



City of Virginia Beach

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VIRGINIA BEACH, VA 23456-9012

December 6, 2021

Patrick A. Duhaney, City Manager
City Manager's Office
City of Virginia Beach
2401 Courthouse Drive
Virginia Beach, VA 23456

Subject: Results of Agreed-Upon Procedures for the Review of City Garage Parts Unit Operations

Dear Mr. Duhaney,

We have performed the Review of City Garage Parts Unit Operations to determine whether internal controls are operating efficiently and effectively.

We were not engaged to perform and did not perform an audit, the objective of which would have been the expression of an opinion or limited assurance. Accordingly, we do not express such an opinion. Had we performed additional procedures; other matters may have come to our attention that would have been reported to you. We completed the procedures on November 5, 2021.

This report is intended solely for the information and use of the City Manager's Office and City leadership. It is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

This engagement was conducted in accordance with Government Auditing Standards (GAS). GAS incorporates financial and attestation standards established by the American Institute of Certified Public Accountants. These standards also provide guidance for performing and reporting the results of agreed-upon procedures. The sufficiency of these procedures is solely the responsibility of those parties specified in this report. Consequently, we make no representation regarding the sufficiency of the procedures described herein, either for the purpose for which this report has been requested or for any other purpose.

The Office of the City Auditor reports to City Council through the Audit Committee and is organizationally independent of all City departments. This report will be distributed to the City’s Audit Committee, City Council, and appropriate management within the City of Virginia Beach. This report will also be made available to the public through the Office of the City Auditor’s webpage.

Background

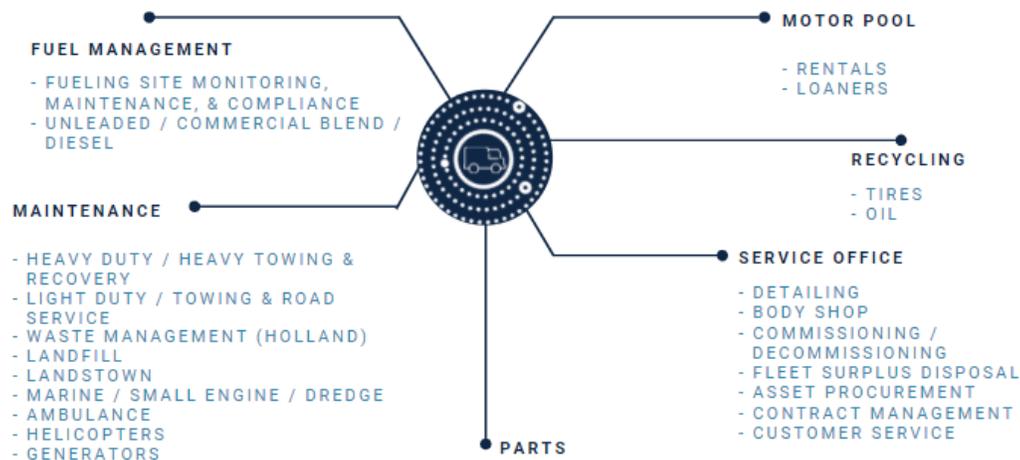
The City Garage Parts Unit is part of the Fleet Management Division of the Department of Public Works. Fleet Management is responsible for the acquisition, repair, maintenance, and disposal of the City’s fleet of nearly 4,000 vehicles and associated equipment used for police, fire, medical emergency, infrastructure, waste collection, and other vital services. Fleet Management has around 80 FTEs in its six units and has an annual budget of \$23 million. See Figure 1 below.

The mission of the Parts Unit is to provide parts for City vehicles and associated equipment in a timely and efficient manner. It operates three storerooms: the Main Storeroom located at Leroy Road, the Holland Road Annex, and the Landstown Road Annex. Its normal staffing complement comprises seven full-time employee (FTE) storekeepers. However, due to difficulties in finding replacements for the past two years of staff transitions, its staff is reduced to just three FTE storekeepers and two recently hired part-time assistants. The inventory value at the end of Fiscal Year (FY) 2020 was \$741 thousand.



Main City Garage Storeroom

Figure 1: Fleet Management Division



Source: FleetStat Package 8-12-21

The Parts Unit has been experiencing increasing challenges associated with qualified staffing, supply chain, inventory shrinkage, and inventory obsolescence in the past few years. For these reasons, the City has decided to outsource the garage parts operations to a qualified contractor that will establish an onsite automotive parts operation. Contractor bidding solicitation is being done through the Request for Proposal (RFP) Process. The current status of the RFP as of the date of our report is shown in Table 1.

