

Report No. 2019-104
January 2019

STATE OF FLORIDA AUDITOR GENERAL

Operational Audit

OFFICE OF FINANCIAL REGULATION

Division of Securities and Prior Audit Follow-Up



Sherrill F. Norman, CPA
Auditor General

Commissioner of the Office of Financial Regulation

The Office of Financial Regulation is established by Section 20.121(3)(a)2., Florida Statutes. The Office is administratively supported by the Department of Financial Services but operates under the direction of the Financial Services Commission which is composed of the Governor, Attorney General, Chief Financial Officer, and Commissioner of Agriculture. The head of the Office is the Director of the Office of Financial Regulation, who may also be known as the Commissioner of Financial Regulation. During the period of our audit, the following individuals served as the Commissioner of Financial Regulation:

Pamela P. Epting, Interim	From July 1, 2018
Drew Breakspear	Through June 30, 2018

The team leader was Angela Mitchell, CPA, and the audit was supervised by Allen G. Weiner, CPA.

Please address inquiries regarding this report to Karen Van Amburg, CPA, Audit Manager, by e-mail at karevanamburg@aud.state.fl.us or by telephone at (850) 412-2766.

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OFFICE OF FINANCIAL REGULATION

Division of Securities and Prior Audit Follow-Up

SUMMARY

This operational audit of the Office of Financial Regulation (Office) focused on the Division of Securities (Division) and included a follow-up on the applicable findings noted in our report No. 2016-196. Our audit disclosed the following:

Securities Regulation

Finding 1: The Division did not always report, or timely report, to the Central Registration Depository system and the Investment Adviser Registration Depository system used by other securities regulators, disciplinary actions taken against broker-dealers, investment adviser firms, and associated persons of broker-dealers and investment adviser firms.

Finding 2: Division procedures for processing and documenting securities regulation complaints in the Regulatory Enforcement and Licensing (REAL) system need improvement.

Financial Investigations

Finding 3: As similarly noted in our report No. 2016-196, Bureau of Financial Investigations records sometimes did not include all required investigation documentation.

REAL System Controls

Finding 4: The Office did not always timely deactivate user access privileges to the REAL system upon an employee's separation from Office employment.

Money Services Business Investigation Referrals

Finding 5: Office controls for ensuring that all money services business referrals for investigation are timely submitted to the Department of Financial Services, Division of Investigative and Forensic Services, continue to need enhancement.

BACKGROUND

Pursuant to State law,¹ the Office of Financial Regulation (Office) is responsible for regulating banks, credit unions, other financial institutions, finance companies, and the securities industry. To carry out these responsibilities, the Office operates through the divisions of Consumer Finance, Financial Institutions, and Securities, and the Bureau of Financial Investigations.

The Office utilizes the Regulatory Enforcement and Licensing (REAL) system to manage and maintain information related to its various regulatory activities, including securities registration and enforcement, financial investigations, and money services business investigation referrals. The REAL system is supported by the Department of Financial Services (DFS), Office of Information Technology, and is

¹ Section 20.121(3)(a)2., Florida Statutes.

subject to DFS policies and procedures governing information technology systems, unless the Office has developed more specific policies and procedures.

FINDINGS AND RECOMMENDATIONS

SECURITIES REGULATION

The securities markets are national in scope, which compels a complementary partnership between State regulators such as the Office, the Securities and Exchange Commission, and self-regulatory organizations such as the Financial Industry Regulatory Authority (FINRA).² To ensure an effective regulatory structure that provides fair markets for all individuals, it is important that information is shared among all regulatory partners.

The Office, Division of Securities (Division), is responsible for administering and enforcing compliance with the Florida Securities and Investor Protection Act (Act).³ The Act is designed to protect the investing public and promote economic growth. The Division focuses its efforts to protect investors by: registering broker-dealers, investment adviser firms, and associated persons of broker-dealers and investment adviser firms; conducting examinations of registered entities; and investigating complaints.

