

**DEPARTMENT OF  
PROFESSIONAL AND OCCUPATIONAL REGULATION**

**REPORT ON AUDIT  
FOR THE YEARS ENDED  
JUNE 30, 2006 AND JUNE 30, 2007**

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**Auditor of  
Public Accounts**

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**COMMONWEALTH OF VIRGINIA**

## **AUDIT SUMMARY**

Our audit of the Department of Professional and Occupational Regulation (Department) for the years ended June 30, 2006, and June 30, 2007 found:

- proper recording and reporting of transactions, in all material respects, in the Commonwealth Accounting and Reporting System and the Department's internal licensing system;
- a matter involving internal control and its operations necessary to bring to management's attention; and
- instances of noncompliance with applicable regulations that are required to be reported.

### **UPDATE ON SYSTEMS DEVELOPMENT PROJECT**

The Department is implementing a licensing and enforcement system called EAGLES that will expand public access through online licensing and permitting services and will also eliminate the maintenance costs associated with their current system. The Department began project execution on EAGLES in October 2007, which will continue through January 2010 when project closeout will take place. The Department will implement the project in three phases. The project cost estimate is approximately \$2.9 million and is currently within budget.

Our review over the EAGLES project began in early 2008. At that time, we noted concerns relating to the status of the project for several reasons including a large amount of customizations to the product, insufficient project documentation, and the absence of a committed, full time project manager. We met with the Department's management in February 2008 and communicated our concerns. After that meeting, the Department's management worked to address some of these issues including hiring a full-time project manager to resolve the project documentation issue and to lead the project team for the duration of the project.

As a whole, the project documentation is still insufficient and the project still lacks plans required by the Commonwealth's Project Management Standard. The project's steering committee ultimately decided to reduce the scope of the project and eliminate many of the customizations causing the resource strain and the schedule delays. The Department now plans to implement these customizations after the completion of phase 3.

The first release of phase 1 went live in June 2008. After going live, the Department discovered several issues with this release; the most severe of which involved data migration problems that forced the Department to suspend parallel processing. In addition to the data migration issues, the Department also found that three separate applications associated with the release were not complete. The project team continues to work on the EAGLES project and address identified issues. We remain cautious that the project will remain on schedule and will continue to monitor this project closely throughout its implementation.

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## **AUDIT FINDINGS AND RECOMMENDATIONS**

### **Improve Information Systems Security Policies**

The Department of Professional and Occupational Regulation (Department) does not have adequate documentation of information systems security policies in the areas of access authentication, password controls, and application and database monitoring. In our review of documentation, we identified the following concerns.

- Inadequate detail in the Information Security Technology Policy to address authentication of system access.
- Inadequate detail in the Information Security Technology Policy to address policies and procedures regarding password controls.
- Inadequate detail in the Information Security Technology Policy to address policies and procedures regarding application and database monitoring.

The Department documents compliance with security practices outlined in the VITA Northrop Grumman IT Infrastructure Partnership Security Practices, however, the Department lacks its own policies that consider risk and business impact relevant to its own mission. By improving its documentation of system security policies specific to the Department's mission critical and sensitive systems, the Department will strengthen the controls surrounding the confidentiality, integrity, and availability of the Commonwealth's information.

The Commonwealth's information security standards require that agencies develop security policies for sensitive and mission critical applications. We recommend the Department develop and document policies specific to the business functions and systems deemed mission critical or sensitive.

### **Properly Complete Employee Eligibility Verification Forms**

The Department did not properly complete Employment Eligibility Verification forms (I-9) in accordance with guidance issued by the U.S. Citizenship and Immigration Services of the U.S. Department of Homeland Security in its Handbook for Employers. The guidance requires the employee to complete, sign, and date Section 1 of the I-9 form on the first day of employment. Furthermore, the employer or designated representative must complete, sign, and date Section 2 of the I-9 form within three days of employment to show that they verified the employee's identity and employment eligibility at the point of hiring.

