

**Office of the Secretary of State**

**Financial Audit**

**For the Two Calendar Years Ended December 31, 1996**

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**May 1997**

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

**97-27**





STATE OF MINNESOTA

**OFFICE OF THE LEGISLATIVE AUDITOR**

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JAMES R. NOBLES, LEGISLATIVE AUDITOR

Senator Deanna Wiener, Chair  
Legislative Audit Commission

Members of the Legislative Audit Commission

The Honorable Joan Anderson Growe  
Secretary of State

We have audited the Office of the Secretary of State for the period January 1, 1995, through December 31, 1996, as further explained in Chapter 1. Our audit scope included receipts, refunds, payroll, and capital equipment expenditures. The following summary highlights the audit objectives and conclusions. We discuss these issues more fully in the individual chapters of this report.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, as issued by the Comptroller General of the United States. These standards require that we obtain an understanding of management controls relevant to the audit. The standards also require that we design the audit to provide reasonable assurance that the Office of the Secretary of State complied with provisions of laws, regulations, and contracts significant to the audit. The management of the Office of the Secretary of State is responsible for establishing and maintaining the internal control structure and for compliance with applicable laws, regulations, and contracts.

This report is intended for the information of the Legislative Audit Commission and the management of the Office of the Secretary of State. This restriction is not intended to limit the distribution of this report, which was issued as a public document on May 7, 1997.

A handwritten signature in black ink, appearing to read "James R. Nobles".

James R. Nobles  
Legislative Auditor

A handwritten signature in black ink, appearing to read "John Asmussen".  
John Asmussen, CPA  
Deputy Legislative Auditor

End of Fieldwork: April 14, 1997

Report Signed On: May 2, 1997



# SUMMARY

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## Office of the Secretary of State

### Financial Audit

For the Two Calendar Years Ended December 31, 1996

Public Release Date: May 9, 1997

No. 97-27

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### Agency Background

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 Grove has served successive terms as the Secretary since January 1975. The Secretary serves as the chief election official of the state. In addition, the Secretary is the custodian of the state seal. The Office of the Secretary of State serves as the official repository for various public documents of the state.

### Audit Areas and Conclusions

Our audit scope included a review of fee and surcharge revenues, refunds, payroll, and capital equipment expenditures for the period from January 1, 1995, through December 31, 1996.

We reviewed fee and surcharge revenue collected by the Office of the Secretary of State, including revenue refunds. The office designed and implemented internal controls to provide reasonable assurance that it properly administered fee and surcharge revenue. The office also complied with applicable finance-related legal provisions for the fees tested.

We also audited payroll and capital equipment expenditures made by the Office of the Secretary of State. The office designed and implemented adequate internal controls to provide reasonable assurance that it accurately paid, recorded, and reported payroll and capital lease expenditures.



## 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
Eric Wion	Auditor
Connie Stein	Auditor

The findings and recommendations in this report were discussed with the following staff of the Office of the Secretary of State on April 24, 1997:

Elaine Voss	Deputy Secretary of State
Jayne Khalifa	Operations Director
Kathy Hjelm	Fiscal Supervisor





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## Chapter 1. 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 Secretary of State since January 1975. The Secretary of State serves as the chief election official of the state of Minnesota. As Election Judge, the Secretary ensures that elections are fair and comply with state rules and statutes. In addition, the Secretary of State is the custodian of the state seal.

The Office of the Secretary of State serves as the official repository for various public documents of the state. The office accepts filing information on businesses operating in Minnesota. The office is responsible for disseminating this information to a wide client group that includes the general public. The office is also responsible for maintaining 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. In addition, the office is responsible for a central notification system for farm product liens. This system contains information on loans from lenders to farmers.

The Office of the Secretary of State receives an appropriation from the Legislature to fund the majority of its activities. The appropriation law provides the office with funds for three activities: administration, operations, and election administration. The office has authority to transfer balances between these activities upon notifying certain legislative committees.

In addition to the General Fund appropriations, the Secretary's office charges customers for on-line access to the uniform commercial code network. The office deposits these receipts into the direct access dedicated account. The office uses dedicated account receipts to maintain the computerized uniform commercial code filing system and to provide electronic-view-only access to other computerized records.

