

PERFORMANCE AUDIT  
OF THE  
REGULATORY SERVICES ADMINISTRATION

DEPARTMENT OF STATE

February 1998

## EXECUTIVE DIGEST

# REGULATORY SERVICES ADMINISTRATION

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### INTRODUCTION

This report, issued in February 1998, contains the results of our performance audit\* of the Regulatory Services Administration (RSA), Department of State.

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### AUDIT PURPOSE

This performance audit was conducted as part of the constitutional responsibility of the Office of the Auditor General. Performance audits are conducted on a priority basis related to the potential for improving effectiveness\* and efficiency\*.

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### BACKGROUND

RSA consists of the Bureau of Hearings, the Office of Internal Audit and Enforcement, and the Bureau of Automotive Regulation.

RSA's mission\* includes providing legal research and counsel, providing due process services, coordinating interfaces with the Department of Attorney General, providing audit and enforcement oversight, and effectively pursuing customer service.

The Bureau of Hearings provides legal research and counsel to the Secretary of State, provides due process services that are required of the Department, and

\* See glossary on page 18 for definition.  
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coordinates interfaces with the Department of Attorney General in litigation and other court action involving the Department.

The Office of Internal Audit and Enforcement, consisting of the Internal Audit Division and the Enforcement Division, provides the audit and enforcement oversight of required Department functions.

The Bureau of Automotive Regulation licenses and regulates automotive mechanics, motor vehicle repair facilities, automotive dealers, and salvage vehicle agents.

RSA had 161 employees as of the pay period ended June 28, 1997. RSA had recorded expenditures of \$6.5 million for the fiscal year ended September 30, 1996.

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**AUDIT OBJECTIVES,  
CONCLUSIONS, AND  
NOTEWORTHY  
ACCOMPLISHMENTS**

**Audit Objective:** To assess the effectiveness and efficiency of the operations of RSA's Internal Audit Division.

**Conclusion:** RSA's Internal Audit Division was generally effective and efficient; however, we noted reportable conditions\* related to a comprehensive audit plan (Finding 1) and cash overage and shortage audits (Finding 2).

**Noteworthy Accomplishments:** The State of Michigan is a member of the International Registration Plan. This Plan requires each member state to audit 15% of its registrants within a five-year period. The Internal Audit Division has aggressively moved toward complying with the Plan requirement. The Division issued audits for 226 (3.83%)

\* See glossary on page 18 for definition.  
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and 415 (6.92%) of its registrants during calendar years 1996 and 1997, respectively, for a total of 641 audits or 10.75% of its registrants in a two-year period.

**Audit Objective:** To assess the effectiveness and efficiency of the operations of RSA's Enforcement Division.

**Conclusion:** RSA's Enforcement Division was generally effective and efficient; however, we noted a reportable condition related to the timeliness of case investigations (Finding 3).

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**AUDIT SCOPE AND  
METHODOLOGY**

Our audit scope was to examine the program and other records of the Regulatory Services Administration. Our audit was conducted in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States and, accordingly, included such tests of the records and such other auditing procedures as we considered necessary in the circumstances.

Our audit scope did not include an examination of the program and other records of the Bureau of Automotive Regulation, a bureau within RSA. This Bureau was audited separately, and the related audit report was issued April 24, 1996.

Our audit included an examination of RSA's records and activities covering the period October 1, 1995 through June 30, 1997.

To accomplish our objectives, we examined RSA's policies and procedures and assessed its internal control

structure\* . We reviewed the Internal Audit Division's

annual audit plans, analyzed selected internal audit reports and supporting documentation, and tested the Division's compliance with the International Registration Plan's\* audit requirements. We also reviewed the Enforcement Division's procedures for assigning cases, analyzed the number of cases assigned to each investigator, and aged the Division's open cases. In addition, we sampled the Division's closed cases and reviewed the documentation for propriety, completeness, and timeliness.

