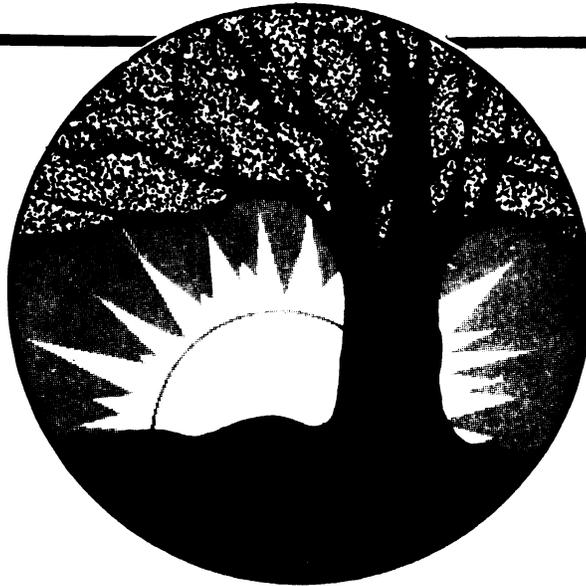


# PERFORMANCE AUDIT

Professional Regulatory Boards  
December 2009



Justin P. Wilson  
Comptroller of the Treasury



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Comptroller of the Treasury  
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December 29, 2009

The Honorable Ron Ramsey  
Speaker of the Senate  
The Honorable Kent Williams  
Speaker of the House of Representatives  
The Honorable Bo Watson, Chair  
Senate Committee on Government Operations  
The Honorable Susan Lynn, Chair  
House Committee on Government Operations  
and  
Members of the General Assembly  
State Capitol  
Nashville, Tennessee 37243

Ladies and Gentlemen:

Transmitted herewith is the performance audit of 11 Professional Regulatory Boards. This audit was conducted pursuant to the requirements of Section 4-29-111, *Tennessee Code Annotated*, the Tennessee Governmental Entity Review Law.

This report is intended to aid the Joint Government Operations Committee in its review to determine whether the 11 Professional Regulatory Boards should be continued, restructured, or terminated.

Sincerely,

Arthur A. Hayes, Jr., CPA  
Director

AAH/dlj  
09-039

State of Tennessee

# Audit Highlights

Comptroller of the Treasury

Division of State Audit

Performance Audit  
**Professional Regulatory Boards**  
December 2009

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## AUDIT OBJECTIVES

The objectives of the audit were to determine the self-sufficiency of the boards and the appropriateness of cost allocation; the timeliness of complaint processing; the sufficiency of monitoring controls over RBS access; whether boards have sufficient verification procedures for applicant information; the sufficiency of board policies that ensure fair and consistent treatment of applicants and licensees by the board; and minority representation among board staff and board membership.

## FINDINGS

**As Found in Both the 1999 and 2005 Performance Audits of the Included Professional Regulatory Boards, the Division and the Individual Boards' System for Processing Complaints Needs Improvement**

Complaint processing continues to be an issue for the professional regulatory boards. There are still few procedures requiring boards to document and record specific complaint information in a standardized format. Division and board management have not developed the tools to provide themselves with the data needed to efficiently and effectively manage complaints (page 8).

**The Department and Division Should Improve Information Security Controls Over Access to the RBS Computer System That Manages Licensing and Complaint Information**

The auditors observed conditions that violated best practices for information security controls

during the audit. The wording of this finding does not identify specific vulnerabilities that could allow someone to exploit the regulatory boards' computer system. Disclosing these vulnerabilities could present a potential security risk by providing readers with information that might be confidential pursuant to Section 10-7-504(i), *Tennessee Code Annotated*. We provided the Division of Regulatory Boards, Department of Commerce and Insurance, with detailed information regarding specific vulnerabilities as well as our recommendations for improvement (page 14).

**Many Boards Do Not Conduct Criminal Background Checks, Even Though Licensing Regulations Require Applicants to Be of Good Moral Character, Honest, and/or Trustworthy and Free of Criminal Convictions**

Only the Private Investigation and Polygraph Commission and Private Protective Services

have the explicit statutory requirement to conduct state and federal criminal background checks on private investigator and security guard applicants, and do conduct those checks (through the TBI and FBI) for initial licensure. However, under Section 38-6-120, *Tennessee Code Annotated*, all state regulatory boards may request state criminal background checks through the TBI. The boards solely rely on self-

reporting by the licensee and do not conduct subsequent criminal background checks on license renewals. However, failure to conduct background checks limits the division's ability to determine whether applicants meet statutory licensure requirements and identify applicants with prior disciplinary problems, and limits its ability to safeguard the citizens of the state from problem licensees (page 15).

## **OBSERVATIONS AND COMMENTS**

The audit also discusses the following issues: the self-sufficiency of regulatory boards; the need for improvement in the regulatory boards' policies, procedures, and rules; statutory changes needed to remove the licensure requirement to sell funeral merchandise; the need for a review of the Private Protective Services Advisory Committee's usefulness and inclusion in the Sunset law; and concerns that the public members of the Tennessee Real Estate Commission and the Board of Examiners for Architects and Engineers may present a potential conflict of interest as they derive their livelihood from the industry or have a personal interest in the industry by association (page 19).

## **ISSUES FOR LEGISLATIVE CONSIDERATION**

The General Assembly may wish to consider the following statutory changes to improve the efficiency and effectiveness of the 11 audited Professional Regulatory Boards' operations.

1. The General Assembly may wish to consider amending statute to specifically require the boards in the Division of Regulatory Boards, Department of Commerce and Insurance, to conduct at least state, if not also federal, criminal background checks on all licensees.
2. General Assembly may wish to reconsider how regulatory activities are funded. If the state chooses not to appropriate funding for these regulatory activities, the use of revenues and fines collected from licensees should be restricted to activities associated with regulating that profession.
3. If it is the General Assembly's intention that the boards not accumulate large reserves, the General Assembly may wish to amend statutes by capping allowed reserves based on a certain percentage of the boards' operating expenses and requiring the boards to lower licensing fees or rebate funds back to licensees.
4. The General Assembly may wish to further define its intentions regarding self-sufficiency requirements for regulatory boards to clarify whether it intended each individual regulatory board's revenues to cover all actual expenses incurred by that board (whether classified as direct or indirect costs) to function and perform its statutory duties.
5. The General Assembly may wish to charge the commissioners of the Department of Finance and Administration and the Department of Commerce and Insurance with periodically assessing the current sufficiency of the \$5 fee collected annually on each active license to cover indirect costs

and ensuring that the state regulatory fees collected are earmarked specifically to offset certain costs incurred by the state's regulatory boards in performing their statutory duties.

6. The General Assembly may wish to consider revising Title 62, Chapter 5, Parts 1 and 3, to clarify licensing requirements for selling funeral merchandise based on court interpretations.
7. The General Assembly may wish to consider the usefulness of the Private Protective Services Advisory Committee as an advisory committee and whether it should transform the committee into a true professional regulatory board for security services, particularly as there are a large number of complaints against private protective services licensees. Otherwise, we recommend the committee's removal from the sunset statute, since private protection service regulation and licensing authority lie with the Commissioner of Commerce and Insurance, and the regulatory activities will continue with or without the advisory committee. In addition, the advisory committee is not required to regularly meet and advise the commissioner, and the commissioner can at any time call upon professional experts for their opinions.
8. The General Assembly may wish to further clarify in statute its intentions regarding the presence of public members on regulatory boards and how separate the public members need to be from the particular profession.

# Performance Audit Professional Regulatory Boards

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# Performance Audit Professional Regulatory Boards

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## INTRODUCTION

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### PURPOSE AND AUTHORITY FOR THE AUDIT

This performance audit of 11 Professional Regulatory Boards was conducted pursuant to the Tennessee Governmental Entity Review Law, *Tennessee Code Annotated*, Title 4, Chapter 29. Under Section 4-29-231, these 11 Professional Regulatory Boards are scheduled to terminate June 30, 2010. The Comptroller of the Treasury is authorized under Section 4-29-111 to conduct a limited program review audit of the boards and to report to the Joint Government Operations Committee of the General Assembly. The audit is intended to aid the committee in determining whether these 11 Professional Regulatory Boards should be continued, restructured, or terminated.

*Board of Examiners for Architects and Engineers*  
*Auctioneer Commission*  
*Board of Barber Examiners*  
*Collection Service Board*  
*Board of Cosmetology*  
*Board of Funeral Directors and Embalmers*  
*Board of Examiners for Land Surveyors*  
*Private Investigation and Polygraph Commission*  
*Private Protective Services Advisory Committee*  
*Real Estate Appraiser Commission*  
*Real Estate Commission*

### OBJECTIVES OF THE AUDIT

The objectives of the audit were

1. to determine the self-sufficiency of the boards and the appropriateness of cost allocation;
2. to determine the timeliness of complaint processing;
3. to determine the sufficiency of monitoring controls over Regulatory Boards System (RBS) access;
4. to determine whether the boards have sufficient verification procedures for applicant information;
5. to determine the sufficiency of board policies that ensure fair and consistent treatment of applicants and licensees by the board; and
6. to determine minority representation among board staff and board membership.

## **SCOPE AND METHODOLOGY OF THE AUDIT**

The activities of the 11 Professional Regulatory Boards were reviewed for the period July 1, 2004, through June 30, 2008. 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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. Evidence obtained came from sources that included

1. review of applicable legislation and policies and procedures;
2. examination of board files, documents, inspections, meeting minutes, licensee files (paper and electronic), and policies and procedures;
3. attendance at board meetings; and
4. interviews with department staff and staff of other state agencies that interact with the department.

