OLA

OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA

Financial Audit Division Report

Office of the Secretary of State

January 1, 2003, through December 31, 2004

JULY 7, 2005 **05-40**

Financial Audit Division

The Office of the Legislative Auditor (OLA) is a professional, nonpartisan office in the legislative branch of Minnesota state government. Its principal responsibility is to audit and evaluate the agencies and programs of state government (the State Auditor audits local governments).

OLA's Financial Audit Division annually audits the state's financial statements and, on a rotating schedule, audits agencies in the executive and judicial branches of state government, three metropolitan agencies, and several "semi-state" organizations. The division also investigates allegations that state resources have been used inappropriately.

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- Promote Accountability,
- Strengthen Legislative Oversight, and
- Support Good Financial Management.

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OLA

OFFICE OF THE LEGISLATIVE AUDITOR
State of Minnesota • James Nobles, Legislative Auditor

Senator Ann H. Rest, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

The Honorable Mary Kiffmeyer
Secretary of State

We have audited the Office of the Secretary of State for the period January 1, 2003, through December 31, 2004. Our audit scope included revenue, payroll expenditures, and administrative expenditures. We also reviewed expenditures for the federal Help America Vote Act (HAVA) program. Our objectives focused on a review of the Office's internal controls over these financial activities and its compliance with applicable legal provisions.

The Report Summary highlights our overall audit conclusions. The specific audit objectives and conclusions are contained in the individual chapters of this report.

We would like to thank the staff from the Office of the Secretary of State for their cooperation during this audit.

/s/ James R. Nobles	*/s/ Claudia J. Gudvangen*
James R. Nobles Legislative Auditor	Claudia J. Gudvangen, CPA Deputy Legislative Auditor

End of Fieldwork: April 29, 2005

Report Signed On: July 1, 2005

Room 140, 658 Cedar Street, St. Paul, Minnesota 55155-1603 • Tel: 651/296-4708 • Fax: 651/296-4712
E-mail: auditor@state.mn.us • TDD Relay: 651/297-5353 • Website: www.auditor.leg.state.mn.us

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Audit Participation

The following members of the Office of the Legislative Auditor prepared this report:

Claudia Gudvangen, CPA	Deputy Legislative Auditor
David Poliseno, CPA, CISA, CFE	Audit Manager
Ken Vandermeer, CPA, CFE	Audit Director
Ellen Sibley, CPA, CIA, CFE	Auditor
Steve Johnson, CPA	Auditor

Exit Conference

We discussed the results of the audit with the following staff of the Office of the Secretary of State at an exit conference on June 21, 2005:

Mary Kiffmeyer	Secretary of State
Alberto Quintela	Chief Deputy
Bert Black	Business and Legal Analyst
Kathy Hjelm	Fiscal Director

Report Summary

Overall Conclusion:

- The Office of the Secretary of State operated within available resources and complied with management's established internal controls. However, we have concerns about the office's contract administration procedures and its use of Help America Vote Act (HAVA) funding.

Key Findings:

- The Office of the Secretary of State did not follow appropriate procedures when it cancelled a computer services contract. (Finding 1, page 8)

- The Office of the Secretary of State did not spend HAVA funds in compliance with state appropriation laws and did not accurately report the use of funds to the Legislature. (Finding 2, page 12)

The audit report contained five audit findings relating to internal control and legal compliance. The board fully resolved the finding included in our prior audit report.

Audit Scope:

Audit Period:
Calendar Years 2003 – 2004

Selected Audit Areas:
- Fee Receipts
- Payroll
- Administrative Expenditures
- Help America Vote Act

Agency Background:

The Office of the Secretary of State has primary responsibility to ensure that elections are conducted in accordance with state legal requirements. The office operates a statewide network connecting all counties and allowing access to business loan and voter registration databases.

The office is funded by a General Fund appropriation and fees deposited in the Special Revenue Fund. Beginning in fiscal year 2003, the office has received federal funding to implement the Help America Vote Act.

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Chapter 1. Introduction

The Office of the Legislative Auditor audits all constitutional offices every two years according to a Legislative Audit Commission policy. We conduct our audits at the mid-point and at the end of each constitutional officer's term.

