Port
of Seattle

# Internal Audit Report

## Limited Operational Audit

## Procurement Card Administration

April 1, 2011 – February 29, 2012

Issue Date: August 7, 2012
Report No. 2012-11

# Table of Contents

Port
of Seattle

**Transmittal Letter**

Audit Committee
Port of Seattle
Seattle, Washington

We have completed a limited operational audit of Procurement Card Administration.

We examined information related to the period April 1, 2011, through February 29, 2012.

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.

We extend our appreciation to the management and staff of the Central Procurement Office, Accounting and Financial Reporting, and the departments throughout the Port where we conducted our testing of Procurement Card Administration for their assistance and cooperation during the audit.

Joyce Kirangi, CPA
Director, Internal Audit

## Executive Summary

**Audit Scope and Objectives** We examined Procurement Card Administration for the period April 1, 2011, through February 29, 2012.

The purpose of the audit was to determine whether:

1. The procurement card (P-card) program is efficient and effective

2. Management controls are adequate to ensure:

   - Proper assignment and monitoring of roles and responsibilities
   - Safe and secure distribution of P-cards
   - Compliance with the requirements of CPO-7
   - Rebate is accurate and maximized

**Background** As of April 1, 2011, the Port of Seattle introduced a new procurement card program and policy (CPO-7), which eliminated separate vendor accounts and associated store cards and substantially expanded the use of procurement cards throughout the Port. Fuel purchases are no longer made, with a few exceptions, with procurement cards, but with separate fuel cards. Although the Port has used procurement cards for eight years, the prior cards were assigned to departments and used to make payments on existing contracts. The new program promotes repetitive, small dollar purchases, and cardholders are not restricted to specific vendors. This new program is intended to provide a more efficient process and reduce the costs of purchasing routine goods and services. As of February 2012, there were 142 active cards. The total procurement card expenditures for the period April 1, 2011, through February 29, 2012, were $5.2 million.

Since 2009, the P-card program has operated under an agreement with Bank of America. Under the agreement, the Port participates in a rebate program for public entities. The rebate program includes procurement cards, travel cards, and electronic payments. From 2009 to 2011, the P-card expenditures tripled and the related rebate has increased four-fold. See Table 1.

Table 1 – Rebate Derived from Procurement Card

| Year | Annual P-card Expenditures | Rebate Amount | Rebate % |
|------|---------------------------|---------------|----------|
| 2009 | 1,572,987 | 15,948 | 1.01% |
| 2010 | 2,033,689 | 27,396 | 1.35% |
| 2011 | 4,758,963 | 65,436 | 1.37% |

Source: Bank of America, Works (proprietary bank software)

The transaction limit on a P-card purchase (one transaction) is $5,000 (with some exceptions), with a monthly maximum expenditure of $25,000 (with a few cardholders having monthly limits of $75,000 and $100,000).

**Audit Result Summary** The Procurement Card Program is effective, with opportunities to increase efficiency and improve process, which are discussed in the Schedule of Findings (Improvement Opportunities) and Recommendations. Controls are adequate to ensure that operations are proper and in compliance with the requirements.

## Background

As of April 1, 2011, the Port of Seattle introduced a new procurement card program and policy (CPO-7), which eliminated separate vendor accounts and associated store cards and substantially expanded the use of procurement cards throughout the Port. Fuel purchases are no longer made, with a few exceptions, with procurement cards, but with separate fuel cards.  Although the Port has used procurement cards for eight years, the prior cards were assigned to departments and used to make payments on existing contracts.  The new program promotes repetitive, small dollar purchases, and cardholders are not restricted to specific vendors.  This new program is intended to provide a more efficient process and reduce the costs of purchasing routine goods and services.

As of February 2012, there were 142 active cards. The total procurement card expenditures for the period April 1, 2011, through February 29, 2012, were $5.2 million.  The transaction limit on a P-card purchase (one transaction) is $5,000 (with some exceptions), with a monthly maximum allowed expenditure of $25,000 (with a few cardholders having monthly limits of $75,000 and $100,000). (Note:  The per-transaction authority is derived from Policy EX-2.)

