
SOUTH FLORIDA WATER MANAGEMENT DISTRICT



Audit of Small Purchasing Practices

Report #00-04

Prepared By
Office of Inspector General

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SOUTH FLORIDA WATER MANAGEMENT DISTRICT

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MGT 08-06F

February 1, 2001

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RE: Audit of Small Purchasing
Practices –
Audit # 00-04

This audit was performed pursuant to the Inspector General's authority set forth in Chapter 20.055, F.S. The audit focused on the adequacy of small purchasing practices. Our audit analyzed purchasing patterns during FY98, FY99, and FY00. Detail testing was limited to the first half of FY00. Fieldwork was conducted between March 2000 and November 2000. This report was prepared by Chris Flierl.

Sincerely,

Allen Vann
Inspector General

AV/cf
Enclosure

c: Frank Finch
James E. Blount

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INTRODUCTION

This audit examines the adequacy of the District's small purchasing practices. In each of the past three fiscal years, small purchases have exceeded \$35 million and 23,000 transactions annually. During FY00, these purchases accounted for almost \$40 million in District expenditures. We conducted our audit pursuant to our approved annual audit plan.

BACKGROUND

For purposes of the audit, we defined a "small purchase" as any purchase made using a purchase order or a credit card.

Purchase orders include several different procurement instruments: centralized purchase orders, decentralized purchase orders, and price agreements. A description of each of these purchase instruments follows.

Centralized Purchase Orders

Centralized purchase orders can be used for any purchase for which a purchase order is appropriate (as opposed to a contract). Centralized purchase orders have no dollar limits and they are available District-wide. Because of this, centralized purchase orders account for the highest dollar value of small purchases but are used less frequently than decentralized purchase orders. Between FY98 and FY00, procurements made using centralized purchase orders have ranged between \$28.2 and \$32.7 million annually. Centralized purchase orders account for over 80% of the dollar value of small purchases.

During this same time period the number of centralized purchase orders issued has decreased from 7,243 to 5,255. The number of transactions, as a percent of total small purchase transactions, has been steadily decreasing from 30% in FY98 to 22% in FY00. This decrease appears to correspond with increases in credit card usage. One of the drawbacks of using a centralized purchase order is that the process generally takes longer. Centralized purchase orders are processed through the Procurement Department. As such, it is not the preferred purchasing instrument for field personnel who often need to make quick purchases for necessary repairs. Notwithstanding, field personnel are required to use a centralized purchase order for all purchases exceeding \$750. While this instrument can be used to purchase anything, it is used most often for high-ticket items such as automobiles, heavy equipment, chemicals,

computer equipment, and any other high dollar procurements not requiring a contract.

Decentralized Purchase Orders

Decentralized purchase orders are used primarily by field stations and other District units who conduct remote operations. Decentralized purchase orders were designed to provide a timely means of making emergency purchases and are limited to \$750 per purchase. They do not require any competition. The low dollar threshold keeps the relative dollar value low, but the number of transactions high. Between FY98 and FY00, decentralized purchase orders ranged between \$1.9 million and \$2 million annually. This represents only 5% to 6% of total small purchase expenditures. More decentralized purchase orders were issued than any other small purchase instrument, ranging from 10,700 to 12,250 for the same period. This represents between 46% to 52% of the total small purchase transactions.

The Procurement Department has no authority over decentralized purchase orders; rather the field unit has complete autonomy in selecting which vendor to use. The field location is fully responsible for the preparation and issuance of these purchase orders. The types of purchases made using this instrument range widely, including auto and marine parts, hardware, and other maintenance and repair type goods and services.

Price Agreements

Some commodities are acquired through price agreements formulated through a competitive bidding process. The vendor that is awarded the price agreement is required to provide the District with a commodity at a fixed price for a specific period of time. Once a price agreement is arranged by Procurement, end users may purchase directly from the vendor without the Procurement Department's involvement. While the number of purchases under price agreement falls well below centralized or decentralized purchase orders, they do, however, represent the second highest transaction in terms of dollar amount. For the past three fiscal years, price agreements have increased from \$3.7 million to \$4.6 million, representing between 10% and 12% of total small purchase dollar volume. Conversely, the number of price agreement transactions has decreased during this period from 3,570 to 3,195, representing from 15% to 14% of total transactional volume. Items purchased under price agreement

include such things as fuel, water, mobile radios, welding gas, newspaper advertising, and many other items which the District buys in sufficient volume to justify the extra effort of developing competitive price agreements.

