



MICHIGAN

OFFICE OF THE AUDITOR GENERAL

AUDIT REPORT

PERFORMANCE AUDIT
OF

STATE SURPLUS

LOGISTICS AND OPERATIONS SUPPORT DIVISION
OFFICE OF SUPPORT SERVICES
DEPARTMENT OF TECHNOLOGY, MANAGEMENT, AND BUDGET

December 2014



Doug A. Ringler, C.P.A., C.I.A.
AUDITOR GENERAL

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– Article IV, Section 53 of the Michigan Constitution

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Performance Audit

State Surplus

Logistics and Operations Support Division, Office of Support Services, Department of Technology, Management, and Budget

Report Number:
071-0139-14

Released:
December 2014

The Management and Budget Act (Act 431, P.A. 1984) authorizes the Department of Technology, Management, and Budget (DTMB) to dispose of all State surplus personal property (surplus). State Surplus manages all surplus disposals, except for information technology equipment. Surplus is transferred to other State agencies, donated to nonprofit organizations, recycled, discarded, or sold to the general public. DTMB assists local governments, school districts, and community colleges in the sale of their respective surplus. Also, DTMB has an agreement with the Transportation Security Administration to sell voluntarily abandoned property from various airports within the State, and the State retains the revenue generated from these sales.

Audit Objective			Audit Conclusion
Objective 1: To assess the effectiveness of State Surplus' efforts to ensure the accuracy and completeness of revenues from asset sales.			Not effective
Finding Related to This Audit Objective	Material Condition	Reportable Condition	Agency Preliminary Response
State Surplus did not maintain sufficient segregation of duties over the collection and recording of revenue, which could result in the misuse of surplus inventory or sales revenue (<u>Finding 1</u>).	X		Agrees

Audit Objective			Audit Conclusion
Objective 2: To assess the effectiveness of State Surplus' efforts to ensure that surplus assets were properly inventoried, sold, or disposed.			Not effective
Findings Related to This Audit Objective	Material Condition	Reportable Condition	Agency Preliminary Response
State Surplus did not maintain sufficient records to accurately account for the disposition of surplus items received from State agencies. As a result, State Surplus could not document the disposition of many of our sampled items (<u>Finding 2</u>).	X		Agrees

Findings Related to This Audit Objective (Continued)	Material Condition	Reportable Condition	Agency Preliminary Response
State Surplus did not monitor access to the vault when Department of Treasury unclaimed property was kept in the vault although four vault keys existed (<u>Finding 3</u>).		X	Agrees

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Office of the Auditor General
201 N. Washington Square, Sixth Floor
Lansing, Michigan 48913

Doug A. Ringler, C.P.A., C.I.A.
Auditor General

Laura J. Hirst, C.P.A.
Deputy Auditor General



OAG

Office of the Auditor General

201 N. Washington Square, Sixth Floor • Lansing, Michigan 48913 • Phone: (517) 334-8050 • <http://audgen.michigan.gov>

Doug A. Ringler, C.P.A., C.I.A.
Auditor General

December 11, 2014

Mr. David B. Behen, Director
Department of Technology, Management, and Budget
Lewis Cass Building
Lansing, Michigan

Dear Mr. Behen:

This is our report on the performance audit of State Surplus, Logistics and Operations Support Division, Office of Support Services, Department of Technology, Management, and Budget.

This report contains our report summary; a description of program; our audit objectives, scope, and methodology and agency responses; comments, findings, recommendations, and agency preliminary responses; and a glossary of abbreviations and terms.

Our comments, findings, and recommendations are organized by audit objective. The agency preliminary responses were taken from the agency's response at the end of our audit fieldwork. The *Michigan Compiled Laws* and administrative procedures require that the audited agency develop a plan to comply with the audit recommendations and submit it within 60 days after release of the audit report to the Office of Internal Audit Services, State Budget Office. Within 30 days of receipt, the Office of Internal Audit Services is required to review the plan and either accept the plan as final or contact the agency to take additional steps to finalize the plan.

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

Sincerely,

Doug Ringler
Auditor General

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LOGISTICS AND OPERATIONS SUPPORT DIVISION
OFFICE OF SUPPORT SERVICES
DEPARTMENT OF TECHNOLOGY, MANAGEMENT, AND BUDGET**

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Description of Program

The Management and Budget Act (Act 431, P.A. 1984) authorizes the Department of Technology, Management, and Budget (DTMB) to dispose of all State surplus personal property* (surplus). State Surplus, within DTMB's Logistics and Operations Support Division, Office of Support Services, manages all surplus disposals, except for information technology equipment.

