An Audit Report on

Procurement Card Processes and Controls

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State Auditor's Office

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Key Points of Report

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Overall Conclusion

Agencies have not consistently implemented effective processes and controls over the use of procurement cards. One of the three agencies we reviewed did not have adequate controls to prevent or detect inappropriate use of procurement cards. In addition, the Building and Procurement Commission (Commission) has not actively managed the contract between the State and the vendor bank that provides the procurement cards. The lack of contract management has cost the State money, but omissions in the contract make it impossible to determine how much.

In fiscal year 2001, Texas agencies and universities charged more than $140 million on procurement cards.

Key Facts and Findings

- The Commission did not maintain a copy of the complete procurement card contract or track contract changes. The parts of the contract that we were able to review lacked sufficient detail to hold the vendor accountable. Because the Commission did not manage the contract well, the vendor may have given state agencies and universities misleading information and may have underpaid or delayed paying the annual rebate due to the State. The Commission has been working to address these problems. A new contract will be negotiated this year.

- The Commission could help agencies develop and implement effective controls over their procurement card programs. The Commission should also use available data on procurement card purchases to improve the Commission's volume buying ability.

- The Parks and Wildlife Department (Parks) does not have sufficient controls over procurement cards. As a result, we found credit card purchases not in the State's interests, such as charges made against the card of a deceased employee, charges for potentially inappropriate purchases, and a charge already reimbursed to an employee through a travel voucher. Parks has already begun to address many of the issues raised in this report.

- The Department of Criminal Justice (TDCJ) has implemented an adequate system of controls that relies on post-payment reviews. Of the purchases we tested, we found only one non-compliant purchase and several split purchases that had not been found by TDCJ. TDCJ can strengthen its system by using data analysis to look for inappropriate purchases.

- The Texas Department of Transportation (TxDOT) has a strong system of controls that relies on pre-authorization of purchases and management review of monthly reports. Except for some split purchases, we did not find any inappropriate purchases in our sample that TxDOT had not already identified.

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Agencies have not consistently implemented effective processes and controls over the use of procurement cards. One of the three agencies we reviewed did not have adequate controls to prevent or detect inappropriate use of procurement cards. In addition, the Building and Procurement Commission (Commission) has not actively managed the contract between the State and the vendor bank that provides the procurement cards. The lack of contract management has cost the State money, but omissions in the contract make it impossible to determine how much.

Agencies use procurement cards to streamline their purchasing processes. However, in using procurement cards to pay for goods and services, some agencies have eliminated traditional internal controls over purchasing such as:

- Purchase requisitions, which help agencies ensure that a purchase is authorized and budgeted

- Purchase orders, which constitute the contract between the merchant and the agency

- Receiving reports, which help ensure that goods purchased with state money are received by the State

Table 1

We focused our review of agency processes on the three agencies that, together, accounted for almost 30 percent of all procurement card expenditures in fiscal year 2001.

Procurement Card Use – Fiscal Year 2001	
Agency	Amount Spent
Texas Department of Criminal Justice	$ 18.3 million
Texas Department of Transportation	$ 12.1 million
Texas Parks and Wildlife Department	$ 10.3 million
All other agencies and universities	$ 99.7 million
Total use, all agencies and universities	**$140.4 million**

Source: SAO analysis of unaudited data from credit card vendor.

Eliminating some of these controls can help agencies reduce the administrative cost of processing small, routine purchases. However, agencies must balance these cost savings against the increased risk of inappropriate card use.

In fiscal year 2001, cardholders at agencies and institutions of higher education charged more than $140 million to their agencies on state procurement cards. Three agencies were responsible for almost 30 percent of the purchases. (See Table 1.) Their methods for controlling card use vary:

- The Parks and Wildlife Department provides cards to a large number of employees, but it does little to determine whether purchases are appropriate.

- The Department of Criminal Justice uses post-payment reviews to mitigate the risk of inappropriate purchases. The system is effective, but it could be enhanced.

- The Department of Transportation (TxDOT) combines pre-authorization with post-payment reviews to manage the use of its cards. TxDOT has a strong system of controls over its procurement cards.

The Building and Procurement Commission Has Not Actively Managed the State's Contract With the Procurement Card Vendor

The Building and Procurement Commission (Commission) has not actively managed its contract with the vendor who provides the procurement cards. In fact, the Commission did not have a copy of the complete contract and has not tracked changes to the contract. The parts of the contract we were able to review lacked sufficient detail to hold the vendor accountable.

The Commission's mission is to acquire and provide goods, services, and facilities for state agencies and other government entities. Managing the contract that it developed for providing procurement cards to agencies falls under its mission.

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However:

- The Commission did not participate in the vendor's communications with state agencies and universities. As a result, agencies may have mistakenly interpreted vendor communications to be authoritative.

- The Commission contracted for an enhancement without knowing what it was buying or how much the enhancement would cost.

- The contract does not specify timing or verification processes for the annual rebate.

The contract for the State's procurement card program will expire in April 2002. The Commission has been working to ensure that the new contract will address the problems identified in this report.

The Building and Procurement Commission Could Help Agencies Better Manage Their Procurement Card Programs

The Commission could help agencies develop and implement effective controls over their procurement card programs. Agencies are responsible for controlling how employees use state money. However, as part of the Commission's post-procurement and payment audit and its reviews of agencies' procurement card policies, the Commission can help agencies ensure that controls are working as intended and that programs meet their goals (such as reducing the use of petty cash or improving relations with vendors).

In addition, the Commission can analyze available procurement card purchase data to improve the State's volume buying ability.

The Parks and Wildlife Department Cannot Ensure Its Employees Use Procurement Cards Appropriately

The Parks and Wildlife Department (Parks) does not have an adequate system in place to provide adequate assurance that its employees use procurement cards appropriately. As a result, we found that some credit card purchases may not have been in the State's interests. For example, we found charges made against the card of a deceased employee, charges for binoculars purchased at what appeared to be an excessive cost, and a charge already reimbursed to an employee through a travel voucher.

Parks' controls are not adequate to prevent or detect these types of transactions. Problems with Parks' controls include:

- Forty-eight percent of Parks' employees have procurement cards, even though some of their job titles do not indicate a need for purchasing authority.

- Cardholders make a purchase, receive the purchased goods, approve payment, and verify that payment was appropriate with limited oversight.

- Parks' reviews of procurement card use do not effectively identify problems. Although Parks has a monitoring system in place, its sampling methodology, the amount of coverage, and the limited scope of the desk reviews reduce its effectiveness.

Parks has already begun to implement some of the changes recommended in this report. Revised procedures were distributed to staff on November 1, 2001.

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The Department of Criminal Justice Mitigates Some of the Risks Associated with Procurement Cards

The Department of Criminal Justice (TDCJ) has an adequate system to ensure that its employees use procurement cards appropriately. Of the purchases tested, we found some split purchases and one non-compliant purchase that had not been found by TDCJ. TDCJ's system is a good example of how agencies can use post-payment audits to mitigate the risks associated with using procurement cards.

Among the strengths in TDCJ's system, the following are the most notable:

- Cardholders know that their use of procurement cards is subject to scrutiny from many different people.

- Fewer than 3 percent of TDCJ's employees have procurement cards.

- The procurement card auditor's random sampling method ensures that those who use procurement cards most and those who buy expensive items have a greater chance of having a transaction reviewed.

There are also opportunities for TDCJ to improve its system. For example, supervisors should review transactions to determine that the cardholders bought only needed items at a reasonable cost. TDCJ should also use data analysis to identify high-risk transactions for further review.

The Department of Transportation Has a Strong Procurement Card Program

Overall, the Department of Transportation's (TxDOT) procurement card program prevents inappropriate purchases and achieves its objectives of eliminating the need for petty cash and reducing paperwork for emergency purchases.

We tested a sample of division and district purchases, and except for several split purchases, all the questionable items we identified had already been identified and addressed by TxDOT staff. TxDOT relies on pre-authorization for procurement card purchases as well as management review of monthly reports that show where the cardholders shopped and the amount they spent for each procurement card transaction.

We identified a number of strengths in TxDOT's system. These include:

- Fifteen percent of TxDOT's staff have cards, but most cardholders (67 percent) are limited to $250 per transaction. If a cardholder has a need for a higher limit, his or her supervisor can request that the program administrator increase the limit.

- Before a cardholder makes a purchase, he or she must receive a supervisor's approval for the price and items to be purchased.

- Cardholders submit their supervisor's approval and the original receipts to the accounting department within three days of the purchase.

Summary of Management Responses

The Building and Procurement Commission, the Parks and Wildlife Department, the Department of Criminal Justice, and the Department of Transportation generally concur with our findings and have begun implementing our recommendations.

Summary of Objectives, Scope, and Methodology

The objective of this audit was to determine whether the State has ensured that agencies and universities have controls over procurement card use to provide adequate assurance of compliance

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with state procurement law and to prevent and detect fraud. When it became apparent that statewide systems do not provide that assurance, we expanded our scope to include review of the controls at the three agencies spending the most money through procurement cards.

Our scope included procurement card transactions between September 1999 and May 2001, and the laws, rules, contracts,

and procedures governing them. We later obtained additional information on purchases made between June and August 2001.

Our methodology included reviews of literature, reviews of procedures manuals, interviews, analysis of data provided through state sources and the credit card vendor, and review of documentation provided to support selected transactions.

The Building and Procurement Commission Has Not Actively Managed the State's Current Contract With the Procurement Card Vendor

The Building and Procurement Commission[1] (Commission) did not actively manage the procurement card contract with the procurement card vendor. In addition, the Commission did not maintain a copy of the complete contract or track changes to it. (See text box.) The parts of the contract that we were able to review lacked sufficient detail to hold the vendor accountable. The Commission's enabling legislation requires it to establish an effective and economical procurement system. The procurement system includes the contract for the procurement card program.

The procurement card program totaled more than $140 million in fiscal year 2001. The current contract with the procurement card vendor will expire in April 2002. As of late February 2002, the Commission is developing a request for proposals for a new contract. The Commission has indicated that the new request for proposals will address the issues raised in this report.

Because the Commission has not managed the contract well, the vendor may have overstepped its authority by giving state agencies and universities misleading information, implementing its new information system in a way that may not benefit the State, and underpaying or delaying rebates due to the State. The lack of contract management has cost the State money, but omissions in the contract make it impossible to determine how much. Within the past year, the Commission has begun to correct these problems.

The Commission did not participate in the vendor's communications with state agencies and universities. As a result, agencies may have interpreted vendor communications as authoritative. For example, in September 1999 the vendor sent a newsletter to all participating agencies with instructions that agencies had a 25-day grace period in which they could pay their bills. Agencies reading the newsletter may have thought that this guidance superseded the Prompt Payment Act[2] requirements. If

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[1] The 77th Legislature (Senate Bill 311) restructured the General Services Commission, transferring most of its responsibilities to the new Texas Building and Procurement Commission. On September 1, 2001, the Building and Procurement Commission took over the General Services Commission's responsibilities for administering the procurement card program. For consistency, we refer to the agency as the Building and Procurement Commission, even when an event predates the change.

