



Audit of Warehouse Inventory Management

The City of Denton's Warehouse has established generally effective inventory controls to manage and adequately safeguard inventory. That being said, it has not established controls to monitor accuracy of transactions and inventory records.

Additionally, opportunities may exist to streamline Warehouse operations and improve efficiency.

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Audit at a Glance

Why we did this Audit:

The City of Denton's Warehouse Division is responsible for maintaining and stocking approximately 4,600 inventory items, processing orders, managing contracts worth approximately \$75 million, and coordinating disposals of surplus items for City Departments. This audit was included on the City's fiscal year 2021-22 Audit Plan as approved by the City Council.

What we Recommend:

Recommendations 1 & 3

Consider implementation of new software to improve low stock monitoring and customer ordering efficiency.

Recommendations 2, 4, 6, & 10

Develop standard procedures for receiving & stocking orders, completing customer orders, managing keys, and processing auctions.

Recommendations 5 & 8

Provide periodic training to staff on return item returns and disposal practices.

Recommendation 7

Ensure all inventory items are verified at least annually.

Recommendation 9

Evaluate asset destruction criteria.

What we Found:

This audit generally evaluated the controls implemented to ensure warehouse inventory is adequately managed and safeguarded, as well as the inventory ordering, distribution, monitoring, and disposal processes. Our findings are summarized below:

Ordering. Warehouse item ordering duties are generally appropriately segregated; however, stock monitoring processes are manual. Automation could further improve efficiency and reduce the risk that items are not ordered timely. Some order receiving documentation was inadequate.

Distribution. The Warehouse has established a generally effective process for customers to order and pickup items; however, the ordering process could be further streamlined with additional software. Documentation of customer pickups and returns could be further improved.

Security & Monitoring. Warehouse inventory is generally safeguarded appropriately, though key management practices could be improved. The Warehouse's cycle count process does not ensure that all inventory items are verified annually.

Disposal. The Warehouse has generally established processes and procedures to dispose of City property per its policy; however, City-wide awareness of these processes may hinder compliance. Still, adjustment of current disposal method value thresholds may improve efficiency.

In addition, while all auction payments were appropriately received and reconciled, documentation of the individual collecting items won through the auction was often missing.

Introduction

The Internal Audit Department is responsible for providing: (a) an independent appraisal¹ of City operations to ensure policies and procedures are in place and complied with, inclusive of purchasing and contracting; (b) information that is accurate and reliable; (c) assurance that assets are properly recorded and safeguarded; (d) assurance that risks are identified and minimized; and (e) assurance that resources are used economically and efficiently and that the City's objectives are being achieved.

The Internal Audit Department has completed a performance audit of the City's warehouse inventory management processes. We conducted this performance audit in accordance with generally accepted government auditing standards. 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.

Management Responsibility

City management is responsible for ensuring that resources are managed properly and used in compliance with laws and regulations; programs are achieving their objectives; and services are being provided efficiently, effectively, and economically.

Audit Objectives, Scope, and Methodology

The Internal Audit Department has completed an audit of the City's warehouse inventory management processes. This report is intended to provide assurance that the City has implemented adequate controls to safeguard and manage inventory.

Audit fieldwork was conducted during May, June, and July 2022. The scope of review varied depending on the procedure being performed. The following list summarizes major procedures performed during this time:

- Reviewed documentation to develop criteria including industry standards, best practices, policies, and procedures;
- Developed process narratives to identify current control activities in the inventory management and disposal processes that were certified by Warehouse Division staff;

¹ The City of Denton Internal Auditor's Office is considered structurally independent as defined by generally accepted government auditing standard 3.56.

- Interviewed Warehouse Division staff and reviewed policies and procedures pertaining to the City's inventory management and disposal requirements;
- Reviewed departmental surplus donations and destructions to determine whether disposals were properly recorded and managed;
- Reviewed completed surplus auctions and related payments to ensure auctions were properly managed and recorded, and payments were appropriately received from the external vendor;
- Reviewed a statistical sample² of cycle counts from April 2020 to April 2022 to determine whether cycle counts were appropriately documented and completed;
- Reviewed a statistical sample³ of processed customer orders, and a statistical sample⁴ of Warehouse inventory orders and Warehouse returns and refunds from April 2020 to April 2022 to verify transactions were appropriately processed, recorded, and contained appropriate support documentation;
- Administered an anonymous survey to 98 Warehouse customers to gauge customer satisfaction and awareness of Warehouse processes and received responses from 27 customers;⁵
- Conducted an on-site inventory review and observed physical safeguards at the City's Warehouse;
- Reviewed Warehouse Stock Request Agreements for a judgement sample of fifteen inventory items;
- Verified if a judgement sample of fifteen inventory items were made on contract; and
- Conducted an on-site visit to of Denton Municipal Electric's pole yard, interviewed Denton Municipal Electric staff and reviewed procedures related to Denton Municipal Electric inventory management.⁶

² This sample size provides with 95 percent confidence that the true population mean is within ± 10 percent of the sample estimate.

