

August 2005

A Review of the South Carolina Research Authority (SCRA)



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LAC

Report to the General Assembly

**A Review of the
South Carolina
Research Authority
(SCRA)**

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Synopsis

Members of the General Assembly requested the Legislative Audit Council to conduct an audit of the South Carolina Research Authority (SCRA). Established in 1983, the SCRA is a public non-profit corporation which does not receive annual state appropriations and has broad authority to manage its own business. The audit requesters wanted to know how the SCRA has benefited the state and how these benefits could be increased. They were also interested in the SCRA's spending and management practices. Overall, we found that the SCRA has provided substantial benefits to the state. We did not identify significant problems with how it has managed its resources. The results of our review are summarized below.

Benefits to the State

The SCRA has provided substantial benefits to the state through activities related to its mission — advancing the research capabilities of the state's universities and promoting the development of research and technology-related industries in South Carolina.

- ❑ SCRA has earned significant revenues primarily for doing research and development projects for the federal government. SCRA developed a strategic plan in 1997 when its revenues were approximately \$40 million. For FY 03-04, its revenues increased to \$68 million. It has generally been successful in meeting operational performance goals, increasing its revenues, and keeping indirect costs low. We found that SCRA generally has adequate documentation to ensure that its performance data is reliable.
- ❑ SCRA has succeeded in other strategic goals, such as establishing research institutes in cooperation with the state's research universities and increasing employment in the research parks it is mandated to operate. It has been less successful in starting for-profit companies, another of its strategic goals.
- ❑ We confirmed SCRA's data for direct spending in the state and bringing companies to the state. SCRA has also completed projects that may impact citizens directly and contributed to other economic development activities, such as bringing research dollars to universities. A recent study from Charleston Southern University estimated the SCRA's return on investment for the state; the study found for every dollar the state has invested, SCRA returns \$6,542 annually.

- ❑ SCRA could improve its communications to state officials. While the agency regularly communicates with the federal government, its annual reports do not contain adequate information about agency structure and operations, as well as performance results.
- ❑ The financial contributions SCRA must make under state law for the establishment of research innovation centers (\$12 million in three years) could have a harmful effect on SCRA's operations and its benefits to the state.

SCRA's Operations

- ❑ The majority of SCRA's revenues and expenditures are directly related to its contracts to conduct research and development programs for the federal government. Contracts comprised more than 96% of SCRA's revenues for FY 03-04. We found that SCRA's financial operations are generally sound. However, SCRA has expended some funds that do not meet criteria for the expenditure of public funds.
- ❑ SCRA's executive salaries may be higher than those of most other state agencies. However, a 2004 compensation study found that SCRA's salaries were below the market for comparable organizations. Some SCRA employee benefits exceed those offered to other state employees, while in other cases their benefits are less generous. SCRA offers additional benefits to six executives, including extra insurance and deferred compensation.
- ❑ SCRA has appropriate oversight and administration of its indirect costs. These costs are sometimes referred to as overhead expenses. Although state agencies are required to remit reimbursements of indirect costs to the state's general fund, SCRA does not benefit from the services of central state government and is not required to do this. SCRA's indirect cost practices have regularly been audited and approved by the federal government.
- ❑ SCRA's efforts to meet its strategic goal of starting new companies have not yet resulted in profits. SCRA has invested in or loaned funds to four companies, and has not yet received financial benefits. In one case, SCRA had a loss of nearly \$300,000.

- ❑ As required by statute, SCRA manages three research parks, one each near Clemson, the University of South Carolina in Columbia, and the Medical University in Charleston. We found that SCRA has managed its property appropriately. We did not identify problems with SCRA's rent or other charges to tenants.
- ❑ We did not identify significant problems in our review of SCRA's expenditures for travel. We reviewed a sample of travel vouchers for SCRA's executives and top travelers and found that SCRA generally has appropriate controls over travel expenses. SCRA has generally adopted the federal government's travel guidelines, which have more controls than state policies.
- ❑ SCRA generally has appropriate controls to prevent conflicts of interest for staff and board members. We did not find evidence of significant conflicts for SCRA's board members or executive management team. However, we noted two cases in which documentation of apparent conflicts could be improved.

Synopsis

Introduction and Background

South Carolina Research Authority (SCRA)

The South Carolina Research Authority (SCRA) is a public non-profit corporation with broad authority to manage its own business. Recognizing that "...the future economic viability of South Carolina can best be assured by building strong industries of advanced technology," the General Assembly created the SCRA in 1983. The statutory purpose of the SCRA is:

- To enhance the research capabilities of the state's public and private universities.
- To establish a continuing forum to foster greater dialogue throughout the research community within the state.
- To promote the development of high technology industries and research facilities in South Carolina.

State law requires the SCRA to operate research parks in cooperation with the state's universities. Specifically, the SCRA was required to establish three research parks, one each near Clemson University, the Medical University of South Carolina, and the University of South Carolina. To accomplish this purpose, the General Assembly gave the SCRA approximately 1,400 acres of undeveloped land, estimated at that time to be worth \$10.7 million, and \$500,000.

In 2005, the General Assembly passed Act 133, which expands the mission of the SCRA to include the establishment of research innovation centers. The SCRA is to establish an innovation center to operate in conjunction with each of South Carolina's three research universities. The innovation centers will be designed to enhance the ability of the universities to move ideas generated at the universities into commercialization by advising and assisting start-up companies. The companies could be located at the centers for up to 4 years or until they exceed \$1 million in annual revenue.

Governance

The SCRA is governed by a board of 23 trustees who have the authority to manage its business and affairs. The Governor appoints the chair of the board, and ten trustees are elected by the serving board members. Each Congressional district is to have at least one of the elected board members. The remaining 12 members serve ex officio and include representatives of higher education, the General Assembly, and the Governor or his designee. Act 133 added the designees of the chairmen of the House Ways and Means and Senate Finance Committees and the Secretary of Commerce to the SCRA board. The act also designated the following officials to serve as the board's executive committee.

- President of Clemson University.
- President of the Medical University of South Carolina.
- President of the University of South Carolina at Columbia.
- Governor or his designee.
- Chairman of the House Ways and Means Committee's designee.
- Chairman of the Senate Finance Committee's designee.
- Chairman of the SCRA Board of Trustees.

The SCRA board is to hire a director, who, with the board's approval hires its staff.

State law gives the SCRA specific authority:

- To acquire, manage, and sell property.
- To borrow money, issue bonds, and invest its funds.
- To establish not-for-profit corporations, which can then establish for-profit corporations.

The SCRA has not received annual appropriations from the General Assembly. It is exempt from paying taxes, and is required by statute to reinvest its earnings to further its purposes and mission. The state is not liable for obligations of the SCRA. The SCRA's employees are exempt from state personnel law with the exception of provisions on nepotism, ethics, and retirement.

Current Operations

The SCRA's primary activity is conducting research and development programs on a contractual basis. The authority develops proposals and obtains grants and contracts from the federal government and private companies. Most of its business comes from the federal government, primarily the Department of Defense. SCRA also performs work for other federal agencies, including the Department of Justice, the National Science Foundation, the Department of Energy, the General Services Administration, and the National Aeronautics and Space Administration. The SCRA subcontracts with a variety of companies and academic institutions, both in South Carolina and around the United States, to complete the work required by the contracts. SCRA has several contracts to manage consortia. Consortia are associations of businesses and academic institutions and other organizations that are interested in doing work in a particular field.

The other primary activity carried out by the SCRA has been developing and marketing a statewide system of research parks, with parks located near Clemson University, in Columbia, and in Charleston. The SCRA also carries out economic development activities designed to increase the presence of technology-oriented business in South Carolina.

The SCRA board oversees the operations of the SCRA and its affiliated organizations. The organizational units of SCRA are described briefly below and shown in Chart 1.1. In addition to units that operate the research parks and provide support services, SCRA includes the following program units.

