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We have completed an audit of the Real Estate Division. This audit is part of the ongoing program of the Legislative Auditor as authorized by the Legislative Commission. The purpose of legislative audits is to improve state government by providing the Legislature, state officials, and Nevada citizens with independent and reliable information about the operations of state agencies, programs, activities, and functions. The results of our audit, including findings, conclusions, recommendations, and the Division's response, are presented in this report.

We wish to express our appreciation to the management and staff of the Real Estate Division for their assistance during the audit.

Respectfully presented,

Paul V. Townsend, CPA
Legislative Auditor

October 13, 2009
Carson City, Nevada

STATE OF NEVADA
DEPARTMENT OF BUSINESS AND INDUSTRY
REAL ESTATE DIVISION

AUDIT REPORT

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EXECUTIVE SUMMARY

DEPARTMENT OF BUSINESS AND INDUSTRY REAL ESTATE DIVISION

Background

The Real Estate Division's mission is to safeguard and promote public interest in real estate transactions by developing an informed public and a professional real estate industry. The Division carries out the statutory duties of administration and enforcement of laws and regulations governing real estate licensees, appraisers of real estate, timeshare agents and representatives, property managers, community association managers, and inspectors of structures. In addition, the Division regulates the subdivision of land, timeshare development and sales, campground sales, and common-interest community associations.

The Division works closely with three commissions: the Commission of Appraisers of Real Estate (Appraisal Commission), Real Estate Commission, and Commission for Common-Interest Communities and Condominium Hotels. These bodies conduct disciplinary hearings, adopt regulations, approve education courses, and advise the Division. Each commission consists of five Governor-appointed members.

The Division has offices in Carson City and Las Vegas. For fiscal year 2009, the agency was authorized for 57 positions. The Division administers four budget accounts, funded primarily through fees and a general fund appropriation. The agency received approximately $8.9 million in revenues during fiscal year 2009 and expenditures totaled about $4.7 million.

Purpose

The purpose of this audit was to evaluate the Division's financial and administrative practices, including whether activities were carried out in accordance with applicable state laws, regulations, policies, and procedures. This audit focused on the Division's financial and administrative activities for calendar year 2008, and included activities through May 2009 for certain areas.

Results in Brief

The Real Estate Division continues to have difficulty controlling certain financial and administrative activities. Although policies and procedures were developed to address weaknesses reported in our prior audits, the Division has been unable to sustain the implementation of controls related to accounts receivable and revenues. Specifically, the Division did not actively pursue the collection of fines, accounts receivable records were not adequate, and receivables were not properly reported to the State Controller. In addition, the Division continues to have problems depositing payments timely and verifying payments were deposited. Also, investigations of appraiser and real estate complaints were not completed timely. Finally, better controls are needed to ensure information technology vulnerabilities are reduced, and certain administrative activities are performed when required.

Principal Findings

- The collection of disciplinary fines was not actively pursued by the commissions and Division staff. Of 19 large fines totaling $808,620, the Division collected only $40,600 (5%) on 2 fines. The commissions gave violators long periods of time before their fines were due. In addition, Division staff did not send past due collection letters for more than 9 months, on average, after violators failed to pay. The total elapsed time from the commissions' hearing to the date collection letters were sent averaged more than 1.5 years for the fines we tested. Furthermore, staff did not submit delinquent fines to the State Controller for outside collections. Similar problems regarding collection activities were reported in our 2000 audit of the Division. (page 9)

- The Division did not maintain adequate accounts receivable information that meets requirements established by the State Controller. Although staff recorded fines receivable information in two separate databases, neither database could provide required information such as individual account balances, the age of accounts, or the total receivables due. Our prior 2000 audit report cited similar problems with incomplete and inaccurate accounts receivable information. (page 11)

- The Division did not properly report accounts receivable to the State Controller or consider delinquent accounts for bad debt write off. For example, the Division incorrectly included about $2 million in its June 30, 2008, accounts receivable report. It also failed to notify the State Controller of about $2.6 million in receivables for the quarter ended December 31, 2008. In addition, old accounts totaling over $1.6 million were included in the Division's active accounts receivable listing. When receivables are not correctly reported and uncollectible accounts are not written off, accurate information is not available regarding debts owed to the State. (page 12)

- Adequate controls have not been established over payments received. Control weaknesses include not depositing payments timely, and not verifying payments were properly deposited. For instance, 124 of 306 (41%) payments tested were not deposited timely. This includes 23 payments held more than 30 days. NRS requires agencies deposit revenues by Thursday of each week for all money received during the previous week. Our prior 2000 audit noted similar problems with untimely deposits. (page 14)

- The Division did not investigate appraiser complaints timely. Of 24 appraiser complaints tested, 10 cases remained open an average of 552 days as of May 2009. In addition, the Division took an average of 580 days to resolve and close 14 cases. Some of the complaint cases involved serious allegations of inflated appraisals that overvalued residential properties. The likelihood of foreclosure increases when a home is overvalued and the house is worth less than the loan. Complaints were not resolved timely because the Division had difficulty managing available resources for appraiser complaint investigations. These resources include three staff and outside contractors who perform appraisal case review services. (page 16)

- Real estate complaints were not always processed timely, especially when disciplinary action was required. Of 25 real estate complaints tested, 9 cases remained open, on average, for more than 1 year as of May 2009. Although staff completed most investigations timely, better monitoring is needed to identify cases that remain unresolved for excessive periods of time. (page 17)

