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Accounting and Information
Management Division

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March 3, 1999

The Honorable John R. Kasich
Chairman, Committee on the Budget
House of Representatives

Subject: Financial Management: Briefing on the Federal Aviation Administration's
Inventory Accountability

Dear Mr. Chairman:

This letter responds to your request that we determine (1) whether the Federal Aviation Administration's (FAA) systems can accurately account for and control inventory quantities and (2) how FAA identifies and manages excess inventory quantities. This letter summarizes the information provided during a February 16, 1999, briefing to your staff on these two areas. The briefing slides are enclosed.

FAA's inventory consists primarily of items centrally warehoused at the Mike Monroney Aeronautical Center (Logistics Center) in Oklahoma City, Oklahoma, and at field spare sites at over 34,000 locations throughout the United States. Many of these field spare sites are at remote locations.

Based on our analysis of Logistics Center inventory test counts of a statistical sample of inventory, we concluded that the Logistics Center's recorded inventory quantities were generally reasonable as of September 30, 1998. In addition, based on our review of Logistics Center inventory system controls, we concluded that the inventory system provides a reasonable basis for tracking and controlling inventory.

We concluded from analyzing the Department of Transportation (DOT) OIG's field spares inventory workpapers that the accuracy of field spares inventory quantities, and the ability of the system to track and control field spares is uncertain. The OIG found numerous errors in inventory recordkeeping, and procedures and controls were not fully implemented. FAA is in the process of implementing new procedures for managing field spares inventory. FAA is also planning a complete field spares inventory count for fiscal year 1999.

We found that FAA has established processes for identifying and managing excess inventory. The Logistics Center processes are in place; however, processes in the field were not fully implemented as of September 30, 1998.

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In January 1999, we designated FAA financial management as a high-risk area. Since 1990, we have periodically reported on government operations identified as high risk because of their greater vulnerabilities to waste, fraud, abuse, and mismanagement. Our high-risk status reports are now provided at the start of each new Congress and the latest, High-Risk Series: An Update (January 1999, GAO/HR-99-1), was recently issued. Over time, as high-risk operations have been corrected, we have removed those improved areas from the list. Also, as other risks have emerged, we have added new ones to keep the Congress current on financial weaknesses needing more management attention. The FAA's high-risk designation means we will be giving sustained attention to monitoring its efforts to achieve financial accountability.

We conducted our work from August 1998 through January 1999 in accordance with generally accepted government auditing standards. We requested comments on our draft briefing slides from the FAA and DOT Office of Inspector General. We received some clarifying comments that we incorporated into our slides as appropriate.

We are sending copies of this letter to the Ranking Minority Member of your Committee, the Secretary of Transportation, the DOT Chief Financial Officer, the FAA Administrator, the Director of the Office of Management and Budget, and other interested parties. Copies will also be made available to others upon request.

If you have any questions about this letter or the earlier briefing, please contact me at (202) 512-9508 or John Fretwell, Assistant Director, at (202) 512-9382.

Sincerely yours,



Linda M. Calbom
Director, Resources, Community,
and Economic Development, Accounting
and Financial Management Issues

Enclosure

(913850)

GAO

Accounting and Information Management Division

FEDERAL AVIATION ADMINISTRATION

Inventory Accountability Review

Status Briefing for the House Budget Committee

February 16, 1999

GAO Contents

- Objectives
- Background
- Logistics Center Review
- Field Spares Review
- Excess Inventory Review
- Actions Being Taken by FAA

GAO Objectives

- Determine whether FAA's systems can accurately account for and control inventory quantities
- Determine how FAA identifies and manages excess inventory quantities

