



An Audit Report on

**Financial Processes at the
Office of the Secretary of State**

January 2019

Report No. 19-020



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Overall Conclusion

The Office of the Secretary of State (Office) did not have adequate controls to ensure that revenue was accurately processed and recorded. Specifically, the Office had weaknesses in its revenue processes and reconciliations. These weaknesses significantly affected the reliability of the **Office's revenue data**.

The Office had processes and controls to help ensure that it administered purchases and other election-related expenditures in accordance with applicable statutes, rules, and Office policies and procedures. However, the Office should update its purchasing and expenditure policies and procedures to ensure that they align with current processes and to ensure that the Office administers expenditures consistently.

In addition, the Office should address certain weaknesses related to passwords, user access, and change management to help ensure the integrity of its financial data. To minimize security risks, auditors communicated details about some of those issues directly to the Office in writing.

State Auditor's Office Prior Finding and Recommendation

One of the findings and recommendations presented in this report is similar to a finding and recommendation previously reported to the Office from a prior audit of **the Office's** financial systems (see Appendix 3). Specifically, **the State Auditor's** Office previously reported that the **Office's** Business Entity Secured Transaction (BEST) system lacked some of the controls necessary to ensure the integrity of its financial data, and the Office was unable to reconcile BEST with the Office of the **Comptroller's** Uniform Statewide Accounting System.

Background Information

The Office's mission is to provide a secure and accessible repository for public, business, and commercial records and to receive, compile, and provide public information. In addition, the Office is tasked with ensuring the proper conduct of elections, maintaining the official statewide list of registered voters, authorizing the creation and registration of business entities, and publishing state government rules and notices.

The Office reported collecting \$215 million in revenue between September 1, 2016, and May 31, 2018. Of that total, \$173 million was unappropriated revenue transferred to the General Revenue Fund, and \$42 million was appropriated revenue that the Office retained.

Source: The Office.

Table 1 presents a summary of the findings in this report and the related issue ratings. (See Appendix 2 for more information about the issue rating classifications and descriptions.)

Table 1

Summary of Chapters/Subchapters and Related Issue Ratings		
Chapter/ Subchapter	Title	Issue Rating ^a
1	The Office Did Not Have Adequate Controls to Ensure That Revenue Was Accurately Processed and Recorded	High
2	The Office Should Improve Certain Controls to Help Ensure the Reliability of Its Financial Data; It Also Should Strengthen Its Information Technology Policies and Procedures to Ensure It Complies with Certain Requirements	High
3-A	The Office Had Processes and Related Controls for Administering Purchase Expenditures	Low
3-B	The Office Had Processes and Related Controls to Help Ensure That It Administered Voter Registration Election Expenditures in Accordance with Requirements	Low
3-C	The Office Had Processes and Related Controls to Help Ensure That It Administered Primary Election Expenditures in Accordance with Requirements	Low
<p>^a A subchapter is rated Priority if the issues identified present risks or effects that if not addressed could critically affect the audited entity's ability to effectively administer the program(s)/function(s) audited. Immediate action is required to address the noted concern and reduce risks to the audited entity.</p> <p>A subchapter is rated High if the issues identified present risks or effects that if not addressed could substantially affect the audited entity's ability to effectively administer the program(s)/function(s) audited. Prompt action is essential to address the noted concern and reduce risks to the audited entity.</p> <p>A subchapter is rated Medium if the issues identified present risks or effects that if not addressed could moderately affect the audited entity's ability to effectively administer program(s)/function(s) audited. Action is needed to address the noted concern and reduce risks to a more desirable level.</p> <p>A subchapter is rated Low if the audit identified strengths that support the audited entity's ability to administer the program(s)/function(s) audited or the issues identified do not present significant risks or effects that would negatively affect the audited entity's ability to effectively administer the program(s)/function(s) audited.</p>		

Auditors communicated other, less significant issues separately in writing to Office management.

Summary of Management's Response

At the end of each chapter or subchapter in this report, auditors made recommendations to address the issues identified during this audit. The Office agreed with the recommendations in this report.

Audit Objective and Scope

The objective of this audit was to determine whether the Office has processes and related controls to help ensure that it administers financial transactions in accordance with applicable statutes, rules, and agency policies and procedures.

The scope of this audit covered the Office's activities related to revenues, purchase expenditures, election expenditures, and applicable information systems for fiscal year 2017 (September 1, 2016, through August 31, 2017) and the first three quarters of fiscal year 2018 (September 1, 2017, through May 31, 2018).

