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Audit of Acquisition Card Use

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TABLE OF CONTENTS

SYNOPSIS.....	i
LIST OF ACRONYMS.....	ii
RESULTS IN BRIEF	1
INTRODUCTION.....	4
Objectives	4
Scope.....	4
Methodology	4
OBSERVATIONS AND RECOMMENDATIONS	5
Optimizing Acquisition Card Use	5
Policy, Controls and Compliance	13
RECOMMENDATIONS AND MANAGEMENT ACTION PLAN.....	19
ANNEX A—KEY CRITERIA	A-1
ANNEX B—RISK ASSESSMENT	B-1
ANNEX C—RESULTS OF COMPLIANCE TESTING	C-1



SYNOPSIS

This report presents the results of an assurance audit of acquisition card use within the Department of National Defence. In fiscal year 2004/05, acquisition cards were used for 350,000 transactions totalling approximately \$139 million. The purpose of the audit was to assess compliance with current policy requirements, to determine if opportunities exist for enhanced controls and to examine enablers and impediments to increased use.

While not always compliant with the letter of policy, users are taking a common sense approach to managing the cards and, for the most part, are compliant with the intent of policy. In some cases, policy requirements should be re-examined and/or stated more concisely.

Acquisition card providers offer preventive and detective controls as part of their acquisition card services. These controls are automated and can support both cardholders and resource centre managers in card monitoring. DND is currently not using these tools to full advantage, but rather continues to rely heavily on paper-based, manual approaches to monitoring. Increased use of automated tools would increase the efficiency and effectiveness of monitoring.

Potential savings associated with acquisition card use have been well documented in accounting literature. While the current level of acquisition card use within DND is consistent with other departments and with industry in general, increased use could conservatively result in savings (primarily efficiency gains) of \$11.9 million annually. However, in order to realize these gains, the procurement and payment processes associated with acquisition cards must be streamlined. In the course of this audit, many situations were observed where, although payment was by acquisition card, few efficiency gains were realized. In part, this is due to stove-piped approaches to procurement and payment, including non-integrated systems. Whether the acquisition card is considered a procurement or a payment tool, maximum efficiency gains will only occur if changes are made to streamline both portions of the process. Local practices, including financial coding approaches and documentation requirements, should be monitored to ensure they do not add unnecessary administration. Alternatives to acquisition card use—such as increased use of electronic data interchange (EDI) and/or consolidated billing—should also be considered as methods to increase payment efficiency.

Policies, procedures and methods of monitoring compliance must all emphasise economy and efficiency if the full benefits of acquisition card use are to be realized. Current departmental and government-wide initiatives, as documented in the report management action plan, will assist in this endeavour.



LIST OF ACRONYMS

ADM(Fin CS)	Assistant Deputy Minister (Finance and Corporate Services)
ADM(HR-Mil)	Assistant Deputy Minister (Human Resources–Military)
ADM(IM)	Assistant Deputy Minister (Information Management)
ADM(Mat)	Assistant Deputy Minister (Materiel)
CFSS	Canadian Forces Supply System
CRS	Chief Review Services
DND/CF	Department of National Defence/Canadian Forces
EDI	Electronic Data Interchange
ERP	Enterprise Resource Planning
FAA	<i>Financial Administration Act</i>
FAA Section 32	<i>Financial Administration Act</i> Section 32
FAA Section 33	<i>Financial Administration Act</i> Section 33
FAA Section 34	<i>Financial Administration Act</i> Section 34
FAM	Financial Administration Manual
FMAS	Financial and Managerial Accounting System
FY	Fiscal year
MASIS	Materiel Acquisition and Support Information System
NCR	National Capital Region
OGD	Other government department
PWGSC	Public Works and Government Services Canada
RC	Resource centre



RESULTS IN BRIEF

BACKGROUND

1. The Department of National Defence/Canadian Forces (DND/CF) has been using acquisition cards since 1995 in an effort to streamline purchasing and payment. Cardholders can acquire and pay for goods and services with a minimum of paperwork and delay. In the audited year, fiscal year (FY) 2004/05, this method of payment was used for 350,000 transactions totalling approximately \$139¹ million dollars.
2. To assist in ensuring control over these transactions, card-issuing companies have developed preventive and detective “Smart Controls.” These technology-enabled controls preclude acquisition card use under certain circumstances (preventive) or highlight unusual usage patterns (detective) and are more efficient and effective than traditional paper-based methods of oversight.

OVERALL ASSESSMENT

3. Increased use of acquisition cards within the Department could result in substantial savings. However, increased use alone will not ensure that the underlying objective of increased efficiency is achieved. Currently, many acquisition card transactions involve excessive administrative effort. As well, given current procurement processes and systems, converting to payment by acquisition card could increase rather than reduce administrative effort, in some cases.
4. While few of the 278 sampled transactions complied with a literal interpretation of current departmental acquisition card policy,² with few exceptions, controls in place appeared adequate to ensure acquisition cards were used only for intended purposes. To a large degree, departmental compliance reviews have focused on card administration rather than card management. Current controls rely heavily on traditional, paper-based methods of monitoring. These approaches are less efficient and effective than a control system that exploits electronic methods.

MAIN OBSERVATIONS

Optimizing the Use of Acquisition Cards

5. **Most departmental transactions are low-dollar value.** In FY 2004/05, 65 percent of departmental payment transactions³ were for amounts less than \$500. These transactions—over 930,000 in total—comprised only 1 percent of total dollars paid to vendors. Moreover, 92 percent of transactions were for amounts under \$5,000, but comprised only 8 percent of total dollars paid. A disproportionate amount of resources are spent administering these low-dollar value transactions.

¹ All dollars are Canadian, unless otherwise stated.

² Detailed sample results are included at Annex B.

³ Includes invoice and acquisition card transactions. Payments for taxis and airline flights have been excluded from the analysis as alternate payment methods exist for these commodities. As well, payments to other government departments through interdepartmental settlements have been excluded.



