

OFFICE OF THE AUDITOR GENERAL

247

REPORT ON
OPERATIONS OF THE
OFFICE OF THE SECRETARY OF STATE

OCTOBER 1974

Joint Legislative Audit Committee

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California Legislature

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October 28, 1974

The Honorable Speaker of the Assembly
The Honorable President of the Senate
The Honorable Members of the Senate and the
Assembly of the Legislature of California

Members:

Transmitted herewith is the Auditor General's report pertaining to the operations of the Secretary of State.

Responsibilities of the Office, which has a budget for fiscal year 1974-75 of approximately \$2.9 million, including 179.5 man-years, include various administrative functions concerning corporations and financing statements of lenders and sellers, providing various information to the public, administrative functions relating to election laws and procedures, and preserving historical public records and other items.

While the clients of the Office of the Secretary of State have been generally satisfied in the manner in which services have been performed, the Auditor General has concluded that his recommendations would enable the Office to administer some of its programs in a more efficient and economical manner.

The Office of the Secretary of State has not obtained information statements from approximately 32,000, or 15 percent of all California corporations which, pursuant to law, are required to file such statements annually. As a result, information used by the public is not current for these corporations, and filing fees totaling approximately \$192,000, or \$96,000 annually, have been lost by the state for calendar years 1973 and 1974. Similar corporate information, including names and addresses, is already filed with the Franchise Tax Board which has the capability to identify nonfiling corporations.

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The Auditor General has recommended that the Secretary of State request the Legislature to require all California corporations to submit the necessary information and fees with their annual tax returns filed with the Franchise Tax Board.

The California State Archives, in the Office of the Secretary of State, has not effectively met its statutory responsibilities relating to historical material because of a lack of adequate personnel and facilities. As a result, historical documents are being maintained without adequate protection against deterioration, and there is an increasing backlog of unprocessed historical material which at present would require an estimated 8.5 man-years to eliminate. Moreover, the state's historical effort is uncoordinated and decentralized.

Approximately one million pages of unprocessed state agency documents are in the basement of the California State Archives building. Although the Office of the Secretary of State has the statutory authority to do so, the Office has not instituted the development of a coordinated program for the compilation and evaluation of all pertinent historical information. Previous budget requests to increase staff by the Office have been disapproved. However, the 1975-76 budget request is only for 2.1 additional professional man-years which, if approved, would still leave nearly one-half million pages of archival documents unprocessed by 1980.

The Auditor General has recommended that sufficient professional archivist personnel, including a state historian, and adequate facilities to protect the documents be requested and approved.

Dishonored checks totaling \$31,900, received from 120 corporations as far back as 1971, have yet to be collected by the Office of the Secretary of State. As a result, these corporations have received the benefits of incorporation without charge by the state. These checks were for fees to pay for corporate filings of articles of incorporation and prepayments of corporate franchise tax. Efforts of the Office to collect amounts due on these checks have not been effective.

The Auditor General has recommended that the Office of the Secretary of State request legislative authorization to conditionally accept and file articles of incorporation until amounts paid from corporations have been received in lawful money, and has

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further recommended that the Office immediately attempt to collect the \$31,900 due to the state for filing fees and franchise tax prepayments.

The balance of the report contains various information requested by the Legislature. Some highlights of this information are as follows:

1. Although none of the nine lawsuits instituted by the Secretary of State were based on his specific statutory duties, it is the judgment of the Chief Counsel for the Office of the Auditor General that all but two of the lawsuits were within the Secretary of State's broad statutory authority to prosecute actions under laws he administers. With regard to these two lawsuits, one has been maintained as a private action with privately employed counsel, and the other was terminated.
2. The Office of the Secretary of State began discussions with the Attorney General's Office in July 1974 regarding the prosecution of foreign corporations (corporations incorporated under laws of states other than California) presumed to be doing intrastate business in California, but which had not yet qualified through the Office of the Secretary of State to do such business. On October 2, 1974 the Secretary of State forwarded to the Attorney General, for possible prosecution, a list of 24 non-qualified corporations as well as 138 corporations that had recently qualified.
3. Employee turnover has not been unreasonable and expenditures for temporary help and overtime have been reasonable and necessary.
4. Security at the California State Archives is adequate.

Respectfully submitted,



VINCENT THOMAS, Chairman
Joint Legislative Audit Committee

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FINDING

The Office of the Secretary of State has not obtained information statements from approximately 32,000, or 15 percent of all California corporations which are required to file such statements annually. As a result, information used by the public is not current for these corporations and filing fees totaling approximately \$192,000, or \$96,000 annually, have been lost to the state for 1973 and 1974.

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RECOMMENDATION

We recommend that the Secretary of the State request the Legislature to require all California corporations to include information statements, accompanied by the annual \$3 fee, as part of their annual tax returns filed with the Franchise Tax Board, and that the Board transmit such information to the Secretary of State.

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SAVINGS AND BENEFITS

Implementation of this recommendation will result in an annual filing of required information by approximately 32,000 additional corporations, and will result in additional annual fee income of approximately \$96,000. Further, current information will be available to the public.

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FINDING

The California State Archives, in the Office of the Secretary of State, has not effectively met its statutory responsibilities relating to historical material because of a lack of adequate personnel and facilities. As a result, historical documents are being maintained without adequate protection against deterioration, and there is an increasing backlog of unprocessed historical material which at present would require an estimated 8.5 man-years to eliminate. Moreover, the state's historical effort is uncoordinated and decentralized.