Office Overview

Article V of the State Constitution established the Office of the Secretary of State, which operates under *Minnesota Statutes*, Chapter 5. The Secretary of State is elected for a four-year term and Mary Kiffmeyer currently serves in this position. The main functions of the office include administering elections, recording business documents and financing statements for business loans, and filing and preserving the official documents of the state. The office operates a statewide network connecting all counties and allowing access to databases containing business loan financing statements and voter registration information.

The office receives a General Fund appropriation to finance the majority of its activities. In addition, the office collects fees from customers who pay for on-line access to the computerized Uniform Commercial Code Network. The office retains these fees and uses them to maintain the network. The office also collects receipts for business filings, records processing, farm liens, and surcharges. It records these collections in the General Fund as nondedicated receipts. In fiscal year 2003, the office began participating in the federal Help America Vote Act program and has received about $45 million over the past three fiscal years to administer the program. (Refer to Chapter 4 for more details.)

Table 1-1 provides a summary of the Office of the Secretary of State's financial activities for fiscal year 2004.

Table 1-1
Sources and Uses of Funds
Budget Fiscal Year 2004

Sources:	
State Appropriation	$ 5,912,000
Direct Access Receipts	941,753
Other Receipts	48,969
Balance Forward In (1)	5,821,698
Total Sources	$12,724,420
Uses:	
Payroll	$ 5,116,792
Professional and Technical Services (2)	1,623,228
Communications	406,097
Space Rental	471,943
Supplies and Equipment	1,164,347
Printing and Advertising (2)	131,794
Computer and System Services	86,541
Repairs and Alterations	142,080
Other	115,659
Total Expenditures	$ 9,258,481
Balance Forward Out	3,465,939
Total Uses	$12,724,420

Note 1: $5,253,794 relates to HAVA funds carried forward from fiscal year 2003 to be spent in fiscal year 2004.
Note 2: These amounts include encumbrances of $2,625 for P/T Contracts and $23,406 for printing costs.

Source: Minnesota Accounting and Procurement System (MAPS) for fiscal year 2004 as of March 31, 2005.

Audit Approach

We conducted our audit in accordance with *Government Auditing Standards,* issued by the Comptroller General of the United States. Those standards require that we obtain an understanding of the office's internal controls relevant to the audit objectives. We used the guidance contained in *Internal Control-Integrated Framework*, published by the Committee of Sponsoring Organizations of the Treadway Commission, as our criteria to evaluate agency controls. The standards also require that we plan the audit to provide reasonable assurance that the office complied with finance-related legal provisions that are significant to the audit. In determining the office's compliance with legal provisions, we considered requirements of laws, regulations, contracts, and grant agreements.

To meet the audit objectives, we gained an understanding of the Office of the Secretary of State's financial policies and procedures. We considered the risk of errors in the accounting records and noncompliance with relevant legal provisions. We analyzed accounting data to identify unusual trends or significant changes in financial operations, and reviewed security clearances for various computer systems. We examined a sample of evidence supporting the office's internal controls and compliance with laws, regulations, contracts, and grant provisions.

Chapter 2. Revenue

Chapter Conclusions

The Office of the Secretary of State's internal controls provided reasonable assurance that it accurately recorded revenue in the accounting records, safeguarded receipts, and complied with significant finance-related legal provisions and management's authorizations.

For the items tested, the office complied with the significant finance-related legal provisions concerning revenue.

Audit Objectives

Our review of revenue focused on the following questions:

- Did the Office of the Secretary of State's internal controls provide reasonable assurance that it accurately recorded revenue in the accounting records, safeguarded receipts, and complied with significant finance-related legal provisions?
- For the items tested, did the office comply with the significant finance-related legal provisions concerning revenue?

Background Information

The Office of the Secretary of State collects revenue from three main business cycles: annual registrations, business services, and Uniform Commercial Code (UCC) filings. The office collects registration fees for corporate registrations, reinstatements, nonprofit amendments, legal newspaper registrations, renewal of assumed names, and filing annual and biennial reports. It also charges fees for business services, the primary purpose of which is to provide a central depository for the general public to register and obtain information related to businesses operating in Minnesota. The office collects UCC and related fees to support its function as an information clearinghouse for liens recorded for businesses across the state. In addition, the office collects a small number of other fees for special registrations and services, as provided in statute. The office deposits these receipts into the state's General Fund as non-dedicated revenue. Table 2-1 summarizes non-dedicated fee revenue by source for fiscal year 2004.

