



# CITY OF WINSTON-SALEM FLEET SERVICES INVENTORY CONTROLS REVIEW

For the Current Period Ended October 31, 2022

**Submitted by:**  
Budget and Performance Management Department  
Internal Audit Division  
November 2022

## **Overview of Fleet Services**

The mission of the Fleet Services division (Fleet) is to provide safe, appropriate, and well-maintained vehicles to all City departments at a competitive cost with high-quality customer service. Fleet provides maintenance for more than 1,879 pieces of rolling stock and other equipment for all City departments and helps with acquisition and disposal of said equipment. Fleet work units include the service station, pool vehicles, heavy equipment repair, light equipment repair, auto parts, and preventive maintenance. Fleet is a division of Property and Facilities Management (PFM).

## **Overview of Fleet Inventory Operations**

Fleet maintains parts and supplies within an inventory warehouse for maintenance and repair of City vehicles. The effectiveness and efficiency of the warehouse impacts the operation's costs, productivity, and vehicle downtime. The Fleet Manager position remains vacant; however, the PFM Director serves as the Fleet Manager on top of his other duties. Fleet's inventory warehouse is normally staffed by at least three dedicated inventory parts employees but currently the inventory warehouse is staffed only by the Parts Team Leader (PTL). As of June 30, 2022, the total Fleet warehouse inventory had a value of \$917,081.

Fleet uses Faster, the division's inventory management system, to track parts and supplies inventory for operational decisions and to provide inventory balances for financial reporting. To ensure the accuracy of inventory records, book inventory records are reconciled to actual quantities.

There are two key methods for the physical count of inventory:

- Cycle Count: partial (section) inventory is counted periodically during the year.
- Wall to Wall Physical Count: 100% of inventory when all sections are counted over a period.

Fleet is currently using the cycle count inventory method and is counting a selected section of parts and supplies every month. The last wall to wall physical count was performed in early 2020.

## **Scope of Review Procedures Performed**

On June 30, 2022, a physical observation of the year-end inventory of supplies at Fleet was performed. During Internal Audit's (IA) physical observation, 39 test count exceptions, or 44.32% of the sample selected, were noted; absolute value of the test count exceptions represented \$31,356.66, or 13.76% of total sample value. Consequently, as IA was unable to verify that inventories of supplies at Fleet were reasonably recorded in the detailed inventory records at June 30, 2022, IA determined it was warranted to pursue this review of Fleet's parts inventory controls.

The scope of the review concentrated on evaluating and assessing the effectiveness of Fleet's inventory controls and procedures.

IA's objectives focused on:

- documenting and evaluating the inventory management process and internal controls,
- examining inventory management documentation, and
- making recommendations (if necessary) to improve internal controls.

To accomplish the review's objectives, IA conducted interviews with staff at Fleet, evaluated existing inventory management policies, and examined inventory management documentation.

### **Findings and Recommendations**

*1. Fleet has not implemented policies and procedures for the entire physical count of inventory process.*

Fleet has not implemented policies and procedures for the entire process of a physical count as is recommended by the Government Accounting Office (GAO) best practices. Specifically, Fleet does NOT: a) have criteria for determining how many times each section should be counted annually; b) have criteria for selection of variances to research such as quantity or dollar value; c) perform blind counts which are considered to provide the greatest degree of assurance. It is recommended that Fleet implements an entire process for physically counting inventory to ensure accurate inventory records, reduce cost, and identify the opportunities for improvement through evaluation of inventory count results.

*2. Fleet has not designed sectional counts to ensure complete wall to wall counts are being completed at least annually.*

Fleet does perform monthly cycle counts of inventory; however, Fleet has not performed a complete wall to wall inventory count since early 2020 as is recommended by GAO best practices. It is recommended that Fleet designs a sectional count method by which a portion of the inventory is counted (daily, weekly, or monthly) until the entire inventory has been counted at least annually.

*3. Fleet does not segregate staff duties during the fast-moving parts daily count.*

Segregation of duties, a commonly used and widely accepted internal control and GAO best practice, entails dividing or segregating key duties and responsibilities among different people. Implemented effectively, this type of control reduces risk of error and fraud so that no single individual can adversely affect the accuracy and integrity of the count. However, Fleet's Parts division has a single individual performing the fast-moving parts daily count. In situations where segregation of duties is not practical or cost-effective, other controls should be employed to mitigate the recognized risk. Such mitigating control procedures include increased supervision and applying dual control by having activities performed by two or more people. It is recommended that Fleet ensures that no single individual can adversely affect the accuracy and integrity of the fast-moving parts daily count by establishing segregation of duties or other controls to mitigate these risks.

