

ABERDEEN CITY COUNCIL

COMMITTEE	Audit, Risk and Scrutiny Committee
DATE	26 September 2017
REPORT TITLE	Internal Audit Report AC1802 – Building Maintenance Year End Stock Checks
REPORT NUMBER	IA/AC1802
LEAD OFFICER	David Hughes
AUTHOR	David Hughes

1. PURPOSE OF REPORT

- 1.1 The purpose of this report is to present the planned Internal Audit report on Building Maintenance Year End Stock Checks.

2. RECOMMENDATION

- 2.1 It is recommended that the Committee review, discuss and comment on the issues raised within this report and the attached appendix.

3. BACKGROUND / MAIN ISSUES

- 3.1 Internal Audit has completed the attached report which relates to an audit of Building Maintenance Year End Stock Checks.

4. FINANCIAL IMPLICATIONS

- 4.1 There are no direct financial implications arising from the recommendations of this report.

5. LEGAL IMPLICATIONS

- 5.1 There are no direct legal implications arising from the recommendations of this report.

6. MANAGEMENT OF RISK

- 6.1 The Internal Audit process considers risks involved in the areas subject to review. Any risk implications identified through the Internal Audit process are as detailed in the attached appendix.

7. IMPACT SECTION

7.1 **Economy** – The proposals in this report have no direct impact on the local economy.

7.2 **People** – There will be no differential impact, as a result of the proposals in this report, on people with protected characteristics. An equality impact assessment is not required because the reason for this report is for Committee to review, discuss and comment on the outcome of an internal audit. The proposals in this report will have no impact on improving the staff experience.

7.3 **Place** – The proposals in this report have no direct impact on the environment or how people friendly the place is.

7.4 **Technology** – The proposals in this report do not further advance technology for the improvement of public services and / or the City as a whole.

8. APPENDICES

8.1 Internal Audit report AC1802 – Building Maintenance Year End Stock Checks.

9. REPORT AUTHOR DETAILS

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ABERDEEN

CITY COUNCIL

Internal Audit Report

Communities, Housing and Infrastructure

Building Maintenance

Year End Stock Take

Issued to:

Bernadette Marjoram, Interim Director of Communities, Housing and Infrastructure
Fraser Bell, Head of Legal and Democratic Services
John Quinn, Head of Land & Property Assets
Steven Whyte, Head of Finance
Kenny Don, Contract Manager
External Audit

EXECUTIVE SUMMARY

The Council's Building Maintenance Service is responsible for the repair and maintenance of Council Houses and Council Operational Buildings with works completed by in-house craft workers. The Service currently holds a stock of materials at 3 Depots (Kittybrewster, Hilton, and Kincorth) and within craft worker vans. There are approximately 1,800 different product lines held in stock at Kittybrewster while the other depots hold approximately 400 to 500 product lines each.

The objective of this audit was to provide assurance over the accuracy of the 2016/17 year end stock taking process and to review the stock procedures.

In general, the year end stock take controls were found to be robust and well managed. Areas identified for improvement included written procedures, control of stock count sheets, stock requisition scanning equipment, identification of counted stock, random stock take procedures and records, investigation and authorisation of write offs and stock take adjustments, and stock system average cost prices.

1. INTRODUCTION

1.1 The Council's Building Maintenance Service is responsible for the repair and maintenance of Council Houses and Council Operational Buildings. Works are completed by in-house craft workers (joiners, electricians, plumbers, painters, plasterers and masons). The Building Maintenance Service currently holds a stock of materials at 3 Depots (Kittybrewster, Hilton, and Kincorth) and within craft worker vans. There are approximately 1,800 different product lines held in stock at Kittybrewster while Hilton and Kincorth both hold approximately 400 to 500 product lines each. Seaton Depot was previously used for storing kitchen and bathroom stock required for the Scottish Quality Housing Standards upgrade of Council Houses. This Depot has since closed with stock and staff being relocated to the Kittybrewster Depot.

1.2 As at the 31 March 2017, stock to the value of £587,223 was held. A breakdown of stock valuations by location over the past three years is shown below.