State law⁴ requires all broker-dealers; associated persons; or issuers of securities desiring to sell or offer for sale any securities in or from offices in the State, or to sell securities to persons in the State from offices outside the State, by mail or otherwise, to register with the Division. State law⁵ also requires all investment adviser firms or associated persons of an investment adviser firm wishing to engage in business from offices in the State, or render investment advice to persons of the State, by mail or otherwise, to register with the Division and all Federal covered advisers make a notice filing⁶ with the Division.

To facilitate uniformity and streamline procedures for persons who are subject to registration in multiple jurisdictions, DFS rules⁷ require broker-dealers, associated persons of broker-dealers, and investment adviser firms to file applications and fees with the Central Registration Depository (CRD) system jointly developed by the North American Securities Administrators Association⁸ and FINRA. DFS rules also require investment adviser firms to file applications and fees with the Investment Adviser Registration Depository (IARD) system developed and operated by FINRA.

The Division receives applications through the CRD system's automatic queue and manual approval queue. If there are no disclosures or criminal history information that may preclude an applicant from

² FINRA is an independent, not-for-profit organization that serves, in part, as a self-regulatory organization for securities firms and registered securities representatives doing business in the United States.

³ Chapter 517, Florida Statutes.

⁴ Section 517.12(1), Florida Statutes.

⁵ Section 517.12(4), Florida Statutes.

⁶ Section 517.1201, Florida Statutes, provides that it is unlawful for a person to transact business in the State as a Federal covered adviser unless the person makes a notice filing with the Office.

⁷ DFS Rules, Chapter 69W-600, Florida Administrative Code.

⁸ The North American Securities Administrators Association is a voluntary organization of securities regulators from the United States, Puerto Rico, the U.S. Virgin Islands, Canada, and Mexico.

being registered as a broker-dealer or associated person of a broker-dealer, applicants are automatically approved by the Division for registration based upon the CRD system's approval. If there are disclosures of prior disciplinary actions that may preclude registration or if criminal background checks identify any criminal history, the Division receives the broker-dealer and associated person of a broker-dealer application through the CRD system's manual approval queue. The Division also receives all applications for associated persons of investment adviser firms through the CRD system's manual approval queue. For applications received through the CRD system manual approval queue, and for all investment adviser firm applications received through the IARD system, the Division reviews applicable disclosure and criminal history information to determine if there is any information that may disqualify registration pursuant to State law.⁹

Finding 1: Regulatory Filings

The Office, like other state securities regulators, can report disciplinary actions against broker-dealers and associated persons to the CRD system and disciplinary actions against investment adviser firms to the IARD system via a Uniform Disciplinary Action Reporting Form (U6 form). Office policies and procedures¹⁰ specified that U6 forms were to be submitted to the CRD and IARD systems within 30 days of a final order. Reporting disciplinary actions improves the regulation of the securities industry by making more information available to other regulators for registration and other regulatory decisions. Additionally, FINRA makes information available to the public¹¹ concerning current and former broker-dealers and investment adviser firms, as well as current and former associated persons.

According to Division records, during the period July 2016 through January 2018, the Division issued final orders for 137 enforcement actions against broker-dealers, investment adviser firms, and associated persons of broker-dealers and investment adviser firms. As part of our audit, we examined Division records related to 25 enforcement actions that resulted in disciplinary actions against 23 associated persons, 11 investment adviser firms, 2 broker-dealers, and 1 unregistered broker-dealer and found that the Division did not always report, or timely report, disciplinary actions by filing U6 forms. Specifically, we found that, as of July 23, 2018, the Division had not filed a U6 form for the final order docketed on July 6, 2017, against an associated person of a broker-dealer and filed four U6 forms for 3 investment adviser firms and 1 associated person of an investment adviser firm 5 to 47 days (an average of 25 days) late. The disciplinary actions related to violations such as borrowing money from customers and selling securities without being registered with the Division. In response to our audit inquiry, Division management indicated that new staff were responsible for filing the U6 forms, which contributed to the untimely filings.

Absent the timely filing of U6 forms, less information is available in the CRD and IARD systems for regulator use in effectively regulating the securities industry. Additionally, the information available from

⁹ Section 517.161, Florida Statutes.

¹⁰ Office, Bureau of Enforcement *Examination Standards and Operations Guide*.