*4. Fleet does not segregate staff duties during the fast-moving parts evening count.*

Segregation of duties, a commonly used and widely accepted internal control and GAO best practice, entails dividing or segregating key duties and responsibilities among different people. Implemented effectively, this type of control reduces risk of error and fraud so that no single individual can adversely affect the accuracy and integrity of the count. However, Fleet's Parts division has a single individual

performing the fast-moving parts evening count. In situations where segregation of duties is not practical or cost-effective, other controls should be employed to mitigate the recognized risk. Such mitigating control procedures include increased supervision and applying dual control by having activities performed by two or more people. It is recommended that Fleet ensures that no single individual can adversely affect the accuracy and integrity of the fast-moving parts evening count by establishing segregation of duties or other controls to mitigate these risks.

*5. Fleet does not segregate staff duties during the general inventory parts section counts.*

Segregation of duties, a commonly used and widely accepted internal control and GAO best practice, entails dividing or segregating key duties and responsibilities among different people. Implemented effectively, this type of control reduces risk of error and fraud so that no single individual can adversely affect the accuracy and integrity of the count. However, Fleet's Parts division has a single individual performing the general inventory parts section count. In situations where segregation of duties is not practical or cost-effective, other controls should be employed to mitigate the recognized risk. Such mitigating control procedures include increased supervision and applying dual control by having activities performed by two or more people. It is recommended that Fleet ensures that no single individual can adversely affect the accuracy and integrity of the general inventory parts section count by establishing segregation of duties or other controls to mitigate these risks.

*6. Fleet does not segregate staff duties during the receiving of inventory parts process.*

The key function areas of segregation of duties (as a GAO best practice) are: (a) physical custody of assets, (b) processing and recording of transactions, and (c) approval of transactions. Ideally personnel performing any one of the above functions would not also have responsibilities in either of the other two functions. Thus, where practical, adequate segregation of duties for the receiving of inventory parts process should include using personnel who do not have overlapping responsibilities in: (1) custody of the inventory stock, (2) recording transactions resulting from receipt of new inventory items, and (3) authority for approving adjustments resulting from the receipt of new inventory stock. However, Fleet's Parts division has a single individual performing the receiving of inventory parts process. In situations where segregation of duties is not practical or cost-effective, other controls should be employed to mitigate the recognized risk. Such mitigating control procedures include increased supervision and applying dual control by having activities performed by two or more people. It is recommended that Fleet ensures that no single individual can adversely affect the accuracy and integrity of the receiving of inventory parts process by establishing segregation of duties or other controls to mitigate these risks.

*7. Fleet does not segregate staff duties during the removing of inventory parts process.*

The key function areas of segregation of duties (as a GAO best practice) are (a) physical custody of assets, (b) processing and recording of transactions, and (c) approval of transactions. Ideally personnel performing any one of the above functions would not also have responsibilities in either of the other two functions. Thus, where practical, adequate segregation of duties for the removing of inventory parts process should include using personnel who do not have overlapping responsibilities in: (1) custody of the inventory stock, (2) recording transactions resulting from the removal of inventory items, and (3) authority for approving adjustments resulting from the removal of inventory stock. However, Fleet's parts division has a single individual performing the removal of inventory parts process. In situations where segregation of duties is not practical or cost-effective, other controls should be employed to mitigate the recognized risk. Such mitigating control procedures include increased supervision and applying dual control by having

activities performed by two or more people. It is recommended for Fleet to ensure that no single individual can adversely affect the accuracy and integrity of the removing of inventory parts process by establishing segregation of duties or other controls to mitigate these risks.

### **Observations and Recommendations**

*1. Fleet management should identify ways to streamline parts inventory management, including complete implementation of a bar code system.*

During the review, IA determined that Fleet partially uses a bar code system, but only for Fast-Moving parts and batteries. Fleet has further created a 'book' on tire barcodes to eventually add these to the Fast-moving parts already in the system. However, beyond these parts, Fleet does not manage any other inventory stock with the bar code system. It is recommended that Fleet continues to streamline their management of inventory stock by including implementation of a bar code system (GAO best practice) to include all parts inventory.

