

FIXED ASSETS/INVENTORY CONTROL

Audit Report No. FA0109

July 30, 2009



**MENTAL HEALTH MENTAL RETARDATION
AUTHORITY OF HARRIS COUNTY**

Internal Audit Report

AUDITOR'S REPORT

Fixed Assets/Inventory Control

Harris County, Texas

Internal Audit Report

July 30, 2009

Henry E. Webb, CFE

Internal Auditor





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Re: Fixed Assets/Inventory Control
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BACKGROUND

The Mental Health and Mental Retardation Authority of Harris County (MHMRA) has formal policies and procedures designed to ensure control and oversight related to recording, valuing, reporting and safeguarding inventory and that fixed assets are adequately accounted for. These policies and procedures were created to provide a mechanism to monitor, by a centralized fixed asset management system (AssetWin), the accountability, care, and disposition of those assets.

The obligation of a unit director or department head is to ensure that the Agency property within their custody is subject to proper use, care, safe-keeping, and disposition. This is inherent by the assignment to that position at any level and includes ensuring the security of all property with that unit or department, whether idle or in use. Additionally, this includes monitoring subordinates to ensure that their activities contribute to the proper support and accountability of site assigned property.

The obligation of staff entrusted with Agency property is best described as an end-user that ensures its proper use, care, and safekeeping. Direct responsibility results from a documented assignment as the accountable person for that asset.

Personal responsibility or obligation for the asset is inherent by all Agency personnel to exercise reasonable and prudent actions regarding the proper use, care, and safeguarding of Agency property in their physical possession or care. This applies to all property issued, used, acquired, or converted to a person's exclusive use.

The following highlights the provisions found in Policy and Procedures **BUS-R/I: 1.1 – F/B: 3.4:**

- All property and equipment are assigned to a unit location
- If property or equipment is to be used off premises, written approval must be obtained
- Property and/or equipment signed out to an employee becomes the financial responsibility of that employee
- MHMRA property shall be inventoried according to guidelines developed and in compliance with the State Property Law

- The numbering of all MHMRA property is to be done with metal tags, decalcomania transfers, or cloth tabs
- The property will be assigned a unique sequenced number
- The Accounting Department will forward a copy of the Voucher and Invoice to the Fixed Asset Manager (source document)
 - ❑ Numbered Property Tag – Each item is to be assigned a number and an identification tag is affixed.
 - ❑ Non-Numbered Property Tag – A non-numbered identification tag is affixed to items of less than \$5,000 value.
 - ❑ Numbered Property Register – A numerical list of all property is maintained showing inventory number, unit number, location number, description of property, and value of item. The Fixed Asset Manager maintains the location register.
 - ❑ Numerical Listing of All Properties – This is to be furnished to each person responsible for property, at least once a year.
- On an on-going basis, the person responsible for property at the unit will be sent a list of all property that he/she is responsible for on the property records
- There will be a physical inventory on a test basis throughout the year. All units and departments will be inventoried at least once during the year
- The person responsible for numbered property will notify the Fixed Asset Manager and the Purchasing Officer in writing when any property becomes surplus
- The Purchasing Officer will transfer the surplus property to a locked, secured place
- The Purchasing Officer will also be responsible for all salvage property
- Receipts from Agency sales go into the General Fund

Currently, MHMRA utilizes the Fixed Asset System called AssetWin, and maintains all fixed assets and required inventoried items in this system. The State of Texas requires MHMRA to safeguard property as described in the Fiscal Year 2009 Performance Contract:

Article 16, Section 16.01 Equipment Purchases. *“Contractor shall implement a capitalization threshold for personal property at \$5,000. Contractor shall manage controlled assets, to include facsimile machines, telecopiers, stereo systems, cameras, video recorder/laserdisc players, televisions, video cassette recorders, camcorders, desktop and laptop computers, and non-portable printers.”*

Section 16.02 Property Inventory. *“Contractor shall maintain a nonexpendable personal property (i.e., equipment) inventory. Contractor shall administer a program of maintenance, repair, and protection of assets under this Contract so as to assure their full availability and usefulness.”*

MHMRA’s approach to asset management is to apply a standard business operating system through AssetWin regarding property control, accountability, responsibility, and general asset management. Additionally, management has tried to provide consistent asset transaction reporting procedures for maintaining and updating site inventory records.

