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# Program and Management Audit of the State's Purchasing Card Program

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A Report to the  
Governor  
and the  
Legislature of  
the State of  
Hawai'i

Report No. 10-05  
June 2010



**THE AUDITOR**  
STATE OF HAWAII

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## Office of the Auditor

The missions of the Office of the Auditor are assigned by the Hawai'i State Constitution (Article VII, Section 10). The primary mission is to conduct post audits of the transactions, accounts, programs, and performance of public agencies. A supplemental mission is to conduct such other investigations and prepare such additional reports as may be directed by the Legislature.

Under its assigned missions, the office conducts the following types of examinations:

1. Financial audits attest to the fairness of the financial statements of agencies. They examine the adequacy of the financial records and accounting and internal controls, and they determine the legality and propriety of expenditures.
2. Management audits, which are also referred to as performance audits, examine the effectiveness of programs or the efficiency of agencies or both. These audits are also called program audits, when they focus on whether programs are attaining the objectives and results expected of them, and operations audits, when they examine how well agencies are organized and managed and how efficiently they acquire and utilize resources.
3. Sunset evaluations evaluate new professional and occupational licensing programs to determine whether the programs should be terminated, continued, or modified. These evaluations are conducted in accordance with criteria established by statute.
4. Sunrise analyses are similar to sunset evaluations, but they apply to proposed rather than existing regulatory programs. Before a new professional and occupational licensing program can be enacted, the statutes require that the measure be analyzed by the Office of the Auditor as to its probable effects.
5. Health insurance analyses examine bills that propose to mandate certain health insurance benefits. Such bills cannot be enacted unless they are referred to the Office of the Auditor for an assessment of the social and financial impact of the proposed measure.
6. Analyses of proposed special funds and existing trust and revolving funds determine if proposals to establish these funds are existing funds meet legislative criteria.
7. Procurement compliance audits and other procurement-related monitoring assist the Legislature in overseeing government procurement practices.
8. Fiscal accountability reports analyze expenditures by the state Department of Education in various areas.
9. Special studies respond to requests from both houses of the Legislature. The studies usually address specific problems for which the Legislature is seeking solutions.

Hawai'i's laws provide the Auditor with broad powers to examine all books, records, files, papers, and documents and all financial affairs of every agency. The Auditor also has the authority to summon persons to produce records and to question persons under oath. However, the Office of the Auditor exercises no control function, and its authority is limited to reviewing, evaluating, and reporting on its findings and recommendations to the Legislature and the Governor.



### THE AUDITOR

STATE OF HAWAII

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# OVERVIEW

## ***Program and Management Audit of the State's Purchasing Card Program***

Report No. 10-05, June 2010

### **Summary**

In 2001, the State Procurement Office (SPO) established its Procurement Card Program (pCard program). As defined by law, a *procurement card*, commonly referred to as a *purchasing card*, *pCard*, or *charge card*, is a limited credit card to be used by government agencies in place of cash or purchase orders for the acquisition of goods, services, or construction. The pCard program was meant to simplify the State's small purchase operations and reduce the administrative burden associated with issuing purchase orders and processing invoices for payment without sacrificing controls. As of April 1, 2005, executive branch agencies were required to use pCards to pay for goods and services under \$2,500.

Our program and management audit of the SPO's Purchasing Card Program focused on the procurement of goods and services by executive branch agencies using pCards from July 2008 to October 2009. We focused on the three executive branch agencies with the highest number of pCard transactions and largest dollar volume of pCard expenditures for the period audited: the Departments of Health (DOH), Human Services (DHS), and Transportation (DOT). In the case of DOT, we focused on two of its four divisions—Administration and Highways.

We found that the pCard program has had some benefits: vendors get paid sooner, cardholders receive their goods and services faster, and the State receives a rebate. However, other benefits, including a more efficient and streamlined government procurement system, have not been achieved. Although the procurement office is ultimately responsible for the program, it has taken a hands-off approach to administering the program by delegating significant responsibilities to the executive departments.

We found that the procurement office has failed to adequately establish and evaluate goals and objectives and meaningful performance measures for the pCard program. In addition, the SPO does not properly evaluate and monitor the program's performance nor has it implemented an effective system for sharing innovations and experiences. Until the SPO becomes more proactive, it will not recognize and address the problems and concerns facing executive departments and cannot make program improvements to realize the full potential of the pCard program.

We also found that the executive branch agencies' current card programs lack streamlined procedures that could save time and money. Lacking guidance from the procurement office, the DOH, DHS, and DOT structured their pCard process to closely mirror that of the purchase order process. We found that the pCard process had more steps than the cumbersome purchase order process, thereby negating administrative efficiencies the program was intended to provide.



Further, the SPO cannot identify where nor quantify how much savings the program has achieved. And finally, staff from the three executive departments we tested could not say that the benefits of the program outweighed the administrative burdens associated with the program.

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## Recommendations and Response

We recommended the procurement office assume a more hands-on approach and play a stronger role as the administrator by ensuring that the intent of the pCard program is being met. We also made specific recommendations for the procurement office to perform a re-engineering effort by formulating and adopting clear guidance that will help the executive branch agencies in achieving consistency and efficiency.

In its response to our draft report, the State Procurement Office claimed that our report contains many misstatements and fails to take into account the limited resources available. Although the SPO provided extensive comments to refute our findings, the SPO acknowledged that there may be more that the pCard program can do for the State and counties. The SPO also stated that it has focused more on internal controls, which supports our findings that it has lost sight of what the pCard program was designed to do. Thus, the pCard program has not realized its potential for efficiency. A perceived shortage of resources does not relieve the SPO of these responsibilities. The SPO acknowledged our recommendations but stated that the recommendations have already been accomplished or it sees no merit in complying. We stand by the findings and conclusions in our report.

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Submitted by

**THE AUDITOR**  
STATE OF HAWAI'I

Report No. 10-05  
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## Foreword

This report was prepared pursuant to Section 23-4, Hawai‘i Revised Statutes, which requires the State Auditor to conduct post audits of the transactions, accounts, programs, and performance of all departments, offices, and agencies of the State of Hawai‘i and its political subdivisions. Additionally, Section 103D-107, HRS, Hawai‘i Public Procurement Code, establishes a procurement compliance audit unit within the Office of the Auditor to review and assess methods of procurement in use in other jurisdictions, and those proposed to determine whether they promote fairness, efficiency, and accountability within the process.

We wish to express our appreciation for the cooperation and assistance extended to us by the director and staff of the State Procurement Office, the Departments of Health, Human Services, and Transportation, and others whom we contacted during the course of the audit.

Marion M. Higa  
State Auditor

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# Chapter 1

## Introduction

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This is a self-initiated audit of the State's Purchasing Card Program, undertaken pursuant to Section 23-4, Hawai'i Revised Statutes (HRS). Section 23-4 requires the State Auditor to conduct post audits of the transactions, accounts, programs, and performance of all departments, offices, and agencies of the State of Hawai'i and its political subdivisions. Additionally, Section 103D-107, HRS of the *Hawai'i Public Procurement Code* (the Code) creates a compliance audit unit within the Office of the Auditor to periodically review and audit the State's procurement practices to ensure compliance with the Code and its rules and to advocate competition, fairness, and accountability in the State's procurement process.

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## Background

In 2001, the State of Hawai'i's State Procurement Office (SPO) established the Purchasing Card Program (pCard program) to economically streamline government procurement. The pCard program was intended to help the State simplify the procurement of small purchases and provide a more timely and efficient system of purchasing and paying for goods and services. The program was to reduce the administrative burden associated with issuing purchase orders and processing invoices for payment without sacrificing controls over safeguarding assets and preventing and detecting errors and fraud. Section 103D-104, HRS, defines a "*procurement card*," commonly referred to as a "*purchasing card*," "*pCard*," or "*charge card*," as a limited credit card to be used by government agencies in place of cash or purchase orders for the acquisition of goods, services, or construction.

In January 2002, the State of Hawai'i contracted with First Hawaiian Bank (FHB) to provide, implement, and support a pCard program. Although the agreement was renewed through February 28, 2010, with a final renewal to 2012, on March 23, 2009 the SPO put out a request for proposals (RFP) for a contractor for the pCard program. The SPO administrator indicated that although procurement officials are happy with FHB's performance, they wanted to find out if there was a better administrator available.

As of April 1, 2005, executive branch agencies were required by the comptroller to use pCards instead of purchase orders to pay for goods and services under \$2,500. Agencies could, however, use the pCard for purchases above \$2,500 if they chose.

## **Organization**

Statewide procurement is governed by the Hawai'i Public Procurement Code and the State Procurement Office. Together they provide a central authority for procurement rules and procedures for all governmental bodies in the State.

### **Hawai'i Public Procurement Code**

Chapter 103D, HRS, *Hawai'i Public Procurement Code*, is based on the American Bar Association's Model Procurement Code and applies to the procurement of goods and services by governmental bodies solicited or entered into from July 1, 1994. Chapter 103F, HRS governs the procurement of health and human services. Chapters 3-120 and 3-143, Hawai'i Administrative Rules (HAR) implement Chapters 103D and 103F, HRS, respectively.

### **State Procurement Policy Board**

The procurement code creates an autonomous, seven-person State Procurement Policy Board assigned to the Department of Accounting and General Services (DAGS) for administrative purposes. The policy board has the authority and responsibility to consider and decide matters of policy and to adopt rules consistent with the procurement code that govern the procurement, management, control, and disposal of goods, services, and construction.

### **State Procurement Office**

Chapter 103D, HRS also established the State Procurement Office, which is administratively attached to DAGS. The SPO is the central authority on procurement statutes and rules for all governmental bodies of the State and its counties. The administrator of the office is designated as the chief procurement officer for all executive branch agencies. In addition to his duties as the State's chief procurement officer, the administrator must also:

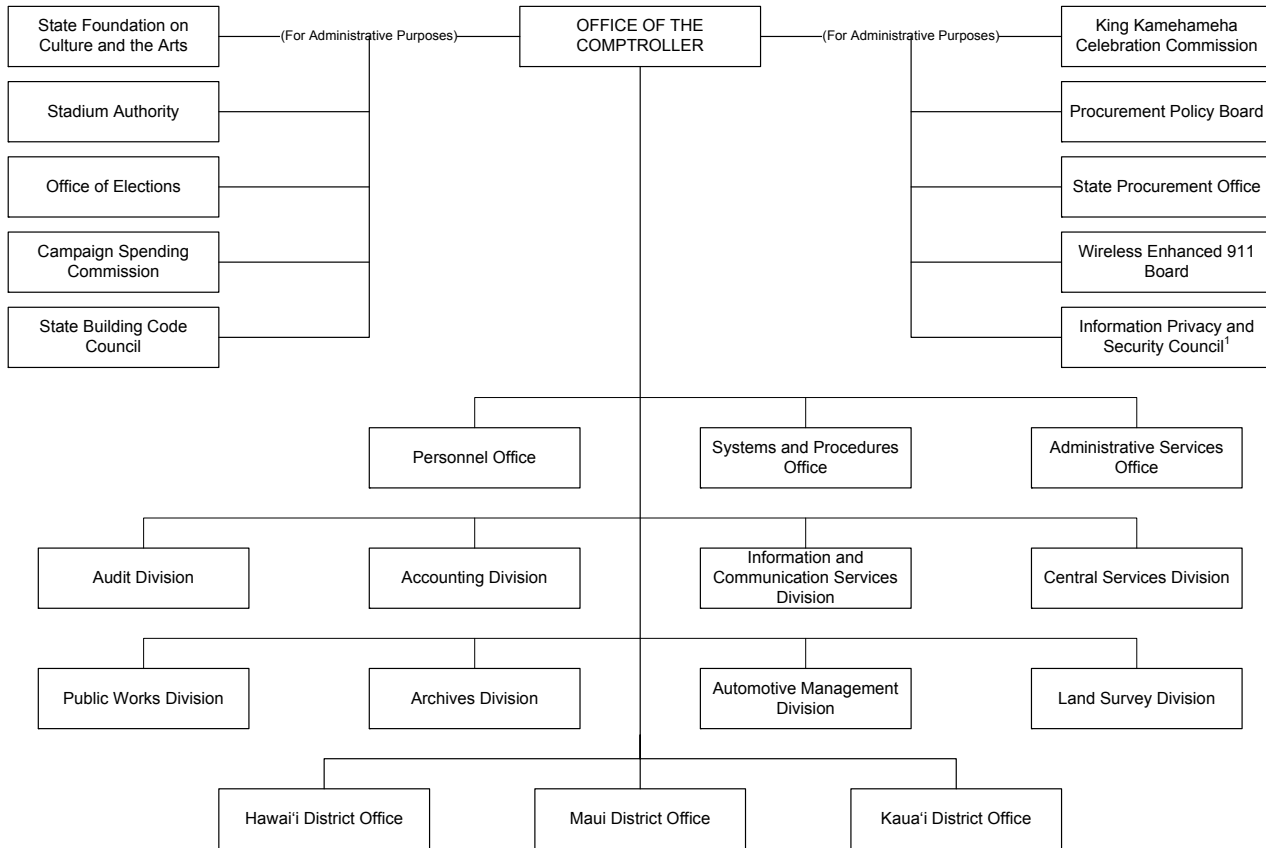
- periodically review the procurement practices of all governmental bodies;
- assist, advise, and guide governmental bodies in matters regarding procurement;
- develop and administer a statewide procurement orientation and training program; and
- develop, distribute, and maintain a procurement manual for state procurement officials and a guide for vendors wishing to do business with the State.

### **Chief procurement officers**

In addition to the State's chief procurement officer, the Code also identifies chief procurement officers (CPOs) throughout the state who carry out procurement functions in their respective jurisdictions. Within each jurisdiction, a chief procurement officer must procure or supervise the procurement of all goods, services, and construction; exercise general supervision and control over all inventories of goods; sell, trade, or otherwise dispose of surplus goods; and establish and maintain programs for the inspection, testing, and acceptance of goods, services, and construction.

Exhibits 1.1 and 1.2 display the Department of Accounting and General Services and the State Procurement Office's organizational structure.

**Exhibit 1.1**  
**Department of Accounting and General Services Organization Chart**

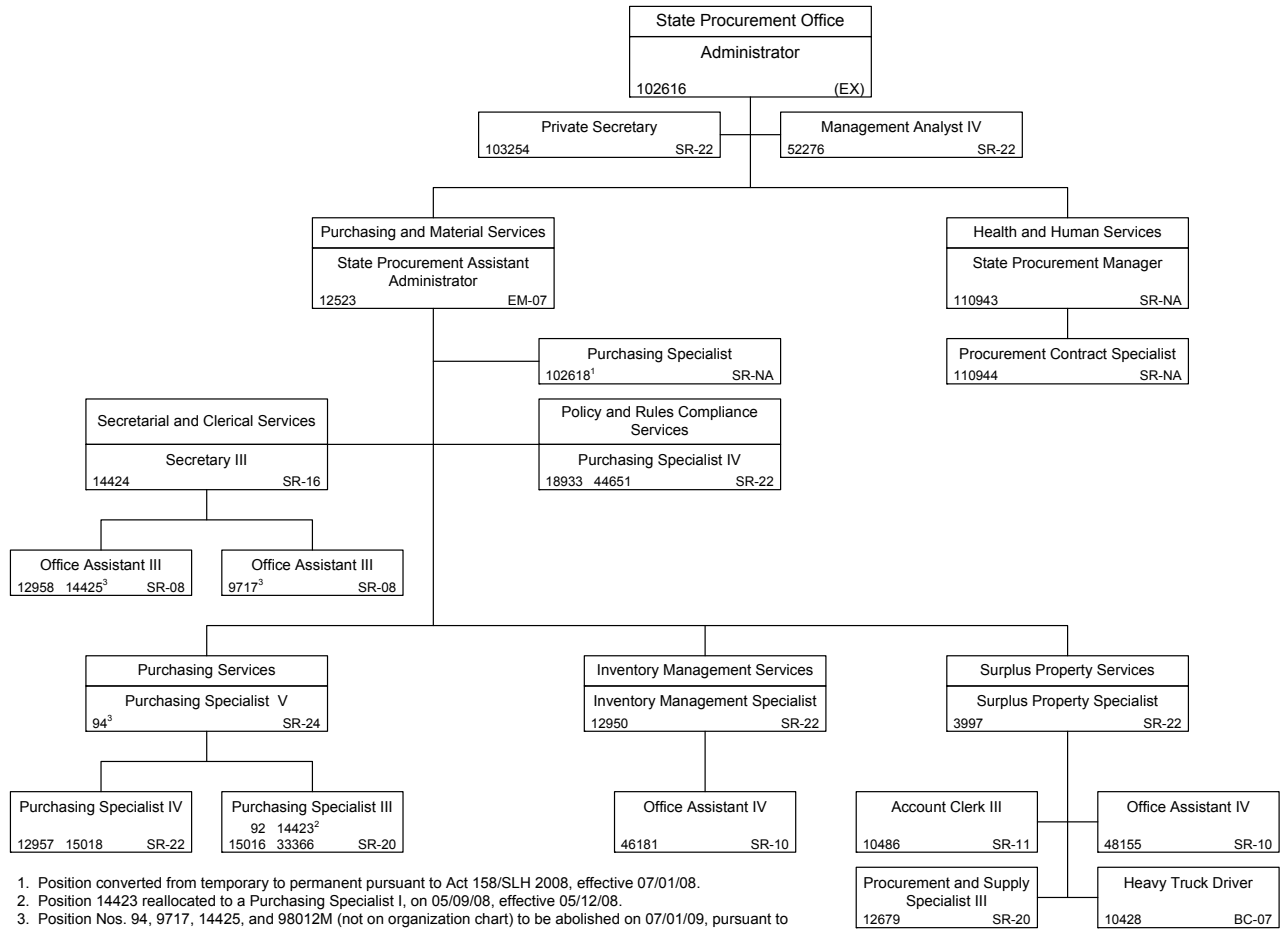


1. Information Privacy and Security Council authorized by Act 10, 2008 Special Session.

06/30/09

Source: State Procurement Office

**Exhibit 1.2  
State Procurement Office Organization Chart**



1. Position converted from temporary to permanent pursuant to Act 158/SLH 2008, effective 07/01/08.  
 2. Position 14423 reallocated to a Purchasing Specialist I, on 05/09/08, effective 05/12/08.  
 3. Position Nos. 94, 9717, 14425, and 98012M (not on organization chart) to be abolished on 07/01/09, pursuant to Act 162/SLH 2009.