Surplus is transferred to other State agencies, donated to nonprofit organizations, recycled, discarded, or sold to the general public. DTMB assists local governments, school districts, and community colleges in the sale of their respective surplus and receives a portion of sale proceeds to cover costs associated with the sale of those items. Also, DTMB has an agreement with the Transportation Security Administration (TSA) to sell voluntarily abandoned property from various airports within the State. The State retains all of the revenue generated from sales of the transferred TSA property. In addition, DTMB assists the Michigan Department of State Police, Department of Natural Resources, and local law enforcement agencies in the sale of their confiscated property.

DTMB sells most surplus through the MiBID Internet auction site. Since 2001, DTMB has utilized a vendor to provide the MiBID Internet auction service to assist in the sale of surplus for the State as well as the other local governmental units served by DTMB. DTMB's Internet auction site vendor has sole responsibility for maintaining the auction site and all hardware, software, and systems needed to operate the auction service. DTMB finances the vendor's services solely from the proceeds of the sales generated by the Internet auctions. In December 2013, DTMB renewed the contract with the vendor to continue its operation of the Internet auction service through December 2018. In fiscal year 2012-13, DTMB generated 91.4% of its revenue using the Internet auction site with 52.9% of that revenue generated by the auction sales of the State's vehicle fleet.

DTMB accounts for State Surplus operations in the Office Services Revolving Fund. In fiscal year 2012-13, DTMB generated \$1.5 million in State Surplus revenue and \$1.1 million in expenses. State Surplus had 5 full-time equated employees as of June 30, 2014.

* See glossary at end of report for definition.

Audit Objectives, Scope, and Methodology and Agency Responses

Audit Objectives

Our performance audit* of State Surplus, Logistics and Operations Support Division, Office of Support Services, Department of Technology, Management, and Budget (DTMB), had the following objectives:

1. To assess the effectiveness* of State Surplus' efforts to ensure the accuracy and completeness of revenues from asset sales.
2. To assess the effectiveness of State Surplus' efforts to ensure that surplus assets were properly inventoried, sold, or disposed.

Audit Scope

Our audit scope was to examine the records and processes related to State Surplus. 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. Our audit procedures, which included a preliminary survey, audit fieldwork, report preparation, analysis of agency responses, and quality assurance, generally covered the period October 1, 2011 through June 30, 2014.

Audit Methodology

We conducted a preliminary survey of State Surplus operations to establish our audit objectives and methodology. During our preliminary survey, we:

- Interviewed State Surplus staff to obtain an understanding of State Surplus operations.
- Reviewed applicable State laws, policies, and procedures.

* See glossary at end of report for definition.

- Reviewed and conducted on-site observations of State Surplus processes and procedures.
- Reviewed State Surplus records, including the contract with DTMB's Internet auction site vendor and the agreement with the Transportation Security Administration.

To accomplish our first objective, we:

- Assessed and observed State Surplus' internal control* related to the receipting of revenues.
- Verified that revenue receipted matched the selling price on the auction Web site.
- Verified that the cash and credit card receipts were properly recorded in the Michigan Administrative Information Network* (MAIN).
- Verified that the Department of Treasury auction receipts matched the amounts reported by State Surplus.
- Reviewed supporting documentation of credit card refunds to determine appropriateness.

To accomplish our second objective, we:

- Assessed and observed State Surplus' internal control related to tracking, selling, and disposing of inventory.
- Conducted an analysis of the State Surplus sales database and the Internet auction site vendor's records to ensure that all auction lots were properly recorded in the State Surplus sales database.
- Judgmentally selected 30 auction lots not recorded in the State Surplus sales database to verify that the items were properly disposed.
- Judgmentally selected 52 items listed on disposal request forms from 8 various State agencies to determine the disposition of those items.

* See glossary at end of report for definition.

- Judgmentally selected 15 confiscated items transferred to State Surplus by the Michigan Department of State Police to determine the disposition of those items.
- Reviewed the auction documentation and controls over the sales process for the Department of Treasury auction conducted in 2014.

We based our audit conclusions on our audit efforts as described in the preceding paragraphs and the resulting material conditions* and reportable condition* noted in the comments, findings, recommendations, and agency preliminary responses section. The material conditions are more severe than a reportable condition and could impair management's ability to operate effectively or could adversely affect the judgment of an interested person concerning the effectiveness of State Surplus. The reportable condition is less severe than a material condition but represents a deficiency in internal control.

When selecting activities or programs for audit, we direct our efforts based on risk and opportunities to improve the operations of State government. Consequently, we prepare our performance audit reports on an exception basis.

Agency Responses

Our audit report contains 3 findings and 3 corresponding recommendations. DTMB's preliminary response indicates that it agrees with all of the recommendations.