Table 2-1
Non-dedicated Revenue by Source
Fiscal Year 2004

Revenue	Amount
Business Services and Annual Registrations	$ 9,670,715
Uniform Commercial Code and Related Fees	2,423,951
Other	47,146
Net Revenue	$12,141,812

Source: Minnesota Accounting and Procurement System (MAPS).

The office also collects direct access fees charged to business entities requesting electronic access to certain public records maintained by the office. Customers prepay the office for fees associated with accessing the data. Minnesota statutes authorize the office to deposit these fees as dedicated revenue in the state's Special Revenue Fund. The office uses this revenue to maintain the computerized network. These receipts totaled nearly $942,000 in fiscal year 2004.

There were no findings in the revenue area.

Chapter 3. Payroll and Administrative Expenditures

Chapter Conclusions

The Office of the Secretary of State's internal controls provided reasonable assurance that it safeguarded assets and properly processed payroll and administrative expenditures. However, the office did not follow appropriate procedures when it cancelled a computer services contract as discussed in Finding 1. In addition, the office did not make timely adjustments to the HAVA payroll allocations as discussed in Chapter 4, Finding 4.

For the items tested, the office complied with the significant finance-related legal provisions concerning payroll and administrative expenditures.

Audit Objectives

Our review of payroll and administrative expenditures focused on the following questions:

- Did the office's internal controls provide reasonable assurance that it properly authorized and processed payroll and administrative expenditures?
- For the items tested, did the office comply with significant finance-related legal provisions concerning payroll and administrative expenditures?

Payroll

The Office of the Secretary of State expended approximately $5.1 million on payroll in fiscal year 2004. Payroll, the largest expenditure category for the office, consisted of regular, part-time, overtime, and premium pay, as well as other benefits. The Office of the Secretary of State currently employs about 70 employees.

Employees use bi-weekly timesheets to record actual hours worked on the various programs funded through the Office of the Secretary of State. The supervisors approve the timesheets and forward them to the fiscal services division where the data is entered into SEMA4, the state's payroll and personnel system. An independent employee reviews the transactions recorded in the system. A personnel representative enters personnel transactions into SEMA4 and works with employees on human resource matters.

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Other Administrative Expenditures

The Office of the Secretary of State incurred other administrative costs totaling $4.1 million in fiscal year 2004. Table 1-1 shows the expenditures by category for fiscal year 2004. Significant increases occurred from fiscal year 2003 to 2004 for professional/technical services and supplies/equipment due to the development of a new computer system. The office leases space in several buildings in the St. Paul area, including the State Office Building, the retirement systems building (Empire Building), and a storage area on Grove Street. The Department of Administration's Real Estate Management Division negotiated lease agreements on behalf of the office.

Finding and Recommendations

1. The Office of the Secretary of State did not follow appropriate procedures when it canceled a professional/technical contract for computer services related to the statewide voter registration system.

The office did not follow standard procedures when it agreed to cancel a computer services contract. As a result, it paid for services that it had previously identified as unsatisfactory. In January 2002, the office entered into a $300,000 contract with a computer vendor to provide professional and technical services to maintain and improve the efficiency of the statewide voter registration system. From February to June of 2002, the office paid the contractor $42,500 for services provided under the contract. However, it appeared that the office became dissatisfied with the work performed by the contractor. The contractor did not bill the office again until March 2003 when it submitted eight invoices totaling $68,000 for the period July 2002 through February 2003. The office responded to those invoices by sending a letter to the vendor dated April 25, 2003, stating: "We are denying payment due to unsatisfactory performance." The office attached a three-page document listing the office's concerns.

During our prior audit, office staff informed us that they were in the process of canceling the contract and planned to meet with representatives from the Department of Administration and the Office of the Attorney General to decide on how to best proceed with the cancellation. However, there is no evidence that the office ever met with either agency. Despite its dissatisfaction with the work product, in June of 2003, the office paid the vendor $48,130 of the $68,000 invoiced by the vendor. Along with the payment, the Secretary of State and the president of the company signed an agreement canceling the contract. The signed agreement said: "The State agrees that all personnel participants to this contract will not give either verbal or written statements to anyone as to the cancellation of this contract other than it was cancelled by reason of the State of Minnesota's budget cuts." We think the office had other options, because section 15.1 of the contract allowed the state to cancel the contract at any time, with or without cause, upon 30 days written notice to the contractor. The contractor would have been entitled to payment only for services satisfactorily performed.