¹¹ FINRA makes information available through BrokerCheck, a free tool to help investors research the professional backgrounds of current and former FINRA-registered broker-dealers, investment adviser firms, and associated persons of broker-dealers and investment adviser firms. BrokerCheck information is based on information in the CRD and IARD systems.

FINRA is potentially limited, impairing the public's ability to investigate the backgrounds of current and former broker-dealers and investment adviser firms and their associated persons.

Recommendation: We recommend that Division management enhance oversight controls to ensure that staff timely file U6 forms in the CRD and IARD systems.

Finding 2: Complaints Processing

Citizens may initiate complaints with the Division regarding potential violations of State securities law encountered and, oftentimes, complaints from citizens alert the Division to potential fraud or unfair practices in the securities industry. Complaints may relate to, for example, problems encountered with companies selling securities or potential violations of securities laws. By analyzing complaints, the Division may detect a pattern of wrong-doing that results in an investigation or action to protect the public.

According to Bureau of Enforcement (Bureau) personnel, complaints are submitted to the Division through various means, including mail, e-mail, and the Office's Web site, regional offices, and complaint hotline. Upon receipt, a Bureau employee is to review the complaint, conduct background research, and determine whether further activity is warranted. Bureau management then determine whether to close the complaint without further action, refer the complaint to other parties (e.g., other state securities regulators), or investigate the complaint.

Office policies and procedures¹² required Bureau staff to enter complaint information in the REAL system as case work progressed. Staff were to acknowledge receipt of citizen complaints through an acknowledgement letter, e-mail, or telephone call to the complainant within 5 business days of being assigned the complaint. The initial contact was to be recorded in the REAL system in the Work Notes section or by attaching the acknowledgement letter. Office policies and procedures also specified that:

- When a complaint resulted in the opening of an examination, the complaint was to remain open in the REAL system until the related examination was closed.
- At the conclusion of a case, the examiner was to send a closing letter to the complainant and, if there were practical reasons why a letter should not be sent, the reasons should be reviewed and approved by the Bureau Chief and documented in the REAL system.

The Bureau utilized a quality assurance process to determine whether complaints were appropriately handled and documented in the REAL system. Periodically, a Bureau employee selected a sample of closed complaints and reviewed the complaints to verify that the complaints were handled and documented in accordance with Office policies and procedures.

According to REAL system records, the Division received 373 complaints during the period July 2016 through January 2018. REAL system records indicated that, of the 373 complaints, 209 (56 percent) were closed without further action, 113 (30 percent) were referred to other parties, and 51 (14 percent) were investigated by Bureau staff. Our examination of REAL system records for 40 of the 373 complaints disclosed that the Bureau did not always acknowledge the receipt of complaints, sometimes closed complaints prior to the completion of the related examination, and did not always include required information in the REAL system. Specifically, we found that:

¹² Office, Bureau of Enforcement *Examination Standards and Operations Guide*.

- REAL system records for 11 citizen complaints did not evidence communication of complaint receipt to the complainant.
- 13 complaints resulted in an examination and Bureau staff closed 3 of the complaints in the REAL system prior to the closure of the related examination. For example, the REAL system close date for 1 complaint was 173 days prior to the close of the related examination and the REAL system close date of another complaint was February 6, 2018, although the examination was still open as of December 20, 2018.
- For 4 complaints, Bureau staff did not include in the REAL system a closing letter or document the reasons why a closing letter was not sent.

According to Bureau management, staffing issues and employee errors contributed to the deficiencies noted.

As part of our audit, we also evaluated the effectiveness of the Bureau’s quality assurance process. The Bureau subjected 95 of the 373 complaints received during the period July 2016 through January 2018 to a quality assurance review. Our examination of the quality assurance records for 19 complaints reviewed by the Bureau disclosed that the Bureau found no exceptions related to the closing letter requirement. However, our examination found that a closing letter for 2 of the 17 applicable complaints was not included in the REAL system. In response to our audit inquiry, Bureau management indicated that staffing issues contributed to the quality assurance review deficiencies.