During our review of sixteen employees, we found the Department did not properly complete forms for three of the employees. These exceptions occurred because the Department's employees did not receive adequate training on the guidelines for completing the I-9 forms. As a result, the employees misinterpreted the requirements regarding the timeframe for completing Section 1 and the use of photocopies as verification documentation. Subsequent to the audit period, the Department's employees have attended training and modified their process for completing the forms.

The federal government has increased its enforcement efforts requiring employers to ensure that all new employees are legally entitled to work in the United States. Failure to comply with these guidelines can result in significant penalties to both the employee and employer. Therefore, we recommend the Department obtain periodic training for its employees to ensure they are aware of the most recent guidelines for completing I-9 forms. In addition, the Department should periodically review and update its policies and procedures as necessary to implement changes in the guidelines.

## UPDATE ON SYSTEMS DEVELOPMENT PROJECT

The Department is implementing a licensing and enforcement system called EAGLES that will expand public access through online licensing and permitting services and will also eliminate the maintenance costs associated with their current system. The Department's current licensing and enforcement system operates using a computer code language no longer supported by the vendor. EAGLES use a commercially available computer product provided by the Canadian-based vendor, VERSA. VERSA has implemented licensing software in several other states and the Department's staff are working collaboratively with VERSA personnel to implement the system.

The Department began project execution on EAGLES in October 2007, which will continue through January 2010 when project closeout will take place. The project cost estimate is approximately \$2.9 million and is currently within budget. The Department will implement the project in three phases. Phase 1 has two releases; the first release went live in June 2008, and we discuss it in more detail below. The second release of phase 1 will go-live in September 2008. Phase 2 and phase 3 are set to go-live in April 2009 and December 2009, respectively.

Our review over the EAGLES project began in early 2008. At that time, we noted concerns relating to the status of the project for several reasons.

- ◆ The original project schedule contained a large amount of customizations that were causing a resource strain on VERSA and delaying tasks in the project schedule.
- ◆ There was insufficient project documentation, which is a critical component to successfully managing the project.
- ◆ The project did not have a committed, full-time project manager.

We met with the Department's management in February 2008 and communicated our concerns. After that meeting, the Department's management worked to address some of these issues. The Department hired a full-time project manager to resolve the project documentation issue and to lead the project team for the duration of the project.

As a whole, the project documentation is still insufficient and the project still lacks plans required by the Commonwealth's Project Management Standard. The project's steering committee ultimately decided to reduce the scope of the project and eliminate many of the customizations causing the resource strain and the schedule delays. The Department now plans to implement these customizations after the completion of phase 3. Although this approach will ultimately increase the implementation time, it will help to ensure a successful project.

As discussed earlier, the first release of phase 1 went live in June 2008. After going live, the Department discovered several issues with this release; the most severe of which involved data migration problems that forced the Department to suspend parallel processing. Parallel processing is important because it ensures the new system is producing the same results as the old system.

In addition to the data migration issues, the Department also found that three separate applications associated with the release were not complete. Currently, two of these applications are now complete and the project team is working on the third. The Department is planning for two additional data migrations in July and August 2008 and plans to resume parallel testing after each migration to ensure it is successful. These migrations will be pivotal to the success of the second release of phase 1 scheduled for September 2008. The project team continues to work on the EAGLES project and address identified issues. We remain cautious that the project will remain on schedule and will continue to monitor this project closely throughout its implementation.

**AGENCY HIGHLIGHTS**

The Department of Professional and Occupational Regulation (Department) protects the citizens of the Commonwealth by regulating commercial occupations and certain professions as designated by the General Assembly. The Department’s responsibilities include certification, licensing, investigation, monitoring compliance, fee collection, record maintenance, and enforcement. The Department provides centralized administrative, examination, and enforcement functions to the following 18 boards:

APELSCIDLA*	Geology
Asbestos, Lead, and Home Inspectors	Hearing Aid Specialists
Auctioneers	Opticians
Barbers and Cosmetology	Polygraph Examiners
Boxing and Wrestling Programs	Real Estate
Branch Pilots	Real Estate Appraisers
Cemeteries	Soil Scientists and Wetland Delineators
Contractors	Waste Management Facility Operators
Fair Housing	Waterworks and Wastewater Works Operators

\*Architects, professional engineers, land surveyors, certified interior designers, and certified landscape architects

Changes to the board structure during the audit period include the addition of Body-Piercing professions to the Barbers and Cosmetology Board as of April 4, 2007.

