



CITY AUDITOR 345 6th Street, Suite 100, Bremerton, WA 98337-1873 & Phone (360) 473-5369

September 2, 2022

To Audit Committee Members:

Deborah McDaniel, Citizen Member, Audit Committee Vice Chair
Maxim Sinitsa, CPA
Jeff Coughlin, Council Member, Audit Committee Chair
Quinn Dennehy, Council Member

Re: Gold Mountain Golf Pro Shop Inventory – Internal Audit

Dear Audit Committee Members:

At your request and based on the information available to date, I hereby submit my internal audit findings regarding the golf shop inventory at Gold Mountain Golf Course Complex (“GMG”). Primary sources of information relied on for this report are listed in [Exhibit 1](#), attached.

RISK

In the retail industry, losses due to shoplifting and employee theft can be a significant concern. The GMG pro shop carries appealing merchandise, including good quality apparel, golf clubs, and related gear that is at risk for these types of losses. Administrative errors can also be a concern in the retail industry if controls are inadequate to detect them.

Another risk in retail is carrying too much or too little inventory. When a retailer overstocks, it may need to discount product to move it. When a retailer understocks, it may miss out on sales.

SCOPE AND OBJECTIVES

The general objectives for this review were to provide reasonable assurance that:

- Segregation of duties and other internal controls are designed to safeguard inventory
- Physical safeguards are in place to reduce risk of theft of pro shop inventory
- Pro shop inventory is reasonably stocked based on the Inventory Turnover Rate



SUMMARY OF FINDINGS

In summary and based on the review outlined in this report, following are my findings.

1. CHI staff are unable to generate an inventory shrinkage cost report from its point-of-sale system, Lightspeed. If the cost of shrinkage cannot be reported from Lightspeed, management should consider an alternative way of tracking inventory shrinkage so it can be monitored. (Refer to [Inventory Shrinkage](#))
2. Several issues relating to segregation of duties were noted. These issues can be resolved by re-aligning staff and/or increasing approval processes or oversight. (Refer to [Segregation of Duties](#))
 - a. Purchasing: A manager should review and approve orders before they are placed to ensure they are reasonable.
 - b. Receiving and recording: Independent spot checks should be conducted to confirm ordered items were received and recorded in inventory records.
 - c. Adjusting inventory levels: Management should approve adjustments and/or require a two-person process for adjustments.
 - d. Conducting inventory counts: Physical counts of valuable items, such as clubs, and items with a history of shrinkage, should be performed more frequently than once a year.
3. Cashiers had greater system user access in Lightspeed than what is needed to perform their jobs. Management agreed to restrict cashier system access to only those functions necessary for the job responsibilities. (Refer to [System Access](#))
4. The purchase order module of its point-of-sale system is not used for purchasing merchandise. Tracking order status is therefore performed manually, which appears cumbersome and prone to mistakes. (Refer to [Automating Purchase Orders](#))
5. The pro-shop has two cash registers that are often shared by multiple cashiers. Although no associated issues were noted, best practices recommend individual cash registers with no sharing. Individual cash registers ensure clerks can be held accountable for till discrepancies, excessive adjustments, and other anomalies. If individual cash registers are implemented, cashiers should maintain unique login credentials as confidential and lock their cash registers when they step away.
6. A security camera, located in the inventory storage area adjacent to the Merchandiser's office, may be non-operational thereby limiting its potential usefulness. Footage from all security cameras should be tested periodically to ensure they are operational. Additionally, the above referenced inventory storage area should always be locked, or at least when the Merchandiser is not in the adjoining office. (Refer to [Physical Safeguards](#))
7. GMG does not perform a complete physical inventory count annually. Certain items are selected to be counted throughout the year; however, not all items are counted during the year. Higher value items and those at greater risk of theft should be counted more frequently. (Refer to [Conducting Inventory Counts](#))
8. Consider increasing City oversight of GMG operations and providing CHI best practice resources regarding internal controls. (Refer to [Oversight](#))
9. Other: Staff had not been advised of proper procedures for obtaining change for tills. Rather than taking funds straight to the bank to obtain change, an employee took \$1,300 home for a



night or two before getting change at the bank. Additionally, no documentation was left in the safe to document when the cash was removed, by whom, and what amount. Employees should never take company funds home and when cash is removed for any reason, it should be documented. (Refer to [Other](#))

Additional details about these findings and other information are reported below.