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Detailed Results

Chapter 1

The Office Did Not Have Adequate Controls to Ensure That Revenue Was Accurately Processed and Recorded

Chapter 1
Rating:
High ¹

The Office of the Secretary of State (Office) had weaknesses in its automated processes and manual reconciliations that significantly affected the reliability of its revenue data. Auditors determined that the balance of customer accounts in the Office's Business Entity Secured Transaction (BEST) system, as of May 31, 2018, was \$2.4 million less than the balance recorded in the Office of the Comptroller of Public Accounts' (Comptroller) Uniform Statewide Accounting System (USAS). The Office had not reconciled that difference as of October 2018.

The Office should strengthen its automated processes and manual reconciliations to help ensure revenue is accurately processed and recorded in BEST and USAS.

The Office should strengthen its revenue reconciliation processes.

The Office's Financial Management department had a manual process to perform a daily comparison of all payments received to verify that they are deposited at the State Treasury and that revenue recorded in BEST matches USAS. (See text boxes for additional details on the BEST system and the Office's revenue process.) However, the daily comparison did not effectively reconcile all identified discrepancies because the Office's Financial Management department did not always document its research and resolution of those discrepancies, as required by its procedures.

The Business Entity Secured Transaction (BEST) System

The Office began using its BEST system in 2001 primarily as a document management system to track document filings. Over time, the Office implemented limited accounting functionality in the system.

Source: The Office.

Revenue Process

The Office of the Secretary of State (Office) asserted that it earns (recognizes) revenue when (1) a service has been provided and (2) payment has been received.

The Office allows customers to prepay their accounts, resulting in a credit balance in the BEST system. Because an Office service has yet to be provided in those prepay instances, the deposits are recorded as **unearned revenue in the Office's Uniform Statewide Accounting System (USAS) suspense account**. Therefore, the total credit balances from all of the customer accounts in BEST should match the balance **in the Office's USAS suspense account**.

Automated processes in the BEST system determine when revenue has been earned (recognized). The Office relies on those automated processes to ensure that earned revenue is recorded in USAS through the transfer of funds from the suspense account to the appropriate revenue accounts.

Source: The Office.

¹ The risk related to the issues discussed in Chapter 1 is rated as High because the issues identified present risks or effects that if not addressed could substantially affect the audited entity's ability to effectively administer the program(s)/function(s) audited. Prompt action is essential to address the noted concern(s) and reduce risks to the audited entity.

In addition, certain supervisory employees are authorized to adjust customers' account balances in BEST for certain reasons, including the resolution of a fee disputed by a customer. However, the Office's Financial Management department did not include a review of all account adjustments in its daily comparison.

Not documenting the detection and resolution of discrepancies and not reviewing all account adjustments reduces the effectiveness of the Office's revenue reconciliation process.

Further, the Office stated that it did not perform monthly reconciliations from September 1, 2016, to May 31, 2018, because the monthly revenue reports generated by BEST were not reliable, and as of October 2018, it had not determined the cause for the issue. As a result, the Office did not verify that monthly revenue was recorded correctly in BEST and USAS, as required by Office policy and the Comptroller's *USAS User's Manual*. The inability to reconcile BEST to USAS significantly affects the reliability of the revenue data recorded in both systems.

Auditors performed an independent comparison of the total balance in the BEST system to the cash balance in USAS as of May 31, 2018, using that month's report generated by BEST. Auditors determined that the balance of customer accounts in BEST was \$2.4 million less than the balance recorded in USAS.

The Office should ensure that its automated processes accurately process and record revenue.

The Office relies on automated processes in its BEST system to record revenue (see text box on the previous page for additional details on the Office's revenue process). Auditors tested a risk-based sample of 30 revenue transactions and determined that 29 of those 30 transactions were accurately calculated and appropriately recorded in BEST and USAS. However, the full amount for 1 of those 30 transactions had not been recorded as revenue in BEST or USAS two years after it occurred. The Office was unable to determine the cause of the unrecorded revenue. While that transaction discrepancy was not a significant amount, given the volume of transactions the Office processes each year and the weaknesses in its reconciliation process, there is a risk that the Office is not accurately recording revenue in BEST or USAS.

The Office's accounting policies and procedures were not consistent with its practices.

The Office's Financial Management department did not have a formal process to review and revise its accounting policies and procedures. In addition, the Office's Financial Management department had three active

versions of its accounting policies and procedures. As a result, those policies and procedures did not always align with the Office's accounting practices. For example, all three versions of the accounting policies and procedures required Financial Management to perform a monthly reconciliation of the revenue recorded in BEST and USAS. However, the Office asserted that it had not required those monthly reconciliations since October 2016.

