



A REPORT
TO THE
ARIZONA LEGISLATURE

Financial Audit Division

Procedural Review

Arizona Department of Real Estate

As of February 28, 2015

September • 2015
Report No. 15-304



Debra K. Davenport
Auditor General

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September 8, 2015

Judy Lowe, Commissioner
Arizona Department of Real Estate

We have performed a procedural review of the Arizona Department of Real Estate's (Department) internal controls in effect for the review period of March 1, 2014 through February 28, 2015. Our review consisted primarily of inquiries, observations, and selected tests of internal control policies and procedures, accounting records, and related documents. The review was more limited than would be necessary to give an opinion on internal controls. Accordingly, we do not express an opinion on the effectiveness of internal controls or ensure that all deficiencies in internal controls are disclosed.

Specifically, we reviewed the Department's policies and procedures for processing cash receipts, cash disbursements, journal entries, transfers, and payroll transactions; purchasing goods and services; reporting capital assets; and complying with state laws.

As a result of our review, we noted two deficiencies in internal controls that the Department's management should correct to ensure that it fulfills its responsibility to establish and maintain adequate internal controls. Our findings and recommendations concerning these deficiencies are described in the accompanying summary.

This report is intended solely for the information and use of the Department and is not intended to be and should not be used by anyone other than the specified party. However, this report is a matter of public record, and its distribution is not limited.

Should you have any questions concerning our procedural review, please let us know.

Sincerely,

Jay Zsorey, CPA
Financial Audit Director

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FINDING 1

Department should strengthen its controls over cash receipts

For the review period of March 1, 2014 through February 28, 2015, the Department received operating revenues totaling approximately \$3.9 million. These revenues consisted of licensing application and renewal fees; subdivision inspection, review, and reporting fees; licensure exam and education fees; and civil penalties and fines. During our review period, the Department received approximately \$16,000 and \$407,000 of these revenues in the form of cash and checks/money orders, respectively. Because cash receipts are susceptible to loss or theft, it is imperative that the Department adequately control and safeguard these monies. Further, the *State of Arizona, General Accounting Office's Accounting Manual*, Topic 20, §10, requires that all state agencies separate cash receiving and recording responsibilities, reconcile daily cash receipts, record cash receipts received by mail at the time the mail is opened, and have two employees present when the mail is opened and cash receipts are logged. However, the Department did not always follow these procedures.

Receipts forms not always issued and daily cash collections not reconciled to detailed accounting records

The Department did not have adequate procedures to help ensure that cash receipts were recorded and deposited. Specifically, the Department's employees were responsible for both collecting and recording daily cash receipts without adequate procedures in place to help mitigate the risk of loss or theft. For example, although the Department's policies appropriately required receipts to be issued to customers, the Department's information technology system was not designed to ensure that receipts were issued to customers and maintained in the Department's records for each cash receipt transaction, such as when processing and issuing new licenses and renewals. In addition, customer records were updated without an independent review. Further, the Department was unable to generate system reports to reconcile daily cash collections to the detailed accounting records, such as the day's licenses and renewals issued to customers and other fees, penalties, and fines charged and processed.

Cash receipts received by mail not always recorded upon receipt

The Department did not have adequate procedures for controlling cash receipts received by mail. Auditors noted that mail receipts were not opened and recorded in the presence of two employees when practicable. While the Department generally had one person open and log all mail receipts, mail that may have contained cash receipts in envelopes marked as confidential were delivered unopened to other department employees without being controlled and logged. Similarly, some

mail that contained customer payments for subdivision inspection, review, and reporting fees; education fees; and civil penalties and fines were not opened and logged centrally. In addition, because the Department did not log all mail receipts, it had no way of reconciling these cash receipts to ensure that they were recorded and deposited.

Recommendations

To help ensure that all cash receipts are properly recorded and deposited and safeguarded from loss or theft, and to comply with the *State of Arizona, General Accounting Office's Accounting Manual*, the Department should:

1. Ensure that receipt forms are issued to customers and maintained in the Department's records for all cash receipt transactions.
2. Reconcile daily cash collections to the detailed accounting records entered into the system using system-generated reports if possible, or to other reliable information on the day's cash receipt transactions. An employee who is not responsible for collecting or recording cash receipts should review and approve the reconciliation.
3. Control and log all cash receipts that arrive through the mail, requiring two employees to open the mail and log the receipts when practicable.

FINDING 2

Department should improve process for ensuring fees charged to public are set in accordance with state laws

As part of carrying out its responsibilities, the Department charges fees for various services it provides to the public, such as processing new and renewal license applications for real estate salespersons, brokers, and brokerages; conducting inspections, reviewing plans, and issuing public reports for subdivisions and certain unsubdivided lands; and overseeing licensure exams and education for potential real estate brokers and salespersons. Accordingly, fees should be evaluated on an annual basis against the associated cost of providing the services and set in accordance with state laws. Specifically, A.R.S. §32-2103 requires the Department to revise its service fees within the range allowed by various statutes. Further, the Department's total revenues from service fees should approximate at least 95 percent but not exceed 110 percent of the Department's anticipated appropriated budget for the succeeding fiscal year. Therefore, the Department revises its fees each year to ensure that it complies with A.R.S. §32-2103. However, the Department did not have an adequate review process in place to ensure that it set its service fees in accordance with all of the applicable state laws authorizing the Department's fees.

While testing for compliance with state laws, auditors noted that the Department's set fees were not always in compliance with the statute authorizing them. Specifically, A.R.S. §32-2132(A)(9), requires that the Department charge at least \$60 but no more than \$200 for real estate broker's branch office license renewals. However, from November 1, 2012 through December 1, 2014, the Department charged only \$50 and received a total of \$37,000 for real estate broker's branch office license renewals. The Department would have received \$7,400 more for that period if it had charged the statutorily required minimum of \$60. The Department detected the noncompliance and appropriately adjusted the fee effective December 1, 2014.

