



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: July 24, 2009
AUDIT: Public Works Warehouse Inventory Audit
PERIOD: Fiscal Year Ended September 30, 2008

This report is the result of a regularly scheduled audit of the Public Works Warehouse Inventory as of September 30, 2008, performed in conjunction with the external auditor's annual financial audit of the City.

INTRODUCTION

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

Job order numbers were created to track the cost of labor, materials, and equipment used in projects performed by the Public Works Department; to allow the Department to know the cost of the projects; and to recover the cost of repair or replacement of City 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 show disbursement at no charge to the employee. These items cannot be charged to a specific job and they are monitored by the warehouse personnel to help ensure that 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 ordering of water meters and a fire line for Ric-Man International, Inc. for installation at the Fontainebleau located at 4441 Collins Avenue.

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 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

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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 copy is maintained internally by the warehouse and filed by the associated number to ensure that all are accounted for. The yellow copy is sent to the operations supervisors (Water, Sewer, etc.) typically at week end and the final (pink) copy is given to the employee receiving the inventory. The operations supervisors are to periodically match the yellow and pink copies to ensure agreement and 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 of goods, deliveries, issuance and payments. They all have the ability to receive and enter inventory in the Cityworks System implemented in April 1, 2006. However, any changes or additions/deletions to the inventory 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 locations on the property also protected by cameras include the following:

- Yard 1, a secure fenced area with a covered roof, is 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 is another secure fenced area located further south of yard 1 by the water tanks and bordering Miami Beach Senior High School. The items stored in this area consist primarily of light poles, hydrants, offsets, and caps.
- All inventory stored on the golf course in years past has been removed except for some meter boxes. Plans are for the meter boxes to be moved to the 75 street yard and for this area to be returned to its natural condition as a golf course.
- City vehicles, and assorted equipment and inventory are stored in the middle of the yard.

Finally, large slow 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.

\$2,280,024 in funding obtained from the General Obligation Bond Neighborhoods and \$580,976 from the General Obligation Bond Parks was previously allocated in 1997 to the replacement of the current Public Works yard facility. Tentative plans included the renovation of the 20,000 square foot facility, a 5,000 square foot expansion, American Disabilities Act compliance, an access road, environmental remediation, paving, drainage, lighting, parking and a fueling facility for City vehicles.

This project has been delayed for a variety of reasons over the last several years. For example, the reconstruction of the water tanks and pump station, which was completed during the 2005/06 fiscal year, was added to Fire Station No. 2's scope of services. Meanwhile, the project is currently on hold pending the completion of Fire Station No. 2, which is estimated to be finished.

Full physical count of the Public Works Inventory is taken at the end of each fiscal year by the warehouse personnel. Internal Audit conducts test counts to verify the warehouse count numbers. Once the final count is in agreement, the warehouse personnel adjust the inventory count numbers on the CityWorks system and a new value for the inventory at year end is calculated. This inventory

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value is forwarded to the City's Finance Department which prepares a journal entry to adjust to the year end inventory value.

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

9/30/2004	9/30/2005	9/30/2006	9/30/2007	9/30/2008
\$1,953,161	\$1,797,500	\$1,981,523	\$2,194,784	\$2,015,324

This fiscal year's ending inventory of \$2,015,324 was 8.18% lower than the previous year. Internal Audit conducted test counts of one hundred twenty (120) part numbers totaling 3,051 items with a value of \$476,401.94 or 23.64% of the current inventory value.

We commend the Public Works warehouse staff and supporting personnel who overcame the problems associated with the recent relocation of parts from the golf course primarily to newly used storage areas located at 75th Street and Dickens Avenue and 81st Street and Hawthorne Avenue. They were also hindered by 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 \$2,015,324 be used as the September 30, 2008 inventory value. The annual physical inventory of the items was conducted in an effective and timely manner, and the corresponding valuation was deemed reasonable. Finally, invoices selected for review were supported by proper approvals from authorized personnel.

In conducting our inventory counts and reviewing the internal controls surrounding the inventory, we noted shortcomings in the following areas in need of improvement:

- A comparison of the Citworks count with Internal Audit's verified sampled physical counts found differences for 40.83% of the tested items. The root cause could not be easily determined but some contributing factors are included in the findings in this report.
- Cityworks, the inventory system effective 04/01/06, has not been fully implemented to better satisfy the warehouse's operational needs.
- Possible improvements to the camera system were listed 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 entries to inventory areas, and an inoperable front gate to the main facility. 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 are not properly safeguarded from damage by driven vehicles or unauthorized intruders.
- Observations relating to parking city equipment and accounting for all inventory issuance forms were noted to necessitate improvements in controls over safeguards and processing.
- 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 inventory is sufficiently counted, valued and recorded; properly safeguarded from theft and breakage; and that tested purchase invoices are appropriately maintained, approved and recorded.

