

OFFICE OF THE CITY CONTROLLER



**FINANCE DEPARTMENT
STRATEGIC PROCUREMENT DIVISION MANAGEMENT**

PERFORMANCE AUDIT OF PCARD PROCUREMENT

Ronald C. Green, City Controller

Courtney E. Smith, City Auditor



OFFICE OF THE CITY CONTROLLER
CITY OF HOUSTON
TEXAS

RONALD C. GREEN

February 24, 2015

The Honorable Annise D. Parker, Mayor and Honorable Council Members

**SUBJECT: REPORT #2015-06
FINANCE DEPARTMENT (FIN), STRATEGIC PROCUREMENT DIVISION (SPD) – PURCHASING CARD
(PCARD) PROCUREMENT PERFORMANCE AUDIT**

Dear Mayor Parker and Council Members:

The Office of the City Controller's Audit Division has completed a Performance Audit of the City of Houston's (City) Purchasing Card (PCard) Procurement processes as administered by SPD. After conducting research on ordinances, policies, purchase card industry data, and interviews with key City personnel involved in the process, we refined our audit objectives to determine the:

1. Existence and effectiveness of controls over the use and approval of PCards assigned to employees;
2. Accuracy of information from the Citibank Purchase Card CitiDirect Global Card Management System (GCMS) for posting to the Enterprise Resource Planning (ERP) / SAP system;
3. Existence and effectiveness of systemic PCard restrictions; and
4. Completeness and accuracy of transaction entries interfaced and appropriately uploaded to SAP.

Based on the results of the procedures performed, we determined that:

The City's PCard program streamlines the purchasing process by reducing paperwork, providing greater management flexibility, and reducing the administrative workload related to procurement. These measures reduce the administrative cost of performing the procurement function. In addition, the City earns cash rebates for high volume card use and Department users are able to take advantage of favorable pricing that can be found when purchasing through the Internet.

Key issues identified during our audit were:

- Internal control weaknesses within the process allow spending limits to be bypassed;
- SPD does not have the capability to efficiently and effectively monitor cumulative vendor spending from both PCard purchases and PO purchases; and
- Purchase transaction data uploaded into SAP was not always complete or appropriately coded.

We appreciate the time and efforts extended to the Audit Division during the course of the project by SPD management and staff.

Respectfully submitted,

Ronald C. Green
City Controller

cc: Kelly Dowe, Director, Finance Department
City Council Members
Lourdes Coss, Chief Procurement Officer, Finance Department
Calvin Wells, Deputy Director, Finance Department
Christopher Newport, Chief of Staff, Mayor's Office
Harry Hayes, Chief Operating Officer, Mayor's Office
Shannan Nobles, Deputy Director, Office of the City Controller
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EXECUTIVE SUMMARY

INTRODUCTION

The Office of the City Controller's Audit Division has completed a Performance Audit of Purchasing Card (PCard) Procurement as administered by the Strategic Procurement Division (SPD). During the period covered by the audit SPD was a Division of the Administrative and Regulatory Affairs Department, however it has since moved to the Finance Department. The audit considered compliance with City of Houston (City) purchase card and procurement policies, and the efficiency and effectiveness of procedures in place to ensure all purchase card transactions were recorded and approved. The audit was included in the Fiscal Year (FY) 2014 Audit Plan and was a direct result of our Enterprise Risk Assessment process.

BACKGROUND

The Texas Comptroller of Public Accounts contracted with Citibank, N.A. to provide procurement services for state agencies, universities and eligible State of Texas CO-OP entities such as the City. The initial contract term of the state contract is from September 1, 2010 through August 31, 2013 with three one year renewal options. The City utilizes this state contract for their PCard program. During FY 2013, PCards were used to process transactions totaling more than \$23,000,000. These transactions represent over 61,000 individual purchases to approximately 5,000¹ vendors.

In an effort to manage local government expenses and maximize savings, more cities are adopting new PCard programs or expanding existing PCard programs. These actions are resulting in an increase in the use of these programs over the past few years. PCard programs allow goods and/or services to be procured without utilizing the more traditional purchase order (PO) process. The City's PO process has strong internal controls that lead to systemic documentation of the authorization, order, goods receipt, and payment activities. In addition, the PO process results in itemized purchase detail within SAP. PCards are a payment tool designed to streamline the purchasing process by reducing paperwork, providing greater management flexibility over spending, and reducing the workload for accounts payable and purchasing departments.

Other key advantages of increased P-Card usage are 1) cash rebates earned for high volume card use, 2) the convenience of swiping a card to complete a transaction with a vendor, and 3) the ability to take advantage of lower priced on-line (Internet) shopping from the office computer. Most organizations recognize that issuing a large number of check payments for low dollar purchases to a large number of suppliers is a costly and inefficient process. When purchase/procurement transactions are switched from the traditional PO process to a PCard, efficiency/savings are gained.

While the advantages noted above are beneficial, there are also disadvantages. The Citibank online system does not interface with the City's financial system, SAP. In addition, all vendor purchase data does not upload to SAP, instead only summary general ledger amounts can be found in SAP. Itemized PCard purchase transaction detail is housed in the banking system, but that detail is only provided by a few vendors.

The transaction information available must be viewed and reported in the Citibank online system and many of the automated controls of SAP are lost, for example:

¹ Certain vendors are duplicated due to the inclusion of a store number in the vendor name, e.g., Home Depot #577.



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- Fund, General Ledger, and Cost Center account coding are not verified as valid during data entry in the Citibank on-line data capture system;
 - City Council approved contract limits and fund limits are not checked until after purchases are made and in most cases after the goods and/or services are received;
 - Purchase summary cost data is not recorded or updated in SAP generally between 15 to 45 days after purchases are made;
 - Vendor year-to-date purchase totals as well as detail of items purchased are not available in SAP for review and reporting; and
 - Management approval prior to actual purchase can be bypassed.

The PCard process has fewer system driven internal controls than the PO process, therefore, management in each City department must take the initiative to supplement the PCard process with strong manual internal controls. During the course of our audit, we noted that some Departments had implemented tight controls around the authorization, order, and payment activities.

AUDIT SCOPE AND OBJECTIVES

Our original audit objectives were broadly defined to encompass controls over issuance, use, and approval of PCards and recording of transactions. After further research, the audit objectives were further refined to determine:

1. Existence and effectiveness of controls over the use and approval of PCards assigned to employees;
2. Accuracy of information from the Citibank Purchase Card CitiDirect Global Card Management System (GCMS) for posting to the Enterprise Resource Planning (ERP) / SAP system;
3. Existence and effectiveness of systemic PCard restrictions; and
4. Completeness and accuracy of transaction entries interfaced and appropriately uploaded to SAP.

The engagement scope consisted of the analysis of PCard related processes and transactions for the period July 1, 2012 through June 30, 2013 (FY 2013).

PROCEDURES PERFORMED

In order to obtain sufficient evidence to achieve audit objectives and support our conclusions, we performed the following:

- Downloaded all FY 2013 PCard transactions from the GCMS system;
- Imported PCard transaction data into our ACL analytical software module for review;
- Downloaded vendor and employee data from SAP;
- Interviewed SPD staff regarding their policies, procedures, and monthly activities
- Documented our understanding of SPD's processes;
- Reconciled PCard bank statement dated January 3, 2013, to journal entry data downloaded by SPD staff from Citibank's custom download for the same period;
- Reconciled journal entry data uploaded into SAP to PCard bank statement of the same period;

-
- Performed substantive testing and documented the results from five (5) City departments; and
 - Reviewed rebate documentation.

