

# INTERNAL AUDIT REPORT

## CITY OF MANCHESTER

### NEW HAMPSHIRE



*P-Card Program Performance Audit*  
*December 2007*

Prepared by  
City of Manchester, NH  
Office of the Independent City Auditor

**INTERNAL AUDIT REPORT  
CITY OF MANCHESTER, NEW HAMPSHIRE  
P-CARD PROGRAM PERFORMANCE AUDIT  
JUNE 2007**

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City of Manchester  
Office of the Independent City Auditor

One City Hall Plaza  
Manchester, New Hampshire 03101  
Phone: (603) 624-6460  
Fax: (603) 624-6549

*Committee on Accounts, Enrollment and Revenue Administration  
City of Manchester, New Hampshire  
Honorable Aldermen: Sullivan, Lopez, Devries, M.Roy, Ouellette*

Dear Honorable Committee Members:

At the January of 2005 meeting of the Committee on Accounts, Enrollment and Revenue Administration, an audit plan was accepted by the Committee. The plan was based on risk of the auditees and is adjusted annually for changes happening at the Departments. The P-Card Program was selected for a performance audit due to the relatively high risk and that the program was new to the City and required an evaluation to see if internal controls were adequate and working as designed. A performance audit systematically examines evidence to independently assess the performance and management of a program against objective criteria. Performance audits provide information to improve program operations and facilitate decision-making.

The audit studied the controls in place and compliance with program goals of the City of Manchester P-Card Program and looked at information from January of 2007 to December of 2007.

The audit procedures began with a documentation and evaluation of the internal control structure in place during the audit period. The audit also looked at State and City laws and regulations in force during the audit period. Department Personnel were interviewed, as were personnel from other communities and departments. P-Card Programs from other jurisdictions were looked at and authoritative literature was obtained to determine best practices.

## **Conclusion**

My testing revealed that the program is falling short of its stated goals and objectives and that in several cases internal controls were determined to be inadequate or could be improved. The program is the preferred method of payment to many vendors and several departments. A few departments had issues with the program and would like to see controls strengthened and enhancements to reporting and tracking of expenditures addressed. In general though the program looks promising and can be made to work more effectively and efficiently.

The draft audit report was sent to the Finance Department for review and comment. The observations generated and the auditee written responses are included on pages eight through twenty-two. The auditee responses indicate general agreement with the report recommendations and states that corrective action will or have been taken. I appreciate the courtesy and cooperation of the staff and administration of the Finance Department on this assignment. At all times they acted in the highest professional manner throughout the course of the audit.

Kevin M, Buckley  
Independent City Auditor

April 9, 2008

## INTRODUCTION

### AUDIT BACKGROUND

During fiscal year 2006 the Finance Department proposed a plan for developing a central purchasing function. The top priority of the plan was to implement a purchasing card (P-Card) program. The plan noted that the following benefits would be obtained from going to a P-Card program:

#### Benefits to the City

- One monthly statement per card will be received for verification and reconciliation
- No need to prepare and obtain approval signatures in internal order forms
- Automated data entry
- Fewer accounts payable checks

#### Benefits to the Cardholder

- Obtain goods and services much faster and easier than before
- Significantly reduces workload related to the purchase of and payment for goods
- Allows the cardholder to be more efficient and to focus on the value added aspects of their job
- Significantly reduces clerical processing time and time associated with the approval process

As a further benefit there is a rebate program that was negotiated with the Bank of Montreal. The City will receive a rebate of .41% of purchases over \$3,000,000, .7% over \$4,000,000 and .91% over \$5,000,000. It was originally estimated that the purchasing card would replace 28,000 purchase orders saving 4,500 man-hours of processing time and generate a rebate of \$518,000.

During the audit of the 2007 financial statements the external auditors noted that the P-Cards program had several internal control weaknesses. FY 2007 was the first full year of the program and due to the noted deficiencies in internal controls I decided that an audit of the program was needed to determine the extent of the internal control deficiencies and if the program was working as designed.

My audit was conducted in accordance with standards applicable to performance audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

## AUDIT SCOPE AND OBJECTIVES

This audit was a performance audit designed to test the effectiveness and efficiency of the operation of the purchasing card program as well as compliance with City purchasing rules and regulations and internal controls.

I tested transactions posted to the program from January of 2007 through December of 2007 for compliance with the City Business Expense Policy and the City Purchasing Policy. I also tested and evaluated the system of internal controls in place during the audit period. In addition I interviewed cardholders, approving officials and the program administrator.