Table 1-1 provides a summary of the Office of the Secretary of State's financial activities for fiscal year 1996. Table 1-2 provides a summary of other revenue for fiscal year 1996. Other revenue is deposited into a separate account and is not available for use by the Office of the Secretary of State. The individual financial areas are discussed in more detail in the remaining chapters of this report.

## Office of the Secretary of State

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**Table 1-1**  
**Office of the Secretary of State**  
**Summary of Financial Activities**  
**Fiscal Year 1996**

	General Fund	Direct Access Account
Beginning Balance	\$ 0	\$ 282,614
<u>Resources:</u>		
General Fund Appropriation	\$6,617,000	\$ 0
Revenues	0	414,684
Total Available Resources	<u>\$6,617,000</u>	<u>\$697,298</u>
<u>Expenditures:</u>		
Payroll	\$2,450,438	\$ 29,346
Capital Equipment Expenditures	2,530,915	326,374
Other Expenditures	1,382,844	69,134
Total Expenditures	<u>\$6,364,197</u>	<u>\$424,854</u>
Ending Balance	<u>\$252,803</u>	<u>\$272,444</u>

Source: Resources and expenditures recorded on the Minnesota Accounting and Procurement System (MAPS) for fiscal year 1996.

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**Table 1-2**  
**Office of the Secretary of State**  
**Other Revenue**  
**Fiscal Year 1996**

Service Charges	\$8,153,503
Surcharges	1,049,622
Farm Liens	17,070
Other Fees	38,848
Less Revenue Refunds	<u>(749,118)</u>
Net Other Revenue (1)	<u>\$8,509,925</u>

(1) As of July 1, 1995, the Secretary of State is required to deposit other revenue into a special revenue account. These funds are not, however, appropriated to the Secretary's office.

Sources: Revenue and revenue refunds recorded on the Minnesota Accounting and Procurement System (MAPS) for fiscal year 1996.

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## Chapter 2. Revenue and Refunds

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### *Chapter Conclusions*

*The Office of the Secretary of State properly designed and implemented internal controls to provide reasonable assurance that it properly charged, recorded, and deposited fee and surcharge revenue. In addition, the office properly designed and implemented internal controls to provide reasonable assurance that it properly authorized, adequately supported, and accurately processed revenue refunds. Finally, the office complied with applicable finance-related legal provisions for the fees tested.*

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### Revenues

The Office of the Secretary of State collects fees for business service filings, records processing filings which includes foreign corporation registrations, uniform commercial code transactions, and other fees. The office also collects a surcharge on uniform commercial code and farm lien filings and searches. Beginning July 1, 1995, Minnesota law requires the Office of the Secretary of State to deposit these receipts into a special revenue account. The Department of Finance and the Office of the Secretary of State review the fees annually. However, the Legislature ultimately establishes the individual fees in state statute.

In addition to the above receipts, the Office of the Secretary of State collects fees from customers who have on-line access to the uniform commercial code statewide computer network. The office deposits these receipts into a direct access account as dedicated revenue.

Table 2-1 summarizes nondedicated and dedicated revenue by source for fiscal year 1996.

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**Table 2-1**  
**Office of the Secretary of State**  
**Revenue by Source**  
**Fiscal Year 1996**

Uniform Commercial Code	\$1,245,139
Business Services	3,925,312
Records Processing	1,651,875
Surcharge	1,049,622
Direct Access	414,684
Other	1,405,608
Less Revenue Refunds	<u>(751,884)</u>
Net Revenue	<u>\$8,940,356</u>

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Source: Revenue recorded on the Minnesota Accounting and Procurement System (MAPS) for fiscal year 1996.

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## **Office of the Secretary of State**

The Office of the Secretary of State has a fiscal services division that centrally receives receipts through the mail or directly from customers at a counter window. The fiscal services division deposits receipts and attaches a receipt voucher to documents accompanying the individual receipts. Fiscal services forwards these documents to other office divisions for processing.

