City of Sacramento
City Council

915 I Street, Sacramento, CA, 95814
www.CityofSacramento.org

Meeting Date: **1/29/2013** **Report Type:** Staff/Discussion

Title: Audit of Citywide Purchase Card Use

Report ID: 2013-00072

Location: Citywide

Recommendation: Pass a motion approving the Auditor's Audit of Citywide Purchase-Card Use.

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Presenter: Jorge Oseguera, City Auditor (916) 808-7270, Mayor/Council

Department: Mayor/Council
Division: Office of the City Auditor
Dept ID: 01001201

Attachments:

1-Description/Analysis

2-Audit of Citywide Purchase Card Use.

City Attorney Review

Approved as to Form
Matthew Ruyak
1/14/2013 5:29:45 PM

Approvals/Acknowledgements

Department Director or Designee: Jorge Oseguera - 1/8/2013 11:47:48 AM

James Sanchez, City Attorney Shirley Concolino, City Clerk Russell Fehr, City Treasurer
John F. Shirey, City Manager

Back to Table of Contents

Description/Analysis

Issue: This audit was incorporated into the 2011-2012 Audit Plan by the City Auditor. According to City Code Chapter 2.18, the City Council should be kept apprised of the City Auditor's work.

Policy Considerations: The City Auditor's presentation of the *Audit of Citywide Purchase-Card Use* is consistent with the Mayor and City Council's intent to have an independent audit function for the City of Sacramento.

Economic Impacts: None

Environmental Considerations: None

Sustainability: None

Commission/Committee Action: On December 11, 2012, the Audit Committee forwarded this report to City Council for approval.

Rationale for Recommendation: The report includes three finding and makes 14 recommendations for improving the City's purchase card controls and processes.

Financial Considerations: The costs of performing this audit were funded out of the Fiscal Year 2012/13 Office of the City Auditor Budget.

Emerging Small Business Development (ESBD): No goods or services are being purchased as a result of this report.

Back to Table of Contents

Report # 2012-06

Audit of Citywide Purchase-Card Use

While transactions reviewed did not reveal extensive personal purchases, some charges violated policy and lacked complete support

The purchase card program lacked complete policy guidance and oversight

The City's credit limit exceeds $2 million per month and the City could reduce risk by limiting the number of cardholders and establishing more comprehensive controls

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Office of the City Auditor
October, 2012

CITY OF SACRAMENTO
CALIFORNIA

Office of the City Auditor
Jorge Oseguera, City Auditor

October 18, 2012

Honorable Mayor and
Members of the City Council
915 I Street - Fifth Floor, New City Hall
Sacramento, CA 95814-2604

Enclosed is the *Audit of Citywide Purchase-Card Use*. We conducted this audit in accordance with generally accepted government auditing standards and City Code Chapter 2.18.

The report contains three findings and makes 14 recommendations for improving the City's procurement card controls and processes. The written response to this report is found on page 20. I will present this audit at the October 23, 2012 *City Council Meeting*.

We would like to thank the Department of General Services, the Department of Finance, and the City Attorney's Office for their time, information, and cooperation during the audit process.

Should you have any questions, please feel free to contact me.

Respectfully submitted,

Jorge Oseguera
City Auditor

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Contents

Introduction 1

Background 1

Scope and Methodology 4

Finding 1: While transactions reviewed did not reveal extensive personal purchases, some charges violated policy and lacked complete support 5

Employees used purchase cards for some unallowable purchases 5

The City could save money by purchasing through Citywide agreements 9

Some purchases were approved without complete documentation 10

Purchase card statements were not always approved by the authorized signers 12

Finding 2: The purchase card program lacked complete policy guidance and oversight 13

Rules are derived from various sources and have not been clearly communicated 13

The number of cardholders who received training is unknown, but appears limited 15

Periodic reviews and targeting risk could help detect and deter unallowable transactions 16

The City would benefit from adopting purchase card best practices 16

Finding 3: The City's credit limit exceeds $2 million per month and the City could reduce risk by limiting the number of cardholders and establishing more comprehensive controls 18

About half of purchase cards received minimal use and it is unclear if keeping these cards is justified 18

Restricting the types of purchases could limit unallowable use 19

Department Response 22

Introduction

We have completed the *Audit of Citywide Purchase-Card Use*. We conducted this performance audit in accordance with Generally Accepted Government Auditing Standards. 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 Office of the City Auditor thanks the Department of General Services, the Department of Finance, and the City Attorney's Office for their time, information, and cooperation during the audit process.

Background

Purchasing Card Policy and Guidance

The City of Sacramento established the Purchasing Card program for City employees with Bank of America. The City created the program, which is administered by the Department of General Services' (DGS) Procurement Services Division, in order to provide a cost-efficient method for purchasing a variety of low dollar amount goods and services. The Purchase Card Program is designed to augment the other methods of purchasing that are available to City organizations, such as requisitions, purchase orders, payment vouchers, and petty cash.

To provide guidance for the use of City purchase cards, the City established API 6- Purchasing Card Program (API 6), which was last revised July 1998. Complimenting API 6 is the City's Purchasing Card Program User's Guide, which was issued in May 2005. New employees who receive a City purchase card are expected to complete the Purchase-Card/Procurement Training prior to the receipt of the card.

According to the Procurement Card Handbook, which is presented during the training, all City employees who have the need to purchase goods and services for the City are encouraged to obtain purchase cards. In order to obtain purchase cards, employees fill out Procurement Card Application forms. Department directors or division managers (approving officials) review the applications and specify credit limits (current average $7,646) and single transaction limits (current average $3,153). Approving officials submit the forms to the Procurement Services Division's Program Administrator, who processes the request with Bank of America. Approving officials assume full responsibility to manage and review account activities, and agree to ensure the cardholders comply with all terms and conditions.

According to API 6, the purchase card can be used for City business purposes only. The individual named on the card is the only one authorized to use the card and when it is not in use, the card should be secured in a safe place.