Additionally, A.R.S. §32-2195.03(B)(2) requires that the Department charge \$250 for applications to amend public disclosure reports for unsubdivided land. From July 29, 2010 through July 23, 2014, the Department charged \$500 and received a total of \$5,500 for applications to amend public disclosure reports for unsubdivided land. The Department would have received \$2,750 less for that period if it had charged the statutorily required amount of \$250. The Department also detected this noncompliance and appropriately adjusted the fee effective July 23, 2014. While the Department was able to detect these instances of noncompliance and properly adjust its fees, the Department's review process did not include a complete review of all applicable statutes authorizing fees prior to setting the fees.

Recommendations

To help ensure that it sets fees for services provided to the public in accordance with statutory fee limits, the Department should continue its process of evaluating fees against the associated costs of providing the services on an annual basis. Additionally, this process should include comparing proposed service fee revisions to the applicable statutes for compliance before submitting them to the Department's commissioner for approval.

DEPARTMENT RESPONSE

DEPARTMENT RESPONSE



STATE OF ARIZONA
DEPARTMENT OF REAL ESTATE

DOUGLAS A. DUCEY
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Ms. Debra K. Davenport
Arizona Office of the Auditor General
2910 N. 44th Street, Suite 410
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September 3, 2015

Ms. Davenport,

Please find the Arizona Department of Real Estate's (ADRE) response to your agency's procedural review. The Department appreciates the professionalism and hard work of your staff in completing this review, as well as their consideration of agency feedback throughout the audit process.

Finding One: Department should strengthen its controls over cash receipts

Response: The Department agrees with, and has implemented the recommendations set forth in Finding One.

Recommendations:

- 1. Ensure that receipt forms are issued to customers and maintained in the Department's records for all cash receipt transactions.*
- 2. Reconcile daily cash collections to the detailed accounting records entered into the system using system-generated reports if possible, or to other reliable information on the day's cash receipt transactions. An employee who is not responsible for collecting or recording cash receipts should review and approve the reconciliation.*

Response: The Department does provide receipts to consumers with every transaction whether payment is made through credit card, cash or check. The detail in Finding One clarifies that the Department's policies required receipts to be issued to customers, but suggested that the information technology system would not generate reports to substantiate the policy in all instances. Steps that were taken in July 2015 to implement these recommendations are as follows:

- The Department revised its walk in customer sign-in sheet to include method of payment, employee to review, employee that processed payment, and customer reason for visit.

This enhanced sign-in sheet is reconciled weekly by the Business Services office against the REALM weekly deposit report to support that all transactions are entered into the electronic system correctly.

- The Department now includes a copy of each receipt for cash and check transactions with the end of day deposit package that is reconciled with the daily deposit.
- The Department's Operation Manual was updated to reflect these new processes.

3. Control and log all cash receipts that arrive through the mail, requiring two employees to open the mail and log the receipts when practicable.

Response: Current processes require the mail clerk to log license receipts received through the mail. These logs have been maintained by the mail clerk and reported to the Business Services office. Steps that were taken in July 2015, before the draft audit report was submitted to the Department are as follows:

- The Department revised its mail policy to require the mail clerk to open all division mail, and log all receipts for all divisions on the mail clerk's monthly mail statistics spreadsheet to be reconciled weekly by the Business Services office.
- A receipt of the transaction will be provided to the consumer, with a copy included with the daily deposit.
- Whenever practicable, a second Department employee will accompany the mail clerk while opening and logging all mail.

Finding Two: Department should improve process for ensuring fees charged to public are set in accordance with state laws

Response: The Department agrees with, and has implemented the recommendations set forth in Finding Two.

Recommendations:

1. Compare proposed service fee revisions to the applicable statutes for compliance before submitting them to the Department's commissioner for approval.

Response: The Department agrees with the recommendation, and the response to the finding is below.

- The Department had a formalized review process to review and revise fees in accordance with the 95/110 provision specified in A.R.S. § 32-2103.
- The Department is the only state agency that currently operates under this budget structure which mandates that fee revenue collection remain between 95 and 110 percent.

- Volatile conditions in the real estate market during the economic downturn, as well as a drastically reduced agency appropriation, caused the Department to significantly reduce fees to near statutory baselines to adhere to the 95/110.
- The real estate broker's branch office license renewal fee was one of the many fees lowered, and in this case below the baseline set in A.R.S. § 32-2132(A)(9). The correction was effective December 1, 2014.

Lastly, the application fee for amended unsubdivided land applications are set in A.R.S. § 32-2195.03(B).

- As stated in Finding Two, the Department revised the amended unsubdivided land application to \$250 effective July 2014.
- The transactions referenced in the audit finding relating to the amended unsubdivided land application totaled eleven which all occurred in 2011. There have been no unsubdivided land amendment applications since 2011.
- The Department understands that legal counsel for the Office of the Auditor General reviewed A.R.S. §§ 32-2195.02, 32-2195.03, and 32-2195.10 to respond to the Department's interpretation that the statutes conflict.
- While the Department concurs that improvements should be made in the overall process for establishing revisions, and that recommended improvement has been specified for any fee revision, it remains the Department's interpretation that the referenced statutes conflict related to this specific fee.
- The Department has implemented a procedure to compare proposed service fee revisions to the applicable statutes for compliance before submitting them to the Department's commissioner for approval.

The ADRE strives to constantly improve all of its processes and operations to ensure all customers are served efficiently, accurately, and with professionalism. We thank you and your staff, and look forward to working together in the future.

Sincerely,

Judy Lowe
Commissioner