**FINANCIAL INFORMATION**

The Commonwealth Accounting and Reporting System includes all financial data except for the activity of two recovery funds. The Department records licensing fees and the expenses associated with regulation in its special revenue funds. The Department records the collection of monetary penalties in the state Literary Fund.

The following schedules summarize the Department’s budgeted expenses compared with its actual results for fiscal years 2006 and 2007.

Analysis of Budgeted and Actual Expenses by Funding Source

Fiscal Year Ended June 30, 2006

<u>Program Expenses</u>			<u>Expenses by Funding Source</u>	
<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual Expenses</u>	<u>Special Revenue</u>	<u>Federal</u>
<u>\$13,286,379</u>	<u>\$13,982,981</u>	<u>\$12,876,972</u>	<u>\$12,596,128</u>	<u>\$280,844</u>

Fiscal Year Ended June 30, 2007

<u>Program Expenses</u>			<u>Expenses by Funding Source</u>	
<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual Expenses</u>	<u>Special Revenue</u>	<u>Federal</u>
<u>\$15,909,646</u>	<u>\$15,943,146</u>	<u>\$13,492,401</u>	<u>\$13,188,922</u>	<u>\$303,479</u>

During fiscal years 2006 and 2007, the Department also collected and deposited penalties from sanctions into the Commonwealth’s Literary Fund of \$310,864 and \$357,046, respectively.

The Department allocates administrative expenses, legal costs, and information system costs to the various boards using a cost allocation system. The Department's actual expenses were less than budget in both fiscal year 2006 and 2007. Personnel vacancies in both years and anticipated relocation costs, which were budgeted for 2007, but occurred in fiscal year 2008, resulted in fewer expenses. The Department's payroll expenses of \$8,927,470 in fiscal year 2006 and \$9,455,204 in fiscal year 2007, accounted for 69 percent and 70 percent, respectively, of total expenses.

Board Activity

The Department uses a dedicated special revenue fund to account for daily operations. The largest source of revenue comes from licensing fees for applications and renewals. The following schedule summarizes the activity of the Department's operating fund for fiscal years 2006 and 2007.

Summary of Operating Activity

	<u>2006</u>	<u>2007</u>
Revenues	\$16,759,637	\$17,174,507
Expenses	<u>12,354,561</u>	<u>12,898,306</u>
Revenues less expenses	4,405,076	4,276,201
Other expenses	<u>(144,344)</u>	<u>(92,342)</u>
Change in cash balance	4,260,732	4,183,859
Prior year cash balance	<u>8,432,670</u>	<u>12,693,402</u>
Current year cash balance	<u>\$12,693,402</u>	<u>\$16,877,261</u>

Source: Commonwealth Accounting Reporting System 0402 Option B1 Report Fund 0900

The schedule below summarizes the Department's the activity and cash balance of the Department's operating fund by Board.

Summary of Operating Activity by Board  
Fiscal Years 2006 and 2007

	<u>APELSCIDLA</u>	<u>Asbestos Lead and Home</u>	<u>Auctioneers</u>	<u>Branch Pilots</u>	<u>Cemeteries</u>	<u>Contractors</u>	<u>Cosmetology and Barbers</u>
2005 cash balance	\$ 934,347	\$544,522	\$395,975	\$(8,675)	\$257,215	\$1,034,645	\$ 955,380
Revenue	1,536,314	217,926	36,995	18,563	33,050	6,684,084	1,984,264
Expenses (direct and allocated)	<u>1,060,825</u>	<u>205,803</u>	<u>52,582</u>	<u>2,964</u>	<u>39,287</u>	<u>5,449,398</u>	<u>1,871,721</u>
2006 cash balance	<u>1,409,836</u>	<u>556,646</u>	<u>380,388</u>	<u>6,924</u>	<u>250,979</u>	<u>2,269,331</u>	<u>1,067,922</u>
Revenue	1,511,125	198,476	89,160	17,800	28,980	7,124,565	2,368,513
Expenses (direct and allocated)	<u>1,112,867</u>	<u>179,379</u>	<u>54,939</u>	<u>3,134</u>	<u>44,066</u>	<u>5,821,353</u>	<u>1,949,030</u>
2007 cash balance	<u>\$1,808,096</u>	<u>\$575,742</u>	<u>\$414,609</u>	<u>\$21,590</u>	<u>\$235,893</u>	<u>\$3,572,543</u>	<u>\$1,487,405</u>