### Audit Objectives:

The objectives of our audit was to determine whether internal controls over the issuance, use, and cancellation of procurement cards was adequate and whether procurement card purchases were in compliance with the Procurement Card Program Policy and Procedures. Specifically, to determine:

- Backup documentation (i.e., statements, original receipts) is received from the departments/divisions and reconciled to the monthly procurement charges.
- Procurement cards are cancelled timely (3-5 days of termination date) after employees terminate employment with the City.
- Procurement cards are not used for personal use.
- Purchase of capital assets (\$5,000 or more) by cardholders with higher spending limit are tagged and recorded in Finance as fixed assets.
- Purchases made by the Procurement Card Program Administrator are independently monitored.
- Purchases are within cardholders' single and monthly limit.
- Split purchases are not made by cardholders to stay within their single purchase limit.
- Discount opportunities on high frequency purchases made from the same vendors are sought by the Procurement Card Administrator.
- Similar purchases that total more than \$10,000 are going through quotes or greater than \$25,000 competitive bid processes rather than procurement cards.
- Procurement cards are used for small purchases (\$0 - \$10,000) rather than using purchase orders.
- Training is given to new cardholders prior to using their procurement cards and annual refresher training is given to current cardholders.
- Savings in time and dollars as noted in the original proposal for the program are being realized.

The results of my testing and the related observations and recommendations are included in the report that follows.

## BACKGROUND OF PROGRAM

### *Organization and Personnel*

Control of the P-Card Program is a function of the Finance Department. The Finance Director is responsible for the implementation, maintenance, program compliance, payment processing, issuance of P-Cards and bank relations to resolve customer complaints. The P-Card Administrator has been delegated by the Finance Director to oversee the program. Currently the P-Card Administrator position is being held by a Financial Analyst I.

Every department participating in the program assigns an Approving Official whose function is to review and approve daily P-Card transactions in the HTE Procurement Card Module. Their duties include reviewing the transaction on-line and compare the amount to supporting documentation, entering the proper accounting information including work orders and/or project number and approve the transaction. As of December 31, 2007 there were 57 approving officials.

Monthly a statement of activity for the department is run, reconciled to the supporting documentation and approved by a department official. The reconciled and approved report is then forwarded to the Finance Department for processing.

Each Approving Official is responsible for ensuring compliance with program regulations of the several P-Card Holders assigned to them. Cardholders are responsible for adhering to the program's Code of Conduct and principles as set out in the User's Guide as well as all City rules and regulations governing the purchase of goods and services. As of December 31, 2007 there were 281 active cardholders in the system.

### *History*

Purchasing cards were developed in the late 1980s as a way of helping federal government agencies to acquire small-dollar items without subjecting their vendors to the payment delays associated with bureaucratic procurement processes. In addition to expediting payment, purchasing cards have been found to have other benefits such as reducing paperwork associated with requisitions, purchase orders and invoices for thousands of small dollar items.

Based on a survey by Richard J Palmer, Mahendra Gupta, Antonio Davila and Tim Mills local governments report an average per transaction savings in administrative paperwork handling of \$46 and an average reduction of 5.4 days in the time elapsed from need determination to receipt of the ordered goods.

During fiscal year 2006 the Finance Department proposed a plan for developing a central purchasing function. The top priority of the plan was to implement a purchasing card program.

An RFP was prepared and the Bank of Montreal was selected as the card vendor. A contract was executed on May 17, 2006. Vendors were notified that they would be required to accept the City purchasing cards no later than July 31, 2006. The Finance Department initially activated 122 cards and the City started using the cards in September of 2006.

At the beginning of implementation the Finance Director and Deputy Finance Director were assigned the position of P-Card Administrators and set up the program and its controls. After implementation the duties of P-Card Administrator were assigned to a temporary P-Card Administrator in the Finance Department. When the employee left their duties fell to the Office Administrator.

Since that time the number and dollar amount of transactions had quickly peaked in early to mid 2007 and has since leveled off.

<b>PCARD ACTIVITY SEPT 2006 THROUGH DEC 2007</b>					
<b>MONTH</b>	<b>ACTIVE CARDS</b>	<b># OF TRANS</b>	<b>\$ OF TRANS</b>	<b>AVE \$ PER TRAN</b>	<b>AVE \$ PER CARD</b>
SEPT 2006	122	62	\$ 27,946	\$ 451	\$ 229
OCT 2006	148	251	113,720	453	768
NOV 2006	170	285	98,291	345	578
DEC 2006	216	426	246,143	578	1,140
JAN 2007	239	528	238,082	451	996
FEB 2007	239	615	312,677	508	1,308
MAR 2007	243	768	293,256	382	1,207
APR 2007	258	694	266,914	385	1,035
MAY 2007	267	741	222,062	300	832
JUNE 2007	279	692	268,575	388	963
JULY 2007	281	701	245,372	350	873
AUG 2007	286	879	340,598	387	1,191
SEPT 2007	286	684	265,203	388	927
OCT 2007	285	747	209,666	281	736
NOV 2007	284	737	227,786	309	802
DEC 2007	284	643	226,316	352	797
<b>TOTAL</b>		<b>9,453</b>	<b>\$ 3,602,607</b>	<b>\$ 381</b>	<b>\$ 927</b>