- The Division collects and stores licensee social security numbers. According to management, the Division stores about 135,000 licensee social security numbers unencrypted in the database which is accessible to all employees. Collecting and storing unencrypted social security numbers increases the risk of identity theft. When agencies maintain this sensitive data, state IT security standards require they control access by the use of encryption software or other methods. (page 18)

- The Division did not comply with state IT security controls to ensure various network security features were maintained. Control weaknesses included computers not updated for current virus definitions, missing critical software security patches, allowing weak computer passwords, and not conducting criminal background checks on employees with access to sensitive information. (page 19)

- The Division's property and equipment records were not accurate. For instance, computer equipment, missing since 2002, was not removed from the inventory records until we started our audit. Overall, 17 of 48 assets tested had recordkeeping discrepancies. These problems occurred because the Division did not conduct annual physical inventories of property and equipment as required by its internal control procedures and state law. (page 21)

- The Division did not complete timely employee performance evaluations for 6 of 10 employees tested. Two of the employees did not receive any performance evaluations when required, and four received untimely performance evaluations. This included three evaluations that occurred after we started our audit. The untimely evaluations ranged between 16 months to 6.5 years late. Without evaluations, deficiencies in performance may not be corrected timely. (page 22)

Recommendations

This audit report contains 12 recommendations to improve the Division's fiscal and administrative practices. Seven recommendations address improving accounts receivable oversight and controls over payments received. We also made a recommendation to improve monitoring of complaint caseloads. Finally, we recommended the Division comply with state IT security requirements, maintain accurate property and equipment records, and ensure employees are evaluated as required by state law. (page 30)

Agency Response

The Division, in response to the audit report, accepted the 12 recommendations. (page 26)

Introduction

Background

The Real Estate Division's mission is to safeguard and promote public interest in real estate transactions by developing an informed public and a professional real estate industry. The Division carries out the statutory duties of administration and enforcement of laws and regulations governing real estate licensees, appraisers of real estate, timeshare agents and representatives, property managers, community association managers, and inspectors of structures. In addition, the Division regulates the subdivision of land, timeshare development and sales, campground sales, and common-interest community associations.

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The Division has offices in Carson City and Las Vegas. For fiscal year 2009, the agency was authorized for 57 positions. The Division administers four budget accounts, funded primarily through fees and a general fund appropriation. The agency received approximately $8.9 million in revenues during fiscal year 2009 and expenditures totaled about $4.7 million. Exhibit 1 shows fiscal year 2009 expenditures by budget account.

Exhibit 1

Real Estate Division Expenditures
Fiscal Year 2009

Budget Account	Amount
Real Estate Administration	$2,859,556
Common Interest Communities	1,384,375
Real Estate Education & Research	463,160
Real Estate Recovery [1]	-
Total	**$4,707,091**

Source: State accounting records.

Note: Excludes interagency transfers.

[1] Real Estate Recovery, a special revenue fund used for satisfying claims against licensees, had no expenditures during fiscal year 2009. The Division transferred $430,000 from this account to the Real Estate Education & Research account in fiscal year 2009.

Scope and Objective

This audit is part of the ongoing program of the Legislative Auditor as authorized by the Legislative Commission, and was made pursuant to the provisions of NRS 218.737 to 218.893. The Legislative Auditor conducts audits as part of the Legislature's oversight responsibility for public programs. The purpose of legislative audits is to improve state government by providing the Legislature, state officials, and Nevada citizens with independent and reliable information about the operations of state agencies, programs, activities, and functions.

This audit focused on the Division's financial and administrative activities for calendar year 2008, and included activities through May 2009 for certain areas. The objective of our audit was to evaluate the Division's financial and administrative practices, including whether activities were carried out in accordance with applicable state laws, regulations, policies, and procedures.

Findings and Recommendations

The Real Estate Division continues to have difficulty controlling certain financial and administrative activities. Although policies and procedures were developed to address weaknesses reported in our prior audits, the Division has been unable to sustain the implementation of controls related to accounts receivable and revenues. Specifically, the Division did not actively pursue the collection of fines, accounts receivable records were not adequate, and receivables were not properly reported to the State Controller. In addition, the Division continues to have problems depositing payments timely and verifying payments were deposited. Also, investigations of appraiser and real estate complaints were not completed timely. Finally, better controls are needed to ensure information technology vulnerabilities are reduced, and certain administrative activities are performed when required.

Accounts Receivable Process Needs Better Oversight

The Division needs better oversight of the accounts receivable process. For example, the Division did not make timely efforts to collect disciplinary fines, utilize debt collection services for delinquent accounts, or maintain adequate accounts receivable records. Further, the Division did not properly report receivables to the State Controller, or request approval to write off uncollectible accounts.

According to Division records, fines receivable totaled about $2.6 million at December 31, 2008. These fines were assessed by the commissions for disciplinary purposes. The Division makes recommendations to the commissions concerning fine amounts and payment terms. Both the Appraisal and Real Estate Commissions may levy fines up to $10,000 per violation. In addition, some individuals may be required to reimburse the Division for investigative costs. Collected fines are deposited into the state's general fund.

Collection of Disciplinary Fines Not Actively Pursued

The collection of disciplinary fines was not actively pursued by the commissions and Division staff. Of 19 large fines totaling $808,620, the Division collected only $40,600 (5%) on 2 fines. The commissions gave violators long periods of time before their fines were due. In addition, Division staff did not send past due collection letters for more than 9 months, on average, after violators failed to pay. The total elapsed time from the commissions' hearing to the date collection letters were sent averaged more than 1.5 years for the fines we tested. Furthermore, staff did not submit delinquent fines to the State Controller for outside collections.

