SOUTH CAROLINA DEPARTMENT OF TRANSPORTATION
COLUMBIA, SOUTH CAROLINA

FINANCIAL STATEMENTS

YEAR ENDED JUNE 30, 2003

State of South Carolina

Office of the State Auditor

1401 MAIN STREET, SUITE 1200
COLUMBIA, S.C. 29201

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November 25, 2003

The Honorable Mark Sanford, Governor
and
Members of the South Carolina Transportation Commission
South Carolina Department of Transportation
Columbia, South Carolina

This report on the audit of the financial statements of the South Carolina Department of Transportation for the fiscal year ended June 30, 2003, 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,

Tom Wagner

Thomas L. Wagner, Jr., CPA
State Auditor

TLWjr/trb

SOUTH CAROLINA DEPARTMENT OF TRANSPORTATION

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ROGERS & LABAN, PA
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 and business-type activities, the major fund and the aggregate remaining fund information of the South Carolina Department of Transportation (the Department) as of and for the year ended June 30, 2003 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. We did not audit the financial statements of the Connector 2000 Association, Inc. (the Association), a component unit of the Department. The financial statements of the Association as of and for the year ended December 31, 2002 were audited by other auditors whose report thereon has been furnished to us, and our opinion, insofar as it relates to the amounts included for that component unit, is based solely on the report of the other auditors.

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 and the report of the other Auditor's provide a reasonable basis for our opinion.

As described in Note 1 to the financial statements, the Department's financial statements are intended to present the financial position, results of operations, and cash flows of only that portion of the funds and account groups of the State of South Carolina that is attributable to the transactions of the Department, an agency of the State, and its discretely presented component unit. They do not purport to and do not present the financial position of the State of South Carolina as of June 30, 2003, 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.

In our opinion, based on our audit and the aforementioned report of the other auditors, the financial statements referred to above present fairly, in all material respects, the financial position of the Department as of June 30, 2003 and its component unit as of December 31, 2002, and the results of its operations for the year ended June 30,2003 and the results of operations and the cash flows of its component unit for the year ended December 31, 2002 in conformity with accounting principles generally accepted in the United States of America.

1529 HAMPTON STREET, SUITE 200 • COLUMBIA, SC 29201 • (803) 779-5870 • FAX (803) 765-0072 • E-MAIL: CPA@ROGERSLABAN.COM

The Management's Discussion and Analysis on pages 3 through 9 and the budgetary comparison information are not a required part of the financial statements but are 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 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 supplementary information is presented for purposes of additional analysis and is not a required part of the financial statements. Also, 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.

The Department discovered errors in the application of accounting principles regarding the capitalization of capital assets and in the classification of certain capital assets. The required corrections of these errors were accounted for as prior period adjustments and reclassifications and are detailed in Note 22. Also in the statement of activities for the year ended June 30, 2002, general revenue of $60,241,208 from taxes and fees and expenses of $60,241,208 for allocations to other entities (Agency Fund – County Transportation Program) were not reported in error; and, in the statement of revenues, expenditures and changes in fund balances for the year ended June 30, 2002 for the State Highway Fund, expenditures of $40,082,702 for capital outlay for infrastructure for road and bridge network and revenue from other financing sources of $40,082,702 from intergovernmental payable – State agency (contribution payable) were not reported in error. The effects of the omissions on prior year amounts are also detailed in Note 22.

In accordance with Government Auditing Standards, we have also issued our report dated October 29, 2003, 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 grants. That report is an integral part of an audit performed in accordance with Governmental Auditing Standards and should be read in conjunction with this report in considering the result of our audit.

Rogers + Laban, PA

October 29, 2003

MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of the South Carolina Department of Transportation (SCDOT), we provide this *Management's Discussion and Analysis* of the Department of Transportation Financial Statements for the fiscal year ended June 30, 2003 as a narrative overview and analysis. We encourage readers to consider this information in conjunction with the Department's financial statements, which follow.

Included in these financial statements is the discretely reported information of one component unit, the *Connector 2000 Association, Inc.*, which operates the Southern Connector toll road in Greenville County under a license agreement with the Department. Component units are legally separate organizations for which the elected/appointed officials of the primary entity are financially accountable. The Department's inclusion of the Association as a component unit is done for the purpose of communicating information about its component unit as required by generally accepted accounting principles. It is not intended to create the perception that the Department has a legal or financial responsibility for the Association. The Association's financial statements are independently audited and a separate annual report with auditor's opinion dated March 10, 2003 has been issued. We refer readers to that report for more detailed information.

FINANCIAL HIGHLIGHTS

DEPARTMENT-WIDE

Net Assets - The assets of the Department exceeded its liabilities at fiscal year ending June 30, 2003 by **$9.0** billion (presented as "net assets"). Of this amount, **$205.7** million was reported as "unrestricted net assets". Unrestricted net assets represent the amount available to be used to meet the Department's ongoing obligations to citizens and creditors. The Department's component unit, Connector 2000 Association, Inc. reported a ***net deficit*** of **$32.8** million as of December 31, 2002, the close of its fiscal year.

Changes in Net Assets - The Department's total net assets increased by **$559.0** million (a **7%** increase) in fiscal year 2003. All or the activities of the Department are considered governmental activities in the Department-wide financial statements. The Department's component unit net deficit increased by **$17.2** million, **$13.7** million of which was interest expense.

Capital Assets – Capital Assets net of depreciation, which include infrastructure, were approximately **$9.7** billion at June 30, 2003 for the Department. Capital additions for the year, including **$338.3** million donated from the South Carolina Transportation Infrastructure Bank, totaled **$851.0** million. The carrying value of capital assets removed from the records this year were **$4.0** million. Capital assets of the component unit, net of depreciation were approximately **$183.0** million at December 31, 2002. The Association classified the capital costs ($191.8 million) of constructing the Southern Connector toll road, including construction period interest, as a license agreement with the Department. The Department, as legal owner of the toll highway, has recorded a like amount in its records as infrastructure. See the Capital Assets section of this management's discussion and analysis for more information about the accounting treatment of capital assets.

Long-term Debt - The Department's total long-term debt obligations increased by **$24.8** million (3.0**%**) during the current fiscal year to **$886.4** million. This change is attributable to a net decrease in bonds payable of **$20.4** million, a net increase in the amount due to the South Carolina State Infrastructure Bank of **$44.6** million, and other increases of **$.6** million.

FUND ACTIVITY

Governmental Funds - Fund Balances - As of the close of fiscal year 2003, the Department's governmental funds reported a combined ending fund balance of **$231.9** million, a decrease of **$142.3** million in comparison with the prior year. Of this total amount, **$222.2** million represents the "unreserved fund balance" which is available for spending at the Department's discretion on future road and bridge construction and maintenance or other necessary activities.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the Department of Transportation's basic financial statements. The SCDOT's basic financial statements include three components: 1) department-wide financial statements, 2) fund financial statements, and
3) notes to the financial statements. This report also contains other supplementary information
in addition to the basic financial statements themselves. These components are described below:

Department-Wide Financial Statements

The *Department-Wide Financial Statements* provide a broad overview of SCDOT's operations in a manner similar to a private-sector business. The statements provide both short-term and long-term information about the Department's financial position, which assists in assessing the Department's economic condition at the end of the fiscal year. These are prepared using the flow
of economic resources measurement focus and the accrual basis of accounting. This basically means they follow methods that are similar to those used by most businesses. They take into account all revenues and expenses connected with the fiscal year even if cash involved has not been received or paid. The department-wide financial statements include two statements:

The S*tatement of Net Assets* presents all of SCDOT's assets and liabilities, with the difference between the two reported as "net assets". Over time, increases or decreases in the Department's net assets may serve as a useful indicator of whether the financial position of the Department is improving or deteriorating.

The S*tatement of Activities* presents information showing how the Department's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will not result in cash flows until future fiscal periods (such as unused vacation leave). This statement also presents a comparison between direct expenses and program revenues for each function of the
Department.

Both of the above financial statements have separate columns for two different types of programs or activities. These two types of activities are:

Governmental Activities – The activities in this column are mostly supported by motor fuel taxes and intergovernmental revenues (federal grants). All services normally associated with SCDOT fall into this category.
Business Type Activities – This is the discretely presented component unit, Connector 2000 Association, Inc., for which SCDOT is considered financially accountable, but it has many independent qualities as well. The Association is a nonprofit corporation for which SCDOT from a legal standpoint, has no legal or financial responsibility.

The department-wide financial statements can be found immediately following this discussion and analysis.

Fund Financial Statements

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Department, like other state agencies uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the Department can be divided into two categories, governmental funds and fiduciary funds. The discretely presented component unit, Connector 2000 Association, Inc., is considered a proprietary fund. It is important to note that these fund categories use different accounting approaches and should be interpreted differently. The three categories of funds are:

Governmental Funds – Most of the basic services provided by SCDOT are financed through governmental funds. Governmental funds are used to account for essentially the same functions reported as governmental activities in the Department-wide financial statements. However, unlike the Department-wide financial statements, the governmental fund financial statements focus on near-term inflows and outflows of spendable resources. They also focus on the balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating the Department's near-term financing requirements. This approach is known as using the flow of current financial resources measurement focus and the modified accrual basis of accounting. These statements provide a detailed short-term view of the Department's finances that assists in determining whether there will be adequate financial resources available to meet the current needs of the Department.

Because the focus of governmental funds is narrower than that of the Department-wide financial statements, it is useful to compare the information presented in governmental funds with similar information presented for governmental activities in the Department-wide financial statements. By doing so, readers may better understand the long-term impact of the Department's near-term financing decisions. Both the governmental funds balance sheet and the governmental funds statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and the Departmental activities. These reconciliations are presented on the page immediately following each governmental fund financial statement.

The Department has two governmental funds which are presented in separate columns in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances. The Department's governmental funds are – the General Fund, consisting of funds appropriated from the State General Fund for public transportation and the Special Revenue Fund which records expenditures of revenues that are restricted to specific programs or projects.

The basic governmental funds financial statements can be found immediately following the government-wide statements.

Fiduciary Funds – These funds are used to account for resources held for the benefit of parties outside SCDOT. Fiduciary funds are not reflected in the Department-wide financial statements because the resources of these funds are not available to support the Department's own programs. Fiduciary funds financial statements use the accrual basis of accounting. The Department's fiduciary funds are the County Transportation Program Fund, The Right of Ways Fund and the Special Deposits Fund.

The basic fiduciary funds financial statements can be found immediately following the Governmental funds financial statements.

Notes to the Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the Department-wide and the fund financial statements. The notes to the financial statements can be found immediately following proprietary fund financial statements.

Required Supplementary Information and Combining Statement

The basic financial statements are followed by a section of required supplementary information. In the Department's case, this section includes a budgetary comparison schedule for the *general fund*, which includes comparisons of original budget to final budget to actual outflow (expenditures) on a budgetary basis. Also included is a combining statement of changes in assets and liabilities – agency funds.

DEPARTMENT-WIDE FINANCIAL ANALYSIS

Net Assets

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. The Department's assets (all classified as governmental activities) exceeded liabilities by **$9.0** billion at the close of business on June 30, 2003 (See **Table A-1** for a summary of net assets for fiscal years 2002-2003 and 2001-2002). The largest portion of the Department's net assets (98.0**%**) reflects its investment in infrastructure and other capital assets such as land, buildings, and equipment less any related debt used to acquire those assets that is still outstanding. The Department uses these capital assets to fulfill its primary mission to provide a safe and efficient transportation system for the state of South Carolina. Consequentially, these assets are not available for future spending. Although the Department's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

At June 30, 2003, a very minimal portion of the Department's net assets ($161 thousand) represents resources that are subject to external restrictions on how they may be used. The remaining balance of net assets (2% or **$205.7** million) is unrestricted and may be used to meet the Department's ongoing obligations to citizens and creditors. Internally imposed designations of resources are not presented as restricted net assets. At the end of the current fiscal year, the Department is able to report positive balances in all three categories of net assets.

Table A-1
SCDOT Net Assets
(expressed in millions)

	Governmental Activities			
	2002 (as restated-Note 22)		2003	
Current Assets	$	269.2	$	333.1
Capital Assets		8,975.6		9,700.0
Other Assets		210.9		10.0
Total Assets	**$**	**9,455.7**	**$**	**10,043.1**
Current Liabilities	$	170.4	$	175.8
Non-current Liabilities		805.1		828.1
Total Liabilities	**$**	**975.5**	**$**	**1,003.9**
Net Assets:				
Invested in Capital Assets, Net of Related Debt	$	8,133.4	$	8,833.4
Restricted		205.2		0.1
Unrestricted		141.6		205.7
Total Net Assets	**$**	**8,480.2**	**$**	**9,039.2**
Total Liabilities & Net Assets	**$**	**9,455.7**	**$**	**10,043.1**

Changes in Net Assets

The Department's net assets increased by **$559.0** million, or **6.6%.** Approximately **$338.3** million of this increase came from the donation of infrastructure capital assets to the Department by the South Carolina Transportation Infrastructure Bank, a sister state agency established to finance major transportation projects. The balance of the increase in net assets can be attributed to an increase in self-constructed infrastructure assets net of accumulated depreciation. As stated earlier, the primary purpose of the Department is to build and maintain these infrastructure assets.

In 2003, the Department's program revenues exceeded expenses by **$96.6** million. A breakdown of the $1.3 billion in gross revenues reveals that motor fuel taxes represented **36%**, while **34%** resulted from Federal highway allocations and grants, **26%** were in the form of contributed infrastructure assets and the balance, **4%**, of revenues came from various sources including toll revenues, motor vehicle fees and interest income.

Table A-2 presents a breakdown of these revenues and expenses for fiscal year 2002-2003 with comparative figures for the prior year.

Table A-2

SCDOT Changes in Net Assets
(Expressed in millions)

	Governmental Activities			
Revenues:	2002 (as restated - Note 22)	% of Revenue	2003	% of Revenue
Program Revenues:				
Capital Grants and Contributions	$ 691.9	55%	$ 697.6	54%
Operating Grants and Contributions	82.7	6%	76.0	6%
Charges for Services	22.1	2%	39.0	3%
General Revenues:				
Motor Fuel Taxes	446.3	35%	458.8	36%
State Appropriations	0.5	0%	0.4	0%
Investment Earnings	19.0	2%	8.2	1%
Total Revenues	**$ 1,262.5**	**100%**	**$ 1,280.0**	**100%**
Expenses:				
Public Transportation	608.9		716.1	
Total Expenses	**$ 608.9**		**$ 716.1**	
Increase in Net Assets Before Transfers	$ 653.6		$ 563.9	
Transfers to State General Fund	5.0		4.9	
Changes in Net Assets	**$ 648.6**		**$ 559.0**	
Net Assets, Beginning of Year	7,831.6		8,480.2	
Net Assets, End of Year	**$ 8,480.2**		**$ 9,039.2**	

FINANCIAL ANALYSIS OF THE DEPARTMENT'S INDIVIDUAL FUNDS

As noted earlier, the Department uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental Funds
The focus of the Department's governmental funds is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the Department's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year. As of the end of the current fiscal year, the Department's governmental funds reported ending fund balances of **$231.9** million, a decrease of **$142.3** million in comparison with the prior year. **95.8%** of these total fund balances or **$222.2** million constitute unreserved fund balances, which are available for spending in the coming year. The remainder of fund balance is reserved to indicate that it is not available for new spending because it has already been committed 1) to bond funded projects (**$80.1** thousand), 2) to pay debt service (**$81.6** thousand), for long-term receivables (**$8.7** million), and to purchase right-of way (**$774** thousand).

GENERAL FUND BUDGETARY HIGHLIGHTS

Not all revenues and expenditures of the Department's *state highway fund* are budgeted and, therefore, a legal operating budget is not adopted for this fund. Budgetary analysis is not provided for the state highway fund.

All of the activity in the Department's *general fund,* which represents only .05% of total revenues, is funded by annual appropriations for public transportation by the General Assembly. The appropriation as enacted becomes the legal operating budget for the general fund. The difference between the original budget and the final amended budget is **$41.6** thousand and represents budget reductions initiated by central state government as part of statewide budget cuts. All of the balance of general funds available was expended creating no variance between final budget and actual.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The Department's investment in capital assets for its governmental activities as of June 30, 2003, amounts to **$11.6** billion, less accumulated depreciation of **$1.9** billion, leaving a net book value of **$9.7** billion. This investment in capital assets includes land, buildings, improvements, equipment, infrastructure and construction in progress. Infrastructure assets (**$9.4** billion, net) are items that are normally stationary in nature and can be preserved for a significantly longer period then most capital assets. In the case of the Department, infrastructure assets are classified into **three networks**: <u>roads</u>, <u>bridges</u> and <u>right of way</u>. Cost or estimated cost of infrastructure and related depreciation were recorded retroactively back to the year 1914. The Department has chosen to depreciate Infrastructure assets (excluding right of way). **Table A-3** summarizes capital assets at June 30, 2003 and June 30, 2002.

Table A-3
SCDOT Capital Assets
(Expressed in millions)

	Primary Government			
	2002 (as restated -Note 22)		2003	
Land	$	3.7	$	4.4
Building and Improvements		53.5		59.4
Furniture and Equipment		197.3		193.6
Infrastructure				
Right of Way		511.1		601.0
Roads and Bridges		7,018.9		7,595.8
Construction in Progress		3,007.4		3,167.5
Total Cost	$	10,791.8	$	11,621.7
Less Accumulated Depreciation		1,816.2		1,921.6
Net Capital Assets	**$**	**8,975.6**	**$**	**9,700.1**

The total increase in the Department's investment in capital assets for the current fiscal year was about **8.0%** in terms of net book value. However, actual expenditures to purchase or construct capital assets were **$513.0** million for the year. **$338.3** million in infrastructure assets were constructed by and donated to the Department by the South Carolina Infrastructure State Bank. Depreciation charges for the year totaled **$122.6** billion.