Financial Highlights

The current procurement card program has resulted in expanded use and increased purchases throughout many departments.  The two departments that have increased P-card use the most are the Port's maintenance operations.    See Table 1.

Table 1 – Top Two Departments' P-card Expenditures

| Department | Procurement Card Expenditures April 30, 2009, thru March 31, 2011 (23 months) Before CPO-7 | Procurement Card Expenditures April 1, 2011, thru February 29, 2012 (11 months) After CPO-7 |
|---|---|---|
| Aviation Maintenance. | $1,080,188.54 | $1,905,439.63 |
| Seaport Maintenance | 392,428.81 | 883,190.98 |

Source:  Bank of America, Works (proprietary bank software)

The top five P-card vendors and other vendors before and after CPO-7 are identified below, with total P-card vendors increasing from 505 to 1,595.  See Table 2.

Table 2 – Top Five P-card Vendors and Total Other Vendors

| Procurement Card Expenditures April 30, 2009, thru March 31, 2011 (23 months) Before CPO-7 | | | Procurement Card Expenditures April 1, 2011, thru February 29, 2012 (11 months) After CPO-7 | | |
|---|---|---|---|---|---|
| XEROX CORP | $589,499 | 15% | KEENEYS OFFICE SUPPLY, | $390,386 | 7% |
| W W GRAINGER | 407,011 | 10% | UNIFORM&CAREER APPAR EL | 373,205 | 7% |
| UNIFORM&CAREER APPAREL | 385,936 | 10% | W W GRAINGER | 204,649 | 4% |
| KEENEY'S OFFICE SUPPLY | 333,291 | 9% | DELL | 129,114 | 3% |
| UNITED REPROGRAPHICS | 281,639 | 7% | BRATWEAR | 83,136 | 2% |
| Others (about 500 vendors) | 1,934,551 | 49% | Others (about 1,590 vendors) | 4,108,340 | 77% |
| Total | $3,931,927 | 100% | Total | $5,288,830 | 100% |

Source:  Bank of America, Works (proprietary bank software)

Since 2009, the P-card program has operated under an agreement with Bank of America.  Under the agreement, the Port participates in a rebate program for public entities. The rebate program includes procurement cards, travel cards, and electronic payments.  From 2009 to 2011, the P-card expenditures tripled, and the related rebate increased four-fold.  See Table 3.

Table 3 – Rebate Derived from Procurement Card

| Year | P-card Annual Expenditures | Rebate Amount | Rebate % |
|------|---------------------------|---------------|----------|
| 2009 | 1,572,987 | 15,948 | 1.01% |
| 2010 | 2,033,689 | 27,396 | 1.35% |
| 2011 | 4,758,963 | 65,436 | 1.37% |

Source:  Bank of America, Works (proprietary bank software)

## Highlights and Accomplishments

- The Procurement Card Program has reduced the number of A-Type purchase orders for transactions under $5,000.  Purchase orders declined from a high of 186 purchase orders in April 2011, when the current program began, to a low of 51 purchase orders in February 2012.  The reduction in POs and the increase in P-card purchases have reduced accounts payable processing costs. See Graph 1.



Graph 1 – Purchase Order Activity less than $5,000
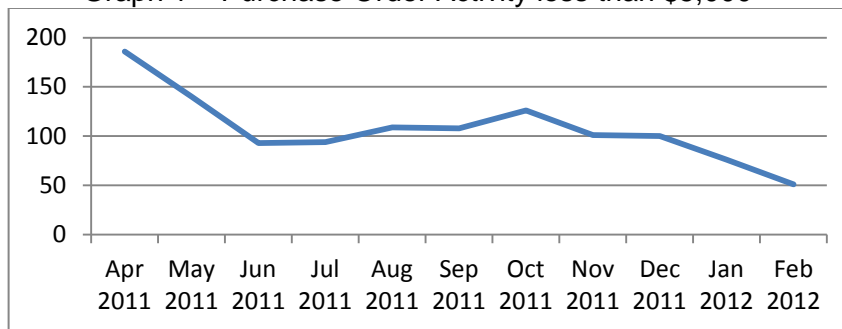
- P-card activity increased by almost 7,000 transactions after CPO-7 was implemented.  Based on the accounts payable costs of processing P-card transactions versus PO transactions, we can impute cost savings.  According to accounts payable management metrics, which are available on the Port's internal web site, the cost of processing purchase orders (PO) is $10.98 per PO, and the cost of processing procurement card transactions is $5.44. See Table 4.

