MEMORANDUM

TO   :   Greg Woods
                       Chief Operating Officer
                       Student Financial Assistance

FROM   :   Mary Mitchelson
                       Assistant Inspector General
                       Analysis and Inspection Services

SUBJECT   :   Results of the OIG Review of SFA's Internal Controls Over the
                       Procurement of Goods and Services Using Third Party Drafts and
                       Purchase Cards (A&I 2000-014)

INTRODUCTION

This memorandum transmits the results of our review of Student Financial Assistance's
(SFA) internal controls over the procurement of goods and services using Third Party
Drafts and purchase cards. This review is part of OIG's Department-wide review of this
area. The Department's management is responsible for establishing and maintaining
internal controls. We will provide a summary report of the Department-wide results to
the Deputy Secretary with copies to the Assistant Secretaries and other senior staff when
we complete our review. On October 4, 2000, OIG staff met with you and members of
your procurement staff to discuss the results of this review.

RESULTS

We identified significant noncompliance with current Department policies and
procedures:

➢ *Many monthly purchase card statements were not reviewed by an Approving Official.*

   We were informed that the Approving Officials had not been receiving, reviewing
   and signing all the monthly purchase card statements before forwarding the
   statements to the Office of the Chief Financial Officer (OCFO) for payment. We
   reviewed records in SFA and OCFO for a period of six months (one month in FY99

and five months in FY00). For any given month, we determined that at least half of the purchase card statements were not reviewed by Approving Officials.

The Departmental Directive *Commercial Credit Card Service* dated March 12, 1990 requires that the Approving Official review and sign the cardholders' monthly purchase card statements and then forward the signed statements to OCFO for payment. The Department's policy is based on requirements in the *Treasury Financial Manual*. The review by Approving Officials is necessary to ensure that all charges on the statement are proper.

➢ *Supporting documentation on some Third Party Drafts was not available for review.*

Supporting documentation (copies of drafts, invoices, receipts, purchase orders) for 22 of the 57 drafts that we judgmentally selected to review from SFA's EDCAPS report on Third Party Payment activity were not available for us to review. These 22 drafts totaled $47,333. Without documentation there is no assurance that these charges are appropriate.

The Department's *Third Party Draft Operating Procedures Manual* dated May 1999 states:

> Government regulations require these documents (copies of the drafts, invoices/SF-1164s) be filed on site for a period of one year, readily accessible for an additional two years, and archived for three more years.

In addition, we want to advise you and SFA managers of an inherent vulnerability we identified in the Third Party Draft System. An individual with signature authority can issue Third Party Drafts without the involvement of anyone else. Therefore, it is important that, at a minimum, a supervisor without signature authority periodically review drafts issued.

We identified other deficiencies in SFA's internal control, which are described in Attachment A. The non-compliance described above and the deficiencies listed in the attachment prevent SFA from satisfying the General Accounting Office (GAO) *Standards for Internal Control in the Federal Government*. In the future, we anticipate conducting a follow-up review to assess the actions you have taken to satisfy these standards.

OTHER MATTERS

Ethics training for all cardholders – During our review, we noted that some SFA staff assigned purchase cards are below the minimum grade level (GS-9) required to receive annual ethics training. Because of their procurement responsibilities, ethics training would benefit these employees. Management should consider requiring them to attend annual ethics training.

Third Party Drafts listed on OPE's reports – Some drafts issued by SFA are assigned Office of Postsecondary Education (OPE) organization codes and thus are listed on OPE's reports of Third Party Draft activity. SFA should work with OPE and OCFO to ensure that drafts issued by SFA are listed on SFA's reports.

Errors on OCFO records of cardholders – Some SFA and OPE cardholders are listed in OCFO records under the wrong office. SFA should work with OPE and OCFO to correct the records.

OBJECTIVE, SCOPE AND METHODOLOGY

Our review objective was to assess the internal controls over compliance with laws and regulations for the procurement of goods and services other than studies or evaluations. We limited our work to procurements in Washington, D.C. (Headquarters) using the Third Party Drafts and purchase cards. We did not conduct testing on SFA's use of "Corporate" Government Travel Accounts. Third Party Drafts are used in certain student financial assistance loan program transactions. Since these transactions are not procurements, we did not include them in our review.

To achieve our objectives, we conducted interviews with SFA staff involved with the procurement process, and we reviewed relevant documents. As part of our work, we reviewed samples of Third Party Draft and purchase card transactions.