Debt Administration

The authority of the Department to incur debt is described in Sections 57-11-210,etseq.of the South Carolina Code and continued and amended by Section 11-27-30 thereof, authorizing the issuance of general obligation State Highway Bonds for highway construction and related purposes backed by the full faith and credit of the state. State Highway Bonds are additionally secured by a pledge of so much of the revenues as may be made applicable by the General Assembly for state highway purposes from gasoline and fuel oil taxes and motor vehicle license fees.

The Department's total bonded debt decreased by **$20.4** million during the current fiscal year, to $**630.7** million. The net decrease is primarily attributed to (1) scheduled bond payments of **$21.9** million; (2) the issue on June 1, 2003, of **$46.1**million in general obligations State Capital Improvement Refunding Bonds, Series 2003B; (3) the advance refunding and defeasence of **$39.7** million in Series 1996B bonds; and (4) the recording of the difference in the reacquisition price and net carrying value of the old debt, **$5.7 million**, for periodic amortization. Other long-term debt includes **$235.4** million due to the SC Infrastructure State Bank and various local governments for financial assistance on transportation projects managed by those entities (net increase for the year of **$44.6** million); and accrued compensated absences of **$19.7** million (net increase for the year of **$.3** million). Due within one year for all long-term debt is **$58.2** million.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

During the period 1998-2003 we have experienced significant increases in Federal highway funding. Federal highway funding is authorized in six (6) year increments because of the long-range nature of highway construction commitments. The current funding legislation, the Transportation Equity Act for the 21st Century (TEA-21), expires on September 30, 2003.

A new Federal authorization bill for the 2004-2009 Federal fiscal years, the "Safe, Accountable, Flexible, and Efficient Transportation Act of 2003" (SAFETEA), is currently being considered by Congress and the President. The bill would increase core federal programs by 19% from 2004-2006, and then hold those funding levels flat from 2006 through 2009. These projected increases plus a provision that would guarantee that states would receive at least 95 cents of each dollar in federal fuel taxes collected within their boundaries will enhance the ability of SCDOT to construct and maintain roads and bridges classified in the federal highway system.

State revenues including motor fuel taxes, however, are projected to increase in fiscal year 2003-2004 by a modest 2%, which would barely match the inflation rate. For several years, motor fuel tax revenues have not increased at a rate sufficient to match the increase in transportation costs. State leaders have not granted an increase in state fuel tax rates since 1987. Because of these factors, maintenance of roads and bridges that are not in the federal highway system has not kept up with needs. During fiscal year 2003-2004 the Department is making a concerted effort to address some of these critical maintenance needs through an aggressive, sophisticated cash management program. Additional state funding will be needed soon to prevent further significant deterioration of the state's highway system, which will lead to greater costs to repair and renovate in the future.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the Department of Transportation finances for all of the Department's taxpayers, customers, and investors and creditors. This financial report seeks to demonstrate the Department's accountability for the money 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 Transportation
Office of Financial Management
955 Park Street, Suite 304
Columbia, South Carolina 29202-0191

The Department's component unit, Connector 2000 Association, Inc. issues its own separately audited financial statements. These statements may be obtained by directly contacting Southern Connector at 880 S. Pleasantburg Drive, Suite 2D, Greenville, SC 29607.

SOUTH CAROLINA DEPARTMENT OF TRANSPORTATION

STATEMENT OF NET ASSETS
JUNE 30, 2003

	Primary Entity Governmental Activities	Component Unit
ASSETS		
Current assets:		
Cash and cash equivalents	$ 143,584,759	$ 369,290
Restricted assets:		
Cash and cash equivalents		1,096,926
Receivables:		
Federal government	98,439,870	
State agencies	62,339,570	
Local governments	8,745,326	
Other entities	7,594,659	
Accrued interest receivable	1,448,239	
Prepaid expenses	4,394,862	221,562
Inventories	6,470,230	
Total current assets	333,017,515	1,687,778
Non-current assets:		
Restricted assets:		
Cash and cash equivalents	161,744	3,631,159
Investments		20,292,531
Accrued interest receivable		3,649
Accounts receivable		37,400
Total restricted assets	161,744	23,964,739
Receivables, net of current portion:		
Local governments	5,310,534	
Other entities	3,422,505	
Other assets	774,475	
Capital assets, net of accumulated depreciation	9,700,053,095	183,051,195
Bond issuance costs, net of accumulated amortization	394,901	4,545,215
Total non-current assets	9,710,117,254	211,561,149
TOTAL ASSETS	$ 10,043,134,769	$ 213,248,927

See accompanying Notes to Financial Statements.

SOUTH CAROLINA DEPARTMENT OF TRANSPORTATION

STATEMENT OF NET ASSETS (CONTINUED)
JUNE 30, 2003

	Primary Entity Governmental Activities	Component Unit
LIABILITIES AND NET ASSETS		
Liabilities:		
Current liabilities:		
Liabilities payable from restricted assets:		
Requisitions payable	$ -	$ 117,494
Accrued interest payable		1,765,750
Accrued early completion bonus		1,850,000
Total		3,733,244
Bonds payable	22,966,377	
Accrued interest payable	6,808,538	
Accounts payable/other liabilities	69,164,779	48,357
Intergovernmental payables:		
Due to State agencies	24,857,485	
Contract retainages payable	2,719,782	
Accrued payroll and related liabilities	15,116,253	
Due to Agency Fund - County Transportation Program	10,271,611	
Due to General Fund of the State	2,687	
Capital leases payable	132,504	
Accrued compensated absences	13,537,469	
Deferred revenue	10,190,249	55,717
Total current liabilities	175,767,734	3,837,318
Noncurrent liabilities:		
Bonds payable, including unamortized premium and net of current portion and unamortized discounts and deferred loss on refunding of bonds	607,763,291	242,177,477
Intergovernmental payable:		
Due to State agency, net of current portion	213,874,813	
Capital leases payable, net of current portion	363,693	
Accrued compensated absences, net of current portion	6,148,866	
Total noncurrent liabilities	828,150,663	242,177,477
TOTAL LIABILITIES	1,003,918,397	246,014,795
Net assets:		
Invested in capital assets, net of related debt (deficit)	8,833,376,034	(16,589,326)
Restricted:		
Debt service (deficit)	81,670	(184,387)
Bond proceeds for capital projects and other purposes	80,074	1,792,208
Unrestricted:		
Balance (deficit)	205,678,594	(17,784,363)
TOTAL NET ASSETS (DEFICIT)	9,039,216,372	(32,765,868)
TOTAL LIABILITIES AND NET ASSETS	$ 10,043,134,769	$ 213,248,927

See accompanying Notes to Financial Statements.

SOUTH CAROLINA DEPARTMENT OF TRANSPORTATION

STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2003

		Program Revenues			Net (Expenses) Revenues and Changes in Net Assets	
Functions/Programs	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Component Unit
Primary entity:						
Public transportation	$ 716,108,878	$ 39,045,269	$ 76,012,021	$ 697,612,429	$ 96,560,841	$ -
Component unit:						
Toll operations	$ 21,499,936	$ 3,083,441	$ -	$ -		(18,416,495)
Total net (expenses) revenues					96,560,841	(18,416,495)
General revenues:						
State appropriations					444,268	
Taxes and fees					458,768,249	
Interest/investment income					8,200,916	1,190,655
Total general revenues					467,413,433	1,190,655
Transfers:						
Transfers to General Fund of the State					(4,940,198)	
Changes in net assets					559,034,076	(17,225,840)
Net assets - Beginning, as restated					8,480,182,296	(15,540,028)
Net assets - Ending					$ 9,039,216,372	$ (32,765,868)

See accompanying Notes to Financial Statements.

SOUTH CAROLINA DEPARTMENT OF TRANSPORTATION

BALANCE SHEET - GOVERNMENTAL FUNDS
JUNE 30, 2003

ASSETS	General Fund	State Highway Fund	Totals
Current assets:			
Cash and cash equivalents	$ 2,454	$ 143,582,305	$ 143,584,759
Receivables:			
Federal government		98,439,870	98,439,870
State agencies		62,339,570	62,339,570
Local governments		8,745,326	8,745,326
Other		7,594,659	7,594,659
Accrued interest receivable		1,448,239	1,448,239
Prepaid expenses		4,394,862	4,394,862
Inventories		6,470,230	6,470,230
Total current assets	2,454	333,015,061	333,017,515
Non-current assets:			
Restricted assets:			
Cash and cash equivalents		161,744	161,744
Total restricted assets		161,744	161,744
Receivables, net of current portion			
Local governments		5,310,534	5,310,534
Other		3,422,505	3,422,505
Other assets		774,475	774,475
Total non-current assets		9,669,258	9,669,258
TOTAL ASSETS	$ 2,454	$ 342,684,319	$ 342,686,773
LIABILITIES AND FUND BALANCE			
Liabilities:			
Current liabilities:			
Accounts payable/other liabilities	$ -	$ 69,164,779	$ 69,164,779
Intergovernmental payables:			
Due to State agencies		3,281,102	3,281,102
Contract retainages payable		2,719,782	2,719,782
Accrued payroll and related liabilities		15,116,253	15,116,253
Due to Agency Fund - County Transportation Program		10,271,611	10,271,611
Due to General Fund of the State	2,454	233	2,687
Deferred revenue		10,190,249	10,190,249
Accrued interest payable		77,961	77,961
TOTAL LIABILITIES	2,454	110,821,970	110,824,424
Fund Balance:			
Reserved:			
Long-term receivables		8,733,039	8,733,039
Other assets		774,475	774,475
Debt service		81,670	81,670
Bond proceeds for capital projects and other purposes		80,074	80,074
Unreserved		222,193,091	222,193,091
TOTAL FUND BALANCES		231,862,349	231,862,349
TOTAL LIABILITIES AND FUND BALANCES	$ 2,454	$ 342,684,319	$ 342,686,773

See accompanying Notes to Financial Statements.

SOUTH CAROLINA DEPARTMENT OF TRANSPORTATION

BALANCE SHEETS - GOVERNMENTAL FUNDS (CONTINUED)
JUNE 30, 2003

RECONCILIATION TO THE STATEMENT OF NET ASSETS:

Fund balances - governmental funds		$ 231,862,349
Amounts reported for governmental activities in the statement of net assets are different because:		
Assets are capitalized and depreciated or amortized in the statement of net assets and are charged to expenditures in the governmental fund:		
Capital assets, net of accumulated depreciation	$ 9,700,053,095	
Bond issuance costs, net of accumulated amortization	394,901	9,700,447,996
Liabilities are not due and payable in the current period, therefore, are not reported in the governmental fund:		
Bonds payable including unamortized premium and net of unamortized deferred loss on refunding of bonds	(630,729,668)	
Intergovernmental payable:		
Due to State agency	(235,451,196)	
Capital leases payable	(496,197)	
Accrued compensated absences	(19,686,335)	
Accrued interest payable	(6,730,577)	(893,093,973)
Net assets of governmental funds		$ 9,039,216,372

See accompanying Notes to Financial Statements.

SOUTH CAROLINA DEPARTMENT OF TRANSPORTATION

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCES - GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2003

	General Fund	State Highway Fund	Totals
REVENUES:			
Taxes and fees	$ -	$ 398,030,790	$ 398,030,790
Restricted taxes		60,737,459	60,737,459
State appropriations	444,268		444,268
Federal grants		431,886,481	431,886,481
Reimbursements from Agency Fund - County Transportation Program		3,399,301	3,399,301
Interest/investment income		8,200,916	8,200,916
Sales of goods and fees for services		2,196,406	2,196,406
Participation agreement/project revenues		30,155,241	30,155,241
Other revenues		3,294,321	3,294,321
TOTAL REVENUES	444,268	937,900,915	938,345,183
EXPENDITURES:			
Current:			
General administration		27,231,583	27,231,583
Engineering		32,094,258	32,094,258
Toll facilities		3,303,157	3,303,157
Public transportation	444,268	17,275,218	17,719,486
Highway maintenance		383,258,698	383,258,698
Capital outlay:			
Land and improvements		752,000	752,000
Right of ways land		66,893,787	66,893,787
Construction in progress			
Infrastructure - road and bridge network		421,421,049	421,421,049
Other		2,893,800	2,893,800
Buildings and improvements		5,548,000	5,548,000
Equipment and furniture		7,066,998	7,066,998
Vehicles		4,727,193	4,727,193
Debt service:			
Principal		43,514,024	43,514,024
Interest		35,693,003	35,693,003
Other		413,379	413,379
Allocations to other entities:			
State agency		22,984,451	22,984,451
Agency Fund - County Transportation Program		70,237,459	70,237,459
TOTAL EXPENDITURES	444,268	1,145,308,057	1,145,752,325
EXCESS OF REVENUES OVER (UNDER) EXPENDITURES	-	(207,407,142)	(207,407,142)
OTHER FINANCING SOURCES (USES):			
Proceeds from refunding bonds issued		46,080,000	46,080,000
Premium on bonds issued		669,284	669,284
Proceeds from capital lease		459,320	459,320
Proceeds from intergovernmental payable - State agency (contribution payable)		65,959,644	65,959,644
Proceeds from sale of capital assets		3,145,003	3,145,003
Remitted to General Fund of the State		(4,940,198)	(4,940,198)
Payment to refunded bonds escrow agent		(46,340,000)	(46,340,000)
TOTAL OTHER FINANCING SOURCES (USES)		65,033,053	65,033,053
EXCESS OF REVENUES AND OTHER FINANCING SOURCES OVER (UNDER) EXPENDITURES AND OTHER FINANCING SOURCES (USES)		(142,374,089)	(142,374,089)
FUND BALANCES, beginning of year		374,236,438	374,236,438
FUND BALANCES, end of year	$ -	$ 231,862,349	$ 231,862,349

See accompanying Notes to Financial Statements.

SOUTH CAROLINA DEPARTMENT OF TRANSPORTATION

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE - GOVERNMENTAL FUND (CONTINUED) FOR THE YEAR ENDED JUNE 30, 2003

RECONCILIATION TO THE STATEMENT OF ACTIVITIES:

Revenues and other financing sources (uses) over (under) expenditures for the governmental fund	$ (142,374,089)
Amounts reported for governmental activities in the statement of activities are different because:	
Costs of capital assets are reported as expenditures in the governmental fund and are reported as capital asset additions in the statement of net assets	442,883,863
Costs of donated capital assets for right of ways land and infrastructure - road and bridge net work are reported in the statement of activities and are not reported in the governmental fund	341,737,969
Depreciation of capital assets is reported as expenses in the statement of activities	(122,558,987)
Costs of issuance of bonds are reported as expenditures in the governmental fund and are reported as assets in the statement of net assets	396,729
Amortization of the costs of issuance is reported as expenses in the statement of activities	(1,828)
Costs of deferred losses on refunding of bonds are reported as expenditures in the governmental fund and are reported as a reduction of liabilities in the statement of net assets	5,708,911
Amortization of deferred losses on refunding of bonds is reported as expenses in the statement of activities	(154,295)
Decrease in accrued interest payable is reported as a reduction of expenses in statement of activities	1,350,162
Proceeds from bond financing are reported as other financing sources in the governmental fund and are reported as an increase in liabilities in the statement of net assets	(46,749,284)
Repayments of long-term debt are reported as expenditures and as other financing uses (escrow deposit for advance refundings of bonds) in governmental fund and are reported as a reduction of liabilities in the statement of net assets:	
Bonds payable	61,600,000
Intergovernmental payable:	
Due to State agency	21,411,799
Capital leases	177,225
Increase in accrued compensated absences is reported as expenses in the statement of activities	(344,886)
Costs less accumulated depreciation of capital assets disposed of are reported as expenses in the statement of activities	(4,049,213)
INCREASE IN NET ASSETS	$ 559,034,076

See accompanying Notes to Financial Statements.

SOUTH CAROLINA DEPARTMENT OF TRANSPORTATION

STATEMENT OF FIDUCIARY NET ASSETS
JUNE 30, 2003

		Agency Funds
ASSETS:		
Cash and cash equivalents	$	107,772,319
Accrued interest receivable		1,148,157
Due from State Highway Fund		10,271,611
Total assets	$	119,192,087
LIABILITIES:		
Accounts payable/other liabilities	$	16,241,308
Deposits for right of ways		327,882
Special deposits and bonds		415,812
Funds held for counties		102,207,085
Total liabilities	$	119,192,087

See accompanying Notes to Financial Statements.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Reporting Entity

The South Carolina Department of Transportation (the Department) was established pursuant to Section 57-1-20 of the Code of Laws of South Carolina as an administrative agency of State government, comprised of a Division of Mass Transit; a Division of Construction, Engineering and Planning; and a Division of Finance and Administration. The Department is responsible for the planning, construction, maintenance and operation of the highway system of the State of South Carolina and the coordination of statewide mass transit activities.

The Department is governed by the South Carolina Transportation Commission, which is comprised of seven members, six of whom are elected by the Legislative Delegations of each of the State's Transportation Districts. These Transportation Districts coincide with the State's Congressional Districts. One at-large member is appointed by the Governor and, upon confirmation by the South Carolina Senate, serves as Chairman of the Commission. The Commission serves as a general policy-making body for the various functions and purposes of the Department as prescribed by law. The Commission defines policies that are to be administered by the Director.

The core of a financial reporting entity is normally the primary government, which has a separately elected governing body. The Department is reported as part of the primary government of the State of South Carolina. An organization other than a primary government may serve as a nucleus for a reporting entity when it issues separate financial statements. The Department is identified herein as such a primary entity. As required by generally accepted accounting principles, the financial reporting entity includes both the primary entity and all of its component units. Component units are legally separate organizations for which the elected officials of the primary entity are financially accountable. In turn, component units may have component units. The Department has determined it has one component unit, the Connector 2000 Association, Inc. (the Association).

A primary government or entity is financially accountable if it appoints a voting majority of the organization's governing body, 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 entity. The primary 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 dependent on the primary entity that holds one or more of the following powers:

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

Based on the above described fiscal dependency criteria, the Department has determined it is not a component of another entity and the Connector 2000 Association, Inc. ("The Association") is a component unit of the Department under Statement 14 of the Governmental Accounting Standards Board. This financial reporting entity includes only the Department (a primary entity) and its component unit.