We tested all fines over $10,000 ordered by the Appraisal and Real Estate Commissions between July 2006 and November 2008. Although collecting large fines is difficult, the Division needs to work with the commissions to establish timely due dates, follow internal control procedures for collecting receivables, and submit delinquent fines to the State Controller for outside collections.

<u>Prompt Payment Terms Not Required</u>

The commissions have not required prompt payment terms for disciplinary fines. On average, payments were due 9 months after the disciplinary hearing. Similarly, our prior 2000 audit noted due dates up to 2 years after the hearing and, no due dates were established in some cases. The likelihood of successful collections decreases with protracted due dates.

Most of the 19 fines we tested were between $10,000 and $30,000, but two were over $100,000. The largest fine was $250,000, due 8 months after the hearing. In that case, the commission suspended a Las Vegas broker's license for 25 years for renting out foreclosed homes to unsuspecting tenants. According to staff, the commissions consider Division recommendations for disciplinary fine amounts and payment terms.

<u>Past Due Collection Letters Not Sent Timely</u>

The Division was slow to mail past due collection letters after violators failed to pay fines by the due dates. Staff did not send collection letters for more than 9 months, on average, after the payments were past due. The 10 letters we examined were sent by staff from 194 to 444 days after the due dates. Moreover, there was no evidence staff attempted to locate addresses for five past due accounts after mail was returned undeliverable.

Collection letters are important tools for effective debt collection practices. Our prior 2000 audit reported the Division's collection practice was limited to sending violators an initial notification letter after the commissions ordered disciplinary fines. In response to our prior audit, the Division developed internal control procedures which specify collection letters are sent at 30, 60, and 90 days past due. These letters serve to remind debtors of their obligations, inform them of the consequences of nonpayment, and document the agency's collection efforts.

Delinquent Fines Not Submitted for Outside Collections

The Division did not pursue collections of delinquent fines through the State Controller's Office. None of the 12 past due accounts we tested were turned over to the State Controller for outside collections. Further, the Division last referred delinquent accounts for outside collections in February 2004, when nine debts totaling $195,759 were sent to the State Controller.

Our prior 2000 audit reported the Division took limited action to collect delinquent fines and had a poor collection rate. In response to our audit, the Division developed internal control procedures for using the State Controller for collection of delinquent accounts. These procedures require staff to send accounts delinquent more than 120 days to the State Controller for outside collections.

Authority to pursue delinquent accounts is provided by NRS Chapter 353C. During our audit, these statutes allowed agencies to request the State Controller perform debt collection services. However, in 2009, the Legislature passed AB 87 requiring the State Controller to act as the collection agent for all agencies that do not have specific debt collections statutes or have not obtained a waiver from the State Controller to engage in its own collection efforts. All such agencies are now required to turn over debts for collection to the State Controller within 60 days after the debt becomes past due. Therefore, the Division should revise its procedures for using the services of the State Controller and ensure staff comply with the new debt collection requirements.

Receivable Reports Lack Necessary Information

The Division did not maintain adequate accounts receivable information that meets requirements established by the State Controller. Although staff recorded fines receivable information in two separate databases, neither database could provide required information such as individual account balances, the age of accounts, or the total receivables due. As a result, Division management and the commissions did not have the information needed to properly oversee the collection of fines.

Receivable records were incomplete and unreliable for 9 of 19 accounts tested. Of these, four disciplinary orders totaling $96,487 were not recorded. Also, the database showed no balance due for five accounts because fines totaling $163,433 were included with other written comments that must be manually reviewed to determine the appropriate balance. Our prior 2000 audit report cited similar problems with incomplete and inaccurate accounts receivable information.

The Division's internal control procedures require staff use an accounts receivable tracking spreadsheet that meets certain requirements for reporting accounts receivable to the State Controller. Staff began taking steps to implement the accounts receivable tracking spreadsheet after our audit began.

Accounts Receivable Not Properly Reported or Written Off

The Division did not properly report accounts receivable to the State Controller or consider delinquent accounts for bad debt write off. For example, the Division incorrectly included about $2 million in its June 30, 2008, accounts receivable report. It also failed to notify the State Controller of about $2.6 million in receivables for the quarter ended December 31, 2008. In addition, old accounts totaling over $1.6 million were included in the Division's active accounts receivable listing. When receivables are not correctly reported and uncollectible accounts are not written off, accurate information is not available regarding debts owed to the State.

Reporting Requirements Not Met

The Division overreported June 30, 2008, receivables to the State Controller because the report included amounts not considered accounts receivable. Specifically, the report incorrectly included about $2 million of unpaid licenses and fees. Unpaid licenses and fees are excluded from accounts receivable because licensees may choose not to renew their licenses. Although staff indicated the Controller's Office brought the reporting error to their attention, the Division did not submit an amended report.

In addition, reports for the quarters ended September 30, and December 31, 2008, were not submitted to the State Controller. According to Division records, staff should have reported $2.6 million in fines receivable for the quarter ended December 31, 2008. The process for reporting receivables to the State Controller is relatively simple when agencies maintain accounts receivable records that meet the state's accounting requirements.

