



# STATE OF TENNESSEE COMPTROLLER OF THE TREASURY

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## Department of State Performance Audit Report

December 2014

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**Justin P. Wilson**  
**Comptroller of the Treasury**



**Department of Audit**  
**Division of State Audit**  
**Risk-Based Performance Audit Group**

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December 11, 2014

The Honorable Ron Ramsey  
Speaker of the Senate  
and  
The Honorable Beth Harwell  
Speaker of the House of Representatives  
and  
Members of the General Assembly  
State Capitol  
Nashville, Tennessee 37243  
and  
The Honorable Tre Hargett  
Secretary of State  
State Capitol  
Nashville, Tennessee 37243

Ladies and Gentlemen:

We have conducted a performance audit of selected programs and activities of the Department of State for the period December 1, 2012, through June 30, 2014.

Our audit disclosed a certain finding which is detailed in the Objectives, Methodologies, and Conclusions section of this report. Management of the Department of State has responded to the audit finding; we have included the responses following the finding. We will follow up the audit to examine the application of the procedures instituted because of the audit finding.

We have reported another less significant matter involving internal control and noncompliance to the department's management in a separate letter.

Sincerely,

Deborah V. Loveless, CPA

Director  
DVL/KBT/mse  
15/004

State of Tennessee

# Audit Highlights

Comptroller of the Treasury

Division of State Audit

Performance Audit  
**Department of State**  
December 2014

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## AUDIT SCOPE

We have audited the Department of State for the period December 1, 2012, through June 30, 2014. Our audit scope included a review of internal control and compliance with laws, regulations, and provisions of contracts or grant agreements in the areas of revenue, expenditures, records management, and information systems. Management of the Department of State is responsible for establishing and maintaining effective internal control and for complying with applicable laws, regulations, and provisions of contracts and grant agreements.

For our sample design, we used nonstatistical audit sampling, which was the most appropriate and cost-effective method for concluding on our audit objectives. Based on our professional judgment, review of authoritative sampling guidance, and careful consideration of underlying statistical concepts, we believe that nonstatistical sampling provides sufficient appropriate audit evidence to support the conclusions in our report. We present more detailed information about our methodologies in the individual report sections.

We conducted our 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 objectives.

## AUDIT FINDING

### **The Tennessee Department of State did not always maintain proper information systems security controls**

Based on our testwork, the department staff did not always maintain proper information systems security controls. The wording of this finding does not identify specific vulnerabilities that could allow someone to exploit the department's computer systems. Disclosing these vulnerabilities could present a potential security risk by providing readers with information that might be

confidential pursuant to Section 10-7-504(i), *Tennessee Code Annotated*. While the conditions observed have the potential to affect department's operations, we are not aware of any instances in which critical information was not available to staff within the Department of State. The conditions mentioned in this finding were internal control issues and do not impact the reliability or security of the department's systems that are critical to the department's mission, nor do they impact information that is available to the public(page 8).

# Performance Audit Department of State

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# Performance Audit Department of State

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## INTRODUCTION

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### POST-AUDIT AUTHORITY

This is the report on the performance audit of the Department of State. The audit was conducted pursuant to Section 4-3-304, *Tennessee Code Annotated*, which requires the Department of Audit to “perform currently a post-audit of all accounts and other financial records of the state government, and of any department, institution, office, or agency thereof in accordance with generally accepted auditing standards and in accordance with such procedures as may be established by the comptroller.”

Section 8-4-109, *Tennessee Code Annotated*, authorizes the Comptroller of the Treasury to audit any books and records of any governmental entity that handles public funds when the Comptroller considers an audit to be necessary or appropriate.

### BACKGROUND

One of the three constitutional officers provided by Tennessee’s constitution, the Secretary of State is to maintain a register of the official acts and proceedings of the Governor and is to be prepared to present them before the General Assembly. Additional functions of the Secretary of State are outlined in state statutes and regulations.

With the Secretary of State as its chief officer, the Department of State keeps all acts and resolutions adopted by the General Assembly, proclamations of the Governor, executive orders, and oaths of office. Statute also requires the department to keep records of corporate charters, trademarks, notary commissions, and state administrative rules and regulations.

