



AUDITOR GENERAL

WILLIAM O. MONROE, CPA



DEPARTMENT OF FINANCIAL SERVICES

REVENUE PROCESSING

AND

FINGERPRINTING CONTRACT

Operational Audit

SUMMARY

This operational audit, covering the period March 1, 2004, through February 28, 2006, and selected actions taken through June 30, 2006, focused on the Department of Financial Services' centralized revenue receipting process. Our operational audit also included a review of a contract between the Department of Financial Services and the Gadsden County District School Board, involving the processing of fingerprint cards.

Finding No. 1: Internal controls relating to the collection and processing of revenues could be improved.

Finding No. 2: The Department did not maintain a control log to track the receipt, status, and disposition of debit memorandums.

Finding No. 3: Department records did not explain the basis for the award of a fingerprint card processing contract to Gadsden County District School Board. The contracting approach employed by the Department resulted in the selection of the primary service providers through other than competitive processes.

FINDINGS AND RECOMMENDATIONS

Revenue Collections

The Department of Insurance and the Department of Banking and Finance were merged on January 7, 2003, into a newly created Department of Financial Services

(Department), headed by the State's Chief Financial Officer.

The same legislation that created the Department also created the Financial Services Commission (Commission), consisting of the Governor, the Chief Financial Officer, the Attorney General, and the Commissioner of Agriculture. The Commission is responsible for the operations of the Office of Insurance Regulation and the Office of Financial Regulation. Both Offices obtain administrative services, including the processing of collections, from the Department.

The Department's Receipts Section is responsible for the processing of cash receipts. According to Department records, the Receipts Section collected and processed approximately \$834 million during the fiscal year ended June 30, 2005.

Finding No. 1: Receipt Processing

As indicated above, the Receipts Section collected and processed \$834 million during the 2004-05 fiscal year. Our review of related internal controls in place in February 2006 disclosed the following:

- Mail containing collections was initially handled and opened by the Department's Mail Center. The Mail Center did not prepare a listing or log of payments received at the time of the initial point of receipt for subsequent

independent reconciliation to the amounts ultimately processed and deposited. We also noted that the checks received were not restrictively endorsed until after the Mail Center transferred the collections to other Department units.

- Department records show that the Receipts Section collected and processed for the Office of Financial Regulation approximately \$36 million during the fiscal year ended June 30, 2005. Our audit disclosed that, when processing Office of Financial Regulation receipts, the Receipts Section had assigned to one employee the incompatible duties of handling the moneys received, recording the receipt transactions, and verifying the recording of the transactions. Specifically, we found that an employee in the Receipts Section recorded each collection into the Receipt Processing System, stamped validation numbers on the back of each check, ran a control tape of the checks, and reconciled the control tape total to a total of the collections previously recorded in the Receipt Processing System. This same employee then bundled together the documentation as support for the preparation of a deposit slip.

The absence of a listing from the Mail Center and the lack of immediate restrictive endorsement of checks, coupled with improper separation of revenue processing duties, increases the likelihood that errors, should they occur, may go undetected.

A report issued on May 14, 2004, by the Department's Inspector General cited similar concerns.

Recommendation: We recommend that the Department implement procedures to record and restrictively endorse all receipts at the initial point of receipt in the Mail Center. We also recommend the Department take actions to appropriately separate the duties relating to the recording, custody, and reconciliation of the receipts processed by the Receipts Section.

Finding No. 2: Debit Memorandums

The Division of Treasury initiates debit memorandums which, when related to the Department's operations, are forwarded to the Department's Receipts Section for further processing. Debit memorandums are used as the basis for adjusting the State's accounting and

licensing records when, for example, checks are returned from previously recorded receipts because of nonsufficient funds, a closed checking account, or the execution of a stop payment.

The Receipts Section is responsible for controlling the Department's activities relating to returned checks. As the receipt of a returned check can also affect the status of a corresponding license record, the Receipts Section is responsible for initiating the adjustment of related licensing records. When necessary, the Receipts Section is also responsible for pursuing any collection efforts.

Department records indicate that for the period January 1, 2005, through February 28, 2006, the Receipts Section received approximately 900 debit memorandums for returned checks totaling approximately \$220,000.