06/30/09

Source: State Procurement Office

### ***Small purchase procurement structure***

The Hawai‘i Public Procurement Code establishes six procurement methods governmental bodies may use. One method is referred to as “small purchase procurement.”

Under Section 103D-305, HRS, and Chapter 3-122, HAR, “small purchases” are those of less than \$50,000 for goods, services, or construction. Procurements must be made according to rules adopted by the policy board to ensure administrative simplicity and as much competition as practicable. Expenditures of under \$5,000 must be made using procedures established by each chief procurement officer. For expenditures of \$5,000 to \$14,999.99, at least three quotes must be solicited; for expenditures of \$15,000 to \$24,999.99, at least three written quotes must be obtained. For expenditures of \$25,000 to \$49,999.99, procurements must be made through the Hawai‘i Electronic Procurement System (HePS), which issues solicitations, receives responses, and posts notices of awards.

As of July 1, 2012, the “small purchase” threshold for goods and services will be \$100,000 and for construction will be \$250,000. Procurements of under \$5,000 are recommended to be made using “adequate and reasonable competition.” For expenditures of \$5,000 to \$14,999.99, at least three quotes must be obtained. Procurements of \$15,000 to \$100,000 are to be made using HePS.

### **Payment methods**

Executive branch agencies may use one of three methods to pay for goods, services, and construction: 1) via a check requested from and processed by DAGS; 2) via a pCard issued to authorized personnel; or 3) via petty cash held by each agency. Checks processed by DAGS must be accompanied by a summary warrant voucher, a purchase order, and other supporting documentation (i.e., an invoice). DAGS then prepares a check and forwards it to the vendor. The Purchasing Card Program, managed by the SPO, makes use of pCards in the same way a major credit card would be used. Petty cash payments are limited to single disbursements of less than \$100 each.

### **Purchase orders**

Purchase orders are documents authorizing the delivery of and payment for specified merchandise or services. A purchase order records the authorization for a purchase, availability of funds, reservation of funds for the current month or quarter, and proves to the vendor the State’s commitment to acquire the goods, services, or construction. Exhibit 1.3 displays a purchase order form.



## pCards

The pCard, which is similar to a credit card, is designed to streamline the state and county governments' small purchase payment process. The pCard program was established to replace the laborious and costly purchase order system by allowing employees to charge small purchases without having to prepare a purchase order and process an invoice for payment. pCards belong to the government but are issued to responsible employees to make official purchases. The program is designed to improve management controls, provide expenditure data, increase purchasing efficiency, and allow payment to vendors by the card issuer generally within a few days of the purchase.

The State's pCard vendor, First Hawaiian Bank, uses the Pro Value Services (PVS) Net software for transaction review, reporting, accounting, and card management. The internet-based PVS Net system allows users to review and report on pCard transactions. The State is currently upgrading to the CentreSuite system, an internet-based platform that will allow users to perform real-time reporting and transaction management functions online. First Hawaiian Bank also offers the Enhanced Merchant Reporting (EMR) system, which provides online reporting tools for tracking purchasing card spending data.

As noted in the State's agreement with FHB, the Executive Branch, Judiciary, Senate, Office of Hawaiian Affairs, Department of Education, Counties of Hawai'i, Maui, and Kaua'i, Honolulu City Council, County Councils of Hawai'i, Maui, and Kaua'i, Honolulu Board of Water Supply, Maui Department of Water Supply, Kaua'i Department of Water, and Hawai'i Health Systems Corporation all agreed to participate in the SPO's pCard program. The University of Hawai'i did not participate as it already had a pCard-type of program in place.

The SPO administers the contract with FHB and manages the overall state program by providing guidance and training to relevant employees. It has authority to direct the executive branch agencies in the use of the pCard, but not other jurisdictions (such as the Judiciary and counties). The other jurisdictions are responsible for their own pCard programs.

According to the SPO, the pCard program has numerous advantages. It can:

- Eliminate purchase orders and processing of individual invoices;
- Eliminate individual checks to vendors—all of an agency's payments are made via one monthly check to the financial institution (in this case, FHB), similar to paying a credit card bill;



- Increase efficiency for the state and business community;
- Reduce expenses (a purchase order costs between \$100 and \$150 to process);
- Improve efficiency—80 percent of checks generated represent 20 percent of all expenditures;
- Significantly reduce late payment fees to vendors;
- Increase employees' available time for core activities;
- Expedite payment to vendors to within three days instead of 30 days;
- Decrease costs by eliminating invoicing, accounts receivables, and deposits; and
- Eliminate credit risk to businesses.

### **Responsibilities**

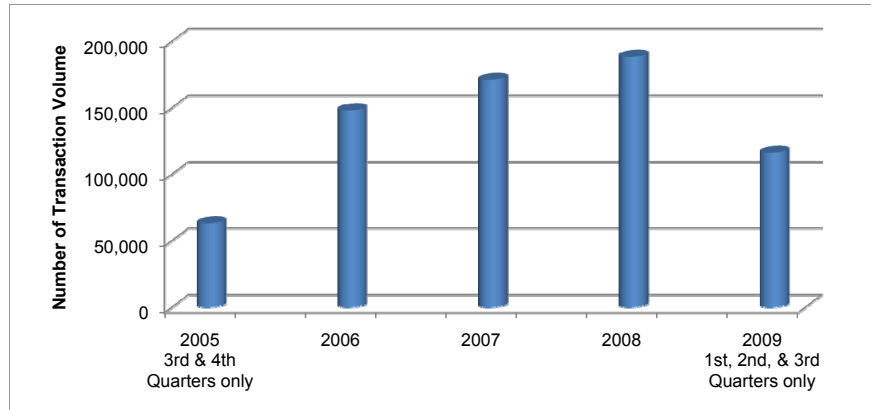
The purchasing card administrator of each executive branch agency serves as that agency's primary administrator for the pCard program. Each administrator's duties include developing purchasing card procedures for their agency, approving cardholder agreements, and coordinating training pCard users.

The CentreSuite administrator, who may be the same as the pCard administrator, is responsible for the daily pCard duties within each executive branch agency. This work can be divided among employees, branches, or offices and includes reviewing pCard transactions for proper use.

Each cardholder must ensure that his or her pCard is used in accordance with the pCard program's policies and procedures. Cardholders are accountable for all charges made to their pCards.

Exhibit 1.4 summarizes the executive branch agencies' pCard use by number of transactions for the period July 2005 through September 2009.

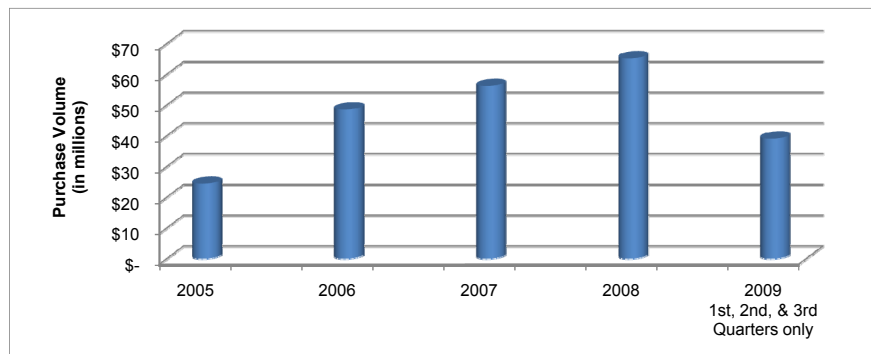
**Exhibit 1.4**  
**Executive Branch Agencies' pCard Use by Number of Transactions, July 2005 – September 2009**



Source: Office of the Auditor. Data obtained from First Hawaiian Bank and the State Procurement Office quarterly reports.

Exhibit 1.5 displays the executive branch agencies' pCard use by dollar amount of expenditures for the period January 2005 through September 2009.

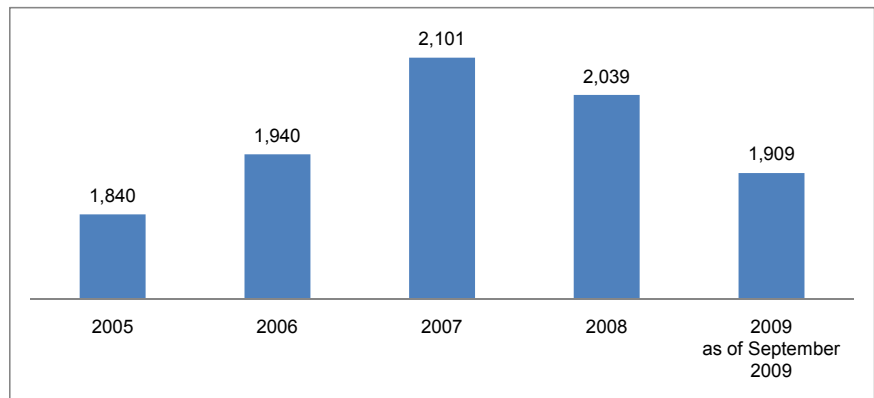
**Exhibit 1.5**  
**Executive Branch Agencies' pCard Use by Purchase Volume, January 2005 – September 2009**



Source: Office of the Auditor. Data obtained from First Hawaiian Bank and the State Procurement Office quarterly reports.

Exhibit 1.6 shows the executive branch agencies' number of pCard holders for 2005 through September 2009.

**Exhibit 1.6**  
**Executive Branch Agencies' Number of pCard Holders, 2005 – September 2009**

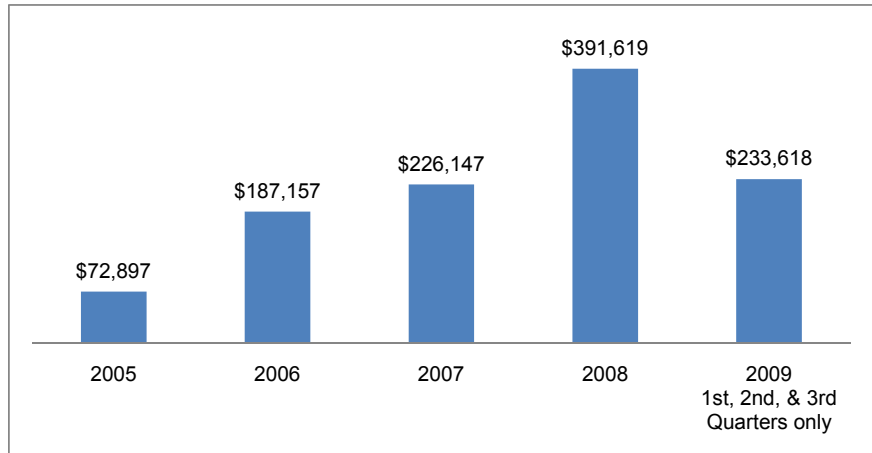


Source: Office of the Auditor. Data obtained from First Hawaiian Bank and the State Procurement Office quarterly reports.

### Rebate program

The pCard program as administered by FHB includes a cash incentive program that pays quarterly cash rebates to the State based on the combined net purchases volume for all agencies. The rebates are treated as revenue to the State, so general-funded programs are required to deposit their rebate checks into the general fund. Non-general fund programs must comply with applicable statutory requirements. Exhibit 1.7 illustrates the growth of the rebate program for the period 2005 through September 2009.

**Exhibit 1.7  
Executive Branch Rebate Program, January 2005 -  
September 2009**

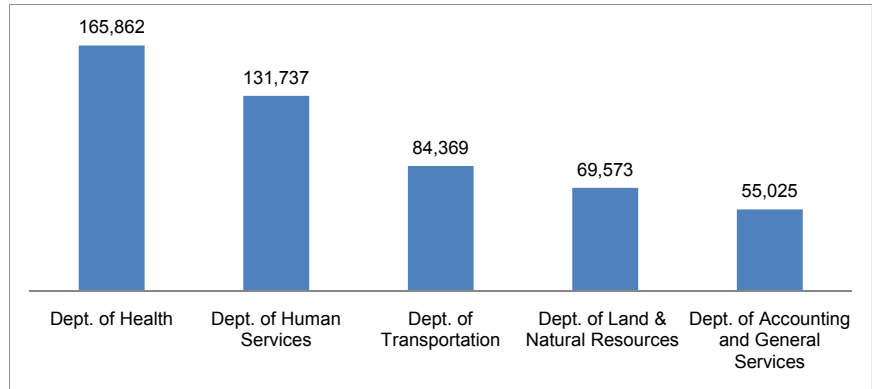


Source: Office of the Auditor. Data obtained from First Hawaiian Bank and the State Procurement Office quarterly reports.

***Top three executive  
branch agencies’  
pCard program  
structure***

The departments of Health, Human Services, and Transportation are the three executive branch agencies with the highest number of pCard transactions and dollar amount of expenditures, as shown in Exhibits 1.8 and 1.9. Exhibit 1.8 shows the five executive branch agencies with the highest number of pCard transactions for the period July 2005 through September 2009.

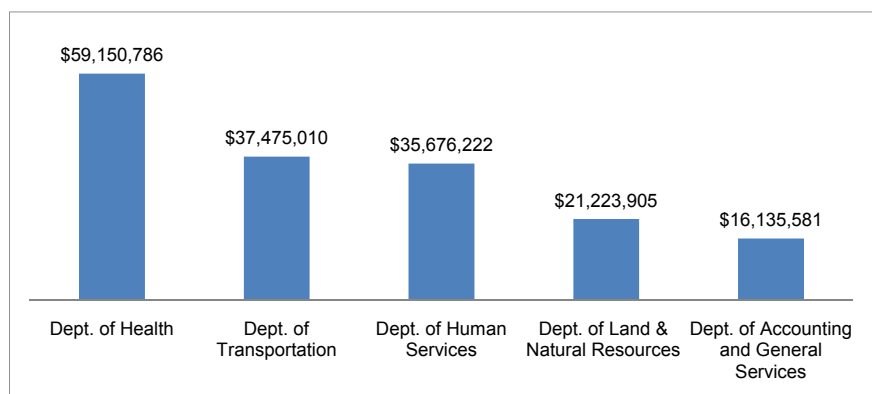
**Exhibit 1.8**  
**Top Five Executive Branch Agencies By Number of pCard Transactions, July 2005 – September 2009**



Source: Office of the Auditor. Data obtained from First Hawaiian Bank and the State Procurement Office quarterly reports.

Exhibit 1.9 shows the five executive branch agencies with the highest amount of pCard expenditures for the period January 2005 through September 2009.

**Exhibit 1.9**  
**Top Five Executive Branch Agencies By pCard Purchase Volume, January 2005 – September 2009**



Source: Office of the Auditor. Data obtained from First Hawaiian Bank and the State Procurement Office quarterly reports.

### **Department of Health**

The Department of Health (DOH) has approximately 3,000 employees, of which about 229—just under 8 percent—are pCard holders. The pCard program is centrally administered by the department's Administrative Services Office (ASO), with the administrative services officer responsible for the proper operation of the program within the department. The department's procurement and supply specialist is the pCard administrator; numerous CentreSuite administrators are located within the DOH's divisions, branches, and administratively attached agencies and state offices (collectively, "DOH's agencies"), and are either the public health administrative officer or the program supervisor for each of those agencies. A public health administrative officer is similar to an ASO, overseeing budgets, contracts, personnel, etc., within a DOH agency. Each DOH agency that has a cardholder also has a CentreSuite administrator.

### **Department of Human Services**

The Department of Human Services (DHS) has approximately 2,500 employees, of which about 405—just under 17 percent—are pCard holders. DHS' pCard program is centrally administered through its Fiscal Management Office (FMO).

The department's procurement and supply specialist serves as the pCard administrator and is responsible for the proper operation of DHS' pCard program. In addition to the procurement and supply specialist, two other employees—the FMO pre-audit staff supervisor and the FMO money payments staff supervisor—have oversight of the program as CentreSuite administrators. The CentreSuite administrators are responsible for reconciling cardholder statements to division statements. The FMO pre-audit staff supervisor and her staff reconcile administrative purchases such as office supplies; the FMO money payments staff supervisor and her staff reconcile client-related purchases, such as clothing for foster children.

### **Department of Transportation**

The Department of Transportation (DOT) has approximately 2,200 employees, of which about 182—just under 8.5 percent—are pCard holders. DOT's pCard program is centrally administered by its Business Management Office (BMO), which is part of its Administration Division.

The department is comprised of four divisions: Administration, Airports, Highways, and Harbors. Each division is responsible for the proper operation of its pCard program. Each division also has its own pCard coordinator, Administrative Services Office, and fiscal office.

The audit supervisor of the Business Process Improvement and Internal Control Staff is the pCard coordinator for the department's Administration Division and the O'ahu Metropolitan Planning Organization. The business management officer of the Administration Division is responsible for issuing and cancelling pCards as well as serving as the liaison between the State Procurement Office and the DOT.

The pCard coordinators perform some of the duties of both the pCard and CentreSuite administrators as defined in the SPO's Purchasing Card Program and Procedures. In addition, some of the duties outlined for the pCard and CentreSuite administrators in the SPO's procedures are also performed by cardholders or the department's fiscal offices.