³ This sample size provides with 95 percent confidence that the true population mean is within ± 5 percent of the sample estimate.

⁴ This sample size provides with 95 percent confidence that the true population mean is within ± 10 percent of the sample estimate.

⁵ Anonymous customer survey responses are summarized in Appendix B.

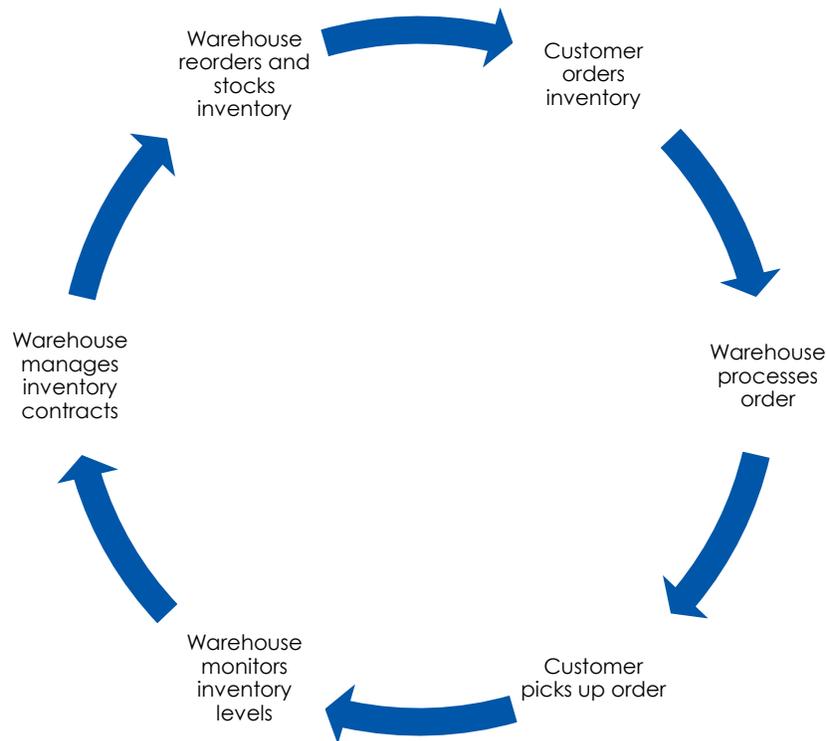
⁶ Denton Municipal Electric's pole yard inventory processes were not reviewed in depth during the scope of this review; however, may be included during an audit in the future.

Findings & Analysis

The City of Denton’s Warehouse Division is responsible for daily management of City inventory⁷ which includes ordering stock, monitoring low-stock inventory, distributing items to customers, managing returns and refunds, and overseeing the surplus disposal processes. Currently, the Warehouse Division manages approximately 4,600 items. Additionally, the Warehouse is responsible for managing inventory contracts, and currently maintains approximately 87 contracts valued at over \$75 million.

The inventory process begins with a customer department placing an order for inventory from the Warehouse’s catalog. The Warehouse then processes and prepares the inventory order for pick-up by the customer. After the inventory has been collected, the Warehouse continuously monitors inventory stock quantities to identify low-stock items, places re-orders as needed, and manages vendor contracts. Once inventory deliveries are received, the items are processed and stocked at the Warehouse.

Figure 1: Overview of City Inventory Management Process



⁷ The Warehouse Division maintains inventory items like: air filters; gloves; ice melt pellets; pvc pipe; nuts & bolts; pavement markers; manholes; and traffic signage.

The Warehouse provides a centralized location for inventory, making it easier to track and manage. It is important to ensure proper controls are established to adequately monitor, record, stock, distribute, and dispose of inventory. The Warehouse also oversees the City's disposal processes, including destructions, donations, and auctions.⁸

This audit generally evaluated the controls implemented to ensure warehouse inventory is adequately managed and safeguarded, during the ordering, distribution, and disposal processes.

Manual Inventory Ordering Processes May Impact Efficiency

The Warehouse Division promotes efficiency throughout the City by centralizing the ordering, receiving, and storage process for items frequently needed by departments when carrying out their functions. In order to be effective, the Warehouse must ensure it has the items its customers need when they are needed. To do this, Warehouse staff must have a process to monitor inventory levels, determine if additional items are needed, and order new items.

What We Found

- The Warehouse Division has created Warehouse Stock Request Agreements that are established with City Departments. These agreements specify inventory brand, model number, and minimum and maximum quantities to maintain in-stock at the Warehouse. If the items are no longer needed, the requesting Department is responsible for purchasing the remaining in-stock items.
 - According to Warehouse personnel, the Warehouse has recorded all available Warehouse Stock Request Agreements into their database. The Warehouse has been established since the 1980's and Warehouse personnel stated the general stock request agreement process has been in place since Warehouse inception; however, the Warehouse does not have record of all established Warehouse Stock Request Agreements due to employee turnover and process changes over the past three decades.
 - The Warehouse centralized the Stock Request Agreement process at the beginning of 2022 through the Stock Request Agreement database. City Departments must complete the Stock Request Agreement form electronically which auto-populates the database and ensures all new Stock Request Agreements are appropriately recorded.

