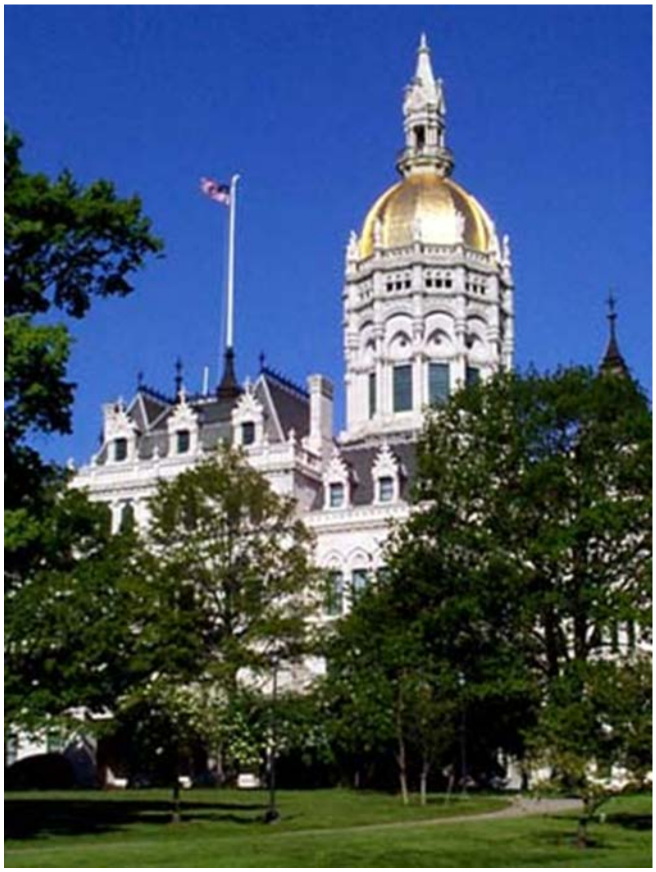
STATE OF CONNECTICUT



AUDITORS' REPORT
OFFICE OF THE SECRETARY OF THE STATE
FISCAL YEARS ENDED JUNE 30, 2013 AND 2014

AUDITORS OF PUBLIC ACCOUNTS
JOHN C. GERAGOSIAN ❖ ROBERT J. KANE

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STATE OF CONNECTICUT

AUDITORS OF PUBLIC ACCOUNTS

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ROBERT J. KANE

January 9, 2018

AUDITORS' REPORT
OFFICE OF THE SECRETARY OF THE STATE
FOR THE FISCAL YEARS ENDED JUNE 30, 2013 AND 2014

We have audited certain operations of the Office of the Secretary of the State in fulfillment of our duties under Section 2-90 of the Connecticut General Statutes. The scope of our audit included, but was not necessarily limited to, the fiscal years ended June 30, 2013 and 2014. The objectives of our audit were to:

1. Evaluate the office's internal controls over significant management and financial functions;

2. Evaluate the office's compliance with policies and procedures internal to the department or promulgated by other state agencies, as well as certain legal provisions; and

3. Evaluate the economy and efficiency of certain management practices and operations, including certain financial transactions.

Our methodology included reviewing written policies and procedures, financial records, minutes of meetings, and other pertinent documents; interviewing various personnel of the department, as well as certain external parties; and testing selected transactions. We obtained an understanding of internal controls that we deemed significant within the context of the audit objectives and assessed whether such controls have been properly designed and placed in operation. We tested certain of those controls to obtain evidence regarding the effectiveness of their design and operation. We also obtained an understanding of legal provisions that are significant within the context of the audit objectives, and we assessed the risk that illegal acts, including fraud, and violations of contracts, grant agreements, or other legal provisions could occur. Based on that risk assessment, we designed and performed procedures to provide reasonable assurance of detecting instances of noncompliance significant to those provisions.

We conducted our audit in accordance with the standards applicable to performance audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United

States. Those standards require that we plan and perform our audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides such a basis.

The accompanying Résumé of Operations is presented for informational purposes. This information was obtained from the office's management and was not subjected to the procedures applied in our audit of the office. For the areas audited, we identified:

1. Deficiencies in internal controls;

2. Apparent noncompliance with legal provisions; and

3. Need for improvement in management practices and procedures that we deemed to be reportable.

The State Auditors' Findings and Recommendations in the accompanying report presents any findings arising from our audit of the Office of the Secretary of the State.

COMMENTS

FOREWORD

The Secretary of the State is an elected state officer whose duties are set forth in Title 3, Chapter 33, of the Connecticut General Statutes. The Secretary of the State serves as the chief election and business registrar and is the official keeper of public records and documents. Denise W. Merrill served as the Secretary of the State and James F. Spallone served as Deputy Secretary of the State during the audited period.

The primary functions of the Secretary of the State are:

- Custodian of the state seal; public records and documents, particularly of the acts, resolutions and orders of the General Assembly; other public documents recorded and filed, including state agency regulations, schedules of state board and commission meetings, town ordinances, and the surety bonds of state officers and employees.

- Commissioner of Elections of the state, which includes being the repository of political party rules and campaign finance statements and compiling voter registration statistics.

- Recording various corporate certifications and reports as well as the collection of appropriate fees.