Our audit of the Department's procedures and controls over debit memorandums, including the testing of 20 returned check transactions disclosed:

- The Receipts Section controlled the processing and disposition of debit memorandums through the use of a manual filing system in which pending debit memorandums were filed until final disposition. However, no control log was maintained to track the receipt, status, and final disposition of the debit memorandums. The absence of such a log may increase the risk of a debit memorandum transaction not being fully pursued or processed. For example:
 - Our audit tests of 20 returned check transactions disclosed a license record from the Division of Workers' Compensation that was not properly updated to reflect the returned check. The effects of returned checks on the various regulatory area's licensing systems were not periodically reconciled to an independently maintained set of records, such as a debit memo control log. Had a central log existed the record deficiency noted above would have had a greater possibility of a timely detection.
 - Department procedures required the Receipts Section to perform certain collection efforts, including the mailing of

collection letters, for applicable returned checks. Our audit tests of the collection efforts taken relative to the 20 returned checks disclosed that for one returned check totaling \$150 and received on September 13, 2005, the Receipts Section was unable to provide a copy of a collection letter. A control log would have provided a basis for more closely monitoring the status of collection efforts.

- Although debit memorandums result in moneys being owed to the Department, the Department does not currently recognize in its accounting records a receivable balance for related amounts due.

We recommend:

- **The Department implement a control log to track the receipt, status, and disposition of each debit memorandum and adopt procedures requiring the dissemination of the applicable portions of the control log to respective regulatory offices so that the control log’s activity can be reconciled to the information shown by the respective licensing systems.**
- **The Department implement procedures for recording receivable balances for amounts due from uncollected debit memorandums.**

Other Matters

Finding No. 3: Gadsden County District School Board Fingerprinting Contract

Our audit disclosed that, in late 2002, the Department (at the time, the Department of Insurance) entered into a noncompetitively awarded contract with the Gadsden County District School Board (DSB) for the period December 1, 2002, through November 30, 2003. Under the contract, the DSB was to scan and digitally process fingerprint cards submitted to the Department by insurance agents, adjusters, companies, and other entities. Automatic contract renewals have extended the term of the contract through June 30, 2006. Through the life of the contract, the Department had paid over \$5 million to the DSB. Approximately \$60,000 of this amount was retained by the DSB for processing invoices, while the remaining portion was

paid to DSB-engaged subcontractors which provided the substantive fingerprint processing services required under the contract.

Our review of the contract and its award disclosed the following:

- In support of the selection of the DSB as the contractor for fingerprinting services, Department records should contain evidence that the Department had determined, based on an evaluation of the DSB’s authority, facilities, past performance, and other criteria, the DSB had the capacity to efficiently, effectively, and economically provide the desired services. Department records contained no such evidence, and it appeared from the terms of the contract that the DSB’s provision of the services through the hiring of subcontractors had been anticipated. The services ultimately rendered by the DSB were limited to the invoicing of the Department, the receipt and deposit of related Department remittances, and the preparation of checks to compensate subcontractors. With respect to the DSB’s legal capacity, as discussed in several of our previous reports on the audit of the DSB, it was not clear that the DSB had legal authority to enter into the contract with the Department.¹
- Although the contract authorized the DSB to subcontract any of the required services, the contract did not include a provision requiring the DSB to use competitive procurement practices when selecting subcontractors. The inclusion of such terms more reasonably ensures that the benefits of competition are received by all stakeholders, including the State.
- Under the laws governing the Department’s purchasing activities (Chapter 287, Florida Statutes), contracts may be awarded to other governmental entities without the employment of competitive processes. However, when competitive processes are not used and the procurement costs more than \$25,000, Section 287.057(20), Florida Statutes, requires that the individuals taking part in the development or selection of criteria for evaluation, the evaluation process, and the award process, attest that they are independent of, and have no conflict of interest in, the entities evaluated and selected. Department personnel have

¹ Auditor General’s Audit Report Nos. 2004-153, 2005-163, and 2006-148.

represented that no written attestations of independence were made for this procurement contract. The lack of these attestations precludes the Department from providing written assurances that the selection process leading to the DSB contract was fair, impartial, and in the best interests of the public.

The contract was not renewed by the Department after the terms of the most recent renewal expired on June 30, 2006.

Recommendation: We recommend:

- **Department files relating to the noncompetitive selection and engagement of contractors always contain information identifying the criteria used to select contractors, and as required by Section 287.057(20), Florida Statutes, attestations as to the independence and absence of conflicts of interest on the part of those individuals involved in the contracting process.**
- **Contract terms authorizing the use of subcontractors require the use of competitive processes in selecting contractors.**

OBJECTIVES, SCOPE, AND METHODOLOGY

The objectives of this audit were:

- To evaluate the effectiveness of key centralized revenue receiving controls.

- To obtain an understanding of processes used by the Department to award a fingerprinting contract to Gadsden County District School Board and to review the contract terms for sufficiency and compliance with applicable Florida Statutes.