AUDIT METHODOLOGY

We conducted this performance audit in accordance with Generally Accepted Government Auditing Standards and the International Standards for the Practice of Internal Auditing as promulgated by the Institute of Internal Auditors. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The scope of our work did not constitute an evaluation of the overall internal control structure of the SPD Division. Management is responsible for establishing and maintaining a system of internal controls to ensure that City assets are safeguarded; financial activity is accurately reported and reliable; and management and employees are in compliance with laws, regulations, and policies and procedures. The objectives are to provide management with reasonable, but not absolute assurance that the controls are in place and effective.

CONCLUSIONS AND SIGNIFICANT ISSUES

We believe that we have obtained sufficient and appropriate evidence to adequately support the conclusions provided below as required by professional auditing standards. Each conclusion is aligned with the related Audit Objective for consistency and reference. For detailed findings, recommendations, management responses, comments and assessment of responses see the “Detailed Findings, Recommendations, Management Responses, and Assessment of Responses” section of this report.

CONCLUSION 1

We noted internal control weaknesses that allowed users to bypass spending limits established in Executive Order 1-42 Purchasing Card Policy and Procedures (E.O. 1-42), Administrative Procedures 5-2 Procurement Procedures (AP 5-2), and City Council approved vendor contracts. Significant issues include:

- The spending limit (\$3,000/transaction) was bypassed by splitting transactions using separate invoices or with two or more cardholders making purchases. **(See Finding #1)**
- Contractual spending limits were effectively bypassed when contract coding was not input in Citibank’s GCMS and when contract coding was input, but rejected by SAP. **(See Findings #2 and #3)**

CONCLUSION 2

Comprehensive procedures do not exist to allow SPD to add vendor spending from PCard transactions and PO transactions in order to monitor spending as cumulative totals approach and/or exceed \$50,000. The lack of data hinders the City’s ability to identify areas of purchase activity that


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may warrant new contractual relationships or authorization of increased contract spending. Based on the procedures performed we noted the following issue:

- Fifteen non contract vendors (of approximately 5,000 vendors) had cumulative purchases over \$50,000. These purchases totaled \$1,277,284. **(See Finding #4)**

CONCLUSION 3

We noted that internal controls were inadequate to ensure that purchase transaction data in Citibank GCMS is accurate, and that transaction data is complete, appropriately coded, reconciled and uploaded into SAP. Issues noted were as follows:

- Monthly journal downloads did not match PCard statement totals and no reconciliation between the download and PCard statements is performed; and **(See Finding #3)**
- An average of 29% of departments did not submit to SPD, the PCard summary reconciliation reports used to verify general ledger account numbers in a timely manner. **(See Finding #5)**

CONCLUSION 4

During our substantive testing procedures, we determined that activities related to renewal training, and documentation of receipt of goods and/or services were not in compliance with existing City policies and state law. In addition, governing documents related to technology and gift card purchases were inadequate to ensure that these purchases were properly managed. Issues noted were as follows:

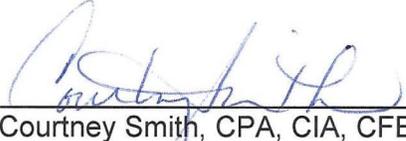
- Executive Order 1-42 – Purchasing Card Policy and Procedures (E.O. 1-42) requires each cardholder to receive training every 2 years, however, only 30% of cardholders received renewal training. **(See Finding #6)**
- PCard supporting documentation does not show evidence that the goods/services purchased were actually received. **(See Finding #7)**
- There are no policies or procedures in place to govern the purchase, distribution, or tracking of gift cards purchased using PCards. **(See Finding #8)**
- The policy requirement in E.O. 1-42 Section 8.0, to obtain Chief Technology Officer (CTO) approval for technology purchases does not clearly define items that require prior approval. **(See Finding #9)**

ACKNOWLEDGEMENT AND SIGNATURES

The Audit Team would like to thank SPD management for their cooperation, time, and efforts throughout the course of the engagement.



David Baszile
Assistant City Auditor III



Courtney Smith, CPA, CIA, CFE
City Auditor

DETAILED FINDINGS, RECOMMENDATIONS, MANAGEMENT RESPONSES, AND ASSESSMENT OF RESPONSES

**FINDING #1 – TRANSACTION AND/OR INVOICE SPLITTING TO BYPASS PCARD SINGLE TRANSACTION CREDIT LIMIT
RISK RATING (IMPACT AND MAGNITUDE) = HIGH**

BACKGROUND:

The City has established guidelines for PCard purchase credit limits. The credit limits are outlined in Executive Order 1-42 – Purchasing Card Policy and Procedures (E.O. 1-42). In addition, Administrative Procedures 5-2 – Procurement Process, the City Charter, and State Law also apply to the City’s procurement process. The requirements of the applicable sections are:

- Executive Order 1-42 Section 6.0 Purchasing Limits Subsection 6.1, states, *“Each user Department will establish spending limits for an individual PCard. The maximum amount of a single transaction will not exceed \$3,000 and the monthly maximum will not exceed \$10,000. Except when specifically stated, PCard limits will not exceed the limits defined in the charter and ordinances of the City of Houston, the procurement laws of the State of Texas and City of Houston Administrative Procedure 5-2.”*
- Administrative Procedure 5-2 Procurement Procedures Section 6.C states; *“Informal bids must be solicited for purchases in excess of \$3,000.00 and up to the State bid law requirement. Quotations must be current and properly documented and written quotations are required.”*
- City Charter Chapter 2; Article III Division 2 Section 2-58(b) states; *“it is hereby declared to be the policy of the city that all purchases and expenditures not exceeding the city council approval requirement limitation amount established pursuant to article II, section 19a of the City Charter may be based on informal bids, except where the department determines that the taking of informal bids would be impracticable (e.g., sole source, emergency, etc.); provided, however, all purchases or expenditures greater than the city council approval requirement limitation amount established pursuant to article II, section 19a of the City Charter shall be authorized by resolution, motion or ordinance of the city council.”*
- Texas Local Government Code Chapter 252; Subchapter B; Section 252.0215 Competitive Bidding In Relation To Historically Underutilized Business states; *“A municipality, in making an expenditure of more than \$3,000 but less than \$50,000, shall contact at least two historically underutilized businesses on a rotating basis, based on information provided by the comptroller pursuant to Chapter 2161, Government Code. If the list fails to identify a historically underutilized business in the county in which the municipality is situated, the municipality is exempt from this section.”*

FINDING:

We performed substantive tests of data from five departments representing twenty-five (25) purchases made to the same vendors on the same date that totaled over \$3,000.

- Of the twenty-five (25) reviewed purchases, five (5) purchases were classified as split transactions. These transactions were either made by the same PCard holder with separate invoices created at the same time or with two or more PCard holders purchasing from the same vendor at the same time. To determine if purchases were indeed splits, we verified that invoice numbers assigned to receipts were consecutive, time of purchase was within minutes of each receipt created, and items purchased had the same descriptions.
- No documentation of an informal bid process or price comparisons were made available for the purchases of items costing more than \$3,000.
- No documentation of requests to bid from historically Underutilized Businesses.

RECOMMENDATION:

We recommend Strategic Procurement Division (SPD) review PCard detail transactions monthly to determine if transaction and/or invoice splitting occurred. In addition, informal bid documentation should be required on all purchases over \$3,000.00 to include soliciting bids from historically underutilized businesses.

STRATEGIC PROCUREMENT DIVISION MANAGEMENT RESPONSE²:

“We concur with the recommendation to increase focus on potential splitting and have instituted this change. With regard to the purchases cited as splits, we agree with four of the five and wish to point out that:

- Three involved purchases pre-approved by user department management; and
- One was identified by the Department Purchasing Card Coordinator (DPCC), resulting in a written caution to the PCard user against splitting.

We also note that the citation of Local Government Code Chapter 252 may not be applicable in certain instances because state law provides for numerous exemptions to the reference section.