Purchase Card Process

The bank sends statements to each individual cardholder, listing all transactions that have been charged on the card during the billing period. Individual cardholders are required to maintain documentation of each purchase made, and reconcile their purchases with the bank statement at the end of each billing period. According to the User's Guide, it is "essential" that the cardholder complete the following:

- Compare the back-up documentation to the transactions listed on the current purchasing card statement
- Indicate the total dollar amount for each budget object code
- Sign the purchasing card statement
- Forward the purchase card statement with receipts to the cardholder's supervisor for review and approval

The bank also provides a billing statement to the Procurement Services Division each month detailing all cardholder charges and the bank automatically deducts the total monthly purchases from a City account. When the Procurement Services Division receives the monthly billing statement from the bank, it sends a copy to the Accounting Division. Accounting uses the statement to create journal entries using the purchase card clearing account[1] for all cardholders to reflect the amounts charged on their purchase card statements. Departments are responsible for preparing journals to reclassify their employees' purchase card transactions from the clearing account to appropriate expenditure accounts. According to Accounting, staff review purchase card clearing accounts at the end of the year to ensure there are no remaining balances. If balances exist, Accounting contacts departments to reconcile the outstanding balance.

In Fiscal Year 2011/12, 263 cardholders charged about $1.4 million. The following exhibits show the numbers of cardholders by department (sorted by total spending) and the categories that received the most purchases:

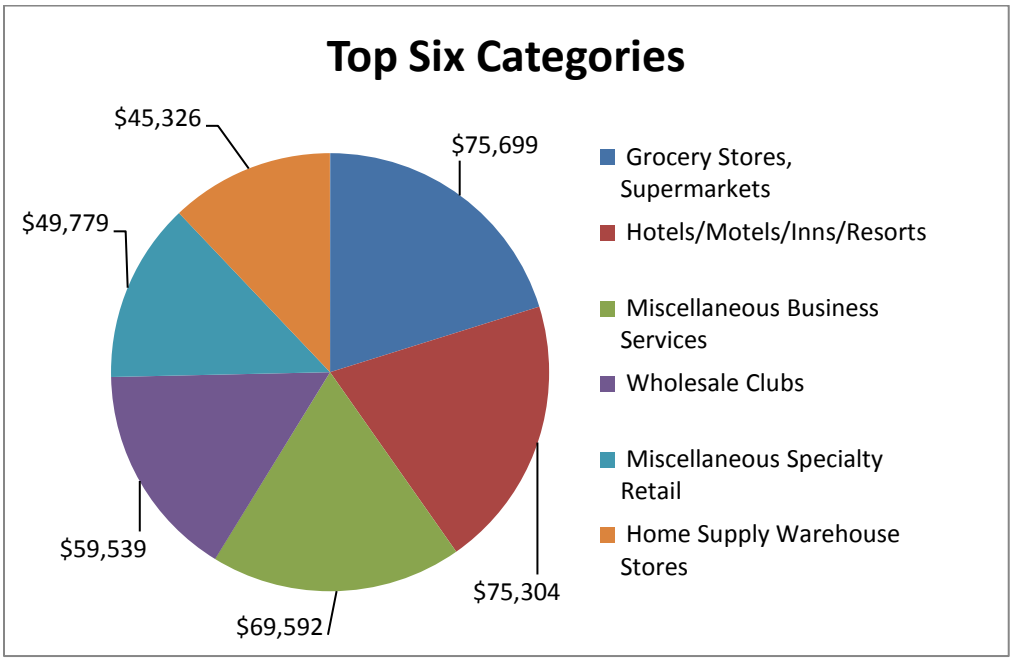
[1] Clearing accounts temporarily hold costs until amounts are reclassified by departments to appropriate expenditure accounts.

Exhibit 1: Employees Charged $1.4 Million On Purchase Cards In Fiscal Year 2011/12

Department	Cardholders With Transactions	Total Spending
Parks & Recreation	57	$391,125.80
Police	34	$243,456.90
General Services	54	$187,206.96
Utilities	17	$122,093.07
Human Resources	24	$102,553.74
Transportation	20	$81,142.49
Fire	11	$59,824.27
Information Technology	8	$43,995.60
Community Development	10	$42,995.10
Economic Development	2	$39,518.33
City Clerk	5	$28,834.23
City Manager	7	$22,579.14
Finance	3	$21,450.48
Convention, Culture and Leisure	8	$12,403.18
City Treasurer	3	$10,856.73
Total	**263**	**$1,410,036.02**

Source: Auditor-generated from Works data

Exhibit 2: Cardholders Charged The Most To Grocery Stores And Hotels



Source: Auditor-generated from Works data

Scope and Methodology

On July 31, 2012, the City Council directed the City Auditor to initiate an Audit of Citywide Purchase Card Use and to structure the audit so it could be completed and made public by the last Council meeting in October. In response, we initiated a limited-scope audit that primarily focused on the City's purchase card transactions that occurred during Fiscal Year 2011/12. However, we were not able to review electronic purchase card data until August 22, 2012 due to an ongoing Police investigation.

Our audit objective was to assess the controls and processes associated with the City's Purchase Card Program to determine if the control system is adequate and if City purchase cards were being used appropriately. The review included all City purchase card transactions except those associated with the Mayor and City Council Offices.[2]

During our audit, we interviewed staff from the Department of General Services' Procurement Services Division and the Finance Department's Accounting Division to gain an understanding of the City's processes. We gathered and reviewed City documents, training materials and contracts. We obtained information from Bank of America's Works[3] application, which tracks all purchase card related activity.

To assess the transactions' business purposes and verify compliance with City policies, we obtained and reviewed the supporting documents for a judgmentally-selected sample of 27 statements. In total, we reviewed 360 transactions. The sample was selected using a risk-based approach. We targeted monthly statements with high dollar amounts, large numbers of transactions, and potentially unallowable charges. Also, the sample was selected to cover a broad range of City departments.

