

Corvus Business Advisors  
Fleet Management Audit Analysis & Recommendations Report  
**Summary of Recommendations**

Recommendation		Adopted by Fleet Services	Comment
1	<b>Replace Retained Earnings with a Dedicated Replacement Reserve</b> Collective initiative - includes: policy update, replacement provision calculation, charging of replacement provision, single corporate replacement reserve theory, Fleet Services/Client Department roles and responsibilities.	√	<i>Refer to Council Report 2009COM019 "Retained Earnings - Use and Disposition"</i>
2	<b>Fleet Replacement Plan and Cash Flow Projections</b>	√	
3	<b>Retention of Fleet Units as Spare Capacity</b>	√	
4	<b>Fleet Services Equipment Replacement Reserve and Provision</b>	X	<i>Will continue to follow capital budget process to fund equipment replacement.</i>
5	<b>Continue to Fund Transit Through Grant and Debt Financing</b>	√	
6	<b>Operating Vehicle and Equipment Rates</b>	√	<i>Refer to Council Report 2009COM019 "Retained Earnings - Use and Disposition"</i>
7	<b>Analysis of Fluid Retirement Assessment Approach</b>	√	
8	<b>Data Management and Integrity</b>	√	<i>Refer to Council Report 2009COM019 "Retained Earnings - Use and Disposition"</i>
9	<b>Review of Fleet Lease Practices</b>	See Comment	<i>To be reviewed with Materials Management as a joint initiative to pursue alternatives.</i>



# **Mobile Equipment Services**

## **Fleet Management Audit Analysis & Recommendations**

### **Executive Summary / Summary of Recommendations**

**May 2009**





## ***MES Fleet Management Audit Analysis & Recommendations***

### **1. Executive Summary**

Mobile Equipment Services provides fleet management and maintenance support to the City of Edmonton. Part of Mobile Equipment Services' (MES) responsibility includes maintenance of a fleet replacement reserve that is intended to replace all civic vehicles and mobile equipment, with the exception of Edmonton Transit vehicles.

MES is concerned that deferral of vehicle maintenance rate increases, escalation of various operating costs and fleet capital replacement costs has impaired MES' ability to replace the fleet in a timely fashion—retained earnings balances may not be adequate to meet fleet replacement demands.

This report reviews MES fleet replacement requirements and provisions, and makes recommendations regarding MES replacement fleet practices.

During our analysis we have determined that a developed MES fleet replacement plan can be sustained by simple retirement provision practices that include the use of a dedicated capital replacement reserve. The nature of the replacement plan and the timing of replacement provisions are such that apart from the first year of implementation there is no need for any other funding source, including the current MES retained earnings balance. As such we recommend that the MES retained earnings balance be returned to the City to fund other financial priorities.

In our analysis we have determined that MES equipment can also be sustained through a separate replacement reserve that is funded through a nominal overhead charge to department users.

At this time we do not recommend replacement provision for the Transit bus fleet or MES facilities. These assets are substantial and best financed through grant and debt financing that is assembled when assets are retired.

We would like to thank MES management and Financial Services staff for their support and efforts during this review.





## **MES Fleet Management Audit Analysis & Recommendations**

### **2. Summary of Recommendations**

The following is a summary of recommendations stemming from our review and analysis of MES fleet replacement plans and provisions.

- **Policy Update** - It is recommended that the details of the fleet replacement provisions and provision charges, as well as parameters placed on the fleet replacement reserve, be outlined in a revised MES policy.
- **Replace Retained Earnings with a Dedicated Fleet Replacement Reserve** - It is recommended that existing retained earnings of MES be turned back to the City to be used for other City priorities. Turning over MES retained earnings would only take place once it had been determined if some allowances were required to deal with retired units still in service, MES supported infrastructure replacement and the like.

The funding of MES fleet replacement (excluding Transit fleet) should be accomplished through a dedicated fleet replacement reserve.

Funding stemming from capital replacement charges should be placed into a dedicated fleet capital replacement reserve along with fleet salvage sales proceeds. The capital replacement reserve funding would be used to meet fleet capital replacement costs. It should be noted that the reserve would not accrue any interest on fund balances. Rather, any investment interest on these funds would be treated as a general revenue recovery.

- **Replacement Provision Calculation** – It is recommended that the current practices used to develop fixed rates (fleet replacement provisions) cease and that fleet replacement provisions be based upon the formula below.

$$90\% \times \left( \frac{(\text{Acquisition Cost} - \text{Salvage Value}) \times \text{Inflation to Anticipated Replacement Date}}{\text{Life Cycle of Unit}} \right)$$

Replacement provision calculations should be undertaken on a unit-by-unit basis.

