

**OFFICE OF THE SECRETARY OF STATE**

**FINANCIAL AUDIT**

**FOR THE PERIOD JANUARY 1, 1991 - DECEMBER 31, 1992**

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**SEPTEMBER 1993**

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**Financial Audit Division  
Office of the Legislative Auditor  
State of Minnesota**

**93-51**

Centennial Office Building, Saint Paul, MN 55155 • 612/296-4708

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# OFFICE OF THE SECRETARY OF STATE

## FINANCIAL AUDIT FOR THE PERIOD JANUARY 1, 1991 - DECEMBER 31, 1992

Public Release Date: September 17, 1993

No. 93-51

### OBJECTIVES:

- EVALUATE INTERNAL CONTROL STRUCTURE: Business service receipts, record processing receipts, uniform commercial code receipts, uniform commercial code surcharge, payroll, and capital expenditures.
- TEST COMPLIANCE WITH CERTAIN FINANCE-RELATED LEGAL PROVISIONS.

### CONCLUSIONS:

We found two areas where the Office of the Secretary of State's internal control structure needed improvement and did not comply with finance-related provisions:

- The Office of the Secretary of State does not verify whether counties remit the proper uniform commercial code surcharges.
- The Office of the Secretary of State does not verify whether foreign corporations are paying the correct annual license fee.

We found one area where the Office of the Secretary of State did not comply with finance-related legal provisions:

- The Office of the Secretary of State did not cancel excess presidential primary reimbursement funds in a timely manner.

Contact the Financial Audit Division for additional information.  
296-1730

FINANCIAL AUDIT DIVISION





STATE OF MINNESOTA  
**OFFICE OF THE LEGISLATIVE AUDITOR**  
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JAMES R. NOBLES, LEGISLATIVE AUDITOR

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Senator Phil Riveness, Chair  
Legislative Audit Commission

Members of the Legislative Audit Commission

The Honorable Joan Anderson Grawe  
Secretary of State

### **Audit Scope**

We have conducted a financial related audit of the Office of the Secretary of State as of and for the two years ended December 31, 1992. Our audit was limited to only that portion of the State of Minnesota's financial activities attributable to the transactions of the Office of the Secretary of State, as discussed in the Introduction. We have also made a study and evaluation of the internal control structure of the Office of the Secretary of State in effect at December, 1992.

We conducted our audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial activities attributable to the transactions of the Office of the Secretary of State are free of material misstatements.

As part of our study and evaluation of the internal control structure, we performed tests of the Office of the Secretary of State's compliance with certain provisions of laws, regulations, contracts, and grants. However, our objective was not to provide an opinion on overall compliance with such provisions.

### **Management Responsibilities**

The management of the Office of the Secretary of State is responsible for establishing and maintaining an internal control structure. This responsibility includes compliance with applicable laws, regulations, contracts, and grants. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that:

- assets are safeguarded against loss from unauthorized use or disposition;
- transactions are executed in accordance with applicable legal and regulatory provisions, as well as management's authorization; and

- transactions are recorded properly on the statewide accounting system in accordance with the Department of Finance policies and procedures.

Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

## Internal Control Structure

For purposes of this report, we have classified the significant internal control structure policies and procedures in the following categories:

### Revenues:

- business service,
- records processing,
- uniform commercial code, and
- uniform commercial code surcharge,

### Expenditures:

- payroll and
- capital expenditures.

For all of the internal control structure categories listed above, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we assessed control risk.

## Conclusions

Our study and evaluation disclosed the conditions discussed in findings 1 and 2 involving the internal control structure of the Office of the Secretary of State. We consider these conditions to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the entity's ability to record, process, summarize, and report financial data.

A material weakness is a reportable condition in which the design or operation of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial activities being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We believe that none of the reportable conditions described above are a material weakness.

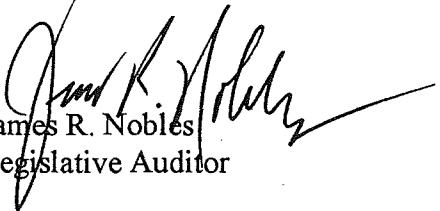
Senator Phil Riveness, Chair  
Members of the Legislative Audit Commission  
The Honorable Joan Anderson Growe  
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We also noted other matters involving the internal control structure and its operation that we reported to the management of the Office of the Secretary of State at the exit conference held on September 1, 1993.