- Recording commercial transactions and collecting applicable fees in accordance with the Uniform Commercial Code (UCC).

- Appointments of notaries public.

- Publishing the State Register and Manual and other publications.

In addition, in accordance with Section 20-280 subsection (e) of the General Statutes, as amended by Public Act 11-48, the State Board of Accountancy was within the Office of the Secretary of the State during the audited period. The board is responsible for licensing and regulating the public accounting profession in this state. Members of the board are appointed by the Governor, and their appointments are coterminous with the Governor's term of office. As of June 30, 2014, the members of the board were:

John H. Schuyler, CPA, Chairman
Mark Aronowitz
Timothy F. Egan, CPA
Dannell R. Lyne, CPA, MST
Marcia L. Marien, CPA
Peter J. Niedermeyer, CPA
Martha S. Triplett, Esq.
As of June 30, 2014, there were two vacancies

The Office of the Secretary of the State has organized itself into five divisions in order to address its duties and responsibilities: State Board of Accountancy, Commercial Recording, Legislation and Election Administration, Information Technology, and Management and Support Services.

Legislative Changes

Public Act 14-154, effective January 1, 2015, authorizes the Secretary of the State to dissolve entities that fail to file annual reports, and make changes regarding the notice of final action the Secretary distributes concerning the following:

- Dissolution, termination, or revocation of authority and authorization of a limited liability partnership to seek reinstatement;
- Changes to the Secretary's procedures to revoke the certificate of authority to conduct business in Connecticut for foreign stock and nonstock corporations;
- Eliminates a number of fees for business entities filing documents with the Secretary to terminate their existence or cease doing business in Connecticut; and
- Requires various business entities to include their email addresses on certain documents filed with the Secretary.

Subsequent Event

Public Act 16-3 of the May Special Session of the General Assembly transferred the State Board of Accountancy and its functions from the Office of the Secretary of the State to the Department of Consumer Protection, effective July 1, 2016.

RÉSUMÉ OF OPERATIONS

Revenues

Revenues for the Office of the Secretary of the State by fund for the fiscal years under review and the preceding year follows:

	2011-2012	2012-2013	2013-2014
General Fund	$ 31,581,096	$ 30,056,604	$ 32,715,784
Federal and Other Restricted Account Fund	924,416	82,271	8
Total Revenues Listed by Fund	**$ 32,505,512**	**$ 30,138,875**	**$ 32,715,792**

General Fund receipts represent the majority of receipts and are discussed further below. The Federal and Other Restricted Accounts Fund decreased significantly during the 2012-2013 and 2013-2014 fiscal years due to the depletion of Help America Vote Act (HAVA) funds. The federal government last allocated HAVA grant funds in the 2009-2010 fiscal year.

Revenues for the Office of the Secretary of the State by revenue account for the fiscal years under review and the preceding year follows:

	2011-2012	2012-2013	2013-2014
Commercial Recording Fees	$ 25,922,044	$ 24,312,097	$ 26,837,599
State Board of Accountancy	2,622,875	2,626,286	2,668,695
Penalties-Corporations	1,297,047	1,276,938	1,554,545
Other Fees-Certificates/Copies	833,719	839,740	891,031
Franchise Taxes	6,543	301	43,968
Notary Public Registrations	769,651	786,975	789,700
Sales of Documents and Publications	96,509	150,936	116,965
All Other Receipts	413,677	492,484	375,399
Federal and Other Restricted Funds	924,416	82,271	8
Refund of Receipts	(380,968)	(429,052)	(562,119)
Total Revenue by Funds	**$32,505,512**	**$30,138,875**	**$ 32,715,792**

Receipts consisted primarily of business filing fees and penalties collected by the Division of Commercial Recording and licensing fees collected by the State Board of Accountancy. Commercial Recording Fees increased during the 2013-2014 fiscal year due to the joint efforts of the Foreign Investigation Unit and the Attorney General's office in collecting fees from out-of-state businesses that conduct business in the state. Revenues from franchise taxes fluctuated based on the number of shares issued or amended by domestic corporations. The decrease in revenue from the sales of documents and publications in the 2013-2014 fiscal year was the result of a reduction in the printing of legislative publications.

Expenditures

Expenditures by fund for the Office of the Secretary of the State are presented below:

	2011-2012	**2012-2013**	**2013-2014**
General Fund	$ 7,358,807	$ 6,924,203	$ 9,308,025
Federal and Other Restricted Account Fund	1,987,314	1,594,297	48,493
Capital Improvement and Other Purpose Funds	716,846	1,537,540	1,842,076
Capital Equipment Fund	6,899	3,214	37,247
Total Expenditures Listed by Fund	**$ 10,069,867**	**$ 10,059,254**	**$ 11,235,841**

Total expenditures remained stable from the 2011-2012 fiscal year to the 2012-2013 fiscal year; however, expenditures increased by 12% for the fiscal year ended June 30, 2014.