SOURCE: BMO Online Monthly Activity Reports

If you use the average savings of \$46 per transaction in administrative paper work cited in the survey by Palmer, Gupta, Davila and Mills the City has realized an average savings of over \$27,000 per month in administrative paper work. These savings are of time that was able to be used in other areas. P-Card use has also resulted in an increase in efficiencies in paying vendors allowing the City to negotiate better prices for commodities such as office supplies for all City Departments and pharmacy purchases by the Welfare Department.

## CUSTOMER SATISFACTION SURVEY

In order to gauge how satisfied users are with the program I used a combination of interviews and questionnaires to judge satisfaction and determine if users were properly trained in card usage procedures. I sampled ten approving officials and 28 cardholders in the survey. Following is a summary of the results.

### *Satisfaction with the program*

In general most cardholders are very satisfied with the program and find it a big improvement over the purchase order system or the old credit cards. Vendors prefer it because they are able to get paid immediately although a very few vendors will not take a credit card due to the associated fees.

Approving Officials and BSOs have mixed feelings about the card. The Welfare Department prefers the card claiming that it saves them time and is more convenient. The police department also likes the program claiming it reduces mail and takes them no more time than the old system.

Of cardholders responding to the question 77% had a favorable opinion of the program, most citing the ease of use as the reason for satisfaction with the program.

Some departments did not like the program. Problems most often cited were:

- Problems with WB Mason posting expenditures but not sending invoices in a timely matter
- Poor reporting functions, no access to online reports
- Additional paperwork, takes more staff time
- Poor internal controls
- Payment occurs prior to getting all receipts
- Requisition/encumbrance process bypassed causing problems at year-end

### *Training*

Approving Officials had the highest percentage of employees who indicated that they were trained by people from the Finance Department (60%) as opposed to 20% of cardholders surveyed. Forty-five percent of cardholders received their training from written material handed out to them as opposed to 20% for approving officials. The remainder indicated that they received no formal training at all (20% approving officials and 35% of cardholders).

When asked if they felt they had enough training and understood the program 75% of cardholders and 60% of approving officials indicated they had adequate training.

When asked questions about the program however 50% of approving officials did not know the spending limits of the cardholders that they approved and 30% of cardholders did not know their own spending limit.

On all questions concerning knowledge of City policies and procedures approving officials claimed they had a thorough knowledge. Several cardholders (30%) did not feel that they had an understanding of City purchasing rules or documentation requirements.

### *Card Security*

When asked where P-cards are kept when not in use 75% of cardholders indicated that when not in use P-Cards are kept in a secured location such as a safe or locked file cabinet drawer. The remaining 25% of cardholders kept their card with them at all times. Some departments such as the police department and library had the cards locked and access to them controlled by a few employees who would check them out and in only when needed.

30 percent of cardholders surveyed are also approving officials who approve their own transactions in the system. Half of the approving officials surveyed are also cardholders and can approve their own transactions in the system. There were two cardholders that were also approving officials but had departmental policies in place against approving their own transactions.

An article in the June 2002 Acquisitions Directions Advisory discusses best practices for a successful purchase card program. Following is a discussion of best practices compared to practices at the City of Manchester.

### ***BEST PRACTICE: MAKE TRAINING MANDATORY***

*The key to a successful program is educating all participants in the proper execution of the program. This means educating the cardholders on applicable procurement regulations, appropriations issues, and reconciliation of monthly purchase card statements. It means educating oversight officials on appropriate review of cardholders' purchases and reconciliations and appropriate use of oversight tools available to them.*

### **OBSERVATION 1: INSUFFICIENT TRAINING PROGRAM**

#### *Observation:*

Many of the card holders are outside of the procurement function and don't have a good knowledge of budgets or purchasing rules. Card holders need to know that purchasing a refrigerator for your office is generally not allowable and there is a fine line on whether food provided for training is allowable.

The P-Card program does not offer any organized and continuing training for card holders or approving officials and instead leaves it up to them to research purchasing rules and determine what is appropriate.