SPD attempted to institute an additional control on splitting by disabling a function in the Citibank GCMS system in March 2014, and advising DPCCs of same by e-mail and in at least one meeting of DPCCs; however, disabling the function did not hamper users’ ability to split transactions. SPD has now developed a report to enable monthly review of transactions for signs of splitting. Review of this report is to be accompanied by more proactive outreach to departments to alert them of potential splitting. SPD also includes discussion of splitting in its new online training (expected to be available in spring 2015), including a specific question on the post-training quiz; we will also ensure that training includes explanation of the opportunity to request a temporary credit limit increase through SPD when circumstances warrant same). Increased departmental outreach and training (including, as appropriate, discussions with department management where splitting shows signs of occurring) are to be accompanied by consistent and stringent

² SPD Management responses to each finding are included verbatim. See Exhibit 1 for the complete FIN Management Response memo.

enforcement of EO 1-42 and other relevant policies and laws, with penalties to include PCard suspension or termination for repeat offenders. SPD will continue to explore other potential system controls restricting PCard users' ability to circumnavigate proper procedure, policy and law by splitting transactions above single-transaction limits into one or more smaller transactions.

Regarding the recommendation's second component, requiring informal bid documentation on purchases over \$3,000, this information will be shared with PCardholders whose single-transaction limits exceed \$3,000; so long as other PCardholders comply with the single-transaction limit, informal bidding is not a concern."

RESPONSIBLE PARTY:

Responsible parties for this item include SPD's PCard team, led by the SPD Deputy Director.

ESTIMATED DATE OF COMPLETION:

JUNE 1, 2015

**ASSESSMENT OF
RESPONSE:**

The Audit Division agrees with and commends SPD's commitment to emphasize this issue in training sessions as we recognize that the majority of PCard purchase activity takes place outside of SPD. We also agree with SPD's commitment to enhance management reporting tools which will allow SPD personnel to effectively monitor and enforce single transaction spending limits. The commitments contained in the response adequately address the issue and proposes to remediate.

**FINDING #2 – MISSING CONTRACT NUMBERS ON PCard JOURNAL ENTRIES DOWNLOADED FROM CITIBANK
RISK RATING (IMPACT AND MAGNITUDE) = HIGH**

BACKGROUND:

Contracts are negotiated by SPD on behalf of the City. Each contract is an “*agreement between the City and a supplier/contractor for goods and/or services to be provided to the City of Houston at an agreed upon rate/price, to include binding terms and conditions that govern each purchase order/change order issued by the City for contract goods and/or services*”.³ These contracts have City Council approved spending limits and spending above those limits must be approved by City Council. Each agreement is assigned a contract number that enables management to document goods and/or services purchased through the contract. These contract numbers should be entered on all purchase order related transactions. These assigned numbers allow the City’s SAP financial system to automatically accumulate and track the total contract purchase amounts as a function of invoice data entry. SAP is programmed to reject purchases that exceed the City Council approved contract limit.

Since the original PCard purchase data recording occurs outside of the City’s SAP system, the contract number must be manually entered into the Citibank Purchase Card CitiDirect Global Card Management System (GCMS), downloaded from GCMS to SPD staff computers and later uploaded into SAP, which will allow automated tracking of spending with the contractor. Department PCard coordinators and assigned support staff are responsible for entering the contract number whenever a purchase of a contract item is made along with other general ledger and cost allocation data in Citibank’s GCMS system prior to month end close procedures performed by SPD.

FINDING:

During our audit we reviewed Citibank invoices⁴ for FY 2013.

- Our review of data downloaded from Citibank found 30,966 invoices representing 151 vendors under City contract. These invoices contain account coding including contract numbers as originally entered by users in the various City Departments. Our audit revealed that overall, 30% of this data (9,325) did not have contract numbers assigned. Although, not every purchase with these vendors will be for a good/service covered by a contract, we would expect these numbers to be much lower.
- We reviewed the journal entry upload process for one month using the PCard statement ending January 3, 2013 and determined that contract numbers on journal entries totaling \$33,294.18 were removed. The entries were rejected by SAP because those entries represented contract purchases which would exceed approved contract limits. The contract numbers were removed during the SPD closing process and the journal entries were uploaded into SAP without contract numbers. Rejected transaction information is not kept by SPD so we were unable

³ City of Houston Administrative Procedure 5-2 Procurement Process, April 2010 – Definition of Contract, Section 4-H

⁴ An invoice is defined as the total amount of one purchase as received from Citibank; a purchase could be 1 item or multiple items.

to perform additional analysis on rejected transactions or to determine an average amount of rejected contract journal entries.

RECOMMENDATION:

We recommend SPD consider the following items to strengthen internal controls over journal entry recording:

- Develop a manual or electronic mechanism to monitor department PCard purchases to vendors/contractors who have contracts which have reached their contract purchase limits;
- Develop reports to alert SPD/ Finance Department management and management of other City Departments to vendors/contractors with contracts that are approaching the contract purchase limits;
- Prepare a listing of contractors who have reached purchased limits to Department PCard Coordinators and require submission for additional funding for these contracts through City Council on a timely basis; and
- Enforce card suspension and cancellation as approved by E.O. 1-42 for department cardholders who continue to purchase goods and/or services on contracts that have reached their spending capacity.

STRATEGIC PROCUREMENT DIVISION MANAGEMENT

RESPONSE:

“We concur with the importance of fiscally responsibility and legal compliance in contract management, a responsibility shared by SPD and PCard user departments. As EO 1-42 already requires PCard users to notify their DPCC when using a PCard for a contract purchase, this represents a potential starting point for monitoring PCard purchases’ impact on total spending toward contract amounts and avoiding inadvertent overspending on contract limits. This was addressed with DPCCs in meetings in May and December 2014. For contracts residing within a single department, SPD will increase efforts to directly communicate to DPCCs and departmental management their responsibility for monitoring and managing contract spending to ensure that it remains within approved parameters. For City contracts utilized by multiple departments, SPD will develop an upgraded reporting and monitoring system that draws from PCard usage data and more traditional methods (purchase orders) to track overall City spending against contracts and ensure compliance with approved spending amounts. While this may require some time to develop and implement, SPD will move quickly to improve performance on contract management through communication and coordination with DPCCs and user departments’ management. Penalties for non-compliance may include suspension or termination of PCard privileges.”

RESPONSIBLE PARTY:

Responsible parties for this item include SPD’s Deputy Director, the PCard team, and the Enterprise Resource Planning (ERP) team.

ESTIMATED DATE OF COMPLETION:

DECEMBER 1, 2015

ASSESSMENT OF

RESPONSE:

The Audit Division agrees with SPD’s commitment to improve contract management through communication and the development of an upgraded reporting and monitoring system. We recognize that enhancement in this area will require collaboration with resources outside of SPD but believe incorporating the consideration of PCard usage is critical to overall contract management. Improved reports will allow SPD to independently monitor vendor spending and related spending limits. The improvements will also better prepare SPD personnel as they perform analysis on purchase activity, evaluate existing contracts, or negotiate new contracts. Management commitments contained in the response adequately address the issue and proposes to remediate.

**FINDING #3 – OMITTED TRANSACTIONS IN CITIBANK’S CUSTOM SAP JOURNAL ENTRY DOWNLOADS
RISK RATING (IMPACT AND MAGNITUDE) = HIGH**

BACKGROUND:

The City’s Strategic Procurement Division (SPD) uses Citibank’s GCMS for management of all PCard transactions. This on-line reporting system allows users access via the internet utilizing unique logons and passwords. Users are both card holders, and department assigned coordinators who have the ability to review and edit accounting and cost allocations within each transaction prior to month end closings. Cardholders can only view their individual purchase detail while coordinators have access to all department transactions.

