

NO. 2000-0114-3
INDEPENDENT STATE AUDITOR'S REPORT
ON CERTAIN ACTIVITIES OF THE
BOARD OF REGISTRATION OF COSMETOLOGY
JULY 1998 TO OCTOBER 2000

**OFFICIAL AUDIT
REPORT
JUNE 19, 2001**

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Chapter 13, Section 8, of the Massachusetts General Laws authorizes the Division of Professional Licensure, previously known as the Division of Registration. The division, within the Commonwealth's Office of Consumer Affairs and Business Regulations (OCABR), is responsible for ensuring the integrity of the licensure process, the continual updating of licenses, and the maintenance of the multiple databases related to licensing, enforcement, and revenue collection. Chapter 13, Section 42, of the General Laws authorizes the Board of Registration of Cosmetology (BORC), which oversees the cosmetology profession and its hairdressers, manicurists, and aestheticians. BORC sets the curricula requirements and regulates the schools that train candidates in these occupations. Our audit examined BORC's controls over the issuance of licenses, licensing revenue, expenditures, contract administration, use of consultants, administrative costs, license renewals and monitoring, and adherence to the Commonwealth's Privatization Law, Chapter 296 of the Acts of 1993.

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1. Inadequate Controls over the Cosmetology License Process: Our audit disclosed that BORC had inadequate controls over data input and employee access to the licensing database and the licensing of cosmetology professionals and salons. For example, the cosmetology license number inventory was inadequately accounted for in various logbooks, all employees had access to the logbooks, and neither employee signatures nor reviewer signatures were available to determine who issued a license number. We also found that various logbook entries were crossed out or blotted out with correction fluid. These deficiencies permitted a former employee of BORC to issue and sell 39 fraudulent cosmetology licenses. During 1999 the employee falsified logbook entries, created unauthorized computer input forms, and sold licenses to individuals, which allowed individuals to obtain licenses without meeting the division's educational and testing standards.

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INTRODUCTION

Background

Chapter 13, Section 8, of the Massachusetts General Laws authorizes the Division of Professional Licensure, previously known as the Division of Registration. The division is within the Commonwealth's Office of Consumer Affairs and Business Regulations (OCABR). Within the division are 36 boards of registration, which were created by Chapters 12 and 112 of the General Laws. The boards are responsible for ensuring the integrity of the licensure process for more than 46 trades and professions; the continual updating of licenses for over 530,000 individuals, corporations, and partnerships; and the maintenance of multiple databases related to licensing, enforcement, and revenue collection. The division's work is accomplished through the combined efforts of the members of the boards and their staff, the Office of Computer Services, the Accounting Unit, the Office of Legal Counsel, the Office of Prosecutions, the Office of Investigations, and the Administrative Office.

Chapter 13, Section 42, of the General Laws authorized the Board of Registration of Cosmetology (BORC), which oversees the cosmetology profession that includes hairdressers, manicurists, and aestheticians. BORC sets the curricula requirements and regulates the schools that train candidates in these occupations. As of April 6, 2001, BORC licensed 55,373 cosmetology professionals, 7,564 salons and shops, and 44 private schools. BORC is responsible for the licensure and oversight of cosmetology professionals, salons, and schools as mandated under the provisions of Chapter 112, Sections 87T through 87KK, of the General Laws. BORC's licensure process protects the general public by ensuring that only those individuals who are competent to practice safely are licensed. The division's responsibility is to establish the acceptable level of safe practice.

The board members of BORC are appointed by the governor. Under the direction of the division's Deputy Directory of Professional Licensure, BORC's administrative personnel, comprising an Executive Director and staff of six, provide support and guidance for BORC members. They coordinate the business processes, perform general planning, and administer responsibilities for licensee testing and renewal. In addition, the Executive Director is responsible for seven additional boards: the Boards of

Electrologists, Funeral Directors and Embalmers, Landscape Architects, Sanitarians, Drinking Water Supply Facilities Operators, Architects, and Engineers and Land Surveyors.

Audit Scope, Objectives, and Methodology

In accordance with Chapter 11, Section 12, of the General Laws, we conducted an audit of BORC for the period July 1998 to October 2000. Our audit was conducted in accordance with applicable generally accepted government auditing standards with specific objectives of (1) reviewing the division's internal control structure; (2) reviewing all BORC activities, including, but not limited to, controls over receipts and expenditures, contract administration, use of consultants, administrative costs, license renewals, and monitoring; (3) reviewing and analyzing BORC's internal controls over licensing and testing practices and procedures; (4) determining how BORC administers its examinations and identifying any internal control weaknesses that might allow licenses to be given to applicants who may not have taken the necessary examinations; (5) reviewing and analyzing any contracts BORC has for its testing and licensing systems to determine how these contracts were awarded, administered, and monitored; (6) reviewing and analyzing the investigations, appeals, and hearing processes available to licensees and applicants; (7) examining how licenses are processed for out-of-state applicants; and (8) determining the division's compliance with Chapter 296 of the Acts of 1993, the Privatization Law.

In conducting our audit, we (1) reviewed the division's internal control procedures for the issuance of cosmetology licenses; (2) reviewed license application files and investigation files; (3) reviewed time and attendance records; (4) reviewed contracts with professional independent testing companies and historical contract data; and (5) interviewed division and OCABR officials and testing company employees.

During 1999 a former employee was engaged in the issuing and selling of fraudulent cosmetology licenses. The employee falsified logbook entries, created unauthorized computer input forms, and sold the licenses to individuals. This fraudulent activity enabled individuals to obtain licenses without meeting the division's educational and testing standards. The employee was prosecuted by the Commonwealth's Attorney General's Office. In addition, during calendar year 2000, it was alleged that an individual

attempted to bribe a BORC employee to issue a cosmetology license without taking the appropriate examination. This case was investigated by the Attorney General's Office.

Our audit indicated that, except as discussed in the Audit Results section, BORC complied with applicable laws, rules, and regulations for the areas tested, including BORC's investigations, appeals, and hearing processes; out-of-state license application process; and compliance with Chapter 296 of the Acts of 1993, the Privatization Law. In addition, BORC had an adequate system of internal controls for the areas reviewed.

