



A REPORT  
TO THE  
MONTANA  
LEGISLATURE

FINANCIAL-COMPLIANCE AUDIT

*Office of the  
Secretary of State*

*For the Two Fiscal Years Ended  
June 30, 2008*

OCTOBER 2008

LEGISLATIVE AUDIT  
DIVISION

08-19

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# LEGISLATIVE AUDIT DIVISION

Tori Hunthausen, Legislative Auditor  
Monica Huyg, Legal Counsel



Deputy Legislative Auditors  
James Gillett  
Angie Grove

October 2008

The Legislative Audit Committee  
of the Montana State Legislature:

This is our financial-compliance audit report on the Office of the Secretary of State (office) for the two fiscal years ended June 30, 2008. The recommendations in this report relate to compliance with state law and policy on ensuring fees charged for business services are commensurate with the cost of providing those services, recording prior year expenses, improving internal controls, and excess vacation leave.

The office's written response to the audit recommendations is included in the back of the audit report, beginning on page B-3.

We thank the Secretary of State and his staff for their assistance and cooperation.

Respectfully submitted,

*/s/ Tori Hunthausen*

Tori Hunthausen, CPA  
Legislative Auditor



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## ELECTED, APPOINTED, AND ADMINISTRATIVE OFFICIALS

### Office of the Secretary of State

Brad Johnson, Secretary of State

Ralph Peck, Chief Deputy

Janice Doggett, Chief Legal Counsel

Jean Branscum, Deputy for Administrative Rules and Notary

Tana Gormly, Deputy for Business Services

Lisa Kimmet, Deputy for Elections

Patti Borsberry, Deputy for Records and Information  
Management

For additional information concerning the Office of the  
Secretary of State, contact Brad Johnson, Secretary of State, at:

PO Box 202801  
Helena MT 59620-2801  
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## REPORT SUMMARY

### Office of The Secretary of State

This financial-compliance audit report documents the results of our audit of the Office of the Secretary of State (office) for the two fiscal years ended June 30, 2008. We issued a qualified opinion on the Schedule of Changes in Fund Balances for the fiscal year ended June 30, 2007 and the Schedule of Expenditures & Transfers-Out for the fiscal year ended June 30, 2007. The reader should use caution when using the information presented in these schedules, as well as the supporting data on the state's accounting system for fiscal year 2006-07. We issued an unqualified opinion on the Schedule of Revenue & Transfers-In for the fiscal year ended June 30, 2007, and on all three financial schedules for the fiscal year ending June 30, 2008. The reader may rely on the presented financial information and the supporting data on the state's accounting system for fiscal year 2007-08.

This audit report contains four recommendations. The recommendations relate to ensuring fees charged for business services are commensurate with the cost of providing those services, recording prior year expenses in accordance with state accounting policy, improving internal controls, and forfeiting excess vacation leave. The prior audit of the office included six recommendations. The office implemented five of these recommendations. The recommendation not implemented relates to the ending fund balance in the Enterprise Fund.

The listing below serves as a means of summarizing the recommendations contained in the report, the office's response thereto, and a reference to the supporting comments.

#### Recommendation #1

We recommend the office comply with state law by ensuring the fees charged for its business services reflect the cost of providing those services, taking into consideration the ending fund balance.....3

Office Response: Conditionally Concur..... B-3

#### Recommendation #2

We recommend the office enhance controls to ensure prior year expenditures are accurately recorded on the state's accounting records in accordance with state law. ....4

Office Response: Concur..... B-3

Recommendation #3

We recommend the office implement procedures for monitoring and testing its internal control procedures as required by state policy. ....5

Office Response: Concur..... B-4

Recommendation #4

We recommend the office ensure excess vacation leave is forfeited as required by state law.....6

Office Response: Concur..... B-4

# Chapter I – Introduction

## Introduction

We performed a financial-compliance audit of the Office of the Secretary of State (office) for the two fiscal years ended June 30, 2008. The audit objectives were to:

1. Determine office compliance with selected laws and regulations.
2. Obtain an understanding of the office’s control systems to the extent necessary to support our audit of the office’s financial schedules and if appropriate, make recommendations for improvements in management and internal controls of the office.
3. Determine the implementation status of prior audit recommendations.
4. Determine if the financial schedules present fairly the results of operations of the office for the two fiscal years ended June 30, 2008.