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**AGENCY RESPONSES  
AND PRIOR AUDIT  
FOLLOW-UP**

Our audit report contains 3 findings and 3 corresponding recommendations. The agency's preliminary response indicated that RSA agreed with all 3 recommendations. RSA has initiated steps to implement 1 of the recommendations and plans to initiate steps to implement the other 2 recommendations.

The Department complied with 3 of 5 prior audit recommendations included within the scope of our current audit. We repeated 1 of the other 2 audit recommendations in this report.

\* See glossary on page 18 for definition.

The Honorable Candice S. Miller  
Secretary of State  
Treasury Building  
Lansing, Michigan

Dear Secretary Miller:

This is our report on the performance audit of the Regulatory Services Administration, Department of State.

This report contains our executive digest; description of agency; audit objectives, scope, and methodology and agency responses and prior audit follow-up; comments, findings, recommendations, and agency preliminary responses; and a glossary of acronyms and terms.

Our comments, findings, and recommendations are organized by audit objective. The agency preliminary responses were taken from the agency's responses subsequent to our audit fieldwork. The *Michigan Compiled Laws* and administrative procedures require that the audited agency develop a formal response within 60 days after release of the audit report.

We appreciate the courtesy and cooperation extended to us during this audit.

AUDITOR GENERAL

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## Description of Agency

The Department of State is one of the principal departments within the State of Michigan government. The Department is organized into the Executive Office and three main organizational units: Department Services Administration, Regulatory Services Administration (RSA), and Service Delivery Administration. The Department's executive officer, the Secretary of State, is an elected official who serves a four-year term. Each of the three organizational units is headed by a deputy.

RSA consists of the Bureau of Hearings, the Office of Internal Audit and Enforcement, and the Bureau of Automotive Regulation.

RSA's mission includes providing legal research and counsel, providing due process services, coordinating interfaces with the Department of Attorney General, providing audit and enforcement oversight, and effectively pursuing customer service.

The Bureau of Hearings provides legal research and counsel to the Secretary of State, provides due process services required of the Department, and coordinates interfaces with the Department of Attorney General in litigation and other court action involving the Department. The Bureau consists of the Hearings Division, the Driver License Appeal Division, and the Compliance and Rules Division.

The Office of Internal Audit and Enforcement, consisting of the Internal Audit Division and the Enforcement Division, provides the audit and enforcement oversight of required Department functions.

The Bureau of Automotive Regulation licenses and regulates automotive mechanics, motor vehicle repair facilities, automotive dealers, and salvage vehicle agents.

RSA had 161 employees as of the pay period ended June 28, 1997. RSA had recorded expenditures of \$6.5 million for the fiscal year ended September 30, 1996.

## Audit Objectives, Scope, and Methodology and Agency Responses and Prior Audit Follow-Up

### Audit Objectives

Our performance audit of the Regulatory Services Administration (RSA), Department of State, had the following objectives:

1. To assess the effectiveness and efficiency of the operations of RSA's Internal Audit Division.
2. To assess the effectiveness and efficiency of the operations of RSA's Enforcement Division.

### Audit Scope

Our audit scope was to examine the program and other records of the Regulatory Services Administration. Our audit was conducted in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States and, accordingly, included such tests of the records and such other auditing procedures as we considered necessary in the circumstances.

Our audit scope did not include an examination of the program and other records of the Bureau of Automotive Regulation, a bureau within RSA. This Bureau was audited separately, and the related audit report was issued April 24, 1996.

### Audit Methodology

Our audit procedures were conducted between April and September 1997 and included examination of RSA's records and activities covering the period October 1, 1995 through June 30, 1997.

Our methodology included a preliminary analysis of RSA's operations. This included interviewing RSA personnel and identifying performance measures\* and performance objectives\* that RSA uses to evaluate its effectiveness and efficiency. Our preliminary

\* See glossary on page 18 for definition.  
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analysis also included reviewing applicable policies and procedures and obtaining an understanding of RSA's internal control structure and operational activities.

To accomplish our first objective, we reviewed the Internal Audit Division's annual audit plans. We analyzed selected internal audit reports and supporting documentation for timeliness and compliance with applicable auditing standards\* . We tested the Division's compliance with the International Registration Plan's audit requirements.