Auditee's Response:

The Division of Professional Licensure appreciates the review and assistance by the State Auditors and the recommendations made in their Report. We wish to note, however, that (before) the audit . . . the Division had discovered and made immediate referral of the thirty-nine (39) licenses at issue to the State Police and the Office of the Attorney General. . . the Division cooperated fully with these agencies and also undertook a review of its own internal controls. The resulting process improvements, coupled with the State Auditor's recommendation, have enhanced the Division's mandates of licensing integrity and consumer protection.

AUDIT RESULTS

1. Inadequate Controls over the Cosmetology License Process

Our audit of the Board of Registration of Cosmetology (BORC) indicated that there were inadequate controls over the cosmetology license process, including (a) inadequate segregation of duties and inadequate controls over data input and employee access to BORC's licensing database and (b) inadequate supporting documentation in license application files. These deficiencies allowed a former BORC employee to falsify logbook entries, create unauthorized computer input forms, and issue and sell 39 fraudulent cosmetology licenses to individuals whose educational and testing standards had not been reviewed.

a. Database Input Deficiencies: The Computer Services department of the Division of Professional Licensure (division) administers licensing systems, provides technology support services, develops information systems, and is the liaison between the Commonwealth's Information Technology (IT) Division, the division's lock box banking institution, and private testing companies. The department develops and maintains license and renewal applications, produces licenses and subsequent renewals, and maintains more than 530,000 license records. Daily, the department receives, records, updates, and disseminates licensure information. Licensure records for all boards of registration are maintained on the division's computer database, a subsystem of the IT Division's mainframe computer applications.

Our review disclosed inadequate controls over the input of data and employee access to the licensing database. Data is input to the licensing database by two methods: (1) Computer Services data-entry personnel enter data into the database as requested by division personnel and (2) division employees access the database online via password-controlled access.

The division uses multi-copy documents called white sheets to add, change, and delete records within the database. The processing of a white sheet is as follows:

- White sheets are required to be completed and reviewed by separate division employees.
- Computer services personnel input white sheet data; licenses are printed in the evening and forwarded to computer systems the next day for review.

- Computer services verifies the license data and forwards the licenses for mailing to the licensees.

Our meetings with division employees and members of the Attorney General's Office disclosed that a former employee bypassed these controls to create 39 fraudulent licenses, as follows:

- The employee would search the BORC logbooks for forfeited license numbers. (A candidate with a forfeited license can reapply within a three-year period since the last renewal and take the board's practical examination.) The employee would blot out the name of the forfeited licensee with correction fluid and write in the fraudulent licensee's name.
- A white sheet would be created and sent to computer services for data input. The appropriate division supervisory personnel did not approve the white sheets, and the computer services personnel did not look for appropriate approvals before input.
- Since licenses are printed on Monday night, the employee would submit the white sheets late Monday afternoon and request to have the licenses pulled on Tuesday morning instead of mailed to the licensee.
- The employee reportedly sold the licenses for \$1,000 to \$2,000 per license.

The employee was prosecuted by the Attorney General's Office, pled guilty to all counts of 11 indictments on September 15, 2000, was sentenced to one year in the house of correction, paid a \$12,500 fine, was ordered to perform 200 hours of community service teaching an adult literacy program, and paid a \$60 victim witness assessment fee.

Our review of the white sheets for the 39 fraudulent licenses disclosed that:

- Twenty-five "Prepared By" sections were completed by the former employee.
- Fourteen "Prepared By" sections were not completed.
- None of the 39 "Approved By" sections was completed.

We conducted an additional review of batches to determine whether the white sheets completed by various division employees had the "Prepared By" and "Reviewed By" sections completed. We selected 11 batches processed during the period June 21, 1999 to September 13, 1999, which consisted of 367 white sheets submitted by 33 different boards. We noted that 362 white sheets had neither the "Prepared By" nor the "Reviewed By" sections completed.

During our review, we noted a white sheet in which a BORC employee requested that the first and last name be changed for a licensee. We were informed that a name change is not an unusual request, as

licensees will request name changes due to marriage or divorce. For the white sheet we questioned, we noted that the licensee's name on a cosmetology license was changed. However, a review of this licensee's database records disclosed that the individual also had a real estate license that was not changed. The division stated that there is no law or procedure requiring a legal document to support a name change. The division's Customer Services Bureau manager stated that the name change policy is as follows:

- For license renewals, if a licensee indicates a "last" name change on the renewal form and they have signed the renewal attesting to the information, then Computer Services will update the record with a new name, status code, and so forth to generate the new license reflecting the name change.
- If a licensee indicates a "first and last" name change on the renewal form, then Computer Services will send it back to the licensee requesting the name change legal document. When the licensee resubmits the renewal and name change information, Computer Services updates the licensee's records with the new name, status code, and so forth to generate the new license. (The name change document is either attached to the renewal form and filed away or in some cases given to the respective board for its records).
- When a name change is requested not during a renewal cycle, the Computer Services department has a standard "Name Change/Address Change/Duplicate License Form" that is sent out electronically to all boards. The boards use this form to send to licensees requesting a license or record change in their new name. The licensee also signs this form attesting to the information. The completed form is submitted to Computer Services, they update the licensing system to generate the new license, and the name change forms are filed by batch number and date.

However, our review noted a deficiency in the division's name change policy. Specifically, if there is an instance where the licensee will not or cannot submit a legal document, the division will still change the licensee's name on the database, as the division does not require a court document before a licensee's name is changed. Our review also noted that, although the database system is designed to record the code, G1, in its history to indicate that a name was changed, it does not retain the previous name in the database and only displays the most up-to-date records. According to the division's Record Disposal Schedule Number 26/85, supporting paper documentation is to be retained for two years. The current database system does not provide an audit trail to review previous names of changed records and thus, after a two-year retention period, the division cannot provide documentation of changed names.

We requested a listing of licenses that had a changed G1 field during fiscal year 1999. From a listing of 1,897 changed licenses, we selected a random sample of 50 licenses and reviewed the supporting documentation. A G1 change can be made by using the white sheet, by using a license renewal form, or through online password maintenance capability. Our review disclosed that changes were made involving 25 last names, eight first names, six middle initials, six addresses, and 16 license cross-reference changes, which is an update in a licensee's professional status. Fourteen of the 50 changes were required to have a white sheet completed to support the change. For the 14 white sheets we noted:

- Three did not have either the "Prepared By" or "Approved By" sections completed.
- Four identified who prepared the form but not who approved it.
- Seven had the same individual complete the "Prepared By" and "Approved By" sections.