The Department of State is organized into ten major divisions: Fiscal and Administrative Services, Human Resources and Organizational Development, Information Systems, Administrative Procedures, Business Services, Charitable Solicitations and Gaming, Elections, Library and Archives, Publications, and Records Management. For administrative purposes, the Tennessee Economic Council on Women, and the Bureau of Ethics and Campaign Finance are attached to the Department of State for all matters concerning receipts, disbursements, budgets, audits, and other related items.

The Fiscal and Administrative Services Division provides the general administrative services necessary to support the department. These include budgeting, accounting, procurement, and other administrative and financial services.

The Human Resources and Organizational Development Division is responsible for the department's human resources activities including the management of staffing benefits, employee relations, policies, and compliance.

The Information Systems Division is responsible for all information technology services necessary to support the Department of State: information systems and technology planning, project development and implementation, technical support, network and telephone administration, and procurement assistance.

The Administrative Procedures Division provides administrative judges to conduct contested case hearings for state administrative agencies and develops uniform rules of procedure for the conduct of those hearings. In addition, the division is also required to assist state agencies in complying with the Uniform Administrative Procedures Act.

The Business Services Division executes the processing and recordkeeping duties of the Secretary of State relating to the following areas: apostilles (a form of authentication issued to documents for use in countries that participate in the Hague Convention of 1961) and authentications, athlete agent registration, corporations, general partnerships, limited liability companies, limited liability partnerships, limited partnerships, mine foreman certificates, motor vehicle temporary liens, nonresident fiduciary appointments, service of process, state deeds and leases, trademarks, Uniform Commercial Code, and workers' compensation exemption registrations.

The Charitable Solicitations and Gaming Division is responsible for the registration and regulation of charitable organizations; charitable gaming events; professional solicitors; and professional fundraising counsels, who solicit contributions for the benefit of charitable organizations. Along with reviewing annual gaming event applications, determining qualifying applicants for annual gaming events for approval by the General Assembly, and regulating those annual events, the division also regulates catastrophic illness trusts established in Tennessee.

The Elections Division is responsible for coordinating the activities of county election commissions and for the uniformity of election procedures throughout the state. Its coordinator interprets questions of the law for the benefit of all election officials, reviews election law legislation, and prepares the election manual and election handbooks for use by election officials.

The Tennessee State Library and Archives Division collects and preserves books and records of historical, documentary, and reference value and encourages and promotes library development throughout the state.

The Publications Division publishes the *Tennessee Blue Book*, *Public and Private Acts of the General Assembly*, the *Tennessee Administrative Register*, the *Tennessee Open Appointments Vacancy Report*, *Rules and Regulations of the State of Tennessee*, and other documents for which the Secretary of State is responsible. This division is also responsible for the creation and maintenance of the department's website.

The Records Management Division was established by Section 10-7-303, *Tennessee Code Annotated*, to assist state agencies in establishing systematic controls for the efficient use and sound preservation of state records. As the primary records management agency for the State of Tennessee, the division provides professional consultative and analytical records management leadership to agencies.

An organization chart of the Department of State is on the following page.

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## **AUDIT SCOPE**

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We have audited the Department of State for the period December 1, 2012, through June 30, 2014. Our audit scope included a review of internal control and compliance with laws, regulations, and provisions of contracts or grant agreements in the areas of revenue, expenditures, records management, and information systems. Management of the Department of State is responsible for establishing and maintaining effective internal control and for complying with applicable laws, regulations, and provisions of contracts and grant agreements.

For our sample design, we used nonstatistical audit sampling, which was the most appropriate and cost-effective method for concluding on our audit objectives. Based on our professional judgment, review of authoritative sampling guidance, and careful consideration of underlying statistical concepts, we believe that nonstatistical sampling provides sufficient appropriate audit evidence to support the conclusions in our report. We present more detailed information about our methodologies in the individual report sections.

We conducted our 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 objectives.