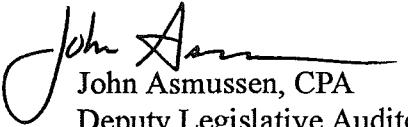
The results of our tests indicate that, except for the issues discussed in findings 1, 2, and 3, with respect to the items tested, the Office of the Secretary of State complied, in all material respects, with the provisions referred to in the audit scope paragraphs. With respect to items not tested, nothing came to our attention that caused us to believe that the Office of the Secretary of State had not complied, in all material respects, with those provisions.

This report is intended for the information of the Legislative Audit Commission and management of the Office of the Secretary of State. This restriction is not intended to limit the distribution of this report, which was released as a public document on September 17, 1993.

We thank the Office of the Secretary of State staff for their cooperation during this audit.



James R. Nobles  
Legislative Auditor



John Asmussen, CPA  
Deputy Legislative Auditor

End of Fieldwork: July 7, 1993

Report Signed On: September 10, 1993



# Office of the Secretary of State

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## Audit Participation

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

John Asmussen, CPA	Deputy Legislative Auditor
Renee Redmer, LPA	Audit Manager
Beth Hammer, CPA	Auditor-in-Charge
Janet Knox, CPA	Auditor
Christina Weiss	Auditor
Geniene Herrlich	Auditor

## Exit Conference

The findings and recommendations in this report were discussed with the following officials of the Office of the Secretary of State at the exit conference held on September 1, 1993:

Joan Anderson Growe	Secretary of State
Elaine Voss	Deputy Secretary of State
Jayne Khalifa	Operations Director
Kathy Hjelm	Fiscal Supervisor
Terry Elizondo	Director of Finance, Budget, and Personnel



## Office of the Secretary of State

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### Introduction

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Article V of the state constitution established the Office of the Secretary of State which operates under Minnesota Statute Chapter 5. The Secretary of State is elected for a four-year term. Joan Anderson Growe has served successive terms as the Secretary since January 1975. The Secretary serves as the chief election official of the state. As election judge, the Secretary ensures that elections are fair and comply with state rules and statutes. In addition, the Secretary is the custodian of the state seal.

The Office on the Secretary of State serves as the official repository for public documents of the state. The office accepts filing information on businesses operating in Minnesota. It disseminates information to a wide client group which includes the general public.

The Secretary's office maintains a statewide computer network connecting the 87 county courthouses. The network links the records of registered voters, uniform commercial code filings, and state and county election results. Beginning July 1, 1993, the office established the central notification system for farm product liens resulting from loans to farmers.

The activities of the Office of the Secretary are financed through General Fund appropriations and revolving fund receipts. The office collects fees for business service filings, records processing filings which includes foreign corporation registrations, uniform commercial code transactions, and other fees. The Secretary's office deposits these receipts in the General Fund as nondedicated receipts. The Department of Finance and the Secretary review the fees annually. However, the legislature ultimately establishes the fees in law.

The Secretary's office and county recorders are required to assess a surcharge on uniform commercial code transactions. County recorders are required to remit the surcharge collected to the Secretary's office. Currently, the office deposits surcharge receipts in the General Fund. Prior to July 1, 1991 these receipts were deposited in a revolving fund.

In addition to the above receipts, the Secretary's office charges customers for on-line access to the uniform commercial code network. These receipts are deposited into a revolving fund which is used to maintain the statewide systems.

During the 1992 legislative session, the Secretary's office received a \$2.4 million appropriation to fund the presidential primary election. The Secretary's office was required to use the appropriation to reimburse counties and municipalities for costs associated with the primary. The office disbursed the funds during fiscal year 1993.

## Office of the Secretary of State

The following is a summary of the Secretary's office revenues and expenditures for fiscal year 1992:

	<u>Fiscal Year</u> <u>1992</u>
<b>Revenue:</b>	
Business Services	\$3,169,046
Records Processing	1,190,171
Uniform Commercial Code	825,226
Uniform Commercial Code Surcharge	951,364
Other Revenues	<u>364,711</u>
<b>Total Revenue</b>	<b><u>\$6,500,367</u></b>
 <b>Expenditures:</b>	
Payroll	\$2,418,745
Capital Expenditures	1,038,915
Other Expenditures	<u>1,645,505</u>
<b>Total Expenditures</b>	<b><u>\$5,103,165</u></b>

Source: Managers Financial Report and Estimated/Actual Receipts Report as of September 6, 1992, and September 5, 1992, respectively.

## Office of the Secretary of State

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### Current Findings and Recommendations

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#### 1. The Office of the Secretary of State does not verify whether counties remit the proper uniform commercial code surcharges.