*Recommendation:*

The P-Card administrator should develop a training program that covers subjects such as:

- The City Business Expense Policy
- The City Procurement Code
- City Budgets
- Year end closing procedures
- Record keeping
- Proper documentation
- Duties of Approving Officials
- How to conduct a review of purchase card transactions

Training should be mandatory and refresher courses provided annually. Refresher courses do not have to be classroom classes but could be done on-line or by written materials that are updated annually for changes to the program or purchasing rules.

*Auditee Response:*

We agree with the auditor's recommendations however, we do not have the available resources to develop and implement these training programs. We intend to implement these recommendations when the Finance Department reaches full compliance in July, 2008.

## INTERNAL CONTROLS

### *BEST PRACTICE: ENSURE STRONG MANAGEMENT, SUPPORT OF CONTROLS*

*The most successful government purchase card programs have a common characteristic: strong commitment and leadership by senior management. A positive control environment is the foundation for all other standards, as it provides discipline and structure.*

The Program Administrator in the Finance Department was assigned the task of administering the program after the program was set up. The program is done in addition to her other duties as office administrator. Daily she performs the functions of the program assigned to her and appears to keep a close eye on the program. The Program Administrator does a good job of fostering a positive control environment based on the program given to her. As noted in the observations that follow the program has some internal control concerns that need to be addressed in order to make it more secure. The auditor has some additional concerns that the Program Administrator's other duties do not allow her the time necessary to make the function run as effectively as possible.

### *BEST PRACTICE: USE THE INFREQUENT BAD APPLES AS EXAMPLES*

*The consequences and penalties of inappropriate behavior should be clearly outlined Prior to issuing a purchase card. The organization should ensure that swift action is taken for those that improperly use the card and make the improper uses – and the consequential actions taken – known to all cardholders.*

The City of Manchester program achieves this best practice by having a code of conduct that cardholders are required to abide by. This is a commendable practice; however, I feel that there are some areas of the Code of Conduct that could be improved.

## **OBSERVATION 2: CODE OF CONDUCT LACKING IMPORTANT ELEMENTS**

Cardholders are required to sign a purchasing card agreement form prior to receiving their card. One of the elements they agree to is that they have read the Purchasing Card Program Cardholder Guide (the Guide) and will abide by the policies contained within. The final section of the Guide is a written code of conduct.

My review of the guide has noted that there are a couple of missing elements that should be in the code of conduct.

- The code of conduct does not have any reference to the City Procurement Code or the City Business Expense Policy. Both these documents are an integral element of control over expenditure of City funds. All cardholders should be familiar with the policies prior to being allowed to spend City funds.

- The Guide has some language in the Overview section and in the Audits section that deals with penalties or corrective action that will be taken if the cardholder does not adhere to the policy. This language is missing from the code of conduct. The language is also vague and does not spell out any steps that will be taken such as suspension of use, required additional training, revocation of use and dismissal.

*Recommendation:*

The code of conduct should be amended to include reference to the Procurement Code and Business Expense Policy as well as language that reflects the penalties for noncompliance.

*Auditee Response:*

We agree with the auditor's recommendation however, with our current compliment we do not have the available resources to dedicate the time and effort needed to implement changes. We intend to implement these recommendations when the Finance Department reaches full compliment in July, 2008.

As of August 2008, the recommended additions relating to policies and penalties were added throughout the Cardholder Guide as appropriate.

***BEST PRACTICE: BE SELECTIVE IN ISSUING CARDS***

*Establish an effective approval process through which applicants must be approved prior to being issued a license to spend taxpayers' money.*

The City of Manchester does have a policy of only issuing P-Cards after the prospective cardholder has signed the P-Card agreement. Written procedures are also in place that requires changes are done timely and only after a signed and approved change order form is presented to the P-Card Administrator. City policy is that cancelations are to be done immediately upon notice of termination. My testing of these controls revealed several errors as noted in observations 3 and 4.

***BEST PRACTICE: TAKE ADVANTAGE OF PREVENTATIVE CONTROLS TO MINIMIZE RISK EXPOSURE***

*Use built in controls of the system to block certain spending categories or purchases from certain vendor categories.*

While the BMO system has a number of controls available to the program, as noted in observations 3, 4 and 5, the City has not taken full advantage of them.

### **OBSERVATION 3: UNTIMELY CARD CANCELLATIONS AND ACTIVATIONS**

*Observation:*

A P-Card Program best practice is that when a person leaves City service the employee's P-Card is immediately cancelled. The P-Card Administrator in the City of Manchester relies on the department to notify her of a P-Card holder change. I ran a report of all P-Cards and their status as of 1/10/08 and a Termination Report for the calendar year ended 12/31/07 from the HTE system. I then compared the termination date on the Termination Report to the termination date on the card holder report and termination dates in the BMO Online system. I noted of the twelve cardholders that were terminated during the year four had cards that were terminated up to seven days, and in one case, 125 days after the employee terminated their service with the City.