⁸ During Covid-19, the Warehouse Division became responsible for managing the City's courier services which was not included in the scope of this review.

- Additionally, as previously mentioned, the Warehouse Division is responsible for managing the contracts related to all stocked inventory items which assists with ensuring inventory is ordered under proper authorization. These contracts detail vendor information, inventory items approved to be purchased, start and end dates of the contract, and the total contract amount.
 - Based on review of a judgment sample of fifteen inventory items, all items were purchased under an established contract, with the exception of one item that was out-of-stock with the contractual vendor due to supply chain issues and had to be purchased through a separate vendor.
- The Warehouse Division performs monitoring in order to prevent inventory stock quantities from falling below the requested minimum quantities. Additionally, based on inventory stock levels and continuous monitoring, the Warehouse places inventory orders for low stock items as needed.
- The current process for Warehouse personnel to monitor low stock inventory quantities requires manual analysis of each inventory record. Specifically, Warehouse staff must import data from the City's financial system into a spreadsheet each week in order to calculate needed quantity based on currently stocked amounts, upcoming project needs, the agreed minimum and maximum quantities, and the estimated time it takes to fill an order.
 - The Warehouse Division has established standard operating procedures for Warehouse personnel to guide staff through the process of identifying low stock inventory and placing orders.
 - Based on an anonymous customer satisfaction survey administered to customers, over 70 percent of respondents said the Warehouse fulfills their orders timely and keeps them updated on the status of their order; however, over 15 percent of respondents indicated inventory restocks were not completed timely. It should be noted that recently, many inventory items have experienced supply chain constraints, resulting in shipping delays and extended lead times.
- Based on the Warehouse Division's monitoring of inventory stock quantities, the Warehouse Specialists place inventory orders through the requisition process in City's financial system.
 - In order to place an inventory order, a vendor contract must be established.
 - The Warehouse Manager is responsible for reviewing and approving all Warehouse orders.

- Once the inventory order is delivered to the Warehouse, the receiving Warehouse employee reviews the delivery to account for all received inventory items, actual quantities delivered, and the Warehouse location for storage. This information is recorded on the Purchase Order Receiving form and the vendor receipt, then saved in the respective Warehouse folder. Additionally, according to Warehouse personnel, the Warehouse Manager reviews all invoices and compares to order receiving documentation prior to processing payment to vendors.
- Based on review of a statistical sample of 94 received and processed inventory orders, approximately 91 percent of inventory orders had appropriate support documentation.
 - The remaining 9 percent of orders did not have accompanying support documentation, accurate recorded quantities received, or Warehouse employee verification of received goods as detailed in Table 1.

Table 1: Processed Inventory Order Exceptions Summary

Documentation	Quantity	Percentage
No Purchase Order & Vendor Receipt Located	5	5%
No Verification of Quantity Received	2	2%
Inaccurate Quantity Recorded	2	2%

- In addition, the Warehouse Division has not established procedures to guide Warehouse personnel when receiving orders, retaining documentation, and stocking inventory.

Why It Matters

Warehouse personnel must manually review inventory stock quantities and identify low stock, which can result in accidental oversights and lack of necessary reorders. Additionally, many inventory items are experiencing supply chain issues and shipping delays so preemptive ordering is beneficial to ensure continuity of City operations.

Ensuring all order documentation is adequately retained provides evidence that items are appropriately received and accounted for. Additionally, ensuring received and stocked inventory orders are properly counted, verified, and recorded reduces the potential for inaccurate inventory quantities and ensures vendors are not paid for items not received. This verification also reduces the possibility for fraud, stolen goods, or missing inventory items with no record of receipt.

Furthermore, development of standard operating procedures that specify inventory delivery verification and stocking expectations would help ensure that all inventory orders are authorized, counted, and recorded appropriately and contain the necessary documentation needed to support each delivery. In addition, this formal guidance would provide Warehouse staff with institutional knowledge, facilitate consistency, and help navigate emergency situations.

Recommendations:

1. Evaluate the business need to adopt a software for monitoring low stock inventory quantities and reduce the risk of critical items being out-of-stock.

Warehouse Division Comments: *The Warehouse is actively looking at ways to improve processes. Warehouse is interested in adopting a software that will provide comprehensive inventory management including tracking stock levels. The City is considering a new ERP and the Warehouse will be included in the process.*

2. Develop standard procedures to detail the processes for receiving and stocking inventory orders. These procedures should include required documentation and retention location(s), and include a periodic review to verify appropriate documentation is retained.

Warehouse Division Comments: *The Warehouse will develop a SOP for receiving and stocking items. This SOP will also outline how to file supporting documentation for the orders.*

Warehouse Provides Generally Effective Customer Service; Some Documentation of Pickups & Returns Missing

Once stocked, inventory items are available for customers to use for City business. In order to ensure these items are adequately safeguarded and accurately charged, organizations typically establish a picking process. In order to have an effective picking process, organizations typically need the following:

- Accurate catalog of items that are stocked;
- Method of communicating the items to be picked;
- Process for accurately documenting receipt of the picked items; and
- Process for accurately documenting returned items.