We asked the staff why they paid the contractor if they were dissatisfied with the performance of the work. They responded that the payment was to ensure that the vendor turned over the source code that it had developed for the new system. They felt the source code had value, and they wanted to avoid a protracted legal battle.

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The office did not complete a final payment approval form as required by the Department of Administration. The form requires the agency head to certify that the contractor has satisfactorily fulfilled the terms of the contract. There is no evidence the office completed this form. During the 2003 Special Session, the legislature amended *Minnesota Statutes* Section 16C.08 requiring agencies to complete performance evaluations for all professional or technical services contracts. The provision went into effect four days after the office made the final payment.

Recommendations

- *The office should work with the appropriate state agencies when canceling contracts.*
- *If a contract is canceled, the office should clearly document that payments to the vendor are for work that has been satisfactorily performed.*
- *The office should complete required approval forms at the completion of all professional/technical services contracts.*

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Chapter 4. Help America Vote Act (HAVA)

Chapter Conclusions

Our review of HAVA expenditures disclosed the following concerns regarding compliance with federal or state laws:

- ***The Office of the Secretary of State did not spend HAVA funds in compliance with state appropriation laws and did not accurately report the use of funds when reporting to the Legislature. (Finding 2)***

- ***The office did not have a process to ensure an accurate allocation of payroll expenses charged to the HAVA grant. (Finding 3)***

- ***The office's cash management practices for the Election Assistance for Individuals with Disabilities (EAID) grant did not maximize the state's use of federal funds. (Finding 4)***

- ***The office did not have a process to ensure that no federal funds were paid to suspended or debarred vendors. (Finding 5)***

Audit Objectives

Our audit of HAVA expenditures focused on the following questions:

- Did the Office of the Secretary of State's internal controls provide reasonable assurance that it properly authorized HAVA expenditures, accurately reported the expenditures in the accounting records, and complied with applicable state and federal legal provisions and management's authorization?

- For the items tested, did the Office of the Secretary of State comply with significant finance-related legal provisions concerning HAVA expenditures?

Background Information

In 2002, Congress passed the Help America Vote Act (Public Law 107-252). The act established a program to provide funds to states to replace punch card voting systems, to establish the Election Assistance Commission to assist in the administration of federal elections and to otherwise provide assistance with the administration of certain federal election laws and programs. The act also established minimum election administration standards for states and local units of government with responsibility for the administration of federal elections.

The state received a grant of $5.3 million for Title I (CFDA 39.011) in fiscal year 2003 to improve the administration of elections for state and federal offices. In fiscal year 2005, the state received a grant of $39,178,788 for the Title III program (CFDA 39.011) for equipment, administrative, educational, and other expenses related to improving the election process. In addition, the state was awarded two Title II grants (CFDA 93.617) of $202,382 and $144,745 to provide greater accessibility to individuals with a full-range of disabilities. Prior to the Secretary of State's Office spending any HAVA funds, the legislature had to pass legislation authorizing the expenditure. The legislature created a separate account in the state treasury to account for HAVA funds and any interest earned on unspent funds.

As of May 10, 2005, the Office of the Secretary of State had expended approximately $5.7 million in federal funds from the Help America Vote Act of 2002. Table 4-1 shows the expenditures charged to the HAVA account by expenditure category.

Table 4-1
Payroll and Administrative Expenditures
Fiscal Years 2003 – 2005 (1)

Expenditure	2003	2004	2005
Payroll	$46,745	$1,136,659	$ 547,167
Professional and Technical Services	980	1,406,300	1,231,884
Communications			8,866
Space Rental		101,707	47,676
Supplies and Equipment	15,630	928,819	10,044
Printing and Advertising		16,527	104,016
Computer and System Services		633	39,436
Repairs and Alterations		41,650	(333)
Other	2,300	36,300	19,152
Total	$65,655	$3,668,595	$2,007,908

Note 1: Expenditures are shown for the period January 1, 2003, through May 10, 2005.