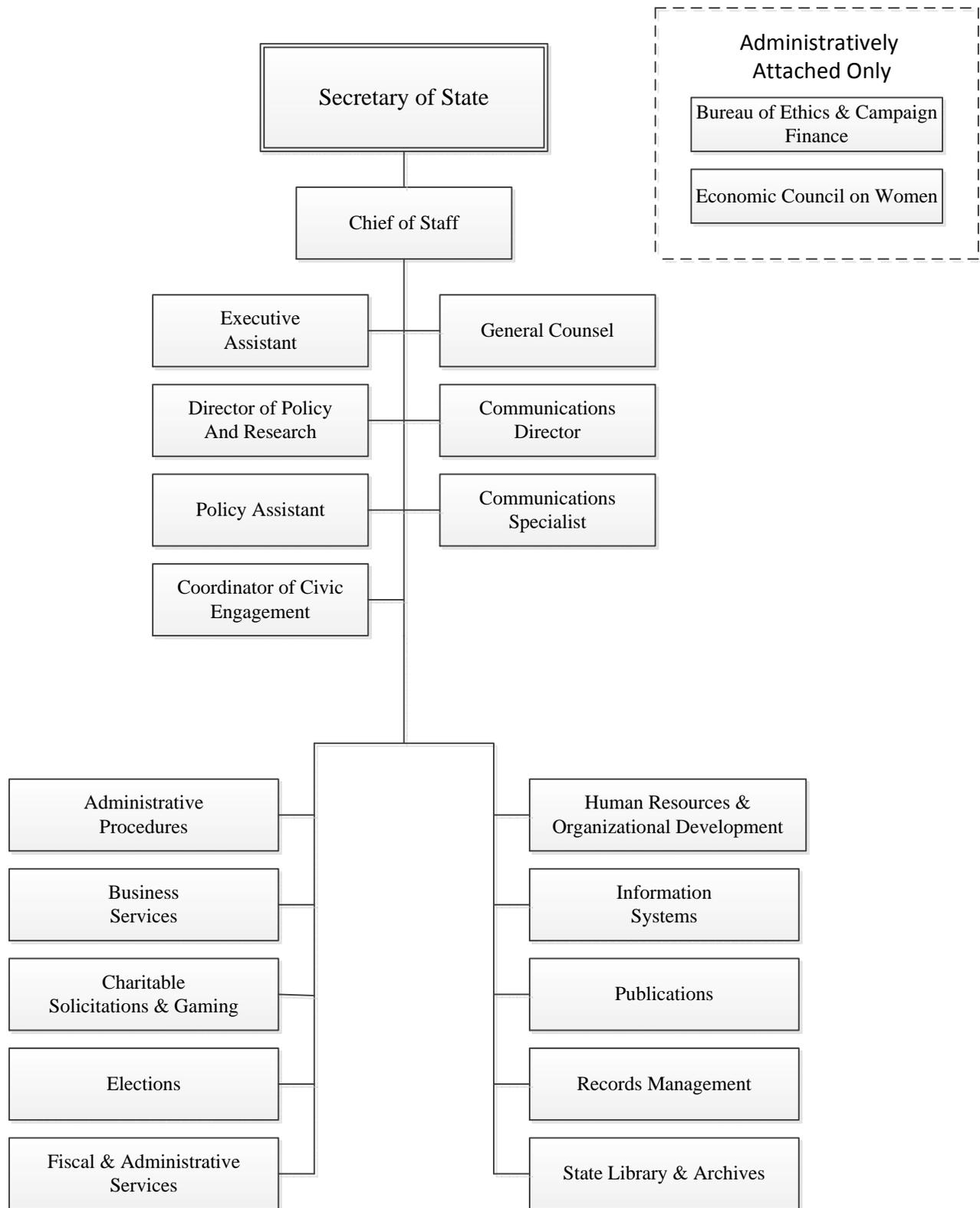
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## **PRIOR AUDIT FINDINGS**

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There were no audit findings in the prior audit report dated February 2013.

