PROJECT SUMMARY

Overview

Controls within certain areas of West Texas A&M University’s physical plant operations require improvement to ensure that resources are used efficiently and effectively and in compliance with laws, policies, regulations, and University rules. Inventory management controls need to be significantly strengthened to properly safeguard and manage the parts and materials maintained in stock which were valued at over $300,000. Also, significant improvement is needed to the work order billing and cost allocation processes. The upgrade of the University’s work order system, currently being implemented, will greatly facilitate improvements in these areas. Other opportunities for improvement include administration and compliance related to construction projects and procurement card purchases.

The University’s Physical Facilities consists of two functional divisions, Physical Plant and Engineering & Architectural Services that oversee all operations including building maintenance, grounds maintenance, custodial services, locksmith, transportation services, and construction administration. Overall feedback received for services provided to other University departments was positive according to a survey completed in fiscal year 2009. Physical Facilities had an operating budget of more than $6.5 million in fiscal year 2010 with approximately 110 employees on staff.

Summary of Significant Results

Warehouse Inventory

Controls over warehouse inventory processes are weak and require improvement to ensure that resources are properly accounted for and used efficiently and effectively to achieve the department’s objectives. Improvements needed include development of comprehensive written inventory control procedures, maintaining updated and accurate perpetual inventory records, periodically counting and reconciling physical inventory to the inventory records, maintaining a proper segregation of duties,
and further restricting physical access to inventory. Weaknesses in controls over the Physical Plant’s warehouse inventory operations increase the risk for inappropriate and inefficient use of inventory resources. Completing the current upgrade of the work order system to track inventory and further centralizing inventory stock would better facilitate the implementation of strong inventory controls and enhance the efficiency and effectiveness of inventory processes.

**Work Order Billings and Cost Allocations**

Current work order billings and cost allocation processes do not provide assurance that customers are properly billed and the Physical Plant receives appropriate cost recovery for services performed. There is currently a large number of open work orders initiated prior to fiscal year 2010 for which it has not yet been determined whether the customer was properly billed. The Physical Plant also charges customers for costs directly incurred such as salaries and materials used, but there was no documentation indicating that depreciation and other overhead expenses were also included in these rates or billings for full cost recovery. There is a greater risk that educational and general funds are indirectly used to subsidize auxiliary enterprises, which is prohibited by the state’s General Appropriations Act.

**Summary of Management’s Response**

*West Texas A&M University identified in fiscal year 2009 the need for better management controls over inventory within the individual departments of the Physical Plant as well as the need for a better management system to monitor work order billings and related analysis of the services provided by the Physical Plant to all departments. As a result of this identified need, a new work order software system was purchased in fall 2009. The work order software system, TMA, will provide an automated inventory system as well as a billing system to include a management reporting function to monitor inventory, work order billings and track time and effort reporting to provide opportunities for efficiencies. Implementation, testing and training occurred throughout fiscal year 2010, with the system scheduled to be fully functional September 1, 2010. Formal written procedures will be completed by the end of November 2010.*
Scope

The review of financial and management controls within the University’s Physical Facilities focused on the areas of warehouse inventory management, billing rates and cost allocations, construction administration, building maintenance, procurement of goods and services, and deferred maintenance processes. Transactions and activities related to these areas were reviewed primarily for the period September 1, 2008 through February 28, 2010. Fieldwork was conducted primarily from March through May 2010.
OBSERVATIONS, RECOMMENDATIONS, AND RESPONSES

1. Warehouse Inventory

Observation

Warehouse inventory items being maintained in stock at the Physical Plant had a total cost of over $300,000 as of the date of test work. Controls over warehouse inventory processes are weak and require improvement to ensure that these resources are properly accounted for and used efficiently and effectively to achieve the department’s objectives. Comprehensive written inventory procedures have not been prepared as recommended during a previous audit and perpetual inventory records are not maintained and periodically reconciled to physical inventory counts. The lack of controls and accurate information also limits the ability to establish accurate inventory reorder points using updated inventory information. The duties of ordering, receiving and issuing inventory are not adequately segregated and physical access to inventory is not restricted to only those who need access.

Lack of adequate controls over the Physical Plant’s warehouse inventory operations increases the risk for inappropriate and inefficient use of inventory resources. Inventory is located at multiple locations within the various Physical Plant shops. The University has also been using an outdated version of the TMA Work Order software which does not facilitate automated inventory management and work order processing. Management has purchased and is currently working to implement a newer version of this software. As a result, resources available for managing the inventory of supplies and materials are spread between multiple locations and few automated inventory management processes have been implemented which inhibits the ability to effectively and efficiently manage this inventory.

