



**June 8, 2011**

**To:** Finance and Administration Committee

**From:** Will Kempton, Chief Executive Officer

**Subject:** Review of Warranty Administration

### **Overview**

The Internal Audit Department has completed a review of the Orange County Transportation Authority's Warranty Administration process. Based on the review, the Internal Audit Department has determined that procedures are in place to ensure that potential claims are processed for possible warranty credit. The Internal Audit Department made one recommendation for enhancement to the Warranty Administration process, and management has implemented the recommendation.

### **Recommendation**

Receive and file the Review of Warranty Administration, Internal Audit Report No. 09-023.

### **Background**

Potential warranty claims are processed by warranty personnel under the Contracts Administration and Materials Management Department (Camm) of the Finance and Administration Division. The warranty group identifies potential warranty claims by gathering information from several sources, including maintenance work orders and receipt of parts physically transferred to the warranty group.

According to the Warranty Claims Summary report prepared by Warranty Administration, the total of all warranty recoveries for the fiscal year ended June 30, 2011, was \$3,274,723.94. Warranty recovery for the nine months ending March 31, 2011, was \$2,057,356.73. Warranty recoveries include vendor payments, vendor credits, and the estimated value of warranty work performed by vendors at no charge to OCTA.

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***Discussion***

The objective was to determine the adequacy of procedures in place to ensure that all potential claims are processed and collected. The scope of the review included the period from January 2010 through March 2011.

The Internal Audit Department (Internal Audit) reviewed Warranty Administration procedures, Warranty Administration summary reports, and a judgmental sample of detail support for the summary reports.

***Summary***

Based on the review, Internal Audit has determined that procedures are in place to ensure that potential claims are processed for possible warranty credit. Internal Audit made one recommendation for enhancement to the Orange County Transportation Authority Warranty Administration process, and management has implemented the recommendation.

***Attachment***

- A. Review of Warranty Administration, Internal Audit Report No. 09-023

**Approved by:**



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Janet Sutter  
Acting Executive Director, Internal Audit  
714-560-5591

# Orange County Transportation Authority Internal Audit Department



## Review of Warranty Administration

INTERNAL AUDIT REPORT NO. 09-023

May 26, 2011



**Internal Audit Team:**

Janet Sutter, CIA, Acting Executive Director, Internal Audit  
Gerry Dunning, CIA, CISA, CFE, Senior Internal Auditor

**ORANGE COUNTY TRANSPORTATION AUTHORITY**  
**INTERNAL AUDIT DEPARTMENT**  
**Review of Warranty Administration**  
**May 26, 2011**

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## **CONCLUSION**

The Internal Audit Department (Internal Audit) has completed a review of the Orange County Transportation Authority's (OCTA) Warranty Administration process. The primary purpose of the review was to verify that procedures are in place to ensure that potential claims are processed for possible warranty credit.

Based on this review, Internal Audit has determined that, procedures are in place to ensure that potential claims are processed for possible warranty credit. Internal Audit has made one recommendation for enhancement to the OCTA Warranty Administration process.

## **BACKGROUND**

The Orange County Transportation Authority Internal Audit Plan for Fiscal Year 2010-11 included a review of Warranty Administration. Potential warranty claims are processed by warranty personnel under the Contracts Administration & Materials Management Department (CAMP) of the Finance and Administration Division. The warranty group includes a senior warranty coordinator, a warranty coordinator and an associate warranty coordinator. The group reports to the section manager of the Inventory Team within CAMP.

The warranty group identifies potential warranty claims by gathering information from several sources, including maintenance work orders and receipt of parts physically transferred to the warranty group. In order to file a potential claim, warranty staff must have the bus number, work order number, and a statement of the problem related to replacement of the part. In most cases, warranty staff must also have possession of the part so that it can be returned to the supplier for credit.

When a potential claim is identified, warranty staff records the details on a Warranty Claims Log that is maintained for tracking purposes. The log includes the claim number, date submitted, bus unit number, part number (if applicable), OCTA work order number, description of the failure, vendor invoice number (if applicable), claim amount, amount received, date closed, and the check number (if applicable).

According to the Warranty Claims Summary report prepared by Warranty Administration, the total of all warranty recoveries for the fiscal year ended June 30, 2010, was \$3,274,723.94. Warranty recovery for the nine months ending March 31, 2011, was \$2,057,356.73. Warranty recoveries include vendor payments, vendor credits, and the estimated value of warranty work performed by vendors at no charge to OCTA. On average, warranty recoveries average between \$100,000 and \$400,000 per month.

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**OBJECTIVES, SCOPE, AND METHODOLOGY**

The objective of this review was to determine the adequacy of procedures in place to ensure that all potential claims are processed and collected. The scope of the review included the period from January 2010 through March 2011. The review methodology included, but was not limited to, the following:

- Interview of the section manager of the Inventory Team responsible for the warranty function
- Interview of the senior warranty coordinator
- Reviewed APTA Standard Bus Procurement Guidelines RFP-Section 7: Warranty Requirements
- Reviewed sample of a Warranty Schedule for New Flyer “CNG” bus
- Performed a walkthrough of the warranty process at the Santa Ana Base
- Reviewed the Warranty Claims Log for the period January 2010 through November 2010
- Reviewed detail support for a monthly warranty recoupe worksheet
- Reviewed sample of the Parts Down, Bus Hold list
- Reviewed samples of the Daily Warranty update report for each base
- Reviewed sample of Ellipse report reflecting potential warranty claims
- Reviewed CAMM Warranty Procedure CAMM/WARR002, Material Management Failures Under Warranty Procedure
- Reviewed CAMM Warranty Procedure CAMM/WARR003, Material Management Updating the Warranty Hold List Procedure
- Reviewed CAMM Warranty Procedure CAMM/WARR004, Material Management Ordering Parts Under Warranty Procedure
- Reviewed CAMM Warranty Procedure CAMM/WARR005, Material Management Filing Warranty Claims Procedure
- Reviewed CAMM Warranty Procedure CAMM/WARR006, Material Management Off-Property Warranty Claims Procedure
- Reviewed collective bargaining agreements for Maintenance and TCU employees that include incentives for Warranty Recovery
- Reviewed a sample of warranty checks received and deposited by OCTA Accounts Receivable

This review was conducted 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 the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

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**Audit Comments, Recommendations and Management Responses**

**Noteworthy Accomplishments**

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Warranty recoveries have averaged \$253,908 per month for the twenty-one months ending March 31, 2011. This amount includes vendor payments, vendor credits, and the estimated cost of warranty work performed by vendors at no charge to OCTA.

**Warranty Claims Log**

The Warranty Claims Log maintained by OCTA warranty staff does not include explanation for claim numbers deleted from the log.

When a potential warranty claim is received it is entered into an excel spreadsheet and assigned a sequential number. If the part is later determined to be ineligible or the claim otherwise invalid, the item is deleted from the spreadsheet, resulting in a spreadsheet with missing sequential numbers.

In order to ensure proper tracking of all potential claims, warranty staff should include all items on the log along with the final disposition of the items; including ineligible items, rejected claims, etc.

**Recommendation:** Internal Audit recommends that staff include and maintain the disposition of all potential warranty claims on the Warranty Claims Log.

**Management Response (CAMP):** Management concurs with the recommendation to include and maintain the disposition of all potential warranty claims on the Warranty Claims Log. This change has already been implemented in the warranty log. The pre-assigned claim numbers listed on the warranty log shall be maintained in sequential order regardless of the claim disposition.