Without adequate controls in place over the completion and retention of the white sheet and limiting the use of password availability, the division cannot be assured that fraud and misuse will not occur and go undetected.

b. License Application File Deficiencies: BORC is responsible for the licensure and oversight of cosmetology professionals, salons, and schools as mandated under the provisions of Chapter 112, Sections 87T through 87KK, of the General Laws.

The division documents disclosed the following number of current licenses as of April 6, 2001:

<u>License Type</u>	<u>Number of Current Licenses</u>
<u>Professionals</u>	
Cosmetologist	25,976
Operator	12,527
Manicurist	11,937
Instructor	935
Demonstrator	131
Aesthetician I	1,227
Aesthetician II	2,552
Aesthetician Instructor	88
<u>Salons</u>	
Cosmetology Salon	4,475
Booth Shop	877
Manicuring Shop	820

Booth Renter	1,135
Aesthetic Shop	257
<u>Schools</u>	
Cosmetology School	29
Aesthetician School	8
Advanced Training Institute	2
Manicuring School	<u>5</u>
Total	<u>62,981</u>

Depending on the type of license, examinations for licenses are conducted by either a division employee or a private professional testing service. The 230 Code of Massachusetts Regulations (CMR), promulgated pursuant to Chapter 13, Section 9a, of the General Laws, authorizes the director of the division to make rules and regulations governing the conduct of examination by the boards of registrations. For the licensure of cosmetology professionals, the division has contracted with a private professional testing service to conduct the following cosmetologist license examinations: operator, aesthetician, manicurist, aesthetician instructor, and cosmetology instructor. Applicants are required to pass both a practical and written examination in order to receive a license. The examination fees payable to the testing company are \$99 for a first-time test and \$74 for a reexamination. The license fee due to the Commonwealth is \$25. During 1999, the testing company conducted 3,296 examinations.

License numbers for cosmetology professionals are issued either by the testing company or by BORC. Prior to September 1999, the inventory was accounted for in six logbooks. Our review of the logbooks to determine the accountability and control of the numbers disclosed that:

- All employees had access to the logbooks. There were no employee or reviewer signatures to determine who issued a license number.
- All the logbooks had numerous entries crossed out or blotted out with correction fluid.

We note that, since the fraudulent licenses were issued, BORC improved its control over the issuance of license numbers by recording the numbers on an Excel database and limiting the access of numbers to three individuals. However, because this information can still be manipulated, further controls, such as exception reporting, review of activity, and segregation of duties, should be explored to further enhance security over database changes to licenses.

To determine whether license application files supported the logbook entries, we selected a sample of 22 logbook entries and found them to be in order. However, we noted that some files did not contain the required supporting documents, as follows:

- For five files neither the applicant nor the examiner signed the practical examination.
- One out-of-state applicant's file did not include a photograph of the applicant.
- One out-of-country applicant's file did not have a completed health certificate and the practical examination was not signed by the applicant and examiner.
- One salon file did not contain an occupancy permit nor have the owner's signature on the plumbing and electrical forms.

Without the required supporting documentation on file, there is inadequate assurance that BORC's license file data are accurate, complete, and up-to-date or that all licenses are in compliance with applicable laws, rules, and regulations.

Recommendation: The division should evaluate current internal controls and institute additional controls to prevent fraudulent activities from occurring. "The Prepared By" and "Approved By" section of the division's white sheets should always be completed, as this is a key internal control element. Given that an employee with full access can change all records across all boards, password capability should be restricted, and the division should randomly conduct quality assurance reviews of data entry and exception reporting. In addition, the division should require and retain the necessary legal documents to support name changes to lessen the opportunity for potential fraud. Further, Computer Services should not process any white sheets that do not meet all of the division's policies and procedures. Moreover, the division should take steps to ensure that licenses issued are supported by valid documents and application forms.

Auditee's Response:

The Division's ultimate goal is to move to an entirely automated system of licensing with the incorporation of automated security controls over data input and employee access to the licensing database and the licensing of cosmetology professionals and salons. The procedures which are highlighted below reflect measures taken after the discovery of standard protocol deviations.

Key measures resulting from this process improvement have included the elimination of hand written license number logging books and implementation of a license number database, with electronic access restricted to designated staff. Also, prior to adding new license numbers to the Commonwealth's Information Technology Division (ITD) licensing database, a second staff person reviews and initials those documents for accuracy and completeness. Finally, no Division employee may remove a printed license from the master batch without a form signed by both a Manager and a Deputy Director of the agency. . .

In addition, the Division also has taken the following measures:

1. Division computer services department has successfully run reports verifying that each fraudulent license has been placed on hold in the division database, thereby eliminating automatic renewal.
2. A cross reference also has been run by computer services to provide a list of the holders of the fraudulent licenses with concurrent valid licenses held within the agency in order to put a hold on the valid licenses as well.
3. The list of individuals remaining who hold the licenses in question are currently being handled by the Office of Investigations (OI) and the Office of Legal Counsel.

2. Inadequate Administrative Controls within the Office of Investigations

Our audit indicated that BORC lacked adequate administrative controls within its Office of Investigations (OI) in the areas of (a) inspection procedures and (b) time and attendance records. As a result of these deficiencies, salons were found to be operating without a license, and there was inadequate assurance that inspections were conducted properly and that time and attendance records are accurate.

a. Inspection Procedures: OI assists consumers in determining the status of licensees, filing complaints, resolving disputes, pursuing legal redress in the courts, and filling out requests for public information. Investigators also respond to the questions and problems of licensees, attorneys, and representatives of various state agencies. In addition, OI investigates allegations of professional misconduct and inspects business premises licensed by the boards.

OI has three full-time investigators dedicated to conduct investigations for BORC, which as of April 6, 2001 licensed 55,373 cosmetology professionals and 7,564 cosmetology salons and shops. Inspections are conducted for the opening of new salons or as a result of a complaint.