Procurement Card

The District's Procurement Card is a credit card administered by a competitively selected financial institution. It is an alternative to the decentralized purchase order and provides field personnel with a more efficient system for making purchase transactions under \$500. It is more efficient because, unlike decentralized purchase orders, the approval for credit card purchases occurs after the purchase has been made. The Procurement Card Program started in FY98 and has made significant gains since that time. Total credit card purchases in FY98 totaled \$59,000 but by FY00 purchases had increased tenfold to \$537,000. The number of transactions increased from 750 to 4,296 during that same time.

The Procurement Card Policy places several restrictions on credit card usage. For example, they are not to be used to make purchases for travel, gasoline or fuel, telephone charges, or inventory items. Credit cards are used to purchase computer peripherals, lab equipment, air conditioning and locksmith services, books and other relatively inexpensive items.

Standards for Competition

The District's standards for competition during the time of our audit fieldwork were as follows:

Total Purchase Amount	Minimum Standard for Competition	
Up to \$5,000	None	Verbal quotations highly desirable
Over \$5,000 up to \$25,000	Yes.	At least 3 written (or faxed) quotations required
Over \$25,000	Yes.	Request for Bids or Requests for Proposals required except for non-construction procurements of \$100,000 or less.

Subsequently, on October 4, 2000, the District increased its standards of competition by doubling the purchasing thresholds.

The District's Procurement Policy addresses special procurements for which the standards of competition are waived. Examples include

procurements using State of Florida Department of Management Services, the U.S. General Services Administration, or other government procurement contracts.

When applied to the various purchasing instruments, the standards of competition do not require competition for over 80% of the small purchase transactions. This includes all decentralized purchase orders, all credit card purchases, and centralized purchase orders less than \$5,000. These non-competed purchases represent over \$8 million in expenditures annually, or approximately 20% of the total dollar volume.

OBJECTIVES, SCOPE, AND METHODOLOGY

The objectives of our audit were to:

- determine whether procurement policies are being complied with,
- evaluate the adequacy of procurement policies and internal controls for small purchasing, and
- ensure that current practices result in obtaining fair and reasonable prices.

The scope of our audit included all purchases made with purchase order instruments and credit cards. We analyzed purchasing patterns during FY98, FY99, and FY00. Detail testing was limited to the first half of FY00.

The methodologies employed during our audit included:

- reviewing purchasing policies, procedures, and practices,
- reviewing relevant laws and regulations,
- analyzing the vendor database,
- performing detail testing of selected purchasing transactions, and
- interviewing personnel.

Our audit was conducted in accordance with generally accepted government auditing standards.

FINDINGS AND RECOMMENDATIONS

RESULTS IN BRIEF

CURRENT PRACTICES DO NOT ALWAYS FULLY COMPLY WITH ESTABLISHED POLICIES

Our audit procedures revealed that purchases are often made before decentralized purchase orders are issued and approved. In addition, decentralized purchase orders are being issued to cover apparent cost overruns, i.e. when vendors' invoices exceed centralized purchase order arrangements made by the Procurement Department, field office personnel, have on occasion, issued a decentralized purchase order to make up the difference.

POLICIES AND CONTROLS NEED IMPROVEMENT

While small purchasing practices follow a generally consistent pattern, written policies and better internal controls are needed to prevent the splitting of purchases into smaller components thus avoiding competition requirements. Price Agreements are sometimes inadvertently bypassed or ignored in favor of purchasing from higher priced vendors. Internal controls relating to segregation of duties between ordering and receiving functions need to be implemented. More clearly defined and disseminated procedures and increased use of procurement cards would result in a more efficient and faster small purchasing system. Finally, the Procurement Department needs to develop a formal vendor approval process prior to registering vendors in the District's vendor database.

OPPORTUNITIES TO INCREASE COMPETITION

Our testing did not reveal any departures from the District's Standards of Competition for purchases greater than \$5,000. However, for procurements of \$5,000 or less, for which there are no standards of competition, the District may not be getting the most competitive prices. This is because staff tends to use favored vendors.