*2. Fleet does not have a process to periodically identify and dispose of idle and obsolete stock items in their parts warehouse.*

During the review, IA determined that Fleet does not have a documented process to periodically identify and dispose of idle and obsolete stock items in their parts warehouse. Fleet has stock items which include items that have unknown issue dates. The number of idle stock items that are obsolete is unknown. Idle or obsolete inventory indicates a waste of resources including: 1) funds that are spent for inventory that is not needed, 2) no recovery of cost through salvage value, and 3) space being used to store unneeded items. IA found that there is no documented process to periodically identify and dispose of the idle and/or obsolete inventory. It is recommended that Fleet management revises their policies to include a documented process to both identify and dispose of idle and/or obsolete inventory.

*3. Fleet has no documented threshold or procedure for staff to explain causes of variation.*

Fleet has no documented threshold or procedure for staff to require explanation for the causes of variation between the book inventory records and actual quantity; however, Fleet's unofficial accuracy performance goal is currently at 80 percent. Furthermore, Fleet's unofficial net adjustments resulting from a count are not to exceed a 20 percent 'offage' rate. From a best practices standpoint, setting high goals for inventory record accuracy rates is one way of establishing accountability for the physical inventory count. High goals 'stretch' the organization and personnel to perform inventory counts with increasingly superior precision. GAO best practice experts agree that inventory record accuracy goals should be set at 95 percent or higher. Other variation best practices establish accountability through alternative performance expectations such as a change in either dollar value or in quantity of adjustments. Fleet should include within their policies inventory record accuracy goals which meet with City management expectations. It is further recommended that Fleet determine and document within their policies a threshold or performance target which requires staff to provide explanations for causes of variation in inventory records.

## Overall Recommendation

IA recommends that Fleet implements industry best practices as cited in Best Practices in Achieving Consistent, Accurate Physical Counts of Inventory and Related Property, released by the GAO in March 2002.

Per the GAO, the best inventory practices:

1. Establish Accountability
2. Establish Written Policies
3. Select an Approach
4. Determine Frequency of Counts
5. Maintain Segregation of Duties
6. Enlist Knowledgeable Staff
7. Provide Adequate Supervision
8. Perform Blind Counts
9. Ensure Completeness of Counts
10. Execute Physical Counts
11. Perform Research
12. Evaluate Count Results

## Management Response

***Issue 1: Fleet Services has not implemented policies and procedures for the entire physical count of inventory process.***

Fleet services received assistance from our software vendor, FASTER, to generate reports to initiate blind counts. Fleet services recently implemented these processes and will conduct blind counts weekly, at a minimum. We have reached out to an auto-parts vendor and other City departments to seek assistance with obtaining policy and procedures focused on inventory and warehouse management. We will review and compile best practices that will be feasible given our staffing constraints to improve the process and formally document current expectations. We will work to create a detailed SOP on how to handle all aspects of the warehouse/inventory management to include formally documenting a "turnover limit" on stock items to assist with ID and removing obsolete items from stock, proper use of the barcode system, and document variation processes.

***Issue 2: Fleet has not designated sectional counts to ensure complete wall to wall counts are being completed at least annually.***

The fleet services parts division has faced extreme staffing shortages, forcing staff to perform additional duties outside of their job descriptions. They have done an excellent job to do what is necessary to keep the shop functional during these unprecedented times. We have constantly shifted resources to remain committed to providing the highest level of customer service and decrease downtime for all our customers. The parts division experienced significant illness related absenteeism over the last fiscal year in both the leadership and frontline staff members, which increased responsibilities on the staff and removed layers of oversight like never before. Fortunately, we have recently hired new talent within the parts division, but it will take considerable time before this person is considered adequately trained for

their position. When fully staffed, the parts division does not have a dedicated position to assign to the task of performing inventory counts. Fleet services has reached out to the utilities department regarding their exceptional warehousing division, to learn they have sufficient staff to allocate several warehouse clerks to counts and division of labor within their inventory operations, a luxury that fleet services does not currently have. The likelihood of implementing a complete, wall to wall, physical count remains exceptionally low considering critical lack of staffing in the parts division. Fleet services continues to advertise vacant positions and will ensure a wall-to-wall count is performed annually once the parts division is fully staffed.


***Issue 3: Fleet does not segregate staff duties on various aspects of the inventory process***

Staffing levels do not allow for the duplication of duties within the parts division. Fleet services has relied on the recommended mitigation controls of “increased supervision” and dedicates these responsibilities to the parts division supervisor to oversee the work of their staff. The preferred method is to have dedicated staff member(s) to managing warehousing and inventory processes to allow for adequate segregation of duties. However, unless additional staffing is allocated to fleet services, we will create formal redundancy to ensure “increased supervision” remains our mitigation strategy regardless of supervisory absenteeism.

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Respectfully submitted,

  
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