

AUDIT OF CONTRACT No. 2017-055 EQUIPMENT, SUPPLIES, SERVICES, AND INVENTORY MANAGEMENT SOLUTIONS

April 2021

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EXECUTIVE SUMMARY

The Clerk of Circuit Court and County Comptroller's *Internal Audit Department and Office of the Inspector General* conducted an independent audit of Contract No. 2017-055 Term Contract for Fleet-Related Maintenance Equipment, Supplies, Services and Inventory Management Solutions. The audit was conducted at the request of County Administration. The purpose of the audit was to evaluate the effectiveness of processes used by the County to monitor for compliance with the terms of the contract.

The audit detected non-compliance with the following contractual stipulations related to:

- Plan pricing,
- NAPA Product Cost,
- Gross profit rate,
- Supporting documentation,
- Inappropriate purchases, and
- Review process for NAPA invoices.

The contractually stated gross profit rate and calculation provided are incongruent. NAPA product costs are not available and NAPA invoices do not clearly define NAPA product costs or Non-NAPA product costs. Additionally, there is a lack of review and monitoring as it relates to the gross profit rates paid and the supporting documentation provided with the invoices, which could result in inappropriate purchases and the County over paying for parts and services.



BACKGROUND AND OBJECTIVES

The Clerk of the Circuit Court and County Comptroller's *Internal Audit Department and Office of the Inspector General* has completed an audit of Contract No. 2017-055 Term Contract for Fleet-Related Maintenance Equipment, Supplies, Services and Inventory Management Solutions. The audit was planned and conducted in conformance with the *International Standards for the Professional Practice of Internal 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 the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. The purpose of the audit was to determine compliance with the terms of the contract.

Background

Sarasota County entered into an equipment, supplies, services, and inventory management solutions agreement (Agreement) with the Genuine Parts Company. The initial Agreement, Contract No. 2011-550, was entered into on September 13, 2011. A second Agreement, Contract No. 2017-055, was entered into on December 1, 2016, and continues to be in place until November 30, 2020. This agreement has been amended twice with an amendment on September 25, 2017 which lowered the gross profit from 10% to either 8% or 6% based on the invoice amount for "outside" purchases or services. The current Agreement may be renewed for up to one additional one year period subject to written agreement of both parties.

The contractor is required to maintain and operate three vehicle and equipment maintenance parts facilities (on-site stores) at existing Fleet Services facilities throughout Sarasota County during normal working hours, five days a week Monday through Friday. The County is invoiced for all inventory purchases pursuant to the Agreement on a monthly basis according to the pricing plan in Exhibit B of the Agreement. The overall goal of the pricing plan is to achieve a 10% net profit for the contractor by adjusting the pricing for two elements, Product Costs and Operational Costs.

Product Costs can be broken down by either "NAPA Product Costs" or "Non-NAPA Product Costs". NAPA Product Costs use the pricing of NAPA supplier manufactured products. Non-NAPA Product Costs use the pricing of products which have not been manufactured by NAPA suppliers but which have been acquired for the County by the Contractor pursuant to the Agreement. Non-NAPA Product Costs also include any "outside" purchases or services, which

may be billed at 8% or 6% based on the invoice amount. Operational Costs are any and all cost and expenses associated with the operation of the on-site stores.

The audit focused on reviewing supporting documentation for both product and operational costs billed to the County. Between the period of October 1, 2017 through April 3, 2020, there were a total of 484 paid invoices that were billed to 23 Purchase Orders related to Contract No. 2017-055. Each of these invoices typically contains multiple individual purchases.

Objectives, Scope and Methodology

The objectives of this audit was to determine that policies and procedures are in place and documentation is available to support the effective and efficient administration of the Agreement.

To meet the objectives of the audit, the procedures performed included, but were not limited to, the following:

- Obtained an understanding of the contract and amendments.
- Performed inquiries of responsible personnel.
- Selected a statistical random sample of 214 invoices and reviewed at least two individual purchases within each invoice.
- Evaluated documentation for compliance with provisions of the Agreement.
- Identified opportunities for improvement.



OPPORTUNITIES FOR IMPROVEMENT AND MANAGEMENT RESPONSES

The audit disclosed certain policies, procedures, and/or practices that could be improved. The audit was neither designed nor intended to be a detailed study of every relevant system, procedure, or transaction. As a result of the audit, observations and recommendations identified below are related to *Standards*:

- (Standard 2110) Ensuring effective organization performance management and accountability,
- (Standard 2120.A1) Effectiveness and efficiency of operations and programs, and
- (Standard 2130.A1) Effectiveness of controls, particularly compliance with laws, regulations, and contracts. As well as, compliance with policies and procedures and the reliability and integrity of financial and operational information.