Due to the limited scope and timeframe to complete this audit, we were not able to review and analyze several potential audit areas. For example, we did not benchmark against other comparable cities, review contracts with the purchase card provider, perform a file review at document retention locations, perform testing on Works system controls, review City clearing account processes, or assess the timeliness of City reconciliation processes. We relied on the information obtained from the Bank of America Works system and did not test the reliability of this data.

[2] The City Code generally does not allow the City Auditor to audit the Mayor and City Council and doing so could create a potential conflict of interest because the City Auditor reports directly to the Mayor and the City Council.
[3] This application allows authorized users to review transactions and run reports about City purchase card use.

Finding 1: While transactions reviewed did not reveal extensive personal purchases, some charges violated policy and lacked complete support

The purpose of the City's Purchase Card Program is to establish an efficient, cost-effective method of purchasing and paying for small-dollar transactions. City policies and other documents define the Purchase Card Program and establish the rules and guidance that employees must follow in order to retain the privilege of having and using City purchase cards. While our review of 27 monthly statements with 360 transactions showed that most transactions appeared appropriate, we found some instances in which employees violated City policies and guidelines. Specifically, we found that:

- Employees used purchase cards for some unallowable purchases;
- The City could save money by purchasing through Citywide agreements;
- Some purchases were approved without complete documentation; and
- Purchase card statements were not always approved by the authorized signers.

As employees become aware of control weaknesses, such as unallowable expenses being approved or unauthorized signers being accepted, employees predisposed to misusing the card may be more likely to attempt to process fraudulent, improper, and abusive purchases. Failure to address these control issues could lead to the erosion and weakening of the control system and increase the City's exposure to inappropriate transactions.

Employees used purchase cards for some unallowable purchases

The Purchase Card Program is intended to facilitate timely purchases with a minimum amount of administrative overhead, while retaining necessary accountability. When applying for the card, cardholders and their approving officials confirm that they understand and will comply with rules governing card use. Failure to adhere to the City's restrictions could result in disciplinary action, up to and including termination.

To assess if the control system is adequate and if City purchase cards were being used appropriately, we judgmentally sampled 27 individual statements with 360 transactions. These charges totaled $84,814 of the $1.4 million in total purchases for Fiscal Year 2011/12. While the nature of the sample may not be representative of the population, testing identified vulnerabilities in key controls that warrant attention.

Our review found some purchases for unallowable expenses that totaled more than $2,000. This is not to imply that the purchases always lacked City business purposes. In fact, it appeared that most of these expenses were for City business. However, given the restrictions established by City documents regarding appropriate purchase card use, these purchases should not have been made on City purchase cards.

The following shows the issues identified in the review of the sample:

Exhibit 3: Several Transactions Violated City Policies

Purchase	Amount		Notes
Alcoholic beverages while on City travel	$	13.50	Employee reimbursed City during audit
Room upgrade while on City travel	$	89.60	Department Director indicated charge was work related
Movie purchase while on City travel	$	14.20	Employee paid back City when completing expense reconciliation
Ammunition	$	783.34	Employee unaware of restriction and department specified purchase was work related
Ammunition	$	284.44	Employee unaware of restriction and department specified purchase was work related
Arizona trip for City business	$	593.06	Arizona Boycott prohibits travel to the state at City expense
Split transaction	$	450.00	Cardholder requested split transactions to avoid single-purchase limit. Amount shown is portion over limit.

Source: Auditor-generated from Works data, department information, and accounting records

The purchase of some items shown above is explicitly prohibited by City policy and guidelines. According to the Procurement Services Manager, DGS views API 6 - Purchasing Card Program (API 6), the Purchasing Card Program User's Guide, and the Procurement Card Program Handbook as authoritative documents that users must follow. Other policy documents, like the Travel Policy (API 7), Arizona Boycott, and purchasing policies also impose restrictions on the expenditure of City funds.

The following provides a further explanation about the issues shown above.

Alcohol Purchase

API 6 specifies that purchase cards can be used for City business purposes only. Purchasing alcohol on the City purchase card is prohibited by the Procurement Card Program Handbook. Additionally, the City's Travel Policy states that the City will not reimburse the cost of alcoholic beverages that are purchased while employees are travelling. We found that an employee purchased three alcoholic beverages for $13.50 on the purchase card as part of a dinner charge.

To obtain additional information about this purchase, we contacted the employee's department director. The director spoke with the employee about the purchase and the employee immediately wrote the City a check to reimburse the alcohol charge. There is nothing in City policy that allows personal charges to be made on the City card, even if the charges are eventually repaid. According to the Procurement Services Manager, if employees charge personal expenses on their City cards, it would be up to their respective departments to rectify the charges.

Room Upgrade

API 6 states that purchase cards can be used for City business purposes only. The Travel Policy states that employees shall seek discounted rates, including government, group, conference, or promotional

rates, when booking hotel rooms while travelling on City business. Additionally, the policy states that the City will not reimburse the traveler for hotel-related expenses like room upgrades, health club fees, or mini-bar usage. Our review found one example of a room upgrade charged on the purchase card for $22.40 per night, for a total upgrade cost of $89.60. The employee was traveling for a work-related conference. According to the hotel, the charges shown on the bill was the fee for upgrading to a better room and that the guest agreed to the charge at the front desk.

According to the department director, this charge was made so that the employee could be in a location that was closer to the "travel/work group in a very large hotel and for work reasons, she needed to be closer to them." The director approved the charge when it was submitted. While such an exception could represent a business need, it is not in line with policy.

Movie Purchase

API 6 specifies that purchase cards can be used for City business purposes only. Additionally, the Travel Policy states that hotel-related movie rentals are non-reimbursable expenses. We found one instance in which an employee charged a $14.20 hotel room movie while on business-related travel. To further evaluate this purchase, we reviewed the employee's travel reimbursement form, which was completed shortly after the trip. The employee claimed reimbursement for travel expenses that were not charged on his City card and subtracted out the $14.20 movie from the amount owed to him (marking that amount on the form as a "personal" expense).