## **STATUTORY RESPONSIBILITIES**

The Department of Commerce and Insurance's Division of Regulatory Boards provides staff and administrative support to the various boards and commissions that perform the occupational licensing and regulation of professions in Tennessee. The boards are responsible for ensuring that licensees comply with the laws and regulations of their professions and for protecting the public from any licensee's unprofessional conduct or illegal activity.

Board of Examiners for Architects and Engineers - Title 62, Chapter 2. The board has the authority to issue and regulate licenses for architects, engineers, landscape architects, and interior designers and their related firms.

Auctioneer Commission - Title 62, Chapter 19. The commission is responsible for examining and licensing auctioneers, apprentice auctioneers, and firms engaged in the auction industry in Tennessee.

Board of Barber Examiners - Title 62, Chapter 3. The board enforces the rules and regulations governing the profession of barbering through certification of master barbers, technicians, and instructors, and certification and inspection of barber schools and shops.

Collection Service Board - Title 62, Chapter 20. The board is responsible for examining and licensing collection service firms and collection managers working in the collections industry in Tennessee.

Board of Cosmetology - Title 62, Chapter 4. The board has responsibility for enforcing the rules and regulations governing the professions of cosmetology and manicuring through licensing of cosmetologists, manicurists, aestheticians, shampoo technicians, natural hair stylists, and instructors, and licensing and inspection of shops and schools.

Board of Funeral Directors and Embalmers - Title 62, Chapter 5. This board licenses and regulates the professions of funeral directing and embalming through registration of apprentices, licensing of funeral directors and embalmers, and licensing and inspections of funeral establishments.

Board of Examiners for Land Surveyors - Title 62, Chapter 18. The board is responsible for certifying land surveyors working in Tennessee.

Private Investigation and Polygraph Commission - Title 62, Chapters 26 and 27. The commission's purpose is to issue and regulate licenses for private investigators, private investigation firms, and polygraph examiners.

Private Protective Services Advisory Committee - Title 62, Chapter 35. The committee's purpose is to advise the Commissioner of Commerce and Insurance on rulemaking and to make formal recommendations to the commissioner or the General Assembly about issues relating to private security matters. The commissioner licenses private security companies and registers security guards/officers. During audit fieldwork, all committee members' terms had expired and the committee was not active.

Real Estate Commission - Title 62, Chapter 13. The commission licenses affiliate brokers, brokers, real estate firms, and time-share agents.

Real Estate Appraiser Commission - Title 62, Chapter 39. The commission regulates, licenses, and certifies real estate appraisers to ensure compliance with the federal Financial Institutions Reform, Recovery and Enforcement Act of 1989.

## **BOARD COMPOSITION AND ORGANIZATION**

Each board is composed of licensed industry members who may be selected from lists of names submitted by relevant trade and professional associations. In addition, the boards have one or two public members. The Governor is the appointing authority for all of the boards covered in this audit except the Private Protective Services Advisory Committee, whose members are appointed by the Commissioner of Commerce and Insurance. This advisory committee was inactive during our audit fieldwork.

The boards have either an administrator or an executive director and staff who are responsible for the board's administrative functions and who report to the board members (but are considered Department of Commerce and Insurance employees). Many boards share staff. Four of the boards in this audit (Auctioneers, Land Surveyors, Real Estate Appraisers, and Collection Service) are part of the Small Boards Unit that is comprised of a total of ten boards with four directors that share five staff positions. Two other boards in this audit (the Private Investigation and Polygraph Commission and the Private Protection Services Advisory Committee) share one director and 16 staff positions with an additional three boards not included in this audit. The Barber and Cosmetology boards share one director and 18 staff positions. The administrative functions of these Professional Regulatory Boards include, but are not limited to, processing applications and renewal notices, licensing, preparing board meeting agendas and

minutes, and handling complaints. The boards' renewal periods, license application fees, and license renewal fees vary. Fees also vary within each board by type of license. In addition to the board staff, the Division of Regulatory Boards has a pool of attorneys and investigators who assist in investigating and handling complaints. A few boards still have their own investigators/inspectors on staff.

The boards maintain data on all licensees using the Regulatory Boards System (RBS), an on-line computer system. This system produces license renewal notifications and licenses, and is also used for tracking applications for licenses, license fee payments, and continuing education information. Some boards use the system to assign a number to a complaint and to enter complaint information. All 11 boards covered in this audit are on the RBS system.

**Board License Periods, Renewal Amounts, and Licensees  
As of October 13, 2009**

<b>Board</b>	<b>License Period and Expiration Date</b>	<b>Renewal Amount</b>	<b>Number of Licensees (b)</b>
Board of Examiners for Architects and Engineers	Biennially on Date of Issue	\$140	14,479 individuals; 4,652 firms
Auctioneer Commission	Biennially on Date of Issue	\$75-175 (a)	1,827 individuals; 1,172 firms
Board of Barber Examiners	Biennially on Date of Issue	\$80 individuals; \$90 instructors; \$100 shops; \$350 schools	5,032 individuals; 2,095 shops; 18 schools
Collection Service Board	Biennially on Date of Issue	\$350 individuals; \$100 branch office; \$50 location mgr	786 individuals; 556 agencies; 18 branch offices
Board of Cosmetology	Biennially on Date of Issue	\$50	46,318 individuals; 8,395 shops; 68 schools
Board of Funeral Directors and Embalmers	Biennially on Date of Issue	\$275 individuals; \$575 establishments	3,568 individuals; 556 establishments
Board of Examiners for Land Surveyors	Biennially on December 31	\$280	1,205 individuals
Private Investigation and Polygraph Commission	Biennially on Date of Issue	\$100 individuals; \$100-\$1,000 company, based on size	1,231 individuals; 648 firms
Private Protective Services Advisory Committee	Biennially on Date of Issue	\$50 unarmed; \$60 armed; \$300-\$600 company, based on size	19,997 individuals; 302 trainers; 1,202 firms
Real Estate Appraiser Commission	Biennially on Date of Issue	\$350	2,260 individuals
Real Estate Commission	Biennially on Date of Issue	\$80	28,616 individuals; 4,472 firms

Notes:

(a) Includes individuals and companies.

(b) Numbers do not include those required only to register with a board.

Source: Title 62, Sections 2-39, *Tennessee Code Annotated*; Rules; RBS reports.

## REVENUES AND EXPENDITURES

	Fiscal Year 2005	Fiscal Year 2006	Fiscal Year 2007	Fiscal Year 2008
		<b>Architects &amp; Engineers</b>		
Net Fee Revenue*	\$1,330,696	\$1,292,225	\$1,389,856	\$1,409,015
Direct Expenditures	994,179	961,041	992,904	1,084,605
Indirect Costs	265,710	222,119	259,094	201,308
Expenditures Total	1,259,889	1,183,160	1,251,999	1,285,913
Fees Less Expenditures	70,807	109,065	137,858	123,102
Adjustments to Reserve	0	0	(1,278)	(1,285,954)
End of Year Reserve Acct.	\$1,368,520	\$1,477,585	\$1,614,165	\$451,313
Indirect Costs as % of Total Exp.	21%	19%	21%	16%
		<b>Auctioneer</b>		
Net Fee Revenue*	\$252,932	\$235,985	\$247,416	\$258,357
Direct Expenditures	181,425	167,813	143,414	164,062
Indirect Costs	71,505	83,418	101,833	83,450
Expenditures Total	252,930	251,231	245,247	247,512
Fees Less Expenditures	2	(15,246)	2,169	10,845
Adjustments to Reserve	0	0	(825)	(43,650)
End of Year Reserve Acct.	\$62,026	\$46,780	\$48,124	\$15,319
Indirect Costs as % of Total Exp.	28%	33%	42%	34%
		<b>Barber</b>		
Net Fee Revenue*	\$339,094	\$361,982	\$376,215	\$360,177
Direct Expenditures	222,901	218,979	245,798	255,538
Indirect Costs	111,863	124,540	130,281	144,214
Expenditures Total	334,764	343,520	376,079	399,752
Fees Less Expenditures	4,330	18,462	136	(39,575)
Adjustments to Reserve	0	0	(875)	0
End of Year Reserve Acct.	\$(181,844)	\$(163,381)	\$(164,121)	\$(203,696)
Indirect Costs as % of Total Exp.	33%	36%	35%	36%
		<b>Collection Services</b>		
Net Fee Revenue*	\$260,000	\$285,210	318,957	350,815
Direct Expenditures	82,799	87,965	\$95,222	\$108,508
Indirect Costs	100,208	86,331	101,155	73,128
Expenditures Total	183,007	174,297	196,376	181,636
Fees Less Expenditures	76,993	110,913	122,581	169,179
Adjustments to Reserve	0	0	(835)	(766,903)
End of Year Reserve Acct.	\$628,674	\$739,587	\$861,333	\$263,609
Indirect Costs as % of Total Exp.	55%	50%	52%	40%

**Fiscal Year 2005    Fiscal Year 2006    Fiscal Year 2007    Fiscal Year 2008**

	<b>Cosmetology</b>			
Net Fee Revenue*	\$1,308,428	\$1,336,659	\$1,362,712	\$1,404,036
Direct Expenditures	845,904	798,890	859,566	880,060
Indirect Costs	259,768	356,429	342,640	501,081
Expenditures Total	1,105,672	1,155,319	1,202,206	1,381,141
Fees Less Expenditures	202,756	181,340	160,506	22,895
Adjustments to Reserve	0	0	(1,271)	(910,322)
End of Year Reserve Acct.	\$866,335	\$1,047,675	\$1,206,910	\$319,483
Indirect Costs as % of Total Exp.	23%	31%	29%	36%