Auditing standards require us to communicate, in writing, control deficiencies we identified as a result of audit objective #2 above and considered to be significant or material. A control deficiency exists when the design or operation of a control does not allow management or employees to prevent or detect misstatements on a timely basis. A significant deficiency is one or more control deficiencies that affects management’s ability to accurately process transactions. A material weakness is one or more significant deficiencies that adversely affect management’s ability to fairly present its financial schedules.

Table 1 below outlines the status of significant deficiencies and material weaknesses we identified during this audit.

Subject	Significant Deficiency	Material Weakness	Page
Prior Year Activity	Yes	No	3

This report contains four recommendations to the office. Areas of concern not having a significant effect on the successful operations of the office are not included in this report but have been discussed with management. In accordance with section 5-13-307, MCA, we analyzed and disclosed the cost, if significant, of implementing the recommendations in this report.

We audited the Enterprise Fund fees charged by the office to determine whether fees were commensurate with the overall costs of the office and reasonably reflected the

prevailing rates charged in public and private sectors for similar services, as required by section 2-15-405(2)(a), MCA. We noted the office's fund balance was not considered when setting fees commensurate with costs, as described on page 3 of this report.

## **Background**

Article VI, section 1, of the Montana Constitution states the executive branch of state government includes a Secretary of State. Title 2, chapter 15, part 4, of the Montana Code Annotated sets forth the Secretary of State's duties. The office has 54.25 FTE in four divisions and the executive office. The office files, stores, maintains, and preserves permanent records of the state and certain public interest records of private citizens. The office publishes the Montana Administrative Register (MAR) and the Administrative Rules of Montana (ARM). The office is also responsible for the commissioning of Notary Publics in Montana. In fiscal year 2008, the office was authorized 54.25 FTE (full-time equivalent employee).

The Secretary of State serves as chief election officer for the state, maintaining uniformity in the application of the election laws and retaining election records through the Elections Bureau. In addition, the Secretary of State serves as a member of the Board of Land Commissioners and the Board of Examiners.

## **Prior Audit Recommendations**

We performed the prior audit of the office for the two fiscal years ended June 30, 2006, which contained six recommendations to the office. The office implemented five recommendations. The recommendation not implemented, which relates to the fund balance in the Enterprise Fund, is discussed on page 3.

## Chapter II – Findings and Recommendations

### Fund Balance in the Enterprise Fund

---

**The fund balance in the Enterprise Fund is excessive due to fees not commensurate with costs in prior years.**

---

Section 2-15-405(2)(a), MCA, requires the office to charge fees that reflect the cost of providing its various business services. During the audit period, revenue collected through fees did approximate the expense. However, the fiscal year 2007-08 ending fund balance is approximately \$3.5 million, which means the fees were not commensurate with expenses in prior years, and the excess was not fully considered in setting rates. Therefore, the prior audit recommendation is not implemented.

Office management indicated the \$3.5 million fund balance will be used to implement the office's information technology systems. The office should examine the costs associated with its various business services, and take into consideration the current fund balance, in order to set rates commensurate with the costs of providing the services.

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#### **RECOMMENDATION #1**

*We recommend the office comply with state law by ensuring the fees charged for its business services reflect the cost of providing those services, taking into consideration the ending fund balance.*

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### Prior Year Financial Activity

---

**The office recorded federal expenditures in the wrong fiscal year.**

---

The office's fiscal staff is responsible for processing approximately \$7 million of expenditure activity each fiscal year in accordance with state law and accounting policy. The following discusses two instances of accounting errors related to prior year transactions.

- ♦ In fiscal year 2007, the office requested a budget amendment for the movement of prior year budget authority. After the budget amendment was approved, the office moved approximately \$2.5 million of prior year federal grant expenditures. However, the transaction contained several coding errors. These coding errors caused fiscal year 2007 Federal Special Revenue

Fund expenditure activity to be understated by \$2.5 million and prior year expenditure activity to be overstated by \$2.5 million. The office intended the expenditures to net against each other as prior year expenditure activity in two different appropriations. This error contributed to the Independent Auditor's Report qualification on page A-3.