INTEGRATED SOLUTIONS GROUP (ISG)

ISG acquires and carries out information technology-related research and development contracts primarily in the areas of defense, public safety, and homeland security.

APPLIED RESEARCH & DEVELOPMENT INSTITUTE (ARDI)

Created in 2000, by agreement with Clemson University, ARDI is located in the Clemson Research Park. Among its projects, ARDI has a contract to manage a consortium of businesses and academic institutions that work in the area of developing composite materials for weapons systems. Among ARDI's other programs is a contract with the Army involving nanotechnology.

BIOMEDICAL APPLICATIONS RESEARCH INSTITUTE (BARI)

Created in 2002, this unit is a partnership with the Medical University of South Carolina. BARI works in the area of bioinformatics, using computers to handle biological information, for example, improving the technology of MRI images.

EXPERIMENTAL PROGRAM TO STIMULATE COMPETITIVE RESEARCH (EPSCoR)

In 2001, at the request of the SC research university presidents, SCRA began to manage the state's EPSCoR program. EPSCoR is a federal program for states that have historically not received their share of federal research and development contract awards. The program generates grant funds for research projects at Clemson, MUSC, and USC. The EPSCoR program has received annual appropriations from the General Assembly (\$1.9 million in FY 04-05) which are used as the state's match for the program.

The SCRA has created two affiliate organizations, both private non-profit corporations, the Advanced Technology Institute, and the Technology Management Company. These companies are called controlled affiliates, as SCRA controls their operations through its positions on their governing boards.

ADVANCED TECHNOLOGY INSTITUTE (ATI)

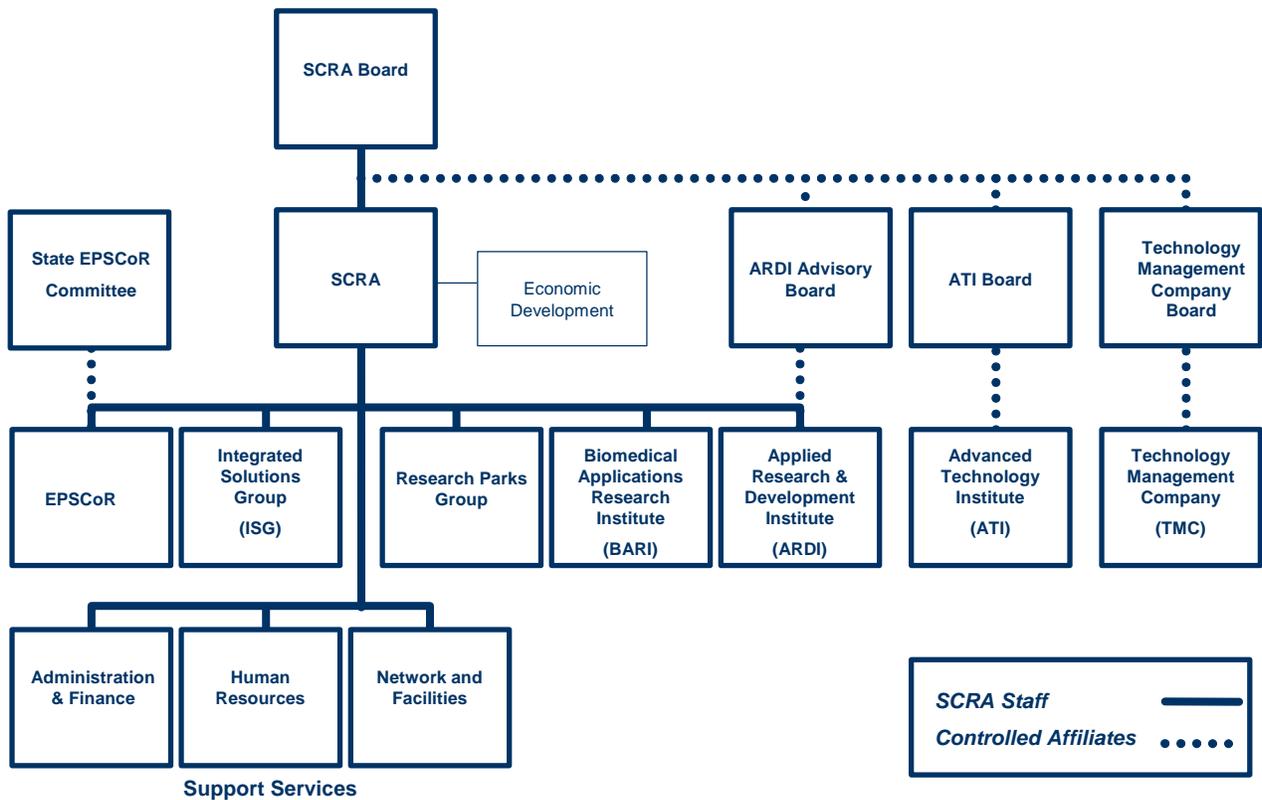
In 1998, the SCRA board separated the Advanced Technology Institute (ATI), which had been a part of SCRA, into a separate non-profit private corporation with its own board. According to officials, they took this step to enable ATI to get funding for some projects that it couldn't get as a public organization. Among its projects, ATI manages consortia in a variety of fields, including health care, metalworking, shipbuilding, and information technology.

TECHNOLOGY MANAGEMENT COMPANY

In 1997 Technology Management Company was organized as a holding company for SCRA's investments in new companies that it develops and spins off (see p. 21). This company has no employees and is currently inactive.

As of February 2005, SCRA had 157 employees, including 62 employees of ATI. Most of these employees are based at the Trident Research Center in North Charleston, although the SCRA's corporate headquarters staff and EPSCoR employees are in Columbia, and other employees are based at ARDI in Clemson.

Chart 1.1: SCRA Organization Chart



Source: SCRA

Audit Objectives

Members of the General Assembly requested an audit of the South Carolina Research Authority (SCRA). The requesters wanted to know how the SCRA has benefited the state and how these benefits could be increased. They also were interested in the SCRA's spending and management practices. Our specific audit objectives are listed below:

- Determine how the SCRA has benefited the state and how it could bring greater benefits.
- Review the SCRA's revenues and expenditures to determine sources of revenue and whether its spending practices and investment decisions have been sound.
- Review executive travel to determine whether it has been appropriate and cost-effective.
- Review SCRA's management of its property to determine whether it has followed statutory mandates and sound business practice.
- Determine whether the SCRA has appropriate controls to prevent its employees and board members from conflicts of interest.

Scope and Methodology

The audit reviewed the SCRA's revenues and expenditures and its management practices. In order to evaluate the SCRA's benefit to the state, we considered its performance measures and other evidence relating to its impact. We excluded review of other South Carolina programs, including those specific to individual universities, that are involved in activities relating to the SCRA's mission. We also did not review prospective programs, such as the innovation centers mandated by 2005 legislation. The primary period of our review was FY 02-03 and FY 03-04.

The following sources of evidence were included in our review:

- SCRA accounting, property, and travel records.
- SCRA board minutes.
- SCRA reports and strategic planning documents.
- Interviews with SCRA employees, other state officials, and interested parties.
- Independent audits of the SCRA and its affiliated entities.
- SCRA policies and procedures.
- Reports and materials from the State Ethics Commission and the Secretary of State's office.
- Surveys of board members and executive staff.
- Consultant and private research reports.

We determined that the audits of SCRA's accounting system provided adequate controls over the reliability of that information, and the use of other computerized information was not central to our audit objectives. We conducted judgmental sampling to review the SCRA's travel records and performance measures. Criteria we used to assess the SCRA's performance included its enabling legislation, state ethics law, previous LAC audits of other agencies, federal contracting criteria, and elements of sound business practice. We reviewed internal accounting controls and controls over employee travel, conflicts of interest, property management, and performance data.