General Fund Expenditures

General Fund expenditures for the Office of the Secretary of the State are presented below:

General Fund	**2011-2012**	**2012-2013**	**2013-2014**
Personal Services & Employee Benefits	$ 5,872,423	$ 5,522,927	$ 5,803,297
Employee Expenses, Allowance and Fees	7,346	21,144	22,481
Purchased & Contract Services	570,070	582,348	496,120
Motor Vehicles Cost	14,538	16,290	10,653
Premises and Property Expenses	20,564	19,902	17,936
Information Technology	535,160	365,645	2,206,392
Communications	66,225	266,879	438,365
Purchased Commodities	151,904	104,510	150,217
Equipment	120,576	24,559	162,564
Total Expenditures Listed by Accounts	$ 7,358,807	$ 6,924,203	$ 9,308,025

General Fund expenditures primarily consisted of personal services and employee benefits. General Fund expenditures decreased by 5.9% from the 2011-2012 fiscal year to the 2012-2013 fiscal year. However, General Fund expenditures increased by 34.4% from the 2012-2013 fiscal year to the 2013-2014 fiscal year primarily due to the upgrades and the maintenance of the computer systems and the agency's support of the Connecticut Data Collaborative. The Connecticut Data Collaborative is a public-private partnership working to increase the quality and availability of data for effective planning and policy, budgeting and decision-making in Connecticut at the state, regional, and local levels.

Federal and Other Restricted Accounts Expenditures

A summary of Federal and Other Restricted Accounts expenditures for the Office of the Secretary of the State is presented below:

	2011-2012	2012-2013	2013-2014
Federal and Other Restricted Accounts			
Information Technology	$ 1,987,314	$ 1,585,028	$ 48,493
Purchased Commodities	0	7,074	0
Personnel Services	0	2,195	0
Total Expenditures	**$ 1,987,314**	**$ 1,594,297**	**$ 48,493**

The Federal and Other Restricted Accounts expenditures decreased by 20.2% from the 2011-2012 fiscal year to the 2012-2013 fiscal year and 96.9% from the 2012-2013 fiscal year to the 2013-2014 fiscal year due to the Help America Vote Act (HAVA) project coming to an end.

Capital Improvement and Other Purpose Fund Expenditures

Capital Improvements and Other Purpose Fund expenditures totaled $1,537,540 and $1,842,076 for the fiscal years ended June 30, 2013 and 2014, respectively. Capital Improvement and Other Purpose Funds increased 114.5% from the 2011-2012 fiscal year to the 2012-2013 fiscal year due to the cost of upgrading the office's computer system and computer servers. In addition, Capital Improvement and Other Purpose Fund expenditures increased by 19.8% from the 2012-2013 fiscal year to the 2013-2014 fiscal year due to an adjustment in equipment made by the State Comptroller in order to comply with Generally Accepted Accounting Principles (GAAP).

Capital Equipment Fund Expenditures

Capital Equipment Fund expenditures totaled $3,214 and $37,247 for the fiscal years ended June 30, 2013 and 2014, respectively. The purchases were primarily for office equipment.

Connecticut Citizenship Fund

The Connecticut Citizenship Fund was established as a foundation, pursuant to Section 4-37e of the General Statutes. This organization was created to increase citizen interest and participation in government, particularly state and local government; increase and improve citizen participation in elections; stimulate more education and involvement of Connecticut's school-aged children concerning government; and engage in any lawful act or activity for which corporations may be formed under said act.

Sections 4-37f through 4-37j of the General Statutes establish certain requirements for foundations affiliated with state agencies. Section 4-37f of the General Statutes sets forth the requirement that any foundation must have a full audit of its books and accounts either annually or every third year, depending on the amount of revenue received each year. The fund's level of revenue required an audit every 3 years. The last audit was performed for the 2010-2011 fiscal year and, per the auditor's opinion, the financial statements were presented fairly in accordance with Generally Accepted Accounting Principles.

STATE AUDITORS' FINDINGS AND RECOMMENDATIONS

Our review of the Office of the Secretary of the State's records disclosed the following areas that require improvement.

Payroll/Personnel – Leave Accruals

Criteria: Section 5-251 of the General Statutes states that employees receiving compensation benefits shall continue to accrue their regular sick and vacation leave for the first 12 months. After that, employees shall accrue based on the ratio of their work compensation in accordance with regulations issued by the Commissioner of the Department of Administrative Services.

Good internal control dictates time and attendance must be recorded in the statewide Core-CT payroll and personnel system.

The Core-CT time reporting code (TRC) leave in lieu of accrual (LILA) is intended to be temporary while leave issues are being resolved. Agencies should run the TRC usage report for the LILA reporting code and change any instances to the appropriate leave balances.

Condition: Our review of the sick and vacation accrual leave time of 7 employees disclosed that 4 employees were accruing leave at an incorrect rate. Employees received 51.42 hours of sick leave and 43.42 hours of vacation leave hours they were not entitled to.

We found that 1 employee earned 33 hours of compensatory time, which was not recorded as earned or used in the state's accounting system.

In addition, we found that LILA balances for 2 employees totaling 13.5 hours were not adjusted.

Effect: Employee time and attendance records were inaccurate.

Cause: There appears to be a lack of managerial knowledge regarding the processing of time and attendance records.

Recommendation: The Office of the Secretary of the State should improve administrative controls over the processing of time and attendance records. (See Recommendation 1.)