10

RECOMMENDATIONS

We recommend that the Secretary of State request that:

- A state historian be appointed in the State Archives, and be given the responsibility and authority for coordinating and centralizing historical efforts of the state; 15
- Sufficient professional archivist personnel be approved for the State Archives to eliminate the present backlog within a reasonable period and to assume increased responsibilities for obtaining historical material of interest to the state; and 15
- The present unacceptable conditions for housing incoming documentation and the existing documentation on the third floor be changed to provide for air conditioning, humidity control and fire-sensing equipment. 15

BENEFITS

Proper implementation of these recommendations will cost the state an undetermined amount, but will result in the elimination of the existing backlog of unprocessed historical documents; will permit valuable state historical material to be stored safely with minimal fire hazard or document deterioration; and will provide the capability to more effectively manage the total historical efforts of the largest state in the nation. 15

FINDING

Dishonored checks totaling \$31,900, received from 120 corporations as far back as 1971, have yet to be collected by the Office of the Secretary of State. As a result, these corporations have received the benefits of incorporation without charge by the state. 16

RECOMMENDATIONS

- We recommend that the Office of the Secretary of State request legislation authorizing it to conditionally accept and file articles of incorporation until amounts paid for such filing fees and for prepayment of franchise tax have been received in lawful money. 17

- We further recommend that the Office of the Secretary of State immediately attempt to collect the \$31,900 due to the state for filing fees and prepayment of franchise tax.

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BENEFITS

Proper implementation of these recommendations will assure that, in the future, filing fees and prepayments of franchise tax will be collected before articles of incorporation are filed unconditionally. Further, it should result in collection of the \$31,900 now owing to the state from dishonored checks.

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INTRODUCTION

In response to a legislative request, we have reviewed the operations of the Office of the Secretary of State. The Secretary of State is a constitutional officer, elected every four years at a general statewide election. Duties and responsibilities of the Office are varied, and are prescribed by both the Constitution and various statutes. The principal duties of the Secretary of State are:

- To perform administrative functions necessary to provide the public information and to allow corporations to conduct business in the state, such as to record all articles of incorporation and amendments thereto, enforce annual filing of corporate officers' and directors' names and corporate addresses, and accept designation of corporations' agents.
- To accept and record the filing of financing statements of lenders and sellers who hold an interest in personal property (other than consumer goods, automobiles, and crops or timber to be cut) involved in secured transactions, and to provide to interested parties information on and copies of such financing statements. This is a direct service to the commercial community, and enables lenders and sellers to protect their interest in personal property covered by financing statements and to determine prior liens on secured property.

- To provide technical information and legal opinions regarding election laws and procedures; to monitor and report on voter registration and state elections conducted by the registrars of voters and county clerks in the 58 counties; to publish and provide each county clerk with ballot pamphlets prior to the election; and to prescribe forms for, accept and file campaign statements of specified candidates.

- To receive, catalog, store and preserve historically significant public records and documents, and other items deemed by the Secretary to be of historical value.

The Office of the Secretary of State was budgeted 179.5 man-years and \$2,915,521 to perform its duties during fiscal year 1974-75. This compares to a budget of 149.5 man-years and \$1,940,049 for fiscal year 1970-71. In fiscal year 1974-75, revenues of \$5,195,035 are expected to be received for the state general fund by the Office of the Secretary of State. These fees are received principally from filing articles of incorporation and related documents, and filing and providing information on financing statements.

In report number 194.1, titled Review of Operations of the Department of Corporations, October 1974, the Auditor General recommended that the corporate functions of the Department of Corporations, such as regulation of the issuance of securities and licensing of franchises, be consolidated with corporate filing functions of the Secretary of State.

Articles of incorporation, financing statements, amendments, and requests for information are expeditiously processed. The majority of law firms, thrift institutions, and county election officials we surveyed are generally satisfied with services provided by the Office of the Secretary of State.

However, we have concluded that the implementation of the recommendations contained in this report would enable the Office of the Secretary of State to administer some of its programs in a more efficient and economical manner.

FINDINGS

THE OFFICE OF THE SECRETARY OF STATE HAS NOT OBTAINED INFORMATION STATEMENTS FROM APPROXIMATELY 32,000, OR 15 PERCENT OF ALL CALIFORNIA CORPORATIONS WHICH ARE REQUIRED TO FILE SUCH STATEMENTS ANNUALLY. AS A RESULT, INFORMATION USED BY THE PUBLIC IS NOT CURRENT FOR THESE CORPORATIONS AND FILING FEES TOTALING APPROXIMATELY \$192,000, OR \$96,000 ANNUALLY, HAVE BEEN LOST TO THE STATE FOR 1973 AND 1974.

The Office of the Secretary of State has not obtained annual filings of information statements (Statement of Officers) from an estimated 32,000 California corporations, or approximately 15 percent of all such corporations. These corporations are required by the Corporations Code to file the statements with the Secretary of State. As a result of this noncompliance, information for these corporations, which is used by the public through the Office of the Secretary of State, is outdated. Further, as a result, annual filing fees of \$3 each for the approximately 32,000 corporations have been lost to the state for calendar years 1973 and 1974. This amounts to \$192,000 in total, or \$96,000 annually.

Since January 1, 1971, all California corporations have been required to annually file with the Secretary of State information statements, including the names and addresses of its officers, together with a statement of the address of its principal business office. This information is used by attorneys and other persons for business purposes.

There are approximately 32,000 domestic corporations which file corporate tax returns annually with the Franchise Tax Board, but do not file

information statements with the Secretary of State. These tax returns require a listing of the names and addresses of corporate officers as well as the corporation address. Further, while the Board has the capability to identify nonfiling corporations, on the contrary, the Secretary of State had not identified nonfiling corporations.