Table 4 – P-card Activity – Pre and Post CPO-7

| Pre CPO-7 April 2010-February 2011 | | Post CPO-7 April 2011 - February 2012 | Increase in P-card Activity Post CPO-7 |
|---|---|---|---|
| **Total Transactions** | **9,131** | **15,964** | **6,833** |
| | | Cost of processing P-card activity | $5.44 |
| | | Total cost of increased P-card activity | $37,172 |
| | | Cost of processing PO activity | $10.98 |
| | | Total cost of decreased PO activity | $75,026 |
| | | Imputed savings due to P-card usage | $37,854 |

- The Port created the position of Procurement Card Administrator in spring 2011, to ensure adequate oversight and administration of the program.  The Procurement Card Administrator conducts regular analysis of P-card activity and on-site reviews of supporting documents for expenditures, which are maintained by the departments.

- The Port established a comprehensive and ongoing schedule of training for the procurement card program, requiring all card holders and managers to attend the training prior to being issued a procurement card.   This training is provided by the Procurement Card Administrator.

## Audit Scope and Methodology

We utilized a risk-based audit approach, from planning to testing.  We gathered information through extensive interviews with administrators, managers, and cardholders in order to obtain a complete understanding of the program and its administration.  We analyzed procurement card activity.  We conducted the following procedures to address our audit objectives:

1. Procurement card program is efficient and effective

    - We benchmarked the Port of Seattle's procurement card program against similar programs at other port districts.

    - We identified process improvements, based on process review, testing, analytics, and benchmarking.  Specific analytics included identifying:

        o Cardholders and departments with the largest expenditures
        o Transactions that could be potential splits
        o Merchant Codes programmed into the cards
        o Purchase orders less than $5,000 processed before and after CPO-7
        o Purchase orders between $5,001 and $24,999 processed after CPO-7
        o Cardholder usage by maximum transaction amounts and by monthly expenditures amounts
        o Comparison of vendors in PO system and in P-card system

2. Management controls are adequate to ensure:

    - Proper assignment and monitoring of roles and responsibilities.

        o We obtained a report of roles and responsibilities for all users as of March 27,  2012, and determined whether:

            - Assignments are monitored
            - Assignments are conflictive
            - Assignments are proper and current

- Safe and secure distribution of P-cards

  o We reviewed the distribution methods for 94 cards (from a total of 142) and determined whether:

    - Distribution methods were appropriate and secure
    - There was clear transfer of accountability over the cards.

- Compliance with the requirements of CPO-7

  Due to the decentralized nature of procurement cards, the primary controls over card use reside within the departments. However, there is a robust central monitoring control performed by the Procurement Card Administrator. We reviewed the audit efforts and results of the Procurement Card Administrator. Based on that robust monitoring control, we were able to reduce our substantive testing.

  We selected cardholders across multiple departments to determine whether controls were adequate and whether processed transactions were in compliance with the requirements. The selection criteria included a variety of risk factors:

    - level of expenditures
    - unauthorized activity on card
    - prior audit issues related to cardholder
    - multiple reconciliations performed by cardholder

  Based on the above risk factors, we selected seven of 136 cardholders across six departments, with total expenditures representing 37 percent ($1,964,551) of the total P-card expenditures ($5,288,830).  Based on additional risk factors within the sampled cardholders, we selected transactions totaling $192,551 – 10 percent of the expenditures of the cardholders tested for control and compliance.