Cards that are active after an employee's termination date increases the risk that improper charges can be made after an employee leaves service.

It was also noted that of the 282 cards reported as active in the HTE module, 24 were cards that have yet to be activated in the banking system and are currently sitting in the Finance Department safe. These cards have been in the department's possession for over a year without being activated. This runs the risk, although a small one, that the cards could be activated and fraudulently used.

This is reflective of the Finance Department initially ordering cards prior to approving the employees for the P-Card Program. From our sample of 28 cardholders 25 were added to the system prior to being approved by the department head, and P-Card administrator. Because cardholders are not required to come to Finance in person and sign for their cards it cannot be determined if the card was held until all approvals were received.

Of our sample of 25 active cardholders 6 of 7 had per purchase limits noted on the application and in the HTE module but no per purchase limit set in the BMO banking system.

*Recommendation:*

When an employee terminates employment the P-Card should immediately be cancelled. For employees who voluntarily leave service the cancellation date should be the date the City is notified of the employee's intent to terminate. If the employee needs to make a purchase after that date they may use a purchase order.

Cards should not be ordered for employees who have not been approved for the program and the cards in the safe should be destroyed after determining that the listed card holder will not participate in the program.

Cardholders should be required to come to the Finance Department and sign that they have received their card.

The P-Card Administrator should ensure that any per purchase limits noted on the application are actually being used in the BMO banking system.

*Auditee Response:*

We agree with the auditor's recommendations and have taken measures to resolve some of the issues noted. The 24 cards that were in the Finance safe have been cancelled and destroyed. In three of the four circumstances noted in the auditor's observation, the departments had specifically requested that the cards remain open for billing reasons ie: update the credit card information with the vendor, and/or a pending credit that was due on the card. Currently, it is not Finance Department policy to order cards prior to approving the employee for P-Card Program. We do not order a card until an application is received by Finance and signed by the applicant, the department head and p-card administrator. We currently do not have the available resources to dedicate the time needed to research and institute the necessary changes to monitoring accounts, updating policies and changing procedures. We intend to implement these recommendations when the Finance Department reaches full compliment in July, 2008.

**OBSERVATION 4: FINANCIAL EXPOSURE NOT ADEQUATELY CONTROLLED**

*Observation:*

One of the goals of an effective internal control system of a purchase card program is to try and understand and reduce the City's financial exposure to loss. The total financial exposure of the P-Card Program is a function of the combined spending limits of the individual cards. Financial exposure is limited by controlling the number of cards allowed to only those necessary to carry out the City's functions and to set both daily and monthly limits to the minimum necessary to carry out each individual cardholders needs. The cards can also be restricted to only certain types of merchant category codes.

To understand the exposure the P-Card Administrator should be aware of the total spending limits and be constantly monitoring the spending habits of the individual cardholders to determine if the limits need to be adjusted. The BMO Online system and the HTE P-Card module provide many report functions that would be useful in an ongoing monitoring program.

The following issues were noted during my review of the P-Card program that affects the financial exposure of the City.

- The P-Card program does not appear to do an adequate job in controlling the issuance of new cards. As of January 10, 2008 the City had 282 active cards. There does not appear to be any written rule or procedures for determining who should be eligible to have a purchasing card. The thought appeared to be to get as many cards out there as possible in order to maximize the use of the program and achieve expenditure levels necessary to take advantage of the rebate program. This has caused a proliferation of cards that may be leading to span of control issues in some departments.

- There do not appear to be any written rules or procedures for setting spending limits. From a review of P-Card spending limits it appears that most cards are set at a default of \$1,500 or \$2,500 for both the monthly and per transaction limits. Even with cards that have high spending limits the per transaction limit defaults to the monthly spending limit. For example there are several cards with spending limits of \$100,000 to \$250,000 for both the monthly and per transaction limit. The rationale is that occasionally that individual will have to purchase a single item such as a vehicle or piece of equipment that would be close to their limit. The program has the ability to temporarily change limits for occasional large purchases but they do not take advantage of this ability.
- The program lacks a written required monitoring program to review spending levels and spending patterns. Departments do not have to certify to the P-Card administrator that the cards under their control have been reviewed and the limits have been set correctly.
- The program lacks a written program to occasionally review spending reports by vendor in order to negotiate price discounts from frequent vendors and uncover cardholders who are not purchasing off of already established contracts.
- For cards that are used infrequently the program has the ability to quickly activate/deactivate cards so they can be used only when necessary. For example some card users only need the card when they travel. The card can be activated prior to their departure and deactivated upon their return. This program does not appear to be taking advantage of this ability.