For each of the audit objectives stated above, our understanding of applicable processes was gained by reviewing agency policies and procedures, interviewing personnel, observing processes, and reviewing other applicable documentation. To meet our audit objectives for our audit of the centralized revenue receipting function, we performed audit tests of selected receipt transactions and debit memorandums. Our operational audit covered the period March 1, 2004, through February 28, 2006, and selected actions taken through June 30, 2006.

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

William O. Monroe, CPA
Auditor General

MANAGEMENT RESPONSE

In a letter dated November 29, 2006, the Treasurer provided responses to our findings. The letter is included in its entirety at the end of this report as Appendix A.

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 conducted in accordance with applicable Generally Accepted Government Auditing Standards. This audit was conducted by Chris Stanisci, CPA, and Matthew Tracy, CPA, and was supervised by Frank T. Belt, CPA. Please address inquiries regarding this report to Kathryn D. Walker, CPA, Audit Manager, via e-mail at kathrynwalker@state.fl.us or by telephone at (850) 487-9085.

This report and other audit reports prepared by the Auditor General can be obtained on our Web site. This report and 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 (G74 Claude Pepper Building, 111 West Madison Street, Tallahassee, Florida 32399-1450).

APPENDIX A
MANAGEMENT RESPONSE



CHIEF FINANCIAL OFFICER
STATE OF FLORIDA

TOM GALLAGHER

November 29, 2006

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

Dear Mr. Monroe:

Pursuant to Section 11.45(4)(d), Florida Statutes, the enclosed response is provided for the preliminary and tentative findings and recommendations included in the Auditor General's Operational Audit of the Revenue Processing and Fingerprinting Contract.

If you have any questions or would like to discuss the matter further, please contact David Harlan, Inspector General at (850) 413-4960.

Sincerely,

A handwritten signature in black ink that reads "Tom Gallagher".

Tom Gallagher

TG:Hc

Enclosure

APPENDIX A
MANAGEMENT RESPONSE (CONTINUED)

**Florida Department of Financial Services
Revenue Processing and Fingerprinting Contract
Operational Audit
Preliminary and Tentative Audit Findings**

Finding No. 1: Receipt Processing: Internal controls relating to the collection and processing of revenues could be improved.

Recommendation: We recommend that the Department implement procedures to record and restrictively endorse all receipts at the initial point of receipt in the Mail Center. We also recommend the Department take actions to appropriately separate the duties relating to the recording, custody, and reconciliation of the receipts processed by the Receipts Section.

Response: We concur and have implemented the following procedure. Mail room staff will open all general delivery mail, separate and endorse all remittances, and complete a receipts tracking sheet for delivery of the checks to the Receipts Section which will indicate the number of checks attached. Upon receipt, the Receipts Section will confirm the count and retain the tracking sheet. After the validation process, the Receipts Section will reconcile the number of checks received to the number deposited. Regarding the appropriate separation of duties in the Receipts Section, we have implemented a procedure so that one employee will receive, code and bundle incoming receipts, another will process the receipts and prepare the deposit and a third employee will verify the deposit.

Finding No. 2: Debit Memorandums: The Department did not maintain a control log to track the receipt, status, and disposition of debit memorandums.

Recommendation: We recommend that the Department implement a control log to track the receipt, status, and disposition of each debit memorandum and adopt procedures requiring the dissemination of the applicable portions of the control log to respective regulatory offices so that the control log's activity can be reconciled to the information shown by the respective licensing systems. We also recommend that the Department implement procedures for recording receivable balances for amounts due from uncollected debit memorandums.

Response: We concur and have implemented a procedure to track all returned items through our bad check database. A monthly report will be sent to each business area indicating the current status of all returned items. This database will provide all information necessary to appropriately record an accounts receivable for the uncollected items.

Finding No. 3: Gadsden County District School Board Fingerprinting Contract: Department records did not explain the basis for the award of a fingerprint card processing contract to Gadsden County District School Board. The contracting approach

**APPENDIX A
MANAGEMENT RESPONSE (CONTINUED)**

employed by the Department resulted in the selection of the primary service providers through other than competitive processes.

Recommendation: We recommend that the Department files relating to the noncompetitive selection and engagement of contractors always contain information identifying the criteria used to select contractors, and as required by Section 287.057(20), Florida Statutes, attestations as to the independence and absence of conflicts of interest on the part of those individuals involved in the contracting process. We also recommend contract terms authorizing the use of subcontractors require the use of competitive processes in selecting contractors.

Response: We concur and will ensure procurement files for noncompetitive contractor selection contain appropriate criteria for the selected vendor. We will also ensure procurement files contain appropriate attestations as to the independence of those individuals involved in the contracting process. By contract terms we will require that, in selecting subcontractors, a governmental unit must follow their own procurement rules, and that the department will have prior approval authority before subcontractors are selected.

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