6. **Current acquisition card use.** While the Department's current level of use of acquisition cards is similar to other government departments and to industry in general, there is significant opportunity for increased use. In FY 2004/05, 30 percent of payments under \$500 were made using acquisition cards, while approximately 25 percent of payments under \$5,000 were made in this fashion.
7. **Potential savings through increased use.** Estimates of potential savings through acquisition card use range from as high as \$165⁴ per transaction to as low as \$0.43.⁵ The savings that can accrue are highly dependant on the current processes in place for both procurement and payment, and the degree to which these are modified through the introduction of acquisition cards. Using a conservative estimate of \$20 per transaction, savings of over \$9.8 million could accrue annually (primarily efficiency gains) by converting 50 percent of current purchases under \$5,000 from invoice/cheque to acquisition card. The Department receives rebates from the card-issuing banks based on the level of acquisition card spending. This increased level of acquisition card spending would increase the departmental rebate by \$2.1 million annually, resulting in total potential gains approaching \$12 million annually.
8. **Increasing efficiency of procurement/payment process.** The Department has established a target to reduce total invoices by 50 percent through the use of acquisition cards. Some units are using this target as a measure of performance. However, there is danger in focusing on the target rather than on the underlying objective of increased efficiency. Many situations were observed where, although acquisition cards are used, efficiency gains are not being fully realized. Many units are producing excess paperwork including purchase orders, and supplemental logs, as well as coding and re-coding these transactions in the departmental Financial and Managerial Accounting System (FMAS) and subsidiary systems. While departmental acquisition card policies and procedures have focused primarily on the payment process, full efficiency gains can only be realized if both procurement and payment processes are modified to accommodate the use of acquisition cards. Currently, when the Canadian Forces Supply System (CFSS) or Materiel Acquisition and Support Information System (MASIS) are used to initiate procurement, payment by acquisition card does not result in efficiency gains.
9. **Card optimization program.** Rather than establishing an across-the-board target to reduce invoices through the use of acquisition cards, the Department may be better served by a program that aims to optimize acquisition card use. Such a program would examine the current pockets of high-volume, low-dollar value invoice use and determine which payment method would result in the greatest savings. Such a program should consider the best fit for acquisition cards in an integrated procurement/payment process that includes CFSS and MASIS, as well as FMAS.

⁴ Morrison, Catherine. "Getting Credit." Summit 7,1 (February 2004): pp. 16-18.

⁵ Eggers, William. *Government 2.0: Using technology to improve education, cut red tape, reduce gridlock, and enhance democracy*. United States: Rowman & Littlefield Publishers, Inc., 2004.



Policy, Controls and Compliance

10. **Risk-appropriate policies.** Many reviews have documented high-levels of non-compliance with departmental acquisition card policy. In this audit, only 5 percent of sampled transactions were fully compliant with all aspects of departmental policy. However, this audit and others have found that while not always compliant with the letter of policy, users are taking a common sense approach to managing the cards and, for the most part, are in accordance with the intent of the policy. Complex and often unclear policies complicate compliance. In some cases, policy seems too restrictive given the low-risk, low-dollar value of these transactions. While a resource centre administrator may be assigned FAA Section 34 authority for invoices (including those of significant dollar value), FAA Section 34 certification for acquisition cards is currently restricted to resource centre (RC) managers—usually a director or a senior officer at a base or wing.

11. **Optimization of existing Smart Controls.** The acquisition card control framework is primarily paper-based, relying on supplemental transaction logs and manual certification of FAA Section 34. This type of control is labour-intensive and not well suited to a high-volume, low-dollar value area. Indeed, requiring much the same type of control for these low-value transactions as for transactions of much higher value may have diverted scarce resources from the review of items of greater significance.

12. Increased reliance should be placed on the preventive and detective Smart Controls already available through card-issuing banks. Rather than requiring RC managers to complete FAA Section 34 certification on each acquisition card transaction, they should be provided with tailored reports that highlight anomalies or potential areas of concern and that allow for more effective monitoring of card use. To date, departmental use of such control methods has been limited, in part because their utility has not been adequately communicated and because detective reports have not been made widely available in a user-friendly format.

OVERALL RECOMMENDATIONS

13. Instead of prescribed targets to reduce invoices through the use of acquisition cards, the Department should implement a program to optimize acquisition card use. Such a program should determine the most appropriate approach to acquisition card use in an integrated procurement/payment process. The program should ensure processes are streamlined, so the underlying objective of increased efficiency is realized. This will involve increasing vendor acceptance in some cases, and exploring alternate means of reducing invoices in others.

14. In addition, departmental policies and controls governing acquisition card use should be revisited to ensure they optimize the use of technology and are appropriate to the level of risk. Monitoring of these transactions must be completed in the most efficient and effective fashion so that review and management attention can be focused on areas of much greater financial significance.



INTRODUCTION

OBJECTIVES

- Consider the potential to increase acquisition card use and identify enablers or impediments.
- Assess whether acquisition cards are used in compliance with Treasury Board and departmental policies.
- Determine whether the existing internal control framework is sufficient to mitigate risk and whether there are opportunities for enhanced monitoring.
- The criteria used to assess these objectives can be found in Annex A.

SCOPE

- Acquisition card transactions during FY 2004/05: 350,000 transactions, \$139 million. Other FYs considered to determine usage trends.
- Invoices paid by cheque in FY 2004/05 for amounts less than \$5,000 were reviewed to determine viability of acquisition card payment.

METHODOLOGY

- Reviewed acquisition card compliance reports completed by other DND/CF groups including Environmental Review Units, ADM(HR-Mil), ADM(IM) and central and regional departmental accounting offices.
- Completed a *Risk Assessment of Acquisition Card Use* with input from various Level 1 staff (see Annex B) to identify controls and risk areas, and to support development of audit criteria.
- Interviewed staff involved in procurement and payment within DND/CF, several other government departments (OGDs), one large municipality, and the Office of the Inspector General.
- Informally surveyed OGDs regarding their current acquisition card usage.
- Selected three DND/CF sites (one in the National Capital Region (NCR) and two outside the NCR) for detailed review. One used acquisition cards for a high percentage of low-dollar value transactions in FY 2004/05; the other two used acquisition cards for only a small percentage of low-dollar value transactions.
- Reviewed 278 acquisition card transactions during site visits. Transactions were selected using random and directed sampling techniques, based on FMAS and card issuer information. Sample results are included in Annex C.
- Conducted four focus groups, comprising 53 participants in total. Participants included acquisition cardholders, RC managers, supply and finance staff. Two focus groups were held in the NCR and one at each of the visited sites outside the NCR.



