

November 20, 1998

The Honorable David M. Beasley, Governor
and
Members of the Board of Trustees
The Medical University of South Carolina
Charleston, South Carolina

This report on the internal control of The Medical University of South Carolina for the fiscal year ended June 30, 1998, was issued by Rogers & Laban, P.A., 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,

Thomas L. Wagner, Jr., CPA
State Auditor

TLWjr/trb

THE MEDICAL UNIVERSITY OF SOUTH CAROLINA
INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL
JUNE 30, 1998

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL

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

In planning and performing our audit of the financial statements of The Medical University of South Carolina (MUSC), Charleston, South Carolina, for the year ended June 30, 1998, we considered its internal control 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. However, we noted certain matters as detailed on pages 2 - 5 involving the internal control and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control that, in our judgment, could adversely affect the organization's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material 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 internal control would not necessarily disclose all matters in internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. We believe the conditions noted on pages 2 - 4 are material weaknesses.

We also noted other matters involving internal control and its operation as detailed on pages 5 - 7.

This report is intended solely for the information and use of the board of trustees, management and others within the organization. This restriction is not intended to limit the distribution of this report which, upon acceptance by the State Auditor's Office, is a matter of public record.

Columbia, South Carolina
October 23, 1998

MANAGEMENT LETTER COMMENTS

A. MATERIAL REPORTABLE CONDITIONS

SCHEDULE OF AMOUNTS DUE FROM OTHER STATE AGENCIES INACCURATE

Our review of the schedule that the University prepared of receivables from other state agencies disclosed the following deficiencies:

1. The schedule contained approximately \$627,000 of receivables that should not have been included because the amounts had already been received.
2. A receivable for approximately \$535,000 was omitted.
3. A receivable was included for \$67,604 instead of the correct amount of \$55,104.

A finding similar to item 1 was cited in last year's management letter. The errors appear to occur because no one timely followed up on the old receivables to see if they had been paid and because the individual responsible for preparing the schedule did not adequately review it for accuracy.

We recommend that additional care be exercised in the preparation of this schedule to ensure that only those receivables that have not been collected are included and that all valid receivables be included for the correct amounts. Procedures should be put in place to ensure that all uncollected receivables are followed up on in a timely manner.

ERRORS IN ACCOUNTS PAYABLE SCHEDULE

Our audit of accounts payable disclosed the following deficiencies:

1. The University included approximately \$270,000 in accounts payable for goods or services which were not received as of June 30, 1998.
2. Our review of invoices paid subsequent to June 30 disclosed \$468,000 in accounts payable that the University should have recorded as accounts payable which were not recorded.
3. There were invoices which were not entered into the accounts payable system or reviewed to determine if they were accounts payable. It did not appear that the University was going to review these invoices to determine if any should be included in accounts payable. After the review, additional accounts payable of \$336,000 had to be recorded.
4. Accounts payable were overstated by approximately \$244,000 because manual checks that paid the invoices were not entered into the accounts payable system. Also, cash was overstated by the same amount. Some of the manual checks were from February, 1998.

We recommend that the University review all of its procedures in preparing the schedules to support accounts payable at year end to ensure that invoices are not included for goods or services which were not received and all accounts payable are included. Additionally, the University should record all manual checks at least weekly.

DEFICIENCIES NOTED IN ACCOUNTING FOR GRANTS

In reviewing the grants receivable schedule that was prepared to support the receivables for grants which had been expended, but for which reimbursement had not been received, we noted the following:

1. Approximately \$1,000,000 in overspent grant expenditures had not been transferred to the unrestricted current fund from the restricted current fund resulting in the recording of grants accounts receivable which are not collectible. Approximately \$416,000 of the expenditures were incurred in the year ended June 30, 1997. Grants receivable of approximately \$249,000 had to be recorded for grants for which funds had been expended and reimbursements had not been received in addition to the grants receivable amounts the University initially recorded.
2. Reimbursement requests for grants are not being filed timely, and, in some cases, are being submitted on the wrong forms. For example, some grants require billings at least quarterly and we observed that this schedule was not being observed.
3. Certain grant files could not be located which contained the grant document, financial reports filed to date and other documentation. The grant files which we reviewed did not appear to be well organized.
4. Some of the grant receivables were over one year old and there did not appear that adequate follow-up had been made as to why the receivables were not collected. We noted one receivable was over two years old.
5. The expenditures for some grants were recorded in one cost center and the offsetting revenues had been recorded in another cost center making it difficult to determine which grants had expenditures that offset the receivables recorded. The University did not offset the amounts in the two cost centers and recorded a receivable to equal the expenditures.
6. Grants receivable were overstated because the University received approximately \$85,000 in funds, which were not identified as of June 30 and were posted to the cost center to offset the expenditures.