The Association is considered a component unit of the Department because the Department initially fixed the toll rates for the Southern Connector in Greenville County, South Carolina and, after consultation with the Association, has the right (but not the obligation) to revise the toll rates from time to time to rates which are not less than 90% and not more than 120% of the optimum toll rates as estimated by an independent traffic consultant retained by the Association. Rates set by the Department must satisfy the applicable revenue covenants contained in the Association's financing documents. Also, the Association is governed by a Board of Directors approved by the Department.

The Association is a South Carolina nonprofit corporation organized as a "public benefit corporation" under the South Carolina Nonprofit Corporation Act of 1994. The Articles of Incorporation of the Association were originally filed with the South Carolina Secretary of State on January 12, 1996 and were amended by a filing on March 5, 1997. The Internal Revenue Service has issued a letter dated October 20, 1997 determining that the Association is an exempt organization that is not a private foundation under Section 501(c)(3) of the Internal Revenue Code. The Association was formed to finance, acquire, construct and operated turnpikes, highway projects and other transportation facilities pursuant to Section 57-3-200 of the Code of Laws of South Carolina.

The Department's inclusion of the Association as a component unit is done for the purpose of communicating information about its component unit as required by generally accepted accounting principles, and the Association's relationship with the Department. It is not intended to create the perception that the Department and the Association are one legal entity. From a legal standpoint, the State of South Carolina and the Department have only a contractual relationship with the Association. This contractual relationship came about as a result of the Association's submittal of the successful proposal to construct and operate the Southern Connector. In addition, the Supreme Court of South Carolina has held that the State of South Carolina and the Department are not a joint owner in the Association, and, accordingly, have no legal or financial responsibility for the Association.

Although the Association was formed in 1996, its first financial activity occurred in February, 1998. At that time, the Association entered into a license agreement (the License Agreement) with the Department that grants the Association rights and obligations to finance, acquire, construct and operate an approximately 16 mile fully controlled access toll highway (the Southern Connector) and to construct the South Carolina Highway 153 Extension (the SC 153 Extension) (collectively, the Projects). Toll road revenue bonds were issued on February 11, 1998 to finance the construction of the Southern Connector. Governmental accounting standards require that the reporting entity's financial statements include the year-end statements of the component unit which falls within the reporting entity's fiscal year.

For the purpose of applying generally accepted accounting principles (GAAP) to its activities, the Association's management has determined that the Association is a governmental entity. The Governmental Accounting Standards Board (GASB), which has jurisdiction over accounting and financial reporting standards applicable to governmental entities, and the Financial Accounting Standards Board (FASB), which has jurisdiction over such standards applicable to nongovernmental entities, have agreed on a definition of a governmental entity that is to be used when determining whether governmental GAAP is applicable. Since (a) the Association is a public benefit corporation, (b) the members of the Association's Board of Directors must be approved by the Department and (c) upon dissolution of the Association, all of the Association's net assets will revert to the Department, the Association meets the criteria set forth in the definition of a governmental entity. Accordingly, the accompanying financial statements of the Association have been prepared in accordance with GAAP applicable to governmental unit proprietary funds.

The financial statements of a component unit are blended in as though it were part of the primary entity if it is, in substance, part of its operations. Since the Association is not a part of the operations of the Department, the Association's financial activity is presented discretely outside of the Department's primary entity financial statements. A complete copy of the Association's financial statements can be obtained from Connector 2000 Association, Inc., c/o Sinkler & Boyd, P.A., 15 South Main Street, Suite 500, Greenville, South Carolina 29601.

The Department is granted an annual appropriation for mass transit operating purposes as authorized by the South Carolina 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 laws of the State and the policies and procedures specified by the State for State agencies and institutions are applicable to the activities of the Department. Generally, all State departments, agencies, and colleges are included in the State’s reporting entity, which is the primary government of the State of South Carolina. These entities are financially accountable to and fiscally dependent on the State. Although the Department operates somewhat autonomously, it lacks full powers. In addition, the Governor and/or the General Assembly appoints most of its board members and budgets a significant portion of its funds.

The reporting entity is part of the State of South Carolina primary government unit and is included in the Comprehensive Annual Financial Report of the State of South Carolina. The accompanying financial statements present the financial position and the results of operations and cash flows of only that portion of the funds of the State of South Carolina that is attributable to the transactions of the Department and its component unit and do not include any other funds or component units of the State of South Carolina.

Department-Wide And Fund Financial Statements

The financial statements of the Department and its component unit 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. In accordance with GASB Statement No. 20, Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting, the Association elected to apply only those standards issued by the Financial Accounting Standards Board on or before November 30, 1989.

Department-Wide Financial Statements

The Department-wide financial statements are prepared on the accrual basis method of accounting and include a “Statement of Net Assets” which discloses the financial position of the Department; and a “Statement of Activities”, which demonstrates the degree to which the direct expenses of the Department’s programs are offset by program revenues.

The Department-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the nonfiduciary activities of the primary government.

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.

Fund Financial Statements

The Department uses funds to report its financial position and results of operations. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

Governmental Funds:

Governmental funds are those through which most governmental functions typically are financed and are used to account for all or most of a government's general activities, including the collection and disbursement of earmarked monies. 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 difference between the assets and liabilities is fund balance.

General Fund – The General Fund accounts for all activities except those required to be accounted for in another fund. For the Department, the general fund consists of funds appropriated from the State General Fund for public transportation.

State Highway Fund – The State Highway Fund generally records the expenditure of revenues that are restricted to specific programs or projects. The special revenue fund accounts for Federal grant program revenues, taxes levied with statutorily defined distributions, and other resources restricted as to purpose. Charges for and costs of operations of vehicles and other equipment utilized for road and bridge network projects are reported in this fund. The State Highway Fund was established pursuant to Section 57-11-20 of the Code of Laws of South Carolina. This Fund accounts for, among others, gasoline tax, including the 2.66 cents per gallon that is allocated to the County Transportation Program Agency Fund; and, other special imposts upon highway users for the construction and maintenance of highways and bridges and for other operations of the Department; and, 20% of motor vehicle license fees as provided by Section 56-3-910 of the South Carolina Code of Laws. This fund also accounts for revenue from the sales of goods and services and from participation agreements between the Department and other entities for the sharing of costs of construction projects. Revenues from participation agreement and other project contracts are recognized as earned based on the percentage of completion method. The unearned portion is reflected as deferred revenue in the liability section of the financial statements of the Department until earned.

Fiduciary Funds:

Fiduciary funds are used to account for assets held by the Department in a trustee capacity or as an agent for individuals, private organizations, other governmental units and/or other funds. The Department uses agency funds which are purely custodial (assets equal liabilities) and thus do not involve the measurement of results of operations. The agency funds used by the Department include the following:

- The County Transportation Program Fund was established pursuant to Section 12-28-2740 of the South Carolina Code of Laws to provide for the receipts from distribution and use of the 2.66 cents per gallon gasoline tax collected by the South Carolina Department of Revenue and remitted to the Department. In addition to the gasoline tax, the Department is required to transfer $9,500,000 annually from the State Highway Fund to the Program. Each county has a county transportation committee that is appointed by the county legislative delegation to administer the use of these funds. Based on the legally prescribed allocation formula, these monies are either paid directly to the counties for infrastructure projects that are administered by the counties or to vendors on behalf of the counties for expenditures incurred on projects that the county transportation committees have contracted the Department to administer.

- The Right of Ways Fund is used to account for payments for the purchase of right of ways land which has been contested by the property owner. In those cases, the property owner is paid 75% of the offer and 25% of the offer is transferred to the county clerk of court. Current year's activity represents receipt of funds from various clerks of court and disbursement to property owners upon settlement of contested cases.

- The Special Deposits Fund is used to account for various funds that are collected from other governments or agencies and outside parties. These funds are held until resolution of various matters, such as anti-trust violations, oversize and overweight charges and other similar items that occur.

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The Department-wide financial statements are reported using the economic resources measurement focus and the accrual basis 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 of accounting. Revenues are recognized as soon as they are both measurable and available. "Measurable" means that the amount of the transaction can be determined and "available" means collectible within the current period or soon enough thereafter to be used to pay obligations of the current period. 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 government considers revenues to be available if they are collected within one year of the end of the current fiscal year. Expenditures generally are recorded when a liability is incurred, as under accrual accounting.

Financial resources of fiduciary funds are reported using the economic resources measurement focus and the accrual basis of accounting.

Management of the Association has determined that its activities are properly accounted for as a proprietary enterprise fund, since its intent is that the costs of providing and operating the Southern Connector will be recovered primarily through the tolls charged to the Southern Connector users. The Association uses the accrual basis of accounting in order to recognize the flow of economic resources. Under this basis, revenues are recognized in the period in which they are earned, expenses are recognized in the period in which they are incurred, and depreciation and amortization of assets are recognized.

The Master Indenture of Trust and supplements (the Trust Agreement) related to the Series 1998A, 1998B and 1998C Bonds; require that the Association adopt governmental GAAP. The Trust Agreement also requires that certain funds and accounts be established and maintained. The Association consolidates these funds and accounts for the purpose of enterprise fund presentation in its external financial statements.

Revenues – Exchange and Non-Exchange Transactions

Revenues resulting from exchange transactions, in which each party gives and receives essentially equal value, are 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 Department on a reimbursement basis. On a modified accrual basis, revenue from nonexchange transactions must be available before it can be recognized.

Budget Policy

All of the activity in the Department's general fund is funded by annual appropriations for public transportation by the General Assembly. The appropriation as enacted becomes the legal operating budget for the general fund. A budget versus actual comparison for the State highway fund is not presented as required supplementary information since all revenues and expenditures of this fund are not budgeted.

Cash and Cash Equivalents

The amounts shown in the financial statements as "cash and cash equivalents" of the Department represent petty cash, 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. The amounts shown in the financial statements as "cash and cash equivalents" of the Association represent cash on deposit in banks and funds invested in open-end money market mutual funds.

Most State agencies, including the Department, participate in the State's internal cash management pool. Because the cash management pool operates as a demand deposit account, amounts invested in the pool are classified as cash and cash equivalents. 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 pertaining to the State's internal cash management pool including investments held by the pool, see the deposits disclosures in Note 2.

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 records 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/investment earnings are allocated based on the percentage of the Department's accumulated daily interest receivable to the income receivable of the pool. Reported income includes interest earnings at the stated 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.

Some State Treasurer accounts are not included in the State's internal cash management pool because of restrictions on the use of the funds. For those accounts, cash equivalents include investments in short-term highly liquid securities having an initial maturity of three months or less at the time of acquisition. At year end, the Department held no short term investments.

The Association considers all investments with maturities of three months or less when purchased to be cash equivalents. The amounts shown in the financial statements as "cash and cash equivalents" of the Association represent cash on deposit in banks and funds invested in open-end money market mutual funds.

Investments – Component Unit

The Trust Agreement requires that all bond proceeds received by the Association be held in trust to be expended in accordance with the indenture guidelines. All monies held in trust that are not insured by the Federal Deposit Insurance Corporation (FDIC) must be secured by and/or invested in investment securities as defined in the Trust Agreement. Investment securities include, but are not limited to, direct obligations of, or obligations guaranteed by, the United States of America or an agency thereof. The Association accounts for its investments at fair value in accordance with GASB Statement No. 31, Accounting and Financial Reporting for Certain Investments and for External Investment Pools. Changes in unrealized gain (loss) on the carrying value of investments are reported as a component of investment income in the statements of revenues, expenses and changes in net assets.

Capital Assets – Primary Entity

Capitalized assets include land, improvements to land, easements, right-of-ways, buildings, building improvements, vehicles, equipment, furniture, and infrastructure, and all other tangible or intangible assets that are used in operations and have initial useful lives extending beyond a single reporting period. Capital assets also include assets purchased with Federal funds in which the Federal government retains a reversionary interest.

Capital assets are recorded at cost at the date of acquisition or fair market value at the date of donation in the case of gift. Assets contributed by another state agency are recorded at the acquisition cost of that agency. The Department follows capitalization guidelines established by the State of South Carolina. Major additions, renovations, and other improvements which provide new uses, or extend the useful life of an existing capital asset, are capitalized. Routine repairs and maintenance are charged to operations in the year in which the expense is incurred.

Depreciation is computed using the straight-line method over the estimated useful lives of the assets. A full year of depreciation is taken in the year the asset is placed in service and no depreciation is taken in the year of disposition.

A summary of the Department's capitalization and useful life by asset category is as follows:

Asset Category	Capitalization	Useful Life (Years)
Land	All, regardless of cost	
Non-depreciable land improvements	All, regardless of cost	
Depreciable land improvements	Any costing more than $100,000	30
Infrastructure:	Any costing more than $500,000	
Roads		75
Bridges		50
Buildings and building improvements	Any costing more than $100,000	30
Vehicles	Any costing more than $5,000	5 - 12
Equipment and furniture	Any costing more than $5,000	5 - 12

Capital Assets – Component Unit

All capital assets, including the intangible interest in the License Agreement with the Department, are stated at cost. The Association has adopted the asset capitalization policies recommended by the State of South Carolina Office of Comptroller General.

Pursuant to this policy, equipment with costs greater than $5,000 and intangible assets with costs in excess of $100,000 are capitalized. Equipment depreciation is computed using the straight-line method over the equipment's estimated useful life of five years. A full year of depreciation is taken in the year as asset is placed in service. The Association's interest in its License Agreement with the Department is amortized over the term of the License Agreement, which ends in year 2038. When capital assets are disposed of, the cost and accumulated depreciation is removed and the resulting gain or loss is included in operations.

Interest Capitalization – Component Unit

In accordance with FASB Statement No. 62, *Capitalization of Interest Cost in Situations Involving Certain Tax-Exempt Borrowings and Certain Gifts and Grants,* the Association capitalized the interest costs incurred during the construction of the Southern Connector. The amount of interest capitalized for assets constructed with tax-exempt borrowings consisted of interest cost of the borrowings, including amortization of the original issue discount, less interest earned on the related interest-bearing investments acquired with proceeds of the related tax-exempt borrowings, incurred prior to commencement of toll road operations.

Receivables

All of the receivables are reported net of any allowances for uncollectible amounts and any discounts, if applicable. The Department's receivables consist of amounts due from the Federal government, State agencies, local governments, and other entities and individuals. Some of the receivables are evidenced by notes and contracts. The notes and contracts are related to costs shared by other entities in construction projects. No allowance for uncollectible amounts was provided for based on management's evaluation of the collectability of the receivable balances at June 30, 2003.

Prepaid Expenses

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid expenses in the accompanying financial statements. Expenditures for prepaid expenses are accounted for using the consumption method of accounting.

Inventories

The Department maintains inventories for its use and resale to other State agencies, local governments, and other entities. All inventories are valued at cost using the weighted average method. Expenditures for inventory are accounted for using the consumption method of accounting.

Other Assets

Other assets consist of right of ways land the Department had to purchase for economic reasons that was not allocable to project construction costs. These purchases are held until they are disposed of and are reflected in the accompanying financial statements at the original cost to the Department. Expenditures for this land are accounted for using the consumption method of accounting in which the purchase is recorded as an expenditure when disposed of. Gains or losses on the disposition of right-of-ways land are included in the other revenues category in the fund financial statements. Right of ways land transferred to county and municipal governments for no consideration are recorded as allocations to other entities - county and municipal governments in the fund financial statements.

Interfund Receivables/Payables

Long-term interfund loans are classified as "advance to" or "advance from" particular funds. Short-term amounts are classified as "due to" or "due from" the particular funds. No interest is charged on the advances to or due from amounts. Short-term amounts are generally repaid within 60 days. There were no advances outstanding as of June 30, 2003.

Bonds Payable, Bond Discounts, Bond Premiums, Bond Issuance Costs and Deferred Loss on Refundings of Bonds

The Department reports bonds payable in the governmental activities in the Department-wide financial statement. The Department defers and amortizes bond discounts and bond premiums over the term of the bonds using the bonds outstanding method, which results in amortization being computed using the percentage of bonds retired to the original amount of bonds issued. Costs incurred in connection with the bond issues are deferred and amortized on the straight-line method over the lives of the related issues. For current refundings and advance refundings of bonds resulting in the defeasance of debt, the difference between the reacquisition price and the net carrying amount of the old debt is also deferred and amortized over the remaining life of the old debt or the life of the new debt, whichever is shorter. The Department reports bonds payable net of the applicable bond premium or discount and the deferred losses on refundings. Unamortized issuance costs are reported as deferred charges.

For the Association, bond issuance costs, discounts and underwriters' fees on all bonds are deferred and amortized over the terms of the bonds. Bond discounts are amortized using the bonds outstanding method, which approximates the effective interest method. Bond issuance costs and underwriters' fees are amortized using the straight-line method. Bond discounts are presented as a reduction of the face amount of the related revenue bonds payable whereas bond issuance costs and underwriters' fees are recorded as other assets.

Rebatable Arbitrage

Arbitrage involves the investment of proceeds from the sale of tax-exempt securities in a taxable investment that yields a higher rate, resulting in income in excess of interest costs. Federal law requires entities to rebate to the government such income on tax-exempt debt if the yield from those earnings exceeds the effective yield on the related tax-exempt debt issued. Governmental units may avoid the requirement to rebate the "excess" earnings to the federal government under certain circumstances, if they issue no more than $5 million in total of all such debt in a calendar year and if they meet specified targets for expending of the proceeds and interest earnings thereon. For this purpose, tax-exempt indebtedness includes bonds and certain capital leases and installment purchases. The federal government only requires arbitrage be calculated, reported and paid every five years or at maturity of the debt, whichever is earlier. However, the potential liability is calculated annually for financial reporting purposes. The Department incurred expenditures of $12,475 in arbitrage costs for the year ended June 30, 2003. $263,146 was paid on the arbitrage liability during fiscal year 2003 including $250,671 that was unpaid at June 30, 2002.