What We Found

- The Warehouse appears to generally be available to provide service to other City departments when needed.

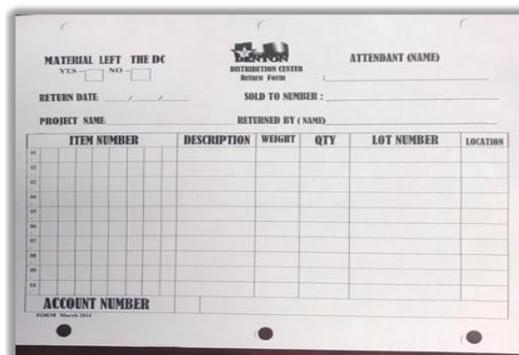
- The Warehouse has established standard operating hours for inventory orders and vendor deliveries. In addition, on-call personnel are maintained for after-hour orders and pick-ups.
- Based on Safety Division records, the Warehouse has been accident-free for over two years.
- Based on an anonymous customer satisfaction survey administered to customers, respondents indicated general satisfaction with Warehouse services. Specifically, 96 percent of respondents agreed that the Warehouse has adequate hours for departmental operations, Warehouse personnel were helpful, and the Warehouse is clean and safe.
- The Warehouse has established electronic and physical catalogs of stocked inventory items to facilitate customer orders. The electronic catalog contains a list of all inventory items and is available on the City's intranet while the physical catalogs are only available at the Warehouse and have items separated by department.
 - Based on the anonymous customer satisfaction survey, over 22 percent of respondents indicated issues related to the physical Warehouse Catalogs and general inventory ordering process. According to responses received, the separated Warehouse Catalogs can cause delays for customers when looking for a specific inventory item that is not listed in their catalog, and the physical catalogs can be difficult to search.
- The Warehouse Division has created a Stock Requisition Form to facilitate and document the items a customer would like picked. Completed Stock Requisition Forms may be submitted via email or in-person. Warehouse personnel use this form to print a pick slip and pull the items for pick up.
 - Upon pick up, customers that placed orders electronically are required to sign the pick slip to acknowledge receipt of the items. A copy of the signed pick slip is then provided to the customer and retained by the Warehouse. Customers that place walk-in orders are not required to sign the pick slip since they completed the Stock Requisition Form in-person.
 - Based on review of a statistical sample selection of 380 processed customer orders, approximately 60 percent of orders did not contain adequate support documentation, including: Stock Requisition Form, Pick Slip, or customer signature to verify receipt of inventory.
 - According to Warehouse personnel, the Warehouse began updating their internal processes around July 2021. Based on comparison of data

from April 2020 to June 2021, and July 2021 to April 2022, some improvements can be seen between those two periods as detailed in Table 2.

Table 2: Processed Customer Orders

Missing Documentation	Pre-July 2021	Post-July 2021
Stock Requisition Form	69%	16%
Pick Slip	65%	12%
Customer Signature ⁹	68%	42%
All Required Items	64%	12%

- In addition, responses to the anonymous customer satisfaction survey suggested the use of a digital kiosk system could streamline the ordering process compared to the current process of manually completing Stock Request Forms to place orders which would improve efficiency.
- The Warehouse Division has established Standard Operating Procedures for customers over the Electronic & Walk-in Ordering and Material Pick-up processes, as well as, Pulling an Order process for Warehouse personnel.
 - The Warehouse Division has not established procedures to overview the process for Warehouse personnel to complete and record the customer's inventory order after completion, including ensuring all documentation is completed, signed, and retained in a centralized location.
- Returns and refunds are processed by the Warehouse when a customer brings back unused items. The Warehouse has created a Return Form as shown in Picture 1 to initiate this process. While the Division has created a Standard Operating Procedure for Returns, it does not appear to be followed consistently by Warehouse personnel.



Picture 1: Return Form

- This standard operating procedure requires a customer to complete a Return Form, then Warehouse staff complete a Pick Slip. Once this is processed it should be signed by the customer and this documentation retained by the Warehouse.
- According to Warehouse personnel, a Return Form is not completed if an inventory item does not leave the Warehouse, or if an item is

⁹ This excludes customer signature on pick-tickets for walk-in orders.

refunded through a Department's Monthly Recon Expense Report process.

- Based on review of a statistical sample of 90 processed returns, approximately 32 percent did not contain adequate support documentation. As mentioned above, according to Warehouse personnel, the Warehouse began updating their internal processes around July 2021. Based on comparison of data from April 2020 to June 2021, and July 2021 to April 2022, some improvements have been made with retained support documentation retention as detailed in Table 3.