Agencies are required to submit annual and quarterly accounts receivable reports to the State Controller. NRS 353C.120 requires agencies submit periodic reports of debts owed to the agency. Further, accounting policies and procedures, issued by the State Controller's Office, require agencies report accounts receivable on a quarterly basis. In addition, the Division's internal control procedures specify receivables consist of unpaid fines and investigation cost reimbursements ordered by the three commissions.

Delinquent Accounts Not Reviewed for Bad Debt Write Off

The Division did not seek to write off bad debts for uncollectible fines receivable. As a result, the Division's $2.6 million accounts receivable balance included $1.6 million in accounts delinquent from 18 months to 13 years. Accounts receivable that cannot reasonably be expected to be collected should be written off. During our audit, the State Controller's policies and procedures required agencies to review delinquent accounts greater than 90 days for write off. Pursuant to NRS 353C.220, write offs must first be approved by the State Board of Examiners.

The Division did not sustain the implementation of our prior audit recommendation to develop policies and procedures for the write off of uncollectible accounts. Although the Division developed write off procedures, they were missing from the current internal control procedures. Consequently, we found amounts identified as uncollectible during our prior 2000 audit were still included in the Division's receivable reports.

In 2009, the Legislature passed AB 87 which transferred the responsibility for requesting a bad debt write off to the State Controller. Effective, July 1, 2009, if the State Controller determines that it is impossible or impractical to collect a debt, the Controller may request the State Board of Examiners to designate the account as a bad debt.

Recommendations

1. Work with the commissions to establish prompt payment terms for disciplinary fines.
2. Follow internal control procedures regarding timely collection efforts.
3. Revise procedures for periodic submission of delinquent accounts to the State Controller for collection action in accordance with state law.
4. Implement an accounts receivable tracking process in accordance with internal control procedures.
5. Follow procedures for quarterly and annual submission of accounts receivable reports to the State Controller.

Inadequate Controls Over Payments Received

The Division has not established adequate controls over payments received. Control weaknesses include not depositing payments by mail timely, and not verifying payments were properly deposited. The Division received approximately $7.5 million in license payments and other revenues in fiscal year 2009. Controls in this area are important to help safeguard revenues by reducing the risk payments will be lost or stolen.

<u>Payments Deposited Untimely</u>

The Division did not deposit payments received by mail timely. Of 306 payments tested, 124 (41%) were not deposited timely. This includes 23 payments held more than 30 days after the payment was received. NRS 353.250(2) requires agencies deposit revenues by Thursday of each week for all money received during the previous week. Untimely deposits increase risk of lost or stolen payments. In addition, the State loses interest income. Our prior 2000 audit noted similar problems with untimely deposits.

The Division's cumbersome process for recording payments by mail resulted in untimely deposits. Administrative staff distributed payments by mail to designated employees throughout the Division, according to the type of revenue. After distribution, the employees recorded the payments in the licensing database. Once they were recorded, payments were deposited. The Division's internal control procedures require staff record payments in the database within 48 hours of receipt by mail. However, we found staff recorded 199 of 306 (65%) payments more than 48 hours after receiving the payments by mail.

Payments Not Compared to Deposits

The Division did not have a process to verify all payments received by mail were deposited. The daily total of payments received was not compared to the bank deposit by someone independent of the receipt and deposit process. This is an important control to safeguard revenues and help ensure all payments received are deposited. This weakness was reported in our prior audits in 2000 and 1994. Although the Division implemented adequate internal control procedures over walk-in payments, problems persist with payments by mail.

We noted payments were distributed to various Division sections for recording, then deposited on different days. For example, 13 payments received by mail on February 29, 2008, were deposited from 5 to 27 days after receipt, and included in 6 different bank deposits. Therefore, verifying all payments by mail were deposited is labor intensive. The Division needs to establish an efficient and effective process to verify all payments received are deposited.

Recommendations

6. Process payments received by mail timely to ensure revenues are deposited in accordance with state requirements.
7. Establish procedures that ensure payments received by mail are reconciled to bank deposits by staff independent of processing and depositing payments.

Oversight Needed for Complaint Investigation Activities

The Division did not adequately oversee complaint activities to ensure investigations of appraiser and real estate complaints were completed timely. The Division's complaint investigation process is critical for proper enforcement of real estate laws. When the complaint investigation process is unduly long, unscrupulous licensees may continue conducting illegal activities against the public. Better monitoring of complaint investigation activities can improve the Division's timeliness in processing complaints and taking disciplinary action.

Appraiser Complaints Not Investigated Timely

The Division did not investigate appraiser complaints timely. Of 24 appraiser complaints tested, 10 cases remained open an average of 552 days as of May 2009. In addition, the Division took an average of 580 days to resolve and close 14 cases. Some of the complaints involved serious allegations of inflated appraisals that overvalued residential properties. The likelihood of foreclosure increases when a home is overvalued and the house is worth less than the loan. Examples of untimely investigation of complaints involving inflated appraisals include:

- In July 2006, the Division received a complaint that a licensed appraiser was involved in a fraud ring. The complaint alleged an appraisal was far above market value. In September 2006, the Division requested and received a copy of the appraiser's work. The Division did not begin its investigation until February 2008, more than 1.5 years after the complaint was received. The investigation was completed in June 2008, and submitted to the Office of Attorney General for legal review. According to the case file, the investigator spent 22 hours on the case. More than 2 years after the complaint was received, the Commission revoked the appraiser's license in September 2008.
- In July 2007, the Division received an anonymous complaint of an appraiser that intentionally overvalued two properties causing harm to the buyer. The complainant requested the investigation to help protect the public. The Division did not begin its investigation until December 2008. As of May 2009, the investigation was still in progress. At that time, the case file indicated staff spent 8 hours on the investigation.
- In October 2006, the Division received a complaint that a misleading appraisal report ignored comparable data to hit the desired sales price. The Division requested and received a copy of the appraiser's report and work file in October 2006. However, upon review of the appraiser's file, the Division discovered the appraiser submitted the wrong file. A second request for the correct file was not sent until April 2008, about 1.5 years after the complaint was received. The Division completed its investigation in June 2008, and the Commission revoked the appraiser's license in December 2008. According to the case file, staff spent 11 hours on the investigation.