Since similar corporate information, currently required to be filed with the Secretary of State, is already filed with the Franchise Tax Board, and since the Board has the capability to identify nonfiling corporations, we conclude that the Franchise Tax Board is the proper agency with which corporations should file their information statements. Such statements could then be transmitted by the Board to the Secretary of State.

RECOMMENDATION

We recommend that the Secretary of State request the Legislature to require all California corporations to include information statements, accompanied by the annual \$3 fee, as part of their annual tax returns filed with the Franchise Tax Board, and that the Board transmit such information to the Secretary of State.

SAVINGS AND BENEFITS

Implementation of this recommendation will result in an annual filing of required information by approximately 32,000 additional corporations, and will result in additional annual fee income of approximately \$96,000. Further, current information will be available to the public.

THE CALIFORNIA STATE ARCHIVES, IN THE OFFICE OF THE SECRETARY OF STATE, HAS NOT EFFECTIVELY MET ITS STATUTORY RESPONSIBILITIES RELATING TO HISTORICAL MATERIAL BECAUSE OF A LACK OF ADEQUATE PERSONNEL AND FACILITIES. AS A RESULT, HISTORICAL DOCUMENTS ARE BEING MAINTAINED WITHOUT ADEQUATE PROTECTION AGAINST DETERIORATION, AND THERE IS AN INCREASING BACKLOG OF UNPROCESSED HISTORICAL MATERIAL WHICH AT PRESENT WOULD REQUIRE AN ESTIMATED 8.5 MAN-YEARS TO ELIMINATE. MOREOVER, THE STATE'S HISTORICAL EFFORT IS UNCOORDINATED AND DECENTRALIZED.

Although the law provides that it may do so, the California State Archives had not had a policy to seek or obtain for the archives historical papers, documents, books, maps or other types of records that are outside of state government. Therefore, the state's historical effort is uncoordinated and decentralized. Numerous state agencies, including the State Library under the control of the Department of Education, the Department of Parks and Recreation under the Secretary of Resources, and the State Archives under the Secretary of State, maintain historical documents and other items of historical value.

There presently exist in the basement of the California State Archives building approximately one million pages of unprocessed, unreferenced and unpreserved state agency documents. It is estimated that it will take 8.5 man-years to eliminate this backlog, and it is increasing annually. This unprocessed material is sorted in boxes where the paper is unprotected from the heat, dust and dryness of the archives building basement.

The third floor of the State Archives presently contains the majority of the state's judicial and military records that date back to the mid-1850's. These valuable documents are kept in non-air-conditioned spaces with no humidity control and no fire-sensing equipment. Because of these conditions, the documents degenerate more quickly since the dryness of the room and the extreme temperatures in the summer and winter months make the documents brittle. Archives personnel tell tour groups that there are enough judicial records to build an eight foot wall around the State Capitol, and they express concern over the deterioration of existing material.

Section 12224 of the Government Code provides that the Secretary of State may receive into the archives any item he deems to be of historical value, and shall receive into the archives any other item from a state agency he is directed to by the Director of General Services. After receiving a document, the archives processes, references, preserves and, in selected cases, exhibits it.

Even though the Secretary of State has the statutory authority to do so, he has not initiated the development of a coordinated program for the compilation, analysis or evaluation of all historical information that is available in California. Because of this, centers on California history have developed that are separate, are under no coordinated management control, and only serve researchers if they are aware of their existence. Such centers include the Bancroft Library at the University of California, Berkeley; Yale University in New Haven, Connecticut; the Henry E. Huntington Library and

Art Gallery in San Marino, California; and the California Section of the State Library in Sacramento.

In an attempt to focus more attention on California's historical activity, the California Heritage Preservation Commission was formed by law in 1963 to provide for the restoration, preservation and display of the historical documents of the state, and its purpose is to improve the State Archives and its facilities. The Historical Landmarks Advisory Committee was formed in 1939 to advise the Department of Parks and Recreation regarding state landmarks, buildings and points of historical interest within the state. Because of their role in maintaining the state's historical landmarks, much historical documentation is under the management of the Department of Parks and Recreation.

Many states have a state historian whose primary responsibility is to provide leadership and coordinate all historical aspects of state history. However, California has no such state historian.

The following table compares California's archival and manuscript staff and state population with other selected states and Ontario, Canada.

Archive and Manuscript Staff and Population
Of Selected States and Ontario, Canada As
Compared to California as of 1971

<u>State/ Province</u>	<u>Agency Title</u>	<u>State/ Province Population (Millions)</u>	<u>Professional Positions</u>	<u>Non-Professional Positions</u>	<u>Total Positions</u>
Alabama	Department of Archives and History	3.5	9	6	15
Colorado	Division of Archives and Public Records	2.1	13	9	22
Georgia	Department of Archives and History	4.6	34	27	61
Illinois	State Archives and Records Management Division	11.0	9	10	19
North Carolina	Department of Archives and History	5.2	16	14	30
Ohio	Archives and Manuscript Division	10.7	20	5	25
South Carolina	Department of Archives and History	2.6	14	20	34
Tennessee	State Library and Archives	3.9	9	17	26
Virginia	Archives Division	4.6	11	6	17
Ontario, Canada	Department of Public Records and Archives	.5	16	14	30
Califor- nia	State Archives	19.4	70/71 3 73/74 3	6 8	9 11

As is obvious from the above, California, with the largest population, has the lowest number of personnel assigned to archival functions.

