



UNITED STATES DEPARTMENT OF EDUCATION

OFFICE OF INSPECTOR GENERAL

OCT 13 2000

**INSPECTION MEMORANDUM**

**TO:** Frank Holleman, III  
Deputy Secretary

**FROM:** Mary Mitchelson  
Assistant Inspector General  
Analysis and Inspection Services

**SUBJECT:** Results of the OIG Review of Internal Controls Over the Use of Purchase Cards and Third Party Drafts (A&I 2000-15)

At the Department of Education's (Department) request, we reviewed the internal control over the Department's use of purchase cards and third party drafts. We previously submitted to you 14 individual principal office reports. In each principal office, we interviewed procurement staff and tested a sample of purchase card and third party draft transactions from FY 1999 and FY 2000 for adherence to internal control procedures and compliance with laws and regulations.

In this memorandum, we highlight the most significant issues from the individual reports and, in Attachment A, provide suggested recommendations that address these issues. Your attention to these concerns will improve the Department's internal control over these two programs. This will help safeguard against potential misuse or waste and ensure that purchase card transactions and third party drafts serve program needs.

Although the Department established control activities to ensure the financial integrity of the purchase card and third party draft programs, we found that prescribed control activities are not always followed. Additionally, we found that the office with responsibility for both programs, the Financial Management Policies and Administrative Programs Group (FMPAP), within the Office of the Chief Financial Officer (OCFO), needs to improve its administration of these programs. Consequently, the Department did not fully satisfy the General Accounting Office (GAO) *Standards for Internal Control in the Federal Government* in all cases.

## **PURCHASE CARDS**

### **Approving official review**

The most important control activity in the purchase card program is approving officials' review of cardholders' monthly statements, as required by the Department of Treasury Financial Manual. Approving officials are responsible for ensuring that all credit card transactions are for authorized purchases and in accordance with Department and other Federal regulations. Approving officials document their review by signing the purchase card statements before submitting the statements to FMPAP for payment. We found several instances, however, where approving officials had not signed monthly statements of individual purchase cardholders.

We reviewed the purchase card statements in FMPAP files for September 1999 and March 2000. In September 1999, for 70 percent of the individual cards with balances either the purchase card statement was missing or the statement was not signed. In March 2000, that figure was 48 percent.<sup>1</sup> These high percentages may be attributable to several factors. Within FMPAP we found a lack of effective communication and program oversight. Additionally, FMPAP does not regularly update its lists of principal office cardholders and approving officials. Without such a list, FMPAP cannot verify that individual purchase card statements have been approved by the appropriate officials.

### **Maintaining supporting documents**

Cardholders must maintain supporting documentation of individual transactions, such as receipts, invoices and purchase orders. That documentation should be readily available for examination. We identified transactions lacking sufficient documentation in most principal offices. This documentation is important to confirm that the purchase cards are being used to support the Department's needs.

In addition, we were unable to trace some purchase card transactions to expenditures on reports from the Department's accounting system, EDCAPS. In some cases, transaction numbers were not listed on the statements. In other cases, the transaction numbers did not appear on EDCAPS reports of expenditures. We also found some transactions recorded with incorrect dollar amounts.

### **Reconciliation of monthly purchase card bill**

FMPAP authorized the payment of the September 1999 and March 2000 purchase card bills without reconciling the monthly Department-wide statement to the individual principal office purchase card statements or to the Department accounting system, EDCAPS. Reconciliation helps ensure that the payment is accurate.

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<sup>1</sup> The percentages are obtained by adding the number of missing statements and statements not signed, divided by the number of statements with activity:  $40 + 95 = 135 / 192 = 70$  percent for September 1999 and  $9 + 85 = 94 / 194 = 48$  percent for March 2000.

## **Purchase card directive**

FMPAP has not updated its *Commercial Credit Card Directive* (Directive), originally released on March 3, 1990 and modified by pen and ink changes in March 1992. FMPAP should update the Directive to reflect current requirements and practices, and to provide necessary guidance to cardholders.

## **Cardholder training**

The Department provides a short training course for new cardholders. The training does not cover certain important areas such as approval procedures, nor does it define improper payments. There also is no requirement that cardholders receive any refresher training.

