



AUDITOR GENERAL

WILLIAM O. MONROE, CPA



OFFICE OF FINANCIAL REGULATION

REGULATION OF FINANCIAL INSTITUTIONS, SECURITIES, AND CERTIFIED CAPITAL COMPANIES

Operational Audit

SUMMARY

Our audit included an evaluation of selected Office of Financial Regulation (OFR) processes associated with the regulation of certified capital companies (CAPCOs), banks, credit unions, and securities entities. Our audit, covering the period January 7, 2003, through February 29, 2004, disclosed the following:

Finding No. 1: Although Section 288.99(8)(a), Florida Statutes, requires that the CAPCOs provide a detailed report relative to the use of CAPCO moneys invested, the statute does not require the CAPCOs to report how other State-provided CAPCO moneys were used. As a consequence, the CAPCOs were not required to describe in annual reports how approximately \$52 million in State-provided CAPCO moneys had been used. While it is not our intent to suggest that the CAPCOs have failed to properly account for moneys provided under the CAPCO Act or to suggest that the moneys have been used by the CAPCOs in a manner not authorized by law, there is a need for the amendment of the statutory reporting requirements in order to facilitate full disclosure of the usage of State moneys.

Finding No. 2: Section 288.99(10)(a), Florida Statutes, requires the OFR to conduct annual reviews of certified capital companies. The OFR had not implemented written policies and procedures to govern the conduct of the CAPCO annual reviews, and the absence of written policies and procedures contributed to the OFR's failure to properly document the nature, timing, and extent of the work performed.

Finding No. 3: Our review of a total of 15 bank examinations performed by the Tampa, Orlando, and Tallahassee OFR Regional Offices (5 from each office) disclosed that the OFR had established reasonable methodologies for conducting these examinations and that examiners had generally complied with these methodologies during the conduct of their examinations.

Finding No. 4: Applications for securities entities (securities dealers, investment advisers, branch offices, and associated persons) are submitted to the OFR for processing and review. Our audit disclosed that, while a supervisory review of an application may be conducted if an OFR analyst develops concerns regarding disclosed disciplinary actions, supervisory evaluations are not conducted of other applications. The absence of documented supervisory evaluations of analysts' decisions to approve applications increases the risk that the OFR may issue a securities permit to an entity that does not meet established eligibility requirements.

Finding No. 5: The OFR uses electronic examination modules to guide the conduct of examinations of securities entities. For two of the ten securities examinations reviewed, the then most current version of the examination module was not used. The failure to use the appropriate examination module may lead to the conduct of examinations which do not, in scope, adequately address applicable laws and rules.

BACKGROUND

Effective January 7, 2003, Chapter 2002-404, Laws of Florida, created the Department of Financial Services, within which was created the Financial Services Commission, consisting of the Governor, the Attorney General, the Chief Financial Officer, and the Commissioner of Agriculture.

Within the Financial Services Commission, the Office of Financial Regulation (OFR) was established. The OFR is responsible for all activities of the Financial Services Commission relating to the regulation of banks, credit unions, other financial institutions, finance companies, and the securities industry. Section 288.99, Florida Statutes, also requires the OFR to participate in the oversight of the Certified Capital Company Act.

Bureaus within the OFR are the Bureau of Financial Investigations, Bureau of Banking Regulation, Bureau of Credit Union Regulation, Bureau of Securities Regulation, Bureau of Finance Regulation, and Bureau of Regulatory Review.

FINDINGS AND RECOMMENDATIONS

Certified Capital Company Act

The 1998 Florida Legislature enacted Chapter 98-257, Laws of Florida, entitled the Certified Capital Company Act (codified as Section 288.99, Florida Statutes). The stated purpose of this Act was to stimulate a substantial increase in venture capital investments in Florida by providing an incentive for insurance companies to invest in State-certified capital companies (CAPCOs) which, in turn, will make investments in new or expanding businesses. The incentives provided to insurance companies are in the form of insurance premium tax credits in amounts equal to the investment in the CAPCOs. The increase in investment capital flowing into new or expanding businesses is intended to contribute to employment growth, create jobs the compensation of which exceed the average wage for the county in which the jobs are

created, and expand or diversify the economic base of Florida.

Under Program One of the CAPCO Act, the insurance industry was able to invest up to \$150 million in CAPCOs and claim insurance premium tax credits totaling \$15 million each year for ten years. Under Program Two, which has yet to be executed, an additional \$150 million in insurance premium tax credits may be allocated upon authorization by the Legislature and the adoption of related rules by the Financial Services Commission.

