

January 2020

OMC Non-Capitalized Rail Parts and Tool Inventory

AUDIT REPORT – INTERNAL AUDIT



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To: Councilmember Robin Arredondo-Savage, Chair, Tempe
Mayor Kate Gallego, Phoenix
Vice Mayor Bill Stipp, Goodyear
Councilmember Lauren Tolmachoff, Glendale
Councilmember Francisco Heredia, Mesa

The purpose of this report is to communicate the results of the Operations and Maintenance Center (OMC) Non-Capitalized Rail Parts and Tool Inventory Audit. The audit was part of Valley Metro's fiscal year 2019/20 Internal Audit Plan.

Based on Internal Audit's review, the processes followed by Finance and OMC personnel and management for non-capitalized rail parts and tools lacked consistency, accountability, and the appropriate segregation of duties.

The annual and weekly counts for rail parts lacked the benefits of blind counts, did not provide a segregation of duties or documented discrepancy investigations, and neglected to address obsolescence of parts on-hand. Additionally, a reconciliation of all items on-hand to the Ellipse records and the Abila financial values had not been completed.

Procurements were performed by OMC personnel and did not involve Contracts and Procurements until approaching \$150,000 spend thresholds.

Efforts to account for tools were ineffective. The tracking logs were inaccurate or did not exist, and there was minimal evidence of management oversight.

OMC personnel were administrators for two key applications; the inventory management (Ellipse) and DSX badge system that grants physical access to the parts stockrooms.

Rather than citing each discrepancy as an issue, Internal Audit considered the discrepancies collectively to determine the root cause and the most beneficial next steps for the Divisions. Therefore, this report contains one recommendation to improve the process of managing non-capitalized rail parts and the tools maintained by the OMC. Internal Controls over rail parts and tools can be strengthened by establishing a written robust Inventory Management Policy and a set of current procedures to address a variety of controls over parts and tools.

Management has provided a corrective action plan for the recommendation and the attached memo to provide additional comments on the report.

The support and assistance received throughout the audit by Finance and OMC personnel, is greatly appreciated.

For questions or further clarification, please contact me at 602-322-4453.



Mary Modelski
Internal Audit Director
January 16, 2020

Performed by:
Jennifer Davis
Senior Internal Auditor

Distribution

Scott Smith, Chief Executive Officer
Paul Hodgins, Chief Financial Officer
Ray Abraham, Chief Operations Officer
Michael Minnaugh, General Counsel

Objective

Determine if non-capitalized rail parts were managed according to procedures, tools were inventoried and tracked, and any other matters that rose to a level of attention.

Scope

The timeframe under review was July 1, 2018 through June 30, 2019. Internal Audit reviewed items that included: non-capitalized rail parts (inventory), tools, and any other purchases that were kept in inventory from July 1, 2018 through June 30, 2019. Internal Audit expanded the testing population to include inventory and tools purchased before and after this timeframe, as their review assisted in the completion of the audit objective.

Methodology

Internal Audit reviewed applicable Valley Metro policies and Operations and Maintenance Center's (OMC) Standard Operating Procedures (SOPs). A judgmental sample of items was selected to determine if inventory, tools, and other purchases were managed according to those policies and procedures. Internal Audit reviewed the documentation for:

- Purchased items
- Receiving of items
- Inventory movements
- Inventory counts
- Inventory values

Internal Audit reviewed documentation and observed the tool inventory processes for a sampling of tools in the following areas:

- Maintenance of Equipment (MOE) toolboxes
- MOE Tool room and Shop floor
- Maintenance of Way (MOW) Shop floor
- MOW trucks
 - Traction Power
 - Signal and Communications
- Facility Maintenance trucks, toolboxes, and Shop floor

Internal Audit tested for Information Technology General Controls (ITGCs) by reviewing the logical access controls to the OMC inventory system (Ellipse), and the physical access controls to the inventory storage areas.