### **Prior audits**

Our office has conducted two audits relevant to the pCard program. In Report Nos. 09-03, *Procurement Audit of the Department of Education: Part 1*, and 09-04, *Procurement Audit of the Department of Education: Part 2*, we found that the Department of Education (DOE) lacked proper leadership and controls over its procurement process, resulting in errors and violations of the State's procurement code. We found that single pCard purchases exceeded the \$2,500 purchase limit. We also found that cards were used both to purchase prohibited items and by personnel other than registered cardholders. We recommended strengthening the department's control environment over procurement, including developing an effective internal control system through formal and enforceable policies and procedures and continuous procurement training, adopting a code of ethics, and establishing a risk management program to assess and implement the department's fraud risk.

### **Other audits**

The Department of Accounting and General Services' Audit Division issued Internal Audit Report Number 09-41, *State of Hawai'i State Procurement Office Review of Procurement Practices June 30, 2007*, dated June 26, 2009. In relation to pCards, the audit found there was non-compliance with the preparation of transaction logs; it recommended training employees on state law and pCard procedures, and implementing a system to monitor compliance.

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## **Objectives of the Audit**

1. Assess the adequacy of the SPO's management oversight and internal control system over the pCard program.
2. Evaluate whether executive branch agencies' purchasing card practices are in compliance with laws, rules, policies and procedures.
3. Make recommendations as appropriate.

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## Scope and Methodology

This audit focused on the procurement of goods and services by executive branch agencies using pCards from July 2008 to October 2009. We included prior years as deemed necessary. We conducted interviews with the State Procurement Office, First Hawaiian Bank, and department managers and personnel of selected executive branch agencies involved in the pCard program, including those responsible for management and oversight of the program. We focused on the three executive branch agencies with the highest number of pCard transactions and largest dollar volume of pCard expenditures for the period audited, namely: the Departments of Health, Human Services, and Transportation. In the case of the Department of Transportation, we focused on two of its four divisions: Administration and Highways.

Our audit work included a review of policies and procedures, training logs, reports, and other documents to assess compliance with statewide policies and procedures. We tested a sample of pCard transactions, reviewing items for compliance with applicable state procurement laws, rules, policies and procedures, as well as the agencies' internal policies and procedures. We performed data mining to help identify instances of potentially improper purchases. Data mining is the act of searching, or "mining," data to identify transactions or patterns of activity exhibiting predetermined characteristics, associations, or sequences, and anomalies between different pieces of information. We relied on First Hawaiian Bank to provide complete and accurate records; we did not seek to validate the integrity of the data provided.

The audit was conducted from October 2009 to February 2010 according to generally accepted government auditing standards. These 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.



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# Chapter 2

## The State's Purchasing Card Program Has Not Realized Its Full Potential for Success

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More than eight years after contracting for the Purchasing Card (pCard) Program, the State Procurement Office (SPO)'s vision of an efficient, cost-effective purchase and payment process remains uneffectuated. Designed to streamline the State's small purchase payment process, the pCard program has instead become almost as onerous as the purchase order system it was intended to replace. The SPO has not focused on pCard program performance and efficiencies, and it could do more to guide executive branch agencies on program implementation. The SPO needs to re-engineer its stalled pCard program and realize the pCard's potential. With an emphasis on doing more with fewer resources, the procurement office can assist by being more responsible for program implementation and improving its training and guidance to executive agencies.

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### Summary of Findings

1. The State Procurement Office's hands-off administration of the statewide Purchasing Card Program has limited the program's broader benefits.
2. Executive branch agencies' individual purchasing card programs lack streamlined procedures that could save time and money.

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### SPO's Hands-off Administration of the Purchasing Card Program Has Limited Its Broader Benefits

As the agency with overall responsibility for implementing the pCard program and assuring it achieves its intended results, the State Procurement Office needs to assume a more hands-on approach to planning and managing the program and play a stronger role as the program administrator. Because the procurement office has decentralized the pCard program and delegated significant pCard responsibilities to the executive branch agencies, it has not embraced its administrator role and has failed to identify meaningful program goals and objectives. As a result, executive branch agencies are not held accountable and are left to determine for themselves how best to ensure controls and processes are adequate, working properly, and cost efficient. In addition, the SPO does not properly evaluate or monitor the program's performance. Until the SPO becomes more proactive, it will not be able to recognize and address the problems and concerns executive branch agencies are facing.

***The pCard program has realized some projected benefits, but not others***

Use of the pCard for state purchases has had some benefits. Department fiscal personnel that we interviewed said vendors are paid sooner and cardholders receive their goods and services faster. In addition, the State receives a rebate from its pCard vendor, First Hawaiian Bank, based on the State's net purchasing volume. Executive branch agencies received total rebates of \$72,897 in 2005; \$187,157 in 2006; \$226,147 in 2007; and \$391,619 in 2008. First Hawaiian Bank has also waived some fees for the program, such as implementation fees, and has not invoiced the State since the program's inception. It is the bank's policy to waive various fees if a customer meets certain criteria.

Some of these benefits were identified by the State Procurement Office in a 2001 letter to chief procurement officers statewide, encouraging their participation in the pCard program. That letter noted that with the pCard, vendors are paid quickly without the necessity of a check being mailed to each of them; and that the bank offers a rebate based on the volume of purchases put on the card. Also, in late 2002, the then-state comptroller said the decision to implement the pCard program was based, in part, on its ability to reduce the administrative burden of processing invoices and its increased benefits to vendors, who would be paid within two to three days of purchase instead of the usual 30 days.

Although these benefits have been realized, other program benefits and goals have not. By replacing the laborious and costly purchase order system, the pCard program was also supposed to build a more efficient and streamlined procurement system, primarily for small purchases. Prior to pCard's implementation, the SPO estimated the cost of processing a purchase was between \$130 and \$190, which can exceed the cost of merchandise purchased. This vision of a more timely and efficient system, however, has remained elusive.

***SPO is the administrator of the pCard program but has shifted its responsibilities to the executive departments***

The State Procurement Office, in its capacity as the central authority on procurement practices and the pCard program administrator, is ultimately responsible for the State's pCard program. Yet we found that the SPO has taken a hands-off approach to administering the program by delegating its responsibilities to the executive departments.

The SPO assistant administrator told us the SPO chose to decentralize administration of the pCard program because it lacked the resources to administer the program centrally. According to the assistant administrator, decentralizing made the most sense because it gave executive departments the flexibility to tailor the program to their needs. The assistant administrator also stated that the pCard is similar to a purchase order or petty cash—it is a means of payment and thus not part of *procuring* the purchase.

At present, the SPO's purchasing specialist serves as the statewide manager for the pCard program. A part-time employee who works six hours a day, she splits her time between managing the pCard program and other responsibilities. She devotes 30 to 40 percent of her time—less than three hours per day—to the pCard program. In this brief period she is expected to carry out her program manager duties, which include initiating studies; providing analysis of other states' programs; participating in working groups with other states to assist in improving and managing the program, including auditing program progress; and providing training.

The purchasing specialist is also responsible for administering the pCard contract with First Hawaiian Bank. In this capacity, she must ensure compliance with the terms of the contract both with the vendor, FHB, and executive departments. According to the SPO's contract administration training materials, a contract administrator's responsibilities include managing the day-to-day oversight of a contract, providing technical guidance to the contractor and users, and ensuring goods and services are received in accordance with the contract. A contract administrator's duties also include ensuring other relevant personnel (in this case, fiscal and procurement staff, program managers, etc.) are informed of significant events, issues and problems, and monitoring contractor performance.

We question whether the part-time purchasing specialist is able to fulfill all of the responsibilities of pCard program manager and contract administrator. She has stated that she wants to do more for the pCard program but does not have the time. Thus, although the purchasing specialist and the SPO administrator both agree they would like to do more, legislative funding was not received and there are no other resources to support the program.

Unable to devote more resources to the program, the SPO delegated its responsibilities to the executive branch agencies. In its view, each executive department has its own pCard process and is responsible for that process. However, the procurement office is still ultimately responsible for the pCard program even though it has decentralized the program's management. As the pCard contract administrator, the procurement office is the state agency with ultimate responsibility for ensuring the program is running according to the terms of the contract. It is the agency best suited to guide the program statewide. Further, the SPO administrator, who is the chief procurement officer for all executive branch agencies, has a statutory obligation to oversee and review the State's procurement practices. The SPO's shifting of its program responsibilities leaves the pCard program without oversight or goals and with vague objectives, ineffective action plans, and empty performance measures.

***SPO has no overall plan for the pCard program and is not measuring its progress***

The State Procurement Office has failed to adequately establish, monitor, or evaluate goals and objectives for the pCard program. It has not established meaningful performance measures to indicate whether objectives are being met. The pCard program manager said the SPO does not have an overall plan nor is it measuring progress of the program. Additionally, the SPO administrator's statutory responsibility for periodically reviewing procurement practices as they relate to the pCard is not conducted systematically; the SPO administrator has said that his office does not have a formal process to evaluate the program.

**pCard program lacks overall planning**

Every year, the Department of Accounting and General Services (DAGS) is required to submit a goals and objectives report for its various programs, including the SPO, to the Legislature. For 2010, the report did not include objectives for the pCard program although it was part of reports from 2005 to 2009. The SPO assistant administrator told us there are no objectives for 2010 because of the possible transition to a new pCard vendor as a result of the Request for Proposal (RFP) issued on March 23, 2009. As of February 26, 2010, the SPO was in the process of evaluating the RFP and could not comment any further on its progress.

Public program managers should fully understand the operations of programs they manage. The National State Auditors Association (NSAA) states in its publication, *Best Practices in Performance Measurement, Developing Performance Measures*, that measuring the performance of a program is a critical element of accountability for public resources. Before beginning the process of developing performance measures, the NSAA recommends that public program managers first know what they are measuring. This involves developing a mission statement, establishing goals, setting objectives, and developing an action plan.

We found that the SPO's planning is inadequate. The SPO administrator told us his office would like to conduct studies on each department's use of the pCard, but that he has neither the staff nor resources to do so.

As manager of the pCard program, the SPO should develop a mission statement, establish goals, set objectives, and develop an action plan for its program. Moreover, as the program's initiator, the procurement office must set the tone and direction for the program with adequate and meaningful planning. According to Sections 6 and 7, Act 100, Session Laws of Hawai'i (SLH) 1999, every state department and agency is required to submit an annual planning report to the Legislature addressing the following:

- Statement of short- and long-term goals;
- Objectives and policies setting forth how each goal is to be accomplished;
- Action plan with a timetable indicating how objectives and policies will be implemented in one, two and five years; and
- Process to be used for measuring performance in meeting stated goals.

In enacting Act 100, SLH 1999, the Legislature believed the development of goals and objectives is essential for state departments and agencies to determine priorities, guide their decisions, and measure the effectiveness of their programs and services. Without setting a clear course or measuring program milestones, however, the SPO is unaware whether or not the pCard program is operating at its full potential. This leaves its accountability as a public program in question.

### **Goals are nonexistent**

Because the SPO did not include objectives for the pCard program in its 2010 report to the Legislature, we reviewed its 2009 report, which did include program objectives. In addition to objectives, the report outlined policies, an action plan, and performance measures as required by Act 100, SLH 1999. It also highlighted the overall goals for the procurement office. However, there were no goals specific to the pCard program. The pCard program manager confirmed that the procurement office does not have formal written goals for the program.

To determine priorities, guide decisions, and measure the effectiveness of programs and services, state law requires every department and agency to submit an annual report of goals and objectives to the Legislature. Additionally, the National State Auditors Association (NSAA) states that public agency managers should develop clear goals for their organization as a whole as well as for the individual programs within their organization. Among the things to be considered in developing sound goals are the following: goals must support the mission; each goal should represent a desired result that can be measured; goals must be realistic and achievable; and each goal should make sense to others outside the organization.

Even purchasing card industry standards recommend the development of specific and measurable goals and objectives. Purchasing card program goals should be actionable and allow for tracking and monitoring, which may include goals for increased discounts received from vendors; increased speed of vendor payment; lower transaction processing cost; and improved employee purchasing effectiveness and efficiency.

Without goals for the pCard program, fulfillment of the vision of a more efficient and cost-effective procurement system remains nebulous and unattainable.

### **Objectives and policies are vague**

We found that the objectives and policies of the pCard program are stated, but the SPO has not identified how they are to be accomplished. In its 2009 report, which repeats the language of its 2006 through 2008 reports, the procurement office states the following objectives and policies for the pCard program:

- Continue to provide training and support for departments to maintain and increase levels of efficiency for small purchase procedures with the use of pCards;
- Establish annual meeting of fiscal officers to network, open discussion of issues or concerns, and provide management reports to assist in the analysis of purchasing activities;
- Integrate the pCard as the preferred method of payment into price list contracts and HePS purchases; and
- Develop a program to conduct periodic audits of compliance with program procedures.

We asked the SPO how it determined the objectives and action plan stated in its annual report. The program manager responded that the SPO administrators simply decided what objectives they wanted to have in the plan, and included them in the report; she confirmed that the SPO did not use a model pCard program on which to base its objectives.

Act 100, SLH 1999, requires that objectives and policies be set forth identifying how each goal is to be accomplished. In addition, according to NSAA's best practices, good objectives have the following characteristics: they are clear, concise, and presented in a logical sequence; specific results are identified in each objective; results for each objective are measurable; each objective has a specific timeframe for completion; and completion of each objective leads to the attainment of stated goals.

Exhibit 2.1 compares the SPO's objectives and policies against the requirements of Act 100 and NSAA best practices.

**Exhibit 2.1**

**Comparison of SPO Objectives and Policies With Act 100 and NSAA Best Practices**

SPO Objective or policy for the pCard program	Act 100 Requirement	NSAA Best Practice			
	Indicates how it is to be accomplished	Objectives and policies are clear and concise	Results are identified	Results are measurable	Timeframe is specified
Continue to provide training and support for departments to maintain and increase levels of efficiency for small purchase procedures with the use of pCards	No	Yes	No	No	No
Establish annual meeting of fiscal officers to network, open discussion of issues or concerns, and provide management reports to assist in the analysis of purchasing activities	No	Yes	No	No	No
Integrate the pCard as the preferred method of payment into price list contracts and HePS purchases	No	Yes	No	No	No
Develop a program to conduct periodic audits of compliance with program procedures	No	Yes	No	No	No

Source: Data compiled by Office of the Auditor

The SPO's written objectives are clear and concise. However, the SPO does not identify specific results for its objectives. For example, there is no definable, measurable result for the pCard becoming the preferred method of payment (such as, "80 percent of all purchases under \$X are made via a pCard."). There are also no timeframes (such as, "By 2012, 90 percent of all purchases are made via a pCard."). Since there are no goals stated for the program, it is difficult to know if achieving the objectives would lead to fulfilling the program's broader goals.

When we asked the SPO personnel how they were achieving the objectives and policies for one of their stated objectives, their answers were vague. For example, in relation to continued training, we asked how this was being achieved and what type of training the SPO was conducting. The SPO program manager told us this was being achieved through the SPO's small purchase training, and is mentioned in relation to payment procedures. When asked to elaborate, the program manager told us it is the departments' primary responsibility to train their cardholders and ensure they attend all applicable training.

### **Action plan is ineffective**

The SPO's 2009 report included the following action plan and timetable for the pCard program:

- One Year: Refine management reports to assist departments in analyzing purchasing activities and to detect unauthorized purchases, fraud and abuse;
- Two Years: Establish the pCard as the primary form of payment for small purchases; and
- Five Years: (a) Devise an audit program to assist departments in verifying purchases and to corroborate cash rebates; (b) Encourage and promote enhanced online systems; and (c) Integrate the pCard as the primary form of payment for purchases made on HePS.

We found that the SPO's action plan is outlined with a requisite timetable; however, there is no indication of how the plans will be implemented nor who will be responsible for their implementation. There are no detailed action steps. The timeframe does not coincide with actual progress to be made. Further, there is no identification of resources to be used or anticipated savings.

State law requires an action plan to include a timetable indicating how its objectives and policies will be implemented in one, two, and five years. Additionally, according to NSAA's best practices, objectives should be established through the development of an action plan which includes, for each objective: identification of who will be responsible and accountable for implementation; detailed action plan steps; expected start and finish dates for each step; timeframe for completion of entire



action plan; what resources are needed to implement the objective; and identification of any anticipated savings.

Exhibit 2.2 compares the SPO’s action plan against the requirements of Act 100 and NSAA best practices.

**Exhibit 2.2  
Comparison of SPO Action Plan With Act 100 and NSAA Best Practices**

	Act 100 Requirement	NSAA Best Practice			
SPO’s Action Plan for the pCard program	Indicates how the objective is to be accomplished	Identifies who is responsible for the objective	Provides detailed steps on how to achieve the objective	Identifies start and finish dates	Identifies resources needed and savings anticipated
<b>One Year:</b> Refine management reports to assist departments in analyzing purchasing activities and to detect unauthorized purchases, fraud and abuse	No	No	No	No	No
<b>Two Years:</b> Establish the pCard as the primary form of payment for small purchases	No	No	No	No	No
<b>Five Years:</b> (a) Devise an audit program to assist departments in verifying purchases and to corroborate cash rebates; (b) Encourage and promote enhanced online systems; and (c) Integrate the pCard as the primary form of payment for purchases made on HePS	No	No	No	No	No

Source: Data compiled by Office of the Auditor

The SPO's comments on the progress of the action plan were not definitive. Regarding the one-year plan to *refine management reports to assist departments in analyzing purchasing activities and to detect unauthorized purchases, fraud and abuse*, the SPO pCard program manager said that the procurement office provided training to departments via webinar (web seminar) before the launch of CentreSuite. Departments can generate their own management reports using CentreSuite. Regarding the two-year action plan to *establish pCard as the primary form of payment for small purchases*, she said the pCard is already the primary form, including the price list and three quote small purchase methods. Regarding the five-year action plan, she said there is currently no audit program. However, the RFP that was issued in 2009 for a new card vendor requires an audit program to allow departments to perform audits. With the launch of CentreSuite, the procurement office has enhanced the online capabilities of the pCard program. However, not all departments have converted from the old PVSnet system to the CentreSuite system. Furthermore, integration of the pCard with HePS will take more than five years because HePS is currently not integrated with the state accounting system. Since the SPO's action plan for the pCard program lacks steps for implementation, identifying program accomplishments is difficult and unclear.