	31 March 2017	31 March 2016	31 March 2015
	£	£	£
Kittybrewster Depot	399,133	394,545	331,818
Vans	88,236	50,446	79,485
Hilton Depot	62,889	66,955	66,772
Kincorth Depot	35,046	38,103	31,372
Seaton Depot	1,919	60,247	22,259
Total	587,223	610,296	531,706

1.3 The objective of this audit was to provide assurance over the accuracy of the 2016/17 year end stock taking process and to review the stock procedures.

1.4 The year-end stock take was completed on 24 March 2017. Kittybrewster Depot was visited on 31 March 2017 and a sample of stock items was selected and counted to determine accuracy. Procedures, stock count sheets and other relevant documentation was also reviewed.

1.5 The factual accuracy of this report and action to be taken with regard to the recommendations made have been agreed with John Quinn, Head of Land and Property Assets and Kenny Don, Contract Manager.

2. FINDINGS AND RECOMMENDATIONS

2.1 Written Procedures

- 2.1.1 Comprehensive written procedures and their effective communication are an essential element in any system of control. They are beneficial for the training of current and new employees and provide management with assurance of correct and consistent practices being followed, especially in the event of an experienced employee being absent or leaving.
- 2.1.2 In order to ensure that there is an accurate value for stock reflected in the Annual Accounts, the Service counts and values the stock at the year end. Written procedures cover all aspects of the year end stock taking process. These are provided by email to all staff involved in the count to ensure all concerned are aware of their roles and responsibilities. Procedures were reviewed and found to be comprehensive.
- 2.1.3 The Annual Accounts 2016/17 – Year End Procedures required Services to submit signed stock certificates to their Service Accounting contact by Monday 10 April 2017. However, these Procedures do not include an example stock certificate or explain what it consists of. It is therefore unclear what is expected of the responsible officers and there is a small risk that required information may not be provided. Finance receive stock valuation information required from the Service electronically, with signed stock count sheets being held by the Service.

Recommendation

The Annual Accounts Year End Procedures should be updated to reflect current practice and to include an example of what is required to be submitted to Finance.

Service Response / Action

Agreed.

Implementation Date

September 2017

Responsible Officer

Accounting Manager

Grading

Important within audited area.

- 2.1.4 In addition to the Annual Accounts Year End Procedures, Annual Stock Count procedures are issued by Finance to Officers in Charge of the stock counts. A declaration is included at the end of the Annual Stock Count procedures for Officers in Charge of counts to sign, date and return to Finance. This confirms the procedures have been received, read and understood prior to the stock count taking place. The signed forms have been requested from Finance and the Contract Manager but were not held.
- 2.1.5 As per the Annual Stock Count procedures, the personnel appointed to carry out the count at each location should be recorded on a Personnel Fact Sheet. This details count location / stock type; Officer in Charge and personnel taking stock. The Personnel Fact Sheet has been completed and the Kittybrewster Depot count included three Finance personnel independent of the day-to-day responsibility for stock being counted. The Contract Manager and Assistant Manager were present in an advisory capacity only as permitted by the Annual Stock Count procedures.
- 2.1.6 The Officer in Charge of the count is responsible for completing a Main Fact Sheet – Annual Stock Count form, detailing the location, time and dates of counts; the nature of stocks; the local officer in charge and their contact details. This should be returned to the Finance Partner before the counts take place, so the information can be made available to internal and external audit. A copy of the main fact sheets has been requested from the Service and Finance however this was not held.

- 2.1.7 The Annual Stock Count procedures state it is the responsibility of the stock count supervisor to ensure all count sheets issued to counters are returned at the end of the count. It is therefore recommended all stock sheets are pre-numbered and a log is maintained of issue and return, signed off by the count supervisor and retained for subsequent inspection. Stock count sheets had system generated batch numbers which could act as unique identifiers however a log of stock count sheets issued and returned was not maintained.

Recommendation

Confirmation of receipt of stocktaking instructions forms should be completed and submitted by Officers in Charge of counts, prior to the stock count taking place.

A Main Fact Sheet – Annual Stock Count form should be completed by Officers in Charge of stock counts and submitted to Finance prior to the counts taking place.

A log of stock count sheets issued and returned should be maintained for the year end stock take.

Service Response / Action

Agreed. This will be actioned prior to the next stocktake.

Implementation Date

September 2017

Responsible Officer

Contract Manager

Grading

Significant within audited area.