Under the Act, the OFR, the Governor’s Office of Tourism, Trade, and Economic Development (OTTED), and the Department of Revenue (DOR) have roles in administering the CAPCO Program. The OTTED allocates tax credits to certified capital companies and provides an annual report to the Governor, President of the Senate, and Speaker of the House. The OFR certifies capital companies and performs an annual review of each certified capital company. The DOR accounts for tax credits claimed by insurance premium taxpayers.

Under Program One, the OFR certified three companies (CAPCOs) eligible to receive investment funds from insurance companies and invest in venture capital. A total of \$150,000,000 was received by these CAPCOs. According to information in the CAPCOs’ annual reports, and as shown by Exhibit A, there were 33 qualified businesses in which the CAPCOs had invested as of December 31, 2003. Amounts invested in qualified businesses averaged \$2,516,606 per qualified business and ranged from \$454,370 to \$7,600,000. Examples of industries represented by the qualified businesses are electronic imaging, medical technology, boat manufacturing, credit card payment processing, vehicle fleet management systems, an internet portal for fishermen, and a cookie manufacturer.

According to the annual reports filed by the CAPCOs, the total number of full-time jobs in qualified businesses at the time of the initial investments in the 33 companies was 820. The total number of full-time

jobs in all qualified businesses as of December 31, 2003, was 658.

Finding No. 1: CAPCO Reporting

In addition to employment-related information, Section 288.99(8)(a), Florida Statutes, requires that on an annual basis, on or before January 31, each certified capital company shall file with the OFR and the OTTED, in consultation with the OFR, on a form prescribed by OTTED, for each calendar year:

- The total dollar amount the certified capital company received from certified investors, the identity of the certified investors, and the amount received from each certified investor during the immediately preceding calendar year.
- The total dollar amount the certified capital company invested and the amount invested in qualified businesses,¹ together with the identity and location of those businesses and the amount invested in each qualified business during the immediately preceding calendar year.

Although the statute requires that the CAPCOs provide a detailed report relative to the use of CAPCO moneys invested, the statute does not require that the CAPCOs include in the above-described report CAPCO moneys used for other purposes. Section 288.99(3)(l), Florida Statutes, authorizes the use of up to 50 percent of the CAPCO moneys for purposes other than acquisition of investments in qualified businesses. For example, CAPCO moneys may be used to pay reasonable costs and expenses of forming and syndicating the CAPCO, including any payments made over time for obligations incurred at the time of

¹ Section 288.99(3)(j), Florida Statutes, defines “qualified business” as a business that: (1) is headquartered in Florida, its principal business operations are located in Florida, or at least 75 percent of its employees are employed in Florida; (2) is involved in manufacturing, processing, or assembling products, conducting research and development, or providing services; (3) is unable to obtain conventional financing; (4) has a business plan that projects that the business is reasonably expected to achieve in excess of \$25 million in sales revenue within 5 years, or the business is located in a designated Front Porch community, enterprise zone, urban high crime area, rural job tax credit county, or nationally recognized historic district; (5) will maintain its headquarters in Florida for the next ten years; and (6) has fewer than 200 employees. Qualified businesses cannot be a business predominantly engaged in real estate, insurance, banking, lending, or oil and gas exploration, or professional services provided by accountants, lawyers, or physicians.

receipt of certified capital, reasonable costs of managing and operating the CAPCO, not to exceed 5 percent of the certified capital in any one year, reasonable and necessary fees in accordance with industry custom for professional services, and any projected increase in Federal or State taxes.

The following table shows as of December 31, 2003, the amounts reported by the CAPCOs in accordance with Section 288.99(8)(a), Florida Statutes, and the amounts not subject to statutory reporting requirements.

Amounts Reported Pursuant to Section 288.99, Florida Statutes:	
Total Certified Capital Received by CAPCOs	\$ 150,000,000
Investments in Qualified Businesses (cost)	(83,047,984)
Investments in Other Than Qualified Businesses (cost)	(15,108,533)
Remaining Certified Capital not Subject to Statutory Reporting	\$ 51,843,483

Source: CAPCO Annual Reports

While it is not our intent to suggest that the CAPCOs have failed to properly account for moneys provided under the CAPCO Act or to suggest that the moneys have been used by the CAPCOs in a manner not authorized by law, there is a need for the amendment of the statutory reporting requirements in order to facilitate full disclosure of the usage of the moneys. Should the reporting requirements be expanded, the statute should also be amended to require OFR verification of the amounts reported.