Absent documentation demonstrating that all applicable complaints are acknowledged, appropriately tracked in conjunction with related examinations, and REAL system records include all required information, Bureau management cannot demonstrate that complaints are appropriately handled in accordance with management’s expectations. In addition, absent an effective quality assurance review process, the Bureau has limited assurance that complaints are handled and documented appropriately.

Recommendation: We recommend that Bureau management strengthen oversight controls, including quality assurance reviews, to ensure that Bureau staff adhere to established policies and procedures for handling complaints and documenting complaint processing activities.

FINANCIAL INVESTIGATIONS

The Office, Bureau of Financial Investigations (Bureau), is responsible for conducting investigations of potential mortgage, securities, collection agency, money services business, and loan broker (advance fee) fraud and unlicensed activity based on consumer complaints and referrals and tips received from Office divisions, State agencies, the Federal Government, law enforcement, and prosecutors. The Bureau is the criminal justice arm of the Office and is authorized¹³ to conduct investigations as necessary to aid the Office in enforcing its regulatory responsibilities. In addition to the Bureau’s Tallahassee office, the Bureau maintains investigative teams in Orlando, Tampa, West Palm Beach, and Miami.

Finding 3: Investigation Records

The Bureau established *Investigative Standards and Operations Guide (Standards)* and associated referenced documents and memoranda for use in the conduct of investigations. The *Standards* required investigators to document investigative activities in the REAL system case records by including, among

¹³ Section 20.121(3)(a)2., Florida Statutes.

other things, the closing report, report of investigation, and related documents such as civil complaints and criminal filings.

In our report No. 2016-196 (Finding 1), we noted that Bureau investigation records were not always complete, and the Bureau did not always sufficiently document case review and approval activities in accordance with established procedures. Effective July 1, 2016, the Bureau required investigators to complete a Case Audit Checklist and add the Checklist to the REAL system to demonstrate that all required investigation documents were included in the case record. Bureau management indicated that, at case closure, Bureau supervisors were to sign the Case Audit Checklist documenting their review of the casefile.

As part of our follow-up audit procedures, we examined REAL system case records for 20 of the 181 investigations closed by the Bureau during the period December 2016 through January 2018. Our examination disclosed that, while the Bureau had taken steps to address the deficiencies noted in our prior audit report, we found that the REAL system case records for 4 of the 20 investigations did not include all required documentation, such as a final order for an administrative action, witness interviews, and arrest warrants. Additionally, for these 4 investigations and another 5 investigations, the REAL system records did not include a Case Audit Checklist. According to Bureau management, the documents were omitted from the REAL system due to employee oversight and the recent implementation of the Case Audit Checklist procedure.

Completion of Case Audit Checklists for all investigations and adequate supervisory review of case records would better ensure that the REAL system includes all required investigation documents at the time of case closure.

Recommendation: We recommend that Bureau management ensure that REAL system records for all investigations include completed Case Audit Checklists and the required investigation documentation.

REAL SYSTEM CONTROLS

Effective information technology (IT) access controls are intended to prevent and detect inappropriate access to IT resources and protect the confidentiality, integrity, and availability of data. Agency for State Technology rules¹⁴ require State agencies to ensure that IT access privileges are deactivated when access to an IT resource is no longer required. Prompt action to deactivate access privileges when a user separates from employment is necessary to help prevent misuse of the access privileges.

Finding 4: REAL System Access Controls

In our report No. 2016-196 (Finding 6), we noted that REAL system controls needed improvement to demonstrate that user access privileges were timely deactivated upon a user's separation from Office employment. To access the REAL system, users were required to first access the DFS network. As part of our follow-up audit procedures, we examined access privilege records for the 79 Office employees with REAL system access privileges who separated from Office employment during the period July 2016 through January 2018 to determine whether the employees' access privileges had been timely

¹⁴ Agency for State Technology Rule 74-2.003(1)(a)8., Florida Administrative Code.

deactivated. Our examination disclosed that REAL system user access privileges for 23 employees remained active 3 to 235 business days (an average of 48 business days) after the employees' separation dates.

In response to our audit inquiry, Office management indicated that they relied on the deactivation of DFS network access privileges to prevent access to the REAL system by former employees. Notwithstanding Office management's response, the prompt deactivation of REAL system access privileges upon an employee's separation from Office employment reduces the risk that REAL system access privileges may be misused by the former employee or others.