The Association records the arbitrage liability using the revenue reduction method, whereby the rebate is recorded as a reduction of interest revenue. At December 21, 2002, no such liability had been incurred.

Interest in License Agreement with the Department

The Association's license agreement with the Department grants to the Association various rights and obligations pertaining to the financing, acquisition, construction and operation of the Southern Connector and construction of the SC 153 Extension. The terms of the license agreement provide that the Association finance and construct the Southern Connector and construct the SC 153 Extension with financing provided by the Department. However, the Department at all times retained fee simple title to the Southern Connector and to the SC 153 Extension, to all real property and improvements thereon, and to all rights of way acquired during construction. The Southern Connector was opened for traffic on February 27, 2001 and began collecting tolls on March 14, 2001. On July 22, 2001, the Southern Connector attained substantial completion. Beginning one year after the date of final completion of construction of the Southern Connector, the Association will be required to pay monthly license fees to the Department. As of December 31, 2002, final completion has not yet been attained.

The Association's interest in the license agreement constitutes an intangible asset relating to the Southern Connector that began generating revenues upon commencement of operations. In order to account for its interest in the license agreement, the Association capitalized all costs of acquisition and construction of the Southern Connector, including interest expense incurred during the construction period. Upon commencement of operations, the Association began amortizing its interest in the License Agreement on a straight-line basis over the remaining term of the License Agreement through 2038.

Restricted Assets – Component Unit

Certain proceeds of the Association's Revenue Bonds are restricted by applicable bond covenants for construction, payment of operating and other expenses, or are set aside as reserves to ensure repayment of the bonds. Certain other assets are accumulated and restricted on a monthly basis in accordance with the Trust Agreement for the purposes of paying debt interest payments, due on a semiannual basis, and principal payments, due on an annual basis, and for the purpose of maintaining reserve funds at the required levels. The Trust Agreement provisions govern payments from the restricted accounts. Limited types of expenses may be funded from these restricted accounts. The funds and accounts are established as follows:

The Construction Fund was established for purposes of holding bond proceeds and investment earnings, which are used to pay the costs of constructing the Southern Connector.

The Revenue Fund was established to hold all revenues from toll road operations. The Trust Agreement provides that all revenues from the operation of the Southern Connector shall be delivered by the Association to the Trustee immediately upon receipt by, or on behalf of, the Association and shall be deposited by the Trustee into the Revenue Fund. The Trustee is obligated to transfer money on a monthly basis from the Revenue Fund to the other various funds established under the Trust Agreement in the priority listed below:

1. Operating costs budgeted by the Association for the next succeeding month shall be distributed to the Association.
2. There shall be transferred to the Rebate Fund amounts, which equal the amount required to be on deposit therein.
3. The Trustee shall transfer to the Senior Bonds Debt Service Account amounts which, when added to other amounts in the Senior Bonds Debt Service Account, and available for such purposes, will provide for accumulation, in substantially equal monthly installments, of the amounts required to pay the sum of:
    a. Any interest to become due and payable on each series of outstanding Senior Bonds on the next interest payment date (within the next six months) for such Series; and
    b. Any principal installments to become due and payable on any series of outstanding Senior Bonds on or before the next date (within the next twelve months) on which such principal installment is payable
4. If the Senior Bonds Debt Service Reserve Account contains less than the Senior Bonds Debt Service Reserve Account requirement, the Trustee shall transfer into the Senior Bonds Debt Service Reserve Account an amount equal to 1/24 of the Senior bonds Debt Service Account requirement or the amount to attain the Senior Bonds Debt service Reserve Account requirement, whichever is less. The transfers shall continue until the Senior Bonds Debt Service Reserve Account contains the Senior Bonds Debt Service Account requirement.
5. The Trustee shall transfer to the Subordinate Bonds Debt Service Account amounts which, when added to other amounts in the Subordinate Bonds Debt Service Account, and available for such purposes, will provide for accumulation, in substantially equal monthly installments, of the amounts required to pay the sum of:
    a. Any interest to become due and payable on each series of outstanding Subordinate Bonds (within the next six months) on the next interest payment date for such Series; and,
    b. Any principal installments to become due and payable on any series of outstanding Subordinate Bonds on or before the next date (within the next twelve months) on which such principal installment is payable.

6. If the Subordinate Bonds Debt Service Reserve Account contains less than the Subordinate Bonds Debt Service Reserve Account Requirement, the Trustee shall transfer into the Subordinate Debt Service Reserve Account an amount equal to 1/60 of the Subordinate Bonds Debt service Reserve Account Requirement or the amount needed to attain the Subordinate Bonds Debt Service Reserve Account Requirement, whichever is less. All transfers shall continue until the Subordinate Bonds Debt Service Reserve Account contains the necessary requirement.
7. After the date of Final Completion of the Southern Connector Project, the Trustee shall deposit into the Renewal and Replacement Fund the amounts included in the annual budget of the Association, which are required pursuant to the Renewal and Replacement Plan then in effect under the License Agreement.
8. The Trustee shall pay to the Department amounts certified by an Authorized Association Representative as being due the Department for (i.) the maintenance costs reimbursable to the Department under the License Agreement, together with any accruals from prior periods and interest owed thereon under the License Agreement, and (ii.) any reimbursement to the Department for condemnation awards for rights of way for the Southern Connector Project in excess of the amounts reserved therefore on the Completion Date.
9. The Trustee shall pay amounts certified by an Authorized Association Representative as being due the Department for the License Fee owing to the Department under the License Agreement, together with any accruals from prior periods and any interest owed thereon under the License Agreement.
10. Money remaining in the Revenue Fund shall be used by the Trustee to make or provide for all deposits, payments, or transfers certified by an Authorized Association Representative as being required by any agreement or other instrument creating or evidencing any obligation or the Association which is not a Senior Bond or Subordinate Bond, at the time and in the amount provided for in such instrument.
11. The Trustee shall transfer any money remaining in the Revenue Fund at the end of any fiscal year to the Program Fund.

The Debt Service Fund, consisting of the Senior Bonds Debt Service Account and the Subordinate Bonds Debt Service Account, was established as a sinking fund for the payment of interest and principal on the revenue bonds.

The Debt Service Reserve Fund consisting of the Senior Bonds Debt Service Reserve Account and the Subordinate Bonds Debt Service Reserve Account, was established for the purpose of paying bond interest and maturing principal in the event that monies held in the Debt Service Fund and other funds would be insufficient for such purposes.

The Renewal and Replacement Fund was established for the purpose of holding monies in reserve to pay the costs of reconstruction, renewal, repair and replacement of the Southern Connector. At December 31, 2002, this account was inactive.

The Program Fund consisting of the Retained Balance and the General Account was established to hold monies in reserve to pay debt service if monies in other accounts are insufficient for such purpose and the pay other fees and costs as defined in the Trust Agreement. The Program Fund General Account was initially funded in 2002 from monies remaining in the Revenue Fund at December 31, 2001. The Program Fund Retained Balance Account was inactive at December 31, 2002.

The Rebate Fund was established for the purpose of holding and paying arbitrage investment earning to the United States Treasury as a result of investing tax exempt bond proceeds at rates of return exceeding the maximum amount that is permitted under the applicable tax code. At December 31, 2002 the Rebate Fund was inactive.

Deferred Revenue

Deferred revenue consists of advance payments for construction projects, which have not been earned. Revenues are recognized in the period in which the project expenditures are made.

Compensated Absences

Generally all permanent full-time State employees and certain part-time employees scheduled to work at least one-half of the agency's work week are entitled to accrue and carry forward at calendar year-end maximums of 180 days sick leave and of 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, but are not entitled to any payment for unused sick leave. The compensated absences liability includes accrued annual leave earned for which the employees are entitled to paid time off or payment at termination. The leave liability also includes an estimate for accrued sick leave and leave from the agency's leave transfer pool for employees who have been approved as leave recipients under personal emergency circumstances which commenced on or before June 30, 2003. The Department calculates the gross compensated absences liability based on recorded balances of unused leave. The entire unpaid liability for which the employer expects to compensate employees through paid time off or cash payments, inventoried at fiscal year-end current salary costs and the cost of the salary-related benefit payments, is recorded as a liability.

Though the Association has no employees, under its Operations Contract, the Association is required to reimburse the toll road management contractor for actual operating costs incurred. Accordingly, any vested or accumulated vacation leave is recorded as benefits accrue to contractor employees. There are no accumulating sick-leave benefits therefore there is no liability that must be recognized. At December 31, 2002, the liability for accumulated absences was immaterial. No liability or expense was recorded in these financial statements.

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 of assets, liabilities, revenues and expenses/expenditures and affect disclosure of contingent assets and liabilities at the balance sheet date of the financial statements and the reported amounts of revenues and expenses/expenditures during the reporting period. Accordingly, actual results could differ from those estimates.

Net Assets

Net assets are classified and presented in three components:

Invested in capital assets, net of related debt – Consists of capital assets including restricted capital assets, net of accumulated depreciation and amortization, and reduced by the outstanding balances of any bonds, mortgages, notes or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.

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 – All other assets that do not meet the definition of "restricted" or "invested in capital assets.

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

The Association's net deficit at December 31, 2002, resulted from shortfalls since commencement of operations due to lower than expected traffic counts and toll revenue. The Association anticipates that future development along the Southern Connector corridor will encourage increased traffic, which in turn, will generate toll revenues that will reduce the deficit.

NOTE 2. DEPOSITS AND INVESTMENTS:

The following schedule reconciles deposits and investments within the footnotes to the amounts in the financial statements:

Financial Statements		Footnotes	
Primary Entity:			
Unrestricted current assets:			
Cash and cash equivalents	$ 143,584,759	Cash on hand	$ 250
Restricted noncurrent assets:		Deposits held by State	
Cash and cash equivalents	161,744	Treasurer	251,518,572
Fiduciary - Agency Funds			
Cash and cash equivalents	107,772,319		
Total primary entity	251,518,822		251,518,822
Component Unit:			
Unrestricted current assets:			
Cash and cash equivalents	369,290	Cash on hand	4,500
Restricted current assets:		Deposits in transit	7,555
Cash and cash equivalents	1,096,926	Bank deposits	66,480
Restricted noncurrent assets:		Investments	25,311,371
Cash and cash equivalents	3,631,159		
Investments held by Financial institutions	20,292,531		
Total component unit	25,389,906		25,389,906
TOTAL	$ 276,908,728		$ 276,908,728

PRIMARY ENTITY:

Deposits Held by State Treasurer

The deposits of the Department held by the State Treasurer are under the control of the State Treasurer who, by law, has sole authority for investing State funds. State law requires full collateralization of all State Treasurer bank balances. The State Treasurer must correct any deficiencies in collateral within seven days.

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 carrying amounts, fair value, and credit risk of the State Treasurer's investments is disclosed in the Comprehensive Annual Financial Report of the State of South Carolina.

Cash and cash equivalents reported include unrealized appreciation of $6,232,394 for the governmental funds and $4,760,104 for the fiduciary funds as of June 30, 2003 arising from changes in the fair value. The interest/investment income includes a loss of $1,627,797 for the year ended June 30, 2003.

Deposits at fair value at June 30, 2003 held by the State Treasurer include $80,074 of unexpended funds from bond issues which are to be used for projects in progress and other purposes and $81,670 for advance funding for debt service.

COMPONENT UNIT:

Deposits

The Association's Trust Agreement requires that all bank deposits that are not insured by the Federal Deposit Insurance Corporation be collateralized by investment securities. The types of investment securities that may be used as collateral are: obligations of or guaranteed by the United States of America or certain of its agencies, repurchase agreements with underlying securities that are obligations of or guaranteed by the United States of America or certain of its agencies, certain obligations of or guaranteed by any State within the territorial United States of America, agreements that provide for the forward delivery of any securities previously described, investments in money market mutual funds rated "AAAm", "AAm", "AAAmG" or better, unsecured investments agreements with any bank or financial institution the unsecured debt or counterparty rating of which is "investment grade" rated as of the date of acquisition; and any other obligation which, at the date of acquisition, is rated by a Rating Agency in one of the two highest rating categories for long-term obligations or in the highest rating category for short-term obligations.

GASB Statement No. 3, *Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements,* requires entities to categorize their band deposits to give an indication of the level of risk assumed at year-end. The credit risk categories are concerned with custodial credit risk, which is the risk that an entity will not be able to recover deposits if the depository financial institution fails to recover the value of collateral securities that are in the possession of an outside party if the counter-party to the deposit transaction fails. There are three categories of deposit credit risk as follows:

(1) Insured or collateralized with securities held by the Association or by its agent in the Association's name
(2) Collateralized with securities held by the pledging financial institution's trust department or agent in the Association's name and
(3) Uncollateralized, 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 Association's name.

All of the Associations' deposits were in category 1 at December 31, 2002.

None of the deposits above were on deposit with the South Carolina State Treasurer.

Investments – Component Unit

Pursuant to requirements of GASB Statement No. 3, the Association's investments in repurchase agreements were categorized to give an indication of the level of risk assumed by the Association at year-end. The credit risk categories are concerned with custodial credit risk, which is the risk that an entity will not be able to recover the value of investment or collateral securities that are in the possession of an outside party if the counter-party to the investment transaction fails. There are three categories of investment risk, which are as follows:

(1) Insured or registered, or securities held by the Association or by its agent in the Association's name,
(2) Uninsured and unregistered, with securities held by the counter-party's trust department or agent in the Association's name, and
(3) Uninsured and unregistered, with securities held by the counter-party, or by its trust department or agent, but not in the Association's name, including the portion of the carrying amount of any repurchase agreement that exceeds the market value of the underlying securities.

The Association's investments in open-end money market mutual funds were not required to be categorized since the investments were not evidenced by securities that exist in physical or book entry form.

The Association's investments at December 31, 2002 by investment risk categories are as follows:

	Risk Category			Carrying	Market
	1	2	3	Value	Value
Repurchase Agreements	$ -	$ 20,292,531	$ -	$ 20,292,531	$ 20,292,531
Not Categorized:					
Open-end Money Market					
Mutual Funds				5,018,640	5,018,640
	$ -	$ 20,292,531	$ -	$ 25,311,171	$ 25,311,171

The investment types listed above include all investment types in which monies were held during the year ended December 31, 2002. None of the above investments were on deposit with the South Carolina State Treasurer.

At December 31, 2002, the Association's restricted assets included $4,728,085 of cash and cash equivalents and $20,292,531 of investments. See Notes 1 and 8 for additional information about restrictions on investments and balances of the various trust funds at December 31, 2002.

NOTE 3. STATE APPROPRIATIONS:

The original appropriation is the Department's base budget amount as presented in the General Fund column of Section 53, Part IA of the 2002-03 Appropriation Act.

Original appropriation	$ 485,818
State budget reductions:	
Interim - 4.5%	(21,862)
Interim - 3.73%	(17,234)
Sequestered amount - 0.5%	(2,454)
Total appropriation	$ 444,268

The sequestered budget reduction amount of $2,454 was not paid as of June 30, 2003 and is included in the liability account Due to the General Fund of the State.

NOTE 4. RECEIVABLES:

The following schedule summarizes receivables at June 30, 2003, which include various notes, contracts and other accounts receivable.

Due From / Description	Current Portion	Long-term Portion (A)	Totals
Intergovernmental:			
Federal government:			
Amounts due under various grant programs and reimbursable contracts	$ 98,439,870	$ -	$ 98,439,870
State Agencies:			
South Carolina Department of Public Safety			
Sales of goods and services	964,234		964,234
South Carolina Department of Revenue			
Gasoline and special fuels taxes	61,257,239		61,257,239
South Carolina Budget & Control Board			
Sales of goods and services	116,504		116,504
Other agencies			
Sales of goods and services	1,593		1,593
	62,339,570	-	62,339,570
Local governments:			
Long term contracts for construction projects	577,468	5,310,534	5,888,002
Participation agreements	5,828,533		5,828,533
Construction projects	2,339,325		2,339,325
	8,745,326	5,310,534	14,055,860
Other			
Long term contracts for construction projects	1,381,957	3,422,505	4,804,462
Participation agreements	2,213,061		2,213,061
Sales of goods and services	3,999,641		3,999,641
	7,594,659	3,422,505	11,017,164
Total receivables	$ 177,119,425	$ 8,733,039	$ 185,852,464

(A) Due to the long-term nature of this portion of the receivables, the entire amount has been offset as a reservation of fund balance as not being currently available.

The balances due under long-term contracts for construction projects from local governments and other entities represent loans to those entities for their share of the costs of construction projects.

The balances due under participation agreements from local governments and other entities represent advances by the Department for construction costs in excess of collections on joint-venture construction projects.

NOTE 5. INVENTORIES:

The following schedule summarizes inventories at June 30, 2003:

Sign shops	$ 4,265,433
Repair shops	1,059,599
Supply depot	1,145,198
Total	$ 6,470,230

NOTE 6. CAPITAL ASSETS:

PRIMARY ENTITY:

The following schedule summarizes changes in capital assets of the Department for the year ended June 30, 2003:

	Beginning Balances as Restated	Increases	Decreases	Ending Balances
Capital assets not being depreciated:				
Land and improvements	$ 3,681,682	$ 752,000		$ 4,433,682
Right of ways land	511,103,732	92,387,585	2,524,527	600,966,790
Construction in progress				
Infrastructure - road and bridge network	3,004,196,383	734,193,005	576,667,111	3,161,722,277
Other	3,176,177	2,893,800	291,774	5,778,203
Total capital assets not being depreciated	3,522,157,974	830,226,390	579,483,412	3,772,900,952
Other capital assets:				
Infrastructure - road and bridge network	7,018,880,098	580,139,326	3,230,982	7,595,788,442
Buildings and improvements	53,540,106	5,839,774		59,379,880
Equipment and furniture	111,038,539	7,066,998	10,795,221	107,310,316
Vehicles	86,253,487	4,727,193	4,667,642	86,313,038
Total other capital assets	7,269,712,230	597,773,291	18,693,845	7,848,791,676
Accumulated depreciation for:				
Infrastructure - road and bridge network	1,660,126,117	106,787,633	2,739,040	1,764,174,710
Buildings and improvements	16,886,440	1,915,543		18,801,983
Equipment and furniture	78,478,623	7,555,945	9,922,908	76,111,660
Vehicles	60,758,525	6,299,866	4,507,211	62,551,180
Total accumulated depreciation	1,816,249,705	122,558,987	17,169,159	1,921,639,533
Total other capital assets, net	5,453,462,525	475,214,304	1,524,686	5,927,152,143
Total capital assets for governmental activities, net	$ 8,975,620,499	$ 1,305,440,694	$ 581,008,098	$ 9,700,053,095

See Note 22 regarding the effect of corrections resulting from accounting and reporting changes and reclassifications of various capital asset account balances as of July 1, 2002.