OBSERVATIONS AND RECOMMENDATIONS

OPTIMIZING ACQUISITION CARD USE

Streamlining the procurement and payment processes for low-dollar value transactions through the use of acquisition cards can save time and money; however, care must be taken to ensure potential efficiency gains are actually realized.

Most departmental payments are low-dollar value.

Payment Value	# of Payments (000's)	% of Payments	Total \$'s (\$M)	% of Total \$'s
<\$500	935	65%	140	1%
\$500-\$5,000	394	27%	590	7%
>\$5,000	112	8%	8,046	92%

Figure 1

Source: FMAS FY 2004/05 Total \$8,776 million

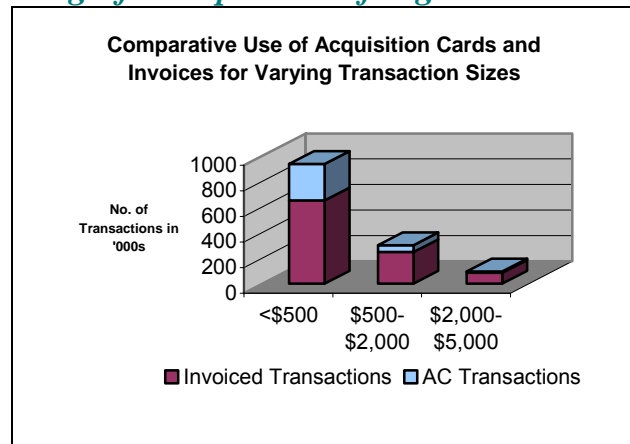
Acquisition card use is increasing slowly.

- As shown in Figure 1, in FY 2004/05 more than 935,000 payments⁶ to vendors were for amounts less than \$500.
 - These payments (under \$500) comprised 65 percent of transactions but only 1 percent of total payments to vendors.
 - Similarly, 92 percent of payments (1.3 million) were for amounts less than \$5,000, but comprised only 8 percent of the total dollars expended.
 - Streamlining the procurement and payment process for low-dollar value transactions will save time and money, and will allow departmental attention to be focused on those transactions with greatest financial impact.
-
- Acquisition cards were introduced within the Department for this purpose.
 - Usage of acquisition cards continues to increase, albeit slowly:
 - in FY 2003/04, 347,000 transactions with a total dollar value of \$129 million were completed using acquisition cards;
 - in FY 2004/05, this increased to 350,000 transactions and \$139 million—a less than 1 percent increase in transaction volume.
 - Most acquisition card purchases are low-dollar value:
 - in FY 2004/05, 81 percent and 92 percent of acquisition card transactions were for amounts less than \$500 and less than \$1,000 respectively.

⁶ Including both acquisition card payments and invoice payments. Payments for taxis and airline flights were removed from this analysis, as an alternate payment method has been put in place for these transactions.



While DND/CF's use of acquisition cards is comparable to other government departments and industry in general, there is significant potential for growth.



Source: FMAS FY 2004/05

Figure 2

Estimates of savings through acquisition card use vary widely.

- There is significant opportunity for increased acquisition card use.
- Figure 2 shows the relative use of acquisition cards and invoices for purchases under \$500; between \$500 and \$2,000; and between \$2,000 and \$5,000.
- The Department's use of acquisition cards is consistent with a 2003 survey of over 500 companies⁷
- Departmental usage rate for similar transactions is 27 percent and 8 percent, respectively.
- In an informal survey performed as part of this audit, other federal government departments indicated they used acquisition cards for between 11 percent and 37 percent of expenditures under \$5,000. DND/CF's usage rate of 25 percent for transactions of this size ranked third.⁸
- The savings achieved using acquisition cards depend greatly on the extent to which procurement/payment processes are modified when acquisition cards are introduced.
- Estimates of savings range from a high of \$165⁹ per transaction to a low of \$0.43.¹⁰
- TB suggests savings, on average, of \$66.42 per transaction based on costs of \$3.58¹¹ using an acquisition card versus \$70.00¹² for a traditional invoice/cheque transaction.

Severed under
Section
20(1)(b)(c)
of the AIA
Third Party
Information

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⁸ A February 2004 article in *Summit Magazine* (Morrison, Catherine. "Getting Credit." *Summit* 7,1 (February 2004): pp. 16-18) suggested that National Defence lagged significantly behind other departments in the use of acquisition cards. The Department ranked 7th, with only 1.93 percent of *expenses* paid by acquisition card. However, this may be an inappropriate measure of comparative use, given the impact of large, capital procurements on the Department's total spending. The same article indicated that National Defence had the largest total expenditures by acquisition card – approx \$110 million in FY 2001/02.

⁹ Morrison, Catherine. "Getting Credit." *Summit* 7,1 (February 2004): pp. 16-18.

¹⁰ Eggers, William. *Government 2.0: Using technology to improve education, cut red tape, reduce gridlock, and enhance democracy*. United States: Rowman & Littlefield Publishers, Inc., 2004.

¹¹ Canada. Treasury Board of Canada Secretariat. Report on Review of the Cost of Various Methods of Payments, January 20, 1998.

¹² C Fin O Comptrollers Conference, Acquisition Cards—Small Tools Big Returns, October 6, 2004.

Severed under
Section
20(1)(c)(d)
of the AIA
Third Party
Information



Increasing acquisition card usage could conservatively save DND/CF \$9.8 million annually and increase revenues by an additional \$2.1 million annually.

Further enablers are needed if targeted usage is to be achieved and efficiency maximized.

Acquisition card processes must be streamlined.