2.2 Depot Count

- 2.2.1 Internal Audit staff visited Kittybrewster Depot on 31 March 2017 to carry out a stock take on a sample of stock items and compare the results to the stock system, which had been updated to reflect the year end stock count the week before. Security arrangements were observed to be satisfactory, with authorised staff gaining access to the Depot using security key cards. In addition, high value mobile stock, e.g. showers, was stored in a cage locked by padlock under view of CCTV. It was confirmed no third party stocks were held at the Depot.
- 2.2.2 A report was provided to Internal Audit from the stock system showing all stock product lines held on site, without stock levels. A sample of 20 different stock items was selected from the stock report and a further 20 different stock items were selected from the shelves. These items were counted and then compared to the stock balances per the system. Since there were discrepancies a further 16 items were counted (8 from sheet to shelf and 8 from shelf to sheet). Counts were undertaken again where differences existed in order to confirm the differences found.
- 2.2.3 The physical count matched the stock system for 41 of the 56 stock items counted. It was established that 6 discrepancies were due to requisitions which were waiting to be processed, whilst a further 3 were due to estimations used for part used materials, resulting in minor differences. Six differences were unexplained.
- 2.2.4 The Service have advised that 4 of the stock items with stock count differences have since been recounted and the count agrees to the stock system. There was no movement on 2 of these items on 31 March 2017 when Internal Audit visited. The Service has been unable to ascertain the reason for differences between the stock count and count per the stock system but has suggested this could include requisitions not having been processed or stock not being located in the correct location.

Recommendation

Staff should be reminded to take care to keep stock in the correct location according to stock code.

Service Response / Action

Agreed. Staff will be reminded.

Implementation Date

September 2017

Responsible Officer

Contract Manager

Grading

Important within audited area.

- 2.2.5 The remaining 2 stock count differences could not be explained, with suggested reasons provided by the Service including stock may be wrongly located, or handheld devices for scanning stock, to record requisitions on the stock system, may have failed due to wireless connection problems in the Depot.

Recommendation

Failure of handheld scanning devices to record stock movements on the stock system should be referred to the supplier and ICT in order that this can be investigated and rectified.

Service Response / Action

Agreed. The Service will liaise with the systems team to resolve connectivity issues.

Implementation Date

April 2018

Responsible Officer

Contract Manager

Grading

Significant within audited area.

- 2.2.6 Completed stock count sheets were tested for the Depots. System generated, pre-numbered stock balance enquiry report sheets were used by count personnel to record quantities and the stock balance column of the report was blank to ensure a "blind" count. Count sheets for the Depots were all signed as required by the Annual Stock Count procedures.

- 2.2.7 The Annual Stock Count procedures require stocks already counted to be marked as such. This is to ensure that all stock is counted and that any obsolete items are identified. Stock counters and recorders should have coloured stickers or some other suitable means of marking stock that has been counted. On walking through the Kittybrewster Depot, it was noted that many items had not been marked as counted.

Recommendation

Stock already counted should be marked as such with a coloured sticker.

Service Response / Action

Agreed. Colour stickers will be used at future stocktakes.

Implementation Date

September 2017

Responsible Officer

Contract Manager

Grading

Important within audited area.

- 2.2.8 A breakdown of the differences between the stock count and stock system over the last three counts is shown below. Vans were excluded as this data was unavailable.

	31 Mar 2017		30 Sep 2016		31 Mar 2016	
	Net (£)	Gross (£)	Net (£)	Gross (£)	Net (£)	Gross (£)
Kittybrewster	523	16,613	1,149	15,832	7,015	85,733
Hilton	89	137	169	187	(442)	2,255
Kincorth	(29)	371	160	329	21	868
Seaton	-	-	45	1,309	(3,107)	9,063
	583	17,121	1,523	17,657	3,487	97,919

The gross variance has decreased by 17.5% of the year end stock balance at 31 March 2016 to 3.4% of the year end stock balance at 31 March 2017. The Contract Manager advised that due to the high instance of gross errors at the 31 March 2016 count, staff were brought in on the Saturday following interim and year end counts to recount stock with variances. This double checking of count variances has resulted in more accurate counts and a reduction in count variances as at 31 March 2017.

