



ARLINGTON COUNTY GOVERNMENT

INTERNAL AUDIT REPORT

ACCOUNTING FOR TANGIBLE ASSETS WITH A LESS-THAN \$5000 PURCHASE PRICE

DEPARTMENT OF ENVIRONMENTAL SERVICES: WATER, SEWER, STREETS BUREAU WATER POLLUTION CONTROL BUREAU

Report Date: May 24, 2017

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The 2016-2017 Proposed Risk-Based Internal Audit Work Plan (the Plan) identified Asset Management as an area for audit. In accordance with the Plan, the Department of Management and Finance Internal Audit Unit has reviewed Arlington County’s procedures and identified processes related to accounting for purchases of tangible assets with an initial, individual cost of less than \$5,000 and an estimated useful life of three years or less (“LT5K”) for further review. The Department of Environmental Service’s Water, Sewers, Streets Bureau and the Water Pollution Control Bureau were selected to audit.

Arlington County’s policy is to expense LT5K as incurred. This report is organized as follows:

Executive Summary	This section gives a background summary of the function and a detailed description of the issues noted during this cycle audit, recommended actions, and management’s corrective action plan, including the responsible party and estimated completion date.
Background	This section provides an overview of the function within the process and pertinent operational control points and related compliance requirements.
Objective and Approach	The review objectives and focus are expanded upon in this section as well as a review of the various phases of our approach.

We would like to express our appreciation to the staff and all others involved with this review.

Respectfully Submitted,

Internal Audit,
 Department of Management and Finance

EXECUTIVE SUMMARY

EXECUTIVE SUMMARY

Each department employs processes that are necessary to address its particular needs and may not be representative of other departments in Arlington County. Departments employ various software applications such as Excel, Cartegraph, MP2, etc. to account for LT5K assets.

The overall objective of this audit is to assess whether systems and processes are adequate and appropriate to permit the proper accountability of LT5K assets. Accountability is generally described as maintaining adequate records that permit the County to:

- Know the quantity, quality, location, condition, and value of assets
- Safeguard assets from physical deterioration, theft, loss, or mismanagement
- Minimize unnecessary storage or maintenance costs
- Properly recognize, allocate, or otherwise charge the use/requisition/depletion of these assets to the proper program/accounting period etc.
- Gather reliable, accurate information in order to make informed decisions

The scope of this audit encompassed the current-state processes at the Department of Environmental Service's (DES) Water, Sewers, Streets Bureau (WSS) and the Water Pollution Control Bureau (WPCB) and an audit of selected transactions on a sample basis. Testing was customized to address the processes and procedures in place for each bureau.

For purposes of this audit, items considered as consumable inventory, replacement parts, supplies, etc. are not in scope.

A detail of the issues identified and their relative risk ratings is provided below, including recommendations for remediation and management's response. Relative risk factors have been assigned to each issue identified. This is the evaluation of the severity of the concern and the potential impact on the operations. There are many areas of risk to consider in determining the relative risk rating of an issue, including financial, operational, and/or compliance, as well as public perception or 'brand' risk. Items are rated as High, Moderate, or Low.

- High Risk Items are considered to be of immediate concern and could cause significant operational issues if not addressed in a timely manner.
- Moderate Risk Items may cause operational issues and do not require immediate attention, but should be addressed as soon as possible.
- Low Risk Items could escalate into operational issues, but can be addressed through the normal course of conducting business.