Background

Valley Metro's fiscal year 2019/20 Internal Audit Plan included the OMC Non-Capitalized Rail Parts and Tools Inventory Audit. The audit plan was approved by the Audit and Finance Subcommittee (AFS) on June 18, 2019. The audit plan included this review due to the concern that the internal controls over the acquisition, disposal, and security of inventory and tools were not adequate. The following policies and procedures were considered during the review to establish a baseline to determine compliance with Valley Metro policies and department procedures:

- *Joint Internal Procurement Manual* (v. 06/25/18)
- *Joint Internal Procurement Manual* (v. 05/08/19)
- *Credit Card, Acceptable Use policy* (v. 07/28/16)
- *Credit Card, Acceptable Use policy* (v. 10/10/18)
- OMC Standard Operating Procedures (SOPs), as applicable

Inventory Valuation

Valley Metro Finance uses Abila as its system of record for the parts inventory value. Ellipse reports are used to adjust Abila for parts purchased and used. The table below shows the inventory values per Abila by division (MOE and MOW) for the past three fiscal years.

Abila Inventory Values

Inventory Area	FY 17	FY 18	FY 19
Spare Parts Inventory MOE	\$ 9,659,866	\$ 10,673,770	\$ 10,927,504
Spare Parts Inventory MOW	\$ 7,169,994	\$ 6,865,723	\$ 6,595,527
Total OMC Spare Parts Inventory	\$ 16,829,860	\$ 17,539,493	\$ 17,523,031

The Ellipse reports accounted for approximately 6,100 stocked items, which represented a quantity of approximately 346,300 items stocked on-hand during the 2018-2019 fiscal year.

Inventory Counts

Valley Metro has not conducted a full parts inventory. The annual inventory count is based upon a sample selected by Finance and counted with OMC personnel at the end of the fiscal year. In lieu of a complete inventory count at the end of the fiscal year, OMC stockroom personnel performed weekly cycle counts of stock coded items throughout the year. However, if an item does not have a stock code within Ellipse, it will not be included in the weekly cycle counts, the annual count, or the year-end inventory value.

Annual Count

At the beginning of June, in preparation for the annual count, Finance pulled the *Inventory Value Extract* reports from Ellipse and then sorted the listing by the "Category" field ("VM" for MOE and "MO" for MOW). Next, Finance sorted the reports by inventory value and selected the 50 highest valued stocked items from each location for the sample. Finance then randomly chose an additional 60 stocked items from each location to add to the samples.

On June 5, 2019, Finance emailed the sample of 100 MOW and 100 MOE stock items, with the quantity of stock on-hand, to the Facilities Maintenance (FM) Manager. This was because the FM Manager needed to work with the Ellipse vendor to configure the inventory reports for the annual count to include the Bin Location for the sampled items. Additionally, the remaining 10 stocked items per location, were used as "surprise counts", were provided on the day of the count, June 28, 2019.

On June 28, 2019, in collaboration with OMC personnel, Finance staff counted 110 of 3,918 MOE items (2.8%) and 110 of 2,053 MOW items (5.4%). See a partial report on the next page.

4101 - VALLEY METRO RAIL, INC - MOE



Inventory Audit

06/28/19 6.03 AM

Bin Location	Stock Code	Description	Inv Cat	Ellipse Qty	Count	Counted By
11-A-01	001002872	Secondary suspension, air spring	VM	104		
22-F	001018886	Bumper assembly, w/o covers and buffers	VM	2		
26-E-02	001026897	Decal,Train Number 120A	VM	4		
26-E-02	001026913	Decal,Train Number 122A	VM	4		
26-E-08	001027671	Decal,Train Number 150B	VM	4		
26-E-09	001026079	Decal,Car ID Number, 146A	VM	4		
26-E-10	001026558	Decal,Car ID Number, 146B	VM	4		

Internal Audit determined eight stocked items, totaling \$174,941, were not included in the Finance inventory population as they were entered incorrectly into Ellipse during the item setup process.

Stock Code	Description	On hand	Weighted Price	Inventory Value
1004993	Chevron Spring*	919	\$ 187.91	\$ 172,685
1001379	Circuit Board	4	\$ 283.81	\$ 1,135
1017920	Flat Blade	16	\$ 35.75	\$ 572
1017946	Pinch weld scraper blade,	15	\$ 16.47	\$ 247
1060201	Electrical Cable	97	\$ 2.12	\$ 206
1035005	Lens Cleaning Station	3	\$ 19.52	\$ 59
1053040	Lambswool Duster	34	\$ 0.68	\$ 23
1053446	Wire brush	8	\$ 1.82	\$ 15
Total				\$ 174,941

*Chevron Springs for the overhaul project

Since Internal Audit’s notification, the OMC has contacted the Ellipse Vendor to have the “Category” field corrected for these eight items. Therefore, once the items are correctly identified in Ellipse, Finance will include these eight items in the MOE inventory population for sample selection and include the additional \$174,941 to the value of MOE’s inventory.