This audit was conducted in accordance with generally accepted government auditing standards.

Benefits to the State

SCRA has provided substantial benefits to the state. SCRA was created to advance the research capabilities of the state's universities and colleges and promote the development of research and technology-related industries in South Carolina. SCRA's activities contribute to the achievement of nationally-recognized goals (see p. 9).

SCRA defined and implemented many of its research and development activities like a private company, with no ongoing support from the state and by monitoring its revenues and operational costs. The state's investment in SCRA was primarily the land it was given to develop research parks. The benefits SCRA has provided to the state can be summarized in two categories:

- Its success in operating a technology-related business.
- Its contributions to the state's economic development.

Success in Business

SCRA has developed a successful business by engaging in activities that are recognized as beneficial to the development of science and technology. Beginning in 1997, when its annual revenues were approximately \$40.6 million, SCRA engaged in strategic planning to guide its activities. In FY 03-04, its revenues had risen to \$68 million. The 1997 strategic plan had a five-year timeline. In 2002, the strategic plan was revised with new goals for 2007. The SCRA board approved the following strategic goals, which are aligned with SCRA's statutory mission.

Strategic Goals

Engage in internationally competitive research and development by teaming with technology leaders. SCRA has earned significant revenues for doing research and development contracts for the federal government.

Move emerging technology rapidly into effective use and into commercially competitive solutions. SCRA has been involved in starting new companies and bringing new technology to existing companies.

Strengthen partnerships with academia, industry and government, focusing on vital technologies. SCRA manages multiple projects that coordinate the work of partners from industry, academia, and government.

Attract advanced technology companies to strategically located research parks. SCRA has developed and currently manages three research parks. It has also attracted some out-of-state companies to locate operations within the state.

Establish affiliated organizations to facilitate accomplishment of our mission. SCRA has established the Applied Research and Development Institute (ARDI), the Biomedical Application Research Institute (BARI), and the South Carolina Nutrition Research Consortium (SCNRC).

Performance Measures

SCRA’s strategic plan includes performance measures that are directly related to its strategic goals. We reviewed SCRA’s performance on 15 of its measures and supporting documentation to assess the accuracy of the data used to measure performance. We found SCRA generally has adequate documentation to ensure performance data is reliable. SCRA has six operating performance measures it reports at quarterly board meetings (see Table 2.1).

SCRA has been generally successful at achieving key operating goals, except for the following:

- MEASURE 4 — SCRA has not yet invested 3% of its revenues back into operations.
- MEASURE 6 — SCRA also has not met its goal for conducting technical work in-house. This goal was established to build capacity within SCRA so that SCRA employees can bring technical talent to the programs it manages and have first-hand knowledge of the work being performed by subcontractors. According to an SCRA official, this goal is very difficult to achieve. For some programs, this goal conflicts with SCRA’s responsibility to secure additional work for its consortia partners.

Table 2.1: SCRA Operating Performance Measures and Progress Toward 2007 Goals

MEASURE	GOAL 2007	ACTUAL		
		FY 02-03	FY 03-04	FY 04-05 (AS OF 03/31/05)
1 Annual revenue will exceed \$80 million.	Greater than \$80 M	\$60.5 M	\$68.2 M	\$51.9 M
2 Indirect costs will be no more than 40% of direct costs.	Less than 40%	20.0%	18.2%	19.4%
3 Net revenue will exceed 3%.	3% or greater	3.1%	2.8%	3.0%
4 At least 3% of revenue will be budgeted to underwrite increased capabilities.	3% gross revenues or greater	1.2%	1.4%	1.0%
5 Backlog* of work will exceed previous year's revenue.	Exceed previous year's revenue	\$68.4 M	\$90.7 M	\$109.1 M
6 Percentage of technical work conducted by SCRA associates will be in the range of 20%–25%.	20% or greater	15.1%	15.1%	17.4%

* Backlog of work is contract work not yet completed from existing contracts or awarded contracts that have not yet begun.

Source: SCRA

We reviewed five additional SCRA performance measures because they are directly related to SCRA's mission. Except for its efforts to start private companies and increase investment in the research parks, SCRA has generally succeeded in these measures.

Start three for-profit companies from 2002-2007. SCRA is in the process of starting for-profit companies. During the 2002-2004 timeframe, SCRA did not start any for-profit companies, but it has one company under development.

Start at least one new group like ARDI, with MUSC, USC, or SCSU. SCRA has started two new groups, SCNRC and BARI. SCNRC is a joint effort of the state's three research universities, and BARI is a joint effort with MUSC.

Win every EPSCoR competition offered over the five year period. The Experimental Program to Stimulate Competitive Research (EPSCoR) is a federal program that helps generate annual grant funding to enhance research infrastructure at MUSC, USC, and Clemson. Although we were unable to document that EPSCoR has won every competition, it has been very successful at getting funding for its grant proposals. Since 2000, South Carolina has received \$103.9 million in funding from six federal agencies.

Increase employment in the parks by 500 employees. SCRA increased employment (excluding SCRA employees working at the parks) in its research parks by 908 employees, from 4,856 in 2002 to 5,764 in 2005.

Increase industrial capital investment in the research parks by \$50 million. SCRA is making slow progress toward its capital investment goal. Capital investment measures expansion or "building out" within the research parks to accommodate more companies. Capital investment has increased from \$237.9 million in 2002 to \$242.3 million in 2004 and 2005.

Technology and Science Index Ranking

SCRA's strategic plan reflects nationally recognized goals. A non-profit organization, the Milken Institute, publishes a State Technology and Science Index which evaluates each state's technology and science assets. The index serves as a benchmark assessment for states and provides a way to monitor progress. In 2004, South Carolina ranked 44th of the 50 states in the index. We noted that SCRA's activities contribute positively to four of the five criteria the index uses to evaluate a state.

- Research and development infrastructure — includes federal government and academic research and development expenditures.
- Risk capital and entrepreneurial assets — includes venture capital and business start-ups.
- Technology and science workforce — includes information on technology and science employees, such as computer programmers, engineers, and scientists.
- Technology concentration — includes percentage of high-tech employment and number of high-tech industries.

The fifth criteria includes educational attainment and spending, and is not part of SCRA's mission.

Impact on the State and Economic Development Efforts

We reviewed and verified information that SCRA uses to demonstrate its impact on the state. We did not identify problems with SCRA's documentation of these facts.

- SCRA has nationally recognized research programs involving over 185 industry and university partners. According to an SCRA executive, this accomplishment enhances the perception of S.C. as an international leader in the development, testing, and implementation of new advances in science and technology. Approximately 12% of these partners have or had operations within the state.
- SCRA's total revenue (through FY 03-04) exceeded \$660 million. Of its total estimated expenditures of \$631 million through FY 03-04, SCRA estimates that almost \$335 million was spent in South Carolina.¹
- SCRA has attracted 11 companies to locate activities in South Carolina. Companies generally have operations in the state because they have partnered with SCRA or because they are physically located within one of SCRA's research parks. The companies are in various fields, including consulting, security, and manufacturing.

¹ SCRA estimated it has spent \$173.6 million in contracts with in-state subcontractors, consultants and vendors; \$82.7 million in in-state labor costs, \$29.5 million in purchased software, material, and equipment, and \$48.6 million in facilities and related costs within South Carolina.

Also, SCRA commissioned the Center for Economic Forecasting at Charleston Southern University to conduct an economic impact study. According to the 2005 study, the state's initial investment has resulted in an annual return on investment of 6,542%. For every dollar the state invested in SCRA, SCRA returns \$6,542 annually to the state.

Other Economic Development Activities

SCRA has been involved in other efforts that enhance the state's economic development efforts. Examples are listed below.