Untimely appraiser investigations have been a lingering problem for the Division. The federal agency charged with oversight of Nevada's appraiser certification program issued an unfavorable review report in December 2008. The Appraisal Subcommittee of the Federal Financial Institutions Examination Council threatened sanctions against

Nevada’s certified appraiser program because of the Division’s longstanding inability to investigate and resolve complaints within 1 year of the complaint filing date.

The Division has had difficulty managing available resources for appraiser complaint investigations. These resources consist of three staff, including one investigator, and outside contractors who perform appraisal case review services. First, the Division’s investigator position was vacant for 10 months until January 2008. Several problems delayed hiring for this position, including a 4-month delay before the job recruitment began. Second, one former investigator did not have any appraisal experience. This contributed to a large complaint backlog. Third, funding to hire contractors to provide appraisal case review services was spent on one large case, resulting in fewer cases reviewed by contractors. Lastly, because complaints were not prioritized, available resources were not directed to investigating appraisers that could harm the public.

The Division has taken steps to reduce the appraiser complaint backlog, but more work is needed. Since filling the investigator position, the Division reported the backlog was reduced from 98 cases in June 2008, to 42 cases in February 2009. Also, if necessary, the Division plans to use the services of a committee to perform the initial review of certain anonymous complaints. However, better management information is needed to monitor the appraiser complaint caseload. For example, the Division’s log of appraiser complaints lacked information necessary for monitoring case status, such as the number of days cases were open, and the estimated completion dates for investigations. In addition, this information should include the type and severity of alleged problems so investigations can be prioritized.

Real Estate Complaint Cases Not Processed Timely

Real estate complaints were not always processed timely, especially when disciplinary action was required. Of 25 real estate complaints tested, 9 cases remained open, on average, for more than 1 year as of May 2009. Seven of these cases were pending hearings, and investigation activities were ongoing for two cases. The 16 cases that did not require legal review or hearings were resolved in less than 90 days after the complaints were received. Although staff completed most investigations timely, better monitoring is needed to identify cases that remain unresolved for excessive periods of time.

We noted the Division's work performance standards for compliance investigators required staff complete real estate investigations within 6 months of assignment. Our testing confirmed this standard was frequently met when investigations were resolved without hearings. However, management reports of investigator caseload were not adequate for monitoring the status of ongoing investigations. For example, the Division did not monitor the number of days cases were open or estimate the investigation completion dates.

Recommendation

8. Develop procedures for monitoring the status of complaints to help ensure timely processing.

Information Technology Controls Need Improvement

The Division needs to ensure compliance with state information technology (IT) security controls to protect sensitive information and ensure network security features are maintained. Weaknesses included collection and storage of unencrypted licensee social security numbers in the licensing database, computers not updated for current virus definitions, and not conducting criminal background checks on employees with access to sensitive information.

Database Contains Unencrypted Social Security Numbers

The Division collects and stores licensee social security numbers. According to management, the Division stores about 135,000 licensee social security numbers unencrypted in the database. All Division employees have access to this confidential information.

The Division uses social security numbers as identifiers to link multiple credentials to the correct license holder. Social security numbers are also required for applicant criminal background investigations, child support compliance, and other agency functions. However, NRS 239B.030 imposes strict limits on agencies collecting and storing social security numbers. When agencies maintain this sensitive data, state

IT security standards require they control access by the use of encryption software or other methods.

Collecting and storing unencrypted social security numbers increases the risk of identity theft. When security over this type of sensitive data is breached, agencies are required to notify each person immediately. This notification process is costly, time consuming, and brings unfavorable public perception.

IT Security Controls Not Adequate

The Division did not comply with state IT security controls to ensure various network security features were maintained. Control weaknesses included computers not updated for current virus definitions, missing critical software security patches, allowing weak computer passwords, and not conducting criminal background checks on employees with access to sensitive information.

Virus Definitions Not Current

The Division's network server did not have current antivirus protection. When we tested the server during our audit, the virus definitions had not been updated for 28 days. Department IT staff indicated the condition occurred after a scheduled update of the server's virus definitions did not properly execute.

State security standards require agencies update virus protection software and definition files as new releases and updates become available. Agencies should review or update virus definition files daily. These definitions allow the software to more easily identify viruses and ensure protection from current threats. Computers without current antivirus protection are at risk of corruption by computer viruses from the Internet or other sources. According to Department IT staff, the virus update problems were corrected during our audit.

Computers Need Critical Security Updates

Of 24 desktop computers tested, 10 at the Carson City office were missing critical software security updates. Department IT staff indicated user intervention was needed to download and install a critical security update. However, users were not instructed to download and install the update.