The following schedule summarizes additions to capital assets and their funding sources for the year ended June 30, 2003:

Additions:	
Increases per above:	
Capital assets not being depreciated	$ 830,226,390
Other capital assets	597,773,291
Less, transfers from construction in progress:	
Infrastructure - road and	
bridge network	(576,667,111)
Buildings and improvements	(291,774)
Total additions	$ 851,040,796
Funding sources:	
Governmental funds	$ 509,302,827
Donated capital assets:	
The Association	3,472,215
South Carolina Transportation	
Infrastructure Bank	338,265,754
Total funding sources	$ 851,040,796

Included in the Department's capital assets as of June 30, 2003 is $191,759,069 that was paid for by the Association for the Southern Connector. This same amount has been capitalized by the Association as the capital asset - Interest in License Agreement with the Department. Accumulated depreciation on these assets was $7,842,543 at June 30, 2003. Depreciation expense on these assets for the year ended June 30, 2003 was $2,645,045.

At June 30, 2003, the estimated total costs of Department projects in progress to construct, acquire and maintain various capitalized assets amounted to approximately $23,380,000 for facilities capital projects and approximately $3,849,000,000 for infrastructure projects including capital and non-capital. The estimated costs to complete the facilities capital projects amounted to approximately $17,602,000 and the infrastructure projects amounted to approximately $1,023,000,000 at June 30, 2003. The outstanding contractual obligations attributable to the facilities capital projects were approximately $4,841,000 and to the infrastructure projects were approximately $639,000,000. The estimated time frame for completion of these projects is several years. The costs of the projects in progress and future projects will be funded from taxes and fees, federal grants, bond proceeds and other revenues of the Department. The amounts for infrastructure projects exclude those infrastructure project costs funded by the South Carolina Transportation Infrastructure Bank.

COMPONENT UNIT:

The following schedule summarizes changes in capital assets of the Association for the year ended December 31, 2002:

	Beginning Balance at	Increases	Decreases	Ending Balance at
Capital assets, being depreciated/amortized:				
Interest in License Agreement with the Department	$ 188,286,854	$ 3,472,215	$	$ 191,759,069
Equipment	440,284			440,284
Total capital assets, being depreciated/ amortized	188,727,138	3,472,215		192,199,353
Accumulated depreciation/amortization:				
Interest in License Agreement with the Department	(3,830,409)	(5,141,635)		(8,972,044)
Equipment	(88,057)	(88,057)		(176,114)
Total accumulated depreciation/amortization	(3,918,466)	(5,229,692)		(9,148,158)
Total capital assets, net	$ 184,808,672	$ (1,757,477)	$	$ 183,051,195

For the year ended December 31, 2002, depreciation and amortization expense related to capital assets was $5,229,692.

The Association had $776,947 of construction commitments outstanding at December 31, 2002, under its signed Development Agreement for construction of the Southern Connector.

NOTE 7. CHANGES IN LONG-TERM OBLIGATIONS:

The following schedule summarizes changes in long-term obligations of the Department for the year ended June 30, 2003:

	Beginning Balances	Increases	Decreases	Ending Balances	Due Within One Year
General obligation bonds:					
Bonds payable	$ 651,135,000	$ 46,080,000	$ 61,600,000	$ 635,615,000	$ 24,810,000
Unamortized premium		669,284		669,284	7,917
Unamortized deferred loss on refunding of bonds		(5,708,911)	(154,295)	(5,554,616)	(1,851,540)
Total bonds payable	651,135,000	41,040,373	61,445,705	630,729,668	22,966,377
Intergovernmental payable - Due to State agency	190,903,351	65,959,644	21,411,799	235,451,196	21,576,383
Capital leases payable	214,102	459,320	177,225	496,197	132,504
Accrued compensated absences	19,341,449	14,122,894	13,778,008	19,686,335	13,537,469
Total governmental activities	$ 861,593,902	$ 121,582,231	$ 96,812,737	$ 886,363,396	$ 58,212,733

The following schedule summarizes principal and interest expenditures/expenses attributable to long-term obligations of the Department for fiscal year 2003:

	Principal	Interest	Totals
Governmental Fund:			
Bonds payable (1)	$ 21,925,000	$ 31,482,632	$ 53,407,632
Contributions payable	21,411,799	4,188,201	25,600,000
Capital leases	177,225	22,170	199,395
Total expenditures	$ 43,514,024	35,693,003	$ 79,207,027
Adjustments to Department - wide statements			
Bond interest attributable to refunded bonds		956,089	
Change in interest accrual - bonds payable		(1,350,162)	
Total interest expense		$ 35,298,930	

(1) Excludes $39,675,000 of bond principal that was advance refunded and included in the governmental funds statement under other financing sources (uses) as escrow deposit for advance refundings of bonds.

NOTE 8. BONDS PAYABLE:

Primary Entity

Sections 57-11-210, et seq. of the South Carolina Code (the "State Highway Bond Act"), as continued and amended by Section 11-27-30 thereof, authorized the issuance of general obligation State Highway Bonds for highway construction and related purposes backed by the full faith, credit, and taxing power of the State. State Highway Bonds are additionally secured by a pledge of so much of the revenues as may be made applicable by the General Assembly for State highway purposes from any and all taxes or licenses imposed upon individuals or vehicles for the privilege of using the public highways of the State. Such taxes include the gasoline tax, the fuel oil tax, the road tax and the motor vehicle license tax described herein.

So long as any State Highway Bonds are outstanding the amount of revenues made applicable thereto by the General Assembly may not be less than the amounts needed to fund the general operations budget of the Department and meet debt service requirements for annual principal and interest payments on such bonds. Section 57-11-240 provides that the debt limit for State Highway Bonds is the maximum annual debt service limitation of approximately $80,200,000 which results from the application of the constitutional limitation imposed by said Paragraph 6(a) of Section 13 of the Article X of the South Carolina Constitution. From time to time, the State Budget and Control Board may authorize the issuance of various amounts of State Highway Bonds for specific types of projects or individual projects and may authorize the total to be issued in one or more series depending on the projections of the timing of project expenditures to be funded from the proceeds.

A listing of the general obligation bonds payable at June 30, 2003 is as follows:

Issue Date	Series	Original Face Amount	Maturity Dates	Interest Rates	Ending Principal Balance
8/1/95	1995	$20,000,000	8/1/10		$12,500,000
1/1/96	1996A	30,000,000	2/1/11		18,545,000
7/1/96	1996B	45,000,000	7/1/21		4,350,000
10/1/97	1997A	30,000,000	10/1/12		22,530,000
4/1/98	1998A	17,500,000	4/1/23		15,535,000
3/1/99	1999A	200,000,000	5/1/19		188,000,000
1/1/01	2001A	2,000,000	1/1/21		1,890,000
4/1/01	2001B	350,000,000	4/1/21		326,185,000
6/4/03	2003B	46,080,000	7/1/21		46,080,000
Add, unamortized premium					669,284
Less, unamortized deferred loss on refundings of bonds					(5,554,616)
Total bonds payable					$630,729,668

The following schedule summarizes the debt service requirements, including principal and interest, of bonds payable by the Department to maturity:

	Principal	Interest	Totals
Year ending June 30:			
2004	$ 24,810,000	$ 29,079,730	$ 53,889,730
2005	26,265,000	28,478,379	54,743,379
2006	27,430,000	27,153,772	54,583,772
2007	30,395,000	25,806,072	56,201,072
2008	35,505,000	24,356,923	59,861,923
	144,405,000	134,874,876	279,279,876
Five years ending June 30:			
2009 - 2013	191,065,000	95,311,543	286,376,543
2014 - 2018	192,585,000	52,642,408	245,227,408
2019 - 2023	107,560,000	9,768,794	117,328,794
Total debt service for bonds payable	$ 635,615,000	$ 292,597,621	$ 928,212,621

On June 1, 2003 the Department issued $46,080,000 in general obligation State Capital Improvement Refunding Bonds, Series 2003B. The purpose of the issuance was for advance refunding of $39,675,000 of the Series 1996B bonds. Proceeds from the new bond issue consisted of the following:

Face amount of bonds	$ 46,080,000
Premium	669,284
Total	46,749,284

Issuance costs of the 2003B bonds consist of the following:

Underwriter's discount	$ 322,560
Other issuance costs	74,169
Total	$ 396,729

Amortization of bond issuance costs for the year ended June 30, 2003 was $1,828.

The Department deposited $46,340,000 in an escrow account with Banc of America Securities, LLC pursuant to an irrevocable trust agreement for the future retirement of the refunded bonds. The deposited funds were invested in U.S. government securities. The $39,675,000 of Series 1996B bonds are considered to be defeased and the liability for those bonds has been removed from the Department-wide statement of net assets. The outstanding balance of these bonds was $39,675,000 at June 30, 2003.

The advance refunding resulted in a difference between the reacquisition price and the net carrying amounts of the old debt $5,708,911. This difference is reported in the accompanying financial statements as a reduction of bonds payable and is being amortized on a straight line basis and will be charged to operations through the fiscal year ending June 30, 2005 since a call premium was pre-funded. The bonds are expected to be redeemed on July 1, 2006. The Department completed the advance refunding to reduce its total debt service payments over the next 18 fiscal years by approximately $2,550,000 and to obtain an economic gain of approximately $2,230,000 (the difference between the present values of the debt service payments on the old debt and the new debt).

The following summarizes the deferred loss on advance refunding of the Series 1996B bonds:

Escrow deposit	$46,340,000
Less:	
Principal amount refunded	(39,675,000)
Accrued interest deposited	(956,089)
Deferred loss on refunding of bonds payable	$ 5,708,911

Amortization of the deferred loss on refundings of bonds payable for the year ended June 30, 2003 was $154,295.

The Series 1995 State Highway Bonds maturing on or after August 1, 2006, are subject to redemption, at the option of the State, in whole or in part at any time in any order of maturity to be determined by the State, on and after August 1, 2005, at the Redemption Prices expressed as a percentage of the principal amount of each Series 1995 State Highway Bond, or portion thereof, to be redeemed, as set forth below, plus accrued interest to the date for redemption:

Redemption Dates	Redemption Price
August 1, 2005 through July 31, 2005	102%
August 1, 2006 through July 31, 2006	101%
August 1, 2007 and thereafter	100%

The Series 1996A General Obligation State Highway Bonds maturing on and after February 1, 2007, are subject to redemption, in whole or in part, at any time in any order of maturity to be determined by the State, on and after February 1, 2006, at the Redemption Prices expressed as a percentage of the principal amount to be redeemed as set forth below, plus accrued interest to the date fixed for redemption:

Redemption Dates	Redemption Price
February 1, 2006 through January 31, 2007	102%
February 1, 2007 through January 31, 2008	101%
February 1, 2008 and thereafter	100%

The Series 1996B State Highway Bonds are not subject to redemption prior to maturity.

The Series 1997A State Highway Bonds maturing on and after October 1, 2008, are subject to redemption, in whole or in part, at any time in any order of maturity to be determined by the State, on or after October 1, 2007, at the Redemption Prices expressed as a percentage of the principal amount to be redeemed set forth below, plus accrued interest to the date fixed for redemption:

Redemption Dates	Redemption Price
October 1, 2007 through September 30, 2008	102%
October 1, 2008 through September 30, 2009	101%
October 1, 2009 and thereafter	100%

The Series 1998A State Highway Bonds maturing on and after April 1, 2009, are subject to redemption, in whole or in part, at any time in any order of maturity to be determined by the State, on or after April 1, 2008, at the Redemption Prices expressed as a percentage of the principal amount to be redeemed set forth below, plus accrued interest to the date fixed for redemption:

Redemption Dates	Redemption Price
April 1, 2008 through March 31, 2009	102%
April 1, 2009 through March 31, 2010	101%
April 1, 2010 and thereafter	100%

The Series 1999A General Obligation State Highway Bonds maturing on and after May 1, 2010 are subject to redemption, in whole or in part, at any time in any order of maturity to be determined by the State, on and after May 1, 2009, at the Redemption Prices expressed as a percentage o the principal amount to be redeemed set forth below, plus accrued interest to the date fixed for redemption:

Redemption Dates	Redemption Price
May 1, 2009 through April 30, 2010	102%
May 1, 2010 through April 30, 2011	101%
May 1, 2011 and thereafter	100%

The Series 2001A General Obligations State Highway Bonds maturing on and after January 1, 2012, shall be subject to redemption, in whole or in part, at any time in any order of maturity to be determined by the State, on and after January 1, 2011, at the Redemption Prices expressed as a percentage of the principal amount to be redeemed set forth below, plus accrued interest to the date fixed for redemption:

Redemption Dates	Redemption Price
January 1, 2011 through December 31, 2011	101%
January 1, 2012 and thereafter	100%

The Series 2001B State Highway Bonds maturing on and after April 1, 2009, are subject to redemption, in whole or in part, at any time in any order of maturity to be determined by the State, on or after April 1, 2008, at the Redemption Prices expressed as a percentage of the principal amount to be redeemed set forth below, plus accrued interest to the date fixed for redemption:

Redemption Dates	Redemption Price
April 1, 2008 through March 31, 2009	102%
April 1, 2009 through March 31, 2010	101%
April 1, 2010 and thereafter	100%

The Series 2003B State Capital Improvement Refunding Bonds are not subject to redemption prior to maturity.

Component Unit

The Association issued three series of tax-exempt toll road revenue bonds pursuant to a Master Indenture of Trust and a First Supplemental Indenture of Trust, both dated February 1, 1998. All of the bonds were issued on February 11, 1998. The bonds are special limited obligations of the Association that are not, and shall never, constitute an indebtedness of the State of South Carolina, the Department, or any agency, department or political subdivisions of the State of South Carolina, including the County of Greenville, South Carolina and the City of Greenville, South Carolina.

The following schedule summarizes changes in bonds payable by the Association for the year ended December 31, 2002:

	Beginning Balances	Increases	Decreases	Ending Balances	Due Within One Year
Senior Bonds:					
Series 1998A Senior Current Interest Toll Road Revenue Bonds, dated February 1, 1998; $66,200,000 original principal amount at issuance; interest payable semi-annually on January 1 and July 1 at rates of 5.25% and 5.375%; $21,400,000 of bonds mature January, 2023; $44,800,000 of bonds mature January, 2038	$ 66,200,000	$ -	$ -	$ 66,200,000	$ -
Original issue discount on Series 1998A bonds; issuance $2,693,952	(2,379,522)	80,280	-	(2,299,242)	-
	63,820,478	80,280	-	63,900,758	-
Series 1998B Senior Capital Appreciation Toll Road Revenue Bonds, dated February 11, 1998; $87,385,622 original principal amount at issuance; interest accretes at various rates ranging from 5.3% to 5.85%; $438,100,000 of bonds mature at various dates from January, 2008 to January, 2038	108,988,741	6,370,140	-	115,358,881	-
Subordinate bonds:					
Series 1998C Subordinate Capital Appreciation Toll Road Revenue Bonds, dated February 11, 1998; $46,592,058 original principal amount at issuance; interest accretes at various rates ranging from 6.15% to 6.3%; $241,800,000 of bonds mature at various dates from January, 2008 to January, 2038	59,168,499	3,749,339	-	62,917,838	
Total bonds payable	$ 231,977,718	$ 10,199,759	$ -	$ 242,177,477	$ -

Additions to bonds payable represent the amortization of original issue discount on the Series 1998A Senior Current Interest Toll Revenue Bonds, and accretions on the Series 1998B and 1998C Capital Appreciation Bonds. At December 31, 2002, no principal payments on bonds were due within one year.

The following schedule summarizes debt service requirements (principal and interest) of the Association to maturity:

	Principal	Interest	Totals
Year Ending December 31:			
2003	$	$ 3,531,500	$ 3,531,500
2004		3,531,500	3,531,500
2005		3,531,500	3,531,500
2006		3,531,500	3,531,500
2007		3,531,500	3,531,500
	$ -	$ 17,657,500	$ 17,657,500
Five years ending December 31:			
2008 - 2012	38,200,000	17,040,625	55,240,625
2013 - 2017	61,300,000	15,557,500	76,857,500
2018 - 2022	93,700,000	13,651,750	107,351,750
2023 - 2027	128,800,000	11,189,563	139,989,563
2028 - 2032	169,400,000	7,914,689	177,314,689
2033 - 2037	197,000,000	3,655,000	200,655,000
2038	57,700,000	112,875	57,812,875
Total debt service for bonds payable	$ 746,100,000	$ 17,657,500	$ 17,657,500

The terms of the Trust Agreement require the establishment of seven accounts (called "funds" in the indenture documents). The proceeds of the bonds were allocated among and deposited into certain of these accounts. The monies deposited into these accounts are invested according to the terms of Trust Agreement. Authorized payments of construction costs, debt service, arbitrage rebates and operating costs and renewal and replacement costs may only be paid from certain accounts as specified in the Trust Agreement. Payment of debt service of the bonds is secured by the Trust Estate, which includes all monies deposited into these various funds, excluding amounts in the rebate account and in the renewal and replacement account. The Trust Estate also includes the Association's interest in revenues as defined in the Trust Agreement, the Association's interest in the license agreement with the Department, and any other property pledged as security for the bonds. The accounts established by the Trust Agreement and the balances therein at December 31, 2002 were as follows:

Fund	Amount
Construction	$ 3,631,159
Revenue	271,758
Debt Service	1,037,205
Debt Service Reserve	20,292,531
Renewal and Replacement	-
Program	-
Rebate	-
Total	$ 25,232,653

Interest costs expensed during the year ended December 31, 2002 totaled $13,731,258.

