

**Performance Audit 14-01:  
Surplus Property Disposal  
Process**

**July 2015**

**City Auditor**

Stan Sewell, CPA, CGFM, CFE

**Senior Auditor**

Pam Swinney, CPA





# OFFICE OF INTERNAL AUDIT

## Stan Sewell, City Auditor

July 17, 2015

To: Mayor Andy Berke  
City Council Members

Subject: Surplus Property Disposal Process, Audit 14-01

Dear Mayor Berke and City Council Members:

The attached report contains the results of our audit of the City's Surplus Property Disposal Process. Our audit found the current controls and processes could be improved to ensure surplus property is properly safeguarded. We found the fixed asset and sensitive minor equipment inventory listings do not always properly reflect surplus disposals.

Our review and analysis of the current process noted several areas for improvement. In order to address the noted areas for improvement, we recommended actions to develop a more fluid inventory and surplus tracking system and increase the use of the CRM work order system. Management has already implemented corrective actions to substantially address the findings and recommendations.

We thank the management and staff of the Purchasing, General Services, Information Services, Finance, Public Works, Fire and Police departments for their cooperation and assistance during this audit.

Sincerely,

Stan Sewell, CPA, CGFM, CFE  
City Auditor

Attachment

cc:    **Audit Committee Members**  
      **Travis McDonough, Chief of Staff**  
      **Brent Goldberg, Chief Operating Officer**  
      **David Carmody, Deputy Chief Operating Officer**  
      **Daisy Madison, City Finance Officer**  
      **Cary Bohannon, Director General Services**  
      **Brent Messer, Chief Information Officer**

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## AUDIT PURPOSE

This audit was conducted in accordance with the Office of Internal Audit's 2014 Audit Agenda. The audit was delayed due to the Procurement Analyst's maternity leave. The Procurement Analyst was our primary contact for the audit.

The objectives of this audit were to determine if:

- The City's controls and processes provide reasonable assurance that surplus property is properly safeguarded, utilized and/or disposed of in compliance with relevant laws and policies; and,
- The fixed asset and sensitive minor equipment inventory listings properly reflect surplus dispositions.

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## BACKGROUND

City Code Section 2-542 authorizes the Purchasing Department to manage the surplus property disposition process. The City of Chattanooga uses various means for disposing of the surplus property. For the selling of City vehicles and some heavy equipment, the City has used Chattanooga Auto Auction. This auction is open to the public and can be viewed on the website for various dates and times of each sale.

In February 2014, the City's Purchasing Department authorized Compass Auctions & Real Estate, LLC (Compass) to prepare and sale the City's property in accordance with the contract terms and conditions. The contractor maintains an online auction at [www.soldoncompass.com](http://www.soldoncompass.com). In return, Compass receives 10% of the gross selling price from the proceeds. In addition, Compass charges, and is paid by each buyer, a buyer premium of 10%. Compass retains the entire buyer premium.

### Financial Information

For informational purposes, Exhibit 1 provides the gross revenues from the sale of city-owned property. Revenues generated from surplus property decreased from \$800 thousand in fiscal year 2012 to \$235 thousand in fiscal year 2014. Although outside the scope of this audit, the current fiscal year has surplus revenues showing a dramatic increase to almost \$1.2 million. Although the majority of the total increase is related to the sale of real property and fleet vehicles, we noted sale of surplus equipment and scrap were on the rise as well.

Exhibit 1: Revenues from Sale of City Property<sup>1</sup>

Fiscal Year	2012	2013	2014
Sale of Back Tax Lots	36,582	387,840	93,282
Sale of Real Estate	588,753	327,625	92,450
Sale of Confiscated Vehicles & Equipment	16,625	24,062	5,925
Sale of Equipment	196,590	325,276	135,214
Sale of Surplus Equip & Scrap	1,281	4,519	3,986
Total Revenues	803,249	681,481	237,575

Sources: Oracle Financial Records

**FINDINGS AND RECOMMENDATIONS**

**A fluid inventory tracking system is needed to efficiently maintain a perpetual inventory.**

City Code Section 2-5 requires each department of the city to “keep a perpetual inventory of the city property under its control”. Under the perpetual inventory system, the entity continually updates the inventory record to account for additions and removals from inventory. The system works best when coupled with a computer database and barcode system.

Overall, the City’s current inventory system is fragmented with the capital assets being inventoried by Finance Department using the Oracle system and the non-capital assets (i.e. sensitive minor equipment) being inventoried at the department level using different tracking systems. To provide guidance to the various City departments, the Finance Department has adopted *Policy and Procedures Guide for Capital Assets* and *Policy and Procedures Guide for Sensitive Minor Equipment*.