During fiscal years 1998, 1999, and 2000 the division reported the following OI inspection data:

	<u>1998</u>	<u>1999</u>	<u>2000</u>
<u>Inspections</u>			
Cosmetologists	4,523	4,413	5,498
Cosmetology Salons	1,871	1,758	1,593
<u>Complaints</u>			
Cosmetologists			
Received	106	96	30
Resolved	73	82	64
Cosmetology Salons			
Received	70	50	94
Resolved	85	51	81
<u>Disciplinary Actions</u>	69	83	81

Our audit revealed that OI could not provide documented procedures for conducting its inspections.

However, an investigator supervisor stated that the procedures are as follows:

- The public or members of the division may submit complaints against cosmetologists, salons, and schools.
- The complaint is documented on the division's Complaint Form and recorded on the division's Complaint Management System database.
- A complaint file is created and assigned to one of three investigators.
- Upon completion of the investigation and consultation with the investigation supervisor, the licensee will be notified of any violations and possible findings via a Show For Cause form.
- The licensee may sign a consent agreement accepting the results of the investigation or appeal the results with a meeting of the BORC board.

The results of OI's and BORC's decisions are documented in the case file, OI's Complaint Management System database, and the division's Public License Query database for each licensee for Internet access. In addition, the division has publicized some of the decisions on its Web page. We selected a sample of completed investigation files to determine whether the Complaint Management System accurately reflects the results of OI investigations. We also selected samples from the results posted to the Public License Query pages and from comments in the minutes from the monthly board member meetings. Our review of 14 case files noted the following:

- An investigation may take anywhere from 25 to 645 days to complete.
- Thirteen case files disclosed fines and penalties imposed on the licensee.

- Three Public License Query screens did not report the investigation results.

The 240 CMR 3.00 outlines the policy and procedures for the licensing of salons. The regulations state, in part:

Every person contemplating the opening of a cosmetology salon, manicuring salon or aesthetics salon shall file the appropriate application for a salon license with the Board, pay required fees, and arrange for the premises to be inspected and approved by the Board. The Board will not issue a license for any premises to be inspected if required local permits and certificates have not been obtained. . . .

As documented on the division's current form, "Salon Applicants Instructions," the division requires the following documents upon inspection:

- Copy of Rules and Regulations (240 CMR)
- Business certificate
- If the business is incorporated, a copy of the Articles of Organization
- Plumbing form, signed by the city inspector
- Electrical form, signed by the city inspector
- Occupancy permit from the city

To determine whether salons are currently licensed in compliance with applicable regulations and requirements and whether the case files contain the required documents, we selected 72 salons listed in a telephone directory. We traced the salon names to the division's Public License Query page and obtained and reviewed the application file to determine if the required documents are on file. Our testing found the following:

- Two salons listed in the telephone directory were unlicensed. BORC determined that one salon relocated without properly notifying BORC. A new inspection is required when relocating. We were advised by BORC that the other salon was in violation and was sent a renewal notification.
- Six application files were unavailable for our review. BORC stated that the files were lost in its archives.
- Fifty-eight application files did not contain an Occupancy Permit.
- Twenty-five application files did not contain plumbing and electrical forms signed by the city inspector.
- Thirteen application files did not contain a floor plan.

OI's Assistant Chief Investigator stated that salons were not required to have occupancy permits until June 14, 1994, the date on which 240 CMR was promulgated. However, we noted that 26 files for which there were no occupancy permits were initially licensed after June 1994.

OI staff stated that there was a backlog of inspections of salons, since OI has only three cosmetology inspectors. We were told that the priority to conduct inspections is to inspect new salons first; other salons are selected depending on when the inspector is in a salon's neighborhood. OI does not have audit or inspection guidelines. Instead, the OI supervisor of inspectors stated, the OI policy is to train new investigators in the field with a veteran investigator.

The number of investigators assigned to OI may be a contributing factor in the proportionally small number of inspections conducted and the failure to adequately document an inspection. OI's failure to inspect salons in a timely and consistent manner allows some salons to operate without a license, in unsanitary conditions, or with unlicensed cosmetologists and manicurists. Moreover, by not having an inspection guide or a documented inspection program, the division cannot be assured that the investigators are conducting an inspection in compliance with legislation and regulations. Posting incomplete or inaccurate data to the division's Internet site will cause the public to be misinformed about the license status of a cosmetologist or salon.

b. Time and Attendance Records: Our audit also disclosed that, within OI, employees and supervisors did not sign employee payroll records and supporting documents, and weekly payroll records submitted to the Office of Consumer Affairs and Business Regulation (OCABR) payroll department were authorized by the use of a management signature stamp instead of an actual signature. BORC's inability to properly and accurately control and account for OI employees' time and attendance could result in employees being improperly paid and inaccurate time reporting to the Commonwealth's payroll system.

OCABR's Internal Control Guide Chapter 5, Section 2.3, Time and Attendance, mandates the following procedures:

Agency staffs are required to account for their time on weekly personnel time sheets. Employees are required to sign the time sheet and record daily hours worked. Agency unit managers check and monitor time sheets for their unit and have responsibility for the

correctness of all time sheets within their specific unit. Agency managers sign off on the time sheets to indicate approval of all time recorded, prior to the submission of the time sheet to the ASU Personnel Officer. The Personnel Officer is separately responsible for assuring that all staff signatures are present and attachments are complete before inputting payroll data into the payroll system.

Our testing of 45 attendance sheet entries for five employees during two weekly payrolls disclosed the following instances of noncompliance with OCABR's Internal Control Guide regulations:

- The division's management did not sign the February 12, 1999, weekly payroll record.
- The February 19, 1999, weekly payroll record was signed using a signature stamp of the OI Assistant Chief Investigator.
- Twenty weekly payroll record entries were not supported by the daily payroll record entries.
- For one employee, seven weekly payroll record entries were not supported by the daily payroll record. The weekly payroll record indicated the employee worked; however there was no employee signature on the daily payroll record.
- For one employee, the daily payroll records for February 10 and 11 noted that vacation time was taken. However, the weekly payroll record noted that the employee worked. Further review of the employee's personal time and attendance records disclosed that the employee was not charged vacation time. The division advised that they have subsequently adjusted the employee's records to reflect vacation time used.
- For one employee, for a nine-day period, the daily payroll record notes "P.T." (part-time), while the weekly payroll records note that the employee worked 7.5 hours on February 9, 11, 16, and 18.