CURRENT PRACTICES DO NOT ALWAYS FULLY COMPLY WITH ESTABLISHED POLICIES

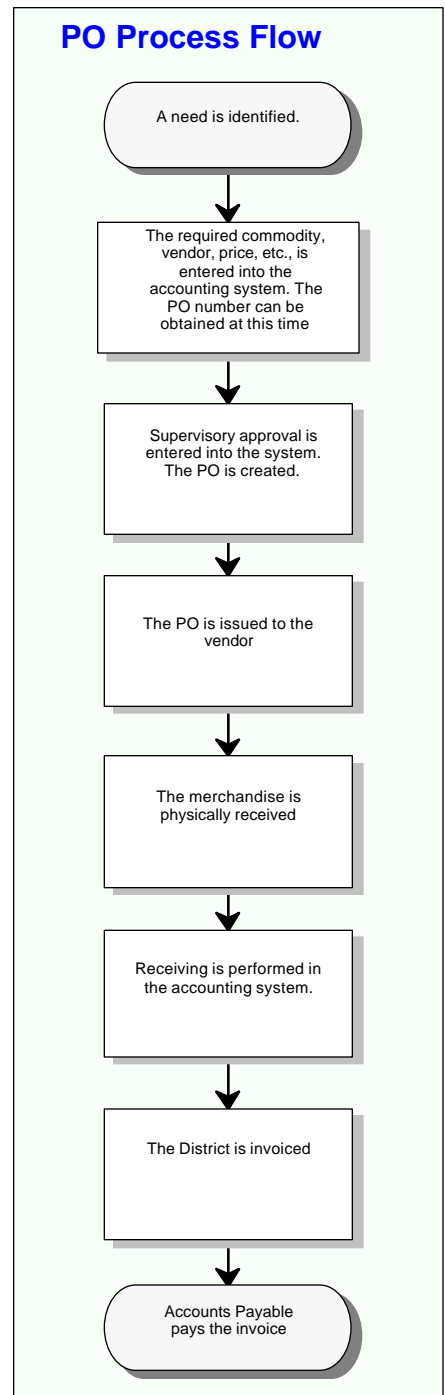
Decentralized Purchase Orders Used To Procure Goods and Services Prior to Approval

For decentralized purchase orders, merchandise is frequently ordered, received, and invoiced by the vendor prior to District personnel processing and issuing a written purchase order. Prior to generating a purchase order the accounting system allows users to obtain an order number. Users order from vendors prior to generating the necessary paper work. This circumvents the established pre-approval process and creates additional clerical work for the central office support staff.

We selected a judgmental sample of 29 decentralized purchase order transactions to test. Of these 29, 13 (44.8%) were dated after the service had been performed or after the goods had been received¹. This is inconsistent with the established process for issuing decentralized purchase orders.

The flow chart to the right illustrates how the process is designed to work.

Supervisory approval for decentralized purchase orders is an important control feature that prevents inappropriate or unnecessary purchases from being made. In order to generate payment to the vendor for goods and services, an approved decentralized purchase order must be in the system and must indicate that the merchandise has been received. However, staff is not restrained from purchasing without a purchase order. Sometimes staff will wait until they receive an invoice before generating an approved purchase order.



¹ This does not include six other purchase orders issued after the period of service for recurring monthly contractual services.

Part of the reason that purchases are made before they are approved is that the approval process for decentralized purchase orders is assigned to Field Station Directors and Assistant Directors who may otherwise be very busy; thus, creating a bottleneck in the procurement process. The West Palm Beach Field Station, alone, issued 2,440 decentralized purchase orders during FY00. Further delegating the approval for decentralized purchase orders to supervisory level staff at Field Stations would likely reduce the temptation to circumvent the appropriate procedures, which as a rule should be followed.

We also observed that making purchases prior to the creation of a decentralized purchase order causes additional work for Accounts Payable personnel. When invoices are received by Accounts Payable without a purchase order in the system, accounting staff need to determine who placed the order and request that the necessary purchase order be prepared, including getting the necessary approval, and receiving information into the system so that a payment can be processed.