To accomplish our second objective, we reviewed the Enforcement Division's procedures for assigning cases and analyzed the number of cases assigned to each investigator. We aged the Division's open cases and reviewed the results for timeliness. We sampled the Division's closed cases and reviewed the documentation for propriety, completeness, and timeliness.

#### Agency Responses and Prior Audit Follow-Up

Our audit report contains 3 findings and 3 corresponding recommendations. The agency's preliminary response indicated that RSA agreed with all 3 recommendations. RSA has initiated steps to implement 1 of the recommendations and plans to initiate steps to implement the other 2 recommendations.

The agency preliminary response which follows each recommendation in our report was taken from the agency's written comments and oral discussion subsequent to our audit fieldwork. Section 18.1462 of the *Michigan Compiled Laws* and Department of Management and Budget Administrative Guide procedure 1280.02 require the Department of State to develop a formal response to our audit findings and recommendations within 60 days after release of the audit report.

The Department complied with 3 of 5 prior audit recommendations included within the scope of our current audit. We repeated 1 of the other 2 audit recommendations in this report.

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# COMMENTS, FINDINGS, RECOMMENDATIONS, AND AGENCY PRELIMINARY RESPONSES

## EFFECTIVENESS AND EFFICIENCY OF THE INTERNAL AUDIT DIVISION

### COMMENT

**Background:** The Regulatory Services Administration's (RSA's) Internal Audit Division audits the Department of State's branch offices located throughout the State. The primary focus of these audits is to verify compliance with cash and inventory control procedures; however, Division audits also include the investigation of a variety of situations, such as cash overages or shortages, missing inventory, break-ins, and defalcations. The Division also performs audits at offices that are not managed by the State, such as county sheriff offices and other offices that register and issue State license tabs for a large number of vehicles.

**Audit Objective:** To assess the effectiveness and efficiency of the operations of RSA's Internal Audit Division.

**Conclusion:** RSA's Internal Audit Division was generally effective and efficient; however, we noted reportable conditions related to a comprehensive audit plan and cash overage and shortage audits.

**Noteworthy Accomplishments:** The State of Michigan is a member of the International Registration Plan. This Plan requires each member state to audit 15% of its registrants within a five-year period. The Internal Audit Division has aggressively moved toward complying with the Plan requirement. The Division issued audits for 226 (3.83%) and 415 (6.92%) of its registrants during calendar years 1996 and 1997, respectively, for a total of 641 audits or 10.75% of its registrants in a two-year period.

## **FINDING**

### **1. Comprehensive Audit Plan**

The Department's Internal Audit Division had not developed a comprehensive audit plan that identified the audits to be completed and the related time budgets to complete the audits.

The *Standards for the Professional Practice of Internal Auditing*, Section 520, require the director of the Internal Audit Division to establish plans to carry out the responsibilities of the Division. Section 520 further requires that audit work schedules be established and include (1) what activities are to be audited, (2) when the activities will be audited, and (3) the estimated time required to audit the activities.

The Division had not developed an audit plan for fiscal year 1995-96. The Division had developed a work plan for fiscal year 1996-97 that identified the total staff hours available; the number of audits, by audit type, that it planned to complete; an estimate of the number of hours required to complete each audit; and listings of branch offices due for audit. However, the Division's fiscal year 1996-97 work plan was not comprehensive. The Division added the listings of branch offices due for audit in response to our prior audit recommendation. These listings were not complete. The listings identified 76 branch offices due for audit, compared to the work plan that indicated that 97 branch offices would be audited.

