



MIAMIBEACH

BUDGET AND PERFORMANCE IMPROVEMENT
Internal Audit Division

INTERNAL AUDIT REPORT

TO: Jorge M. Gonzalez, City Manager
VIA: Kathie G. Brooks, Budget and Performance Improvement Director
FROM: James J. Sutter, Internal Auditor 

DATE: June 30, 2010
AUDIT: Public Works Warehouse Inventory Audit 
PERIOD: Fiscal Year Ended September 30, 2009

This report is the result of an annually scheduled audit of the Public Works Warehouse Inventory as of September 30, 2009, performed in conjunction with the external auditor's annual financial audit of the City. This audit did not include testing of quotes received, prices invoiced, quantities received, etc. and their supporting documentation as those topics were covered in two recently completed audits entitled Public Works Department Inventory Processing and Public Works Department Warehouse Purchasing.

INTRODUCTION

The Public Works warehouse located at 451 Dade Boulevard, supplies materials for all phases of Public Works operations. These materials are received for and issued to the various divisions (Water, Sewer, Storm Water, Engineering, Environmental, Streets and Streetlights) and are either charged to specifically assigned job orders or individual vehicles.

When the Public Works warehouse purchases inventory during the fiscal year by City check through purchase orders and Requests for Direct Payment, general ledger account number 191-4400-000481 (Inventory Purchase MX Stock) is debited and the MX Stock pooled cash account is credited. The Inventory Purchase MX Stock account is related to bond monies received by the City and needs to be reported separately.

The monies are subsequently reclassified or assigned to the appropriate divisions/areas as designated by warehouse personnel in Cityworks when the inventories are issued. Similarly, the corresponding pooled cash account is also adjusted. These adjustments are done via journal entry number 005 monthly by a Financial Analyst III based on data received from the Cityworks report called Warehouse Issue Report Summary.

These reclassification entries are needed because warehouse personnel do not always know who will use the inventory at the time of purchase as some parts may be used by a number of different division/area (bolts, screws, etc.) at a later date. Therefore, this Inventory Purchase MX Stock account is continually decreasing as parts are issued until the balance is so low that the account needs to be replenished.

As part of the inventory tracking process, job order numbers are created to track the cost of labor, materials, and equipment used in projects performed by the Public Works Department; allow the Department to know the cost of the projects; and recover the cost of repair or replacement of City

Internal Audit Report
Public Works Warehouse Inventory Audit
June 30, 2010

property damaged by or caused by an outside party. Small materials and equipment that are not job specific are charged to the individual truck number where the crew is assigned for such personal items as tools, raincoats, etc. to record disbursement at no charge. These items cannot be charged to a specific job and their issuance can be monitored by warehouse personnel to help ensure that departmental employees are not misplacing or being careless with City property.

In addition to material receipt, storage and distribution, the warehouse orders, maintains and supplies parts to outside contractors in support of other City capital projects. This may occur in instances where either the outside contractor damages City materials during his work (the contractor pays for materials ordered through a special budget code and work order), or when the City agrees to supply the materials and the contractor provides the labor (in this case, the City pays for both the materials and the labor). According to the Warehouse Supervisor, this occurred an estimated ten times during the audit period, with one recent example being the purchase of two meter boxes by G.T. McDonald for installation at 1111 Lincoln Road after the existing ones were inadvertently damaged by the contractor.

Received parts are accepted by warehouse staff and compared to the packing slip for completeness. In addition, the charged prices are checked against those quoted to confirm their agreement. Once approved, the inventory is accepted, entered into the Cityworks system and ultimately paid through normal procurement channels.