Recommendation: We recommend that Office management strengthen controls to ensure that REAL system access privileges are timely deactivated upon an employee's separation from Office employment.

MONEY SERVICES BUSINESS INVESTIGATION REFERRALS

The Office, Division of Consumer Finance, is responsible for licensing and regulating non-depository financial service industries and individuals and conducting examinations and complaint investigations of licensed entities to determine compliance with State law. Among the financial service industries regulated by the Office are money services businesses (MSBs).¹⁵

Finding 5: Referrals to the DFS Division of Investigative and Forensic Services

Pursuant to a February 2013 Memorandum of Understanding (MOU) between the Office and the DFS, Division of Investigative and Forensic Services (DFS DIFS), the Office was to refer to the DFS DIFS all cases involving suspected fraud where an MSB:

- Negotiated third-party business-to-business checks totaling \$500,000 or more within a 6-month period,
- Was referred to the Department of Law Enforcement for potential felony criminal activity, or
- Was conducting business with a person or entity identified by the DFS DIFS as a known or suspected participant in an MSB-facilitated workers' compensation premium fraud scheme.

In our report No. 2016-196 (Finding 8), we noted that the Office did not ensure that all MSB referrals for investigation were appropriately submitted to the DFS DIFS. Effective July 2016, Office procedures required Office personnel to mail or e-mail referral letters to a specific DFS DIFS contact, enter the referral information in the REAL system, and assign referrals to compliance staff. Referrals were to remain open in the REAL system until the Office received a response from the DFS DIFS indicating whether the DFS DIFS opened a case. On a quarterly basis, the DFS DIFS was to provide the Office the outcomes of the referrals made and, if the Office did not receive the required information within 30 days of a quarter-end, compliance staff were to follow up with the DFS DIFS to ensure that the referrals had been received.

¹⁵ Section 560.103(22), Florida Statutes, defines a money services business as any person located in or doing business in the State, from the State, or into the State from locations outside of the State or the United States who acts as a payment instrument seller, foreign currency exchanger, check casher, or money transmitter.

The Office reported in the REAL system that ten referrals were sent to the DFS DIFS during the period July 2016 through January 2018. As part of our follow-up audit procedures, we obtained from the DFS DIFS a listing of referrals received during the same period and compared that listing to REAL system records. We found that Office staff e-mailed four of the ten referrals to the DFS DIFS contact after that individual was no longer employed by the DFS DIFS. As a result, the referrals were received by the DFS DIFS 261 to 600 days (an average of 385 days) after the original referral date. In response to our audit inquiry, Office management indicated that compliance staff could not track three of the four referrals as the referrals had been closed on the date they were e-mailed to the DFS DIFS. Office management also indicated that compliance staff had not followed up with the DFS DIFS to ensure receipt of the fourth referral.

Absent compliance with established procedures, the Office has reduced assurance that all MSB referrals for investigation are received by the DFS DIFS.

Recommendation: We again recommend that Office management take appropriate actions to ensure that all MSB investigation referrals are timely sent to, and received by, the DFS DIFS.

PRIOR AUDIT FOLLOW-UP

Except as discussed in the preceding paragraphs, the Office had taken corrective actions for the applicable findings included in our report No. 2016-196.

OBJECTIVES, SCOPE, AND METHODOLOGY

The Auditor General conducts operational audits of governmental entities to provide the Legislature, Florida's citizens, public entity management, and other stakeholders unbiased, timely, and relevant information for use in promoting government accountability and stewardship and improving government operations.

We conducted this operational audit from January 2018 through November 2018 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.

This operational audit of the Office of Financial Regulation (Office) focused on the Division of Securities (Division). The overall objectives of the audit were:

- To evaluate management's performance in establishing and maintaining internal controls, including controls designed to prevent and detect fraud, waste, and abuse, and in administering assigned responsibilities in accordance with applicable laws, administrative rules, contracts, grant agreements, and other guidelines.
- To examine internal controls designed and placed in operation to promote and encourage the achievement of management's control objectives in the categories of compliance, economic and efficient operations, the reliability of records and reports, and the safeguarding of assets, and identify weaknesses in those internal controls.

