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TO: Gene Herndon

DATE: April 18, 1978

FROM: Rex Wood

SUBJECT: Dallas Audit

The Dallas branch was audited the week of March 27, 1978. Excellent cooperation was received during the visit.

The following is a listing of major exceptions noted during the audit:

- Extension errors were found on C.O.D. sales orders. Payments to differ from the invoiced amount.
- Credit limits were exceeded which pointed out a need for better credit approval procedures and a need to update limits.
- Tax exemption certificates need updating.
- Truck leasing charges were paid at rates differing from the contracted price.
- Caustic Soda 50% is being lost or usage is not being reported properly.
- Better controls are needed in reporting production.
- Driver's logs are not being properly prepared.
- Truck usage is not being reported properly.
- Several safety violations were noted.

Details of our findings are listed in the attached SUMMARY OF REVIEW.

Rex
Rex Wood

RW:cjb
Attachment

Subj. to Stipulation of Confidentiality &
Order, *Sowle, et al. v. A.P. Green*
Refractories, et al., Jackson County, MO.
Case No. 800-CV-307056

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SUMMARY OF REVIEW

I. FINANCIAL REVIEW

Branch Operating Statements for 1976, 1977, and the first quarter of 1978 were reviewed and major income and expense categories were compared as follows:

<u>Descriptions</u>	<u>Y.E. 12/31/76</u>		<u>Y.E. 12/31/77</u>		<u>1st Qtr 1978</u>	
	(000) \$	% Reg Sales	(000) \$	% Reg Sales	(000) \$	% Reg Sales
Regular Sales	\$5,668 cr	100.0%	\$6,125 cr	100.0%	\$1,558 cr	100.0%
Direct & Inter Co. Sales	2,971 cr	-	3,275 cr	-	1,023 cr	-
Total Sales	\$8,639 cr	-	\$9,400 cr	-	\$2,581 cr	-
Gross Profit	1,522 cr	-	1,782 cr	-	462 cr	-
Margin	17.6%	-	-	-	17.9%	-

Expenses

Freight Out	86	1.0%	111	2.0%	32	2.1%
Total Selling Expense	295	3.4%	269	4.4%	81	5.2%
Total W/D Expense	417	4.8%	436	7.1%	97	6.2%
Total L & O Applied	67	0.8%	78 cr	(1.3)	24 cr	(1.5)
Net W/D Expense	350	4.0%	358	5.6%	73	4.7%
Total Office Expense	1.1	0.0%	72	1.2%	17	1.1%
Total Operating Expense	853	14.2%	794	12.7%	206	13.2%
Total Operating Profit	786 cr	9.5%	680 cr	11.1%	207 cr	13.3%
Return on Assets Managed	11.1%	-	24.7%	-	7.4%	-

Regular sales increased \$57,087 between 1976 and 1977 and the Gross Profit Margin increased 1.1%. Major expense categories have shown a decline as a percent of regular sales except freight out which has increased companywide due to freight rate increases.

- It appears that the branch is financially sound and has shown some growth to date.

II. CASH REVIEW

A listing of all open cash and C.O.D. sales at 3/21/78 was reviewed and cash sale procedures were examined.

There were (6) extension errors on C.O.D. sales orders which made the payment amount differ from the invoiced amount. All the errors noted involved TMD customers.

Recommendation: A procedure should be set up to double check extensions on C.O.D. sales orders. A final check of extensions should be made by a second person before the sales order is released to the warehouse.

III. CREDIT AND COLLECTION

The Aged Trial Balance of 3/1/78 and credit approval procedures were reviewed at the branch.

The Aged Trial Balance had (14) accounts with no credit limits and (43) accounts were over the printed credit limits. Kardex files used to reference customers did not list the credit limits for all customers.

Recommendation: The Branch Manager should request updated credit limits from the Kansas City Credit Manager for all accounts with no credit limits or those accounts that need a higher limit. Kardex files for all customers should include the updated and approved credit limits.

IV. CREDIT SALES ORDERS

A procedural review was performed concerning the issuance of credit sales orders.

It was noted that some return reports for 150 pound chlorine cylinders noted that full cylinders were returned by customers. It was difficult for the clerk to determine if credit or merchandise credit was due on the return report.

Recommendation: Return reports should be noted whether or not merchandise credit is due and the reason for the return. Warehouse personnel should be instructed to include this information on return reports.

A Quantity Change Report was not being prepared for full 150# chlorine cylinders when merchandise credit is given. Since the credit puts the merchandise back into inventory and it is subsequently "sniffed", these returned cylinders should be deducted from inventory.

Recommendation: The clerk preparing credits for returned cylinders should bring the credits involving merchandise returns to the attention of the clerk preparing quantity changes so that they may be written off. It was also suggested that 150# chlorine cylinders be included on the next monthly cycle count so inventory can be corrected.

V. DEBIT SALES ORDERS

The sales order procedures at the branch were reviewed for proper controls. Also, tax exemption certificate files were reviewed for (65) customers granted exempt status.

Of the (65) customers granted exempt status, (7) had no exemption certificate on file at the branch.

Recommendation: Tax exemption certificate files should be updated to assure that all customers granted exempt status have a certificate on file.