The Office of the Secretary of State attempted to increase its professional archival staff by three persons in the fiscal year 1974-75 budget after a report by the Legislative Analyst recommended increased staffing because of the backlog in unprocessed historical documents. The attempt, however, was not supported by the administration and was refused. On the fiscal year 1975-76 archives budget proposal, the Office of the Secretary of State is requesting an increase of 2.1 professional man-years which will only decrease the backlog by 54 percent over a five-year period. This will leave nearly a half million pages of archival documents still unprocessed by 1980.

The lack of action and support in state government in response to archival attempts to safeguard important segments of California state history shows the low priority and esteem granted the California State Archives.

We conclude that the lack of a coordinated effort in California to combine all the historical activities of the state under one administrative body is not in the state's best interest. Further, a lack of such an effort poses the possibility of loss, disappearance or nondiscovery of valuable historical materials.

RECOMMENDATIONS

We recommend that the Secretary of State request that:

- A state historian be appointed in the State Archives, and be given the responsibility and authority for coordinating and centralizing historical efforts of the state;
- Sufficient professional archivist personnel be approved for the State Archives to eliminate the present backlog within a reasonable period and to assume increased responsibilities for obtaining historical material of interest to the state; and
- The present unacceptable conditions for housing incoming documentation and the existing documentation on the third floor be changed to provide for air conditioning, humidity control and fire-sensing equipment.

BENEFITS

Proper implementation of these recommendations will cost the state an undetermined amount, but will result in the elimination of the existing backlog of unprocessed historical documents; will permit valuable state historical material to be stored safely with minimal fire hazard or document deterioration; and will provide the capability to more effectively manage the total historical efforts of the largest state in the nation.

DISHONORED CHECKS TOTALING \$31,900, RECEIVED FROM 120 CORPORATIONS AS FAR BACK AS 1971, HAVE YET TO BE COLLECTED BY THE OFFICE OF THE SECRETARY OF STATE. AS A RESULT, THESE CORPORATIONS HAVE RECEIVED THE BENEFITS OF INCORPORATION WITHOUT CHARGE BY THE STATE.

Since 1971, the Office of the Secretary of State has received checks totaling \$31,900 which were subsequently dishonored by the banks on which they were drawn. These 120 checks were for fees and prepayment of franchise tax for 120 organizations filing articles of incorporation. Representatives of the Office of the Secretary of State estimated that they have received 161,000 checks from organizations filing articles of incorporation since 1971. The Office of the Secretary of State had already filed the articles of incorporation for the 120 organizations by the time the checks were dishonored, and thus, the corporate status of the organizations could be affected only if the Secretary of State filed a civil suit to suspend the corporation.

The average amount of these dishonored checks is only \$266. Therefore, probable higher cost of action to suspend the corporations would not be justified solely to collect the amounts due.

Efforts by the Office of the Secretary of State to collect amounts due on the dishonored checks have not been effective, and the \$31,900 was still shown on the Secretary of State's records as owing to the state as of October 7, 1974. At that date, 74 of the 120 checks, or 62 percent, had been held by the Secretary of State for six months or more. An estimated 37 percent of the checks are from attorneys filing the articles of incorporation for their clients.

Alternative procedures for collecting these amounts due to the state include referring the makers of the dishonored checks to local district attorneys for possible legal action, referring makers who are attorneys to the State Bar of California for possible disciplinary action, and turning the dishonored checks over to a commercial collection agency which would charge a fee for its services.

RECOMMENDATIONS

- We recommend that the Office of the Secretary of State request legislation authorizing it to conditionally accept and file articles of incorporation until amounts paid for such filing fees and for prepayment of franchise tax have been received in lawful money.
- We further recommend that the Office of the Secretary of State immediately attempt to collect the \$31,900 due to the state for filing fees and prepayment of franchise tax.

BENEFITS

Proper implementation of these recommendations will assure that, in the future, filing fees and prepayments of franchise tax will be collected before articles of incorporation are filed unconditionally. Further, it should result in collection of the \$31,900 now owing to the state from dishonored checks.

INFORMATION REQUESTED BY THE LEGISLATURE

LEGAL ACTIONS INITIATED
BY THE SECRETARY OF STATE

Since 1971, the Secretary of State has initiated nine lawsuits on such subjects as enforcing filing requirements under campaign disclosure laws; alleging massive fraud in securing signatures on initiative petitions, and attempting to halt initial work on the site of the Governor's mansion for environmental and historical reasons.

Although none of the lawsuits were based on specific statutory duties of the Secretary of State, it is the judgment of the Chief Counsel of the Auditor General's Office that all but two of them were within the Secretary of State's broad statutory authority to prosecute actions under laws which he administers.

One of the exceptions was a lawsuit involving disclosure of contributions to organizations opposing Proposition 18 on the November 1970 ballot. The Secretary of State initiated this lawsuit as Secretary of State, but in his individual capacity. The action has been maintained with privately employed counsel. The amount of state costs incurred in this action, if any, cannot be determined.

Office of the Auditor General

The second exception was a lawsuit to enjoin, or prohibit, the initial work on the proposed Governor's mansion in Carmichael, which was brought by the Secretary of State in his official capacity. The Attorney General responded:

"That plaintiff, Edmund G. Brown, Jr., Secretary of State, has not the legal capacity to sue in that it appears on the face of the complaint that this action is brought in his official capacity as Secretary of State, and that neither the California Constitution nor the laws of this state empower the Secretary of State to bring this action."