- To identify statutory and fiscal changes that may be recommended to the Legislature pursuant to Section 11.45(7)(h), Florida Statutes.

Our audit also included steps to determine whether management had corrected, or was in the process of correcting, all applicable deficiencies noted in our report No. 2016-196.

This audit was designed to identify, for those programs, activities, or functions included within the scope of the audit, deficiencies in management's internal controls, instances of noncompliance with applicable governing laws, rules, or contracts, and instances of inefficient or ineffective operational policies, procedures, or practices. The focus of this audit was to identify problems so that they may be corrected in such a way as to improve government accountability and efficiency and the stewardship of management. Professional judgment has been used in determining significance and audit risk and in selecting the particular transactions, legal compliance matters, records, and controls considered.

As described in more detail below, for those programs, activities, and functions included within the scope of our audit, our audit work included, but was not limited to, communicating to management and those charged with governance the scope, objectives, timing, overall methodology, and reporting of our audit; obtaining an understanding of the program, activity, or function; exercising professional judgment in considering significance and audit risk in the design and execution of the research, interviews, tests, analyses, and other procedures included in the audit methodology; obtaining reasonable assurance of the overall sufficiency and appropriateness of the evidence gathered in support of our audit's findings and conclusions; and reporting on the results of the audit as required by governing laws and auditing standards.

Our audit included the selection and examination of transactions and records. Unless otherwise indicated in this report, these transactions and records were not selected with the intent of statistically projecting the results, although we have presented for perspective, where practicable, information concerning relevant population value or size and quantifications relative to the items selected for examination.

An audit by its nature, does not include a review of all records and actions of agency management, staff, and vendors, and as a consequence, cannot be relied upon to identify all instances of noncompliance, fraud, abuse, or inefficiency.

In conducting our audit, we:

- Performed inquiries of Division management and inspected documents and records to determine whether Division management had adequately designed and implemented controls, including policies and procedures, for securities registration and enforcement activities.
- From the population of 8,103 broker-dealer and investment adviser firm associated person applications manually reviewed by the Division during the period July 2016 through January 2018, examined records for 40 selected associated person applications to determine whether the Division appropriately registered associated persons and properly documented registration activities in the Regulatory Enforcement and Licensing (REAL) system.
- From the population of 166 Enforcement, Risk-Based, and Special examinations conducted by the Division related to investment adviser firms during the period July 2016 through January 2018, examined Division records for 25 selected examinations to determine whether the Division appropriately and timely conducted the examinations and properly documented examination activities in the REAL system.

- From the population of 137 enforcement actions finalized by the Division against broker-dealers, investment adviser firms, and associated persons of broker-dealers and investment adviser firms during the period July 2016 through January 2018, examined Division records for 25 selected enforcement actions to determine whether the enforcement actions complied with significant governing laws and rules, were properly conducted, documented, and consistently applied, and a Uniform Disciplinary Action Reporting Form was timely filed with the Central Registration Depository (CRD) system or the Investment Adviser Registration Depository (IARD) system.
- From the population of 373 complaints related to broker-dealers, investment adviser firms, and associated persons of broker-dealers and investment adviser firms, received by the Division during the period July 2016 through January 2018, examined Division records for 40 selected complaints to determine whether the Division appropriately and timely processed the complaints and properly documented complaint handling activities in the REAL system. Additionally, we examined the quality assurance records for 19 of the 95 complaints received by the Division during the period July 2016 and January 2018 and subject to a quality assurance review to determine whether the reviews were appropriately conducted.
- Compared Florida Accounting Information Resource Subsystem (FLAIR) fee revenue data to data from the CRD and IARD systems for broker-dealer branch, investment adviser branch, and associated person registration applications for the period July 2016 through June 2017 to determine whether the fee revenue recorded in FLAIR was reasonable.
- Analyzed data from the CRD and IARD systems related to broker-dealer branch, investment adviser branch, and associated persons registrations for the 2016-17 fiscal year to determine whether the number of registrations were comparable to the number of registrations during the 2013-14 through 2015-16 fiscal years.
- Examined employment and training records for 25 of the 88 staff who were employed with the Division at some point during the period July 2016 through January 2018 to determine whether the employees satisfied applicable position requirements, received required training, and were subject to required background screenings.
- Evaluated Office actions to correct the applicable findings noted in our report No. 2016-196. Specifically, we:
 - From the population of 181 investigations closed by the Bureau of Financial Investigations (Bureau) during the period December 2016 through January 2018, examined REAL System case records for 20 selected investigations to determine whether investigation activities were adequately documented in the REAL system, including required approval activities, in accordance with the Bureau's *Investigative Standards and Operations Guide*.
 - From the population of 25 quarterly case reviews conducted by the five Bureau regional offices during the period June 2016 through January 2018, examined Bureau records for 5 selected quarterly case reviews to determine whether the reviews were properly conducted and documented.
 - From the population of 384 complaints received by the Bureau during the period December 2016 through January 2018, examined REAL system records related to 25 selected complaints to determine whether the Bureau accurately recorded complaint information in the REAL system, acknowledged the receipt of complaints, and timely processed complaints.
 - Evaluated the effectiveness of selected logging and monitoring controls for Filenet, the REAL system's image content manager.
 - Performed inquiries of Office management, observations, and inspections of documents and records to determine whether the Office appropriately monitored the contractor