- In determining savings, acquisition card purchases are often compared to a centralized procurement model, where a requisition is raised, quotes obtained, and a purchase order issued regardless of the nature or size of the transaction.
- To a large degree, the Department, through the devolution process, has migrated from this model, in particular for low-dollar value purchases.
- As a result, a portion of the efficiency gains may have already been realized through a decentralized approach to procurement, regardless of the payment methodology employed.
- A 2002 United States Department of Defense study¹³ quotes savings of US\$20 per acquisition card transaction including rebates.
- Using an estimate of C\$20 (excluding rebate), the Department could potentially save over \$9.8 million annually (primarily efficiency gains) by converting 50 percent of current purchases under \$5,000 from invoice/cheque to acquisition card.¹⁴
- The Department receives rebates from card-issuing banks based on the level of acquisition card spending. The resultant \$264 million increase in acquisition card expenditures would increase the departmental rebate by approximately \$2.1 million annually.¹⁵
- Total savings from such an acquisition card optimization program could conservatively amount to \$11.9 million¹⁶ annually.
- ADM(Fin CS) has embarked on an Acquisition Card Revitalization Program.
- The target of this program is to reduce invoice transactions by 50 percent overall through the increased use of acquisition cards.¹⁷
- Some RC managers are using achievement of this target as a performance measure.
- However, if this target is to be achieved, and efficiency maximized in the process, several enablers must be put in place.
- In focus groups conducted as part of this audit, participants were asked to indicate their level of agreement with the statement:

“An acquisition card involves less work than a traditional invoice.”

¹³ Department of Defense Charge Card Task Force Final Report, June 27, 2002.

¹⁴ Based on FMAS FY 2004/05 data – 981,578 invoice transactions under \$5,000 x 50 percent x \$20 savings/transaction=\$9.8 million.

¹⁵ Using an average transaction value of \$538, and estimated bank rebate of 0.79 percent of expenditures.

¹⁶ \$9.8 million savings (primarily efficiency gains), and \$2.1 million additional revenue from bank rebates.

¹⁷ Weadon, Cmdre Bryn, DG Fin Mgmt. Memorandum “Acquisition Cards,” January 31, 2005.



Coding practices should be made more efficient.

- While 83 percent of RC managers agreed with the statement, only 56 percent of cardholders were in agreement.
- RC managers appear to believe that the acquisition card should generate savings, but cardholders do not necessarily see that it is more efficient in practice.
- Acquisition card transactions are input into FMAS using an electronic download from the issuing bank, based on default financial coding assigned when each card is issued.
- Rather than using default coding that is accurate for the majority of transactions, many groups are assigning the transactions to “clearing” accounts in order to provide increased visibility.
- Each transaction must then be manually re-coded to provide accurate management information.
- While it is not possible to determine total additional effort required as a result of this practice, it is not unreasonable to estimate that up to 25 percent of the nearly 350,000 annual acquisition card transactions require re-coding.
- Situations were observed where large volumes of acquisition card entries were re-coded to either add an internal order so that the charge could be tracked to a particular activity, or to code against an established commitment for budget monitoring purposes.
- Given the very low-dollar value of the majority of these transactions, it is questionable whether the alleged improvement in management information warrants this effort.
- Food Services groups are currently unaware that acquisition cards can be default coded as “tax exempt.”
- As a result they are reluctant to use the cards because of the additional effort required to ensure all food transactions are properly coded to exclude GST/HST.
- In FY 2004/05, more than 65,000 invoices for food products were paid, with an average value of \$1,350.

Paperwork should be minimized.

- The Financial Administration Manual (FAM) chapter on acquisition cards requires cardholders to maintain a register of their monthly acquisition card transactions.
- In one observed group, this register had evolved into a control sheet that was completed for each transaction and essentially duplicated all information that would be found on a local purchase order, thus negating some of the efficiency gains of using an acquisition card.



Focus on realizing efficiencies, not simply reducing invoices/cheques.

Must determine where acquisition cards fit in an integrated procurement/payment strategy.

- Another of the observed groups was making high use of acquisition cards, but with questionable overall efficiency gains:
 - they used a very centralized approach to purchasing, restricting the procurement of many goods, and all services to the Supply group;
 - the Supply group, based on an ADM(Mat) directive,¹⁸ documented each procurement in the CFSS system and produced a purchase order; and
 - the net effect was that additional time and additional paperwork were required.
- While achieving the target of reduced invoices/cheques, the underlying objective of streamlining the procurement/payment process was not fully achieved.
- The Department's acquisition card policy, championed by ADM(Fin CS), has focused on modifying the payment process. However, a large portion of the potential efficiency gains occur by streamlining procurement practices.
- Several departmental procurement initiatives seem to be at odds with increased acquisition card use. For example:
 - MASIS. In part to address the long-standing issue of stove-piped procurement and payment systems, the Department is widely implementing the MASIS system.
 - This system promises to provide the long sought link between procurement documents (including contracts) and subsequent payments.
 - The system will allow for acquisition card payment; however, high-volume users complain that reconciliation of the month-end acquisition card statement is more labour intensive than making payment by invoice/cheque.
 - As currently designed, there is concern that, using this system, payment by acquisition card may actually be less efficient than payment by cheque.
 - Information Technology Management System (ITMS). Telecom groups are recording cellular phone, pager, and personal data assistant expenses in a tailored system that allows them to monitor usage and track expenditures against contracts.
 - The system interfaces with FMAS to effect payment by cheque.
 - During FY 2004/05, approximately 4,000 invoices with an average value of \$144 were paid using ITMS.
 - As currently designed, payment by acquisition card would require additional effort.

¹⁸ Director Materiel Management and Distribution 003-Mandatory Use of the CFSS for Local Procurement, January 2004.



Contract value, as well as payment size must be considered in determining when to use acquisition card payment.

Effort should be placed on increasing cost-effective vendor acceptance.

Other methods of reducing the volume of invoices/cheques should be explored.