Source: Minnesota Accounting and Procurement System (MAPS) as of May 10, 2005.

Findings and Recommendations

2. The Office of the Secretary of State did not spend HAVA funds in strict compliance with state appropriation laws and did not accurately report the use of funds when reporting to the Legislature.

Laws of 2003, 1st Special Session, Chapter 7 appropriated $6.5 million to the Office of the Secretary of State for HAVA related activities. The appropriation is available until June 30, 2005. The law further identified the following seven activities that the office could spend the funds on:

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- Develop the state plan required under the act,
- Modify the statewide voter registration system,
- Develop and administer a procedure to process complaints,
- Improve polling place accessibility,
- Prepare training materials,
- Provide assistance to persons with limited proficiency in the English language, and
- Train local election officials.

The appropriation law did not limit the amount that could be spent in each category. The office established separate activity codes and budgets to monitor the expenditures. Table 4-2 shows the amounts recorded in the accounting records as expended or encumbered for each activity code as of April 26, 2005.

Table 4-2
Summary of Charges to HAVA Accounts by Activity
As of April 26, 2005

Activity	Amount
Develop the state plan	$ 597,059
Modify the statewide voter registration system	5,293,627
Develop and administer a procedure to process complaints	12,786
Improve polling place accessibility	244,619
Prepare training materials	116,287
Provide assistance to persons with limited English language proficiency	21,816
Train local election officials	104,776
Total	$6,390,970

Source: Secretary of State's accounting records.

We reviewed the office's accounting records and supporting documentation and identified various problems with expenditures charged to the HAVA appropriation. The office charged some costs to the appropriation that were not explicitly identified in the appropriation law. Also, the office did not charge some costs to the correct activity identified in the appropriation law. In addition, we question the department's rationale in its allocation of certain administrative costs to the HAVA funding. The office has historically received General Fund appropriations to finance its Elections Division and administrative costs have historically been funded from that appropriation.

State Plan Development

One of the requirements for the state to receive federal funding was to develop a state plan for administering the HAVA program. The federal government required that certain provisions be included in the state plan as well as the state's method for complying with the act. The office completed its state plan in July 2003 and released it for comment. Minnesota's final state plan appeared in the March 24, 2004, Federal Register. Table 4-3 shows the costs charged by the Secretary of State's Office for developing the state plan. The office charged most of the $597,059 in costs after it had developed the state plan.

Table 4-3
Summary of Charges to State Plan Development
As of April 26, 2005

Expenditure Category	Amount
Payroll	$312,429
Advertising [(1)]	104,446
Staff Augmentation [(2)]	92,103
Interagency Agreement with Public Safety [(3)]	37,000
Voting Registration Cards	12,692
Out of State Travel and Conferences	10,181
Office of Administrative Hearing's Services	7,260
Lease Payments [(4)]	5,100
Chairs	3,064
Other Expenditures	12,784
Total	$597,059

Note 1: The advertising costs relate to "get out the vote" commercials that aired prior to the 2004 election.
Note 2: Computer services miscoded to the state plan activity code. (See third bullet.)
Note 3: This will allow driver license matches.
Note 4: This was part of the office's cost of its leased office space at the Empire (Retirement) Building.

Source: Office of the Secretary of State's accounting records as of April 26, 2005.

The appropriation law did not specifically allow for administrative costs to be charged to the HAVA account. The office charged various administrative costs to state plan development, thereby inflating the actual costs incurred to develop the state plan. Although the expenditures comply with the federal laws, we question compliance with the state appropriation laws. The following examples describe some concerns from our review of expenditures allocated to the state plan:

- The office charged an unreasonable amount of payroll costs to developing the state plan. As indicated in the table above, the office allocated $312,429 of payroll costs to plan development. Most of these costs were not incurred to develop the state plan, but rather, to implement some of its provisions. The office required employees to record the amount of time spent on their timesheets by activity code. The office loaded the information into its accounting system and allocated charges based on this information. However, employees continued to charge time worked to developing the state plan, long after it had been issued.

- The office charged about $104,000 of advertising costs to the activity code for developing the state plan. The office paid to produce public service announcements as well as the airtime to run them. The "get out the vote" commercials ran on local media outlets prior to the 2004 election.