Recommendations

- 1. The accounting system should be modified so that purchase order numbers cannot be obtained until supervisory approval is given.**

Management Response: Management concurs with the recommendation, however, the purchasing software (LGFS) is not designed to allow that type of modification. Accounts Payable will report invoices referencing decentralized purchase order numbers, which are not approved, to the appropriate Field Station Director or Department Director. The correct process will be clearly identified with the development of a procedural instruction for decentralized purchase orders.

Responsible Department: Procurement/Accounts Payable

Estimated Completion Date: May 31, 2001

2. **Further delegate the approval for decentralized purchase orders to field station supervisors.**

Management Response: Management concurs with the recommendation. Delegation of authority will be revised in the Procurement Standards.

Responsible Department: Procurement

Estimated Completion Date: April 30, 2001

Inappropriate Use of Decentralized Purchase Orders

We discovered instances where field personnel issued decentralized purchase orders inappropriately to pay the difference between the amount specified on a centralized purchase order and the amount invoiced by the vendor. In one instance, a centralized purchase order authorized \$1,177 for transmission repairs to a District vehicle. The vendor invoice was \$456 higher than the authorized amount. Instead of providing justification to District Procurement Department staff for the higher amount, field staff issued a decentralized purchase order to enable the Accounts Payable unit to pay the higher amount requested by the vendor.

Likewise, purchases for water level monitoring device parts were authorized using the required centralized purchase order. Several months later, when the order was finally filled, additional charges of \$239, above the original \$4,847 centralized purchase order, were paid for by issuing a separate decentralized purchase order rather than amending the original purchase order.

Use of centralized purchase orders are required for purchases over \$750 to ensure centralized control through the use of a knowledgeable Purchasing professional who is required to obtain the best price for the required goods or services in a consistently applied manner. Additional charges being incurred after a purchase order is issued may mean that the Purchasing Agent did not have complete information when the price was negotiated with the vendor. In the case of the transmission repair, there was a substantial unexplained price difference (39%) between the estimate and the actual cost. Issuing a decentralized purchase order results in a loss of accountability. A procedure should be established that precludes the issuance of decentralized purchase orders to cover additional charges on a centralized purchase order. Instead, the purchasing agent should be contacted and the centralized purchase order modified if justification exists to do so.

Recommendation

3. **A policy should be put in place that prevents issuance of decentralized purchase orders to cover additional charges associated with a centralized purchase order.**

Management Response: Management concurs and will incorporate the recommendation into procedural instructions for decentralized purchase orders. Also, Procurement will closely monitor the award of decentralized purchase orders via LGFS Report DISTP003.

Responsible Department: Procurement

Estimated Completion Date: May 31, 2001

POLICIES AND CONTROLS NEED IMPROVEMENT

Split Purchases Circumvent Procurement Thresholds

Our limited testing revealed that purchases are sometimes “split” into two or more smaller transactions in order to circumvent procurement authorization thresholds.² This practice is prohibited by the Florida Statutes and, to some extent, by District policy.³ The result is that purchases are being made using inappropriate procurement instruments and without the appropriate level of consideration given to price. The reason that this happens is twofold: split purchases are not adequately addressed in the District’s procurement policy, and there are no controls in place to prevent this type of abuse from occurring.

Decentralized purchase orders, which for the most part are limited to remote locations, can not exceed \$750. For purchases in excess of \$750, a centralized purchase order is required. Of 13 suspect transactions selected for more detailed review,⁴ three, in our opinion, represent split purchases. In one instance, two decentralized purchase orders were issued for auto body and paint work, with the same vendor, for the same vehicle for a total of over \$906. In another instance, new mobile radios were installed in District vehicles at a total cost of \$1,124. Two decentralized purchase orders were issued: one for \$495 and one for \$629. All the work was performed on the same day. Lastly, parts were ordered from a diesel supplier prior to the creation of a purchase order.⁵ When the invoice for \$873 was received, two decentralized purchase orders were subsequently issued to pay for it. Water Resources Operations, in their draft procedures, has recommended that the threshold

² For purposes of our audit, a “split purchase” results when the purchase of goods and/or services is broken down into smaller components than necessary so as to fall below some established threshold. The thresholds that we tested were the \$750 decentralized purchase order threshold (13 selections sampled), the \$5,000 threshold for three written quotes (ten selections sampled), and the \$25,000 threshold for Request For Bid (four selections sampled).

