

**DEPARTMENT OF ENVIRONMENTAL SERVICES
BUREAU OF WATER
HEMLOCK OPERATIONS CENTER STOCKROOM INVENTORY OBSERVATION**

**Office of Public Integrity
Date: December 9, 2015**

I. EXECUTIVE SUMMARY

The Office of Public Integrity (OPI) observed the physical inventory of the Bureau of Water, Hemlock Operations Center stockroom on September 17, 2015. This was the second physical inventory that Bureau of Water personnel have conducted on this stockroom. The results of the inventory indicate that the Bureau of Water maintains adequate inventory control.

- ◆ OPI noted variances in 1.2% of our sample selection of stockroom inventory items indicative of differences between the physical counts and the quantities recorded in the perpetual records. In the previous inventory we noted a variance of 2.2%.

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 Bureau of Water conducted its second physical inventory of the Hemlock Operations Center stockroom on September 17, 2015. OPI participated in these counts at the request of the Department of Environmental Services.

B. Background

The Materials and Equipment unit of the Director's Office stores and manages an inventory of supplies and materials necessary to operate and maintain the water distribution system. In addition to the main inventory storage area on Felix Street, the Bureau of Water maintains a stockroom inventory at its Hemlock Operations Center facility. As of September 17, 2015 this inventory consisted of 1,880 line items valued at \$814,999.

Bureau of Water personnel have recently added the inventory stockroom at the Hemlock facility to the automated inventory system. The system assists in controlling quantities and providing information to management. A perpetual inventory record is an essential feature of this system. Prior to the installation of this system, a comprehensive, automated inventory management system was not in use at the Hemlock facility.

C. Objective and Scope

The objectives of this review are 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.

We conducted this audit in accordance with Generally Accepted Government Auditing Standards (GAGAS). 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 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.

III. RESULTS OF REVIEW

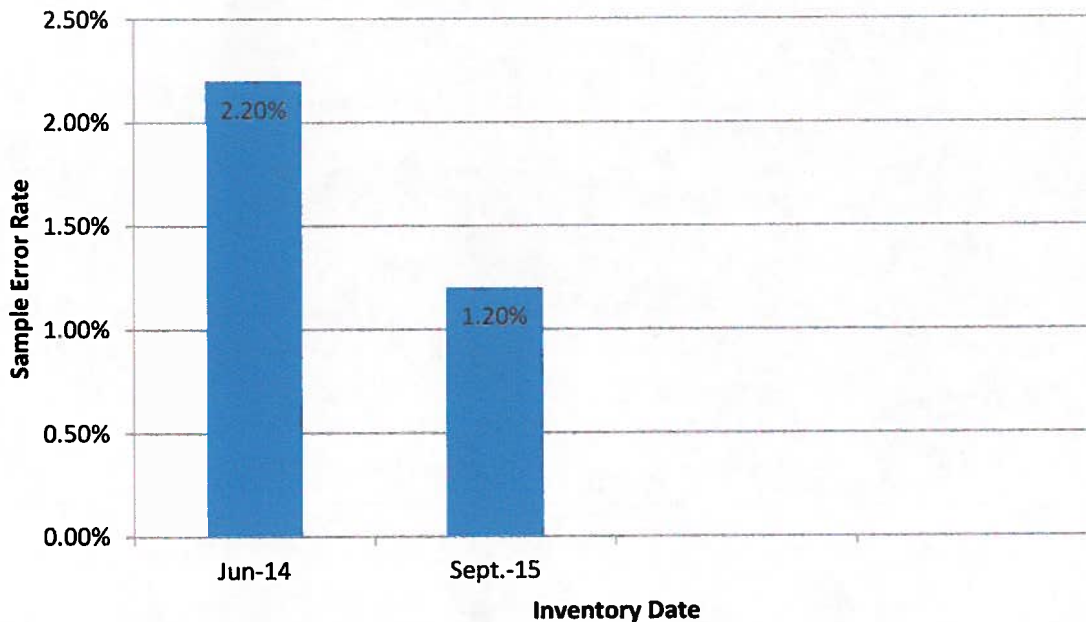
The results of this physical inventory indicate that Water Bureau personnel maintain adequate control over the inventory.