2.3 Van Counts

- 2.3.1 In addition to the stock held in the Depots, stock is held in craft workers' vans. As per the Building Services Valuation Summary, the value of the stock held in the vans on 31 March 2017 totalled £88,236. Stock count sheets for a sample of 5 out of 74 vans were reviewed. The Annual Stock Count procedures require all finalised stock count sheets to be signed and dated by the stock counter and recorder on the day the stock was counted. The count supervisor is then required to sign the stock sheets to evidence that they have been examined for clarity. This did not happen for the sampled vans.

Recommendation

Stock supervisors should ensure stock count sheets are signed as required by Annual Stock Count procedures.

Service Response / Action

Agreed. Checks will be introduced to ensure stock sheets are properly signed off.

Implementation Date

September 2017

Responsible Officer

Contract Manager

Grading

Significant within audited area.

2.4 Interim and Random Stock Takes

- 2.4.1 The Service advised that an interim stock take is carried out in September each year. All stock items in each of the Depots are checked (one per week). The Service also advised that random stock checks are carried out on a regular basis. The Service aims to count all stock randomly at least twice between interim and year end stock counts.
- 2.4.2 The Contract Manager advised the year end procedure is used for interim stock takes as the same process is followed. A procedure was not available for random stock takes. The process followed during random stock takes differs from interim stock takes in that the count is specific to particular items and count sheets were not observed to be used. A central record of stock checked and stock still to be checked is not maintained either. Lack of a random stock take procedure and record of counts due to be undertaken increases the risk that stock balances will be misstated due to counts being undertaken incorrectly or failing to be undertaken when required.
- 2.4.3 A staff list was not available for the interim stock count however the Contract Manager advised the same staff that undertook the 2016/17 year end stock takes undertook the

September 2016 interim stock takes. Staff lists should be prepared for interim stock counts to ensure all staff involved understand what is required and the health and safety of staff involved in the process is considered and addressed i.e. all staff issued procedures and required safety equipment.

<u>Recommendation</u>		
Random stock count procedures should be prepared.		
A record should be maintained of random stock counts undertaken and counts outstanding.		
Staff lists should be prepared for all counts undertaken.		
<u>Service Response / Action</u>		
Agreed. The Service will introduce a structured schedule of weekly stock balance checks.		
<u>Implementation Date</u>	<u>Responsible Officer</u>	<u>Grading</u>
September 2017	Contract Manager	Significant within audited area.

2.4.4 Count sheets were in place for a sample of 5 randomly selected stock items for Kittybrewster Depot, all stock items at Kincorth and Hilton Depots, and a randomly selected van. The sheets were each signed by 2 members of staff. All were dated with the exception of 1. It was noted a third signature was absent from all count sheets indicating either the counter, recorder or supervisor did not sign and date the count sheets as required by the procedure.

2.4.5 A list of random stock takes undertaken was provided and a random sample of 3 counts was selected and count documentation requested. Excel spreadsheets were provided showing the count results as compared to the original system stock balances. Signed count sheets were unavailable. In the absence of signed count sheets there is a higher risk of error since it cannot be demonstrated that there was segregation of duties between counting, recording and supervising the count.

<u>Recommendation</u>		
Random stock count sheets should be signed and dated by counters, recorders and count supervisors.		
<u>Service Response / Action</u>		
Agreed. The Service will ensure that count sheets are signed and retained for future checks.		
<u>Implementation Date</u>	<u>Responsible Officer</u>	<u>Grading</u>
September 2017	Contract Manager	Important within audited area.

2.5 Stock Adjustments / Write Offs

2.5.1 Following the stock counts, any variances noted are recounted the day following the count and variances are calculated in a spreadsheet. The Contract Manager stated variances exceeding 5% are investigated prior to approval by the Contract Manager. Once the count values have been verified, the final count figures are authorised and entered into the stock system by the Contract Manager. Signed recount sheets and the excel variance reports were provided to Internal Audit. A sample of 5 count variances exceeding 5% was selected and evidence of investigation into the reasons was requested from the Contract

Manager. Adequate reasons were provided for 4 of the 5 stock items. The unexplained difference was assumed by the Contract Manager to be due to a previous count being incorrect. Despite reasons being provided, evidence of investigation of stock count variances and authorisation of stock count adjustments is not maintained.