In nearly every case, personnel employed by MHMRA are users of either fixed assets or those assets which require tracking. The policy and procedures provides specific guidance and procedures towards the proper use and care of such assets, including the disposition of stolen, lost, damaged or destroyed property. It further defines the accountability, responsibility, and liability of Agency personnel regarding property use, including the reporting of transactions necessary for the effective record maintenance of AssetWin.

Capital Assets

Capital assets with useful lives of more than one year are stated at cost. Donated capital assets are valued at their estimated fair market value on the date received. The Agency capitalizes assets with an initial, individual cost of \$5,000 or more. Depreciation is computed using the straight-line method over the estimated useful life of the assets. No depreciation is calculated on land. Depreciation expense on assets specifically identified with a function/program is included in its direct expenses, and the depreciation on shared capital assets are included ratably.

The following lives are used:

Buildings	45 years
Building Improvements	20 years
Furniture, Machinery, Vehicles and Other Equipment	5-20 years
<u>Telecommunications and Peripheral Equipment</u>	<u>10 years</u>

Table 1 presents total Capital Assets (Net of Depreciation) for FY 2007 – 2008.

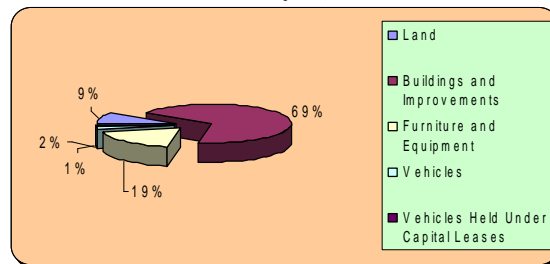
Table 1
MHMRA OF HARRIS COUNTY
Capital Assets (Net of Depreciation)
Fiscal Year 2007 – 2008
Unaudited

	<u>Fiscal Year</u> <u>2008</u>	<u>Fiscal Year</u> <u>2007</u>	<u>Increase</u> <u>(Decrease)</u>
Land	\$3,314,761	\$3,314,761	\$ -0-
Buildings & Improvements	14,176,580	15,098,891	<922,311>
Furniture & Equipment	622,188	925,585	<303,397>
Automobiles	182,496	157,345	25,151
Vehicles Under Capital Leases	484,013	335,560	148,453
Total Capital Assets	<u>\$18,780,038</u>	<u>\$20,032,142</u>	<u>\$<1,052,104></u>

Source: Agency CAFR for Fiscal Years Ended August 31, 2008 and 2007.

Exhibit 1 presents total Capital Assets as a percentage (%) by group.

Exhibit 1
MHMRA of Harris County
Total Fixed Assets as a Percentage (%) by Group
As of May 31, 2009



During the month of September 2008, MHMRA had a number of facilities damaged by Hurricane Ike. The majority of damage due to the storm was sustained at the main administrative offices at 7011 Southwest Freeway in Houston. Approximately two-thirds of the roof was lost and damaged due to wind and water was realized throughout the 6-story building. Carpet, ceiling grids, tiles, drywall, insulation as well as furniture and numerous electronic devices, such as computers, printers, monitors and copiers were rendered unusable.

Total damages to MHMRA property is estimated at \$6.2M, consisting of buildings, furniture and equipment. Reimbursement for all or the majority of damages is expected from MHMRA's insurance carrier, the Texas Council Risk Management Fund and from the Federal Emergency Management Agency.