Recommendation: We recommend that the Legislature amend Section 288.99(8)(a), Florida Statutes, to require an accounting for all CAPCO moneys received and that Section 288.99(10), Florida Statutes, be amended to require that the OFR, as part of its annual reviews of the CAPCOs, verify the amounts reported.

Finding No. 2: CAPCO Reviews

Section 288.99(10)(a), Florida Statutes, requires the OFR to conduct an annual review to determine if the certified capital company is abiding by the requirements of certification, to advise the certified capital company as to the eligibility status of its qualified investments, and to ensure that no investment has been made in violation of the Certified Capital Company Act.

As the reviews for the 2003 year had not been finalized at the time of our audit, we requested from OFR personnel the three CAPCO review reports and working papers supporting procedures performed and conclusions reached for the 2002 annual reviews for each of the three CAPCOs. The OFR provided us with a document entitled “Annual On-Site Review for Year Ending December 31, 2002,” for each of the three CAPCOs. These documents provided various information concerning each CAPCO, such as CAPCO organization information, information related to certified capital, descriptions of bank records maintained, and descriptions of investment and distribution activity. However, these documents did not contain any reference to the three required determinations described in Section 288.99(10)(a), Florida Statutes. Also, “Annual On-Site Review for Year Ending December 31, 2002,” reports were not dated or signed.

In addition to the “Annual On-Site Review for Year Ending December 31, 2002,” a letter from the OFR was sent to each CAPCO to advise it of the results of the annual review. This letter to each CAPCO addressed the three determination requirements of Section 288.99(10)(a), Florida Statutes, in addition to other financial information related to certified capital received and its distribution. The letter contained wording stating that the OFR had determined that for the year ending December 31, 2002, the CAPCO was in compliance with the Certified Capital Company Act.

Documentation provided by the OFR in support of the procedures performed and conclusions reached

consisted only of copies of some documents described in the document “Annual On-Site Review for Year Ending December 31, 2002.” There was generally no documentation describing the nature, timing, or extent of the verification procedures performed or explanations to show how conclusions were reached.

Further inquiry disclosed that the OFR had not implemented formal written policies and procedures to govern the conduct of the CAPCO annual reviews. The absence of written policies and procedures contributed to the failure to properly document the nature, timing, and extent of the work performed.

We were advised that standard operating procedures for CAPCO examinations are under development.

Recommendation: We recommend that the OFR complete the development of standard operating procedures that will result in a documented determination of compliance and take steps to ensure that the procedures are appropriately implemented by examination staff.

Regulation of Financial Institutions

Section 655.045(1)(a), Florida Statutes, requires the OFR to conduct examinations of the condition of each State financial institution during each 18-month period unless reliance is placed on an examination performed by an appropriate Federal regulator or insuring or guaranteeing corporation or agency. However, at least once during each 36-month period, the OFR is required to conduct an examination of each State financial institution in such a manner as to allow the preparation of a complete examination report.

During the audit period, the OFR completed 234 bank or credit union examinations. The OFR was responsible for regulating 108 credit unions, 189 banks, 51 foreign banks, and 18 trust companies with total assets exceeding \$67.5 billion.

Finding No. 3: Examinations of Banks

Our review of a total of 15 bank examinations performed by the Tampa, Orlando, and Tallahassee OFR Regional Offices (5 from each office) disclosed that the OFR had established reasonable methodologies for conducting these examinations and that examiners had generally complied with these methodologies during the conduct of their examinations.

Regulation of Securities

Section 517.12(1), Florida Statutes, provides that no dealer, associated person, or issuer of securities shall sell or offer for sale any securities in or from offices in this State, or sell securities to persons in this State from offices outside of this State, by mail or otherwise, unless the person has been registered with the OFR. Section 517.121(2), Florida Statutes, requires the OFR to examine the affairs and books and records of each registered dealer, investment adviser, branch office, or associated person.

Finding No. 4: Registration of Securities Entities

Florida law and OFR administrative rules govern registration eligibility requirements for securities dealers, investment advisers, branch offices, and associated persons. Generally, the law and rules require that applications contain information and supporting documents establishing a basis for determining the identity and background of the applicant and the applicant’s qualifications for registration. Applications are submitted to the OFR electronically through the Central Registration Depository System or by hard copy.