	<b>Funeral Directors and Embalmers</b>			
Net Fee Revenue*	\$386,581	\$999,825	\$410,447	\$997,834
Direct Expenditures	305,880	337,619	416,354	436,435
Indirect Costs	136,868	165,555	170,638	195,030
Expenditures Total	442,749	503,174	586,993	631,465
Fees Less Expenditures	(56,168)	496,651	(176,545)	366,369
Adjustments to Reserve	0	0	(1,686)	(4,457)
End of Year Reserve Acct.	\$(503,198)	\$(6,547)	\$(184,778)	\$177,133
Indirect Costs as % of Total Exp.	31%	33%	29%	31%

	<b>Land Surveyors</b>			
Net Fee Revenue*	\$35,805	\$363,235	\$37,985	\$375,465
Direct Expenditures	94,668	91,699	76,149	88,167
Indirect Costs	95,878	72,612	79,275	55,312
Expenditures Total	190,546	164,311	155,424	143,479
Fees Less Expenditures	(154,741)	198,924	(117,439)	231,986
Adjustments to Reserve	0	0	(752)	(73,704)
End of Year Reserve Acct.	\$(122,565)	\$76,359	\$(41,831)	\$116,451
Indirect Costs as % of Total Exp.	50%	44%	51%	39%

	<b>Private Investigators and Polygraph Examiners</b>			
Net Fee Revenue*	\$222,846	\$238,824	\$247,196	\$234,185
Direct Expenditures	143,837	140,885	119,509	134,573
Indirect Costs	114,890	88,039	112,626	51,871
Expenditures Total	258,727	228,924	232,135	186,444
Fees Less Expenditures	(35,882)	9,900	15,061	47,742
Adjustments to Reserve	0	0	(872)	(212,240)
End of Year Reserve Acct.	\$214,896	\$224,796	\$238,986	\$74,487
Indirect Costs as % of Total Exp.	44%	38%	49%	28%

**Fiscal Year 2005    Fiscal Year 2006    Fiscal Year 2007    Fiscal Year 2008**

		<b>Private Protective Services</b>			
Net Fee Revenue*	\$1,002,609	\$1,108,800	\$1,176,395	\$1,215,364	
Direct Expenditures	546,041	494,641	459,528	534,624	
Indirect Costs	291,409	183,861	198,132	298,139	
Expenditures Total	837,450	678,502	657,661	832,762	
Fees Less Expenditures	165,159	430,298	518,735	382,602	
Adjustments to Reserve	0	0	(1,301)	(1,689,115)	
End of Year Reserve Acct.	\$951,586	\$1,381,884	\$1,899,318	\$592,805	
Indirect Costs as % of Total Exp.	35%	27%	30%	36%	
		<b>Real Estate Appraisers</b>			
Net Fee Revenue*	\$373,339	\$657,661	\$471,557	\$735,826	
Direct Expenditures	262,548	261,435	240,678	267,609	
Indirect Costs	135,442	140,064	177,641	160,483	
Expenditures Total	397,991	401,499	418,319	428,092	
Fees Less Expenditures	(24,652)	256,162	53,238	307,733	
Adjustments to Reserve	0	0	(1,296)	(443,373)	
End of Year Reserve Acct.	\$(16,860)	\$239,302	\$291,244	\$155,604	
Indirect Costs as % of Total Exp.	34%	35%	42%	37%	
		<b>Real Estate Commission</b>			
Net Fee Revenue*	\$2,192,930	\$1,163,492	\$3,012,756	\$3,686,583	
Direct Expenditures	1,529,063	1,435,751	1,710,403	1,841,507	
Indirect Costs	292,827	342,428	379,920	538,143	
Expenditures Total	1,821,890	1,778,179	2,090,323	2,379,651	
Fees Less Expenditures	371,040	(614,687)	922,433	1,306,933	
Adjustments to Reserve	0	0	(3,000)	(5,089,619)	
End of Year Reserve Acct.	\$5,264,171	\$4,649,484	\$5,568,917	\$1,786,231	
Indirect Costs as % of Total Exp.	16%	19%	18%	23%	
<b>Total for all 11 boards</b>					
Net Fee Revenue*	\$7,705,260	\$8,043,898	\$9,051,492	\$11,027,657	
Direct Expenditures	5,209,245	4,996,719	5,359,525	5,795,686	
Indirect Costs	1,876,369	1,865,396	2,053,236	2,302,160	
Expenditures Total	7,085,614	6,862,115	7,412,761	8,097,846	
Fees Less Expenditures	619,646	1,181,783	1,638,731	2,929,811	
Adjustments to Reserve	0	0	(13,989)	(10,519,338)	
End of Year Reserve Acct.	\$8,531,742	\$9,713,525	\$11,338,267	\$3,748,740	
Indirect Costs as % of Total Exp.	26%	27%	28%	28%	

\*Net Fee Revenue = Total Revenue minus State Regulatory Fee.

For the four fiscal years covered by this audit, only the Board of Barber Examiners was not self-sufficient across a two-year period.

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## FINDINGS AND RECOMMENDATIONS

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### **1. As found in both the 1999 and 2005 performance audits of the included professional regulatory boards, the division and the individual boards' system for processing complaints needs improvement**

#### **Finding**

Complaint processing continues to be an issue for the professional regulatory boards. There are still few procedures requiring boards to document and record specific complaint information in a standardized format. Division and board management have not developed the tools to provide themselves with the data needed to efficiently and effectively manage complaints.

#### 1999 Audit

In the 1999 performance audit, we found that the Division of Regulatory Boards did not have a uniform system to process complaints filed against licensees, and there was no central repository documenting complaint information and complaint status for all boards. All boards appeared to track general complaint information, but the type of information tracked was neither uniform nor accessible through a centralized data system. Some information was recorded in paper files, while other information was entered in RBS (Regulatory Boards System - the electronic information system used by the Division of Regulatory Boards). Thus, the division's ability to track complaints was limited.

Management concurred and responded in 1999 that the diversity of the professions regulated made it impractical to establish uniformity in the amount of time provided for licensees to respond to complaints. The division stated it was in the process of implementing enhancements to RBS to develop a single, more efficient source of complaint information and tracking.

#### 2005 Audit

In the 2005 performance audit, we found that the Division of Regulatory Boards had established written guidelines to provide a basic framework for handling complaints and a 180-day deadline for complaint resolution. However, a file review found that the guidelines were not consistently being followed and time frames were not being met. Board staff tracked progress on complaints in several different ways, with varying degrees of success, including the use of RBS, a ledger, tickler files, and a logbook, with each board using one or more of these mechanisms. The boards audited received 1,072 complaints in fiscal year 2004. Twenty-two percent had been closed (20% of which took over 180 days to close), while 78% remained open (42% of which had been open more than 180 days).

Management concurred in 2005 and stated that written guidelines had been followed to varying degrees by each board. They stated that the division created a Consumer Ombudsman position whose responsibility included addressing the inconsistency in complaint handling. The Consumer Ombudsman was to develop standard operating procedures for complaint handling with deadlines for all phases of the complaint process. All of the boards within the division were to be required to follow these procedures. The Consumer Ombudsman was also to be responsible for helping members of the public understand the complaint process, coordinating disciplinary action reports, and ensuring that respondents complied with disciplinary action. Management stated that they expected that the department would have a new case and complaint tracking system in the near future that would further assist in the uniform handling of these matters.

### 2006 Follow-Up

In April 2006, in the six-month follow-up to the 2005 audit, the department stated that it had evaluated complaint procedures and determined one standard operating procedure needed to be implemented for all boards. The department stated that this was officially implemented on August 1, 2005, and set time guidelines for each step of the complaint process and stipulated how these processes are to be tracked uniformly in RBS to ensure accuracy and consistency of data. The department also stated it was in the final stages of reviewing an informal audit recently completed by the Consumer Ombudsman of each licensing program's adoption of the standard operating procedures, focusing on timelines and tracking of complaints. The division was also in the process of developing and implementing a new electronic complaint tracking system that would be in place in 2007, that would further assist in the uniform handling of complaints, tracking repeat offenders, and ensuring respondents comply with disciplinary actions.

### 2009 Conditions

Today, in varying degrees, all the previously identified problems still exist as departmental attention was focused away from fixing the existing RBS/paper system and, instead, was focused on developing a new electronic information management system. Multiple vendors have tried and failed to provide a new electronic regulatory system that would have been used by multiple departments with regulatory duties (Commerce and Insurance, Health, Education, and Financial Institutions) and would have captured all information in one centralized system. A general review of the complaint processing system and complaint files revealed that various complaint information is recorded in administrative paper files maintained by regulatory board staff, is stored in paper files maintained by the legal section, and is entered in the RBS system. Occasionally, information in RBS does not match the information in the paper file. The type of information tracked is neither accessible through a centralized data system nor standardized and uniform. In addition to the information being stored in three different filing systems, each complaint is handled by three, and sometimes four different groups of people—board administrative staff, attorneys, investigators, and board members. However, the division is not ensuring that all the information is being captured about the length of time each group is handling a complaint before the complaint is sent on to the next step in the complaint process. The division is also not ensuring that the boards define each stage of the process the same way. For example, in determining when a complaint is closed, one board uses the final board action

date, another board uses the date the attorney's closure memo is received by board staff (which can take up to a month after final board action in some observed cases), and still another board uses a different date. Thus, management's ability to track the complaint process consistently between boards to ensure timely closure **and** to identify and resolve problematic stages of the process continues to be limited.

