Audit #12-01:

Fiscal Year-End 2011 Citywide Inventory

Executive Summary Report

Office of the City Auditor and Clerk
Internal Audit

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EXECUTIVE SUMMARY
AUDIT 12-01: FISCAL YEAR-END 2011 CITYWIDE INVENTORY

AUDIT SCOPE

The scope of this audit included a review of departmental inventory activities, including physical inventory counts, compliance with inventory policies and procedures, and physical and information system security regarding City assets for the fiscal year ending September 30, 2011. The time period for the audit was October 1, 2010 - September 30, 2011.

The following table summarizes inventory information by Department or Division:

Department or Location	Inventory Costing Method In Use (Appendix B)	Inventory Count Method	Automated Inventory System In Use?	Ending Inventory Balance as of 9/30/11	Percent of 2011 Inventory Balance Tested by Internal Audit
Municipal Auditorium and Payne Park	Last Invoice	Periodic	No	$863.25	36.0%
Public Utilities-Utility Stores	First-In-First-Out (FIFO)	Perpetual	Yes	$47,864.99	24.63%
Public Works-12th Street Equipment Maintenance and Fuel/Oil	First-In-First-Out (FIFO)	Perpetual	Yes	$207,590.20	19.24%
Bobby Jones Golf Club Pro Shop	Weighted Average	Perpetual	Yes	$47,829.61	41.8%
Van Wezel Performing Arts Hall	Last Invoice	Periodic	No	$1,616.19[1]	89.5%
Sarasota Police Department	Last Invoice	Perpetual	Yes	$108,565.49	9.3%
Grand Total Inventory Valuation/ Percent Tested by Internal Audit				**$414,329.73**	**20.2%**

REPORT CONTENT AND LIMITATION OF USE

This executive summary report is limited in detail. In order to obtain the full background on a particular item, please review the Detailed Audit Report prior to drawing conclusions based on the limited information contained in this report.

[1] Actual ending inventory amount was $1,707. Incorrect amount reported by department due to an item count misstatement; the department has expressed plans to correct the discrepancy in its next inventory adjustment.

AUDIT OBJECTIVES AND CONCLUSIONS

This audit focused on determining whether:

Audit Objective	Objective Rating		
1) Departmental inventory procedures were adhered to during counts of inventory;	X		
2) Physical access to inventory was appropriately restricted to safeguard City assets;		X	
3) Access to inventory information systems was appropriately restricted to necessary personnel;		X	
4) Reported inventory included usable or saleable items;	X		
5) Inventory cut-off procedures were adequate to ensure that inventory transactions are reported in the correct fiscal year;	X		
6) Inventory amounts were properly recorded; and		X	
7) Management oversight of the physical inventory count and reconciliation process was adequate to ensure adjustments were properly reviewed and authorized.		X	

*Objective ratings indicate the levels at which the objectives were met; rating definitions are included in A**ppendix A**.*

The results of our review indicate:

- Physical inventory counts were generally performed in compliance with inventory instructions.
- Adequate physical access controls were observed for the majority of the departments with regards to secure, lockable storage areas. *(See Detailed Audit Report for relevant exception.)* With regards to segregation of duties concerns, opportunities exist for all departments to realign job tasks to better reduce theft/ fraud risk.
- Inventory information systems were better restricted to necessary users when compared with prior Audit #10-01; however, there were some concerns specifically regarding the Cartegraph system where the number of users with capabilities to modify records was excessive, considering job responsibilities.
- Reported inventory values appropriately included usable, or saleable, items.
- Departments were in compliance with inventory cut-off procedures.
- Generally, inventory amounts were accurately reported to the Financial Administration Department. *(See Detailed Audit Report for two relevant exceptions.)*
- Management was appropriately present at several of the physical counts; however, evidence of management approvals on final adjustments to inventory values was not noted for most departments.

A complete list of audit recommendations begins on page 4 of this report.