GAO Background--FY 1997 Financial
Statement Audit Results

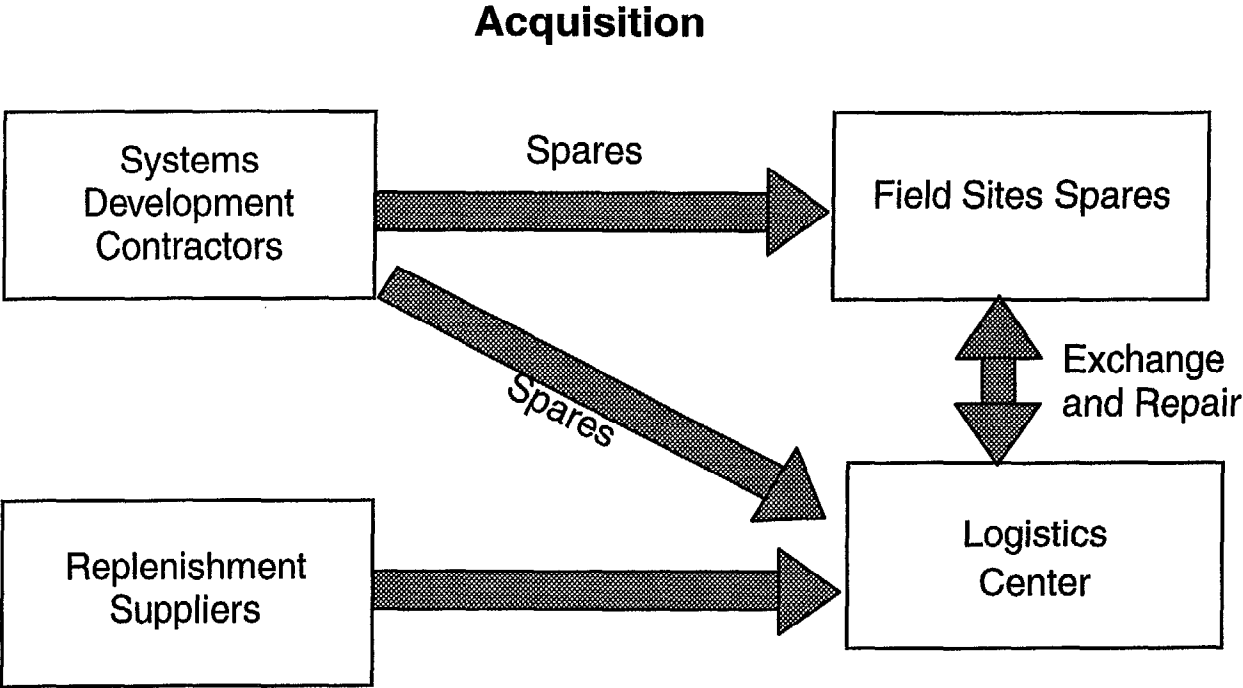
- OIG unable to issue an opinion due in part to significant deficiencies in accounting for inventory and related property
- OIG concluded that there were significant inconsistencies in inventory counting procedures and unexplained variances in inventory amounts.