Agency Response: "Upon the auditors' prior year's findings, the agency separated the human resources (HR) function from our Managerial Support Services Division (MSS). For a time, HR functions were performed by the HR Specialist, who reported to the Deputy Secretary, and the payroll administrator reported to the MSS manager, thus creating a separation between HR and payroll. However, the payroll administrator retired and was replaced part-time by an existing SOTS employee, who otherwise reports to the Business Services Division.

In the meantime and in response to these findings, the agency's human resources associate and part-time payroll administrator were refreshed about approximately nine (9) new—for this staff—payroll reports that had not been run before. Both employees received training in running and analyzing these reports. In addition, a tracking system was implemented to monitor leave accruals, SEBAC v Rowland compensatory damages accrual time, Compensatory Time Earned and Compensatory Time Used, Family and Medical Leave Act coding, Leave In Lieu of Accrual and other payroll, HR and/or benefits use based on monthly and/or biweekly payroll timesheet coding. Management encourages, and the staff continues to seek, additional training on these new reporting documents. Also, a comprehensive audit of all leave accrual assignments and use in CORE-CT was conducted on each employee. A summary report of the findings was prepared and submitted."

Inventory Control and Reporting:

Criteria: Section 4-36 of the General Statutes requires an agency to establish and maintain an inventory system as prescribed by the Office of the State Comptroller. The State Property Control Manual specifies requirements and standards that state agency property control systems must comply with, including tagging, recording, and maintaining capital assets and controllable property in the Core-CT Asset Management module. During the audited period, assets with a value of $1,000 or more were capitalized and, when applicable, property with a unit value of less than $1,000 was recorded as controllable. The agency is required to transmit an annual Asset Management Report (CO-59) to the Office of the State Comptroller, which is the detailed inventory of all property, real or personal, owned by the state and in custody of such agency.

Condition: Amounts disclosed on the CO-59 report for several categories were inaccurate for the fiscal years ended June 30, 2013 and 2014. Our review of the fiscal year 2012-2013 records disclosed that the equipment additions were understated by $17,753, equipment deletions were understated by $8,860, capital software was overstated by $8,240, and licensed software was overstated by $575,304. Our review of the fiscal year 2013-2014 records disclosed that the equipment additions were understated by $27,158, equipment deletions were understated by $1,854, and licensed software was overstated by $30,000.

We also noted a variance of $3,048,333 between the GAAP Personal Property balances listed on the Core-CT Cost Activity Report and the amount disclosed on the CO-59 report as of June 30, 2014. This variance was not reconciled by the agency.

Effect: The annual inventory reports submitted to the Office of the State Comptroller are inaccurate and incomplete.

Cause: The purchasing department did not correctly code capital items when they were acquired; therefore, capital items were not captured in the Core-CT Asset Management Module. The inventory unit included controllable items in the equipment balances and did not reconcile the Core-CT capital purchases to the Core-CT Asset Module. Undetected errors in the ending inventory of the asset management reports have accumulated over several years.

Recommendation: The Office of the Secretary of the State should abide by the policies and procedures within the State Property Control Manual and strengthen internal controls to ensure that balances disclosed on the CO-59 reports are accurate and reconciled to the Core-CT Cost Activity Report. (See Recommendation 2.)

Agency Response: "The agency agrees with the finding of conditions stated above. In response, the Fiscal Manager has reviewed the State Property Control Manual with staff to ensure inventory controls are met. All staff has the most updated chart of accounts and General Letters, and has been directed to the Comptroller's website to access the property control manual. Our Central Duplicating Supervisor and a temporary staffer have spent a great deal of time properly tagging assets over the dollar threshold that needs to be reported in CORE. They also worked with staff to list all non-controllable assets that must be listed on a spreadsheet. Bi-Annual inventory is conducted on all assets, both controllable and non-controllable items. A revised copy of the CO-59 is being submitted with the 2016 report to the Office of the State Comptroller."

Inventory Control – Software and Merchandise for Sale Inventory

Criteria: The Comptroller's Property Control Manual establishes the guidelines for maintaining a software inventory and merchandise for sale inventory. This includes the inventory format, procedures for conducting an annual physical inventory, and preparing an annual inventory report.

Condition: The office software inventory records did not include all of the information required by the State Property Control Manual.

Merchandise for sale inventory was inaccurate and incomplete. The office maintains a perpetual merchandise inventory of its publications consisting of approximately 41 items, including 21 items for sale and 20 items that were free to the public. Our review disclosed that 9 out of 10 (90%) of the items for sale tested were inaccurate. For 1 item, the 2014 State Register and Manual, the inventory records presented 73,274 copies on hand when only 662 copies were on hand and only 5,400 copies had been purchased. The remaining items were misstated by 14 to 877 copies.

Effect: The office was not in compliance with the State Property Control Manual software inventory and merchandise inventory requirements.

Inaccuracies in the merchandise for sale inventory may result in undetected losses.

Cause: There appears to be lack of managerial oversight.

Recommendation: The Office of the Secretary of the State should abide by procedures within the State Property Control Manual for software inventory and strengthen internal controls to ensure the perpetual inventory records of merchandise for sale are accurate and complete. (See Recommendation 3.)

