

CITY AUDITOR'S OFFICE



AUDIT OF PURCHASING AND CONTRACTS DIVISION — CENTRAL STORES

Report No. CAO 0608-0910-08

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TABLE OF CONTENTS

BACKGROUND	1
OBJECTIVES	2
SCOPE AND METHODOLOGY	2
CONCLUSIONS, FINDINGS AND RECOMMENDATIONS.....	2
1. Department Receipt of Supplies	4
2. Incomplete Move Orders	5
3. Surplus Property	6
4. Cycle Count Historical Information	7
5. Cycle Count Tolerance Indicators	8
6. Annual Physical Inventory	9
7. Obsolete and Slow Moving Inventory Monitoring	11
MANAGEMENT RESPONSE	13

**AUDIT OF
PURCHASING AND CONTRACTS DIVISION -
CENTRAL STORES
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BACKGROUND

Central Stores is a section in the Purchasing and Contracts Division (Purchasing) of the Department of Finance and Business Services (Finance). Central Stores is manned by a supervisor and three inventory control clerks.

Central Stores is responsible for the receipt, storage, and delivery of selected supplies used by City of Las Vegas (City) departments. Central Stores currently carries approximately 770 inventory items in their warehouse. The inventory includes items for which price breaks are obtained for large quantity purchases (e.g., batteries), items of a critical nature for City operations (e.g., Fire and Rescue equipment), and items that need close monitoring of usage (e.g., medical supplies).

The following is a summary of some of the primary functions of Central Stores:

Inventory Purchases - Central Stores uses the warehousing module of the Oracle computer system (Oracle). Inventory levels in the Central Stores warehouse are maintained at optimal levels through an automated process using Oracle. On a daily basis, Oracle calculates what inventory purchases are necessary using established minimum and maximum inventory levels and pending department order requests within the system. Central Stores reviews and confirms the purchase requisition from Oracle and forwards it to Purchasing who then processes the purchase order.

Department Supply Orders - Department representatives order items from Central Stores using what is known as the move order process in Oracle. After the order has been authorized by the department representative, Move Order Pickup Slips are generated from Oracle and Central Stores staff members fill these orders and provide the supplies to the respective department.

Inventory Controls - Central Stores staff members monitor the accuracy of the inventory records through daily cycle counts and an annual physical inventory each June.

Surplus Property - Central Stores also oversees the disposition of City surplus property by picking up surplus items from City departments and submitting them to an auction company.

OBJECTIVES

The audit objectives were to:

- Evaluate the adequacy of controls over the receipt of inventory from vendors.
- Evaluate the adequacy of the department ordering process.
- Evaluate the adequacy of the surplus property disposition process.
- Evaluate the adequacy of the physical inventory process.
- Evaluate the adequacy of monitoring obsolete and slow moving inventory.
- Determine whether Oracle warehousing access groups include only current City employees.

SCOPE AND METHODOLOGY

The scope of our audit was limited to fiscal year 2009 transactions. The last date of fieldwork for this audit was October 8, 2009.

The scope of our work on internal control was limited to the controls within the context of the audit objectives and the scope of the audit.

Our audit methodology included:

- Research of applicable guidelines,
- Interviews of City employees,
- Observations of work processes, and
- Analysis and detail testing of available data.

We conducted this performance audit in accordance with generally accepted government auditing standards except for the requirement for an external peer review every three years. 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.

The exception to full compliance is because the City Auditor's Office has not yet undergone an external peer review. However, this exception has no affect on the audit or the assurances provided.

CONCLUSIONS, FINDINGS AND RECOMMENDATIONS

The following conclusions were noted:

Evaluate the adequacy of controls over the receipt of inventory from vendors:

- No issues were noted during detail testing of the receipt of inventory from vendors.

Evaluate the adequacy of the department ordering process:

- Department representatives do not sign documentation confirming that they verified the receipt of their supply orders. (Finding #1)
- Central Stores monitoring procedures failed to detect department orders that were not processed. (Finding #2)

Evaluate the adequacy of the surplus property disposition process:

- We identified inconsistencies with the information recorded on the documents used in the surplus property disposition process. Procedures are not in place to account for surplus property sold at auction. (Finding # 3)

Evaluate the adequacy of the physical inventory process:

- We identified that the cycle count historical information was deleted from Oracle. (Finding # 4)
- We determined that reports used to track the accuracy of inventory records did not include all cycle count variances because of how the tolerance indicators were established in Oracle. (Finding # 5)
- We identified needed improvements to the annual physical inventory process. (Finding # 6)

Evaluate the adequacy of monitoring obsolete and slow moving inventory:

- We identified erroneous information on the Inactive Items Report that impacts the effectiveness in monitoring obsolete and slow moving inventory. (Finding # 7)

Determine whether Oracle warehousing access groups include only current City employees:

- We determined that as of July 15, 2009, the Oracle warehousing access groups only included current City employees.