*Recommendations:*

1. The P-Card administrator should develop criteria for the issuing of P-Cards and expand the application to include an explanation for the necessity of having a P-Card, expected highest monthly and per transaction level, and frequency of use.
2. Rules and procedures should be developed for the setting of P-Card spending limits. Per transaction level should be based on the usual highest expected transaction and not the occasional highest transaction. If a temporary increase in spending limit is required the reason for the increase and time period required should be documented.
3. The program should have an ongoing continuous monitoring program to determine if spending limits are set correctly. This can be done at the approving official level on an annual basis. The approving official will then certify to the P-Card Administrator that the levels are set correctly or that adjustments need to be made.
4. The program should have a vendor spending monitoring program to try and find opportunities for negotiating price breaks with vendors and discovering card holders who are not buying on pre-negotiated contracts unless they are able to purchase at a lower price for an equal or better commodity.
5. The P-Card administrator should take advantage of the ability to activate cards only when needed and deactivate when the activity is over or to temporarily raise the spending limits for the occasional large purchase.

*Auditee Response:*

We agree with the auditor's recommendations and are looking at current spending limits and spending. However, with our current compliment we do not have the available resources to dedicate the time and effort needed to continuously monitor department spending, credit limits and vendor relations. We intend to implement these recommendations when the Finance Department reaches full compliment in July, 2008.

**OBSERVATION 5: CONTROLS OVER CHANGES NOT CONSISTENTLY APPLIED**

*Observation:*

I selected all changes made to account limits during CY 2007 from BMO Details Online and traced the information to the P-Card Account Maintenance Form. Of the 31 changes that took place 14 (45%) had errors noted as noted below:

- Three changes had per purchase changes noted on the form that were not included in BMO Details Online.
- Three changes in BMO Details Online had no P-Card Maintenance Form on file.
- Two instances where the final approval was done subsequent to the change in BMO Details Online.
- Six instances where the P-Card Maintenance Form lacked the P-Card Administrator approval
- One P-Card had all limits removed from the card with no P-Card Maintenance Form on file.

*Recommendation:*

- The one card where the limit was removed should be changed to reflect a reasonable limit level.
- P-Card Maintenance forms should be maintained for all changes.
- All approvals should be obtained prior to making the change in BMO Details Online.
- As also noted in observation N-5 per purchase limits while noted on many of the card applications and change forms are rarely included in BMO Details Online. The program should take advantage of this feature to limit exposure to large expenditure errors or irregularities being charged to the card.

*Auditee Response:*

We agree with the auditor's recommendations and have are in the process of correcting any discrepancies. We are also carefully monitoring all requests and forms prior to making any changes on P-Card accounts.

## ***BEST PRACTICE: ESTABLISH SPENDING LIMITS COMMENSURATE WITH NEEDS***

*Agencies should strive to align cardholder limits with actual needs and to establish a process by which spending limits are reviewed on a regular basis and cardholders can receive a one-time spending limit increase if the legitimate need to do so arises.*

The City does have a process to set limits when a card is issued but as noted in the following observations does not have written rule or procedures to set the limits and does not have a program to review limits on a regular basis to ensure that they are set correctly. They do have a process to allow a one-time spending increase under certain circumstances that testing has shown appears to be working adequately.

### **OBSERVATION 6: SPENDING LIMITS SET EXCESSIVELY HIGH**

#### *Observation:*

I selected 34 cardholders for testing to determine if the monthly and per purchase expenditure limits were set at a level that would minimize the exposure to the City for loss due to inappropriate card use. For the cardholders selected I obtained all expenditures charged to the card in calendar year 2007 and calculated the highest monthly and per purchase item charged during that time period.

#### Per-Purchase Limit Testing

In my sample of 34 cardholders the-per purchase limit appeared to be selected in only one card. As noted in Observation 4, the per-purchase limit option is rarely used as a control. When the-per purchase control is not selected it defaults to the monthly amount. From my sample only 2 cardholders demonstrated a need to have as high of a per purchase amount as was set in the BMO Banking system.

#### Monthly Purchase Limit Testing

For testing purposes a monthly purchase limit was determined to be unnecessarily high if the highest monthly balance during the year was less than 50% of the cardholder's monthly limit set in the system. Out of the 34 card selected for testing 27 (79%) had monthly limits that appear to be unnecessarily high. Eleven cards (32%) had no activity throughout the 12 months. As part of my sample I selected all cards with a per month limit of over \$70,000. Of these six cards one had no activity for the year and three others had seven or less transactions during the year.

