

I. EXECUTIVE SUMMARY

The Office of Public Integrity (OPI) observed the annual physical inventory of the Department of Environmental Services, Bureau of Operations and Parks, Equipment Services Division auto parts stockrooms on December 1, 2007. The results of the inventory indicate that the variance rate for the main auto parts has increased slightly since the last inventory date and the variance rate for the new tire inventory is the same as that noted in the last inventory.

- ◆ The Office of Public Integrity noted seven variances in our sample selection for main auto parts, indicative of differences between the physical counts and the quantities recorded in the perpetual records. Additionally, we did not note any variances in the new tire inventory items.
- ◆ This inventory included six additional storerooms containing items not inventoried in prior years. We noted variances in all of these areas.
- ◆ OPI noted 28 out of 4,858 stockroom inventory items in which stockroom personnel did not accurately update the perpetual inventory system with the quantities counted during the physical inventory count. This represents an error rate of .6%. The effect of this condition is to negate the benefit of taking a physical inventory.

II. BACKGROUND, OBJECTIVES AND SCOPE

A. Assignment

The Office of Public Integrity routinely observes and participates in annual physical inventories of various City stockrooms. The Equipment Services Division of the Department of Environmental Services conducted its annual physical inventory on December 1, 2007. The Office of Public Integrity participated in these counts at the request of Equipment Services.

B. Background

Equipment Services maintains and repairs City motor vehicles, except Fire Department vehicles. Equipment Services stores and manages an inventory of supplies and materials necessary to perform these functions. As of

December 1, 2007, the main auto parts inventory comprised 4,193 line items valued at approximately \$513,957 and the new tire room inventory comprised 96 line items valued at approximately \$39,040. In addition to these inventories there are six smaller storerooms, including two service trucks, with a combined 569 items valued at \$60,748. We included these storerooms in this inventory count. Stockroom personnel use an automated inventory system that assists in controlling quantities and providing various management information. Equipment Services installed this system in August 2002. A perpetual inventory record is an essential feature of this system.

Objective And Scope

The objectives of this review were to assure an accurate and complete physical inventory count and to assess the effectiveness of inventory controls.

Management is responsible for establishing and maintaining a system of internal accounting and administrative control. Fulfilling this responsibility requires estimates and judgments by management to assess the expected benefits and related costs of control procedures. The objectives of a system are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of accurate, informative reports that are fairly stated.

Because of inherent limitations in any system of internal accounting and administrative control, errors or irregularities may nevertheless occur and not be detected. Also, projection of any system evaluation to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the degree of compliance with procedures may deteriorate.

The recommendations presented in this report include the more significant areas of potential improvement that came to our attention during the course of the examination, but do not include all possible improvements that a more extensive review might develop.

The results of this physical inventory indicate that the variance rate for main auto parts has slightly increased since the last inventory date and the variance rate for new tires is the same as that of the last physical inventory that Equipment Services conducted on June 24, 2006. Overall, inventory control of these two areas appears adequate. However, this inventory included six additional storerooms where weaknesses exist in the maintenance of the perpetual inventory. A variance was noted in each of the six storerooms.

A. Variance Analysis - Auto Parts

OPI selected a statistical sample of items included in the stockroom inventory. The sample selection assures proper representation throughout the entire population of inventory items and accurately projects the results against the entire inventory. The range of unit costs included in the sample extends from \$.01 to \$667.84. OPI compared the actual count of each of these selected items to perpetual records and noted any variances.

Of the 273 inventory items tested in the sample, we noted seven variances. This represents a sample error rate of 3%. The graph below presents historical error rates as a reference.