During the year ended December 31, 2002, payments from the various accounts were made in accordance with the terms of the bond indenture.

The Trust Agreement contains certain other bond covenants including, but not limited to, the following:

- The Association is prohibited from taking any action or omitting to take any action that would cause the bonds to lose their tax-exempt status.

- After the Southern Connector is completed and operational, the Association's Engineer must inspect the toll road annually and submit a report documenting the physical condition of the toll road, offering advice, recommendations and a cost estimate as to the proper operation of the toll road during the ensuing fiscal year, offering advice and recommendations regarding the insurance to be carried, and stating the amount to be deposited into the Renewal and Replacement Fund for the next fiscal year.

- Prior to the end of each fiscal year, the Association is required to file an annual budget for the next fiscal year with the Trustee.

- Beginning on the first day of the second full fiscal year immediately following the later of (i) the Final Completion date of the Southern Connector, and (ii) the last date through which interest on any of the bonds is to be paid from proceeds of the bonds, the tolls charged by the Association shall equal or exceed the greater of (a) 1.25 times the aggregate debt service on all outstanding Senior Bonds due in that fiscal year, and (b) the amount required to fund all transfers to the Senior Bonds Debt Service Reserve Fund as defined in the Trust Agreement and to equal not less than 1.10 times the aggregate debt service on all outstanding bonds due in that fiscal year. The Trust Agreement also specifies actions to be taken if the Association determines that revenues may be inadequate to meet this covenant.

The Association monitors the covenants for compliance throughout the year. The Association believes it was in compliance with its bond covenants throughout 2002.

The following schedule summarizes changes in bond issuance costs of the Association and the account balances as of each year end:

	Beginning Balance	Changes	Ending Balance
Original costs	$ 5,228,730	$ -	$ 5,228,730
Amortization	(544,495)	(139,020)	(683,515)
Carrying value	$ 4,684,235	$ (139,020)	$ 4,545,215

NOTE 9. Intergovernmental Payable – Due to State Agency – Primary Entity

The Department entered into various intergovernmental agreements with the South Carolina Transportation Infrastructure Bank (the Bank) and various local governments to provide financial assistance for highway and transportation facilities projects. Details of the agreements follow in which the Department has a financial obligation.

Horry County RIDE I Project. The total costs for this project are estimated to be $888 million. Funding consists of a $340 million financial assistance award by the Bank of which a $114 million contribution which is being paid to the Bank by the Department of Transportation in annual installments of $10 million each for eleven years and $4 million in the 12th year and an additional $95 million contribution which is being paid to the Bank by the Department in annual installments of $7.6 million including 5% interest per annum for 20 years; a $300 million interest free loan to Horry County; and, a $247,577,664 interest bearing loan to Horry County.

Charleston County Project. The total estimated project costs are $650 million. Funding for the project consists of a $540 million financial assistance award by the Bank and the funding of $110 million of expenditures by the Department and claimed as federal expenditures. In addition, the Department is to contribute $200 million to the Bank at the rate of $8 million per year for 25 years without interest commencing in fiscal year 2003.

The following schedule summarizes changes in contributions payable – State agency (the South Carolina Transportation Infrastructure Bank) for the year ended June 30, 2003 and account balances of each year end:

Project	Beginning Balance	Increases	Decrease	Ending Balance
Horry County Ride Project				
Phase I	$ 64,000,000	$ -	$ 10,000,000	$ 54,000,000
Phase II	86,820,649		3,411,799	83,408,850
Charleston County Project	40,082,702	65,959,644	8,000,000	98,042,346
Totals	$ 190,903,351	$ 65,959,644	$ 21,411,799	$ 235,451,196

The following schedule summaries the debt service requirements, including principal and interest, of the Department to maturity:

	Principal	Interest	Total
Year Ending June 30			
2004	$ 21,576,383	$ 4,023,617	$ 25,600,000
2005	21,748,906	3,851,094	25,600,000
2006	21,929,752	3,670,248	25,600,000
2007	22,119,322	3,480,678	25,600,000
2008	22,318,037	3,281,963	25,600,000
	109,692,400	18,307,600	128,000,000
Five years ending June 30			
2009 - 2013	68,923,078	13,076,922	82,000,000
2014 - 2018	49,585,468	6,456,878	56,042,346
2019	7,250,250	349,750	7,600,000
Totals	$ 235,451,196	$ 38,191,150	$ 273,642,346

NOTE 10. LEASE OBLIGATIONS:

The Department is obligated under various operating and capital leases for the use of office equipment.

The Department entered into various capital leases for the purchase of imaging equipment costing $1,301,232. Principal payments made to date totaled $805,035 leaving unpaid balances of $496,197. The leases are secured by the equipment purchases. Interest rates range from 4.36% to 5.34%. Certain of the capital leases provide for renewal options and none of the leases include any purchase options. Total payments on these leases during the fiscal year ended June 30, 2003 totaled $272,989 of which $177,225 was principal, $22,170 was interest and $73,594 was executory costs. The carrying value of the imaging equipment purchased with capital leases at June 30, 2003 was $355,369. Depreciation for the fiscal year 2003 amounted to $167,822 and is included in depreciation expense.

The Department's non-cancelable operating leases having remaining terms of more than one year expire in various fiscal years from 2004 through 2005. Certain operating leases provide for renewal options for periods 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. Operating leases are generally payable on a monthly basis. The operating lease expenditures in fiscal year 2003 were approximately $167,000. In addition to the non-cancelable operating leases, the Department incurred approximately $227,000 in expenditures applicable to contingent rental agreements that are based on a pay-per-copy arrangement, with no required minimum usage requirements. All operating leases are with external parties.

The following schedule summarizes future commitments for capital leases and operating leases having remaining non-cancelable terms in excess of one year as of June 30, 2003:

Year Ending June 30,	Capital Leases	Operating Leases
2004	$ 202,228	$ 68,346
2005	195,678	4,592
2006	170,966	-
2007	150,096	-
2008	24,974	-
2009		-
Totals	743,942	$ 72,938
Less:		
Interest	(46,384)	
Executory costs	(201,361)	
Capital lease obligations, at June 30, 2003	$ 496,197	

NOTE 11. INTEREST IN LICENSE AGREEMENT WITH THE DEPARTMENT – COMPONENT UNIT:

On February 11, 1998, the Association entered into a license agreement (the License Agreement) with the Department regarding the construction and operation of the Southern Connector and SC 153 Extension projects (the Projects). The agreement grants the Association the exclusive right (1) to acquire in the name of the Department rights of way and other real property necessary to the development and operation of the Projects, (2) to develop and construct the Projects, (3) to finance the Southern Connector, (4) to operate, repair, renew and replace the Southern Connector in accordance with terms of the agreement, and (5) to collect tolls from the users of the Southern Connector.

In order to finance the Southern Connector, the Association issued three series of toll road revenue bonds pursuant to the Trust Agreement dated February 1, 1998. Interest on the bonds is exempt from federal income tax and from South Carolina income tax. The bonds are special, limited obligations of the Association, payable solely from net revenues and monies held in certain accounts and other property included in the trust estate. The bonds are not, and shall never, constitute an indebtedness of the State of South Carolina, of the Department, or of any agency, department or political subdivision of the State of South Carolina.

The License Agreement specifies that, upon its termination, the Association is to convey to the Department full title to all property and equipment acquired in whole or in part with proceeds of the bonds issued to finance the Southern Connector project. As stated in the License Agreement, the title to all real property and improvements thereon acquired or constructed during the term of the License Agreement is held by the Department. The License Agreement specifies a termination date 50 years after substantial completion of the Southern Connector. However, the License Agreement automatically terminates upon repayment, redemption or defeasance of the bonds and all other project debt. Since the bonds mature January 1, 2038, management considers that date to be the effective termination date of the License Agreement.

In order to fulfill its responsibilities under the License Agreement, the Association entered into an agreement (the Development Agreement) with Interwest Carolina Transportation Group, LLC (the Developer) whereby the Developer agreed to perform the obligations of the Association under the License Agreement with respect to construction of the Southern Connector and has assumed various additional responsibilities with respect to the construction. In order to fulfill its responsibilities under the Development Agreement, the Developer in turn entered into contracts with various subcontractors for the performance of certain obligations. The Developer agreed to complete the construction of the Southern Connector at a guaranteed price of $173,802,263, which includes acquisition of all rights of way, relocation of utilities and railroads, and all design and construction activities including toll plazas, toll collection equipment, operations systems and other costs. The Developer commenced construction on February 27, 1998. On February 23, 2001, the Association received notification from the Department of its acceptance of the roadways and bridges, thereby permitting the Association to commence operations of the South Connector. The Southern Connector was opened to the public on February 27, 2001. At that time, traffic was allowed on the Southern Connector for free for a two-week introductory period. Toll collection operations began on March 14, 2001. Substantial completion was reached on July 22, 2001.

On December 28, 2000 the Association entered into a contract (the Operations Contract) with Southern Interwest, LLC (the Contractor) whereby the Contractor operated the Southern Connector on behalf of the Association for a fee. This initial Operations Contract was for a period of four years. Under the Operations Contract, tolls for the use of the southern Connector were collected on behalf of the Association. Toll revenues are deposited into the Revenue Fund and applied as described in Note 1, herein. Ninth in priority, the Association will be required to pay a license fee to the Department in the amount of $125,000 per month for a period of 25 years, and of $1 per month thereafter for the remainder of the term of the License Agreement. Payment of the monthly license fees are to commence on the first day of the calendar month following the first anniversary of the final completion date of the Southern Connector. So long as any project debt remains outstanding, any license fees not paid when due will be deferred and will accrue interest at a rate of 5% per annum compounded annually.

The Association's rights under the License Agreement as described above constitute an intangible asset that is valued and recorded at an amount equal to the cost of construction of the Southern Connector, including related capitalized interest.

The Department is responsible for maintaining the Southern Connector (costs of maintenance are to be reimbursed by the Association in eight priorities in the flow of funds set forth in Note 1) and will be responsible for setting the toll rates in accordance with the terms of the license Agreement. The SC 153 Extension, the costs of which are not included in the Association’s financial statements, is operated, maintained, renewed and replaced by the Department as part of the South Carolina highway system.

Also, under the terms of the Operations Contract, the Contractor is responsible for all work relating to operations of the Southern Connector and all obligations of the Association under the License Agreement relating to the operation, toll operation, repair, maintenance and insurance of the Southern Connector. The Operations Contract originally expired December 31, 2004, and provided renewal options of successive one-year terms, upon the mutual agreement of the parties. Effective December 31, 2002, the operations contract was terminated – see Note 21.

As compensation for the Contractor's performance under the Operations Contract, the Association paid the Contractor for certain costs of work as defined in the Operations Contract plus an annual management fee. The Operations Contract provided that any subordinated fee not paid when due would be deferred and would accrue interest at a rate of 10% per annum compounded annually. Monthly payments commenced in February 2001. The total management fee incurred during the year ended December 31, 2002, was $100,000 regular fee and $16,667 subordinate fee. The Association considers the management fee incurred following the opening of the toll road to be an operating expense. (See Note 8 for additional information.)

Effective March 1, 2002, the Association renegotiated the amount of the annual management fee. The annual fee was reduced to $100,000 payable in monthly installments. The subordinated fee of $100,000 was eliminated. The subordinate fee amount paid through February 2002 was the $16,667. All employees who assist the Contractor in fulfilling its obligations and responsibilities under the Operations Contract were under the direction and control of the Contractor and were not considered employees of the Association. Accordingly, the Contractor was responsible for payment and reporting of all salaries and wages, payroll taxes, employee benefits and insurance.

NOTE 12. PENSION PLANS:

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 of the State Budget and Control Board, 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.

The Retirement Division 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.

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 service and qualify for a survivor's benefit upon completion of 15 years credited service (five years effective January 1, 2001). Disability annuity benefits are payable to employees totally and permanently disabled provided they have a minimum of five years credited service (this requirement does not apply if the disability is the result of a job related injury). 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, 2002, the employer contribution rate became 10.70 percent, which included a 3.15 percent surcharge to fund retiree health and dental insurance coverage. The Department's actual contributions to the SCRS for the years ended June 30, 2003, 2002 and 2001 were approximately $ 11,716,000, $11,727,000 and $11,575,000 respectively, and equaled the required contributions of 7.55 percent (excluding the surcharge) for each year. Also, the Department paid employer group-life insurance contributions of approximately $233,000 in the current fiscal year at the rate of .15 percent of compensation.

The South Carolina Police Officers Retirement System (PORS) is a cost-sharing multiple employer defined benefit public employee retirement system. Generally, all full-time employees whose principal duties are the preservation of public order or the protection or prevention and control of property destruction by fire are required to participate in and contribute to the System as a condition of employment. This plan provides annuity benefits as well as disability and group-life insurance benefits to eligible employees and retirees. In addition, participating employers in the PORS contribute to the accidental death fund which provides annuity benefits to beneficiaries of police officers and firemen killed in the actual performance of their duties. These benefits are independent of any other retirement benefits available to the beneficiary.

Employees covered under PORS are eligible for a monthly pension payable at age 55 with a minimum of five years service or 25 years credited service regardless of age. In addition, employees who have five years of credited service prior to age 55, can retire yet defer receipt of benefits until they reach age 55. A member is vested for a deferred annuity with five years service. The benefit formula for full benefits effective since July 1, 1989, for the PORS is 2.14 percent of the employee's average final salary multiplied by the number of years of credited service. Disability annuity benefits and the group-life insurance benefits for PORS members are similar to those for SCRS participants. Accidental death benefits provide a monthly pension of 50 percent of the member's budgeted compensation at the time of death.

Since July 1, 1988, employees participating in the PORS have been required to contribute 6.5 percent of all compensation. Effective July 1, 2002, the employer contribution rate became 13.45 percent, which, as for the SCRS, included the 3.15 percent surcharge. The Department's actual contributions to the PORS for the years ended June 30, 2003, 2002 and 2001 were approximately $10,800, $13,200 and $9,900, respectively, and equaled the required contributions of 10.3 percent (excluding the surcharge) for each year. Also, the Department paid employer group-life insurance contributions of approximately $210 and accidental death insurance contributions of approximately $210 in the current fiscal year for PORS participants. The rate for each of these insurance benefits is .20% of compensation.

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 employee/employer contributions for each retirement system. Employee and employer contribution rates to SCRS (and PORS) 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 12 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 plans 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 plans is limited to the amounts appropriated therefore in the South Carolina Appropriation Act and amounts from other applicable revenue sources. Accordingly, the Department recognizes no contingent liability for unfunded costs associated with participation in the plans.

At retirement, employees participating in the SCRS or PORS may receive additional service credit for up to 90 days for accumulated unused sick leave.

NOTE 13. POSTEMPLOYMENT AND OTHER EMPLOYEE BENEFITS:

In accordance with the South Carolina Code of Laws and the annual Appropriation 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 and certain permanent part-time employees of the Department are eligible to receive these benefits.

The State provides postemployment 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 and Control Board for all participating State retirees except the portion funded through the pension surcharge and provided from other applicable 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, 24,000 State retirees met these eligibility requirements at June 30, 2002.

The Department recorded employer contributions expenditures within the applicable functional expenditure categories for these insurance benefits for active employees of approximately $18,053,000 for the year ended June 30, 2003. As discussed in Note 13, the Department paid approximately $4,888,000 applicable to the 3.15 percent 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 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 State General Assembly periodically directs the Retirement Systems to pay supplemental (cost of living) increases to retirees. Such increases are primarily funded from Systems' earnings; however, a portion of the required amount is appropriated from the State General Fund annually for the SCRS and PORS benefits.

NOTE 14. 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. 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 15. TRANSACTIONS WITH STATE ENTITIES / RELATED PARTIES:

Primary Entity:

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

The Department purchases goods and services from various State agencies. Total purchases from State agencies were approximately $12,044,000 for the year ended June 30, 2003.

The Department sells supply items and provides services for various State agencies. Total sales to State agencies were approximately $401,000 for the year ended June 30, 2003.

The gasoline and special fuels tax is collected by the South Carolina Department of Revenue (DOR) and remitted on a monthly basis. Taxes collected by DOR for the State Highway Fund amounted to $381,282,824 for the year ended June 30, 2003. Gasoline tax revenues collected by DOR for the County Transportation Program Agency Fund amounted to $60,737,459 for the year ended June 30, 2003. $61,257,239 was unremitted and due to the Department by DOR at June 30, 2003.

Section 56-3-910 of the South Carolina Code of Laws provides for 20% of the motor vehicle fees collected by the South Carolina Department of Public Safety (SCDPS) are to be credited to the Department beginning with fiscal year 2002. $8,460,911 was allocated to the Department for fiscal year 2003.

The Department purchased from SCDPS on February 18, 2003 the 35% interest in the office building and lot located at 955 Park Street, Columbia, SC for $6,300,000. The charges for utilities and other costs totaling $238,347 for the period January 1, 2001 – June 30, 2001 and reported as a long-term receivable by the Department at June 30, 2002 was paid by SCDPS to the Department during the current fiscal year. During the fiscal year ended June 30, 2003, SCDPS paid the Department $472,477 for utilities and other costs related to the Park Street property.

Services received at no cost from the various offices of the State Budget and Control Board include pension plans administration, insurance plans administration, audit services, personnel management, assistance in the preparation of the State Budget, review and approval of certain budget amendments, procurement services, 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 plan contributions and health insurance premiums, insurance coverage, office supplies, printing, telephone, and interagency mail. Payments were also made to other agencies for unemployment insurance and workers' compensation coverage. The amounts of expenditures applicable to related party transactions are not readily available.