Further information is contained in the sections below.

1. Department Receipt of Supplies

Criteria

The segregation of key duties and responsibilities in authorizing, processing, recording, and reviewing transactions is a method used to reduce the risk of error or inappropriate actions relating to inventory transactions. Proper segregation of duties includes ensuring that employees independent of the inventory function verify and confirm the delivery of their supplies.

Condition

Central Stores either delivers supply orders to departments or distributes orders to department representatives at the warehouse. Central Stores gives the department a copy of the Move Order Pickup Slip upon transfer of the supplies, however, department representatives do not sign the slip as evidence they verified the receipt of their supplies.

Audit fieldwork procedures included randomly selecting 48 department move orders from fiscal year 2009 and requesting that department representatives confirm that they received their supplies. It was not possible to confirm the delivery of all the supply items listed on the Move Order Pickup Slips, as follows:

- One department representative indicated she did not receive the item listed on the Move Order Pickup Slip.
- One department representative indicated a smaller quantity was received for two items than what was represented on the Move Order Pickup Slip.
- Several department representatives indicated they could not confirm that they received the supplies listed on a particular Move Order Pickup Slip.

Central Store staff members have keys to access fire stations to deliver supplies when fire personnel are out on calls and the facility is locked. The supplies are delivered to a designated location within the facility and may include medications such as lidocaine, narcon, nitrolingual, albuterol, and gulagon.

Cause

- Current policy does not require department representatives to sign for the receipt of their supply deliveries.
- Departments have turnover in staff and different employees are assigned the function of ordering supplies from Central Stores.
- Not all department representatives maintain adequate documentation relating to their supply deliveries.
- Deficient security precautions over delivery of medications.

Effect

- Inadequate documentation supporting the movement of supplies from Central Stores to departments.
- Medications are not adequately secured.

Recommendation

Central Stores management should document and implement procedures that require department representatives sign documentation confirming they have verified the receipt of their supply orders.

2. Incomplete Move Orders

Criteria

Proper oversight of pending supply requests ensure that orders are correctly and timely processed or canceled.

Condition

Department representatives order supplies from Central Stores by processing move orders in the warehousing module of Oracle. A query of pending department orders for fiscal year 2009 was completed. It was determined that four move orders dated March 5, 2009, June 1, 2009, June 9, 2009, and June 19, 2009 had a status of incomplete and had not been processed as of October 1, 2009. Move orders that are not timely processed and closed could impact inventory levels since Oracle includes pending department order amounts when calculating required inventory purchases.

Cause

- Department representatives prepared but did not approve their move orders. Without approval, move orders are not printed or processed by Central Stores.
- Procedures performed by Central Stores failed to timely identify move orders with a status of incomplete.

Effect

- Inventory levels may not be at the optimal level.
- Departments may not timely receive their supply orders.

Recommendation

Central Stores management should implement more timely monitoring procedures and follow-up on incomplete move orders.

3. Surplus Property

Criteria

Management controls over surplus property ensure that property items are adequately secured until taken to auction and that the City is paid for all property sold at auction.

Condition

Central Stores is responsible for the control and disposal of surplus property items. The process is as follows:

- Department representatives complete the Property Disposition forms and notify Central Stores that they have surplus property items.
- Central Stores picks up and secures the property items.
- Central Stores completes an Excel spreadsheet listing the property they pick up.
- Central Stores delivers the property items to the auction location and gives a copy of the Excel spreadsheet to the auction company.
- After the completion of the auction, the auction company forwards a check and itemized listing of the items sold (auction list) to Finance.

A comparison of the documentation for the May 28, 2009, February 28, 2009, and November 17, 2008 auctions was completed. The comparison showed the following inconsistencies:

Comparison of the Property Disposition forms to Central Stores Excel spreadsheets:

- Certain items identified on the Property Disposition forms were missing on the Central Stores Excel spreadsheet.
- No Property Disposition forms were available for certain property items included on the Central Stores Excel spreadsheet.