### **Performance measures are deficient**

In its 2009 Act 100 report, the SPO listed the following performance measures for the pCard program:

- Conduct analysis of expenditure and pCard usage reports obtained from the pCard system; and
- Review the number of purchasing cards being used by the agencies and the dollar value of pCard purchases annually.

We evaluated the SPO's performance measures by assessing whether the measures 1) met the Act 100 requirement by stating the process by which performance in meeting the stated goals would be measured and 2) were developed as part of the action plan, as recommended by NSAA. According to NSAA, a comprehensive and balanced set of performance measures should compare actual performance with expected results. Performance measures should be defined so that all users can understand the: a) source of the data for the measures; b) methods used to calculate the measure; and c) timeframe over which the measure will be reported. Performance measures should also be meaningful and the data should enable comparison over time.

Overall, we found that the SPO's pCard program performance measures are deficient. Although processes are stated briefly (i.e., *conduct analysis and review*), there is no reference to the SPO's pCard program goals. The SPO's assistant administrator acknowledged that the SPO

is the responsible agency for meeting pCard’s goals; however, the SPO’s program manager confirmed that the procurement office has not developed such goals. As such, the SPO’s Act 100 report falls short of its reporting requirement. And without goals, the SPO cannot identify what it is hoping to achieve.

We also found that the pCard program’s performance measures have not been developed as part of an action plan. The measures do not identify what outcome is expected, source of data to be measured, methodology for calculation, or timeframe. When we asked how performance was being measured, the pCard program manager stated that there is no “grand plan” and that the SPO is not measuring the pCard program’s progress or work performance.

Exhibit 2.3 compares the SPO’s pCard program performance measures against the requirements of Act 100 and NSAA’s best practices.

**Exhibit 2.3  
Comparison of SPO Performance Measures With Act 100 and NSAA Best Practices**

	Act 100 Requirement	NSAA Best Practice			
SPO’s Performance Measures for the pCard program	Identifies process to measure	Identifies source of data to be used	Identifies method of calculation	Identifies period to be examined	Is a meaningful measure of performance
Conduct analysis of expenditure and pCard usage reports obtained from the pCard system	No	No	No	No	No
Review the number of purchasing cards being used by the agencies and the dollar value of pCard purchases annually	No	No	No	No	No

Source: Data compiled by Office of the Auditor

In the absence of a proper plan and the process by which to measure performance, the SPO is unable to lead the pCard program on an efficient and meaningful course.

***SPO's oversight and monitoring of the executive branch agencies could be improved***

Although the SPO is responsible for managing and administering the pCard program, it does not review reports, policies and procedures, or training materials developed by executive branch agencies. It also does not utilize bank reports for monitoring purposes, has not performed risk assessments, and has no formal risk assessment process in place. The SPO also has not implemented an effective system for sharing innovations and experiences in areas such as internal controls or operational efficiencies. As a result, the SPO has no clear understanding of how effective the executive branch agencies are in reviewing and monitoring their respective programs and ensuring that pCard user training is properly performed. Without such clear knowledge, the SPO cannot enact meaningful changes to the pCard program to help it reach its full potential.

**SPO's guidance for the pCard program is insufficient**

The State Procurement Office issues pCard guidance but cannot ensure that departments are in compliance. The procurement office delegates the pCard program's operational and cardholder training responsibilities to executive branch agencies, but does not require any reporting back to the SPO. This deficiency can be found throughout the SPO's various policies and procedures. For instance, we found that the SPO's guidelines state that the responsibilities to develop purchasing card procedures and coordinate training of pCard users for a department belong to each department's purchasing card administrator. Similarly, the SPO guidelines place responsibility for monitoring and reviewing cardholder transactions on each department's CentreSuite administrator. Furthermore, the SPO's pCard program does not include procedures for departments to report problems, issues, concerns, or data information to the SPO.

According to the U.S. Government Accountability Office's (GAO) *Standards for Internal Control in the Federal Government*, monitoring is an important internal control for assessing the quality of performance over time, and should occur in the course of normal operations. Monitoring includes regular management and supervisory activities, comparisons, reconciliations, and other actions. Further, the GAO also points out that key to a good internal control environment is management's commitment to competence. All personnel need to possess and maintain a level of competence that allows them to accomplish their assigned duties, as well as to understand the importance of developing and implementing good internal controls.

The pCard program manager told us that the SPO does not review the procedures or training materials developed by executive branch agencies. The pCard program manager also confirmed that the SPO does not receive reports from departments on any problems or violations relating to the pCard program. The program manager stated that pCard user training is the responsibility of the departments, and that the SPO informs departments of updates to the program but does not conduct pCard user training. According to the program manager's job duties description, she serves as the pCard central administrator for all executive branch agencies, which includes responsibility for training.

In our review of the SPO procurement circulars, directives, and comptroller's memorandums, we noted that the SPO has no method to ensure executive department compliance with pCard program requirements. For example, in the SPO Procurement Circular No. 2003-06, Amendment 2, "Management Oversight and Controls," the SPO recommends that agencies address training as a key to ensure that employees have the necessary skills to perform their functions and understand the department's goals. The procurement office also recommends that cardholders understand proper pCard procedures, restrictions, responsibilities, and penalties for noncompliance. When asked how it ensures that departments adhere to this circular, the SPO administrator told us she does not know, and said that departments are responsible for holding their employees accountable.

The SPO is one of three agencies (including DAGS and our office) responsible for randomly auditing departments' purchasing card activity to ensure adherence to the pCard's program and procedures. However, the SPO administrator informed us that the SPO has not performed any departmental audits. Further, the SPO does not perform annual risk assessments or have a formal risk assessment process in place.

In the absence of any review of pCard procedures and training materials, any method to ensure executive department compliance, any random audits of departmental pCard programs, or any formal risk assessment process for the pCard program, the SPO cannot ensure that executive departments are in compliance with the SPO's pCard program and procedures.

### **Oversight and monitoring reports are available, but barely used by the SPO or departments**

First Hawaiian Bank's CentreSuite system is capable of producing ten standard reports on the pCard program which the SPO and executive departments may use. However, we found that the procurement office does not use any of these reports to facilitate review and monitoring. We also found that the departments use few, if any, of the reports. Of the

ten standard reports, three are not activated and one is activated for only three executive departments. The two reports used by the departments we tested are the Transaction Report and Statement of Account. Both are used by those departments to facilitate monthly operational reconciliations.

Examples of the reports that are available but which have not been activated are the Multiple Transaction Exception Report (MTER) and the Expense Report. The MTER illustrates purchases that may have been split between multiple receipts because they exceed the single purchase limit; the report can be used to identify transactions that may violate the pCard's business rules. The Expense Report contains transactions relevant to a specific business purpose, and can be used to analyze out-of-pocket and card transactions attached to a cardholder's expense reports.

Although the SPO does not use CentreSuite reports, we found that it does obtain two other reports from First Hawaiian Bank, namely, the Monthly Spend Report by Department and the Quarterly Rebate Report by Department. The SPO uses these two reports to compile statistics which are then used during training to illustrate savings and rebate revenues. The two reports are not used for any other purpose. In our discussion with First Hawaiian Bank's assistant vice president of the Commercial Card Department, we were told that the SPO does not request any other reports. The bank was not aware whether the SPO or any of the executive branch agencies generate any pCard reports.

According to the SPO program manager, the Enhanced Merchant Reporting (EMR) system is capable of providing reports that can be used to analyze usage and detect abuse and fraud. We found, however, these reports are little used. We found that although the SPO notified departments that they could obtain such reports if they were interested, other than the initial training by the bank, the SPO has provided no subsequent training sessions regarding Enhanced Merchant Reporting to the departments and hence they have been largely overlooked. The SPO's program manager told us that departments could follow up with the bank if needed. The Enhanced Merchant Reporting that is being used by the departments is described in more detail later in this chapter.

Reporting capabilities were included in the SPO's 2001 Request for Proposals (RFP) requirements for a pCard program vendor. At a minimum, the vendor needed to be able to provide reports which included detailed records of transactions and could be used to detect fraud and misuse, as well as detailed monthly transaction histories, by cardholder, that could be used to verify cardholder activity. Although

First Hawaiian Bank's reporting capabilities are robust and fulfill the SPO's requirements, few if any of these reporting capabilities are used by the SPO or executive departments.

The pCard program manager stated that she does not use any of the reports available on CentreSuite, nor is she aware whether the departments make use of them. She further stated that it is each department's responsibility to review and monitor its own performance and compliance. However, as stated earlier, her job duties include administering the pCard program for state and county agencies; receiving, reviewing, and analyzing reports submitted by the pCard vendor; and reporting findings, initiating studies, auditing program progress, and training. Given her responsibilities, not only should she be aware of departments' pCard performance and compliance, she should have provided more guidance to departments' pCard administrators on the use of the available CentreSuite reports and should know whether the reports meet departments' needs.

### **SPO has not implemented an effective system for sharing innovations and experiences**

In 2006, the SPO identified a need for the executive departments to network and have a forum in which to share pCard issues and concerns. However, since then the SPO has made only one attempt to establish such networking opportunities among the executive branch agencies. The SPO reported that its sole attempt was not successful.

In its annual reports for 2006 through 2009, the SPO maintained that one of its objectives was to establish an annual networking meeting of fiscal officers, have open discussion of issues or concerns, and provide management reports to assist in analyzing purchasing activities. The first Annual Financial Officer's Seminar for pCard administrators was held on October 17, 2007 to address updates and issues with the executive branch agencies. One of the seven items on the seminar's two-hour agenda was entitled "Networking opportunities." In our review of the meeting materials, we found no information relating to networking opportunities. When we asked the procurement office about details of these networking opportunities, we were told that seminar attendees formed working groups to discuss pCard successes and failures. The SPO's pCard manager stated that the networking opportunity was not particularly successful and that there was very little interaction in the working groups. The SPO is considering other networking options for the future, such as using smaller groups. The pCard program manager noted that she has one-on-one discussions with the departments in relation to their networking needs.

According to the GAO's *Acquisition Reform, Purchase Card Use Cuts Procurement Costs, Improves Efficiency Report, August 1996*, agencies that have identified the savings or efficiencies they have gained from using pCards have done so by reengineering their programs or using automated tools to improve their processes. The report also noted that agency officials were interested in communicating with each other about their efforts and have identified instances where tools developed by one agency can be useful to others.

Not surprisingly, we found there were differences in the pCard account management, month-end reconciliation, and use of management or statistical reports in the three executive departments we tested. The differences are shown in Exhibit 2.4. The agencies selected were the Departments of Health, Human Services, and Transportation (Administration and Highways Divisions). These three agencies were chosen because they had the highest number of pCard transactions and dollar amount volume of pCard purchases for the period audited.



**Exhibit 2.4**

**Differences Among Selected Executive Departments' pCard Processes**

<b>pCard Program</b>	<b>DOH</b>	<b>DHS</b>	<b>DOT - Administration</b>	<b>DOT - Highways</b>
Account management: 1. Number of CentreSuite administrators or approving officials to cardholders 2. Set single transaction limits 3. Set credit limits	No set number. No listing available. \$5,000  \$10,000	No set number.  Does not use.  \$30,000	Ten approvers to 20 cardholders.  None. Determined by manager.  None. Determined by manager.	No set number. Could not determine. \$2,500  \$5,000
Use of Management or Statistical Reports obtained from the Enhanced Merchant Reporting (EMR) System	Yes. They found limitations, which they mentioned to FHB but did not pursue.	No. They were informed but never heard anything more about it.	No. Does not use.	No. Does not use.
Performs month end pCard reconciliations and reviews: 1. At division/unit level 2. At department level	No No	No Yes	Yes No	Yes No
Completes monthly billing cycle reconciliations after the end of the billing cycle	Yes. It is done within two months after the end of the billing cycle.	Yes. It is done within one month after the end of the billing cycle.	Yes. It is done prior to payment to FHB.	Yes. It is done prior to payment to FHB.
A certification that the goods were received in good order and condition must be noted on the documents	No. DOH was unaware that it was required.	Yes	No. *DOT obtained approval from DAGS requiring certification only on the pCard vendor statement.	No. *DOT obtained approval from DAGS requiring certification only on the pCard vendor statement.

\*According to DOT's business management officer, the department obtained approval from DAGS at the onset of the pCard program that certification was not required on individual documents but only on the statement that supports payment to the pCard vendor. DAGS has since issued a Comptroller's Memorandum No. 2010-01, dated January 13, 2010, that amends Comptroller's Memorandum No. 2007-20 and which effectively eliminates the requirement for certification on all documents to only the payment made to a pCard issuer.

Source: Data compiled by Office of the Auditor

We also found that executive departments were not depositing their rebates in accordance with the SPO's procurement circular, which states that general-funded programs must deposit rebate checks into the general fund and non-general funded programs must comply with *applicable statutory requirements*. The SPO personnel clarified that for non-general funded programs, rebates generated from the use of general, special, or federal funds should be returned to the respective fund. The SPO program manager told us departments should know, and do appear to know, how to properly allocate their rebates, since the SPO has not received any inquiries.

We found that the Department of Human Services (DHS) and the Department of Health (DOH) deposit the entire rebates into the State's general fund, even though they have special and federal funds. The Department of Transportation (DOT) deposits its rebate into the Transportation and State Highways (special) Funds, although there may be a small rebate allotted to some federal funds.

The DOH administrative services officer stated that it would be difficult for the department to allocate its rebate among its various federal funds because program spending differs every month and it would take the department a long time to calculate the amounts. The officer told us she is not sure what is meant by *applicable statutory requirements* or how the department is to allocate its rebate to federally funded programs; she also remarked, "We would be interested to know how we are supposed to allocate."

DOT-Highways does not separate its rebate between its special and federal funds. The DOT-Highways accountant explained that rebate amounts for federal funds are small and difficult to separate and "may need someone to be dedicated to do just that."

Likewise, DOT-Administration (DOT-A) does not separate its rebate between its special and federal funds. According to DOT-A's business management officer, in relation to purchases for some of the division's federal projects, it is difficult to determine what amount should be credited to which fund.

In addition to the issue of how and where to deposit rebates, one agency in our audit sample was not aware that any pCard process could be handled differently and expressed surprise when informed of another agency's method for a similar process. Agencies should be made aware of alternative procedures and processes, whether by the SPO or via a forum with other agencies, so that they know of the different methods and can select the one(s) most appropriate for their agencies.

We found two examples where a procedure or process was made more efficient by one department and in a manner which would have benefited other departments:

- A comptroller's memorandum required a certification on all documents that goods and services were received, whereas the DOT obtained approval from DAGS at the onset of the pCard program to provide certification only on the statement that supports payment to a pCard vendor.
- The DOH has incrementally lowered single transaction and credit limits, both at an individual cardholder and department level, and decreased the number of pCards issued to those who really need them. This process is performed by reviewing allotment balance reports monthly to identify programs that exceed their pCard funding allotments.

In its *Governmentwide Purchase Cards* report, the GAO made several points regarding the General Services Administration's (GSA) responsibilities as administrator of the federal government's purchase card program:

With respect to governmentwide purchase card issues, GSA's role as the purchase card program manager puts it in a unique position to identify challenges to agency internal control systems and assist agencies with improving their internal controls governmentwide. We believe that GSA has a number of tools already at its disposal, such as online training and annual conferences, where GSA could easily remind cardholders and approving officials to pay particular attention to governmentwide issues, including asset accountability and independent receipt and acceptance of goods and services identified in this report.

Hawai'i's SPO assistant administrator confirmed that the SPO's role is similar to the GSA's.

We asked the SPO if executive branch agencies would benefit from sharing best practices among each other. The pCard program manager responded that it is always a benefit to hear what other departments are doing. We believe the SPO is in the best position to identify challenges to agency internal control systems and assist agencies with improving their internal controls. Had the SPO provided departments with more sharing opportunities, it may have resulted in better departmental processes.

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## **Executive Branch Agencies' Purchasing Card Programs Lack Streamlined Procedures That Could Save Time and Money**

We found that the SPO's claims of pCard program cost savings are questionable and that operational efficiencies are lacking. The SPO's decentralized environment has evolved into various, rather than uniform, processes and methods to accommodate the program and department needs. Because the SPO has not provided concrete guidance on how best to implement the pCard program, departments have created their own pCard programs that are just as, or perhaps more, labor intensive than the old purchase order process the pCard was supposed to replace. Although we found that executive departments' internal controls for their pCard programs are adequate, the focus on controls has overshadowed one of the pCard program's original intentions, to promote operational efficiencies.

### ***Concerns of inadequate internal controls have been unfounded***

We found that internal control weaknesses over pCard activities in the purchase card program do not exist. Instead, we found the pCard program has sufficient controls in place because the program was structured so similarly to that of the purchase order process. Such controls mitigate the weaknesses we did find, which were mainly limited to one executive department. Ironically, we found that because departments focus their efforts on controls over pCard activities rather than on promoting operational efficiencies, overall control activities in relation to the pCard program are adequate.

To illustrate the types of significant weaknesses in pCard internal controls that have been found in other states and put Hawai'i's controls into perspective, we obtained audit reports relating to purchasing cards from five other states. Overall, these reports cited weaknesses in internal control components, mainly in the control environment and activities. They reported deficiencies in oversight by overall administrators, supervisory review, training, and clear policies and procedures; which, in some cases, led to fraudulent and improper use of the purchasing cards. The majority of these other states' audit reports concluded that better oversight was needed at both the central administrator level and individual agency level. Examples of fraudulent, abusive, and improper purchases included a diamond band purchased from Amazon.com; a fox fur stole purchased for a theater production; and Visa debit cards purchased from a shopping mall, some of which were used to make car payments through Western Union.