Three of these high limit cards belonged to department heads and had limits of \$100,000 with almost no activity.

*Recommendation:*

The P-Card administrator should require that annually every approving official should review the activity and limits for all cardholders under their control and either adjust the limits or justify the reason for maintaining such a high limit.

Department heads should not have high limits set on their cards. Department heads should use their cards for travel related expenses only.

*Auditee Response:*

We agree with the auditor's recommendation. Currently, spending limits are set by the department head and changed (i.e.: limits are increased or decreased) as necessary. We are looking into current spending limits versus actual spending however we do not have the resources to dedicate the time and effort needed to monitor this control. We intend to implement the recommendation when the Finance Department reaches full compliment in July, 2008.

***BEST PRACTICE: COMMIT THE RESOURCES NEEDED TO ACHIEVE SUCCESS***

*Allocate sufficient resources to effectively manage and perform oversight.*

The City appears to have assigned sufficient numbers of approving officials to manage the oversight function. The federal GSA suggests that five to ten cardholders per approving official is an appropriate number. The City seems to be well within that range. From a survey of approving officials none indicated that they had too many cardholders assigned to them.

***BEST PRACTICE: IDENTIFY APPROPRIATE OVERSIGHT OFFICIALS AND CLEARLY DELINEATE RESPONSIBILITIES***

*Agencies should establish and apply the same high standards of cardholder selection to the selection of approving officials. Approving officials should be sufficiently independent and of sufficient rank to question the cardholder when additional information is needed about specific transactions. Approving officials should be held accountable for performing adequate, timely reviews as part of their job performance review and should be held accountable for cardholder abuse when inadequate reviews were a contributing factor.*

As noted in observation 7 the P-Card program does not always do an adequate job in assigning approving officials.

***BEST PRACTICE: ENSURE SEPARATION OF DUTIES***

*Responsibilities of cardholders, reviewing officials, and reviewing and approving the A900 report should not overlap. Cardholders should not be approving their own transactions either at the approving official level or when signing off on the A900 report. In general, a single individual should not buy, receive and certify funds available for purchases. Key duties such as authorizing, approving, and recording transactions; issuing or receiving assets; making payments; preparing*

*checks and check signing; certification of funding; and reviewing or auditing should be assigned to separate individuals.*

In general the program has adequate separation of duties but testing revealed certain instances where approving officials approved their own transactions and in some cases also signed the A900 as noted in observation 7.

***BEST PRACTICE: ESTABLISH A MULTI-FACETED APPROACH TO MONITORING AND OVERSIGHT***

*A strategic multi-faceted approach to monitoring is warranted that addresses who conducts reviews and how they will be conducted. This includes the strategic use of automatic reporting tools, primary oversight at the department level and a higher level of oversight protection in the case that departmental oversight fails.*

The P-Card program has both department level monitoring and monitoring at the Program Administrator/Finance Department A/P processing level. As noted in observation 7 the program does not make full use of available reports for program monitoring.

**OBSERVATION 7: WEAK CONTROLS OVER APPROVING OFFICIALS**

*Observation:*

The P-Card program consists of three layers of control agents.

- The P-Card Administrator in the Finance Department has overall control of the program. She controls access to the system by granting approval of P-Cards and setting dollar limits on card use by month and per transaction.
- The Approving Official is the first line of defense against waste, fraud and abuse. Their job is to review P-Card transactions in the system to ensure that the correct amount has been charged, that sufficient and proper documentation is available and that all charges are legitimate and follow all City procurement and expense policies.
- P-Card users are responsible for obtaining proper documentation for their transactions and following correct procurement and expense policies and procedures.

A best practice for P-Card programs is to clearly identify oversight officials and clearly delineate responsibilities. Agencies should establish and apply the same high standards of cardholder selection to selection of approving officials. Approving officials should be sufficiently independent and of sufficient rank to question the cardholder when additional information is needed about specific transactions. Approving officials should also be assigned only the number of cardholders to review that they can easily handle in conjunction with their regular duties (also known as Span of Control).

The City of Manchester P-Card Program does not follow this best practice in several important ways.