## **THIRD PARTY DRAFTS**

### **Separation of duties**

To prevent noncompliance and safeguard assets by separating duties, the Department's policy is that a person with signature authority (an authorizing official) cannot produce (print) a draft that he or she signs. Drafts are to be produced by a data entry person. We identified six employees from five offices who serve both as authorizing officials and data entry personnel. While we did not identify any drafts that these individuals both signed and printed, FMPAP has not identified any physical or system control activities that would prevent or detect such an occurrence.

### **Monitoring of drafts**

The Department's *Third Party Draft Operating Procedures Manual* (Manual) requires that authorizing officials periodically review drafts issued under their authority. The system in which issued drafts are recorded, EDCAPS, contains a number of errors. EDCAPS reports on third party draft activity listed drafts with more than one mutually exclusive status code: outstanding, voided, and cleared. Therefore, it is not a reliable record for the authorizing official's use. In addition, some principal offices were not maintaining logs of blank drafts, which are negotiable instruments. Without such a log, an authorizing official would find it difficult to identify missing drafts. Moreover, this review control from the Manual does not provide for sufficient separation of duties because it calls for review by the same official who approves the drafts.

### **Maintaining Supporting Documents**

We also discovered that principal offices were not maintaining sufficient documentation to support individual third party draft transactions. In some cases, approval signatures were missing from claim documents or files were either missing or unavailable for our review. In other cases, the invoice amount did not match the amount of the draft.

## **INTERNAL CONTROL OVER BOTH PROGRAMS**

### **Risk Assessment**

We found the Department is not conducting a comprehensive, formal risk assessment of its purchase card and third party draft programs. While staff in some principal offices told us that they had discussed vulnerabilities and controls over the programs, we noted the absence of a formal risk assessment process in all principal offices.

### **Procurement Authority**

Department policy requires employees with single purchase limits above \$2,500 to take simplified acquisition training and obtain warrants. Several cardholders had not satisfied this requirement. In addition, we found errors in the list of staff with procurement authority maintained by Contracts and Purchasing Operations (CPO), within OCFO. For example, some warrants were not cancelled when employees left the Department or changed principal offices, as required by Department policy. Also, the current list does not include information about third party draft signature authority.

### **Security Clearances**

In some offices, we identified procurement staff members that had been assigned lower risk levels when the employees' procurement responsibilities suggested that a higher risk level should be considered.

## **RESULTING PROBLEMS**

These control deficiencies increase the vulnerability of the Department to potential misuse or waste. We identified several problems that deserve special attention.

### **Sole-source procurement without appropriate documentation**

We identified transactions exceeding the \$2,500 micro-purchase threshold that lacked appropriate documentation to demonstrate compliance with the FAR. The FAR requires solicitation of quotes or offers from a reasonable number of sources or sole-source justification for any purchase of more than \$2,500.

### **Split procurements**

We identified acquisitions that were split into multiple purchases, apparently to avoid the \$2,500 micro-purchase threshold or the spending limits of individual purchase cardholders. The FAR prohibits the division of an acquisition to "avoid any requirement that applies to purchases exceeding the micro-purchase threshold."

## **Sharing of purchase cards**

We discovered several instances of cardsharing among employees with their approving officials' knowledge. To prevent purchase card misuse, Treasury Department policy states that only the person assigned the purchase card may use that card. In addition, although Department policy does not permit an approving official to serve as a cardholder, we found some approving officials used cardholders' purchase cards to make purchases. As a result, there was no separation of duties because these approving officials were both making and reviewing their own purchases.

## **Late payments**

We found several invoices that were not paid in accordance with the Prompt Payment Act. We also found several invoices that were not date stamped upon receipt to establish the proper payment due date under the Act.

## **OBJECTIVE, SCOPE, AND METHODOLOGY**

We reviewed internal control over the Department's use of purchase cards and third party drafts. We assessed the Department's internal control against the GAO *Standards for Internal Control in the Federal Government* issued November 1999. (Appendix B contains a summary of the GAO Standards.)

We limited our review to purchase card and third party draft use in Washington, D.C. (Headquarters). In evaluating the Department's internal control, we focused on the objective of compliance with laws and regulations.

