COUNTY OF LOS ANGELES
DEPARTMENT OF AUDITOR-CONTROLLER

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WENDY L. WATANABE
AUDITOR-CONTROLLER

August 21, 2013

TO: Supervisor Mark Ridley-Thomas, Chairman
Supervisor Gloria Molina
Supervisor Zev Yaroslavsky
Supervisor Don Knabe
Supervisor Michael D. Antonovich

FROM: Wendy L. Watanabe
Auditor-Controller

SUBJECT: **DEPARTMENT OF PUBLIC WORKS PROCUREMENT REVIEW**

In August 2007, your Board instructed the Auditor-Controller to develop a risk-based plan to audit procurement operations in all County departments. In accordance with the developed plan, we completed a review of the Department of Public Works' (DPW or Department) compliance with County procurement policies and procedures.

Background

DPW's Administrative Services Division and Fiscal Division have primary responsibility for ordering items, receiving deliveries, issuing payments, managing supply inventories, and monitoring equipment. DPW also delegates some of these functions to larger units (e.g., Waterworks, Road Maintenance, etc.). The Department's services and supplies budget for Fiscal Year 2012-13 was over $1 billion.

Review Scope and Summary

We reviewed DPW's procurement practices for compliance with County policies and procedures. Our review included interviewing DPW personnel, reviewing purchases, evaluating internal controls, and inventorying equipment and supplies.

We noted that DPW's purchases were appropriate and necessary for their operations. DPW also manages equipment and supplies as required by County policies. However,

DPW management needs to ensure that staff comply with all purchasing requirements, and appropriately segregate incompatible purchasing, equipment, and supply functions. The following are the detailed results of our review.

General Purchasing and Payment Controls

County Fiscal Manual (CFM) Chapter 4 requires department staff to complete purchase requisitions to request items and obtain management approval. Approved requisitions are sent to procurement staff, who subsequently issue purchase orders to vendors to order the requisitioned items. Purchase orders are formal agreements between the County and vendors which identify purchasing terms (e.g., item type, quantity ordered, price, etc.), and are used to encumber budgeted funds. Purchases should not be initiated until the Department has properly approved requisitions and purchase orders in place so there is no ambiguity about what is being purchased and the agreed upon pricing.

The CFM also requires staff to review receiving documents provided by vendors (e.g., packing slips, etc.), verify that all items were received, and complete receiving reports to record results. It also requires invoice processing staff to match invoices to purchase orders and receiving reports before paying vendors. This ensures that payments are only made for items that were actually ordered and received, and that the correct prices are paid.

We reviewed 29 purchases DPW made over a 12-month period, totaling approximately $300,000, and noted the following:

- **Overpayment** – DPW was overcharged $2,200 for one (3%) purchase. DPW paid the full invoice amount ($19,800), even though prices and quantities were not correct. We also noted that DPW entered 40% more items on receiving reports in the Countywide Accounting and Purchasing System (eCAPS) than they actually received for this purchase.

- **Purchase Orders** – DPW issued purchase orders after they received items for two (7%) purchases, totaling $33,400. As noted above, purchases should not be initiated unless there are already approved purchase orders in place to ensure appropriate managerial pre-approval. We also noted that DPW's purchase orders were inaccurate/incomplete (i.e., did not include all of the items or actual costs) for three (10%) purchases, totaling $28,100. DPW revised these purchase orders after receiving the goods and services, based on invoices and receiving documents. Since purchase orders are formal agreements that identify purchasing terms, DPW needs to ensure that the purchase orders are completed accurately.

- **Receiving Documents** – DPW did not have packing slips or other documents identifying the items received for one (3%) purchase, totaling $10,000.

Recommendations

DPW management ensure staff:

1. **Match invoices to purchase orders and receiving reports before they pay vendors.**

2. **Review and recover the overpayment identified.**

3. **Complete purchase orders and receiving reports accurately and in a timely manner.**

4. **Maintain all procurement documentation (e.g., packing slip, etc.).**

Non-Agreement and Agreement Purchases

The Internal Services Department (ISD), as the County's purchasing agent, delegated DPW the authority to purchase non-agreement items under $10,000. All purchases over the delegated authority must be processed by ISD. Departments must comply with ISD policies when making non-agreement purchases under their delegated authority, including obtaining three price quotes for purchases over $1,500.