The OI supervisor indicated that the Chief Investigator, who was appointed on June 27, 1999, does not use a signature stamp and hand signs all documents. To test this assertion, we expanded our review to include an additional 20 entries for four employees for the week ended November 19, 1999 and noted that the employees signed the daily payroll records and that a supervisor signed the weekly payroll records. In addition, the Deputy of Administration stated that he has informed all employees that signatures are required on all daily payroll records and that the department manager must authorize them.

Recommendation: The division should take action to address its concern that the OI is understaffed relative to cosmetology inspectors, whether by obtaining adequate funding to hire additional staff or by reallocating existing staff resources. Investigations should be conducted in a timely and consistent manner and documented to comply with existing regulations. To ensure that investigators are performing

thorough and consistent investigations, an inspection audit guide should be developed. Every effort should be made to ensure that the division's Internet site publishes current and factual data relative to a licensee's status. To ensure that the employees' payroll records are controlled and employee attendance is accounted for, the division should take the necessary actions to ensure that all employees sign payroll records and that the weekly payroll records submitted to payroll are accurate. In addition, time and attendance internal control procedures, as documented in OCABR's Internal Control Guide, should be complied with.

Auditee's Response:

INSPECTION ISSUES

The Office of Investigations reorganized in November of 2000 from three teams of investigators to five teams. While this change did not include the additions of new investigators it did reduce the number of investigators assigned to each team, particularly the Trades Team which includes the BORC. The net result is increased availability of the supervisor to the investigators allowing greater attention and assistance to be focused on the investigators and the process. . .

The average investigative age of cases for all cases in FY 2001 is lower than in previous years, in part due to the continued updating of the complaint database at each stage of the process when the status of the complaint changes. . . Internal practices were changed to update the database at each step of the process as the case moves through the system. This has resulted in a more accurate representation of the investigative age of each case.

All new salons are inspected prior to opening for business. All other salons are inspected either randomly or as a result of a complaint against the salon. During FY2000 there were 1593 general inspections and 925 new salon inspections. No salon openings were delayed due to backlogged inspections. Inspection procedures are specified in Chapter 8 of the Office of Investigations Investigator Manual. This section discusses the different types and frequency of inspections, why they are performed, and also dictates the inspector's conduct and demeanor during the inspections. Inspection results are recorded on Standardized Inspection Forms unique to the profession in question, recorded in the database, and maintained pursuant to current state guidelines for retention. . . While copies of the various permits are not always available for file retention, inspectors consistently record the results of the inspection on the indicated form. Also, the purpose of random inspections is to detect and discipline those salons that ignore the regulatory requirements and open without the required paperwork, inspections and licenses.

TIME AND ATTENDANCE ISSUES

Several remedial steps had been implemented to address these issues prior to this report and its recommendations. Signature stamps are no longer used. The Auditors examined the Office of Investigations time and attendance records upon their arrival to the agency and found no discrepancies at that time.

3. Cosmetology School Surety Bond Coverage Inadequately Documented

Our audit found that BORC could not provide full and complete documentation that privately owned and operated cosmetology schools had adequate surety bond coverage. Cosmetology schools are required to have surety bond coverage to cover the cost of students' tuition in the event that a school defaults on its obligation to provide the cosmetology programs. Chapter 112, Section 87BB, of the General Laws empowers BORC to register privately owned schools to satisfactorily meet the division's standards of professional training. The division's regulations governing the operation of cosmetology schools, aesthetic and manicuring schools, and advanced seminars in hair dressing are provided in 240 CMR 4.00: Operation of Cosmetology Schools, 5.00: Operation of Aesthetic Schools, and 7.00: Operation of Manicuring Schools. The bond coverage amount for cosmetology and aesthetic schools is \$10,000 if the student enrollment does not exceed 25 students and \$20,000 if the enrollment exceeds 25 students. For manicuring schools, the bond coverage requirement is \$10,000.

As of April 6, 2001, 44 privately owned schools were licensed by BORC to offer courses in cosmetology. Our review of BORC's school license files for a sample of six schools found that, contrary to 240 CMR, only one school file contained evidence of current bond coverage. For the other five schools, the documents were inadequate for us to make a determination of bond coverage. Due to the lack of documentation, it could not be determined whether the private cosmetology schools had adequate surety bond coverage.

Furthermore, the \$10,000 and \$20,000 bond coverage required by 240 CMR appears to be inadequate to cover the costs of students' tuition in the event that a school defaults on its obligations. We reviewed the Web pages for two licensed schools in Massachusetts and determined an average tuition for a student enrollment of 25 and compared that to the coverage required in the CMR. For students paying full tuition on enrollment, the following chart shows that the CMR bonding requirement may not be sufficient.

<u>Program</u>	<u>Tuition</u>	<u>Total Tuition Paid for 25 Students</u>	<u>CMR Requirement</u>
Cosmetology	\$7,600	\$190,000	\$20,000
Aesthetic	\$3,400	\$85,000	\$20,000
Manicure	\$1,100	\$27,500	\$10,000

Students' tuitions cannot be protected unless the division requires private schools to obtain adequate surety bond coverage.

Recommendation: To ensure that students' tuition is protected in the event that private cosmetology, aesthetic, or manicuring schools default on their educational commitment, BORC should annually determine that surety bond coverage is obtained and current. Moreover, BORC should review and evaluate 240 CMR to determine whether the current surety bond amounts required therein are adequate.

Auditee's Response:

The BORC disagrees that it is required under law to hold the original bonds of each private Cosmetology School in Massachusetts. Rather, pursuant to MGL c. 75D, §14, each such school is responsible for forwarding a copy of its bond to the Department of Education. However, the BORC agrees that it is prudent to hold a duplicate copy of each such bond and has instituted procedures to do so...

Board Counsel, in coordination with the Executive Director and Computer Services, will also amend the cosmetology school renewal application to contain a provision attesting under the pains and penalties of perjury that the bond requirements set forth in MGL c 75D, §14 have been met.

With regard to the bond amounts, Board Counsel is presently drafting revised regulations, which will increase the amount of the bond to reflect the current market.

