers of Medicaid services. We value professionalism in our staff and completion of our audit work in accordance with established professional standards.

#### **2. Major Achievements**

The Office of the State Auditor succeeded in maintaining an adequate level of audit coverage of State government agencies and Medicaid providers with the limited funding and personal services resources available. Other major achievements include:

- The audit of the State of South Carolina's Basic Financial Statements was completed on schedule. The Comptroller General was awarded the Certificate of Achievement for Excellence in Financial Reporting for the State's CAFR.
- The Single Audit Report was completed on time and under budget. It was accepted by the U.S. Department of Health and Human Services without revision.
- Fifty-nine Medicaid audit reports were issued representing 32 providers. The audit reports identified adjustments to payments made to providers resulting in the Department of Health and Human Services certifying receivables of more than \$2.53 million.
- Audit engagements of 84 of the 112 state departments, agencies and institutions were completed during the year. The State Auditor's Office is on schedule to complete an audit of each state agency at least once every three years.
- Oversight of \$2 million in audit contracts with CPA firms.

### 3. Key Strategic Goals

The strategic goal that is key to accomplishing the mission of the Office of the State Auditor is to provide adequate audit coverage of state agencies and Medicaid providers. Adequate audit coverage ensures that these organizations and their employees recognize that mismanagement, fraud, and misuse of assets will be discovered.

### 4. Opportunities and Barriers

The primary barrier to achieving our mission and strategic goals continues to be limited funding of our programs. Current funding does not allow the Office of the State Auditor to complete all of the audits of state agencies mandated by statute and could lead to marginal audit coverage of Medicaid providers. The application of information technology to audit processes continues to improve the efficiency of our audit programs and to provide our elected officials and the general public better access to our audit reports.

### 5. Use of the Accountability Report

The accountability report is used by the management team for strategic planning. We analyze the information relative to previous years as well as our objectives for the coming years and balance the assignment of available resources to the major agency objectives.

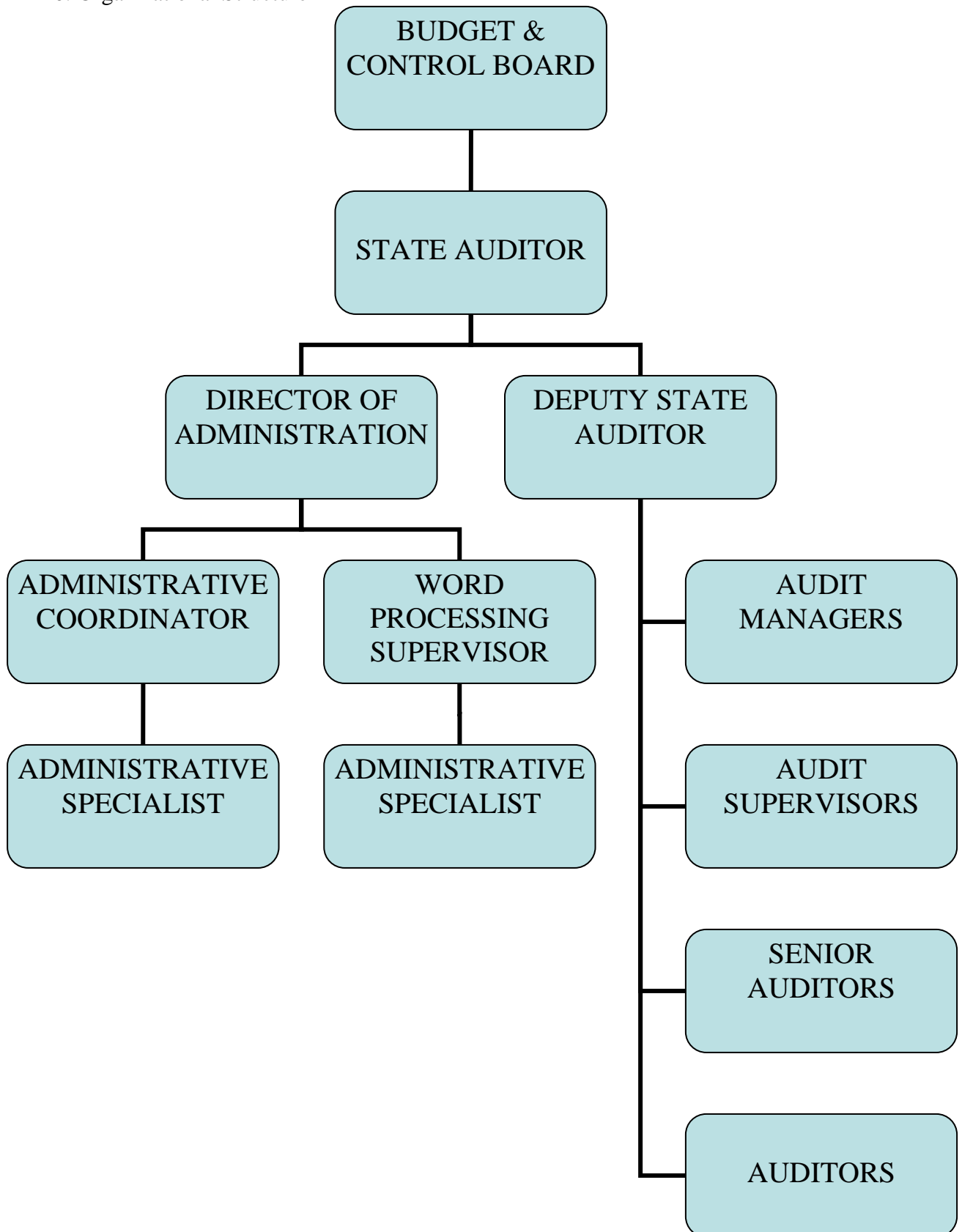
## **Section II – Organizational Profile**