Having accounting policies and procedures that do not align with current practices increases the risk of both process errors and weaknesses in controls designed to ensure the integrity of the Office's financial processes.

Recommendations

The Office should:

- Ensure that its revenue accounting system has appropriate controls and functionality to accurately process and record revenue.
- Ensure that its daily reconciliation encompasses all transactions that affect revenue, including account balance corrections, and document the resolution for all identified discrepancies.
- Perform and document monthly reconciliations to ensure that revenue is accurately recorded in BEST and USAS, according to requirements.
- Consolidate its existing accounting policies and procedures into a single set of accounting policies and procedures that aligns with its current financial and accounting practices, and establish a process to review and maintain those policies and procedures.

Management's Response

A. *Ensure that its revenue accounting system has appropriate controls and functionality to accurately process and record revenue.*

Management agrees

The Business Entity Secured Transaction (BEST) system was deployed in 2001. While incremental technology upgrades have been incorporated into this system to ensure that it remains reliable and supported, the basic technical architecture of the system has reached end of life. The agency is investigating the best solution to upgrade or replace this system. It is anticipated that a major information systems project will be initiated in fiscal years 2022 through 2025 to deploy the next generation of the BEST system.

Management anticipates performing a needs analysis for 2020-21 biennium and request funding for 2022-23 biennium with estimated go live date in 2025. The requirements analysis for the new system will include appropriate controls and functionality to accurately process and record revenue. The next generation of BEST will also consider separating the secured transactions filings and the financial reporting functions into separate components.

Replacing and/or upgrading the BEST system is a long term solution. In the meantime, the Office will review the controls and functionality of the accounting system to identify deficiencies and evaluate potential solutions to address those deficiencies. This may include a combination of compensating controls and system modifications.

Responsible employee title: Director Administrative Services, Director of Business & Public Filings, and IT Director

Target date for completion: August 2019

B. Ensure that the daily reconciliation encompasses all transactions that affect revenue, including account balance corrections, and document the resolution for all identified discrepancies.

Management Agrees.

We will revise our daily reconciliation process to ensure that all transactions affecting revenue, including account corrections are included. Additionally, we will document all discrepancies identified and their related resolution. Finally, our revised procedures will include management review and approval of all account corrections or adjustments.

Responsible employee title: Director of Finance

Target date for completion: January 2019

C: Perform and document monthly reconciliations to ensure that revenue is accurately recorded in BEST and USAS, according to requirements.

Management Agrees.

Monthly reconciliations between BEST and USAS will be performed as required. Until such time as the next generation of BEST can be implemented, monthly reconciliations will be based off of the daily reconciliations noted in response B above.

Responsible employee title: Director of Finance

Target date for completion: January 2019

D. Consolidate its existing accounting policies and procedures into a single set of accounting policies and procedures that aligns with its current financial and accounting practices, and establish a process to review and maintain those policies and procedures.

Management Agrees.

We will review, revise, and compile our accounting policies and procedures into one comprehensive document and ensure that our practices are aligned with those policies and procedures.

Responsible employee title: Director of Finance

Target date for completion: August 2019

The Office Should Improve Certain Controls to Help Ensure the Reliability of Its Financial Data; It Also Should Strengthen Its Information Technology Policies and Procedures to Ensure It Complies with Certain Requirements

Chapter 2
Rating:
High ²

The Office should strengthen its information technology (IT) controls to address significant security risks that could affect the reliability of data used for reporting financial information.

Passwords

Auditors identified certain weaknesses related to password settings. To minimize security risks, auditors communicated details about certain issues directly to the Office’s management in writing.

User Access

The Office had not performed formal reviews of user access to its IT systems, including its databases and servers, as required by Title 1, Texas Administrative Code, Section 202.22. (See text box for additional information on Office IT systems.) As a result, access to the Business Entity Secured Transaction (BEST) system, the Expenditure System, and the Online Primary Finance System was not restricted to appropriate personnel. Implementing effective user access controls helps to ensure that access to critical information systems is appropriately restricted to minimize the risk of unauthorized changes to data.

Change Management

The Office had a change management process in place to help ensure that changes to IT systems and the data within them were appropriately tested, approved, and documented. However, the controls in that process were not effective because the Office had not established a proper segregation of duties, as required by the Department of Information Resources’ *Security*

Office IT Systems Tested

Auditors performed limited reviews of the following four IT systems the Office used to manage the data it reported and that were applicable to the audit objective:

- Business Entity Secured Transaction (BEST) system – used agency-wide to record information for all sales (revenue) for which a charge has been made for a product or service.
- Expenditure System – used to process electronic payment vouchers.
- Voter Registration Expense Reporting System – used to facilitate reimbursement to county elections officers for voter registration expenses as defined in Texas Election Code, Chapter 19.
- Online Primary Finance System – used to facilitate pre-payment and reimbursement of costs to county party organizations, county elections officers, and elections system vendors for primary elections expenses, as defined in Texas Election Code, Chapter 173.