These deficiencies resulted in an overstatement of assets, revenues and expenditures in the current restricted fund and an understatement of expenditures in the unrestricted current fund.

The failure to timely and properly bill for federal grant receivables and follow-up on their collection will result in the loss of interest earnings and could result in the loss of funds if the grants are not collected.

These errors appeared to occur because adequate care was not taken in the preparation of the grants receivable schedule and entries were not posted in a timely manner to reclassify the overexpenditure of grant funds from the restricted to the unrestricted current funds. The schedule had to be reworked three times at our request before it was considered to be materially correct.

We recommend that the University ensure that the amounts recorded for grant receivables are correct. Overspent funds should be reclassified between funds in a timely manner. Billings should be prepared in a timely manner as required by the grant documents. The grants receivable schedule should be reviewed after it is prepared by an individual with adequate accounting knowledge to ensure that it is complete and correct. In addition, the University should ensure that all grant files are available and well organized.

ENTRIES POSTED WITHOUT REVIEW OF SUPPORTING DOCUMENTATION

The University has an agreement with University Medical Associates (UMA) to split the profit or loss from the urgent care agreement on a 50/50 basis. The University recorded a payable to UMA for approximately \$77,500 when UMA actually owed them approximately \$257,000. This occurred because University personnel did not obtain and review supporting documentation to support the recording of the payable to UMA.

Generally accepted accounting principles dictate that entries should not be posted to the accounting records without supporting documentation being present. Failure to review this information resulted in UMA underreporting their net loss by approximately \$335,000 and the medical center overreporting their loss by the \$335,000.

We recommend that no entries be posted to the general ledger without supporting documentation being present and reviewed.

EQUIPMENT EXPENDITURES NOT RECONCILED TO FIXED ASSET ADDITIONS

The University did not reconcile equipment expenditures recorded in its current funds with the amount of equipment additions recorded in the investment in plant fund. The failure to perform this reconciliation resulted in equipment additions in the plant fund being understated by approximately \$4,800,000.

The failure to timely reconcile expenditures to additions could result in the misstatement of the investment in plant fund.

We recommend that the equipment additions be reconciled to the equipment expenditure account on a monthly basis.

B. OTHER REPORTABLE CONDITIONS

IMPROVEMENTS NEEDED OVER STUDENT LOANS AND ACCOUNTS RECEIVABLE

The prior year's management letter stated that the University was not regularly and timely reconciling the student loans receivable subsidiary listings to the general ledger. While this was done in a regular and timely manner this year, the required adjustments to the subsidiary and general ledger were not posted to the records. We noted that student loans advanced in July, 1997 had not been posted to the subsidiary records as of June 30, 1998.

Other deficiencies noted over student loans and accounts receivable are as follows:

1. The University did not review the adequacy and adjust the allowance for doubtful accounts for student loans receivable.
2. The subsidiary records for student accounts receivable were not reconciled to the general ledger in a timely and regularly scheduled manner.
3. The required general ledger account had not been set up to record approximately \$18,000 in student accounts receivables that had been posted to the subsidiary records.

Good accounting controls require that all balance sheet accounts be reconciled to the supporting detail in a timely manner.

We recommend that all subsidiaries for student loans and accounts receivable be reconciled to the general ledger monthly.

Procedures should be implemented to ensure that all required journal entries are posted to the general ledger or subsidiary records at the time the accounts are reconciled. The University should consider implementing a student loan and accounts receivable processing package that is integrated with the general ledger.

ERRORS NOTED IN INVENTORY COUNTS, PRICING AND LISTINGS

Our physical counts of inventory disclosed that there were four errors in the twenty-five items test counted in the pharmacy, three errors in the sixteen items test counted in the ambulatory care operating room, and three errors in the twenty items test counted in central stores. A similar finding was cited in last year's management letter.

Our tests also revealed that the priced inventory listing for the pharmacy contained some items based on the list price instead of the actual price the University pays. In all cases, the list price is higher causing the inventory to be overstated. One item the University paid \$818 for was listed on the inventory at \$1,848. Also, the University is pricing the inventory for dental gold using current prices instead of actual costs.

The control substance inventory listing did not add correctly because of errors in the formulas on the computerized listing.

Failure to correctly count inventories could result in a loss of control over the assets and a misstatement of the account balances. Failing to price the inventory based on the University's actual costs results in the University carrying its inventory at a value not in accordance with generally accepted accounting principles. Also, the failure to accurately prepare the listings results in a misstatement of the inventory balances.