Auditor's Reply: We do not agree that private cosmetology school surety bond requirements fall within the guidelines of Chapter 75D of the Massachusetts General Laws. According to MGL Chapter 75D, Section 1, "the provisions of this chapter shall not apply to any schools giving instruction in health and allied health related occupational skills if such schools are licensed by any agency of the commonwealth. . . ." We therefore reassert that cosmetology schools are governed by Massachusetts General Laws, Chapter 112. This position was confirmed during our audit by the Deputy Director and Chief Counsel of the Division.

4. BORC Board Not Fully Constituted

As of April 2001, there were only six members on BORC's board, contrary to Chapter 13, Section 42, of the General Laws, which states that the board should consist of seven members appointed by the governor. The members of the board comprise five members that are licensed cosmetologists and two members that are representatives of the general public. Our review of the members' status and terms of appointment disclosed that BORC's board comprises only six members; the last appointment was made in April 2000. The vacant position must be filled by a representative of the general public. BORC's board indicated that it was experiencing difficulty filling the position due to the time demands on board members and because members are not compensated for their duties.

Failure to have a fully staffed BORC board as mandated by law may contribute to the inadequate representation, oversight and monitoring of the cosmetology profession.

Recommendation. The vacant position on the board must be filled in order to comply with the current legislation to ensure that the public is properly represented on the BORC and that the cosmetology industry is properly monitored and regulated.

Auditee's Response:

The BORC statute, MGL c. 13 §42, makes provisions for five (5) licensed cosmetologists and two (2) public members to be appointed by the governor. The Board is currently operating at almost full capacity with one (1) public member and all five (5) licensed cosmetologists. Due to board member resignations, it is unavoidable that some vacant positions occur from time to time. The BORC makes every effort to locate prospective members and forward potential candidates to the Governor's Office for review.

5. Improper Destruction of BORC Records

We selected a sample of license numbers issued by BORC and its contracted testing company to determine whether the numbers were issued, accounted for in the division's database, and supported by application files. As a result of our request for support of licenses issued by the testing company, BORC contacted the company and was informed that the company had shredded approximately 10,300 original applications and examinations during the period July 1995 to April 1999. Therefore, the division, which discovered the shredding of the documents as a direct result of our audit testing and document requests,

could not provide the actual applications and examinations conducted for cosmetology licenses that were issued.

Effective February 1, 1999, the division, acting on behalf of the BORC and the Board of Registration of Barbers (BORB), entered into an agreement with Assessment Systems, Inc. (ASI), a for-profit corporation based in Pennsylvania. BORC and BORB are charged with the administration of examinations leading to the licensure of cosmetologists and barbers, and ASI is a national testing firm with experience in the development and administration of professional and occupational licensing examinations.

Our review of the current contract the division has with the testing company notes the following in Section 10 – Record Retention, “ASI and the Division will, at a minimum, retain all documents and records related to each examination for a period of two (2) years from the date of the administration of that examination.” The contract language is not in compliance with the record retention guidelines on file with the Commonwealth’s Records Conservation Board. Disposal Schedule Number 26/85, approved July 9, 1985, and amended May 6, 1992, for the OCABR, governs the disposition of records for the division. Item 3 of the schedule, Applications For Registration, states that “registration files (for) licensed applicants may include applications, exam scores, transcript, etc., (to be) arranged numerically by application or licensed number... and shall be retained for 60 years.”

When we brought this noncompliance to the attention of the division’s Deputy Director for Professional Licensure, the deputy responded, in part:

In our contracts the records retention language you cited refers specifically to examinations. The two-year period is in accordance with Sections 2f and g of Disposal Schedule 26/85. The Division retains Registration Files for failed applicants for at least three years and licensed applicants for the requisite period.

However, the schedule clearly states that such registration data should be kept for 60 years. Moreover, some registration files were destroyed without being held for three years, contrary to the Deputy Director’s assertion.

The Agreement specifies, as one of ASI's responsibilities, that "ASI shall annually audit the examination/licensure process to verify the accuracy of the licensing data transmitted to the respective board." In response to our request for copies of audits for 1998 and 1999, BORC stated that in May 2000 it requested copies of the audits from ASI. However, as a result of our request, BORC requested that a tape match audit of ASI records to the division's licensing database be conducted. The audit disclosed 14 mismatches due to name changes out of 2,900 items sent during calendar year 2000. In addition, BORC indicated that it will have such audits conducted semi-annually.

We also found that the division is not in compliance with the requirements of the 801 CMR 21.00: Procurement of Commodities or Services, Including Human and Social Services. The code provides all departments with uniform rules and standards governing the procurement of commodities and services. All contracts negotiated by agencies and departments are required to have a signed Standard Contract Form on file. The form, which documents the terms and conditions of the contracts negotiated, is issued by the Executive Office for Administration and Finance, the Office of the Comptroller, and the Operational Services Division for use by all Commonwealth departments. For the ASI Agreement effective February 1, 1999, the division provided the Standard Contract Form that was signed in April 2000 by ASI and in May 2000 by the division, more than one year after the contract began.

Without the proper licensing and examination documents on file and available for independent review, the division cannot be assured that all cosmetology licenses are valid and issued to qualified candidates. Moreover, as previously mentioned, failure to have proper documentation and internal controls can result in the issuance of fraudulent licenses.

Recommendation: Controls should be in place to ensure that testing companies retain documents as required. The division should review the existing contracts with testing companies and perform periodic spot checks of records and facilities to determine that the contract language and processes comply with the record retention guidelines. The division should consider whether amendments should be made to the current disposal schedule to standardize the retention period for all division records. However, until such amendments are made, the division should maintain documents and files as required by legislation and

regulations and adopt and follow procedures as necessary to comply with all applicable laws and regulations regarding procurement of commodities and services.

Auditee's Response:

In a breach of specific contract terms, the private professional testing company with which BORC contracted failed to retain original applications and examinations and further failed to return them to the BORC for proper archiving. When BORC became aware of this, [the company] was immediately notified, through both oral and written communication on several occasions.

Upon request by BORC, [the company] implemented a program designed to reconstruct the records as fully as possible in order to meet the requirements of the Commonwealth Records Conservation Board.

6. Chapter 647 Report Not Filed

As noted in Audit Result No. 1, a former BORC employee was engaged in the fraudulent issuance and sale of cosmetology licenses. However, our review indicated that, although BORC became aware of this fraudulent activity in September 1999, it did not file a required "Report on Unaccounted for Variances, Losses, Shortages, or Thefts of Funds or Property" with the Office of the State Auditor (OSA) until April 10, 2000.