Citibank’s technical staff created the custom download to facilitate automated general ledger journal entry uploads into the City’s SAP accounting system. Each month the SPD PCard Administrator (or designee) runs the custom download report in the GCMS system and creates text files with summary journal totals by general ledger account number. The text files are manually downloaded to local SPD computers and later uploaded into the City’s SAP system. This process is necessary as all PCard purchases are recorded outside of the SAP system.

Once the text files are downloaded by SPD staff, the files are then placed on a designated SAP drive for IT staff to run a custom upload program creating journal entries in SAP. This process creates a journal log which delineates whether each transaction is accepted or rejected into SAP. A transaction is rejected if it has one or more of the following:

1. Incorrect general ledger account number;
2. Transaction amount over departmental budget limit for the contract;
3. An incorrect⁵ contract number;
4. The contract amount entered will exceed the maximum contract dollar limit;
5. An incorrect business area;
6. An incorrect fund number;
7. The total fund amount has been exceeded; or
8. An incorrect grant number was entered.

At this point, SPD staff must contact the department coordinator to resolve the reason for the rejection. Once resolved, the transaction is corrected and resubmitted to IT staff for upload in SAP. New logs are created on each upload process until all transactions which were rejected on initial upload are finally uploaded. This process usually takes four (4) or five (5) upload attempts.

SPD provided copies of one month of journal files downloaded from Citibank’s GCMS system, which we tested against the same month’s PCard bank statement. We imported the text files into an Excel file and totaled all the detail transactions. SAP journal entries representing PCard purchases for the same period were extracted and imported to an Excel file. Comparisons were made between the downloaded GCMS totals and the SAP journal entry totals.

⁵ The term “incorrect” refers to a contract number, business area, or fund number that is not valid (not set up) in SAP. If the contract, fund or business area is valid but was keyed incorrectly, the entry will not be rejected.

FINDING:

- Journal entry download did not match PCard statement total. As a result, several transactions were missing from the custom SAP download due to programming errors. The errors were not discovered by the City or Citibank during initial download program testing. The missing transactions resulted in the posting of an incorrect amount of PCard expenditures to SAP. These errors, although not very significant on a monthly basis (approx. \$2,100.00 for one month), can result in overstating or understating financial statement reporting over time. Transactions were not downloaded as a result of the following:
 1. Citibank applied credits to the City's account due to fraud related findings (security credits); and
 2. Purchases where general ledger entries for an individual invoice had been split between contract and non contract purchases.

- Rejected journal entries encountered during the monthly SAP journal upload process were not always resolved correctly. This occurred in two ways:
 1. Journal entries were rejected because the approved maximum contract spend amount had been exceeded. In these cases, SPD staff removed the contract number from the transaction in order to record the purchase in SAP, however this allowed the department to exceed City Council approved maximum spending limits with the designated vendor; and
 2. Journal entries were rejected and never resubmitted for upload into SAP. This resulted in unresolved entries that were not entered into the financial system. Unresolved journal entries totaled approximately \$24,000.00 for the month tested. The effects on the City's financial reporting can be significant if the entries are never resolved and uploaded.

RECOMMENDATION:

SPD should establish a PCard monthly statement balancing process which reviews both Citibank download files and the SAP uploaded journal data to ensure: 1) all PCard transactions are downloaded, and 2) all rejected transactions during upload to SAP are resolved with department coordinators in a timely manner and re-uploaded to SAP each month.

STRATEGIC PROCUREMENT DIVISION MANAGEMENT

RESPONSE:

"We concur with the recommendation; SPD has already initiated discussions with the ERP team and Citibank to achieve accurate downloading of PCard transactions, including credits. The goal of these discussions is to obtain from Citibank a data file that will capture all secure credits and instances where a single invoice includes both contract and non-contract purchases. SPD will also increase communication and coordination with DPCCs to ensure that journal entries rejected during the SAP upload are resolved and re-uploaded timely and accurately."

RESPONSIBLE PARTY:

Responsible parties for this item include SPD's Deputy Director, the PCard team, and the Enterprise Resource Planning (ERP) team.

ESTIMATED DATE OF COMPLETION:

December 1, 2015

ASSESSMENT OF

RESPONSE:

The Audit Division is aware that SPD has conducted meetings with the ERP team regarding this issue and agrees with management's commitment to resolve programming errors that prevented transactions from being downloaded from the Citibank system. The commitments contained in the response adequately address the issue and proposes to remediate.

**FINDING #4 – SINGLE AND CUMULATIVE PURCHASES OVER \$50,000.00 WERE NOT SUBMITTED FOR CITY COUNCIL APPROVAL
RISK RATING (IMPACT AND MAGNITUDE) HIGH**

BACKGROUND:

Purchases totaling over \$50,000.00 whether one-time or collectively from the same vendor and/or contractor during a fiscal period are governed by both State Law and City of Houston (City) Code of Ordinances. The Texas Local Government Code (Subchapter B, Sec. 252.021) requires that these purchases be formally bid. City Charter Article II, Section 19 requires that these same purchases be approved by City Council. These requirements are supported in Executive Order 1-42 Purchasing Card Policy and Procedure (E.O. 1-42), Section 3.0 (Scope), and Administrative Procedure 5-2 Procurement Procedures (AP 5-2), Section 4, item NN (State Law Bid).

PCard vendor purchases are only tracked in Citibank's GCMS and the system only transfers summary general ledger account, cost allocation, and contract number information to SAP monthly. All purchases are posted through the SAP purchase order (PO) module records and maintains vendor purchase information.

FINDING:

In reviewing more than 5,000 non-contract vendors, we stratified the data and performed detailed analysis of those vendors with PCard purchases totaling more than \$30,000. We added PCard purchases to SAP PO purchases for those vendors and determined that:

- One single non contract vendor purchase exceeded the \$50,000.00 bid requirements.
- Fifteen (15) non contract vendors had cumulative fiscal year purchases of over \$50,000.00 ranging from \$51,717 to \$150,459 for a grand total of \$1,277,284.
- SPD has no procedures in place to identify vendors with high purchase amounts from PCards and traditional PO activity.

RECOMMENDATION:

We recommend that SPD develop a system to combine non-contract vendor purchases from both SAP and Citibank's GCMS for periodic review of those vendors with spending totals over the \$50,000 threshold and seek input from the Department regarding the possible need for contract bidding.

In addition, SPD should limit providing additional credit limits to PCard holders in compliance with E.O. 1-42 which specified transaction and monthly credit limits (\$3,000/\$10,000) without specific oversight of the purchases to be made by the department.

STRATEGIC PROCUREMENT DIVISION MANAGEMENT

RESPONSE:

"We concur with the recommendation, noting that the instances cited by the audit represent a very small portion of the City's non-contract vendors (as the audit suggests, the exact number is difficult to determine, but if it is 5,000, the instances cited would

represent about 0.3 percent of all non-contract vendors). In addition, we note that the section of state law cited includes a list of exemptions against which the instances cited by the audit have not been vetted, so some of the expenditures are likely within the requirement of state law. SPD already reviews non-contract vendor spending via PCard every six months; this will be conducted on a quarterly basis going forward. Further, SPD will initiate enhanced monitoring of City spending with non-contract vendors, including working with the ERP team to develop a system that will combine spending via PCard and purchase orders to identify vendors where total City spend is approaching \$50,000 (this may be linked to the work done regarding Finding 2's recommendation for tracking spending against contracts). SPD will also work with DPCCs to more closely track spending with non-contract vendors, and will re-evaluate training and education offerings to ensure that relevant policies and laws are transparent and clear to all PCard users. Where additional credit limits are granted, SPD will ensure that user department management and staff are aware of relevant rules and restrictions and will also increase its oversight of purchases made with enhanced credit limits."