[2] The Prompt Payment Act (Government Code, Section 2251.021) requires that agencies pay bills as close as possible to 30 days from the date of the invoice. According to the Comptroller of Public Accounts, the goal of payment scheduling is to pay vendors at the latest possible time.

all agencies had paid their bills five days early for calendar year 2000, it would have cost the State more than $100,000 in lost interest. Last summer, the Commission began to require that the vendor route communications to agencies through the Commission. By August 1, 2001, this practice was in place.

The Commission contracted for an enhancement without knowing what it was buying or the enhancement's full cost. In September 2000, Commission staff signed a contract amendment with the vendor for an enhanced information package. The amendment did not clearly describe what was included or what the full cost would be. Although the amendment stated that the first year's cost would be between $5,500 and $300,000, it did not specify the actual cost or provide enough information to determine the cost. For example:

- The amendment specified that standard reports were free and custom reports would be charged at $150 per hour, but there was no description of what a standard report was.

- The amendment promised two free training sessions, and, although there have been several demonstrations of the new system, the Commission is not clear as to whether these demonstrations were the training sessions referred to in the amendment. The amendment states that additional training sessions will cost $1,000 each.

Furthermore, the person who signed the amendment was not authorized to do so.

The contract does not describe timing or verification processes for the annual rebate. As a result, the vendor may be underpaying or delaying rebate payments. The contract specified that the State would be paid a rebate based on early payment. (The rebate amount is 0.002 times the amount paid within 14 days of billing if the State's annual purchase volume exceeds $20 million.) Problems with the Commission's management of the rebate include:

- There is no way to know whether the amount that the vendor has said qualifies for the rebate is accurate. The contract did not require the vendor to provide the State with enough data to recalculate the rebate amount, and the eligible amount depends on the vendor applying payments promptly. For calendar year 2000, the rebate for the State was $18,376 on total expenditures of $122 million. The vendor reported that only $9.2 million qualified for the rebate, and the State has no way to verify this claim. (In calendar year 1999, the State received a rebate of $54,686 on statewide expenditures of $84 million. There is also no way to verify whether that was the right amount.)

- The contract did not specify when the vendor would pay the rebate. For the last three years, the rebate has been delivered annually, 5.5 to 7 months after the end of the year. As a result, the vendor used the State's money for half a year. This delay caused the State to lose interest on the rebate amount.

- The Commission negotiated a relatively small rebate. Other states have negotiated much better rebate rates, and in some cases have rebates based on the amount of purchases only and not the timing of payments. The National

Association of State Auditors, Comptrollers, and Treasurers published *A Survey of Procurement Card Use in the States* in August 2001. That survey indicated that some states had negotiated both a volume rebate and a separate incentive to pay quickly. For example, California receives a quarterly rebate based on sales volume, and an additional rebate if it makes payment within 40 days.

As of late February 2002, the Commission is developing a request for proposals for a new contract. The Commission has indicated that the new request for proposals will address the issues raised in this report.

Recommendations:

The Commission should actively manage the procurement card contract. Active management includes:

- Maintaining a complete copy of the executed contract.
- Tracking changes to the contract.
- Ensuring that the vendor adheres to the terms of the contract.

The current contract expires in April 2002. The new contract should:

- Stipulate that the vendor should route written information through the Commission before providing it to agencies.

- Base any rebate on purchase volume only, and base any early payment incentive on payments paid within 30 days of invoice, which is consistent with the requirements of the Prompt Payment Act. (This calculation method would allow the State to recalculate the amount of the rebate.) In addition, include a statement as to when the rebate will be paid, for example within 30 days of the end of each calendar quarter.

- Require that the vendor provide several entities (the Commission and the Comptroller of Public Accounts) with enough data to perform trend analyses and to verify that the vendor's calculations are accurate.

- Allow for the naming conventions discussed in Section 2-B of this report.

Management's Response:

We agree with the recommendation that the Texas Building and Procurement Commission (TBPC) should actively manage the procurement card contract. The procurement card contract reviewed by the State Auditor's Office (SAO) was awarded and managed as if it were a term contract for a commodity or routine service. This practice led to a number of the deficiencies noted by the State Auditor.

To eliminate the deficient contract management practices noted by the SAO we will ensure that a complete copy of the executed contract is maintained, all contract amendments are tracked, and that contractor performance is diligently monitored to ensure that the vendor adheres to the terms of the contract.
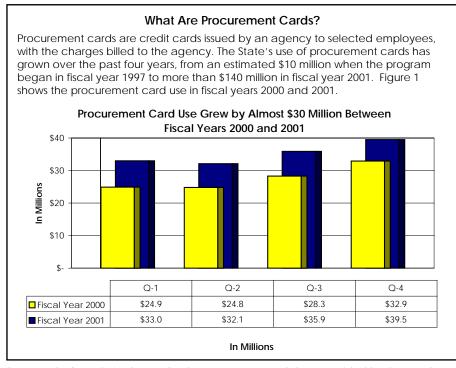
We also agree with the SAO's recommendations to enhance the new procurement card contract. Actions taken or in process to address SAO's recommendations include:

1. *In the spring of 2001, TBPC initiated a procedure which required the current procurement card vendor to obtain TBPC approval on all written communications prior to releasing communications to agency procurement card program administrators. TBPC will also ensure that this requirement is included in the new procurement card contract.*

2. *The current draft Request for Proposal (RFP) requests the potential vendors to propose revenue sharing opportunities that will benefit the State of Texas. We are also considering including a requirement in the RFP that requires any rebates to be paid directly to ordering entities by the specified deadline with a penalty to the vendor for late payment. The basis for any rebates will be negotiated to ensure that the State receives the maximum benefit, and will take into consideration the SAO's recommendations on the timing and basis of the rebates.*

3. *We are including a provision in the RFP that requires the selected vendor to provide a web-based application to allow statewide data access and retrieval abilities for TBPC, the Comptroller of Public Accounts, and the SAO in lieu of cumbersome standardized and customized reporting requirements. The web-based application will also be required to allow on-line administration of the procurement card program by agency procurement card administrators.*

4. *We will also add a requirement to the RFP that addresses the issues surrounding naming conventions discussed in section 2-B of the SAO report.*

The Building and Procurement Commission Could Help Agencies Better Manage Their Procurement Card Programs

Figure 1

What Are Procurement Cards?

Procurement cards are credit cards issued by an agency to selected employees, with the charges billed to the agency. The State's use of procurement cards has grown over the past four years, from an estimated $10 million when the program began in fiscal year 1997 to more than $140 million in fiscal year 2001. Figure 1 shows the procurement card use in fiscal years 2000 and 2001.

Procurement Card Use Grew by Almost $30 Million Between Fiscal Years 2000 and 2001

	Q-1	Q-2	Q-3	Q-4
Fiscal Year 2000	$24.9	$24.8	$28.3	$32.9
Fiscal Year 2001	$33.0	$32.1	$35.9	$39.5

In Millions

Source: SAO analysis of unaudited procurement card data provided by the vendor.

The Commission could help agencies develop and implement effective controls over their procurement card programs. Agencies are responsible for controlling how their employees use procurement cards. However, as part of the Commission's post-procurement and payment audits and its reviews of agencies' procurement card policies, the Commission can help agencies ensure that controls are working as intended and that procurement card programs meet their goals (such as reducing the use of petty cash or improving vendor relations). In addition, the Commission can analyze available data from the procurement card vendor to enhance its volume buying ability.

Section 2-A:

The Commission Is Uniquely Situated to Help Agencies Reduce Risks Associated With Procurement Cards

The Commission can help agencies reduce the risk associated with using procurement cards. (See text box on next page.) The Commission has not traditionally involved itself with how agencies manage their internal systems over purchasing. The Commission performs post-procurement and payment audits to provide assurance that agencies comply with statewide purchasing rules over delegated purchases. It also reviews agencies' procurement card procedures. The Commission does not generally advise agencies on how to address risks associated with the way an agency has implemented its procurement card program.

Agencies use procurement cards almost exclusively for "delegated" purchases of less than $2,000. The Commission has minimal involvement in delegated purchases. The Commission is responsible for rules, policies, and procedures governing procurement.

All agencies must comply with these requirements, regardless of how they plan to pay for a purchase. Agencies are responsible for adopting internal procedures for issuing, administering, and overseeing credit cards.

The Commission can help agencies develop procurement card programs that meet their needs and mitigate risks. Currently, the Commission is involved with agencies' credit card purchases at two points—it requires that an agency submit procedures before starting a program, and it performs "post-procurement and payment audits" of a sample of agency purchases every two years, including procurement card purchases, to ensure compliance with the procedures. However, neither of these is designed to help agencies ensure that their procurement card programs address their needs and mitigate risks.

Some agencies need help evaluating their goals for the procurement card program and implementing the appropriate controls. The Commission is well situated to help agencies when it conducts its current reviews of agency procedures and purchases. Additionally, the creation of a best practices guide would help agencies evaluate their own procedures and controls.

The Commission can help ensure that agencies use the controls that are available from the vendor. The Commission required that the vendor be able to provide certain controls as part of the procurement card program. However, the Commission does not advise agencies on the best ways to use those controls. The primary controls available are:

- Credit limits: Agencies can set a different monthly spending limit—similar to limits on personal cards—for each cardholder. Agencies should base credit limits on job duties, anticipated purchases, and historical spending patterns.

- Transaction limits: Agencies can limit the amount cardholders spend on each transaction. Because the Commission requires agencies to obtain competitive bids for purchases of more than $2,000, many agencies have set their default transaction limit at $2,000. Some agencies set low transaction limits for most cardholders and higher limits for people with training in procurement. Agencies should base transaction limits on their goals for the procurement card program, such as reducing petty cash or improving vendor relations.

- Restricted merchants: Agencies can block merchants of certain goods and services (such as fuel, legal services, and entertainment services) from accepting procurement cards. Although the codes used to identify merchants

(Merchant Category Codes, or MCCs) are not always reliable, agencies can use them to reinforce monitoring.

The Commission is ideally suited to advise agencies on the best ways to use these controls and could review existing controls during its regular post-payment review. Commission staff have expertise in procurement requirements and controls, and also have access to information on what controls the vendor has made available to the State. In addition, when Commission staff perform post-procurement and payment audits at other agencies, they learn about creative ways other agencies use controls.

Recommendations:

To help agencies reduce the risks associated with procurement cards, the Commission should:

- Coordinate with other agencies as needed to develop "best practices" that will help agencies identify and limit the risks associated with using procurement cards. Appendix 2 of this report provides a foundation for the Commission to use. The Commission's experience with procurement issues will allow it to enhance these suggestions into a more definitive set of best practices.

- Include in its biennial post-procurement and payment audits a review of the agencies' procedures manuals and a test to ensure that the controls are working as intended.

- Work with agencies to ensure that they are using options available from the vendor to maximize the benefits they receive from procurement cards. For example, before the biennial post-procurement and payment audits, the Commission could request a list of the credit limits and transaction limits for each cardholder and review with the agency's card administrator whether these limits help the agency achieve its objectives for the cards.