The OFR’s Bureau of Regulatory Review is responsible for reviewing all applications to conduct business as a financial service company or securities firm, reviewing registration applications for individuals, and imposing registration restrictions or denying registration based on the findings of the

application review. During the audit period, the OFR received 64,740 electronic applications and 4,106 hard copy applications.

Once an application has been received and an applicant has been approved for registration, a supervisory evaluation of such determination should be conducted to ensure the application was processed according to OFR policies and procedures. Such supervisory evaluations could take the form of a review of the processing of each application, or considering the volume of the registration applications processed, a periodic review of a sample of the applications processed by each analyst.

Our audit disclosed that, while a supervisory review of an application may be conducted if the OFR analyst develops concerns regarding disclosed disciplinary actions, supervisory evaluations are not conducted of other applications. OFR personnel did indicate that several times a year, the supervisor conducts an evaluation of a sample of applications approved by OFR analysts to verify that the OFR policies and procedures were followed. However, the OFR had not adopted written procedures requiring these evaluations and describing their frequency or scope, and to the extent that the evaluations were done, they were not documented.

The results of our tests of applications approved by the OFR analysts did not indicate that, with respect to the tested applications, the OFR had approved unqualified applicants for registration. However, the absence of documented supervisory evaluations of analysts’ decisions to approve applications increases the risk that the OFR may issue a securities permit to an applicant that does not meet established eligibility requirements for registration.

Recommendation: We recommend that the OFR adopt procedures which require periodic supervisory evaluations of a sample of applications. The procedures should describe the frequency and scope of the evaluations and the means to be used to document and communicate the results of the evaluations.

Finding No. 5: Examinations of Securities Entities

The OFR periodically conducts examinations of securities entities (registered dealers, investment advisers, branch offices, or associated persons) as required by Sections 517.121 and 517.201, Florida Statutes. During the audit period, the OFR conducted 137 examinations of securities entities.

Procedures for conducting examinations are contained in an electronic examination module, which is a computer-based, standardized examination tool used to ensure that examinations of securities entities are conducted in a uniform manner and in a manner that achieves the examination objectives established by management. Examination modules were first put into use in 2001 and have been periodically updated. In February 2003, OFR staff met to disseminate a new policy requiring the use of electronic examination modules by all examiners.

We reviewed ten examinations (five conducted by the Tampa Regional Office, and five conducted by the Orlando Regional Office) conducted during the period February 2003 through January 2004. Of the ten examinations reviewed, two were not conducted using the then most current version of the examination module. In one of the two instances, an undated version of an Investment Adviser Examination Outline was used when the 2002 Investment Adviser Examination Module should have been used. In the other instance, a 2001 Branch Office Examination Module was used when the 2002 Branch Office Examination Module should have been used.

The failure to use the appropriate examination module may lead to the conduct of examinations which do not, in scope, adequately address applicable laws and rules.

Recommendation: We recommend that the OFR adopt procedures to ensure that all examiners use the most current examination procedures adopted by management.

OBJECTIVES, SCOPE, AND METHODOLOGY

Objectives of the audit were:

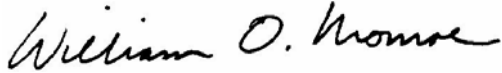
- To evaluate the OFR’s efficiency and effectiveness of regulation and oversight of financial institutions, securities entities, and certified capital companies.
- To evaluate selected internal controls relevant to the OFR’s regulatory functions.
- To evaluate the extent to which the OFR has complied with significant governing laws.
- To identify statutory changes that may be recommended to the Legislature.

The scope of this audit focused on the OFR’s regulation of financial institutions, securities entities, and certified capital companies.

In conducting our audit, we interviewed OFR personnel, observed selected operations, tested selected OFR records, and completed various analyses and other procedures. Our audit included examinations of various documents (as well as events and conditions) applicable to the period January 7, 2003, though February 29, 2004.

AUTHORITY

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.



William O. Monroe, CPA
Auditor General

OFFICE'S RESPONSE

In a letter dated September 17, 2004, the Commissioner of the Office of Financial Regulation provided responses to our preliminary and tentative findings. This letter is included in its entirety at the end of this report.

To promote accountability in government and improvement in government operations, the Auditor General makes operational audits of selected programs, activities, and functions of State agencies. This operational audit was made in accordance with applicable *Government Auditing Standards* issued by the Comptroller General of the United States. This audit was conducted by Joe D. Dykes, CPA, Bob Gay, CPA, and Melisa B. Hevey, and supervised by Don Reeder, Jr., CPA, Audit Coordinator. Please address inquiries regarding this report to Don Hancock, CPA, Audit Manager, via email at donhancock@aud.state.fl.us or by telephone at (850) 487-9037.