Although the issue was not decided by a court, the Chief Counsel for the Office of the Auditor General agrees with the conclusion of the Attorney General.

Following is a list of the actions maintained by or on behalf of the Secretary of State, the nature of the action, and the resolution of the action:

<u>NAME OF ACTION</u>	<u>NATURE OF ACTION</u>	<u>RESOLUTION</u>
1. Brown v. Citizens for San Francisco	To compel defendants to comply with campaign disclosure law	Temporary restraining order granted to Brown, requiring defendants to comply
2. Brown v. Computing and Software Inc.	Action for damages for commercial use of voter registration lists	Computing and Software made \$22,593.27 settlement to state
3. Brown v. Sup. Ct. L.A. County	Action to compel Superior Court to hear cases of Brown v. Californians against the Road Tax Trap, etc.	Supreme Court ruled in Brown's behalf
4. Brown v. Reagan	Action to require use of Legislatures' reapportionment plan or use of court plan	Supreme Court adopted its own plan
5. Brown v. Clinton (Action handled by Attorney General)	Action requesting a change in occupation designation on election	Defendant not required to change ballot

<u>NAME OF ACTION</u>	<u>NATURE OF ACTION</u>	<u>RESOLUTION</u>
6. Brown v. General Services	Action to halt initial work on new Governor's mansion	Defendants were allowed to continue
7. Brown v. Durley	Action to avoid placing Proposition 22 on 1972 ballot because of alleged massive fraud in petitions qualifying measure	Judgment for defendants Secretary of State assessed costs incurred by defendants
8. Brown v. Californians against the Road Tax Trap, et al	Action to require full disclosure of contributions and expenses on ballot proposition	Still pending as action financed by private funds with private counsel
9. Brown v. Scott et al	Action to require specified candidates in 1972 election to file campaign disclosure statements	Still pending against those candidates who have not complied; dismissed on motion of Secretary as to those defendants who did file statements

QUALIFICATION OF FOREIGN CORPORATIONS

Foreign corporations, which are corporations incorporated under the laws of other states rather than California, must obtain a certificate of qualification from the Secretary of State prior to transacting intrastate business in California. The purpose of the state's requirement for qualification of foreign corporations to do intrastate business in California is to protect local citizens and local business from any unfair practices, and to insure business responsibility by setting uniform standards for doing business. California citizens may file suit in California against qualified foreign corporations. By qualifying in California, the foreign corporation also acquires certain rights, such as protection of its corporate name, and the right to sue in California.

A one-time fee for a foreign corporation to file for qualification with the Secretary of State is \$350. If a foreign corporation engages in intrastate activities without first qualifying, it is subject to a civil penalty of \$20 per day for each day, up to one year, that it willfully transacts such business, as well as to a fine of \$500 to \$1,000. A nonqualified foreign corporation must also pay a fee of \$250, in addition to any other necessary fees (i.e., \$350) and any franchise or other taxes, before it can maintain any action arising from intrastate activity in a California court.

The \$20 per day penalty and \$500 to \$1,000 fine are recoverable only by prosecution by a district attorney or the State Attorney General, and are imposed at the discretion of the court.

Neither the Corporations Code nor the Government Code specifically imposes upon the Secretary of State a duty to enforce the above penalty provisions. The Secretary of State's actions over the years to qualify foreign corporations have consisted of periodic attempts by letter to have foreign corporations, which have been identified by the Franchise Tax Board, qualify with the Secretary of State.

Two attempts, in 1964 and 1969, were made by the Office of the Secretary of State to collect qualification fees from foreign corporations identified by the Franchise Tax Board. Each program lasted about one year and consisted of writing letters to suspected nonqualified foreign corporations pointing out penalty provisions in an attempt to persuade the corporations to submit qualification papers to the Secretary of State and to pay the filing fee.

The 1964 program was basically a one-man operation, with most of the work being done after business hours and on weekends. After about one year, 274 corporations had filed with the Secretary of State as a direct result of this program, resulting in payment of \$97,818 in filing fees. The program was abandoned in 1965 when the Secretary of State refused to allocate staff time to the program.

The 1969 program is not documented, and the employees primarily involved have left state service. We were unable to document the success or failure of this program. However, personnel in the Office of the Secretary of State told us that it lasted about one year, but was not as successful as the 1964 program. The 1969 program was discontinued because of insufficient staffing.

Office of the Auditor General

From 1970 to 1973, the Franchise Tax Board forwarded suspected nonqualified foreign corporations to the Office of the Secretary of State, but the Office took no action. In November 1973, the Secretary of State requested from the Franchise Tax Board a complete list of suspected nonqualified foreign corporations for follow-up purposes. This action was prompted by a report prepared by the Legislative Analyst which recommended that such action be taken. Since November 1973, the Franchise Tax Board has forwarded suspected nonqualified foreign corporations to the Secretary of State on a regular basis.

As of October 1, 1974, 138 foreign corporations have filed with the Secretary of State, and have paid \$49,226 in filing fees, as a direct result of this program.

The Secretary of State began discussions with the Attorney General's Office in July 1974 regarding the prosecution of foreign corporations presumed to be doing intrastate business in California that have not qualified with the Secretary of State. On October 2, 1974, the Secretary of State forwarded to the Attorney General, for possible prosecution, a list of 24 nonqualified foreign corporations as well as the 138 corporations that had recently qualified.

In April 1973, at the recommendation of the Committee on Conference for the 1973-74 Budget Bill, the Secretary of State and Franchise Tax Board began discussing the possibility of the Franchise Tax Board enforcing the foreign corporation qualification requirement in lieu of the Attorney General.