- ◆ In August 2006, fiscal staff recorded the payment of \$235,000 in other services costs as a fiscal year 2007 expenditure. The invoice, dated June 19, 2006, was a request for payment of the 10 percent holdback on project deliverables on a computer system. The system was completed as of June 19, 2006 and the 10 percent holdback was due upon completion and therefore a fiscal year 2006 expenditure. The office should have recorded a prior year expenditure. As a result, fiscal year 2007 other services expenditures are overstated by \$235,000 in the Federal Special Revenue Fund and fiscal year 2007 beginning fund balance is overstated by the same amount.

Section 17-1-102(4), MCA, requires the office to record financial activity on the state's accounting records in accordance with generally accepted accounting principles. These principles include recording expenditures in the proper fiscal year.

Office management explained the fiscal staff that recorded and monitored the above activity are no longer with the office. Current fiscal procedures include monitoring fiscal activity and budgets on a monthly basis and tracking invoices to ensure they are paid timely. The office should enhance controls to monitor the financial activity at the fiscal and program year level to ensure activity is recorded in the proper fiscal year.

---

### **RECOMMENDATION #2**

*We recommend the office enhance controls to ensure prior year expenditures are accurately recorded on the state's accounting records in accordance with state law.*

---

## **Internal Controls**

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**The office has not fully implemented its internal control procedures in accordance with state accounting policy.**

---

State policy effective December 1, 2007, outlines management's responsibility for establishing and maintaining office internal controls to safeguard and account for the resources entrusted to them to carry out government programs. State policy requires the office to develop internal control procedures, and monitor and test its internal controls.

Auditing standards require us to evaluate and in some cases report on the sufficiency of written control procedures and of the entity's monitoring and testing procedures.

During the course of the audit, the office put significant effort towards documenting its control procedures. To accomplish this, office staff created flowcharts and procedure/policy manuals documenting controls and monitoring points. Although, the office does have a plan for how they will test control procedures, no actual testing has been completed. Office management should continue their efforts and implement a monitoring and testing plan to ensure the controls are working as intended. The previous report section on prior year activity is an indication of where control procedures may need to be improved and/or monitoring for compliance with controls procedures needs to occur.

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**RECOMMENDATION #3**

*We recommend the office implement procedures for monitoring and testing its internal control procedures as required by state policy.*

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## **Excess Vacation Balance**

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**The office did not forfeit excess vacation leave for one employee as required by state law.**

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Section 2-18-617, MCA, limits the accumulation of employee vacation leave to twice the amount an employee earns in a calendar year. Leave accumulated above these amounts is considered "excess" and must be used by the employee within the first 90 days of each calendar year. If the employee requests, and management denies, the use of excess leave during the 90-day period, forfeiture may be delayed until the end of the end of the calendar year. In no case does the law allow excess vacation leave to be held past the end of the calendar year.

The office was not in compliance with this state law for one employee. The office allowed one employee to carry forward 84 hours of calendar 2006 vacation leave in excess of the amount allowed under state law. The 84 hours should have been forfeited in January 2008 since the employee did not use the leave by December 31, 2007. The value of the excess vacation leave is \$2,625.

Office management approved the carry forward of the excess vacation leave because they thought a separate employment agreement applied to the employee's vacation leave. However, upon further research they determined the employment agreement only applied to excess exempt compensatory time. The office has informed the employee that the excess vacation leave will be forfeited in accordance with state law.

The office would not have incurred the liability of \$2,625 if the excess leave would have been forfeited as required by state law. The office should consistently forfeit excess leave as required by state law, to guarantee fair and consistent treatment of all office employees.

---

**RECOMMENDATION #4**

*We recommend the office ensure excess vacation leave is forfeited as required by state law.*

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# Independent Auditor's Report and Office Financial Schedules



Tori Hunthausen, Legislative Auditor  
Monica Huyg, Legal Counsel



Deputy Legislative Auditors  
James Gillett  
Angie Grove

## INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee  
of the Montana State Legislature:

We have audited the accompanying Schedules of Changes in Fund Balances, Schedules of Total Revenues & Transfers-In, and Schedules of Total Expenditures & Transfers-Out of the Office of the Secretary of State for each of the fiscal years ended June 30, 2008, and 2007. The information contained in these financial schedules is the responsibility of the office's management. Our responsibility is to express an opinion on these financial schedules based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial schedules are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial schedules. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial schedule presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in note 1, these financial schedules are prepared on the basis of Montana state accounting policy, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The schedules are not intended to be a complete presentation and disclosure of the office's assets, liabilities, and cash flows.