State security standards require agencies develop, maintain, and test procedures for handling security patches and updates. The standards require agencies process critical security patches within 3 working days from the date of vendor release. When software security updates are missing, there is an increased risk a malicious entity could exploit the Division's computer network vulnerabilities to gain unauthorized access. Department IT staff indicated the updates were installed after we brought the issue to their attention.

Password Controls Need Strengthening

The Division did not ensure strong computer password controls were in place. The system allowed users more than three unsuccessful login attempts and permitted passwords that did not use special characters or numbers. State security standards require that passwords be complex by including upper and lower case letters, special characters, and numbers. Further, after three unsuccessful login attempts the account must be locked out.

Weak password controls compromise security by allowing increased opportunity to gain unauthorized access to the Division's computers and sensitive information. During our audit, Department IT staff indicated the password controls were set to meet the state's standard.

Employee Background Investigations Not Conducted

The Division had not conducted criminal background investigations on staff with access to sensitive information. All Division employees had access to the database containing licensee social security numbers. Background investigations help reduce the risk that individuals with criminal backgrounds could access sensitive information stored in the licensing database. State security standards require agencies conduct background investigations on employees with access to sensitive information. Management was unaware of this state standard.

Employees Need IT Security Awareness Training

The Division had not conducted IT security training for existing staff or new hires. In addition, the Division's employees did not sign security awareness statements. State standards require each agency conduct ongoing IT security awareness training. The intent of this training is to ensure that all new and existing employees, consultants, and contractors are aware of their responsibilities in protecting the state's information systems and data processed through them.

All employees with access to sensitive information should sign security awareness statements to document they understand their responsibilities regarding the confidential nature of the information they have access to. Such statements also inform employees of the penalties associated with the unauthorized disclosure or use of this sensitive information. Management indicated employees signed security awareness statements for their specific access to state databases such as the payroll system, but such statements were not completed for the Division's licensing database.

Recommendations

9. Develop procedures to comply with security requirements for sensitive data collected and stored in the database.
10. Develop procedures to ensure ongoing compliance with the state's IT security standards.

Certain Administrative Activities Not Performed as Required

The Division did not perform certain administrative activities as required by state law. Specifically, the Division did not maintain accurate property and equipment records, and employee evaluations were not completed timely.

Inaccurate Property and Equipment Records

The Division's property and equipment records were not accurate. For instance, computer equipment, missing since 2002, was not removed from the inventory records until we started our audit. In addition, some equipment transfers were not properly recorded, and other items were on hand but not listed on the inventory report. Overall, 17 of 48 assets tested had recordkeeping discrepancies. For example,

- Two computers were observed at the Carson City office but not listed on the Division's inventory report. Staff informed us the equipment was incorrectly assigned to other agencies in the state inventory system.
- The Division had difficulty resolving the location of three computer servers. Management explained two of the items were software misreported as computers on the state inventory records since July 2005. Management found the third server in the Las Vegas office but the asset identification tag was missing.
- Two computers, located in Las Vegas, were listed on the Carson City office inventory.

The Division did not conduct annual physical inventories of property and equipment as required by its internal control procedures. Before our audit, the last physical inventory was conducted in April 2006, but the results of the count were not reconciled to the state inventory records as required by NRS 333.220.

Accurate property records maintain accountability and enhance loss prevention. Nevada law requires agencies conduct annual physical inventories and reconcile the results to the state's inventory records. In addition, agencies are required to attach identification tags to all property and equipment and notify the State Purchasing Division when changes to property records occur. Reportable changes include equipment transfers, additions, corrections, and deletions.

Performance Evaluations Not Completed Timely

The Division did not complete timely employee performance evaluations for 6 of 10 employees tested. Two of the employees did not receive any performance evaluations when required, and four received untimely performance evaluations. This included three evaluations that occurred after we started our audit. The untimely evaluations ranged between 16 months to 6.5 years late. Without evaluations, deficiencies in performance may not be corrected timely.

NRS 284.340 requires annual evaluations for employees in the classified service who achieve permanent status. Management has not ensured supervisors conduct timely performance evaluations.

Recommendations

11. Follow procedures over property and equipment to ensure an inventory is taken annually, the inventory count is reconciled to the state's inventory records, and inventory identification tags are attached to equipment.
12. Ensure employees receive performance evaluations when required.

Appendices

Appendix A
Audit Methodology

To gain an understanding of the Real Estate Division, we interviewed agency staff and reviewed state laws, regulations, policies, and procedures significant to the agency's operations. We also reviewed financial information, prior audit reports, budgets, minutes of various legislative committees, and other information describing the activities of the agency. We documented and assessed the agency's internal controls over accounts receivable, revenues, expenditures, information systems, property and equipment, and personnel administration.

To evaluate the effectiveness of the Division's collection practices, we tested all accounts over $10,000 established from July 2006 through November 2008. We traced the sample of 19 accounts to supporting documentation to verify the accuracy of the Division's receivable databases. Also, for each account, we documented the Division's collection efforts and any payments received. Next, we traced a sample of commission orders to the receivable reports to verify completeness. We also confirmed the Division did not report accounts receivable or submit delinquent accounts to the State Controller for outside collections.

To determine if payments by mail were properly safeguarded, deposited, and recorded, we tested a sample of payments received by mail. We selected 1 mail log per month for each office, for a sample of 24 logs. These logs contained 306 payments. Each payment was traced to the licensing database, bank deposit, and state accounting records. In addition, to determine if fees were properly recorded, we tested a random sample of 30 licensees, 5 each from 6 license categories. Each payment was compared to the Division's fee schedule and license expiration date. Next, we randomly selected 10 returned checks to verify returned check fees were properly charged.