- In these cases, the advantages of payment by acquisition card must be examined.
- In the longer term, the Public Works and Government Services Canada (PWGSC) e-purchasing program¹⁹ may impact departmental procurement/payment practices. This program was developed to make buying easier overall, and to facilitate Internet purchasing using an acquisition card.
- However, this program will only be successful at achieving efficiencies if it is successfully integrated with other departmental procurement/payment strategies.
- In some cases, low-dollar value payments are made on high-dollar value contracts.
- For example, in FY 2004/05, 6,500 invoice payments under \$5,000—totalling \$14 million—were made to major van lines. In the same FY, an additional 6,000 invoice payments for amounts over \$5,000 were made to these companies—in total, \$60 million. Individual payments were as high as \$150,000.
- Using multiple payment methods to the same vendor, often against the same contract, will result in fragmented, incomplete information and will increase the risk of duplicate payments and over-expenditure of contracts.
- Several high-volume vendors currently do not accept acquisition card payments.
- In FY 2004/05, DND/CF made over 11,000 payments to providers of telecommunications landline services. These vendors currently do not accept acquisition card payment.
- In some cases, contractual terms must be adjusted to allow for acquisition card payment.
- Vendor banking charges should not be passed on to the Department, either directly through surcharges, or indirectly through increased prices.
- In the course of the audit, one standing offer was observed which included a surcharge of 2.5 percent on acquisition card payments.
- Such incremental charges, in particular on large dollar purchases, could quickly negate any gains through process efficiencies or rebates.
- Analysis of FY 2004/05 payments highlighted several categories of high-volume, low-dollar value invoice payments.
- A strategy to optimize efficiency should examine each of these categories to determine the most efficient procurement and payment method.

¹⁹ Canada. Public Works and Government Services Canada. E-Purchasing makes buying easier, November 2004.



Particular commodities could be targeted for mandatory acquisition card use.

- Fleet credit card payments. In FY 2004/05, over 7,000 fleet credit card payments were made—more than 60 percent of these were for amounts less than \$200.
 - In contrast to the acquisition card, these credit card payments are decentralized and, from a payment perspective, closely resemble a traditional invoice.
 - Moving to a centralized payment model, or adopting electronic data interchange (EDI) payment for these transactions, could significantly reduce the number of cheques and produce efficiencies.
 - Courier company payments. In FY 2004/05, courier companies submitted more than 12,000 invoices—5,000 of which were for amounts less than \$25. Approximately one-third were in the NCR.
 - EDI payment could be considered. Alternatively, if security warrants using a single pick-up/delivery point, consideration could be given to centrally funding these services.
 - Office Equipment/Rentals. Over 29,000 invoices for office equipment/rentals were observed, with an average cost of \$245. Again EDI and/or a consolidated billing approach could be considered.
-
- In FY 2004/05, more than 73,000 invoices with an average value of \$243 were for office supplies.
 - If devolved procurement is used, acquisition cards appear to be the most efficient payment tool.
 - Monitoring to ensure acquisition cards are used for such commodities could be readily accomplished.
 - Strategies must be put in place to ensure efficiencies are realized in the procurement/payment of low-dollar value items.
 - Whether the acquisition card is considered a procurement or a payment tool, maximum efficiency gains will only occur if changes are made to streamline both portions of the process.
 - For this reason, the combined efforts of ADM(Fin CS) and ADM(Mat) will be required.



An acquisition card “optimization” approach rather than a targeted reduction of invoices may be more effective in ensuring efficiencies are realized.

- The selected approach to acquisition card use must be well communicated, and adequately supported with training.
- Only 47 percent of participants in the focus groups felt they had received sufficient training to ensure the card was used in compliance with all departmental policies.
- Interviews and discussions established that using the card is straightforward; however, departmental and local contracting/purchasing requirements complicate its use.
- Using an optimization approach to increasing acquisition card use will increase the odds of achieving the underlying goal of savings rather than simply ensuring a usage target is achieved.

RECOMMENDATIONS

To ensure efficiency gains are realized through the use of acquisition cards, ADM(Fin CS) in consultation with ADM(Mat) must:

- ❖ **Ensure streamlined processes are implemented, including modifying interfaces where appropriate;**
- ❖ **Increase cost-effective vendor acceptance;**
- ❖ **Explore alternate means of reducing invoice volume in some cases; and**
- ❖ **Target particular commodity types for mandatory use.**



POLICY, CONTROLS AND COMPLIANCE

Policies have not been sufficiently adjusted to reflect the low-risk nature of the majority of acquisition card transactions. While not always compliant with the letter of policy, users are taking a common sense approach to managing the cards and, for the most part, are in accordance with the intent.

Compliance issues observed are not unique to acquisition cards.

- The results of 26 compliance reviews completed by wings/bases and headquarter staff between FY 2001/02 and FY 2004/05 were reviewed.
- These reviews documented a variety of issues including purchases made without contracting authority, missing documentation, missing or inappropriate FAA Section 34 certification, sole sourcing and contract splitting.
- The observations were consistent with our own review of 278 acquisition card transactions,²⁰ as well as the results of previous CRS audits.²¹
- Many of the reviews documented very high degrees of non-compliance with the “letter” of the departmental policy.
- In our transaction sample, there was only 5 percent compliance with a literal interpretation of departmental policies. However, we found that, in general, cardholders are using the card responsibly, and are compliant with the “intent” if not the letter of the policy. Compliance issues identified were most often related to poor administration, or to inappropriate or inconsistent policy interpretation.
- The types of issues observed are not unique to acquisition cards. Many of the compliance reports, as well as previous CRS audits, have documented similar issues with respect to other payment types.
- Concentrating a significant amount of review effort on these low-dollar value transactions may have diverted scarce departmental resources from the review of much more significant issues.
- In this and other audits, some staff expressed frustration that the same low-dollar value acquisition card transactions had been reviewed by up to three different groups.

²⁰ Detailed compliance results can be found in Annex C.

²¹ Previous CRS audit reports can be found at www.forces.gc.ca/crs.



Clarity of the acquisition card FAM could be improved.

- This is, in part, due to over-reliance on traditional controls, i.e., manual verification through FAA Section 34 and FAA Section 33, rather than increased development of Smart Controls.
- Individuals contributing to the risk assessment saw policy direction as outlined in the FAM as a key component of the acquisition card risk mitigation strategy.
- In any situation, a clear understanding of policy requirements is a precursor to ensuring compliance. However, only 34 percent of focus group participants agreed with the statement:

“Policies on the use of acquisition cards are easy to understand.”

- A significant portion of the current non-compliance can be attributed to policy that is unclear, or not well communicated.
- One visited organization had created its own standard operating procedure, including user-friendly policy clarification.
- This should help cardholders comply with requirements; however, having each base/wing complete such a document results in much duplication of effort and increases the risk of inconsistent interpretation among locations.

Current departmental FAA Section 34 requirements may be excessive.