While the employee, in effect, paid back the movie charge shortly after returning to Sacramento, there is nothing in City policy that allows unallowable charges to be made on the City card even if the charges are temporary. There is a risk associated with allowing employees to make unallowable charges even if the intent is to repay the charges since it creates an opportunity for possible abuse.

Ammunition

While there can be a City business need to purchase ammunition, doing so on the purchase card is prohibited by the Procurement Card Program Handbook. Our sample found two instances in which employees[4] in two different departments purchased ammunition. The two ammunition charges totaled $1,067.78. According to both departments, the cardholders were not aware that purchasing ammunition was a prohibited purchase since the prohibition was not specified in the Purchase Card Policy or the User's Guide.

Arizona Boycott

In June 2010, City Council adopted Resolution No. 2010-346, known as the Arizona Boycott, in response to the April, 2010 passage of the State of Arizona's immigration laws. The Boycott prohibits Sacramento City employees from traveling to Arizona at City expense and restricts purchases from Arizona-headquartered businesses.

We found that a City employee travelled to Phoenix, Arizona for a work-related conference. While there, the employee charged $593.06 on his purchase card. The bulk of these charges, about $500, covered three nights at a hotel. Other charges were for meals and taxi service. While the transactions generally

[4] Purchases were made by Police and Animal Control staff.

appeared to be in line with what would be charged as part of a trip to a conference, travelling to this location using City funds was banned.

According to the employee's department director, the City did not have to pay for the conference as the employee had a free pass to attend. Additionally, the director said that attending the conference had allowed the employee to meet with vendors, which will save the City $200,000. Although there may be a potential benefit, the department did not seek an exception to the policy and instead allowed this travel despite the Arizona Boycott.

As mentioned above, the Boycott also restricts purchases from Arizona-headquartered companies. Some exceptions and thresholds apply. We analyzed all transactions for the fiscal year to understand how many charges were made to vendors with Arizona addresses. According to transaction records, it appears that $17,535.47 was charged to Arizona vendors. However, we did not review if these purchases were under the specified threshold, made under exception to the Boycott, or confirm if the companies were headquartered in Arizona.

Split Transactions

The City's purchase cards are set to have a single-transaction limit. According to API 6, the limit is usually $3,000. However, it can be changed at the discretion of the departments. Having such a limit sets a maximum single transaction amount, which ensures card purchases are not used to circumvent the City's competitive bidding process. For certain City purchases, a competitive process must be used for purchases that are greater than $5,000. Additionally, setting a transaction limit reduces the City's overall risk and ensures the cards are used for small transactions.

API 6, the Purchasing Card Program User's Guide, and the Purchase Card Handbook all prohibit attempts to make purchases greater than the single transaction limit or request vendors to split transactions to avoid the limit. We found one instance in which a vendor was requested to split a purchase card transaction in order to circumvent the single transaction limit.

In this case, the employee had a $2,000 single transaction limit and requested that the vendor split a $2,450 purchase into two transactions after the purchase was initially declined. The charge was for a City business related training course. The employee asked the training company to split the transactions in two payments to avoid the $2,000 transaction limit. The company complied and charged the full amount in two payments on two different days. The e-mail communication between the employee and the business was included as part of the purchase card receipt packet.

We have provided the City Manager's Office with a summary of all the unallowable purchases identified in this finding.

RECOMMENDATIONS:

We recommend that DGS:

1. **Work with the City Manager's Office to review unallowable transactions identified through this audit and take appropriate action.**

The City could save money by purchasing through Citywide agreements

Our review found that purchase cards were often used to buy cleaning and hardware supplies. While the reviews of such purchases showed that they were for City business purposes, buying these items with purchase cards is out of line with the intent of the City's Procurement of Supplies Policy and could be more costly than alternatives. The Procurement of Supplies Policy: AP-4001 states that, when possible, "departments shall use City-wide contracts."

The Procurement Services Division has almost 30 Citywide contracts[5] or cooperative agreements[6] in place and purchase cards are not meant to be used to circumvent these agreements, according to the Procurement Services Manager. He explained that the City sets up these Citywide agreements or participates in cooperative purchasing agreements in order to receive competitive prices based on the high volume of purchases. Some examples include agreements for:

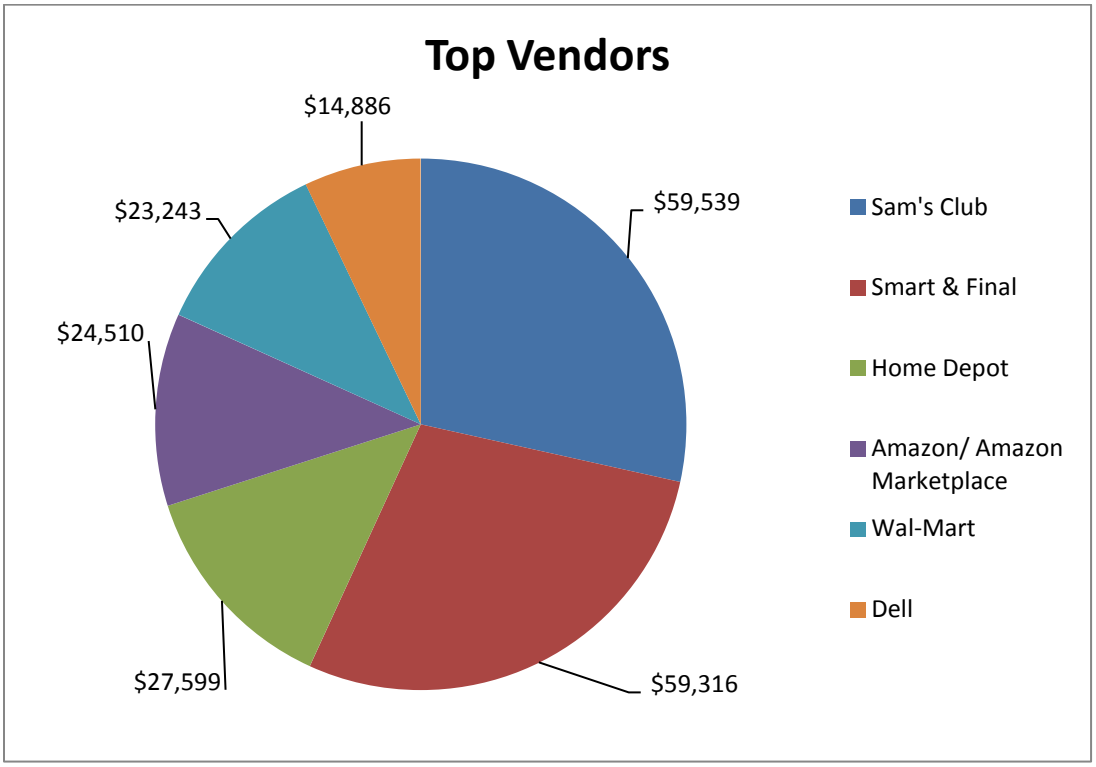
- Records storage
- Printing services
- Janitorial supplies
- Hardware supplies
- Electrical and industrial supplies
- Copy machines
- Office supplies
- Package delivery