AUDIT 12-01: FISCAL YEAR-END 2011 CITYWIDE INVENTORY
OBSERVATIONS AND RECOMMENDATIONS

Management Action Plans					
Audit Recommendation	**Priority**	**Concur**	**Do not concur**	**Proposed Management Action**	**Action Item Due Date**
1. ***All Departments:*** **Separate inventory duties**, or implement compensating controls for duties, so that: 1) The person who receives/ signs off on inventory is not involved in the purchasing process (particularly, cash disbursement), 2) The person who has custody of the merchandise (Custodian) does not modify the inventory system or reconcile inventory counts to the inventory system/ general ledger, 3) The person who modifies the inventory system (adds/ edits/ deletes items) does not reconcile inventory counts to the inventory system/ general ledger. *(See **Exhibit B** for additional information on Segregation of Duties and Potential Compensating Controls.)* ***Bobby Jones Golf Club, Public Utilities, Public Works, SPD:*** **Modify access rights in departmental inventory systems** so that they are commensurate with job responsibilities and reflect an appropriate segregation of duties (ie, Custodian should not be able to modify records). ***Public Utilities, Public Works:*** **Review user groups in Cartegraph** and explore the possibility of reducing the number of users with the capability to modify/ delete records.	High	X		***Bobby Jones Golf Club:*** Continue to review and implement compensating controls with consideration to staff and system limitations. POS system provider was contacted about modifying access rights, however, with the current version this is not possible but they will consider for future version. ***Public Works:*** Continue to review and implement compensating controls with consideration to staff and system limitations. Staff is currently reviewing the potential of outsourcing the fleet stock room function. Staff has reviewed user group assignments and IT has been contacted to adjust Cartegraph permissions to comply. ***Public Utilities- Utility Stores:*** 1. Accounting Specialist will process invoice after goods are received by the Supervisor of Utility Stores. 2. Supervisor of Utility Stores would modify inventory system but only with an Inventory Adjustment Form which is signed by Department Finance & Administration Manager or Director. Cycle counts will also be instituted. 3. The Department Finance & Administration Manager is now responsible for the reconciliation of inventory counts to the inventory system/general ledger. ***SPD:*** Since audit recommendations in December of 2009, SPD Maintenance Staff (Terry Ruthruff and Paul Shumway) have been receiving stock for the Stockroom. This can be verified independently by Internal Audit by going into FMS (the City's Financial System), searching by SPD Stockroom vendor, Design Lab, for instance, and looking for the receiving initials on the invoice. Police Fiscal Office or Lisa Shay, in City Accounting, could provide those documents. See attached example with "PS" in upper left-hand comer for Paul Shumway, indicating that Paul signed and received the goods, from March of 2010. No modifications have been made to the inventory taken at 9/28/11. A separate employee, with a separate desk and logon from our Custodian (Miguel Gomez) will be posting the incoming invoices. See the Stockroom Inventory Flow-chart (attached). It is a first draft (created by our Custodian, Miguel) to fit the Stockroom's Inventory system to Audit recommendations. Once approved, our MIS Unit will restrict access in the System and the Custodian will be unable to modify inventory. Support Services Manager will be working with a volunteer to perform cycle counts and reconciliations of the inventory monthly, therefore eliminating cumbersome year-end inventory, and at the same time providing better control and a more timely reconciliation process. ***Van Wezel Performing Arts Hall:*** We agree with this statement and are in the process of looking within our department to see who can take on these tasks.	Varies

Management Action Plans					
Audit Recommendation	**Priority**	**Concur**	**Do not concur**	**Proposed Management Action**	**Action Item Due Date**
2. Ensure inventory final report and adjustment is reviewed and approved by someone with higher authority than the Custodian (ie, Department Director).	Medium	X		***Bobby Jones Golf Club:*** Approval by Department Director ***Public Works 12th Street Garage:*** Approval by Department Director ***Public Utilities- Utility Stores:*** Department Director will sign off on inventory final report at Fiscal Year End. ***SPD:*** Support Services Manager will send adjustment to Inventory via memo with Chiefs approval to City Accounting for processing, rather than communicate via email with Accounting Manager, going forward. ***Van Wezel Performing Arts Hall:*** We agree and will make this happen.	9/30/12

APPENDIX A
AUDIT RATING SYSTEM

The audit ratings listed below are based on the auditor's assessment of whether the audit objectives were met.

Red**- A red control rating denotes significant business risk or exposure to the City that requires immediate attention and remediation efforts.** The controls reviewed do not appear to provide reasonable assurance that the control objectives are being met. The City is being exposed to a high level of business risk and exposure. Management is advised to immediately review the design and effectiveness of existing controls or consider implementing new or additional controls.

Yellow**- A yellow control rating denotes opportunities for improvement exist relating to the controls reviewed.** If this state of control is not improved, it could lead to a higher than acceptable level of business risk or exposure to the City. The controls reviewed provide some, but not sufficient assurance that control objectives are being met. Management is advised to review the design and effectiveness of existing controls or consider implementing new or additional controls on a priority basis.

Green- **A green control rating indicates that the controls reviewed at the time of the audit indicated a satisfactory or acceptable state of control, where risk appears to be minimized and appropriately managed.** Controls reviewed appear to provide a high degree of assurance that control objectives are being met. To maintain this rating management is advised to continue to assess the control systems and monitor existing controls for efficiency and effectiveness as business and organizational changes occur.

APPENDIX B
INVENTORY COSTING METHODS USED BY CITY DEPARTMENTS

Last Invoice Cost- All items in inventory are re-priced based on the last price paid. When this method is utilized, if prices have changed over time, the values used to price current inventory may not match the actual costs of the items. This method is not in accordance with generally accepted accounting principles (GAAP).

Weighted Average- Inventory amounts are based on an average of the actual prices paid over time.

First-In-First-Out (FIFO)- Under this method, the cost of goods sold is based on the cost of the first items purchased, while ending inventory amounts are based on the prices of the most recent items purchased (the last items in). This results in inventory being valued close to current replacement cost.