### **Audit Objectives and Methodology**

We focused our review of receipts on the following objectives:

- Did the Office of the Secretary of State design and implement internal controls to provide reasonable assurance that receipts were properly collected, recorded, and deposited in the correct accounts?
- Did the Office of the Secretary of State charge appropriate fees and surcharges for services provided in accordance with applicable finance-related legal provisions?

To address these objectives, we interviewed fiscal service division personnel to gain an understanding of the process of collecting and depositing receipts. In addition, we selected a random sample of all receipts and verified whether the office properly accounted for, deposited, and charged the appropriate fees. Finally, we interviewed staff from other divisions and performed additional tests and analytical reviews on some of the specific revenue sources to determine whether the office appropriately charged and deposited the receipts into the correct accounts. We discuss these specific tests in the remaining part of this chapter.

### **Direct Access Revenues**

The Office of the Secretary of State offers electronic access to certain public records it maintains. 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 direct access account. Office staff maintain account balances for each customer.

In addition to the electronic access, the office allows these customers to phone or fax in orders for copies of uniform commercial code files and business records, certificates of business records, and certified searches. Once the office performs the service, the fee is deducted from the customer's account. During our last audit, we questioned the Office of the Secretary of State's policy of retaining most of these fees in its direct access account. We recommended the office reconsider this policy. Beginning July 1, 1995, the office began transferring these funds from the direct access account to a special revenue account.

On a test basis, we verified that the office was accurately updating customer accounts for direct access receipts. In addition, we verified the accuracy of the amounts transferred from the direct access account to a special revenue account.

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### **Foreign Corporation Annual Registration**

Minnesota Statute Section 303.07 requires the Office of the Secretary of State to collect an annual license fee from each foreign corporation conducting business in Minnesota. The annual fee is based on each corporation's Minnesota taxable income for the last taxable year ending, plus a \$20 filing fee. Annual license fees are due from foreign corporations by May 15 or October 15 if an extension is filed. Failing to file by the deadline may result in the office revoking the corporation's certificate to operate in the state.

On a test basis, we verified whether foreign corporations paid appropriate fees by reviewing the annual registration forms. The office properly designed and implemented internal controls to provide reasonable assurance that it properly collected and deposited the correct registration fees.

### **Uniform Commercial Code (UCC) Surcharge**

The Office of the Secretary of State administers the statewide computer network for UCC activities. The 87 counties in Minnesota and the office use the system to record UCC filings and access this information. County recorders and the office are to access a \$5 surcharge on each UCC filing or search transaction. Minnesota law requires the office to collect and deposit surcharge revenues from the counties. The office maintains a computerized transaction log that tracks the total surcharge owed by the counties based on UCC transaction activity. Using this log, the office generates invoices for each county on a quarterly basis.

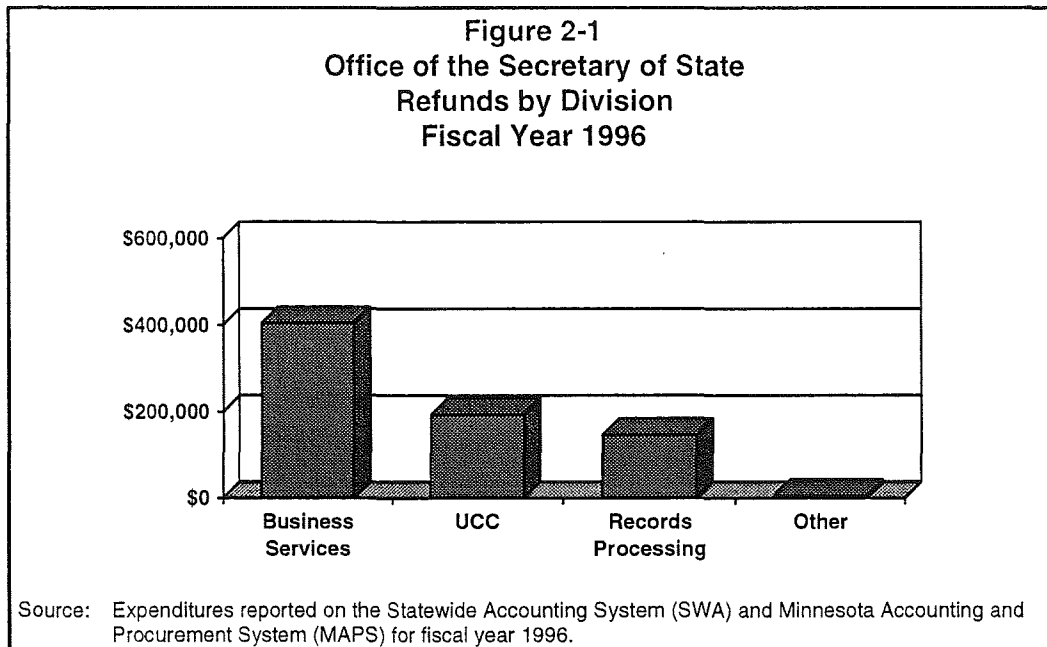
We completed an analysis to determine if amounts billed to counties were accurate using a computerized download of the UCC transaction activity. The office properly designed and implemented internal controls to provide reasonable assurance that the counties were charged accurately.