- SCRA led the state's technology strategy development efforts. In 1997, SCRA's CEO chaired the South Carolina Technology Advisory Council, an ad hoc group, created by the Governor and composed of representatives of higher education and private business. The council drafted the state's first technology strategy.
- SCRA works with universities to enhance existing research infrastructure. The agency has helped universities write several proposals for the endowed chair program, and it was a sponsor of conferences which encourage businesses to invest in the program.
- ARDI has contributed to making Clemson a more competitive research university. According to SCRA and Clemson officials, during academic years 2003-2004 and 2004-2005, ARDI contributed approximately \$10.3 million and \$12.5 million, respectively, in research funding to Clemson University.

SCRA assisted the Department of Commerce in bringing aerospace companies to the state. For example, SCRA has leased space in its Trident Research Center to Vought Aircraft Industries, Inc. and The Boeing Company at cost.

Activities That Impact Citizens

According to an SCRA official, SCRA has also received funding for and coordinated projects that have had an impact on the citizens of the state:

- South Carolina is one of a few states that have an interoperable 800MHz radio system that allows emergency preparedness and disaster officials from different jurisdictions to communicate during an emergency; 1,600 radios have been installed across the state. This radio system was used during the 2005 train wreck in Aiken county.
- Charleston is one of two cities in the nation to participate in the Shotspotter program, which is an acoustic system that is able to identify where shots have been fired.

- SCRA received a grant to develop wearable computers for law enforcement officers. Currently, this technology is being piloted in a Charleston school.
- Through its information technology improvement project, SCRA helped develop an information system for Charleston, Dorchester, and Berkeley counties to share criminal data without compromising each sheriff's department's information technology security. If a criminal crosses county lines, other counties may be notified and given appropriate information.

SCRA Communications

While SCRA regularly communicates to federal stakeholders, it has not adequately communicated to the state about its mission and operations. SCRA's communication to federal entities is necessary since an overwhelming percentage of its revenues are from federal contracts. As of 2004, 93.3% of SCRA's funding was generated from federal contracts.

SCRA is required by S.C. Code §13-17-40 to file annual reports with the General Assembly "...including information on all acts of the board of trustees together with a financial statement and full information as to the work of the authority." SCRA's main communication to the state has been through its annual report, which does not provide adequate information to state officials. Unlike most other state agencies, SCRA is not required to file an accountability report.

As required by S.C. Code §1-1-810 and §1-1-820, most state agencies regularly communicate relevant information to the Governor and the General Assembly through annual accountability reports. The accountability report includes specific information about an agency's or department's mission, objectives to accomplish the mission, and performance measures that show the degree to which objectives are met. The FY 04-05 appropriations act also requires agencies to provide descriptions of key program areas and expenditures and to link these to key financial and performance results. SCRA's 2002, 2003, and 2004 annual reports focused on highly technical descriptions of its research and development work and omitted basic information about agency structure and operations.

Recommendation

1. South Carolina Research Authority should communicate more fully to the General Assembly regarding its mission, operations, activities, and organizational structure.

Mandated Contributions From SCRA

As a result of Act 133 of 2005, SCRA will be involved in establishing research innovation centers. However, the financial contribution from SCRA mandated by state law could have a harmful effect on SCRA's operations and its benefits to the state. Historically, SCRA has not made cash contributions to the state. Legislation enacted in 2005 mandates that SCRA dedicate \$12 million in funding over three years for innovation centers located near USC, MUSC, and Clemson. The legislation specifies "the payments must be at least three million dollars for the first year and at least four million dollars for the second year.... By the end of the third year, total funding dedicated...must be twelve million dollars..." (§13-17-87(D)(1)).

According to SCRA officials and a banking executive we consulted, funding this amount within three years does not allow SCRA sufficient operating cash flow. SCRA officials stated that funding of the innovation centers and a building for ARDI (see below) could result in a cash shortfall of over \$708,000 by FY 06-07, increasing to almost \$5.8 million by FY 07-08 (see Table 2.2).

SCRA's financial and credit ratings could suffer since financial rating services, such as Dunn and Bradstreet, report entities' available operating cash. SCRA officials fear lower financial or credit ratings could impact their ability to secure government contracts. We reviewed SCRA's documentation and found it to be reasonable.

Table 2.2: SCRA's Projected Cash Shortfall

	FY 04-05	FY 05-06	FY 06-07	FY 07-08
Beginning Cash*	\$17,085,252	\$17,359,564	\$12,647,591	\$6,650,020
Innovation Centers	0	-3,000,000	-4,000,000	-5,000,000
ARDI Building	0	-2,000,000	-2,300,000	0
SUBTOTAL	\$17,085,252	\$12,359,564	\$6,347,591	\$1,650,020
Average Net Cash Flow **	274,312	288,027	302,429	317,550
ENDING TOTAL CASH	\$17,359,564	\$12,647,591	\$6,650,020	\$1,967,570
Total Monthly Cash Outlay ***		7,008,157	7,358,565	7,726,493
CASH SHORTFALL			(-\$708,545)	(-\$5,758,923)

* Beginning cash is total cash less restricted cash, investments, and deferred compensation. Restricted cash is monies advanced by the federal government on grants and agreements being held in escrow by SCRA.

** Average net cash flow is based on fiscal year end cash balances as reflected in the financial statements.

*** FY 05-06 data is based on preliminary data available in June 2005. FY 06-07 and 07-08 data is based on the assumption there will be 5% growth.

Source: SCRA

Since 2001, SCRA has been in discussions with Clemson to construct a building for ARDI, mainly for the purpose of conducting classified laboratory work. SCRA has secured an almost \$4 million contract with the Army to do classified active coatings research. This contract is based upon the Army's assumption that a majority of this work would be conducted in a classified laboratory to be constructed by SCRA.

SCRA officials question the ability of the agency to provide funding in the amount of \$12 million, as required by Act 133. They also question the timing of the required funding. The need to spend \$3 million in the first year for the innovation centers is unlikely. The universities are to construct the physical facilities for the innovation centers using bonds, and start-up costs could be expected to increase gradually with the volume of projects.

Recommendation

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2. The General Assembly should consider amending §13-17-87(D)(1) to adjust South Carolina Research Authority's funding requirements to an amount that will preserve SCRA's operations and benefits to the state.

SCRA's Operations

Sources and Uses of Funds

We found that SCRA's financial operations are generally sound and are accounted for appropriately. The majority of SCRA's revenues and expenses are directly related to its contracts to conduct research and development programs for the federal government. Evidence did not indicate problems with the SCRA's expenditures for salaries (see p. 17). However, SCRA has expended some funds that do not meet the criteria for the expenditure of public funds.

Accounting System and Financial Audits

SCRA's accounting system is similar to those used by private sector companies rather than government entities. For accounting purposes, SCRA separates its various business divisions into segments that are then consolidated into a single set of financial statements. SCRA's consolidated financial statements as well as separate statements for Advanced Technology Institute (ATI) and Technology Management Company (TMC) are audited each year by an independent CPA firm. For fiscal years ending June 30, 2002, and 2003, SCRA received an unqualified ("clean") opinion from its auditors on the consolidated financial statements. However, the auditors disclaimed an opinion on the financial statements for 2004 because of a question about whether SCRA or the Budget and Control Board held title to \$12 million worth of real property. This issue has now been resolved (see p. 30). SCRA has implemented comprehensive internal guidelines, including financial and procurement policies and procedures, and travel guidelines. These policies provide controls over SCRA's systems to authorize, verify, and properly account for transactions.

Contracts are Primary Source of Funds

Table 3.1 outlines SCRA's sources and uses of funds. Contracts comprised over 96% of SCRA's revenues for FY 03-04 and over 94% for FY 02-03. In addition, expenses directly identifiable to these contracts made up over 83% of total expenses for FY 03-04 and over 81% of expenses for FY 02-03.