As we had discussed and as demonstrated by our report analysis, the MES fleet should be replaced using a stand-alone vehicle capital replacement rate. The rate





## ***MES Fleet Management Audit Analysis & Recommendations***

would be based on 90% of each unit's anticipated net replacement cost (net replacement cost = gross replacement cost less anticipated salvage value of the replaced unit). The 90% factor has been seen to satisfy fleet replacement requirements without building up of unnecessary fleet replacement funds (see Section 9, Fleet Replacement Plan Sensitivity Analysis).

Further, the capital replacement rate should not include any administrative or overhead charge, as is now the case. The cost of vehicle registration, technical staff used in managing fleet replacement, and the administrative costs associated with tendering fleet replacement should all be treated as an operating expense and included as costs factored into the development of fleet maintenance / operating charges, discussed further below.

- **Charging of the Fleet Replacement Provision** – It is recommended that fleet provisions be paid by departments from the date of unit acquisition to the deemed date of retirement. Should a unit be prematurely retired, the replacement provision on the unit will cease to be charged. Should a unit be retained beyond its deemed date of retirement, the replacement provision will be reduced to reflect only the additional impacts of escalation associated with the unit's new retirement date.
- **Single Corporate Replacement Reserve** – It is recommended that fleet replacement (other than the Transit fleet) be accomplished through a single Corporate reserve and that the reserve be used to serve Corporate interests and priorities—the reserve not be disaggregated into department reserve interests. Further, it should be recognized that departments should not have any claim on this reserve as a result of organizational structure changes, etc. As such, once capital reserve provisions are collected from departments they will be used to best serve corporate interests and priorities.

**Fleet Replacement Plan and Cash Flow Projections** – It is recommended that MES establish a 25-year fleet replacement plan that considers fleet retirement requirements, anticipated fleet retirement provisions, and the projected balance of the fleet replacement reserve. This plan should be used to inform the administration and Council of the current and future status of the fleet replacement reserve and fleet replacement requirements.

**Retention of Fleet Units as Spare Capacity** – It is recommended that MES establish





## ***MES Fleet Management Audit Analysis & Recommendations***

approval and review procedures for fleet units that are retained after replacement.

**MES Equipment Replacement Reserve** – It is recommended that an MES equipment replacement reserve (not to include facility capital replacement) be established that is separate from the above noted dedicated fleet replacement reserve.

**MES Equipment Replacement Provision** – It is recommended that an MES equipment replacement provision be established and charged to departments as a percentage overhead charge to their fleet replacement provision charge. It is recommended that the MES equipment replacement provision be 7.75% (7% / 90%) of the unit fleet replacement provision. The 7.75% will provide for anticipated MES equipment replacement requirements again based upon an assumed fleet replacement provisions factor of 90%. The 90% fleet replacement factor will satisfy MES fleet replacement requirements without unnecessarily building up fleet replacement reserves (see Section 9, Fleet Replacement Plan Sensitivity Analysis).

**Continue to Fund Transit Through Grant and Debt Financing** – It is recommended that the Transit bus fleet continue to be financed through debt and grant funding that is assembled at the time of Transit bus fleet replacement. The timing and nature of bus replacements are such that funding of replacement through reserves and Transit bus replacement provisions are not considered a viable / practical solution.

**Operating Vehicle and Equipment Rates** - All costs associated with the operation of MES, excluding fleet capital replacement, should be charged to City fleet and other maintained vehicles and equipment (such as EPCOR fleet and equipment) through a maintenance / operating charge. There is some thought that the volatility of fuel costs are such that fuel costs should be excluded from the maintenance / operating charge. Fuel costs would be charged to vehicles and equipment on an actual direct charge basis.

**Analysis of Fluid Retirement Assessment Approach** – It is recommended that MES determine whether there is financial advantage to continue its current approach of assessing individual units for retirement rather than replacing units as a matter of course once their deemed retirement date has been achieved.

**Data Management** – It is recommended that MES simplify the data and factors used to establish fleet replacement requirements and fleet replacement provisioning.





## ***MES Fleet Management Audit Analysis & Recommendations***

**Data Integrity** – It is recommended that MES review the base data in management information and billing systems. During our review we spent a number of hours validating and cross analyzing data to ensure that it was correct. Many of the reports provided suffered from various cut off dates being used to generate data. Further, there were differences between accounting records and fleet management records that required one-to-one matching of thousands of records to ensure that the data plan was both accurate and fully reflective of fleet units held by the City. The following is an example of a due diligence item raised regarding data integrity issues.

- **Review of Billing System** – During our review and analysis of the current fixed rate charge, we determined that the existing EXCEL based tool contained a systemic error. It is recommended that MES review its billing system to ensure that the results of this tool have not created billing calculations issues.

**MES / Department Roles and Responsibilities** – It is recommended that MES establish clear roles and responsibilities regarding fleet retirement and fleet retirement provisioning practices. These roles and responsibilities should clearly outline MES responsibilities for establishment of standards.

**Review of Fleet Lease Practices** – It is recommended that fleet lease practices be reviewed to ensure that leasing activities are appropriate. The review should also consider whether leasing should form part of MES' core responsibilities.