- The office did not accurately report its HAVA expenditures by category to the Legislature. In addition to the previously discussed payroll costs that did not relate to development of the state plan, the office erroneously charged $92,103 to the state plan activity account for staff augmentation. According to office staff, these costs should have been charged to the statewide voter registration system activity code. The office made similar payments to the voter registration system contractor and coded them properly.

The office entered into an agreement with the Department of Public Safety for $37,000 to verify voters' driver's license information. This activity pertains to voter registration and not to developing the state plan and should not have been charged to developing the state plan. These costs comply with the state appropriation laws, but should have been coded to a different activity code.

Other Charges

- The office charged about $172,500 of lease payments for office space rental to the HAVA appropriation account. In addition to the $5,100 lease payment charged to state plan development, as identified in Table 4-3, the office also charged $106,800 to the statewide voter registration system activity, $54,250 to the training activity accounts, and $6,374 to the complaint process activity. The Office of the Secretary of State did not incur any additional rental costs for office space once it began administering the HAVA grant, and it did not provide adequate documentation to support the allocation of space rental charges to the HAVA grant.

The Office of the Secretary of State must develop appropriate procedures and records to support the allocation of costs to the various activities financed from the HAVA appropriation.

Recommendation

- *The Office of the Secretary of State should establish appropriate procedures and controls to ensure that costs charged to the federal HAVA grant comply with applicable legal requirements and represent an appropriate distribution of costs based on services provided.*

3. The Office of the Secretary of State did not have a process to ensure an accurate allocation of payroll expenses charged to the HAVA grant.

The Office of the Secretary of State did not allocate fringe benefits consistently for employees directly and indirectly charged to the HAVA program. In addition, the office did not correct other allocation errors pertaining to overtime charges and posting of actual hours worked. The office designed a labor distribution spreadsheet to meet federal requirements governing payroll allocation. The labor distribution spreadsheet captured both estimated and actual hours worked by employees charged to the HAVA program. We identified various allocation errors totaling $114,000. The net affect of the errors was that the General Fund owed the HAVA account $30,177.

Currently, the office does not produce or review monthly allocation summaries that would help identify posting errors. Office of Management and Budget (OMB) Circular A-87, *Cost Principles for State Governments*, requires that the allocation system provide periodic reports to identify and adjust estimated versus actual amount variances. The office explained that the allocation system, which began recording charges on July 1, 2003, was not fully operational.

Periodic reports could provide management with the opportunity to detect posting errors and inconsistencies in hours reported for overtime and other fringe benefits.

Recommendation

- *The office should generate periodic payroll summaries and promptly correct identified allocation errors.*

4. The office's cash management practices for the Election Assistance for Individuals with Disabilities (EAID) grant did not maximize the state's use of federal funds.

As part of the HAVA program, the office received a separate $202,382 grant for improving access to and participation by individuals with disabilities in the election process. The office awarded approximately $190,000 to 126 local units of government to improve polling place accessibility. The awards ranged from $90 to $3,500.

The office did not draw down the federal funds in a timely manner. The office began disbursing the grants to local units of government in July 2004. As of April 26, 2005, the office had disbursed about $170,000 of the grant award, but had not requested any reimbursement from the federal government. Instead, the office used Title 1 HAVA moneys to fund these costs. The office should have requested the federal EAID reimbursements as it made disbursements, in order to maximize investment income on accumulated balances.

In addition, the office did not accurately report its financial activity for this program to the federal government. The federal government's A-133 Compliance Supplement, Letter L, requires each recipient to report disbursement activity as prescribed by the awarding federal agency. The office submitted its financial status report, dated November 17, 2004, to the federal government for the period September 1, 2003, through August 31, 2004. Although the office had disbursed about $9,400, it did not show this on the financial status report.

Recommendations

- *The Office of the Secretary of State should draw down the federal share of its EAID grant expenditures as incurred to minimize the use of Title 1 funds.*

- *The office should establish appropriate controls to ensure it submits accurate financial status reports to applicable federal agencies.*

5. The Office of the Secretary of State did not have a process to ensure that no federal funds were paid to suspended or debarred vendors.