Conversely, parts are issued to authorized personnel upon the proper completion of Public Works originated three-part Inventory Issuance (MX-1) forms. Among other information, these pre-numbered sequential forms require the preparer to enter the date, job order number, part number, quantity, part description, job location and issuer name. The cost assigned to the item is based on the Cityworks calculated weighted average cost which factors in each time that the item has been purchased since 1984. The white copies of the form are maintained internally by the warehouse clerk and filed by the associated number to ensure that all are accounted for. The yellow copies are sent to the respective Operations supervisor (Water, Sewer, etc.), typically at week's end. The pink final copy is given to the employee receiving the inventory. The Operations supervisors are to periodically compare the yellow and pink copies to ensure that quantities and costs match and to investigate any differences.

Warehouse personnel currently consists of a Warehouse Supervisor, a Storekeeper III, two Storekeeper IIs, a Municipal Service Worker I and an Administrative Aide I. These personnel interact with the Procurement Division, Finance Department, and vendors in the purchase and delivery of goods, inventory issuances and payments. They all have the ability to receive and enter inventory in the Cityworks System, implemented in April 1, 2006, whose purchase was authorized by City Commission Resolution No. 2006-26231. However, any changes or additions/deletions to the inventory in the Cityworks system are limited to the Warehouse Supervisor and Storekeeper III.

A majority of the Public Works inventory is stored inside the warehouse located at 451 Dade Boulevard. It is the largest and most secure facility, as it is protected by cameras and locked alarmed doors. Other inventory storage locations on the property also protected by cameras include the following:

- Yard 1- A secure fenced area, with a covered roof, located directly south of the warehouse at the bottom of the loading dock ramp. This secure area is used to safeguard such larger, frequently issued items as selected clamps, valves, glands, etc.
- Yard 2 - A secure fenced area located south of Yard 1, by the water tanks, and bordering

Internal Audit Report
 Public Works Warehouse Inventory Audit
 June 30, 2010

Miami Beach Senior High School. The items stored in this area consist primarily of light poles, hydrants, pipe, offsets, and caps.

- Central Yard Area - City vehicles, as well as assorted equipment and inventory are stored in the middle of the yard.

Finally, large slower moving inventory was moved to fenced facilities located at 75th Street and Dickens Avenue and 81st Street and Hawthorne Avenue. Examples of inventory stored in these facilities are selected bends, sleeves, light poles and concrete bases.

A full physical count of the Public Works inventory is taken at the end of each fiscal year by warehouse personnel. Internal Audit conducts test counts to verify their count, with any noted differences counted again with a supervisor until a consensus is reached as to the correct total. Once the final count is agreed upon, warehouse personnel adjust the inventory count numbers in the Cityworks system and a new value for the inventory at fiscal year end is calculated. This inventory value is then forwarded to the City's Finance Department which prepares a journal entry to adjust the applicable general ledger beginning fiscal year inventory balances to equal the previous fiscal year's year end physical count inventory values.

Public Works warehouse inventory was valued at the following amounts for the last five fiscal years:

9/30/2005	9/30/2006	9/30/2007	9/30/2008	9/30/2009
\$1,797,500	\$1,981,523	\$2,194,784	\$2,015,324	\$2,215,242

This Fiscal Year 2008-09 ending inventory of \$2,215,242 was 9.92% higher than the previous fiscal year. Internal Audit conducted test counts of one hundred twenty-five (125) part numbers totaling 5,473.80 items with a value of \$628,632.40 or 28.38% of the current inventory value. We commend Public Works warehouse staff that faced occasional interruptions due to the need to disburse emergency items during the approximately two weeks that the warehouse was closed for inventory.

OVERALL OPINION

Based upon the results of the test counts and the inventory reports, we recommend that the valuation of \$2,215,242 be used as the September 30, 2009 inventory value. The annual physical inventory of the items was conducted in an effective and timely manner, and the corresponding valuation was deemed reasonable. In conducting our inventory counts and reviewing the internal controls surrounding the inventory, we noted shortcomings in the following areas in need of improvement, with any repeat of prior year's findings noted by an asterisk:

- A comparison of the Citworks count with Internal Audit's verified sampled physical counts found differences totaling \$643.49 for 31.20% of the tested items which represented an improvement over the last two years but is still well above the desired maximum internal goal of 10%. *
- Obsolete inventory has not been regularly discarded prior to the annual physical counts thereby overstating the fiscal year end carrying balance.
- Possible improvements to the camera system protecting 451 Dade Boulevard are listed

Internal Audit Report
Public Works Warehouse Inventory Audit
June 30, 2010

which should increase their effectiveness.