BACKGROUND

Golf Course Facility

GMG is a full-service facility with two 18-hole championship courses (the Cascade Course and the Olympic Course), four practice putting greens, two bunker practice areas, a driving range, private covered teaching studio, pro shop, full-service restaurant and bar including banquet facilities to accommodate nearly 400 people, and various buildings and related facilities used for storage of maintenance and related golf course equipment, golf carts and other golf course related supplies. The Cascade Course opened in 1971 and the Olympic Course opened in 1996.

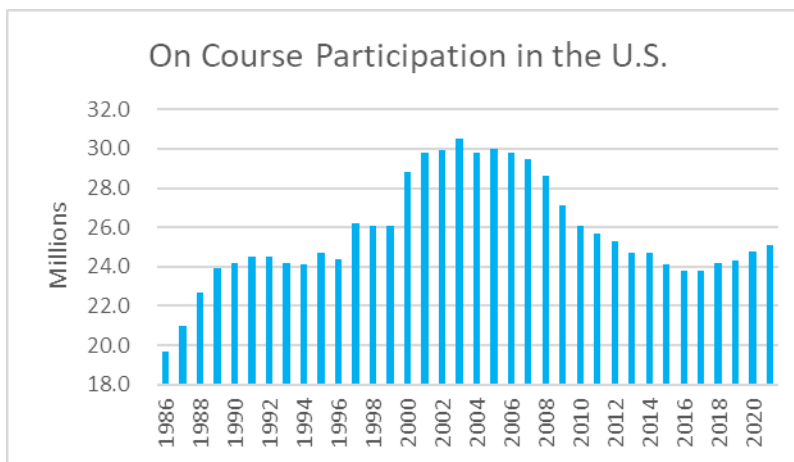
Management Agreement

Columbia Hospitality, Inc. (“CHI”) has been managing GMG as an independent contractor since October 2012. The initial term of the current golf course management agreement (“Agreement”) with CHI commenced January 1, 2020 and continues until December 31, 2024 (five years). Following the expiration of the initial term, CHI may request renewals for two successive three-year renewal terms.

The Agreement states CHI is engaged to service, operate, promote, and manage all the facilities at GMG. The inventory under review in this audit is the merchandise (golf equipment and apparel) sold in the pro-shop.

Industry: On Course Golf Participants in the U.S.

Golf participation is a core measure of golf’s vitality. The graph below shows how many people in the United States played on a golf course annually from 1986 through 2021. As shown, the industry has been growing each year since 2017.





FINANCIALS

GMG’s income statements from 2018 through 2021 are summarized in Exhibit 2, attached to this report. Excerpts from the income statements are reported below, as well as commentary.

Revenue

Revenue data is shown below to provide a sense of the size of the GMG operation and to illustrate the relative size of the pro shop. Total revenue has grown each year from 2018 through 2021, with the growth in 2021 revenue being almost \$1.25 million greater than in 2020, a 26.1 percent increase. For the first time in at least ten years and probably in GMG’s history, revenue exceeded \$6 million in 2021. The growth in 2021 was in part due to increased participation since the COVID-19 pandemic¹ and a great year of local golf-friendly weather.

Description	2018	2019	2020	2021	Average
<i>Rounds of golf</i>	73,194	72,107	84,904	93,594	80,950
Revenue:					
Beverage	\$ 443,230	\$ 441,554	\$ 407,379	\$ 529,383	\$ 455,387
Food	842,174	812,914	375,014	672,390	675,623
Golf	2,892,531	2,949,871	3,569,604	4,292,798	3,426,201
Pro shop	420,118	411,388	438,853	545,238	453,899
Total revenue	\$ 4,598,053	\$ 4,615,728	\$ 4,790,850	\$ 6,039,810	\$ 5,011,110

Year to year change	\$ 17,675	\$ 175,123	\$ 1,248,959
Revenue percent change	0.4%	3.8%	26.1%

As shown above, the pro shop, which represents about nine percent of total revenue, also experienced considerable growth from 2018 to 2021. The only department that experienced a decline in revenue during this period was Food, which was hard hit by the pandemic mandates that significantly impacted the hospitality industry, especially in 2020.

Inventory

The GMG pro shop sells golf apparel and equipment, including golf clubs, balls, tees, bags, and push/pull carts. The pro shop also sells pre-packaged snacks and bottled drinks. As shown in the table below, from 2018 through 2021 the pro shop year-end inventory averaged \$190,578. The lowest and highest inventory levels during this period were in 2020 and 2021, respectively, and the increase from 2020 to 2021 was \$67,514 or 40.5 percent.²

¹ The nature of golf is conducive to maintaining social distance.