We found several instances in which purchases likely could have been made through a Citywide contract instead of with purchase cards. For example, employees purchased cleaning supplies from Wal-Mart. The Procurement Services Manager said that ordering such purchases through the Citywide janitorial supplies contract would likely save departments money. He said that purchases for janitorial supplies can be made easily online and that supplies are usually delivered the next day.

The following shows the six vendors with the most purchase card purchases in Fiscal Year 2011/12:

[5] These are purchase agreements between the City and vendors.
[6] These purchase agreements, which the City can buy through, are between vendors and an outside organization.

Exhibit 4: Top Vendors Included Sam's Club And Smart & Final



Source: Auditor-generated from Works data

Based on the broad range of Citywide contracts and cooperative agreements, and the top purchase card vendors shown, it is likely that many items bought with cards could have been purchased – possibly at discount prices – through agreements. As shown above, the vendor with the third-most City purchase card purchases was Home Depot. The City has a Citywide contract in place with that company for maintenance and hardware supplies.

RECOMMENDATIONS:

We recommend that DGS:

2. **Provide departments and cardholders more information about the benefits of purchasing through Citywide and cooperative agreements**

Some purchases were approved without complete documentation

According to the Purchasing Card Program User's Guide, employees are responsible for keeping receipts, logging transactions, and reviewing their card statements for accuracy. They are required to sign the purchase card statements to indicate review and to submit the statements along with supporting receipts to their supervisors for review and approval. The guide states the following about this reconciliation:

> "This process is MANDATORY and is The Program's principal control. Failure to comply with these procedures could result in cancellation of your Purchasing Card privileges."

Additionally, the Procurement Card Program Handbook stresses the importance of the review process. It states that "prohibited use of the purchase card will result in loss of purchase-card privileges for the cardholder and the approving official." Also, the current Procurement Card Application form states that the approving official assumes "full responsibility to manage and review activity of this account, and agree[s] to ensure the Cardholder complies with all Terms and Conditions."

We found instances in which card purchases were approved even though they lacked required receipts or sufficient detail to understand the nature of the transactions. The following figure provides details of these transactions:

Exhibit 5: Some Purchase Statements Were Approved Despite Inadequate Support

Stated Reason for Purchase	Amount	Issue
Conference hotel rooms for four travelers (charged as four transactions)	$1,464.96	Lack of itemized receipts used for approval made the number of nights and other charges unclear. Support was provided during the audit.
Various supplies for a program that serves children	$728.74	Six transactions on this monthly statement had lost receipts. The cardholder completed six "Lost Receipt Justification" forms that specified reasons for purchases totaling this amount. The department provided three of these receipts during the audit.
Sam's Club purchase for supplies for a program that serves children	$104.19	Purchase noted on log, but no receipt was provided. The department provided this receipt during the audit
iPad upgrade	$21.43	Purchase Information was written on statement, but no receipt was provided.

Source: Auditor-generated from Works data, department information, and accounting records

As shown above, there were two transactions that were approved even though receipts were missing. These included a $104.19 charge to Sam's Club and a $21.43 purchase to Fry's Electronics. The cardholder's log noted a City-business purpose for the Sam's purchase, but the receipt was not included in the support packet. However, the department was able to provide a copy of the receipt during the audit. The statement with the Fry's purchase included a note that the purchase was for an upgrade to an item that was also purchased on the card for a City purpose. However, the lack of receipt meant that the transaction could not be verified.

While it is reasonable to expect that cardholders will occasionally lose receipts, cardholders usually submit lost receipt justification forms or memos to document the City purpose of the purchases. In the above cases, no such justification forms or memos were included as part of the reconciliation process. While lost receipt justification forms could provide some assurance that charges were made for City purchases, departments should ensure that they are used sparingly.

We found that one cardholder had submitted six lost receipt justification forms on one monthly statement for a total of $728.74 in charges. This meant about 12 percent of the statement's 51 purchases were explained by lost receipt justification forms. While the forms included the stated purposes of the purchases, there was no way for the approver to verify their accuracy. During the audit, the department was able to provide three receipts that supported about $440 of the charges.

Besides lost receipts, we found instances in which expenses were approved even though purchases lacked itemized receipts. For example, receipts for hotel charges did not specify the name or location of the hotel, or breakdown any specific hotel charges. The department was able to provide detailed support of these expenses during the audit.

RECOMMENDATIONS:

We recommend that DGS:

3. **Establish a consistent form and guidance to departments for processing lost receipt justifications.**

Purchase card statements were not always approved by the authorized signers

In addition to the reconciliation process at the department level, there is also a review from the Accounting Division. While the bank automatically deducts the amount of all City charges from one City account, departments are responsible for preparing journals to reclassify their employees' purchase card transactions to appropriate City expenditure accounts. As part of processing these journals, Accounting is tasked with reviewing sign-off documents to ensure purchase card statements were approved by the appropriate departmental staff. Each year, departments provide the Accounting Division with authorized signature forms that specify who is allowed to sign off on City purchase card statements.