1. **Main Products and Services** – The Office of the State Auditor conducts audits of state government and providers of Medicaid services. The State Audits section performs financial audits of state agencies, the annual financial audit of the State's Basic Financial Statements, and the annual Single Audit of the State's Schedule of Federal Financial Assistance. These audits cover all state agencies with total funds of over \$18 billion and appropriated funds of over \$5.6 billion. The size of the agencies ranges from very small to an agency with appropriations of \$2.1 billion. The Medicaid Audits section conducts audits and reviews of cost reports filed by institutional providers of Medicaid services. These cost reports are used by the Department of Health and Human Services to establish amounts to be paid to these providers for services provided to qualified Medicaid recipients. Also, technical assistance is provided to other governmental entities by either assisting with or conducting reviews of financial records and record keeping systems.
2. **Customer Segments and Key Requirements/Expectations** - All financial and compliance audit reports and management letters are provided to the Governor's Office, Comptroller General, State Treasurer, Senate Finance Committee, House Ways and Means Committee, the Board's Budget Division, Legislative Audit Council, and State Library. They are also published on our internet website for review by the citizens of South Carolina. These reports are particularly important because they point out material weaknesses in an agency's accounting system or procedures. They also highlight instances in which regulations or laws were violated. A key element in accomplishing the agency's mission is to provide sufficient audit coverage of state agencies and Medicaid providers such that these organizations and their employees recognize that mismanagement, fraud, and misuse of assets will be detected.

3. Key Stakeholders – The citizens of the state are ultimately the key stakeholders in the mission of the Office of the State Auditor to be a deterrent to fiscal mismanagement, fraud, and misuse of assets by state agencies and providers of Medicaid services.
4. Key Suppliers – The Office of the State Auditor contracts with private CPA firms for audit services. In FY 2005-06 audit contracts totaled over \$ 2.0 million.
5. Operation Location - The Office of the State Auditor is located at 1401 Main Street, Suite 1200, Columbia, South Carolina. Administrative, managerial and audit functions are carried out at this location; a significant portion of the audit work is conducted on-site at state agencies and Medicaid provider facilities.
6. Number of Employees - The FY 2005-06 Appropriations Act included fifty-nine full time equivalent positions for the Office of the State Auditor. Because of budget limitations, staff size was forty on July 1, 2005 and thirty-eight on June 30, 2006. All positions are classified except the agency head and two unclassified management positions.
7. Regulatory Environment – The Office of the State Auditor conducts all audit work in accordance with professional auditing standards. Therefore, all of our audit work complies with applicable standards of the American Institute of Certified Public Accountants. Also, the Government Finance Officers' Association awarded South Carolina the Certificate of Achievement for Excellence in Financial Reporting for the State's Comprehensive Annual Financial Report, which includes the State's General Purpose Financial Statements.
8. Strategic Challenges – The key strategic challenge continues to be the lack of resources needed to provide the audit coverage required by statute and contractual agreement. Thirty-five percent of our positions were vacant at the end of the fiscal year because of funding shortages. Exacerbating the problem is the salary levels required to attract and retain qualified auditors, as well as the time and expense involved in recruiting.