Management's Response:

We agree with the recommendation that TBPC should help agencies reduce the risks associated with procurement cards. TBPC is taking the following actions to address SAO's recommendations:

- *TBPC agrees that a best practices guide would be useful and will coordinate with other agencies, such as the Comptroller of Public Accounts, to ensure that both payment and purchasing controls associated with the use of the procurement card are addressed. In January 2002 TBPC initiated a focus group of procurement card administrators to assist in identifying procurement card risks and addressing them appropriately in the Request for Proposal (RFP). We plan on continuing the focus groups after the RFP is issued, and will use the information obtained from the groups to assist in the identification of best practices.*

- *TBPC's biennial post-procurement and payment audits currently include review and testing of all purchasing controls related to the purchasing statutes, rules, policies, and procedures that must be adhered to when a procurement card is used to pay for a purchase. Also, as noted in the report, TBPC requires agencies to submit their internal procedures for the issuance, security, and use of the credit cards for review at the time an application is submitted to the credit card vendor. These procedures are considered during the tests of purchasing controls included in the post-procurement audits.*

- *TBPC will take a more active role in working with agencies to ensure that they are using options available from the vendor to maximize the benefits received from procurement cards. We are currently revising the State-purchasing manual, and will include information on the available options in the manual. We will also provide information on the various procurement card options in procurement training courses provided by TBPC. Finally, we will continue to look for other opportunities and methods to assist the agencies in using controls provided by the procurement card vendor.*

Section 2-B:
The Commission Has Not Analyzed Data To Monitor And Enhance Procurement Card Use

The Commission has not analyzed data to monitor or improve the State's procurement card use. The Commission's contract with the vendor requires that data be available, but the Commission has not requested access to this information. This data would be helpful for identifying potential problems, negotiating discounts for frequently purchased items, and identifying best practices. (For the data to be most useful, agencies will need to follow guidelines for cardholders and agency names. See text box.)

We obtained data for fiscal year 2000 and for the first three quarters of fiscal year 2001 and found innovative uses of the card as well as indicators of weak controls. For example:

Naming Conventions Would Help The Commission and Agencies Analyze Their Data

Effective data analysis depends upon being able to compare one set of data with another. However, because agencies have not adopted certain standard conventions, it was hard to analyze the data provided by the vendor. For example:

- A cardholder's name on a credit card is not always the same as is listed in the payroll office for the employee. Cardholders are allowed to use initials and nicknames. Without confirming information from the agency, we were not able to verify that current cardholders were current employees. One agency confirmed that a former employee's card had not been cancelled when he died, and there were some charges to that card after his death.

- There was no reliable way to sort transactions by agency. Agencies sometimes list specific divisions' names on the cards instead of the agency name. For example, the cards at the Department of Transportation had more than 100 different names for different parts of the Department. Although the vendor said that all of TxDOT's names were coded in a separate field of the database, we found that was not true. (In fact, for the data we received for fiscal year 2000, more than 139,000 transactions—almost 17 percent of all transactions—had no entry in the field that was supposed to identify the agency.)

These issues have not been raised before because no one has used the data. Except for the reports provided to each agency, the vendor had never provided data that could be manipulated in spreadsheets or databases to either the Commission or to the Comptroller.

- The Parks and Wildlife Department (Parks) had weak controls over cell phones charged on procurement cards. During the first five months of calendar year 2001, the data showed that Parks was responsible for 42 percent

of all cell phone use charged to procurement cards. (Parks is only responsible for 7.3 percent of all state procurement card expenditures, so 42 percent is a significant overrepresentation.) Further review found that Parks employees often arrange their own cell phone contracts and do not have their phone bills reviewed consistently. In several instances employees failed to reimburse the State for personal cell phone calls. For example, one employee made 52 calls to residential phones after 5:00 p.m. or on weekends for a single month, for a marginal cost of about $80. Another employee had 61 calls to residential phones, for a cost of more than $200 for that month.

- The Department of Protective and Regulatory Services (Department) developed an innovative use for procurement cards. To simplify large purchases occurring statewide, the Department dedicated one card to paying for office supplies from its contracted supplier. This card has a larger credit limit than the Department's other cards, all of which the Department assigns to employees within its purchasing office. This approach is a good example of an agency analyzing its needs and customizing the procurement card process to fit those needs.

State Auditor reports from 1997 and 1999 found that the Commission had not fully pursued strategies to maximize the State's volume buying power. The 1999 audit recommended that the Commission review the purchases that agencies make on their own (the "delegated" purchases) to see whether the State would benefit from having a statewide contract for additional commodities. At the time, the Commission said that there were no mechanisms in place to track delegated purchases. However, the data available from the vendor would provide a mechanism for regular review of a portion of delegated purchases.

Recommendations:

In the next procurement card contract, the Commission should require (in addition to the items listed in the recommendation to Section 1-A):

- Access to data on a statewide level, which it should use to identify possible problems and best practices. It should also use the data to determine whether the State should develop term contracts for certain items.

- Naming conventions for cardholders and agencies. The first line of the card should contain the same name the cardholder uses in other state records. The second line of the card should start with the three-digit agency number. The rest of the line could be used however the agency prefers. If the current vendor gets the next contract, it should be required to re-issue cards using these conventions.

Management's Response:

TPBC agrees that we should have access to statewide procurement card data, and as indicated in the response to Section 1-A of the report, will require access to this data in the new contract. TBPC also agrees that the data should be used to identify opportunities for developing new term contracts and will include the procurement card data in current initiatives designed to improve the state's volume buying ability.

TBPC also agrees with the recommendation to require naming conventions for cardholders and agencies and will include this as a requirement in the Request for Proposal for the new contract.

Section 3:
The Parks and Wildlife Department Cannot Ensure Its Employees Use Procurement Cards Appropriately

The Parks and Wildlife Department (Parks) does not have an adequate system in place to ensure its employees use procurement cards appropriately. As a result, we found that some credit card purchases did not protect the State's interests. For example:

- One staff member charged the State for travel on a procurement card and was reimbursed for the same expense through a travel voucher.

- Two staff members collaborated to purchase 12 pairs of binoculars at $500 per pair, when normally Parks uses binoculars that cost less.

- Many staff members may have failed to reimburse the State for personal calls made on state cell phones paid for with procurement cards. (Parks' policy requires reimbursement for personal calls.)

- A deceased employee's card was still being used four months later. Parks did not cancel the card until six months after the employee's death.

Additionally, we identified numerous purchases that should have received additional scrutiny, but did not. We found these by searching for purchases made from entertainment providers, pawn shops, specialty retail stores, and other types of merchants not usually associated with state business.

Parks' controls are not adequate to prevent or detect these types of transactions. Problems with Parks' controls include:

- Forty-eight percent of Parks employees have procurement cards, even though some of their job titles do not indicate a need for purchasing authority. In addition, cardholders are not always trained in appropriate procurement card use, and their credit limits are not tailored to their job responsibilities.

- Cardholders are not required to get approval before or after making a purchase, and no one ensures that purchases benefit the State. The cardholder

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makes the purchase, receives the purchased goods, approves the payment, and verifies that the payment was appropriate.

- Parks' reviews of procurement card use do not effectively identify problems. Although Parks has a monitoring system in place, its sampling methodology, the amount of coverage, and the limited scope of the desk reviews reduce its effectiveness.

These conditions provide opportunities for fraud. To address this, we expanded our original sample, and referred questionable transactions to the agency for further investigation and resolution.

In fiscal year 2001, Parks spent $10.3 million through procurement cards.

Parks' system is assessed and compared to other agencies in Appendix 2. Parks has already begun to implement many of the recommendations in this section of the report. Revised procedures that address many of these issues were distributed to staff on November 1, 2001.

Section 3-A:
Parks Has Not Adequately Controlled the Issuance of Procurement Cards

Because Parks does not adequately control who gets cards, train its cardholders, or limit how much they can spend, there is an increased risk that cardholders will make inappropriate purchases. Parks delegates more purchasing authority to its non-procurement staff than other agencies, and these staff members are not always trained in using procurement cards. Parks is not limiting the availability of cards or tailoring credit limits to the job responsibilities of staff. In addition, Parks does not automatically cancel staff members' cards when they stop working for Parks.

Table 2

Almost Half of Parks Employees Used Procurement Cards in 2000			
	Parks	TxDOT	TDCJ
Number of Approved Full Time Equivalents (FTEs)	2,954	14,726	42,841
Number of Cards Used	1,747	2,164	1,543
Number of Cardholders [a]	1,422	2,127	1,041
Percentage of Staff With Cards	48%	14%	2%
[a] Some employees have more than one card.			

Sources: General Appropriations Act, and procurement card vendor records of cards used in calendar year 2000.

Almost half of Parks employees used procurement cards during calendar year 2000. This is significantly higher than the percentages for other agencies. Both the Department of Criminal Justice and the Department of Transportation have widely dispersed staff with needs for immediate purchases, but neither agency has provided cards to more than 15 percent of their staff. (See Table 2.) The wide distribution of cards makes approving purchases difficult. For example, many supervisors have cards, even though their normal job duties do not include procurement. It is unlikely that a staff member will question the appropriateness of a supervisor's purchases.

Parks does not consistently offer training. Although Parks' policy requires its Division Credit Card Coordinators to ensure that all cardholders receive training, training is not consistently offered. Some individual parks have made training available, but not all have. Because only 3 of the 1,422 cardholders are certified as purchasers, it is important for Parks to ensure that cardholders understand the rules governing state purchases.

Parks does not base credit limits and other limits on need. Parks is not using the controls available from the procurement card vendor. (See Section 2-A of this report.) If used, these controls would help ensure that employees are accountable for purchases. More than 98 percent of Parks' active cards have credit limits of $20,000. Only three cardholders had a credit limit of less than $20,000 per month. All active cards except one had a $2,000 transaction limit.

Parks does not always cancel cards when cardholders leave Parks' employment. Although it is difficult to compare records because staff members use nicknames on their procurement cards, we identified one case in which a cardholder died in April but his card was still being used in August. In this case, Parks staff members indicated that they had kept the card active so that others at that location could use it. The risk of fraud increases when procurement cards are not cancelled after a cardholder leaves employment, especially at an agency like Parks where payment information goes to the cardholder for payment approval.

Recommendations:

For staff members who currently have procurement cards, Parks should immediately implement the following changes:

- Evaluate which employees have legitimate needs for procurement cards and cancel all other cards. Employees who do not need to make purchases on behalf of the agency on a regular basis should not have access to cards.

- Require each cardholder's supervisor to identify the kind of usage anticipated for that employee so that the credit card administrator can establish credit limits, transaction limits, and Merchant Category Code exclusions and Parks can provide appropriate training.

- Review which supervisors should or should not be cardholders. If it is important for a specific supervisor to hold a procurement card, ensure that someone in a parallel position, who does not work with the supervisor, receives the goods and ensures that the purchase is appropriate.

As new procurement cards are needed, these procedures should become part of the card issuance process. Specifically, Parks should:

- Establish credit limits, transaction limits, and Merchant Category Code exclusions based on the anticipated use for a specific card, as established by the employee's supervisor.

- Implement mandatory training for all new cardholders that corresponds to the cardholder's purchasing authority, and update that training based on the needs identified in its oversight of card use.

In addition, Parks should ensure that only current employees have cards and establish a better system to cancel cards as soon as cardholders leave Parks' employment. The system could consist of keeping cardholder agreements in the employees' personnel files and having Human Resources notify the vendor and the credit card administrator when an employee leaves.