Chapter 647 of the Acts of 1989, "An Act Relative to Improving the Internal Controls within State Agencies," states in part:

All unaccounted-for variances, losses, shortages, or thefts of funds or property shall be immediately reported to the state auditor's office, who shall review the matter to determine the amount involved which shall be reported to appropriate management and law enforcement officials.

The prompt reporting of all such losses ensures that the OSA can conduct an independent review to determine the internal control weaknesses and conditions that allowed the fraudulent activity to occur, determine the amount involved to be reported to management and law enforcement officials, and recommend the necessary corrective action to be taken by management to correct any deficiencies and preclude further occurrences of such activities.

BORC officials claimed that they did not immediately file a 647 Report with the OSA on instructions of the Office of the Attorney General, which prosecuted the former BORC employee.

Recommendation: BORC should take the necessary measures to ensure that it complies with Chapter 647 of the Acts of 1989 and immediately report all unaccounted-for variances, losses, and thefts of funds or property to the OSA.

Auditee's Response:

BORC believes that the spirit and intent of Chapter 647 was fully met by BORC's full and open disclosure to the Office of Consumer Affairs and to the Attorney General's Office. The BORC, while aware of the requirements for reporting losses or thefts of property, was fully involved with the Department of the Attorney General and the State Police, both of whom were notified by the BORC immediately upon discovery of the possibility of mishandling of BORC licenses. The Division General Counsel, in conjunction with the Attorney General's Office, advised BORC that the Assistant Attorney General responsible for the prosecution of the matter had requested that BORC not make any disclosure of the pending investigation due to the sensitive nature of the investigation and the Attorney General's desire to locate and prosecute any and all potential individuals involved in the license mishandling. BORC did, through General Counsel, inform the Director of the Office of Consumer Affairs and fully cooperated with all law enforcement officials to ensure that all persons responsible were brought to justice.

Auditor's Reply: While we understand that BORC believes that the spirit and intent of Chapter 647 was met, we respectfully submit that the requirement of the law is to immediately notify the Office of the State Auditor. (See Appendix I) Therefore, regardless of any other agencies that were notified, it is the mandated responsibility of the department that incurred the fraud to meet this requirement to ensure that the OSA can determine in a timely manner the internal control weaknesses and conditions that allowed the fraudulent activity to occur and recommend the necessary corrective action to be taken by management.

APPENDIX I

Chapter 647, Acts of 1989

An Act Relative to Improving the Internal Controls within State Agencies

H 5

Chapter 647

THE COMMONWEALTH OF MASSACHUSETTS

In the Year One Thousand Nine Hundred and Eighty-nine

AN ACT RELATIVE TO IMPROVING THE INTERNAL CONTROLS WITHIN STATE AGENCIES.

Be it enacted by the Senate and House of Representatives in General Court assembled, and by the authority of the same, as follows:

Notwithstanding any general or special law to the contrary, the following internal control standards shall define the minimum level of quality acceptable for internal control systems in operation throughout the various state agencies and departments and shall constitute the criteria against which such internal control systems will be evaluated. Internal control systems for the various state agencies and departments of the commonwealth shall be developed in accordance with internal control guidelines established by the office of the comptroller.

(A) Internal control systems of the agency are to be clearly documented and readily available for examination. Objectives for each of these standards are to be identified or developed for each agency activity and are to be logical, applicable and complete. Documentation of the agency's internal control systems should include (1) internal control procedures, (2) internal control accountability systems and (3), identification of the operating cycles. Documentation of the agency's internal control systems should appear in management directives, administrative policy, and accounting policies, procedures and manuals.

(B) All transactions and other significant events are to be promptly recorded, clearly documented and properly classified. Documentation of a transaction or event should include the entire process or life cycle of the transaction or event, including (1) the initiation or authorization of the transaction or event, (2) all aspects of the transaction while in process and (3), the final classification in summary records.

(C) Transactions and other significant events are to be authorized and executed only by persons acting within the scope of their authority. Authorizations should be clearly communicated to managers and employees and should

APPENDIX I (Continued)Chapter 647, Acts of 1989An Act Relative to Improving the Internal Controls within State Agencies

H 5

Include the specific conditions and terms under which authorizations are to be made.

(D) Key duties and responsibilities including (1) authorizing, approving, and recording transactions, (2) issuing and receiving assets, (3) making payments and (4), reviewing or auditing transactions, should be assigned systematically to a number of individuals to ensure that effective checks and balances exist.

(E) Qualified and continuous supervision is to be provided to ensure that internal control objectives are achieved. The duties of the supervisor in carrying out this responsibility shall include (1) clearly communicating the duties, responsibilities and accountabilities assigned to each staff member, (2) systematically reviewing each member's work to the extent necessary and (3), approving work at critical points to ensure that work flows as intended.

(F) Access to resources and records is to be limited to authorized individuals as determined by the agency head. Restrictions on access to resources will depend upon the vulnerability of the resource and the perceived risk of loss, both of which shall be periodically assessed. The agency head shall be responsible for maintaining accountability for the custody and use of resources and shall assign qualified individuals for that purpose. Periodic comparison shall be made between the resources and the recorded accountability of the resources to reduce the risk of unauthorized use or loss and protect against waste and wrongful acts. The vulnerability and value of the agency resources shall determine the frequency of this comparison.

Within each agency there shall be an official, equivalent in title or rank to an assistant or deputy to the department head, whose responsibility, in addition to his regularly assigned duties, shall be to ensure that the agency has written documentation of its internal accounting and administrative control system on file. Said official shall, annually, or more often as conditions warrant, evaluate the effectiveness of the agency's internal control system and establish and implement changes necessary to ensure the continued integrity of the system. Said official shall in the performance of his duties ensure that: (1) the documentation of all internal control systems is readily available for examination by the comptroller, the secretary of administration and finance and the state auditor, (2) the results of audits and recommendations to improve departmental internal controls are promptly evaluated by the agency management, (3) timely and appropriate corrective actions are effected

APPENDIX I (Continued)

Chapter 647, Acts of 1989

An Act Relative to Improving the Internal Controls within State Agencies

H 5

by the agency management in response to an audit and (4), all actions determined by the agency management as necessary to correct or otherwise resolve matters will be addressed by the agency in their budgetary request to the general court.