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 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 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.
5. Confirm that unit costs on sampled purchase invoices are accurately reflected on inventory reports and that all sampled invoices are properly approved and authorized.

FINDINGS, RECOMMENDATIONS AND MANAGEMENT RESPONSES

1. Finding – Physical Count Comparison
Internal Audit conducted test counts of one hundred twenty (120) part numbers totaling 3,051 items with a value of \$476,401.94 or 23.64% 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 count was then used as the basis for the inventory valuation.

Another test conducted was the comparison of these verified counts of sampled items with the amounts listed in Cityworks initial 09/15/08 recorded count. It was subsequently discovered that there was a count difference for 40.83% (49/120) of the items tested although sometimes the Cityworks count was higher and other times the physical count was higher. A net overage of \$21,978.34 or 4.61% 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 taken by Public Works' staff, with the adjustments for Internal Audit counts, to help ensure that valuation is reasonably correct as of 09/30/08.

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The reasons for the difference (shrinkage, sloppy recordkeeping, incorrect part numbers, access to yard locations, etc.) between the verified count and the Cityworks count could not be determined. However, the following facts noted during testing would have contributed to the difference:

- Pre-numbered sequential inventory issuance (MX-1) forms are used to record all relevant information when inventory is issued by the warehouse. Proper procedure requires warehouse personnel maintain the white copy of these forms and file them accordingly. Four of the fifty-five forms sampled or 7.27% (numbered 78344, 78349, 78357, and 78358) were not provided upon request and were presumed missing. Consequently, Internal Audit cannot confirm that the inventory disbursements listed on these MX-1 forms were correctly entered into Cityworks.
- Cityworks reported the existence of seventy-five units of YCON-08.3 at a price of \$62.17 each. It was subsequently discovered during testing that \$62.17 represented the price by the box rather than the each. Additionally, it was determined that forty-one of the seventy-five found parts were mislabeled and were actually part number YCON-08.0.

Recommendation(s):

The compensating control of performing full scale physical inventory counts should continue to be performed as the present difference of 40.83% is material. Steps should be taken to reduce this percentage to a more reasonable figure (less than 10%) which should at a minimum include the following:

- All pre-numbered MX-1 forms (including voids) should be accounted for as missing forms could mean that issued inventory was not deducted from the Cityworks.
- Although the volume of parts received and disbursed is large, greater care should be taken when parts are received to ensure that they are labeled and priced correctly.

Management Response:

Management is working with Warehouse staff to improve future inventories along with implementing a warehouse materials, including a parts bar code part system that works hand-in-hand with Cityworks. Improvements have been made since the completion of this audit as stored inventory parts are now better secured with limited keys to restricted areas granted and with all cameras now functioning properly.

2. Finding – Cityworks Inventory System

The current Public Works warehouse inventory computer system called Cityworks was implemented April 1, 2006. Although this system contains many improvements over the previous PWK system, the following shortcomings were still noted to exist at fiscal year end:

- a. Inventory items continue to be valued using a weighted average costing approach that includes all purchases made of the item since 1984. Technology advancements and component materials' price changes have caused some parts' most recent purchase prices to vary both negatively and positively from the recorded weighted average prices. As a result, fiscal year end inventory valuations continue to be impacted. Public Works Administration is currently researching the materiality of the conversion to FIFO (First In First Out) method of inventory valuation and plans to implement this new method pending the approval of the Finance Department.

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- b. Maximum and minimum quantities have not yet been recorded in Cityworks to facilitate ordering. In their absence, ordering continues to be done manually which could lead to inadvertent stockouts or overstocks thereby negatively affecting carrying costs and inventory turns.

Recommendation(s):

Plans to convert from the weighted average inventory valuation method to first-in-first-out should be continued in an effort to more accurately reflect the actual value of the inventory currently in stock. Among other improvements, the full adoption of Cityworks should help reduce labor costs and the warehouse's downtime in future fiscal year inventories

Management Response:

The implementation of a warehouse materials / parts bar code part system that works hand-in-hand with Cityworks, should be in-place during the first quarter of 2010.