### **Refund Expenditures**

The Office of the Secretary of State issued revenue refunds primarily for rejected filings. In addition, the office generated some refunds due to fee overpayments. During fiscal year 1996, the office issued approximately \$750,000 in refund payments. Figure 2-1 shows a breakdown of these refund expenditures by division. The office deposited checks when received. If a division later rejected a filing, the office generated a refund payment.

As seen in figure 2-2, the UCC division had the greatest number of refunds. However, the business services division generated the largest dollar amount of refunds. Office staff reject filings due to customers failing to pay the correct fee or failing to include all required information within the document.

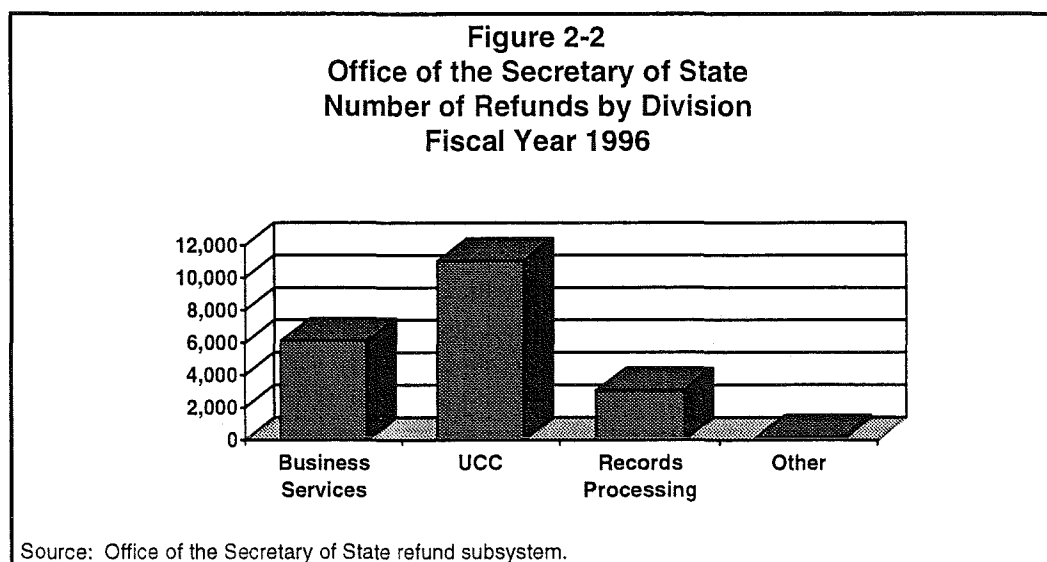
## Office of the Secretary of State



We focused our review of refunds on the following objective:

- Did the Office of the Secretary of State design and implement internal controls to provide reasonable assurance that refunds were properly authorized, adequately supported, and accurately processed?