2.5.2 Obsolete or damaged stock should be held separately, written off and disposal plans made. Any stock which is required to be written off must be authorised by a senior member of staff prior to write-off. At the time of the count a shower was identified as being damaged. This was held within the office behind the Category Manager’s desk awaiting collection from the manufacturer. If stock is damaged, a remedial job number is requested by the Contract Manager to charge the write off to, unless the stock is being replaced by the manufacturer. The costing team then consider the request and provide a remedial job number, if appropriate. The damaged stock is then charged to the remedial job number in the stock system.

2.5.3 A list of stock returned to manufacturer or written off since 1 April 2016 was requested from the Contract Manager and the Finance Development Officer, to determine if authorisation was obtained for a sample of write offs. The Contract Manager advised there is no formal process for documenting the investigation and authorisation of write offs and stock count adjustments. A draft form was prepared during the course of the audit as a result, which documents the officer requesting approval for write off, position, date, item description, stock details, reason for disposal and method of disposal. A flow chart has also been prepared detailing the process to be followed and necessary authorisation. An equivalent form and process should be put in place to evidence investigation and authorisation of material stock count adjustments as a result of stock counts i.e. 5% as prescribed by the Corporate Governance Annual Stock Count procedure. A recommendation is included for tracking purposes.

Recommendation

The process for investigating and authorising write offs and stock take adjustments should be formalised.

A form for documenting investigations and authorisation of stock write offs and stock count adjustments should be prepared and made available to those concerned.

Service Response / Action

Agreed. A write-off procedure is now in place, and a stock adjustment procedure will be implemented.

Implementation Date

September 2017

Responsible Officer

Contract Manager

Grading

Significant within audited area.

2.6 Stock Valuation

2.6.1 The Annual Accounts 2016/17 – Year End Procedures state stock should be valued at the lower of cost or net realisable value. Cost is calculated using a weighted average cost, in line with the Code of Practice on Local Authority Accounting in the UK 2016/17. Stock is written off where required as detailed in paragraph 2.5.2, above, which should ensure the stock valuation is not overstated.

2.6.2 The Contract Manager explained that when an invoice is paid in the stock system, the price to be paid is compared to the average price held in the system. This ensures variances are monitored on an on-going basis facilitating investigation of material movements in price. A report of current to average price variances was requested to determine the number of variances exceeding 10%. The purchase price exceeded cost

price per unit by more than 10% for 119 of 1,319 different stock items delivered between 1 April 2016 and 6 June 2017. A sample of 5 variances was selected to establish the reason for variances. Reasonable explanations were provided in 3 cases for the difference. In 2 of the 5 cases the average price was incorrect. Incorrect average prices in the stock system increase the risk the stock balance is misstated in the Council's Annual Accounts.

Recommendation

Variances between stock average cost price and unit of issue cost price exceeding 10% should be investigated.

Service Response / Action

Agreed. The Service will develop a process for investigating variances over 10% on a regular basis.

Implementation Date

September 2017

Responsible Officer

Contract Manager

Grading

Significant within audited area.

2.6.3 The Service has provided detailed system stock reports to Finance showing quantity and valuation of stock by location for the Annual Accounts.

2.7 Reconciliation

2.7.1 A reconciliation of the ledger to the stock system is not undertaken. This is because the stock value in the balance sheet does not change in the ledger throughout the year with stock transactions only recorded in the stock system and the revenue ledger. Once the stock counts have taken place and adjustments recorded in the stock system, Finance adjust the ledger stock balance to agree to the stock system balance as at 31 March 2017. A reconciliation is therefore not required.

AUDITORS: D Hughes
A Johnston
A Mitchell

Appendix 1 – Grading of Recommendations

GRADE	DEFINITION
Major at a Corporate Level	The absence of, or failure to comply with, an appropriate internal control which could result in, for example, a material financial loss, or loss of reputation, to the Council.
Major at a Service Level	<p>The absence of, or failure to comply with, an appropriate internal control which could result in, for example, a material financial loss to the Service/area audited.</p> <p>Financial Regulations have been consistently breached.</p>
Significant within audited area	<p>Addressing this issue will enhance internal controls.</p> <p>An element of control is missing or only partial in nature.</p> <p>The existence of the weakness identified has an impact on a system's adequacy and effectiveness.</p> <p>Financial Regulations have been breached.</p>
Important within audited area	Although the element of internal control is satisfactory, a control weakness was identified, the existence of the weakness, taken independently or with other findings does not impair the overall system of internal control.