ISD also establishes agreements with vendors for commonly purchased items. Departments can purchase items covered by the agreements without obtaining price quotes, and purchases are not subject to the delegated authority limits. ISD purchasing policies indicate that departments should assist in identifying the potential need for additional agreements by monitoring frequent non-agreement purchases (i.e., vendors and/or items), and notifying ISD to establish new agreements when it is beneficial to the County.

We reviewed DPW's purchases and noted the following:

- **Price Quotes** – DPW did not obtain the required price quotes for one (7%) of 14 non-agreement purchases reviewed, totaling $4,800. DPW also did not indicate item quantities when they requested price quotes for one (7%) purchase, totaling $3,600. To ensure DPW receives the lowest possible prices, staff should request price quotes and identify item quantities on the requests.

- **Agreement Pricing** – DPW did not review agreement prices before ordering the items for three (20%) of 15 agreement purchases we reviewed, totaling $19,000. For two of these purchases, DPW ordered items at higher than agreement

prices. The vendors subsequently corrected the error and billed DPW the agreement prices.

- **Frequent Purchases** – During the 12 months we reviewed, DPW made frequent purchases from five non-agreement vendors (average of 200 times each), totaling $790,000. DPW should monitor frequent non-agreement purchases, and notify ISD regarding additional vendor agreements to potentially lower item costs.

Recommendations

DPW management ensure staff:

5. **Request price quotes as required by County policy, and identify item quantities on requests.**

6. **Review vendor agreement prices before ordering items.**

7. **Monitor frequent non-agreement purchases, and notify the Internal Services Department of the potential need for additional vendor agreements.**

eCAPS Security Access

eCAPS allows departmental staff to initiate and approve various purchasing functions online. The requisitioning, ordering, receiving, and invoice processing functions should be segregated to reduce the risk of errors or fraud. We reviewed the eCAPS access profiles for DPW staff and noted the following:

- Three staff could process requisitions, purchase orders, and payments.

- Six staff could process requisitions and purchase orders.

- Four staff could create vendors and modify vendor information in eCAPS, and process payments or purchase orders.

- Two former DPW employees still had eCAPS access an average of 36 days after leaving County service.

Recommendation

8. **DPW management segregate requisitioning, ordering, receiving, and invoice processing functions in eCAPS to different staff, and remove access when staff leave the Department.**

Capital and Non-Capital Equipment

Capital equipment includes items with a useful life over one year and acquisition costs over $5,000, and non-capital equipment includes portable items under $5,000. CFM Chapter 6 requires departments to keep accurate equipment lists, track equipment with property tags, and assign responsibility for equipment. Departments must also conduct a physical inventory of capital equipment every two years, and non-capital equipment every year.

As of June 2012, DPW's capital equipment had a total acquisition cost of $166.9 million. We could not determine the total cost of non-capital equipment because DPW's records did not include costs for some items. We noted that DPW conducts physical inventories of equipment as required by the CFM. We also conducted an inventory of DPW's equipment and noted that equipment lists were generally accurate, items were tagged, and responsibility was assigned to specific employees. However, we could not locate one (5%) of the 20 capital equipment items reviewed, totaling $907,000. We found that DPW staff disposed of the item, but did not update the capital equipment list.

DPW also needs to segregate incompatible equipment functions. We noted that staff responsible for equipment could also modify the equipment lists. These employees could misappropriate items and remove them from the lists to avoid being detected. It should be noted that our review did not find any evidence of this occurring.

Recommendations

DPW management:

9. **Ensure equipment lists are updated when items are disposed.**

10. **Segregate equipment responsibility and recordkeeping functions.**

Warehousing and Supply Inventory

DPW has 14 supply warehouses and stockrooms with inventory totaling $9.9 million, as of June 2012. We noted that DPW's warehousing and supply operations generally comply with CFM Chapter 5 requirements. DPW appropriately manages supply levels, maintains accurate perpetual inventory records, and conducts annual physical supply inventories. Supply adjustments (e.g., additions, issuances, etc.) are also appropriately authorized.

However, DPW needs to segregate incompatible supply functions. We noted that staff with warehouse access (e.g., supply custodians, etc.) were responsible for modifying the perpetual inventory records. These employees could misappropriate supplies and record supply issuances to avoid being detected. Again, our review did not find any

evidence of this occurring. DPW management indicated that they will evaluate the warehousing and supply operating structure, including functions assigned to staff.

Recommendation

11. DPW management segregate supply access and recordkeeping functions.

Review of Report

We discussed the results of our review with DPW management. They generally agreed with our findings and recommendations. DPW's attached response describes the corrective actions they have taken, or plan to take, to address the recommendations in our report.