To address this objective, we interviewed agency staff to gain an understanding of the refund process. In addition, we obtained a download of refund payments made during our audit scope. Using this download, we completed detailed transaction testing and analytical reviews to determine whether refund payments were properly authorized and supported.



Our last audit of the Office of the Secretary of State stated that the office did not have an adequate separation of duties over refund processing. In addition, the office did not have a

## **Office of the Secretary of State**

process in place to track whether it issued refunds to the appropriate customer. In October 1995, the office implemented an on-line refund authorization process. This process requires an on-line authorization of refund requests prior to the office issuing a refund payment. Using the download of refund transactions after October 1995, we tested refund payments and found that refunds were appropriately authorized. The Office of the Secretary of State designed and implemented controls to provide reasonable assurance that refunds were properly authorized, adequately supported, and accurately processed.

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## Chapter 3. Administrative Expenditures

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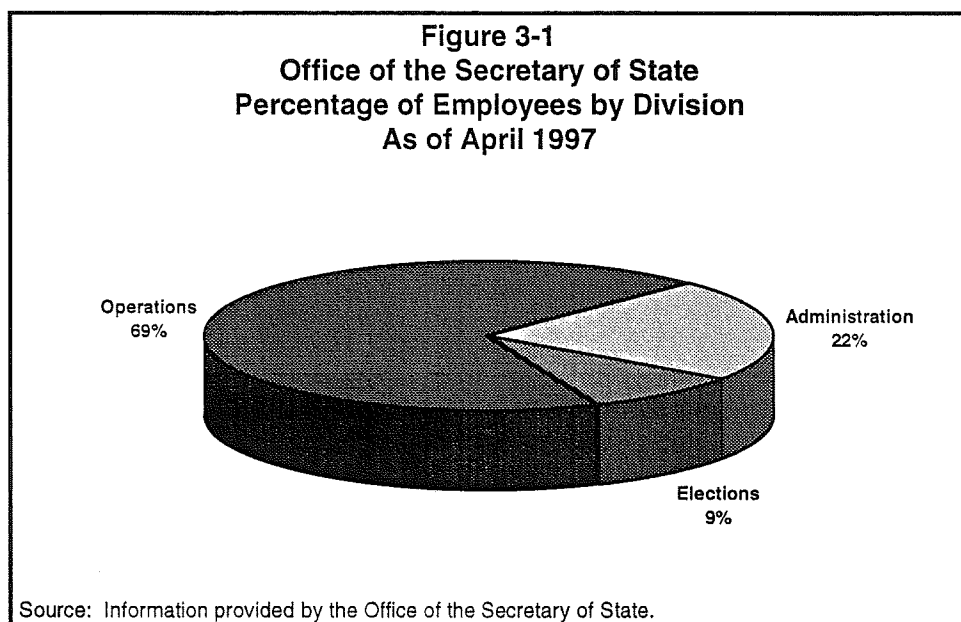
### *Chapter Conclusions*

*The Office of the Secretary of State designed and implemented adequate internal controls to provide reasonable assurance that it accurately paid, recorded, and reported payroll and capital equipment expenditures. In addition, the office adhered to the financial provisions of the capital lease agreement for the items tested.*

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### **Payroll**

The Office of the Secretary of State has approximately 64 full-time employees; most employees serve in classified positions. Minnesota Statutes authorize a separate compensation plan for the office's four unclassified employees. The office allocates and monitors personnel costs in three divisions. Figure 3-1 shows the percentage of employees in each division.



Employees process payroll biweekly using the statewide payroll system. For fiscal year 1996, the office disbursed approximately \$2.5 million in personnel expenditures.