A. Variance Analysis

The Office of Public Integrity selected a statistical sample of 171 items included in the stockroom inventory. The sample selection assures proper representation throughout the entire population of inventory items and allows us to accurately project the results against the entire inventory. The range of unit costs included in the sample extends from \$0.05 to \$16,676. OPI compared the actual count of each of these selected items to perpetual records and noted any variances.

Of the 171 inventory items tested in the sample, OPI noted two variances. The sample error rate is therefore 1.2%. The following graph presents historical error rates as a reference.

**Bureau of Water
Hemlock Operations Center Stockroom Inventory
Sample Error Rate Percentages**



The attached table presents the variance analysis 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.

When OPI extends the sample error rate of 1.2% to the entire population of 1,880 different stock items, the projection indicates that the actual number of errors in the population is in the range of 2 to 100 stock items. When comparing the current error rate of 1.2% to the prior error rate of 2.2% in 2014, it appears that, based on the results of the sample selection, Bureau of Water personnel have continued to maintain adequate control over the stockroom inventory.

◆ Recommendation

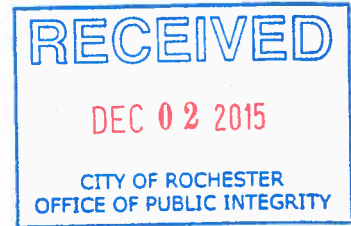
Management should continue to make inventory control a priority.

IV. DEPARTMENTAL RESPONSE

The response of the Department of Environmental Services follows.

Department of Environmental Services
 Bureau of Water
 Hemlock Facility Stock Room Inventory – September 17, 2015
Schedule of Sample Selection Variances Only

<u>Stock Number</u>	<u>Part Description</u>	<u>Booked Quantity On Hand</u>	<u>Actual Quantity On Hand</u>	<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>	
144406	Posts Sign 12' Large	62	63	1		\$67.95	\$ 67.95		
124720	Painters Tape 1" Blue	11	13	2	-	3.83	7.66		
		<u>73</u>	<u>76</u>	<u>3</u>	<u>0</u>		<u>\$75.61</u>	<u>\$ 0.00</u>	
Net Variance.....								<u>\$75.61</u>	



To: Daniel Mastrella, Internal Audit/OPI
From: Norman Jones, Commissioner/DES *ufj*
Date: October 27, 2015
Subject: Inventory Audit Results of 09/17/15 – Hemlock Operations Center

The Water Bureau conducted the second official physical inventory of the Hemlock Operations Center stockroom on September 17, 2015. The Office of Public Integrity observed this inventory. The previous physical inventory was on May 19, 2014. The 2015 inventory was comprised of 1,880 different line items valued at \$815,656. Reliant Inventory Group performed a 100% physical inventory of all line items in the database. The line items that were included in this audit were separate from the inventory maintained by the Water Bureau's Materials and Equipment stockroom on Felix Street.

I am very pleased to report that the true variance rate was 0.75% by item, which represents a 66% improvement of the previous variance rate of 2.18% by item. The statistical findings by OPI of 1.2% are also well within acceptable limits. Both variance rates are an improvement over the previous findings. The net variance amounted to (-14) units that, when calculated out, added \$619 to the booked value.

The Materials, Equipment, Fleet and Facilities Coordinator has dedicated the resources and staff so that significant progress was made to add all stock items to the perpetual inventory system. Since the 2014 audit, line items increased 79% from 1,053 to 1880. The number of units counted increased 252% from 17,092 to 60,139. As a result, the book value of inventory items at the Hemlock Operations Center increased 201% from \$271,174 to \$815,656.

Based on the previous work by Water Bureau Materials and Equipment staff, with the continued support of the Manager of Water Production, and ongoing training of the Water Bureau's Hemlock Operations Center staff, I am confident that all parties involved will continue to make inventory control a top priority.

Attachments: 09/17/2015 OPI Findings
09/24/2015 M&E Results

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