The Office of the Secretary of State did not ensure whether it received the correct surcharge amount from counties for uniform commercial code (UCC) transactions. The Secretary's office administers the statewide computer network for UCC activities. The 87 counties in Minnesota and the Secretary's office use the system to record UCC filings and access this information. Currently, county recorders and the Secretary are to assess a \$5 surcharge on each UCC filing or search transaction. During fiscal year 1992, the counties remitted \$644,000 of surcharges to the Secretary. The Secretary's office directly collected \$307,000 in surcharges during this same time period for UCC transactions that occurred in the Secretary's office.

The Secretary's office does not confirm the accuracy of the UCC surcharges received from the counties to the transactions recorded on the statewide computer network. The Secretary's office maintains a computerized transaction log which tracks the total surcharges owed by counties based on UCC transaction activity. We noted large variances between the transactions recorded on the log and the surcharges received from the counties. Upon further investigation, the Secretary's office discovered two computer programming errors which it believed were causing these variances. The amounts collected directly by the Secretary's office for transactions that it processed agreed with a separate transaction log.

The Secretary should correct the computer programming errors and use the computerized log as a basis to ensure that the counties remit the proper amount of surcharges. Without verifying whether the counties send the appropriate surcharges to the Secretary, errors and irregularities could go undetected.

#### *Recommendation*

- *The Secretary's office should correct the computer programming errors and use the transaction log as a basis to ensure that the counties remit the proper surcharges.*

2. **The Secretary's office does not verify whether foreign corporations are paying the correct annual license fee.**

The Secretary's office has not established a process to verify the information used in the calculation of foreign corporation's annual license fees. Minn. Stat. Section 303.07 requires the Secretary to collect an annual license fee from each foreign corporation conducting business in Minnesota. Approximately \$1 million in foreign corporation fees was deposited in fiscal year

## Office of the Secretary of State

1992. The minimum fee is \$60. This amount includes a \$40 license fee, based on Minnesota taxable income for the last taxable year ending of up to \$200,000, plus a \$20 filing fee. If a foreign corporation's income exceeds \$200,000, then an additional \$20 is owed for each \$100,000 of income or fraction of that amount.

Foreign corporations complete an annual registration form and calculate the fee owed. The corporations send the form and fee to the Secretary's office. The Secretary's records processing division verifies the extensions on the form to the payment received. However, the division does not verify whether the Minnesota taxable income figure is accurate. By not completing this verification, the Secretary's office does not know whether the corporations paid the appropriate fee.

Currently, the Secretary's office does not have access to the corporate tax returns which contain the taxable income figure needed. In order for the Secretary to verify the taxable income figure, it would need to seek legislation to gain access to the tax returns.

### *Recommendation*

- *The Secretary's office needs to develop controls to verify the Minnesota taxable income figure on foreign corporations annual licenses.*

### **3. The Secretary's office did not cancel excess presidential primary reimbursement funds in a timely manner.**

The Secretary's office did not return \$961,000 to the General Fund at the end of fiscal year 1992, as required by law. This amount remained from a \$2,483,375 appropriation for the Secretary of State to reimburse counties and municipalities for expenses incurred during the presidential primary election. Rather than cancel the unspent appropriation balance, the Secretary's office held it throughout fiscal year 1993, pending final program reimbursements.

Minnesota held the primary on April 7, 1992. The legislation authorizing expense reimbursements, Minn. Stat. Section 207A.10, became effective on April 25, 1992. It required counties and municipalities to certify reimbursement requests to the Secretary no later than 60 days after the presidential primary. The Secretary's office notified counties and municipalities of the funds availability on May 8. Despite the restrictive timeline, counties and municipalities sent 85 percent of the expense certifications to the Secretary's office by the June 8 deadline. However, the Secretary continued to accept expenses certified after the 60 day statutory deadline.

The appropriation law allowed the Secretary to carry forward an amount adequate to pay the reimbursements claims that counties and municipalities certified within the 60 day limit. However, the Secretary carried forward the total unliquidated appropriation to fiscal year 1993. This amount exceeded the certified reimbursement request amount by \$961,000. The Secretary paid an additional \$48,000 for late requests and corrections during fiscal 1993. Also, a 1993 amendment to the statute authorized additional payment of eligible costs which totaled \$29,000. The

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office was authorized \$7,500 for administrative costs. This resulted in a remaining unliquidated appropriation of \$877,000 which will cancel to the General Fund at the end of fiscal year 1993.

The Secretary's office believes that it administered the reimbursement within the intent of the Legislature. The Secretary's office did not cancel the balance because it wanted to ensure that all local units of government received reimbursements for the presidential primary.