The office made errors in recording prior year activity in the Federal Special Revenue Fund in fiscal year 2006-07. On the Schedule of Changes in Fund Balances, the Budgeted Expenditures & Transfers-Out is understated and the Prior Year Expenditures & Transfers-Out is overstated by \$2,498,940, respectively. On the Schedule of Expenditures & Transfers-Out, Prior Year Expenditures & Transfers-Out Adjustments is overstated, the Actual Budgeted Expenditures & Transfers-Out is understated by \$2,498,940 respectively. Also, the total Unspent Budget Authority and Federal Special Revenue unspent budget authority are overstated by \$2,498,940, respectively.

A-4

In our opinion, except for the effects of the errors discussed in the preceding paragraph, the financial schedules referred to above present fairly, in all material respects, the results of operations and changes in fund balances of the Office of the Secretary of State for each of the fiscal years ended June 30, 2008, and 2007, in conformity with the basis of accounting described in note 1.

Respectfully submitted,

*/s/ James Gillett*

James Gillett, CPA  
Deputy Legislative Auditor

September 2, 2008

SECRETARY OF STATE'S OFFICE  
SCHEDULE OF CHANGES IN FUND BALANCES  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

	Federal Special Revenue Fund	Enterprise Fund
FUND BALANCE: July 1, 2007	\$ <u>4,038,715</u>	\$ <u>3,808,191</u>
ADDITIONS		
Budgeted Revenues & Transfers-In	226,443	5,120,911
Nonbudgeted Revenues & Transfers-In	1,061	1,069
Prior Year Revenues & Transfers-In Adjustments		34,917
Direct Entries to Fund Balance	<u>5,394</u>	<u>(21,804)</u>
Total Additions	<u>232,898</u>	<u>5,135,093</u>
REDUCTIONS		
Budgeted Expenditures & Transfers-Out	1,151,109	5,169,940
Nonbudgeted Expenditures & Transfers-Out		292,289
Prior Year Expenditures & Transfers-Out Adjustments	<u>7,624</u>	<u>5,813</u>
Total Reductions	<u>1,158,733</u>	<u>5,468,042</u>
FUND BALANCE: June 30, 2008	\$ <u><u>3,112,880</u></u>	\$ <u><u>3,475,242</u></u>

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-11.

SECRETARY OF STATE'S OFFICE  
SCHEDULE OF CHANGES IN FUND BALANCES  
FOR THE FISCAL YEAR ENDED JUNE 30, 2007

	Federal Special Revenue Fund	Enterprise Fund
FUND BALANCE: July 1, 2006	\$ <u>5,119,047</u>	\$ <u>3,893,786</u>
ADDITIONS		
Budgeted Revenues & Transfers-In	264,521	5,006,579
Nonbudgeted Revenues & Transfers-In	1	1
Prior Year Revenues & Transfers-In Adjustments		1,918
Direct Entries to Fund Balance		616,678
Total Additions	<u>264,522</u>	<u>5,625,176</u>
REDUCTIONS		
Budgeted Expenditures & Transfers-Out	(1,153,295)	4,926,998
Nonbudgeted Expenditures & Transfers-Out	(70)	873,646
Prior Year Expenditures & Transfers-Out Adjustments	<u>2,498,219</u>	<u>(89,873)</u>
Total Reductions	<u>1,344,854</u>	<u>5,710,771</u>
FUND BALANCE: June 30, 2007	\$ <u><u>4,038,715</u></u>	\$ <u><u>3,808,191</u></u>

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-11.