Performance Measure Targets Not Met. The Division of Regulatory Boards has been unable to meet the performance measure for percentage of complaints resolved within 180 days that it has set in its budget and strategic plan documents.

<b>Fiscal Year</b>	<b>Target Percentage Resolved Within 180 Days</b>	<b>Actual Percentage Resolved Within 180 Days</b>
2006-2007	85%	49%
2007-2008	60%	52%
2008-2009	70%	52%
2009-2010	70%	

Source: State's published annual budgets and agency strategic plans for fiscal years 2007-2009.

Current Status of Open Complaints. As of October 16, 2009, for the 22 boards and one office (Burial Services) that make up the Division of Regulatory Boards, 58% of open complaints have been open over 180 days. Following is a listing of open complaints as of October 16, 2009, for the 11 boards in this audit.

<b>Board or Commission</b>	<b>Board Meeting Frequency</b>	<b>Staff Attorney Positions<sup>3</sup></b>	<b>Number of Open Complaint Cases</b>	<b>Percentage of Complaints Over 180 Days</b>
Architects and Engineers	7-8/year	¼	44	48%
Auctioneers	5-8/year	⅕	45	13%
Barbers	5-7/year	⅓	71	77%
Collection Service	4-6/year	⅓	209	35%
Cosmetology	7-10/year	⅓	311	53%
Funeral Directors and Embalmers <sup>1</sup>	8-9/year	⅕	101	32%
Land Surveyors	3-4/year	¼	16	63%
Private Investigation and Polygraph	3-4/year	⅕	45	67%
Private Protective Services <sup>2</sup>	Na	½	315	68%
Real Estate	12/year	1	208	41%
Real Estate Appraisers	11-12/year	½*	107	42%

<sup>1</sup>Number of open complaint cases does not include those connected to the Burial Services Office.

<sup>2</sup>Private Protective Services Advisory Committee has not met since 2006.

<sup>3</sup>Fractions of an attorney position indicate that a single attorney is assigned to more than one board (e.g., a ¼ notation indicates that board shares one attorney with three other boards).

\*This attorney, on rare occasions, also assists a third board within the department but not in the scope of this audit.

It appears that attorney workloads and board meeting frequency, as noted in the chart above, may play a significant role in the timely resolution of complaints. Complaint files show that boards' administrative staff spend relatively little time on complaint intake and closure tasks. Most of the time a complaint is open occurs between the time the staff attorney receives the complaint file and when the board makes its final decision. After the staff attorney receives a complaint, the attorney may do some investigation on his or her own or may forward the case to the investigations section. Once the case is presented to the board, the board may request additional information or render a decision; the respondent may appeal the board's decision; the board may rehear the case; and ultimately, the case may require a hearing before an administrative law judge. However, these various phases of the process are not being reported and analyzed as part of management's responsibility for timely complaint processing. Because information concerning different stages of the complaint process is maintained in more than one place and format (i.e., by board staff and legal staff, in RBS and in paper files), and all individual stages of the complaint process are not centrally tracked, management still does not have all the information needed to identify the problem areas within the process and make any needed changes.

### **Recommendation**

Division of Regulatory Boards management should ensure that each board adopts and consistently applies the established complaint-handling guidelines. Management should adopt formal, written procedures that set time guidelines for all phases of the complaint process—receipt, correspondence with complainant/respondent, legal, investigations, initial/final board actions, etc.—and should ensure all boards and division staff capture the dates of such activities for management purposes.

The Commissioner of Commerce and Insurance should provide sufficient legal resources to the regulatory boards to ensure timely complaint processing. The commissioner, in conjunction with the boards, should also ensure that boards meet frequently enough to dispose of complaints as promptly as possible.

The division may wish to study its division-wide 180-day closure policy and determine whether it is realistic for all boards, particularly for the more technical professions such as real estate appraisers. When studying this issue, division and board management should also consider any federal guidelines or recommendations for complaint closure, such as the Federal Financial Institutions Examination Council Appraisal Subcommittee's one-year deadline for closure of complaints against licensed real estate appraisers.

Further, management should continue to pursue the establishment of an electronic system to replace RBS that captures all licensing and complaint information and can provide management with useful data and statistics that can be used to improve operations' efficiency and effectiveness.

## Management's Comments

### Comment From the Department of Commerce and Insurance

We concur with the general finding that the regulatory boards' system for processing complaints needs improvement. As part of the entrance interview with the Comptroller's auditors, division management discussed the comprehensive review of the regulatory boards' complaint-handling process that was initiated by new division management in 2008. New management's review of past audit findings and responses and a review of the existing conditions found that prior division management had diligently attempted to address the individual findings of previous audits and implement proposed solutions. However, new division management's review of the complaint-handling process concluded that a more comprehensive approach was needed to address the underlying issues and persistent challenges in making significant improvement in the efficiency and effectiveness of the complaint-handling process.

Specifically, management identified the following underlying issues:

- a) Concluded that there were insufficient legal resources and legal support resources to handle the volume of complaints and the other legal responsibilities to the board.
- b) Identified the turnover and attrition rate in the division's legal personnel as a structural challenge that compounded the previously identified issue (a), and was a major impediment to achieving and maintaining desired performance levels.
- c) Identified the lack of appropriate management tools/reports to identify bottlenecks and monitor progress in the complaint-handling process.
- d) Identified the lack of sufficient and/or appropriate investigatory or technical resources to support case preparation or presentation.
- e) Concluded that responsibility for various aspects of the complaint-handling process had become too diffuse and that sustained improvement in outcomes would come from driving shared accountability from the board staff and the legal department monitored by division management.

To address these underlying issues, new division management, in coordination with the department's legal division, began a systematic restructuring of the resources and processes supporting the complaint-handling process. Specifically:

1. Division management created four (4) new Attorney 3 positions to create a dedicated litigation unit to handle the formal disciplinary hearings by reclassifying existing vacant administrative positions. The new litigation team will have primary responsibility to conduct formal hearings under the Uniform Administrative Procedures Act. Each litigation unit attorney is being assigned to conduct such hearings for specific regulatory programs and to work in conjunction with the program attorneys in a team effort to maintain a historical knowledge base of the

- complaints in the event an attorney leaves the department. (Implemented October-December 2009)
2. Division management sought a budget improvement, and the General Assembly authorized one (1) new Attorney 4 position to assist the deputy general counsel in supervising and monitoring the program attorneys and to be available to fill any short-term gaps in program coverage due to attorney attrition or turnover. (Implemented July 2009)
  3. Prior division management created three (3) new paralegal positions to provide necessary support to the Legal Division in October 2007. New division management is reviewing if additional legal support positions are needed. (Begun in October 2009 and continues in process)
  4. Division management, in coordination with the Legal Division and the Real Estate Appraiser Commission staff, contracted the services of an expert witness to review complaints, to expedite the review process and improve the quality of the case preparation and analysis. (Implemented July 2009)
  5. Division management has installed new management in the division's investigation section to conduct a review and reorganization of the section's training, management and standard operating procedures. (Implemented December 2009)
  6. Division management has coordinated efforts with the department's IS department and the individual board complaint coordinators to create a common complaint tracking report format. Division management has directed board directors and staff attorneys to meet at least monthly to review progress on the complaint reports. (Implemented July 2009)
  7. Division management has directed board directors and their attorneys to draft new complaint intake forms that provide complainants better clarity and direction on how to describe and categorize actionable offenses by licensees. The new forms should help expedite and improve the processing of the initial complaints and assist in better tracking of data on the types of disciplinary cases being filed. (Begun in September 2009 and in process)
  8. Division management has worked with IS to develop a comprehensive management report that monitors the progress of every complaint as it works through the key phases of the complaint process. The report will highlight when specific complaints have exceeded the standard amount of time currently mandated in the Standard Operating Procedure (SOP). Division management will meet at least monthly with Legal Division management and each individual board director and staff attorney to review progress on complaint processing. (Implemented December 2009)
  9. Division management will review the data from the new comprehensive management report and determine if any practical changes need to be made to the complaint

process SOP, and will, at the next opportunity, transition the division's performance measure of a 180-day closure of complaints to more discreet tracking of the steps in the complaint process and establish in the SOP specific tracking requirements for all data. (Begun in December 2009 and continues in process)

10. Division management has directed department IS staff to monitor the progress of the Department of Health in its procurement process for a new regulatory tracking system and to begin the process to redefine the system requirements. (Begun March 2009 and continues in process)

We believe that the Comptroller's audit finding is consistent with the independent evaluation concluded earlier this year by new division management and that all of the Comptroller's recommendations have already been substantially implemented or will be shortly. Accordingly, we concur with all of the Comptroller's recommendations and will have them all implemented by July 1, 2010.

#### Comment From the Chairman of the Auctioneer Commission

We concur in part that the Auctioneer Commission should have a procedure manual in place to handle complaints and that more information is given when a complaint is initially filed. However, for most complaints over 180 days, we are usually waiting on the result of legal proceedings.

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## **2. The department and division should improve information security controls over access to the RBS computer system that manages licensing and complaint information**

### **Finding**

Division of Regulatory Boards' personnel, Department of Commerce and Insurance information systems personnel, Department of Finance and Administration's Office for Information Resources personnel, and some vendor personnel all have some level of access to RBS, the regulatory boards' computer system. The auditors observed conditions that violated best practices for information security controls during the audit.