Table 3: Warehouse Returns

Status	Pre-July 2021	Post-July 2021
No Documentation Located ¹⁰	26%	8%
No Return Form	58%	46%
No Pick Slip	40%	21%

- In addition, one instance was noted where the return quantity recorded on the Pick Slip did not match the total return recorded in JD Edwards. This return also did not have an attached Return Form to verify accuracy.

Why It Matters

While the Warehouse Division currently has electronic and physical catalogs to assist with customer inventory orders, the current process to order inventory is manual and inventory item availability can vary daily. Due to this manual process and inventory fluctuation, catalogs may not reflect the most current inventory. Furthermore, it may be environmentally and financially unsustainable to develop new physical catalogs for each inventory addition or removal. An inventory ordering software would maintain accurate inventory, streamline the ordering process for customers and Warehouse personnel, and improve order efficiency.

In addition, it is important for there to be clear documentation of what a customer ordered and what was received. While improvements in supporting documentation retention have been made, development of standard operating procedures covering customer order processing would provide further guidance to staff to help ensure that all orders are documented and authorized appropriately. In addition, this formal guidance would provide Warehouse staff with institutional knowledge, facilitate consistency, and help navigate emergency situations.

¹⁰ This includes a Return Form, Pick Slip, or Monthly Recon Expense Report.

Lastly, the Warehouse has established standard operating procedures for Warehouse personnel to process returns; however, returns appear to be managed and documented inconsistently. Updating the procedures to specify required documentation retention requirements and providing periodic training to staff would ensure all returns and refunds are processed and recorded appropriately.

Recommendations:

3. Consider acquisition of an inventory ordering software to streamline inventory orders.

Warehouse Division Comments: *The Warehouse is actively looking at ways to improve processes and is interested in implementing a software that will provide comprehensive inventory management including a streamlined ordering process. The City is considering a new ERP and the Warehouse will be included in the process.*

4. Develop standard procedures to detail the processes for completing customer orders. These procedures should include required documentation and retention location(s), and include a periodic review to verify appropriate documentation is retained.

Warehouse Division Comments: *The Warehouse will review and update the current SOP's for customer orders and include an outline of the process.*

5. Provide periodic training to staff over Warehouse Return procedures and update the Warehouse Internal Return SOP to include required documentation and retention location(s).

Warehouse Division Comments: *Warehouse Management will implement a standardized and centralized filing system for returns. The current SOP will be revised to reflect the new process. Warehouse staff will be trained during the bi-weekly meetings.*

Warehouse Physical Safeguards Appear Effective; Not All Items Verified Annually

As part of continuous monitoring efforts to ensure inventory is properly managed, Warehouse best practices suggest:¹¹

¹¹ Best practices reviewed included: GAO Standards for Internal Control in the Federal Government; AU Section 901 Public Warehouses—Controls and Auditing Procedures for Goods Held; and Office of Internal Oversight Services.

Physical Safeguards

- Inventory areas be adequately lit;
- Access to inventory is managed through a single entry and exit;
- Premises have continuous video monitoring;
- Warehouse doors be locked;
- Premises be secured by an alarm system and a fence; locked doors, an alarm system, and a secured fence;

Monitoring Controls

- Inventory be periodically counted at least annually to identify missing items;

Access Controls

- Access should be restricted to only employees whose job duties require it; and
- Keys to the warehouse should be managed by an independent custodian.

What We Found

- The Warehouse is secured with locked doors, a locked gate (see Picture 2), a security system, and security cameras that are accessible 24 hours and seven days a week.



Picture 2: Warehouse Gates

- The Warehouse is set-up with a security system through an external vendor. In the event of a security breach notification, the Warehouse Manager is contacted by the security vendor and checks the security footage. These security measures assist with ensuring City inventory is properly safeguarded.
- Warehouse Division management is responsible for managing the keys and electronic lock codes that allow access to the Warehouse.
 - According to staff, the electronic lock codes for the security system and gate are updated at least annually and in the event of employee turnover.
 - The Warehouse Division has not established a formal key management schedule to monitor access to the Warehouse and track issued and returned keys.
- The Warehouse Division has established a process to complete periodic cycle counts. The periodic cycle counts are completed by Warehouse staff during their down time. Each staff member is assigned a certain area of the warehouse to complete at least annually. Any discrepancies are corrected by Warehouse personnel.
 - The Warehouse Division has developed a documented Standard Operating Procedure outlining the cycle count process.
 - Based on review of completed cycle count data, the Warehouse Division completed 367 cycle counts and reviewed over 9,455 items

between April 2020 to April 2022. Based on analysis of reviewed inventory, there were 199 inventory items (two percent) that had not been counted during a periodic cycle count. Specific details related to the cycle count exceptions are summarized in Table 4.

Table 4: Cycle Count Exceptions

Comment	Number of Items	Percentage
Area not yet counted	8	4%
JDE did not que count	3	1%
Phasing out ¹²	141	71%
Other ¹³	28	14%
New Stock	19	10%
Total	199	100%

Why It Matters

The Facilities Division is in the process of developing a key schedule for the City; however, the Warehouse Division is currently responsible for managing key access to the Warehouse. Development of a formal key policy for recording when an individual receives and returns a key ensures keys are monitored, returned, and employee access is appropriate. In addition, if a key is not returned, the Warehouse should take measures to ensure locks are changed and new keys are issued as appropriate.

