



Audit of DPW Infrastructure and Milwaukee Water Works Inventory

City of Milwaukee
Internal Audit Division
April 2024

Agenda

- Scope & Objectives
- Procedures
- Conclusions
- Findings
- Next Steps

Audit Scope

The scope of this audit was the Department of Public Works (DPW) Infrastructure and Milwaukee Water Works (MWW) inventory processes including receiving, disbursements, cycle counts, physical security, and inventory accounting for the period July 2022 through June 2023.

Audit Objectives

- Evaluate and test the inventory management policies, procedures, and internal controls.
- Evaluate and test the accuracy of inventory records and management reports.
- Evaluate the extent of obsolete, slow moving or missing inventory.
- Evaluate and test the physical security controls in place at each warehouse location.

Audit Procedures

Audit activities consisted of:

- Process walkthroughs
- Review of relevant policies and procedures
- Observations
- Testing of controls

Audit Conclusions

The audit concluded that the inventory management control environment needs improvement. Certain control activities and monitoring efforts are not operating effectively to address the risks associated with current operations.

Internal audit details 10 findings and recommendations to further improve the effectiveness of key inventory management processes to protect against compliance, financial or other operational risk.

Audit Finding 1: Inventory Counts and Resulting Inventory Adjustments

Finding	Risk and Rating	Recommendations
<p>Internal Audit conducted blind count testing while on-site at the inventory warehouses.</p> <ul style="list-style-type: none"> The Tower warehouse had 3 out of 7 inventory count differences and the Canal warehouse had 12 out of 18 inventory count differences. Additionally, Audit noted that the cycle count performed by the Inventory Manager on high demand/higher value stock items at both Tower and Canal had 7 out of 16 count differences. 	<p>Risk: Inventory may be inaccurately counted and/or omitted resulting in inaccurate financial reports.</p> <p>Rating: High</p>	<ul style="list-style-type: none"> ➤ Perform complete physical inventory verification process for all warehouses. ➤ Use of Target Variance Guidelines detailed within the Inventory Materials and Management Policy ➤ Annually conduct Warehouse Variance Scoring assessments

Audit Finding 2: Account Reconciliation Segregation of Duties

Finding	Risk and Rating	Recommendations
<p>DPW Purchasing and Inventory Manager prepares and reviews all reconciliations prior to submitting the final results to the Comptroller's Office.</p>	<p>Risk: Reconciliations could be inaccurate resulting in both erroneous and inappropriate actions.</p> <p>Rating: High</p>	<ul style="list-style-type: none">➤ Reconciliation preparation and review should be conducted by two separate representatives in the administration office on all reconciliations that are submitted to the Comptroller's Office.➤ Reconciliation documents should contain a signature line item for the preparer and approver to sign and date during the review process.➤ Processes should be updated within relevant procedures and/or policy.

Audit Finding 3: Physical Security and Security Control Environment

Finding	Risk and Rating	Recommendations
<p>Inventory Management does not review inactive employees or personnel access from other departments at both the Canal and Tower Warehouse locations.</p> <ul style="list-style-type: none"> • Semi-Annual Inventory Facility Assessments and Annual Security Access Review were not conducted in accordance with procedures. • Inventory Management has not reviewed the Weekly Security Access Reporting since 2022. • The Canal warehouse did not have a camera system on the second floor or an after-hour access log sheet. 	<p>Risk: Unauthorized or unlawful entry may be attempted or made into City warehouses without detection. Additionally, City assets may be stolen, damaged, or otherwise compromised.</p> <p>Rating: Medium</p>	<ul style="list-style-type: none"> ➤ Semi-annual assessments and annual reviews should be conducted. Specifically, the review of access activity for inactive employees. ➤ An after-hours access log at Canal should be used and reviewed daily by management, and weekly security access reporting should be reviewed by management. ➤ The physical camera systems should be reviewed annually for functionality, practicality and quality to reduce the risk of theft.

Audit Finding 4: Inventory Price and Carrying Value Monitoring

Finding	Risk and Rating	Recommendations
<p>Inventory price change processes and procedures were not formally documented to ensure price changes are performed consistently and subsequently are properly monitored within the system of record.</p> <p>DPW Inventory Materials and Management Policy and procedure manuals did not include detailed inventory price change process.</p>	<p>Risk: Inventory valuation may be misstated in financial statements. Critical decisions on inventory price, obsolescence, and sourcing may be based upon inaccurate information.</p> <p>Rating: Medium</p>	<ul style="list-style-type: none"> ➤ Historical and current pricing on each inventoried stock item should be maintained within the system of record and monitored daily for accuracy. ➤ FMIS average unit cost (AUC) method should be monitored for accuracy on all current inventory for all warehouses on a monthly basis. ➤ Standard Operating Procedures should include specific steps on how to update inventory stock prices.