In addition, the Department transferred the following amounts to the General Fund of the State of South Carolina for its proportionate share of the cost of administration of central state services, other specified support and pay telephone revenue pursuant to the following provisions of the fiscal year 2003 Appropriations Act:

Statewide Cost Allocation Plan (Proviso 53.4)		
Collection of highway revenues	$	3,067,429
Central Service Agencies recoveries		1,872,536
Pay Telephone Revenue (Proviso 72.69)		233
Total	$	4,940,198

$4,939,965 was paid to the State during the year. $233 was unpaid and included in the financial statements in the account Due to the General Fund of the State at June 30, 2003.

The Department provided no material services free of charge to other State agencies during the fiscal year except as noted on the next page. The Department participates in the statewide dual employment program.

Workers' compensation insurance premiums for the fiscal year 2003 of $4,612,001 were paid to the State Accident Fund.

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See Note 9 regarding transactions resulting from intergovernmental agreements entered into by the Department, the South Carolina Transportation Infrastructure Bank (the Bank), and other local governments. The Department provided the Bank administrative services and clerical assistance during fiscal year 2003 for which it was paid $145,000. Allocations to other entities - State agency represented amounts paid to the Bank and totaled $22,984,451 for the year ended June 30, 2003 of which $2,954,451 was unpaid at year end. The payments were from gas tax collections and represented an amount not to exceed the one cent per gallon collected in accordance with Section 11-43-160 of the South Carolina Code of Laws for the on-going funding of construction and maintenance of highways. .

A summary of intergovernmental payables to State agencies at June 30, 2003 is as follows:

Due To / Description	
South Carolina State Infrastructure Bank	
1 cent per gallon gasoline tax	$ 2,954,451
Purchases of goods and services:	
University of South Carolina	8,954
State Budget and Control Board	117,608
S.C. Department of Health and Environmental Control	18,750
S.C. Department of Public Safety	60,388
State Treasurers Office	5,576
Clemson University	17,081
South Carolina State University	36,224
S.C. Department of Corrections	9,312
S.C. Department of Revenue	44,609
S.C. Archives & History Department	8,149
Total	$ 3,281,102

Component Unit

During the year ended December 31, 2002, the Association paid $125,012 for advertising to an advertising agency controlled by a member of the Association's Board of Directors.

NOTE 17. FEDERAL GRANTS:

The Department has grants and reimbursable contracts with the Federal government for the funding of costs related to the programs described in the grants. These funds are subject to audit and/or adjustment by the various funding sources.

Management feels that adjustments, if any, will not have a material adverse effect on the financial position of the Department. Furthermore, there is no evidence to indicate that a liability should be recorded at June 30, 2003.

NOTE 18. RISK MANAGEMENT:

Primary Entity

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 that carried in the prior year. Settled claims have not exceeded this coverage in the prior 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 deductibles.

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-insured plan except dependent and optional life premiums 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:

- Theft of, damage to, or destruction of assets
- Theft of, damage to, or destruction of assets;
- Real property and contents;
- Motor vehicles;
- Data processing equipment
- Business interruptions
- Torts; and,
- Medical malpractice claims against covered employee for nurse.

The IRF is a self-insurer and purchases reinsurance to obtain certain services and specialized coverage and to limit losses in the areas of certain property and equipment and auto liability. Reinsurance permits partial recovery of losses from re-insurers, but the IRF remains primarily liable. The ISF's rates are determined actuarially.

State agencies and other entities are the primary participants in the State's Health and Disability Insurance Fund and ISF.

The Department obtains coverage up to $50,000 through a commercial insurer for employee fidelity bond insurance for the Executive Director for losses arising from theft or misappropriation. Employee fidelity bond coverage is not maintained on the Department's Commission members or its other employees. The Department self-insures itself for any losses because it feels the likelihood of losses are remote.

The Department has not transferred the portion of the risk of loss related to insurance policy deductibles and limits for capital assets and fidelity coverages to a State or commercial insurer. The Department has not reported an estimated claims loss expenditure, and the related liability at June 30, 2003, based on the requirements of GASB Statement No. 10 and No. 30 which state that a liability for claims must be reported only if information prior to issuance of the financial statements indicates that it is probable that an asset has been impaired or a liability has been incurred on or before June 30, 2003 and the amount of the loss is reasonably estimable. Liabilities include an amount for incurred but not reported (IBNR) losses when it is probable a claim will be asserted. Claims liabilities when recorded are based on estimates of the ultimate cost of settling known but not paid claims and IBNR claims at June 30 using past experience adjusted for factors that would modify past experience.

In management's opinion, claims losses in excess of insurance coverage, except as mentioned above for certain tort claims, 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; and, therefore, no loss accrual has been recorded.

Component Unit

The Association is exposed to various types of risk including loss related to torts; theft of, damage to, and destruction of assets; injuries to construction workers and others; professional design; and damage to property of others. The Association obtained commercial insurance covering all of its known risks of loss as follows:

Automobile Liability	Professional Design
Worker's Compensation	Crime
Directors and Officers	Force Majeure
Builders Risk	General Liability

No claim settlements have exceeded insurance coverage during the previous three years. There were no significant reductions in insurance coverage during the year ended December 31, 2002.

NOTE 19. OTHER LIABILITIES – COMPONENT UNIT

Accrued Interest Payable

At December 31, 2002, accrued interest payable was $1,765,750, which consisted of the Senior Current Interest Bond (Series 1998A) payment due January 1, 2003. Interest is paid January 1 of each year to holders of the Senior Bonds at rates of 5.25% and 5.375% per annum.

Requisitions

Requisitions payable consisted of requisitions for payment of construction costs and services that had been incurred as of December 31, 2002, but were not yet paid. The Association's engineer approves all requisitions prior to payment from the Construction Fund. In addition to the requisitions payable amounts, $1,850,000 has been accrued as an early completion bonus due to the Developer. (See Note 20 for additional information pertaining to the early completion bonus.)

NOTE 20. OTHER MATTERS – COMPONENT UNIT

In prior years, the Association was a Development Stage Enterprise focused on construction of the Southern Connector. During the Development Stage, expenses incurred by the Association increased its net deficit, since toll road operations had not begun and no revenues were earned. The road was opened to public traffic in early 2001 and toll collection commenced March 14, 2001.

Since commencing operations, the Southern Connector has experienced significantly lower traffic counts than those projected during the Traffic and Revenue Study performed in 1997 during the planning phase of the Southern Connector Project. An average of 10,868 toll transactions per day occurred during the 12 months of operations in 2002 – less than half of the traffic volume projected in the Revenue Study.

Several factors have contributed to this shortfall. The Southern Connector is the first toll road in Upstate South Carolina. Since citizens in the Greenville, South Carolina vicinity are unaccustomed to using toll roads, they have been resistant to the concept of paying tolls. Furthermore, the Southern Connector was envisioned as a means of fostering development in southern Greenville County, and its corridor runs through a largely undeveloped area, serving as a thruway connecting Interstate 385 with Interstate 85. This lack of development in the area, coupled with the fact that the Southern Connector was opened almost nine months ahead of schedule, means that the demand for the toll road is in its infancy. In addition, current economic conditions have slowed potential new economic development along the Southern Connector.

Due to the factors discussed above, the Association's revenues for 2002 fell short of amounts anticipated, and the Association suffered a decrease in net assets (loss) of $17,225,840 for 2002.

NOTE 21. CONTINGENCIES AND SUBSEQUENT EVENTS:

PRIMARY ENTITY:

The Department is a defendant in various lawsuits arising from the conduct of its normal business primarily regarding right of ways. Although any litigation has an element of uncertainty, it is management's and legal counsel's opinions that the outcome of any litigation pending or threatened, or the combination thereof, will not have a materially adverse effect on the financial position of the Department. The risk of material loss in excess of insurance coverage is unlikely. Furthermore, there is no evidence that an additional expenditure and liability should be recorded.

Through June 30, 2003 the State's Joint Bond Review Committee approved the issuance by the Department not to exceed $1,072,000,000 in General Obligation State Highway Bonds for projects. As of June 30, 2003, $598,080,000 in bonds have been issued. The Commission authorizes the timing and amounts of the various bond issues to be determined by the Department's staff.

In May, 1997, the State Budget and Control Board authorized the Department to transfer an island consisting of approximately 8,000 acres to the South Carolina Department of Natural Resources (DNR), another State agency upon exhaustion of mitigation banking credits. The acreage was banked to provide an offset for environmentally sensitive lands that are required for future highway projects. An agreement to transfer the land to DNR will be executed when the Department has used up all the mitigation banking credits.

In connection with the allocation of assets pursuant to the January 19, 2001 agreement between the Department and Public Safety, as surveys, legal, and other requirements are met to the satisfaction of both agencies, quit claim deeds are prepared and recorded on the applicable county records. Both agencies have agreed to execute the deeds necessary to make the property transfers and to share equally in the cost of preparation and recording of such deeds and plats as may be necessary to effectuate the transfers. The Department's property is to be titled in the name of the Department and Public Safety's property is to be titled in such manner as directed.

COMPONENT UNIT:

On March 21, 2003, the Trustee sent Notice #2 to the registered owners of the Associations bonds. In such notice, the Trustee informed the bondholders of a dispute concerning the interpretation of Section 505 (1) of the Trust Agreement. As previously communicated to the bondholders, on January 2, 2003, the Trustee made a withdrawal of approximately $72,320 from the Senior Bonds Debt Service Reserve Account in order to pay a portion of an interest payment then due on the Association's Series 1998A Senior Current Interest Bonds. On February 6, 2003, the Trustee notified the Association by letter that there were not sufficient revenues available to replenish the Senior Bonds Debt Service Reserve Account to the level that existed prior to such withdrawal. The Trustee contends that Section 505(1) of the Trust Agreement requires the Association to deliver to the Trustee on or before the last day of each month monies sufficient to replenish the Senior Bonds Debt Service Reserve Account to the Senior Bonds Debt Service Reserve Account requirement. The Association reminded the Trustee that the Indenture is a "lock box" structure in that all of the revenues available to pay the Bonds and replenish the funds and accounts of the Indenture are already transferred to the Trustee. The Association contends that the provisions of Section 505(1) merely direct the Trustee as to the disposition of revenues among the various accounts and the ordering of transfers of such revenues. The Trustee and the Association were unable to resolve their differences in the interpretation of such section of the Trust Agreement and the Trustee notified the bondholders that an event of Default has occurred under Section 902(3) of the Trust Agreement. The Trustee informed bondholders it intends to forebear from initiating legal actions in connection with the alleged default and solicited their comment and direction. The Trustee and the Association entered into a Tolling Agreement dated as of April 16, 2003, (the "Tolling Agreement") whereby, among other matters, the Trustee and the Association agreed that the above-described event would not be deemed to be and Event of Default under the Trust Agreement during the term of the Tolling Agreement. In the Tolling Agreement, the Association agrees not to assert any defense it may have based on the lapse of time under the statute of limitations during the term of the Tolling Agreement relating to the above-described events.

As explained in Note 11, the Association contracted with Southern Interwest, LLC to provide management and administration services, as well as other services for the Association. This contract was terminated effective December 31, 2002, and the employees of Southern Interwest, LLC responsible for operating the Southern Connector became employees of the Association on January 1, 2003.

On January 8, 2003, Standard and Poors downgraded its rating of the Senior Bonds (Series A and Series B) from BBB- to B- with a stable outlook. The Association had not requested a bond rating for its Series 1998C bonds.

In January of 2003, the attorneys representing the Connector 2000 Association, Inc. and those representing the developer reached an agreement on the amount of a completion bonus that had been in dispute. The total amount due the developer was settled to be $2,322,500. Of the amount $525,000 had been accrued as a liability in the prior year. The remaining $1,797,500 has been accrued and capitalized into the interest in License Agreement with Department. $472,500 of the settlement amount had been paid as of December 31, 2002. The balance of such bonus was paid by the Trustee on January 27, 2003, reducing the balance remaining in the construction fund to $776,947.

NOTE 22. PRIOR PERIOD RECLASSIFICATIONS/ ADJUSTMENTS:

The Department noted errors that required the reclassification of certain capital assets from one category to another. Reclassifications were made as of July 1, 2002 to correct these classifications.

Also, the Department made corrections of errors involving the application of accounting principles regarding the capitalization of certain infrastructure. Adjustments were made as of July 1, 2002 to correct these errors. $3,582,533 of costs attributable to certain projects were included in construction in progress – infrastructure that did not meet the capitalization limit requirements and $675,959 of costs attributable to an infrastructure project were not included in the amount capitalized.

The effects of the reclassifications and the accounting and reporting changes on the various account balances as of July 1, 2002 in the Department-wide financial statements are as follows:

Capital Asset Category	Balances, as previously reported	Reclassifications	Prior Period Adjustments	Balances, as restated
Capital assets not being depreciated:				
Right of ways land	$ 402,711,642	$ 108,392,090	$ -	$ 511,103,732
Construction in progress - infrastructure	$ 3,116,171,006	$ (108,392,090)	$ (3,582,533)	$ 3,004,196,383
Other capital assets:				
Infrastructure	$ 7,018,204,139	$ -	$ 675,959	$ 7,018,880,098
Equipment and furniture	$ 109,450,233	$ 1,588,306	$ -	$ 111,038,539
Vehicles	$ 87,841,793	$ (1,588,306)	$ -	$ 86,253,487
Net assets	$ 8,483,088,870	$ -	$ (2,906,574)	$ 8,480,182,296

The Department determined that certain revenues from taxes and fees and expenses for allocation to other entities – Agency Fund were omitted from the statement of activities for the year ended June 30, 2002. The effects of the omissions are as follows:

	Balances, as previously reported	Additions	Balances, as restated
Expenses	$ 545,742,714	$ 60,241,208	$ 605,983,922
General revenues:			
Taxes and fees	$ 385,944,118	$ 60,241,208	$ 446,185,326

The Department determined that certain expenditures for capital outlay for infrastructure - road and bridge network and revenues from other financing sources from intergovernmental payable – State agency (contribution payable) were omitted from the statement of revenues, expenditures and changes in fund balance for the State Highway Fund for the year ended June 30, 2002. The effect of the omissions are as follows:

	Balances, as previously reported	Additions	Balances, as restated
Expenditures:			
Capital outlay:			
Infrastructure - road and bridge network	$ 481,567,682	$ 40,082,702	$ 521,650,384
Total Expenditures	$ 1,052,829,541	$ 40,082,702	$ 1,092,912,243
Other financing sources (uses):			
Proceeds from intergovernmental payable - State agency (contribution payable)	$	$ 40,082,702	$ 40,082,702
Total other financing sources (uses)	$ (2,403,551)	$ 40,082,702	$ 37,679,151

SOUTH CAROLINA DEPARTMENT OF TRANSPORTATION

SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE
BUDGET AND ACTUAL - GENERAL FUND
FOR THE YEAR ENDED JUNE 30, 2003

	Budgeted Amounts		Actual	Variance with Final
REVENUES:	Original	Final	Amounts	Budget
State appropriations	$ 485,818	$ 444,268	$ 444,268	$ -
EXPENDITURES:				
Public transportation	485,818	444,268	444,268	
Total expenditures	485,818	444,268	444,268	
NET CHANGE IN FUND BALANCE	-	-	-	-
FUND BALANCE - BEGINNING		-	-	-
FUND BALANCE - ENDING	$ -	$ -	$ -	$ -

SOUTH CAROLINA DEPARTMENT OF TRANSPORTATION

COMBINING STATEMENT OF CHANGES IN ASSETS AND LIABILITIES -
ALL AGENCY FUNDS
FOR THE YEAR ENDED JUNE 30, 2003

	Assets				
	Cash and Cash Equivalents		Accrued Interest Receivable	Due from State Highway Fund	Total Assets
RIGHT OF WAYS					
Balances, June 30, 2002	$ 328,347		$	$	$ 328,347
Additions	184,886				184,886
Deductions	(185,351)				(185,351)
Balances, June 30, 2003	327,882				327,882
SPECIAL DEPOSITS					
Balances, June 30, 2002	1,219,385				1,219,385
Additions	1,708,117				1,708,117
Deductions	(675,403)				(675,403)
Balances, June 30, 2003	2,252,099				2,252,099
COUNTY TRANSPORTATION PROGRAM					
Balances, June 30, 2002	107,994,973		1,136,881	5,161,769	114,293,623
Additions	83,017,733		4,535,872	60,737,459	148,291,064
Deductions	(85,820,368)		(4,524,596)	(55,627,617)	(145,972,581)
Balances, June 30, 2003	105,192,338		1,148,157	10,271,611	116,612,106
TOTALS - ALL AGENCY FUNDS					
Balances, June 30, 2002	109,542,705	(1)	1,136,881	5,161,769	115,841,355
Additions	84,910,736		4,535,872	60,737,459	150,184,067
Deductions	(86,681,122)		(4,524,596)	(55,627,617)	(146,833,335)
Balances, June 30, 2003	$ 107,772,319	(1)	$ 1,148,157	$ 10,271,611	$ 119,192,087

(1) Includes unrealized appreciation of $4,760,104 at June 30, 2003 and $2,808,704 at June 30, 2002.