The fiscal year 1996-97 work plan also did not include an accurate projection of the number of audit hours required to complete the number of audits identified. The fiscal year 1996-97 work plan indicated that 1,600 hours would be required to perform 40 cash overage and shortage audits. We reviewed 10 of the Division's 54 overage and shortage audits performed during fiscal year 1995-96. According to the Division's audit files, the number of hours actually reported for these 10 audits ranged between 8 and 28 hours and averaged 15 hours. Therefore, only approximately 600 hours would be required to perform the 40 cash overage and shortage audits; the 1,600 hours identified in the fiscal year 1996-97 work plan was not an accurate projection. The Division indicated that the hours that we identified and used in our calculation did not include follow-up or rewrite hours attributable to

the audits. Therefore, the Division indicated that our estimate of 600 hours was low. However, the Division could not provide any basis for its estimate of 1,600 hours.

A comprehensive audit plan that identifies audits and time budgets would assist the Division in planning and controlling its audits and provide the Division with a means to monitor its audit activities.

We noted the same condition in our prior audit of the Internal Audit Division. The Department agreed with the prior audit finding and indicated that it had already complied with the related recommendation. However, the Department's compliance was not sufficient. It did not include a complete listing of audits to be performed, it did not provide any indication of when the audits that were identified would be performed, and it did not provide an accurate estimate of the time required to perform the audits.

### **RECOMMENDATION**

WE AGAIN RECOMMEND THAT THE DIVISION DEVELOP A COMPREHENSIVE AUDIT PLAN THAT IDENTIFIES THE AUDITS TO BE COMPLETED AND THE RELATED TIME BUDGETS TO COMPLETE THE AUDITS.

### **AGENCY PRELIMINARY RESPONSE**

The Department agreed with this recommendation. The Department informed us that the Division's annual work plan will include a list of audits to be completed, with estimated completion dates, and the related time budgets based on past audits.

### **FINDING**

#### **2. Cash Overage and Shortage Audits**

The Internal Audit Division's procedures did not require the Division to perform a risk assessment to evaluate the necessity of performing each cash overage and shortage audit.

Section 511 of the Department's Internal Audit Manual states that the Division will perform a special audit when an overage or shortage of \$100 or more occurs. To promote increased effectiveness and efficiency of the Department's Internal Audit Division, a variety of factors could be considered in determining whether the performance of a particular audit is necessary. These factors include, but are not limited to, audit risk, materiality, the internal control structure, prior errors, and the auditor's judgment.

We reviewed 10 of the Division's 54 audit files related to cash overage and shortage audits performed in fiscal year 1995-96. Based on the State of Michigan's fiscal year 1995-96 average annual salary and travel rates, we determined that the Division's cost to complete these 10 audits ranged from approximately \$215 to \$750. Also, we determined that the discrepancies identified in 44 (81%) of the 54 overage and shortage audits were left unresolved.

We realize that the purpose of the Division's cash overage and shortage audits is not only to ensure the accuracy of the Department's accounting records, but also to provide a mechanism to prevent and detect fraud and abuse. However, if the Division considered some of the factors previously cited, the audit selection process may lead to increased effectiveness and efficiency within the Division.

### **RECOMMENDATION**

We recommend that the Division revise its procedures to require the Division to perform a risk assessment to evaluate the necessity of performing each cash overage and shortage audit.

### **AGENCY PRELIMINARY RESPONSE**

The Department agreed with this recommendation. The Department informed us that the Division will document a cash overage or shortage audit with either a formal preliminary risk assessment or a statement that the audit is specifically requested.

## **EFFECTIVENESS AND EFFICIENCY OF THE ENFORCEMENT DIVISION**

### **COMMENT**

**Background:** The Regulatory Services Administration's (RSA's) Enforcement Division investigates fraud issues related to titles, registrations, insurance, driver licenses, personal identification cards, and retagged vehicles. The Division is the Department's liaison with local, state, and federal law enforcement agencies, and driver and vehicle investigation units throughout the United States and Canada.

**Audit Objective:** To assess the effectiveness and efficiency of the operations of RSA's Enforcement Division.

**Conclusion:** RSA's Enforcement Division was generally effective and efficient; however, we noted a reportable condition related to the timeliness of case investigations.

### **FINDING**

#### **3. Timeliness of Case Investigations**

The Enforcement Division did not complete a significant percentage of its case investigations on a timely basis.