Agency Response: "The agency agrees with the finding of conditions stated above. Since the time of this audit, the Information Technology (IT) Division has undergone a change of management. Management and Support Services works in concert with our new IT Manager and his staff. In turn, IT receives copies of requisitions for all software ordered along with a detailed CORE report on all software purchases. IT staff can then keep a record in our agency Track-it system which should balance with our CORE system. Over the next 8 months the IT staff will enter all previously purchased software into the Track-it system and reconcile it to CORE. Regarding inaccuracies in the agency's merchandise for sale inventory, we experienced the loss of one of the two staff assigned to manage this inventory. In response to this finding, and lacking the ability to replace this employee, the agency recently utilized a temporary employee to correct past inaccuracies and to bring these records up to date."

Petty Cash Reporting

Criteria: The Office of the State Comptroller requires agencies to submit a petty cash report as of April 30th, no later than May 31st of each fiscal year. In addition, the Office of the State Comptroller requires agencies to reconcile the petty cash fund account.

Condition: During our review of the petty cash fund, we noted that the agency did not reconcile the petty cash fund for the 2012-2013 and 2013-2014 fiscal years.

In addition, we found that the agency did not submit the 2013-2014 fiscal year petty cash report to the State Comptroller in a timely manner.

Effect: When reconciliations do not occur in a timely manner, errors in the recording of cash may not be detected and could increase the risk of loss.

Cause: There appears to be a lack of managerial oversight.

Recommendation: The Office of the Secretary of the State should improve internal controls over the petty cash fund by preparing reconciliations and submitting the annual petty cash reports to the State Comptroller in a timely manner. (See Recommendation 4.)

Agency Response: "The agency agrees with the finding of conditions stated above. The Fiscal Manager was on medical leave in 2014 which caused a delay in reporting the petty cash report in a timely manner. The Fiscal Administrative Assistant was retrained several times on how to reconcile the petty cash fund. The Fiscal Manager had to assume those duties to work on closing out the account. The reports in 2015 and 2016 were reported in a timely manner."

Administration of Foreign Corporation Investigations and Receivables

Background: Sections 33-920, 33-1210, 34-38g, 34-223, 34-429 and 34-531 of the General Statutes require foreign corporations, limited liability companies, limited partnerships, and limited liability partnerships to file a certificate of authority or registration with the Secretary of the State before transacting business in Connecticut. A foreign corporation is organized under a law other than the law of Connecticut. Foreign corporations requiring a certificate must submit an application fee, annual reports, and the associated fees to the office.

Investigations of unauthorized foreign corporations often begin with a complaint from competing business entities or consumers, or when a foreign corporation submits an application for a certificate of authority indicating that they have transacted business in Connecticut in excess of 90 days, or from analyzing registration of surety bonds of nonresident contractors.

Criteria: The State Accounting Manual sets forth the procedures to account for receivable amounts and establishing and maintaining effective internal controls, for which the Secretary of State is responsible. Internal controls should provide for proper documentation of transactions, reconciliation of accounts, timely collection efforts, and write-off of uncollectible accounts.

In addition, a sound information system should allow management and employees to effectively monitor various phases of cases. This includes generating an accounts receivable aging report, determining whether the case is open or closed and reviewing payment balances. This would allow management to take proper steps to collect outstanding receivables.

Condition: The Foreign Corporation Investigation database could not provide management and employees useful tools to monitor investigations in their various phases. The information system could not produce an accounts receivable aging report or a report that would assist the staff to monitor payments.

Our review disclosed that potential revenue-generating events were not immediately reviewed. We noted that 6 out of 20 (30%) closed investigations included in our review had a time lag of 5 to 8 months between the date that the office discovered a late registration and the date the office issued demand letters for the penalties and registration fees. Furthermore, the agency has not requested the Contractor Bond Registration List from the Department of Revenue Services (DRS) since 2007. This list would have allowed the office to determine whether there were entities conducting business in the State of Connecticut without the proper authorization, and if so, assess the required penalties and fees.

Effect: The management information system did not have useful data to manage accounts receivable. Employee resources were diverted from other activities to compensate for deficiencies of the information system.

Loss of revenues to the state may have occurred due to the delayed request for the Contractor Bond Registration List from the Department of Revenue Services. Delays in issuing demand letters resulted in delays in the collection of revenues.

Cause: The information system used by the Foreign Corporation Investigation Unit was not designed for financial information. The system was initially designed for investigation staff to record notes and approvals. The office has planned to improve the system since 2010. However, budget constraints did not permit system improvement during the audited period since other system modifications to accommodate internet filing took priority.

Due to the Foreign Corporation Investigation Unit's limited staffing and its current workload, the agency did not request the Bond Registration List from the Department of Revenue Services and issued demand letters quarterly instead of monthly.

Recommendation: The Office of the Secretary of the State should implement changes to the Foreign Corporation Investigations Unit's information system so that users can effectively monitor investigations in their various stages and generate essential receivable reports. In addition, the Office of the Secretary of the State should analyze the cost and benefits of allocating additional resources to the unit so that potential revenue-generating events can be promptly reviewed. (See Recommendation 5.)