OBJECTIVES

The overall objectives of the audit were to determine whether the departments:

- Managed and used resources in an efficient, effective, and economical manner
- Administered funds in compliance with applicable laws, regulations, policies and procedures
- Implemented internal controls to prevent or detect material errors and irregularities

The specific objective in this audit was to:

- Assist management with the assessment of the adequacy of internal controls related to recording, valuing, reporting, and safeguarding the Agency's inventory and fixed assets.

SCOPE

The scope of the work did not constitute an evaluation of the overall internal control structure of the units. The examination was designed to evaluate and test compliance with established policies and procedures and to test the internal control over tested areas and material. The audit scope was from September 1, 2008 through May 31, 2009.

Department management is responsible for establishing and maintaining a system of internal controls to adequately comply with approved policies and procedures. The objectives of an internal control system are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or theft, and that transactions are executed in accordance with management's authorization and are recorded properly.

Because of inherent limitations in any system of internal accounting control, errors or irregularities may occur and not be detected in a timely manner. Also, projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions, or that the degree of compliance with procedures may deteriorate.

The purpose of the audit report is to furnish management independent, objective analyses, recommendations, and information concerning the activities reviewed. The audit report is a tool to help management discern and implement specific improvements. The audit report is not an appraisal or rating of management.

Although due professional care in the performance was exercised, this should not be construed to mean that unreported noncompliance or irregularities do not exist. The deterrence of fraud is the responsibility of management. Audit procedures alone, even when carried out with professional care, do not guarantee that fraud will be detected. Specific areas for improvement are addressed later in this report.

Other minor findings, not included in this report, have been communicated to management and/or corrected during the audit process. Internal Audit would like to thank management and staff for their cooperation throughout the audit.

METHODOLOGY

In order to meet the objectives, Internal Audit flowcharted and evaluated controls over the acquisition, accounting, transfer and disposal of assets, and reviewed policies and procedures for compliance and completeness. MHMRA staff were interviewed and audit tests and procedures were conducted as considered necessary.

The sample size and selection were statistically generated using a desired confidence level of 95%, expected error rate of 5%, and a desired precision of +/-5%. Statistical sampling was used in order to infer the conclusions of test work performed on a sample to the population from which it was drawn and to obtain estimates of sampling error involved. When appropriate, judgmental sampling was used to improve the overall efficiency of the audit.

STATEMENT OF AUDITING STANDARDS

The audit was conducted in accordance with generally accepted government auditing standards (GAGAS). Those standards require that Internal Audit plan and perform the audit to afford a reasonable basis for the judgments and conclusions regarding the organization, program, activity, or function under audit. An audit also includes assessments of applicable internal controls and compliance with requirements of laws and regulations when necessary to satisfy the audit objectives. An audit also includes assessing the estimates, judgments, and decision made by Agency management. It is believed that this audit provides a reasonable basis for the findings, conclusions, and recommendations.

RESULTS

As a result of the audit procedures and surveys conducted, it was determined that controls over inventory and fixed assets generally meet Agency policy and procedures, that the controls are adequate and provide reasonable assurance that the Mental Health and Mental Retardation Authority of Harris County's fixed assets and inventory are accurately recorded, valued, reported, and adequately safeguarded. However, there were areas that were noted that needed improvement over internal controls. Those areas are discussed below.

FINDING

Electronic Signature and Forms

At the time of the audit, MHMRA owned or leased facilities with approximately 24 different addresses, and 67 Primary Fixed Assets Designees (FAD) assigned to provide control over the approximately 4,200 inventoried assets (excluding leasehold items). In most cases, each FAD has a backup to support the primary duties.

The breakdown of inventoried items to an individual FAD was from 2 items to as high as 988 (24% of assets assigned to one FAD), one FAD has the responsibility for 7 locations throughout Harris County (from Pasadena to Katy).

Each FAD has multiply responsibilities outside that of asset/inventory control, which contributes to the 27% error rate in documentation that was noted for the audit period.