Table 3.1: SCRA Consolidated Operating Statement

	FY 02-03	FY 03-04
REVENUES		
Contract Revenues	\$57,321,378	\$65,943,784
Other*	3,177,775	2,213,405
TOTAL Revenue	<u>\$60,499,153</u>	<u>\$68,157,189</u>
EXPENSES		
Directly Identifiable Contract Costs	\$47,886,028	\$55,942,073
Salaries, Wages & Related Costs	5,179,053	5,584,068
General and Administrative	2,234,372	2,209,704
Facility and Park Operating Costs	1,484,526	1,544,147
Depreciation**	1,310,849	1,230,647
Other	953,292	353,598
TOTAL Expenses	<u>\$59,048,120</u>	<u>\$66,864,237</u>
OPERATING INCOME	\$1,451,033	\$1,292,952

* Includes rent, proceeds from the sale of land, regime fees and revenues relating to a project at the Clemson research facility (see p. 30).

** Primarily for Charleston office facility (see p. 30).

Source: SCRA

Expenditures Not Meeting a Public Purpose

We reviewed SCRA's expenditures which were unallowable for federal government contract billing. According to federal regulations, unallowable costs include categories such as entertainment expenses, advertising costs, contributions, interest on debt, and lobbying expenses. SCRA must identify and exclude any unallowable costs from its billings on federal contracts. For FY 02-03 and FY 03-04, unallowable spending totaled \$794,189 or 1.3% of total expenditures and \$1,083,052 or 1.6% of total expenditures, respectively. Most of SCRA's unallowable spending appeared to be related to its mission. For example, its expenditures to aid in the state's economic development activities were unallowable for reimbursement by the federal government.

SCRA has used some funds to make financial contributions to charitable organizations and for parties for its employees which do not meet criteria for the expenditure of public funds. As an employee benefit, SCRA gives each regular employee an opportunity once a year to designate an amount up to \$100 to a non-political, non-religious, South Carolina charity. Amounts spent for unallowable contributions for FY 02-03 and FY 03-04 totaled \$16,452 and \$29,600, respectively.

In addition, SCRA typically hosts two annual social events for its employees:

- A picnic in May with soft drinks, beer, food, door prizes and games.
- A holiday party in December with food, alcohol, and music.

For the past two fiscal years hosting these events has cost SCRA \$27,364.

In past audits, the LAC has found that other state entities have violated state law by improperly spending public funds on meals, receptions, entertainment and contributions. Under South Carolina law, public funds must be expended for both a public and corporate purpose. Public funds are not limited to tax revenues but include funds from any source in the hands of a public official. Therefore, SCRA funds would be considered public funds and must be spent in ways that directly promote a public purpose.

Recommendation

3. The South Carolina Research Authority should ensure that public funds are spent in compliance with state law.
-

Salaries and Benefits

SCRA's executive salaries may be higher than those of most other state agencies. However, a 2004 compensation study found that SCRA's salaries were below the market for comparable organizations. In some cases, SCRA employees receive benefits that exceed those offered to other state employees, while in other cases their benefits are less generous.

SCRA is exempt from provisions of state personnel law that apply to classification and compensation of employees. SCRA employees are "at will," that is, they do not have grievance rights and may be terminated without cause. SCRA's salaries, as of February 2005, were distributed as shown in Table 3.2.

Table 3.2: Salaries of SCRA/ATI Employees, February 2005

SALARY* RANGE	NUMBER OF SCRA/ATI EMPLOYEES
Greater than \$200,000	1 (1%)
\$150,000 – \$200,000	9 (6%)
\$100,000 – \$149,999	26 (16%)
\$ 75,000 – \$ 99,999	23 (15%)
\$ 50,000 – \$ 74,999	29 (18%)
\$ 25,000 – \$ 49,999	57 (36%)
Less than \$25,000	12 (8%)

*Base salary, excludes benefits and bonuses.

Source: SCRA

In addition to their salaries, SCRA/ATI employees may receive annual bonuses based on the performance of SCRA and their work groups. According to an SCRA official, if SCRA's net revenues exceed 2%, employees are eligible for bonuses based on points awarded to their work groups for meeting performance goals. For FY 03-04, SCRA employees received bonuses averaging approximately \$2,300 each. Apart from these bonuses, SCRA's CEO received bonuses approved by the SCRA board in the amounts of \$24,000 and \$23,000 for his performance in FY 01-02 and FY 02-03, respectively. ATI did not participate in the SCRA bonus distribution for FY 03-04, but had a separate bonus program in which some employees earned significantly higher bonuses. For FY 03-04, SCRA employees received a total of approximately \$185,000 in bonuses and ATI employees received approximately \$248,000.

Employee Benefits

SCRA employees generally have similar benefits to other state employees. SCRA employees participate in the state health insurance plan; ATI employees do not participate in the state plan but have a similar private plan. Some ways that SCRA's employee benefits differ from those of other state employees are listed below:

- While the state offers a defined benefit retirement plan as well as a defined contribution plan (Optional Retirement Program), the SCRA offers only a defined contribution plan.
- The SCRA offers more term life insurance to employees. It provides free life insurance to employees in an amount of twice their salary up to \$200,000, and employees may purchase additional insurance. Other state employees receive the amount of their annual salary plus \$3,000 in life insurance, and may purchase additional insurance.

- While the SCRA has a bonus program described above, other state employees do not have an ongoing performance-based bonus; however, state employees may receive a bonus of up to \$2,000 annually.
- Other state employees have more paid leave than SCRA employees. Other state employees receive 15 days annually in sick leave and 15 or more days (based on years of service) in annual leave with a maximum of 15 days sick leave and 30 days annual leave. SCRA employees do not receive separate sick and annual leave, but receive paid time off in the amount of 15 days per year, increasing to a total of 25 days with more than 15 years of service.

SCRA's Executive Benefits

Six members of SCRA's executive team receive benefits in addition to those received by all SCRA employees. These benefits were authorized by the SCRA board of trustees and include the following:

- \$150,000 additional term life insurance.
- Additional deferred compensation in the amount of 5% of the employee's salary (received one year after separation from SCRA if employee has not competed with the SCRA).
- Annual physical (up to \$300).
- Club membership.
- Monthly auto allowance for two employees.

As of June 30, 2004, SCRA had approximately \$1.3 million allocated to executive deferred compensation. Generally, state agencies do not have benefits such as these for their executive employees but they are common in the private sector. However, two other state entities, Santee Cooper and the S.C. Ports Authority, which are similar to the SCRA because they do not receive state appropriations, have similar benefits for some executive employees.

Compensation Study

According to an SCRA official, SCRA obtained a study of its compensation in order to determine whether it was competitive in attracting national research talent to the agency. The study was conducted in 2004 by an international company that specializes in compensation and benefits consulting. The study, which cost approximately \$66,000, evaluated SCRA's internal salary structure, the external competitiveness of its pay, and its benefits program.

The study compared SCRA's salaries to the national general industry (approximately 800 organizations) and national non-profit (70-80 organizations) markets and found SCRA's salaries were below the market. Specifically, SCRA's salaries (and salaries plus bonuses and incentives) were below the 25th percentile of both the general industry market and the non-profit market. However, SCRA's benefits were found to be above average for both markets. The study recommended that SCRA increase salaries to the 25th percentile in the short term and to the 50th percentile in the long term. According to an SCRA official, during FY 04-05 they made salary adjustments to reach 80% of the 25th percentile level at a cost of approximately \$105,000.

We reviewed the methodology of the compensation study and did not identify problems. The consultant analyzed SCRA's jobs for content and responsibilities and compared them to similar jobs in the comparison organizations. This methodology neutralizes the size of the organization and is not based on job titles, but rather on job content.

Indirect Costs

We found that SCRA has appropriate oversight and administration of its indirect costs. These costs are sometimes referred to as overhead expenses. The federal government reimburses the SCRA for both its direct contract costs and its indirect or overhead expenses. Although state agencies are required to remit reimbursements of indirect costs to the state's general fund, SCRA is not required to remit its indirect costs to the general fund. As a separate authority, SCRA does not benefit from the services provided by state agencies such as the State Treasurer, the Comptroller General, or the State Auditor like a typical state agency. In addition, research grants are specifically excluded from the law that requires indirect costs to be remitted to the general fund.