Source: The Office.

² The risk related to the issues discussed in Chapter 2 is rated as High because the issues identified present risks or effects that if not addressed could substantially affect the audited entity’s ability to effectively administer the program(s)/function(s) audited.

Control Standards Catalog. Specifically, two programmers had administrative access to the production database associated with the Office’s financial applications, which could allow them to circumvent the Office’s change management process and controls. Implementing a proper segregation of duties would aid in enforcing compliance with the change management process and would help to ensure that changes to information resources do not alter data or promote weaknesses that could affect data.

IT Policies and Procedures

The Office’s information systems security policies and procedures addressed significant IT functions, including password requirements, user access, and change management. However, those policies and procedures did not always align with (1) the revised requirements of Title 1, Texas Administrative Code, Chapter 202, and (2) the Department of Information Resources’ *Security Control Standards Catalog* (see text box for additional details).

For example, the Office’s IT security policies did not establish a process for performing and documenting an annual risk assessment of Office information and information systems. As a result, the Office did not perform or document a risk assessment of its IT systems during the audit scope (September 1, 2016, through May 31, 2018), as required by Title 1, Texas Administrative Code, Section 202.25, and the Department of Information Resources’ *Security Control Standards Catalog*.

Title 1, Texas Administrative Code, Chapter 202
Title 1, Texas Administrative Code, Chapter 202, established a baseline of security standards for Texas state agencies and higher education institutions.
In March 2015, the Department of Information Resources made significant revisions to Title 1, Texas Administrative Code, Chapter 202, to align those rules with the requirements of the Federal Information Security Management Act of 2002 and the National Institute of Standards and Technology’s **Special Publication 800-53**.
Subsequently, the Department of Information Resources issued as mandated a *Security Control Standards Catalog* that defined the security control standards for all state agencies to use to provide information security according to risk levels.
Source: The Department of Information Resources.

Recommendations

The Office should:

- Address the identified password weaknesses.
- Develop, document, and implement formal reviews of user access for its IT systems and conduct those reviews at least annually.
- Assign user access rights appropriately based on users’ job responsibilities.
- Implement a proper segregation of duties to ensure that changes to its IT systems comply with its change management policy.

- Review and update its IT security policies to ensure compliance with the requirements in Title 1, Texas Administrative Code, Chapter 202, and the Department of Information Resources' *Security Control Standards Catalog*.
- Perform and document an annual risk assessment of its information and IT systems as required by Title 1, Texas Administrative Code, Section 202.25, and the Department of Information Resources' *Security Control Standards Catalog*.

Management's Response

A. Address the identified password weaknesses.

Management Agrees

The Office has reviewed the identified weaknesses and made adjustments to correct.

Responsible employee title: *Director of Information Technology*

Target date for completion: *Completed*

B. Develop, document, and implement formal annual reviews of user access for IT Systems.

Management Agrees

The Office has reviewed and revised existing policies and procedures to ensure that system access reviews are completed not only at the network access layer, but also within all applications at least annually.

Responsible employee title: *Director of Information Technology*

Target date for completion: *Complete*

C. Assign appropriate user access rights based on job responsibilities.

Management Agrees.

The Office will review access rights at both the network and application layers to ensure that the principle of least privilege is followed.

Responsible employee title: *Director of Information Technology*

Target date for completion: *March 2019*

D. Implement proper segregation of duties to ensure that changes to its IT systems comply with the change management policy.

Management Agrees

The Office will review job duties to ensure that proper separation of duties exists within current staffing constraints.

Responsible employee title: *Director of Information Technology*

Target date for completion: *March 2019*

E. Review and update IT policies to ensure compliance with the requirements in 1 Texas Administrative Code, Chapter 202, and the DIR Security Controls Catalogue

Management Agrees

The Office will review and update its IT security policies to ensure compliance with the requirements in Title 1, Texas Administrative Code, Chapter 202, and the Department of Information Resources' Security Control Standards Catalog.