RECOMMENDATION

- It is recommended that the Fixed Assets Department review the assignment of all FAD's and reallocate inventory control workload to provide a more efficient and economical allocation of staff time.
- It is recommended that the forms used for moving assets throughout the Agency system be temporarily automated and electronic signatures or scanned documents with signatures be delivered through email to one central "shared" folder.

As a possible long term solution, MHMRA Fixed Assets Department should explore the feasibility of a "workflow" process, whereby the automatic routing of electronic fixed asset documents and upload can be achieved.

Management Response

"We fully support moving the forms to an electronic process with an electronic method of approving, signing, and transmitting the forms to the Fixed Asset Department. This will alleviate the burden of searching for staff for signatures and eliminate the possibility of lost paperwork. The IT Department will work with the Fixed Asset Staff to develop a mechanism to process the forms electronically."

The Fixed Assets Department will work with the FADs to help distribute the workload per FAD/Unit. We will establish an average for which each FAD will be responsible and make the necessary changes to AssetWin.”

FINDING

Manual and Paper Intensive Reviews

The Physical Inventory Reconciliation is the most important phase of the inventory. Inventory counts will produce assets expected but not found, found but not expected and assets located in different locations than the database has indicated or under the control of a different unit than that indicated in the database.

Efficiency and accuracy are paramount in conducting inventory counts. The use of scanners affords both efficiency and accurate data when used properly.

Data Integrity

When assets tags are scanned, there is no doubt that the equipment was located. The scan automatically updates the building and room number, eliminating the potential for human error in making the changes manually. With a traditional printed inventory report, the tendency is to flip through the report looking for each item assigned to a room, a process called working "sheet to shelf". When an entire room of equipment is scanned any item not listed on the inventory will be located. These may include items that had previously been missing, or brand new items not yet added to the database, or even items listed in a different location.

Time Savings

The handhelds should save all Agency departments time. Conducting an inventory with the scanner will take less time than submitting a paper inventory report. They are relatively easy to use, and require less direction than a manual inventory. If a unit scans an item, Fixed Assets does not also have to physically verify it when performing the annual review.

Cost Savings

A variety of Inventory reports can be produced from AssetWin from the data received from the scanners. Less man hours, manual tracking and more analysis of problem areas can be conducted.

RECOMMENDATION

It is recommended that Fixed Assets conduct a “pilot” project utilizing a scanner for asset/inventory control. At a minimum, the project should result in the following efficiencies:

Use of a scanner should allow the Agency to identify fixed assets/inventory quickly and accurately. Once the barcode tags are in place, keeping the inventory up-to-date is painless. No more printouts and paper forms. Just scan and upload to keep on top of Agency inventory.

A barcode is applied to each asset the Agency owns. Using AssetWin software, the asset barcode is scanned, and information about the asset is directly entered onto the scanner. The software should allow you to enter data using the keyboard or stylus on a handheld barcode scanner, or scan in commonly used terms from a barcode sheet.

Track Assets by Location

The Fixed Asset Department can track assets by location using a hierarchical scheme.

Easily Upload to Asset Tracking Database

Once the initial information is completed, the scanner is usually placed into its cradle and the data is uploaded into the AssetWin database.

Review of Assets/Inventory

At any point, the Fixed Assets Department should be able to review the assets with improved accuracy and efficiency, by scanning the location and asset barcodes and uploading the scans. AssetWin will be able to provide information on where the assets are located, what assets are missing, what has moved, and who is responsible.

Management Response

“The IT Department purchased a wireless bar code scanner in June and began testing it with the initial adds of fixed assets. We have it fully functional for scanning the asset tag and serial numbers into the Add sheets. We will work with the Fixed Asset Department to develop a mechanism to use the scanner for transfer of equipment and future auditing of assets. This should speed up the process and ensure reliability of the data.