- Noted security weaknesses included staff having possession of master keys to open gate locks protecting inventory in remote yards, unsupervised access to charge out inventory items and an inoperable main facility front gate. These items were mentioned to warehouse management as they may increase the City's risk exposure of the likelihood that City property could be damaged or misappropriated. *
- The City's water tanks located at 75th Street and Dickens Avenue are not properly safeguarded from unauthorized intruders.
- The Public Works Department had not updated its policies and procedures to better detail the newly instituted warehouse and Cityworks practices. *

PURPOSE

The purpose of this audit is to determine whether Public Works warehouse inventory is sufficiently counted, valued and recorded; properly safeguarded from theft and breakage; and that entries are correctly recorded in the City's Financial System.

SCOPE

1. Confirm that documented operating policies, standards and procedures exist to ensure efficient and effective administration of the warehouse and that there is compliance with these policies, standards and procedures, as well as all laws and regulations.
2. Confirm that warehouse inventory items are stored at all locations in an orderly manner, are clearly labeled, are properly safeguarded and are reasonably valued.
3. Confirm that the physical inventory was performed in an efficient, effective and timely manner with sufficient personnel and adequate procedures to ensure an accurate count.
4. Confirm by test counts that the final inventory report accurately reflects the final inventory valuation as determined by the physical count and that this information is communicated to the external auditors and reported in the City's Financial System.
5. Confirm the financial viability of the Public Works inventory fund over the long term.

FINDINGS, RECOMMENDATIONS AND MANAGEMENT RESPONSES

1. Finding – Physical Count Comparison
Internal Audit conducted test counts of one hundred twenty-five (125) part numbers totaling 5,473.80 items with a value of \$628,632.40 or 28.38% of the current inventory value. Our test counts were compared to Public Works staff's physical counts and if they agreed then the corresponding total was used as the final count. If they disagreed, then the item was counted again with a supervisor until a consensus was reached as to the total. This verified

Internal Audit Report
Public Works Warehouse Inventory Audit
June 30, 2010

count was then used as the basis for the item's inventory valuation.

These sampled items' verified counts were compared with the amounts listed in Cityworks initial 09/24/09 report's recorded count. These counts should be equal as Cityworks uses the perpetual inventory method meaning that the item's inventory balance is increased as parts are received and reduced accordingly as they are issued.

Testing showed that a count difference existed for 39 of the 125 total sampled part numbers or 31.20% although sometimes the Cityworks count was higher and other times the physical count was higher. A net immaterial overage of \$643.49 of the tested inventory value resulted as sometimes the sampled part's cost was high and other times it was relatively inexpensive. The Cityworks inventory totals were subsequently adjusted to reflect the full inventory physical count recorded by Public Works' staff, with the adjustments for Internal Audit counts, to help ensure that valuation is reasonably correct as of 09/30/09.

The reasons for the difference (shrinkage, improper recordkeeping, incorrect part numbers, etc.) between the verified count and the Cityworks count could not be determined. Although still much higher than the desired internal goal of 10% or less, this fiscal year's percentage difference of 31.20% represents an improvement over the last two years 40.83% and 47.97%.

Recommendation(s):

The compensating control of performing full scale physical inventory counts should continue to be performed as the present difference materially exceeds the desired 10% maximum goal. Public Works Department management should also more closely review this process to determine where the breakdowns are occurring so that procedures and internal controls can be created and/or amended to help achieve desired levels going forward.

Management Response:

Although improvements were made Management continues to strive to reduce the percentage difference and meet or exceed the 10% goal or better. Staff will flowchart process to identify potential problems and identify improvement opportunities within 60 days. At 90 days staff will reassess, make necessary adjustments, set targets, and provide training to staff as needed. At year end Public Works Management will evaluate results.