Weekly Counts

Weekly, the Ellipse Administrator, pulled the *Count Sheet Detail* reports from Ellipse. On average, the *Count Sheet Detail* report provided an Ellipse determined sample of 83 MOE and 43 MOW stock items. However, the report also indicated the current stock on-hand for those items. See a partial report below.

4101 - VALLEY METRO RAIL, INC - MOE											
Count Sheet Detail											
 VALLEY METRO 06/17/19 8.28 AM											
Stocktake Number: 000190			Count Sheet No: *			SOH- Stock on-hand					
Program Id: 000010			Program Group: 000011								
Sched Start Date: 06/16/19			Sched End Date: 06/22/19								
Bin Loc	Invent Cat	Stk Code	Item Name	Stock Item Description	UOI	SOH	Inv Price	Current SOH	Date Counted	Counted By	Adj Form Y/N
26-D-08	VM	001054220	DECAL	POIC vehicle number, 109C	EA	8	2.26				
26-D-08	VM	001054857	DECAL	POIC vehicle number, 128B	EA	10	0.31				
26-D-08	VM	001055458	DECAL	POIC vehicle number, 148A	EA	10	0.31				
26-E-03	VM	001027077	DECAL	Decal,Train Number 138A	EA	4	3.83				

The Ellipse Administrator emailed the *Count Sheet Detail* report to stockroom personnel for MOE and MOW. OMC stockroom personnel:

- Performed the weekly counts;
- Recorded on the *Count Sheet Detail* reports:
 - Current stock on-hand
 - Date counted
 - Counted by
 - Indicated if the item required an adjustment form
- Investigated any discrepancies between the count and the report, and
- Turned the report into their supervisor/manager; whom sent the reports to the Ellipse Administrator for finalization.

Internal Audit reviewed the 102 *Count Sheet Detail* reports for the year, and the reports indicated the current stock on-hand, date counted, and initials of the counter. Interviews with the stockroom personnel and observation of the weekly count process disclosed discrepancies frequently occurred during the weekly counts. Due to the combination of:

- The *Count Sheet Detail* reports were printed on Mondays;
- The counts were completed typically one to four days later, and
- Some parts had been assigned to work orders in the interim.

Stockroom personnel indicated they reviewed inventory records to investigate any discrepancies, but they did not record the specifics of the reviews and indicated no variance on the reports. Therefore, Internal Audit was unable to test the discrepancy investigation process.

Throughout the year, Finance reviewed the weekly *Count Sheet Detail* reports for completion and recorded the following information on a tracking log (*Stocktake Program Cycle Log*):

- Stocktake number and scheduled start date;
- Number of stocked items counted each week;

- Reconciled the report with any supporting adjustment documentation, and
- Indicated the Finance staff member’s initials.

At the end of the fiscal year, Finance compared the current year’s total number of stocked items counted weekly (MOE 4,280 and MOW 2,201) to the prior year’s stocked items totals (MOE 3,861 and MOW 2,088). This comparison provided Finance with a degree of certainty that OMC personnel counted all stock coded items throughout the year.

Obsolete Inventory

Valley Metro maintains stocked items in inventory that have no present or future use to rail operations and there is no documented process to identify and remove these items from inventory. Internal Audit compared the FY 19 *Inventory Value Extract* reports to the FY 18 reports. Audit determined that year-over-year, 2,261 (57%) of MOE’s and 1,714 (80%) of MOW’s stocked items did not materially change in net value. Internal Audit observed items during walk throughs and inquired to the inventory’s usefulness.

Seven cash carts for the Ticket Vending Machines (TVMs) are maintained in the MOE basement and were added to the MOW Ellipse inventory in April 2009 for \$7,104 each, totaling \$49,728.

The TVM cash carts are still wrapped in original packing, have not been used, and per MOW staff, they will not be used, as the TVM cash collection function is a contracted service with Brink’s Incorporated.



Valley Metro has also not performed a reconciliation of all inventory items on-hand to ensure they are recorded in Ellipse. For example, fifteen air compressors had signs marked “Do Not Inventory” and Defect Tags dated 01/10/19.