The Office of the Secretary of State did not have a process to determine whether a potential vendor had been suspended or debarred by the federal government prior to obligating federal funds. Federal regulations prohibit states from using federal money to procure goods or services from vendors who are suspended or debarred. In addition, the federal government requires state agencies to ensure that subgrantees certify that they refrain from contracting with suspended or debarred vendors. The federal government suspends or debars vendors when it determines, or is informed, that the vendors have abused public trust or violated program provisions. The federal government has a process to identify suspended or debarred vendors, and requires states to prevent those venders from receiving federal funds in the future. Without following proper certification or verification procedures, the department is liable for all disallowed costs resulting from any payments to suspended or debarred vendors.

Recommendations

- *The Office of the Secretary of State should establish procedures to ensure it does not pay suspended or debarred vendors.*

- *The office should include standard language relating to suspension and debarment in its subgrantee contracts.*

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Status of Prior Audit Issues
As of April 29, 2005

Most Recent Audit

Legislative Audit Report 03-40, issued in July 2003, examined certain activities of the Office of the Secretary of State for the two years ended December 31, 2002. The scope included revenue and refunds, payroll, and other administrative expenditures. The report contained one finding recommending the Office of the Secretary of State perform reconciliations between its business systems and the state's accounting system. The office implemented the recommendation.

State of Minnesota Audit Follow-Up Process

The Department of Finance, on behalf of the Governor, maintains a quarterly process for following up on issues cited in financial audit reports issued by the Legislative Auditor. The process consists of an exchange of written correspondence that documents the status of audit findings. The follow-up process continues until Finance is satisfied that the issues have been resolved. It covers entities headed by gubernatorial appointees, including most state agencies, boards, commissions, and Minnesota state colleges and universities. It is not applied to audits of the University of Minnesota, any quasi-state organizations, such as metropolitan agencies or the State Agricultural Society, the state constitutional officers, or the judicial branch.

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MINNESOTA SECRETARY OF STATE OFFICE
Mary Kiffmeyer, Secretary of State

James Nobles
Legislative Auditor
140 Centennial Building
658 Cedar Street
Saint Paul MN 55155-1603

Dear Auditor Nobles,

I want to thank you and your staff for your cooperation during the audit of the activities of the Office of the Secretary of State for the period concluding December 31, 2004.

The Office of the Secretary of State is best known for supervising elections in Minnesota. Last year, Minnesotans once again led the nation in turnout percentage and our election ran very smoothly. The election was the first conducted in conformance with the new Federal Help America Vote Act (HAVA) legislation.

As you know, the Office is small but has a great deal of fiscal activity, generating hundreds of thousands of fiscal transactions each biennium. Office staff are expert and honest stewards of the funds left with us by Minnesotans in fee-for service activities such as the filing of Uniform Commercial Code financing statements, the registration of new and updated business organizations, and retrieval of the records of these and other similar past transactions.

As a result of the fees paid for these transactions, the Office of the Secretary of State is a net contributor of approximately $6 million per year to the general fund of Minnesota, which is unusual among state offices and agencies.

This letter is a response to your report.

During this audit period, this Office faced some new challenges. The Office handled Federal funds for the first time. This has been a learning experience. The Federal funds were structured in a way that was different from the usual and standard configuration. We understand and appreciate the suggestions made in the audit report, although there are clearly some items with which the office disagrees.

The following portion of this response focuses on your specific findings and recommendations, as referenced in the report. After the comments on each recommendation is listed the individual names of the staff assigned to resolve these issues and the date by which resolution is expected. Some issues have already been resolved.

180 State Office Building * 100 Rev. Dr. Martin Luther King Jr. Blvd * St. Paul, MN 55155-1299
651-296-2079 * 1-877-600-8683 * TTY: MNRelayService 1-800-627-3529 * Fax 651-215-0682
* Web site www.sos.state.mn.us * E-mail secretary.state@state.mn.us

With regard to Finding 1, Fiscal and supervisory staff of the Office have been directed to be meticulous in documenting contract activities. The position of the Office is that based on the terms of the computer system maintenance contract in question, the Office was authorized to cancel the contract with or without cause, as provided in paragraph 15.1 of the contract. Between the time the maintenance contract was entered into and the time it was cancelled, HAVA was passed and the requirements for statewide voter registration systems changed such that the old system could never have met those requirements. In addition, the source code provided by the vendor as a result of the cancellation was critical to the functions of the statewide voter registration database and provided a time savings value that allowed the HAVA compliant SVRS system to be implemented in time for the Fall 2004 elections. Finally, the office also wishes to point out that the office paid only $90,630 of a $300,000 contract, which reflected the satisfactory work product delivered, which was the source code.