Management's Response:

- *Management recognizes the audit concerns and will develop (1) a definition of adequate justification for a procurement card and (2) an appropriate method to identify anticipated usage. Current cardholders will be reviewed based on these criteria and on past usage of their card. Current cardholders who do not demonstrate a valid need will be asked to surrender their procurement card. All future justifications for the issuance of new procurement cards will be evaluated based on the established criteria. The anticipated usage will determine the transaction limit, credit limit and merchant category code exclusions for current and future cardholders. The definition of adequate justification for a procurement card for a supervisor will specifically be addressed by management as will the appropriate level of controls and post-purchase reviews of these accounts.*

- *The response above describes the approach we intend to take with respect to establishing credit limits, transaction limits, and merchant code exclusions. With respect to training, the current procedures, implemented on November 1, 2001, require an employee to attend procurement card training before receiving their new card. In addition, the cardholder will be required to pass an on-line test prior to the renewal of their card. The training will be updated as needed based upon needs identified in our audits of procurement card transactions.*

- *At the present time only current employees have cards and a procedure exists to ensure that only current employees have cards in the future. Management will continue to review these procedures for identifying employees leaving TPW's employment and identify any appropriate changes, as necessary.*

Primary Responsibility for Implementing Corrective Action:
Finance Director/Director Purchasing, Payments, & Property
Expected Completion Date: September 1, 2002

Parks Does Not Ensure Purchases Made With Procurement Cards Benefit the State

Parks' administration of its procurement card program does not hold cardholders accountable for their purchases. Cardholders are responsible for requisitioning, ordering, and receiving items. Supervisors are not required to review or approve cardholders' purchases, and each cardholder is responsible for reconciling his or her records to the billing statement and approving payment. As a result, the State risks paying for items that it does not need.

No one independent of the cardholder approves or reviews purchases. No one with an understanding of what the cardholder needs for performing his or her job is required to review or approve the items the cardholder buys with state money. The person performing the oversight function discussed in Section 3-C of this report will not know the cardholder's needs well enough to be able to determine whether the State got the best value for the money. When the same person orders and receives goods—and no one reviews the purchase to ensure the State really needs the goods—the person could order items for personal benefit rather than for the State's benefit. For example:

- A cardholder could pay too much by using a non-competitive merchant (and possibly receiving a kickback) or by ordering a top-of-the-line item when a simpler one would do. In August 2000, two cardholders bought 12 sets of binoculars for more than $500 per pair. Because no one independent of the cardholder approved or reviewed the purchases, the cardholders did not have to justify why they needed such expensive binoculars.

- Cardholders can circumvent statewide standards. The purchase of these binoculars was split between two cardholders and between two dates. By splitting the purchase, these cardholders circumvented a requirement by the Building and Procurement Commission that purchases for more than $2,000 be competitively bid to help ensure that the State receives the best value for its money.

Potentially Inappropriate Purchases

Although most of the purchases that we reviewed appeared to have adequate documentation, not all of them did. For example:

- A purchase of over $800 from an art dealer was simply described as "furnishings."
- One charge was to ship six boxes of pottery to an individual. There was no explanation as to why this was a legitimate state expense.
- One cardholder bought a quilt and other items from an antique store. There was not enough documentation submitted to determine how these will be used for the State's benefit.

We identified numerous purchases that should have received additional scrutiny. These were identified by searching for purchases through vendors with Merchant Category Codes that identified them as entertainment providers, pawn shops, specialty retail stores, and others not usually associated with state business. We reviewed the supporting documentation associated with 20 of these purchases and found that in most cases there was adequate support for the purchase. Although the particular cases we saw appear to have been legitimate, they represent the types of purchases that require greater scrutiny, especially in the absence of supervisory review. (See Appendix 3 for discussion of how to identify questionable purchases.)

Cardholders reconcile their own statements. When cardholders reconcile their own statements, they could approve payment for items that did not benefit the State. At Parks, bills are sent directly to Accounts Payable, and a copy is sent to the individual cardholders. Each cardholder is supposed to audit his or her own statement by comparing receipts and transaction logs with the purchases listed on the statement. If the cardholder disagrees with some of the charges, he or she is to investigate immediately. Cardholders are to keep all monthly statements and receipts and logs for three years. Accounts Payable pays the entire bill, even if there are disputed charges.

The easiest way to ensure that there is some level of supervisory review for Parks' procurement card purchases would be for each cardholder's supervisor to initial and keep the itemized receipts when the items are received (certifying that the items were received and that they were for the benefit of the State). The purchase would then be entered onto the transaction log and the supervisor, or a staff member, would reconcile the bill to the transaction log and investigate any discrepancies. Having someone other than the cardholder keep the receipts eliminates the possibility that a cardholder could duplicate a receipt or otherwise fabricate documentation when the receipts are requested.

Recommendations:

Parks should:

- Implement supervisory approval or review of procurement card purchases. Supervisors could initial and keep all receipts and transaction logs when an item is received. Generally, supervisors should not be cardholders.

- Require cardholders to turn in receipts and a transaction log for all purchases, and require someone else to reconcile the log to the bill. Any item on the bill that is not on the log and is not supported with receipts should be investigated as a potentially fraudulent charge.

- Require the person performing the reconciliations to tell Accounts Payable whether there are receipts to support all items on the bill.

Management's Response:

Procedures were implemented on November 1, 2001 to require supervisors to review and sign each monthly transaction log. The transaction log was modified to include both an item description and a reason for the purchase. A supervisor's signature approval line was also added to the transaction log along with a place for supervisor's comments. Cardholders and supervisors were provided detailed instructions on how to complete a transaction log and what to look for when reviewing the log. Management will review the current procedures and identify appropriate modifications. The procedures to be developed by management will specify who will reconcile and keep receipts, the transaction log, and the monthly statement. The procedures will also stipulate the course of action to be taken when an item on the statement is not included on the transaction log. However, getting verification from all reconcilers that bills are accurate prior to making monthly

payments may compromise the agency's ability to comply with the Prompt Payment Act. The current procedures require the individual performing the reconciliation to notify Accounts Payable when receipts do not support the payment and require adjustments in future bills if payment has already been made.

Primary Responsibility for Implementing Corrective Action:
Finance Director/Director Purchasing, Payments, & Property
Expected Completion Date: September 1, 2002

Section 3-C:
Parks' Reviews of Procurement Card Use Do Not Effectively Identify Problems

Parks' reviews are inadequate to detect misuses of procurement cards. Reviews to verify compliance with procurement rules and regulations are infrequent—most likely, cardholders will only have to justify their purchases every four or five years. (See text box.) Parks does not review high-risk transactions, and there has been no effort to identify split purchases beyond those that emerge from the sample of about 30 cards per month. When we asked for documentation for our review of high-risk transactions, three cardholders submitted personal checks with the support for purchases. A comprehensive review could have easily identified these transactions.

Other Parks Reviews

Besides the reviews performed by the procurement auditor, other reviews are conducted by Parks' Internal Affairs Division, which investigates procurement cards as part of a fraud investigation when requested by management. Since 1998, there have been three such requests, two of which are still open.

Parks has already begun to change the way it reviews credit card transactions. The revised procedures, distributed to staff on November 1, 2001, appear to address many of the problems raised in this report.

Reviews affect very few cardholders. The procurement auditor selects about 30 cardholders each month, checks his database to make sure that these cardholders have not already been audited, asks cardholders for all documentation associated with that month's purchases, and reviews the documentation for compliance with specific criteria. At the current rate of auditing, it will be almost five years between reviews for each cardholder. By using a cardholder account as the sampling unit, rather than using individual transactions, Parks' reviews do not affect very many cardholders. As a result, cardholders can reasonably expect that most of their transactions will never be reviewed by anyone.

In addition, cardholders are responsible for retaining their own receipts. Because so few of them have been audited, they may not be retaining data they would need to support the legitimacy of their purchases. Cardholders supply documentation only upon request, so they know which purchases will be reviewed and when. This knowledge gives them an opportunity to enhance the documentation before the reviewer sees it. If cardholders were required to turn in all their documentation, then they would have to assume that any purchase could be reviewed at any time.

Reviews do not catch significant problems. The current reviews are limited in what they find. Specific deficiencies in the reviews include the following:

- There is no review of transactions identified as high-risk through reviews of Merchant Category Codes or other available data. Data analysis identified a number of transactions that may have been inappropriate. For example:

  − In the first eight months of 2001, Parks employees charged almost $30,000 worth of goods at Home Depot, Lowes, and Wal-Mart on Saturdays and Sundays. These may have been appropriate purchases, but they warrant additional review.

  − A travel expenditure occurred more than six months before our review of the data, but the employee only reimbursed Parks when we asked for the documentation to support the purchase. Travel expenditures are never supposed to be charged to a procurement card—the State has a separate contract for a travel card. However, this expenditure was especially egregious because the State had paid for it twice—once through the procurement card and again when the employee filed a travel voucher.

  − When we noted the number of charges to cellular phone companies from individuals' cards, we asked for support that heavy users of cellular services had reimbursed the State for personal calls, as required by Parks' policies. We found evidence that staff members failed to reimburse the State for these calls. Some of the amounts may be significant: one employee made 61 calls to residential telephones during a single month, with a marginal cost of more than $200 for those calls.

Split Purchases

When a single purchase is divided into two or more smaller purchases, each of which stays under the threshold that would trigger more scrutiny, it is referred to as a split purchase. If payments are split to circumvent competitive bidding or to divert business to a favored vendor, the agency may pay more than necessary to receive the materials it needs.

Split purchases typically occur when one cardholder divides a purchase into smaller ones (asking the merchant to put half of the purchase on one ticket and half on another, or to divide the purchase between different dates), or when two cardholders divide a purchase between their cards.

- The current reviews do not specifically search for split purchases (see text box) unless the purchase is split between two transactions on the same card (rather than split between two cards) during a month selected for review.

- More than 100 transactions appeared to be split purchases. Supporting documentation for 15 of the suspected split purchases showed that 12 were actually split purchases. Parks purchasing staff revoked the card of one cardholder when he would not agree to stop splitting purchases to avoid competitive bidding requirements.

- Procurement audits should focus on whether cardholders complied with procurement rules. Parks' reviews do not provide a comprehensive review of compliance. For example, they do not determine that competitive bid requirements are met. Of the findings generated by procurement audits between June 1998 and April 2001:

  − One-third of the findings (58 of 178) were for cardholders paying tax on purchases. (State agencies are not required to pay a state sales tax.)

− Another third of the findings (61 of 178) were for missing information on the transaction log.

  − The remaining findings were for purchase of items available through state contract or unauthorized goods or services.

- Some of the procurement auditor's activities are not meaningful without a coordinating supervisory review. For example, the auditor checks to see whether cardholders logged the reason for each purchase. However, a cardholder could comply with this requirement and still not have needed to make the purchase. The purchase of 12 pairs of $500 binoculars were listed on the transaction log as "binoculars" with no explanation of how many pairs were purchased, or why such expensive binoculars were needed.

We provided Parks with an extensive list of high risk transactions for staff review. Parks has begun to improve the quality of the oversight that it provides.

Recommendations:

Parks should:

- Investigate and resolve all of the questionable transactions we provided to the procurement auditor, and to report the State Auditor's Office, in accordance with Texas Government Code, Section 321.022. Develop procedures to identify and investigate potentially fraudulent charges.