Responsible employee title: *Director of Information Technology*

Target date for completion: *March 2019*

F. Perform and document an annual risk assessment of agency information and IT systems as required by 1 Texas Administrative Code, Section 202.25

Management Agrees

The Office conducts numerous risk assessment activities throughout the year including third party penetration testing, Department of Homeland Security (DHS) weekly cyber hygiene scans, other DHS assessments, Purchase Card Industry Data Security Standards annual assessment and monthly vulnerability scans, Data Center Services monthly vulnerability scans, an annual third party risk assessment based on TAC 202 and the Department of Information Resources' Security Control Standards Catalog, as well as numerous internal scans and assessments by internal security staff. The Office will consolidate and summarize the results of these efforts into a single document to satisfy the requirement in TAC, Section 202.25.

Responsible employee title: *Director of Information Technology*

Target date for completion: *March 2019*

The Office Had Processes and Related Controls to Help Ensure That It Administered Expenditures in Accordance with Requirements

The Office had adequate processes and related controls to help ensure that it administered expenditures³ in accordance with state statutes, rules, and Office policies and procedures.

However, the Office should ensure that purchase expenditures are administered consistently. It also should strengthen its review process for voter registration election expenditures and retain adequate documentation of its review of primary election expenditures.

Chapter 3-A
Rating:
Low⁴

Chapter 3-A

The Office Had Processes and Related Controls for Administering Purchase Expenditures

The Office had adequate controls over purchase expenditures. It recorded purchase expenditures totaling \$12.1 million for fiscal year 2017 and \$17.1 million for the first nine months of fiscal year 2018 (September 1, 2017, through May 31, 2018).

Auditors tested 25 purchase expenditures totaling \$2.9 million and determined that all 25 were:

- Allowable and procured through an appropriate procurement method.
- Accurately calculated and promptly paid.
- Processed in the Uniform Statewide Accounting System (USAS) by someone other than the preparer and reviewer of the payment voucher.

³ For the purpose of this report, the term “purchase expenditure” refers to an Office purchase of a good or service. The term “election expenditure” refers to an Office expenditure for the reimbursement of election-related costs incurred by counties, county political party chairpersons, and State voter registrars.

⁴ The risk related to the issues discussed in Chapter 3-A is rated as Low because the audit identified strengths that support the audited entity’s ability to administer the program(s)/function(s) audited or the issues identified do not present significant risks or effects that would negatively affect the audited entity’s ability to effectively administer the program(s)/function(s) audited.

The Office's purchasing and expenditure policies and procedures did not always align with its processes.

Receiving Report

The Office requires a recipient to sign a receiving report to document the Office's receipt of a purchased good or service. The receiving report is compared to the purchase order and the vendor invoice to ensure all three match before payment is processed.

Source: The Office.

For 10 (40 percent) of 25 purchase expenditures tested, the expenditure vouchers contained supporting documentation, but did not include a signed receiving report, as required by Office policy (see text box for more information on receiving reports). The Office's management asserted that receiving reports were not required for certain types of services. However, the Office's purchasing and expenditure policies did not define when alternative documentation supporting the receipt of a good or service may substitute for a receiving report.

The lack of standardized, well-defined purchasing and expenditure policies increases the risk that the Office may administer its purchase expenditures inconsistently, potentially resulting in unauthorized expenditures.

Recommendation

The Office should update its purchasing and expenditure policies and procedures to define and standardize its requirements for documenting the receipt of a purchased good or service.

Management's Response

The Office should update and standardize its purchasing and expenditure policies and procedures to define and standardize its requirements for documenting receipt of a purchased good or service.

Management Agrees

We will review and revise our purchasing and expenditure policies and procedures as necessary to include defining and standardizing documentation required for receiving reports. The revised policies will specifically address the requirements for one time purchases of tangible goods, and services, as well as recurring purchases such as equipment leases, and intangible goods such as software licenses.

Responsible employee title: Finance Manager, and Manager of Operating Support

Target date for completion: August 2019

Chapter 3-B

The Office Had Processes and Related Controls to Help Ensure That It Administered Voter Registration Election Expenditures in Accordance with Requirements

The Office had adequate controls over voter registration election expenditures. Voter registration funds are state-allocated funds issued to voter registrars in Texas to help defray the cost of counties' voter registration expenses. The Office recorded voter registration election expenditures totaling \$2.7 million for fiscal year 2017 and \$1.3 million for the first nine months of fiscal year 2018 (September 1, 2017, through May 31, 2018).

Auditors tested 25 voter registration election expenditures totaling \$1.1 million and determined that all 25 were:

- Approved by required personnel in the Office's Elections Division.
- Supported by adequate documentation.
- Allowable according to administrative rules and Office policy.
- Paid during the defined period of reimbursement.
- Accurately recorded and processed in USAS by someone other than those who prepared and reviewed the payment voucher.