Audit Finding 5: Replenishment Stock Process

Finding	Risk and Rating	Recommendations
<p>There were no procedures to review overstock inventory.</p> <ul style="list-style-type: none">• One of the overstock items reviewed for testing was purchased in 2021 at a quantity of \$3.8 million for future projects.• This inventory item is currently valued at \$1.9 million. There was no supporting documentation for the over stock item.	<p>Risk: Overstock inventory may lead to inaccurate counts and valuation of inventory, misclassified financials, theft and fraud.</p> <p>Rating: Medium</p>	<p>➤ Improve the process for calculating stock replenishment orders to avoid overstocking items. Inventory Management should create policies and procedures to review overstock inventory.</p>

Audit Finding 6: Policies and Procedures

Finding	Risk and Rating	Recommendations
<p>DPW Inventory Policies and City of Milwaukee procedures have not been updated for a significant amount of time and do not contain approvals by senior management of the department.</p> <p>The current policies and procedures were last revised in 2012 or prior.</p>	<p>Risk: Personnel may not have adequate information, tools and/or skills to perform necessary functions.</p> <p>Rating: Medium</p>	<ul style="list-style-type: none"> ➤ Inventory management should review and update the current DPW Inventory and Materials Management Policy and all City of Milwaukee inventory procedure manuals, as necessary. ➤ Revised policy and procedures should be approved by DPW senior management. All pertinent approved changes should be communicated to the inventory staff. Policies and procedures should be continuously reviewed and updated on an annual (or as-needed) basis.

Audit Finding 7: Management Reporting

Finding	Risk and Rating	Recommendations
<p>Inventory Management and/or staff did not prepare or use several management reports as specified within the Inventory Management Policy, Functional Procedure/Warehouse/Transaction Entry manuals. See Audit Report for a list of reports.</p> <p>There are no documented SOPs for activities conducted at the warehouse and administration level.</p>	<p>Risk: Reports may not be accurate, which could result in critical decisions possibly being made upon erroneous information.</p> <p>Rating: Low</p>	<ul style="list-style-type: none"> ➤ Policies and procedures should specify a timeline for the occurrence of all management reporting, and clarify which reports are supplemental and not critical to operational needs. ➤ Policies and Procedures should also reference SOPs for activities conducted at the warehouses and by administration. SOPs should provide clear-cut directions and detailed instructions needed to perform specific tasks consistently and efficiently.

Audit Finding 8: Obsolete Stock Process

Finding	Risk and Rating	Recommendations
<p>There were no updated policies and procedures for obsolete inventory that define when an inventory item is obsolete and an inventory disposal process.</p> <p>Obsolete inventory that was not disposed of or sold was kept in the warehouses without being tracked and occupies space while holding no value.</p>	<p>Risk: Critical decisions may be based upon financial statements, records, or manufacturing reports which are inaccurate. Inaccurate information may result in excessive inventory levels if unnecessary inventory is ordered or produced.</p> <p>Rating: Low</p>	<p>➤ Update policies and procedures to improve the process for managing obsolete material by defining when and how items should be disposed of.</p>

Audit Finding 9: Transaction Processes – Returned Goods

Finding	Risk and Rating	Recommendations
<p>A system module for historical returned stock inventory transactions does not exist. DPW was unable to monitor or track returned inventory stock outside of the system.</p>	<p>Risk: Inaccurate inventory counts and on-hand value for the respective business unit may result in inaccurate financial reports.</p> <p>Rating: Low</p>	<ul style="list-style-type: none">➤ In the absence of an FMIS system-based solution, an alternative solution may be used to track and monitor stock returns. Though return of physical inventoried goods is infrequent, this process should be performed on a routine basis. (Physical returns as well as administrative-related returns)➤ Policies and procedures should be updated to reflect the solution being implemented by the department.

Audit Finding 10: Transaction Processes – Disbursement of Goods

Finding

During the review of a sample of 45 inventory disbursement transactions, Audit noted the following exceptions:

- Four out of 45 disbursement transactions were processed untimely when comparing the Inventory Transaction Report (ITR) prepared by warehouse staff to the ship date indicated in FMIS. These four transactions resulted in a ship date being greater than 14 days from the date of the ITR.
- Three out of 45 transactions contained accounting detail in FMIS that did not match the fund, department, program or class data indicated on the ITR forms.
- One ITR was missing accounting detail for a disbursed stock item that should have been classified as a shop job item.
- The Inventory Transaction Report contains an "Entered By" line item that is frequently initialed for approval/tracking purposes; this component is not included in the signature requirement section of the DPW Inventory and Materials Management Policy.

Audit Finding 10: Transaction Processes – Disbursement of Goods

Risk and Rating	Recommendations
<p>Risk: Inventory transaction information may be inaccurate within the system and financial reports.</p> <p>Rating: Low</p>	<ul style="list-style-type: none">➤ Monitoring for untimely shipping activity should occur weekly to ensure accuracy of monthly reconciliation.➤ DPW administration staff should reject ITRs with missing accounting detail, or maintain appropriate documentation disclosing instances when the accounting detail entered into FMIS will differ from information included on the report. Inventory management should continue to enforce the two-signature requirement.➤ The "Entered By" line item currently used on the ITRs should be added to the signature requirement section of the DPW Inventory and Materials Management Policy.

Next Steps

Phase 1

- Auditees will execute audit finding remediation action plans.



Phase 2

- Internal Audit will solicit audit finding remediation progress updates annually.



Phase 3

- Internal Audit will report remediation status to the F&P committee annually.



Thank You.

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