3. Finding – Security Cameras

The Public Works facility located at 451 Dade Boulevard is protected by twenty-five digital cameras to record activities. The system hardware, computer monitors and digital video recorder with compact discs are safeguarded in the Control Room, which is continually staffed. Nine 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 an 11/20/08 site visit found the following shortcomings:

- Two cameras; Bank 1, Cameras 3 and 8; were not functioning as they showed a blank screen.
- Two cameras; Bank 2, Cameras 5 and 9; had dirty lens thereby making it difficult to determine what was being recorded.
- Bank 2, Camera 1 covering the entry road positioned between Fire Station #2 and Miami Beach Senior High School is partially blocked by overhanging tree limbs.
- None of the cameras oscillated to cover a larger area.
- A black screen is typically recorded during the nighttime hours due to the absence of lighting towers and/or infrared lighting.
- Camera positions should be adjusted so as to better protect Public Works inventory. For example, cameras were not positioned inside the electrical room, warehouse or yard 1, areas in which most of the inventory is stored.
- The outside of the security cameras were not clearly labeled to facilitate identifying which were not functioning properly, where they were positioned, etc.

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. Areas surrounding the cameras should be kept clear of trees and other obstacles to increase sight lines. Finally, labeling the outside of the cameras in accordance with the viewing monitors should help make them easier to locate.

Management Response:

To date, stored inventory parts are better secured with limited keys to restricted areas and all

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cameras in working condition. Superintendents and Control Operations Supervisors are monitoring weekly (by inspection) to help ensure that all cameras are functioning properly.

4. Finding – *Security Weaknesses*

Internal Audit identified the following security weaknesses during testing that could increase the possibility that City assets may be misappropriated, vandalized, 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 personnel have the master key and therefore can easily and unsupervised access the facilities and their contents. These locations do not have security cameras and/or security personnel.
- b. A Municipal Service Worker II on long term light duty is permitted to store his small City vehicle inside the secure yard 1 located at 451 Dade Boulevard during non-working hours. He was observed alone and unsupervised inside yard 1 on several occasions sitting in his vehicle.
- c. Although the warehouse entrances are properly secured with working card readers and locks, Public Works personnel that do not work in the warehouse were allowed unsupervised entry inside. Some entered for job related reasons, while others entered for personal reasons. When left alone inside the warehouse, the possibility exists that these individuals could misappropriate inventory.
- d. The front gate was made inoperable due to the renovations of Fire Station #2 and has yet to be repaired to help prevent access by unauthorized individuals, especially during non-peak working hours.
- e. The parts stored on the golf course were not as protected as those inside the warehouse or yards 1 and 2. Similarly, Public Works staff may have accessed these parts for work related usage but did not notify warehouse personnel or submit a MX-1 form. These parts were moved during the fiscal year to more secure locations.

Recommendation(s):

The implementation of the following recommendations can help ensure the safety of the inventory 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 & c. Access to the inventory should be restricted only to those needed. If inside a secure facility, visitors should not be left alone and should be escorted outside when their business is finished.
- d. The front gate should be made functional as soon as possible to better protect the City's assets.
- e. Stored inventory should be adequately safeguarded (cameras, restricted access,

etc.) to help prevent misappropriation or usage without the submittal of the corresponding MX-1 forms.

Management Response:

Items a thru c have been resolved. Meanwhile, item d will be resolved when Fire Station # 2 construction is completed as there is a currently high amount of vehicular traffic in and out. We are presently working on obtaining quotes from fence companies for a security rolling gate for closure at nights. Improvements have been made since the completion of this audit as stored inventory parts are now better secured with limited keys to restricted areas granted and with all cameras now functioning properly.

5. Finding – Water Tanks Safety

The Public Works yard houses two large water tanks located directly south of the warehouse and yard 1. In previous inventory audits, we observed both City and personal vehicles parking dangerously close to the tanks and were even told of a minor accident. Public Works management took proper steps to reduce the risk by adding parking stops and by issuing a 10/05/07 Parking Policy memo to all employees.

Furthermore, the 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 trees, etc. can make unauthorized access easier.

Recommendation(s):

Public Works 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 fence deficiencies.

Management Response:

Parking spaces at the operations yard continues to be a challenge. As soon as Fire Station # 2 construction is completed, parking will improve. Also, relocating construction and debris material from the center of the yard to the southeastern corner of the facility will also help as a capital project request has been made for FY 2009/10. To date, the fence has been repaired and is an on-going challenge year after year with teenagers or homeless breaking the chain link fence. Cameras will be in-place by December 2009.

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:

Individual performance is determined by the Job Descriptions of warehouse employees,

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such as Warehouse Supervisor and Storekeepers I and II. Any classification lower than the Storekeeper position (Municipal Service Worker) is given work assignments by Storekeepers or Warehouse Supervisor.

EXIT CONFERENCE

An exit conference was held on July 2, 2009 in the Public Works Department. Participants included Michael Alvarez (Assistant Public Works Director), Martha Torres (Warehouse Supervisor), Elie Fakie, Water and Sewer Superintendent, 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)

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cc: Tim Hemstreet, Assistant City Manager
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