The wording of this finding does not identify specific vulnerabilities that could allow someone to exploit the regulatory boards' computer system. Disclosing these vulnerabilities could present a potential security risk by providing readers with information that might be confidential pursuant to Section 10-7-504(i), *Tennessee Code Annotated*. We provided the Division of Regulatory Boards, Department of Commerce and Insurance, with detailed information regarding specific vulnerabilities as well as our recommendations for improvement.

## Recommendation

Department and division management should ensure that these conditions are remedied by the prompt development and implementation of effective controls. Management should ensure that risks associated with this finding are adequately identified and assessed in the department, division, and boards' risk assessments; this would include determining if any weaknesses have actually been exploited. Management should implement effective controls to ensure compliance with applicable requirements, assign staff to be responsible for ongoing monitoring of the risks and mitigating controls, and take action if deficiencies occur.

## Management's Comment

### Comment From the Department of Commerce and Insurance

We concur with the general finding. Department management has met with the Comptroller's audit staff to review the specific weaknesses identified and has developed and will have implemented appropriate procedures and effective controls to address or mitigate the concerns raised by January 15, 2010. Management's review of the identified weaknesses shows no evidence that those weaknesses were exploited in any way. Further, management's review found that the risks identified were either substantially limited to department staff access to information that is deemed a public record by statute or the potential risks were limited by other controls and procedures.

Department management will request to meet again with Comptroller's audit staff on or before January 31, 2010, to review that all appropriate steps have been taken to implement effective controls to ensure compliance with applicable requirements and that staff has been assigned to be responsible for ongoing monitoring of the risks and mitigating controls.

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### **3. Many boards do not conduct criminal background checks, even though licensing regulations require applicants to be of good moral character, honest, and/or trustworthy and free of criminal convictions**

#### Finding

The state's professional regulatory programs are intended to safeguard the public from unqualified and untrustworthy practitioners. Professional regulatory boards, under the authority of statute, establish and enforce rules and regulations detailing the qualifications each applicant is required to have to obtain a license and what the licensee must do in order to retain the license. With the exception of private investigator and security guard licensing, statute does not specifically require criminal background checks for the professions included in this audit. However, failure to conduct background checks limits the division's ability to determine whether

applicants meet statutory licensure requirements and identify applicants with prior disciplinary problems, and limits its ability to safeguard the citizens of the state from problem licensees.

By statute, all of the licensing boards included in this audit require for licensure that the applicant be of good moral character, of good repute, honest, or trustworthy. By statute, boards may also refuse to issue or renew, suspend, or revoke licenses if the licensee has been convicted of a crime in general or of particular crimes. The current practice is to require licensees to report any arrest and conviction information voluntarily on the license application or renewal form. Only the Private Investigation and Polygraph Commission and Private Protective Services have the explicit statutory requirement to conduct state and federal criminal background checks on private investigator and security guard applicants, and do conduct those checks (through the TBI and FBI) for initial licensure. However, under Section 38-6-120, *Tennessee Code Annotated*, all state regulatory boards may request state criminal background checks through the Tennessee Bureau of Investigation. For license renewal, all boards except Auctioneer and Collection Service request licensees to attest to the presence of any subsequent criminal activities or convictions. However, the boards solely rely on this self-reporting by the licensee and do not conduct subsequent criminal background checks on renewals.

### **Recommendation**

Board management should work with their individual boards and board staff to maximize consistency in evaluating more subjective licensing requirements, such as applicants' moral character, and should conduct state criminal background checks at initial licensure and periodically thereafter. The Division of Regulatory Boards should pursue legislation that would allow the boards to conduct a federal criminal background check through the Federal Bureau of Investigation as prescribed by Section 38-14-101 et seq., *Tennessee Code Annotated*, the National Crime Prevention and Privacy Compact. The fee for criminal background checks can be incorporated into licensing fees and passed along to the licensee as it has been with the Private Investigation and Polygraph Commission and Private Protective Services. Boards should also consider the specific types of offenses/convictions or other circumstances that might result in denial of an application or that should preclude someone from ever being licensed in a particular profession and may result in a permanent denial or revocation of a license. Where necessary, recommendations for statutory and rule changes should be made.

Board staff should, wherever available, use national databases, such as those currently used by the Real Estate Commission and the Board of Examiners for Architects and Engineers, to identify professional disciplinary actions originating outside Tennessee.

The General Assembly may wish to consider amending statute to specifically require the boards in the Division of Regulatory Boards, Department of Commerce and Insurance, to conduct at least state, if not also federal, criminal background checks on all licensees.

## Management's Comment

### Comment From the Department of Commerce and Insurance

We concur in part. The auditors correctly state that outside of the Private Protective Service program and the Private Investigation and Polygraph Commission, the regulatory entities subject to this performance audit lack explicit statutory authority to conduct state and federal criminal background checks through the Tennessee Bureau of Investigation (TBI) and the Federal Bureau of Investigation (FBI).

The Board of Examiners for Architects and Engineers, the Auctioneer Commission, the Board of Barber Examiners, the Collection Service Board, the Board of Cosmetology, the Board of Funeral Directors and Embalmers, the Board of Examiners for Land Surveyors, the Real Estate Appraiser Commission, and the Real Estate Commission do not have an explicit statutory requirement or authority to run state or federal criminal background checks on all licensees. All of the regulatory entities do require all licensees to disclose any criminal history.

Of these boards, only the Collection Service Board has specific statutory language that would explicitly bar licensure for specific criminal offenses within specific time periods. The remaining regulatory entities have more general provisions that provide a method for the regulatory bodies to deny or revoke a license on the basis of "good moral character" and/or a criminal conviction. In these instances, the finding of a criminal conviction is not an automatic statutory disqualification. At the same time, the act of failing to disclose the criminal conviction can result in the denial or revocation of a license.

Management concurs that the licensing review process for the Collection Service Board would be strengthened by requiring a state TBI criminal report for each licensee on initial licensure and renewal, because of the specific statutory prohibitions related to criminal history. Management intends to recommend to the Collection Service Board that it consider through the rule making process, requiring Collection Service Manager applicants to complete and pay the appropriate fee for a TBI criminal background check on initial application and renewal. There are currently 725 active Collection Service managers.

Management would defer to the will of the General Assembly to determine if the public interest is best served by authorizing and mandating state and federal criminal background checks for all licensees, as recommended by the Comptroller's auditors. The nine regulatory programs that do not currently conduct state or federal criminal background checks handle approximately 85,000 initial applications or renewals annually (the Division of Regulatory Boards handles a total of 161,000 initial applicants and renewals annually). Management estimates applicants would be charged a minimum of an additional \$50-60 per initial application and renewal to have their TBI and FBI criminal background checks run and reviewed by program staff. This would represent between **\$4-\$5 million** annually in additional fees paid by individuals seeking initial professional licenses or renewal for these nine programs. Additionally, it can take up to six weeks to get a complete FBI criminal background check completed, and management's experience with existing programs with background check requirements is that it can take licensees significant time and difficulty to get certified court documents to demonstrate the final adjudication or

disposition of prior criminal charges. This very issue is addressed in the Comptroller's September 2009 performance audit of the TBI that reported that 77% of arrests reported between 1995-2003 lacked dispositions and that 41% of arrests reported between 2001-2008 lacked dispositions.

As to the two programs that currently have the statutory authority to run state and criminal background checks, new division management in 2008 began a review of the criminal background check process for the Private Protective Service regulatory program. Under existing policy, program staff conducts a TBI criminal background check on initial licensure of unarmed security guards and FBI criminal background checks on all armed security guard applicants. After an extensive review of disciplinary records of licensees for 2008-2009, new division management instructed program staff to begin running TBI background checks on all armed guard renewals effective July 1, 2009. Management reallocated existing resources to begin in-house checking of the TBI criminal report for the approximately 2,000 armed guards that seek renewal annually (there are approximately 3,600 eligible armed guards that could seek renewal annually—but fewer actually seek renewal). Based on new management's review of the available data, management has proposed and will institute rule making that will add a federal criminal background check for all unarmed guards on initial licensure and all armed guards on renewal. The proposed rule would also require all unarmed guards to have state criminal background checks on renewal. These proposed changes can only be accomplished via rulemaking because it will require an additional expense be assessed to the licensee. Management intends to conduct the initial rule making hearing in February or March 2010.

Consistent with management's findings, division management will also recommend to the Private Investigation and Polygraph Commission that it conduct a similar review of its licensing and disciplinary data and consider where similar changes to the renewal of licensees to the Private Investigation and Polygraph Commission would be advised.

#### Comment From the Chairman of the Auctioneer Commission

We concur that there should be more clearly defined guidelines that would deny licensure, such as a national database as used by the Real Estate Commission.

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## OBSERVATIONS AND COMMENTS

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The topics discussed below did not warrant a finding but are included in this report because of their effect on the operations of the 11 Professional Regulatory Boards included in this audit and on the citizens of Tennessee.