² 2020 inventory levels were low due to global supply disruptions resulting from the COVID-19 pandemic. Conversely, GMG boosted its 2021 inventory to avoid inventory shortages from supply disruptions.



Year	Year End Inventory	Year to Year Change	Percent Change
2018	\$ 173,783		
2019	187,721	\$ 13,938	8.0%
2020	166,646	(21,075)	-11.2%
2021	234,160	67,514	40.5%
Average		\$ 190,578	

INVENTORY SHRINKAGE

GMG was able to generate a report of units of inventory written off but not the cost, which purportedly is only available on Inventory Count Sheets (ICS).^{3 4} Based on a review of 22 inventory count sheets summarizing counts taken October 30, 2021 through January 27, 2022, about a three-month period, net shrinkage (the difference between book and actual) totaled approximately \$7,500. These count sheets do not include all the inventory so actual shrinkage is greater.

If the dollar value of shrinkage cannot be generated in Lightspeed, GMG might consider another means for tracking it so management knows whether it is significant or increasing and respond accordingly.

SYSTEM AND MERCHANDISER CHANGE

In late 2020, GMG switched its point-of-sale system from Tee Snap to Lightspeed. In late 2021, GMG had a turnover of its Merchandiser (aka Buyer) position when the former Merchandiser relocated to another CHI property⁵ and the GMG Assistant Merchandiser was promoted to Merchandiser.

WRITTEN PROCEDURES

Not everything needs a written procedure; they are necessary when an issue is important or if there will be a significant benefit from clarifying a process. Written procedures can be particularly useful when there is staff turnover, especially if the turnover is unanticipated⁶.

GMG has a Golf Shop Operations Manual that includes information regarding opening the golf shop, breaks, greeting guests, how to make a tee time, and other similar customer service procedures. GMG also has Standard Operation Procedures (SOPs) that instruct the user how to use Lightspeed. At the onset of this audit, GMG had no written procedures for managing inventory; however, the new Merchandiser is in the process of drafting some.

³ ICS summarize actual counts versus what is in the system.
⁴ From the system user access matrix, it appears shrinkage cost should be available in Product Cost. GMG could contact Lightspeed to learn how to access this data.
⁵ The former Merchandiser transferred to Semiahmoo Golf and Country Club.
⁶ The Merchandiser turnover referenced above was anticipated.



SEGREGATION OF DUTIES

The GMG Merchandiser monitors inventory levels, orders merchandise, receives and checks the merchandise for quality and to confirm they received what was ordered. The Merchandiser enters the products into inventory; she approves the invoices for payment and submits them to CHI accounts payable, and she performs the physical inventory counts and makes adjustments in the system as needed. The Merchandiser also periodically works in the pro shop selling merchandise and rounds of golf.

Ideally, the position of the person directly managing inventory is separate from authorizing purchases, recording the receipt of goods, conducting inventory counts, and adjusting inventory. Although segregating these duties is likely not feasible because the size of the pro shop inventory is relatively small, there are some mitigating controls that should be implemented to compensate for GMG's biggest risks.

Purchasing

When the same employee who is responsible for managing the merchandise also purchases the merchandise, it is easier to order extra and convert it to personal use. Although the Merchandiser reviews prior year orders and coordinates with management to assess the types and quantities of merchandise needed, to mitigate risk GMG should also have a manager review and approve the orders before they are placed to ensure they are reasonable.

Receiving and Recording

When the same employee who is responsible for managing the merchandise also records items as received, there is an opportunity to not record everything that is received which can make theft easier to hide. A compensating control is to have another employee (besides the Merchandiser) periodically conduct independent spot checks that ordered items were received and recorded in inventory records. The spot check should include valuable or high-risk items.

Adjusting Inventory Levels

When the person who manages the inventory can also adjust the inventory in the system, merchandise can be stolen and the theft concealed by adjusting inventory records. Management review of adjustments is a good mitigating control. Additionally or alternatively, requiring a two-person approval process to make adjustments mitigates risk.

Conducting Inventory Counts

The person who manages the inventory should not also perform the inventory counts. The risk is inventory might be missing but no one is alerted. If GMG feels it is necessary to have the Merchandiser involved in the counts, perhaps because of her product knowledge, the Merchandiser could share her product knowledge and accompany another person who performs the counts. As previously noted, the person who currently performs the counts (the Merchandiser) also enters the associated adjustments in the system. Thus, theft can be concealed via a physical inventory write-off. As with other inventory adjustments, management approval would be a good mitigating control.