Our review of the 27 statements found that while all the statements were signed by department staff, six were processed even though they were signed by people who were not authorized to approve them. Authorized signature sheets serve as a control. To be an effective control, Accounting should carefully review statements to ensure they are only approved by authorized signers.

RECOMMENDATIONS:

We recommend that Finance:

4. **Provide training to ensure Accounting staff only process purchase card statements with authorized signatures.**

Effective internal controls like a review and signoff process allow management to provide assurance that unallowable purchases are being prevented or, if occurring, are being promptly detected and followed by appropriate corrective actions. As this finding illustrates, some key controls could be improved to further ensure compliance with the City's purchase card program and prevent and deter purchase card abuse.

Finding 2: The purchase card program lacked complete policy guidance and oversight

Various City documents set rules related to purchase card use. API 6 specifies cardholder responsibilities. It says "Each individual to whom a card is issued is responsible for safeguarding that card. All cards will be issued in an individual's name, and are to be used for ***City business purposes only.*** The individual on the card is the only one authorized to use the Purchasing Card, and when not in use the card should be secured in a safe place." Various other documents and policies restrict purchase card use, but there is no one source that was communicated to all cardholders and clearly addresses all requirements. We found that:

- Rules are derived from various sources and have not been clearly communicated;
- The number of cardholders who received training is unknown, but appears limited;
- Periodic reviews and targeting risk could help detect and deter unallowable transactions; and
- The City would benefit from adopting purchase card best practices.

As a result, employees and approving officials may not fully understand all purchase card requirements. Opportunities exist for DGS to better communicate appropriate purchase card use and to increase program oversight.

Rules are derived from various sources and have not been clearly communicated

API 6 stresses that the cards are for "City business purposes only" and that cardholders should secure the cards and be the only ones who use them. The policy, which became effective in 1998, provides these fundamental rules. However, it does not specify what purchases would constitute appropriate and inappropriate use. Instead, other City documents offer additional guidance and restrictions. The following shows some of the rules related to purchase card use and specifies the source of the restrictions:

Exhibit 6: Various Documents Must Be Reviewed to Understand What Purchase Card Charges Are Prohibited:

Document	Examples of Prohibited Purchases[7]
API 6	Non-City business purchases and purchases made by a non-cardholder
Arizona Boycott	Travel to Arizona and some purchases from Arizona-headquartered businesses
Handbook	Food for non-City business, drugs, alcohol, ammunition, public utility bills, insurance, and payment of traffic violations
Travel Policy	Hotel-related purchases like room upgrades, movie rentals and mini-bar use; auto-related like rental car upgrades and parking tickets; and alcohol
User's Guide	Capital equipment, items for personal use, and items exceeding the authorized limit

Source: Auditor-generated from City policies and Procurement Services Division documents

As shown in the above exhibit, various sources must be reviewed in order for cardholders to understand what types of purchases are prohibited. There is no one source that includes all current purchase card rules and we found these various documents set restrictions for at least 30 types of purchases. Additionally, based on when they received their cards, different cardholders may not be aware of all requirements. For example, the Purchasing Card Request form that was in use from August 2004 until December 2009 said that an employee's signature "acknowledges receipt of the City of Sacramento Purchasing Card User's Guide. The employee's signature certifies that the employee understands the guidelines for use of the Purchasing Card, and that failure to follow the guidelines can result in disciplinary action, up to and including termination." As shown in the examples above, the User's Guide provides general guidance, but it does not include the specifics shown in the Handbook – like bans on ammunition, insurance, or utility bills.

The card request form was changed in December 2009. Signing that form indicates the employee agrees to attend purchase card training prior to receiving the card and "certify that you have received, read, understand, and will abide by all provisions of City of Sacramento purchasing requirements for commodities and services as outlined in Purchasing Card Handbook. . ." According to the Procurement Services Manager, DGS began offering purchase card training around the time that this form was updated. The Handbook, which is referred to in the form and mentioned in the previous exhibit, is presented during training. However, it was not distributed to employees who did not attend the training and is not available on the division's CityNet[8] page.

[7] This figure provides examples and is not a complete list.
[8] CityNet is the intranet page for City employees.

RECOMMENDATIONS:

We recommend that DGS:

5. **Update the Purchase Card Policy to make it consistent with other City policies.**
6. **Create an authoritative document that clearly states what types of purchase card transactions are allowable and prohibited, and distribute it to all cardholders and approving officials.**
7. **Ensure that the document is updated annually to reflect policy changes.**

The number of cardholders who received training is unknown, but appears limited

According to the Procurement Services Manager, DGS did not have a complete record of which cardholders attended the purchase card training. He said that he did not believe that all current cardholders completed the training since doing so was not required until approximately 2009. The available records note that 77 employees completed the purchase-card training.

Based on the sample[9] of 27, we found support showing that four cardholders completed the training. While more cardholders may have taken the course (as records were incomplete), the sample indicates that many may not have received the training.

As noted above, the training includes a presentation of the Handbook. This document provided the most detailed information about restricted purchases. According to DGS, the Handbook was not distributed to all cardholders. Without receiving the training and/or the Handbook, it is likely that some cardholders did not fully understand purchase card restrictions.

We found confusion about requirements during our review of sample transactions. Specifically, employees from two departments purchased ammunition on their City cards. The purchase of ammunition on these cards is prohibited by the Handbook, but not other policy documents. In a request for more information about these purchases, both departments said that the cardholders were not aware of this restriction since it was not specified in the Purchase Card Policy or User's Guide. Additionally, a review of purchase card training records showed that there was no indication that these two cardholders had completed the training.

As explained in Finding 1, some charges violated the Arizona Boycott. While DGS sent out a Citywide e-mail in 2010 with information related to the Boycott, no purchase card documents currently reflect this restriction. Additionally, the Travel Policy has not been updated to include the Boycott.