2. Finding – Obsolete Inventory

Inventory occasionally becomes obsolete due to technological improvements, time, etc. and loses much or all of its value. Unless these items are scrapped and their value downgraded, the fiscal year end inventory carrying value will be inflated. Inquiries found that Public Works has not performed this exercise during the past three years. Warehouse staff met with operational supervisors during this year's physical count and it was determined that 2,652.00 items from water, street lights and pump shops having a value of \$139,445.18 were obsolete and were therefore removed from inventory and not included in the final inventory valuation.

Recommendation(s):

Public Works materials and equipment should be reviewed annually before the fiscal year end physical inventory is completed to determine if any items are obsolete so that their carrying value can be adjusted accordingly. Obsolete inventory should be disposed in accordance to the Procurement Division's Surplus and Confiscated Property Auction Procedures.

Management Response:

Obsolete parts are associated mostly with pump station equipment. Staff will forward a separate memorandum to Internal Audit Dept. Director requesting specific assistance and next steps for dealing with obsolete parts in general. Once this is clarified it will be incorporated into the policy and procedures manual. Staff will flowchart process and address every 6 months to check for obsolete parts and provide management report on how obsolete parts were handled.

3. Finding – Security Cameras

The Public Works facility located at 451 Dade Boulevard is now protected by thirty-two digital cameras to record daily activities as seven new cameras have been added during the past year. The system hardware, computer monitors and digital video recorder are safeguarded in the Control Room, which is continually staffed. These cameras are primarily used as a detective measure or are reviewed only after an incident has occurred to help determine fault. Sixteen cameras' activities can be viewed on one computer monitor called "Bank 1" and the remaining sixteen are visible on the other monitor called "Bank 2". Review of these cameras during a 08/10/09 interim site visit and inquiries with staff detected the following shortcomings:

- a. Five items totaling \$2,107.49 that were already charged out and were being stored in a container inside the Public Works yard were misappropriated on 07/10/09. There were no cameras at the time focused directly on this area and parked vehicles obstructed the view of the other cameras distantly aimed toward the three containers. A police report was filed and case number 2009-26296 was assigned. To date, the offenders have not been caught and a new camera was installed that records all activities at these storage containers to help prevent similar occurrences.
- b. Two cameras, bank 2 camera 2 and bank 2 camera 4, were not functioning as only a blank screen was shown. One of these cameras supposedly recorded activities in yard 2 which may be more subject to misappropriation due to its location behind the water tanks and bordering Miami Beach Senior High School.
- c. None of the cameras oscillated to cover a larger area.
- d. Camera angles were not properly positioned so as to better protect Public Works inventory. For example, cameras were not covering and recording daily activities inside the electrical room, warehouse or yard 1, areas in which most of the inventory is stored.

Recommendation(s):

The positioning and effectiveness of the cameras should be more frequently reviewed to maximize their benefit to the City. Furthermore, the manufacturer should immediately be notified of any malfunctioning cameras so that they can be promptly repaired. Public Works procedures should clearly define who has the responsibility for ensuring that the cameras are operational and for performing periodic random reviews of the recordings.

Management Response:

With respect to a): A new camera was installed that records all activities at these storage containers to help prevent similar occurrences

With respect to b): At the time of inventory, cameras were working. Additional cameras were added prior to this inventory as well as additional lighting in the yard. The responsibilities of

ensuring the cameras are operational and notifying the manufacturer immediately of any defects are assigned and in place. Cameras are positioned properly and the monitors are at the control room operator's desk in order to maximize monitoring.

With respect to c): These are fixed cameras. Cost of replacing 32 cameras will exceed \$55K. We will evaluate the installation of oscillating cameras at key locations.

With respect to d): Contractor was notified to correct.

Appropriate camera and monitor procedures will be included in the warehouse policies and procedures manual that will address monitoring frequency responsibilities.