The Committee of Sponsoring Organizations (COSO) Report, Internal Control – Integrated Framework, states that as a physical control – “Equipment, inventories, securities, cash and other assets are secured physically, and periodically counted and compared with amounts shown on control records.”
Recommendation

1. Warehouse Inventory (cont.)

Complete the upgrade and implementation of the new version of the TMA work order system software. Develop and implement comprehensive written internal procedures for the Physical Plant warehouse inventory operations which addresses the inventory control issues noted above as well as the use of any new work order system functionality. Ensure that these procedures are properly disseminated to all relevant employees and corresponding training is provided for use of the work order system as needed.

Ensure all supply inventory is tracked and safeguarded including any excess supplies that have continuing value to the University such as those remaining from construction projects or other physical plant activities. Consider these items prior to ordering similar items for increased efficiency of inventory purchases. Identify all obsolete items and send to surplus in order to reduce the amount of inventory that must be tracked and controlled.

Consider further consolidating all inventory items within one main warehouse operated with trained inventory staff. The main warehouse could house bulk inventory and distribute inventory items to satellite locations as requested. This would help streamline inventory operations by allowing implementation of centralized inventory controls such as one inventory reconciliation and one physical security structure to maintain for the majority of the inventory.

Management’s Response

Warehouse Inventory

The Physical Plant uploaded the entire Physical Plant warehouse inventory into the newly installed TMA 8.1.0.16 version during the week of August 30, 2010. The new warehouse inventory system is now in operation. Formal written procedures will be completed by the end of November 2010. These procedures will include requirements for tracking and safeguarding excess supplies such as those remaining from construction projects and identifying obsolete items to send to be surplused.

The TMA program will provide daily warehouse inventory usages by billing the item on a work order, and then reducing that item from the existing stock. The tracking of used items from inventory occurs instantly and the reorder points are more easily identified. This development offers a rapid reconciliation of warehouse inventory items as they are used. This program enhances the billing of warehouse inventory and allows a monthly, quarterly or annual
The work order billing and cost allocation process does not ensure accurate and complete billings for work performed and is not in compliance with A&M System regulations.

The Physical Plant has 400 "Demand" work orders and 418 "Preventative" work orders initiated prior to fiscal year 2010 that are still open with some that date back several years. There are also thirteen emergency work orders initiated between October 2009 and March 2010 that are still listed as being open. Physical Plant staff recently contacted customers who initiated some of these open work orders and concluded that the work had been completed, but have not yet determined whether University customers were properly billed.

Comprehensive written procedures have not been developed for establishing billing rates and allocating costs at the Physical Plant. In addition, portions of the rate setting and cost allocation process are not adequately documented with supporting schedules and other accounting records in compliance with A&M System regulations. The Physical Plant charges customers for costs directly incurred such as salaries and materials but there was no documentation indicating that depreciation and other overhead expenses were also included in these rates or billings for full cost recovery. In addition, rates and corresponding accounting records related to costs, revenues, billings, collections, and surpluses or deficits are not established and adjusted annually for each separate service provided in compliance with A&M System regulations.
Adequate work order billing and cost allocation processes are important to ensure that customers are properly billed and the Physical Plant receives appropriate cost recovery for services performed. This also helps ensure that educational and general funds are not indirectly used to subsidize auxiliary enterprises, which is prohibited by the state’s General Appropriations Act. A&M System Regulation 21.01.05 states that each System component is responsible for establishing user rates, maintaining proper documentation of rate calculations, verifying that rates are not discriminatory towards different groups of users, and periodically reviewing operations for compliance.

Recommendation

Research existing open work orders and take the necessary actions to close these out. Implement a procedure to regularly monitor and address open work orders in a timely manner and ensure that all work performed is properly billed. Upon completing the upgrade to the TMA work order system, attempt to capture the labor and material usage information to the extent feasible within this system to better ensure work order billings are accurate and complete as well as provide additional management information for decision-making.

Develop and implement comprehensive internal documentation for the rate setting and cost allocation process at Physical Facilities. This documentation should include written procedures and other supporting schedules and accounting records used to establish rates and allocate costs for each service provided especially indirect costs such as overhead and depreciation. Ensure that the requirements within A&M System Regulation 21.01.05, Service Departments, are incorporated into this process and the related procedures. Coordinate with the Business Office for assistance in establishing these rates and the necessary supporting schedules and accounting records as needed.