9. Performance Improvement System – The Office of the State Auditor uses an interim evaluation system and an audit status information system to focus our efforts on performance improvement. The auditor in charge of each audit completes an interim evaluation of each member of the audit team at the conclusion of the audit. These interim evaluations are later used in completing the annual Employee Performance Management System evaluation. This system provides immediate feedback to the staff auditors about their performance and opportunities for improvement. Audit managers maintain a system that tracks the status of each audit engagement and provides feedback regarding performance improvements.

## 10. Organizational Structure



11. Expenditures/Appropriations Chart

## Accountability Report Appropriations/Expenditures Chart

### Base Budget Expenditures and Appropriations

Major Budget Categories	FY 04-05 Actual Expenditures		FY 05-06 Actual Expenditures		FY 06-07 Appropriations Act	
	Total Funds	General Funds	Total Funds	General Funds	Total Funds	General Funds
Personal Service	\$ 1,795,336	\$ 795,336	\$ 1,915,539	\$ 1,915,539	\$ 2,242,059	\$ 2,242,059
Other Operating	\$ 869,763	\$ 384,633	\$ 898,042	\$ 567,422	\$ 935,215	\$ 391,215
Special Items					\$	\$
Permanent Improvements					\$	\$
Case Services					\$	\$
Distributions to Subdivisions					\$	\$
Fringe Benefits	\$ 481,052	\$ 481,052	\$ 491,643	\$ 491,643	\$ 607,180	\$ 607,180
Non-recurring					\$ 855,652	\$ 855,652
<b>Total</b>	<b>\$ 3,146,151</b>	<b>\$ 661,021</b>	<b>\$ 3,305,224</b>	<b>\$ 2,974,604</b>	<b>\$ 4,640,106</b>	<b>\$ 4,096,106</b>

Expenditures/Appropriations Chart - continued

**Other Expenditures**

<b>Sources of Funds</b>	<b>FY 04-05 Actual Expenditures</b>	<b>FY 05-06 Actual Expenditures</b>
Supplemental Bills	\$	\$
Capital Reserve Funds	\$	\$
Bonds	\$	\$



12. Major Program Areas Chart

**Major Program Areas**

<b>Program Number and Title</b>	<b>Major Program Area Purpose (Brief)</b>	<b>FY 04-05 Budget Expenditures</b>	<b>FY 05-06 Budget Expenditures</b>
II. AUDITS	Financial audits of state agencies, providers of Medicaid services, the State's Basic Financial Statements, and the State's Schedule of Federal Financial Assistance.	<b>State:</b> 1,915,802.00 <b>Federal:</b> 0.00 <b>Other:</b> 485,130.00 <b>Total:</b> 2,400,932.00 <b>% of Total Budget:</b> 76%	<b>State:</b> 2,174,480.00 <b>Federal:</b> 0.00 <b>Other:</b> 330,620.00 <b>Total:</b> 2,505,100.00 <b>% of Total Budget:</b> 76%

**Below: List any programs not included above and show the remainder of expenditures by source of funds.**

I. ADMINISTRATION and III. EMPLOYEE BENEFITS

<b>Remainder of Expenditures:</b>	<b>State:</b> 745,217.00 <b>Federal:</b> <b>Other:</b> <b>Total:</b> 745,217.00 <b>% of Total Budget:</b> 24%	<b>State:</b> 800,123.00 <b>Federal:</b> <b>Other:</b> <b>Total:</b> <b>% of Total Budget:</b> 24%
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### **Section III – Elements of Malcolm Baldrige**