This report, as well as other audit reports prepared by the Auditor General, can be obtained on our Web site (<http://www.state.fl.us/audgen>); by telephone (850) 487-9024; or by mail at G74 Claude Pepper Building, 111 West Madison Street, Tallahassee, Florida 32399-1450.

Exhibit A
Office of Financial Regulation
Certified Capital Companies
Investments in Qualified Businesses
As of December 31, 2003

Qualified Business Name	Total Invested (at cost)	Business Description	Initial Positions	12/31/2003 Positions
AquaGene, LLC	\$ 542,617	Manufacturer of proteins for medicine	3	0
Authen Tec, Inc.	7,078,571	Fingerprint image processing	36	52
Automated Fuel Technologies, Inc.	7,600,000	Vehicle fleet management systems	0	4
Automated Merchant Services, Inc.	2,000,000	Credit card processing sales	16	16
Control Center, LLC	4,105,882	Design and engineering for power generation market	73	28
Copharos, Inc.	1,000,000	Cancer diagnostic and therapeutic technology	1	0
Cylex Systems, Inc.	1,771,099	Document management application service	17	12
Audience Bank/Desktop Dollars, Inc.	2,000,000	Digital media	8	0
Distribution Video & Audio, Inc.	1,200,000	Distribution of video and audio entertainment products via the internet	24	35
Down to Earth Distribution, LLC	580,000	Distribution of fertilizers and pesticides	0	0
eAngler, Inc.	750,000	Internet portal for fishermen	32	7
Electronic Data Resources	1,000,000	Electronic processing of credit cards	17	30
EmailChannel, Inc.	1,600,000	Infomediary between email marketers and consumers	12	0
Entomos, LLC	3,553,945	Production of beneficial insects and other natural agents for control of pests	8	3
Fortress Technologies, Inc.	500,000	Internet communications	36	55
Global Small Business Services, LLC	3,550,000	Customer relationship management sales	0	1
Group Management Technologies, LLC	635,000	Bookkeeping, outsourced small business services	0	8
Image-Guided Neurologics, Inc.	2,700,000	Minimally-invasive neurological access	25	25
Intelligent Machine Concepts, LLC	7,575,000	Development of automated optical inspections systems	10	0
In.vision Research Corp.	1,800,000	E-business infrastructure software	36	27
Knowledge View, Inc., now PCHowTo, Inc.	5,725,000	Multimedia content for e-learning, e-help, and e-marketing applications	160	21
LaserTech USA, LLC	1,000,000	Laser welding and seam tracking technology	3	0
Merchant Data Systems, Sales & Marketing, LLC	3,500,000	Credit and debit card processing	0	0
Merchant Data Systems, LLC	1,400,000	Credit, debit, and check processing	10	0
Nichedirectories, LLC	1,344,000	Directory services, website development	8	9
Payformance Corporation	750,000	Business-to-business payment automation systems	70	76
Pilgrim Software	2,150,000	Software and business process improvement solutions to manufacturers	85	89
PTG Precision Technology Center, ACA/Precision Technologies	5,392,500	Glass technology with lasers	32	0
Silver Tray Cookies, Inc.	900,000	Cookie manufacturer	28	28
Starphire Technologies, LLC	2,400,000	Software developer	0	2
Transworld Business Brokers, LLC	4,090,000	Business brokerage	12	34
Xytrans, Inc.	454,370	Manufacturer of wave transceivers used in broadband and wireless communications	0	30
Twin Vee Marine Group, Inc.	2,400,000	Manufacturer of catamaran boats	58	66
Total	\$ 83,047,984		820	658

Source: CAPCO Annual Reports



OFFICE OF FINANCIAL REGULATION

DON B. SAXON
COMMISSIONER

FINANCIAL
SERVICES
COMMISSION

JEB BUSH
GOVERNOR

TOM GALLAGHER
CHIEF FINANCIAL OFFICER

CHARLIE CRIST
ATTORNEY GENERAL

CHARLES BRONSON
COMMISSIONER OF
AGRICULTURE

September 17, 2004

Mr. William O. Monroe
Auditor General
G74 Claude Pepper Building
111 West Madison Street
Tallahassee, Florida 32399-1450

Dear Mr. Monroe:

Enclosed is the Office's response to the preliminary and tentative audit findings for the audit of Regulation of Financial Institutions, Securities, and Certified Capital Companies.