The primary purpose of the *Policy and Procedures Guide for Capital Assets* is to maintain physical accountability over the capital assets<sup>2</sup>. Finance monitors purchase orders for assets, processes updates to the capital asset record, and provides the department with identification tags. Removals from inventory are processed based on information (asset disposition forms) received from the various departments. On a quarterly basis, Finance forwards an inventory listing to each department requiring they perform a physical inventory and report back any changes to Finance.

<sup>1</sup> “Sale of Equipment” includes the resale or scrap of city-owned vehicles and heavy equipment. “Sale of Surplus Equip & Scrap” includes the resale of all other personal property, including computers, appliances, furniture, etc.

<sup>2</sup> Capital assets are defined as major assets with benefits more than a single fiscal period and costing in excess of \$5,000.

The sensitive minor equipment<sup>3</sup> policy ensures the accountability of equipment that cost under the \$5 thousand threshold. Unlike capital assets, each department is tasked with tagging and tracking all sensitive minor equipment using a perpetual inventory system. On a quarterly basis, the departments are required to perform a physical inventory and submit the detailed SME Inventory Listing to Finance noting any changes since the last inventory was performed.

To determine if the perpetual inventory systems properly reflect surplus dispositions, we reviewed a random selection of current fixed assets found on the September 2014 Citywide Fixed Asset Listing. We also selected a random sample of property removed from the various departmental SME Inventory listings. We found discrepancies in both inventories including items removed from the listings without corresponding surplus forms and assets sold that were not properly removed from the inventory listings.

Both the perpetual inventory system and surplus disposition process require a fluid system to ensure city assets are properly safeguarded. Our current system does not ensure all assets are properly accounted for and the respective inventory listings reflect all additions and deletions in a timely manner.

### **Recommendation 1:**

We recommend the Finance Department, with the assistance of the IT Department, consider developing or purchasing a computerized inventory tracking system.

***Auditee Response (Finance):** We concur with the audit finding and recommendation. The 2015-2016 Capital Budget includes funding to purchase a citywide inventory system which will encompass the surplus process.*

### **Purchasing should maintain a perpetual inventory of all surplus property.**

Although a standard excel template<sup>4</sup> was developed and encouraged by the Finance Department, not all departments use this standard version. We found various modifications were made to the template reducing our ability to analyze, on a citywide basis, the additions and deletions from inventory. We also noted departments did not report disposals in

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<sup>3</sup> Sensitive minor equipment is defined as moveable, high-risk, sensitive property, such as TVs, cameras, chainsaws, tools, lawn mowers and small office machines, as well as furnishings and works of art.

<sup>4</sup> The standard excel template is used to record and track additions and disposals of Sensitive Minor Equipment (SME Inventory) only.

a consistent manner or with all the required information (e.g. date of disposal, reason for disposal) on its quarterly SME Inventory Listing.

Since the Purchasing Department has the responsibility to dispose of surplus property, City departments transfer property to Purchasing through a surplus process. Once the property has transferred, Purchasing is responsible for maintaining an accurate perpetual inventory until the items are disposed of or sold at auction. We found, as reported in our previous 2008 audit, Surplus Property Audit 08-12, Purchasing has not developed or maintained a perpetual inventory system for all the surplus property under its control.

### **Recommendation 2:**

Until a single cohesive system is in place, we recommend Purchasing develop and maintain a perpetual inventory system for all surplus property under its control.

***Auditee Response (Purchasing):** We concur with the audit finding and recommendation.*

**Using an excel format for the asset disposition form would assist Purchasing with maintaining its surplus inventory.**

Our review of completed surplus forms found that the departments did not always include all the necessary information to identify the property. In many cases, the City tag numbers were missing as well as serial numbers. Departments also rarely complete the fair market value of the property and the form does not provide an option to indicate the property's current condition. We also found the form lacks an approval signature from IT personnel that would provide assurance that all technology equipment is properly inspected and approved for resale or disposal.

Currently surplus forms, see Appendix "B", are submitted in PDF format. Although the form was developed to include an automatic submission, the mechanism is not functioning properly. We found the form cannot be saved and therefore must be completed and printed immediately. If a standard form was developed in an excel type format, Purchasing could easily add the items to its surplus inventory listing with minimal effort.

### **Recommendation 3:**

We recommend Purchasing change the surplus template to an excel format and update the form to include approval area for IT personnel.

*Auditee Response: We concur with the audit finding and recommendation.*

#### **Recommendation 4:**

We recommend Purchasing implement a procedure to follow up with the department if they submit incomplete forms.