The agency preliminary response that follows each recommendation in our report was taken from the agency's written comments and oral discussion at the end of our audit fieldwork. Section 18.1462 of the *Michigan Compiled Laws* and the State of Michigan Financial Management Guide (Part VII, Chapter 4, Section 100) require DTMB to develop a plan to comply with the audit recommendations and submit it within 60 days after release of the audit report to the Office of Internal Audit Services, State Budget Office. Within 30 days of receipt, the Office of Internal Audit Services is required to review the plan and either accept the plan as final or contact the agency to take additional steps to finalize the plan.

* See glossary at end of report for definition.

COMMENTS, FINDINGS, RECOMMENDATIONS,
AND AGENCY PRELIMINARY RESPONSES

EFFECTIVENESS OF EFFORTS TO ENSURE THE ACCURACY AND COMPLETENESS OF REVENUES FROM ASSET SALES

COMMENT

Audit Objective: To assess the effectiveness of State Surplus' efforts to ensure the accuracy and completeness of revenues from asset sales.

Audit Conclusion: Not effective.

Factors leading to this conclusion included the:

- Significant portion of revenue received as cash and the lack of segregation of duties increases the risk of misappropriating State Surplus revenue.
- Lack of oversight related to changes made to the State Surplus sales database.
- Material condition related to the lack of segregation of duties.

FINDING

1. **Segregation of Duties**

State Surplus did not maintain sufficient segregation of duties over the collection and recording of revenue. As a result, the potential existed for staff to misappropriate surplus personal property (surplus) items and sales receipts.

Section 18.1485(2)(a) of the *Michigan Compiled Laws* requires each internal accounting and administrative control system to include a plan of organization that provides segregation of duties and responsibilities among employees.

Our review of controls disclosed that some State Surplus staff who collected revenue for items sold at auction also have full access to the various State Surplus databases used to track surplus items sold. This access provided staff with the ability to change or delete items within the databases. One of the staff was also responsible for completing the monthly billing reconciliation between items sold on the auction site and payments received for those items. As a result, some State

Surplus staff had the ability to misappropriate sales receipts and alter State Surplus records while avoiding detection.

State Surplus management stated that continued declines in revenue led to a decline in staffing levels, which impacted State Surplus' ability to maintain sufficient segregation of duties.

RECOMMENDATION

We recommend that State Surplus maintain sufficient segregation of duties over the collection and recording of revenue.

AGENCY PRELIMINARY RESPONSE

DTMB provided us with the following response:

DTMB agrees with the recommendation and will work to maintain sufficient segregation of duties over the collection and recording of revenue. DTMB will identify specific staff within the Surplus program to handle only money collection or database data entry. Additionally, the Surplus program will collaborate with DTMB Financial Services to further segregate the revenue collection and data entry duties. Finally, DTMB will implement additional security and change management controls to protect the database's confidentiality, integrity and availability.

EFFECTIVENESS OF EFFORTS TO ENSURE THAT SURPLUS ASSETS WERE PROPERLY INVENTORIED, SOLD, OR DISPOSED

COMMENT

Audit Objective: To assess the effectiveness of State Surplus' efforts to ensure that surplus assets were properly inventoried, sold, or disposed.

Audit Conclusion: **Not effective.**

Factors leading to this conclusion included the:

- Significant number of lots missing from the State Surplus sales database.
- Material condition related to the lack of documentation for the disposition of surplus items and the reportable condition related to Department of Treasury auction controls.

FINDING

2. Lack of Documentation for Disposition of Surplus Items

State Surplus did not maintain sufficient records to accurately account for the disposition of surplus items received from State agencies. As a result, State Surplus property could have been misappropriated.

Section 18.1485(2)(c) of the *Michigan Compiled Laws* requires each internal accounting and administrative control system to include a system of recordkeeping procedures to control assets.

We judgmentally selected items from various State agency disposal request forms and Michigan Department of State Police (MSP) property release receipts. We also compared lot numbers in the State Surplus sales database with a listing of lot numbers provided by the Internet auction site vendor and judgmentally selected lot numbers that were not recorded in the State Surplus sales database for sold items. We requested State Surplus to provide us with documentation regarding the disposition of the items transferred to State Surplus. Our review disclosed:

- a. State Surplus did not document the disposition of 11 (21%) of 52 items selected from disposal requests submitted by eight different State agencies.

State agencies transfer items to State Surplus using a disposal request form for excess personal property that the agency no longer needs. State Surplus determines how to dispose of these items, such as donating, recycling, or discarding the items; transferring the items to another State agency; or selling the items in a public sale.

- b. State Surplus did not document the disposition of 6 (40%) of 15 items selected from MSP property release receipts.