To determine if complaint investigations were processed and resolved timely, we randomly selected 24 appraiser and 25 real estate complaint cases. For each case, we reviewed the investigation files and calculated the case age. We also tested the completeness and accuracy of the real estate and appraiser caseload listings by selecting 10 case files and tracing the information to the listing.

To evaluate information security controls, we examined the Division's adherence to the state's IT standards. We also determined if the administrative and physical access to the Division's server was appropriate. We tested the server for current antivirus software protection and critical operating system updates. A sample of 24 desktop computers was tested for current critical operating system updates and antivirus software protection. We determined whether the Division conducts IT security awareness training and if the network server's group policy settings complied with state IT standards. Further, we tested for 'backdoors' into the Division's network through unauthorized wireless devices.

To determine if financial and administrative activities were properly carried out, we randomly selected 19 non-payroll expenditures including 5 contract payments and 5 travel claims. Each payment was tested for proper recording, approval, and compliance with laws, regulations, policies, and procedures. In addition, we judgmentally selected six expenditures to verify these transactions were recorded in the correct fiscal year and five credit entries to determine their propriety. Judgment was based on high dollar transactions and categories with little budgeted funds remaining.

To determine the existence of property and equipment, we judgmentally selected and located 18 assets on inventory lists from both office locations, based on the inherent risk of loss or misuse. We also judgmentally selected all computer equipment observed at the Carson City office and five items observed at the Las Vegas office and verified they were properly included on the inventory listings.

To evaluate the Division's compliance with personnel laws, we randomly selected 10 classified employees and determined whether work performance standards were established, reviewed annually, and a copy provided to the employee. We also determined whether employee evaluations were completed timely and supervisors received mandatory training. Additionally, we verified all unclassified employee salaries agreed to the amounts authorized by statute.

Our audit work was conducted from September 2008 through June 2009. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

In accordance with NRS 218.821, we furnished a copy of our preliminary report to the Director of the Department of Business and Industry and the Administrator of the Real Estate Division. On September 29, 2009, we met with agency officials to discuss the results of the audit and requested a written response to the preliminary report. That response is contained in Appendix B, which begins on page 26.

Contributors to this report included:

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Jeff Rauh, CIA, CISA
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Appendix B

Response From the Real Estate Division

JIM GIBBONS
Governor

STATE OF NEVADA

DIANNE CORNWALL
Director

GAIL J. ANDERSON
Administrator

DEPARTMENT OF BUSINESS AND INDUSTRY
REAL ESTATE DIVISION
www.red.state.nv.us

October 9, 2009

Paul V. Townsend, Legislative Auditor
Legislative Counsel Bureau
401 S. Carson Street
Carson City, Nevada 89701

Re: Real Estate Division Audit Report

Dear Mr. Townsend:

In response to the Legislative Counsel Bureau preliminary Audit Report of the Department of Business and Industry, Real Estate Division's (Division) calendar year 2008 financial and administrative activities, the Division respectfully submits our "Agency Response to Audit Recommendations."

The Division agrees that the Audit Recommendations are appropriate and will improve agency operations and compliance with state administrative guidelines and statutory requirements. All twelve Audit Recommendations are accepted and our response is enclosed along with the audit recommendations checklist.

If you have any comments or questions, please contact me at 702-486-4034. The Division shall have the required Corrective Action Plan submitted to your office prior to the expiration of the sixty business-day response period.

Sincerely,

ON BEHALF OF
Gail J. Anderson, Administrator
Real Estate Division

Enc: Agency Response to Audit Recommendations
Cc: Dianne Cornwall, Director, Department of Business and Industry

2501 E. Sahara Avenue, Suite 102, Las Vegas, Nevada 89104-4137 Telephone: (702) 486-4033 Fax: (702) 486-4275
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Agency Response to Audit Recommendations

1. Work with the commissions to establish prompt payment terms for disciplinary fines.

Presentations have been made to the commissions regarding accounts receivable and with recommendations from the Division on the structuring of payment due dates. Additionally, the Division has worked with the Deputy Attorneys General on the structuring of payment plans when requested by a Respondent which include default clauses. Division personnel are mindful of payment terms when making oral or written recommendations for disciplinary action before the commissions. The Attorney General's office has developed language to be included in disciplinary Orders and stipulated settlements with extended payment plans that would accelerate the full balance due if any interim payment should be missed. **COMPLETED**

2. Follow internal control procedures regarding timely collection efforts.

Internal control procedures regarding timely collection of disciplinary fines have been followed by new fiscal staff since April 2009, including monthly reviews of accounts receivable, mailing of delinquency letters, and referral of accounts to the Controller's office for collection and submission of bad debts to the Board of Examiners for write-off approval. **COMPLETED**

3. Revise procedures for periodic submission of delinquent accounts to the State Controller for collection action in accordance with state law.