LINK LIGHT RAIL DEFECT TAG	
UNIT / LRV# :	L160
WORK ORDER:	CLX-LRV-2019-190
JOB NUMBER:	
PART NO.:	100597
PART DESCRIPTION:	AIR COMPRESSOR
SERIAL NO. (IF ANY):	
QUANTITY:	1
EMPLOYEE NAME:	DATE: 01/10/19
CHIEF: [Signature]	DATE: 1/10/19
REASON (COMMENTS / OBSERVATIONS):	

The movement of parts in Ellipse has not been analyzed to determine the usefulness/value/ necessity of unused/obsolete inventory and there is no documented process to dispose of identified items.

Precious Metals

The MOW maintains spools of copper wire in the MOE basement. Personnel removing wire are to write on the spool the remaining length of wire. However, there are no documented procedures to determine if wire has been removed or to verify remaining length of wire on spools. Below are photos of loose copper wire and the copper wire spools.



Tool Inventory Counts

The OMC has calibrated torque wrenches and multimeters, hand tools, tool sets, and tool kits in the following locations: MOW's Traction Power and SigCom, MOE's 46 Toolboxes, MOE Tool room and Shop floor, and Facilities Maintenance (FM).

Calibrated Tools

The OMC's Quality Assurance Administrator (QAA) maintains separate calibration tracking spreadsheets and binders of calibration documentation for the tools used at each of the three locations (Traction Power, SigCom, and MOE). As part of an on-going process, the QAA reviewed calibrated tools and testing equipment throughout the year as annual calibrations were required. The QAA tracked active and inactive items, as well as items noted as "calibration no longer required" to maintain a historical log of items purchased.

Internal Audit reviewed the QAA's calibration tracking spreadsheets and in the binders, and determined:

- 145 active items were listed as:
 - 13 past due calibrations
 - 132 active calibrations
- 217 non-active items were listed as:
 - 47 not located
 - 93 inactive, decommissioned, retired, or returned
 - 77 not requiring calibration, due to being either:
 - Spares
 - Used for spare parts
 - No longer required calibration, or
 - Used for troubleshooting
- Six of FM active items had not been submitted for inclusion on the calibration schedule.

Upon Internal Audit's inquiry, past due and FM items have been added to the calibration schedule.

MOW

In the fall of 2018, MOW management began securing vehicle keys, specialty tools, tool cabinet keys, and the MOE parts room key in the CribMaster storage container. The CribMaster is a vending machine type container with a carousel for key storage and a divided drawer system for tool storage. Items in the CribMaster were accessible and trackable through the employee's Valley Metro badge. The MOW Assistant Manager/CribMaster Administrator received *Usage Reports* from CribMaster emailed daily to monitor activity of items checked out.

For items not in the CribMaster, MOW management had a community of shared tools that were used for work on the light rail alignment by Traction Power and SigCom personnel. As a result, monthly, the MOW Manager issued Ellipse workorders that required Traction Power and SigCom personnel to inventory the department's tools on community trucks and the Shop floor tools. The Ellipse workorder files recorded who performed the periodic counts. The Excel inventory tracking spreadsheets recorded the existence or absence of the tools counted.

Internal Audit reviewed the inventory tracking sheets and determined:

- Traction Power tracked 706 tools and 147 tool sets, of which:
 - 176 tools were indicated as missing, and
 - 78 tool sets were incomplete
- SigCom tracked 265 tools and 90 tool sets, of which:
 - 78 tools were indicated as missing, and
 - 42 tool sets were incomplete

Management could not validate the accuracy of the tracking spreadsheets or determine if tools were missing as of the current fiscal year.

Based on the Snap-On Incorporated and Grainger website pricing in November 2019, Internal Audit determined an approximate replacement values for the tools indicated as missing as; \$23,000 for the 176 Traction Power tools and \$9,100 for the 78 SigCom tools.

MOE

MOE management assigns toolboxes to the Light Rail Vehicle (LRV) Maintenance Technicians and Inspectors and maintains a community of tools on the Shop floor or in the Tool room for work on the light rail vehicles.

Toolboxes

The MOE had 46 toolboxes on the Shop floor, each furnished with either a 204-piece Snap-On tool set or a 211-piece JH Williams tool set. The toolboxes remained at the facility for work on the light rail vehicles. During the new-hire process, MOE personnel completed a *New Employee Check List* form and recorded the toolbox number assigned to Light Rail Vehicle (LRV) Maintenance Technicians and Inspectors. The employee and LRV Technical Trainer inventoried the toolbox and then recorded the results on the *Contents of Employee Tool Box* form.