GAO **Background--Recorded Inventory
Amounts at September 30, 1998**

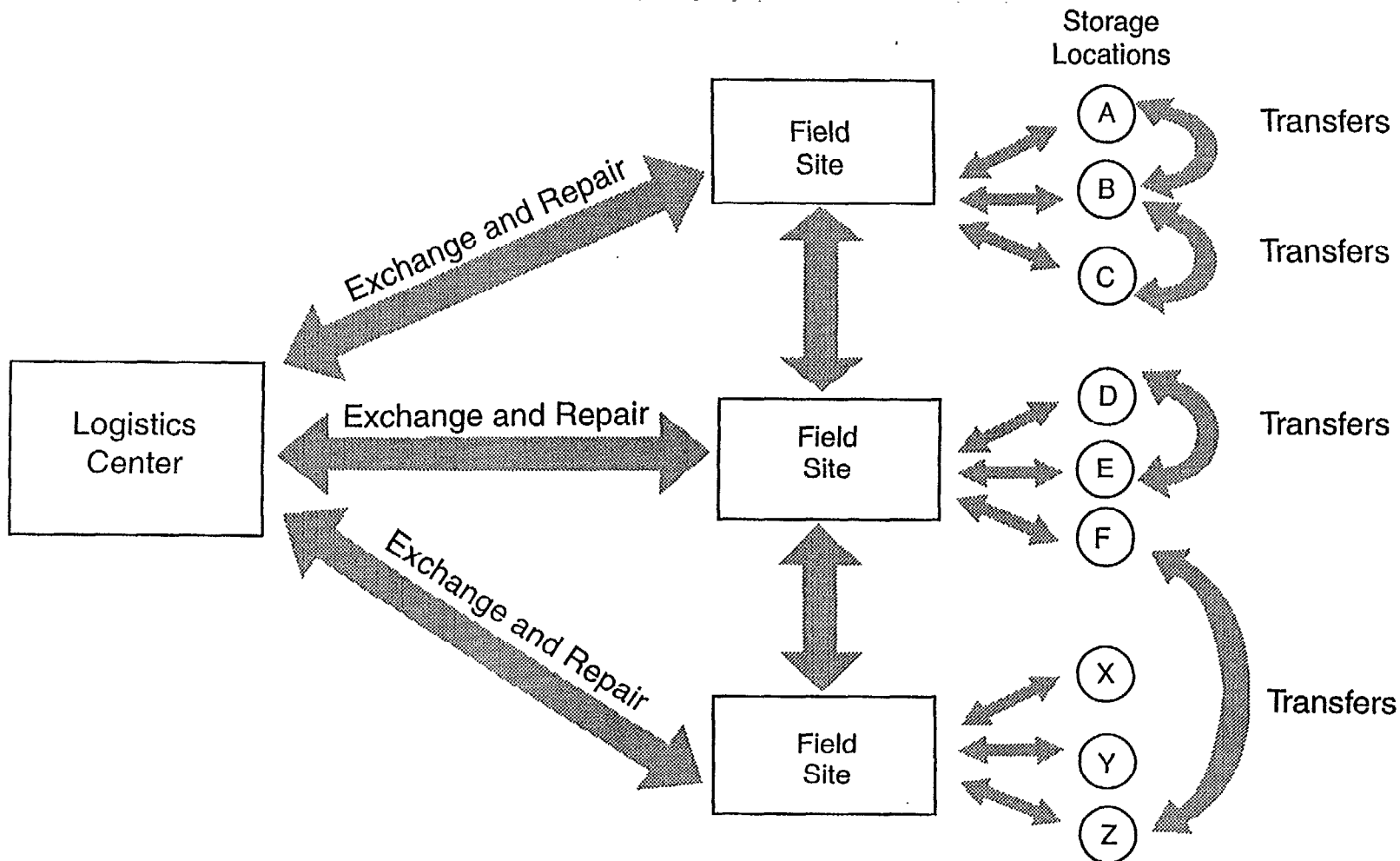
<u>Locations</u>	<u>Dollars (Millions)</u>	<u>Percent</u>
Logistics Center	\$543	59.7
Field spare sites	338	37.2
Aviation sites	<u>28</u>	<u>3.1</u>
Total	\$909	100.0

Note: The total amount presented represents balances before valuation reductions at year end for items to be repaired and for excess inventory.