Comparison of Central Stores Excel Spreadsheets to the auction list:

- Certain items included on the Central Stores Excel spreadsheet were missing on the auction list.

- The auction list did not indicate the number of items sold but rather just “radios” or “TVs”.
- The auction list used generic terms such as “office equipment” or “misc”.
- Certain items identified on the Property Disposition forms that were missing on the Central Stores Excel spreadsheet were also missing on the auction list.

Discussions with City employees involved with the auction process indicated that procedures are not completed to ensure that all property items that are turned in to Central Stores as represented on the Property Disposition forms are included on the their Excel spreadsheet. In addition, when Central Stores delivers property to the auction location, the auction company directs Central Stores where to place the property in their warehouse. Neither Central Stores personnel nor a representative of the auction company confirm what property is dropped off. At the completion of the auction, City personnel do not ensure that property listed on that Central Stores Excel spreadsheet are included on the auction listing and if sold are paid for.

Cause

Lack of adequate oversight of surplus property.

Effect

The City may not be accurately compensated by the auction company for the sale of surplus property.

Recommendation

Central Stores management should further evaluate the surplus property disposition process and implement increased oversight procedures to ensure that the City is being compensated for all property sold at auction.

4. Cycle Count Historical Information

Criteria

Properly retained historical data allows for research of past transactions and the evaluation of the effectiveness of an organization.

Condition

Daily counts of randomly selected inventory items are completed to evaluate the accuracy of the Central Stores inventory records. The Cycle Count Hit/Miss Analysis report

summarizes the daily results. Audit procedures included requesting randomly selected Cycle Count Hit/Miss Analysis reports from fiscal year 2009 to be used for fieldwork procedures. Historical Cycle Count Hit/Miss Analysis reports could not be retrieved. It was determined that the cycle count history was inadvertently deleted by the Central Stores supervisor. Attempts to reinstate the historical data were unsuccessful.

The Purchasing Initiative Officer represented that access to the purge cycle count function has been eliminated and it will not longer be possible to delete historical cycle count data.

Cause

The Central Stores supervisor was given access to an Oracle function that allowed him to purge historical cycle count data.

Effect

Historical cycle count information can no longer be retrieved from Oracle.

Recommendation

Purchasing and Contracts management should complete an analysis of all Oracle warehousing access functions to determine who has the ability to delete historical data. Oracle system access functions that enable staff to delete historical information should be disabled.

5. Cycle Count Tolerance Indicators

Criteria

Useful inventory reports identify all differences between actual quantities on hand versus quantities indicated in the computer records.

Condition

Central Stores performs daily counts of randomly selected inventory items and compares them to Oracle inventory amounts to maintain the accuracy of their inventory records. These variances are documented in a report called the Cycle Count Hit/Miss Analysis. Oracle enables users to decide whether to include or exclude variances in this report by establishing the cycle count tolerance indicators from zero percent to one hundred percent. Variances are included the report when the indicator is set to zero percent and excluded when the indicator is set to one hundred percent.

A review of the cycle count tolerance indicators showed that the positive tolerance indicator was set to zero percent and the negative tolerance indicator was set to 100 percent.

Cause

The cycle count tolerance indicators in Oracle were incorrectly established.

Effect

When tolerance indicators are incorrectly established certain variances are not identified on the Cycle Count Hit/Miss Analysis report. Excluding variances causes inaccurate reporting of the results of the inventory accuracy testing.

Recommendation

Purchasing and Contracts management should evaluate the variance tolerance indicator process to ensure that all variances are included in the daily cycle count results as indicated in the Cycle Count Hit/Miss Analysis report.

6. Annual Physical Inventory

Criteria

Annual physical inventories when properly completed provide for confirmation of the accuracy of fiscal year end inventory totals.

Condition

Central Stores performed their annual physical inventory of the warehouse on June 23 2009. Internal Audit performed an observation of the physical inventory and observed the following procedural inefficiencies:

- Although department representatives were notified by e-mail on June 1, 2009 that Central Stores would be closed on June 23, 2009 for the annual physical inventory, a follow-up e-mail reminder was not sent. As a result, during the physical inventory, Central Stores staff members were sidetracked by department representatives who had questions and requests.
- The count team members recorded the physical counts of inventory on the Physical Inventory Tag Listing. This listing did not include the unit of measure of inventory items. Count team members not familiar with the inventory items needed to determine unit of measures for their counts. Two of

the initial inventory variances were due to an incorrect unit of measure being used for the physical count.