#### **Category 1 - Leadership**

The State Auditor, in conjunction with the audit directors and audit managers, defines and communicates the values of the organization to the staff. The State Auditor meets with the audit directors and managers monthly to discuss organizational priorities, problems and progress. This senior management team works collectively with the State Auditor to define the organizational values and priorities. This team is primarily responsible for communicating the direction and priorities of the agency to the staff.

To monitor progress on this goal, the Audit Managers (senior leaders) maintain management information of the status of audits planned for the fiscal year at all times. This system communicates to the staff the importance of completing the audits on time and maintains accountability for the audit function.

The auditor in charge of each audit completes an interim evaluation of each member of the audit team at the conclusion of the audit. These interim evaluations are later used in completing the annual Employee Performance Management System evaluation. This system provides immediate feedback to the staff auditors about their performance and opportunities for improvement.

When a staff auditor leaves the Office of the State Auditor, the Director of Administration conducts an exit interview with the individual on his/her last day. The purpose is to get valid, honest information about staff perceptions, morale, and suggestions for improving the employment experience at the Office of the State Auditor. The information is shared with and analyzed by the State Auditor and the program directors. The information is also shared in general terms with the audit managers. This process has proven to be a very effective way to identify improvements to the office policies and procedures.

The Office of the State Auditor is instrumental in supporting and strengthening the financial community within state government. The standards of financial responsibility in state government are, to a large degree, defined by the audits conducted by the Office of the State Auditor. The emphasis on professional standards, certification as a CPA, and the Governmental Finance Officers Association Certificate of Excellence in Financial Reporting are examples of the leadership of the Office of the State Auditor in state government.

### Category 2 - Strategic Planning

Statutes and regulations define the responsibilities of the Office of the State Auditor and drive the strategic planning process. It is a process of developing and allocating resources to accomplish each of these responsibilities. Because of deadlines during the year for much of our audit work, the planning requires careful coordination and timing of the allocation of resources. The State Auditor in conjunction with the program directors does the strategic planning on a continual basis. The strategies are communicated to the audit managers in the monthly management meeting and to the entire staff through the agency intranet.

The strategic planning process in this Office consists of some well-defined steps; each one analyzed on short and long term bases:

- 1) Identify the audit work that must be done to satisfy our statutory and regulatory mandates.
- 2) Analyze the audit time required (based on historical data).
- 3) Analyze the time frames (deadlines) for each of the audit programs.
- 4) Identify the resources available and timing of availability.
- 5) Determine the priority of the audits and the ramifications of not completing all the requirements.
- 6) Identify strategies for development of the resources needed to meet all requirements within the time frames.

One component of strategic planning is workforce planning. Our efforts in this area have resulted in:

- 1) A more diverse workforce as indicated by our meeting our Affirmative Action Program goals.
- 2) Development of online recruiting capability, resulting in more qualified applicants.
- 3) Adoption of a variable work schedule policy that shows indications of helping with retention of current employees.
- 4) Tuition Assistance Program (when funding allows) that has contributed to several staff members pursuing certification as a CPA.

## Strategic Planning

<b>Program Number and Title</b>	<b>Supported Agency Strategic Planning Goal/Objective</b>	<b>Related FY 05-06 Key Agency Action Plan/Initiative(s)</b>
II. AUDITS	Audit the State of South Carolina's Basic Financial Statements prepared by the Comptroller General.	Contract with a private CPA firm for one-half of audit work. Reassign staff auditors from Medicaid audits as needed to provide the 4000 audit hours budgeted to complete the audit by the December deadline.
II. AUDITS	Audit the State of South Carolina's Schedule of Expenditures of Federal Awards as mandated by the Single Audit Act Amendments of 1996.	Assign staff auditors as necessary to provide the 13,750 audit hours budgeted to complete the audit by the March deadline.
II. AUDITS	Audit cost reports filed by institutional providers of Medicaid services.	Conduct as many audits as possible with available staff toward the objective of auditing 55 Medicaid providers this year.
II. AUDITS	Audit the financial records of state agencies.	Conduct as many audits as possible with available staff toward the objective of auditing each state agency each year.