- The current Acquisition Card FAM²² requires that only RC managers certify FAA Section 34 on monthly acquisition card statements, regardless of the fact that a resource centre administrator may have this authority for much higher value invoice payments.
- Treasury Board acquisition card policy does not include this restriction.
- In our acquisition card transaction sample, we found that where transactions had FAA Section 34 certification, individuals with FAA Section 34 authority for invoices only (i.e., not a RC manager) had signed 83 percent (134 of 162), while only 17 percent (28 of 162) had been certified by a RC manager.²³
- Fifty-eight percent of focus group participants were not aware that FAA Section 34 certification on acquisition cards was limited to the RC manager.
- Completing a detailed monthly review of acquisition cards transactions may not be the best use of a RC manager's time, in particular as these transactions represent less than 3 percent of total departmental spending.

²² FAM Chapter 1016-7-1 – Acquisition Cards, Date of Issue: July 27, 2004.

²³ Overall, FAA Section 34 certification by RC manager was confirmed for only 10 percent (28 of 278) sampled transactions. See Annex C for further details.



Policies are not sufficiently clear on the requirement for FAA Section 32 and contracting authority.

- Providing RC managers with tailored reports to monitor vendors used, commodities purchased, prices paid, etc. would be a more effective, efficient approach.
- Regardless of the payment method, both Treasury Board and departmental policies require that individuals purchasing items of any value have delegated contracting authority or specific pre-approval from an individual with this authority.
- This requirement is not well understood by RC managers and administrators, and is often not met for either low-dollar invoices or acquisition card purchases.
- Overall, 79 percent (220 of 278) of sampled transactions complied with this requirement; however, results varied by site from 35 percent to 97 percent.
- Often, RC managers intended cardholders to be able to make independent low-dollar procurement decisions; however, this intent had not been documented by delegating the appropriate contracting authority.
- Without some delegation of this authority, full potential efficiencies of acquisition card use cannot be realized.
- While most compliance reviews focused on the absence of contracting authority, there is similar confusion regarding cardholders' requirement for documented FAA Section 32²⁴ authority.
- The acquisition card FAM does not provide clear direction with respect to FAA Section 32 requirements.

²⁴ FAA Section 32 requires that funds be confirmed as available, and committed, before a contract is entered into or an item is purchased.



Multiple methods of recording financial authorities have created confusion.

- Currently, a cardholder's contracting authority and purchasing limitations, including commodity type and transaction size, are documented as part of the card application process.
- This can lead to confusion if the cardholder is also delegated authorities using the departmental Delegation of Authorities form.
- CRS audits have documented situations where the authorities and limitations documented for the same individual varied on the two forms.
- In addition, while the Delegation of Authorities form requires annual review and authorization by the current RC manager, no similar requirement exists for authorities delegated using the acquisition card application form.
- Several cardholders and their RC managers had no knowledge of the limitations or authorities that were documented on their card application form.
- Much of this confusion could be alleviated if, as other audits have suggested, the Delegation of Authorities form became the sole method for recording financial authorities.

Greater use of Smart Controls could be made.

- Treasury Board defines smart controls as "...effective controls that are less resource intensive."²⁵
- Previous CRS audits have recommended the development of smart controls, and the 1997 Office of the Auditor General report included a section on acquisition cards that asserted: "...increased use of electronic tools are needed to modernize controls over cards."²⁶
- Acquisition card providers offer preventive and detective smart controls as part of their acquisition card services.
- **Preventive controls.** Preventive controls are established when the cardholder applies for an acquisition card and are applied at the point of sale. The RC manager can select the controls to be applied to the card, including:
 - **Merchant Blocking**—Purchases cannot be made at blocked vendors. Using this control, a cardholder could be blocked from buying at vendors not listed on particular standing offers.
 - **Merchant Category Blocking**—To preclude using the card for travel purposes, for example, blocking could be established for all travel agencies.

²⁵ Canada. Treasury Board. *Internal Audit Planning Perspectives: Risks Facing the Delivery of Results for Canadians*, August 2001.

²⁶ Canada. Office of the Auditor General. *Report on Acquisition Cards*, April and October 1997.



DND usage rates of currently available preventive controls:

Smart Control Available	% of MasterCard with Smart Control Activated
Merchant Blocking	6%
Country Blocking	2%
Merchant Category Blocking	30%
Transaction Limits	30%
Credit Limits	100%
Cash Advances	100%

Figure 3

- Country Blocking—The card can be blocked for use outside of a specific country. If a cardholder does not travel or do any Internet purchasing, the card could be blocked for all countries except Canada.
 - Transaction Limits—The dollar limit for each transaction can be set. For example, a transaction limit of \$5,000 could be set to ensure proper contracting advice is sought for transactions larger than this amount.
 - Credit Limits—The maximum monthly spending allowed for each individual card can be set. All DND cards have established credit limits.
 - Cash Advances—Cash advances are available with the card. DND blocks all cards from being used for this purpose.
- Figure 3 shows the current preventive card controls available to DND/CF and their usage rate.
 - The Department could make more use of existing controls. As well, additional preventive controls could be explored, including limiting the number of daily or monthly transactions.
 - **Detective Controls.** Because some inappropriate transactions cannot be eliminated through the use of preventive controls, detective controls have also been developed.
 - Detective controls are applied after the fact and are used to highlight unusual transactions that may require follow-up.
 - Such controls can be developed by resource managers, card co-ordinators and/or post payment verification staff using the electronic monitoring systems provided by the banks as part of their acquisition card services.
 - Using these systems, tailored reports can be produced highlighting expenditures by specific cardholders or with specific merchants. Reports can also be produced that include information on potential contract splitting or any transactions that occurred at unusual times—weekends or holidays—for example.
 - The reports could be used to highlight areas where further monitoring is warranted.
 - Cardholders could also make use of the system to regularly verify charges against their account rather than verifying on a monthly basis, as is now occurring.
 - Where card numbers have been compromised, unauthorized transactions could be identified on a timelier basis.



Improved access to electronic monitoring systems is required.