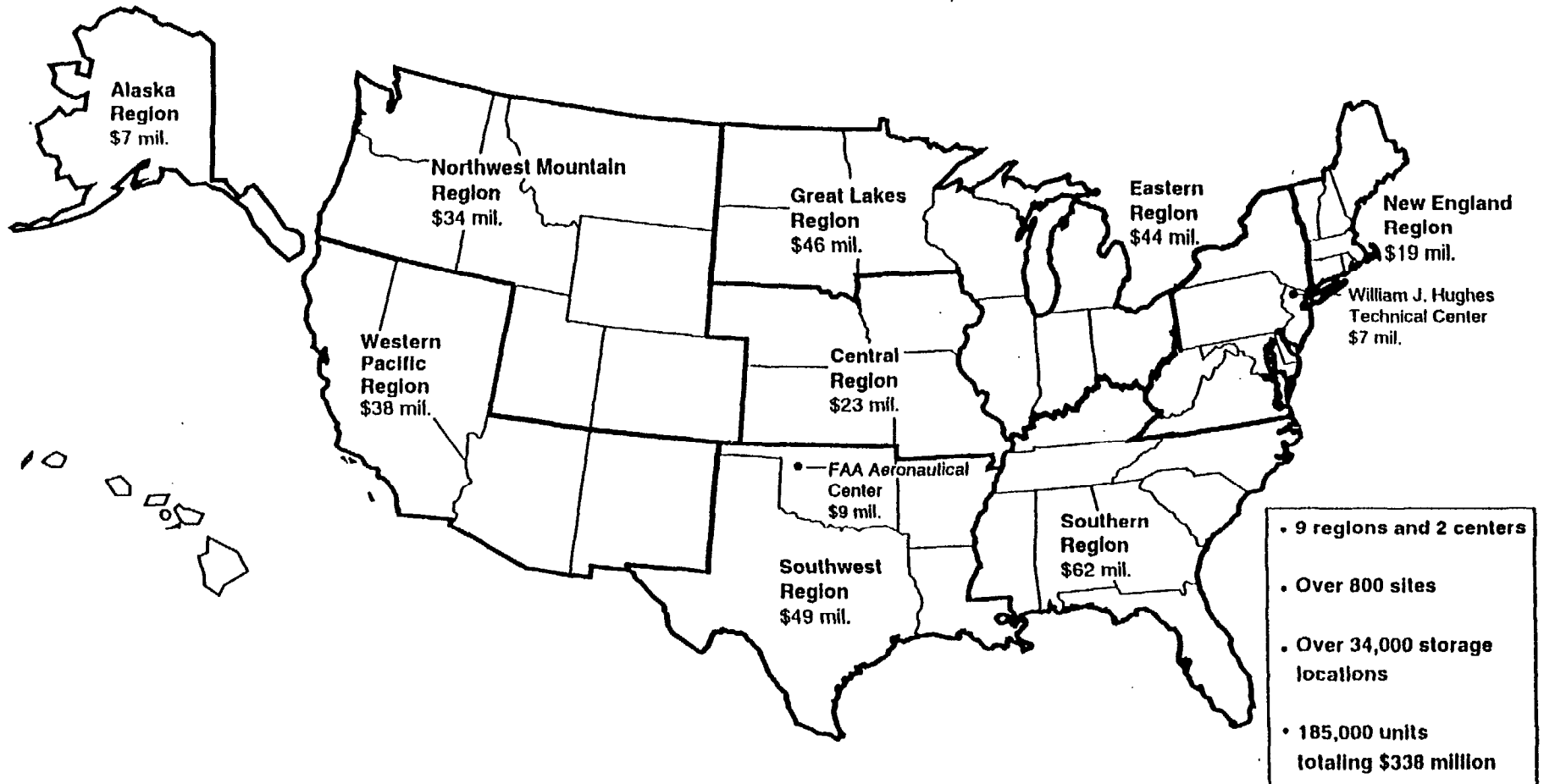
Background--Inventory Overview Acquisition Activities



GAO Background--Inventory Overview Exchange & Repair (E&R) Spares Activity



Background--Field Spares in FAA Regions and Centers



Source: FAA

GAO Logistics Center Review--
Scope and Methodology

- Reviewed centralized warehouse inventory at Mike Monroney Aeronautical Center in Oklahoma City, Oklahoma
- Test counted statistical sample of inventory
- Analyzed results
- Projected errors
- Assessed systems controls over quantities

GAO Logistics Center Review-- Inventory Accountability

Test Count Results

	Units (Thousands)	Dollars (Millions)
Total tested	2,126.7	\$145.72
Overstatements	40.0	\$1.58
Understatements	.4	\$1.62
Differences-gross	40.4	\$3.20
Gross percentage difference	1.9%	2.2%

GAO Logistics Center Review--
Inventory Accountability

Examples of More Significant
Dollar Differences

<u>Exception item</u>	<u>Record quantity</u>	<u>Actual count</u>	<u>Quantity difference</u>	<u>Dollar difference (Thousands)</u>
Rotary joint	72	66	(6)	(\$269)
Digital data set	16	17	1	55
VHF receiver	746	834	88	269

GAO Logistics Center Review--
Inventory Accountability

- Reasons for Test Count Differences
 - 7% - Commingling similar items
 - 9% - Timing of processing documents
 - 22% - Prior erroneous adjustments
 - 62% - Unknown

GAO Logistics Center Review--
Inventory Accountability

Test Count Conclusions

- Dollar effect of projected quantity differences not significant to FAA's financial statements
- Some differences warrant follow-up
 - high dollar/low quantity
 - unknown reasons

GAO Logistics Center Review--
Inventory Accountability

Supplemental Tests of Limited Items

- Unknown reasons category eliminated
- Reasons for differences were similar to original test counts

GAO Logistics Center Review--
Inventory Systems Controls

Major Systems Capabilities

- Master inventory inquiry record
- Transaction history record
 - Receipts
 - Issues
 - Adjustments
- Excess inventory records

GAO Logistics Center Review--
Inventory Systems Controls

Assessment Results

Controls over quantities generally appear to be effective; however, minor control weaknesses were identified