We recommend that additional care be taken in the counting of inventories. Additionally, the University should ensure that all inventories are priced using its actual costs and all inventory listings are mathematically correct.

OTHER WEAKNESSES

IMPROVEMENTS NEEDED OVER FISCAL MANAGEMENT AND RESPONSIBILITY

Our audit disclosed various deficiencies in the handling of financial affairs of the University which included the following:

1. Billings to other State agencies were not performed in a timely manner. Billings in July, 1998 included services performed in 1997.
2. Changes in employment or employee status were not submitted timely to the State Office of Insurance Services that bills the University for health and dental insurance.
3. Reimbursement requests under grants were not filed in a timely manner and there was inadequate follow-up over billings which had not been received. During our audit, we noted billings over two years old that had not been collected according to the grant files.

4. The University allowed University Medical Associates (UMA) to expend approximately \$1,100,000 more than it had on deposit in its Agency Fund account.
5. The University allowed UMA to retain ambulatory care receipts of approximately \$7,000,000 as of June 30, 1998 that had been collected under the old ambulatory care agreement. These receipts were due to the University.
6. The University Board agreed to pay UMA an additional \$900,000 after June 30, 1998 to cover expenses incurred by UMA under the ambulatory care clinical education agreement. A memorandum signed by the ambulatory care clinical education committee stated that no additional funds would be paid to UMA should UMA exceed the approved budget for \$15,000,000 for the January, 1998 to June, 1998 period.
7. The University advanced approximately \$11,500,000 in grant funds to the Medical University Research Foundation (the Foundation) as of June 30, 1998. The Foundation earned approximately \$300,000 of interest on these funds.
8. The University entered into a written agreement with the Foundation to pay the Foundation \$750,000 per calendar year. The University paid the \$750,000 to the Foundation in January, 1998 for the calendar year beginning January 1, 1998. In addition, the University paid the Foundation an additional \$750,000 in July, 1998 for the calendar year beginning January 1, 1999.
9. We noted two instances in which the Medical Center did not timely bill for services to Medicaid patients. Medicaid allows billings to be submitted when patient charges exceed \$200,000. The unbilled charges for one patient totaled \$824,840 and for another patient totaled \$279,079. The billings were processed the day after we brought this condition to the Medical Center's attention.

Good fiscal management requires the University to bill and collect all funds which are due in a timely manner. The failure to timely bill and collect these funds increases the likelihood that the funds will not be billed and collected and results in the loss of interest earnings. Also, by advancing funds or not demanding timely repayment from its related parties, the University does not earn interest on the advanced funds.

We recommend that the University review its procedures to ensure that all receivables are billed timely and that follow-up is performed in a timely manner for any uncollected receivables. An aged listing should be maintained of all outstanding receivables to ensure timely follow-up. At the present time, many receivables are only posted to the general ledger at year-end. In addition, care should be taken to ensure that funds are only advanced under agreements, contracts or grants as they are needed to pay expenditures for the recipient. Care should be taken in the preparation of all agreements, contracts and grants to ensure that all required provisions are included to ensure good fiscal management.

IMPROVEMENTS NEEDED IN CONTROLLING FIXED ASSETS

In testing ten items located at the University to its fixed asset ledger records, we noted that one item was located in a different room and one item was located in a different building than shown on the fixed asset ledger records. Out of the twenty items which we attempted to inspect that were included on the fixed asset ledger records to the actual physical asset, eight were located in different locations; two were obsolete and not in use and should have been surplused; and three could not be located. We also noted that the University no longer employed some of the custodians shown on the fixed asset records. A similar finding was cited in last year's management letter.

It appears that the Department responsible for the fixed asset ledger records is not being notified when equipment is moved. It also appears that the University is not adequately controlling fixed assets to ensure that disposals are timely recorded. Certain assets that were not being used or were obsolete were not surplused in a timely manner. The failure to report the changes in locations of fixed assets resulted in an excess amount of time being spent by University personnel and the auditors in attempting to locate the items.

We recommend that the University review its procedures over the control of fixed assets. The individual departments of the University should be held responsible for ensuring that all required forms are completed and submitted to the fixed asset department in a timely manner for changes in custodians, movement, disposals, or obsolete equipment.