Description of Indirect Costs

SCRA's indirect costs include the operations of the corporate office in Columbia, the human resources department, the computer and telephone network support services, business development costs, and common use areas at the Trident Research Center. For the most part, these indirect costs are maintained within SCRA's accounting system and are automatically charged to particular divisions of SCRA's operations. However, some costs are allocated based on specific facts such as the number of telephones or computers a business unit has been assigned. For example, to properly allocate the cost of the telephone or computer service centers, the number of telephones or computers assigned to each unit is entered into the accounting

system on a monthly basis to allocate these costs. SCRA maintains complex cost equations for each of its business units and allocates indirect costs according to cost accounting standards and federal acquisition regulations. In addition, SCRA must outline and certify its cost accounting practices and any changes to these practices in a disclosure statement required by the Cost Accounting Standards Board pursuant to federal law.

Audits of Indirect Costs

SCRA's indirect cost practices have regularly been approved by the federal government. Since SCRA contracts with the federal government, its indirect costs must be audited by a federal audit agency on a regular basis. SCRA proposes indirect cost rates to the federal government. These rates are audited by the Defense Contract Audit Agency (DCAA) and are approved for use as provisional billing rates for the following fiscal year. During the audit of these indirect cost rates, the audit agency performs tests, such as comparing estimated and actual costs for the prior year and reviewing the accounts to ensure that they do not include unallowable costs. In addition, costs billed by SCRA to the U.S. Government pursuant to Department of Defense contracts are subject to audit for a two-year period by the DCAA. Audits conducted by the DCAA covering periods through fiscal year 2002 were completed without adjustment.

Investments in Start-Up Companies

SCRA's activities in support of its strategic goal of helping to start new companies have not been profitable. SCRA has invested in or loaned funds to four start-up companies, but has not received any income from these investments. Just one of the companies has earned substantial revenues, and one company never began operations and resulted in a total loss to SCRA of over \$293,000.

A 2004 U.S. Bureau of Labor Statistics study found that just 38% of information-based businesses were still operating four years after they started. Also, according to an SCRA official, SCRA should not be "...in the business of investing in companies solely for the purpose of making money," since that is the objective of venture capitalists. Rather, he stated that SCRA should take an ownership interest when assisting in starting companies in order to reinvest any profits in subsequent start-up companies. SCRA's investments are described below.

Patient Management Business

In 1999, SCRA's affiliate, Technology Management Company (TMC), purchased common stock in a start-up patient management business for \$196,331. This business was described as a "healthcare enhancement company" that would enrich "...healthcare while improving the economics for physicians and hospitals through the use of technology." According to an SCRA official, SCRA was partnering with the business incubator at the University of South Carolina to help businesses get started, and the patient management business came through this incubator. SCRA agreed to invest the amount of money needed to pay the president of the company for a three-year period. In addition, an anticipated federal grant through the Department of Rural Health was to be used to help fund the operations of this company. In order to protect SCRA's substantial investment in the company, SCRA's president was a director on the company's board.

During the start-up phase in 2000, the company hired a president and several other employees in order to demonstrate computer software in Allendale and Bamberg counties. This software would schedule diagnostic, screening, and preventive procedures based on patients' histories. Due to delays in the federal grant funds in the start-up phase, TMC provided \$90,000 worth of loans to the company in addition to its initial purchase of common stock. However, in 2000 the president of the company died, and the remaining investors, including TMC, decided not to continue the business. TMC suffered a total loss in this investment of \$293,629.

Environmental Services Business

SCRA holds ownership in an environmental services company with current revenues of \$3 million for a six-month period. The Base Realignment and Closure Act of 1993 closed the naval base in Charleston. As a result, in 1996 the Navy formed an environmental detachment in Charleston composed of former naval shipyard employees to assist in the environmental cleanup of closed bases. SCRA was interested in supporting a privatization initiative for this group to become an employee-owned, Charleston-based private corporation. The company was incorporated in 2000, and in 2001 TMC entered into a Shareholders' Agreement with the company and its key employees. TMC owns 19.6% of the company, which was granted for SCRA's involvement in support of the former employees of the environmental detachment group after their disassociation with the federal government prior to the start of the company. During 2000, TMC made loans to the company totaling \$6,200 that were paid back the following year.

The company provides environmental services, engineering, planning, construction, field implementation, and regulatory report preparation. For the six months ended March 31, 2005, this company had revenues of over \$3 million. As of May 2005, TMC had not yet received any funds from its investment in this company.

Eye Care Business

During 2002 and 2003, SCRA's affiliate ATI invested a total of \$28,125 in a business that diagnoses eye diseases using computer technology. According to the company's operating agreement, ATI owns 25% of the company. In addition, an ATI official personally owns 12% of the company (see p. 32), and physicians own the remaining balance. As of March 2005, the company had no revenues and a negative retained earnings balance.

Personalized Machined Parts Business

In 2002 SCRA entered into an agreement with a company that provides technical data services and has web-based capabilities to match customers with vendors to manufacture personalized machined parts. Under this agreement, SCRA sold a web site and domain name, a vendor network database, and other assets for the price of \$100,000. Also, in exchange for its ownership interest, SCRA provides web server hosting and maintenance to the company and has agreed to license and maintain certain software to the company.

According to a separate operating agreement, TMC owns 25% of the company and is to receive 75% of the net income of the company up to the \$100,000 purchase price to be paid on a quarterly basis. Since this company has not yet earned any net profits, SCRA has not received any payments. In addition, SCRA continues to provide web server hosting and maintenance since the costs to do so are insignificant. According to an SCRA official, this company has not had any sales and is not currently using the software licensed to it by SCRA.

Expenditures for Travel

We did not identify significant problems in our review of SCRA's travel expenditures. Travel-related expenses were approximately \$1.6 million in FY 03-04. We reviewed a sample of travel vouchers for SCRA's executives and top travelers and found that SCRA generally has appropriate controls over travel expenses.

SCRA Travel Policy

SCRA has generally adopted federal travel guidelines because a significant percentage of its revenues are from federal contracts. As of 2004, 93% of SCRA's funding was generated from federal contracts, and the federal government pays for most of SCRA's travel.

Federal travel guidelines provide more controls than South Carolina's travel policies. Federal guidelines contain limits for lodging and meal expenses, while South Carolina does not have limits on reimbursements for lodging expenditures. Also, the federal government has contracts for airfare, while South Carolina state government does not. In our 2005 audit, *A Review of State Travel*, we recommended that the state adopt lodging limits and obtain a contract for airfares for state government employees.

We also recommended that the state establish a central travel office to coordinate travel purchases. The SCRA uses a private travel agency for some travel-related duties, such as air travel, car rental, and lodging. The agency compiles data about SCRA's travel and tries to find cost-effective means of travel. SCRA pays a \$30 air ticket transaction fee for each ticket it purchases to the travel agency.

Travel Sample Review

We reviewed a judgmental sample of travel expenses incurred during FY 03-04 and included six SCRA executives in the sample. The ten SCRA employees with the highest amount of travel expenses in FY 03-04 comprised the rest of the sample. Approximately \$1.6 million in travel expenses were incurred during FY 03-04, and our sample accounted for \$180,000, or 11% of total travel expenses.

We found that SCRA employees clearly documented the reasons for their travel, which included business development, conferences, meetings with congressional members and staff, and to make presentations. With the exception of two trips to Brazil and Germany for business development and conferences, travel was within the United States. Approximately one-half (52%) of trips were within South Carolina or to Washington, D.C.