*Auditee Response: We concur with the audit finding and recommendation.*

**Comprehensive policies and procedures provide guidance to City departments.**

The primary goal of the surplus process is to ensure the City receives the maximum return for surplus assets at the least cost to the City. A strong policy and procedures guide, along with ongoing analysis of the process, is essential in meeting this primary goal. The surplus property policies and procedures are scattered among three manuals; the two Finance policies, mentioned above, and section 5 of Purchasing's *Procurement Instruction Manual*. Although the policies adequately outline the responsibilities of each department, it doesn't consider the following:

- What to Declare Surplus;
- How to surplus Dangerous Items (e.g. ammunition, handguns);
- What items to hold for redistribution/transfer to other departments;
- What items to sell;
- How to determine fair market value of items;
- How long to keep items in the warehouse;
- Criteria for Determination of Method of Disposal; and,
- What items require approval from IT Department.

Written policies and procedures provide a basic framework of management's expectations and enable the city departments to accomplish their mission and goals. To ensure consistency and accuracy of the surplus process, the Purchasing Department should create more detailed procedures.

#### **Recommendation 5:**

We recommend Purchasing incorporate detail surplus procedures, including exceptions, in its policy manual (or adopt a separate surplus property manual). The inventory clerks, supervisors and administrators

should receive training on the appropriate procedures and be provided the updated policy and procedure manual.

***Auditee Response:** We concur with the audit finding and recommendation.*

**Enhancements to the surplus request process can improve its overall efficiency.**

Per the Purchasing Department, the surplus process begins when the department head approves, by signature, the surplus form. The department submits the completed disposal form to Finance and Purchasing typically via email. Using the City's 311 Call Center, Purchasing will then submit a service request<sup>5</sup>, attaching the asset disposition form, for building maintenance to pick up the items.

Using the Motorola CRM system, a service request is generated and Building Maintenance receives a work order in its Que. After Building Maintenance transfers the property to the surplus warehouse, the service request is closed and the final surplus form is forwarded to Purchasing.

We examined the process efficiency through staff interviews, review of surplus requests and physical observation. We sampled "Move-Furniture" service requests, purchasing emails and surplus disposition forms. We developed process flowcharts of the surplus process based on staff interviews and our observations. The process flowcharts are found in Appendix "C". Based on our understanding of the current process, we identified the following areas for possible improvements.

**Implement procedures to reduce the multiple times property is moved by City employees.**

In Appendix C, we identified (highlighted in yellow) multiple times surplus property may be handled by city employees. As the process flowchart depicts, downtown building maintenance staff could be required to move property up to four times. In departments with onsite maintenance staff, the property could be moved up to five times prior to final disposal.

Surplus property has several possible outcomes: garbage, scrap, sale at auction, or transfer to new department. Typically, the department with original ownership can identify a recommended means of disposal. For instance, if the item is broken beyond repair, it would be more cost-effective for Purchasing to approve the disposal and eliminate the

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<sup>5</sup> A service request type, Move-Furniture, is generated by the City's 311 work order system. Building Maintenance receives a work order which provides workflow priority and tracking.

need for building maintenance to transfer the items to the warehouse and then to the garbage.

This approval procedure could be accomplished by forwarding photographs with the surplus form to Purchasing. Purchasing could review and approve the disposal, forward the signed approval to the department and either require building maintenance to dispose of the items or defer to the department the responsibility to place the items in the dumpster.

Other possible strategies include, but are not limited to:

- Require photographs be submitted for all surplus items along with the surplus form;
- Develop an internal database for department's to submit pictures of equipment and request transfers;
- Require departments to indicate the condition of the property on the surplus form; and,
- Require departments with maintenance personnel to schedule a delivery time and deliver surplus property directly to the surplus warehouse.

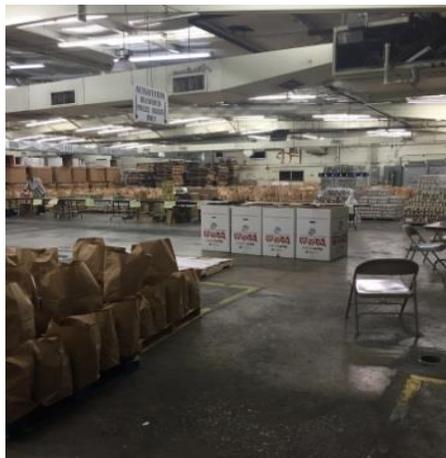
### Recommendation 6:

We recommend Purchasing implement procedures to eliminate, as much as possible, the multiple times surplus property is handled by employees.

*Auditee Response: We concur with the audit finding and recommendation.*

### The surplus property should be properly safeguarded and have dedicated space in the warehouse.

The warehouse used to store surplus property is located off Main Street. This warehouse is not used exclusively for surplus property. We found areas in the warehouse were used to store the LED streetlight inventory, various department records (in individual cages), Toys for Tots (during Christmas season), and YFD Commodities (3 to 4 times per year). In addition, a portion of the warehouse has been leased to a non-profit organization,



Chattanooga Goodwill, to provide surplus and donated furniture, appliances, and other household goods to individuals and families entering permanent housing through the Chattanooga Furniture Bank.