### Category 3 - Customer Focus

The General Assembly, the public through its elected officials, and state agency directors are the customers of the Office of the State Auditor. The customers have clearly communicated their focus by passing the statutes defining our programs and audit responsibilities. The statutes and regulations require an annual audit of state government entities and Medicaid providers. Being responsive to our customers means conducting audits in a timely manner and according to professional standards.

The State Auditor has been effective in working with the General Assembly. His many years of experience in state government and the public accounting field provides the background and perspective to effectively communicate with members of the General Assembly and agency management regarding the functions of the Office of the State Auditor.

To more effectively and efficiently communicate the results of our audits to our customers, the Office of the State Auditor now publishes audit reports on our internet website. Auditees are notified of the report by email or letter. Hard copies of reports are provided upon request or when required by law or regulation. This approach not only saves the cost of printing and postage, it also makes the reports more readily available to the public and other public officials. Audit results are communicated to our customers more effectively and at a lower cost to the State.

### Category 4 - Measurement, Analysis, and Knowledge Management

Since the statutes and regulations define the programs of the Office of the State Auditor, the performance measures are logically defined as efficiency and effectiveness. We measure efficiency by determining how well our staff completes each audit within the assigned budget of audit hours and within the required time frames. We measure effectiveness by our degree of compliance with professional auditing standards. All audit work is subject to an internal compliance (quality control review). Additionally, we undergo an external review every three years. An independent auditor,

usually a private CPA firm under contract, conducts the peer review. The standards and time frames are established by the federal government and by professional entities such as the Government Finance Officers Association and the American Institute of Certified Public Accountants.

#### Category 5 - Human Resource Focus

A crucial element in the development and motivation of our employees is the interim evaluation that each auditor receives at the conclusion of an audit. The auditor in charge of each audit completes the interim evaluation of each member of the audit team. This system provides immediate feedback to the staff auditors about their performance and opportunities for improvement. The interim evaluations are also used in completing the annual Employee Performance Management System evaluation and in identifying staff training needs.

One of the important ways that the Office of the State Auditor encourages employees to develop their full potential is the emphasis on achieving certification as a CPA. The State Auditor's Office supports and encourages staff members in this effort by providing qualifying experience and the in-house training required to meet the continuing education requirements of maintaining a CPA certificate. When funds are available, tuition assistance is also offered to encourage auditors to acquire the necessary academic requirements to apply for the CPA. One factor considered when evaluating a candidate for employment is his/her interest in pursuing certification as a CPA. In addition, promotion policies require staff members to achieve certification as a CPA in order to progress to Audit Supervisor or above.

## Category 6 - Process Management

The production process used by the Office of the State Auditor is one of service delivery. It consists of conducting audits and reporting the results of the audit to our customers. The process of conducting an audit and reporting the results are well defined by professional standards. Our efforts in this area are largely directed at developing the competencies and expertise of our staff to conduct audits and report results in accordance with professional standards. Our continuous professional training, in-house training, tuition assistance, emphasis on certification, performance review system, and audit quality control processes are all components of our focus on ensuring that our audit processes conform to established professional standards.

Developments in information technology have allowed us to improve the efficiency of our audit processes and to make our audit reports more accessible to our customers. The Office of the State Auditor now publishes audit reports on its internet website. This eliminated the printing and postage cost of our reports. Audit results are communicated to our customers more effectively and at a lower cost to the State.

## Category 7 - Results

The mission of the Office of the State Auditor is to bolster public confidence in state government finance by serving as a deterrent to fiscal mismanagement, fraud, and misuse of assets by state agencies and providers of Medicaid services. The mission is accomplished by providing adequate audit coverage of state agencies and Medicaid providers as required by statutes, regulations and contractual agreements.