**Equipment Services Division
Main Auto Parts Inventory
Sample Error Rate Percentages**

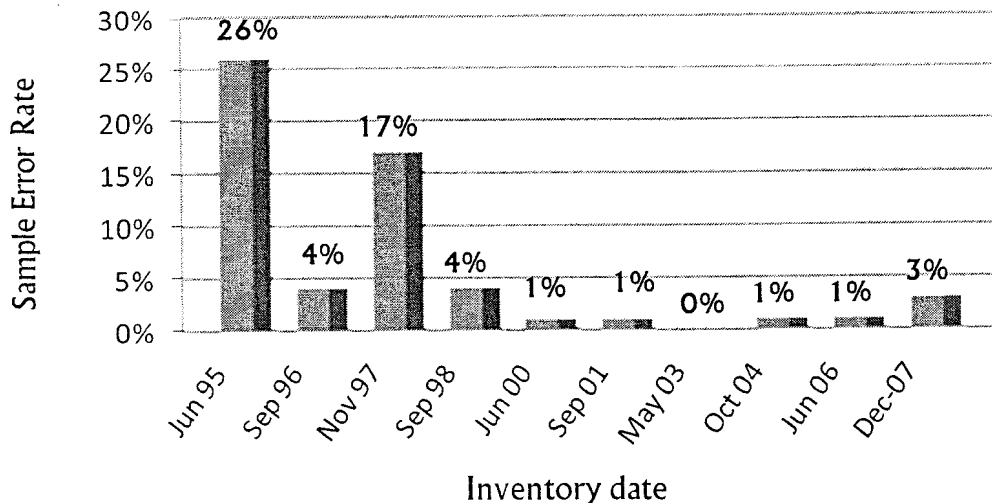


Table I (attached) presents the variance analysis of the statistical sample selection for those items in which a variance exists. It demonstrates individual variances between actual physical counts and quantities recorded in the perpetual records, and presents positive and negative variances separately. Additionally, the table includes the net variance at the end of the table.

When OPI extends the sample error rate of 3% to the entire population of 4,193 different stock items, the projection indicates that the actual number of errors in the population is in the range of 50 to 264 item types. The sample error rate of 3% is higher than the prior error rate of 1% in the June 2006 inventory and the 1% variance noted in the October 2004 physical inventory.

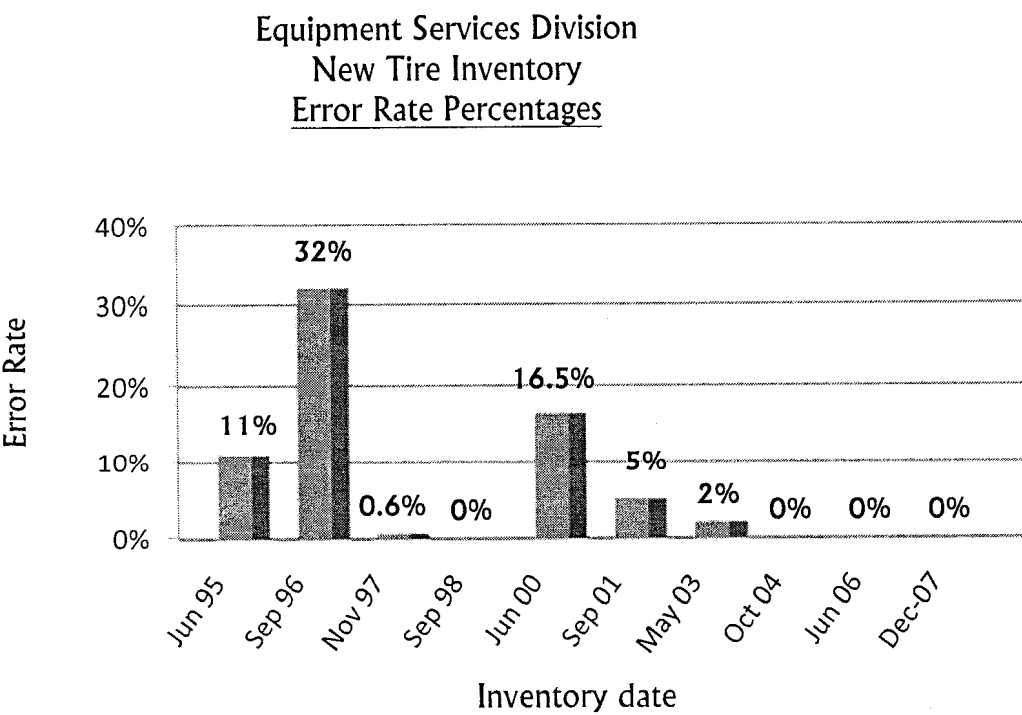
◆ **RECOMMENDATION**

Equipment Services should identify the causes of the increased variance rate and should take corrective action to reduce it. Additionally, Equipment Services should conduct cycle counts.

B. Variance Analysis - Tires

The Office of Public Integrity counted and compared all new tire quantities to quantities recorded in the perpetual records. This is in contrast to the statistical sample taken of auto parts.

Of the 96 inventory line items located in the new tire stockroom, we did not note any variances. This represents an error rate of 0%. The following graph presents historical error rates as a reference.