- Use individual transactions as a sampling unit to ensure greater audit coverage, except in the case where a cardholder is judged to be high risk. An individual cardholder may be high risk if he or she has a history of noncompliance, or if his or her job duties require that he or she make purchases for which it is difficult to verify the need.

- Implement a process by which Parks randomly selects some transactions for review and judgmentally selects others. Judgmental samples should be based on data analysis and should include reviews for split purchases and transactions at specific kinds of vendors.

Management's Response:

- *The transaction in question was referred to the agency's Internal Affairs for investigation. The agency has revised the audit procedures to increase identification of potentially fraudulent transactions. When potentially fraudulent transactions are identified they will be immediately handed over to the Internal Affairs for investigation and resolution.*

Primary Responsibility for Implementing Corrective Action:
Purchasing Manger/Purchasing Auditor
Completion Date: February 6, 2002

- *The audit procedures have been revised to use transactions instead of cardholders as a sampling unit. The revised audit procedures require the review of both random transaction selection and judgmental samples. The judgmental samples include reviews of all potential split transactions, potential duplicate billed transactions, and purchases made with vendors in high-risk categories (as identified by Merchant Category Codes).*

Primary Responsibility for Implementing Corrective Action:
Purchasing Manger/Purchasing Auditor
Completion Date: November 1, 2001

Section 4:
The Department of Criminal Justice Mitigates Some Risks Associated with Procurement Cards

Strengths in TDCJ's system

Among the strengths in TDCJ's system, the following are the most notable:

- Cardholders know that their use of procurement cards is subject to scrutiny from many different people. Generally, the fear of being detected is a good deterrent to fraud.

- Fewer than 3 percent of TDCJ's employees have procurement cards. The Institutional Division (TDCJ's largest division) goes to each prison unit at least once every two years. During these visits, staff tests to ensure that a sample of Institutional Division cardholders still have the same job title as when they were issued the cards.

- The procurement card auditor's random sampling method ensures that those who use the card most and those who buy expensive items will have a greater chance of having a transaction reviewed.

The Department of Criminal Justice (TDCJ) has an adequate system to ensure that its employees use procurement cards appropriately. Of the high-risk purchases we tested, only one non-compliant purchase had not been found by TDCJ. TDCJ's system is a good example of how agencies can use post-payment procurement audits to mitigate the risks associated with using procurement cards. TDCJ spent more than $18.2 million on procurement cards in fiscal year 2001.

Some of the strengths in TDCJ's system are described in the text box at left. There are also opportunities for TDCJ to improve its system. Specifically:

- Supervisors should be required to review all transactions to ensure that the cardholders bought only needed items at a reasonable cost.

- The procurement card auditor should expand the review of high-risk transactions, providing additional scrutiny over purchases from unusual types of merchants. Examples of these merchants would include pawn shops, antique stores, or foreign vendors. In addition, purchases by TDCJ staff with a history of noncompliance should be given additional review.

- TDCJ should reinstate its procurement card training program.

In addition, some divisions and departments may not take sufficient action when the procurement auditor identifies noncompliance.

We found TDCJ's purchasing system significantly improved since we last reviewed it in 1996.

TDCJ's process is assessed and compared to other agencies in Appendix 2.

Section 4-A:
TDCJ Supervisors Do Not Review All Transactions

TDCJ's administration of its procurement card program does not entirely address the risk that a cardholder's purchases may not benefit the State. At TDCJ, the cardholder orders, receives, and approves payment for all items purchased with the card. No one with experience in the cardholder's department is required to certify that the item was needed or that the cost was reasonable. In addition, cardholders reconcile their receipts to their monthly billing statement.

Cardholders know that any number of people may review their purchases, but none of the reviewers would know if an item was needed or if there was a reason to buy it from a specific merchant. A supervisor would be able to determine whether there was a legitimate reason for these purchases, but a procurement auditor probably would not.

We did not find evidence of abuse in our review of TDCJ purchases. Several transactions lacked complete documentation. In three cases, we felt that TDCJ's reviewers should have questioned purchases based on where they were made. For example, one cardholder bought file boxes at an antique store, and another made a purchase at a liquor store. (The antique store also operated a U-Haul franchise, and the liquor store also sold plants and nursery items.) TDCJ reviewed the purchases at our request and found all but one to be in compliance.

The easiest way to ensure that there is some level of supervisory review for TDCJ's procurement card purchases would be for each cardholder's supervisor to initial and keep the itemized receipts when the items are received (certifying that the items were received and that they were for the benefit of the State). The purchase would then be entered onto the transaction log and the supervisor, or a staff member, would reconcile the bill to the transaction log and investigate any discrepancies. Having someone other than the cardholder keep the receipts eliminates the possibility that a cardholder could duplicate a receipt or otherwise fabricate documentation when receipts are requested.

TDCJ uses a version of this system for the 50 accounts that are not assigned to individuals. According to the program administrator, these 50 cards are kept at the cashier's office. Work supervisors check out a card for a specific time period and use it to pay for food for inmates while they are working away from a prison unit. The work supervisor returns the card and all receipts to the cashier when the work detail is completed. The cashier reconciles billing statements to receipts each month, and investigates charges that have no receipts. The cashier can determine who had the card during the period that the charge was made. This allows reviewers to investigate the charges to the card.

Recommendations:

TDCJ should require supervisors to review purchases made with procurement cards. Supervisory review could be accomplished by making the following changes to the current system:

- Have cardholders turn in their receipts to their supervisors and enter the purchases on a transaction log. Supervisors would initial the receipt and the log entry, certifying that the purchases were needed, reasonable, and received.

- Have supervisors or a member of their staff reconcile the billing statement to the transaction log each month and ask for support or reimbursement for any purchase that does not appear on the transaction log.

Management's Response:

We agree that the successful supervisory review process utilized by some TDCJ departments should be the model for Agency-wide policy. Procedures for Agency-wide use will be evaluated by 05/01/2002 and implementation of formalized procedures will begin by 09/01/2002.

Section 4-B:
TDCJ's Method For Selecting Transactions To Review Does Not Target Enough High-Risk Transactions

TDCJ does not target enough high-risk transactions. By reviewing high-risk transactions, we found three split purchases and several questionable purchases.

TDCJ's procurement auditors use random sampling to select most of the transactions they review. The random sampling process—one sample selected from the population of all transactions and another sample taken from the population of purchases over a certain dollar value—ensures that every transaction has a chance of being reviewed, but cardholders with many or with large transactions have a greater chance of having a transaction selected for review. This method operates as a deterrent to fraud, and is probably the best way to test for purchases of items that should have been purchased from a specific merchant because of a state contract. However, there are other ways to use data analysis to identify likely split purchases or other high-risk purchases.

Tests for split purchases could be improved. Cardholders may try to circumvent requirements for competitive bids by dividing purchases into two or more transactions, none of which exceeds $2,000. Currently, the procurement auditor scans records for all purchases over $1,000 to identify possible split purchases. TDCJ has successfully identified a number of split purchases, but may be missing those that involve one large transaction and one or more smaller transactions (under $1,000).

By querying the database for purchases as described in the text box, we found three split purchases made in the second

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Using Data Analysis to Identify Split Purchases

Procurement auditors can identify most of the population of potential split purchases by querying the database of transactions for those merchants at which TDCJ employees spent more than $2,000 on a single day.

quarter of fiscal year 2001 that the procurement auditor had not found. In one case, a cardholder charged $1,995 on one credit slip and the remainder (about $45) on another. In another case, a purchase was split between four transactions on two different cardholders' cards. The procurement auditor found two parts of this split purchase, but not the other two parts.

Data analysis helps identify other potentially abusive purchases. Currently, procurement auditors do not review transactions to determine whether the purchase was needed or whether the cost was excessive. By querying the database for specific Merchant Category Codes, we identified transactions that occurred at pawn shops, foreign vendors, and antique shops. We thought these transactions merited further investigation. The database provides the name of the merchant and the amount, but supporting documentation from the cardholder is needed to determine what items were purchased. The procurement audit group reviewed these purchases upon our request and found only one to be non-compliant.

Some cardholders should be monitored more frequently. When the procurement auditor finds that a cardholder has made unallowed purchases, she notifies the cardholder's division director, but does not increase the level of monitoring performed on that cardholder. Because not all divisions treat the lack of compliance with the same level of seriousness, it may be useful for procurement audit to increase coverage of cardholders with a history of noncompliance.

We found two people who continued to make purchases that were not allowed, even after their division directors were notified. The money involved was not significant, but the fact that noncompliant purchases recurred suggests that additional training or disciplinary action is in order.

Recommendations:

TDCJ procurement auditors should:

- Select more high-risk transactions for review. These can be identified through data analysis.

- Work with cardholders' supervisors to determine the State's need for items purchased from vendors whose Merchant Category Codes are in high-risk areas.

- Monitor staff with a history of noncompliance more frequently.

TDCJ should develop agency-wide guidelines on how to address abusive use of state procurement cards and implement appropriate training or discipline for those staff who do not comply with requirements.

Management's Response:

We agree that TDCJ should increase the number of high-risk transactions that are identified and reviewed. To select more high-risk transactions, TDCJ will expand our

use of data analysis. We will work with the cardholder's supervisor to determine the need for items purchased from vendors whose merchant category codes are identified in high-risk areas. Methods for increased data capturing and monitoring will be implemented by 09/01/2002.

Section 4-C:
TDCJ Provides Limited Training to Cardholders

When TDCJ began its procurement card program, it developed a training program that was presented to all cardholders. However, since then, TDCJ has stopped offering the training. Cardholders are expected to learn what they need to know by reading the guide they receive.

The fact that certain problems recur, such as split purchases and the example above of a cardholder who continued to purchase items that are not allowed, suggests that staff could benefit from training.

Other entities have developed creative ways to provide training. For example, at Texas Tech Health Sciences Center, new cardholders are given a video with written support documents. They must watch the video and pass a test before receiving their cards. This solution helps ensure that cardholders receive training without unduly tying up training or procurement staff.

Recommendation:

TDCJ should expand its training for cardholders.

Management's Response:

We agree that the TDCJ training accomplished through Cardholder Manuals and our Help Desk may not be sufficient to address all issues. We will evaluate various forms of training to make available to all cardholders and other relevant personnel. We will train in conjunction with implementation of new procedures targeted to begin 09/01/2002.

The Department Of Transportation Has A Strong Procurement Card Program

Overall, the Department of Transportation (TxDOT) has successfully implemented a procurement card program that achieves its objectives of eliminating the need for petty cash and reducing paperwork for emergency purchases. (See text box.) We tested a sample of division and district purchases, and except for several split purchases, all the questionable items we identified had already been identified and addressed by TxDOT staff.

TxDOT relies on pre-authorization for procurement card purchases as well as management review of monthly reports that show where cardholders shopped and the amount spent for each procurement card transaction. TxDOT provides cards to about 15 percent of its staff, but it limits its risk by giving most cardholders a small transaction limit.

In fiscal year 2001, TxDOT spent over $12 million through procurement cards.

TxDOT's process is assessed and compared to other agencies in Appendix 2.