City of Denton Policy requires a physical inventory of warehouse items be conducted annually. The Warehouse staff currently conducts periodic cycle counts to physically review inventory quantities; however, these cycle counts do not appear to be covering 100 percent of inventory items on an annual basis. As summarized in Table 4, over 70 percent of inventory not included in a cycle count was due to the inventory being phased out and was counted prior to going to auction; however, this inventory should be verified during the Warehouse’s cycle count process as it is at a higher risk of theft. Ensuring all inventory is reviewed and counted at least annually assists with accurate inventory records and City financial statements.

Recommendations:

- 6. Develop a process to manage key controls to the Warehouse and record employee key access, including logging when an employee receives and returns a key.

¹² Inventory items being phased out are counted as part of the phase out process to prepare for auction; however, these items were not included in a cycle count completed within April 2020 to April 2022.

¹³ This includes inventory items included in a cycle count outside the scope of review, item not yet received at time of cycle count, and non-inventory items.

Warehouse Division Comments: *The primary security system at the Warehouse is the alarm system keypad. Individuals entering the Warehouse must use a keycode to disable the alarm. If an incorrect keycode is used, the alarm will activate, and the Warehouse Manager will be notified immediately. The alarm company also notifies the Police Department of an alarm activation. The keycode is changed annually or in the event of employee turnover. Additionally, the Warehouse is under 24/7 video surveillance, with capability to remotely access live camera feeds and past footage on demand. The key is used as a secondary form of access. Rekeying a lock can be done if a specific threat is identified, however, a key holder will still need the alarm keycode for uninterrupted access. Warehouse staff will work with Facilities on reviewing best practices for security.*

7. Establish a standard cycle count schedule to ensure cycle counts cover 100 percent of warehouse inventory. If 100 percent annual coverage cannot be achieved with the cycle count process, a complete annual inventory should be conducted.

Warehouse Division Comments: *Warehouse Management will develop and implement a process that improves tracking of bi-annual cycle counts performed by the Warehouse Specialist II's to ensure that 100% of inventory is being covered on scheduled cycle counts. When items are no longer needed or being discontinued, they go through a phase out process where the item is counted, and a disposal process is immediately initiated. Phase out inventory is not included on bi-annual cycle counts but is being counted through a separate tracking process. This allows Warehouse staff to initiate a phase out at any time and the majority of phased out times are disposed of prior to the next cycle count.*

Item Disposal Processes Recently Centralized; City-wide Awareness of Disposal Process Could be Improved

City of Denton Policy encourages reuse of City property and equipment; criteria for surplus disposals through destruction, donation, or auction have generally been set. The Warehouse Division has developed workflow databases to track destructions, donations, and auctions. City Departments are responsible for ensuring surplus is properly disposed, updating the Warehouse databases with disposal information, and completing required forms. A general overview of the disposal process is illustrated in Figure 2.

Figure 2: Disposal Process



What We Found

- Based on an anonymous customer satisfaction survey administered to customers,¹⁴ approximately 20 percent of respondents indicated they were unaware of the City’s surplus disposal processes.

Destructions

- Per the Procurement Manual, items valued less than \$100 and not considered in good working order may be destroyed. The Warehouse has created a process for Departments to record these destructions in an Asset Disposal database.
 - City Departments must complete the Asset Disposal database form for disposals to be recorded in the database. This form does not require review or approval from the Warehouse Division. According to Warehouse staff, there is no way for them to know if surplus items are being disposed unless they are notified by other City employees.
 - Based on review of City surplus disposals, there were eight recorded permanent disposals in the Asset Disposal database since initial development between December 2021 through May 2022.
 - Based on review of third-party disposal procedures,¹⁵ items reasonably considered to be office supplies (i.e. notepads, pens, etc.) do not require handling through the established disposal process and can be disposed of as determined appropriate by the department.
- The Warehouse Division has established Standard Operating Procedures to overview the steps for City Departments to dispose of City-owned property.
 - These Standard Operating Procedures do not include disposal guidance for hazardous waste materials. Although Warehouse Division is not centrally responsible for hazardous waste disposal, coordination with the City’s Solid Waste Division could enhance disposal procedures.

¹⁴ Anonymous customer survey responses are summarized in Appendix B.

¹⁵ Research based on review of Columbus State Community College disposal procedures.

Donations

- The donation process was centralized through the Warehouse in 2022.
 - The Warehouse has established a Surplus Donation form to be completed by the donating City Department detailing the donation item, estimated value, valuation explanation, and non-profit entity receiving donation. This form is required to be reviewed by the Department Supervisor, Non-Profit Representative, and Warehouse and Compliance Divisions.
- Based on review of City surplus donations, there were two recorded donations in the Asset Donation Database since inception.
 - One donation did not have documented review and approval from the Warehouse Division and Compliance Division.