- Approving officials do not have to sign an agreement or be approved by the P-Card Administrator in order to be an approving official.
- The P-Card Administrator does not track approving officials. When asked for a list of approving officials it took a few days and the combined efforts of two people to put one together. The P-card administrator should be aware of who is an approving official and should be monitoring them.
- There is no written guidance or any policies and procedures for being an approving official.
- There is no training program for approving officials.
- There is no policy on the span of control that is appropriate for an approving official. The Department of Defense issued guidance that each approving official should be responsible for between five to ten cardholders. The federal General Services Administration cites that the most common ratios are between four and ten cardholders per approving official.
- Approving officials should not also be card holders as these are incompatible duties. From a review of approving officials it was noted that some were also card holders.
- From the review of approving officials and cardholders it was noted that several department and division heads had P-Cards and the approving officials were staff who worked for them. In some cases a card holder was also an approving official for their supervisor which poises an independence problem.

*Recommendation:*

1. The Finance Department should develop a written approving official guide and policy and procedures manual for approving officials that clearly spells out the duties and responsibilities of approving officials. The guide should also set a range for the span of control that any single approving official should have that would ensure that the official will have the time to adequately perform their crucial control functions.
2. The Finance Department should develop a training program for all approving officials. Training should be a required prerequisite to becoming an approving official. There should also be an annual refresher course that would discuss new policies and procedures or problems encountered with the program.
3. Approving officials should be required to submit a purchasing card approvers request form and a purchasing card approvers agreement much like the cardholders submit before they can use a card. This form would be evidence that only qualified employees who have been trained and understand their required duties are allowed to be approving agents.
4. The P-Card Administrator should monitor the activities of approving officials to ensure that they are attending annual training sessions and that they are performing their job functions adequately. The P-Card Administrator should be made aware of any problems with documentation or questioned expenses found by the Accounts Payable employee in the Finance Department. A pattern of rejected monthly invoices could indicate a problem that may be corrected with additional training.

5. Approving officials should not be cardholders who have the ability to approve their own transactions. This is extremely important in smaller agencies where the approver may also be the person who receives the goods or service and thereby controls the entire process.
6. Department head P-Cards should be limited to travel expenses only when the approving official is an employee reporting directly to them. No approving official should be in charge of approving expenses of an employee who is in a position that does not allow the approving official to question the cardholder for additional information.

*Auditee Response:*

We agree with the auditor's recommendations and have been updating the current p-card approver's guide. However, with our current compliment we do not have the available resources to dedicate the time and effort needed to research, develop and implement the recommended changes to training, policies and procedures. We intend to implement these recommendations when the Finance Department reaches full compliment in July, 2008.

## **PROGRAM GOALS AND OBJECTIVES**

When the P-Card Program was proposed two important parts of the justification to start the program were:

1. Use of the card would save time and money by shifting time and costs away from the processing of purchase orders and reconciliation of checks.
2. The program would provide an additional revenue source from a rebate program offered by vendors.

Based on a study done by the National Association of Purchasing Card Professionals the average savings from using a purchase card was \$60 per transaction compared to the traditional PO process. In July of 2006 the Finance Department presented the P-Card Program as part of an overall Central Purchasing Program. They identified over 28,000 purchase orders requiring 4,500 man-hours of processing time during calendar year 2005. They claimed that if the P-Card system was in place the City would have received \$518,652 in rebates during that year.

### **OBSERVATION 8: PROGRAM NOT MEETING USAGE GOALS**

During calendar year 2007, the first full year that the P-Card Program was in effect the program replaced approximately 8,200 transactions and returned rebates of \$12,679.

There were several reasons for the low rate of use compared to the estimate.

1. Many of the vendors that it was assumed would accept the P-Cards with either would not accept or were unable to accept the cards for certain transactions.
2. Not all departments were willing to shift immediately to the program and only used the cards for part of the year or used them for only limited transactions until they figured out how to best use the cards and how to control their use. There were many unanswered questions about the card use that made some business officers uncomfortable with their use. They felt uncomfortable with the lack of an encumbrance at year end and also felt that several internal controls were weakened.
3. Several employees chose not to use the card because they felt that they would be exposed to personal risk from some of the requirements in the P-Card Agreement that they would have to sign.

#### *Recommendation:*

1. The City should continue to work with vendors to gain acceptance for the program.
2. Procedures should be developed in order to address the concerns of card users. More training and communication with departments is necessary in order to identify and solve card issues as they come up.

3. The card agreement should be modified to make it clear that employees could be held responsible for transactions only if they are in willful violation of the policy. It should be made clear that employees would not be held personally responsible to pay back the City for honest mistakes but only for willful violation of policy.

*Auditee Response:*

We agree with the auditor's recommendations. We have worked with our credit card provider as well as contacting our vendors directly and unfortunately the utility companies, which make up a significant amount of our spending, will not allow the City to use credit cards to pay bills. We intend to implement these recommendations when the Finance Department reaches full compliment in July, 2008.

## **APPENDIX**