During the employee's off-boarding/termination process is the only other time the contents of toolbox is inventoried. Valley Metro then incurs the expense to replace any missing tools. Management stated the time and resources required to perform more frequent inventory counts is more costly than the expenses incurred to replace any missing tools.

Internal Audit observed the inventory process for four toolboxes took an average of 30 minutes each and the results were recorded on the *Contents of Employee Tool Box* inventory forms.

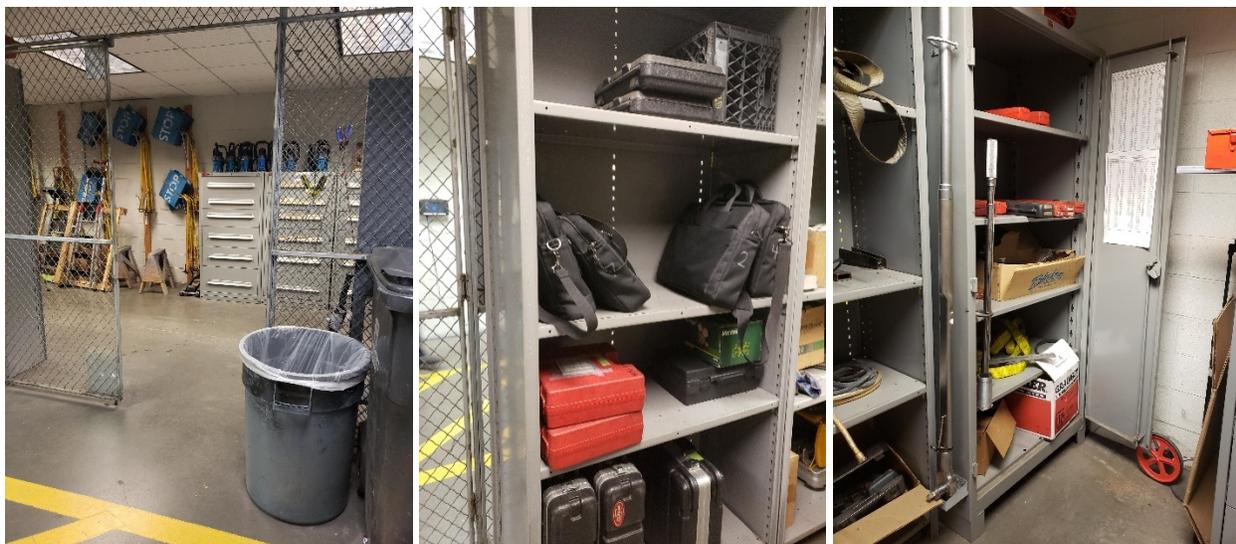
Review of four toolbox inventory forms found 22 of 823 tools assigned were marked as missing. For those 22 tools, Internal Audit determined an approximate replacement value as \$726.

In September 2019, MOE management ordered ten new Snap-On toolboxes through Arizona’s State Contract (CTR040594) for \$40,320, before shipping and taxes. These ten toolboxes will accommodate the upcoming increase in LRV staff. Each toolbox (\$1,565 each) will be stocked with a 204-piece Snap-On tool set (\$2,467 each) and will bring the total MOE toolboxes on the Shop floor to 56.

Tool Room and Shop Floor

The MOE facility has a Tool room across from the LRV supervisors’ office for additional tools used for work on the light rail vehicles. An inventory listing for this area was not provided, as such Internal Audit did not perform an inventory of items in the Tool room.

Nevertheless, Internal Audit observed items such as power tools, meters, torque wrenches, troubleshooting computers (PTUs), rail safety lanterns, and blue flags stored there. A *Tool Room Tool Sign Out* log was in place for employees to self-checkout and return these and other items (levels, N2 kits, Accu-gauges, and heat guns) to the room.



Internal Audit noted 42 of 843 entries on the *Tool Room Tool Sign Out* log throughout the fiscal year 2018-19 were not signed in, and notations evidencing management review were not present. Since the audit, management implemented a task for MOE supervisors to review the *Tool Room Tool Sign Out* log, verify tool status, and counsel employees with missing sign-ins.

LRV personnel also used tools located in functional areas (I.e. the brake shop or HVAC repair area) of the MOE Shop floor for LRV repair and maintenance. An inventory listing for these tools was not provided, as such Internal Audit did not perform an inventory of items on the Shop floor.