responsible for REAL system operations and maintenance, including whether contractor employees were subject to required level 2 background screenings.

- From the population of 5 quarterly reviews of REAL system user access privileges conducted by the Office during the period July 2016 through January 2018, examined Office records for 1 selected quarterly access review to determine whether quarterly access reviews were performed in accordance with established policies and procedures.
 - Examined REAL system user access records for the 79 REAL system users who separated from Office employment during the period July 2016 through January 2018 to determine whether the users' access privileges to the REAL system were timely deactivated upon the employees' separation from Office employment.
 - From the population of 341 commercial collection agency renewal registrations issued by the Office during the period October 2016 through January 2018, examined REAL system records for 25 renewal registrations to determine whether the Office ensured that the registrants provided all information required by State law.
 - Compared REAL system records for the ten money services business investigation referrals reported by the Office as being submitted to the Department of Financial Services, Division of Investigative and Forensic Services (DFS DIFS), during the period July 2016 through January 2018, to a DFS DIFS-provided listing of referrals received by the DFS DIFS during the same time period and evaluated the reasons for the differences noted, if any.
- Communicated on an interim basis with applicable officials to ensure the timely resolution of issues involving controls and noncompliance.
 - Performed various other auditing procedures, including analytical procedures, as necessary, to accomplish the objectives of the audit.
 - Prepared and submitted for management response the findings and recommendations that are included in this report and which describe the matters requiring corrective actions. Management's response is included in this report under the heading **MANAGEMENT'S RESPONSE**.

AUTHORITY

Section 11.45, Florida Statutes, requires that the Auditor General conduct an operational audit of each State agency on a periodic basis. Pursuant to the provisions of Section 11.45, Florida Statutes, I have directed that this report be prepared to present the results of our operational audit.



Sherrill F. Norman, CPA
Auditor General

MANAGEMENT'S RESPONSE



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January 18, 2019

Ms. Sherrill F. Norman, CPA
Auditor General
Claude Pepper Building, G74
111 West Madison Street
Tallahassee, FL 32399-1450

Re: Response to Preliminary and Tentative Audit Findings
Operational Audit of the Office of Financial Regulation, Division of Securities and
Prior Audit Follow-up

Dear Auditor General Norman,

Enclosed is the Office of Financial Regulation's (Office) response to the Auditor General's preliminary and tentative audit findings and recommendations dated December 20, 2018.

The Office wishes to thank the staff of the Auditor General's Office for their professionalism and thoroughness during this engagement.