Although citizens have limited opportunity to access the building, **we found non-building maintenance employees have unfettered access to the warehouse**; including the employees of the Furniture Bank, employees from Compass Auction and individuals associated with the Toys for Tots and Commodities program.

The five year lease agreement with the non-profit provides use of approximately 8,600 square feet of usable space and 450 square feet of common area space. During our onsite visit we found what appeared to be encroachment by Furniture Bank to areas outside those provided under the lease. We found stacks of used mattresses in two additional areas of the warehouse.



In addition to the limited space available to store the surplus property, we learned the use of the warehouse during the Toys for Tots and YFD Commodities programs require the surplus property be moved to another area in the warehouse. All these factors decrease the efficiency of the surplus process and increase the possible risk of loss or theft.

### **Recommendation 7:**

We recommend a dedicated area in the warehouse be used for surplus property.

***Auditee Response:** We concur with the audit finding and recommendation.*

### **Recommendation 8:**

We recommend the General Services Department enforce the terms of the contract and have the non-profit organization remove any non-city property from the areas not provided under contract.

***Auditee Response:** We concur with the audit finding and recommendation.*

**Recommendation 9:**

We recommend the General Services Department limit access to the areas containing surplus property.

*Auditee Response: We concur with the audit finding and recommendation.*

**Expanding the use of the CRM system could streamline the process.**

Currently, only the building maintenance portion of the surplus process uses the work order system. Neither the Purchasing nor the IT Departments have access to the CRM system. The majority of the surplus process requires multiple emails amongst these departments.

We found the service request type used to generate surplus service requests were neither unique to the surplus process nor consistently used (could be “Move-Furniture” or “Misc-Building Maintenance”). However, we did note the “Move-Furniture” type included several surplus property-related questions. It did not inquire whether it was computer-related equipment and/or if the IT Department had inspected and approved the equipment for sale or disposal.

Based on our review, we conclude the CRM service request system could be more fully utilized. Greater use of the system could streamline the process by consolidating the communications and records retention in one location. However, the new process would require the departments to initiate all surplus requests using only the CRM system (i.e. remove email requests).

**Recommendation 10:**

We recommend Purchasing, with the assistance of the IT Department, develop a service request type dedicated to surplus property. The service request flex questions should include all necessary information to properly route the work order between IT, Purchasing and Building Maintenance.

*Auditee Response: We concur with the audit finding and recommendation.*

**Recommendation 11:**

We recommend Purchasing, with the assistance of the IT Department, expand the use of the CRM system to more efficiently organize and track the surplus process.

***Auditee Response:** We concur with the audit finding and recommendation.*

**Recommendation 12:**

We recommend Purchasing include a procedural requirement that all surplus requests be initiated by the departments using the CRM system only.

***Auditee Response:** We concur with the audit finding and recommendation.*

**Recommendation 13:**

We recommend Purchasing, with the assistance of the IT Department, consider providing a surplus request link on the 311 website.

***Auditee Response:** We concur with the audit finding and recommendation.*

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## APPENDIX A: SCOPE, METHODOLOGY AND STANDARDS

Based on the work performed during the preliminary survey and the assessment of risk, the audit covers the surplus property process from July 1, 2013 to June 30, 2014. When appropriate, the scope was expanded to meet the audit objectives. Source documentation was obtained from Finance, Purchasing, Information Technology and General Services departments. Original records as well as copies were used as evidence and verified through physical examination.

To evaluate the efficiency of the surplus process, we reviewed the policies and procedures, interviewed staff from Finance, Fire, Police, Purchasing, Public Works, Information Technology and General Services Departments, and visited the departments and the surplus warehouse.