VI. IMPREST CHECKS

Imprest checks written in 1978 were reviewed for propriety and proper coding.

It was found that Hudgins Truck Rental was billing the branch for leased vehicles per the lease agreement rates effective January 1, 1978. The billed rates on the regular units appeared to be below the contract price while the billing for mileage on substitute units appeared to be excessive in most cases. The billed rates and contract rates are as follows:

Unit #	Billed		Per Contract	
	Monthly Rate	Mileage Rate	Monthly Rate	Mileage Rate
2051, 2052, 2053	\$185.00	.087	\$191.00	.090
2479, 2480, 2481	117.00	.1020	123.00	.1050
2888	196.55	.0840	204.55	.0880
<u>Substitute Unit</u>				
for: 2051 & 2052	\$185.00	.0970	\$191.00	.090
		.1140		
for: 2479	117.00	.0970	123.00	.1050
for: 2480	117.00	.1140	123.00	.1050
for: 2481	196.55	.1140	204.55	.088

Recommendation: The clerk paying leasing invoices should check the invoices to assure that they are priced per the contract. This exception was brought to the Branch Manager's attention.

Imprest check stock was stored in an unlocked storeroom.

Recommendation: Blank imprest checks should be locked up to avoid easy access.

VII. PRODUCTION ORDERS

A review of production order procedures was performed to determine if controls were adequate.

Bleach and acid filling operations are performed in the plant area then, the plant worker comes to the office to report the production performed. There is the possibility that plant personnel might neglect to report some production.

Recommendation: No production should be performed without a production order number being assigned in advance. Blank production orders should be given to the warehouse area. If, before production is performed, the office should assign and log a number to the production. When production is completed, a log should be noted and the production order should be completed.

A shortage of 44,030 pounds of 50% Caustic Soda occurred at physical inventory in 1977. The product was cycle counted in February, 1978 and it was found that again this product was short 44,031 pounds since physical inventory in 1977. The storage tank is leaking but it is doubtful that this could account for the sizeable shortage. We feel that the shortage is developing due to failure to realize proper useage when producing 20% Caustic.

Recommendation: It is recommended that the 50% Caustic tank be measured before and after the next pumping to the 20% cutting tank. Useage from the 50% tank should be compared to useage reported on the 20% tank to determine if the amounts are comparable. Also, 50% Caustic should be cycled throughout the year to determine if further losses are occurring.

VIII. TRANSPORTATION

A. Truck Inspections

A safety inspection was performed on the vehicles at the branch.

The following exceptions were noted during the vehicle inspections:

	<u>Exceptions</u>
Tractor # 019	Turn signals and brake lights inoperative.
Bobcat # 300	Right turn signal inoperative, fire extinguisher needed a recharge.

Recommendation: These exceptions were pointed out to the Branch Manager for correction.

B. Driver's Logs

Driver's logs for January, 1978 were examined for proper preparation.

The following exceptions were noted on driver's logs:

<u>Drivers</u>	<u>Exceptions</u>
William Calhoun	No safety inspection noted for (6) days of driving during the month.
Martin Braswell	No logs had been prepared.
Chester Duke	No logs had been prepared.
Orville McKim	1-6-78 showed 210 miles driven in 3.5 hours for an average of 60 mph. 1-7-78 showed 140 miles driven in 2.0 hours for an average of 70 mph. 1-26-78 showed 365 miles driven in 5.0 hours for an average speed of 73 mph.
Sherman Weatherford	Failed to note safety inspections and list sales order numbers on logs for the entire month.

Recommendations: Logs should be prepared for each driver, each day they drive per Mr. Ralph Wiley's letter of November 18, 1977. Exceptions noted should be discussed with each driver so they can be corrected.

IX. TRUCK TRIP REPORTS

Truck trip reports for January and February, 1978 were reviewed for proper preparation.

Truck trip reports were not being prepared for each unit, each day, as required per Mr. Ralph Wiley's letter of November 18, 1977.

Suggestion: Usage of each vehicle for each day must be reported. If a vehicle is not used on a particular day, a truck trip report should be prepared and noted "Not Operated".

X. SAFETY

Files for required OSHA reports were reviewed and a safety inspection was performed at the branch. The following exceptions were noted.

1. One fire extinguisher was missing at a marked extinguisher station.
2. A leaking drum of Aqua Ammonia had not been repacked.

3. There was no warning sign in the asbestos storage area. Shrink packs had been removed on (12) skids of asbestos from a damaged shipment and material was leaking on some of the skids.
4. Required tests of the air in the asbestos storage area had not been taken.
5. There was trash and dented drums of material on the grounds around the warehouse.

Recommendation: These exceptions were pointed out to the Branch Manager for correction.

XI. PERSONNEL

A listing of branch personnel at the branch was prepared by Kansas City Payroll and checked to personnel at the branch.

It was found that 1977 vacations had not been reported to the Payroll Department for all salesmen at the branch.

Recommendation: Form T-12 should be completed any time an employee is to be absent from work. This form should be forwarded to the Kansas City Payroll Department so accurate attendance records can be maintained. The Branch Manager stated that the forms had been completed but had not been sent to Kansas City.