Each year the Office of the State Auditor and a nationally recognized accounting firm jointly audit the State of South Carolina's Basic Financial Statements, which are prepared by the Comptroller General. The credibility of the State's Basic Financial Statements is very important in the financial community and can affect the State's bond rating. This year the Office of the State Auditor completed the audit on schedule, but, since this was the first year of a five year partnership with a new CPA firm, it was completed 15% over budget. By completing the audit on schedule the Comptroller General was able to submit the State's Comprehensive Annual Financial Report to the Government Finance Officers Association for the Certificate of Excellence in Financial Reporting.



The Single Audit Act Amendments of 1996 requires an annual audit of the State of South Carolina's Schedule of Expenditures of Federal Awards. The audit was completed on time and under budget, but missed the mailing deadline by three days. The U.S. Department of Health and Human Services accepted the audit without revision.

The Office of the State Auditor is required by statute to audit each state agency annually. These audit engagements cover all State agencies with total funds of over \$18 billion and appropriated funds of over \$5.6 billion. Funding limitations in FY 2005-06 prevented the Office of the State Auditor from auditing every state agency. The Office of the State Auditor completed audit engagements for eighty-four (84) of the one hundred and twelve (112) state departments, agencies and institutions and is on schedule to complete an audit of each state agency at least once every three years. All audits complied with applicable professional standards.

Contractual agreement with the Department of Health and Human Services requires the Office of the State Auditor to audit each Medicaid provider at least once every four years. During FY 2005-06 the Office of the State Auditor issued fifty-nine audits representing 32 of the 150 providers in the State. The engagements were completed 16% under budget. The audit reports identified adjustments to payments made to providers resulting in receivables for the Department of Health and Human Services of more than \$2.53 million.

Private sector CPA firms are important suppliers of audit services to State government. Institutions of higher learning and a number of other state government entities pay these firms to conduct the annual audit of their agencies. Statutes require that the State Auditor approve all such audit contracts. The Office of the State Auditor issues the RFP's, conducts the bid conferences and awards the contracts. This procedure insures competitive charges, responsive contractors, and professional standards of audit work. In FY 2005-06 the Office of the State Auditor was responsible for overseeing seventy audit contracts totaling over \$2 million.

The Office of the State Auditor provides expert technical assistance to other State government entities in the areas of finance and accounting. During the year the State Auditor's Office assisted numerous State agencies in procuring auditing and accounting services. In addition, the State Auditor's Office continued to serve on various State committees (e.g., SCEIS oversight committee and the Government Records Advisory Council).

For the Office of the State Auditor customer satisfaction is defined primarily by statute and Federal regulation. Our customers are the citizens of South Carolina and the elected officials representing them. It is impractical to measure their satisfaction directly. Furthermore, we believe that customer satisfaction depends on the Office of the State Auditor carrying out its mission efficiently and in accordance with professional auditing standards. Therefore, all of our audit work complies with applicable standards of the American Institute of Certified Public Accountants. The Government Finance Officers' Association awarded South Carolina the Certificate of Achievement for Excellence in Financial Reporting for the State's Comprehensive Annual Financial Report, which includes the State's Basic Financial Statements. Also indicative of this high level of professionalism is the fact that the majority of our audit staff members are either certified public accountants or working toward obtaining their certification.

Every three years the State Auditor's Office is required by Government Auditing Standards to undergo a peer review by an independent external auditor. The last peer review was in October 2003 and resulted in an unqualified opinion with no letter of comment. Another peer review is scheduled for FY 2006-07.

In FY 2005-06 the Office of the State Auditor addressed staff development policies. The level of professionalism sought for our staff requires considerable continuing education efforts within the agency and there is an expectation of our junior staff to continue with the education and development required to be certified as CPAs. Additionally, the U. S. General Accountability Office requires 40 hrs of CPE each year for auditors. This year the Office of the State Auditor took steps to improve the efficiency and effectiveness of its training program. Historically we have used internal resources to provide staff training. However, this approach is inefficient since it reduces audit effectiveness (i.e., our most experienced and senior staff are taken off of audit engagements to prepare the course materials). This year we took input from senior level staff members and hired professional trainers to present the courses.