However, auditors identified overpayments totaling \$6,605 of voter registration election expenditures for 2 (8 percent) of 25 counties tested. Office policy was to review all expenditure submissions for accuracy and allowability before reimbursement approval in accordance with Title 1, Texas Administrative Code, Chapter 81. However, for those two counties' invoice submissions, the Office did not ensure in its review that invoice submissions matched claimed amounts.

⁵ The risk related to the issues discussed in Chapter 3-B is rated as Low because the audit identified strengths that support the audited entity's ability to administer the program(s)/function(s) audited or the issues identified do not present significant risks or effects that would negatively affect the audited entity's ability to effectively administer the program(s)/function(s) audited.

Recommendation

The Office should strengthen its review process for voter registration election expenditures to ensure reimbursements to counties are accurate and allowable.

Management's Response

The Office should strengthen its review process for voter registration election expenditures to ensure reimbursements to counties are accurate and allowable.

Management Agrees

Although the review process is already very strong as evidenced by the questioned costs representing less than one percent of the total costs in the audit sample, management agrees the process can be strengthened. SOS has administrative rules governing the use of voter registration election expenditures (Chapter 19 funds) as well as other guidelines, including policies and procedures. SOS has an electronic tool for counties to submit reimbursement requests, which requires the user to select from a list of eligible categories when requesting payment. Furthermore, the county must submit supporting documentation with each request. Staff reviews the request for eligibility and verifies that the amount is supported by documentation. As a result, every expense is verified.

The Election Funds Management Team of the Elections Division will review its guidelines, including policies and procedures, to ensure adequate steps are being taken to verify submissions are reviewed properly and thoroughly.

Responsible employee title: Election Funds Manager

Target date for completion: April 2019

Chapter 3-C
Rating:
Low⁶

Chapter 3-C

The Office Had Processes and Related Controls to Help Ensure That It Administered Primary Election Expenditures in Accordance with Requirements

The Office had processes and related controls to help ensure that it administered primary election expenditures in accordance with requirements (see text box for more information on primary election expenditures). It recorded primary election expenditures totaling \$2.7 million for fiscal year 2017 and \$9.4 million for the first nine months of fiscal year 2018 (September 1, 2017, through May 31, 2018).

Auditors tested 20 primary election Final Cost Reports with expenditures that totaled \$1.47 million and determined that all 20 were:

- Approved by required personnel in the Office's Elections Division.
- Supported by adequate documentation.
- Recorded accurately in the Uniform Statewide Accounting System (USAS).

In addition, the expenditures for 19 (95 percent) of the 20 Final Cost Reports tested were accurately calculated and paid and were allowable expenses, according to the Office's policy and procedures and Title 1, Texas Administrative Code, Chapter 81.

However, for 1 (5 percent) of the 20 Final Cost Reports tested, the Office reimbursed the county for an inaccurate and unallowable expense totaling \$1,973. Specifically, the Office reimbursed the county for a portion of the cost of election equipment used for both general and primary elections, which is unallowable according to Title 1, Texas Administrative Code, Section 81.109.

Primary Election Expenditures

Texas Election Code, Section 173.001, enables the Office to distribute state funds to pay expenses incurred by a political party in connection with a primary election.

The Office initially distributes this funding to the county chairs, county election officers, and voting system vendors, based on estimated primary and primary runoff election costs, which are calculated by using actual costs from the prior primary cycle along with specific recipient-requested adjustments. In other words, the funds are distributed by the Office in advance of the primary elections.

After a primary and primary runoff, the county chairs and county election officers must submit to the Office a Final Cost Report detailing actual costs of the elections. If a county chair's final costs exceed its estimated costs, the Office will distribute additional funds. If a county chair's final costs are less than its estimated costs, the county chair will refund the unexpended balance to the Office.

Source: The Office.

⁶ The risk related to the issues discussed in Chapter 3-C is rated as Low because the audit identified strengths that support the audited entity's ability to administer the program(s)/function(s) audited or the issues identified do not present significant risks or effects that would negatively affect the audited entity's ability to effectively administer the program(s)/function(s) audited.

The Office did not consistently retain records of its detailed review and reconciliation of the supporting documentation.

For 4 (20 percent) of 20 primary election Final Cost Reports tested, the Office did not retain records that it performed a detailed review and reconciliation of the supporting documentation and the summarized amounts in the Final Cost Reports. However, auditors were able to verify the amounts were accurate for those four primary election expenditures by independently reviewing the supporting documentation submitted to the Office.

Recommendation

The Office should document and implement a policy to retain records of its detailed review and reconciliation of the supporting documentation to ensure that primary election expenditures are accurate and allowable.

Management's Response

The Office should document and implement a policy to retain records of its detailed review and reconciliation of the supporting documentation to ensure primary election expenditures are accurate and allowable.