Auctions

- The Warehouse Division coordinates with an external vendor to manage the auction process and auction payments. Auction proceeds are sent to the City after the auction concludes. Based on review of City surplus auction data, there have been approximately 151 completed auctions since 2020.
 - The Warehouse Division has established draft procedures outlining the internal Warehouse processes for managing auctions; however, these do not include the process for reconciling received payments from the vendor.
 - The Warehouse Division established an auction database in April 2021, and prior to this database, auction information was managed internally by Warehouse personnel.
- In order to pick-up auctioned surplus, the auction winner or authorized individual must show identification, receipt of payment, and provide a signature to certify receipt of goods. A copy of this documentation is retained in Warehouse auction records.
- According to Warehouse personnel, the auction process was updated in April 2021.
 - Based on review of completed auctions processed from February 2020 to March 2021 were recorded, however, auction payment receipts were the only documentation retained and the department did not document auction buyer identification during this period.

- Based on review of completed auctions from April 2021 to April 2022, over 16 percent did not have record of the auction buyer's identification to verify appropriate pick-up.¹⁶

Table 5: Auctions Completed Since April 2021

Missing Data	Quantity	Percentage
Auction Buyer Identification	14	16.3%
Auction Buyer Signature	2	2.3%
Auction Receipt	1	1.2%

- Auction proceed payments are sent to the City of Denton Finance Division to be processed then transferred to the Warehouse Auction Proceed Account.
 - Approximately \$52,300 has been received from auction proceeds since September 2020. All auction proceed payments were appropriately received from the external vendor based on completed auctions.
 - Additionally, there have been two processed auction refunds totaling \$301 during calendar year 2021. Both refund requests were reviewed and approved by the Warehouse Manager and were processed through the City of Denton Procurement Division.

Why It Matters

The City has established methods for asset disposal that encourage reuse and promote sustainability. Determining the appropriate disposal method for assets is generally the responsibility of Departments; however, the Warehouse has established standard procedures outlining the steps for City Departments to destroy, donate, and auction surplus items, including a process for tracking items that are disposed. While tracking items for donation and auction seems appropriate, requiring items that meet destruction criteria to be tracked may increase inefficiency and encourage departments to retain items unnecessarily.

In addition, only assets valued more than \$5,000 are considered fixed assets and are thus tracked by the Finance Department to calculate depreciation. Assets valued below this threshold are expensed upon purchase and are generally not tracked as part of the City's inventory. For this reason, requiring departments to track the destruction of these assets may not add value to City operations. That being said, reuse of City items such as desks, cabinets, and exercise equipment should continue to be encouraged.

¹⁶ The auction winner can complete an Auction Authorization of Release Form to designate a different person for auction pick-up. This individual is also required to verify identification and provide a signature to acknowledge receipt of the auction item.

Development of standard operating procedures that specify surplus auction requirements would help ensure that all auctions are managed, recorded, and authorized appropriately and contain the necessary information and documentation needed to support verification of each coordinated auction and auction pick-up. In addition, this formal guidance would provide Warehouse staff with institutional knowledge, facilitate consistency, and help navigate emergency situations.

Recommendations:

- 8. Periodically provide reminders to City personnel to promote awareness of the surplus disposal processes related to destructions, donations, and auctions. Consider including messaging about the City's commitment to sustainability.

Warehouse Division Comments: *Employee forums, emails, and department trainings have all been used to communicate the surplus disposal process. The Warehouse Manager presented a presentation in the December 2021 Employee Forum informing city personnel of the procedures. Staff will continue to utilize these and other identified platforms to provide periodic updates to City staff. Information on sustainability can be included.*

- 9. Evaluate the asset destruction criteria to determine if it should be more closely aligned with the Finance Department's fixed asset criteria. Consider eliminating the requirement for departments to record asset destructions that met the criteria. Ensure disposal procedures are updated to reflect criteria guidelines.

Warehouse Division Comments: *Warehouse will review the fixed asset criteria and update the asset destruction criteria for consistency across both programs.*

- 10. Develop procedures outlining the internal Warehouse Auction process including auction preparation, required documentation to be retained for each auction and pick-up, and auction payment reconciliation.

Warehouse Division Comments: *Warehouse Management has drafted a Standard Operating Procedure for Internal Auction Processes. This document was not finalized due to additional changes in processes at the time the SOP was drafted. Warehouse Management will revise and finalize the Internal Auction SOP to reflect current practice to conduct auctions.*

Appendix A: Management Response Summary

The following summarizes the recommendations issued throughout this report. The auditors found that staff and the Department were receptive and willing to make improvements to controls where needed. Management has provided their response to each recommendation.