However, based on our experience, the recommendation to upload the data straight from the scanner may not function as well as expected and this will need further review. Currently, we have found that the wireless scanner can be used to scan directly into the electronic forms, then data is subsequently uploaded from the electronic form. The end result may be a hybrid scenario of these processes.

Regardless of which method is used, the end result will better ensure the integrity of our data. Our intention is to review the entire process including building an electronic method to process the forms and integrate the scanners into that process.”

FINDING

Agency Supplied Equipment for Contract Employees

On various occasions it is advantageous for the Agency to require services provided by independent contractors. An integral part of the contract details the terms, conditions and services that are to be provided by both the contractor and the Agency. To ensure a clear line of expectations, all contracts that may require use/loan of Agency equipment should detail the equipment to be furnished by both the contractor and the Agency.

Audit observations from the sampled selection provided one case where a outside contractor for the Agency was issued a laptop. It should be noted that the contractor was required to sign the Laptop Agreement Form; however, the contract with the individual did not contain any provisions for providing the equipment.

RECOMMENDATION

It is recommended that as the Agency's needs are frequently met by use of contractors, detailed information as to the various equipment needs of each party should be provided in the contract between the parties.

Management Response

“The contract for services will be revised to ensure that it stipulates the contractor's responsibility.”

FINDING

Policy and Procedures

The current Performance Contracts with the Texas Department of State Health Services (DSHS) and the Aging and Disability Services (DADS) provide the following guidance:

DSHS (as posted on their website 07/17/09): Article 16, Section 16.01 Equipment Purchases.

“Contractor shall implement a capitalization threshold for personal property at \$5,000. Contractor shall manage controlled assets, to include facsimile machines, telecopiers, stereo systems, cameras, video recorder/laserdisc players, televisions, video cassette recorders, camcorders, desktop and laptop computers, and non-portable printers.”

Section 16.02 Property Inventory. *“Contractor shall maintain a nonexpendable personal property (i.e., equipment) inventory. Contractor shall administer a program of maintenance, repair, and protection of assets under this Contract so as to assure their full availability and usefulness.”*

DADS: 107a: Capital Outlay – Expenses associated with the purchase of buildings, land construction in progress, building user fees, capital improvements, and leasehold improvements over \$2,500; purchase of furniture, equipment and vehicles with a purchase price of over \$2,500. Operating and capital leases associated with vehicles are also included in this category. Also includes computer hardware, software and related equipment with a cost of over \$2,500. Note: This item amount is more restrictive than what is allowed by UGMS.

DADS: 107b: Non-capitalized equipment – Expenses associated with the purchase of furniture, equipment and vehicles with a purchase price under \$2,500. Also includes computer hardware, software and related equipment with a cost under \$2,500.

Note: DADS’ monitors have communicated that the threshold will be amended to \$5,000.

Uniform Grant Management Standards (UGMS) – “...Requires records to be maintained with the description, serial number, source, title, acquisition date and cost, percentage of federal or state participation in the cost of the property, location use and condition of property. Physical inventory should be taken and a control system must be maintained to ensure adequate safeguards to prevent loss, damage, or theft of the property. Any loss, damage, or theft shall be investigated. Certain types of equipment are classified as “controlled assets.” Firearms must be maintained on the grantee’s or sub recipient’s inventory system irrespective of cost, and the following equipment with costs of \$500 or more must be maintained on the grantee’s or sub recipient’s inventory system...”

From documentation provided to the auditor, the contract submitted to DSHS contained changes that were not incorporated in the DSHS website version. **Section 12.20** (not included in the DSHS website version) provides: **Equipment (Including Controlled Assets) Purchases.** Equipment means an article of nonexpendable, tangible personal property having a useful lifetime of more than one year and an acquisition cost of \$5,000 or more, and “controlled assets.” Controlled assets include firearms regardless of the acquisition cost, and the following assets with an acquisition cost of \$500 or more: desktop and laptop computers, non-portable printers and copiers, emergency management equipment, communication devices and systems, medical and laboratory equipment, and media equipment.