SECRETARY OF STATE'S OFFICE  
SCHEDULE OF TOTAL REVENUES & TRANSFERS-IN  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

	<u>Federal Special Revenue Fund</u>	<u>Enterprise Fund</u>	<u>Total</u>
<b>TOTAL REVENUES &amp; TRANSFERS-IN BY CLASS</b>			
Charges for Services		\$ 4,836,144	\$ 4,836,144
Investment Earnings	\$ 152,504	153,650	306,154
Sale of Documents, Merchandise and Property		116,413	116,413
Miscellaneous		50,690	50,690
Federal	75,000		75,000
Total Revenues & Transfers-In	<u>227,504</u>	<u>5,156,897</u>	<u>5,384,401</u>
Less: Nonbudgeted Revenues & Transfers-In	1,061	1,069	2,130
Prior Year Revenues & Transfers-In Adjustments		34,917	34,917
Actual Budgeted Revenues & Transfers-In	<u>226,443</u>	<u>5,120,911</u>	<u>5,347,354</u>
Estimated Revenues & Transfers-In	456,000	4,913,000	5,369,000
Budgeted Revenues & Transfers-In Over (Under) Estimated	<u>\$ (229,557)</u>	<u>\$ 207,911</u>	<u>\$ (21,646)</u>
<b>BUDGETED REVENUES &amp; TRANSFERS-IN OVER (UNDER) ESTIMATED BY CLASS</b>			
Charges for Services		\$ 245,181	\$ 245,181
Investment Earnings	\$ (229,557)	(41,419)	(270,976)
Sale of Documents, Merchandise and Property		(19,437)	(19,437)
Miscellaneous		23,586	23,586
Budgeted Revenues & Transfers-In Over (Under) Estimated	<u>\$ (229,557)</u>	<u>\$ 207,911</u>	<u>\$ (21,646)</u>

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-11.

SECRETARY OF STATE'S OFFICE  
SCHEDULE OF TOTAL REVENUES & TRANSFERS-IN  
FOR THE FISCAL YEAR ENDED JUNE 30, 2007

	<u>Federal Special Revenue Fund</u>	<u>Enterprise Fund</u>	<u>Total</u>
<b>TOTAL REVENUES &amp; TRANSFERS-IN BY CLASS</b>			
Charges for Services		\$ 4,598,903	\$ 4,598,903
Investment Earnings	\$ 207,522	196,073	403,595
Sale of Documents, Merchandise and Property		134,916	134,916
Miscellaneous		78,606	78,606
Federal	57,000		57,000
Total Revenues & Transfers-In	<u>264,522</u>	<u>5,008,498</u>	<u>5,273,020</u>
Less: Nonbudgeted Revenues & Transfers-In	1	1	2
Prior Year Revenues & Transfers-In Adjustments		1,918	1,918
Actual Budgeted Revenues & Transfers-In	<u>264,521</u>	<u>5,006,579</u>	<u>5,271,100</u>
Estimated Revenues & Transfers-In	172,000	3,480,933	3,652,933
Budgeted Revenues & Transfers-In Over (Under) Estimated	<u>\$ 92,521</u>	<u>\$ 1,525,646</u>	<u>\$ 1,618,167</u>
<b>BUDGETED REVENUES &amp; TRANSFERS-IN OVER (UNDER) ESTIMATED BY CLASS</b>			
Charges for Services		\$ 1,304,692	\$ 1,304,692
Investment Earnings	\$ 67,521	176,072	243,593
Sale of Documents, Merchandise and Property		25,901	25,901
Miscellaneous		18,981	18,981
Federal	25,000		25,000
Budgeted Revenues & Transfers-In Over (Under) Estimated	<u>\$ 92,521</u>	<u>\$ 1,525,646</u>	<u>\$ 1,618,167</u>

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-11.



SECRETARY OF STATE'S OFFICE  
SCHEDULE OF TOTAL EXPENDITURES & TRANSFERS-OUT  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