Table 1. RFP Schedule	
Actions	Date
Department review and finalize proposal	September 28, 2021
Issue RFP	September 30, 2021
Advertise in newspaper	October 7, 2021
Addendum #1 - Modification of the terms of the RFP document for the site tour	October 13, 2021
Site tour	October 19 & 21, 2021
Deadline for questions	November 1, 2021
Addendum #2 - Response to supplier's questions	November 3, 2021
Addendum #3 – Response to final supplier's questions	TBD
Closing date*	December 3, 2021

Source: Purchasing Department

* Future date is tentative and subject to change.

Based on our review, we identified the findings shown below and provided recommendations for management to take immediate corrective actions.

Finding 1: High Variance Rate Found During Physical Inventory Testing

Our physical inventory testing of 90 samples from the three main locations resulted in a 27% variance rate. The net value of the variances was \$5,167, which equates to 5% of the sample population's value of \$97,494. We also noted that the Main Storeroom needs better organization, as numerous parts and boxes were scattered in many places. Management stated that the Parts Unit's considerable understaffing issue could have been a significant contributor. See Table 2.

Table 2. Inventory Testing Results Summary				
Variance Type	Number	%	Value	%
Shortage	21	23%	\$ (8,314)	-8%
Overage	3	3%	\$ 3,148	3%
Totals	24	27%	\$ (5,167)	-5%

Recommendation:

- 1.0 Management should increase monitoring activities in the storeroom through frequent interactions with Parts Unit staff and visits to the storerooms to promptly identify and correct internal control deficiencies.

Finding 2: Yearly Physical Inventory Not Independently Conducted

The yearly physical inventory conducted by the Parts Unit Supervisor is a conflict of interest as he is in-charge of that unit's day-to-day operations. It should be conducted by an independent person, such as a Fleet Management manager or the Accountant, to ensure independence, objectivity, and accuracy. The absence of these three elements increases the risk of errors and improprieties that could lead to inaccurate financial statement reporting.

Recommendation:

- 2.0 Management should assign an independent person to conduct physical inventory while having Parts Unit staff and other assigned personnel provide support.

Finding 3: Results of Yearly Physical Inventory Not Investigated

Fleet Management's FY 2021 year-end physical inventory shortage of \$10,045, which equates to 1.32% of \$763,633 total value, was not investigated to identify systemic errors, negative trends, and possible improprieties that may have been the underlying causes. Since physical inventory is conducted just once per year, discrepancy investigations are especially important to mitigate the risks of adverse impacts to the financial statement.

Recommendation:

- 3.0 Management should investigate yearly physical inventory discrepancies to ensure appropriate corrective actions are taken.

Finding 4: Absence of Internal Controls Over Inventory Adjustments

There are no controls in place to ensure inventory adjustments are properly performed. Parts Unit staff make quantity and price adjustments in the inventory management system almost daily and without management approval. We reviewed the *Parts Inventory Adjustment Transactions* report and found that there were 1,794 adjustments having an absolute value of \$331,196 (net value \$33,272) made in FY 2021.

Inventory adjustments are necessary to adjust the book balances to the actual physical count. However, it should be done only after an official physical count and with management's authorization. Absence of these internal controls drastically undermines the integrity of the inventory process.

Recommendations:

Management should:

- 4.0 Ensure that inventory adjustments are only done after official physical counts and after its review and approval.
- 4.1 Generate the *Parts Inventory Adjustment Transactions* periodically to ensure that no adjustments are made without its approval.

Finding 5: Physical Access Restriction to the Storerooms Not Constantly Enforced

Physical access restriction to the storerooms is not constantly enforced. We observed unauthorized personnel occasionally entering and exiting the storerooms without being accompanied or monitored by Parts Unit staff. For example, the Main Storeroom's two side gates were constantly left open, thus allowing free access of unauthorized personnel while Parts Unit staff were working at the front desk. Unrestricted or unmonitored access leaves inventory significantly vulnerable to theft.

Recommendation:

- 5.0 Management should ensure that physical access restrictions are constantly enforced to protect inventory assets.