- counting items received
- receiving documentation
- delays in recording receipts
- data entry

GAO Logistics Center Review--
Inventory Systems Controls

Conclusions

- Test counts and control assessment indicate that recorded inventory quantities are generally reasonable as of September 30, 1998
- Inventory system provides a reasonable basis for tracking and controlling inventory

GAO Field Spares Review--
Scope and Methodology

- Relied on OIG inventory test counts for 14 sites
- Gathered information from FAA officials in Headquarters and Logistics Center
- Reviewed OIG inventory workpapers
- Analyzed results
- Assessed systems controls over quantities

GAO Field Spares Review--
Inventory Accountability

Summary of OIG Tests

	<u>Sites</u>	<u>Value</u> <u>(Millions)</u>	<u>Quantity</u> <u>(Thousands)</u>
Total field spares	834	\$322	153
Sites with completed physical inventory	354	63	34
Sites tested	14	14	7
Sites with test count differences	9	9	5

Note: OIG judgmentally selected items to test at each site based on an April 1998 site listing

GAO Field Spares Review--
Inventory Accountability

Examples of OIG Test Count Differences

	<u>Quantity per record</u>	<u>Quantity per OIG count</u>	<u>Net quantity difference</u>	<u>Net Value of difference</u>
Site A	27	6	(21)	(\$67,183)
Site B	41	51	10	3,992
Site C	4	13	9	4,686
Site D	0	65	65	105,747

Field Spares Review-- Inventory Accountability

Examples of Selected Items Counted by OIG

	<u>Quantity per record</u>	<u>Quantity per OIG count</u>	<u>Difference</u>	<u>Value of difference</u>
Hard copy	0	7	7	\$13,412
	1	0	(1)	(1,370)
Hard copy	1	10	9	6,696
	6	4	(2)	(3,984)

GAO Field Spares Review--
Inventory Accountability

Type of Difference

- New parts not recorded
- Recorded items not located

Reasons for Differences

- Inventory recordkeeping not a high priority
 - Count procedures not available or not disseminated
 - Lack of training in taking physical inventory
 - Records not updated timely
-

GAO Field Spares Review--
Inventory Systems Controls

Major Systems Capabilities

- Inventory by location, quantity on hand, description of item, and system item supports
- Physical inventory history
- 3-year demand history to determine excess

GAO Field Spares Review--
Inventory Systems Controls

Assessment results

- Systems and controls had not been fully implemented as of September 30, 1998
 - Controls not established over data input
 - Receipted inventory not always recorded

GAO Field Spares Review--
Inventory Systems Controls

Conclusion

Field spares inventory accuracy and the ability of the system to track and control inventory is uncertain.

GAO Excess Inventory Review--
Scope and Methodology

- Reviewed FAA procedures for identifying and managing excess quantities
- Reviewed OIG workpapers on excess field spares
- Made limited observations of excess inventory at Logistics Center

GAO Excess Inventory Review

- Logistics Center Excess Procedures
 - Process is structured
 - Process uses monthly on-hand and usage data
 - System automatically identifies potential excesses which item managers research and resolve
 - Excess amount of \$26 million identified by FAA as of September 30, 1998
-

GAO Excess Inventory Review

- Examples of Logistics Center excess items
 - Cable--about 1 million feet--\$900,000
 - Outdated electronic sensing devices--over 1,300--\$1.3 million
 - Circuit card assemblies--over 120--\$123,000
 - Obsolete printers--over 1,400--\$2.9 million
-

GAO Excess Inventory Review

- Field Spares Excess Procedures
 - Biennial review by location--over 3-year demand considered excess
 - Excess review done when systems decommissioned
 - Procedures not fully implemented as of September 30, 1998
 - Potential excesses identified by OIG and FAA personnel in FY 1998, but not quantified
-

GAO **Actions Being Taken by FAA to
Improve Inventory Management**

- For Logistics Center FAA is developing
 - a physical inventory integrity guide
 - a long term excess inventory plan
 - procedures to check excess stock records before procuring new stock
 - plans for a bar coding system

GAO **Actions Being Taken by FAA to
Improve Inventory Management**

- For Field Spares Inventory, FAA is
 - implementing new procedures for managing field spares
 - developing a perpetual inventory system
 - developing a bar coding system
 - planning a complete physical inventory for FY 1999

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