We thank DPW management and staff for their cooperation and assistance during our review. Please call me if you have any questions, or your staff may contact Robert Smythe at (213) 253-0101.

WLW:RS:YK

Attachment

c: William T Fujioka, Chief Executive Officer
Gail Farber, Director, Department of Public Works
Tom Tindall, Director, Internal Services Department
Department Heads
Public Information Office
Audit Committee

COUNTY OF LOS ANGELES

DEPARTMENT OF PUBLIC WORKS

"To Enrich Lives Through Effective and Caring Service"

GAIL FARBER, Director

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IN REPLY PLEASE
REFER TO FILE: FI-2

August 8, 2013

TO: Wendy L. Watanabe
Auditor-Controller

FROM: Gail Farber
Director of Public Works

RESPONSE TO PROCUREMENT REVIEW

We have reviewed your audit report for the Department of Public Works, and we are in general agreement with your recommendations. Public Works strives to adhere to County fiscal policies. As indicated in the attached response, we have taken immediate corrective actions and continue to implement additional measures to strengthen controls. Regarding our warehouse operations, we will require additional time to evaluate and assess how to cost effectively segregate the incompatible supply functions you have identified. Accordingly, we intend on conducting a study to evaluate our warehouse operations.

Thank you for the opportunity to respond to your report. We also extend our appreciation for your staff's professional conduct during this audit.

AC:dbm
P:\iapub\INTAUDIT\OUTSIDE AUDITS\A-C Procurement Review\Response to DPW Procurement.docx

Attach.

County of Los Angeles
Department of Public Works
Response to Procurement Audit Recommendations

General Purchasing and Payment Controls

Recommendations

DPW management ensure staff:

1. **Match invoices to purchase orders and receiving reports before they pay vendors.**

   Response: Agree and Implemented

   Staff will continue to use eCAPS to match invoices, purchase orders, and receiving reports before paying vendors. In addition, we have instructed Accounts Payable staff to thoroughly review receiving reports to ensure the service dates and quantities match invoices.

2. **Review and recover the overpayment identified.**

   Response: Agree

   We will review the overpayment identified and work with the vendor to recover the overpayment.

3. **Complete purchase orders and receiving reports accurately and in a timely manner.**

   Response: Agree

   We will retrain staff to ensure that purchase orders and receiving reports are reported accurately and in a timely manner. However, in some instances modifying purchase orders is necessary for estimated services (i.e., tonnage of rubbish removal).

4. **Maintain all procurement documentation (e.g., packing slip, etc.).**

   Response: Agree and Implemented

   We reminded staff to maintain source documents to substantiate receiving.

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Response to Procurement Audit Recommendations

Non-Agreement and Agreement Purchases

Recommendations

DPW management ensure staff:

5. **Request price quotes as required by County policy, and identify item quantities on requests.**

   Response: Agree

   We will remind staff to request price quotes as required by County policy and identify item quantities on requests.

6. **Review vendor agreement prices before ordering items.**

   Response: Agree

   We will remind staff to review all applicable vendor agreement prices prior to ordering items.

7. **Monitor frequent non-agreement purchases, and notify the Internal Services Department of the potential need for additional vendor agreements.**

   Response: Agree

   We will remind staff to monitor frequent non-agreement purchases, and we will notify the Internal Services Department of the potential need for additional vendor agreements.

eCAPS Security Access

Recommendations

DPW management:

8. **DPW management segregate requisitioning, ordering, receiving, and invoice processing functions in eCAPS to different staff, and remove access when staff leave the Department.**

   Response: Agree and Partially Implemented

   We have segregated or removed eCAPS functions for all but one staff, and corrective action is under way for the remaining employee. We have also revised procedures to ensure eCAPS access is removed when staff leaves the Department.

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Response to Procurement Audit Recommendations

Capital and Non-Capital Equipment

Recommendations

DPW management:

9. **Ensure equipment lists are updated when items are disposed.**

   Response: Agree and Implemented

   We revised procedures to ensure equipment lists are updated timely when items are disposed.

10. **Segregate equipment responsibility and recordkeeping functions.**

    Response: Agree and Implemented

    We created two new Security roles for DPW property custodians in May 2011 to separate equipment responsibility and recordkeeping functions.

Warehousing and Supply Inventory

Recommendation

11. **DPW management segregate supply access and recordkeeping functions.**

    Response: Agree

    We agree with the intent of the recommendation. We are working with a consultant to conduct a study of the warehouse network to address the issue.