The feasibility was discussed of transferring the enforcement of the filing requirement to the Franchise Tax Board, by placing the penalty provision in the Revenue and Taxation Code. This provision would avoid the necessity of the Attorney General or district attorneys initiating court action, and would place the burden of proof on the corporation. No legislation has been requested by either agency as of October 15, 1974, however.

The number of nonqualified foreign corporations currently doing intrastate business in California is not determinable at this time. However, the Franchise Tax Board is conducting a study to identify such corporations for purposes of collecting franchise tax. Based on a review of property tax records of 17 counties, the Franchise Tax Board identified 2,812 corporations presumed to be nonqualified foreign corporations doing intrastate business in California. The Franchise Tax Board sent questionnaires to the 2,812 corporations. Responses to 917 questionnaires received as of September 27, 1974 show that only 14 of those 917 corporations are still presumed to be nonqualified foreign corporations doing intrastate business in California. In many cases it is very difficult to prove that a corporation is in fact doing intrastate business. Under existing state law, the Attorney General or a district attorney must prove this in court.

SPECIAL HANDLING FEES

Since February 17, 1972, the Office of the Secretary of State has charged fees when requests are made for special handling of corporation documents, filing of financing statements, furnishing name reservation and information certificates. However, the public is still allowed to submit documents or requests for information for routine processing over the counter or through the mail without paying a special handling fee. The special handling fee is required only on certain services, when the customer requests immediate attention.

The fees for the above services were administratively set, pursuant to Section 12208 of the Government Code, at \$5.00 for filing corporation documents and \$2.00 for other services. These fees were established based on estimates of additional costs to the Secretary of State when special handling is requested.

Officials of the Secretary of State's office told us that they began charging special handling fees to discourage unnecessary over-the-counter services. They also believed that persons requiring preferential treatment resulting in extra costs to the Secretary of State should pay those costs.

PROCEDURES FOR RESPONDING TO REQUESTS FOR
INFORMATION ON SECURITY INTERESTS IN
PERSONAL PROPERTY

The public may request information on security interests in personal property filed with the Secretary of State. Such requests may be made either by mail or in person.

All mail requests are processed in the order received. In-person requests are processed along with the mail requests, in the order received, unless special handling is requested and an additional \$2 special handling fee is paid. Only persons who submit requests in person have the option of requesting special handling. These procedures do not meet the needs of certain businesses which require such information on a timely basis and cannot request the information in person at the Sacramento Office of the Secretary of State.

The average response time for mail requests for information on security interests in personal property for the year ended June 30, 1974 was 9.1 days. Approximately 6.6 of the 9.1 days represents mail time, weekends and holidays, and time awaiting computer access. In-person service when special handling was requested required 15 minutes to one day.

We have surveyed 30 firms which file security interests in personal property and obtain such information from the Office of the Secretary of State. The firms represented attorneys, public accountants, banks, finance companies, savings and loans, miscellaneous manufacturers, and firms providing data retrieval services.

Five firms expressed dissatisfaction with the time required to get responses to information requests. All other firms reported satisfaction with the response time.

We conclude that the business community is generally satisfied with the level of service provided by the Secretary of State pertaining to the filing for financing statements, addendums and certain requests for information. However, a minor segment of the business community is dissatisfied.

ELECTRONIC DATA PROCESSING SYSTEM
FOR CORPORATE OFFICER FILING

Section 3301 of Corporations Code requires all domestic corporations to file a statement of corporate officer names and addresses with the Secretary of State annually.

To comply with the provisions of Section 3301, the Secretary of State created a computer file of active domestic corporations. This computer file is used to print labels to facilitate an annual mailing of statement of corporate officer forms to domestic corporations. The corporations may then complete the forms and return them for filing.

The EDP program which generates the mailing labels was developed by the Secretary of State's Office prior to 1971 for less than \$10,000. The program has had certain problems during the last four years. For example, in 1972, mailing labels were not prepared for corporations that had not filed statements with the Secretary of State in 1971, although they should have been prepared. In 1973, a program error caused an unknown number of corporation names and addresses to be accidentally dropped from the computer file maintained by the Secretary of State.

LOS ANGELES OFFICE SPACE

After taking office in January 1971, the Secretary of State requested space to establish an office in Los Angeles. The Department of General Services advised the Secretary that no space was available that would meet his requirements in either of the two state office buildings in downtown Los Angeles. In June 1971 the Secretary of State began occupying approximately 1,300 square feet of executive office space in the Century City area of Los Angeles. This space was leased by the Department of General Services at a cost of \$755 per month, or 58 cents per square foot.

In July 1971 the Secretary of State requested the Department of General Services to provide additional space of approximately 1,350 square feet to provide corporate filing service in Los Angeles. The Department of General Services again found that there was no space available in state buildings. Accordingly, the lease for the Secretary of State's space was amended on October 15, 1971 to provide an additional 1,350 square feet of space, effective December 1, 1971. The total monthly rental for the 2,650 square feet of space was \$1,468.50, or 55 cents per square foot per month. The lessor provided all necessary alterations and improvements.

The Budget Act of 1972 (Chapter 156; Statutes of 1972, Item 56) provided that "...on and after January 1, 1973, the Los Angeles Office of the Secretary of State shall be in one of the state buildings in Los Angeles only...". On June 26, 1972 the Office of the Secretary of State formally requested the Department of General Services to find it space in a state building in Los Angeles, to be occupied starting January 1, 1973.