The error rate of 0% is the same as that noted in both the 2004 and 2006 inventories.

◆ RECOMMENDATION

Equipment Services should continue to make inventory control a priority.

C. Additional Storeroom Variances

A key element in any inventory control system is the proper maintenance of perpetual inventory records. Equipment Services maintains an automated perpetual system that provides on-going recordkeeping for the stockroom inventory. Equipment Services utilizes various locations within their facility to store inventory. They separate these locations on the automated perpetual system as different storerooms. Using this method, they can individually control each storeroom.

In addition to the main storeroom and new tire storeroom, Equipment Services inventoried all other storerooms individually separated on the perpetual inventory system. These include used tires, the “other” (miscellaneous) tire parts storeroom, the Rochester Police Department vehicle parts storeroom, the “other” (obsolete) auto parts, and two service trucks. We noted weaknesses in inventory control over these additional inventory storerooms.

Following is a table of these storerooms and the variances noted. The other tire parts storeroom and the two service trucks contain primarily low cost, consumable items. Therefore, we selected for testing only those line items with a unit cost of \$5.00 or more.

Department of Environmental Services
Equipment Services
Additional Inventory by Location

<u>Location</u>	<u>Storeroom</u>	<u>Total Line Items</u>	<u>Total Value</u>	<u>No. of Items Tested</u>	<u>% of Items Tested</u>	<u>No. of Variances</u>	<u>Error Rate</u>
103	Other Auto Parts Storeroom	161	\$11,472.60	161	100%	7	4%
106	Used Tire Storeroom	48	2,697.71	48	100%	12	25%
108	Other Tire Parts Storeroom	112	4,195.04	60	54%	29	48%
109	RPD Auto Parts Storeroom	49	41,134.55	49	100%	20	41%
ST1	Service Truck	106	825.29	33	31%	11	33%
SVT	Service Truck	<u>93</u>	<u>423.22</u>	<u>12</u>	13%	<u>7</u>	58%
	Total	<u>569</u>	<u>\$60,748.41</u>	<u>363</u>	64%	<u>86</u>	24%

These error rates indicate weaknesses in the perpetual inventory maintenance of the additional storerooms. Differences between physical (actual counts) and perpetual records are important indicators of the operational efficiency of the inventory control system. Analysis of significant differences between the records may indicate weaknesses in data processing, ineffective security measures, theft, posting errors, inadequate physical verification procedures or any combination of these. Management should be interested in explanations of the differences as a basis for taking corrective action in controlling inventories.

Especially noteworthy is the excessive variance of 41% for the RPD auto parts storeroom. Equipment Services personnel stated that police personnel have unrestricted access to the parts stored in this inventory location. This weakness in inventory control compromises the integrity of the inventory. Only authorized Equipment Services stockroom personnel should have access to the inventory.

When analyzing the causes of inventory variances, it is important to analyze significant line item differences as well as the total variance for the entire inventory. Additionally, management should analyze positive and negative line item variances separately, rather than combining them to consider a net figure. This is because events causing negative variances may be different from those causing positive variances.

Table II, Table III and Table IV (attached) present the variance analysis of those items in which a variance exists for the RPD auto parts, the other auto parts and the used tire parts storeroom locations on the perpetual system. Each demonstrates individual variances between actual physical counts and quantities recorded in the perpetual records, and presents positive and negative variances separately. Additionally, the tables include the net variance.

◆ RECOMMENDATION

Equipment Services management should determine the causes of the variances and make inventory control a priority for these additional inventory storerooms.

RPD personnel should not have access to the inventory storeroom locations and should consult with authorized Equipment Services personnel for all stockroom requests.

◆ Inaccurate Updates To The Perpetual Inventory System

Equipment Services personnel record quantities counted on preprinted count sheets, and clerical staff update the perpetual records by transferring this information to the automated inventory system. As a result, the quantities recorded on the count sheets should agree to the post-inventory perpetual records generated by the automated inventory system.

The Office of Public Integrity noted 28 items out of 4,858 stockroom inventory line items in which the quantities recorded on the count sheets do not agree to the quantities recorded on the post-inventory perpetual records. This may have occurred because personnel did not clearly indicate on the count sheets the updates that clerical staff needed to make on the automated system. These discrepancies represent an error rate of .6%. Consequently,

the perpetual inventory records do not always reflect accurate quantities counted during the physical inventory.

The effect of this condition is to negate the benefit of taking a physical inventory and to perpetuate inaccurate records within the automated system, a key management tool.