4. Finding – Security Weaknesses

The following security weaknesses were identified during testing that could increase the possibility that City assets may be misappropriated, vandalized, damaged by the weather, etc.:

- a. Both the 75th Street and Dickens Avenue and 81st Street and Hawthorne Avenue facilities perimeter fences were secured with standard 3252 model locks. Numerous Public Works Department personnel have the master key and therefore can easily obtain unsupervised access to the facilities and their contents. These locations presently do not have any compensating controls such as security cameras, security personnel, etc.
- b. The main facility's (451 Dade Boulevard) front gate was made inoperable due to the renovations of Fire Station #2 and Miami Beach Senior High School. However, Internal Audit believes that renovations have progressed enough so that the gate can be re-installed to help prevent access by unauthorized individuals, especially during non-peak working hours.
- c. Charged out inventory was observed unprotected lying outside the three storage containers positioned directly east of the old pumping station at 451 Dade Boulevard where the theft addressed in finding number 3a occurred. Public Works management promptly secured this area upon notification.

Recommendation(s):

The implementation of the following recommendations should help better protect the City's assets stored at the three tested Public Works facilities:

- a. Greater security precautions should be taken at these remote facilities to better prevent unauthorized entry. Included among the ideas suggested are new locks whereby keys are only given to designated Public Works personnel, a separate fenced area could be created to safeguard inventory, etc.
- b. The front gate should be made functional as soon as possible.
- c. Public Works Department personnel should secure all unused items in the storage containers or be subject to possible disciplinary actions.

Management Response:

- a. Possession of keys are designated to supervisors and responsible maintenance staff.
- b. New front gate will be installed no later than May 1, 2010.
- c. During working hours, there may be times that unused materials or small equipment

may be outside a respective division container until the end of the day.

5. Finding – Water Tanks Safety

Water tanks located at 75th Street and Dickens Avenue were only protected by a chain link fence. Gaps in the chained gates, missing sections of barb wire, overhanging tree limbs, etc. can make unauthorized access easier.

Recommendation(s):

Public Works Department management should better enforce the yard parking rules and discipline anyone that does not conform. Meanwhile, the water tanks at the 75th Street location may be better safeguarded through repairing fencing deficiencies and pruning nearby trees.

Management Response:

Public Works Department Operations conducts repairs and pruning on an on-going basis at this location. Unfortunately, this is a recurring problem due to trespassing kids and transients. New heavy duty locks with special keys have been purchased and installed. The Public Works Operations Division Director has approval to duplicate keys.

6. Finding – Policies and Procedures

Although descriptive and covering a wide array of topics, the Public Works Department's policies and procedures were last revised (effective 10/01/02) and did not fully address warehouse operations. Some of the previous procedures changed with the implementation of the Cityworks System in April 2006. This process is known entirely by few and should be better documented to avoid further difficulties if personnel change.

Recommendation(s):

The Public Works Department's operating policies and procedures should be updated as soon as possible and should more descriptively outline current warehouse operations. Policies and procedures serve both as a benchmark to measure individuals' performance and as an instruction manual in the event employees' change.

Management Response:

Operations Management is working on revising the Policies and Procedures, no later than June 30, 2010.

EXIT CONFERENCE

An exit conference was held on June 8, 2010 in the Office of Budget & Performance Improvement. Participants included Jorge Cano (Administration and Business Officer), Michael Alvarez (Infrastructure Division Director), James Sutter (Internal Auditor) and Mark Coolidge (Senior Auditor). All parties were in agreement as to the contents of this report. Management responses were solicited and included in our report.

JJS:MC:mc

Audit performed by Mark Coolidge (Senior Auditor)

Internal Audit Report
Public Works Warehouse Inventory Audit
June 30, 2010

cc: Jorge Gomez, Assistant City Manager
Fred Beckmann, Public Works Director
Michael Alvarez, Infrastructure Division Director
Patricia Walker, Chief Financial Officer