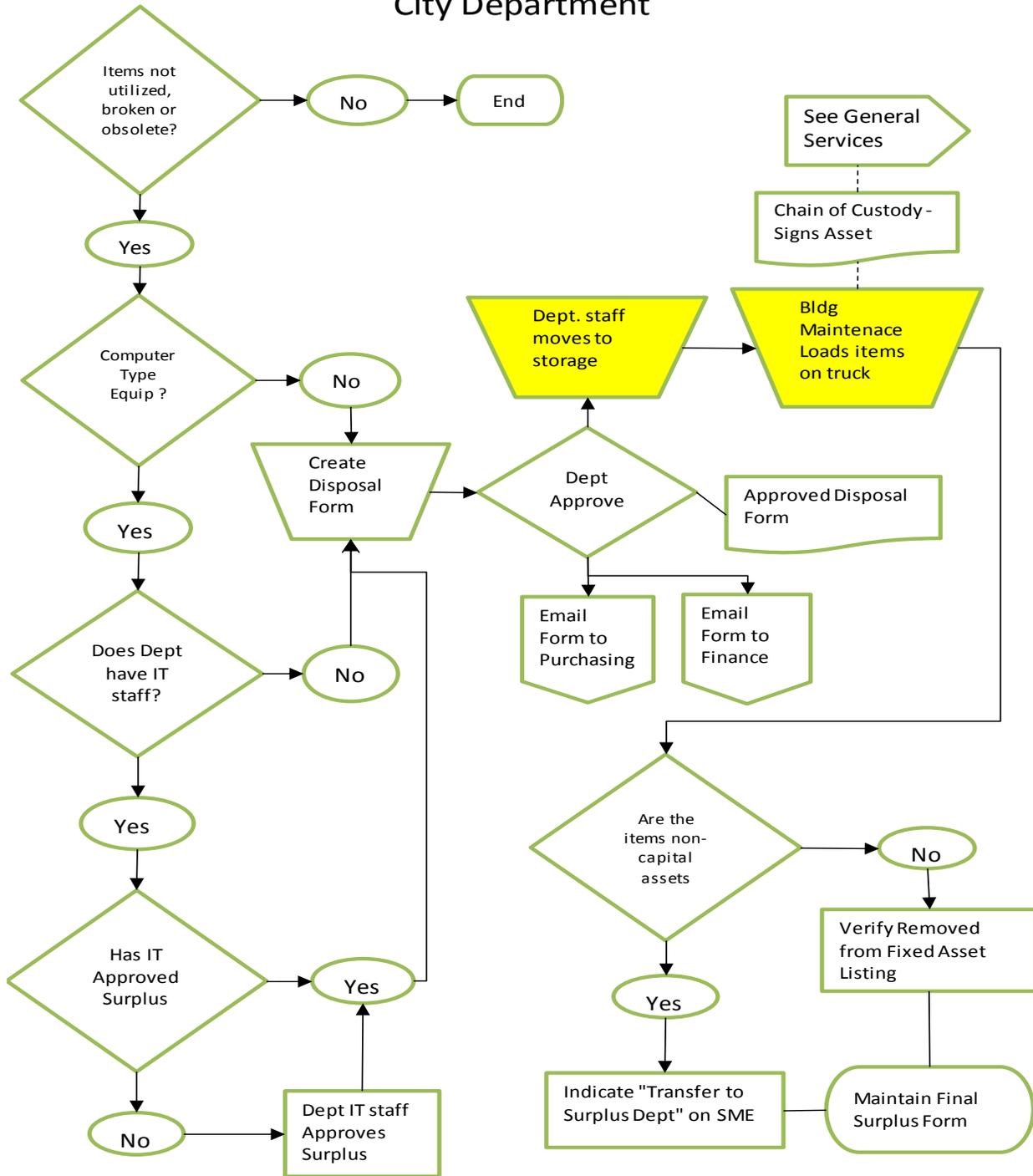
The sample size and selection were statistically generated using a desired confidence level of 90 percent, expected error rate of 5 percent, and a desired precision of 5 percent. Statistical sampling was used in order to infer the conclusions of test work performed on a sample to the population from which it was drawn and to obtain estimates of sampling error involved. When appropriate, judgmental sampling was used to improve the overall efficiency of the audit.

We conducted this performance audit from September 2014 to May 27, 2015 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.