Management’s Response

Work Order Billings

The identified demand work orders that were still open have been closed. From November 2005 through August 2009 there were 69 open work orders. Of the open work orders there was 1 in 2005, 5 in 2006, 32 in 2007, 19 in 2008, and 12 prior to September 1, 2009.
2. Work Order Billings and Cost Allocations (cont.)

Of the remaining open work orders there was a total projects loss of $2,055.00 in chargeable work that occurred but was never closed or billed. All of these work orders have been closed and the Physical Plant is working on the current 2009-2010 year-end closing to track, close and bill all remaining work orders for this year.

The identified preventative work orders that were open have been closed. These preventative work orders do not include a cost variable to the Physical Plant, they are completed as routine work assignments and no billings occur. These are internal work orders to the various Physical Plant departments as reminders for performing routine preventative maintenance. Examples are changing air filters, cleaning steam traps and greasing of bearings.

With the new TMA program, the tracking of preventative work orders can occur on a monthly basis. Each shop manager has access now to the TMA program which historically was not the case. The preventative work orders will appear on each manager’s computer and it will serve as a reminder to not only complete the work but document it in the TMA Program. The Director of Physical Plant Operations shall provide a printout each month of open preventative maintenance work orders to shop managers to increase efficiency.

Cost Allocations

The Physical Plant has historically billed work at a per hour rate for shop labor, and a per hour rate for manager labor. Most work was billed at a minimum of one (1) hour per work order; however, last year the Physical Plant implemented a quarter hour billing charge where minor work requests that took a less amount of time could be billed appropriately.

The Physical Plant charges labor rates and material on a cost basis. By charging on a cost basis for labor and material, this mechanism allowed for the “cost neutral” impact to E&G expenditures. The University will revise the calculation based on A&M System regulations that provide for the formal comprehensive internal documentation. This analysis and documentation will be completed by end of February 2011.

3. Construction Administration

Observation

Eighteen minor construction projects were initiated by the University during the audit period totaling more than $13 million. Physical Facilities administers these projects through its Engineering & Architectural Services division and primarily relies on job order
contracting with outside contractors to perform the work. However, the University’s job order contracting process for construction projects is not in compliance with state requirements related to the use of preapproved price lists or tasks, job order contract term lengths, and bid opening procedures. Testing performed on six of the minor construction projects initiated during the audit period indicated that these projects were generally in compliance with System construction requirements. However, it was noted that one construction project tested totaling $3 million was completed in phases which resulted in each phase of the project falling under the University’s $2 million delegated authority limit. This allowed the construction work to be administered at the university-level. A project analysis or other documentation supporting the reason for completing the project in phases was not available. In addition, construction contracts reviewed during testing did not include a "Right to Audit" or a "Business Ethics Expectations" clause which is considered standard business practice in construction contract provisions.

Comprehensive procedures have not been developed to document the construction administration process including the areas mentioned above. Without adequate written procedures there is a greater risk that construction projects will not be performed in compliance with various laws, policies, and regulations. Texas Education Code 51.784, Job Order Contracts for Construction or Repair, states that an institution may award job order contracts for the minor construction, repair, rehabilitation, or alteration of a facility if the work is of a recurring nature but the delivery times are indefinite and indefinite quantities and orders are awarded substantially on the basis of pre-described and pre-priced tasks. In addition, sealed job order contract proposals shall be publicly opened and the base term of a job order contract may not exceed two years without further advertisement and solicitation of proposals if the institution fails to advertise the term.

Recommendation

Develop and implement comprehensive written procedures for the University’s construction process. Ensure compliance with state job order contracting requirements by utilizing preapproved contract unit pricing for job order contracts, adding the stated term of the job order contract in the advertised proposal or restricting the term of these agreements to two years, and opening the sealed job order contract proposals received publicly. Provide adequate analyses or other documentation of management decisions to complete construction projects in phases especially when the total project costs will exceed current delegations of authority. Include a "Right
3. Construction Administration (cont.)

Management’s Response

The University will develop and implement comprehensive written procedures for the construction process. These procedures will be developed, approved and implemented December 2010. The University construction contracts have been revised to include the “Right to Audit” and “Business Ethics Expectations” clause for all future contracts effective September 1, 2010.