RESPONSIBLE PARTY:

Responsible parties for this item include SPD's Deputy Director, the PCard team, and the Enterprise Resource Planning (ERP) team

ESTIMATED DATE OF COMPLETION:

DECEMBER 1, 2015

**ASSESSMENT OF
RESPONSE:**

The Audit Division agrees with the commitment to develop and enhance SPD's ability to monitor and identify vendor spend that reaches or exceeds spending limits. The commitments in the response adequately address the issue and propose to remediate.

While we agree that a small percentage of the stratified population of vendors had spending greater than \$50,000 in Fiscal Year 2013, the scope of our audit included the determination of the existence and effectiveness of controls over the use of PCards and the existence and effectiveness of systemic PCard restrictions. These instances represented gaps in the controls governing this area.

**FINDING #5 – DEPARTMENT MONTHLY PCard SUMMARY RECONCILIATION REPORTS WERE NOT SUBMITTED TIMELY
RISK RATING (IMPACT AND MAGNITUDE) = HIGH**

BACKGROUND:

The City of Houston Executive Order 1-42, Purchasing Card Policy and Procedures (E.O. 1-42) 14.0 states: *“Each department will receive their individual Monthly PCardholder statements and a Transaction Summary Report. The PCardholders will use these documents to reconcile their PCard charges within 10 (ten) working days of the date these documents are received. Once the reconciliation is [sic] process is completed, the Department’s PCard Coordinator will sign the Transaction Summary Report, and forwarded [sic] it to the Purchasing Card Program Administrator. **Failure to meet timely submission requirements from PCardholders to the Purchasing Card Program Administrator may cause suspension or cancellation of PCards.** The Purchasing Card Program Administrator sets the cardholder statement due date with the Department PCard Coordinators and may delay the monthly statement deadline based on holidays or operational requirements.”*

At the end of each PCard statement period, Strategic Procurement Division (SPD) staff print and forward copies of the monthly PCard transactions for each department to reconcile and approve. Each PCard is assigned a default general ledger account number and cost allocation at the time it is issued. As part of the reconciliation process, department coordinators must access the Citibank Purchase Card CitiDirect Global Card Management System (GCMS) online and make adjustments to the general ledger account number of each purchase made on the PCard that month as appropriate for the actual goods and/or services purchased.

After the coordinator completes the reconciliation process, signed copies of these statements should be returned to SPD by the designated due date. This process is the internal control SPD has in place to ensure that the charge is appropriate and the general ledger account has been updated in the GCMS system prior to closing the month.

Once the statement month is closed, all general ledger journal information is downloaded from GCMS and then uploaded into the City’s SAP Financial System.

When statements are submitted late, there is no assurance that the account number data has been updated for the purchase transaction detail to be uploaded into SAP.

FINDING:

A review of SPD tracking documentation of monthly statement submission dates shows that on average, 29% of department statements for FY2013 were submitted late. The percentage of late submissions each month ranged from a low of 4% to a high of 60%.

RECOMMENDATION:

We recommend that SPD emphasize the importance of the submission date to the departments and enforce the E.O. 1-42 Section 14.0 authorization to suspend or cancel PCards for those departments that continue to submit statements late each month.

STRATEGIC PROCUREMENT DIVISION MANAGEMENT

RESPONSE:

“We concur with the recommendation, though we believe a risk rating of low is more appropriate. SPD will reinforce the requirements of EO 1-42 Section 14.0 in written and verbal communication with DPCCs and other departmental management. This communication will include a reference to EO 1-42’s potential penalties of suspension or termination of PCards for users that cause late submittal. Timeliness has also been emphasized with training of DPCCs by Citibank in January 2015, and with an accompanying requirement that DPCCs generate their own departments’ statements without waiting for SPD to generate and provide the statements; this shortens the process and increases the likelihood of timely submittal. SPD will also develop a mechanism by which to report non-compliance to user department management, and will review the reconciliation submittal process for other opportunities to improve timely submittal of reconciliation statements.”

RESPONSIBLE PARTY:

Responsible parties for this item include SPD’s Deputy Director and PCard staff.

ESTIMATED DATE OF COMPLETION:

JULY 1, 2015

ASSESSMENT OF

RESPONSE:

The Audit Division agrees with SPD’s commitment to emphasize adherence to reporting deadline dates, monitoring more closely the timely submission of reconciled statements by City departments, and seeking ways to streamline the review process. The timeliness of these submissions assists SPD in the reconciliation process which is an important control. The commitments contained in the response adequately address the issue and proposes to remediate.

**FINDING #6 – PCard RENEWAL TRAINING DOES NOT COMPLY WITH EXECUTIVE ORDER 1-42
PURCHASING CARD POLICY AND PROCEDURE (E.O. 1-42) REQUIREMENTS
RISK RATING (IMPACT AND MAGNITUDE) = HIGH**

BACKGROUND:

E.O. 1-42 Section 5.2.2 states “...Completing **Exhibit 1** (City of Houston Purchasing Card [PCard] Internal Cardholder [Employee] Agreement Form), when a PCard is requested for an employee. Additionally, an updated **Exhibit 1** should be completed for each employee when they receive renewal training which is currently every 2 years.”⁶

The U.S. Government Accountability Office (GAO) Audit Guide⁷ Testing Key Elements of the Control Environment, lists training of all card holders, approving officials and department coordinators as a major procedure to establishing good processing and internal controls. As one of the six key elements of the control environment, training should be designed specifically for the three PCard user groups. Approving officials must be aware of all documentation requirements as well as insuring compliance with correct accounting and cost allocation posting for each PCard purchase.

The guide further states that management should identify the appropriate knowledge and skills needed in the purchase card program, require the needed training, and maintain documentation evidencing that required training is current for all program personnel. The process of updating SAP financials with data entered in Citibank’s GCMS is vital to accurate financial data uploads to SAP.

The Department PCard coordinators are required to manually enter this data, therefore, training of coordinators is an important part of a strong system of internal controls. Coordinators are the first line of defense in the prevention and detection of fraud, waste, and/or abuse in the PCard system. The extent and type of training provided should vary in relation to authority and responsibility the user (Cardholder, Coordinator, Approving Official) has in the program and to the amount of transaction authorization given to the cardholder. At a minimum, a cardholder should receive the standard purchase cardholder training provided by SPD before receiving a purchase card.

FINDING:

Our review of training logs for a two year period (Fiscal Years 2012 and 2013) showed that only 30% or 333 of the 1,128 card holders were documented as obtaining renewal training as required by E.O. 1-42.

- Only one training class format is used for all three user groups, i.e., Approving Officials, Cardholders, and Coordinators.
- Tracking logs were not in place and sign-in sheets were the only proof of attendance at training.

RECOMMENDATION:

We recommend the Strategic Procurement Division (SPD) implement the following:

⁶ **Exhibit 1** should be completed by the Department PCard Coordinator

⁷ Government Accountability Office – Auditing and Investigating the Internal Control of Government Purchase Card Programs

- Increase the number of training offerings and/or the type of training delivery (classroom, online) to accommodate all cardholders.
- Develop specific training agendas for each type of user (Cardholders, Coordinators, Approving Officials).
- Design and implement an automated tracking database system for training and scheduling.

STRATEGIC PROCUREMENT DIVISION MANAGEMENT

RESPONSE:

“We concur with the recommendation to develop a tracking log for refresher training. Additionally, we recommend a risk rating of medium. While EO 1-42 is cited correctly, the background above correctly notes that completion of the referenced forms is – per the EO - the responsibility of DPCCs. To support DPCCs in this responsibility, a tracking log was developed in mid-2014. Finance/SPD appreciate the guidance offered by the City Auditor’s office in this regard; the log will be used to monitor when PCard refresher training is required for individuals involved with PCard usage and approval, and reminders will be issued ahead of the deadline for refresher training. In addition, SPD will perform spot-checks in user departments to ensure that DPCCs are maintaining required documentation of training and refresher training as specified in EO 1-42. Where the provisions of EO 1-42 are not complied with in a timely manner, PCards may be suspended or cancelled.