To achieve our objective, we reviewed internal control in each principal office. For those reviews, we treated OCFO and the Office of the Chief Information Officer as one office because the offices share an Executive Office and Executive Officer. We also treated the Office of the Secretary, the Office of the Deputy Secretary, and the Office of Legislation and Congressional Affairs as one office for the same reason. In total, we conducted 14 individual office reviews. In each principal office, we interviewed staff involved with procurement.

We tested a sample of purchase card and third party draft transactions from FY 1999 and FY 2000 for adherence to internal control procedures and compliance with laws and regulations. We also verified the security clearance of some of the staff involved with procurement. After we completed the review of each principal office, we interviewed and briefed the office's senior official on the review results and issued a memorandum summarizing our findings.

In addition to the work in each principal office, we interviewed OCFO staff involved with the purchase card and third party draft programs and reviewed the policies and procedures for these programs. We examined the staff procurement authority records.

We also examined purchase card records maintained by FMPAP for the months of September 1999 and March 2000.

We interviewed more than 100 staff and senior officials. We conducted our interviews and internal control and compliance tests between February 24, 2000 and October 4, 2000. We conducted our work in accordance with the President's Council on Integrity and Efficiency (PCIE) *Quality Standards for Inspection* dated March 1993.

We have designated you as the primary action official for the recommendations attached to this memorandum. Please respond within 45 days from the date of this memorandum on what actions, if any, you plan to take.

We appreciate the cooperation shown by your staff during our review. If you have any questions regarding the results of this review, please call me at 260-3556.

Attachments

cc: Senior Officers

**OIG Recommendations Regarding the Department's  
Internal Controls Over the Use of Purchase Cards  
and Third Party Drafts**

**CONTROL ENVIRONMENT: Management and employees should establish and maintain an environment throughout the organization that sets a positive and supportive attitude toward internal controls and conscientious management.**

**Recommendations**

Based on our review we recommend the following actions be taken by the Department to strengthen the control environment over the use of purchase cards and drafts:

1. Increase the scope of procurement training to ensure that all cardholders, approving officials, data entry personnel, authorizing officials, supervisors and senior officials involved with simplified acquisitions have an adequate understanding of procurement requirements and procedures.
2. Establish a requirement for refresher training for all staff with procurement authority.
3. Establish a training requirement for FMPAP personnel, and ensure that FMPAP staff adhere to established policies and procedures.
4. Require that all staff with procurement authority, regardless of grade level, attend annual ethics training or include an ethics component in the procurement training.

**RISK ASSESSMENT: Internal controls should provide for an assessment of the risks the agency faces from both external and internal sources.**

**Recommendations**

Based on our review we recommend the following actions be taken by the Department to strengthen risk assessment in the use of purchase cards and drafts:

1. Establish formal policies and procedures to identify, analyze and, as appropriate, take steps to mitigate procurement risks at all levels.

2. Require all principal offices to assess the level of security clearance performed on their staff with procurement authority and schedule appropriate updates as necessary.

**CONTROL ACTIVITIES: Internal control activities help ensure that employees carry out management directives. The control activities should effectively and efficiently accomplish agency control objectives.**

### **Recommendations**

Based on our review we recommend the following actions be taken by the Department to strengthen control activities over the use of purchase cards and drafts.

1. Update the *Commercial Credit Card Directive* and communicate it to all cardholders, approving officials and Executive Officers.
2. Enforce Department policy that approving officials must be at a managerial level and may not serve as a cardholder or use a cardholder's account.
3. Require that all approving officials review and sign monthly purchase card statements.
4. Reduce spending limits for cardholders until they obtain required warrants from CPO.
5. Reestablish the policy of written delegation from CPO to all cardholders as defined in the Department of Treasury Financial Manual.
6. Require that principal offices submit their signed purchase card statements to FMPAP on time.
7. Ensure that each principal office is provided with a sequentially numbered stock of blank third party drafts and that each principal office maintains a log of the stock received and updates the log as each draft is issued.
8. Require that each principal office have a manager, other than an authorizing official, perform periodic reviews of the EDCAPS reports on third party draft activity and the log of issued third party drafts.
9. Ensure that the Department's accounting system (currently EDCAPS) correctly records and reports procurement activity.