Other than accessories such as tees and bulk ball markers, which generally are not counted, the Merchandiser performs physical inventory counts of segments of inventory (such as shoes, clubs, Nike apparel, etc.) throughout the year. There is no year-end physical inventory and based on the inventory count sheets provided, it appears not all inventory is counted during the course of a year.



The City Finance Director, Mike Riley, stated he would like physical counts of valuable items, such as clubs and items with a history of shrinkage, to be performed more frequently. And all items should be counted⁷ at least once during the course of a year.

AUTOMATING PURCHASE ORDERS

When placing merchandise orders, the Merchandiser first consults with pro shop staff to assess inventory needs. Then GMG management and the Merchandiser meet with sales representatives to see what merchandise is likely to appeal to GMG customers and is in the desired price point. The Merchandiser then places orders with the sales representatives who provide purchase orders for GMG records. Prior to the COVID-19 pandemic, orders were placed about three months in advance. However, due to global supply chain disruptions resulting from the pandemic, GMG now places its orders about five months in advance.

By using the vendors' order forms rather than creating purchase orders in Lightspeed, the Merchandiser tracks orders manually. GMG purchased \$443,068 of inventory in 2021. Assuming the median price of its inventory is about \$30, GMG purchased a magnitude of about 14,000 to 15,000 units of inventory in 2021, which seems like a lot of inventory to track manually.

Generally, using a purchase order module in a point-of-sale system is a more efficient means for retailers to track inventory in real time and something GMG should consider doing. Lightspeed can likely also be used to track reorder points, desired inventory levels, back orders, and other data helpful for managing inventory.

SYSTEM ACCESS IN LIGHTSPEED

Lightspeed allows the company (GMG) to set up multiple classifications of employees in its system and specify different access permissions by classification. GMG uses two classifications: cashiers and managers.

After discussing internal control concerns with John Sitton, GMG Golf Operations Manager, Mr. Sitton agreed to eliminate cashier access to the Inventory module in Lightspeed, as well as a few other areas. Changes to access are highlighted in the table below:

⁷ Small bulk, low-cost items, such as tees, can be estimated.



System Access	Access by User Type			Access Description
	Cashiers		Managers	
	Initial	Revised		

General - All

External Login	x	x	x	Can log into POS from any device via Internet when system is closed
Reports	x	x	x	Can access the Reports area.
Service	x	x	x	Can access the Service area.

Sales - All

Sales	x	x	x	Can access the Sales area.
Refund	x	x	x	Can process a refund.
Open Register	x	x	x	Can open a register (till) to process sales and refunds.
Register Withdraw	x		x	Can withdraw money from a register.
Close Register	x	x	x	Can close a register.
Change Prices	x	x	x	Can change an item's price for all subsequent sales
Import Catalog Item	x		x	Can import items from catalogs to the local inventory.
Layaways & Special Orders	x		x	Can create layaways & special orders.
Line Only Discount	x	x	x	Can apply a discount to individual line items.
Entire Sale Discount	x	x	x	Can apply discounts to an entire sale.

Inventory - All

Basic	x		x	Can access the Inventory area
Product Cost	x		x	Can view, edit and export item cost; view margins and cost of shrink
Product Create & Edit	x		x	Can create new items or edit existing items
Special Orders	x		x	Can view existing special orders.
Purchase Orders	x		x	Can create and edit purchase orders.
Inventory - Add received	x		x	Can add received items in purchase orders to inventory.
Vendor Returns	x		x	Can access and send vendor returns.
Counts	x		x	Can create inventory counts and enter count data.
Inventory - Reconcile Counts	x		x	Can reconcile an inventory count.
Transfers	x		x	Can create, build and receive transfers between locations.
Send stock for transfer	x		x	Can send items in transfers between locations.
Import Images and Items	x		x	Can import both items and item images into inventory.
Vendors	x		x	Can edit vendors.
Categories	x		x	Can edit categories.
Brands	x		x	Can edit brands.
Tags	x		x	Can edit tags.
Vendor Return Reasons			x	Can edit vendor return reasons.

eCom - All

Basic	x	x	x	Can access eCom from the main menu drop-down (Internet sales.)
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Customers - All

Basic	x	x	x	Can access the Customers area. Can also edit existing serial numbers.
Export	x		x	Can export customer data
Credit Limit	x	x	x	Can set credit limits for customers.
Customer Deletion			x	Can delete customer accounts
View Gift Card Numbers	x	x	x	Can see full gift card numbers instead of just the last four digits.