The **Opportunities for Improvement** presented in this report may not be all-inclusive of areas where improvement may be needed. There were six *Opportunities for Improvement* identified as a result of the audit:

1. **Plan Pricing Summary**
2. **NAPA Product Costs**
3. **Gross Profit Rate**
4. **Supporting Documentation**
5. **Inappropriate Purchases**
6. **Review Process for NAPA Invoices**

1. Plan Pricing Summary.

Observation

In Exhibit B of the Agreement, the “Fee Schedule”, refers to a Price Plan Summary which outlines the net profit rate that the contractor is to bill the County for product costs. Language in the contract states that NAPA product costs and Non-NAPA product costs are to be billed to the County at a 10% gross profit rate, unless the Non-NAPA product cost is listed as an “outside” product or service. Any “outside” purchase would result in either an 8% or 6% gross profit rate, based on the amount of the invoice. However, directly underneath the language that states a 10% gross profit rate, a calculation is also provided that states the gross profit is to be calculated by the “acquisition cost divided by .9”. The auditor determined that the gross profit rate is actually 11.1% when using this calculation.

Recommendation

The County should review the contract and determine which gross profit rate was intended and then the language and calculation should be modified so that they are both in alignment.

Management Response

Amendment No. 3 was approved September 9, 2020 by the BCC, with a new “Gross Profit” Rate amount of 8% on NAPA products costs, Non-NAPA product costs, and “Outside” products or services. The new pricing will be effective October 1, 2020.

As stated in the Amendment, the “Gross Profit” is calculated by dividing the Current NAPA Jobber Acquisition Cost by 0.92. The Fleet Services Division has reviewed this calculation and confirms that this is an accurate methodology for calculating the Agreement “Gross Profit.” “Gross Profit” is based on a percentage of the delivered price; markup is based on a percentage of the vendor cost.

In addition, the Fleet Services Division has adopted a new Internal Procedures that include purchase threshold approvals for high-cost items. Any item purchase of \$250,000 or above requires approval from the Generals Services Director. Items costing \$50,000 or more require approval from the Facilities and Fleet Operations Manager. All other items are approved and reviewed weekly by the Fleet Manager or Assistant Fleet Manager. Furthermore, the monthly audit of the profit rate charged and verifies the “Gross Profit” on “outside” service invoices with supporting documents showing vendor cost are attached prior to submitting to the Clerk’s Office. NAPA has created a monthly report that reflects the vendor cost of the product sold and the delivered price of the product which will be utilized for the monthly audit.

2. NAPA Product Costs.

Observation

In Exhibit B of the Agreement, the “Fee Schedule”, refers to the contractor being able to bill the County at a specified gross profit rate. The contract states that NAPA Product Costs are to be “billed to the County at a 10% gross profit rate.”

The contractor provides County staff with access to a live database that shows pricing for over 750,000 parts. After an order is processed, the County is invoiced and the prices are based on the live database prices. The auditor obtained access to the database and reviewed details related to pricing listed in the database. Each part listed includes the List price and the Cost price. The Cost price is what the County pays when they order from the contractor.

It appears the County is receiving a discounted rate. However, based on the pricing provided in the database, there is no way to determine if the contractor is yielding a gross profit of 10% on NAPA Product Costs. Additionally, there is no documentation being retained that would indicate the list price at the time of the purchase.

Recommendation

The County should require the contractor to include their cost for parts listed in the database, or consider modifying the language of the contract to reflect the percentage discount the County is entitled to that would approximately equate to yield a gross profit of ten percent.

Management Response

The NAPA billing system does not have the capability to show the vendor cost on the invoice. However, NAPA has created a monthly report that reflects the cost of the product sold and the delivered price of the product. The Fleet Services Division has adopted a new Internal Procedure that includes a monthly audit of this report and verification that the correct Profit rate was charged.

3. Gross Profit Rate.

Observation

In Exhibit B of the Agreement, the “Fee Schedule”, refers to the contractor being able to bill the County at a specified gross profit rate. The contract states both “NAPA Product Costs and Non-NAPA Product Costs shall be set by the Contractor to yield a gross profit of ten percent (10%).” However, in the first amendment, on September 25, 2017 “outside” purchases and services (Non-NAPA Product Costs) are to be charged a gross profit rate of 8% for purchases under \$25,000 and 6% for purchases over \$25,000.

The auditor identified a total of 484 paid invoices against Purchase Orders issued between Fiscal Year 2018 and 2020. Of those paid invoices, a statistical sample of 214 paid invoices were selected for review. Each invoice batches multiple invoices into a single invoice that is applied to a Purchase Order.

Upon review of the 214 sampled invoices and supporting documentation, it was determined that 13 individual invoices (or 6.1%) exceeded the allowed gross profit rate. This resulted in an overpayment of \$1,584.

Recommendation

To ensure compliance with the contract, the County should review and verify the gross profit rate of each invoice prior to approving them for payment.

Management Response

The Fleet Services Division has adopted a new Internal Procedure that includes a monthly audit of the Profit rate amount, and verification of the “Gross Profit” calculation on “Outside” service invoices where supporting documents showing vendor cost are attached prior to submitting to the Clerk’s Office. NAPA has created a monthly report that reflects the cost of the product sold and the delivered price of the product.