- P-card rebate is accurate and maximized

  We reviewed monthly rebate calculations and determined whether rebate:

    - Agreed to the bank statement
    - Calculated accurately based on expenditures
    - Earnings could be increased

## Conclusion

The Procurement Card Program is effective, with opportunities to increase efficiency and improve process, which are discussed in the Schedule of Findings (Improvement Opportunities) and Recommendations.  Controls are adequate to ensure that operations are proper and in compliance with the requirements.

| Schedule of Findings (Improvement Opportunities) and Recommendations |
|:---:|

**1.** **The Current Guidance Of CPO-7 Could Be Improved To Optimize the Use Of The Procurement Card, While Continuing To Manage Risks To The Port.**

Port management implemented a new procurement card program to effect process improvements, promote increased use of procurement cards, and decrease the delays between requesting and receiving goods. Simultaneously, management wanted to ensure that there were strong controls over this more robust program, to prevent misuse and abuse. Management took a conservative approach, to ensure that the rules were easy to implement and minimized risks.

Some of the current requirements of CPO-7, while ensuring strong controls and creating efficiencies over the use of the procurement cards, could be improved to further maximize efficiency and use of the procurement cards. Since the inception of CPO-7, management has made a concerted effort to tailor the P-card program to the business needs of the cardholders; however, some areas may warrant further improvements.

a. P-card transaction limits and monthly expenditure limits seem higher than business needs. Most transaction limits per cardholder have been set at $5,000 within Policy EX-2 by the Executive Team, and this limit has been built into each cardholder's profile. We analyzed maximum expenditures per transaction for each of 136 cardholders, from April 1, 2011, through February 29, 2012, and determined the following:

- The majority of cardholders (78 percent) appeared not to need a transaction limit this high.
- A minority of cardholders (22 percent) might have benefited from a higher limit.

See Table 1.

Table 1 – Breakout of Maximum Expenditures Per Transaction

| Maximum Amount | Number of Cardholders | Percentage |
|---|---|---|
| < $1000 | 59 | 43.4% |
| $1001 - $2000 | 22 | 16.2% |
| $2001 - $3000 | 12 | 8.8% |
| $3001 - $4000 | 13 | 9.6% |
| $4001 - $5000 | 28 | 20.6% |
| > $5000 | 2 | 1.5% |
| Grand Total | 136 | 100.0% |

The monthly expenditure limit of $25,000 seems higher than necessary for most cardholders. We analyzed the maximum monthly expenditures for each cardholder, from April 1, 2011, through February 29, 2012, and determined the following:

- The majority (89 percent) did not need such a high monthly limit.

- For four of the cardholders (3 percent), the limit was appropriate.
- Ten cardholders (8 percent) have been granted higher limits, based on business needs.

See Table 2.

Table 2 – Breakout of Maximum Expenditures Per Month

| Amount | No. of Cardholders | % of Cardholders |
|---|---|---|
| $0 | 3 | 2.2% |
| $1 - $2,499 | 65 | 47.8% |
| $2,500 - $4,999 | 22 | 16.2% |
| $5,000 - $7,499 | 12 | 8.8% |
| $7,500 - $9,999 | 7 | 5.1% |
| $10,000 - $12,499 | 4 | 2.9% |
| $12,500 - $14,999 | 0 | 0.0% |
| $15,000 - $17,499 | 5 | 3.7% |
| $17,500 - $19,999 | 4 | 2.9% |
| $20,000 - $22,499 | 2 | 1.5% |
| $22,500 - $24,999 | 2 | 1.5% |
| Greater than $25,000 | 10 | 7.4% |
| | 136 | 100% |

Excess expenditure capacity on cards exposes the Port to increased risk of a card being compromised. The fraudulent charges identified below could have been even higher, due to excess monthly expenditure limits.   See Table 3.

Table 3 – Fraudulent Charges

| Card No. | Fraudulent Charge (1) | Current Monthly Limit | Typical Monthly Expenditures |
|---|---|---|---|
| 3484 | $150.00 | $25,000 | $5000 |
| 5663 | $166.31 | $25,000 | $2,000 (with one month's exception of $7,000) |

**(1)** These fraudulent charges were made by parties external to the Port.
These fraudulent charges were reversed by Bank of America.

b. Another perspective on transaction limits takes into account purchase order (PO) activity between $5,001 and $24,999. Transactions within these parameters could translate into additional procurement card transactions, lowering processing costs and increasing rebates. The procurement card program could be expanded into A-Type purchase orders to maximize efficiency and cost savings.