PROGRAM (ORG) EXPENDITURES & TRANSFERS-OUT	<u>BUSINESS &amp; GOVERNMENT SERVICES</u>
Personal Services	
Salaries	\$ 2,272,661
Employee Benefits	771,234
Personal Services-Other	83,791
Total	<u>3,127,686</u>
Operating Expenses	
Other Services	1,397,773
Supplies & Materials	172,427
Communications	209,063
Travel	158,520
Rent	251,517
Utilities	1,186
Repair & Maintenance	295,201
Other Expenses	308,741
Goods Purchased For Resale	12,608
Total	<u>2,807,036</u>
Equipment & Intangible Assets	
Equipment	53,912
Total	<u>53,912</u>
Grants	
From State Sources	4,350
From Federal Sources	447,185
Total	<u>451,535</u>
Benefits & Claims	
OPEB Expenses	186,606
Total	<u>186,606</u>
Total Expenditures & Transfers-Out	<u>\$ 6,626,775</u>
 EXPENDITURES & TRANSFERS-OUT BY FUND	
Federal Special Revenue Fund	\$ 1,158,733
Enterprise Fund	5,468,042
Total Expenditures & Transfers-Out	6,626,775
Less: Nonbudgeted Expenditures & Transfers-Out	292,289
Prior Year Expenditures & Transfers-Out Adjustments	13,436
Actual Budgeted Expenditures & Transfers-Out	6,321,050
Budget Authority	10,113,630
Unspent Budget Authority	<u>\$ 3,792,580</u>
 UNSPENT BUDGET AUTHORITY BY FUND	
Federal Special Revenue Fund	\$ 2,554,593
Enterprise Fund	1,237,987
Unspent Budget Authority	<u>\$ 3,792,580</u>

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-11.

SECRETARY OF STATE'S OFFICE  
SCHEDULE OF TOTAL EXPENDITURES & TRANSFERS-OUT  
FOR THE FISCAL YEAR ENDED JUNE 30, 2007

PROGRAM (ORG) EXPENDITURES & TRANSFERS-OUT	BUSINESS & GOVERNMENT SERVICES
Personal Services	
Salaries	\$ 1,923,626
Employee Benefits	640,699
Personal Services-Other	46,555
Total	2,610,880
Operating Expenses	
Other Services	1,768,603
Supplies & Materials	110,409
Communications	676,833
Travel	97,315
Rent	189,658
Utilities	1,023
Repair & Maintenance	168,840
Other Expenses	840,573
Goods Purchased For Resale	9,782
Total	3,863,036
Grants	
From Federal Sources	580,722
Total	580,722
Transfers	
Accounting Entity Transfers	987
Total	987
Total Expenditures & Transfers-Out	\$ 7,055,625
 EXPENDITURES & TRANSFERS-OUT BY FUND	
Federal Special Revenue Fund	\$ 1,344,854
Enterprise Fund	5,710,771
Total Expenditures & Transfers-Out	7,055,625
Less: Nonbudgeted Expenditures & Transfers-Out	873,576
Prior Year Expenditures & Transfers-Out Adjustments	2,408,345
Actual Budgeted Expenditures & Transfers-Out	3,773,704
Budget Authority	10,768,043
Unspent Budget Authority	\$ 6,994,339
 UNSPENT BUDGET AUTHORITY BY FUND	
Federal Special Revenue Fund	\$ 6,913,883
Enterprise Fund	80,456
Unspent Budget Authority	\$ 6,994,339

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-11.

**Office of the Secretary of State**  
**Notes to the Financial Schedules**  
**For the Two Fiscal Years Ended June 30, 2008**

## **1. Summary of Significant Accounting Policies**

### **Basis of Accounting**

The Office of the Secretary of State (office) uses the modified accrual basis of accounting, as defined by state accounting policy, for its Federal Special Revenue Governmental fund category, and certain liabilities of defined benefit pension plans and certain post employment healthcare plans. In applying the modified accrual basis, the office records:

- ◆ Revenues when it receives cash or when receipts are realizable, measurable, earned, and available to pay current period liabilities.
- ◆ Expenditures for valid obligations when the department incurs the related liability and it is measurable, with the exception of the cost of employees' annual and sick leave. State accounting policy requires the office to record the cost of employees' annual and sick leave when used or paid.

The office uses accrual basis accounting for its Proprietary (Enterprise) fund. Under the accrual basis, as defined by state accounting policy, the office records revenues in the accounting period when realizable, measurable, and earned, and records expenses in the period incurred when measurable.

Expenditures and expenses may include: entire budgeted service contracts even though the office receives the services in a subsequent fiscal year; goods ordered with a purchase order before fiscal year-end, but not received as of fiscal year-end; and equipment ordered with a purchase order before fiscal year-end.

### **Basis of Presentation**

The financial schedule format is in accordance with the policy of the Legislative Audit Committee. The financial schedules are prepared from the transactions posted to the state's accounting system without adjustment.