◆ RECOMMENDATION

Equipment Services personnel should accurately update all counted inventory items on the automated perpetual inventory system. Personnel should correct current errors on the perpetual inventory records so that the errors do not carry over into future periods.

IV. DEPARTMENTAL RESPONSE

The response of the Department of Environmental Services follows.

TABLE I: Department of Environmental Services
Equipment Services Division
Stock Room Inventory – December 1, 2007
Variance Analysis of Main Auto Parts – Location 100
Schedule of Inventory Variances Only

[illegible]

TABLE II: Department of Environmental Services
Equipment Services Division
Stock Room Inventory – December 1, 2007
Variance Analysis of RPD Auto Parts – Location 109
Schedule of Inventory Variances Only

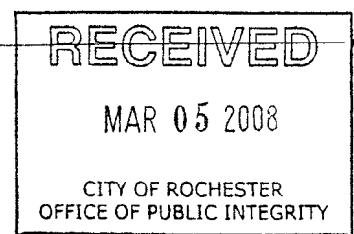
Stock Number	Part Description	Quantity On Hand	Quantity Counted	Item Count Over	Variance Short	Unit Cost	Dollar Variance Over	Variance Short
61600	Antenna Connector	5	35	30	0	0.01	0.30	0.00
CP2591	UHF Male Crimp	8	9	1	0	0.01	0.01	0.00
CPL2591	UHF Antenna Connector	2	1	0	1	0.01	0.00	(0.01)
CHB2EN	Enclosed Cupholder	13	12	0	1	19.50	0.00	(19.50)
IMPO6MT	Mount Kit	13	12	0	1	109.95	0.00	(109.95)
HAT47	Adjustable Hat	13	12	0	1	29.50	0.00	(29.50)
LI900000	Console Kit, w/cup hldr	13	12	0	1	286.85	0.00	(286.85)
PPJHDARM9	Armrest with printer mount	14	12	0	2	247.50	0.00	(495.00)
9203516	Lightbar mounting kit	15	14	0	1	10.87	0.00	(10.87)
LCS850FKIT	Command Center w/ Mic	13	12	0	1	642.45	0.00	(642.45)
RSK242WKIT	Remote Strobe Kit	13	12	0	1	135.00	0.00	(135.00)
5421H	Light bar kit	1	0	0	1	0.01	0.00	(0.01)
82014D1B	Blue Lower Level LED Array	0	10	10	0	54.03	540.30	0.00
TD772	Control Unit	23	25	2	0	0.01	0.02	0.00
Z8572001A	Clear Vision Dome	11	10	0	1	0.01	0.00	(0.01)
FA4CRDG	Alternating Flasher	15	11	0	4	0.01	0.00	(0.04)
Z8572001A01	Red Vision Dome	19	20	1	0	0.01	0.01	0.00
UMNCTR	Hand Microphone Kit	16	15	0	1	0.01	0.00	(0.01)
UNCOR	Microphone	10	11	1	0	0.01	0.01	0.00
D40	Siren Speaker	<u>12</u>	<u>11</u>	<u>0</u>	<u>1</u>	118.00	<u>0.00</u>	<u>(118.00)</u>
		<u>229</u>	<u>256</u>	<u>45</u>	<u>18</u>		<u>\$540.65</u>	<u>(\$1,847.20)</u>
								<u>(\$1,306.55)</u>
	Net Variance							

TABLE III: Department of Environmental Services
Equipment Services Division
Stock Room Inventory – December 1, 2007
Variance Analysis of Other Auto Parts – Location 103
Schedule of Inventory Variances Only

		Booked	Actual					
Stock Number	Part Description	Quantity On Hand	Quantity Counted	<u>Item Count Variance</u>		<u>Unit Cost</u>	<u>Dollar Variance</u>	
				<u>Over</u>	<u>Short</u>		<u>Over</u>	<u>Short</u>
USR7AC	Spark Plug	1	4	3	0	\$ 0.01	\$ 0.03	\$ 0.00
41331904001A	Recoil Assembly	9	5	0	4	13.50	0.00	(54.00)
11291237502	Gromnet	2	1	0	1	2.70	0.00	(2.70)
248840	Wheel Bearing Retaining Ring	11	15	4	0	22.17	88.68	0.00
05IMPALARLID	Trunk Lid	4	2	0	2	25.00	0.00	(50.00)
05IMPALALF	Drivers Front Door	1	2	1	0	50.00	50.00	0.00
05IMPALARF	Passenger Front Door	<u>1</u>	<u>2</u>	<u>1</u>	<u>0</u>	50.00	<u>50.00</u>	<u>0.00</u>
		<u>29</u>	<u>31</u>	<u>9</u>	<u>7</u>		<u>\$188.71</u>	<u>\$ (106.70)</u>
	Net Variance.....							<u>\$ 82.01</u>