We do not necessarily agree PCard users’ failure to participate in required refresher training (or lack of documentation of participation) reflects a shortage of training opportunities, nor that trainees would benefit from distinct and specific trainings targeting approving officials, PCard holders, and DPCCs. However, SPD is in the process of finalizing online refresher training in partnership with the City’s Learning and Development Center; this is expected to be available during spring 2015 and will make refresher training more convenient for City staff (it is also to replace refresher training conducted by some individual departments without direct participation from SPD). Additionally, we will evaluate training and refresher training materials and offerings. This work will focus on making certain that training addresses unique responsibilities of the various roles in the PCard process, with an emphasis on how those roles relate to one another. To reinforce initial and refresher training, we plan to develop a PCard user’s guide or handbook that will outline key responsibilities for all key participants in the PCard process. We also note that, while group training for all participants remains the preferred method, SPD has also held meeting solely for DPCCs as indicated above. Where these are appropriate and necessary, SPD will continue this practice, which helps to address the recommendation for separate training for different roles in the PCard process.”

RESPONSIBLE PARTY:

Responsible parties for this item include SPD’s Deputy Director and PCard team.

ESTIMATED DATE OF COMPLETION:

JULY 1, 2015

**ASSESSMENT OF
RESPONSE:**

The Audit Division agrees with SPD management's commitment to developing enhancements in training delivery. The response adequately addresses the issue and proposes to remediate. Management's proposed enhancements will improve their ability to comply with the training requirements of E.O. 1-42.

**FINDING #7 – LACK OF DOCUMENTATION OF RECEIPT OF GOODS OR SERVICES PURCHASED ON P CARDS
RISK RATING (IMPACT AND MAGNITUDE) = HIGH**

BACKGROUND:

SPD management expressed concerns regarding the ultimate destination of items procured using PCards.

Administrative Procedure 5-2 – Procurement Procedures, 5.A. (1) n and 5.A. (1) p address: 1) the PCard User Department requirements of both documenting the receipt of purchased goods and services, and 2) segregation of duties of personnel performing purchasing, receiving and payment functions. Section 5.A. (1) c of Executive Order 1-42 Purchasing Card Policy and Procedures (E.O. 1-42) outlines the proper use of PCards, but does not address evidence of receipt procedures. Section 5.1.1 of E.O. 1-42 states that *“The Strategic Purchasing Division (SPD) should develop procedures and administer a procurement plan for the use of PCards that complies with the City Charter, and City Ordinances, and the laws of the State of Texas.”*

Under Government Code Title 10, Subtitle D, Chapter 2155, Subchapter A, Section 2155.322 INSPECTION AND CERTIFICATION, (a) A state agency shall:

“(1) inspect and evaluate at the time of receipt all goods or services that the agency receives to determine whether the goods or services comply with the contract under which they were purchased”.

FINDING:

None of the PCard documentation obtained during transaction testing shows evidence of actual receipt of the goods and services purchased.

RECOMMENDATION:

We recommend SPD develop procedures to specifically address the responsibility of management to document evidence of the delivery of goods and services purchased using PCards.

STRATEGIC PROCUREMENT DIVISION MANAGEMENT

RESPONSE:

“We concur with the recommendation, though the finding’s background citations are not directly applicable (AP 5-2 exempts PCards, while the state law referenced applies to state agencies rather than municipalities). While no governing document or law has been produced that requires documentation of receipt of goods or services acquired with PCards, we agree that the autonomy granted to a PCard user carries with it a responsibility to safeguard resources acquired with public funds. Because of this, the PCard program’s goals of expediting small purchases and reducing paperwork must be balanced with accountability and controls. Toward this end, SPD will work with DPCCs to initiate spot audits seeking evidence of receipt of goods and services and will consider requiring a second signature on PCard receipts to establish separation of duties between receiver and payer. SPD will also look to best practices from other cities and PCard programs, with a particular focus on goods easily misappropriated for other purposes than City business (e.g., hand tools, small technology items). Failure to provide evidence of receipt of goods or services may result in penalty up to and including PCard

suspension or cancellation. While the work above is in progress, this area will also be a focus for Finance's ERM initiative mentioned earlier in this memo."⁸

RESPONSIBLE PARTY:

Responsible parties for this item include SPD's Deputy Director and PCard team.

ESTIMATED DATE OF COMPLETION:

JULY 1, 2015

ASSESSMENT OF

RESPONSE:

The Audit Division agrees with SPD's commitment to work with Department PCard coordinators to develop documentation to support actual receipt of goods and services. The commitment contained in the response adequately addresses the issue and proposes to remediate.

⁸ See Exhibit 1 for the complete FIN Management Response memo.

FINDING #8 – NO POLICY ON GIFT CARD PURCHASES WITH P CARDS
RISK RATING (IMPACT AND MAGNITUDE) = HIGH

BACKGROUND:

Prepaid cards (gift cards) are becoming popular among consumers, gift givers, employers, and charities. They allow the individual to purchase goods and/or services of a specified value wherever the card is accepted. The cards may require the payment of upfront fees but do not have an individual's name embossed on the front. This allows holders of these cards to use them like cash. Because of this cash-like quality, many agencies restrict the purchase of these cards through the PCard system. When gift card purchases are allowed, best practices would include stringent tracking requirements by the Department Purchasing Unit (as defined in Administrative Procedure 5-2, Procurement Procedures, Section 4.L.) of gift card request forms along with distribution and reconciliation logs.

Gift cards can now be purchased at almost any retail outlet including office supply stores, home improvement stores, restaurants, grocery, and convenience stores. Many of these retailers do not provide detailed information on purchased items to the PCard bank, which limits the ability of the Strategic Procurement Division (SPD) to identify or track these purchases within the Citibank on-line reporting system.

FINDING:

We noted gift cards were purchased on at least 4 separate dates using PCards. SPD does not have any policies and/or procedures on the purchase, distribution, or tracking requirements of gift cards.

RECOMMENDATION:

We recommend that SPD develop policies and procedures regarding the purchase of gift cards using PCards. The policies and procedures should also include the distribution, and tracking of gift cards. Consideration should also be given to restricting gift card purchases to purchase order system purchases only.

STRATEGIC PROCUREMENT DIVISION MANAGEMENT

RESPONSE:

"We concur with the audit's recommendation regarding the use of PCards to purchase gift cards. As part of the update to EO 1-42 referenced earlier, SPD will institute a policy prohibiting the use of PCards to purchase gift cards."

RESPONSIBLE PARTY:

Responsible parties for this item include SPD's Deputy Director and PCard team.

ESTIMATED DATE OF COMPLETION:

JULY 1, 2015

ASSESSMENT OF

RESPONSE:

The commitment contained in the response adequately addresses the issue and proposes to remediate.

**FINDING #9 – NO CLEAR DEFINITION OF TECHNOLOGY ITEMS NEEDING CHIEF TECHNOLOGY OFFICER APPROVAL
RISK RATING (IMPACT AND MAGNITUDE) =MEDIUM**

BACKGROUND:

Technology is an integral part of the City’s current working environment. Information Technology (IT) related products encompass a broad range of items that are used by personnel in office settings, first responders, inspectors, and a variety of other City operations. IT related items include:

- Hardware – Examples are Desktops, laptops, monitors, printers, routers and handheld devices;
- Software – Customized development or a standard product such as Microsoft Office; and
- Accessories - Examples include adapters, radios, chargers, etc.

In interviews with the audit team, IT management stated, “*Key IT components must be approved by Department’s Chief Technology Officers (CTO) in order to assure that these purchased items are compatibility with current system hardware/software requirements*”.

Establishing contracts with key IT vendors is an important part of the procurement process and equally important is clearly defining those items that require CTO approval prior to purchase.