Facilities Maintenance

The Facilities Maintenance (FM) Manager had drafted procedures and forms for tracking the department’s tools. The FM Manager then used Internal Audit’s review of this area as a catalyst to implement those controls. In September 2019, FM completed a full inventory of tools, organized the department’s work space, and updated inventory documentation. Therefore, creating tighter internal controls over its 389 tools, 25 tool sets, and 28 tool kits. FM has tools on two assigned vehicles, within four assigned toolboxes, and shared tools within the shop.

Tracking spreadsheets were created to include:

- Tool description
- Manufacturer
- Part and serial numbers, as applicable
- Quantity
- Location
- Condition
- Employee and manager initials

Internal Audit observed the full inventory count and reviewed the tracking sheets were updated to reflect the count information. Additionally, the *Tool Requisition Form* (v. 08/29/19) below, was created and implemented to track and approve the purchase of new or replacement tools.

VALLEY METRO

Tool Requisition Form

Date:

Department:

Employee Requesting:

	New Purchase	Replacement Purchase	Description	Quantity	Budget Code	Activity	Inventory List Updated (date)	Employee Initials
1.			Serial# and disposition of tool being replaced:					

New controls over tool kits included a *Tool Equipment Sign Out Procedure* (v. 08/30/19), a sign out log, a listing of tracked tool kits, and the attachment of the bright green tag (as seen below) on each tracked item.



The FM team plans to perform another inventory in the Spring of 2020 and change the tracking spreadsheets, tool kit listings, forms, and procedures, as needed.

Procurement

The OMC's non-contract procurement practice allows OMC personnel to process purchase orders through Ellipse. Contracts and Procurement personnel have no access to Ellipse. OMC purchase orders were processed for the MOE, by the LRV Maintenance Administrative Assistant II and for the MOW, by the OMC's Senior Management Analyst. Purchase orders were supported by:

- Ellipse generated requisitions that were based on the stock minimums and re-order parameters set during stock code setup, or
- Manual requisitions based on LRV Maintenance work order or MOW service needs.

The LRV Maintenance Administrative Assistant II obtained the quotes, as applicable. The approval signatures from either the Superintendent of LRV Maintenance or the Assistant Superintendent of LRV Maintenance were obtained on the MOE requisitions.

The OMC's Senior Management Analyst obtained the quotes, as applicable, and indicated that the MOW Manager has a standing approval for processing the Ellipse generated MOW requisition orders and any TVM service repairs.

Invoices are received at the OMC, matched to receiving documentation and purchase orders. Management's signature for payment approval is obtained. The Chief Operations Officer signs if invoice exceeds \$7,500. Requisition, receiving, and quote documents are kept on-file at the OMC and not forwarded to accounting with final invoices for payment processing. Finance receives the signed invoice and a copy of the purchase order.

Internal Audit review the Ellipse reports for "purchase orders received" during the fiscal year and determined the OMC processed MOE purchase orders totaling \$2,369,606 through 115 vendors and MOW purchase orders totaling \$567,840 through 65 vendors.

The OMC obtained Contracts and Procurement's assistance and approval for the single or aggregate annual purchases exceeding \$150,000 listed on the next page. The Board of Director's approval is required for a goods/services contract/purchase order at or above \$150,000. Internal Audit identified the following five vendors with purchases greater than \$150,000 and verified if Board approval and contracts were currently in place:

Vendor	Amount	Description	Contract #	Board Approval
Vulcanite	\$ 226,720	Motor truck chevrons	17028 MCTOP	11/30/17
Bridgestone Industrial Products	\$ 572,750	Air spring assemblies	17028 MCTOP	11/30/17
Hutchinson Aerospace & Industry	\$ 235,132	Bolster anchors and lateral stops	Sole Source-Purchase Order Only	02/22/18
Penn Machine Co.	\$ 184,803	Rubber block tire kits	Board Approved Purchase Order, Contract 19011	03/17/16 10/18/18
NASG, Holdings, Inc.	\$ 153,661*	LVR window glass	None, then 19023	05/16/19

*Contract was initiated and obtained as purchase order spend approached \$150,000.

Since Contracts and Procurement personnel have no access to Ellipse and are not involved in OMC’s purchases less than \$150,000, they cannot proactively monitor for exceeding approval thresholds. The OMC’s Senior Management Analyst monitors thresholds.