Section 5-A:
TxDOT Could Fine-Tune Cardholders' Compliance With Procedures

TxDOT has good procedures for approving and documenting its procurement card purchases, but it does not always ensure that cardholders provide all proper documentation for their purchases. Currently, when a cardholder who is not a purchaser needs to make a purchase, he or she must first obtain a supervisor's signature on a Materials Requisition Form approving the needed item and its estimated price. Within three days of the purchase, the cardholder sends the form and the original receipts to the accounting office. If the cardholder does not provide the documentation, the accounting office allocates the cost to overhead. Therefore, it is possible for a cardholder to avoid scrutiny by neglecting to send in the documentation as required. We did not identify any abusive purchases that occurred as a result of this hole in the system, but neither did we see a systematic way to check for compliance.

Also, TxDOT cardholders could benefit from training on split purchases. Although TxDOT's procedures manual describes and prohibits split purchases, they have been a recurring issue. TxDOT's internal auditors found examples of split purchases, and we found additional examples. Given this, it appears that cardholders could benefit from additional training.

Recommendations:

TxDOT should:

- Identify and review purchases for which cardholders do not provide proper documentation.

- Consider developing additional training for cardholders on split purchases.

Management's Response:

- *We concur with the first recommendation. We are developing specific guidelines to the districts and divisions on the actions that will be taken when personnel repeatedly fail to provide credit card purchase documentation in a timely manner.*

- *We have already developed such training. The requirement was incorporated into the Procurement Manual in October 2001.*

Section 5-B:

The Department's General Services Division Cannot Review District Purchases

Every month, the director of purchasing reviews data on procurement card purchases made by division staff and questions division directors about unusual merchants or amounts. However, districts review their own purchases, and the director of purchasing does not have access to information about purchases made in the districts. (See Table 3.)

A recent internal audit found that different districts treat procurement card compliance differently. These differences make it even more important for the director of purchasing to be able to oversee all procurement card purchases.

The Director of Purchasing does not have access to information made by staff in the districts because TxDOT set up each of the 25 districts as a separate agency. As a result, the vendor sends data and reports only to that district.

If the Director of Purchasing begins reviewing district purchases in addition to

Table 3

Fiscal Year 2001 Procurement Card Use At TxDOT Divisions And Districts		
	Divisions	Districts	Could Not Determine
Amount spent	$ 1,257,142	$ 10,404,161	$ 398,088
Number of transactions	7,794	122,234	4,686

Source: SAO analysis of procurement card data

Divisions: TxDOT's divisions form a central resource for offices around the state. They manage statewide programs and provide other support for the districts. Examples of divisions are Finance and Construction.

Districts: The state is divided into 25 districts. Each district is responsible for its own transportation development, including planning, design, right-of-way acquisition, construction oversight, and maintenance.

Could Not Determine: "Could Not Determine" means that the name on the card gave no hint as to whether the cardholder was in a district or in a division. For example, the name on one card was "Tax Exempt." See Section 2-B of this report for our recommendations related to naming conventions.

division purchases, he may need to review a sample rather than all of them. The General Services Division could use the data analysis techniques described in Appendix 3 of this report for selecting its sample.

Recommendation:

TxDOT should work with the Building and Procurement Commission and the credit card vendor to provide General Services Division staff with access to automated reports for all district and division staff. This may require that cards be re-issued.

Management's Response:

Concur with the recommendation. The previous reporting system, SmartData, allowed us access only to the division data. The recent Bank of America implementation of EAGLS, an Internet based card management system they developed, will allow the General Services Division to review district data as well. We have been working with the Texas Building and Procurement Commission on the development of the request for proposal [RFP] to advertise for the next contract and the Internet reporting capability is a requirement in the RFP. Other providers, in addition to Bank of America, offer this capability now.

Management's Responses

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Randall H. Riley

February 14, 2002

Mr. Lawrence A. Alwin, CPA
State Auditor
State Auditor's Office
Robert E. Johnson Building
1501 North Congress Avenue
Austin, TX 78701

Dear Mr. Alwin:

We concur with the recommendations included in *An Audit Report on Procurement Card Processes and Controls*. The practices used to develop, award, and manage the procurement card contract in the past are not acceptable to current management and are already in the process of being changed. The current contract expires in April 2002, and the draft Request for Proposal for the new contract already addresses many of the issues included in the audit report. We will also strive to assist agencies in adopting effective internal procedures for issuing, administering, and overseeing credit cards by working together with other oversight agencies to develop a best practice guide.

We appreciate the opportunity to respond to the audit report and the cooperation and assistance of your staff during the audit. Our responses are enclosed.

Sincerely,

Randall H. Riley
Acting Executive Director

RHR:dcb

Enclosure

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February 8, 2002

Mr. Lawrence F. Alwin, CPA
State Auditor
Robert E Johnson Building
1501 N. Congress Avenue
Austin, Texas 78701

Dear Mr. Alwin:

This department appreciates the review and recommendations provided by your staff on our procurement card system. As you know, TPW is largely decentralized with its approximately 300 field locations consisting of state parks, historic sites, wildlife management areas, fish hatcheries, and statewide game and fish law enforcement. While our operational sites may be decentralized, the support for these sites is centralized at our Austin headquarters. As a result, the procurement card purchasing system is valuable in providing effective and timely purchasing support to these sites for small dollar purchases.

The use of procurement cards also provides significant cost avoidance to our department and the state. The Comptroller's office has estimated that it costs about five and a half cents to process every dollar of purchases while the private sector's average processing cost is one cent. Using the procurement card, when appropriate, brings the cost to our department of processing purchases closer to the cost in the private sector. We also firmly believe that our low level of interest paid on late payments, in comparison to other large agencies, is a direct result of our extensive use of the procurement card program. However, we agree that, even with its advantages, the use of the procurement card can only be successful if sufficient controls are in place to ensure the protection of the state's best interests.

I want to assure you that we have been and will continue to be aggressive in taking actions needed to make our program one of the very best in the state. In fact, we took immediate actions back on November 1, 2001, to revise our procedures implementing most of your staff's recommendations. Attached is our management response on each recommendation.

In closing, we welcome a follow-up audit at your convenience so that we can document our improvement in this area and to show the state's leadership and the taxpayer that we are a responsible agency fully deserving of their trust.

Sincerely,

Robert L. Cook
Executive Director

RLC:BD:cds

Enclosure

*To manage and conserve the natural and cultural resources of Texas for the
use and enjoyment of present and future generations.*

TEXAS DEPARTMENT OF CRIMINAL JUSTICE

www.tdcj.state.tx.us   P.O. Box 99   •   Huntsville, Texas 77342-0099

Gary Johnson
Executive Director

February 12, 2002

Mr. Lawrence Alwin, CPA
State Auditor
P.O. Box 12067
Austin, Texas 78711-2067

Dear Mr. Alwin:

Thank you for the opportunity to respond to the draft procurement card report. Your report contains a number of opportunities for improvement that we will address. In fact, corrective action has already begun on a number of the recommendations. We fully support the enhancement of our procurement card processes and sincerely believe your work will assist us in our ongoing efforts to improve agency operations.

Again, thank you for your staff's assistance. If we can provide further information, please do not hesitate to call on us.

Sincerely,

Gary Johnson
Executive Director

Texas Department of Transportation

DEWITT C. GREER STATE HIGHWAY BLDG. • 125 E. 11TH STREET • AUSTIN, TEXAS 78701-2483 • (512) 463-8585

February 13, 2002

Ms. Rachel Cohen
Project Manager
State Auditor's Office
1501 N. Congress Avenue
Austin, Texas 78701

Dear Ms. Cohen:

In response to your memorandum dated January 24, 2002 and subsequent conversation with Lawrence J. Zatopek of this office, the following is our formal response to Section IV of the report on procurement card processes and controls.

The Texas Department of Transportation (TxDOT) appreciates the review and recommendations the State Auditor's staff provided on our procurement card system. We fully concur with your recommendations and, in fact, have already implemented some of those recommendations. We offer the following specific comments:

Report Recommendations - TxDOT should:
- Identify and review purchases for which cardholders do not provide proper documentation.
- Consider developing additional training for cardholders on split purchases.

TxDOT Management Response:
- We concur with the first recommendation. We are developing specific guidelines to the districts and divisions on the actions that will be taken when personnel repeatedly fail to provide credit card purchase documentation in a timely manner.
- We have already developed such training. The requirement was incorporated into the Procurement Manual in October 2001.

We would like to thank your staff for their work. It was a pleasure working with them. If you have any questions, please contact Silvio J. Romero, CPPO, C.P.M. at (512) 416-2047.

Sincerely,

Michael W. Behrens, P.E.
Executive Director

cc: Owen Whitworth, Director, Audit Office, TxDOT
Lawrence J. Zatopek, Director, General Services Division, TxDOT
Silvio J. Romero, CPPO, C.P.M., Director of Purchasing, General Services Division, TxDOT

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Objective, Scope, and Methodology

Objective

The objective of this audit was to determine whether the State has ensured that agencies and universities have adequate controls over procurement card use to provide assurance of compliance with state procurement law, and to prevent and detect fraud. When it became apparent that statewide systems do not provide that assurance, we expanded our scope to include review of the controls at the three agencies that spent the most money through procurement cards.

We focused on answering the questions:

- Is money being spent as the Legislature intended?
- Are assets protected and used properly?

Scope

Our scope included procurement card transactions and the laws, rules, contracts, and procedures governing them. Our original test population was transactions posted between September 1999 and May 2001. In October 2001, we received information on purchases made between June and August 2001, and developed summary information from that data to include in this report.

Methodology

Information collected to accomplish our objective included the following:

- Interviews and other communications with staff at the Building and Procurement Commission, the Comptroller's Office, and at agencies and universities with active procurement card programs

- Data generated by the procurement card vendor relating to procurement card transactions posted between September 1, 1999 and August 31, 2001

- Data generated by the Parks and Wildlife Department, the Department of Criminal Justice, and the Department of Transportation related to procurement card transactions

- Policies and procedures relating to the use of procurement cards from agencies and universities with active procurement card programs

- Procedures and results for post-payment audits of agencies and universities, performed by the Comptroller of Public Accounts and the Building and Procurement Commission

- Review of literature on procurement cards, including audit reports from other states and survey results and other information from national associations and trade groups

Procedures and tests conducted:

- Analytic review of USAS documentation
- Analytic review of transaction-level data obtained from the vendor
- Tests of support for selected transactions

Analysis techniques used:

- Process flow mapping
- Trend analysis
- Data comparison

Criteria used:

- State Auditor's Office accountability project methodology criteria related to procurement

- Texas Statutes and Texas Administrative Code

- Policies and procedures adopted by the agencies we reviewed

- Documents relating to the contract for procurement card services between the vendor and the Building and Procurement Commission

- Other standards and criteria developed through secondary research sources

Other Information

Fieldwork was conducted from April through August 2001. The audit was conducted in accordance with generally accepted government auditing standards.