Internal control procedures were revised and implemented in March 2009 resulting in monthly review of delinquent accounts and referral of accounts to the Controller's office for collection in May, June and August 2009. The Division is in full compliance with current collection regulations and awaits pending regulation revisions pursuant to AB 87 (2009 Legislative Session). **COMPLETED**

4. Implement an accounts receivable tracking process in accordance with internal control procedures.

An accounts receivable tracking process was implemented in March 2009 in accordance with internal control procedures and remains effective. **COMPLETED**

5. Follow procedures for quarterly and annual submission of accounts receivable reports to the State Controller.

All calendar year 2009 quarterly and annual accounts receivable reports to the State Controller have been submitted as required and future due dates have been entered on the fiscal section's calendar to ensure timely submissions. **COMPLETED**

6. Process payments received by mail timely to ensure revenues are deposited in accordance with state requirements.

The Division fully appreciates the necessity of timely deposits of all revenue. In order to consistently achieve this objective for mail payments, a substantial revision of our current mail processing, payment receipting and revenue reconciliation procedure is required. Revising this process could potentially have an adverse effect on customer service due to staffing limitations. We have begun the investigation of various options and will have an action plan in place to address this issue within sixty business-days. **IN PROCESS**

7. Establish procedures to ensure that payments received by mail are reconciled to bank deposits by staff independent of processing and depositing payments.

In order to achieve this objective for mail payments, a substantial revision of our current mail processing, payment receipting and revenue reconciliation procedure is required. We have begun the investigation of various options and will have an action plan in place to address this issue within sixty business-days.
IN PROCESS

8. Develop procedures for monitoring the status of complaints to ensure timely processing.

While existing processes provide details of the status of both real estate and appraisal complaints under investigation and each program provides monthly statistical reports on workload statistics, there currently is no tracking system in place to easily provide management with an indication of the time involved in each step of the receipt of complaint, complaint review, assignment, and investigation time spent on an individual case. Division management appreciates the value of such a tracking tool and intends to implement an automated case tracking system utilizing the enforcement module of SOAR (Statewide Optimal Access for Real Estate), the Division's customized integrated licensing and enforcement data system. We have defined the various data fields to be measured and will soon begin discussions with the software vendor in order to understand the monitoring and reporting options. The Division will have an action plan in place to address this issue within sixty business-days. We also note that recent Federal Appraisal Subcommittee correspondence with the Division acknowledges a "significant improvement" in case backlog processing. **IN PROCESS**

9. Develop procedures to comply with security requirements for sensitive data collected and stored in the database.

The Division has implemented a security awareness statement for SOAR (Statewide Optimal Access for Real Estate, the Division's customized integrated licensing and enforcement data system), which formally documents each employee's signed acknowledgement that they understand their responsibilities regarding the confidential nature of the information to which they have access, and which also informs them of the penalties associated with the unauthorized disclosure or use of this sensitive information. **COMPLETED**

The Division is working, with the Department of Business and Industry's involvement, to evaluate options available to the agency to provide protection of sensitive data while fulfilling statutory requirements. The Division is investigating ways to implement back ground checks of employees and/or limiting access to sensitive data in a manner that simultaneously satisfies security requirements and can be accomplished within budget constraints. The Division will have an action plan in place to address both of these recommendations within sixty business-days. **IN PROCESS**

10. Develop procedures to ensure ongoing compliance with the state's IT security standards.

The Division will have an action plan in place to address this issue within sixty business-days. However, as the agency does not have an IT position on staff and no direct Division tie with DoIT for policy updates, we note that the effective long-term implementation of the recommended IT security procedures may require resources outside of the Division or funding for a position not presently in the budget. **IN PROCESS**

11. Follow procedures over property and equipment to ensure an inventory is taken annually, the inventory count is reconciled to the state's inventory records, and inventory identification tags are attached to equipment.

The Division completed FY 2009 physical inventory according to the fiscal section's calendar and in compliance with State requirements. All equipment was properly accounted for, state records updated and equipment tags replaced as necessary. On an ongoing basis records are promptly adjusted to reflect equipment purchases, dispositions and transfers. Responsible staff have been identified and trained and this duty has been added to their work performance standards. **COMPLETED**

12. Ensure employees receive performance evaluations when required.

The Division understands the importance of timely employee evaluations and has implemented procedures to address this deficiency, including a tracking system to notify supervisors to schedule upcoming evaluations and monitor their completion. The Administrator has made this issue a topic at agency management meetings and has added the requirement of prompt employee evaluations as a job element for every supervisor's work performance standards. **IN PROCESS**

Real Estate Division
Response to Audit Recommendations

Recommendation Number		Accepted	Rejected
1	Work with the commissions to establish prompt payment terms for disciplinary fines..	X	
2	Follow internal control procedures regarding timely collection efforts	X	
3	Revise procedures for periodic submission of delinquent accounts to the State Controller for collection action in accordance with state law	X	
4	Implement an accounts receivable tracking process in accordance with internal control procedures	X	
5	Follow procedures for quarterly and annual submission of accounts receivable reports to the State Controller..	X	
6	Process payments received by mail timely to ensure revenues are deposited in accordance with state requirements	X	
7	Establish procedures that ensure payments received by mail are reconciled to bank deposits by staff independent of processing and depositing payments..	X	
8	Develop procedures for monitoring the status of complaints to help ensure timely processing	X	
9	Develop procedures to comply with security requirements for sensitive data collected and stored in the database...	X	
10	Develop procedures to ensure ongoing compliance with the state's IT security standards	X	
11	Follow procedures over property and equipment to ensure an inventory is taken annually, the inventory count is reconciled to the state's inventory records, and inventory identification tags are attached to equipment...	X	
12	Ensure employees receive performance evaluations when required...	X	
	TOTALS	12	0