- Central Stores did not complete procedures to ensure that all department orders had been processed in Oracle prior to the physical inventory count. Two of the initial inventory variances were due to the department receiving their supply orders without the move orders being processed in Oracle.
- Central Stores prints out the Physical Inventory Tag Listing and uses it to document the actual count for each inventory item. Each inventory item is assigned a physical location in the warehouse that is cross referenced to the inventory item in Oracle. The Physical Inventory Tag Listing excludes inventory items that have zero balances in Oracle. At the completion of the physical inventory, Central Stores staff walked through the warehouse looking for inventory locations that had not been tagged. Their procedures did not include confirming that the Oracle inventory items with zero balances had no actual counts and the warehouse locations are still current.
- A financial analyst performs independent test counts of randomly selected inventory items and compares his results to the counts written on the Physical Inventory Tag Listing. The Physical Inventory Tag Listing inventory counts are actual counts which have not yet been verified against Oracle figures.

Cause

Inadequate documented inventory procedures.

Effect

Potential for inaccuracies in inventory item counts.

Recommendation

Central Stores management should document and implement procedures to improve the effectiveness of the annual physical inventory as follows:

- E-mail department users the day before the physical inventory and remind them that the warehouse will be closed and that Central Stores staff members will not be available to process orders or answer questions.
- Modify the Physical Inventory Tag Listing to include a column for unit of measurement to ensure accurate counts.
- Confirm that all department deliveries are processed as move orders and included in the Oracle inventory balances prior to the physical inventory.
- Confirm that inventory items in Oracle that have zero balances do not have actual counts and the identified warehouse locations are still current.
- Ensure that the financial analyst receives verified inventory amounts.

7. Obsolete and Slow Moving Inventory Monitoring

Criteria

Properly implemented warehouse inventory monitoring procedures help ensure that obsolete and slow moving inventory items are removed from inventory and are no longer available for department ordering.

Condition

The Inactive Items Report is used by Central Stores to evaluate whether inventory items are obsolete or slow moving. Audit fieldwork procedures included reviewing the June 30, 2009 Inactive Items Report. The report included 11 pages and 179 specific inventory items. The review showed that the report includes erroneous information, as follows:

- Nine inventory items were categorized as “Obsolete” with no quantity on hand. The vendor has discontinued these items and they are no longer available for purchase.
- Forty-three inventory items were categorized as “Inactive” with no quantity on hand. The City no longer uses these items and they are no longer available for department ordering.
- Fifty inventory items were categorized as “Active” with a last transaction date of November 5, 2007 with no quantity on hand.
- Two inventory items were categorized as “Active” with no quantity on hand. These items are listed with last transaction dates of July 9, 2005 and March 15, 2007, respectively. A review of the transaction histories showed that the inventory items are assigned different warehouse locations and continue to be ordered by and given to departments.
- One inventory item was categorized as “Active” with no quantity on hand with a last transaction date of September 16, 2008. A review of the transaction history showed that the item is still assigned to this warehouse location and continues to be ordered by and given to departments.
- The above inventory items represent 105 of 179 or 59 percent of the inventory items included on the June 30, 2009 Inactive Items Report.

As a result of audit fieldwork procedures, the status of four inventory items were changed from “Active” to “Inactive” and two inventory items were identified for research to determine whether they should continue to be carried and categorized as “Active”.

Cause

- Ineffective Inactive Items Report.
- The Inactive Items Report is not being adequately reviewed for obsolete and slow moving inventory items.

Effect

- Additional time is required to research whether inventory items should continue to be stocked and made available for department ordering.
- Inventory items that are incorrectly categorized with an “Active” status remain available for department ordering and could be selected by Oracle for the daily cycle count.

Recommendation

Central Stores management should evaluate and identify better information/reports that would improve the effectiveness of the review of obsolete and slow moving inventory items.

MANAGEMENT RESPONSE

1. Department Receipt of Supplies

Recommendation

Central Stores management should document and implement procedures that require department representatives sign documentation confirming they have verified the receipt of their supply orders.