Executive Order 1-42 Purchasing Card Policy and Procedure (E.O. 1-42) Section 8.0 (shown below) addresses the approval process for IT related purchases on PCard by simply listing these purchases as “*Technology*”.

8.0 PURCHASES PROHIBITED WITH THE PURCHASING CARD

- Cash advances
- Restocking Inventory
- Personal expenditures
- Furniture (consult with Building Services Committee)
- Food/Travel (with prior written approval by Mayors Office)
- ***Technology (with prior written approval by Departmental Chief Technology Officer)***
- Sales Tax except in cases of rental equipment where State law does not exempt local government

FINDING:

Departments are unclear regarding which IT related items require CTO approval. This lack of clarity led to the following:

- CTO approval was not requested prior to the purchase of most IT related items; and
 - Some card holders requested approval for items such as phone cases or printer ink replacement cartridges.
-

RECOMMENDATION:

We recommend SPD establish and publish an itemized list of specific IT related items that require prior CTO approval utilizing specialized forms to be kept in a goods/services purchase packet for review.

STRATEGIC PROCUREMENT DIVISION MANAGEMENT

RESPONSE:

“We concur with the recommendation’s emphasis on ensuring that PCard user departments understand and comply with requirements for technology purchases as laid out in EO 1-42, although we do not agree that a specialized form is required for approval of technology items. Additionally, we recommend a risk rating of low. SPD has worked with department to eliminate technology merchants from many PCardholders purchasing capability during FY15, but recognizes that this will not prevent a PCard user from purchasing technology at a different merchant (i.e., purchasing a tablet from a vendor classified as an office supply merchant). To further strengthen controls in this area, SPD has secured a list of IT-related items and services from HITS, and will share the list with DPCCs for dissemination/distribution to all PCard holders and departmental CTOs (we also expect to include it in the user’s guide mentioned in the response to Finding #6). Written approval by the proper CTO or HITS team member will be required as backing documentation for any applicable technology purchase, and SPD will perform spot checks to ensure this is done. This issue will also be highlighted in updates to training materials and offerings.”

RESPONSIBLE PARTY:

Responsible parties for this item include SPD’s Deputy Director and PCard team.

ESTIMATED DATE OF COMPLETION:

JULY 1, 2015

ASSESSMENT OF

RESPONSE:

The actions SPD management has taken to-date to help clarify approval requirements related to purchases of IT products and services as well as the expressed commitment to raise awareness through training opportunities are adequate to address this issue. The commitments contained in the response adequately address the issue and propose to remediate.

EXHIBIT 1



CITY OF HOUSTON

Finance Department

Interoffice

Correspondence

To: Courtney Smith, City Auditor **From:** Kelly Dowe, Chief Business Officer & Finance Director
cc: City Controller Ronald C. Green **Date:** February 18, 2015
Subject: Response to Purchasing Card Procurement Audit

John Kelly Dowe

The Finance Department and Strategic Procurement Division (SPD) thank the City Controller and City Auditor for their audit of FY2013 Purchasing Card (PCard) Procurement activity, as administered by SPD (then the Strategic Purchasing Division) when the division was located in the Administration and Regulatory Affairs Department. The audit was conducted professionally and represents a helpful guide for continuous improvement in managing the City of Houston's PCard program.

We generally concur with the audit's recommendations and have included responses for each; however, we wish to begin with overriding observations that may provide additional context:

- Finance has launched an Enterprise Risk Management initiative designed to identify areas of risk (i.e., where the City's internal processes lack controls or proper administration), recommend improvements and support City implementation of same. We have already taken steps to move forward with a comprehensive review of the PCard program as it stands in FY2015, and expect this to augment the City Auditor's work. Paired with internal reviews by Finance staff to identify opportunities for improvement in management and oversight of the PCard program, we expect this analysis of the PCard program to be an important step in ensuring that the PCard program properly balances a need for speed and efficiency in public procurement with the requisite concern for safeguarding public resources and protecting against waste, fraud and abuse.
- While in general agreement with the audit's findings, Finance/SPD note our objection to citations of Administrative Procedure 5-2 (AP 5-2) throughout the audit. AP 5-2, which governs Procurement Procedures, clearly excepts PCard purchases from its scope and states that such purchases are covered under Executive Order 1-42 (EO 1-42, Purchasing Card policies and procedures). Although EO 1-42 does at one point reference AP 5-2, we recognize this inconsistency as one of several potential improvements to EO 1-42; our intent is to update and strengthen EO 1-42 so that it serves as a more comprehensive and robust guide for PCard usage. SPD is developing a new Procurement Code for Council consideration, and expects to revise procurement policies in an associated effort. A key aspect of this will be review and enhancement of EO 1-42, which may be converted to an AP in the process.

- As indicated by the responsibilities assigned in EO 1-42, Finance and SPD rely heavily on PCard user departments to understand and honor relevant policies and laws regarding public procurement. As PCard usage is not visible to SPD until after the fact, it is possible for user departments (specifically, individual PCardholders) to work outside the letter and spirit of policy and law. We are committed to building stronger partnerships with user departments and PCardholders to ensure that adequate and proper controls are instituted not just across the City, but within departments. This will include a review of all training materials and offerings to ensure that departments and PCardholders are well aware of their responsibilities and obligations in using PCards as a purchasing tool.
- In conjunction with the Enterprise Risk Management initiative addressed above, Finance's Performance Improvement group will be asked to provide resources to assist SPD staff with development of processes and policies to aid in implementation of the improvements referenced in several of the responses below.

Responses to the audit's recommendations follow:

Finding 1:

We concur with the recommendation to increase focus on potential splitting and have instituted this change. With regard to the purchases cited as splits, we agree with four of the five and wish to point out that:

- Three involved purchases pre-approved by user department management; and
- One was identified by the Department Purchasing Card Coordinator (DPCC), resulting in a written caution to the PCard user against splitting.

We also note that the citation of Local Government Code Chapter 252 may not be applicable in certain instances because state law provides for numerous exemptions to the referenced section.

SPD attempted to institute an additional control on splitting by disabling a function in the Citibank GCMS system in March 2014, and advising DPCCs of same by e-mail and in at least one meeting of DPCCs; however, disabling the function did not hamper users' ability to split transactions. SPD has now developed a report to enable monthly review of transactions for signs of splitting. Review of this report is to be accompanied by more proactive outreach to departments to alert them of potential splitting. SPD also includes discussion of splitting in its new online training (expected to be available in spring 2015), including a specific question on the post-training quiz; we will also ensure that training includes explanation of the opportunity to request a temporary credit limit increase through SPD when circumstances warrant same). Increased departmental outreach and training (including, as appropriate, discussions with department management where splitting shows signs of occurring) are to be accompanied by consistent and stringent enforcement of EO 1-42 and other relevant policies and laws, with penalties to include PCard suspension or termination for repeat offenders. SPD will continue to explore other potential system controls restricting PCard users' ability to circumnavigate proper procedure, policy and law by splitting transactions above single-transaction limits into one or more smaller transactions.

Regarding the recommendation's second component, requiring informal bid documentation on purchases over \$3,000, this information will be shared with PCardholders whose single-transaction limits exceed \$3,000; so long as other PCardholders comply with the single-transaction limit, informal bidding is not a concern.

Responsible parties for this item include SPD's PCard team, led by the SPD Deputy Director.

Estimated date of completion is June 1, 2015.