For this audit, we tested the control activities we considered key to preventing and detecting fraudulent, improper, and abusive purchase card activity. We found that control activities were generally in place over the pCard program.

### **Departments' internal controls for pCard purchases are adequate**

We found that the selected executive departments we reviewed had similar and sufficient internal control activities in place, mainly because they structured their pCard process to mirror that of the purchase order process. Our audit included a review of whether selected executive branch agencies had proper control activities in place over key aspects of their purchasing card programs and were effective in adhering to statewide as well as internally prepared pCard policies and procedures. The agencies selected were the Departments of Health (DOH), Human Services (DHS), and Transportation (DOT). Our assessment was based on reviews of pCard policies and procedures, inquiries of pCard administrators and affected personnel, and tests over a sample of procurement card transactions.

The GAO has found that internal control weaknesses in agency purchase card programs expose the federal government to fraudulent, improper, and abusive purchases and loss of assets. Fraudulent purchases include the use of the government purchase cards to acquire goods or services that are unauthorized and intended for personal use or gain. Improper transactions are purchases that, although intended for government use, are not permitted by law, regulation or government/agency policy. Abusive purchase card transactions involve those that are excessive, questionable, or improper when compared to behavior a prudent person would consider reasonable and necessary.

According to the GAO's *Standards for Internal Control in the Federal Government*, internal control activities help ensure that management's directives are carried out. Control activities should be effective and efficient in accomplishing an agency's control objectives and should occur at all levels and functions of an agency.

We based our testing on the population of all pCard purchases for the period July 1, 2008 through October 31, 2009. We judgmentally selected a total sample of 75 purchases from data provided by First Hawaiian Bank. We examined these purchases individually for propriety of transaction. We also reviewed relevant purchase documentation to determine the reasonableness of the purchase and compliance with applicable policies and procedures.

For data mining testing, we judgmentally selected a total sample of 75 purchases from data provided by the bank. Our analysis centered on identifying transactions that exhibited characteristics of potentially fraudulent, improper, or abusive purchases, such as questionable merchants, suspicious cardholders, and unusual amounts or relationships.

We reviewed relevant purchase documentation to determine the appropriateness and reasonableness of the purchase, given the nature of the department.

We reviewed a variety of pCard activities that, if properly designed, would minimize fraudulent, improper, and abusive pCard activity. For the most part, the agencies had properly designed processes to ensure program risks were minimized. We noted compliance with applicable policies and procedures in the areas of training, account management, and pCard usage. We also found that the departments had implemented a pCard process that resulted in an adequate level of controls through the use of a purchase requisition form with multiple reviews and approvals. We did not identify significant patterns of misuse.

Both DOT and DHS files were orderly and easily accessible. Although we selected, but did not access, transaction files ourselves, the DOT-Administration and DOT-Highways division files that were delivered to us were neatly organized and complete. We could easily locate individual monthly statements. Similarly, pCard files from DHS were also well organized. We were able to locate files without assistance. All files for transactions in our test list were readily available and the files were consistently organized, thereby facilitating our fieldwork.

Our review of pCard activities included testing whether each agency exercised controls over:

- Requesting a card;
- Training;
- Credit limits;
- Blocked merchant category codes and restricted purchases;
- Transaction documentation;
- Tracking purchases;
- Reconciling monthly statements;
- Approving official reviews of monthly statements; and
- Cancelling cards.

We did note certain instances at one of executive branch agencies where cardholders and approving officials did not consistently adhere to established policies and procedures. For example, in two of 25 cases (8 percent), the pCard authorization form or requisition was signed by the cardholder as both the cardholder and the approving official. In five instances (20 percent), certain required documents were not found in the file. Four of the five missing documents were required by the agency and recommended by the SPO. In three instances (12 percent), required documentation was not submitted with the month end supporting documents as required.

This executive branch agency told us these instances were oversights by the cardholder and reviewing officials. We found no improper, fraudulent, or abusive purchases and noted that charges were for legitimate state business purposes. The cause of the inconsistencies appears to stem from vague guidance or lack of training at the cardholder and CentreSuite administrator level. However, we find these inconsistencies to be isolated to this one agency and, taken as a whole, there appear to be sufficient controls in place over the pCard transactions to mitigate these deficiencies.

### **SPO has focused on internal controls, not operational efficiencies**

We found that the SPO and DAGS have focused their efforts more on ensuring that executive branch agencies have adequate internal controls and security over the pCard program, rather than providing guidance on operational efficiencies. We saw this throughout the various instructions issued by the SPO and DAGS pertaining to the pCard program, as well as in training materials given to the executive departments.

This is understandable, given that the GAO has found that increased purchase card use increases risk. If not properly managed and controlled, use of a purchase card can result in fraudulent, improper, and abusive purchases. However, as we have stated, we found internal controls over the pCard program to be generally adequate. The GAO similarly found, when it reviewed the federal government's pCard program at about the same point in its lifecycle as Hawai'i's is now, that internal controls were sufficient and there was no increased abuse, but that the program was not realizing its potential for efficiency. Hawai'i is now in a similar position.

Since inception of the pCard program, the SPO administrator has issued several procurement circulars and memos offering guidance to executive departments regarding the pCard program. The state comptroller has also issued comptroller's memos specific to the pCard program. For instance, the SPO's procurement circular dated September 23, 2003—after the pCard program's pilot phase was completed—recommends three control features for the pCard program in addition to any already established by the agencies. In subsequent circulars, the SPO emphasized the need for department management to maintain oversight and internal controls over pCard usage from the top of the agency through the supervisory levels, and provides direction on some of those control activities. The SPO also told agencies to take precautions to prevent fraudulent, improper, and abusive purchases as well as theft or misuse of government property. Other procurement office memos instructed agencies that “as an added security feature,” photographs are required on all pCards.

The comptroller's memos dealt mainly with procedural authority, such as documentation requirements for purchases of goods or services and encumbering of pCard transactions. However, like the SPO administrator, the state comptroller also focused on executive departments having adequate internal controls, rather than on promoting operational efficiencies in the pCard program.

One comptroller's memo states that each executive department must determine the number of pCards it needs, maintain adequate internal controls to prevent misuse, and ensure staff are trained and informed of the consequences of the misuse. It also enumerates fiscal staff's responsibilities for ensuring cardholder documentation is submitted and for reconciling and certifying that monthly pCard statements are reviewed. The memo described the benefits of using the pCard, but did not provide specifics or quantify how those benefits were to be achieved. We noted no other discussion of ways to save on cost or operational efficiency in relation to the pCard program.

In our review of SPO's training materials, we also found greater emphasis on controls and security rather than on resources and cost efficiencies. Instead of offering to assist agencies with two pCard enhancements with the potential to help them achieve some operational efficiencies—the CentreSuite reporting capabilities and Enhanced Merchant Reporting system—the SPO leaves the departments to determine any efficiencies themselves.

The SPO offers two training workshops relating to pCards:

- Workshop No. 175 – pCard Overview and Updates; and
- Workshop No. 176 – pCard Program Changes and Updates.

The office recommends all pCard holders attend Workshop No. 175, which is an overview of the pCard program and procedures, and covers such controls as restricted purchases, blocked merchant category codes, and security measures. It also covers program updates and changes such as CentreSuite reporting functionalities. However, the SPO has stated that it is unaware whether departments make use of the CentreSuite reports, and that the SPO itself does not use any of the CentreSuite reports.

The SPO requires all pCard administrators to attend Workshop No. 176, which briefs administrators on the status of the pCard program's security measures, latest statistics, and other changes and enhancements in the program, such as the emergency pCard program. Our review of training materials revealed that other changes discussed are similar to those covered in workshop No. 175, in addition to procedural changes such as revisions to cardholder agreements and the pCard program procedures manual.



We previously noted that the Enhanced Merchant Reporting (EMR) system available from First Hawaiian Bank is capable of showing users how and where moneys are spent so that users can negotiate better discounts from suppliers and ensure reporting compliance. The SPO told us that departments interested in using EMR were initially trained via a webinar provided by the bank. Thereafter, departments were told they could make arrangements with the bank to access and use EMR. We find this level of guidance from the SPO to be inadequate. The cost efficiencies possible through the use of EMR have not been sufficiently realized because the SPO has failed to earnestly assist executive departments in making EMR's existence known and readily available.

In a best practices study for purchasing cards sponsored by Visa, the certified public accounting firm of Deloitte & Touche LLP saw a need to strike a balance between controls and efficiency for purchasing cards when establishing required approvals for purchasing items. The study suggested designing a purchasing approval process that balances the requirement to exercise appropriate controls with minimizing the cost and time required to purchase a product or service.

The SPO has stated that decentralization of the pCard program was the result of a lack of resources to adequately manage the program from within the SPO. Overall, decentralization has worked because it gives individual departments the flexibility to tailor programs to their specific needs. However, by focusing mainly on controls, the SPO has lost sight of what the pCard program was designed to do, namely, to streamline government procurement in terms of manpower, time, and cost.

***SPO's anticipated cost savings associated with the pCard have not been achieved***

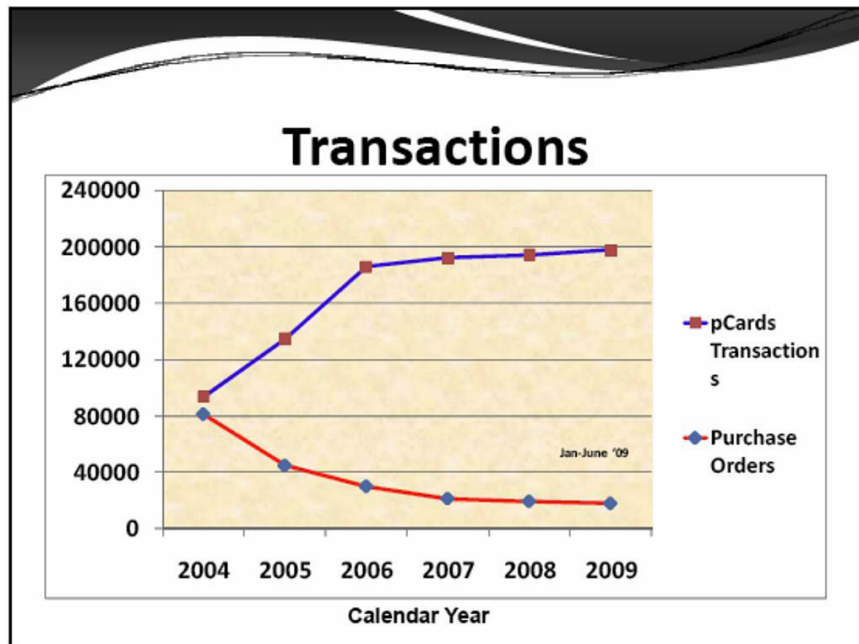
Despite claims that the pCard program has generated substantial savings through the use of pCards instead of purchase orders, the SPO cannot identify where, nor quantify how much, savings have been achieved by the program. Instead, the SPO relies on the National Association of Purchase Card Professionals' (NAPCP) calculations. Furthermore, we found that barriers in the pCard program's processes prevent executive agencies from achieving the full benefits of the program.

At the inception of the pCard program, the SPO identified possible benefits such as the elimination of purchase orders and processing of individual invoices, reduction of expenses, improvement of efficiency, and streamlining of purchasing by empowering employees to obtain necessary goods and services. The office announced to state chief procurement officers that the pCard would reduce processing time and cut costs considerably, with total costs reduced to as little as one-tenth the cost of processing a purchase order. Instead, we found the pCard program's processes to be as cumbersome as the purchase order process it was designed to replace.

### SPO's cost savings estimates are unreliable

According to the SPO, the pCard program has generated savings for executive branch agencies of \$2.3 million in 2005, \$1.2 million in 2006, \$1 million in 2007, and \$113,832 in 2008. The SPO derived this reduction in administrative costs by multiplying the decrease in the annual number of purchase orders (a figure obtained from DAGS) by \$68 (the NAPCP's figure for savings per purchase order), as shown in Exhibit 2.5. The SPO could not provide documentation on how the NAPCP arrived at the figure of \$68 per purchase order, but did provide documentation from a 2007 Purchasing Card Benchmark Survey showing a savings of \$69 per purchase order. The survey did not show the methodology for calculating the savings.

**Exhibit 2.5**  
**Chart Showing Decline in Number of Purchase Orders Processed**



Source: State Procurement Office

The NAPCP's calculated savings of \$68 per purchase order may not accurately reflect Hawai'i's savings per purchase order. The SPO administrator stated that at the federal level, the cost to process a purchase order is about \$75 to \$100. The State's cost could be similar,

with pCard transactions costing less. However, the SPO staff have not performed any calculations using actual state information and are relying on the NAPCP for statistics.

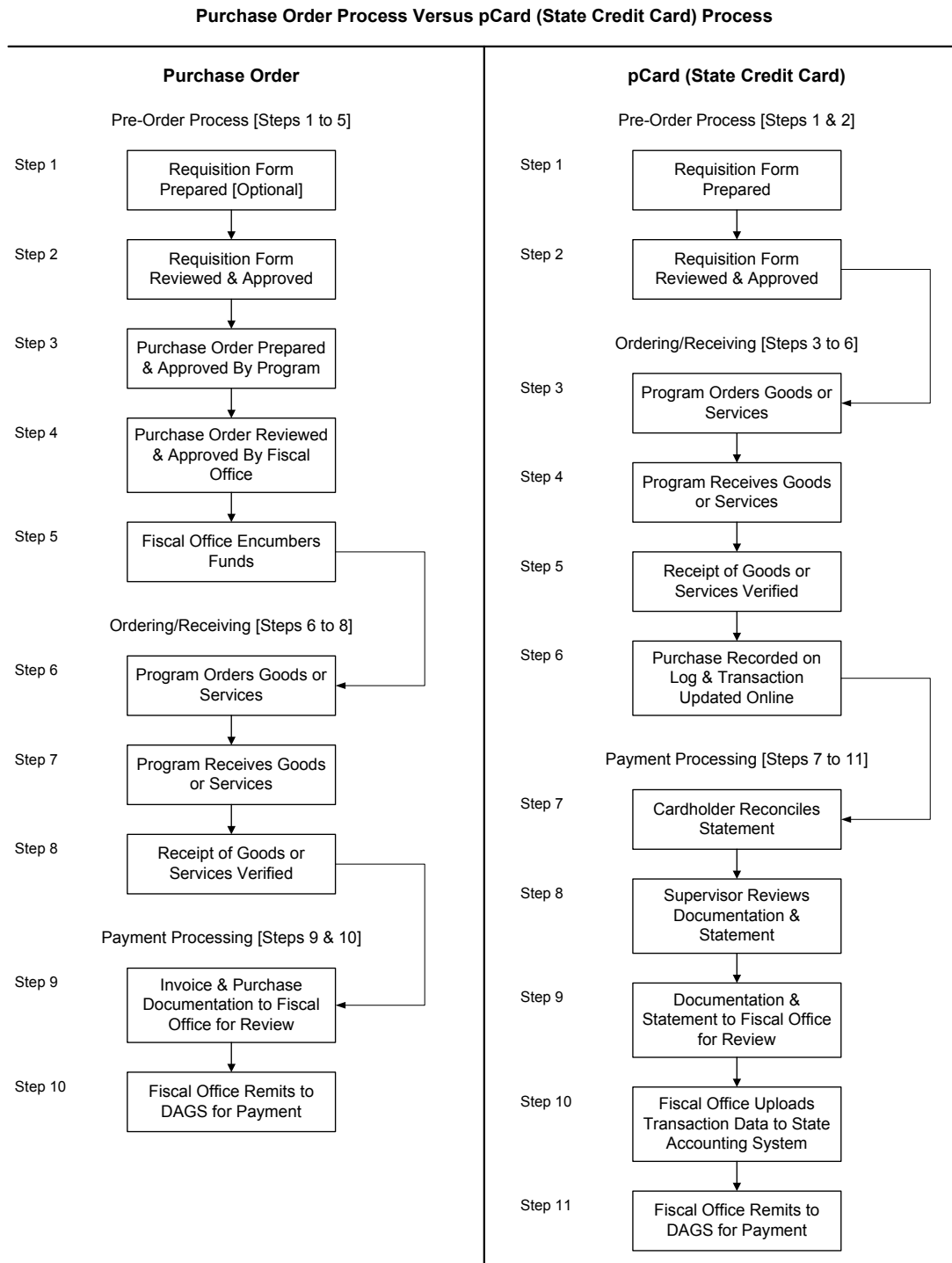
The SPO assistant administrator also told us that savings are generated from the amount of time it takes staff to process the purchase order, including time for accounting and issuing the check. However, she added that the SPO has not done an analysis of such savings using figures from Hawai'i since the SPO does not have the resources to do so.

The pCard program manager annually reviews pCard transactions and usage and includes those figures in her training materials for pCard administrators. The manager stated that Hawai'i's pCard usage is comparable to other states of similar size. However, she neither documents this analysis nor compares Hawai'i's usage statistics to any criteria. Unless actual savings using Hawai'i's figures are calculated, the SPO has no idea of the true cost savings of its pCard program.

### **Departmental pCard process diminishes cost savings**

We found the pCard processes implemented by the departments we reviewed were similar to the processes they used to review, approve, and file purchase orders. In fact, department pCard processes may have even more steps than the purchase order process. Exhibit 2.6 compares the purchase order process and the departmental pCard process. As shown in the exhibit, the departmental pCard process has more steps than the purchase order process.

**Exhibit 2.6  
Comparison of Purchase Order Process and pCard Process**



Source: Data compiled by Office of the Auditor and the Department of Accounting and General Services

Notable similarities between the two processes include the use of a requisition form and multiple reviews and approvals of the purchase. We also noted that the departments perform month-end reconciliations and reviews of pCard purchases, steps that do not exist in the purchase order process.