**INFORMATION AND COMMUNICATION: Employees should record and communicate information to management and others within the entity who need it in a form and within a time frame that enables them to carry out their internal control (and other) responsibilities effectively and efficiently.**

#### **Recommendations**

Based on our review we recommend the following actions be taken by the Department to strengthen information and communication regarding the use of purchase cards and drafts:

1. Maintain and publicize an updated, consolidated, user-friendly web site on the Department's Intranet to convey procurement requirements and information.
2. Identify, obtain and distribute management reports necessary for monitoring purchase cards and drafts.
3. Continuously update procurement authority records.
4. Provide to all staff with procurement activity clear instructions on how to handle and report suspected abuse or fraud.

**MONITORING: Internal control monitoring should assess the quality of performance over time and ensure that audit and other review findings are promptly resolved.**

#### **Recommendations**

Based on our review we recommend the following actions be taken by the Department to strengthen monitoring over the use of purchase cards and drafts:

1. Reconcile the monthly Department-wide purchase card statement to the monthly statements from the principal offices and to the Department's accounting system (EDCAPS).
2. Manage and monitor primary controls such as the approving official signature on monthly purchase card statements.
3. Monitor information on staff with procurement authority provided by CPO.

**GAO's Standards for Internal Control in the Federal Government**  
**Components of Internal Control**

- **Control Environment** – Management and employees should establish and maintain an environment throughout the organization that sets a positive and supportive attitude toward internal controls and conscientious management.

Factors:

- ✓ Management and staff maintain and demonstrate integrity and ethical values.
  - ✓ Management maintains an active commitment to competence.
  - ✓ Management's philosophy and operating style exert a positive influence on the organization (especially toward information systems, accounting, personnel functions, monitoring and audits).
  - ✓ Organizational structure is appropriately centralized or decentralized, and facilitates the flow of information across all activities.
  - ✓ Agency delegates authority and responsibility and establishes related policies throughout the organization in a manner that provides for accountability and control.
  - ✓ Agency establishes human resource policies and practices that enable it to recruit and retain competent people to achieve its goals.
- **Risk Assessment** – Internal controls should provide for an assessment of the risks the agency faces from both external and internal sources.
    - ✓ Precondition – establishment of clear and consistent agency objectives.
    - ✓ Risk assessment – the comprehensive identification and analysis of relevant risks associated with achieving agency objectives, like those defined in strategic and GPRA annual performance plans, and forming a basis for determining how the agency should manage risks.
    - ✓ Risk identification – methods may include qualitative and quantitative ranking activities, management conferences, forecasting and strategic planning, and consideration of findings from audits and other assessments.
    - ✓ Risk analysis – generally includes estimating the risk's significance, assessing the likelihood of its occurrence, and deciding how the agency should manage its risk.

- **Control Activities** – Internal control activities help ensure that employees carry out management directives. The control activities should effectively and efficiently accomplish agency control objectives.
  - ✓ The control activities are the policies, procedures, techniques, and mechanisms that enforce management's directives. They help ensure that employees take actions to address risks.
  - ✓ Control activities occur at all levels and functions of the entity, and include a wide range of diverse activities such as approvals, authorizations, verifications, reconciliations, performance reviews, maintenance of security, and creation and maintenance of related records that document the execution of these activities.
  
- **Information and Communications** – Employees should record and communicate information to management and others within the entity who need it in a form and within a time frame that enables them to carry out their internal control (and other) responsibilities effectively and efficiently.
  - ✓ An organization must have relevant, reliable, and timely communications relating to internal as well as external events. Information is needed throughout the agency to achieve all its operational and financial objectives.
  - ✓ Effective communications should occur in a broad sense with information flowing down, across, and up the organization.
  - ✓ Management should ensure there are adequate means of communicating with, and obtaining information from, external stakeholders that may have a significant impact on the agency achieving its goals.
  
- **Monitoring** – Internal control monitoring should assess the quality of performance over time and ensure that audit and other review findings are promptly resolved.
  - ✓ Includes regular management and supervisory activities, comparisons, reconciliations, and other actions employees take in performing their duties.
  - ✓ Should include policies and procedures for ensuring that audit and other review findings are promptly resolved.