The following members of the State Auditor's staff performed the audit work:

- Rachel Cohen, CPA (Project manager)
- Scott Boston, MPA (Assistant project manager)
- Ricardo Garcia, MPA
- Willie Hicks, MBA
- Cesar Saldivar
- Ed Santiago
- Tracy Waite, MA/CBA
- Menza Webster
- Julie Ivie, CIA (Audit manager)
- Frank Vito, CPA (Audit director)

Appendix 2:
Procurement Card Processes

Appendix 2 divides the procurement card process into three areas—card issuance, card administration, and card oversight. It describes a process with good controls ("ideal process"), and then reviews how the three Texas agencies that use procurement cards the most handle each area. Not all of the areas we identify are equally important. As a result, it would not be appropriate to weight them equally when assessing the overall performance of an agency.

Card Issuance

Card issuance refers to the decisions made about who should get a procurement card, what limitations cardholders have on their spending, how the card is collected when a cardholder no longer needs it, and what training cardholders need.

Table 4

Ideal Process for determining which employees need cards:		
A card is issued when an employee's supervisor requests the card. The supervisor's decisions should be based on the agency's goals for its procurement card program, the employee's job duties, and the supervisor's ability to oversee the use of the card.		
Parks	Weak	Staff who want to get a card download and complete an application and submit it to the Division Credit Card Coordinator. That person completes some budget information and forwards the application to the Agency Credit Card Coordinator.
		In 2000, 48 percent of Parks employees used procurement cards.
		Forty-eight managers and eight directors are cardholders. Distribution of cards to upper management increases the risk that employees will circumvent controls because supervisory review is less feasible.
TDCJ	Strong	A card is issued when an employee's supervisor requests the card.
		In 2000, about 2.5 percent of employees at TDCJ used procurement cards.
TxDOT	Strong	A card is issued when an employee's supervisor requests the card.
		In 2000, about 15 percent of employees at TxDOT used procurement cards.
Ideal Process for setting card limits:		
Limits on cards, such as credit limits, single purchase limits, and Merchant Category Code restrictions, are established based on the individual cardholder's job responsibilities, historical usage data, and anticipated use. (This is better than having a single set of "default" limits for all users.) In addition, agencies should have a process to document and approve increased limits if a cardholder has a legitimate need. This process would consider what additional training the cardholder would need and whether additional controls need to be put into place (allowed merchant categories, for example).		
Parks	Weak	More than 98 percent of Parks' active cards have credit limits of $20,000. Only three Parks cardholders had a total credit limit of less than $20,000 per month. All active cards except one had a $2,000 transaction limit.
TDCJ	Mixed	Single purchase limits are established by each cardholder's supervisor, up to the agency-wide limit of $2,000.
		Of the 2,536 accounts, 70 percent have credit limits set at $5,000 per month. Of the 2,292 accounts with a single purchase limit, 90 percent are set at $2,000. Therefore, it may be that TDCJ is not considering actual needs and historical usage.

| TxDOT | Strong | In general, field users have transaction limits of $250, although some can charge up to $1,000. Trained purchasers have higher limits. |
| | | At the end of September 2001, 1,719 cards were active. Of these, approximately 74 percent had transaction limits of $250. |

Ideal Process for cancellation of cards:

Cards are cancelled when an employee no longer has a legitimate job need for the card, whether that is a result of promotion, transfer, or separation from the agency.

One way to ensure that transfers lead to cancellation of cards would be to forward the cardholder agreements to Human Resources, who would cancel the cards directly with the vendor in case of a personnel action.

Parks	Weak	Parks has not always cancelled cards when staff have left. In April 2001, a staff member died, and the Department decided to leave the card open for use by others in the department. There were about $1,500 in charges during the next 3 months. In October, the Department cancelled the card.
TDCJ	Not Tested	We did not test for terminated staff with subsequent charges at TDCJ. However, TDCJ's operational reviews at each prison unit check whether a cardholder's job title has changed since he or she was issued a card.
TxDOT	Strong	TxDOT's recent internal audit found that cards were not all cancelled promptly. However, we did not find examples of staff members whose cards were used after they left TxDOT employment.

Ideal process for training cardholders:

Cardholders are given enough training so that they understand how to use the card appropriately. In addition, they sign an agreement to use the card appropriately.

(Although training should be updated to address issues that are identified by audits, training does not need to be in a classroom setting. For example, at the Texas Tech Health Sciences Center, new cardholders are given a video with written support documents. They must watch the video and pass a test before receiving their cards.)

Parks	Weak	Parks does not ensure that all cardholders to receive formal training on the use of procurement cards.
		Because of the number of Parks employees with cards and because of the small number of Parks staff trained as purchasers, training on appropriate use of procurement cards is even more important. (Parks has only three purchasers certified by the Texas Building and Procurement Commission.)
TDCJ	Weak	Cardholders are provided with procedures, which they are expected to read. Currently, this is the extent of training for new cardholders.
		Cardholders sign a cardholder agreement.
		The fact that TDCJ continues to find evidence of split purchases and other failures to comply with requirements suggests that additional training is needed.
TxDOT	Strong	TxDOT has minimized its exposure to risks of not training staff by limiting the transaction limits for most of its cardholders.
		Also, TxDOT has given cards to purchasers to use for high-dollar purchases. Although purchasers only accounted for 7 percent of the cardholders, they were responsible for almost 35 percent of the purchases ($3.9 million out of TxDOT's total $11.1 million) in calendar year 2000. Purchasers are more likely to have had training on procurement issues than other staff.
		All cardholders are required to sign a cardholder agreement and return it to the Human Resources Office and the employee's supervisor.
		Nonetheless, consistent findings of split purchases show that training in this area could be strengthened.

Card Administration

Card administration refers to how the agency manages the everyday use of procurement cards. Card administration includes what resources are made available to cardholders, what is done to ensure that purchases benefit the State, and how documentation is reconciled and stored.

Table 5

Ideal process for providing cardholders with expertise on procurement:		
Cardholders can obtain guidance on purchasing rules and processes, including help finding an appropriate vendor, from procurement staff.		
Parks	Not rated	Parks' procedures manual provides the names and telephone numbers of procurement staff.
TDCJ	Not rated	TDCJ's procedures manual provides the names and telephone numbers of procurement staff.
TxDOT	Strong	TxDOT cardholders fall into two groups: trained purchasers and line users. The trained purchasers have the same resources as they have for other purchases if they run into purchasing questions. Line users need to get pre-approval before making a purchase. The pre-approval process identifies situations where additional help is needed.
Ideal process for ensuring that the purchases are necessary :		
Cardholders obtain approval from a supervisor either before or after making a purchase. This helps ensure that items purchased with a card were really used to benefit the State, and it minimizes the occurrence of problems related to having the same person order and receive the goods.		
When one person orders and receives goods and approves payment --- and no one reviews the purchase to ensure that the State needed it, the cardholder could order items that do not benefit the state. For example:		
• A cardholder could pay too much by using a non-competitive merchant (and possibly receiving a kickback), or by ordering a top-of-the-line item when a simpler one would do.		
• Cardholders could buy items that the State does not need or could buy more than necessary of a needed item and divert the excess to personal use.		
• Cardholders could approve payment for items that did not benefit the State.		
Parks	Weak	Cardholders are not required to obtain approval from a supervisor either before or after making a purchase. There is no required supervisory review of goods purchased.
TDCJ	Weak	Cardholders are not required to obtain approval from a supervisor either before or after making a purchase. There is no required supervisory review of goods purchased.
TxDOT	Strong	Supervisory review occurs on all purchases before a purchase is made. Cardholders must obtain approval for all purchases "before purchase and by someone with signature authority other than the cardholder." This approval generally comes from a supervisor, unless the cardholder is a purchaser. The preapproval describes what will be purchased and (approximately) how much it will cost.
Ideal process for reconciling and storing documentation:		
Someone other than the cardholder (either the supervisor, his or her staff members, or someone in the accounts payable department) reconciles the billing statement to the transaction log or to the receipts. Any items not on the transaction log as approved would be investigated. When cardholders bear sole responsibility for reconciling their purchases, they could approve payment for items that did not benefit the State.		
Having someone other than the cardholder keep the receipts eliminates the possibility that a cardholder could duplicate a receipt or otherwise fabricate documentation when the receipts are requested.		
Parks	Weak	Cardholders receive monthly activity statements from the procurement card vendor for all purchases made within the billing cycle. Cardholders are responsible for reconciling this to their receipts. All documentation is supposed to be retained by the cardholder for 3 years "in the event your account is audited." The bill is paid unless a cardholder says that a charge is in dispute. Cardholders do not have to certify that charges are appropriate.

TDCJ	Weak	Cardholders receive monthly activity statements from the credit card company for all purchases made within the billing cycle. Cardholders are responsible for reconciling this to their receipts. All documentation is to be retained by the cardholder for 5 years. The bill to the vendor is paid unless a cardholder says that a charge is in dispute. Cardholders do not have to certify that charges are appropriate. However, TDCJ uses a different system for 50 accounts that are not listed in individuals' names, but are instead listed as "cashier office." The cards for these 50 accounts are held by the cashier's office, are signed out for a specific purpose by work supervisors, and are used to pay for food for inmates out on a job. They are returned, with receipts, to the cashier, who reconciles billing statements to receipts each month. The cards have the appropriate Merchant Category Code restrictions. This system adds additional controls to the process.
TxDOT	Strong	Within three days of purchase, cardholders are required to submit the approved material request and the signed receipt to a third party, who is responsible for reconciling these documents to the bill. TxDOT is the only agency we visited that had totally segregated the reconciliation function from the cardholder. TxDOT had one of the strongest systems we saw.

Card Oversight

Card oversight refers to those after-the-fact processes that an agency uses to identify and correct misuse of the cards. Card oversight includes the purchase review process, documentation collection review for compliance with purchasing requirements, and response to problems.

Table 6

Ideal process for reviewing purchases:		
Cardholders know that misuse is likely to be detected. This can happen when cardholders believe that purchases will be scrutinized.		
Parks	Weak	Every month the procurement card auditor reviews cardholder compliance for about 30 cardholders. At the current rate, each cardholder will be audited about once every 5 years. Although Internal Affairs also investigates procurement cards, it only does so as part of a fraud investigation when requested by management. Since 1998, there have been three such investigations, two of which are still open. Internal Audit has not reviewed procurement card use recently.
TDCJ	Strong	Post-purchase oversight is performed regularly by TDCJ's Procurement Audit staff and its Operational Review staff. Reviews have also been performed recently by Internal Audit and others. The number of people who are likely to review purchases, and the fact that cardholders know to expect this, is one of TDCJ's system's greatest strengths.
TxDOT	Strong	Numerous reviews occur for each purchase: • <u>Before the purchase</u>: Each purchase must be preapproved, using the regular materials requisition forms. As a result, using the procurement cards does not create additional risk beyond that in a traditional procurement process. • <u>Immediately after the purchase</u>: Cardholders submit documentation to staff. Because the documentation is then out of their hands, cardholders do not know how much scrutiny is given to each purchase. • <u>Monthly</u>: Procurement staff members review reports from the vendor to look for merchants and dates that look suspicious. Some purchases are referred to the cardholder for additional discussion. • <u>Sporadically</u>: Internal audit has reviewed procurement card use recently. In the districts, some of the internal reviewers have performed their own reviews. Because each purchase is approved before it is made, there is little need for post-purchase compliance reviews.