From inception, the pCard program was intended to free employees to perform more meaningful and productive program tasks. Yet, when we asked the SPO what progress has been made on this objective, the pCard program manager responded that the SPO did not know whether employees had been freed because the SPO has not measured work performance. Again, the SPO has not studied the issue.

Since the SPO has not conducted a cost/benefits study, we referred to a study of the federal purchase card program to illustrate potential savings. That study of the federal program was conducted at about the same post-inception point as Hawai'i's program is now. The U.S. Army Audit Agency (AAA) conducted the study and issued its report dated January 7, 1997 quantifying the cost to process a purchase order versus the cost to process a credit card (pCard) transaction.

The AAA found that the average cost to process a purchase order was \$155.09 while a credit card purchase cost \$62.49 to process, a savings of \$92.60 (60 percent) per transaction. The AAA also found that the Army's credit card procedures could still be improved for additional cost savings. For example, even with the credit card, numerous approvals were required. By eliminating formal pre-purchase approvals for most purchases and by reviewing purchases after completion, the AAA found the Army could still maintain an adequate level of management control. Likewise, we found similar pCard procedures in Hawai'i that could be eliminated without compromising management control.

Additionally, the AAA found that a cardholder, an approving official, and a program coordinator all reviewed and reconciled credit card statements, resulting in redundant reconciliations. Approving officials only need to review statements to verify that items purchased were legitimate and that cardholders have reconciled their statements. Program coordinators should rely on summary reports from the bank and random oversight audits. Again, we found similar redundancies during our audit and recommend their elimination.

### **Departments have not realized significant cost savings or reduction of workload**

In terms of cost savings, all three departments we sampled were unsure of any savings attributable to the pCard program. According to the DOT business management officer, cost savings are difficult to quantify. She

said, “As compared to the [purchase order] process, the pCard review process has been condensed in spurts, but it’s the same amount of work, or more.” The DHS procurement and supply specialist stated that although she has not performed any calculations on cost or time savings, she feels the pCard program is working well. The DHS money payments staff supervisor said that, overall, “There’s not any less work, but also not any more work. It’s just a shifting of workload.” Similarly, DOH has not performed any studies to determine the effects or savings of the pCard; however, its staff did say that the pCard is “a lot of work.”

Compared to the purchase order process, the DOT believes DAGS benefits from pCard use, since there are fewer summary warrant vouchers to prepare for each transaction. The DHS Money Payments section is still processing about the same number of purchase orders as before implementation of the pCard program, but the Pre-Audit section has seen a decrease. According to the DOH Administrative Services Office, the pCard has improved procurement because it has decreased the amount of paperwork associated with purchase orders. However, although the DOH uses similar forms for pCard purchases and purchase orders, the pCard requires more work than the purchase order. Additional pCard steps include reconciliations and card maintenance, such as increasing and decreasing card and single transaction limits, and issuing and cancelling cards.

We asked the three departments whether they had any other comments on the pCard program, with mixed results. One department stated that employees were apprehensive at first because it was a new process. Some felt it would increase their workload, but now that the program is operational, the employees are happy with the program. Another department told us that since purchases are audited after the fact, any damage from losses is already done—as opposed to a purchase order, where payment could be withheld. Although the department cannot envision going back to the purchase order process because of the processing time, it raised concerns regarding overspending and the inability to check what employees are purchasing before the transaction is made. One department official said departments “don’t see the monster” the pCard program can become. A third department asked whether we would recommend eliminating the pCard program; one staff member remarked that there are employees who “would be happy that they don’t need to do all that paperwork.”

Based on departmental feedback, not all executive departments are satisfied with the pCard program. As a whole, staff could not say that the benefits of the program (rebates, faster delivery of goods, quicker vendor payments, no interest fees due to late payments to vendors) outweighed the administrative burdens associated with the program (concerns regarding post audit process; more paperwork; pCard maintenance

duties). We conclude that the departmental pCard programs, as currently set up, do not achieve the administrative efficiencies they were intended to provide.

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## Conclusion

The pCard program has achieved only limited success in streamlining the state government procurement process, a direct result of the State Procurement Office's surrendering its responsibility for the overall planning and administration of the program. The office has delegated its oversight and monitoring duties to the executive departments without providing the necessary guidance and tools for the departments to best effectuate these duties. In addition, the SPO has not created an environment for open communication among pCard users to share experiences and innovations. It has also failed to provide a mechanism for executive departments to report and provide feedback on their concerns, problems, and other relevant information.

Most importantly, the SPO has failed to quantify the cost savings of the pCard process in comparison to the purchase order process; thus, it has no idea what the true savings to the State are. The SPO also has no idea whether executive departments have implemented laborious pCard processes that may negate anticipated cost- or time-saving benefits. In its role as the pCard administrator, the SPO has the authority to assist executive departments in finding a balance between strengthening internal controls and having simplified, consistent, and efficient pCard processes that achieve the cost savings intended by the pCard program.

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## Recommendations

We recommend that the State Procurement Office (SPO) assume a more hands-on approach to the overall planning and management of the State's Purchasing Card (pCard) Program and play a stronger role as its administrator.

1. The SPO should ensure that the intent of the pCard program—to streamline the state and county government's small purchase payment process—is being met. To address this, the procurement office should:
  - a. Set meaningful goals and objectives for the program and identify how they will be accomplished;
  - b. Devise an action plan to include a timetable indicating how its objectives and policies will be implemented; and

- c. Develop performance measures that are part of the action plan and that compare actual performance with expected results.
2. The State Procurement Office should re-engineer the pCard program by formulating and adopting clear guidance that will help executive branch agencies in achieving consistency and efficiency in operating and administering the pCard program by:
  - a. Analyzing, streamlining, and unifying or codifying the various steps within the pCard program with a focus on simplification, standardization, and efficiency. This may include elimination of multiple reviews and the refinement of the functions and responsibilities of key personnel;
  - b. Identifying and developing data and reporting requirements to assist in streamlining and monitoring the program;
  - c. Issuing minimum core standards and policies for pCard users to simplify and expedite the pCard transaction process; and
  - d. Assisting and being more responsible for program implementation and improving its training to executive agencies.



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## Response of the Affected Agency

### Comments on Agency Response

We transmitted a draft of this report to the administrator of the State Procurement Office on May 11, 2010. A copy of the transmittal letter to the agency is included as Attachment 1. The agency's response is included as Attachment 2.

In its response, the State Procurement Office (SPO) claims that our report contains many misstatements and fails to take into account the limited resources available. The SPO acknowledges our recommendations but states that it has already implemented them or disagrees with their merits.

The SPO claims that our report does not acknowledge the pCard program's success, particularly in reducing the administrative burden of processing numerous purchase orders and vendor invoices. To the contrary, our report does recognize that the pCard program has realized some projected benefits. But the SPO fails to acknowledge, or perhaps is not aware, that the executive departments have replaced the purchase order with a requisition form that similarly requires multiple reviews and approvals. Along with performing month-end reconciliations that did not exist in the purchase order process, the executive departments follow a pCard program process that is as cumbersome as the purchase order process it was designed to replace. The Department of Accounting and General Services (DAGS) may be the only executive department that is benefiting with the reduction in the number of purchase orders.

The SPO also claims that it maintains a "hands-on" and pro-active approach with the executive departments but does not dictate their policy and operational decisions and resources. The office states that the executive departments know best what controls and processes are appropriate to meet their needs within their available resources. We disagree and reiterate support for our recommendation. The SPO is the agency best suited to guide the program statewide. The fact that the SPO has delegated its responsibilities to the executive departments does not relieve that office of these duties. The SPO has not focused on pCard program performance and efficiencies and could do more to guide the executive departments by providing alternative procedures and processes to select from for their respective departments. A perceived shortage of resources does not absolve the SPO of these responsibilities.

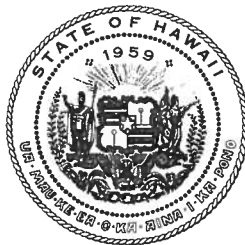
The SPO also states that it has focused more extensively on internal controls with operational efficiency efforts secondary, which supports our finding that the SPO has lost sight of what the pCard program was also designed to do; namely, to streamline the State's small purchase payment

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process. We maintain that the executive departmental pCard programs, as currently operated, do not achieve the administrative efficiencies they were intended to provide.

We stand by our findings.

STATE OF HAWAII  
OFFICE OF THE AUDITOR  
465 S. King Street, Room 500  
Honolulu, Hawaii'i 96813-2917



MARION M. HIGA  
State Auditor

(808) 587-0800  
FAX: (808) 587-0830

May 11, 2010

*COPY*

Mr. Aaron S. Fujioka  
State Procurement Administrator  
State Procurement Office  
Department of Accounting and General Services  
Kalanimoku Building  
1151 Punchbowl Street  
Honolulu, Hawaii'i 96813

Dear Mr. Fujioka:

Enclosed for your information are three copies, numbered 6 to 8, of our confidential draft report, *Management Audit of the State's Purchasing Card Program*. We ask that you telephone us by Thursday, May 13, 2010, on whether or not you intend to comment on our recommendations. If you wish your comments to be included in the report, please submit them no later than Tuesday, May 18, 2010.

The Governor and presiding officers of the two houses of the Legislature have also been provided copies of this confidential draft report.

Since this report is not in final form and changes may be made to it, access to the report should be restricted to those assisting you in preparing your response. Public release of the report will be made solely by our office and only after the report is published in its final form.

Sincerely,

A handwritten signature in cursive script, appearing to read "Marion M. Higa".

Marion M. Higa  
State Auditor

Enclosures

LINDA LINGLE  
GOVERNOR

AARON S. FUJIOKA  
ADMINISTRATOR



PROCUREMENT POLICY BOARD  
LESLIE S. CHINEN  
DARYLE ANN HO  
KEITH T. MATSUMOTO  
RUSS K. SAITO  
PAMELA A. TORRES

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SPO 10-152

May 20, 2010

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OFC. OF THE AUDITOR  
STATE OF HAWAII

Ms. Marion M. Higa  
State Auditor  
Office of the Auditor  
465 South King Street, Room 500  
Honolulu, Hawaii 96813-2917

Dear Ms. Higa:

This is in response to your May 11, 2010 letter inviting our comments to the confidential draft report, *Management Audit of the State's Purchasing Card Program*, hereafter referred to as 'Report'. The State Procurement Office (SPO) is encouraged that the Report "... found no improper, fraudulent, or abusive purchases and noted that charges were for legitimate state business purposes." In this finding the audit has served a purpose in validating that the SPO's pCard program and overall system with its internal control provisions and security features have been successful.

There is always room for improvement, and SPO acknowledges there may be more that the pCard program can do for the State and counties. When the pCard program was launched in 2001, the SPO Administrator met with the State Legislative auditor in early 2002 to share his thoughts about the pCard program initiative and asked for feedback at any time to assist our efforts. No feedback was provided even though the auditor's office is the user of the pCard program since 2005; and has never taken advantage of the PVSnet system and has not been utilizing the on-line reconciliation process and currently has not transitioned to CentreSuite. The Report failed to recognize that the State's pCard program actually effectively began in 2005 with the Administration's support for mandatory use for purchases less than \$2500, and today still continues to develop and broaden its horizons.

The Report is based on a "Perfect World" scenario, on the ideal premise that SPO has infinite resources (funds and staffing) to administer and manage the statewide pCard program. It fails to take into account the limited resources available to government as a whole. The Report delves into areas that are not under the purview of the SPO and has channeled our limited resources in correcting many misstatements ultimately creating a counterproductive activity in responding to the Report's many non-substantive matters as if having merit.

Our comments to Chapter 2 of the Report to clarify and correct many misstatements are provided herein.

**Page 17 - Chapter 2 – “*The State’s Purchasing Card Program Has Not Realized Its Full Potential for Success*”**

The SPO pCard program is an encompassing statewide program utilized by departments as well as most jurisdictions, including the Judiciary, Legislature and all counties. The program has been exceptionally successful, particularly considering the limited resources available to implement a statewide, multi-jurisdictional program. It is unfortunate that the Report does not acknowledge this pCard program’s success as being an example of how a single initiative having positive systemic affects for State and county governments and the business community was accomplished with very nominal resources allocated by the SPO. Contrary to the overall tone of the Report this was accomplished through research, planning, collaboration and communication with all affected parties and methodically and deliberately moved forward through each phase of the pCard program. The benefits and achievements of the program objectives have been numerous for the State, counties and the business community.

**pCARD BENEFITS TO THE STATE & COUNTIES**

- Reduced the amount of purchase orders and processing of individual invoices.
- Reduced the amount of individual checks to vendors - one monthly check to financial institution.
- Increased efficiency for the State & counties.
- Goods and services are received faster.
- Reduced expenses - a purchase order costs between \$100-\$150 to process.
- Improved efficiency - 80% of the checks volume represents 20% of expenditures.
- Significantly reduced late payment fees.
- Rebates are received based on the State’s net purchasing volume.

**pCARD BENEFITS TO BUSINESSES**

- Expedited payment to vendor from within 30 days versus within three days.
- Reduced costs due to eliminating invoicing, accounts receivables, and deposits.
- Guaranteed payment - no credit risk to businesses.
- Enhanced customer relations.
- Improved businesses cash flow as payment is received within a few days.
- Increased efficiency for the business community.

**pCARD ACHIEVEMENTS OF PROGRAM OBJECTIVES**

- Reduced administrative costs associated with purchase orders.
- Maintained and improved controls on purchasing activities.
- Captured detailed expenditure data on every transaction.
- Increased employee’s ability to devote more time to their program’s mission and goals.
- Enhanced relationship with business community.

SPO achieved these objectives by methodically planning and developing guidelines and policies as tools to assist departments and jurisdictions in efficiency and cost savings. SPO provides all users, with the pCard program and procedures manual, forms, circulars, and memoranda, easily accessible on the SPO website at <http://hawaii.gov/spo>; select *pCard (purchasing card)* from the menu to view:

General Overview

Purchasing Card Program and Procedures (Manual)

Emergency pCard Notification Procedures

Cardholder Agreement

Purchasing Card Agreement (FHB)

Commercial Account Set-Up Information (sample)

Transaction Log (sample)

Instructions to Interface to pCard Transactions (FAMIS)

Procurement Circular 2003-06

State of Hawaii Purchasing Card (Program Overview)

Amend 1 Restricted and Blocked Purchasing Card Transactions

Amend 2 Management Oversight and Controls

Amend 3 Merchant Category Code

Amend 4 Rebate

Amend 5 SPO Price List Vendors

Amend 6 Frequently Asked Questions

Amend 7 Restricted and Block Purchasing Card Transactions

Amend 8 Emergency pCard

Amend 9 State of Hawaii Emergency pCard

Comptroller's Memoranda:

2004-36 Mandatory Use of pCards

2005-08 Clarification on Mandatory Use of pCards

2005-10 pCard Charges Made Prior to Receipt of Goods

2005-14 Encumbering pCard Transactions

2007-20 Documentation Requirements for Purchases of Goods or Services

2008-23 Documentation Requirement for Payment of pCard Charges

Training information is also available at <http://hawaii.gov/spo>, click on *Training for State and County Procurement Personnel* to view applicable workshops.

In addition assistance is provided to develop departmental policies and procedures as desired. SPO does not impinge on any department's and jurisdiction's determination to develop policies and procedures that best fit their requirements. For example, the respective Chief Procurement Officers for the Judiciary, House of Representatives, and Senate are the Administrative Director of the Courts, Speaker of the House of Representatives and President of the Senate and we would not interfere in their policy and operational decisions as they are responsible for the policies and resources of their respective jurisdiction.

The SPO utilized statistical reports from First Hawaiian Bank (FHB) and CentreSuite an online management tool, to carefully review and monitor pCard transaction activities and measure the program's progress. SPO has an open communication line between FHB, departments, and participating jurisdictions that allows a free flow of ideas and encourages open dialogue for discussion of issues and concerns.

The Report failed to recognize that the State's pCard program is in its developmental stage and continues to broaden its horizons. SPO's emphasis on internal controls was the primary focus of attention and we are pleased that the audit has determined that "no improper, fraudulent, or abusive purchases and noted that charges were for legitimate state business purposes".

As the departments and jurisdictions become more comfortable with the use of the pCard and the various management features such as approval modules for streamlining processes, advance reporting data for management analysis, and unusual transaction reports, additional benefits and efficiency will ensue for detecting potential misuse to even further minimize risk to the State and counties. SPO continues to work with the pCard provider, departments and participating jurisdictions to take advantage of technological advances in the field of purchasing cards and explore ways the pCard can enhance their ability to streamline, maintain, and control purchasing activities and gain further efficiencies.

**Page 17 – “SPO’s Hands-off Administration of the Purchasing Card Program Has Limited Its Broader Benefits”**

The Report states that SPO has a 'hands-off' policy shifting responsibility to the departments is erroneous. SPO maintains a "HANDS-ON" administrator role, but does not dictate departmental or jurisdictional policies. SPO thoroughly embraced its administrator role in the pCard program by conducting extensive preparatory work with the contractor, the affected unions, chief procurement officers of each participating jurisdiction, and pilot agencies, including informational sessions, prior to launch. A proactive approach was applied to ensure departments and jurisdictions were knowledgeable on program policies and procedures through training workshops. Training was, and is continuously available to assist all departments and jurisdictions. Systemic issues are addressed immediately and departments and jurisdictions are kept abreast via procurement circulars, memos, and pCard workshops of updates and changes. For example, customized hands-on training was coordinated by SPO with the pCard contractor, FHB, demonstrating the online system for each department and jurisdiction. With the upgrade from PVS Net to CentreSuite, the online reconciliation system, guidelines were customized to each department and jurisdiction at SPO's insistence to ensure departments and jurisdictions would have maximum flexibility to use the program tailored to their requirements and to fully comprehend the advantages of the new program. In addition, continuous efforts such as weekly phone conferences are conducted between SPO and FHB to monitor any on-going issues or upcoming events. Ad hoc meetings are held to inform departments and jurisdictions of updates or changes to the program, such as the Enhanced Merchant Report (EMR). SPO has the responsibility to provide all the information necessary for departments and jurisdictions to conduct pCard activities to best meet its operational needs. SPO does not dictate departmental or jurisdictional policies and procedures, and does not interfere with their operation and management control or their resources. Departments and jurisdictions know best what controls and processes are appropriate to meet their needs within its available resources; and responsible and accountable for every expenditure and pCard transaction.