4. Supporting Documentation.

Observation

Section 8.2.1 of the contract states “invoices shall contain a complete account of all activity for the month ending, including, but not limited to:

- a. part numbers
- b. quantity sold
- c. cost of parts sold to the County
- d. cost of delivery (shipping & handling) for County pre-approved special order requests on direct charge and/or non-stock items as specified in this Term Contract”

As a result of the testing methodology identified in *Opportunity for Improvement No. 4 – Gross Profit Rate*, it was determined that 10 individual invoices (or 4.7%) either:

- failed to provide any supporting documentation, or
- provided supporting documentation that:
 - did not match with the invoice,
 - was not complete,
 - was scanned in and left off the cost, or
 - did not provide any description as to what was being purchased other than part numbers.

Recommendation

In order to ensure compliance with the contract and to make the invoices clear for reviewers, the County should require that all invoices are supported with documentation that:

- is complete and matches the invoice,
- includes legible parts numbers, item descriptions, quantities sold, and costs, and
- includes a description of what was purchased.

Management Response

Fleet Services management will ensure the vendor follows the new contract Amendment Scope of Services – Section 8.0 Billing. The Fleet Services Division has adopted a new Internal Procedure that includes review and verification that all supporting documentation is attached and meets the recommended criteria.

5. Inappropriate Purchases.

Observation

In Exhibit A of the Agreement, Section 6.0 states that the “Contractor shall provide/coordinate technical (mechanical) training to County employees as deemed appropriate for use of new or current products. The cost, if any, for such training will be mutually agreed upon in writing by the county and the Contractor via an amendment to this Agreement”.

As a result of the testing methodology identified in *Opportunity for Improvement No. 4 – Gross Profit Rate*, it was determined that there were a total of four transactions, totaling \$37,478.11 that appeared to be inappropriate purchases against the contract. The four transactions were listed below:

- Two purchases were related to an agreement with Stryker (\$13,746.24),
- One purchase was related to an agreement for the Fuel Island (\$15,091.87), and
- One purchase was related to vendor training (\$8,640).

The auditor determined that the purchase related to the Fuel Island was erroneously paid against a Purchase Order associated with Contract No. 2017-055. The error was identified and a refund for the full amount was returned to the County.

Upon review of the two amendments, a mutually agreed upon price for training was not included in either amendment. Additionally, the other three purchases were for two different maintenance agreements, which appears they should not have been paid against this agreement.

Recommendation

To ensure compliance with the intent of the agreement, the Fleet Department should monitor purchases to ensure that they meet the contractual requirements in order to be purchased using the agreement. If future training is to be purchased through the agreement, ensure the cost is mutually agreed upon by both parties and that the agreement is amended to include the agreed upon cost of training.

Management Response

First, in reference to the Stryker maintenance agreement passed thru NAPA, Fleet Services management acknowledges that this was purchased through NAPA. In the future, we will look to other procurement methods that may be more appropriate for these or similar services.

Second, regarding the Mansfield document noted on the backup documentation that was provided to Fleet Services, Fleet identified an error where NAPA had mistakenly paid the invoice. After identifying this error, the County received a full refund. This invoice was purchased under Mansfield PO 183793.

Third, Fleet Services management acknowledges an oversight in not obtaining an Amendment for the cost of the mentioned vendor training, Fleet Services will comply with the NAPA Agreement regarding any training in the future.

In addition, as a part of the new Internal Procedure, the Fleet Manager will be directly monitoring purchases that are made utilizing this agreement.

6. Review Process for NAPA Invoices.

Observation

NAPA creates weekly invoice packets, separates the purchases by each of the three locations, and then sends an excel spreadsheet to the Fleet Department. The spreadsheet includes the invoice number, date, amount, and corresponding purchase order. The Fleet Administrative Specialist will then update the spreadsheet with the week ending date and break down each individual purchase into different “Line” items that reflect the different costs that are allowable under the contract (i.e. – parts, labor, and service costs). NAPA then provides the Fleet Department with a coversheet for the weekly invoice packet which includes information such as:

- Purchase Order No.
- Contract No.
- Account No.
- Invoice No.
- Statement Date
- Detailed Line Item Amounts
- Total Invoice Amount

The auditor determined that the Fleet Department has written procedures in place for processing NAPA invoices. The procedures requires a Fleet Manager to review each weekly invoice packet. However, when the auditor met with the Fleet Administrative Specialist and the Manager II, they stated that after the Administrative Specialist receives the coversheet and weekly invoice packet, the Administrative Specialist reviews it and submits it to the Finance Department without manager review as required in their procedures.

Recommendation

To help ensure the County is reviewing and monitoring NAPA purchases, the Fleet Department should include a statement, preparer’s signature, and reviewer’s signature on the Coversheet. Per the department procedure, the Fleet Manager should be reviewing and approving all invoices. Additionally, the procedure should also require that the manager is to sign each invoice to document the approval process.

Management Response

Fleet Services will include a coversheet on all weekly packages including the preparer's signature and the Management Reviewer's signature. In addition, the Fleet Services Division has adopted a new Internal Procedure that includes a monthly audit of the Profit rate charged and verifies the "Gross Profit" on "outside" service invoices where supporting documents showing vendor cost are attached prior to submitting to the Clerk's Office. This monthly audit will also include a coversheet with the Auditor's and Manager's signatures.