We noted SCRA frequently spent more on airfares than would be desirable. While there is no federal travel policy that mandates maximum amounts for airline tickets, there were 11 instances in our sample where airline tickets from S.C. cities (Columbia and Charleston) to Washington, D.C., were more than \$1,000. According to an executive of SCRA's private travel agency, airlines are not flexible and do not consider SCRA employees to be federal employees, so SCRA employees are unable to receive federal government airline ticket rates. The executive stated the average SCRA domestic airline ticket is below the industry standard. He noted an average domestic airline ticket for a business traveler in February 2005 was \$494.99. For April 2005, the average airline ticket for the SCRA traveler was \$392.63.

We also found there were 37 cases (26%) when employees spent more for lodging than the federal limits allowed. When lodging limits were exceeded, SCRA employees or SCRA's travel agency documented the reason and provided justification for the lodging choice, such as how many hotels were contacted to get a less expensive rate, or why the traveler needed to stay in that particular hotel. This justification also serves as a reasonable control over lodging, even though limits were exceeded.

SCRA travel vouchers in our sample also included payments for business entertainment expenses such as alcohol, spouses' expenses, and event tickets. Several expenses were unallowable for reimbursement by the federal government (see p. 16). Many of these expenses appeared to be related to SCRA's operations and mission, but some expenses, such as Family Circle Cup tennis tournament tickets, were mainly used to reward employees and were not directly related to SCRA's business. This use of SCRA monies for non-business-related reasons is a questionable use of public funds (see p. 16).

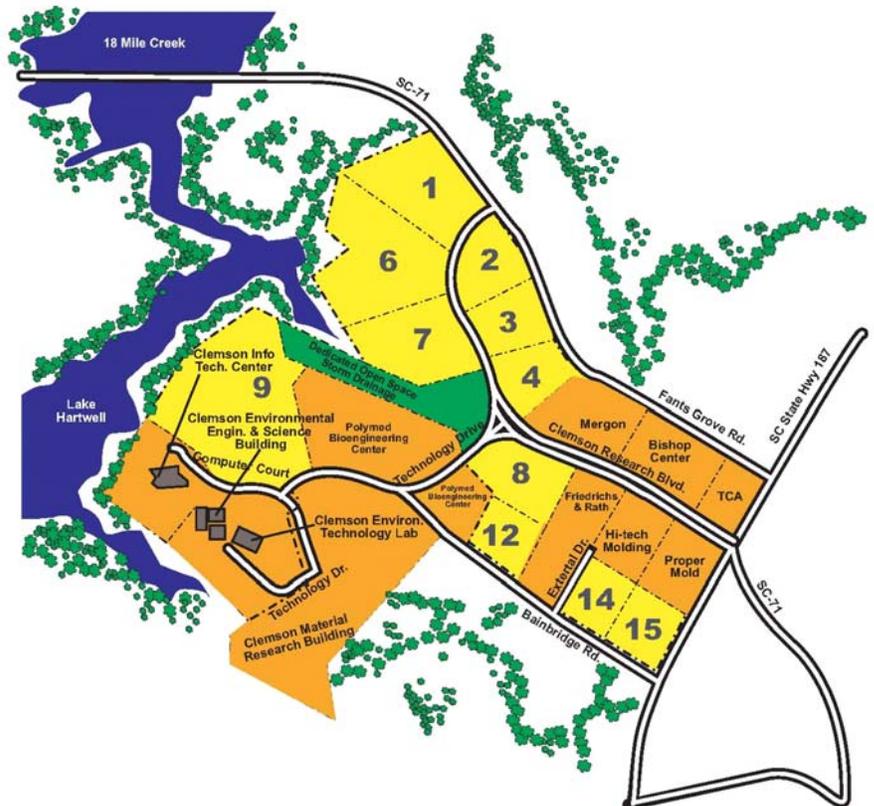
Property Management

The South Carolina Research Authority (SCRA) has followed statutory mandates and managed its real property appropriately. State law required the authority to establish a research park near each of the three research universities — Clemson University, the Medical University of South Carolina, and the University of South Carolina. SCRA currently operates the Clemson Research Park in Anderson County, the Carolina Research Park in Columbia, and the Trident Research Center in North Charleston.

Carolina and Clemson Research Parks

SCRA owns the land where the Clemson and Carolina research parks are located. Parcels within the parks are sold to tenants who then build their own buildings on their parcels. To help ensure that tenants are involved in science and technology, the SCRA has required any tenant in these parks to have at least 15% of its employees working as scientists or engineers. The SCRA most recently monitored this requirement in 2004 when it requested and obtained documentation from tenants regarding their employees' jobs. SCRA charges tenants an annual regime fee of \$600 per acre for maintenance of the parks' common areas. The Clemson park has 11 tenants including university-related entities and manufacturers of molded parts (see Map 3.3). The Carolina park has 12 tenants in fields such as engineering, software design, and manufacturing of automotive parts and liquid packaging (see Map 3.4).

Map 3.3: Clemson Research Park:
265 Acres



Source: SCRA

Map 3.4: Carolina Research Park:
246 Acres



Source: SCRA

Trident Research Center

SCRA owns the buildings that make up the Trident Research Center (TRC) in North Charleston. The 23 acres of land where the buildings are located is leased until 2047 by the SCRA from the Charleston County Aviation Authority. SCRA currently pays \$92,000 annually to lease this land. SCRA originally constructed the TRC buildings to house manufacturing equipment for a contract with the United States Navy. At the end of this project, the equipment was moved and SCRA converted the empty space into offices. SCRA leases the office space within the TRC to tenants. Other than SCRA and its affiliated entities, which lease about 39% of the available space, the 14 tenants in the TRC include those involved in higher education and aircraft manufacturing.

Property Transactions

When the SCRA was established, the state contributed almost 1,400 acres of land near Clemson, in Columbia, and in Dorchester county worth \$10.7 million. SCRA has sold some of this land and bought other property to establish its current research parks. Table 3.5 summarizes SCRA's property transactions.

Table 3.5: SCRA Property Transactions

LOCATION	TRANSACTION	DATE	SIZE IN ACRES	AMOUNT/VALUE	PURPOSE
CAROLINA RESEARCH PARK/COLUMBIA	Received from state	1983-88	709.116	\$8,810,134	
	Sale	1984	77.575	\$3,375,000	To fund parks
	Sale	1989-90	383.860	\$5,902,301	To purchase TRC
CLEMSON RESEARCH PARK	Received from state	1985	210.000	\$383,500	
	Purchase	1986	55.000	\$226,277	To expand park
CHARLESTON	Purchase	1985	10.500	\$1,405,468	To develop park
	Sale	1989	2.260	\$410,000	Not needed
	Sale	1997	3.960	\$780,000	Not needed
	Sale	1998	4.280	\$1,500,000	Not needed
	Purchase	2004	4.658	\$1,450,000	Joint effort with MUSC

Source: SCRA

In addition to transactions shown in Table 3.5, when it was created, SCRA also received from the state 470 acres valued at \$1.5 million in Dorchester county which were later sold for \$1.9 million to purchase the TRC. SCRA also received 9.5 acres in Florence in 1997. This property was sold in 1999 for \$50,000 because it was not significant enough to develop.

Within the research parks, SCRA has also sold individual parcels to tenants. SCRA has sold 138 acres in the Carolina Research Park for a total of approximately \$4.9 million. At the Clemson Research Park, 101 acres have been sold for a total of approximately \$1.2 million, and 17 acres are leased to Clemson University to facilitate Clemson's technology initiatives.

As of July 2005, SCRA owns a total of 134 acres which could be sold, worth between \$5 and \$5.6 million:

- 26 acres in the Carolina Research Park valued between \$2 and \$2.6 million.
- 103 acres in the Clemson Research Park valued at \$1.5 million.
- 4.658 acres in Charleston, valued at \$1.5 million, leased to the MUSC Health Sciences Foundation for \$1 until 2103 (currently a parking lot, potential research facility site).