Finding 6: Concurrence with Outsourcing Parts Unit Operation

Based on our review of the Parts Privatization Project white paper, discussions with management, and onsite observations, we agree with management's decision to outsource the Parts Unit operation to a highly qualified contractor that will establish an onsite automotive parts operation. We considered the following points:

- The difficulty in hiring and retaining qualified staff has been amplified due to the increased competitiveness in the labor market. The constant repair and maintenance requirements of the City's vehicles necessitate a full staff knowledgeable and experienced in inventory control and parts maintenance. Only through this can the Parts Unit properly manage day-to-day tasks, adequately exercise internal controls, and proactively employ inventory calculation methods, such as reorder points and turnover ratios, to maximize operational efficiency and effectiveness.
- The City's large and diverse automotive and specialized vehicle fleet constantly demands large monetary investments to maintain optimal inventory levels. This also requires increasing inventory maintenance due to the growing number and continuing model changes of City vehicles, which elevates the risk for parts obsolescence and shrinkage.
- Outsourcing reduces the administrative burdens not only for Public Works, but also for other departments that provide support, such as Finance, Management Services, and Human Resources.

The core business objective of Fleet Management is to perform quality repair and maintenance services to City vehicles while maximizing turnover rates. The Parts Unit plays an important yet clearly supportive role. Continued efforts in trying to overcome its significant challenges could detract from accomplishing the core business objective; the consequences of which could impact the City's ability to provide vital services to its citizens.

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Our findings and recommendations have been discussed and agreed upon with management.

We would like to thank the management and staff of the Department of Public Works' Fleet Management Division for their courteous assistance during our engagement.

Should you have any questions, please do not hesitate to contact me at 385-5872 or via e-mail at lremias@vbgov.com.

Sincerely,



Lyndon S. Remias, CPA, CIA
City Auditor

LSR/ag

c: LJ Hansen, Director of Public Works
Lisa A. Henrickson, Fleet Management Administrator
James W. Yost, Fleet Management Operations Coordinator



City of Virginia Beach

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INTER-OFFICE MEMORANDUM

DATE: November 19, 2021

TO: Lyndon Remias, CPA, CIA

FROM: LJ Hansen via Lisa Henrickson *LJH*

SUBJECT: Audit of City Garage Parts Operations response

Finding 1:

Public Works / Fleet Management concurs with the audit findings. Management with the Storeroom Supervisor will conduct regular cycle counts together to monitor activities and promptly identify errors.

Finding 2:

Public Works / Fleet Management concurs with the audit findings. The Fleet Management Operations Coordinator and Accountant II were present, but not leading the inventory. The dates and time of the inventory were forwarded to Audit for an independent auditor visit if needed. Arrangements will be made in the future to coordinate separation of duties during the inventory process.

Finding 3:

Public Works / Fleet Management concurs with the audit findings. In the future Fleet Management will investigate the results of yearly inventory to identify and correct problems.

Finding 4:

Public Works / Fleet Management concurs with the audit findings. A formal process will be established to require all adjustments to be approved by management before the adjustment is made. Management will run a weekly "Parts Adjustment Detail Report" in Asset Works Fleet Focus, under Reporting tab/Parts Adjustment Details/ Dates=current week/ All Locations/All Adjustment Reasons)

Home Work Management Supervisor Portal Technician Portal Storekeeper Portal Mobile Apps Fuel Reporting Query Customer Access Service Request Scheduler Warranty Support

Reporting

Reports:

- My Favorites
- Capital Planning
- Cost Analysis
- Enterprise Purchasing
- Equipment Info
- Fuel Info
- Greenhouse
- Incident Info
- Linear Info
- Motor Pool
- NAPA
- NTD
- Operations Info
- Parts Info
- Purchasing Info
- Shop Operations
- Utilities

Parts info

Publish report files to InfoCenter:
Choose File | No file chosen | Upload File

Issued Parts Charges	About
Issued Parts with Warranty Soon Expiring	About
Least Issued Parts	About
Master Parts List	About
Non-Fleet Inventory Valuation to Excel	About
Not from Inventory Issued Parts	About
Obsolete Parts	About
Part Cross References	About
Part Failures	About
Part Request Pick List	About
Part Stockout Companion	About
Parts Adjustment Details	About
Parts by Bin Location	About
Parts by Bin Range	About
Parts Detail	About
Parts End of Month Inventory	About
Parts Inventory Adjustment Transactions	About
Parts Past Due	About

Enterprise Asset Management - Google Chrome
Not secure | infocenter-prod/InfoCenter/Reporting/

Show Report To PDF Schedule

Enter a date range for the parts adjustment date:

(MM/DD/YYYY) (Select a date function)

(MM/DD/YYYY)

Select the Inventory Location(s): (Supports wildcards * and ?)

[ALL] Add Remove Remove All

Select the Adjustment Reason(s): (Supports wildcards * and ?)

[ALL] Add Remove Remove All

Finding 5:

Public Works / Fleet Management concurs with the audit findings. Management will confirm physical restrictions are in place and stay in place.

Finding 6:

Public Works / Fleet Management concurs.