Summary of Operating Activity by Board, continued  
Fiscal Years 2006 and 2007

	<u>Fair Housing</u>	<u>Geology</u>	<u>Hearing Aid Specialists</u>	<u>Opticians</u>	<u>Polygraph Examiners</u>	<u>Real Estate Appraisers</u>	<u>Real Estate</u>
2005 cash balance	\$ -	\$ 90,299	\$163,195	\$73,045	\$22,014	\$211,700	\$3,576,545
Revenue	11,520	67,655	11,625	43,540	5,645	315,457	5,483,261
Expenses (direct and allocated)	<u>11,520</u>	<u>25,146</u>	<u>30,992</u>	<u>86,186</u>	<u>28,948</u>	<u>225,763</u>	<u>3,176,616</u>
2006 cash balance	-	<u>132,808</u>	<u>143,827</u>	<u>30,398</u>	<u>(1,289)</u>	<u>301,393</u>	<u>5,883,190</u>
Revenue	38,970	2,895	22,812	177,724	6,800	254,396	5,056,074
Expenses (direct and allocated)	<u>38,970</u>	<u>22,936</u>	<u>35,671</u>	<u>92,254</u>	<u>15,379</u>	<u>163,785</u>	<u>3,280,284</u>
2007 cash balance	\$ -	<u>\$112,767</u>	<u>\$130,968</u>	<u>\$115,868</u>	<u>\$ (9,868)</u>	<u>\$392,006</u>	<u>\$7,658,980</u>

	<u>Soil Scientists Wetland Delineators</u>	<u>Waste Mgmt Facility Operators</u>	<u>Waterworks Wastewater Operators</u>	<u>Total By Board</u>	<u>Miscellaneous</u>	<u>Donations</u>	<u>Total</u>
2005 cash balance	\$ 25,536	\$ 88,111	\$ 62,123	\$ 8,425,977	\$ 6,693	\$ -	\$ 8,432,670
Revenue	23,215	20,000	266,291	16,759,406	231	-	16,759,637
Expenses (direct and allocated)	<u>9,741</u>	<u>6,817</u>	<u>218,262</u>	<u>12,502,571</u>	<u>(3,666)</u>	<u>-</u>	<u>12,498,905</u>
2006 cash balance	<u>39,010</u>	<u>101,295</u>	<u>110,151</u>	<u>12,682,808</u>	<u>10,590</u>	<u>-</u>	<u>12,693,402</u>
Revenue	39,890	23,000	200,009	17,161,188	3,319	10,000	17,174,507
Expenses (direct and allocated)	<u>34,129</u>	<u>20,781</u>	<u>159,885</u>	<u>13,028,843</u>	<u>(38,195)</u>	<u>-</u>	<u>12,990,648</u>
2007 cash balance	<u>\$ 44,771</u>	<u>\$103,514</u>	<u>\$150,275</u>	<u>\$16,815,158</u>	<u>\$52,104</u>	<u>\$10,000</u>	<u>\$16,877,261</u>

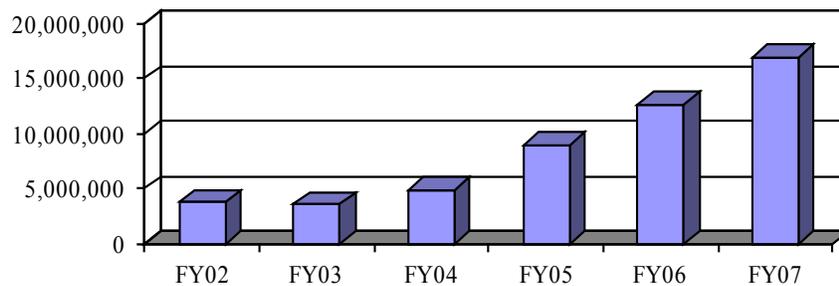
*Source: Commonwealth Accounting Reporting System 0402 Option B1 Report Fund 0900 and the Department's Board Financial Statements*