- At the time of the audit, information in the bank-provided monitoring systems could be accessed at two levels: the individual card level or amalgamated at a base/department level. Only department/base card co-ordinators had access to this information.
- As designed, the monitoring reports were of limited use to individual managers, as they could not accumulate information on all acquisition card transactions against their budget.
- In December 2005, the Department completed the changes required to assign the cards to the appropriate cost centre for reporting purposes in the banking systems.
- ADM(Fin CS) now needs to extend access to the banks' monitoring systems to all RC managers.
- Reports should subsequently be tailored/enhanced based on feedback from RC managers.
- Acquisition cards are intended to streamline the procurement/payment process, thereby creating efficiency gains and savings.
- Part of the savings will accrue by implementing a monitoring and review process that is not only appropriate to the level of risk, but which relies heavily on technology-enabled tools.
- Traditional, paper-based and manual systems of monitoring, should be replaced by more efficient and effective preventive and detective controls.

RECOMMENDATIONS

Policies and controls governing acquisition card use should be revisited to ensure they optimize the use of technology and are reflective of the low-risk nature of these transactions. In particular:

- ❖ **ADM(Fin CS) (with input from ADM(Mat)) should clarify FAA Section 32, FAA Section 34, and FAA Section 33 requirements, along with the requirement for documented contracting authority, for acquisition card purchases and payments.**
- ❖ **ADM(Fin CS) should eliminate delegation of authorities from the cardholder application form, and use the departmental Delegation of Authorities form for this purpose.**
- ❖ **ADM(Fin CS) (with input from the regional departmental accounting officers) should strive to ensure full use is made of existing Smart Controls (both preventive and detective), and work to develop additional technology-enabled controls as appropriate.**



RECOMMENDATIONS AND MANAGEMENT ACTION PLAN

CRS Recommendation	OPI	Management Action
<p>To ensure efficiency gains are realized through the use of acquisition cards:</p> <ul style="list-style-type: none"> ▶ Ensure streamlined processes are implemented, including modifying information system interfaces where appropriate; ▶ Increase cost-effective vendor acceptance; ▶ Explore alternate means of reducing invoice volume in some cases; and ▶ Target particular commodity types for mandatory use. 	<p>ADM(Fin CS) in consultation with ADM(Mat)</p>	<p>The following two initiatives have been launched by ADM(Mat), with ADM(Fin CS) support, to streamline the acquisition and payment process:</p> <ul style="list-style-type: none"> • A common acquisition card solution is being investigated to replace the current complex interfaces between FMAS, MASIS and CFSS. As this work will need to be linked to the DND Single Enterprise Resource Planning (ERP) initiative, full implementation is not expected to occur until FY 2008/09 at the earliest. • The Defence Oversight Committee on Contracting has directed the establishment of a team to develop a standard procurement and payment instructional guide and training package. The team will initially focus on under \$5K local contract transactions. Promulgation is expected by March 2007. <p>This recommendation is partially being addressed via the PWGSC Way Forward, where the Commodity Teams are looking at using acquisition cards as the payment method for standing offers on common government equipment, as long as there is no surcharge for acquisition card use. Ultimately, this is a matter between vendors and their respective financial institution, and beyond DND's control.</p> <p>Adoption of EDI, currently in use in the private sector, offers the best potential for invoice volume reduction. While the number of EDI-enabled vendors is increasing, full implementation requires achievement of a single ERP environment. Consolidated billing may be possible for some commodities, especially in the IM/IT area where resources are being transferred to a single Level 1. The optimum method for invoice reduction in the short term remains increased acquisition card usage.</p> <p>Until such time as the necessary information system changes have been implemented, adoption of mandatory acquisition card use is not supported. Individual commodities are being addressed with PWGSC Way Forward—the mandatory use of Standing Offers—and will be considered on an individual basis.</p>



CRS Recommendation	OPI	Management Action
<p>Polices and controls governing acquisition card use should be revisited to ensure they exploit the use of technology and are risk appropriate. In particular:</p> <ul style="list-style-type: none"> ▶ Methods of meeting and documenting FAA Section 32, FAA Section 34, FAA Section 33, and Treasury Board contracting requirements should be re-examined and clarified; ▶ The departmental Delegation of Authorities form should be the exclusive method for recording assignment of these authorities; and ▶ Efforts should be taken to ensure existing preventive and detective Smart Controls are fully utilized; additional technology-enabled controls should be developed where appropriate. 	<p>ADM(Fin CS) in consultation with ADM(Mat)</p>	<p>The FAA and Treasury Board policy requirements have been reviewed and only one DND policy change is recommended. The FAA Section 34 certification of monthly statements will be modified by ADM(Fin CS) to enable any Section 34 holder (other than the acquisition card holder) to certify the statement vice only the RC manager. This policy change will be implemented as part of the change of the DND FAM's focus from acquisition card to payment card and is expected to be promulgated by March 2007.</p> <p>This recommendation is supported and is being implemented by ADM(Fin CS). A revised Delegation of Authorities form will be implemented prior to March 2007. In addition, a revised Request for a Standard Payment Card form will be implemented prior to March 2007 as part of the revised FAM chapters on payment cards.</p> <p>With the change in departmental card hierarchy, enhanced access to BMO Details-on-line is now possible. A comparable product is under development by the other card supplier. Cardholder awareness of these products and the Smart Controls they offer has been under way for the last year and will be continued. Adoption of additional technology-enabled controls will depend on product decisions by the card suppliers and are beyond DND's control.</p> <p><i>Auditor Note: While DND may not be able to influence controls developed by the card suppliers, the Department is in a position to develop additional detective controls on its own, using data in FMAS and from acquisition card providers.</i></p>



ANNEX A—KEY CRITERIA**INCREASING USE**

- ❖ Acquisition cards are used in the most efficient and effective manner.
- ❖ Maximum acquisition card use is supported and encouraged where appropriate.

COMPLIANCE

- ❖ Transactions are compliant with Treasury Board and departmental policies.
- ❖ Policies regarding acquisition card administration and usage are clear and understood.

INTERNAL CONTROL FRAMEWORK

- ❖ Mechanisms including Smart Controls are in place to identify and assess risk.
- ❖ A strategy is in place to address areas of risk for current and future growth of acquisition card use.