### **Audit Objectives and Methodology**

We focused our review of payroll on the following objective:



## Office of the Secretary of State

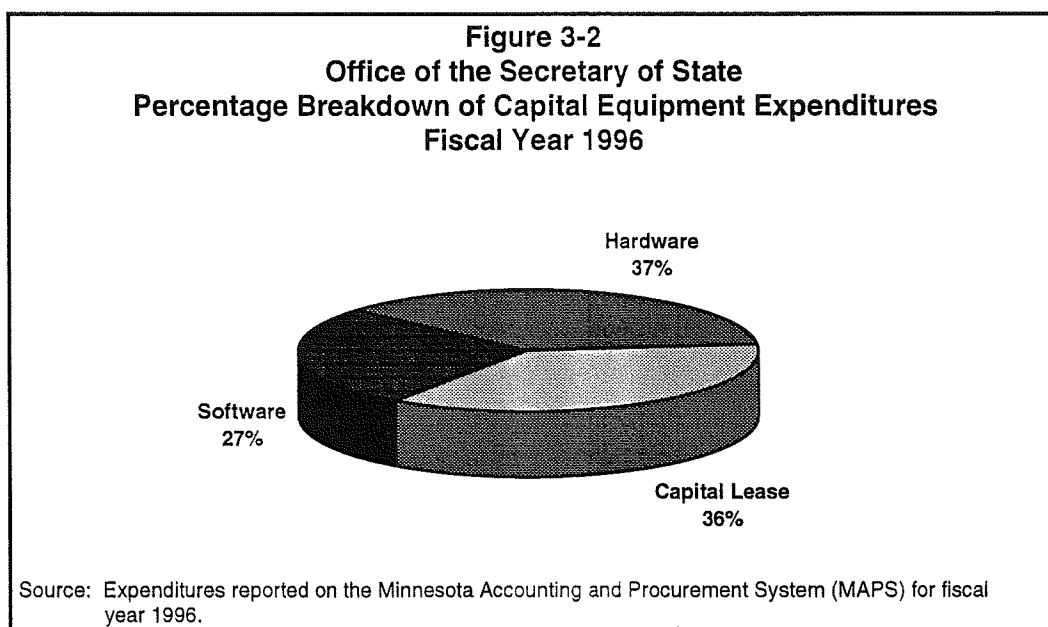
- Did the Office of the Secretary of State design and implement internal controls to provide reasonable assurance that payroll expenditures were properly authorized, adequately supported, and accurately processed?

To address this objective, we interviewed agency staff to gain an understanding of the payroll process. In addition, we selected a random sample of payroll transactions to ensure the office properly authorized, adequately supported, and accurately processed payroll.

The Office of the Secretary of State designed and implemented internal controls to provide reasonable assurance that it properly authorized, adequately supported, and accurately processed payroll expenditures.

## Capital Equipment Expenditures

The Office of the Secretary of State expended approximately \$3 million in computer and software expenditures during fiscal year 1996. Figure 3-2 shows a breakdown of how the office spent these funds. The office's fiscal year 1996 General Fund appropriation included approximately \$1 million to replace computer equipment in the 87 county recorder and county auditor offices.



The Office of the Secretary of State entered into a leasing agreement in 1989 to purchase a computer system to link the 87 counties to the office. The lease required principal and interest payments semi-annually of \$517,186 for a total of seven years. The office funded these payments primarily with its General Fund appropriation. However, the office funded a small portion with its direct access dedicated account. The office made its last lease payment on July 1, 1996.

## **Office of the Secretary of State**

### **Audit Objectives and Methodology**

We focused our review of capital equipment expenditures on the following objectives:

- Did the Office of the Secretary of State design and implement internal controls to provide reasonable assurance that computer and software purchases were properly authorized, adequately supported, appropriately accounted for, and accurately processed?
- Did the Office of the Secretary of State adhere to the financial provisions of the capital equipment lease agreement? Specifically, were the payments for principal and interest accurate?

To address these objectives, we interviewed agency staff to gain an understanding of the purchasing and disbursing process. We also interviewed agency staff to gain an understanding of the capital lease agreement. In addition, we selected a random sample of capital equipment expenditures and verified that the office properly authorized, adequately supported, and appropriately accounted for the expenditures. Finally, we reviewed the lease payments to ensure the office paid the correct amount.

The Office of the Secretary of State designed and implemented adequate internal controls to provide reasonable assurance that it properly authorized, adequately supported, appropriately accounted for, and accurately processed capital equipment expenditures. We also concluded that the Office of the Secretary of State had complied with financial provisions of the lease agreement for the items tested.