The Division investigates title, registration, and driver license fraud and performs special investigations for the Department. The Division also collects dollar amounts owed the State for nonsufficient funds checks that the Department has received.

The Enforcement Division's Policy Book, Section C, states that investigators should close case investigations within 90 days of receipt by the Division. Further, this policy requires that if a case is to remain open past 90 days, the investigator must submit a supplemental report stating the status of the investigation and the reasons the case should remain open.

We reviewed 38 of the Division's 1,873 case investigations closed between October 1, 1995 and June 30, 1997. We determined that 17 (45%) of these 38 cases extended beyond the 90-day limit and that the required supplemental reports were not prepared for 16 of these 17 cases.

In addition, our review of the Division's listing of cases open as of June 30, 1997 disclosed that 460 (74%) of the 623 open cases had been open longer than 90 days. The following table categorizes the number of cases by the length of time that the cases had been open as of June 30, 1997:

Length of Time Cases Were Open	Number of Cases
> 90 days and $\leq$ 1 year	244
> 1 year and $\leq$ 2 years	135
> 2 years and $\leq$ 3 years	57
> 3 years and $\leq$ 4 years	22
> 4 years and $\leq$ 5 years	1
> 5 years and $\leq$ 6 years	1

Note:            > stands for "more than."  
                       $\leq$  stands for "less than or equal to."

The Division informed us that it had limited staff resources to meet the demands of its case load.

Timely completion of case investigations may help ensure that vehicles possess proper title and registration, drivers are properly licensed, and that the Division is able to obtain evidence necessary for those cases that warrant prosecution. However, when a case cannot be completed on a timely basis, requiring investigators to complete supplemental reports and document the reasons for the delay may help ensure that cases are investigated and followed up on a more timely basis, and that the purpose for extending a case beyond 90 days was valid.

This documentation may also serve to support the need for additional resources to better meet the case load demands of the Division.

## **RECOMMENDATION**

We recommend that the Division complete its case investigations on a timely basis to help ensure that vehicles are properly titled and registered, that drivers are properly licensed, and that the Division is able to obtain the necessary evidence for those cases that warrant prosecution.

## **AGENCY PRELIMINARY RESPONSE**

The Department agreed with this recommendation. The Department informed us that a re-evaluation of the Division's policy is being made. The implementation of a new case management system will allow the gathering of data to better determine an approximate completion time requirement for specific types of allegations. A new policy that allows for a difference in investigating certain allegations as opposed to others, but continues to rely on regular reviews of agent case loads by the supervisor, will be established.

## Glossary of Acronyms and Terms

auditing standards	generally accepted auditing standards and <i>Standards for the Professional Practice of Internal Auditing</i> .
effectiveness	Program success in achieving mission and goals.
efficiency	Achieving the most outputs and outcomes practical for the amount of resources applied or minimizing the amount of resources required to attain a certain level of outputs or outcomes.
internal control structure	The management control environment, management information system, and control policies and procedures established by management to provide reasonable assurance that goals are met; that resources are used in compliance with laws and regulations; and that valid and reliable performance related information is obtained and reported.
International Registration Plan	A registration reciprocity agreement among states of the United States and provinces of Canada providing for payment of license fees on the basis of fleet miles operated in various jurisdictions.
mission	The agency's main purpose or the reason the agency was established.
performance audit	An economy and efficiency audit or a program audit that is designed to provide an independent assessment of the performance of a governmental entity, program, activity, or function to improve public accountability and to facilitate decision making by parties responsible for overseeing or initiating corrective action.

performance measures	Information of a quantitative or qualitative nature indicating program outcomes, outputs, or inputs. Performance measures are typically used to assess achievement of goals and/or objectives.
performance objectives	Specific outputs a program seeks to perform and/or inputs a program seeks to apply in its efforts to achieve its goals.
reportable condition	A matter coming to the auditor's attention that, in his/her judgment, should be communicated because it represents either an opportunity for improvement or a significant deficiency in management's ability to operate a program in an effective and efficient manner.
RSA	Regulatory Services Administration, Department of State.