Management Agrees.

As with voter registration election expenditures, the questioned costs represent less than one percent of the total costs in the audit sample. However, management agrees there may be opportunities to make the process more consistent and efficient, namely via its rulemaking authority.

The supporting documentation requirement is outlined in §81.107(b) of Title 1, Texas Administrative Code ("Primary-Fund Records"). One of the largest challenges in the review and reconciliation of documents is the variation and volume of documentation. This is particularly true of personnel. For instance, there are seven election worker personnel cost categories in addition to the county and temporary staff that may be hired for various duties, such as equipment preparation. Although SOS urges submitters to categorize and label documentation so that it can be readily identifiable during the review process, it is met with varying success.

To help alleviate the challenges of collecting and reconciling voluminous and varied documentation, SOS will consider amending its rule regarding primary finance records to allow reports generated by electronic systems, such as payroll and other accounting systems, to qualify as supporting documentation. In addition, SOS may require that payroll expenditures be submitted to SOS in a SOS-prescribed spreadsheet format that would include

data such as worker category/type, hours worked, rate of pay, and total compensation. This would be in lieu of time and compensation sheets. The spreadsheets can be tested for allowability and reasonableness based on worker category, county size, number of workers, average hours worked, and any other relevant data points.

SOS must adopt rules for the 2020 Primary Election no later than October 2019. Implementation of the recommendation will depend largely on the rulemaking process, i.e., public feedback.

Responsible employee title: Election Funds Manager

Target date for completion: October 2019

Appendices

Appendix 1

Objective, Scope, and Methodology

Objective

The objective of this audit was to determine whether the Office of the Secretary of State (Office) has processes and related controls to help ensure that it administers financial transactions in accordance with applicable statutes, rules, and agency policies and procedures.

Scope

The scope of this audit covered the Office's activities related to revenues, purchase expenditures, election expenditures, and applicable information technology systems for fiscal year 2017 (September 1, 2016, through August 31, 2017) and the first three quarters of fiscal year 2018 (September 1, 2017, through May 31, 2018).

Methodology

The audit methodology included collecting information and documentation; performing selected tests and procedures on the information obtained; analyzing and evaluating the results of tests; and conducting interviews with Office management and staff. In addition, the methodology included performing a limited review of the general controls over the information technology systems that the Office used to administer its financial data.

Data Reliability and Completeness

To determine the reliability, validity, and completeness of the revenue and expenditure data in the Uniform Statewide Accounting System (USAS), auditors (1) reviewed user access, (2) performed a high-level review of data fields and their contents for appropriateness, and (3) compared that information to other sources. Auditors determined that the revenue and expenditure data in USAS was sufficiently reliable for the purposes of this audit.

Auditors also assessed the reliability of the detailed revenue data in the Business Enterprise Secure Transaction (BEST) system and determined that the revenue data was not sufficiently reliable for the purposes of this report due to significant weaknesses related to the Office's inability to reconcile BEST to USAS, inappropriate user access, and ineffective change management controls. Having unreliable data is significant because it could lead to the Office reporting inaccurate information, and the Office could

make decisions based on incorrect information. While auditors determined that the data was not sufficiently reliable, that data was the most complete population of the detailed revenue transactions available; therefore, auditors used that data for the purposes of this audit.

Sampling Methodology

Auditors selected a nonstatistical sample of days for testing related to revenue deposits primarily through random selection. The sample days were not necessarily representative of the population; therefore, it would not be appropriate to project those test results to the population.

Auditors selected risk-based items to test revenue transactions, purchase expenditures, primary election expenditures, and voter registration expenditures. The sample items generally were not representative of the population; therefore, it would not be appropriate to project those test results to the population.

Information collected and reviewed included the following:

- Office policies, procedures, and guidelines.
- Office revenue data from BEST and USAS.
- Office purchase expenditure data from USAS.
- Office revenue and expenditure supporting documentation.
- Office voter registration election expenditure data from USAS.
- Payment vouchers, Voter Registration Expense system records, and other supporting documentation for voter registration election expenditures.
- Primary election expenditure data from USAS.
- Payment vouchers, Primary Finance Expense system records, estimate reports, Final Cost Reports, and other supporting documentation for primary election expenditures.
- User access data, password settings, and other supporting documentation related to the general controls over the Office's financial-related information systems.

Procedures and tests conducted included the following:

- Interviewed Office staff to identify the Office's financial and operational processes, including financial internal controls, and the information systems that support those processes.