If you have any questions, please contact Inspector General Bob Dyar at 410-9712.

Sincerely,

Don B. Saxon
Commissioner

Enclosure

Office of Financial Regulation**Preliminary and Tentative Findings
Regulation of Financial Institutions, Securities, and
Certified Capital Companies**

Finding # 1: Although Section 288.99(8)(a), Florida Statutes, requires that certified capital companies (CAPCOs) provide a detailed report relative to the use of CAPCO moneys invested, the statute does not require the CAPCOs to report how other State-provided CAPCO moneys were used. As a consequence, the CAPCOs were not required to describe in annual reports how approximately \$52 million in State-provided CAPCO moneys had been used. While it is not our intent to suggest that the CAPCOs have failed to properly account for moneys provided under the CAPCO Act; or, to suggest that the moneys have been used by the CAPCOs in a manner not authorized by law, there is a need for the amendment of the statutory reporting requirements to facilitate full disclosure of the usage of State moneys.

Recommendation: We recommend that the Legislation amend Section 288.99(8)(a), Florida Statutes, to require an accounting for all CAPCO moneys received, and that Section 288.99(10), Florida Statutes, be amended to require that the OFR, as part of its annual reviews of the CAPCOs, verify the amounts reported.

Auditee Response: The Office concurs that all entities receiving state funds should be held accountable for the use of those funds through annual reporting requirements. CAPCOs are required by Section 288.99(4)(g) to submit audited financial statements to the OFR by April 30 of each year. These financial statements provide disclosure of many of the expenses addressed in the finding (e.g., management fees, professional fees, etc.). The OFR, the Department of Revenue, and the Office of Tourism, Trade, and Economic Development concurrently regulate CAPCOs. Any changes to regulatory requirements would require coordination between the aforementioned agencies. A "rule change" may be a more suitable and expeditious approach to accomplishing this, if appropriate rulemaking authority exists. The OFR will review options to pursue full disclosure and usage of State moneys.

Finding # 2: Section 288.99(10)(a), Florida Statutes, requires the OFR to conduct annual reviews of certified capital companies. The OFR had not implemented written policies and procedures to govern the conduct of the CAPCO annual reviews, and the absence of written policies and procedures contributed to the OFR's failure to properly document the nature, timing, and extent of the work performed.

Recommendation: We recommend that the OFR complete the development of standard operating procedures that will result in a documented determination of compliance, and take steps to ensure that the procedures are appropriately implemented by examination staff.

Auditee Response: Concur. Standard operating procedures have been documented and were implemented for the annual reviews conducted during second quarter 2004 for the year ending December 31, 2003. These procedures were provided to the Auditor General's staff prior to the completion of the audit.

Preliminary and Tentative Findings
Regulation of Financial Institutions, Securities, and
Certified Capital Companies
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Finding # 4: Applications for securities entities (securities dealers, investment advisers, branch offices, and associated persons) are submitted to the OFR for processing and review. Our audit disclosed that, while a supervisory review of an application may be conducted if an OFR analyst develops concerns regarding disclosed disciplinary actions, supervisory evaluations are not conducted for other applications. The OFR had not adopted written procedures requiring supervisory reviews of a sample of applications, nor were the evaluations that were conducted, documented.

Recommendation: We recommend that the OFR adopt procedures that require periodic, supervisory evaluations of a sample of applications. The procedures should describe the frequency and scope of the evaluations, and the means to be used to document and communicate the results of the evaluation.

Auditee Response: Concur. The Office will amend procedures to document the requirement for a periodic review of a sampling of applications to ensure that the criteria for licensure have been met. Appropriate sample size, based on the volume of applications and the experience of the individual Analyst, will be established in the procedures.

Finding # 5: The OFR uses electronic examination modules to guide the conduct of examinations of securities entities. Two of the ten securities examinations reviewed were not conducted with the most current version of the examination module.

Recommendation: We recommend that the OFR adopt procedures to ensure that all examiners use the most current examination procedures adopted by management.

Auditee Response: Concur. Examination staff is currently utilizing the 2003 Edition of the Examination Modules. The Office will develop written procedures to instruct staff on the proper use of the modules. Recent review by OFR management of examination reports and supporting documentation has confirmed the use of the updated modules.

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