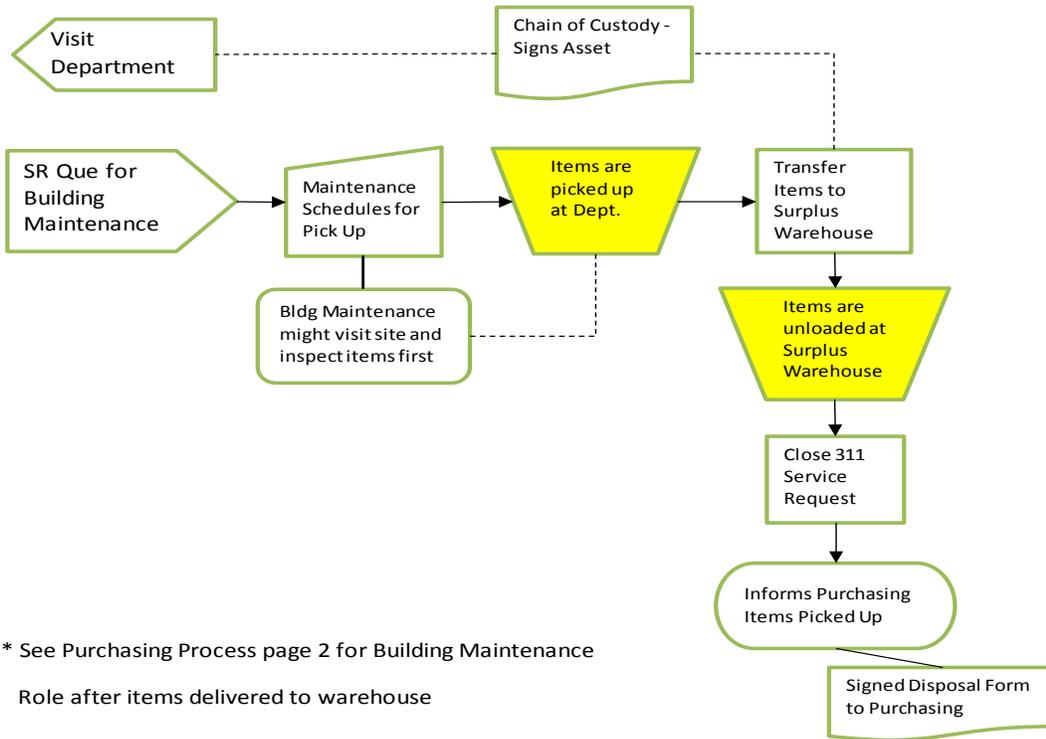


# APPENDIX C: SURPLUS PROCES OF CAPITAL AND NON-CAPITAL ASSETS

## City Department



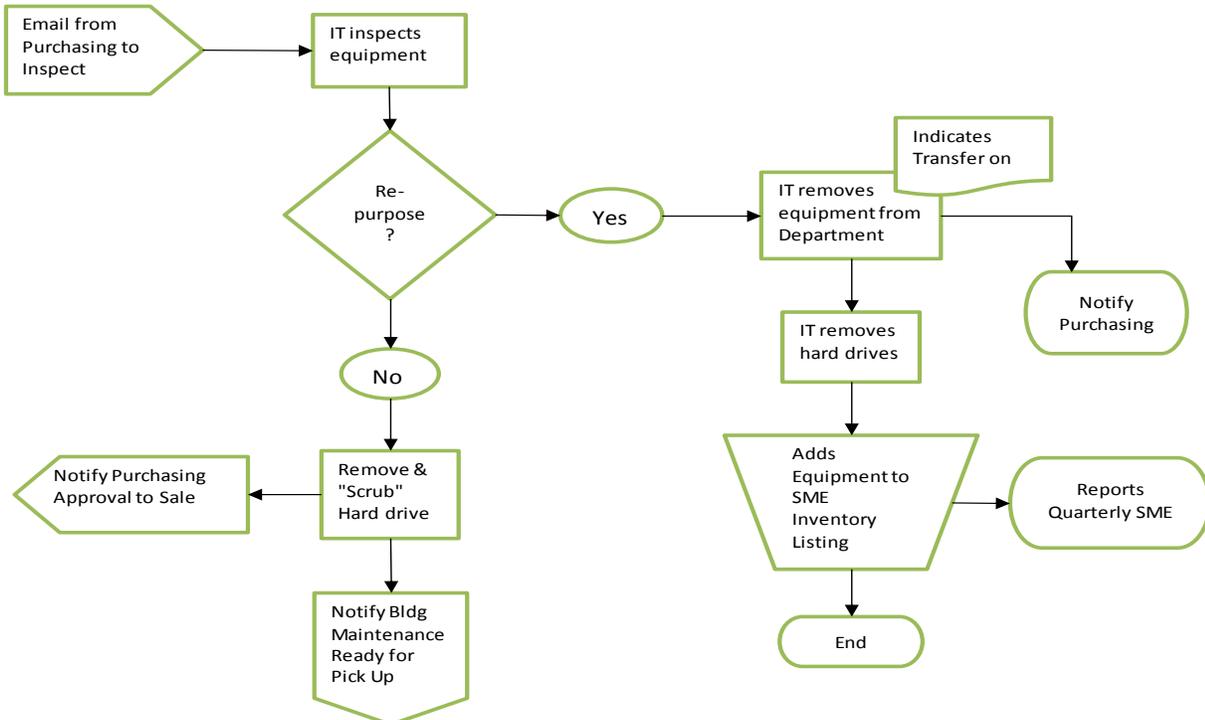