The Secretary of State's Los Angeles office was moved to the state building at 107 South Broadway, Los Angeles, on January 13, 1973. These offices presently occupy 3,365 square feet of space. For the period January 15, 1973 through June 30, 1973 the Department of General Services charged the Secretary of State a monthly rent of \$1,346, or 40 cents per square foot. The monthly rental was \$1,446.95, or 43 cents per square foot, from July 1, 1973 through May 1974.

Assuming the Secretary of State's Office occupied the same amount of space in the state building as they occupied in Century City, the annual reduction in rental costs to the Secretary of State would have been \$4,900. However, the Secretary of State incurred moving costs of \$765.87 for the move from Century City to the state building, and paid \$25,969.50 for building alterations and \$4,507.65 for carpets in the offices in the state building.

The Department of General Services was unable to find a tenant to sublease the space in Century City for the remaining term of the lease which expired June 1, 1974. The Department of General Services, rather than the Secretary of State, paid the \$21,676 rent for the Century City space for the period February 1, 1973 through May 1974 while it was vacant.

EMPLOYEE TURNOVER

During fiscal year 1973-74, the Office of the Secretary of State was budgeted approximately 165 personnel man-years. The average monthly turnover from voluntary separations in the Secretary of State's Office was 1.7 per 100 employees during fiscal year 1973-74. The statewide average for such turnovers, as computed by the State Personnel Board for calendar year 1972, was 1.0.

The average monthly turnover in the Secretary of State's Office during fiscal year 1973-74 per 100 employees from total separations, exclusive of transfers to other state agencies, was 3.8. The statewide average for these latter separations compiled by the State Personnel Board for calendar year 1972 was 2.02. Termination of temporary help used in the Secretary of State's Office (particularly from April through June to assist with corporate officer filing) accounted for 2.09 of the higher rate experienced by the Secretary of State's Office.

We conclude that employee turnover in the Office of the Secretary of State is not unreasonable in view of the needed temporary employees at peak workload periods.

TEMPORARY HELP AND OVERTIME
ALLOCATIONS AND USAGE

In fiscal year 1973-74 the Office of the Secretary of State received allocations of \$123,791 for temporary help and overtime. This equals about seven percent of the total amount provided in the Budget Act for personal services. The Office was allocated \$97,551 through the Budget Act of 1973 (Chapter 129; Stats. 1973) and \$26,240 through budget revisions approved by the Department of Finance's Budget Division. The latter amount was for the following purposes:

Move from State Capitol	\$ 402
Administration of the Campaign Disclosure Act and Conflict of Interest Act	18,305
Workload adjustments for:	
Semi-official canvass	2,957
Corporation filings	1,665
Uniform commercial code	<u>2,911</u>
Total allocated by budget revision	<u>\$26,240</u>

During fiscal year 1973-74, \$118,789 of the total \$123,791 was expended for temporary help and overtime.

The percentage of temporary help and overtime expended by the Secretary of State's Office in relation to the total salaries and wages expended by each division is shown below.

Office of the Auditor General

<u>Division</u>	(1) <u>Total Salaries and Wages</u>	(2) <u>Temporary Help and Overtime</u>	(3) <u>% (2) ÷ (1) = (3)</u>
Executive	\$ 205,899	\$ 2,226	1.1
Administrative and staff services	452,745	30,218	6.7
Archives	108,522	1,463	1.4
Corporation filings	485,989	53,086	10.9
Elections	133,564	22,314	16.7
Uniform commercial code	<u>153,302</u>	<u>9,482</u>	6.2
Totals	<u>\$1,540,021</u>	<u>\$118,789</u>	7.7

Our examination of expenditures for temporary help and overtime indicates that such expenditures were reasonable and necessary to meet the deadlines and requirements imposed upon the Secretary of State's Office by statute or workload.

CAMPAIGN REPORTING FORMS

The passage of the Waxman-Dymally Campaign Disclosure Act of 1973 generally revised the law relating to campaign reporting with respect to both candidates and ballot measures. This law requires the Secretary of State to prescribe campaign reporting forms. The information to be contained in the forms, however, is prescribed and limited by the Waxman-Dymally Act.

Based on our review, it appears that due care and appropriate procedures were used by the Office of the Secretary of State in the development of the forms to insure that the forms were understandable. While the forms are somewhat complicated, we conclude that they reflect the complexity of the law which requires the maintenance of detailed records by candidates and committees.

In January 1975, when Proposition 9 of the June 1974 election becomes effective, the responsibility for prescribing the forms will be transferred to the Fair Political Practices Commission.

VOTERS PAMPHLET FOR THE JUNE 1974 ELECTION

The format and content of the voters pamphlet for the June 1974 election was a departure from that of previous years. The change to the larger 8-1/2" x 11" size was specifically required by legislation enacted in 1973. Another change was not specifically required or authorized, however. That was a letter to the voters from the Secretary of State explaining the new style of the pamphlet, the nine propositions to be voted on, and urging a careful study of the pamphlet.

The Legislative Counsel concluded on April 3, 1974 that the inclusion of such a letter in the voters pamphlet would not be authorized by law. The Attorney General concluded the same on August 28, 1974. However, on April 12, 1974, between the time of the two above-mentioned decisions, the case of Fitzrandolph v. Brown was decided in Los Angeles Superior Court. The decision in that case was that the material contained in the voters pamphlet did not constitute a wrongful act by the Secretary of State. The Attorney General took cognizance of the decision and stated that even though, in his opinion, parts of the letter were not authorized, the decision in Fitzrandolph "is a practical indication that the courts would probably uphold the legality of the payment of the entire costs of printing and distributing the voters' pamphlet."