From 4/1/2011 to 2/29/2012, there were 1,184 A-Type purchase orders for less than $5,000 and 549 A-Type purchase orders between $5,001 and $24,999. Transactions within these parameters could translate into additional procurement card transactions, lowering processing costs and increasing rebates.

According to accounts payable management metrics, which are available on the Port's internal web site, the cost of processing purchase orders (PO) is $10.98 per PO, and the cost of processing procurement card transactions is $5.44. The per-transaction savings is $5.54. The following table projects the potential cost savings and the potential rebate, if all of the PO activity cited below were to become P-card activity. (It is important to keep in mind that all POs cited below would not become P-card transactions, due to legal and other risk issues.) See Table 4.

Table 4 – Projection of Savings and Rebate Earnings

| Period – 4-1-11 thru 2-29-12 | Count | Expenditure Total |
|---|---|---|
| A-Type POs less than $5,000 | 1,184 | $ 1,542,398 |
| A-Type POs Between $5,001 and $24,999 | 549 | $ 5,818,005 |
| Total | 1733 | $ 7,360,403 |
| **Potential Savings** | | |
| Difference Between the Cost of PO and Credit Card Processing | $ 5.54 X 1733 | $ 9,601 |
| Potential Additional Rebate | 1.37% in 2011 | $ 100,838 |

Of the 320 vendors paid with A-Type purchase orders between $5,001 and $24,999, over 35 percent of these vendors are also used for P-card purchases. See Table 5.

Table 5 – Vendor Comparison

| A-Type Purchase Order Vendors | | |
|---|---|---|
| Is the Vendor also a P-card Vendor? | No. Vendors | % |
| NO | 206 | 64.4% |
| YES | 114 | 35.6% |
| Grand Total | 320 | 100.0% |

c. The requirement of a pre-purchase request for approval of procurement card purchases is not a typical control over procurement card purchases. Although management imposed this requirement to prevent fraud, misuse, and abuse, the pre-purchase request creates a process step that P-card programs are intended to eliminate. In the benchmarking survey of ten other airports, 80 percent of the respondents do not require a pre-purchase authorization. In the majority of procurement card programs, the assignment of a procurement card is the authorization to purchase (within policy guidelines and the limits imposed on each cardholder). (Note: This issue is only related to the requirement within CPO-7; it does not relate to any department's internal requirement for a pre-purchase request.)

**Recommendations**

1. Consider instituting scaled limits for P-card transactions and monthly expenditures, based on each cardholder's history and/or business needs, rather than continuing to establish limits that align with the upper limits authorized under EX-2. (In other words, consider embedding lower limits based on the cardholder's expenditure history.)

2. In concert with Recommendation 1, consider establishing the role of "requester" in the "Works" system. The "requester" role would allow the "approver" to authorize isolated instances of one-time increases in transaction limits (keeping in mind that limits established by Policy EX-2 cannot be exceeded).

3. Consider expanding the P-card program into A-Type purchase orders over $5,000.

4. Consider eliminating the requirement within CPO-7 of a pre-purchase request authorization.

### *Management Response*

CPO appreciates the time and effort taken by the Internal Auditor in auditing the Port of Seattle (Port) P-Card Program. In April 2011, the Port kicked off a new progressive program significantly expanding utilization of the P-Card in the procurement of small dollar value items and services. This audit provides information and insight into the success of our program while looking for ways to improve the program.

CPO recognized the significant value of an expanded P-Card program and was conscientious about avoiding misuse and fraudulent purchases in the launching of the program. In implementing the P-Card program, we employed a strong training program and user forum. To improve the success of the program, we made certain we had resources to assist cardholders and approvers.