Agency Response: "The agency agrees with the finding of conditions stated above. The agency has developed a new system for administration of foreign investigations. The new, web based system allows users to monitor investigations in their various phases by providing a dashboard that lists all open and closed files by name and case number. Each individual file includes case status, penalty assessment information and correspondence and payment histories. Although the new, web based system allows the user to make status changes, it does not allow files to be deleted. Our Information Technology Manager is working with the vendor to add this function to the new, web based system (a document status report is used to identify receivables in the parallel, legacy system). The Agency will analyze the cost and benefits of allocating additional resources so that potential revenue generating events can be promptly reviewed."

Segregation of Duties

Criteria: A good internal control system requires separation of duties among payroll and human resources personnel. The Core-CT Change Management Team's Combined Human Resources Management System (HRMS) Role Assessment Handbook emphasizes that agencies should not request that the agency human resources specialist role be assigned to an employee who has the agency payroll specialist role. Access to these roles could allow an individual to hire and pay someone inappropriately and without oversight. The agency HRMS security liaison role is responsible for monitoring all authorized access to the Core-CT HRMS application assigned to the agency personnel. Access should be granted to employees to complete their work assignments. To ensure separation of duties and reduce the risk of error and fraud in the payroll and human resources roles, the same employee should not authorize, record, and review transactions unless other compensating controls are established.

Condition: During our review of access to the Core-CT information system, we noted that 1 employee had access to both the human resources specialist role and the agency payroll specialist role. In addition, there did not appear to be any compensating controls, since the payroll clerk reported to the human resources specialist.

Effect: When an employee has access to both payroll and human resources functions, there is increased risk that fraudulent transactions can be processed and not detected.

Cause: Management overrode automated controls within Core-CT by requesting that certain security access be granted to one individual.

Recommendation: The Office of the Secretary of the State should implement proper segregation of duties between payroll and personnel functions. (See Recommendation 6.)

Agency Response: "The agency agrees with the finding of conditions stated above. The deficiencies cited above are due in part to budget constraints that do not permit the agency to maintain adequate staffing levels to support the best practices recommended.

Following these findings in the previous report, the agency made a request to hire a separate payroll staffer. In 2013, the Department of Administrative Services addressed the issue of segregation of duties by stating that in extraordinary circumstances it may be necessary for an individual to have such conflicting roles. The Department of Administrative Services clarified that in order to ensure compliance with accepted security procedures, updated justification must now be provided to explain the continued necessity of the conflicting role, as well as to explain the internal audit procedures in place to prevent inappropriate or fraudulent transactions. A sample justification was provided to the agency. The agency complied with the request for justification and entered it into CORE Security. The justification explained the extraordinary circumstances and the internal audit, that Human Resources was a necessary back-up for payroll, that a supervisor would approve Human Resources and Payroll entries into CORE (to avoid inappropriate or fraudulent transactions) and that reports would be submitted to a supervisor for review or follow-up.

The extraordinary fiscal circumstance that the agency faced in 2013 and 2014 continues. The current system will be maintained and strengthened due to increased reporting requirements, monitoring and tracking.

The agency did adhere to established segregation of duties, but also qualified as having extraordinary circumstances, via approved justification to CORE-CT HRMS security."

Recording, Reconciling, and Reporting of Revenues and Receivables Accounts

Criteria:

Good internal controls require the proper documentation of transactions, reconciliation of accounts, timely write-off of uncollectible accounts, and timely consideration of customer refunds. Reviewing and reconciling customer account balances ensures that recording errors can be detected in a timely manner.

Section 3-99a subsection (c) of the General Statutes establishes a 1-year limit for refunds of any overpayments related to documents or fees.

The State Accounting Manual requires that a receipts journal be maintained by all agencies receiving money. The journal must consist of sufficient columns for the date of receipt, receipt number when pre-numbered receipts are issued, name of payer, or other identification. Separate columns are also required for listing receipts by revenue classification (revenue account code), total receipts, the amount deposited, the deposit slip number, and the date of deposit.

Good internal controls require segregation of duties between the persons who receive, deposit, and record receipts.

Condition:

Our review of 25 of 128,673 customer accounts totaling $9,936,040 disclosed that the account balances of 14 customer accounts were overstated by $1,182,525 (12%) of the total balance reviewed. These overstatements were caused by data entry errors in which check numbers, credit card numbers or financial transaction identification numbers were recorded as the payment amounts, and the inability of the financial system to generate historical accounts receivable reports. These data entry errors occurred in July 1995 through March 2015.

The office does not have a separate non-lapsing fund that would allow it to maintain a deferred revenue fund. All funds collected are deposited in the General Fund. Customers with multiple work orders (called frequent filers) often pay in advance or receive credits for any rejected filings. A frequent filer customer's account balance is increased when advance payment is received or when credit is provided for a rejected filing. In addition, since Section 3-99(a)(c) of the General Statues requires a 1-year limit for the refund of overpayments, this practice appears to violate the General Statutes.

The agency does not maintain a cash receipts journal to support the daily receipt of monies by the Commercial Recording Division.

As stated in the prior audit report, we continued to note a lack of separation of duties within the Financial Unit. A Financial Unit employee continues to have the ability to receive, record receipts, modify customer account balances and perform daily reconciliation of deposits without supervisory review.

Effect: Current internal controls over revenue do not provide management with reasonable assurance that all receipts are properly accounted for and that revenue losses are not occurring. The lack of segregation of duties and monthly reconciliations increases the risk of undetected losses. In addition, there is noncompliance with the General Statutes.