Therefore, while a subjective question remains of whether the cost of including the letter in the voters pamphlet was a prudent expenditure of public funds, such expenditure was lawful.

STATEMENT OF VOTE

According to Section 18756 of the Elections Code the Secretary of State is required to compare and estimate the vote and make out and file in his office a statement thereof not later than the 35th day after the day of election, or as soon as the returns have been received from all the counties of the state, if received within that time. In addition, Section 18756.5 requires the Secretary of State to compile, and make a copy available to the public upon request, a supplement to the Statement of Vote showing the number of votes cast in each county, city and certain types of districts for certain candidates and for each statewide ballot proposition of major interest.

The Statement of Vote for the June 1974 primary election was prepared by the Office of the Secretary of State, beginning on the day of the election, based upon information provided by the various counties. The Statement of Vote was continually updated as additional data were received from the counties. However, changes were made to the Statement of Vote even after the 35-day deadline, because certain counties did not submit certified abstracts of the vote until later than the 35th day after the election. In addition, some certified abstracts from certain counties contained errors which were corrected by later certification by the counties to the Secretary of State. The time when the supplement is to be available to the public is not specified in the statute.

The published supplement to the Statement of Vote for the June 4, 1974 election includes a signed certificate of correctness dated by the Secretary of State on August 5, 1974. This is 62 days after the date of the

election. According to the State Printers office, the printing of the supplement was completed on August 23, 80 days after the election.

The Statement of Vote for the special election of November 1973, which was signed in January 1974, contained errors, including the total votes cast. County summaries, used by the Secretary of State to compile the Statement of Vote, were not in agreement with the abstracts submitted by the counties. Since that time the Secretary of State's Office has made it a practice to compare these two documents, which are submitted and certified to by the counties, before compiling and printing the Statement of Vote.

Because of the number of errors in the January 1974 Statement of Vote, the Secretary of State ordered the statement corrected and reprinted. The corrected Statement of Vote was signed in March of 1974. The cost of reprinting the Statement of Vote was \$1,529 according to the State Printing Plant. The State Printing Plant has not billed the Secretary of State the reprinting as of October 1, 1974, although they plan to do so.

SECURITY AT THE CALIFORNIA STATE ARCHIVES

Precautionary security measures have been taken at the California State Archives to avoid the loss of historical material. Measures that have been instituted are:

1. No public users of the research room are allowed into the areas where historical documentation is stored.
2. Persons who have business that allows them into the stacks are accompanied by archives personnel.
3. All brief cases of persons doing business in or with the archives are deposited and kept away from storage areas and are under surveillance by the archives receptionist.
4. Researchers or users of the archives research room are in view at all times by the archives receptionist.
5. All visitors to the archives must sign in and out of the archives area.
6. In cases where historical documents are used by researchers in the research room of the archives, a form to request use of historical materials is completed identifying the researcher and the materials to be used.

Use of this form was instituted approximately three years ago when a bottle collector unsuccessfully attempted to pilfer old trademarks and labels to increase the value of his collection.

Archives personnel stated that since that time no files have been stolen or lost, even though 2,512 researchers used the archives in fiscal year 1972-73, 2,233 used the archives in 1973-74, and an estimated 2,500 will use the archives in fiscal year 1974-75.

We conclude that security at the California State Archives is adequate.

CAPITAL OUTLAY APPROPRIATIONS

Three minor capital outlay appropriations have been made to the Office of the Secretary of State since 1966. These appropriations are:

Chapter 156, Statutes of 1972 - \$25,000 - (archives display facility)

Chapter 129, Statutes of 1973 - \$25,000 - (elevator, archives building)

Chapter 375, Statutes of 1974 - \$25,000 - (alteration, archives building)

As of June 30, 1974, \$21,000 of the 1972 appropriation had been transferred to the Department of General Services for construction of the project. The archives display facility was opened to the public in September 1974. The remaining \$4,000 of the \$25,000 appropriation was unexpended on June 30, 1974.

The 1973 appropriation has also been transferred by the Secretary of State to the Department of General Services. The Department of General Services has not awarded the contract to begin work on the elevator.

Funds from the 1974 appropriation remained with the Secretary of State as of September 1974 and are unexpended to date.

SUMMARY OF COMMENTS
OF THE SECRETARY OF STATE

1. The problems relating to the nonfiling California corporations were previously discussed with the Franchise Tax Board. The Franchise Tax Board stated that there would be numerous problems if corporations were to file information statements as part of their annual tax returns.

2. The archival functions should not necessarily be under the jurisdiction of the Secretary of State. An evaluation should be made to determine the feasibility of merging the archives, under the Secretary of State, with other existing organizations such as the State Library, the Bancroft Library, or the School of Library Science at the University of California.

3. To conditionally accept and file articles of incorporation, until amounts paid for such filing fees and for franchise tax have been received in lawful money, would create excessive concern and uncertainty within the corporate community.

4. With regard to the lawsuits involving Proposition 18 and the Governor's mansion, no state costs were incurred. Further, the Secretary of State had the capacity to bring these suits.

SUMMARY OF COMMENTS OF THE
ASSISTANT TO THE EXECUTIVE OFFICER
OF THE FRANCHISE TAX BOARD

1. The Franchise Tax Board could receive annual information statements, along with the corporations' annual tax returns, and forward the information to the Office of the Secretary of State. This might require some additional personnel, and there might be some initial problems enforcing the filing of such information.



Harvey M. Rose
Auditor General

Date: October 18, 1974

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