Each board is self-supporting through regulant-assessed fees. The Code of Virginia requires the Department to adjust fees at the end of each biennium if expenses vary more than ten percent from revenues. In the past, several boards had substantially reduced their excess cash balances and projections indicated that revenues collected from the reduced fees would not be adequate to cover future operating expenses. Therefore, in order to ensure collection of sufficient revenues, six boards adopted fee increases during the 2002-2004 biennium. By the 2004-2006 biennium, one board projected revenue collections greater than the operating expenses. These projections indicated that cash balances would continue to increase. As a result, a fee decrease became effective for the Branch Pilot Board during the 2004-2006 biennium.

Many boards have experienced an unusually high increase in the volume of new applications and growth in the number of regulants. Also, some boards have increased their number of licensing programs to include additional professions. As a result of higher than anticipated regulants, revenue collections have increased cash balances substantially for some of the Boards. The Department will continue to evaluate the activity to ensure fees are appropriate. The Department expects expenses will increase as the Department responds to the increased regulatory and enforcement associated with this growth.

The following summarizes the changes in cash reserves for fiscal years 2002-2007:

Cash Reserve Balances  
Fiscal Years 2002-2007



### Recovery Funds

The Department controls two recovery funds held in the Local Government Investment Pool (LGIP), a short-term investment pool managed by the State Treasurer. The following schedule shows the total cash and investment balances (including principal and accrued interest) for the two recovery funds for fiscal years 2006 and 2007.

Cash and Investment Balances  
Fiscal Years 2006-2007

	<u>Fiscal Year</u>	<u>Amount</u>
Virginia Real Estate Transaction Recovery Fund	2006	\$3,099,688
	2007	3,139,036
Virginia Contractor Transaction Recovery Fund	2006	\$3,464,848
	2007	2,715,424

The Department's recovery funds pay individuals who have claims against licensees who are bankrupt, cannot be located, or otherwise cannot pay a claim when found guilty in court of improper and dishonest conduct. In fiscal year 2006, the statutory limit on claim payments from the Virginia Contractor Transaction Recovery Fund increased from \$10,000 to \$20,000. This increase along with the Department's efforts to efficiently reduce the accumulation of recovery claims caused an increase in the number of payments made during fiscal years 2006 and 2007. The following schedule shows claims payments from the recovery fund for fiscal years 2002-2005.

Recovery Fund Payments  
Fiscal Years 2002-2005

<u>Fiscal Year</u>	<u>Virginia Real Estate Transaction Recovery Fund</u>		<u>Virginia Contractor Transaction Recovery Fund</u>	
	<u>Number of Payments</u>	<u>Amount</u>	<u>Number of Payments</u>	<u>Amount</u>
2002	1	\$ 7,530	86	\$ 621,642
2003	2	10,388	128	818,231
2004	2	23,200	49	310,065
2005	2	34,150	85	604,996
2006	2	60,000	126	1,101,377
2007	1	20,000	193	1,955,520

Fair Housing Assistance Program

The Department's federal fund consists primarily of revenue and expenses from its participation in the Fair Housing Assistance Program administered by the U.S. Department of Housing and Urban Development (HUD). Pursuant to a cooperative agreement between HUD and the Department, HUD provides financial support to assist with the Department's processing of complaints alleging unlawful discrimination in housing. Additionally, HUD provides funds for training of agency staff involved with the processing of these complaints. The Department processed 229 and 179 complaints related to fair housing in fiscal years 2006 and 2007.



# Commonwealth of Virginia

**Walter J. Kucharski, Auditor**

**Auditor of Public Accounts  
P.O. Box 1295  
Richmond, Virginia 23218**

July 17, 2008

The Honorable Timothy M. Kaine  
Richmond, Virginia

The Honorable M. Kirkland Cox  
General Assembly Building  
Richmond, Virginia

We have audited the financial records and operations of the **Department of Professional and Occupational Regulation** for the years ended June 30, 2006, and June 30, 2007. 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 objectives.