SOUTH CAROLINA DEPARTMENT OF TRANSPORTATION

COMBINING STATEMENT OF CHANGES IN ASSETS AND LIABILITIES -
ALL AGENCY FUNDS
FOR THE YEAR ENDED JUNE 30, 2003

	Liabilities				
	Accounts Payables/ Other Liabilities	Deposits for Right-of-Ways	Special Deposits and Bonds	Funds Held for Counties	Total Liabilities
RIGHT OF WAYS					
Balances, June 30, 2002	$	$ 328,347	$	$	$ 328,347
Additions		192,586			192,586
Deductions		(193,051)			(193,051)
Balances, June 30, 2003		327,882			327,882
SPECIAL DEPOSITS					
Balances, June 30, 2002	814,681		404,704		1,219,385
Additions	1,697,258		1,696,513		3,393,771
Deductions	(675,653)		(1,685,404)		(2,361,057)
Balances, June 30, 2003	1,836,286		415,813		2,252,099
COUNTY TRANSPORTATION PROGRAM					
Balances, June 30, 2002	6,127,905			108,165,718	114,293,623
Additions	14,877,680			140,822,830	155,700,510
Deductions	(6,600,564)			(146,781,463)	(153,382,027)
Balances, June 30, 2003	14,405,021			102,207,085	116,612,106
TOTALS - ALL AGENCY FUNDS					
Balances, June 30, 2002	6,942,586	328,347	404,704	108,165,718	115,841,355
Additions	16,574,938	192,586	1,696,513	140,822,830	159,286,867
Deductions	(7,276,217)	(193,051)	(1,685,404) -	(146,781,463)	(155,936,135)
Balances, June 30, 2003	$ 16,241,307	$ 327,882	$ 415,813	$ 102,207,085	$ 119,192,087

SOUTH CAROLINA DEPARTMENT OF TRANSPORTATION
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

FOR THE YEAR ENDED JUNE 30, 2003

Federal Grantor / Program Title	Federal CFDA Number	Total Federal Expenditures	Expenditures To Subreceipients
Direct Programs:			
U.S. Department of Transportation			
Highway Planning and Construction	20.205	$ 421,683,121	$
Federal Transit-Capital Investment Grants	20.500	2,879,535	2,879,535
Federal Transit-Metropolitan Planning Grants	20.505	482,711	482,711
Formula Grants for Other Than Urbanized Areas	20.509	5,117,140	2,541,377
Capital Assistance Program for Elderly Persons and Persons with Disabilities	20.513	1,045,867	1,018,704
Job Access: Reverse Commute	20.516	678,108	591,617
Total Direct Programs		431,886,482	7,513,944
Indirect Programs:			
Federal Emergency Management Agency			
Passed Through SC Emergency Preparedness Division Public Assistance Grants	83.544	155,476	-
Totals		$ 432,041,958	$ 7,513,944

NOTE: The Department used the accrual basis method of accounting in preparing the above schedule. This is the same basis of accounting used by the Department in the preparation of its annual financial statements. 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.

ROGERS & LABAN, PA
CERTIFIED PUBLIC ACCOUNTANTS AND FINANCIAL CONSULTANTS

REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING 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 the South Carolina Department of Transportation (the Department) as of and for the year ended June 30, 2003, and have issued our report thereon dated October 29, 2003. 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.

Compliance

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 grants, 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.

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 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 assertion of management in the financial statements. The reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as items 03-1–03-3.

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 misstatements 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 are material weaknesses.

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We also noted two other matter involving the internal control over financial reporting which are described as items 03-4 and 03-5.

This report is intended solely for the information and use of the Governor of the State of South Carolina, Commission members and management of the Department, and federal awarding agencies and is not intended to be and should not be used by anyone other than these specified parties.

Rogers & Laban, PA

October 29, 2003

REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH 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 audited the compliance of the South Carolina Department of Transportation (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 each of its major federal programs for the year ended June 30, 2003. The Department's major federal programs are 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 each of its major federal programs 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 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.

In our opinion, the Department complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2003.

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 of the State of South Carolina, Commission members and management of the Department, and federal awarding agencies and is not intended to be and should not be used by anyone other than these specified parties.

Rogers + Laban, PA

October 29, 2003

SOUTH CAROLINA STATE DEPARTMENT OF TRANSPORTATION

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2003

SUMMARY OF AUDITOR'S RESULTS

Financial Statements

1. Type of auditor's report issued: Unqualified Opinion

2. Internal control over financial reporting:
   - Material weaknesses identified: __x__ yes _____ no
   - Reportable conditions identified not considered to be material weaknesses? __x__ yes _____ no

3. Non-compliance material to the Financial Statements noted? _____ yes __x__ no

Federal Awards

4. Internal control over major programs:
   - Material weaknesses identified: _____ yes __x__ no
   - Reportable conditions identified not considered to be material weaknesses? _____ yes __x__ no

5. Type of auditor's report issued on compliance for major programs: Unqualified Opinion

6. Any audit findings disclosed that are required to be reported in accordance with Circular A-133, Section .510(a)? _____ yes __x__ no

7. Identification of major programs:

CFDA Number	Name of Federal Program
20.205	Highway Planning and Construction
20.509	Formula Grants for Other Than Urbanized Areas

8. Dollar threshold used to be distinguished between Type A and Type B Programs: $ 3,000,000

9. Auditee qualified as low-risk auditee? _____ yes __x__ no

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 generally accepted government auditing standards.

03-1 FINANCIAL RECORDS DEFICIENCIES

Condition:

Several conditions as noted below required additional work and procedures to be performed at year-end to ensure that the financial statements were presented in accordance with GAAP.

- The Department did not post all of the adjusting journal entries to its general ledger that were made in connection with the audit of the Department's financial statements for the year ended June 30, 2002. This resulted in the fund balance in the Department's general ledger being $5,443,111 different from the audited financial statements as of June 30, 2002. Several adjusting journal entries were required to correct this balance as of June 30, 2003.

- The following deficiencies were noted regarding the accounting for capital assets:
    - The Department purchased the 35% interest in the Park Street property from the SC Department of Public Safety and did not record the purchase as a capital asset addition.

    - The Department included the cost of right of ways land acquired during fiscal year 2003 in the construction in progress account instead of the right of ways land account.

    - The accumulated depreciation for certain infrastructure capital assets as of June 30, 2002 was not included in the beginning balance for accumulated depreciation as of July 1, 2002.

    - The category groupings of depreciation schedules for movable equipment and furniture, including vehicles, were not maintained so that changes to accounts and account totals were readily available to prepare the schedule of capital assets and changes thereto in accordance with the categories prescribed by the South Carolina Office of Comptroller General.

    - For current year additions, enhancements and labor associated with extending the useful lives of previously purchased capital assets were added to the original costs of the capital asset and not separately listed on the year-end depreciation schedules. This resulted in the additional costs being treated as purchased on the original purchase date of the capital asset for depreciation calculation purposes. Thus, current year depreciation and accumulated depreciation were overstated for these assets. Year-end adjustments were made to correct this deficiency.

- Bond issuance costs of $322,560 that were paid for the underwriter's fee from closing proceeds were netted against the revenue account - bond proceeds. Also, $77,960 for accrued interest sold was included in the revenue account - bond proceeds instead of accrued interest payable.

- Certain bond issuance costs were paid prior to June 30, 2003 from the Series 2003B cost of issuance cash account and not recorded by the Department. Also, certain other issuance costs totaling $63,855 were incurred prior to June 30, 2003 and were not recorded as accounts payable.

- Schedules and reports that were prepared by the Department and furnished to the audit firm to support certain financial activity were incorrect and had to be reworked. These deficient schedules included inventories, accrued compensated absences and other accounts.

Similar findings were included in prior management letters.

Cause:

The Department's general ledgers, supporting schedules and reports were not maintained in a format to produce accurate and complete financial statements in accordance with GAAP.

Effect:

Failure to maintain complete financial records could result in possible misstatements in the Department's financial statements and other financial reports.

Criteria:

State regulations, good business practices and GAAP require the Department to maintain complete and accurate financial accounting records that properly reflect all of its financial activities and support its financial statements and other financial reports.

Recommendation:

We recommend that the Department:

- Maintain financial records that fully convert general ledger account balances to the GAAP reporting basis, including posting adjusted journal entries that were made as of June 30, 2003.

- Ensure that all reports and schedules that are prepared to support financial activities and account balances are complete and accurate.

- Review all transactions that are to be posted to its general ledger to ensure they are properly prepared in accordance with GAAP.

03-2 ACCOUNTS RECEIVABLE DEFICIENCIES

Condition:

The Department's accounts receivable balances include amounts from numerous sources, including other State agencies, local governments and other entities. During our testing of subsequent receipts, approximately $3.3 million of receipts were recorded in fiscal year 2004 that should have been recorded in fiscal year 2003 and treated as accounts receivable.

Similar findings were included in the prior management letter.

Cause:

The Department's staff did not accurately identify and record all of its accounts receivable at year-end.

Effect:

The Department's failure to include all accounts receivable results in misstatements of assets and revenues in its financial statements.

Criteria:

Good accounting practices require the recording of all accounts receivable due to the Department as of each year-end.

Recommendation:

We recommend that the Department follow its fiscal year-end revenue and account receivable cutoff procedures to ensure that all receivables and related revenues of the Department are recorded as of each year-end.

03-3 IMPROVEMENTS NEEDED OVER ACCOUNTING FOR PARTICIPATION AGREEMENTS

Condition:

A review of the client prepared schedule for outstanding participation agreements and supporting documentation disclosed the following deficiencies:

- Several projects on the prepared schedule did not agree with the allotment ledger posting master listing of total project costs.
- Our tests of the various contracts disclosed several old agreements for which there was no actual written agreement. Collection of amounts due from these contracts appears to be question.
- Two projects reflected overpayments by a third party and the schedule disclosed these overpayments as deferred revenue instead of accounts payable.
- We noted several errors on the Department's original schedule such as contracts paying specific amounts instead of a percentage of total project costs.
- There appears to be a lack of communication between the Program Development Office, the Contract Audit Service Office, and the financial accounting staff regarding the setting up and administration of the contracts.

Year-end adjustments were required to account balances for participation agreement accounts receivable, deferred revenue, accounts payable and revenue.

Similar findings were included in prior management letters.

Cause:

The Department's accounting staff did not correctly update all the components of the participation agreement schedule and prepare the required adjusting entries for outstanding participation agreements as of year-end.

Effect:

Failure to update the financial activity for participation agreements on a monthly basis increases the likelihood that the financial information will be inaccurate and incomplete because of errors and omissions. Without timely updating of accurate and complete project information, the accounting records and schedules will not provide management with current information for monitoring projects.

Criteria:

Good business practices and generally accepted accounting principles require accurate and complete financial data to be maintained to support the asset, liability and revenue account balances for participation agreements.

Recommendation:

We recommend that the Department prepare and update participation schedules monthly that reconcile to the control records maintained in the Contract Audit Services Office that will provide accurate and complete accounting of all participation agreements. The schedule should be prepared and updated for changes as of each month end to help ensure it is mathematically correct; properly reflects all contract data; properly includes all contracts completed and closed during the current fiscal year; and, properly reflects all amounts due and/or deferred revenues. This schedule and all supporting documentation should be reviewed and approved by a designated senior management staff person.

FINDINGS AND QUESTIONED COSTS FOR FEDERAL AWARDS

No findings and questioned costs for federal awards were noted that are required to be reported under Section .510(a) of OMB Circular A-133.

SOUTH CAROLINA DEPARTMENT OF TRANSPORTATION

OTHER MANAGEMENT LETTER COMMENTS
FOR THE YEAR ENDED JUNE 30, 2003

We noted the following matters involving the internal control over financial reporting:

03-4 ACCOUNTS PAYABLE DEFICIENCIES

Condition:

We noted deficiencies regarding accounts payable. They include the following:

- The schedule of additional accounts payable for the current fiscal year included expenditures applicable to the subsequent fiscal year. This resulted in accounts payable being overstated by approximately $349,000.

- See item 03-1 regarding bond issuance costs.

Similar findings were included in the prior management letters.

Cause:

The Department's staff did not identify and accurately record its accounts payable as of year-end.

Effect:

The failure to properly record all accounts payable results in misstatements of liabilities and expenses/expenditures in the Department's financial statements.

Criteria:

Good accounting practices require the correct recording of all accounts payable as of each year-end.

Recommendation:

We recommend that the Department implement fiscal year-end expenditure and liability cutoff procedures to ensure that all accounts payable are recorded as of each year-end.

03-5 INVENTORY DEFICIENCIES

Condition:

We noted the following deficiencies during our testing of inventories:

- Several quantity differences were noted at one site. This resulted in a complete recount being conducted.

- Errors were noted in the schedules that summarized the inventory quantities, unit prices and extended totals.

Similar findings were noted in the prior management letter.

Cause:

The Department has procedures in place to count inventories and prepare summarized inventory schedules. It appears that these procedures were not followed.

Effect:

The failure to properly count and recap the inventories will result in a misstatement of asset and expenditure amounts.

Criteria:

Good accounting procedures require the Department to properly count and value its inventories.

Recommendation:

We recommend that the Department's personnel responsible for inventory counts and the recap thereof follow the Department's procedures.

SOUTH CAROLINA DEPARTMENT OF TRANSPORTATION

STATUS OF PRIOR MANAGEMENT LETTER COMMENTS
FOR THE YEAR ENDED JUNE 30, 2003

During our current audit, we reviewed the status of corrective action taken on the management letter comments reported in the prior auditor's report on the financial statements of the Department dated October 21, 2002 resulting from the audit of the financial statements for the year ended June 30, 2002. We found that adequate corrective action was taken for the following management letter comments:

- Cash Deficiencies
- Capital Asset Deficiencies
- Cash Disbursement Deficiencies

The other prior year findings are repeated in the current year's Schedule of Findings and Questioned Costs and/or Other Management Letter Comments

APPENDIX A

CORRECTIVE ACTION PLAN

SCDOT
South Carolina
Department of Transportation

CORRECTIVE ACTION PLAN

November 12, 2003

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

Dear Mr. Wagner:

The South Carolina Department of Transportation respectfully submits the following Corrective Action Plan for the year ended June 30, 2003.

This Plan outlines actions taken, or to be taken, to address "reportable conditions" contained in the audit report prepared by Rogers and Laban, PA, CPA's dated October 29, 2003. Each audit recommendation is repeated prior to our response and numbered as in the audit report.

FINDINGS RELATED TO THE FINANCIAL STATEMENTS

03-1 Financial Records Deficiencies

Recommendation:

We recommend that the Department:

- Maintain financial records that fully convert general ledger account balances to the GAAP reporting basis, including posting adjusted journal entries that were made as of June 30, 2003.
- Ensure that all reports and schedules that are prepared to support financial activities and account balances are complete and accurate.
- Review all transactions that are to be posted to its general ledger to ensure they are properly prepared in accordance with GAAP.

SCDOT Corrective Action

The Department maintains its records on the Modified Accrual basis of accounting, the method used by most governmental units. All funds are self-balancing. Year-end entries are made to convert to the full accrual basis, and to properly record, to the extent possible, additional transactions to report the financial position of the Department in accordance with GAAP.

- The Department agrees to post all adjusting entries feasible. Due to the timing of the closing process of the Department's records, there are certain adjustments that cannot be made at the time of the audit. A reconciling schedule will be provided to the audit staff of all entries posted and those not posted to the accounting records.

- The Department did not receive information from the Treasurer's office in the normal course of business to record bond issuance cost. In the future, we will ensure that all information relating to the issuance of bonds is received and properly recorded.

- The Department concurs that all schedules created for the audit should be correct. The Accounting and IT Services areas have already researched the way schedules are electronically prepared and will ensure that the same financial records are used to create any schedules requested by the audit firm in the future.

  The Department has examined all transactions noted by the auditors and will ensure that all future general ledger transactions are prepared in accordance with GAAP.

03-2 Accounts Receivable Deficiencies

Recommendation:

We recommend that the Department follow its fiscal year-end revenue and account receivable cutoff procedures to ensure that all receivables and related revenues of the Department are recorded as of each year-end.

SCDOT Corrective Action

The $3.3 million in additional accounts receivable were identified after the cut-off period for the Department. Every effort was made to carefully examine cash receipts written during July and the first of August. These items did not have receipts written until after the reasonable examination period. The Department will adopt an Accounts Receivable Policy that will be used every year and will employ every effort to ensure additional receivables and revenues are properly recorded.

03-3 Improvements Needed Over Accounting for Participation Agreements

Recommendation:

We recommend that the Department prepare and update participation schedules monthly that reconcile to the control records maintained in the Contract Audit Services Office that will provide accurate and complete accounting of all participation agreements. The schedule should be prepared and updated for changes as of each month end to help ensure it is mathematically correct; properly reflects all contract data; properly includes all contracts completed and closed during the current fiscal year; and properly reflects all amounts due and/or deferred revenues. This schedule and all supporting documentation should be reviewed and approved by a designated senior management staff person.

SCDOT Corrective Action

The Department concurs with the finding. A participation agreement control schedule is prepared, reconciled, and balanced to the general ledger each month during the year. We will adopt a formal Participation Agreement Policy to be adhered to by all departments within the agency. This will ensure that all participation agreements are forwarded to the accounting and budget staff to properly record the budget, revenue, receivable, and payable entries. In order to convert to a full GAAP basis, we will continue to prepare a modified schedule at year-end to reflect deferred revenue.

OTHER MANAGEMENT LETTER COMMENTS

03-4 Accounts Payable Deficiencies

Recommendation:

We recommend that the Department implement fiscal year-end expenditure and liability cutoff procedures to ensure that all accounts payable are recorded as of each year-end.

SCDOT Corrective Action:

The Department implemented a formal expenditure and liability cut-off procedure for fiscal year ending June 30, 2003. The Department recorded $46.9 million in payable transactions through fiscal month 13 with the Comptroller General, and an additional $17.8 million in transactions through fiscal months 01 and 02 of the current year. The audit staff was supplied an additional schedule of $5.5 million to be recorded for financial statement purposes. The overstatement of $349,000 in payables represents approximately one-half of one percent of total accounts payable. The Department will continue to search diligently for all accounts payable at year-end.

03-5 Inventory Deficiencies

Recommendation:

We recommend that the Department's personnel responsible for inventory counts and the recap thereof follow the Department's procedures.

SCDOT Corrective Action:

The Department concurs with the recommendation. Instructions on accounting for inventory (stock) items are sent to each responsible unit every year. The director of the affected areas will stress the importance of correct inventory counts in the future.

If you need additional information, please do not hesitate to contact me.

Sincerely,

Robert W. Wilkes, Jr. CPA
Director of Financial Management