Since employees were given different criteria and were not always provided updates about purchase card rules, it is unclear if all cardholders were aware of the program's variety of restrictions. As rules related to prohibited purchase card use are not clearly communicated and centralized, it is difficult to hold cardholders and approving officials accountable for purchases that might be banned in one document and not others. While the prohibition on personal purchases is direct and consistent in all policy documents, other purchase card requirements are less clear.

[9] This sample of cardholders was the same sample used in monthly-statement testing.

RECOMMENDATIONS:

We recommend that DGS:

8. **Provide mandatory annual purchase card-use training for cardholders, and require them to sign a form agreeing to program terms and acknowledging their responsibilities.**
9. **Provide mandatory annual purchase card-approval training for approving officials, and require them to sign a form agreeing to program terms and acknowledging their responsibilities.**

Periodic reviews and targeting risk could help detect and deter unallowable transactions

While DGS administers the Purchase Card Program, it does not generally review if purchases were appropriate and instead relies on departments to provide oversight for their cardholders' purchases. However, the department has discussed reviewing purchase card charges in the future.

Setting up a process to periodically review transactions could detect unallowable and personal purchases and deter cardholders from making inappropriate charges. According to the Association of Certified Fraud Examiners' (ACFE) 2012 *Report to the Nations on Occupational Fraud and Abuse*, "the controls with the greatest associated reduction in fraud duration are those often credited with increasing the perpetrator's perception of detection." The report notes the detection and deterrence benefits associated with performing surprise audits.

To perform audits, DGS could review a sample of transactions or statements periodically for questionable purchases. Its staff could then work with other departments and possibly cardholders to gain further details. Additionally, the bank's Works application allows users to run standard and custom purchase card reports that could provide useful information. Approaches could vary and testing could be random or targeted to focus on things like largest purchases or charges to specific vendors.

RECOMMENDATIONS:

We recommend that DGS:

10. **Perform occasional surprise audits of purchase card transactions and present any concerns to respective departments and the City Manager's Office.**
11. **Consider running standard Works reports to help monitor purchase card activity and provide this information to respective departments and the City Manager's Office.**

The City would benefit from adopting purchase card best practices

The Government Finance Officers Association (GFOA), a group with the mission of enhancing and promoting the professional management of government, produces best practices for governments. The GFOA's best practice direction on Purchasing Card Programs stresses the importance of establishing appropriate controls.

The following are key GFOA purchase-card recommendations:

- Provide instruction on employee responsibilities and written acknowledgements signed by employees

- Ongoing training for cardholders and supervisors
- Spending and transaction limits
- Recordkeeping requirements for the review and approval process
- Clear guidelines on the appropriate use of purchase cards
- Periodic audits for card activity
- Timely reconciliation by cardholders and supervisors
- Procedures for card issuance and cancellation
- Segregation of duties for payment approvals, accounting and reconciliations
- Regular review of spending per vendor and merchant category codes

The Government Accountability Office (GAO), which has performed purchase card audits at federal agencies, has focused on many of the same points in its Purchase Card Audit Guide. In addition to those shown above, the GAO also has noted the importance of keeping a current list of cardholders and approving officials, and ensuring items bought through purchase cards are received and inventoried.

While the City follows many of these practices, they are not consistently applied and areas for improvement exist. For example, the GFOA recommends timely reconciliation of charges by cardholders and supervisors. We found multiple instances in which reconciliations were completed several months after statements were issued. Strengthening these areas based on recommended practices could enhance the purchase card program and help deter unallowable transactions.

RECOMMENDATIONS:

We recommend that DGS:

12. **Strengthen controls that are already in place and consider adding controls that are in line with best practices.**

Finding 3: The City's credit limit exceeds $2 million per month and the City could reduce risk by limiting the number of cardholders and establishing more comprehensive controls

Based on cardholder's credit limits, cardholders could charge just more than $2 million per month. While the amount actually charged per month in Fiscal Year 2011/12 was on average about $117,000, allowing that much outstanding credit represents a risk.

We found that:

- About half of purchase cards received minimal use and it is unclear if keeping these cards is justified; and
- Restricting the types of purchases could limit unallowable use.

The City can reduce its potential financial risk in various ways. Specifically, it can reduce the number of outstanding cards and establish controls to limit the types of purchases that can be charged.

About half of purchase cards received minimal use and it is unclear if keeping these cards is justified

The 263 cardholders reviewed charged about $1.4 million in Fiscal Year 2011/12. While some cardholders had several thousand dollars in purchases, others rarely used their cards. It is unclear if these low-use cards are needed and if keeping them is worth the risk. More cards in use increases the risk that cards will be used for unallowable purchases. It also means that employees must spend time reviewing and processing card transactions.

The half of cardholders (131) who spent the least on their cards during Fiscal Year 2011/12 charged on average $85.59 per month. These purchases accounted for about $134,500, or just less than 10 percent of the annual total. However, these cardholders' credit limits would have allowed them to charge as much as $889,800 per month. While there may be reasons to keep some of these purchase cards, it is likely that employees who make infrequent purchases with the cards could use other methods – like purchase orders – to pay City expenses.

While a low-use card might indicate that the card was not needed, other criteria could be used to limit the number of cards citywide. For example, departments could reassess if providing the cards to current cardholders is appropriate based on types of charges, frequency of use, and purchasing alternatives.

Under the purchase card program, departments currently have the authority to decide which employees should have purchase cards. While DGS administers the program, it does not issue or cancel cards without the instruction of departments. Given the number of cards with low use, the City should evaluate if all cards currently in place are needed.

RECOMMENDATIONS:

We recommend that DGS:

13. **Work with the City Manager's Office to reduce the number of purchase cards so only necessary cards are in use.**

Restricting the types of purchases could limit unallowable use

While the City has processes in place to review purchase-card transactions, it is possible that more controls could be established to stop certain purchases from occurring. The bank that administers the City's purchase card program can limit purchases to vendors by Merchant Category Codes (MCCs).