## Building Maintenance Division



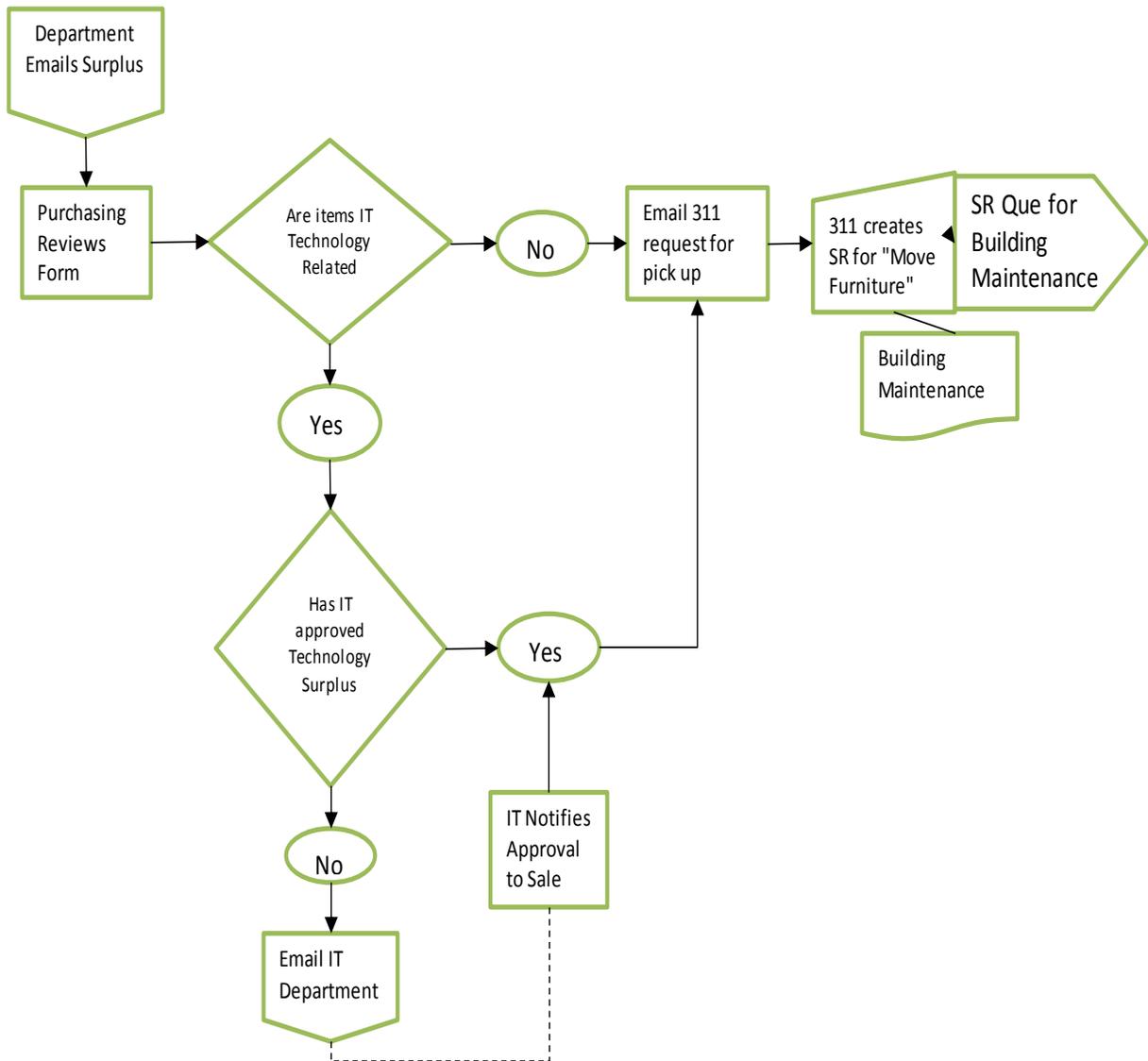
\* See Purchasing Process page 2 for Building Maintenance