Management Plan of Action

Central Stores implemented a process of requiring department representatives to confirm receipts of supplies received in the City Hall Tower and for picked-up items from Central Stores and also with the cooperation of Chief Gammon, Chief Washington and Chief Miramontes has implemented a process for signing for receipt of deliveries at Fire Stations and other Fire locations, including having the Captains fax the receipt if the delivery is made when no Fire personnel is present at the time of delivery. These changes were implemented on November 3.

Estimated Date of Completion

Completed on November 3, 2009

2. Incomplete Move Orders

Recommendation

Central Stores management should implement more timely monitoring procedures and follow-up on incomplete move orders.

Management Plan of Action

Central Stores management will request the IT Department create an Oracle report to enable an efficient method of reporting incomplete move orders. In the meantime, the Central Stores Supervisor will run a weekly query to identify incomplete move orders and ensure follow-up action is made to the appropriate move-order initiator to finalize the transaction.

Estimated Date of Completion

Weekly queries were initiated effective November 2, 2009.

3. Surplus Property

Recommendation

Central Stores management should further evaluate the surplus property disposition process and implement increased oversight procedures to ensure that the City is being compensated for all property sold at auction.

Management Plan of Action

P&C Management began reviewing an alternative surplus disposition process prior to this audit which would implement the use of an on-line auction similar to e-Bay rather than the current use of an auctioneer. The use of the on-line process would eliminate the physical transport and change of custody of material with the auctioneer and enable on-line tracking of surplus material by identification number, tracking of sales, and records retention. Based on inquiries made to date it appears the on-line auction solution may increase proceeds from surplus auctions, which will be most beneficial to vehicle sales coordinated by Field Operations, but also helpful to Central Stores whose FY09 surplus proceeds were minimal at \$4764. This also appears to be a better option since our the current auctioneer indicates he does not have the resources to track and report the receipt and disposition/sales of the surplus material in the manner recommended in this audit report.

Estimated Date of Completion

March 2010

4. Cycle Count Historical Information

Recommendation

Purchasing and Contracts management should complete an analysis of all Oracle warehousing access functions to determine who has the ability to delete historical data. Oracle system access functions that enable staff to delete historical information should be disabled.

Management Plan of Action

The "Purge" option has been eliminated from the Central Stores Responsibility in Oracle

Estimated Date of Completion

November 3, 2009

5. Cycle Count Tolerance Indicators

Recommendation

Purchasing and Contracts management should evaluate the variance tolerance indicator process to ensure that all variances are included in the daily cycle count results as indicated in the Cycle Count Hit/Miss Analysis report.

Management Plan of Action

The tolerance setting was corrected.

Estimated Date of Completion

November 3, 2009

6. Annual Physical Inventory

Recommendation

Central Stores management should document and implement procedures to improve the effectiveness of the annual physical inventory as follows:

- E-mail department users the day before the physical inventory and remind them that the warehouse will be closed and that Central Stores staff members will not be available to process orders or answer questions.
- Modify the Physical Inventory Tag Listing to include a column for unit of measurement to ensure accurate counts.
- Confirm that all department deliveries are processed as move orders and included in the Oracle inventory balances prior to the physical inventory.
- Confirm that inventory items in Oracle that have zero balances do not have actual counts and the identified warehouse locations are still current.
- Ensure that the financial analyst receives verified inventory amounts.

Management Plan of Action

- 1) P&C Management will ensure that multiple notices of Central Stores closure for physical inventory will be sent prior to department users.
- 2) P&C Management will request IT modify the Physical Inventory Tag Listing to include a column for UOM
- 3) Central Stores Supervisor will ensure final processing of all move orders are processed to ensure Oracle inventory balances prior to the physical inventory

Audit of Purchasing and Contracts Division -
Central Stores
CAO 0608-0910-08
January 28, 2010

- 4) Since Oracle does not report on physical locations with a quantity of zero, Central Stores staff will continue to perform physical checks of locations not listed on the physical inventory report to verify no inventory is located in that location.
- 5) The Financial Analysis will be provided as requested for audit purposes.

Estimated Date of Completion

June 2010

7. Obsolete and Slow Moving Inventory Monitoring

Recommendation

Central Stores management should evaluate and identify better information/reports that would improve the effectiveness of the review of obsolete and slow moving inventory items.

Management Plan of Action

P&C Management will request that IT create a more effective Oracle report for identifying obsolete and slow moving inventory. In the meantime the last page of the current report is utilized to identify these items and will be reviewed at least monthly.

Estimated Date of Completion

Bi-monthly review was implemented November 3, 2009