The bank that administers the purchase card program can set restrictions by broad category like retail stores, contracted services, or transportation. Or, more distinct MCCs could be blocked. The City could establish customized blocks for groups (like different departments) and individual cardholders. Some examples of MCCs that could be blocked in order to reduce the opportunity for personal and other unallowable purchases include amusement parks, babysitting services, bars, betting, jewelry, and pawn shops.

Based on information from the bank, restrictions by MCCs appear to be in place for some City cardholder groups. However, Procurement Services could not provide information about the number of cardholders in these groups and we could not verify during audit work that restrictions were in place for current cardholders.

Since blocking by MCCs has the potential to prevent unallowable purchases, the City would likely benefit from a thorough review of what categories are currently blocked and what could be blocked on all or most cards.

RECOMMENDATIONS:

We recommend that DGS:

14. **Review merchant categories and block purchases from certain categories for all users as a default, but allow for an exception process based on departments' requirements.**

DEPARTMENT OF
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October 15, 2012

To: Jorge Oseguera, City Auditor

From: Reina J. Schwartz, Director, Department of General Services

Re: Response to Audit of Citywide Purchase-Card Use

I want to thank the Office of the Auditor for a very thorough audit of the Citywide Purchase-Card Use. The audit was conducted professionally and will be a useful document for continuous improvement.

Below are my detailed responses. Where the response incorporates comments from multiple departments, those departments are identified.

With respect to the Audit Recommendations:

Recommendation No.1: Work with the City Manager's Office to review unallowable transactions identified through this audit and take appropriate action.

Procurement Response: Procurement will review unallowable transactions with the City Manager's Office and correct identified deficiencies through annual training for card holders and blocking prohibited merchant category codes.

Recommendation No. 2: Provide departments and cardholders more information about the benefits of purchasing through City-wide and cooperative agreements.

Procurement Response: Procurement will periodically provide departments with the 'Citywide Contracts' list that identifies active citywide and cooperative agreements available to staff. The purchase card User's Guide and Handbook will be updated to advise staff to review the 'Citywide Contracts' list for active agreements to curtail purchase card use for purchases when 'Citywide Contracts' exist.

Recommendation No. 3: Establish a consistent form and guidance to departments for processing lost receipt justifications.

Procurement Response: A standard 'Lost Receipt Justification' form and guidance will be developed and incorporated into the purchase card User's Guide and Handbook.
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Recommendation No. 4: Provide training to ensure Accounting staff only process purchase card statements with authorized signatures.

Finance Response: On September 12, 2012, the Accounting Division provided instructions to all personnel responsible for approving Purchase Card journals. The instructions state that approvers should ensure that purchase card statements are signed by those specified on the authorized signature forms.

Recommendation No. 5: Update the Purchase Card Policy to make it consistent with other City policies.

Procurement Response: A draft of an updated Purchase Card Administrative Policy (AP) was already being developed prior to this audit. It will be ready for review and finalization within the next 30-60 days. Procurement will publish and disseminate once it is approved.

Recommendation No. 6: Create an authoritative document that clearly states what types of purchase card transactions are allowable and prohibited, and distribute it to all cardholders and approving officials.

Procurement Response: The purchase card User's Guide update will include an expanded list of allowable and prohibited transactions. The updated User's Guide will be distributed to, and acknowledged by existing and new card holders.

Recommendation No. 7: Ensure that the document is updated annually to reflect policy changes.

Procurement Response: Procurement will establish mandatory annual training (either classroom or online) and acknowledgements to ensure purchase card holders are updated each year on policy changes and agree to program terms, conditions and sanctions.

Recommendation No. 8: Provide mandatory annual purchase card-use training for cardholders, and require them to sign a form agreeing to program terms and acknowledging their responsibilities.

Procurement Response: Concur, same as response to Recommendation #7.

Recommendation No. 9: Provide mandatory annual purchase card-approval training for approving officials, and require them to sign a form agreeing to program terms and acknowledging their responsibilities.

Procurement Response: Procurement will establish mandatory annual training (either classroom or online) and acknowledgements to ensure purchase card approving officials agree to program terms and acknowledge their responsibilities on an annual basis.

Recommendation No. 10: Perform occasional surprise audits of purchase card transactions and present any concerns to respective departments and the City Manager's Office.

Procurement Response: Under the direction of the City Manager, the Procurement purchase card administrator will conduct surprise audits of purchase card transactions and present any concerns to respective departments and the City Manager's Office. Follow-up audits will be performed to verify that violations are corrected and are not recurring.

Recommendation No. 11: Consider running standard Works reports to help monitor purchase card activity and provide this information to respective departments and the City Manager's Office.

Procurement Response: The Works program and reporting capabilities will be used more extensively to monitor purchase card activity and provide information to respective departments and the City Manager's Office. The standard Works reports will also be part of the feedback to departments and the City Manager's Office for surprise audits (Recommendation #10).

Recommendation No. 12: Strengthen controls that are already in place and consider adding controls that are in line with best practices.

Procurement Response: Procurement will incorporate the key Government Finance Officers Association (GFOA) purchase card recommendations identified in this audit as best practices. The Purchase Card Administrative Policy (AP), User's Guide and Handbook will be updated to include the recommendations.

Recommendation No. 13: Work with the City Manager's Office to reduce the number of purchase cards so only necessary cards are in use.

Procurement Response: The City Manager has already directed department heads to review the current holders of purchase cards to reduce the number of cards. The Purchasing Card Request form will be enhanced to include a justification for card issuance. Card use will be evaluated on an annual basis and those cards that are not used, or seldom used, will be identified as potential candidates for elimination.

Recommendation No. 14: Review merchant categories and block purchases from certain categories for all users as a default, but allow for an exception process based on departments' requirements.

Procurement Response: Procurement will block all merchant category codes that are not indentified for routine use by the card holder during card set-up and issuance. Seldom used merchant category codes that are not prohibited would be allowed for a limited period, with the approving official's written approval.

Once again, I would like to thank the Office of the Auditor for their professional efforts performing this review. I look forward to implementing the recommendations and subsequent reviews by the Office of the Auditor.

c:
John Shirey, City Manager