SCRA could sell or use the land in the research parks for the innovation centers which the SCRA will be developing in response to the 2005 legislation (see p. 1).

Management of Research Parks

We did not identify problems with SCRA's rent or other charges to tenants. The research parks group of SCRA is responsible for managing the parks. This includes upkeep and marketing of the research parks in Clemson and Columbia and acting as a landlord for the Trident Research Center. Table 3.6 shows SCRA's revenues and expenditures for the Clemson and Carolina research parks and the TRC for FY 02-03 and 03-04.

Evidence indicated that the rents charged to TRC tenants are in line with the market. The rents charged to tenants at the TRC vary from approximately \$14 per square foot to \$21 per square foot. The amount of space leased by each tenant ranges from 259 square feet to 12,000 square feet. According to SCRA, the lease rates are influenced by up-fit costs, market conditions at the time of the lease, and the length of the lease. The average lease rate for the lower North Charleston area for 2004 was \$19.82 per square foot. The average rate charged at the TRC was \$18.19.

Tenants that lease space from SCRA also can receive other services such as telephone or computer network. SCRA charges for these services based on the level of service required and type of services used. The charges for these services are determined based on the total cost of the computer network support which includes salaries, depreciation, and cost allocations. We found no evidence that the calculation of these charges was unreasonable.

Table 3.6: SCRA Revenues and Expenditures

DESCRIPTION	FY 02-03		FY 03-04	
	PARKS	TRC	PARKS	TRC
REVENUES				
Sale of Land	\$448,503	\$0	\$228,750	\$0
Regime Fees and Other	129,955	152,715	143,172	89,432
Rent	0	1,399,794	0	1,524,365
Clemson Research Fac.*	804,051	0	0	0
TOTAL	\$1,382,509	\$1,552,509	\$371,922	\$1,613,797
EXPENSES				
Cost of Land Sale	\$150,501	\$0	\$59,414	\$0
Sales Comm. & Closing	4,665	0	1,553	0
Clemson Research Fac.*	808,115	0	0	0
Salaries & Wages	61,300	113,946	52,341	98,544
Professional Services	187	5,818	10,685	3,010
Fac. Oper. & Maint.	83,865	666,948	118,435	737,889
Rents & Leases	0	92,052	0	92,052
Travel & Relocation	6,154	1,966	8,954	2,068
General & Admin	2,942	71,414	2,225	59,234
Depreciation	0	1,004,803	1,623	961,623
TOTAL	\$1,117,729	\$1,956,947	\$255,230	\$1,954,420

* SCRA had planned to build a facility in the Clemson Research Park and lease the space to Clemson. The university decided to build the facilities so SCRA stopped its development of a building and Clemson reimbursed SCRA for its work on the project.

Source: SCRA

Title to Real Property

SCRA's statute, §13-17-70(5), gives it the authority to buy and sell real property. A proviso was included in the FY 04-05 appropriations act requiring that all real property held by state agencies be titled in the name of the state under the control of the Budget and Control Board. As a result of this proviso, SCRA's financial auditors were unable to express an opinion about SCRA's financial position. However, legislation enacted in 2005 exempts SCRA from the requirements of this proviso and allows it to keep and control the property in its name.

Conflicts of Interest

SCRA generally has appropriate controls to prevent conflicts of interest for staff and board members. We did not find evidence of significant conflicts for SCRA's board members or executive management team. However, we noted two cases in which documentation of apparent conflicts could be improved.

SCRA has an appropriate conflict of interest policy for its staff. The policy, which also applies to ATI staff, states that "Associates shall make every effort to avoid situations that may result in a conflict of interest." The policy gives examples of these situations and provides that employees should consult management before undertaking a questionable relationship. SCRA board members and employees are also governed by the state ethics law (S.C. Code §8-13-700 *et seq.*). Although SCRA does not have an explicit conflict of interest policy for board members, SCRA's board members and two SCRA executives are required by §8-13-1110 to file annual statements of economic interests with the State Ethics Commission.

SCRA's board members have filed annual statements of economic interests with the Ethics Commission. Just 1 of the 27 members who served during the period FY 02-03 through March 2005 failed to file the statements of economic interests. The forms which were filed did not indicate any conflicts of interest for the board members.

We surveyed 11 SCRA board members (generally excluding ex officio members) and the 9 members of SCRA's management team regarding their board memberships. We asked what boards they served on, their compensation for their service, and whether any business with which they are associated had also conducted business with the SCRA or its affiliated entities. All of the survey recipients responded to the survey. Three of SCRA's board members and executive managers reported serving on a total of 11 boards for which they received some compensation beyond expenses. We reviewed SCRA's payments to these 11 entities and 3 others where the respondents reported an economic relationship, and found no material problems.

The managers and board members also reported serving on approximately 60 boards for which they do not receive compensation. Many of these organizations were non-profits of an educational, civic, or arts nature.

Documentation of Apparent Conflicts

There were two instances in which documentation of apparent conflicts for members of SCRA's executive management team could be improved.

- An SCRA/ATI official personally invested in an SCRA spin-off company and owns a 12% share of the company. As of April 2005, SCRA/ATI has invested \$28,125 in the company (see p. 23). The official's job responsibilities encompass the field in which the company operates. SCRA has recognized this conflict of interest. Both the official and his supervisor stated that he must not do anything for the company during the hours he works for SCRA/ATI, and that he does not have authority to make financial decisions, such as deciding whether to include the company as a sub-contractor in an SCRA proposal. A 2002 memorandum from the supervisor to the employee, however, addressed just one part of the conflict, stating that the employee should ensure that "all activities that you undertake for (the company) be done at a time different from any hours you charge, in any way, to ATI programs, projects, or overhead." There was no documentation about the employee's ability to make financial decisions for SCRA involving the company, and no documentation that the ATI board knew and approved of the relationship. Because the company has not yet made profits, neither SCRA/ATI nor its employee has received economic benefits.
- An SCRA/ATI official serves on the board of a company which has been a sub-contractor for ATI. The official reported receiving \$800 – \$1,000 per meeting for serving on the board. Although he stated he has not been directly involved in deciding to use the company as a sub-contractor, he approves all ATI expenditures. There was no documentation that the ATI board was informed of his relationship with the company and approved of his serving on its board.

Recommendation

4. SCRA and its affiliated entities should recognize and document any apparent conflicts of interest involving its employees and ensure that the relevant governing board is informed and approves of these situations.

Agency Comments

Appendix A
Agency Comments



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August 15, 2005

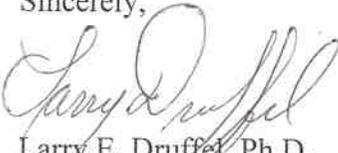
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Legislative Audit Council
1331 Elmwood Avenue, Suite 315
Columbia, SC 29201

Dear Mr. Schroeder:

We believe this audit to be accurate, and fair. It identifies two areas requiring better documentation. That documentation process has been initiated.

We have a different perspective on the charitable contributions and events we conduct to recognize and reward our people. We understand that it would be inappropriate to use appropriated funds for such purposes. However, SCRA was established as a self supporting non-profit corporation. As the audit notes, SCRA has made significant contributions to the state and generates revenue that will enable SCRA to launch the new Innovation Centers Operation. Those revenues are earned through the initiative of our people who prepare the proposals and effectively manage their execution – they know the customer and the technology. It is reasonable to spend a relatively insignificant amount of those revenues (less than 0.07%) to reward the people who generate the benefit. It contributes to the morale and esprit de corps of the organization. In the community of non-profits in which we operate, such events are the norm. In our view, it is a cost of doing business and a legitimate employee benefit. We acknowledge the potential for abuse through extravagance and will continue to avoid abuse.

Sincerely,



Larry E. Druffel, Ph.D.
President and CEO

Sincerely,



William T. Mahoney
President and CEO
As of August 1, 2005