### **Self-Sufficiency of Regulatory Boards**

The General Assembly has made clear, through statute and in continued discussion, that it expects the regulatory boards of this state to be self-sufficient by means of the licensing fees they collect. Sections 4-29-121 and 4-3-1011, *Tennessee Code Annotated*, respectively, require that the regulatory boards “collect fees in an amount sufficient to pay the cost of operating the board, commission or entity” and “the commissioner [of the Department of Finance and Administration] shall include the direct costs allocated to each board for the current fiscal year and the subsequent fiscal year, it being the legislative intent that fees and expenditures should be equal over a two-year period for each board.” The General Assembly also made it clear that it intended the monies collected from licensees, and only those monies, minus a \$5 state regulatory fee per license per year for indirect costs, be used solely for covering the costs of regulating those professions. Section 56-1-310, *Tennessee Code Annotated*, states that

- (a) Notwithstanding any law to the contrary, all moneys collected by any board attached to the division of regulatory boards pursuant to [TCA] 4-3-1304 shall be deposited in the state general fund and credited to a separate account for each board.
- (b) Disbursements from the accounts shall be made solely for the purpose of defraying expenses incurred in the implementation and enforcement of the boards’ areas of regulation.
- (c) The expenses shall not be paid from any other state funds.
- (d) Funds remaining in board accounts at the end of any fiscal year shall not revert to the general fund but shall remain available for expenditure in accordance with law.

Section 4-3-1011(b)(2), *Tennessee Code Annotated*, states, “In addition to the board fee, each regulatory board shall also assess a state regulatory fee in such amount as is set each year in the general appropriations act. The state regulatory fee shall be in lieu of any allocation of indirect costs that would otherwise be allocated to such boards.” Annual appropriations bills set this state regulatory fee at \$5 per license per year.

However, the General Assembly has not provided statutory definitions or explanation of what it intended by the terms “self-sufficiency,” “cost of operating,” and “direct costs.” This calls into question actual determinations of self-sufficiency for the regulatory boards by the Department of Finance and Administration, the Department of Commerce and Insurance, and the General Assembly. Are all costs of licensing and regulating each individual profession being captured and allocated to each individual regulatory board? What indirect costs is the state regulatory fee offsetting for each individual regulatory board? What are the implications of subsidizing those individual boards that are not self-sufficient and allowing others to accumulate large reserves by collecting more in fees than is needed to cover expenditures? What contingencies have been made by the departments and the General Assembly for unexpected expenditures, lawsuits, etc., following the transfer of board reserve funds to cover other state expenses outside the boards?

### Cost Allocation

Department of Commerce and Insurance and Division of Regulatory Boards administrative costs that are charged to the boards are not an individual board’s actual cost but are based on a complicated formula involving estimated averages of department and division totals and other subjective factors. The Department of Commerce and Insurance allocates administrative overhead costs to the Division of Regulatory Boards by determining, in relation to the department’s total expenditures, the average of the division’s percentage of total expenditures, percentage of full-time equivalent positions, percentage of purchase orders/contracts/travel authorizations, percentage of cash deposits, and percentage of mail opened. The Division of Regulatory Boards allocates its own internal administrative costs and the division’s part of departmental overhead costs to the individual regulatory boards by determining, in relation to division totals, each board’s average of the percentage of total licensees, percentage of staff assigned to each board, percentage of administrative effort required for each board (subjectively determined), and the percentage of travel expenditures. This allocation occurs following the end of the fiscal year.

Legal, investigative, and information systems costs are billed separately from departmental and division administrative costs. Legal costs (attorney salaries) are allocated at the end of the fiscal year to each board based on the estimated percentage of time attorneys spend on work for each board (attorneys do not track their billable hours) and a subjective complexity factor assigned to each board. The investigative costs are allocated at the end of the fiscal year to each board as a percentage of the total investigation expenses based on actual hours worked. The division’s information systems costs are allocated monthly to the individual boards using the same average percentage used to determine a board’s share of the departmental and division administrative costs.

Other factors complicating the complete accounting of regulatory board expenses include

- staff being shared between boards (9 of 11 boards in this audit share staff with at least one other board or section);

- some board staff occupying positions in another part of the division or department; and
- the department's Office of Internal Audit conducting routine work not normally associated with such an office for a few boards that is not captured and charged back specifically to those boards as an expense but is instead included in department administrative costs that are reallocated to all the department's divisions.

The Department of Commerce and Insurance refers to the departmental and division administrative costs allocated to the boards as "costbacks." In fiscal year 2008, costbacks as a percent of total expenditures ranged from 16% for the Board of Examiners for Architects and Engineers to a high of 40% for the Collection Service Board. The current formula used to allocate administrative, legal, and investigative costs back to the individual regulatory boards is overly complex and difficult to explain, even by departmental fiscal staff; if any errors were made in the calculation, it is unlikely that anyone at the individual board level would discover them. The department and division's communication of the extent of these administrative, legal, and investigative "costbacks" to the individual boards also appears to be a problem. Almost all of the costbacks are not allocated to the individual regulatory boards until after the end of the fiscal year, and board directors state they receive no costback information before then, forcing boards and their directors to estimate these expenses based on the past year and making it difficult for the individual boards and their directors to effectively manage their budgets.

If the department is not effectively recording, calculating, and reporting actual expenditures by the individual regulatory boards, then the boards' compliance with the statutory requirement that they be self-sufficient across a two-year period is called into question.

#### State Regulatory Fee Usage

Since 1989, a flat annual state regulatory fee of \$5 has been collected on each license and is meant to be in lieu of any allocation of indirect costs that would otherwise be allocated to the regulatory boards. At the end of each fiscal year, the Division of Regulatory Boards determines the number of active licensees and determines the amount of the fee for each board. These funds are then transferred to the Department of Finance and Administration (F&A). In fiscal year 2008, the 11 boards included in this audit were required to transfer \$861,560 to F&A; for fiscal years 2005-2008, the total amount transferred was \$3,281,645.

However, there is no indication whether, 20 years later, this flat \$5 fee still represents appropriate and current indirect costs. In light of statutory self-sufficiency requirements and requirements on the usage of the state regulatory fees collected, an assessment of the fee amount and an accounting of the disposition of the state regulatory fees by the Department of Finance and Administration and the Department of Commerce and Insurance is warranted.

#### Transfer of Board Reserve Funds

At the end of fiscal year 2008, the General Assembly passed Public Chapters 1191 and 1203 authorizing the legislature in fiscal years 2008 and 2009 to transfer funds from the

regulatory boards' reserve accounts. Of the 11 boards covered in this audit, all but 3 had 74% of their reserves taken by the Department of Finance and Administration, or a total of approximately \$10.5 million. The Board of Barber Examiners, the Board of Funeral Directors and Embalmers, and the Board of Examiners for Land Surveyors had 0%, 2.5%, and 39%, respectively, taken from their reserve accounts because they already had negative or very small reserve account balances.

Some boards, particularly those that issue licenses that do not require renewal every year, rely on their reserves to pay expenses in non-renewal years. During the period July 1, 2004, through June 30, 2008, the following boards and commissions used some of their reserves to make up the shortfall between license fee revenue and board expenditures and to meet self-sufficiency requirements in the noted fiscal year(s):

- Real Estate Commission – fiscal year 2006
- Auctioneer Commission – fiscal year 2006
- Board of Examiners for Land Surveyors – fiscal years 2005 and 2007
- Private Investigation and Polygraph Commission – fiscal year 2005
- Real Estate Appraisers Commission – fiscal year 2005

The following boards and commissions had a negative reserve account in each of the noted years during the period July 1, 2004, through June 30, 2008:

- Board of Barber Examiners – fiscal years 2005, 2006, 2007, and 2008
- Board of Funeral Directors and Embalmers – fiscal years 2005, 2006, and 2007
- Board of Examiners for Land Surveyors – fiscal years 2005 and 2007
- Real Estate Appraiser Commission – fiscal year 2005

Reserves may also provide boards a cushion against the cost of informing all licensees when statutes and rules change or when a board has unexpected legal costs and fines. In addition, the reserves can provide transition funding when an event or change seriously impacts the number of licenses in a positive or negative direction. The General Assembly's transfer of the regulatory boards' reserve funds will require that the Department of Finance and Administration and the Department of Commerce and Insurance have in place contingency plans for regulatory board shortfalls and that the General Assembly is prepared to consider the possibility of required special appropriations for the boards.

Recommendation. The General Assembly may wish to reconsider how regulatory activities are funded. If the state chooses not to appropriate funding for these regulatory activities, the use of revenues and fines collected from licensees should be restricted to activities associated with regulating that profession.

Alternatively, if it is the General Assembly's intention that the boards not accumulate large reserves, the General Assembly may wish to amend statutes by capping allowed reserves

based on a certain percentage of the boards' operating expenses and requiring the boards to lower licensing fees or rebate funds back to licensees.

The General Assembly may wish to further define its intentions regarding self-sufficiency requirements for regulatory boards to clarify whether it intended each individual regulatory board's revenues to cover all actual expenses incurred by that board (whether classified as direct or indirect costs) to function and perform its statutory duties.

The Commissioner of the Department of Commerce and Insurance and the Assistant Commissioner for the Division of Regulatory Boards should, along with their staffs, create a more simple and direct formula and system to capture and charge all actual costs to individual regulatory boards. The system should not contain subjective factors but be solely based on objective and verifiable data.

The General Assembly may wish to charge the commissioners of the Department of Finance and Administration and the Department of Commerce and Insurance with periodically assessing the current sufficiency of the \$5 fee collected annually on each active license to cover indirect costs and ensuring that the state regulatory fees collected are earmarked specifically to offset certain costs incurred by the state's regulatory boards in performing their statutory duties.