Ideal process for collecting documentation: Documentation is pulled from a central storage place when an item is selected for review. Keeping documentation in a separate storage place, out of the control of the cardholder, minimizes the risk that a cardholder could fabricate documents needed for the review.		
Parks	Weak	Cardholders are given a date by which they must submit documentation for the month selected.
TDCJ	Weak	Cardholders have 14 days to provide documentation for items selected for review.
TxDOT	Strong	Users submit documentation at the time of the purchase.
Ideal process for selecting transactions to review: Transactions are sampled to ensure compliance with procurement requirements. The sampling methodology should ensure that: • All transactions have some chance of being reviewed. • High-dollar transactions are more likely to be reviewed than low-dollar ones. • Cardholders using procurement cards frequently are more likely to have a transaction reviewed than others. • High-risk users (for example, new users or those with a history of noncompliance) and high-risk transactions (for example, transactions from certain kinds of merchants) are sampled more extensively.		
Parks	Weak	The procurement card auditor selects cardholders for review, not transactions. Cardholders who have already been audited are eliminated from the population until all other cardholders have been audited. No additional review is performed on judgmental samples based on review of MCCs or searches for split purchases. At the current rate of auditing, each cardholder will be audited approximately once every 5 years. Cardholders can reasonably expect that most of their transactions will escape scrutiny.
TDCJ	Mixed	*(Note: although numerous people review TDCJ transactions, these comments relate to the review performed by the procurement audit group.)* TDCJ draws two separate random samples, one from all transactions and another from transactions over $1,000. This ensures that all transactions have some chance of being reviewed, but that transactions made by high-dollar transactions and transactions made by high-frequency users receive more review. Transactions of more than $1,000 are scanned to look for split purchases. TDCJ has caught most of its split purchases in this way. No additional review is performed on judgmental samples based on review of MCCs, and transactions made by high-risk users do not receive additional review.
TxDOT	Strong	TxDOT performs, in effect, 100 percent sampling of all transactions through its pre-approval process, and through its review of vendor reports.
Ideal process for reviewing compliance with purchasing requirements: Procurement review focuses on adherence to procurement requirements, but works with supervisory review. Together, they ensure that the right items are purchased using appropriate means. In addition, common deficiencies identify areas in which training is needed.		
Parks	Weak	Parks' desk reviews are limited to a check of basic compliance, some of which is meaningless without supervisory review. Staff members are not used to being questioned about their purchases.
TDCJ	Mixed	Procurement audit performs checks for basic compliance. Other groups, however, review other issues, such as card security, whether the cardholder is actually performing reconciliations, and so on. Since TDCJ's training program is not active, recurrent findings do not feed in to training.
TxDOT	Mixed	Procurement audit reviews occur differently in different districts. However, we did not find anything that had not already been identified by TxDOT.

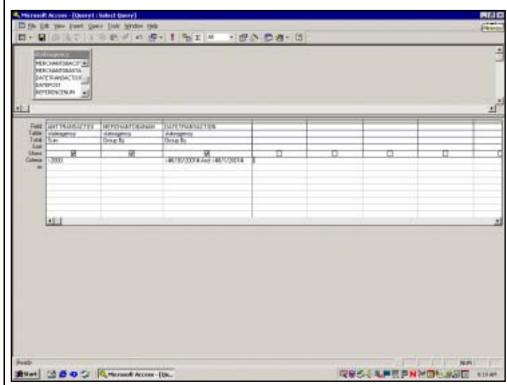|		**Ideal process for responding to problems:**
		When noncompliance is identified, the procurement department and the cardholder's supervisor work together to determine whether it is a training issue or whether it requires disciplinary action. Both groups agree to a plan to address the deficiency.
		The noncompliant cardholder is placed in a "high risk" category and more of his or her transactions are reviewed in subsequent months.
Parks	Mixed	If a compliance review of a cardholder's account receives less than a 90 percent rating, that cardholder's account is reviewed again in 60 days. If the rating is still below 90 percent, the card is cancelled. According to the procurement auditor, two cards have been cancelled for failing to maintain a 90 percent compliance rating.
		Parks' process has some strengths and some weaknesses:
		• The fact that there is follow-up when someone has been noncompliant is good, but the 60 days may be too predictable to be a good control.
		• Since the cardholder will not be reviewed again for almost 5 years after he or she passes the 60 day follow-up, there is no way to know whether the changes continue beyond follow-up.
		• This would be a stronger process if more significant items were reviewed in the procurement audit process, such as whether the item was needed in the first place.
TDCJ	Weak	When the procurement auditor finds noncompliance, she notifies the cardholder's supervisor. Different divisions treat noncompliance differently. There is no follow-up to ensure that problems are addressed. We found a widely differing set of processes at different departments:
		• At Texas Correctional Industries, the department head handles the situation himself and takes different action depending on whether it is the first, second, or third instance of noncompliance.
		• At Parole, the department head has assigned the task to someone who keeps track of noncompliance issues.
		• At Facilities, the task is assigned to someone besides the department head, and there is no tracking or follow-up.
		We found two staff members who continued to make the same kinds of purchases even after being cited for noncompliance. The money involved was not significant, but the fact that this type of purchase recurred suggests that additional training or discipline is in order.
TxDOT	Mixed	Although TxDOT does not have an agency-wide policy for tracking noncompliance, some of the districts are doing this independently.

Query Techniques for Procurement Card Processes

Query Techniques for Split Purchases

Procurement card monitors can identify most of the population of potential split purchases by querying only those merchants at which agency employees spent at least $2000 on a single day.[3] See Figure 2, a Microsoft Access screen print, for the design view of a query for all merchants at which employees spent at least $2000 on any single day in July 2001.

This query uses three fields: the amount of the transaction, the name of the merchant[4], and the date of the transaction. To build this type of query, select Totals from the View menu. Use the drop down box to select Sum for the AMT Transaction field. Set the criteria for this field at >2000. The query will yield all merchants at which cardholders spent more than $2000[5] on any single day, for the period designated in the Date Transaction field.[6]

Figure 2

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[3] Some merchants will allow cardholders to split transactions over two or more days.

[4] Merchants and employees referenced in Appendix 3 are not real.

[5] This query assumes a single transaction limit of $2000 for all cards.

[6] For the example query, July 2001 was selected.

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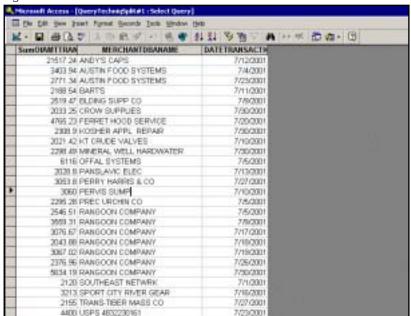Processes_CBG\4 - PD Final\02-022.doc

Figure 3

Figure 3 shows the results of the query: a list of all merchants with at least $2000 of charges from cardholders on any single day in July 2001, including the date of the purchases. Purchases in the list may have been split to avoid a $2000 limit.[7]
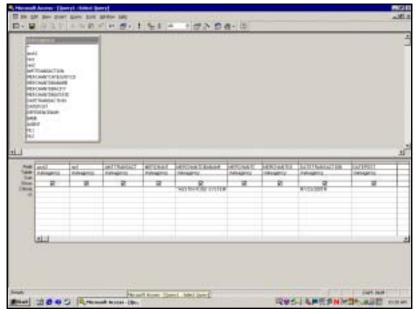
Figure 4

Figure 4 shows the design view of a query for detail transaction information for an item in Figure 3. For this query, more data fields are added so that sufficient detail will be available for an auditor to request support documentation. This query is for all transactions at Austin Food Systems on July 23, 2001.

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[7] Our query assumes that different transactions making up a split purchase would be charged on the same day. Some merchants will delay charges of remaining amounts for days or weeks.
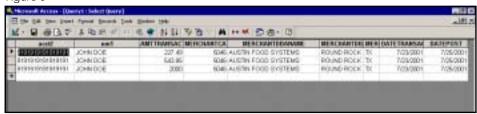
Figure 5

Figure 5 shows the result of the query performed in Figure 4. There were three purchases on July 23; all were made by the same cardholder. The fact that one of the transactions is equal to the single transaction limit makes it likely that two, or perhaps all three, transactions constitute a split purchase.

Of course, auditors would need to request and review the support documentation to be certain that the cardholder split the purchase.
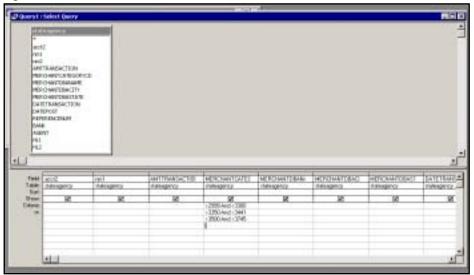
Querying by Merchant Category Codes[8]

Figure 6

Figure 6 shows the design view of a query for all travel-related expenditures.[9] In this example, auditors have included three ranges of Merchant Category Codes (MCC). The 3000-3299 range is for all airlines. The 3351-3440 range is for all car rental agencies. The 3501-3744 range is for all hotels.[10]

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[8] Merchant Category Coding is a standardized system that assigns a numeric code to general merchant types. For example, 5992 is the number designated for florists. Lists of merchant category codes can be found on the Internet. As of the publication date of this report, a list is available at www.usda.gov/procurement/card/card_x/mcc.pdf.

[9] The risk with travel-related expenditures is that cardholders will pay for travel with a procurement card and also receive reimbursement via a travel voucher. This double-bills the State to the benefit of the cardholder.

[10] Querying other MCCs may also identify travel-related expenditures.

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Figure 7

Figure 7 shows the results of the query performed in Figure 6. Nine transactions from seven cardholders were from the Merchant Category Codes shown in Figure 6. In this case, all of the charges were to hotels.

Two cardholders seem to have reversed their transactions. Two other transactions may be credits for expenditures that occurred before the period in our query.

Auditors should request support documentation for the three positive expenditures that were not backed out.

Querying for Computer Purchases

Merchant Category Codes (MCCs) may be used to identify purchases of computers and other items specifically prohibited in agencies' procurement card policies and procedures. For example, auditors can identify some computer purchases by querying the transaction database for the following Merchant Category Codes:

> 4816   Computer Network/ Information Services
> 5045   Computers, Computer Peripheral Equipment, Software;
> 5734   Computer Software Stores

This can be helpful if an agency restricts software purchases to specific staff members. However, this search will not identify software purchases made from merchants with other MCCs. For example, if a purchase had been made from a merchant with the MCC of 5999, for "Miscellaneous and Specialty Retail Stores," it would not appear in the results of this query.

Querying for Abusive or Fraudulent Transactions

There are a number of MCCs that auditors may use to identify transactions with a higher risk for fraud and abuse.

Some examples of Merchant Category Codes that may be useful in identifying high-risk transactions are:

5921 Package Liquor Stores	7932 Billiard/Pool Establishments
5933 Pawn Shops	7992 Golf Courses – Public
5944 Jewelry Stores	7994 Video Game Arcades
5971 Art Dealers and Galleries	7995 Betting/Casino Gambling

Copies of this report have been distributed to the following:

Legislative Audit Committee

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The Honorable Bill Ratliff, Lieutenant Governor, Vice Chair
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The Honorable Robert Junell, House Appropriations Committee
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Governor of Texas

The Honorable Rick Perry, Governor

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