### *Recommendation*

- *The Secretary's office should make a reasonable estimate of need when certifying open encumbrances.*





# Office of the Secretary of State State of Minnesota

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St. Paul, MN 55155-1299

**Joan Anderson Growe**  
*Secretary of State*  
**Elaine Voss**  
*Deputy Secretary of State*

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September 9, 1993

James R. Nobles  
Legislative Auditor  
1st Floor Centennial Office Building  
St. Paul, MN 55155

Dear Mr. Nobles:

The purpose of this letter is to respond to the findings of the legislative audit on the Office of the Secretary of State for the two year period ending December 31, 1992.

**1. Finding:** The Office of the Secretary of State does not verify whether counties remit the proper uniform commercial code surcharges.

**Recommendation:** The Secretary's office should correct the computer programming errors and use the transaction log as a basis to ensure that the counties remit the proper surcharges.

**Response:** The Office of the Secretary of State has been collecting surcharge amounts from the 87 counties for the Uniform Commercial Code (UCC) computer network since 1987. We have been collecting the surcharge without verifying the amount collected against the daily transaction log. We concur with the audit finding that these surcharge amounts should be verified and that it is the responsibility of the Office of the Secretary of State to be proactive when there is a discrepancy between the daily transaction log and the surcharge amount submitted.

Programming errors were discovered as a result of earlier identification of discrepancies between county transaction logs and the county surcharge amounts paid. These programming errors have been corrected. The log now accurately computes the UCC transactions at the county and the state level.

September 9, 1993

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Beginning with the 1994 fiscal year, the Office will send a quarterly invoice to each county based on the activities as recorded in the computerized transaction log. The billing system will be in place in time to provide invoices for the quarter ending September 30, 1993.

To be implemented by: Kathy Hjelm Date: September 30, 1993

2. **Finding:** The Secretary's office does not verify whether foreign corporations are paying the correct annual license fee.

**Recommendation:** The Secretary's office needs to develop controls to verify the Minnesota taxable net income figure on foreign corporations annual licenses.

**Response:** The annual registration for a foreign corporation is required in order for the corporation to maintain its authority to do business in the State. Part of the registration is the payment of a fee based on the foreign corporation's Minnesota taxable net income. The Secretary acknowledges that we do not currently verify the amount of the taxable net income reported. However, it should be noted that income tax returns are statutorily classified as confidential so the Office has no authority to require the corporation to produce it or access those returns at the Minnesota Department of Revenue. Therefore, these avenues of verification are not currently available to us.

The recommendation made by the audit report will require that the Office seek legislation which authorizes us to access tax returns filed with the Department of Revenue or receive a copy of the tax return from the corporation. The Secretary will pursue legislation in the 1994 session to address this recommended change in procedures. If legislation is approved, it will be implemented immediately.

To be implemented by: John Hughes By: Authority from the legislature

3. **Finding:** The Secretary's office did not cancel excess presidential primary reimbursement funds in a timely manner.

**Recommendation:** The Secretary's office should make a reasonable estimate of need when certifying open encumbrances.

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**Response:** The Secretary's office acknowledges that the estimate of open encumbrances exceeded what was ultimately needed but believes the estimate to have been reasonable given the information available at the end of fiscal year 1992. At the end of fiscal year 1992, approximately \$1,500,000 had been paid to local units of government, but several hundred (402) jurisdictions had not yet submitted reimbursement requests. As of the end of the biennium, 356 jurisdictions had still not submitted a request for reimbursement. Although it was ultimately determined that more money was carried forward into fiscal year 1993 than was needed to reimburse local units of government, the full balance of the unliquidated appropriation, \$877,000, was cancelled at the end of the 1992-1993 biennium.

As noted in the report, the Secretary administered the reimbursement program based on the understanding that the intent and goal of the legislature was to reimburse all local units of government for the cost of conducting the presidential primary. The 1993 legislature confirmed the validity of this belief by retroactively authorizing an additional use of funds from the appropriation to pay the expense of publishing the sample ballot which had not been previously included as a reimbursable expense. The 1993 amendment was based on requests to the Office from counties to add the sample ballot publication expense to the list of those authorized to be reimbursed. Once the amendment was passed, additional reimbursements were made from the appropriation.

To be implemented by: Joe Mansky Date: end of fiscal year  
in which a  
presidential  
primary occurs

Finally, please extend to your staff my sincere thanks for their objectivity, assistance and professionalism in conducting their audit of this Office.

Sincerely,

*Joan A. Growe*  
Joan Anderson Growe  
Secretary of State

JAG/kae