Role after items delivered to warehouse

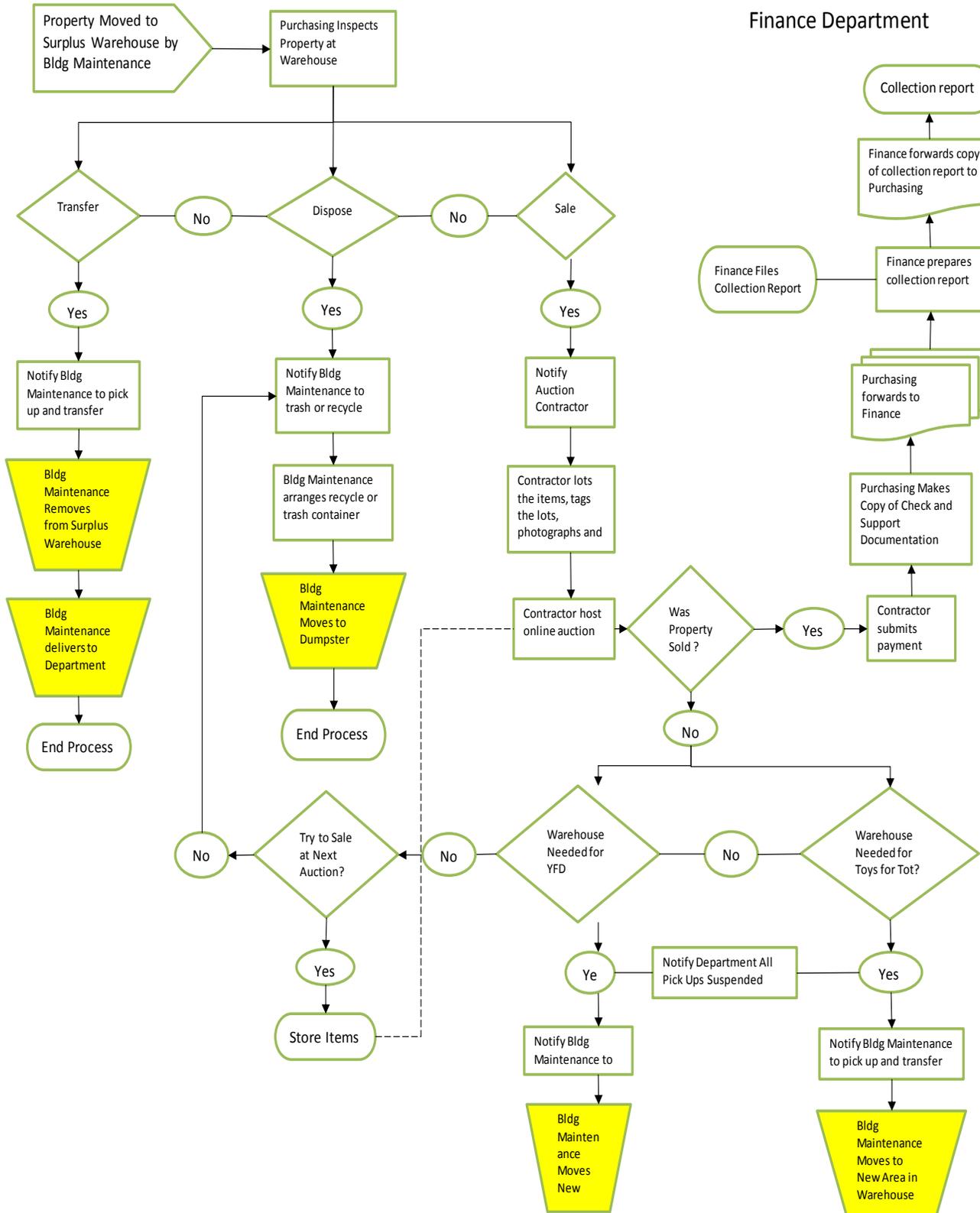
## Information Technology Department



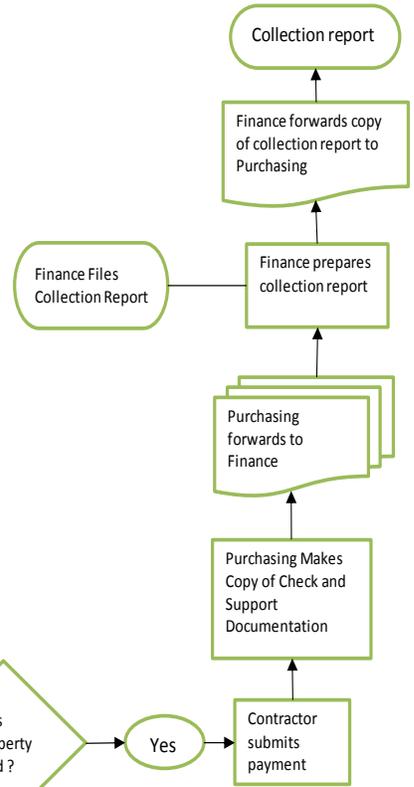
# Purchasing Division



## Purchasing Division: Process Continued



## Finance Department



### **City of Chattanooga Fraud, Waste, and Abuse Hotline**

Internal Audit's Fraud, Waste, and Abuse Hotline gives employees and citizens an avenue to report misconduct, waste or misuse of resources in any City facility or department.

Internal Audit contracts with a hotline vendor, The Network, to provide and maintain the reporting system. The third party system allows for anonymous reports. All reports are taken seriously and responded to in a timely manner. Reports to the hotline serve the public interest and assist the Office of Internal Audit in meeting high standards of public accountability.

To make a report, call 1-877-338-4452 or visit our website:

[www.chattanooga.gov/internal-audit](http://www.chattanooga.gov/internal-audit)