Third Party Drafts listed on SFA's Reports – We judgmentally selected a sample of 57 drafts issued between October 1998 through February 2000 (FY99 and the first five months of FY00) from EDCAPS reports on SFA's Third Party Draft activity. Supporting documentation (copies of drafts, invoices, receipts, and purchase orders) were not available during fieldwork for 22 of the 57 drafts.

Third Party Drafts not listed on SFA's Reports – During our review of OPE, we determined that 16 of the drafts selected for our sample from EDCAPS reports on OPE's Third Party Draft activity were actually issued by SFA. The drafts were assigned organizational codes under OPE and thus appeared on OPE's EDCAPS reports rather than on SFA's EDCAPS reports. Supporting documentation (copies of drafts, invoices, receipts, and purchase orders) were not available during fieldwork for 3 of the 16 drafts.

Purchase Cards Statements – SFA has approximately 30 Headquarters cardholders and 40 Regional cardholders. As mentioned in the "Results" section of this report, Approving Officials were not receiving all of the monthly purchase card statements. The Approving Officials keep a copy of the monthly purchase card statements that they receive in their files. We inventoried purchase card statements located in the Approving Officials' files for six months: September 1999 (FY99) and November 1999 through March 2000 (FY00). We then compared our results to the Department's monthly purchase card bills in OCFO's files to determine which statements were missing from the Approving Officials' files. We limited our review to cardholders located at Headquarters. We identified 20 statements belonging to Headquarters cardholders that

had activity but were not in the Approving Officials' files. By the end of our fieldwork, SFA provided us with 14 of the 20 statements. Subsequent to our work in SFA we were provided with four of the six remaining statements which we did not include in the transaction sampling.

Purchase Card Transactions – We judgmentally selected 20 purchases from the purchase card statements originally in the Approving Official's files. In addition, we judgmentally selected 19 purchases and three credits from the 14 purchase card statements that were not originally in the Approving Officials' files but were produced during our fieldwork.

We based our conclusions about SFA's internal controls from information gathered during our interviews and transaction testing. We conducted our interviews and transaction testing between May 1, 2000 and August 25, 2000. We assessed SFA's internal controls based on GAO's *Standards for Internal Control in the Federal Government* issued November 1999. Attachment B to this memorandum contains a summary of the GAO Standards. We conducted our work in accordance with the President's Council on Integrity and Efficiency (PCIE) *Quality Standards for Inspections* dated March 1993.

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: Deputy Secretary

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.

Control Component	Deficiencies

Control Environment	• Overall — We identified significant noncompliance with current Department policies and procedures regarding purchase cards. While OCFO did not ensure that Approving Officials reviewed monthly purchase card statements, SFA was ultimately responsible for ensuring that transactions complied with laws and regulations. Review of the monthly purchase card statement as described in the Department's Directive on *Commercial Credit Card Service* would provide reasonable assurance that purchase card transactions comply with laws and regulations.
	
	• Assignment of Authority — The assignment of Approving Officials in SFA does not comply with the Department's Directive on *Commercial Credit Card Service*. OCFO's records of purchase cardholders list two Approving Officials and more than 70 cardholders. One Approving Official is the Executive Officer and the other is a cardholder. The Executive Officer serves as the Approving Official only for the other Approving Official/cardholder.
	  ✓ The assignment of one Approving Official does not comply with the Department's Directive, which states that "an Approving Official may not be a cardholder." In addition, the Approving Official/ cardholder is not at the managerial level required by the Directive. The Directive states: "The duties of the Approval Official shall not be delegated lower than an office head or service area director."
	  ✓ With OCFO's knowledge, part of the workload of the Approving Official/cardholder was given to another cardholder. This other cardholder also does not meet the requirements in the Directive for an Approving Official.
	  ✓ Even with their duties split, these individuals are responsible for more cardholders than most of the other Approving Officials in the Department.
	
	• Training — The Executive Officer, who has responsibility for procurement, has not taken formal procurement training. In addition, all procurement staff could benefit from refresher training.

Control Component	Deficiencies
Risk Assessment	• Identification of Risks — Currently, SFA has no formal procurement risk assessment procedures. In addition, the Executive Officer has not been involved with the Federal Managers' Financial Integrity Act (FMFIA) reporting process. • Identification of Risks — Some staff have been assigned moderate risk levels when their procurement responsibilities and authority suggest a higher risk level may be warranted.

Control Activities	• Policies and Procedures — Although required by the Department's Directive on *Commercial Credit Card Service*, SFA has no written purchase card policies and procedures.
	
	• Documentation — Files were not easily accessible to SFA staff as the files were in boxes from a prior office move. Some documentation was not available for review.
	