SPO diligently evaluates and monitors the program's performance. Every month FHB generates reports for SPO detailing transaction and expenditure volume. Quarterly rebates outline each departments and jurisdiction's shared participation. Other reports, i.e. year-to-date, life-reports, pCards by department, transactions by department and expense category or merchant category codes are used to monitor and evaluate the program's progress.

**Page 18 – “The pCard program has realized some projected benefits, but not others”**

SPO disputes this statement, and the Report that further criticizes SPO for not “*building a more efficient and streamlined procurement system...*”. SPO has achieved the projected benefits of the pCard program which has provided departments and jurisdictions with the tools to substantially reduce the number of purchase orders issued, and a quick and efficient payment system for vendors.

The Report acknowledges limited benefits, but diminishes the SPO achievement on the entire program. The benefits to departments and jurisdictions are notable and should be extolled for its contribution to the success of the pCard program. Departments and jurisdictions received goods and services quicker, obtained rebates totaling more than \$1.4 million for the period 2008 to 2010, and reduced the administrative burden of processing numerous vendor invoices and purchase orders, distributing and mailing vendor payment checks, and bookkeeping the accounts.

In 2004, for the departments there were an estimated 86,500 purchase orders versus 11,800 pCard transactions; a ratio of 7 to 1. Realistically that amounts to an average of 7,208 checks processed per month for purchase orders issued, versus an average of 50 checks to FHB processed per month for departments for pCard transactions resulting in staggering efficiency and cost savings.

In 2009, there were approximately 16,000 purchase orders versus 170,000 pCard transactions, a ratio of 1 to 10. The number of checks issued was reduced significantly by replacing the cumbersome and more costly purchase order process with the pCard thereby achieving efficiencies. The Report failed to recognize the obvious, that the reduction in the number of checks issued is an efficiency component of the pCard program.

Executive Branch Departments/Agencies Details By Fiscal Year		
Fiscal Year	Est. No. of Purchase Orders (for major object codes)	Est. No. of pCard Transactions
2004	86,534	11,870
2005	70,267	90,387
2006	31,152	155,917
2007	21,132	171,000
2008	20,845	188,339
2009	15,975	170,504



The pCard program has greatly benefited vendors who are guaranteed payment and paid within three days, instead of the usual 30 days, or longer period. The business community supported and praised the State for implementing the program, and in many cases vendors have denied acceptance of purchase orders. The pCard has enabled vendors to lessen or replace their tedious and costly accounts receivable system which was maintained to accommodate government purchase orders. Today the pCard business environment provides departments and jurisdictions the ability to purchase services, such as airline tickets, interisland barge service, and online purchases which would otherwise not be possible if still using the purchase order process.

The benefits are evident. The Report did not find a single instance of pCard abuse.

**Page 18 – “SPO is the administrator of the pCard program but has shifted its responsibilities to the executive departments”**

Again, the SPO maintains a “HANDS-ON” administrator role, but does not dictate departmental or jurisdictional policies. The SPO provides guidance to departments and jurisdictions. SPO implemented the pCard program in a decentralized procurement environment. Decentralization allows departments and jurisdictions to tailor their operational requirements within its available resources. The pCard is not to be confused with any method of procurement; the pCard is an alternate form of payment to replace the purchase order whenever appropriate. It is not within the SPO authority to dictate purchase order procedures nor impose uniform departmental or jurisdictional policies or procedures for pCard transactions because departments and jurisdictions vary in complexity, resources and comfort levels.

There is no dispute that SPO is responsible for ensuring the program is running according to the terms of the contract with FHB. SPO is continuously in contact with FHB to monitor for any compliance issues; thus far all terms have been fulfilled or exceeded.

**Page 20 – “SPO has no overall plan for the pCard program and is not measuring its progress”**

We disagree. We believe the goals, objectives and policies as outlined in our annual report to the Legislature is well-defined. It states that “customer satisfaction surveys will be developed for and distributed to targeted groups.” Will “conduct analysis of expenditure and pCard usage reports obtained from the pCard system. . .” “annual reviews will be done to measure monetary savings . . .”

SPO measures performance using various reports provided by FHB, i.e. ongoing expenditure data reports. SPO continuously evaluates the program. Weekly conference calls, adhoc meetings, and telephone conversations are held with departments and jurisdictions to address any issues or concerns.

**Page 20 subheading – “pCard program lacks overall planning”** - SPO has very thoroughly and meticulously planned the pCard program moving deliberately in developing the internal controls. These deliberate actions resulted in no inappropriate use, fraud or abuse, from over reaching and operating hastily at optimum level with the increased potential of exposing the State and counties to unacceptable risk for misuse and abuse. The plan for the growth of the program is a methodical approach to expand into areas that currently are not being used, for example, mandatory usage at a higher dollar volume, debit cards or travel card, encourage and promote advanced reporting programs for departmental and jurisdictional administrative use.

The current pCard contract allowed for an extension to 2012. However although SPO was extremely satisfied with the performance of FHB, in 2008 the SPO analyzed the credit card industry which had undergone changes and new offerings, infusing numerous technological improvements and therefore determined to obtain an improved product for our user departments and jurisdictions. SPO re-issued the solicitation, RFP No. RFP-09-039-SW for *Furnishing, Implementing, and Supporting a Purchasing Card Program for the State of Hawaii*, in 2009 to take advantage of these enhancements and changes, instead of waiting to 2012.

SPO affirms that the SPO administrator is responsible to oversee and review the State's procurement practices; however, this should not be confused with auditing practices. The Report repeatedly refers to the National State Auditors Association (NSAA) best practices. SPO is not an audit agency, nor does it possess any auditors or trained personnel capable of carrying out an audit of the magnitude recommended by the Report. Nor do we think this is necessary. The Auditor's office and Department of Accounting and General Services (DAGS) Audit Division has the professional staff with the capability to perform audits. SPO would not duplicate these agencies' audit responsibilities as this would be wasteful.

**Page 21 subheading – “Goals are nonexistent”** – We disagree. As stated in SPO's 2009 annual report on goals, objectives and policies, we plan to “continue to provide training and support for departments to maintain and increase levels of efficiency for small purchase procedures with the use of pCards. Establish annual meeting of fiscal officers to network, open discussion of issues or concerns, and provide management reports to assist in the analysis of purchasing activities. Integrate the pCard as the preferred method of payment into price list contracts and HePS purchases. Develop a program to conduct periodic audits of compliance with program procedures.” Most of our goals have been accomplished or partially accomplished. The development of a program to conduct periodic audits of compliance with program procedures is still a goal, but our limited resources have not allowed this to be accomplished as of yet.

The auditor's lack of knowledge of government procurement practices is evident in the suggestion to include vendor discounts as a pCard program goal. Procurement methods are detailed in the procurement code and Hawaii administrative rules, which results in a contract for the needed goods or services. Vendor discounts and rebates are achieved by competition through the procurement process whereby companies compete to be the awardee of the pCard contract and vendor discounts, rebates or other incentives would be addressed through the procurement process. Additional vendor discounts can be achieved when offered in the original solicitation and contract agreements.

**Page 22 subheading – “Objectives and policies are vague”** - The Report is contradictory. It first states that the objectives and policies are vague on page 22, however on page 24, the Report states that “The SPO written objectives are clear and concise.” The Report also insinuates that SPO's pCard objectives were randomly chosen and stuck into the plan which we disagree with. SPO methodically and conscientiously developed the plans and objectives to achieve the most feasible results.

SPO's response for achieving the objectives is through training on the pCard guidelines and policies and applicable methods of procurement. It is the departments and jurisdiction's responsibility to train their cardholders on specific departmental or jurisdictional procedures and requirements and ensure staff attends all applicable training. This allows departments and jurisdictions the flexibility of effectuating policies and procedures that adequately meets their needs and ensures that they are engaged directly in the responsibilities associated with their pCard usage.

**Page 24 subheading – “Action plan is ineffective”** – SPO's plan has always been to diligently forge ahead to accomplish the goals and objectives as detailed in the annual report on goals, objectives and policies to the Legislature with the limited resources available, in a timeframe that is practical for the program. SPO is definitive on the progress and achievements of the pCard program. The one-year plan to “. . . refine management reports to assist departments in analyzing purchasing activities and to detect unauthorized purchases, fraud and abuse,” has been achieved through MasterCard's EMR and CentreSuite's reporting module. These reporting programs are available to all departments and jurisdictions, which may be utilized to analyze purchasing activities. It is the department's and jurisdiction's decision on how they utilize these reports in conjunction with their operation and oversight responsibilities. The two-year plan to “Establish the pCard as the primary form of payment for small purchases” for departments has been achieved with the Comptroller Memorandum 2004-36, Mandatory Use of pCards, which is still in effect. Also every SPO solicitation reinforces this requirement by including provisions on the use of the pCard for purchases less than \$2,500.

All executive branch departments transitioned to CentreSuite as of June 2009, which is contrary to the Report statement “*However, not all departments have converted from the old PVSnet system to the CentreSuite system.*” on page 26. The CentreSuite has additional reporting capabilities to assist departments and jurisdictions to monitor their pCard usage.

The Report misrepresents the pCard audit function. The reporting system, via CentreSuite or EMR, serves as an audit function permitting departments and jurisdictions secure access to expenditure data for review and analysis, and cardholder account activity. The 2009 SPO request for proposal No. RFP-09-039-SW for *Furnishing, Implementing, and Supporting a Purchasing Card Program for the State of Hawaii*, requires the vendor to have an audit program which would give departments and jurisdictions the opportunity to perform internal reviews. It is not a third party examination of transactions as conducted by a licensed auditing firm. SPO is not an audit agency, nor does it possess any auditors or trained personnel capable of carrying out an audit of the magnitude recommended by the Report.

**Page 26 subheading – “Performance measures are deficient”** – We disagree and believe the performance measures are more than sufficient for the pCard program requirements and needs. Monthly, quarterly, and annual expenditure reports are generated by the pCard system provided by FHB. SPO continuously monitors and evaluates the progress of the pCard program, through the reporting mechanisms and constant communication with departments, jurisdictions and FHB to make the pCard an efficient and effective payment tool for the State and counties.

**Page 28 – “SPO’s oversight and monitoring of the executive branch agencies could be improved”**

There is always room for improvement in every aspect of government, and SPO has chosen to balance its finite resources to fulfill its program needs. The pCard program is one of numerous programs and services offered by SPO. To overly utilize its resources directed to the pCard program would be wasteful. The SPO oversight encompasses various programs, services, activities under HRS Chapter 103D and Chapter 103F, usually on a statewide basis, and includes all branches of governments (Executive, Legislative, Judicial), and the counties. A brief listing of SPO’s Programs, Services and Activities follow:

- **Procurement Policy Board** is the authority to adopt Hawaii Administrative Rules (HAR) for the applicable statutes; SPO provides administrative and clerical support services such as drafting HARs, preparing for monthly meetings, conducting public hearings, etc.
- **Legislation** is developed or reviewed and testified on at the Legislature on procurement matters to promote efficiency and effectiveness for the State and counties.
- **Hawaii Administrative Rules** for HRS Chapters 103D and 103F are developed to establish and amend procurement policies and procedures to maintain a highly ethical and professional procurement program.
- **Health and Human Services program** (HRS Chapter 103F) develops, coordinates and manages the statewide process for purchases of health and human services.
- **Community Council on Purchases of Health and Human Services** provides overall support to the Council.
- **Procurement Circulars and Procurement Directives** are established and managed, and available on the SPO website.
- **Procurement Training** available to Executive branch departments and jurisdictions; plans, directs and coordinates education programs for all State and county procurement personnel to ensure the highest degree of professionalism.
- **Private Sector Workshops/training** for vendors, contractors and service providers seeking to do business with the State and counties are conducted.
- **Hawaii Electronic Procurement System (HePS)**, an online procurement system is administered and managed for all State and county procurement personnel; vendors, contractors, and service providers register online to receive notifications.
- **Hawaii Compliance Express (HCE)**, an online system to verify vendor compliance with statutes prior to award of a contract.
- **Procurement Notices System (PNS)**, an online system for procurement notices available to vendors, contractors, and service providers to view available solicitation notices.
- **Procurement Reporting System (PRS)**, an online system for contract award information.
- **Procures** or supervises the procurement of all goods, services, and construction; investigates and resolves bid protests or recommends appropriate action.
- **SPO Price and Vendor List Contracts** - Issues and manages 50+ statewide contracts for use by State and county agencies and available on the SPO website; including coordination, administration and management of cooperative agreements such as the Western States Contracting Alliance (WSCA).

- **pCard Program available to all departments and jurisdictions that are subject to compliance with HRS Chapter 103D, Hawaii Public Procurement Code.**
- **SPO website** contains links to SPO online systems (ie HePS, PNS, PRS, HCE, etc), various procurement information, including statutes and rules, directives and circulars, guidance and training, notices, etc. that is constantly undergoing updates to managed and maintained the systems and the numerous information.
- **Contract Administration** - Manages the various contracts issued by SPO, executes supplemental contracts on changes and amendments, extensions, etc.
- **Chief Procurement Officer (CPO) requests** from executive departments for procurement exemptions to HRS Chapter 103D and Chapter 103F, sole source and emergency purchases, contract extensions, restrictive and crisis procurements, and procurement violations are action items.
- **Advise and assist** all State and county agencies on all aspects of procurement such as interpreting the law and rules, procurement processes to use, protest process, etc.; also addresses inquiries from the public on procurement related matters.
- **Reviews procurement practices** of State and county purchasing agencies for compliance with procurement laws and rules.
- **Hawaii Products program** administers and manages the certifications for various Hawaii products.
- **Inventory Management** administers the centralized statewide Fixed Asset and Inventory System (FAIS), a computerized property inventory records system.
- **Property Disposal applications** are action items.
- **Excess State Property** listing available on the SPO website monthly for states agencies to re-utilize excess property from other agencies at no cost to agency.
- **Surplus Property** manages program to acquire, store, transfer and distribute Federal and State surplus property to state and county government agencies and eligible donees (ie. educational and homeless programs, 8(a) disadvantage businesses, etc.).

In recent years, retirements of SPO procurement staff, and the freeze on hiring, the SPO was not allowed to fill vacant positions with qualified replacements. SPO has gone from 23 positions to a current count of 13 and out of the 10 vacancies, 5 purchasing specialist vacancies alone amounted to over 140+ years of procurement experience lost due to retirements with no replacements. Additionally, the Inventory Management program is 100% vacant, the 2 positions vacant due to retirement. SPO's compliance staff is 100% vacant due to retirements. The clerical support staff has been reduced by 50%. To fulfill the Report's "Perfect World" scenario, at a minimum, two FTE positions would be required to meet the recommendations as proposed by the Report.

SPO will continue to oversee and monitor the departments and assist jurisdictions to maintain the no abuse level. SPO does not interfere with a department's or jurisdiction's operations, instead continues to provide them with the management tools, via pCard program and procedures manual, circulars, memoranda, and training, to develop appropriate policies and procedures consistent with their operational needs and available resources. Contrary to what is stated in the Report, SPO utilizes FHB reports for monitoring purposes and measuring performance of the overall pCard program. Reports are generated on a regular basis, and ad hoc reports are generated upon request. SPO has an open door policy which encourages the pCard program manager and pCard administrators to frequently converse sharing ideas and concerns.

To accurately measure the cost savings associated with the pCard and for the utmost efficiency the State would need to pursue electronic reporting, data integration between systems, online statement delivery, electronic review and approvals, and automatic transaction reconciliation. A major overhaul of the State's 27-year old financial management system; accounting functions and activities would be required in order to accomplish this feat which would cost an estimated \$25 to 50 million to overhaul. The SPO does not have the authority or the needed funding to pursue the major overhaul of the State's accounting and financial management system.

**Page 28 subheading – “SPO’s guidance for the pCard program is insufficient”** – We disagree with this statement. To ensure compliance, SPO provided the departments and jurisdictions with the tools necessary to operate a successful pCard program. However, the SPO has not and will not interfere with department and jurisdiction responsibilities to establish their own procedures as they are responsible for their transactions and resources. The SPO provides guidance through the pCard program and procedures manuals, Comptroller memoranda, procurement circulars, and training. The information is distributed and is readily available through the SPO website. SPO has made itself accessible through e-mail, telephone and face-to-face meetings and training workshops. Departments and jurisdictions may report problems, issues or concerns through any of these media. SPO is in continuous and close communication with departments and jurisdictions and has not received any reports on any problems or violations relating to the pCard program which is consistent with the auditor’s finding that “. . . no improper, fraudulent, or abusive purchases and noted that charges were for legitimate state business purposes”. The SPO pCard training is an overview of the entire program, highlighting the responsibilities of the cardholders. It would not be practical to conduct training on department or jurisdiction procedures as they vary by departments and jurisdictions. SPO guidance is unrivaled as evident by the lack of any incidence of inappropriate use of the pCard.