For MHMRA purposes, property is categorized as either "capital," "controlled," or "non-capital" (expensed). Capital assets consist of non-consumable items having a value of five thousand dollars (\$5,000) or more. Controlled assets consist of non-consumable items having a value of up to \$4,999.99 per unit. Capital and controlled items are placed on the Agency's inventory system and are accounted for each year by a physical inventory. New acquisitions costing less than \$5,000 that do not meet the criteria for

capital or controlled equipment are considered non-capitalized. Department heads are also responsible for the custody, safekeeping, and proper use of such non-capitalized items.

RECOMMENDATION

- It is recommended that MHMRA of Harris County incorporate the following to provide fewer tracking requirements of items that are quickly immaterial and not cost effective for tracking.

Equipment (Including Controlled Assets) Purchases. Equipment means an article of nonexpendable, tangible personal property having a useful lifetime of more than one year and an acquisition cost of \$5,000 or more, and “controlled assets.” Controlled assets include firearms regardless of the acquisition cost, and the following assets with an acquisition cost of \$500 or more: desktop and laptop computers, non-portable printers and copiers, emergency management equipment, communication devices and systems, medical and laboratory equipment, and media equipment.

- It is recommended that the General Ledger Account posting codes need to be updated to reflect the current capital expenditures amounts of \$5,000 where appropriate in **Policy and Procedure BUS-R/I: 9.2:12.**

Management Response

“According to the guidelines, the State will allow us not to track items under \$500. The Fixed Assets Department will move forward with identifying these items to be removed. The department will then seek approval from the Unit, Senior Management and the Board prior to removing any items from the system. This will eliminate hours of staff time searching for small dollar items.”

-S-

Henry E. Webb, CFE, Internal Auditor

Cc: Rose Childs, MSW, CSWM, Deputy Director, Mental Health Division
Kenneth Collins, LMSW, Deputy Director, Mental Retardation Division
Barbara Dawson, MSE, Deputy Director, Comprehensive Psychiatric Emergency Program Division
Daryl Knox, MD, Medical Director, Comprehensive Psychiatric Emergency Program Division
Sarah Flick, MD, Medical Director, Mental Retardation Services
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Tom Hamilton, Ph.D. (Chairman)
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Charles O. Buckner, CPA
Vicki S. Raynold, CPA
Bob Borochoff

ATTACHMENT A
SUMMARY OF RECOMMENDATIONS
July 30, 2009

Unit: All		
Area: Fixed Assets and Inventory Control		
Inherent Risk:	Control Environment:	Overall Risk:
Low	Well Controlled	Low
Moderate	Acceptable	Moderate
High	Poorly Controlled	High
Type of Procedures: Audit		
Scope: * Using Internal Control Evaluation (ICEs) forms, documented the internal controls * Conducted a preliminary survey reviewing applicable policies and procedures, etc. * Interviewed various staff to obtain understanding of management controls * Examined detailed invoices/work orders, statements provided by the vendor, etc.		
Priority Rating:	Audit Recommendations:	
1	Create electronic signatures and forms	
1	Use scanner for inventory	
1	Provide details as to equipment provided by contractor vs. Agency	
1	Up date Policy & Procedures	
Follow-up: 2 years		

Priority Rating

1. Implement immediately (30 - 90 days) - Serious internal control deficiencies; or recommendations to reduce cost, maximize revenues, or improve internal controls that can be easily implemented.
2. Work towards implementing (6 - 18 months) - Less serious internal control deficiencies, or recommendations that can not be implemented immediately because of constraints imposed on the unit (i.e. budgetary, technological constraints, etc.).
3. Implement in the future (2-3 years) - Recommendations that should be implemented, but that can not be implemented until significant and/or uncontrolled events occur (i.e. legislative changes, buy and install major systems, or require third party cooperation, etc.).