### **The Professional Regulatory Boards Need to Improve Their Policies, Procedures, and Rules to Assist Them in Making Sure That Board Members and Their Staff Are Timely and Consistent in Their Work**

While various statutes and rules set out the general requirements and procedures for licensure and the boards' general duties for the regulation of their respective professions, the individual boards, the Division of Regulatory Boards, and the Department of Commerce and Insurance are responsible for the formal, detailed policies and procedures that govern the day-to-day operations of the boards in fulfillment of their statutory duties. However, the division and boards could improve their policies, procedures, and rules that provide direction to the boards and their staff regarding their daily duties and decisions. A few boards included in this audit (Private Investigation and Polygraph, Private Protective Services, Land Surveyors, Real Estate Appraisers, and Real Estate) have some official policies and procedures establishing and/or explaining how a certain situation will be viewed or handled, but many do not. The efficiency and effectiveness of the regulatory boards and their staff would be improved if their policies, procedures, and rules included

- detailed policies regarding time frames within which applications will be processed by staff to ensure consistent and timely vetting of applicants and issuing of licenses;
- board interpretations and definitions that would provide guidance to staff and board members alike and allow consistent treatment of similar situations;

- penalty matrices that break down the broad statutory penalty range of \$0 - \$1,000 or \$2,000 into smaller ranges based on the severity and repeated nature of the offense that can still accommodate individual circumstances; and
- a better understanding of the definition of “good moral character,” which is required for most licensure, and whether persons with certain types of convictions should perhaps never be licensed in a particular profession.

Some board directors have stated that their boards and staff attorneys are reluctant to establish official board policies and guidelines, despite being encouraged to do so by some directors to ensure consistent treatment of applicants and licensees. Instead, administrative staff and board members prefer the method of reviewing past board minutes and reports to try and be consistent. But such an approach permits important policy to be set on an informal “ad hoc” basis rather than providing the accountability and transparency the public should have regarding such material decisions.

Recommendation. The boards and commissions would be more efficient and consistent if they were to create specific internal operating policies and procedures, or improve such policies and procedures that already exist. Where third-party rights may be impacted, additional policies and procedures should be created through the rule-making process. Providing such additional guidance would help ensure consistent interpretation and application of regulations and fair and equitable treatment of applicants and licensees by staff and the boards themselves.

### **Requiring Licensure as a Funeral Director to Sell Funeral Merchandise Has Been Found to Be Unconstitutional**

Section 62-5-303(a)(1-2), *Tennessee Code Annotated*, requires that “only properly qualified persons shall engage in funeral directing. . . . Any person engaged therein in this state shall be licensed by the board.” According to Section 62-5-101(6)(A)(ii), *Tennessee Code Annotated*, the definition of “funeral directing” includes the “making of arrangements to provide for funeral services and/or the selling of funeral merchandise, and/or the making of financial arrangements for the rendering of the services, and/or the sale of such merchandise.”

However, this requirement that an individual must be a licensed funeral director to sell a casket or an urn has been found to be unconstitutional, as it violates the due process and equal protection clauses of the 14<sup>th</sup> Amendment of the U.S. Constitution and bears no rational relationship to any legitimate purpose other than protecting the economic interests of licensed funeral directors. [*Craigmiles v. Giles*, 110 F. Supp. 2d 658, 2000 U.S. Dist. LEXIS 12582 (E.D. Tenn. 2000); *Craigmiles v. Giles*, 312 F. 3d 220, 2002 FED App. 417P, 2002 U.S. App. LEXIS 24637 (6<sup>th</sup> Cir. Tenn. 2002).]

Recommendation. Though the department is not attempting to enforce this statute, the General Assembly should revise Title 62, Chapter 5, Parts 1 and 3, to clarify licensing requirements based on court interpretations.

## **The Private Protective Services Advisory Committee Rarely Meets, Not Having Met in Over Three Years, and Its Usefulness and Existence in the Sunset Statute Should Be Reviewed**

The Private Protective Services Advisory Committee, established by Section 62-35-129, *Tennessee Code Annotated*, is to be a commissioner-appointed committee of experts in the field of security guard and patrol service that is to advise the Commissioner of Commerce and Insurance with respect to any contemplated rulemaking and may make formal recommendations to the commissioner or the General Assembly. However, the actual power to license and regulate security guards and security companies lies with the Commissioner of Commerce and Insurance. As of mid-2009, the committee had not met in three years and its members terms had expired in 2008.

The Division of Regulatory Boards' Private Protective Services office regulates armed and unarmed security guards, guard-certified trainers, contract security companies, and proprietary security organizations in compliance with duties allocated by statute, including license and registration determination, and disciplinary actions resulting from complaints against licensees. On October 13, 2009, Private Protective Services had 19,997 active security guard licenses, 302 state-certified trainer licenses, and 1,423 security company/business licenses.

Recommendation. The General Assembly may wish to consider the usefulness of this entity as an advisory committee and whether it should transform the committee into a true professional regulatory board for security services, particularly as there are a large number of complaints against private protective services licensees. Otherwise, we recommend the committee's removal from the sunset statute, since private protection service regulation and licensing authority lies with the Commissioner of Commerce and Insurance, and the regulatory activities will continue with or without the advisory committee. In addition, the advisory committee is not required to regularly meet and advise the commissioner, and the commissioner can at any time call upon professional experts for their opinions.

## **Though They Meet Statutory Restrictions, the Public Members of the Tennessee Real Estate Commission and the Board of Examiners for Architects and Engineers Derive Their Livelihood From the Industry or Have a Personal Interest in the Industry by Association, and May Give the Appearance That They May Not Be Able to Appropriately Represent the Consumer and General Public's Interests in the Regulation of These Professions**

One of the rationales for regulating the professions represented by the boards covered in this audit is to protect consumers from any licensee's unprofessional conduct or illegal activity. As stated in the June 2005 performance audit of the regulatory boards in which we recommended increasing the number of public members on boards, public members provide the consumer-focused perspective. This presumes that the public members will have no connection with the industry and will represent the public's interests regarding the regulation of the industry. All 10 active boards of the 11 boards in this audit have public members. We found no evidence that eight of the ten boards' public members have any connection to the industry regulated by the

board on which they serve. However, two boards' public members derive their livelihood from the industry or have a personal interest in the industry by association.

In 1980, the General Assembly revised statute to add two public members, appointed by the Governor, to the board of the Tennessee Real Estate Commission. Section 62-13-201(c)(1), *Tennessee Code Annotated*, reads, "Each of the remaining two (2) members of the commission shall be a person who is not engaged in or conducting the business, or acting in the capacity of a real estate broker or affiliate broker; nor shall such members be engaged in the business of real estate financing or development." However, a review of commission members as of August 2009 revealed two members whose livelihoods are derived from real estate law and/or involve representing clients in regulatory, zoning, and residential and commercial real estate development matters. Though technically in compliance with the restrictions placed on public members of the Real Estate Commission, the members have not declared the details of their professions as potential conflicts of interest, and we believe their situations may give the appearance that these members have too close a business and personal relationship with the real estate industry for them to present a consumer-focused perspective and represent the public.

Likewise, Section 62-2-201(b), *Tennessee Code Annotated*, reads, ". . . the board of architects and engineers shall also include one (1) member who is not engaged in the practice of architecture, engineering or landscape architecture." A review of the Board of Examiners for Architects and Engineers members as of August 2009 revealed the one public member to have a personal interest in the profession by association. The board member's spouse and the spouse's immediate family own substantial businesses involved in real estate development, construction, and the providing of commercial development, property management, and affordable housing services—businesses that have a vested interest in the practice and regulation of architects and engineers. Though technically in compliance with the restrictions placed on the public member of the Board of Examiners for Architects and Engineers, the member has not declared the connection by association to the profession as a potential conflict of interest, and we believe the situation may give the appearance that this member has too close a business and personal relationship with the industry for the member to provide a consumer-focused perspective and represent the public's interests.

Recommendation. We recommend that these three public members (two on the Tennessee Real Estate Commission and one on the Board of Examiners for Architects and Engineers) be replaced by new members who have no potential conflicts of interest because of an affiliation with the profession and industry in any capacity. This will ensure that the independent consumers' interests are represented on the respective commission or board.

The General Assembly may wish to further clarify in statute its intentions regarding the presence of public members on regulatory boards and how separate the public members need to be from the particular profession.

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## RECOMMENDATIONS

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### LEGISLATIVE

This performance audit identified areas in which the General Assembly may wish to consider statutory changes to improve the efficiency and effectiveness of these 11 Professional Regulatory Boards' operations.

1. The General Assembly may wish to consider amending statute to specifically require the boards in the Division of Regulatory Boards, Department of Commerce and Insurance, to conduct at least state, if not also federal, criminal background checks on all licensees.
2. The General Assembly may wish to reconsider how regulatory activities are funded. If the state chooses not to appropriate funding for these regulatory activities, the use of revenues and fines collected from licensees should be restricted to activities associated with regulating that profession.
3. If it is the General Assembly's intention that the boards not accumulate large reserves, the General Assembly may wish to amend statutes by capping allowed reserves based on a certain percentage of the boards' operating expenses and requiring the boards to lower licensing fees or rebate funds back to licensees.
4. The General Assembly may wish to further define its intentions regarding self-sufficiency requirements for regulatory boards to clarify whether it intended each individual regulatory board's revenues to cover all actual expenses incurred by that board (whether classified as direct or indirect costs) to function and perform its statutory duties.
5. The General Assembly may wish to charge the commissioners of the Department of Finance and Administration and the Department of Commerce and Insurance with periodically assessing the current sufficiency of the \$5 fee collected annually on each active license to cover indirect costs and ensuring that the state regulatory fees collected are earmarked specifically to offset certain costs incurred by the state's regulatory boards in performing their statutory duties.
6. The General Assembly may wish to consider revising Title 62, Chapter 5, Parts 1 and 3, to clarify licensing requirements for selling funeral merchandise based on court interpretations.
7. The General Assembly may wish to consider the usefulness of the Private Protective Services Advisory Committee as an advisory committee and whether it should transform the committee into a true professional regulatory board for security

services, particularly as there are a large number of complaints against private protective services licensees. Otherwise, we recommend the committee's removal from the sunset statute, since private protection service regulation and licensing authority lies with the Commissioner of Commerce and Insurance, and the regulatory activities will continue with or without the advisory committee. In addition, the advisory committee is not required to regularly meet and advise the commissioner, and the commissioner can at any time call upon professional experts for their opinions.