	• Purchase Cards
	  ✓ Incomplete review of monthly statements by Approving Officials.
	    ♦ The Approving Officials stated that many cardholders sent their statements directly to OCFO instead of forwarding the statements to them for review.
	    ♦ We inventoried purchase card statements for FY 99 (September 1999) and FY 00 (November 1999 through March 2000) located in the Approving Officials' files and compared our results to OCFO's monthly purchase card bills to determine which statements were missing from the Approving Officials' files. For any given month at least half of the statements with purchase card activity were missing from the Approving Officials' files.
	    ♦ Five of the six monthly statements of the cardholder with the largest monthly purchase balance were not in the Approving Officials' files. That cardholder's monthly balance was as high as $96,925.38.
	  ✓ Documentation — We requested SFA to obtain 20 statements belonging to Headquarters' cardholders that were not originally in the Approving Officials' files. SFA was able to obtain 14 of the statements prior to our finishing fieldwork on August 25, 2000. Subsequent to the completion of our fieldwork, we were provided with four of the six remaining statements.

Control Component	Deficiencies

	✓ Purchase Card Sharing — During our review of purchase card statements, we noted invoices where the name of the person ordering was not the cardholder. This situation may indicate that employees were sharing purchase cards. The Department's Directive states: "Each card has the cardholder's name embossed on it and may be used only by that person. No one else is authorized to use the card."
	
	• Purchase Card Transactions from Statements found in Approving Officials' Files — We reviewed 19 transactions judgmentally selected from statements in the Approving Officials' files.
	  ✓ Preapproval — Six of 19 transactions had written evidence that the purchase was approved by a supervisor before it was executed.
	  ✓ Documentation — One transaction was larger than the $2,500 micro purchase threshold. The FAR requires the solicitation of quotes or offers from a reasonable number of sources or sole-source justification for any purchase of more than $2,500. No documentation was available to verify that the purchase was made with the solicitation of at least three bids or a justification statement for a sole-source purchase.
	
	• Purchase Card Transactions from Statements Not Originally in Approving Officials' Files — We judgmentally selected 19 charges to review. No supporting documents (invoices, receipts or purchase orders) were attached for five of those transactions.
	  ✓ Preapproval — Of the 14 with documentation, four transactions had written evidence that the purchase was approved by a supervisor before it was executed.
	  ✓ Recording — EDCAPS transaction numbers were not listed on the card statements for three transactions. The three transactions were recorded on three different statements belonging to two cardholders.
	  ✓ Documentation — Nine transactions were larger than the $2,500 micro purchase threshold. The FAR requires the solicitation of quotes or offers from a reasonable number of sources or sole-source justification for any purchase of more than $2,500.
	    • One of those transactions was missing all supporting documents.
	    • Six others lacked documentation to verify that the purchase was made with the solicitation of at least three bids or a justification statement for a sole-source purchase.

Control Component	Deficiencies

	• Third Party Drafts listed on SFA's EDCAPS reports — We judgmentally selected 57 drafts to review. Files could not be found for 22 of the drafts during fieldwork. We were able to review supporting documentation for 35 drafts.
	  ✓ Preapproval — All but two transactions had written evidence that the purchase was approved by a supervisor before it was executed.
	  ✓ Date stamping — 18 invoices were not date stamped when received or paid.
	  ✓ Prompt payment — In 14 instances, invoices do not appear to have been paid timely as required by the Prompt Payment Act.
	  ✓ Documentation — In 8 instances, drafts did not have one of the following required documentation to verify purchase transactions: invoice, purchase order or packing slip.
	  ✓ Policy on use of drafts — The Department strongly encourages all principal offices to maximize purchase card use, because each card usage saves ED substantial processing costs as opposed to other payment mechanisms. In 22 instances, SFA may have been able to use the corporate purchase card, electronic fund transfer or Treasury checks instead of a draft.
	
	• Third Party Drafts listed on OPE's EDCAPS reports — During work in OPE, we selected 16 drafts from OPE's EDCAPS reports that were determined to be SFA drafts. Files could not be found for 3 of those drafts. We were able to review supporting documentation for 13 drafts.
	  ✓ Date stamping — 5 were missing date stamps.
	  ✓ Prompt payment — One invoice was marked "Past Due Notice."

Information & Communications	• Communication of Key Information — Only one member of the procurement staff that we interviewed was familiar with the Department's Directive on *Commercial Credit Card Service*. • Recordkeeping — The EDCAPS reports on OPE's Third Party Draft activity include drafts issued by SFA.
Monitoring	• On-going Monitoring — SFA managers do not periodically review drafts issued as required by the Department's *Third Party Draft Operating Procedures Manual* issued May 1999.