OMC Systems

The OMC has two applications, Ellipse to order, receive, issue, and track inventory items and the DSX system to grant access via badges to the inventory storage areas. Access to Ellipse and the DSX System was granted to Valley Metro employees, as applicable to job function and to specific contracted vendors, as business needs warranted.

Internal Audit reviewed the Ellipse active user listings and compared them to the active and terminated employee listings provided by Valley Metro Human Resources (HR). Two of 144 active Ellipse users were no longer engaged by Valley Metro. One employee was termed 05/21/2019 and one contracted vendor was released, no term date available. Upon Internal Audit’s inquiry, access was removed for both individuals by the Ellipse Administrator. There were 22 additional Valley Metro employees terminated during fiscal year 2018-19 that had Ellipse access. Internal Audit calculated the number of days between HR’s termination date and the Ellipse access removal date, and summarized below:

	1-7 days	16-25 days	36-58 days	106-185 days
Users	6	5	4	7

The Ellipse Administrator disclosed that user access was modified or terminated as notified by the department/contractor or during periodic reviews, however department notification was not consistent and timely.

Internal Audit reviewed the DSX system reports for the OMC stockrooms and compared them to the active and terminated employee listings. Five of 88 cardholders were no longer engaged by Valley Metro. One employee termed 06/18/2014, another employee termed 6/20/2017, and three former contractors, no term dates available, but none of the five were active in past 90 days. Upon Internal Audit’s inquiry, access was removed for all five individuals.

Per the OMC’s Administrative Assistant III, DSX system access was modified or removed only as notified by the department/contractor. Additionally, it was noted the physical badges required for access should be surrendered upon termination of employment. In September 2019, the OMC’s Administrative Assistant III started reviewing the DSX System users and continues to monitor and correct.

Standard Operating Procedures

The OMC has a shared drive containing the division's Standard Operating Procedures (SOPs) to guide staff through 17 Operational areas within the division. The Quality Assurance Administrator (QAA) maintained an Excel spreadsheet that listed the OMC's SOPs as an index. The *SOPs Index as of 06/04/19*, listed 251 active procedures of which:

- 80 procedures had revision dates within the past two years,
- 171 procedures had revision dates prior to 2017, of which:
 - 22 procedures required updates, because they did not reflect current processes.

For example, SOP 1800.11 *Calibration of Tools and Test Equipment Rev. B* (v. 4/26/12) did not indicate processes for tools and testing equipment items that:

- Were not located for calibration,
- Did not pass calibration testing, and were either:
 - Made inactive,
 - Decommissioned/Retired, or
 - Returned
- Did not require calibration testing, and were either:
 - Spares,
 - Used for spare parts, or
 - Used in shop to troubleshoot.

During Internal Audit's inquiry, the QAA disclosed a process to review the SOPs regularly. The last review occurred in September 2018 but results of the review were not documented. On December 16, 2019, the OMC issued the updated SOP 100.01, *Standard Operating Procedures and Rulebook Review Rev. B*, effective 12/03/19. The revised SOP included an annual review of SOPs by "the applicable discipline associated with the SOP."

Audit Recommendation

No Established Inventory Management Policy

A written Inventory Management Policy for the parts and tools used at the OMC does not exist. Procedures were not documented, and the processes followed were inefficient in addressing the handling of precious items (e.g., copper and steel), and the reconciliation, disposal, and obsolescence of parts and tools. Management could not provide a documented base knowledge of all items on-site to include in the OMC tools and parts inventories.

The OMC has not conducted a full inventory of the parts and tools for the MOE and MOW. A reconciliation of parts on-site to the parts recorded in Ellipse and the tools on-site to the Excel tracking spreadsheets has not been completed. Additionally, the stock movement of parts in Ellipse has not been analyzed to determine the usefulness/value/necessity of unused/obsolete inventory.

Without a written Inventory Management Policy and documented procedures, parts and tool records may be incomplete and inconsistent, and obsolete inventory may remain on-site and on the books, and parts, tools, and precious items may be unsecured.

Recommendations:

Management should establish a written:

(A) Inventory Management Policy to address:

- (1) Accounting and securing precious items, metals, parts, and tools;
- (2) Disposal of obsolete or broken parts and tools;
- (3) Reconciliation of on-hand quantities of parts and tools, and
- (4) Employee counseling and/or reimbursement for lost or damaged agency assets.