8. The General Assembly may wish to further clarify in statute its intentions regarding the presence of public members on regulatory boards and how separate the public members need to be from the particular profession.

## **ADMINISTRATIVE**

These 11 Professional Regulatory Boards, the Division of Regulatory Boards, and the Department of Commerce and Insurance should address the following areas to improve the efficiency and effectiveness of their operations.

1. Division of Regulatory Boards management should ensure that each board adopts and consistently applies the established complaint-handling guidelines. Management should adopt formal, written procedures that set time guidelines for all phases of the complaint process—receipt, correspondence with complainant/respondent, legal, investigations, initial/final board actions, etc.—and should ensure all boards and division staff capture the dates of such activities for management purposes.
2. The Commissioner of Commerce and Insurance should provide sufficient legal resources to the regulatory boards to ensure timely complaint processing. The commissioner, in conjunction with the boards, should also ensure that boards meet frequently enough to dispose of complaints as promptly as possible.
3. The division may wish to study its division-wide 180-day closure policy and determine whether it is realistic for all boards, particularly for the more technical professions such as real estate appraisers. When studying this issue, division and board management should also consider any federal guidelines or recommendations for complaint closure, such as the Federal Financial Institutions Examination Council Appraisal Subcommittee's one-year deadline for closure of complaints against licensed real estate appraisers.
4. Further, management should continue to pursue the establishment of an electronic system to replace RBS that captures all licensing and complaint information and can provide management with useful data and statistics that can be used to improve operations' efficiency and effectiveness.

5. Department and division management should ensure that the information security control conditions that were found are remedied by the prompt development and implementation of effective controls. Management should ensure that risks associated with this finding are adequately identified and assessed in the department, division, and boards' risk assessments; this would include determining if any weaknesses have actually been exploited. Management should implement effective controls to ensure compliance with applicable requirements, assign staff to be responsible for ongoing monitoring of the risks and mitigating controls, and take action if deficiencies occur.
6. Board management should work with their individual boards and board staff to maximize consistency in evaluating more subjective licensing requirements, such as applicants' moral character, and should conduct state criminal background checks at initial licensure and periodically thereafter. The Division of Regulatory Boards should pursue legislation that would allow the boards to conduct a federal criminal background check through the Federal Bureau of Investigation as prescribed by Section 38-14-101 et seq., *Tennessee Code Annotated*, the National Crime Prevention and Privacy Compact. The fee for criminal background checks can be incorporated into licensing fees and passed along to the licensee as it has been with the Private Investigation and Polygraph Commission and Private Protective Services. Boards should also consider the specific types of offenses/convictions or other circumstances that might result in denial of an application or that should preclude someone from ever being licensed in a particular profession and may result in a permanent denial or revocation of a license. Where necessary, recommendations for statutory and rule changes should be made.
7. Board staff should, wherever available, use national databases, such as those currently used by the Real Estate Commission and the Board of Examiners for Architects and Engineers, to identify and verify education and disciplinary actions originating outside Tennessee.
8. The boards/commissions would be more efficient and consistent if they were to create specific internal operating policies and procedures, or improve policies and procedures that already exist. Where third-party rights may be impacted, additional policies and procedures should be created through the rule-making process. Providing such additional guidance would help ensure consistent interpretation and application of regulations and fair and equitable treatment of applicants and licensees by staff and the boards themselves.
9. We recommend that these three public members (two on the Tennessee Real Estate Commission and one on the Board of Examiners for Architects and Engineers) be replaced by new members who have no potential conflicts of interest because of an affiliation with the profession and industry in any capacity. This will ensure that the independent consumers' interests are represented on the respective commission or board.

## APPENDIX

### Title VI Information

All programs or activities receiving federal financial assistance are prohibited by Title VI of the Civil Rights Act of 1964 from discriminating against participants or clients on the basis of race, color, or national origin. In fiscal years 2005-2008, the Department of Commerce and Insurance received federal funds from the Federal Emergency Management Agency and the U.S. Department of Health and Human Services. None of the 11 regulatory boards covered in this audit received state appropriations or federal funds. The Chief Counsel for Consumer Affairs and Administration is the Title VI Coordinator for the department. According to management, the department has received no Title VI complaints in the last four years and has performed no compliance reviews. For more detailed Title VI information, see the April 2009 performance audit of the Department of Commerce and Insurance.

### Title VII Information

All programs or activities receiving federal assistance must comply with Title VII of the Civil Rights Act of 1964, that prohibits employment discrimination based on race, color, religion, sex, or national origin. In fiscal years 2005-2008, the Department of Commerce and Insurance received federal funds from the Federal Emergency Management Agency and the U.S. Department of Health and Human Services. None of the 11 regulatory boards covered in this audit received state appropriations or federal funds. Division of Regulatory Boards staff are a combination of executive and career (civil) service. Board directors and others like them who report directly to the assistant commissioner of the division are generally executive service, not subject to Section 8, Chapter 30, *Tennessee Code Annotated* (the Civil Service Act), and can be hired and fired at will. Staff who report to board directors and work for specific boards are generally career (civil) service, and the hiring, firing, and treatment of such staff are subject to the Civil Service Act.

**Division of Regulatory Boards Staff  
by Gender, Ethnicity, and Job Title  
(Includes Staff for All 22 Boards and Commissions)  
As of October 2009**

Job Title	Gender		Ethnicity			
	Male	Female	Asian	Black	White	Other
Account Clerk	0	1	0	0	1	0
Accountancy Board Investigator	1	0	0	0	1	0
Administrative Secretary	0	2	0	0	2	0
Administrative Services Assistant 3	0	3	0	0	3	0
Administrative Services Assistant 4	1	2	0	0	3	0
Administrative Services Manager	0	1	0	0	1	0
Assistant Commissioner 2	1	0	0	0	1	0

<b>Job Title</b>	<b>Gender</b>		<b>Ethnicity</b>			
	<b>Male</b>	<b>Female</b>	<b>Asian</b>	<b>Black</b>	<b>White</b>	<b>Other</b>
Auditor 2	3	0	0	0	3	0
Auditor 3	4	2	0	1	5	0
Auditor 4	0	1	0	0	1	0
Clerk 3	2	1	0	0	3	0
Contractor Inspector	3	0	0	0	3	0
Executive Administrative Assistant 2	0	1	0	0	1	0
Information Systems Analyst 4	0	1	0	1	0	0
Information Systems Manager 3	1	0	0	0	1	0
Licensing Technician	5	23	0	8	20	0
Programmer/Analyst 4	2	0	1	0	1	0
Regulatory Board Administrative Assistant 1	3	16	0	5	14	0
Regulatory Board Administrative Assistant 2	1	11	0	2	9	1
Regulatory Board Administrative Assistant 3	3	3	0	0	6	0
Regulatory Board Administrative Director 1	0	2	0	0	2	0
Regulatory Board Administrative Manager	2	4	0	1	5	0
Regulatory Board Executive Director	5	4	0	1	8	0
Regulatory Board Field Representative	8	6	0	2	12	0
Regulatory Board Investigator	10	5	0	0	15	0
Regulatory Board Investigation Asst Director	1	0	0	0	1	0
Secretary	0	1	0	0	1	0
<b>Totals*</b>	<b>56</b>	<b>90</b>	<b>1</b>	<b>21</b>	<b>123</b>	<b>1</b>
<b>Percentages</b>	<b>38.4%</b>	<b>61.6%</b>	<b>0.7%</b>	<b>14.4%</b>	<b>84.2%</b>	<b>0.7%</b>

\*Totals may be slightly higher as it is known some PRB staff technically hold positions assigned to areas of the department other than the Division of Regulatory Boards.

Source: Employees assigned to Budget Code 335.10 (Division of Regulatory Boards) in Edison HCM (Human Capital Management).

**Eleven Professional Regulatory Boards' Members  
By Gender and Ethnicity  
As of October 2009**

<b>Board</b>	<b>Gender</b>		<b>Ethnicity</b>		
	<i>Male</i>	<i>Female</i>	<i>White</i>	<i>Black</i>	<i>Other</i>
Architects and Engineers	10	2	11	0	1
Auctioneers	4	1	5	0	0
Barber Examiners	5	0	2	3	0
Collection Service	4	1	4	1	0
Cosmetology	0	9	7	2	0
Funeral Directors and Embalmers	5	2	6	1	0

<b>Board</b>	<b>Gender</b>		<b>Ethnicity</b>		
	<i>Male</i>	<i>Female</i>	<i>White</i>	<i>Black</i>	<i>Other</i>
Land Surveyors	3	1	4	0	0
Private Investigation and Polygraph	6	3	7	2	0
Private Protective Services*	0	0	0	0	0
Real Estate	7	2	7	2	0
Real Estate Appraisers	8	1	8	1	0
<b>Total</b>	<b>52</b>	<b>22</b>	<b>60</b>	<b>12</b>	<b>2</b>

\* As of October 2009, the Private Protective Services Advisory Committee was not active.