Payments Reports - All

Card Sales and Payouts			x	
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Settings - All

Basic			x	Can access the Settings area.
Setup Shops			x	Can access Locations under Settings.
Employee Setup			x	Can access Employee Setup and Employee Roles under Settings.
Employee Account Deletion			x	Can delete employee accounts
Sales Setup			x	Can set price rules, discounts, payment types, and taxes.
Void Sales			x	Can void transactions.
Pricing			x	Can access inventory-related settings under Settings.
Financial Services			x	Can add, configure and archive register rules.



PHYSICAL SAFEGUARDS

At certain times of the day and year, particularly summer, the pro shop is a busy place as evidenced by over \$6 million of revenue and close to 94,000 rounds of golf in 2021. There are four entry ways to the pro shop: one employee entrance to the pro shop off the hallway, which just recently had a lock installed on the door, plus three public entrances. During busier times of the day, it is likely challenging to service the customers and keep a watchful eye on merchandise.

The shop has some no cost and low-cost measures in place to deter theft. The shop always appears organized and tidy, which can make it easier for staff to notice when something is missing. The shop has security cameras and GMG strategically stages its more expensive inventory (golf clubs) near the cash registers where it is in better view of employees. Discounted items are placed near the main entrance. Additionally, the Merchandiser is currently developing a training document to improve employee awareness on safeguarding inventory, particularly as it pertains to shoplifting. GMG could consider whether installing anti-theft mirrors would help staff better observe customers in less visible areas of the shop.

In addition to the pro shop, inventory that has not yet been put on the sales floor is kept in a storage room located just outside the Merchandiser office. There are cases of balls, boxes and racks of apparel, some clubs, etc. The door to this room is across the hallway from the pro shop. This room is also used for receiving merchandise deliveries.

The storage room is unlocked throughout the day when the Merchandiser is working, whether she is in the office or not. The storage room is locked when the Merchandiser is not working and all managers plus sales associates who open or close the pro shop have a key. Inventory in this storage area would be more secure with a door that is locked, particularly when the Merchandiser office is unoccupied.

Based on discussions with staff, it is unclear whether the security camera in the storage room is operational. Although the mere presence of a security camera may deter theft, an operational security camera is more effective, particularly for identifying perpetrators. Footage from all security cameras should be tested periodically, perhaps quarterly, to ensure the cameras are operating as expected.

INVENTORY TURNOVER

A key financial ratio for assessing retailers inventory management is the Inventory Turnover (IT) ratio, which indicates how many times a year a retailer turns its inventory into sales. IT ratios vary by type of product sold: Groceries that have a short shelf life tend to have a low profit margin and a high IT ratio; while industries that sell one-of-a-kind high-end products, like custom jewelry tend to have a high profit margin and low IT ratio. An IT ratio of two essentially means new inventory is on the shelves twice a year; an IT ratio of four means inventory turns four times in a year.

According to an executive with the National Golf Federation, an IT ratio of 2 to 4 is common for pro shops. If the turnover is low, it may indicate that a product or products being sold are not as popular as expected. It can also indicate staff may need additional training or education about the products and/or how to conduct sales. In most situations, a high IT ratio indicates a company is performing well.



Although GMG’s IT ratio from 2019 through 2021 averaged 1.7, which may be somewhat low, it is encouraging to note it is trending upward, as shown below:

Year	Year End Inventory	Average Inventory	Cost of Goods Sold	Inventory Turnover
		A	B	B/A
2018	\$ 173,783			
2019	187,721	\$ 180,752	\$ 266,228	1.5
2020	166,646	177,184	306,487	1.7
2021	234,160	200,403	375,554	1.9
Average	\$ 190,578	\$ 186,113	\$ 316,090	1.7

To deal with slow moving inventory, the Merchandiser works with the vendors to seek inventory credits or returns. She also tries to move slow moving inventory by discounting it. The Merchandiser also provides sales instruction to staff.

Although the Merchandiser appears to be very aware of which products sell well and which do not, she might find it helpful to occasionally review an Inventory Aging report that shows the date inventory was purchased. Additionally, re-order points can likely be entered in Lightspeed so that the Merchandiser is alerted when specific items are low and need to be ordered.