In response to the first recommendation under this Finding, again, fiscal and legal staff have been directed to redouble efforts to ensure that proper procedures are followed. The Office has in the past utilized and will continue to utilize resources of appropriate offices when applicable. The person responsible for resolution of this issue is Kathy Hjelm and it has been resolved as of June 30, 2005.

Fiscal and supervisory staff have been directed to be meticulous in documenting contract activities as suggested by the second recommendation under this finding. The Office only paid for the portion of the work that was satisfactorily performed. The person responsible for resolution of this issue is Kathy Hjelm and it has been resolved as of June 30, 2005.

With regard to the last recommendation under this finding, the Office has completed approval forms at the completion of all other professional/technical services contracts as now required by law. While in this case a final letter stating terms of the cancellation was the equivalent of the approval form, Fiscal staff have been directed to complete an approval form at the conclusion of any contract where a payment is to be made, as required by statute. The person responsible for resolution of this issue is Sue Swanson and it has been resolved as of June 30, 2005.

The second finding (Finding 2), involves the categorization of HAVA funding. The Office of the Secretary of State spent HAVA funds in accordance with Federal appropriations. All amounts spent were in accordance with the Help America Vote Act. However, as a result of discussions with the audit staff as this audit proceeded, costs cited in the audit report are being reallocated as closely as possible to the actual program activities for which they were incurred. All of the expenditures were made to promote the specific functions set forth in the state legislation

The Office has expended all Federal funds consistent with Federal law. Fiscal staff have been directed to reallocate these expenditures in a way that more closely follows the auditor's coding preferences. In the future, based on legislation passed during the 2005 Legislative session, the categories are far more specific, dollar amounts are assigned to each activity and those amounts were determined with input from the Office, and there is a separate amount for HAVA administration. The person responsible for resolution of this issue is Sue Swanson and it has been resolved as of June 30, 2005.

Payroll tracking for the HAVA program was the concern in Finding 3. The Office monitored payroll reconciliation reports to detect or correct errors. The reconciliation process was planned for the end of the biennium, which was after the audit period

Fiscal staff have been directed to generate reports that reflect the auditor's allocation coding preferences. The person responsible for resolution of this issue is Kathy Hjelm and it has been resolved as of June 30, 2005.

In the HHS grant project for polling place access discussed in Finding 4, the Office allocated EAID funds in such a way to maximize benefits to the public, through local government and to improve polling place accessibility as broadly as possible. Over $170,000 in project funding was sent to local government and all of the administrative costs for the polling place accessibility project. were absorbed by the Title I fund money. Following the auditor's recommendation would have resulted in less money being available to local governments and for polling place improvements and that money being delayed in disbursement. It should also be noted that premature draw-down results in the payment of interest to the Federal government.

There were no state funds used in the grant process. All HAVA activities in fiscal years 2003 and 2004 only use Federal funds. The EAID grant funds will be deposited in and will augment the other Federal funds in the HAVA Account as required by Laws 2003, First Special Session, chapter 7, and they are unavailable for direct expenditure by the Office or subrecipients. The person responsible for resolution of this issue is Kathy Hjelm and it will be resolved as of July 31, 2005.

Finally, with regard to the last finding (Finding 5), the Office of the Secretary of State did not contract with any vendor subject to suspension and debarment. The Office has now established a procedure to assure that the Federal suspension and debarment list is reviewed prior to contracting with any vendor when Federal funds are used. The person responsible for resolution of this issue is Kathy Hjelm and it has been resolved as of June 30, 2005.

In addition, legal staff have been directed to include this suspension and debarment language as standard in all future contracts where Federal funds are used. The persons responsible for resolution of this issue are Bert Black and Kathie Battle-Sayles and the issue has been resolved as of June 30, 2005.

I hope that you find this response useful in continuing our dialogue and working relationship. We look forward to future interactions as we move forward with the challenges of the next biennium including the implementation of additional Federal programs.

Sincerely,

/s/ Mary Kiffmeyer

Mary Kiffmeyer
Secretary of State.