Issues	Risk Rating
Absence of documented, County-wide LT5K policy – County Level	Moderate
<p>Currently, no County-wide policy exists that describes the policies and procedures necessary to properly account for tangible assets with an initial, individual cost of less than \$5,000 and an estimated useful life of three years or less.</p> <p>Properly crafted policies inform employees, departments, bureaus etc. of the County’s expectations necessary for it to achieve its overall mission. Effective policies link the County’s vision to its day-to-day operations.</p>	
Recommendations	
<p>The policy should identify the key activities and provide a general strategy on how to achieve desired accountability for these assets. The following are general subject matter areas to consider in the policy:</p> <ul style="list-style-type: none"> ✓ Policy Statement <ul style="list-style-type: none"> ○ Formulate a statement that describes the purpose of this policy such as: The purpose of this policy is to set forth the guidelines for the physical and reporting control of the County’s tangible assets with an initial, individual cost of less than \$5,000 and an estimated useful life of three years or less. ✓ Reason for Policy <ul style="list-style-type: none"> ○ State that the intent of the policy is to describe the standard policies required for recording new and existing Assets, changes in Assets and the methodology of record keeping. ✓ Roles and Responsibilities <ul style="list-style-type: none"> ○ Discuss how each department/division which has custody over the assets are responsible to establish effective procedures necessary to comply with the policy. ✓ Types of Assets <ul style="list-style-type: none"> ○ Itemize, in general terms, the types of assets subject to this policy. ✓ Valuation of Assets <ul style="list-style-type: none"> ○ Assets are recorded at historical cost and are periodically reviewed for proper valuation. ✓ Effective asset identification measures such as: <ul style="list-style-type: none"> ○ Performing periodic physical inventory counts and establishing an identification system (tag, bar code) ✓ Effective segregation of duties ✓ Processes for properly disposing of assets 	
Management Response	
<p>DMF will consider all of the recommendations provided above and draft the necessary County-wide policy. Once the new policy is approved, it will be posted on the County’s intranet.</p> <p>Responsible Party: DMF Comptroller Estimated Completion Date: Modified to correct to May 1, 2018</p>	

Issues	Risk Rating
Absence of Documented Departmental Procedures- WSS and WPCB	Moderate
<p>Currently, WSS and WPCB do not have documented procedures to account for their LT5K assets. Establishing and documenting procedures are essential. Procedures demonstrate management's commitment to effectively maintaining accountability for LT5K assets as well as establishing processes and providing all personnel clear communication and comprehensive instructions and guidelines. Establishing written procedures helps ensure consistent and accurate compliance and application needed to achieve high levels of integrity and accuracy.</p>	
Recommendation	
<p>Upon completion of the County-wide LT5K policy (as discussed above), WSS and WPCB should each develop a Standard Operating Procedure to properly account for LT5K assets. Effective procedures will achieve the following objectives:</p> <ul style="list-style-type: none"> ✓ Provide employees the proper awareness and wherewithal to execute their roles and responsibilities within these processes, minimize ambiguity, and firmly establish management expectations ✓ Facilitate transitioning of roles and responsibilities when staff leave ✓ Afford a basis for training and informing staff; consider including checklists to support procedures ✓ Formally document an internal control framework and ensure accountability and consistency in daily transactions and financial reporting ✓ Include all aspects of a physical count process, including the activities or tasks that take place before, during, and after the physical count, objectives of the count, types and timing of counts, instructions for counting and recording, and researching and adjusting variances. Items to consider: <ul style="list-style-type: none"> ○ Establish responsibility for overall count and accuracy goals ○ Select an approach such as cycle counts (such as annual, bi-annual, etc.), full-counts, surprise counts as well as which items to count ○ Maintain segregation of duties such as those performing counts do not have recordkeeping responsibilities ○ Train staff on proper count practices and provide proper supervision ○ Ensure completeness of count including effective cutoff procedures ○ Perform effective reviews, evaluate count results and timely resolve differences between records and count totals ✓ Create protocols that describe procedural steps when an asset is received, how it is recorded and how its disposition is reflected in the department's records <p>Elements to consider:</p> <ul style="list-style-type: none"> ✓ Establish accountability and responsibility for physical counts, set accuracy goals ✓ Select approach - cycle counts (portions of inventory counted on a rotating basis), wall-to-wall counts (full count at a particular time), blend of the cycle and wall-to-wall etc. 	

Recommendation (Cont'd)

- ✓ Effective segregation of duties:
 - Optimal segregation of duties occurs when no one individual has custody of inventory, access to systems that record and process inventory, and the ability to approve transactions. Individuals who perform the inventory counts should be independent of these processes. If not possible considering limited resources, cost/benefit etc. consider alternatives means such as engaging a resource from another department to perform the count(s)
- ✓ Train participants on effective count processes, expected results, unique elements of the inventory etc.
- ✓ Provide proper supervision including clear instructions, proper completion of count sheets, disposition of differences between records and counts, etc.
- ✓ Consider “blind counts” or “surprise counts”:
 - Blind counts are inventory counts performed without its associated records
 - Surprise counts are inventory counts without prior notice
- ✓ Ensure completeness of counts:
 - Verify proper cut-off such as only counting assets that the department has custodial responsibilities over, items in-transit, items deemed retired but not removed from service, etc.
- ✓ Evaluate results
 - Compare/contrast records against physical counts, immediately review unexpected differences
 - Debrief/report to stakeholders
 - Modify policies/procedures to improve process

Management Response

WSS and WPCB will draft their respective LT5K policy within six months after the County’s policy is approved.