The office uses the following funds:

### **Governmental Fund Category**

- ◆ **Federal Special Revenue Fund** – to account for activities funded from federal revenue sources. The office's Federal Special Revenue Funds includes activity related to the Help America Vote Act (HAVA), Election Reform Payments and Election Assistance for Individuals with Disabilities.

### Proprietary Fund Category

- ♦ **Enterprise Fund** – to account for operations (a) financed and operated in a manner similar to private business enterprises, where the Legislature intends that the department finance or recover costs primarily through user charges; (b) where the Legislature has decided that periodic determination of revenues earned, expenses incurred or net income is appropriate; (c) where the activity is financed solely by a pledge of the net revenues from fees and charges of the activity; or (d) when laws or regulations require that the activities' cost of providing services, including capital costs, be recovered with fees and charges rather than with taxes or similar revenues. The office's Enterprise Fund includes business services, administrative rules, elections filings, management services, information services, and records management services.

## 2. Federal Special Revenue Fund

- ♦ **Fiscal year 2007 prior year activity** – The Prior Year Expenditures & Transfers-Out of \$2,498,219 shown on the Schedule of Changes in Fund Balances should be netted with the Budgeted Expenditures & Transfers-Out of (\$1,153,295) to reflect the actual fiscal year 2007 Federal Special Revenue Fund expenditures of \$1,344,854.
- ♦ **Fund Balance** – The office received three installments of the HAVA funds in prior years. The federal special revenue fund balance of \$3,112,880 at fiscal year-end 2008 will be used to replace the hardware and software associated with the statewide voter registration database as well as for providing accessibility grants to counties and voter outreach.

OFFICE OF THE  
SECRETARY OF STATE

OFFICE RESPONSE



OFFICE OF THE SECRETARY OF STATE  
STATE OF MONTANA

B-3

BRAD JOHNSON  
SECRETARY OF STATE



STATE CAPITOL BUILDING  
PO Box 202801  
HELENA, MT 59620-2801

September 26, 2008

RECEIVED

SEP 30 2008

LEGISLATIVE AUDIT DIV.

Ms. Tori Hunthausen  
Legislative Auditor  
Legislative Audit Division  
P.O. Box 201705  
Helena, Montana 59620-1705

Dear Ms. Hunthausen:

We could like to thank the Legislative Auditor and staff for the assistance provided during the audit, and we appreciate working with the auditor and the professionalism of the fiscal audit staff. The financial compliance audit includes four recommendations. Our response to each recommendation is provided below.

Recommendation #1: Comply with state law by ensuring the fees charged for its business services reflect the cost of providing those services, taking into consideration the ending fund balance.

*We conditionally concur.*

The Secretary of State has been working with ITSD and procurement in developing a comprehensive work plan to provide prompt and efficient services to the citizens of Montana through adoption of an all-inclusive Secretary of State Information Management System (SIMS). As an enterprise fund, management has planned and projected revenue to meet the expenditures of this capital investment. We anticipate the contract will be awarded by the end of October. The SIMS project will be implemented this year and will continue through the next biennium. The implementation will deplete the enterprise fund balance and reflect that the fee structure is commensurate with costs. The fee structure will continue to be monitored to ensure fees are commensurate with costs.

Recommendation #2: Establish procedures to ensure prior year expenditures are accurately recorded on the state's accounting records in accordance with state law.

*Concur.*

The Office has hired a staff accountant with a CPA. The accounting staff ensures prior year expenses are reported in the correct fiscal year.

Tori Hunthausen, Legislative Auditor  
Page 2  
September 26, 2008

Recommendation #3: Implement procedures for monitoring and testing its internal control procedures as required by state policy.

*Concur.*

The Secretary of State's internal controls were created in the spring of 2008 and will be tested. The Secretary of State will monitor and test controls by conducting transaction oriented bi-annual tests to ensure the proper controls are in place. The controls will be tested by a team of staff independent of processing and approving the transactions being tested. The team will test to determine if proper controls are in place, document their findings, and respond appropriately through the internal control officer.

Recommendation #4: Ensure excess vacation leave is forfeited as required by state law.

*Concur.*

Due to employee turnover, an error was made. Existing staff has been trained and procedures are in place to prevent errors from occurring.

Respectfully yours,

  
BRAD JOHNSON  
Secretary of State

BJ:sba