MSP transfers confiscated personal property to State Surplus for disposition using a property release receipt. State Surplus only tracks items in its sales database if the item sold.

- c. State Surplus did not have a record of 11 (37%) of 30 auction lots listed on the auction site but not included in the State Surplus sales database. The 11 auction lots ranged in final auction prices from \$28 to \$1,228.

State Surplus sells most assets using a Web-based auction site administered by a vendor. State Surplus personal property items were sold in lots consisting of single items or similar items grouped together and ranged in final bid prices from \$10 to \$82,101.

State Surplus could not locate or provide an accurate disposition of the exceptions noted in this finding. State Surplus management stated that most items transferred from State agencies for disposition were generally not worth the expense of inventorying.

RECOMMENDATION

We recommend that State Surplus maintain sufficient records to accurately account for the disposition of surplus items received from State agencies.

AGENCY PRELIMINARY RESPONSE

DTMB provided us with the following response:

DTMB agrees with the recommendation and will work to maintain sufficient records to accurately account for the disposition of surplus items received from State agencies. DTMB will research available options for an inventory management system (IMS) to track the items received into State Surplus. While researching potential IMS solutions, DTMB will identify a threshold for tracking items received and will track all items above the established threshold for each disposal request received.

FINDING

3. Auction Controls

State Surplus did not monitor access to the vault when Department of Treasury unclaimed property was kept in the vault although four vault keys existed.

A signed agreement between DTMB and the Department of Treasury authorizes DTMB to use its contracted auction vendor to liquidate unclaimed property escheated to the Department of Treasury. Two Department of Treasury unclaimed property auctions managed by State Surplus occurred during our audit period. State Surplus policy requires the use of a key sign-out sheet to account for the four vault keys when Department of Treasury unclaimed property is in the vault.

We requested key sign-out sheets for the vault for our audit period. DTMB management informed us that it discontinued the use of the key sign-out sheet after it moved into its current location in early 2012. The lack of key sign-out sheets prevents management from monitoring access to the vault when Department of Treasury unclaimed property is in the vault. The last three Department of Treasury unclaimed property auctions generated \$449,984, \$332,974, and \$209,890 in March 2014, July 2012, and July 2011, respectively.

RECOMMENDATION

We recommend that State Surplus monitor access to the vault when Department of Treasury unclaimed property is kept in the vault.

AGENCY PRELIMINARY RESPONSE

DTMB provided us with the following response:

DTMB agrees and has complied with the recommendation. DTMB will continue to monitor access to the vault when Department of Treasury unclaimed property is kept in the vault. To comply with the recommendation, DTMB incorporated the use of a key sign-out log to track staff that enter the vault and their reason for accessing the vault.

GLOSSARY

Glossary of Abbreviations and Terms

DTMB	Department of Technology, Management, and Budget.
effectiveness	Success in achieving mission and goals.
IMS	inventory management system.
internal control	The plan, policies, methods, and procedures adopted by management to meet its mission, goals, and objectives. Internal control includes the processes for planning, organizing, directing, and controlling program operations. It also includes the systems for measuring, reporting, and monitoring program performance. Internal control serves as a defense in safeguarding assets and in preventing and detecting errors; fraud; violations of laws, regulations, and provisions of contracts and grant agreements; or abuse.
material condition	A matter that, in the auditor's judgment, is more severe than a reportable condition and could impair the ability of management to operate a program in an effective and efficient manner and/or could adversely affect the judgment of an interested person concerning the effectiveness and efficiency of the program.
Michigan Administrative Information Network (MAIN)	The State's automated administrative management system that supports accounting, purchasing, and other financial management activities.
MSP	Michigan Department of State Police.

performance audit	An audit that provides findings or conclusions based on an evaluation of sufficient, appropriate evidence against criteria. Performance audits provide objective analysis to assist management and those charged with governance and oversight in using the information to improve program performance and operations, reduce costs, facilitate decision making by parties with responsibility to oversee or initiate corrective action, and contribute to public accountability.
personal property	Items other than real estate or buildings. Specific to State Surplus, personal property is all office supplies and furnishings, as well as law enforcement confiscated items and TSA abandoned property from various airports within the State.
reportable condition	A matter that, in the auditor's judgment, is less severe than a material condition and falls within any of the following categories: an opportunity for improvement within the context of the audit objectives; a deficiency in internal control that is significant within the context of the audit objectives; all instances of fraud; illegal acts unless they are inconsequential within the context of the audit objectives; significant violations of provisions of contracts or grant agreements; and significant abuse that has occurred or is likely to have occurred.
surplus	surplus personal property.
TSA	Transportation Security Administration.