Department of State  
 Organizational Chart  
 As of July 24, 2014



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## OBJECTIVES, METHODOLOGIES, AND CONCLUSIONS

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### REVENUE

The Department of State requires businesses and individuals to pay filing fees when they file state mandated documents such as apostilles and authentications, athlete agent registration, and business reports. In addition to processing the filing documents, the Business Services Division collects the fees on site through the department's cashier's window, by mail, or online. The number of online fee transactions the department processes increased from 145,978 in fiscal year 2013 to 210,048 in fiscal year 2014. While the Business Services staff record all documents in the Tennessee Business Entity and Annual Reporting system, the fiscal staff within the Fiscal and Administrative Division reconcile revenue transactions processed online with the third-party online vendors; record all collections in the department's Great Plains Accounting System; and use iNovah, the state's cash receipting system, to record the revenue in Edison (the state's accounting system).

The objectives of our review of revenue were to determine whether

- Business Services management adequately segregated staff responsibilities within the revenue collection process, and the cashier's office staff properly secured cash;
- Business Services staff collected the correct filing fees based on the type of document filed;
- fiscal staff deposited revenue collections in accordance with Department of Finance and Administration (F&A) Policy 25, "Deposit Practices";
- Business Services staff and fiscal staff properly recorded revenue transactions in Great Plains and in Edison; and
- fiscal staff reconciled online transactions with payments from the third-party online vendors on a daily basis.

To gain an understanding of the department's procedures, systems, and controls to secure, record, and deposit revenue collections, we interviewed key department personnel and made observations during walk-through procedures. We obtained a population of 50,799 cash receipts totaling \$4,872,824 for the period December 1, 2012, through June 30, 2014, from the Great Plains Accounting System and tested a nonstatistical random sample of 25 cash receipts totaling \$2,103 to meet the following objectives. To determine whether Business Services staff collected the correct filing fee, we compared the cash receipt amounts to the applicable laws that detailed the fee amount for the document filed. To determine whether fiscal staff deposited cash promptly in accordance with F&A Policy 25, we evaluated the length of time between deposit and cash collection. To determine if Business Services staff and fiscal staff properly recorded revenue transactions, we compared the cash receipts from Great Plains Accounting System, sales posting journals, bank deposit slips, batched revenue sheets, and Edison.

We selected a nonstatistical random sample of 25 business days during the period December 1, 2012, through June 30, 2014, and performed testwork to determine whether fiscal staff performed a daily reconciliation of online fee transactions processed in the Tennessee Business Entity and Annual Reporting system to payments received from third-party online vendors.

Based on our interviews, reviews, and testwork, we determined that

- Business Services management adequately segregated responsibilities within the revenue collection process, and the cashier's office properly secured cash;
- Business Services staff collected the correct filing fees amount based on the type of document filed;
- fiscal staff deposited revenue collections in accordance with F&A Policy 25;
- Business Services staff and fiscal staff properly recorded revenue transactions in Great Plains Accounting System and in Edison; and
- fiscal staff reconciled online transactions with payments from the third-party online vendors on a daily basis.

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## **EXPENDITURES**

The Department of State's operating expenditures include, but are not limited to, payroll, equipment, supplies, printing public documents, and access to electronic references for the state libraries. The Fiscal and Administrative Services Division staff are responsible for ensuring expenditures are properly and timely processed and accurately recorded into Edison (the state's accounting system).

The objectives of our review of expenditures were to determine whether

- fiscal staff ensured expenditure transactions were adequately supported, properly approved, and correctly recorded in the accounting system; and
- fiscal staff made timely payments for goods and services needed for daily operations.

We reviewed applicable laws and regulations, interviewed key personnel, and reviewed supporting documentation to gain an understanding of the division's controls over expenditures. We obtained a listing of 45,311 expenditure transactions totaling \$31,932,676 and tested a nonstatistical random sample of 25 transactions totaling \$12,101 for the period December 1, 2012, through May 31, 2014. To determine if the expenditures were adequately supported, correctly recorded, and properly approved, we reviewed invoices and the approval history in Edison. To determine if payments for goods and services were paid timely, from the listing of expenditures transactions, we selected a nonstatistical random sample of 60 expenditures totaling \$51,804 and evaluated the length of time between the invoice due date and the date fiscal staff paid the invoice.

Based on our review and testwork performed, we determined that

- fiscal staff ensured expenditure transactions were adequately supported, properly approved, and correctly recorded in the accounting system; and
- fiscal staff promptly paid for goods and services, with minor exceptions.