- Tested a sample of Office revenue deposits, revenue journal vouchers, purchase expenditures, primary election expenditures, and voter registration election expenditures to determine compliance with the Office’s policies and procedures and state laws and regulations.
- Compared the unearned revenue in BEST (the credit balance of customer accounts) to the USAS suspense account balance.
- Reviewed supporting documentation related to general controls and application controls over the Office’s financial process systems.

Criteria used included the following:

- Texas Government Code, Chapter 2251.
- Business Organizations Code, Chapters 4, 9, and 12.
- Title 1, Texas Administrative Code, Chapters 81 and 202.
- Office of the Comptroller of Public Accounts’ *eXpendit* purchasing procedures.
- Office of the Comptroller of Public Accounts’ *Manual of Accounts*.
- Office of the Comptroller of Public Accounts’ *Fiscal Policies and Procedures*.
- Office of the Comptroller of Public Accounts’ *Accounting Policy Statements*.
- Office of the Comptroller of Public Accounts’ *USAS User’s Manual*
- *State of Texas Procurement and Contract Management Guide*, Version 1.1.
- Department of Information Resources’ *Security Control Standards Catalog*, Version 1.3.
- Office policies and procedures.

Project Information

Audit fieldwork was conducted from June 2018 through November 2018. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the 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 a reasonable basis for our findings and conclusions based on our audit objective.

The following members of the State Auditor's staff performed the audit:

- Justin H. Griffin, CISA (Project Manager)
- Rachel Lynne Goldman, CPA (Assistant Project Manager)
- Cody Bogan
- Benjamin Nathaniel Keyfitz, CPA, CFE
- C. Eric Navarro, MSOM
- Nathan Stein
- George D. Eure, CPA (Quality Control Reviewer)
- Cesar Saldivar, CFE, CGAP (Audit Manager)

Issue Rating Classifications and Descriptions

Auditors used professional judgement and rated the audit findings identified in this report. Those issue ratings are summarized in the report chapters/sub-chapters. The issue ratings were determined based on the degree of risk or effect of the findings in relation to the audit objective.

In determining the ratings of audit findings, auditors considered factors such as financial impact; potential failure to meet program/function objectives; noncompliance with state statute(s), rules, regulations, and other requirements or criteria; and the inadequacy of the design and/or operating effectiveness of internal controls. In addition, evidence of potential fraud, waste, or abuse; significant control environment issues; and little to no corrective action for issues previously identified could increase the ratings for audit findings. Auditors also identified and considered other factors when appropriate.

Table 2 provides a description of the issue ratings presented in this report.

Table 2

Summary of Issue Ratings	
Issue Rating	Description of Rating
Low	The audit identified strengths that support the audited entity's ability to administer the program(s)/function(s) audited <u>or</u> the issues identified do not present significant risks or effects that would negatively affect the audited entity's ability to effectively administer the program(s)/function(s) audited.
Medium	Issues identified present risks or effects that if not addressed could <u>moderately affect</u> the audited entity's ability to effectively administer program(s)/function(s) audited. Action is needed to address the noted concern(s) and reduce risks to a more desirable level.
High	Issues identified present risks or effects that if not addressed could <u>substantially affect</u> the audited entity's ability to effectively administer the program(s)/function(s) audited. Prompt action is essential to address the noted concern(s) and reduce risks to the audited entity.
Priority	Issues identified present risks or effects that if not addressed could <u>critically affect</u> the audited entity's ability to effectively administer the program(s)/function(s) audited. Immediate action is required to address the noted concern(s) and reduce risks to the audited entity.

Related State Auditor's Office Work

Related State Auditor's Office Work		
Number	Product Name	Release Date
06-013	An Audit Report on Financial Systems at the Office of the Secretary of State	November 2005
<p>Summary of Related Finding</p> <p>The Office of the Secretary of State's (Office) Business Entity Secured Transaction (BEST) system lacks some of the controls necessary to ensure the integrity of its financial data. BEST is not programmed to close financial records at the end of an accounting period. As a result, the Office is unable to effectively reconcile BEST with the Uniform Statewide Accounting System.</p> <p>Recommendation</p> <p>The Office should program BEST to close out accounting periods monthly.</p>		

Copies of this report have been distributed to the following:

Legislative Audit Committee

The Honorable Dan Patrick, Lieutenant Governor, Joint Chair

The Honorable Dennis Bonnen, Speaker of the House, Joint Chair

The Honorable Jane Nelson, Senate Finance Committee

The Honorable Robert Nichols, Member, Texas Senate

The Honorable John Zerwas, House Appropriations Committee

Office of the Governor

The Honorable Greg Abbott, Governor

Office of the Secretary of State

Mr. David Whitley, Secretary of State



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