4. Procurement Cards

Observation

Procurement card purchases tested were not in compliance with certain University and state purchasing requirements.

The University’s Physical Plant purchased over $1 million of goods and services using procurement cards during fiscal year 2009. During testing of twenty procurement card purchases over $2,000, it was noted that 13 were not bid due to being either an emergency or a proprietary purchase based on the description provided. However, full written explanations were not provided for eleven or 85% of these exceptions as required by University and state purchasing requirements. In addition, receiving documentation was not available for procurement card purchases made via the mail, Internet, and phone.

Procurement cards have a $2,000 single purchase limit at the University which precludes them from many purchasing requirements such as purchase requisitions, bidding, etc. However, an exemption has been made to allow the Physical Plant to make purchases up to $25,000 using the procurement card. Although procurement card procedures have been developed, they do not specifically address additional requirements for procurement card purchases over $2,000 such as purchase requisitions, bidding, and required documentation for emergency and proprietary purchases. In addition, there is currently no University requirement for receiving documentation to be maintained for procurement card purchases made via the mail, Internet, and phone.

The University’s Standard Administrative Procedure for Purchasing Authority requires that whenever possible, purchases shall be based on competitive bids and in accordance with the best value decision process. Negotiation of contracts is allowed for emergency purchases when there is insufficient time to solicit bids and proprietary purchases of items for which there is only one source of supply. For an emergency purchase exceeding $2,000,
4. Procurement Cards (cont.)

a department must provide a full written explanation of the emergency along with other specific documentation. For purchases which limit consideration to one manufacturer, one product, or one service provider, a written justification must be provided and is subject to review by the University. In addition, Texas Administrative Code 34, Rule 5.57, Use of Payment Cards by State Agencies, requires that a purchase document that a state agency submits to the uniform statewide accounting system for payment to a payment card issuer must comply with the Comptroller’s general requirements for the submission of those documents. Recently the State Comptroller’s Office, as part of their post payment audits, has required that separate receiving documentation be maintained indicating receipt of goods or services for procurement card purchases other than point-of-sale.

Recommendation

Revise current procurement card procedures to address requirements for purchases over $2,000 including written justifications for emergency and proprietary purchases and maintaining receiving documentation for purchases made via the mail, Internet, and phone. Monitor for compliance with these procedures including the purchasing requirements noted above.

Management’s Response

The A&M System recently made a revision to the delegation of authority Regulation 27.04.01. The University is reviewing all of the delegated authority documents. The University expects to have reviewed and modified our procedures by end of February 2011.
BASIS OF REVIEW

Objective

The objective of the audit was to review and assess financial and management controls over the University’s physical plant operations to determine if resources are used efficiently and effectively and in compliance with laws, policies, regulations, and University rules.

Criteria

Our review was based upon standards as set forth in the System Policy and Regulation Manual of The Texas A&M University System; Texas Administrative Code; West Texas A&M University Rules and procedures; the Texas Procurement and Support Services Procurement Manual; the Treadway Commission’s Committee of Sponsoring Organization’s Internal Control - Integrated Framework (COSO); and other sound administrative practices. This audit was performed in compliance with the Institute of Internal Auditors’ “International Standards for the Professional Practice of Internal Auditing.”

Additionally, we conducted this performance audit in accordance with generally accepted government 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 that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

Physical Facilities is comprised of approximately 110 full-time positions that report to the Associate Vice President of Physical Facilities who in turn reports to the Office of the Vice President of Business and Finance. The mission of Physical Facilities is to provide an environmentally safe, aesthetically pleasing, physically secure and pleasant campus in the most economical manner possible for students, faculty, and staff. To achieve this mission the Physical Facilities has two primary functional divisions which provide most of the physical plant operations for the University. The two divisions are Physical Plant and Engineering & Architectural Services. The Physical Plant is further divided into nine shops including Air Conditioning/Refrigeration, Carpentry, Custodial,
Electric, Grounds Maintenance, Lock, Paint, Plumbing, and Transportation. These functional divisions perform a wide range of services to the University including building maintenance, grounds maintenance, custodial, locksmith, transportation services, and construction administration. In fiscal year 2009 and fiscal year 2010, the annual operating budget was approximately $6.23 million and $6.68 million, respectively. Physical Facilities is responsible for maintaining approximately two million square feet of building space and 114 acres of landscape.
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