TABLE IV: Department of Environmental Services
Equipment Services Division
Stock Room Inventory – December 1, 2007
Variance Analysis of Used Tire Parts – Locations 106
Schedule of Inventory Variances Only

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To: Daniel Markese / Office of Public Integrity

From: Paul Holahan, Commissioner / DES

Date: March 4, 2008

Subject: Response to Equipment Services Stockroom Inventory Audit

The Division of Equipment Services completed its annual inventory audit on December 1, 2007. The last physical audit was conducted in June 2006. The Office of Public Integrity (OPI) observed these inventories.

The results of the Equipment Services stockroom inventory audit are as follows.

- The main auto parts storeroom is comprised of almost 4,200 line items with a value of approximately \$513,957. There was an increase in the variation rate from 1% to 3%.
- The new tire room inventory is comprised of 96 line items with a value of approximately \$39,040. The error rate for this inventory was 0% variance.

The OPI has indicated that the overall inventory control of these two areas appear adequate.

The following storerooms were added to the fleet management system this year, and were audited for the first time.

- The used tire storeroom is comprised of 48 line items with a total value of \$2,697.71. There was an error rate of 25% with 12 variances.
- The tire parts storeroom which is comprised of 112 line items with a value of \$4,195.04 had an error rate of 48% with 29 variances.
- Other auto parts storeroom which is comprised of (obsolete) auto parts. These parts are removed from the physical inventory and placed in a separate storeroom waiting auction. The total line items counted were 161 with a dollar value of \$11,472.60. The number of variances was 7, with an error rate of 4%.
- RPD auto parts storeroom is comprised of 49 line items with a total value of \$41,134.55. These are items purchased by the police department and stored in our stockroom for outfitting new police vehicles. The error rate was 41% with 20 variances.
- There are two service trucks with small inventories. The average value of these inventories is approximately \$625.00. Total line items are about 100 with most of the items low cost consumables. Items tested had a unit cost of \$5.00 or more. The error rate was roughly 45%.

The OPI indicated these variances may indicate a weakness in data processing, ineffective security control measures, posting errors, and inadequate physical verification procedures, or any combination of these.

As recommended by the OPD; Equipment Services will identify causes of variances and possible weaknesses in our procedures. We will implement sound corrective actions to continually improve our operation and make inventory control a priority for the additional storerooms. Some of the corrections are as follows,

- Restrict police personnel who had unrestricted access to the parts stored in the RPD auto parts storeroom. This weakness in inventory control compromised the integrity of the inventory.
- Equipment Services personnel will accurately update ALL counted inventory items on the automated inventory system. Personnel will correct current errors on the perpetual inventory so errors will not carry over into future periods.
- Only Equipment Services personnel will have access to the inventory.

Please keep in mind that the retirement of the Parts and Materials Manager in August has been a huge loss to our operation. We anticipate hiring a new manager to oversee this operation as soon as possible.

We are planning our next physical inventory for June 2008 to ensure our corrective actions are successful. Please contact Mary Gaudioso of my staff should you have questions or comments.

cc: Pete Scott
Lou Guilmette
Mike Quattrone
Mary Gaudioso



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JUN 04 2008

CITY OF ROCHESTER
OFFICE OF PUBLIC INTEGRITY

To: Daniel Markese, Office of Public Integrity

From: Paul Holahan, Commissioner of Environmental Services 

Date: May 29, 2008

Subject: **Results from Inventory Audit – Water & Street Lighting Stockrooms**

The Bureau of Water conducted its physical inventories of both the water materials and street lighting stockrooms on April 26, 2008. The last physical inventory of these stockrooms was performed on September 29, 2007.

I am pleased the results of the physical inventory indicate that the variance rates for the water and street lighting stockrooms both declined. The variance rate for the water stockroom decreased from 8.5% to 3.6%, with the variance for the street lighting stockroom decreasing from 21.0% to 5.7%.

The department will continue to make inventory control a top priority in the management of this bureau.

cc: Robert Morrison
Gary Giudice