ANNEX B—RISK ASSESSMENT

Process	Key Risks	Exposure	Risk Level	Key Controls	Control Assessment	Residual Risk	Potential Controls
Authorization	Unauthorized individual is issued an acquisition card	The card is used for unauthorized purchases/no way of recovering card when person leaves	Low	RC manager must sign for each card issued/Gov't identification required when cards are re-issued	Inadequate—central or current list of RC managers does not exist, regional card coordinator does not always verify RC manager signature	Low	<ul style="list-style-type: none"> Central repository documenting RC managers in progress Annotation on personnel file
	Unauthorized individual uses acquisition card	Card is lost or stolen/staff are sharing cards/reduced accountability	Low	Cardholder is advised when card is issued not to allow anyone else to use it/RC manager monitors signatures when completing FAA Section 34/lost and stolen cards are reported immediately	Adequate—if FAA Section 34 is certified appropriately	Low	<ul style="list-style-type: none"> Increased training Allow administrators to complete FAA Section 34 certification Provide checklist to aid in certifying FAA Section 34 on acquisition card statements
	Cardholder makes purchases without contracting authority	Breach of Treasury Board/DND policies & guidelines/unauthorized purchase made	High	Spending limits on cards/FAA Section 34 review	Inadequate—requirement for delegated contracting authority is not clear, authorities are not clearly documented	High	<ul style="list-style-type: none"> Cardholders are given contracting authority consistent with transaction limit at time of card issue Annual review of acquisition card delegated authorities Increased training
	FAA Section 34 is inadequate and/or not completed by authorized individual	Breach of Treasury Board/DND policies & guidelines/unauthorized purchase made	High	Post-payment verification process	Inadequate	High	<ul style="list-style-type: none"> Implement electronic FAA Section 34 Allow administrators to certify FAA Section 34 Improve methods of monitoring FAA Section 34 certification Annual post payment verification for each unit
	Employee leaves position or transfers to another section and maintains acquisition card	Previous cost centre absorbing cost of different cost centre/unauthorized purchases made	Medium	RC manager requests card when employee leaves/RC manager monitors budget for unauthorized expenditures	Incomplete	Medium	<ul style="list-style-type: none"> Annotate cardholders personnel file Make card coordinators aware of all staff turnover



ANNEX B

Process	Key Risks	Exposure	Risk Level	Key Controls	Control Assessment	Residual Risk	Potential Controls
Credit Limits	Established credit limits exceeds monthly budget for acquisition cardholder or RC manager	Breach of Treasury Board/DND policies & guidelines/unauthorized purchases made/may result in expenditures in excess of budget	Low	FAA Section 34 review	Adequate—if FAA Section 34 is certified appropriately	Low	<ul style="list-style-type: none"> Initial credit limits are established considering available budget Monthly credit limits are reviewed and adjusted on an annual basis to reflect use Transaction limit reflects contracting authority
	Transactions split to meet transaction limit	Breach of Treasury Board/DND policies & guidelines/unauthorized purchases	Medium	FAA Section 34 review/ monthly credit limit	Adequate—if FAA Section 34 is certified appropriately	Low	<ul style="list-style-type: none"> Contract splitting report
	Dormant/inactive cards	Loss or theft of card/unauthorized purchase when used	Low	Policy on cards security	Inadequate	Low	<ul style="list-style-type: none"> Annual review of card usage Restricted credit limits for cards not used regularly
Purchases	Individual makes personal purchases using card	Breach of Treasury Board/DND policies & guidelines	Medium	FAA Section 34 review/ transaction limit/monthly credit limit	Adequate—if FAA Section 34 is certified appropriately	Low	<ul style="list-style-type: none"> Increase use of preventive controls Allow administrators to certify FAA Section 34 Enforce consequences of improper card use
	Quotes are not obtained where required	May not get best price	Medium	FAA Section 34 review/ purchase log	Adequate—if FAA Section 34 is certified appropriately	Low	<ul style="list-style-type: none"> Do not restrict FAA Section 34 to RC manager Mandatory use of standing offers Increased training
	Item purchased is coded incorrectly in the general ledger	Breach of Treasury Board/DND policies & guidelines/reduced accuracy of management information	Low	FAA Section 34 review/ purchase log	Adequate—if FAA Section 34 is certified appropriately	Low	<ul style="list-style-type: none"> Prohibit the use of clearing accounts Streamline general ledger accounts



ANNEX C—RESULTS OF COMPLIANCE TESTING

278 transactions were selected for review, using both random and directed selection techniques.

	Site 1			Site 2			Site 3			TOTAL		
	Compliant	Non-Compliant	Not Confirmed*	Compliant	Non-Compliant	Not Confirmed	Compliant	Non-Compliant	Not Confirmed	Compliant	Non-Compliant	Not Confirmed
FAA Section 34 By RC Manager***	9	133	4	4	70	2	15	41	0	28	244	6
FAA Section 34 By person with Delegated Authority	69	14	63**	63	11	2	30	11	15	162	36	80**
Contracting Authority Documented	142	0	4	27	48	1	51	0	5	220	48	10
Receipts Attached	140	2	4	70	2	4	56	0	0	266	4	8
Approved Item for AC Purchase	142	0	4	70	2	4	56	0	0	268	2	8
PST Not Paid	142	0	4	67	4	5	54	2	0	263	6	9
Transaction Log Maintained****	53	81	12	55	17	4	15	0	41	123	98	57
Appropriate Financial Coding	141	1	4	68	4	4	53	3	0	262	8	8
Fully Compliant with departmental policy	1	-	-	0	-	-	12	-	-	13	-	-

* Not Confirmed: These criteria could not be confirmed as not all documentation was made available, e.g., cardholder posted or on leave, transaction log not available. No documentation could be found for eight of the selected documents. (Site visits were completed in June/July 2005 during active posting and vacation season).

** At Site 1, one cardholder completed 58 of the selected transactions. Each individual transaction had been certified FAA Section 34 (on supporting documentation) by an authorized individual; however, no documented delegation of authority for FAA Section 34 was provided by local comptroller for the individual signing the monthly statement.

*** Departmental policy requirement, not stipulated in Treasury Board policy.

**** The policy requirement to maintain an acquisition card register has been interpreted by review groups to require that a detailed supplemental log of all transactions be maintained.