Responsible Party: WSS Bureau Chief and WPCB Bureau Chief

Estimated Completion Date: Six months after effective date of County Policy.

Issue	Risk Rating
Access to the Small Engine Shop – WSS	Low
<p>Access to the Small Engine Shop (the Shop) is not properly restricted. The WSS Bureau Chief and Small Engine Shop custodian advised Internal Audit that access rights granted to employees via card swipe or shop key wrists among too many employees. Furthermore, while performing test counts of the Small Engine shop, we noted the Shop door was open and employees were walking in and out. Management also advised me the log that documents the issuance and subsequent return of equipment is not updated at the time when an item is issued or returned but on a periodic basis.</p>	
Recommendations	
<p>Access to the Shop should be restricted to employees on an as-needed basis. On a regular basis, the WSS Bureau Chief should review current key card access rights as well as those who have an actual key and eliminate such access for those who do not need it. The Shop should be locked when a custodian is not present. Also, the sign-in/sign-out log must reflect each transaction on a current basis; doing so will promote accountability/movement of assets. After-hour entrance to the Shop should require a manager, supervisor, or security officer to accompany the employee needing to enter the Shop. In the remote instance where access is necessary for an employee who does not have access rights, a key should be obtained from the Control Center. A log should be maintained in the Control Center that documents who the key was issued to and the day and time it was issued and returned.</p>	
Management Response	
<p>WSS Bureau Chief has implemented the new access control process in early April through the Security System Manager by limiting the entry to the Small Engine Shop to Supervisors and above in the management team. The Head Mechanic continues to use the sign-in and out sheet for equipment check out. It has been the normal practice at the Control Center to log in/out for key access of warehouse and small engine shop.</p> <p>Responsible Party: WSS Bureau Chief Estimated Completion Date: Completed</p>	

Issue	Risk Rating
Furniture and Fixture Records- WSS	Low
<p>The furniture and fixtures inventory counts were manually entered on a pdf of a prior inventory listing prepared by a third-party vendor.</p>	
Recommendation	
<p>WSS should consider recording its furniture and fixture assets in an application that enables it to document the quantity, quality, location, condition and value of its assets on a continuous basis.</p>	
Management Response	
<p>Tracking is a centralized function through DES Facilities and Engineering Division. The tracking is not per unit of furniture but through monitoring replacement and repair orders for furniture per each business unit. Furniture and fixtures are effectively monitored via coordination with DES Facilities and Design Construction as well as review of financial activity toward identifying unexpected spend/replacement trends. The tracking and monitoring process currently in place provides the ability to account for furniture and fixtures at WSS. Furniture assets are noticeable and likely to be missed, if stolen, etc., and since all furniture orders are processed centrally through the DES Facilities and Engineering Division, irregularities are likely to be quickly discovered at the time of (re)ordering.</p>	
<p>A furniture tracking system could be introduced starting with installation of new furniture as part of the Court House Plaza interior renovation during CY 2020-2023. Additional Interiors Group resources would be needed to establish and continually monitor the data base, which would include tracking relocations of existing inventory as rearrangements occur and new inventory is added. Creating the data base for existing furniture would require outside resources to inventory furnishing in all County buildings. Such an activity could be initiated after a County-wide policy is created addressing inventory control and tracking for all LT5K assets.</p>	
<p>Responsible Party: NA Estimated Completion Date: NA</p>	