**Page 29 subheading – “Oversight and monitoring reports are available, but barely used by SPO or departments”** - SPO utilizes various reports produced by FHB from both the CentreSuite’s reporting module and FHB data banks. FHB reports include the Monthly Expenditure Report, and the quarterly reports which are used to compile statistic, monitor and measure progression of pCard usage, and illustrate savings and rebate revenues for departments and jurisdictions. CentreSuite reports are used to facilitate and monitor expenditure activities by department and jurisdictions. The Multiple Transaction Exception Report (MTER) and the Expense Report were two examples given which have not been activated. The MTER would not be a useful report for SPO without the background knowledge of every cardholder profile in the system and SPO does not have the resources to take on that challenge. The pCard is a corporate liability card, and therefore the Expense Report would not be used as all expenses should be allocated for specific business purposes. Expense reports would typically be used for travel cards, which the State does not currently utilize and may be a future enhancement.

The EMR system is made available to all departments and jurisdictions, and incumbent upon them to utilize this reporting capability. Departments and jurisdictions must make their own determination if the EMR warrants usage or further investigation given their operational needs and available resources.

The conversion to CentreSuite was completed in June 2009. Most of the departments and jurisdictions concentrated their efforts in the transition and may consider the reporting module as need arises and resources permits. It is not appropriate for SPO to determine department's or jurisdiction's timetable or whether EMR or CentreSuite reports will fulfill their requirements.

**Page 31 subheading – “SPO has not implemented an effective system for sharing innovation and experiences”-** In the 2007 meeting for fiscal officers, networking opportunities were provided to share experiences and provide insight for the less experienced departments and jurisdictions. The SPO administrator was available at fiscal officers' meetings where executive departments were able to use this venue to address issues and network with other departments. Many of the issues and concerns are discussed on an ongoing basis and had been previously addressed, so there was little need to be repetitive. In the pCard training, cardholders are invited to share experiences, issues or concerns.

Pursuant to Procurement Circular 2003-06, Amendment 4, departments were instructed on the disposition of the FHB rebates. The requirement of allocating the rebates to non-general funded programs are in accordance with the applicable statutory requirement as established for those funds, and is not a requirement by SPO. Rebates are the result of collective transactions by the State and all participating jurisdictions through the terms of the original solicitation. The *Purchasing Card Program and Procedures*, and training materials and workshops will be updated to further remind departments and jurisdictions on the rebate program to share experiences.

**Page 36 – “Executive Branch Agencies’ Purchase Card Programs Lack Streamlined Procedures That Could Save Time and Money”**

The suggestion that streamlining uniform procedures could save time and money is generally reasonable. However, SPO does not control departments' or jurisdictions' operational decisions or their resources. Departments and jurisdictions have created their own procedures based on their need to balance efficiency and risk. It is not appropriate for SPO to impede operational decisions or to usurp their responsibilities by dictating their operations and allocations of their resources.

**Page 36 – “Concerns of inadequate internal controls have been unfounded”**

We are pleased with this finding.

**Page 37 subheading – “Departments’ internal controls for pCard purchases are adequate” -**

SPO appreciates the auditor's acknowledgement that the internal controls to prevent and detect fraud are adequate. It is ironic that the report would contain examples of some other state's abuse, i.e. diamond band, fox fur stole, car payment, which confirms SPO's insistence on stringent controls and security features to avoid such incidents. Departments and jurisdictions should be acknowledged for their diligence which has resulted in minimizing risk to the State and counties.

**Page 39 subheading – “SPO has focused on internal controls not operational efficiencies” -**

SPO has focused more extensively on internal controls with operational efficiency efforts secondary. The program is in its sixth year of mandatory usage and it was imperative that internal controls were the primary focus before moving forward. It would have been counterproductive to allow the program to hastily move forward without the necessary controls and expose the State and counties to heightened and increased risk for abuse and criticism that would ensue. The SPO training and materials are focused on controls and security. Armed with the tools provided by SPO, the departments and jurisdictions are in the best position to determine the procedures necessary to streamline their operations and gain additional efficiencies.

The Report suggest that using EMR could result in savings by showing users how and where funds are expended so that users can negotiate better discounts reveals the lack of understanding of the Procurement Code. There are specific guidelines to follow, based on dollar thresholds and procurement methods. A buyer cannot simply contact a vendor asking for discounts based on amounts charged to the pCard. The pCard program is bound by contractual agreements, through the terms of the original solicitation, and any changes are contractual issues made through supplemental contract agreements.

SPO actively encouraged participation in the EMR training and earnestly promoted the benefits of the EMR. SPO registered all departments and jurisdictions in the EMR, and were encouraged to participate and to take advantage of the EMR system as they can utilize the data to meet their needs.

The SPO provides guidance to departments and jurisdictions. SPO implemented the pCard program in a decentralized procurement environment. Decentralization allows departments and jurisdictions to tailor their operational requirements within its available resources. The SPO concentrated more extensively on internal controls but has not lost sight of the efficiencies that can be gained in terms of resources and cost.

There should never be too much emphasis or concerns placed on pCard internal controls and security features to protect taxpayers from unauthorized and improper spending. We are always cognizant of the potential for misuse and abuse. Even with all the control provisions and security features we have in place, it is still dependent on the behavior of the 3900 cardholders. Below is a sampling of headlines that we have diligently worked toward avoiding:

Government workers sometimes abuse credit cards *Without proper oversight, employees use cards for personal expenses* - <http://www.creditcards.com/credit-card-news/government-employee-credit-card-abuse-1282.php>

Investigators probe Hanford purchase card use – <http://www.thenewstribune.com/2010/04/06/1136988/fraud-probe-to-look-at-hanford.html>

2<sup>nd</sup> ex-Hanford employee indicted in P-card fraud - <http://www.tri-cityherald.com/2010/04/16/978214/2nd-former-hanford-employee-indicted.html>



Three more indicted in Hanford purchasing fraud -  
<http://www.hanfordnews.com/2010/04/23/15227/three-more-indicted-in-hanford.html>

Credit card fraud, misuse found at 5 Florida universities - [http://articles.sun-sentinel.com/2010-04-19/news/fl-university-credit-cards-20100419\\_1\\_credit-card-universities-credit-limits](http://articles.sun-sentinel.com/2010-04-19/news/fl-university-credit-cards-20100419_1_credit-card-universities-credit-limits)

City pays for auditor's Colorado lawyer license -  
<http://www.cggazette.com/index.cfm?dsp=news.view&nid=2355>

Chesapeake man sentenced in government fraud case -  
<http://www.norfolk.com/2009/11/chesapeake-man-sentenced-government-fraud-case>

Palm Beach County schools audit finds fraudulent purchases, more than \$220,000 in lost records; prosecutors to weigh criminal charges -  
<http://www.palmbeachpost.com/news/schools/palm-beach-county-schools-audit-finds-fraudulent-purchases-55787.html>

Four UF employees resign after fraud accusations -  
[http://www.alligator.org/news/uf\\_administration/article\\_24b6cc40-fb0b-55ae-84be-b721a61bcd3e.html](http://www.alligator.org/news/uf_administration/article_24b6cc40-fb0b-55ae-84be-b721a61bcd3e.html)

Ex-Interior exec pleads guilty to credit-card misuse -  
[http://www.washingtonexaminer.com/local/112708\\_Ex-Interior\\_exec\\_pleads\\_guilty\\_to\\_credit-card\\_misuse.html?c=y](http://www.washingtonexaminer.com/local/112708_Ex-Interior_exec_pleads_guilty_to_credit-card_misuse.html?c=y)

Lingerie, iPods on government credit cards -  
<http://www.cnn.com/2008/POLITICS/04/09/gao.spending/index.html>

Attorney General Baker Indicts Former Georgia Tech Employee in Massive Purchasing Card Abuse Case -  
[http://www.georgia.gov/00/press/detail/0,2668,87670814\\_103214659\\_109802758,00.htm](http://www.georgia.gov/00/press/detail/0,2668,87670814_103214659_109802758,00.htm)  
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Regents credit card audit finds fraudulent charges -  
<http://www.redandblack.com/2008/03/19/regents-credit-card-audit-finds-fraudulent-charges/>

Georgia System's Investigation of Purchasing Card Fraud Finds \$350,000 Theft -  
<http://chronicle.com/article/Georgia-Systems-Investigation/40289/>

Meals, gas put on Knox p-card tab -  
<http://www.knoxnews.com/news/2007/nov/13/meals-gas-put-on-knox-p-card-tab/?partner=RSS>

DPS probes exec's use of debit card -  
<http://detnews.com/article/20070501/SCHOOLS/705010388/DPS-probes-exec-s-use-of-debit-card>

Homeland Security Department Is Accused of Credit Card Misuse  
<http://www.nytimes.com/2006/07/19/washington/19cards.html>

2 employees suspected in P-card fraud -  
[http://wc.arizona.edu/papers/98/238/01\\_4.html](http://wc.arizona.edu/papers/98/238/01_4.html)

Procurement Card Fraud - [http://govpro.com/technology/gov\\_imp\\_27902/index.html](http://govpro.com/technology/gov_imp_27902/index.html)

Audit Uncovers Credit Card Abuse At Usda -  
<http://news.google.com/newspapers?nid=861&dat=20030713&id=oLAbAAAAIBAJ&sjid=SloEAAAAIBAJ&pg=6728,2688408>

Arrests made in fraud case involving state employees -  
<http://www.chipleypaper.com/articles/arrested-5329-wildlife-individuals.html>

Navy Sailors Used Gov't Credit Cards to Hire Prostitutes -  
<http://www.foxnews.com/story/0,2933,65051,00.html>

Probe Finds Interior Dept. Employees Used Gov't Credit Cards for Casino,  
Jewelry - <http://origin.foxnews.com/story/0,2933,49932,00.html>

Former FAA Employee Jailed for Government Credit Card Fraud -  
<http://www.oig.dot.gov/library-item/2840>

**Page 41 – “SPO’s anticipated cost savings associated with the pCard have not been achieved”**  
The Report criticized SPO for not performing any calculations using actual State information and relying on the figures by National Association of pCard Professionals (NAPCP). The SPO does not have the resource for such study, even if it did, would not waste resources to determine the obvious. Numerous reputable organizations have done these studies such as NAPCP and U.S. Army Audit Agency (AAA), therefore it is unnecessary nor wise to expend funds and resources wastefully to conduct additional studies. Businesses worldwide rely on third party industry studies to benchmark their progress. The SPO’s cost savings are conservative and considerably lower than if SPO used the Report’s reference AAA saving figures.

**Page 42 subheading – “SPO’s cost savings estimates are unreliable”** - SPO’s cost savings estimates are based on statistics provided by the NAPCP and the “2007 Purchasing Card Benchmark Survey Results” (RPMG Research Corporation) of \$68.00 savings per transaction. The program cost savings are unquestionably conservative. By the auditors own sources, the AAA the State should be saving \$92.69 per transaction. The cost savings of \$68.00 per transaction is a reliable indicator of the pCard program’s calculated savings.

**Page 43 subheading – “Departmental pCard process diminishes cost savings”** - The Report comparison chart on purchase order process versus pCard process is incomplete. The chart failed to reflect that the purchase order process takes place for every single purchase order transaction, which for a department can run into the hundreds each month versus the pCard process which is done once a month as a consolidated payment thereby eliminating many of the purchase orders processes and the hundreds of checks for these purchase orders. The chart also neglects to take into account what happens after the fiscal office remits to the DAGS for payment. The following are the additional Purchase Order steps that were missing in the Report:

- Step 11 DAGS reviews the purchase order/summary warrant vouchers.
- Step 12 DAGS issues check.
- Step 13 Returns the check to the department as applicable, or mails the check to the respective vendor adding the cost of postage and processing for each mailed check.
- Step 14 DAGS bookkeeping services for coordination of processing of financial transactions into FAMIS; including daily system reconciliation.
- Step 15 Tracking cancelled, lost or stolen checks, which may require reissue of another check.

A department can pay the same vendor multiple times in a one month period. In the pCard process, the payment steps are done once a month in one department consolidated statement to FHB. The vendors have already been paid through FHB therefore no additional paperwork for the vendor is needed which has diminished the business community's cost of doing business with the State and counties.

In fiscal year 2004 approximately 7,211 checks per month were issued by DAGS to vendors (assuming one check per purchase order) plus approximately 30 checks to FHB for a total of 7,241 checks. In 2009 approximately 1,331 monthly checks were issued by DAGS to vendors (purchase order generated), and an average of 50 checks were processed to FHB for a total of 1381 checks. That is an astounding 5860 fewer checks per month that were issued. The cost savings and efficiencies are obvious. Fewer checks issued, less work involved, increased efficiency for the State and counties and the business community.

**Page 45 subheading – “Departments have not realized cost savings or reduction of workload”**

The statement that departments have not realized cost savings is erroneous. The decrease in number of purchase orders and summary warrant vouchers alone is a significant cost savings, as evidence by prior statements. The pCard has created a shift in workload. Employees are no longer processing thousands of purchase orders and issuing multiple checks.

The ability to research and compare information for travel activities on-line and purchase airline tickets on-line is a cost savings in itself. Prior to the availability of the pCard, an individual would need to use their personal charge cards for travel arrangements incurring expenses and requiring subsequent reimbursement. Rebates, faster delivery of goods and services, expedient vendor payment, no interest or late fees are additional benefits versus the purchase order process. In addition, the Report does not acknowledge the tremendous benefits gained by the business community.

### **Page 47 – “Conclusion”**

The pCard program has been, and continues to be an overwhelming success. At the time the pCard program was initiated SPO’s goal was to make the pCard program available to all departments and jurisdictions that are subject to compliance with HRS Chapter 103D, Hawaii Public Procurement Code. SPO undertook the challenge and established the pCard program that has grown to encompass 3900 cardholders with an annual expenditure of over \$104 million used by 19 executive departments and 14 other governmental jurisdictions. There is a free flow of communication between departments, jurisdictions and SPO, exchanging ideas and addressing concerns. With no legislative support in terms of funding or staffing, SPO is performing remarkably.

SPO rolled out the pCard programs to all departments and participating jurisdictions, established pCard policies and procedures, functions as the liaison between cardholders and FHB. SPO has identified and quantified cost savings in the areas of efficiency and rebates. As the pCard administrator, SPO embraces the challenge to continue supporting and providing guidance to departments and jurisdictions in the effort to maximize efficiencies and cost savings, while allowing them reasonable flexibility to determine their appropriate course of action. SPO should be commended for their diligent efforts to move the State into the 21st century with the pCard program. It is unfortunate that the Report reflects a negative approach to the pCard program instead of providing more constructive feedback. The sensational tone of the Report focused on non-substantive matters as if having merit.

### **Page 47 – “Recommendations”**

SPO acknowledges the recommendations by the Report; however, most of the recommendations have already been accomplished. Meaningful goals and objectives as well as performance measures for the program have been established. Identifying and developing data and reporting requirements to monitor the program have been achieved. SPO issues guidelines and procedures for the departments and jurisdictions to incorporate into their program. The SPO has been responsible for program implementation and will support departments and jurisdictions in their training efforts.

As stated earlier, to accurately measure the cost savings associated with the pCard and for the utmost efficiency the State would need to pursue electronic reporting, data integration between systems, online statement delivery, electronic review and approvals, and automatic transaction reconciliation. A major overhaul of the State’s 27-year old financial management system; accounting functions and activities would be required in order to accomplish this feat which would cost an estimated \$25 to 50 million to overhaul. The SPO does not have the authority or the needed funding to pursue the major overhaul of the State’s accounting and financial management system.

The Report is recommending the streamlining for only executive departments. For clarification, does “executive branch agencies” include the Department of Education, University of Hawaii, Hawaii Health Systems Corporation and the Office of Hawaiian Affairs? If they are included, you believe the pCard administrator can in effect impose by requiring processes and directing their resources which would likely conflict with a department or jurisdiction’s independence and autonomy. If not included, why would uniform processes and directing their resources work for some executive departments, but not the others?

Why are the other State jurisdictions for example, the Judiciary and the legislative branch not included? For a comprehensive and accurate audit, why wasn't the other branches of State government reviewed as part of the audit to provide a more balanced perspective? Shouldn't the ". . . uniform processes and methods to accommodate the program . . ." be applicable to all, including the Legislature and its attached agencies, since the SPO is the pCard administrator for not only the departments but all participating jurisdictions? If yes, you are saying the pCard administrator can in effect impose by requiring processes and directing the jurisdiction's resources which would likely conflict with their jurisdictional independence and autonomy. If no, why would uniform processes and directing their resources work for executive departments, but not the other State jurisdictions?

If by answering that the pCard administrator should be "analyzing, streamlining and unifying or codifying the various steps within the pCard program with a focus on simplification, standardization, and efficiency." only applies to departments under the SPO administrator, who serves as that jurisdiction's Chief Procurement Officer, then the Report's intent is to create two sets of standards. One for the departments under the purview of the SPO administrator and one for the other 19 statutorily designated Chief Procurement Officers. We will not impose two standards.

As a user of the pCard, why didn't the Report include the auditor's office first-hand experience and share their policies, procedures and processes involved to help in the "streamlining" and to improve the pCard program?

The SPO as the pCard administrator for the departments and all participating jurisdictions will continue to provide the leadership and remain in the forefront of the pCard industry as we have. We see no merit or purpose to re-engineer the pCard program as suggested in the Report and will continue to utilize our finite resources as we have and will be shortly awarding a new contract in response the 2009 SPO request for proposal No. RFP-09-039-SW for *Furnishing, Implementing, and Supporting a Purchasing Card Program for the State of Hawaii*, for purchasing card services that will include the latest industry advances. SPO has consistently provided clear guidance to departments and jurisdiction to help them achieve cost savings and efficiencies. The departments and jurisdictions are responsible and accountable for their expenditures and SPO will continue to support them but not interfere with their policy and operational decisions and resources.

Sincerely,



Aaron S. Fujioka

- c: The Honorable Linda Lingle, Governor
- The Honorable Colleen Hanabusa, Senate President
- The Honorable Calvin Say, Speaker of the House
- The Honorable Russ Saito, Comptroller