We established a $5,000 single transaction threshold, which is high compared to industry standard of $2,500. To mitigate risks of abuse and fraud, we established controls, including the requirement for pre-authorization. Compared to the benchmark survey, implementation of this new program has been successful with minimal personal use and external fraud. The few personal use items were self-reported and addressed quickly and we have not canceled cardholder privileges. The known external fraud was investigated and reported to Internal Audit and the Port Police as required.

The Port's P-Card program has resulted in savings to the Port. We have received an increase in the rebate from $27,396 in 2010 to $65,436 in 2011. Additionally, the Port benefits from a transaction process cost reduction. According to Government Procurement magazine, published February/March 2012, the typical cost of processing a standard purchase order is $93.00, while the cost of processing P-Card transactions is $22. Utilization of the P-Card results in a cost per-transaction savings of $71. Assuming an average of reduction of 2,300 purchase orders, nets a process savings of $163,300. Our program has also resulted in increased timeliness from "requisition" to delivery. Typically, CPO processes POs within four (4) business days. The P-Card provides for the immediate placement of an order with the vendor which reduces the order placement time by four (4) days, has the potential to reduce the time it takes to deliver the item, and the manual transmission of PRs to CPO through the interoffice mail.

CPO will take all four (4) audit recommendations under consideration.

With respect to the pre-purchase request authorization, the decision to embed this requirement into CPO-7 was made jointly by CPO, Legal, Accounting, and the Internal Auditor. The purpose for the authorization was threefold: (1) validate business purpose; (2) budget control; and (3) control for fraud/inappropriate use. This requirement creates a control point and separation of duties between the requestor and cardholder. Without such separation, the cardholder has greater opportunity to purchase and receive small attractive items without any substantive oversight. Additionally, this pre-authorization assists in the ability for another cardholder to reconcile the paperwork when the main cardholder is absent.

It is important to note that approximately 60% of the pre-approvals would not be eliminated as Marine Maintenance and Aviation both utilize the Maximo system which generates a Purchase Requisition (PR) and requires approval prior to any purchase. The ICT Service Request would also not be eliminated as that is part of their department's business process prior to making purchases on behalf of Port employees. No additional controls were implemented in those areas and the PR generated from the Maximo system and the ICT Service Request is acceptable under CPO-7. For other purchases, an e-mail is an acceptable and expeditious method of pre-approving the purchase. In considering this request, CPO will meet with Legal, Accounting, and the Internal Auditor to revisit the business decision surrounding this requirement.

*Points of Clarification on Benchmarking Study:*

- Question 2 indicates that the Port began using a Procurement Card (P-Card) eight (8) years ago. While that statement is accurate it may be slightly misleading. The original program was only a payment vehicle for existing contracts. On April 1, 2011, the Port's P-Card program was significantly revised and expanded as a procurement tool under CPO-7.

- Question 12 indicates that there are two (2) Port personnel who administer the P-Card Program. The Port has one (1) full-time P-Card Administrator who is responsible for the overall compliance with the Program and making recommendations for improvement to management. CPO Purchasing is in the process of expanding the role to include overview of the roles, card activity, establishing a regular schedule of monitoring these activities and to establish a method for direct communication with Bank of America (BOA) so that efficiencies may be gained in working with the system and in dealing with disputes, fraudulent activities, and increasing customer service to cardholders and approvers.

  The AFR AP Lead has the assignment in the BOA Works System role as the "administrator". The administrative duties of that person include:

    - Providing access to the BOA Works Program
    - Liaison with BOA
    - Process Bank Interface and payment
    - Issuing cards, entering in BOA Works Program the authorized limits as approved and validated by the P-Card Administrator
    - Assist users with reconciliation, adjustments, coding
    - Monitor accounts not reconciled/approved
    - Monitor active cards for unusual activity – fraud when notified by BOA that a P-Card has been flagged as a Decline Score 1 and advising the P-Card Administrator for further investigation and reporting as may be required.

- Question 18 indicates that the Port has experienced personal purchases having been made. There have been two (2) incidents of personal use. Individuals self-reported the purchases quickly and reimbursed the Port.

Thank you for providing CPO with an opportunity to provide a response, speak to the progression of the program, and provide clarification.