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## **RECORDS MANAGEMENT**

The Records Management Division is responsible for establishing statewide procedural guidelines for oversight and retention of paper and electronic records. To ensure state records are properly retained, the division requires state entities to complete a Records Disposition Authorization (RDA) form, which is reviewed and approved by the division, the State Library and Archives Division, the Office of the Comptroller of the Treasury, and the Public Records Commission.

The department contracts with a vendor to maintain the actual storage of the state's records and to destroy documents at the end of the record retention period. The contractor provides the records management division with a certificate of destruction for documents destroyed.

The objectives of our review of the records management process were to determine if

- records management staff followed the RDA approval process; and
- records management staff paid the vendor based on adequate supporting documentation, evidence of vendor compliance with contract terms, and based on proper approval by management.

To gain an understanding of management's approval processes for RDAs and for payment of vendor contract expenditures, we interviewed key personnel and conducted walk-through procedures. We obtained a population of 435 RDAs entered into the Records Management System as of September 11, 2014, and tested a nonstatistical random sample of 25 approved RDAs to determine if the RDAs were properly approved by all parties.

We obtained a population of 198 vendor contract expenditures totaling \$375,030 for the period December 1, 2012, through May 31, 2014, and tested a nonstatistical random sample of 25 transactions totaling \$25,667. We reviewed the department's supporting documentation for vendor payments (invoices, work orders, and certificates of destruction,) for evidence that the vendor met contract terms and that records management approved the vendor payments prior to payment. Based on testwork performed, we determined that

- records management staff followed the RDA approval process; and
- records management staff paid the vendor based on adequate supporting documentation, vendor compliance, and proper approvals.

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## INFORMATION SYSTEMS

The Department of State relies on various information systems, databases, and applications to capture and maintain information that supports Department of State activities. The Information Systems Division is responsible for maintaining the department's network and computer systems, such as the Tennessee Business Entity and Annual Reporting system and NetTN, which allows employees access to the department's files.

The objectives of our review of information systems were to determine if

- the department had a current disaster recovery plan and if the Information Systems Division tested the plan during the audit period; and
- the department followed information systems' industry best practices regarding disaster recovery plans and information systems security controls.

To determine whether management followed industry best practices, we compared management's internal control activities to the industry's best practices.

Based on the procedures performed, we determined that management followed information systems' industry best practices for disaster recovery, with minor exceptions. We determined that management did not follow information systems' industry best practices for system security controls (see finding).

### **Finding – The Tennessee Department of State did not always maintain proper information systems security controls**

Based on our testwork, the Department of State's staff did not always maintain proper information systems security controls, resulting in an increased risk of data loss. The wording of this finding does not identify specific vulnerabilities that could allow someone to exploit the department's computer systems. Disclosing these vulnerabilities could present a potential security risk by providing readers with information that might be confidential pursuant to Section 10-7-504(i), *Tennessee Code Annotated*. We provided the department's management detailed information regarding specific vulnerabilities we identified as well as our recommendations for improvement.

While the conditions observed have the potential to affect the department's operations, we are not aware of any instances in which critical information was not available to staff within the Department of State. The conditions mentioned in this finding were internal control issues and do not impact the reliability or security of the department's systems that are critical to staff.

### **Recommendation**

The department's management should ensure that these conditions are remedied through procedures that encompass all aspects of effective security controls. In addition to ensuring that risks associated with this finding are adequately identified and assessed in the department's documented risk assessment, management should implement effective controls to ensure compliance with applicable requirements, assign staff to be responsible for ongoing monitoring of the risks and mitigating controls, and take action if deficiencies occur.

### **Management's Comment**

We concur. Policies and procedures that address the situation are under development and will be placed into operation at the earliest possible date.

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## **APPENDIX**

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### **BUSINESS UNIT CODES**

- 305.01 Secretary of State
- 305.02 State Election Commission
- 305.03 Public Documents
- 305.04 State Library and Archives
- 305.05 Regional Libraries
- 305.06 Library Construction
- 305.07 Bureau of Ethics and Campaign Finance
- 305.08 Economic Council on Women
- 305.09 Charitable Solicitations and Gaming
- 305.10 Help America Vote Act
- 305.12 Community Enhancement Grants
- 305.13 Records Management