All unaccounted for variances, losses, shortages or thefts of funds or property shall be immediately reported to the state auditor's office, who shall review the matter to determine the amount involved which shall be reported to appropriate management and law enforcement officials. Said auditor shall also determine the internal control weaknesses that contributed to or caused the condition. Said auditor shall then make recommendations to the agency official overseeing the internal control system and other appropriate management officials. The recommendations of said auditor shall address the correction of the conditions found and the necessary internal control policies and procedures that must be modified. The agency oversight official and the appropriate management officials shall immediately implement policies and procedures necessary to prevent a recurrence of the problems identified.

House of Representatives, December 21, 1989.

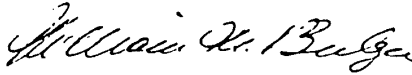
Passed to be enacted,



, Speaker.

In Senate, December 22, 1989.

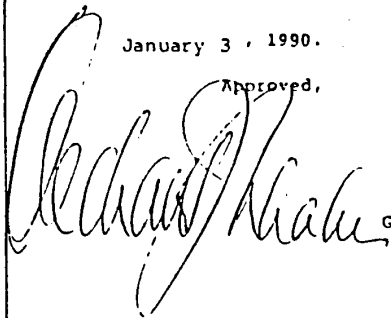
Passed to be enacted,



, President.

January 3, 1990.

Approved,



Governor.

APPENDIX IIChapter 647 Awareness LetterFrom the State Auditor and the State Comptroller

The Commonwealth of Massachusetts

Office of the State Auditor
State House
Boston, MA 02133

Office of the Comptroller
One Ashburton Place
Boston, MA 02108

September 19, 2000

Legislative Leadership
Judicial Branch Administrators
Elected Officials
Secretariats
Department Heads

The State Auditor and the Comptroller are both committed to departmental improvements in the Internal Control structure of the Commonwealth. A good system of controls, as you know, assists management in meeting objectives while avoiding serious problems. Chapter 647 of the Acts of 1989, *An Act Relative To Improving Internal Controls Within State Agencies*, establishes acceptable Internal Control systems for state government operations and constitutes the criteria against which we will evaluate internal controls. With the passage of this law, we began a campaign to educate all department staff on the significant role of internal controls in department operations.

In the past few years, departments have made significant progress in the area of internal controls. Every department has certified that they have documented internal controls in the form of an Internal Control Plan. In Fiscal Year 2001, we are focusing our Internal Control Campaign on the review of department risk assessments, as documented within the departments' internal control plans. Internal control plans must, of course, include all aspects of a department's business, programmatic operations as well as financial.

A major requirement of Chapter 647 is that "an official, equivalent in title or rank to an assistant or deputy to the department head, shall be responsible for the evaluation of the effectiveness of the department's internal controls and establish and implement changes necessary to ensure the continued integrity of the system". This official, whom we refer to as the Internal Control Officer, is responsible for ensuring that the plan is evaluated annually or more often as conditions warrant.

During this annual Statewide Single Audit, we continue with our review of the Commonwealth's internal controls. We analyze and evaluate information obtained during the audit process in our continuing effort to educate agencies regarding both the need for internal controls and the risks of not having adequate internal controls in place.

APPENDIX II (Continued)
Chapter 647 Awareness Letter
From the State Auditor and the State Comptroller

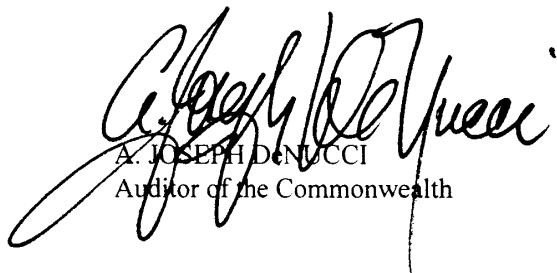
To assist departments with this effort, we provide the following support activities:

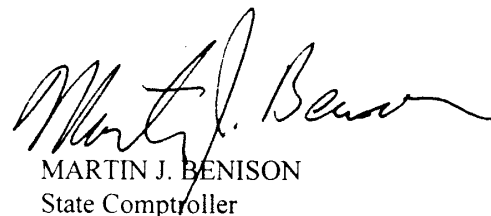
- ◆ The Office of the Comptroller offers departments free monthly training on internal controls. These classes are listed in the *OSC Training Bulletin*.
- ◆ The Office of the Comptroller provided a new document entitled the *Internal Control Guide for Managers* on the Office of the Comptroller's Web page: <http://www.osc.state.ma.us/>. Part II of the guide will be available shortly and will replace the current *Internal Control Guide for Departments*, currently available on the Web.
- ◆ Upon request, the Office of the Comptroller provides assistance to departments in the process of redefining or reviewing their internal control plans.
- ◆ As part of the Statewide Single Audit, auditors will review and comment upon departments' internal control plans, risk assessments, and the reporting level of the Internal Control Officers.
- ◆ We have updated and automated the Internal Control Questionnaire (ICQ) for easier submission. These changes to the ICQ will enable OSA and OSC to evaluate department internal controls and monitor their progress.

Chapter 647 also requires that "all unaccounted for variances, losses, shortages, or thefts of funds or property be immediately reported to the Office of the State Auditor" (OSA). The OSA is required to determine the amount involved and the internal control weaknesses that contributed to or caused the condition, make recommendations for corrective action, and make referrals to appropriate law enforcement officials. In order to comply with this law instances must be reported on the *Report on Unaccounted for Variances, Losses, Shortages, or Thefts of Funds or Property* and be submitted to the OSA. Reporting forms can be obtained by contacting the Auditor's office, Room 1819, McCormack State Office Building, or Web Site: <http://www.magnet.state.ma.us/sao/>.

In conjunction with the above requirement, please note that management is responsible for financial records and systems and must inform, disclose and make representations to the auditors with regards to their management of funds, account activities, programs and systems.

The Offices of the State Comptroller and the State Auditor are committed to the goal of improving the Internal Control structure of the Commonwealth. Thank you for your cooperation and attention on this worthwhile task. Please do not hesitate to call upon the staff of either office for assistance.


A. JOSEPH DENUCCI
Auditor of the Commonwealth


MARTIN J. BENISON
State Comptroller