Issues	Risk Rating
Maintenance of LT5K Assets in MP2 – WPCB	Moderate
<p>Our testing identified the following:</p> <ul style="list-style-type: none"> ○ Various WPCB’s LT5K assets are maintained in MP2 along with other WPCB related assets. However, they are not designated as such nor is their cost basis included. In certain instances, the serial number and model number reflected on MP2 does not agree with its related asset. ○ LT5K furniture and fixtures and LT5K equipment on vehicles are not maintained on MP2. 	
Recommendations	
<p>Maintaining complete and accurate MP2 records would permit the WPCB to effectively track the location, quantity, condition and maintenance of its LT5K assets and provides a safeguard from theft, loss or mismanagement.</p> <ul style="list-style-type: none"> ○ The MP2 records should be revised to identify the LT5K assets and each asset’s cost basis. A review of the serial numbers and/or model numbers between MP2 and its related asset is necessary. MP2 should be revised as needed. ○ LT5K furniture and fixtures and LT5K equipment on vehicles should be recorded in MP2. 	
Management Response	
<ul style="list-style-type: none"> I. WPCB will designate all future LT5K assets in MP2. Minor modifications to MP2 will be required to make this designation possible – to be completed within 4 months if contract with vendor is in place. WPCB will work with DES to identify a proper tracking entity for furniture and fixtures – possibly centralize within DES. II. Furniture assets are noticeable and likely to be missed, if stolen, etc., and since all furniture orders are processed centrally through the DES Facilities and Engineering Division, irregularities are likely to be quickly discovered. If a more labor-intensive approach is desired, additional resources would be required on a Department and County-wide level. <p>A furniture tracking system could be introduced starting with installation of new furniture as part of the Court House Plaza interior renovation during CY 2020-2023. Additional Interiors Group resources would be needed to establish and continually monitor the data base, which would include tracking relocations of existing inventory as rearrangements occur and new inventory is added. Creating the data base for existing furniture would require outside resources to inventory furnishing in all County buildings. Such an activity could be initiated after a County-wide policy is created addressing inventory control and tracking for all LT5K assets</p> <p>Responsible Party: WPCB Bureau Chief for item I; NA for item II Estimated Completion Date: September, 2017 (item I)</p>	

Issue	Risk Rating
Workstation Tool and Equipment Inventory - WPCB	Low
There are no records that capture the quantity, cost or description of tools and other equipment located in the mobile tool cabinets.	
Recommendation	
An immediate physical inventory of such parts and equipment is necessary. Upon completion of the inventory, the results along with each item's cost and description should be entered into MP2. Upon issuance of workstation tools and equipment, each technician should sign an acknowledgement confirming the tools/equipment they have received for their workstation. Periodic, unannounced inventory counts should be completed as this is an effective measure to maintain proper accountability of such assets.	
Management Response	
WPCB will conduct a test inventory for practical application. The focus will be to inventory only unique or critical items of sufficient value.	
Responsible Party: WPCB and DES Estimated Completion Date: October, 2017	

BACKGROUND

Overview

Arlington County Department of Management and Finance (DMF) has an established policy where purchases of tangible assets with an initial, individual cost of less than \$5,000 and an estimated useful life of three years or less are expensed as incurred (“LT5K”). As part of the FY17 Internal Audit Work Plan, Internal Audit reviewed and tested the policies and procedures currently in place to account for LT5K assets.

OBJECTIVES AND APPROACH

Objectives

The overall objective of this review was to assess whether systems and processes are adequate and appropriate to permit the proper accountability of LT5K assets. Accountability is generally described as maintaining adequate records that permit the County to:

- Know the quantity, quality, location, condition, and value of assets
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Approach

The overall approach consisted of the following phases:

Understanding and Documentation of the Process

- Research current policies, procedures, and protocols
- Understand the processes in place to record, account for, and analyze asset activity employed by DMF, WSS and WPCB
- Conduct interviews with departmental leaders, process owners, and other necessary resources
- Obtain, review, and inspect relevant documents

Evaluate the Processes and Controls Design and Test Operating Effectiveness

The Process and Control Evaluation phase of this audit consisted of an evaluation of the design and operating effectiveness of LT5K processes. We performed walkthroughs and other detailed testing of transactions to achieve the audit objectives, including testing the processes currently in place. Procedures we performed include, but not limited:

- Review reasonableness of pricing (when possible)
- Compare, on a test basis, entries per records to physical inventory
- Test documents used to summarize inventory
- Observe inventory count (when possible)