If you have any questions, please contact our Audit Director, Angela Roddenberry at angela.roddenberry@flofr.com

Sincerely,



Pamela P. Epting
Deputy Commissioner

Enclosure

cc: Bradley Perry, Inspector General
Angela Roddenberry, Audit Director

Interim Commissioner Pamela P. Epting
101 East Gaines Street, Tallahassee, Florida 32399-0370
(850) 410-9601 • FAX (850) 410-9663
Mailing Address: 200 East Gaines Street, Tallahassee, Florida 32399-0370

RESPONSE TO AUDITOR GENERAL FINDINGS

Finding No. 1: Regulatory Filings

Auditor General Recommendation: We recommend that Division management enhance oversight controls to ensure staff timely file U6 forms in the CRD and IARD systems.

OFR Response: We concur and agree with the recommendation. A weakness in the U6 process was identified by management during a staffing assessment by the Bureau of Enforcement in late 2017. The Bureau took immediate steps to input any outstanding Form U6 filings to remedy the issue. In response to this audit the Division has further enhanced its oversight of this process within the Bureau of Enforcement in the following ways: the manager overseeing the process is now being copied on all disciplinary actions originated by the Bureau of Enforcement and will perform monthly quality control checks; the position accountable for preparing Form U6 filings has allocated time on a weekly basis to ensure that the filings are made timely; and lastly, performance measures will be added to the responsible party's position so that timeliness can be measured.

Finding No. 2: Complaints Processing

Auditor General Recommendation: We recommend that Bureau management strengthen oversight controls, including quality assurance reviews, to ensure that Bureau staff adhere to established policies and procedures for handling complaints and documenting complaint processing activities.

OFR Response: We concur and agree with the recommendation. The Division has reviewed its complaint process and will amend the Bureau of Enforcement Examination Standards and Operation Guide during the first quarter of 2019 to clarify the complaint handling process. Management will provide training to both the area financial managers and examiners on the proper protocols relating to each phase of the complaint process during the first quarter of 2019. This training will be documented for staff as a reference tool. Lastly, the quality assurance process will be strengthened to ensure that each component of the complaint procedures is being adhered to by staff.

Finding No. 3: Investigation Records

Auditor General Recommendation: We recommend that Bureau management ensure that REAL system records for all investigations include completed Case Audit Checklists and the required investigation documentation.

OFR Response: We concur. The Bureau of Financial Investigations (BFI) Investigative Standards and Operations Guide currently requires BFI investigators to complete a Case Audit Checklist, have it reviewed and signed by their supervisor, and attach it to the REAL record. BFI is taking the additional step of creating a performance measure to be added to the Performance Evaluation for each BFI manager to ensure proper completion of the Case Audit Checklist. BFI management will continue to train its investigators and managers to attach all required investigative documents and the completed Case Audit Checklist to the REAL record. In addition, Bureau Management is requiring the BFI training coordinator to review all closed investigations in REAL within 30 days of case closure to ensure that the required investigative documents are attached to the REAL Record and to ensure that all case audit

checklists have been properly completed. Completion of the review by the BFI training coordinator will be noted in the REAL record by a newly created activity code.

Finding No. 4: REAL System Access Controls

Auditor General Recommendation: We recommend that Office management strengthen controls to ensure that REAL system access privileges are timely deactivated upon an employee's separation from Office employment.

OFR Response: We concur. Office management will continue to reinforce the importance of timely deactivation of REAL system access upon employee separation from the Office. In addition, the Office will update its procedures to ensure proper communication between all employees responsible for this task and add a layer of control to follow up and validate timely deactivation. The Office expects to finalize the updated policy within 30 days.

Finding No. 5: Referrals to the DFS Division of Investigation and Forensic Services

Auditor General Recommendation: We again recommend that Office management take appropriate actions to ensure that all MSB investigation referrals are timely sent to, and received by, the DFS DIFS.

OFR Response: We concur. The Division of Consumer Finance has enhanced its internal procedures by adding an additional layer of control to ensure referrals are being handled in accordance with protocols. The additional layer of control is in the form of a monthly and quarterly REAL report that identifies all activities documenting investigative referrals to DFS DIFS. The report will provide management the ability to ensure the referrals were entered correctly, assigned to the appropriate staff, and followed up in a timely manner with DFS DIFS when a response has not been received confirming receipt of the referral. The revised procedure was updated on 1/15/2019 reflecting the additional layer of control.