## Audit Objectives

Our audit's primary objectives were to evaluate the accuracy of recorded financial transactions on the Commonwealth Accounting and Reporting System and in the Department's internal licensing system, review the adequacy of the Department's internal controls, and test for compliance with applicable laws and regulations.

## Audit Scope and Methodology

The Department's management has responsibility for establishing and maintaining internal control and complying with applicable laws and regulations. Internal control is a process designed to provide reasonable, but not absolute, assurance regarding the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.

We gained an understanding of the overall internal controls surrounding these cycles, both automated and manual, sufficient to plan the audit. We considered control risk in determining the nature and extent of our audit procedures. Our review encompassed controls over the following significant cycles, classes of transactions, and account balances:

Revenues  
Payroll Expenses  
Contractual Service Expenses

Recovery Fund Accounts  
Small Purchase Charge Card

We performed audit tests to determine whether the Department's controls were adequate, had been placed in operation, and were being followed. Our audit also included tests of compliance with provisions of applicable laws and regulations. Our audit procedures included inquiries of appropriate personnel, inspection of documents and records, and observation of the Department's operations. We reviewed the Department's Board minutes and applicable sections of the Code of Virginia and the 2006 and 2007 Virginia Acts of Assembly. We tested transactions and performed analytical procedures, including budgetary and trend analysis.

### Conclusions

We found that the Department properly stated, in all material respects, the amounts recorded and reported in the Commonwealth Accounting and Reporting System and in its internal licensing system. The Department records its financial transactions on the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The financial information presented in this report came directly from the Commonwealth Accounting and Reporting System.

We noted certain matters involving internal control and its operation and compliance with applicable laws and regulations that require management's attention and corrective action. These matters are described in the section entitled "Audit Findings and Recommendations."

### Exit Conference And Report Distribution

We discussed this report with management on July 24, 2008. Management's response has been included at the end of this report.

This report is intended for the information and use of the Governor and General Assembly, management, and citizens of the Commonwealth of Virginia and is a public record.

AUDITOR OF PUBLIC ACCOUNTS

SAH/clj



COMMONWEALTH of VIRGINIA  
DEPARTMENT OF PROFESSIONAL AND OCCUPATIONAL REGULATION

JAY W DeBOER  
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NICK A CHRISTNER  
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Administration & Finance

July 29, 2008

Mr. Walter J. Kucharski  
Auditor of Public Accounts  
Post Office Box 1295  
Richmond, VA 23218

Dear Mr. Kucharski:

Thank you for the opportunity to respond to the audit findings and recommendations included in your audit report. The Department constantly looks for ways to improve and upgrade its operations and your recommendations will be promptly implemented.

Improve Information Systems Security Policies

The Department is fully compliant with VITA's Information Technology Security Policies and therefore believes this issue is a documentation problem only. In developing our policies and procedures, our agency practice has always been to reference authoritative guidance rather than repeat it within our internal documents. However, we will modify our policies and procedures to include the detail requested by the Auditor of Public Accounts.

Properly Complete Employee Eligibility Verification Forms

The Department recognizes the importance of the I-9 Form in verifying employment eligibility and implemented new procedures prior to the start of the audit to address these types of discrepancies. Prior to December 2007, Human Resources staff mistakenly believed that employees had three days to complete Sections 1 and 2 of the form. This resulted in Section 1 of the form being completed two days late for two employees included in the auditor's sample. In December 2007, Human Resources staff received new training on I-9 preparation and modified their procedures to ensure that Section I of the form is completed on or before the employee's first day of work.

Again, we appreciate the opportunity to provide our comments.

Very truly yours,

Jay W. DeBoer

JWD/jas

AGENCY OFFICIALS

as of June 30, 2007

Jay W. DeBoer  
Director

David B. Ashe  
Chief Deputy Director

Steven L. Arthur  
Deputy Director for Administration and Finance