Finding 2:

We concur with the importance of fiscal responsibility and legal compliance in contract management, a responsibility shared by SPD and PCard user departments. As EO 1-42 already requires PCard users to notify their DPCC when using a PCard for a contract purchase, this represents a potential starting point for monitoring PCard purchases' impact on total spending toward contract amounts and avoiding inadvertent overspending of contract limits. This was addressed with DPCCs in meetings in May and December 2014. For contracts residing within a single department, SPD will increase efforts to directly communicate to DPCCs and departmental management their responsibility for monitoring and managing contract spending to ensure that it remains within approved parameters. For City contracts utilized by multiple departments, SPD will develop an upgraded reporting and monitoring system that draws from PCard usage data and more traditional methods (purchase orders) to track overall City spending against contracts and ensure compliance with approved spending amounts. While this may require some time to develop and implement, SPD will move quickly to improve performance on contract management through communication and coordination with DPCCs and user departments' management. Penalties for non-compliance may include suspension or termination of PCard privileges.

Responsible parties for this item include SPD's Deputy Director, the PCard team, and the Enterprise Resource Planning (ERP) team.

Estimated date of completion is December 1, 2015.

Finding 3:

We concur with the recommendation; SPD has already initiated discussions with the ERP team and Citibank to achieve accurate downloading of PCard transactions, including credits. The goal of these discussions is to obtain from Citibank a data file that will capture all secure credits and instances where a single invoice includes both contract and non-contract purchases. SPD will also increase communication and coordination with DPCCs to ensure that journal entries rejected during the SAP upload are resolved and re-uploaded timely and accurately.

Responsible parties for this item include SPD's Deputy Director, the PCard team, and the ERP team.

Estimated date of completion is December 1, 2015.

Finding 4:

We concur with the recommendation, noting that the instances cited by the audit represent a very small portion of the City's non-contract vendors (as the audit suggests, the exact number is difficult to determine, but if it is 5,000, the instances cited would represent about 0.3 percent of all non-contract vendors). In addition, we note that the section of state law cited includes a list of exemptions against which the instances cited by the audit have not been vetted, so some of the expenditures are likely within the requirements of state law. SPD already reviews non-contract vendor spending via PCard every six months; this will be conducted on a quarterly basis going forward. Further, SPD will initiate enhanced monitoring of City spending with non-contract vendors, including working with the ERP team to develop a system that will combine spending via PCard and purchase orders to identify vendors where total City spend is approaching \$50,000 (this may be linked to the work done regarding Finding 2's recommendation for tracking spending against contracts). SPD will also work with DPCCs to more closely track spending with non-contract vendors, and will re-evaluate training and education offerings to ensure that relevant policies and laws are transparent and clear to all PCard users. Where additional credit limits are granted, SPD will ensure that user department management and staff are aware of relevant rules and restrictions, and will also increase its oversight of purchases made with enhanced credit limits.

Responsible parties for this item include SPD's Deputy Director, the PCard team, and the ERP team.

Estimated date of completion is December 1, 2015.

Finding 5:

We concur with the recommendation, though we believe a risk rating of low is more appropriate. SPD will reinforce the requirements of EO 1-42 Section 14.0 in written and verbal communication with DPCCs and other departmental management. This communication will include a reference to EO 1-42's potential penalties of suspension or termination of PCards for users that cause late submittal. Timeliness has also been emphasized with training of DPCCs by Citibank in January 2015, and with an accompanying requirement that DPCCs generate their own departments' statements without waiting for SPD to generate and provide the statements; this shortens the process and increases the likelihood of timely submittal. SPD will also develop a mechanism by which to report non-compliance to user department management, and will review the reconciliation submittal process for other opportunities to improve timely submittal of reconciliation statements.

Responsible parties for this item include SPD's Deputy Director and PCard staff.

Estimated date of completion is July 1, 2015.

Finding 6:

We concur with the recommendation to develop a tracking log for refresher training. Additionally, we recommend a risk rating of medium. While EO 1-42 is cited correctly, the

background above correctly notes that completion of the referenced forms is – per the EO – the responsibility of DPCCs. To support DPCCs in this responsibility, a tracking log was developed in mid-2014. Finance/SPD appreciate the guidance offered by the City Auditor's office in this regard; the log will be used to monitor when PCard refresher training is required for individuals involved with PCard usage and approval, and reminders will be issued ahead of the deadline for refresher training. In addition, SPD will perform spot-checks in user departments to ensure that DPCCs are maintaining required documentation of training and refresher training as specified in EO 1-42. Where the provisions of EO 1-42 are not complied with in a timely manner, PCards may be suspended or cancelled.

We do not necessarily agree PCard users' failure to participate in required refresher training (or a lack of documentation of participation) reflects a shortage of training opportunities, nor that trainees would benefit from distinct and specific trainings targeting approving officials, PCardholders, and DPCCs. However, SPD is in the process of finalizing online refresher training in partnership with the City's Learning and Development Center; this is expected to be available beginning in spring 2015 and will make refresher training more convenient for City staff (it is also to replace refresher training conducted by some individual departments without direct participation from SPD). Additionally, we will evaluate training and refresher training materials and offerings. This work will focus on making certain that training addresses unique responsibilities of the various roles in the PCard process, with an emphasis on how those roles relate to one another. To reinforce initial and refresher training, we plan to develop a PCard user's guide or handbook that will outline key responsibilities for all key participants in the PCard process. We also note that, while group training for all participants remains the preferred method, SPD has also held meetings solely for DPCCs as indicated above. Where these are appropriate and necessary, SPD will continue this practice, which helps to address the recommendation for separate training for different roles in the PCard process.

Responsible parties for this item include SPD's Deputy Director and PCard team.

Estimated date of completion is July 1, 2015.

Finding 7:

We concur with the recommendation, though the finding's background citations are not directly applicable (AP 5-2 exempts PCards, and the state law referenced applies to state agencies rather than municipalities). While no governing document or law has been produced that requires documentation of receipt of goods or services acquired with PCards, we agree that the autonomy granted to a PCard user carries with it a responsibility to safeguard resources acquired with public funds. Because of this, the PCard program's goals of expediting small purchases and reducing paperwork must be balanced with accountability and controls. Toward this end, SPD will work with DPCCs to initiate spot audits seeking evidence of receipt of goods and services and will consider requiring a second signature on PCard receipts to establish separation of duties between receiver and payer. SPD will also look to best practices from other cities and PCard programs, with a particular focus on goods easily misappropriated for other purposes than City business (e.g., hand tools, small technology items). Failure to provide evidence of receipt of goods or services may result in penalty up to and including PCard

suspension or cancellation. While the work above is in progress, this area will also be a focus for Finance's ERM initiative mentioned earlier in this memo.

Responsible parties for this item include SPD's Deputy Director and PCard team.

Estimated date of completion is July 1, 2015.

Finding 8:

We concur with the audit's recommendation regarding the use of PCards to purchase gift cards. As part of the update to EO 1-42 referenced earlier, SPD will institute a policy prohibiting the use of PCards to purchase gift cards.

Responsible parties for this item include SPD's Deputy Director and PCard team.

Estimated date of completion is July 1, 2015.

Finding 9:

We concur with the recommendation's emphasis on ensuring that PCard user departments understand and comply with requirements for technology purchases as laid out in EO 1-42, although we do not agree that a specialized form is required for approval of technology items. Additionally, we recommend a risk rating of low. SPD has worked with departments to eliminate technology merchants from many PCardholders purchasing capability during FY15, but recognizes that this will not prevent a PCard user from purchasing technology at a different merchant (i.e., purchasing a tablet from a vendor classified as an office supply merchant). To further strengthen controls in this area, SPD has secured a list of IT-related items and services from HITS, and will share the list with DPCCs for dissemination/distribution to all PCard holders and departmental CTOs (we also expect to include it in the user's guide mentioned in the response to Finding #6). Written approval by the proper CTO or HITS team member will be required as backing documentation for any applicable technology purchase, and SPD will perform spot checks to ensure this is done. This issue will also be highlighted in updates to training materials and offerings.

Responsible parties for this item include SPD's Deputy Director and PCard team.

Estimated date of completion is July 1, 2015.