GENERAL LEDGER ACCOUNTS NOT RECONCILED TO SUPPORT

The University did not reconcile the student health insurance liability, commencement fee liability, and the liability accounts for State retirement to supporting documentation in a timely manner. Also, the patient revenue accounts and patient accounts receivable accounts were not reconciled timely or correctly at year end. The University does not maintain a subsidiary listing by student or semester supporting the amounts that were being held for future periods for commencement fees.

Failure to timely reconcile all general ledger accounts to supporting documentation in a timely manner could result in inaccurate financial information.

We recommend that all general ledger accounts be reconciled to supporting documentation monthly before the end of the following month.

D. STATUS OF PRIOR AUDIT FINDINGS

We performed an audit similar in scope for the year ended June 30, 1997. A management letter dated October 13, 1997 was issued which contained two reportable conditions and two other weaknesses. Adequate corrective action was taken on the material reportable condition regarding accounts receivable not being properly accrued. The other weakness regarding not capitalizing items in plant funds did not occur after we reported the finding to University staff. The remaining findings cited in last year's management letter are included in this year's comments.

MANAGEMENT'S RESPONSE

**MUSC
RESPONSE TO FY 1998 MANAGEMENT LETTER**

SCHEDULE OF AMOUNTS DUE FROM OTHER STATE AGENCIES INACCURATE

Management agrees with this recommendation. Review procedures will be put in place to ensure that only valid receivables are included on the schedule and that all uncollected receivables are followed up on in a timely manner. In addition, procedures have been modified to include enhanced communication with Grants and Contracts Accounting to facilitate more accurate reporting of their activity.

ERRORS IN ACCOUNTS PAYABLE SCHEDULE

Management agrees with this recommendation and will continue its efforts to improve the accuracy of the payables schedule and our review procedures. In addition, manual checks will be entered on a weekly basis whenever possible.

DEFICIENCIES NOTED IN ACCOUNTING FOR GRANTS

Management agrees with these recommendations. Grants and Contracts Accounting feels that the situation noted in the Management Letter regarding the use of a wrong form was an isolated case. Management has been working with the information technology report writers on the design of several reports from the University's new finance system. These reports will be run weekly to enhance the department's ongoing monitoring of grants, the tracking of receivables and the preparation of a more accurate Grants Receivable Schedule. The department is scheduled to relocate to a larger area that will include a central file room that will allow for better control of grants files. Central Administration continues to provide personnel and financial resources to the Grants and Contracts Accounting Department that will enable it to support the University's growing research activities through accurate and timely reporting of grant activity.

ENTRIES POSTED WITHOUT REVIEW OF SUPPORTING DOCUMENTS

Management agrees with this recommendation and will implement procedures to correct.

EQUIPMENT EXPENDITURES NOT RECONCILED TO FIXED ASSET ADDITIONS

Management agrees with the finding but believes the error was a timing issue only as reconciliations of equipment expenditures to equipment additions are performed regularly on a monthly basis. A large amount of equipment scheduled for the Rutledge Tower clinics that was received during the last few days of the fiscal year was not available for tagging and therefore had not yet been added to the equipment listing.

IMPROVEMENTS NEEDED OVER STUDENT LOANS AND ACCOUNTS RECEIVABLE

Student Accounting will continue its efforts to improve procedures in this area. Efforts are underway to upgrade the information systems and provide additional staff training.

ERRORS NOTED IN INVENTORY COUNTS, PRICING AND LISTINGS

Management agrees with this recommendation. Efforts to improve the counting and calculating of inventory will continue. Also, additional care will be taken to ensure a correct count and that actual costs

be used to price the inventory.

IMPROVEMENTS NEEDED OVER FISCAL MANAGEMENT AND RESPONSIBILITY

Management is reviewing procedures related to the preparation of contracts and agreements, and continues its efforts to improve the timeliness of all reconciliations, billings and collections. In addition, management is working with the related parties to establish payment schedules for FY99 and to establish a process to transfer funds in a timely manner between the organizations.

To facilitate improvement in Medicaid billing, a weekly report is now being generated to review all inpatients who are still in the hospital but whose insurance carrier will accept interim or cycle bills which will allow billing and collection of these accounts in a timely manner.

IMPROVEMENTS NEEDED IN CONTROLLING FIXED ASSETS

The Physical Asset Management Division is in the process of implementing a new Asset Management System which will provide more timely information and increased internal controls. Retirement and movement of equipment will then be completed on-line. In response to changing Federal regulations, the University will move to a \$5,000 capitalization limit. Additional procedures will be implemented to monitor departmental compliance.

GENERAL LEDGER ACCOUNTS NOT RECONCILED TO SUPPORT

Management agrees with these suggestions and will implement procedures to timely reconcile general ledger accounts.