Cause: Commercial Recording Division (CRD) staff did not reconcile the daily receipts to the daily data entry. Therefore, data entry errors went undetected for several years. CRD staff has never reviewed the customer account balances to determine whether the funds on account are accurate and complete.

The office faced challenges in improving its business filing information system to accommodate new filing requirements and to financially account for its services. The current information system could not separate the customer account balances pertaining to credits provided for rejected filing and balances pertaining to advanced cash payments by customers.

Management has not established internal controls that would manage deferred revenues.

The lack of segregation of duties and recording deficiencies can be attributed to a lack of available staffing.

Recommendation: The Office of the Secretary of the State should strengthen internal controls over receipts and should implement procedures to comply with the General Statutes. (See Recommendation 7.)

Agency Response: "This issue, inherited by the current administration, is not easily resolved. It became apparent upon the elimination of the non-lapsing account in 2009. Facing a fiscal crisis, the General Assembly eliminated the SOTS' and similar accounts. The agency, on its own initiative and in response to audit reports, has taken actions to correct the problem and has sought guidance from appropriate agencies.

The office took action pursuant to law to eliminate balances of less than $5.00. Staff also took action to correct key stroke errors through review of accounts. Additionally, the office corresponded with the attorney general, seeking advice of whether accounts older than one year could be written off. On February 6, 2014 the attorney general's office issued an informal opinion that because overpayments were customarily credited toward future payments, this might toll the statutory one-year limit, making it difficult to determine when the right to a refund accrued and when the state's right to retain the sums vested. The attorney general's office characterized this as an accounting problem. The agency then met with senior staff at the Office of Policy and Management about potential administrative actions or legislative changes. No clear course of action emerged.

In 2016, the Secretary introduced online filing of business entity formations and foreign entity registrations, expanding a catalog of online options, including online annual report filing. These are paid for by credit card; overpayments resulting in credits on account are not possible. This transition is a perfect time to end the practice of permitting moneys to be held on account. The Secretary intends to end the practice on a date certain, most likely January 1, 2017. Customers will receive notice to use the credits by a date certain thereafter, thus providing a date from which the right to any refund will run. This should allow the agency to fully address the problem."

Connecticut Citizen Foundation Reporting Requirements

Criteria: Section 4-37f, subsection (8), of the General Statutes requires that any foundation which has receipts and earnings totaling less than $100,000 in each fiscal year during any 3 of its consecutive fiscal years, shall have completed on its behalf for the third fiscal year in any such 3 year period, a full audit of the books and accounts of the foundation. Also, for each fiscal year in which an audit is not required, the foundation shall provide financial statements to the executive authority of the state agency.

Condition: The Connecticut Citizen Foundation has not had a full audit of its books and accounts since the 2010-2011 fiscal year. In addition, the foundation did not provide the Secretary of the State with financial statements for the 2011-2012 and 2012-2013 fiscal years for which its receipts and investment earnings were less than $100,000.

Effect: The foundation was not in compliance with the Section 4-37f, subsection (8) of the General Statutes.

Cause: There was a lack of managerial oversight.

Recommendation: The Office of the Secretary of the State should strengthen internal controls to ensure that the Connecticut Citizen Foundation complies with the statutory requirements regarding audits of its books and accounts and the submission of financial statements in each year that an audit is not required. (See Recommendation 8.)

Agency Response: "The agency agrees with the finding of conditions stated above. The agency engaged a firm to complete an audit of the Connecticut Citizen Foundation upon being made aware that it was not in compliance. The audit was completed on June 30, 2014. The agency will comply with this audit requirement going forward."

Statutory Reporting

Criteria: Section 4-60 of the General Statutes requires that the executive head of each budgeted agency shall, on or before September 1st, deliver to the Governor a report of the activities of such agency during the preceding fiscal year. The Governor shall immediately file such reports with the Commissioner of Administrative Services, who shall edit the same with regard to contents, arrangement and brevity, and cause them to be published in convenient form for distribution not later than December 1st.

Section 9-612 subsection (g)(1) of the General Statutes requires state agencies to submit on a monthly basis to the State Elections Enforcement Commission (SEEC) a list of the (1) names of the state and prospective state contractors with which they have or could have a contract and (2) state contract solicitations or prequalification certificates they have issued.

Condition: Our review disclosed that the Office of the Secretary of the State did not submit the required monthly Contract Certificate Report to the State Elections Enforcement Commission (SEEC) for 5 months in the 2012-2013 fiscal year and 6 months in the 2013-2014 fiscal year. We also noted that the office did not submit a report to the Department of Administrative Services for inclusion in the 2014 Digest of Administrative Reports to the Governor.

Effect: The Office of the Secretary of the State was not in compliance with the state's statutory reporting requirements.

Cause: It appears that inadequate management oversight contributed to a lack of reporting.

Recommendation: The Office of the Secretary of the State should strengthen internal controls to ensure that all statutorily required reports are submitted in a timely manner. (See Recommendation 9.)

Agency Response: "The agency agrees with the finding of conditions stated above. The office is in the midst of a strategic plan. Among the matters being addressed is intra-office communication. This issue will be addressed in the context of that plan, but in the short term the agency will develop a tickler system to ensure that all report requests are properly logged and reports are filed on time. Often these report requests come from an executive branch email in the ordinary course of business and can easily get overlooked. A master calendar and tickler system will help avoid this problem."