OTHER

At a site visit during this review, we performed a surprise cash count. While counting the money, an employee stated \$1,300 was in transit for the purpose of getting change for the tills. The \$1,300 had been taken home by the employee the day before and was still at home. The employee explained that he did not have an appointment to get change at the bank so he ended up leaving the cash at home until the bank could meet with him. The employee stated another employee knew he removed the cash from the premises; however, no receipt or other documentation was in the safe to document the removal or amount of the cash.

Employees should never take company money home. If appointments with the bank are necessary, an appointment should be made and then the cash can be taken directly to the bank. Additionally, someone else should sign a receipt or other form witnessing the date, time and amount of funds taken and the name of the employee who has the funds. The return of the funds should also be witnessed.

OVERSIGHT

There are multiple acceptable philosophies on the extent of oversight an owner should exercise over a managed contract: from completely hands off to micromanaging, or somewhere in between. The Parks Department is responsible for overseeing the GMG contract. Jeff Elevado, Parks Director, stated he is involved in decision making on GMG capital projects; but primarily leaves CHI to manage the operations of GMG, which it is paid to do.

Although the City’s limited oversight of operations may be acceptable, increased oversight could result in improved operations. It is recommended the City also consider sharing best practice resources with CHI to help guide them with internal controls of other processes. My



review did not identify any material concerns about CHI's management of the property; however, GMG is a valuable asset that seems worthy of increased City oversight, assuming resources can be made available.

GMG ASSISTANCE

I wish to acknowledge my appreciation of GMG staff assistance and cooperation during this audit. Any feedback, questions, or comments are always welcome.

Please contact me if you have questions or need additional information.

Sincerely,

Jennifer L. Sims CPA/CFF, CFE
City Auditor

cc: Mayor Wheeler
Jeff Elevado, Parks Director
Mike Riley, Finance Director
City Council



Exhibit 1

Information Sources

1. [Columbia Hospitality Management Agreement](#)
2. [GMG Golf Shop Operations Manual](#)
3. [Association of Golf Merchandisers Merchandise Manual \(Excerpt: Golf Retail Operations\)](#)
4. [Select Inventory Counts 2021 – 2022](#)
5. [Year End Inventory Reports 2018 – 2021](#)
6. [Financial Statements from 2018 – 2021](#)
7. [Kitsap Sun Article dated October 5, 2017](#)
8. [KIRO News Article dated June 5, 2014](#)



Exhibit 2

Gold Mountain Golf Course Income Statement Summary (Before debt service, insurance, depreciation, and other charges paid directly by the City)

Description	2018	2019	2020	2021
Revenue				
Food and Beverage	\$1,285,404	\$1,254,468	\$ 782,393	\$1,201,773
Golf	2,892,531	2,949,871	3,569,604	4,292,798
Golf Shop	420,118	411,388	438,853	545,238
Total Revenue	4,598,053	4,615,727	4,790,850	6,039,810
Cost of Sales				
Food and Beverage	337,945	326,644	252,011	337,074
Golf	16,806	20,166	22,563	45,728
Golf Shop	265,773	266,228	306,487	375,554
Total Cost of Sales	620,523	613,038	581,060	758,356
Direct Expenses - Operating & Payroll				
Food and Beverage	547,522	588,696	434,039	530,443
Golf	496,058	495,795	595,840	705,239
Golf Shop	24,756	17,300	15,451	19,762
Total Direct Expenses	1,068,335	1,101,790	1,045,330	1,255,444
Department Profit	2,909,194	2,900,899	3,164,460	4,026,010
Undistributed Operating Expenses				
General and Administrative	449,950	453,545	471,919	513,640
Repairs and Maintenance	78,846	79,501	140,997	179,921
Golf Course Ops & Maintenance	1,029,670	971,499	972,774	1,178,003
Sales & Marketing	119,685	121,693	54,275	108,007
Utilities	122,677	105,130	89,731	119,501
Total Undistributed Operating Expenses	1,800,828	1,731,367	1,729,697	2,099,072
Gross Operating Profit	1,108,367	1,169,532	1,434,762	1,926,938
Other Expenses				
Management Fees Paid to CHI	298,581	326,637	333,986	525,926
Capital Reserves	137,942	138,472	191,634	241,592
Taxes and Insurance	59,443	60,648	57,329	99,318
Total Other Expenses	495,966	525,756	582,949	866,837
Net Operating Income	\$ 612,401	\$ 643,776	\$ 851,813	\$1,060,102