1	<i>Evaluate the business need to adopt a software for monitoring low stock inventory quantities and reduce the risk of critical items being out-of-stock.</i>	Concur	Expected Completion: 12/2025
Warehouse Division Comments: The Warehouse is actively looking at ways to improve processes. Warehouse is interested in adopting a software that will provide comprehensive inventory management including tracking stock levels. The City is considering a new ERP and the Warehouse will be included in the process.			Responsibility: Assistant Director
2	<i>Develop standard procedures to detail the processes for receiving and stocking inventory orders.</i>	Concur	Expected Completion: 12/2022
Warehouse Division Comments: The Warehouse will develop a SOP for receiving and stocking items. This SOP will also outline how to file supporting documentation for the orders.			Responsibility: Warehouse Management
3	<i>Consider acquisition of an inventory ordering software to streamline inventory orders.</i>	Concur	Expected Completion: 12/2025
Warehouse Division Comments: The Warehouse is actively looking at ways to improve processes and is interested in implementing a software that will provide comprehensive inventory management including a streamlined ordering process. The City is considering a new ERP and the Warehouse will be included in the process.			Responsibility: Assistant Director
4	<i>Develop standard procedures to detail the processes for completing customer orders.</i>	Concur	Expected Completion: 12/2022
Warehouse Division Comments: The Warehouse will review and update the current SOP's for customer orders and include an outline of the process.			Responsibility: Warehouse Management
5	<i>Provide periodic training to staff over Warehouse Return procedures and update the Warehouse Internal Return SOP to</i>	Concur	Expected Completion: 12/2022

	<i>include required documentation and retention location(s).</i>		
	Warehouse Division Comments: Warehouse Management will implement a standardized and centralized filing system for returns. The current SOP will be revised to reflect the new process. Warehouse staff will be trained during the bi-weekly meetings.		Responsibility: Warehouse Manager
6	<i>Develop a process to manage key controls to the Warehouse and record employee key access, including logging when an employee receives and returns a key.</i>	Partially Concur	Expected Completion: 12/2022
	Warehouse Division Comments: The primary security system at the Warehouse is the alarm system keypad. Individuals entering the Warehouse must use a keycode to disable the alarm. If an incorrect keycode is used, the alarm will activate, and the Warehouse Manager will be notified immediately. The alarm company also notifies the Police Department of an alarm activation. The keycode is changed annually or in the event of employee turnover. Additionally, the Warehouse is under 24/7 video surveillance, with capability to remotely access live camera feeds and past footage on demand. The key is used as a secondary form of access. Rekeying a lock can be done if a specific threat is identified, however, a key holder will still need the alarm keycode for uninterrupted access. Warehouse staff will work with Facilities on reviewing best practices for security.		Responsibility: Logistic Specialist
7	<i>Establish a standard cycle count schedule to ensure cycle counts cover 100 percent of warehouse inventory.</i>	Partially Concur	Expected Completion: 12/2022
	Warehouse Division Comments: Warehouse Management will develop and implement a process that improves tracking of bi-annual cycle counts performed by the Warehouse Specialist II's to ensure that 100% of inventory is being covered on scheduled cycle counts. When items are no longer needed or being discontinued, they go through a phase out process where the item is counted, and a disposal process is immediately initiated. Phase out inventory is not included on bi-annual cycle counts but is being counted through a separate tracking process. This allows Warehouse staff to initiate a phase out at any time and the majority of phased out times are disposed of prior to the next cycle count.		Responsibility: Logistic Specialist
8	<i>Periodically provide reminders to City personnel to promote awareness of the</i>	Concur	Expected Completion:

<p><i>surplus disposal processes related to destructions, donation, and auction.</i></p>	<p>On-going</p>
<p>Warehouse Division Comments: Employee forums, emails, and department trainings have all been used to communicate the surplus disposal process. The Warehouse Manager presented a presentation in the December 2021 Employee Forum informing city personnel of the procedures. Staff will continue to utilize these and other identified platforms to provide periodic updates to City staff. Information on sustainability can be included.</p>	<p>Responsibility: Warehouse Staff</p>
<p>9 <i>Evaluate the asset destruction criteria to determine if it should be more closely aligned with the Finance Department's fixed asset criteria.</i></p>	<p>Concur Expected Completion: 12/2022</p>
<p>Warehouse Division Comments: Warehouse will review the fixed asset criteria and update the asset destruction criteria for consistency across both programs.</p>	<p>Responsibility: Assistant Director</p>
<p>10 <i>Develop procedures outlining the internal Warehouse Auction process including auction preparation, required documentation to be retained for each auction and pick-up, and auction payment reconciliation.</i></p>	<p>Concur Expected Completion: 12/2022</p>
<p>Warehouse Division Comments: Warehouse Management has drafted a Standard Operating Procedure for Internal Auction Processes. This document was not finalized due to additional changes in processes at the time the SOP was drafted. Warehouse Management will revise and finalize the Internal Auction SOP to reflect current practice to conduct auctions.</p>	<p>Responsibility: Warehouse Management</p>

Appendix B: Customer Satisfaction Survey Responses

Table 6 illustrates the responses received from the anonymous customer satisfaction survey administered to Warehouse Division customers. The City Department of each respondent was requested for informational purposes but removed to maintain anonymity. In addition, comments from the survey have been provided to the Warehouse Division.

Table 6: Summary of Warehouse Customer Survey Results