RECOMMENDATIONS

The prior audit contained 6 recommendations. One has been implemented or otherwise resolved and 5 have been repeated or restated with modifications during the current audit. The following is a summary of the action taken on the prior recommendations.

Status of Prior Audit Recommendations:

- **The Office of the Secretary of the State should improve its monitoring of employees' leave balances and Core-CT Personnel Actions History Reports and obtain proper authorization to transfer funds between specific appropriations.** We found that this condition has been partially resolved and will be repeated in a modified form. (See Recommendation 1.)

- **The Office of the Secretary of the State needs to improve recordkeeping for its customer account balances.** We found that this condition has not been resolved and will be repeated in a modified form. (See Recommendation 7.)

- **The Office of the Secretary of the State should consider other internal control procedures to mitigate the lack of segregation of duties over receipts, completely reconcile its in-house revenues and receipts records to Core-CT, and prepare accountability reports for revenues of the State Board of Accountancy.** This recommendation has been partially resolved and will be modified to remove prior findings that were corrected. (See Recommendation 7.)

- **The Office of the Secretary of the State should review the cost and benefits of allocating additional resources to the Foreign Investigations Unit so that receivables can be effectively managed.** We found that this condition has not been resolved and will be repeated in a modified form. (See Recommendation 5.)

- **The Office of the Secretary of the State should abide by the policies and procedures within the State Property Control Manual for software inventory, and ensure that balances in the CO-59 forms are accurate and reconciled to the Core-CT Cost Activity Report.** We found that this condition has not been resolved and will be repeated in a modified form. (See Recommendations 2 and 3.)

- **The Office of the Secretary of the State should request the necessary authority to enforce annual report filing requirements to improve collections and the accuracy of its business database.** This recommendation has been resolved.

Current Audit Recommendations:

1. **The Office of the Secretary of the State should improve administrative controls over the processing of time and attendance records.**

   Comment:

   Our review disclosed errors in the time and attendance records.

2. **The Office of the Secretary of the State should abide by the policies and procedures within the State Property Control Manual and strengthen internal controls to ensure that balances disclosed on the CO-59 reports are accurate and reconciled to the Core-CT Cost Activity Report.**

   Comment:

   Our review disclosed several errors in the preparation of annual inventory reports.

3. **The Office of the Secretary of the State should abide by procedures within the State Property Control Manual for software inventory and strengthen internal controls to ensure the perpetual inventory records of merchandise for sale are accurate and complete.**

   Comment:

   Our review disclosed that software inventory records were incomplete and the perpetual merchandise for sale inventory records contained significant errors.

4. **The Office of the Secretary of the State should improve internal controls over the petty cash fund by preparing reconciliations and submitting the annual petty cash reports to the State Comptroller in a timely manner.**

   Comment:

   Our review disclosed that the petty cash account was not reconciled during the audited period and the petty cash report was not submitted to the State Comptroller in a timely manner.

5. **The Office of the Secretary of the State should implement changes to the Foreign Corporation Investigation Unit's information system so that users can effectively monitor investigations in their various stages and generate essential receivable reports. In addition, the Office of the Secretary of the State should analyze the cost and benefits of allocating additional resources to the unit so that potential revenue-generating events can be promptly reviewed.**

Comment:

Our review disclosed that the Secretary of the State's information system did not effectively assist users to monitor investigations and receivables. In addition, a lack of resources prevented staff from reviewing potential revenue-generating sources.

6. **The Office of the Secretary of the State should implement proper segregation of duties between payroll and personnel functions.**

   Comment:

   Our review disclosed that 1 employee was given access to both payroll and personnel functions within Core-CT without proper compensating controls.

7. **The Office of the Secretary of the State should strengthen internal controls over receipts and should implement procedures to comply with the General Statutes.**

   Comment:

   Our review disclosed that customer account balances were misstated, not compliant with the 1-year limit on refunds of overpayments, lacked a cash receipts journal, and had inadequate segregation of duties in the Financial Unit.

8. **The Office of the Secretary of the State should strengthen internal controls to ensure that the Connecticut Citizen Foundation complies with the statutory requirements regarding audits of its books and accounts and the submission of financial statements in each year that an audit is not required.**

   Comment:

   Our review disclosed that the Connecticut Citizen Foundation did not submit financial statements to the Secretary of the State for the 2011-2012 and 2012-2013 fiscal years, which were the years an audit was not required. In addition, as of June 1, 2015, the required 2013-2014 fiscal year audit report had not been completed.

9. **The Office of the Secretary of the State should strengthen internal controls to ensure that all statutorily required reports are submitted in a timely manner.**

   Comment:

   Our review disclosed that the Office of the Secretary of the State did not submit several of its statutorily required reports in a timely manner.

CONCLUSION

In conclusion, we wish to express our appreciation for the courtesies and cooperation extended to our representatives by the personnel of the Office of the Secretary of the State during the course of our examination.

Kathrien E. Williams
Associate Auditor

Approved:

John C. Geragosian
State Auditor

Robert J. Kane
State Auditor