(B) Set of current procedures to address:

- (1) Performance of full inventory counts of all parts and tools;
- (2) Enhancement of the inventory process to not display on-hand quantities during cycle and full counts;
- (3) Standardization of inventory records, so consistent inventory documentation and descriptions are used on logs and in Ellipse;
- (4) Determining and disposing of obsolete inventory;
- (5) Securing and disposing of precious items;
- (6) Investigation requirements for inventory count discrepancies;
- (7) Management oversight of tool check-out and return processes, and
- (8) Timely removal of physical and logical access to the inventory and associated data.

Views of Responsible Officials:

Taking into account the attached comments, management will establish a written Inventory Management Policy that addresses the four (4) components listed in the audit recommendation. Also, management will establish or modify current written procedures that addresses the other eight (8) components listed in the audit recommendation. These policies and procedures will be written in a manner that will provide the most operationally efficient and economical method.

Responsible Parties:

Chief Financial Officer & Chief Operations Officer

Due Date:

August 31, 2020



Memo

To: Mary Modelski - Internal Audit
From: Ray Abraham, Chief Operations Officer
Date: December 23, 2019
Re: OMC Non-Capitalized Rail Parts and Tools Inventory Audit

Below are additional comments related to the OMC Non-Capitalized Rail Parts and Tools Inventory Audit for attachment to the report.

- 1. Inventory Counts (Page 5)** - The items that do not have a stock code would be those in which a quantity would not need to be on hand. They would not be stock coded as they are procured when needed in the field (MOW).
- 2. The counts were completed typically one to four days later (Page 7)** - Count sheets will now be prioritized to be counted upon receipt of them.
- 3. Stockroom personnel indicated they reviewed inventory records to investigate any discrepancies, but they did not record the specifics of the reviews and indicated no variance on the reports. Therefore, Internal Audit was unable to test the discrepancy investigation process. (Page 7)** - Any variances are corrected through research. If the issue cannot be identified and a correction cannot be performed, the discrepancy will be noted on the sheet.
- 4. Obsolete Inventory (Page 8)** - Inventory parts register: Inventory counts of all items that should be in Ellipse will be conducted by the Asset Management Consultant and identified for entry to the upcoming new asset maintenance system. Obsolete items are directed from staff (MOW) to finance for approval to remove from inventory.
- 5. The MOW maintains spools of copper wire in the MOE basement. Personnel removing wire are to write on the spool the remaining length of wire. However, there are no documented procedures to determine if wire has been removed or to verify remaining length of wire on spools. (Page 9)** - We will begin using cable seals to secure to the ends of the cables (See Attached Picture). A procedure will be developed to monitor and replace.

Page 2

6. **Based on the Snap-On Incorporated and Grainger website pricing in November 2019, Internal Audit determined an approximate replacement values for the tools indicated as missing as; \$23,000 for the 176 Traction Power tools and \$9,100 for the 78 SigCom tools (Page 10).** – It is important to note that the missing tools identified could be a cumulation of shrinkage over a long period of time.
7. **Procurement (Page 13)** - At manager level, the MOW purchaser has authority to purchase up to \$25,000. When necessary, an approved requisition is received from the MOW manager for specific items. Hutchinson was approved and contracts handled bid prior to the PO. (See attached Board approval Feb 2018). Contracts and Procurement staff can have access to Ellipse. They do not choose to use it. One CA is trained on Ellipse. Ellipse Administrator can run a report anytime if C&P wants it. Supply agreement suppliers are sent to C&P for a supply agreement. The current run of PO's for the year (see attached) shows no vendor over \$150,000 unless board approved and on contract (or C&P approved sole source PO (over \$50k) was obtained).
(A) Inventory Management Policy to address:
 8. **Accounting and securing precious items, metals, parts, and tools (Page 16)** - See comment 5. Also, once the larger stockroom has been built it will allow us more room to create lockable storage.
 9. **Disposal of obsolete or broken parts and tools (Page 16)** - We have been engaged with finance regarding this issue.
(B) Set of current procedures to address:
 10. **Enhancement of the inventory process to not display on-hand quantities during cycle and full counts (Page 16)** - Not sure why this is needed. During cycle counts the counter will not know if there is a discrepancy with the QTY's.
 11. **Investigation requirements for inventory count discrepancies (Page 16)** - We do not agree to eliminate the Stock on-hand quantities from the cycle count sheets. This will create another tedious procedure that will not benefit the process.