³ District policy precludes the splitting of purchases for purposes of avoiding the Standards for Competition but does not address the splitting of purchases for purposes of determining the appropriate procurement instrument.

⁴ Each sample item consisted of two to three separate purchase orders.

⁵ See our previous comments, *Decentralized Purchase Orders Used To Procure Goods and Services Prior to Approval* on page 7.

for decentralized purchase orders be increased to \$2,000. While this might be a more realistic threshold, splitting of purchases should not be permitted.

Next, we tested the \$5,000 threshold. District policy requires that 3 written quotes be obtained. We identified 10 suspicious pairs of centralized purchase orders. Of these ten, four give the appearance of being split purchases. In two of the instances, system limitations were cited as the reason that the purchase was split. In both instances the purchasers thought that the purchase requisition was limited to five line items. Therefore, if the purchase requires additional lines for activity codes, they thought that an additional purchase order must be created. The first pair of purchase orders, issued for \$4,645 and \$3,242, were for various electrical supplies charged to eight different activity codes combined. The second pair of transactions were for the purchase of two generators, split between six different activity codes. Each generator cost \$2,798.

Procurement personnel informed us that up to 99 different activity codes could be used on a single purchase requisition. However, unknown to some system users, after the five line items are entered, the requisition must be “modified.” Procurement personnel should have provided additional training to users in how to modify a requisition. Regardless of the “system’s limitations” there was no other apparent explanation or justification for not obtaining the three required written quotes.

Of the remaining 2 split purchases, one was for painting services. Corporate Resources’ Facilities Planning/O&M unit hired a painting contractor. Two purchase orders were issued to this contractor, one for \$2,760, and the other for \$4,710. Both purchase orders were issued on the same day one after the other. The vendor invoices were dated the same day and were sequentially numbered. The purchase orders and the invoices indicated two different areas that were painted: the loading dock at B-1, and the cooling pipes on top of B-1. While the nature of the work differed in the type of preparation required, the surfaces to be painted, and when painting could be performed, the work for both locations in the same building could have easily been obtained through a single purchase order. Instead, the work was given, without competition, to a vendor that had a history of providing quality service to the District. Logically, proper procurement planning would have dictated combining the work on one purchase order, providing at least two other firms an opportunity to price the work.

For the last split purchase for the \$5,000 threshold, the vendor provided the District with a single quote for various diesel parts totaling \$5,457. Two purchase orders, one for \$1,550 and another for \$3,907, were issued for the parts contained on the quote. Both purchase orders were charged to the same activity code. No other quotes were obtained. The purchaser stated that he made “a mistake” when he charged the same activity code and that the order was split to reflect different pump stations. Again, sound procurement practices would require combining the work and obtaining three written quotes.

Finally, we tested the \$25,000 threshold for the issuance of a Request for Bid (RFB). We identified 4 pairs of multiple transactions, none of which represented split purchases.

In conclusion, our testing revealed that there are insufficient controls in place to detect and prevent split purchasing. Additionally, District purchasers are not provided with any guidance as to what constitutes a split purchase. It also appears that not all system users understand how to properly use the system.

Recommendations

- 4. The District’s Procurement Policy should better define what constitutes a split purchase and state that this practice is prohibited.**

Management Response: Management concurs with the recommendation. Split purchases will be clarified in Procurement Instructions for decentralized purchase orders.

Responsible Department: Procurement

Estimated Completion Date: May 31, 2001

5. **Internal controls should be established that detect split purchasing.**

Management Response: Management concurs with the recommendation. Procurement will closely monitor the award of decentralized purchase orders via LGFS Report DISTP003. Purchasing Agents will be alerted to report any suspected split requisitions to Management for review.

Responsible Department: Procurement.

Estimated Completion Date: January 30, 2001

6. **Consideration should be given to raising the thresholds for decentralized procurements.**

Management Response: Management concurs with the recommendation. The Procurement Standards are being modified to increase the threshold from \$750 to \$1,500.

Responsible Department: Procurement

Estimated Completion Date: April 30, 2001

7. **Procurement should offer guidance in how to modify a requisition so as to accommodate more than five line items/activity codes.**

Management Response: Management concurs with the recommendation. The information will be added to the LGFS training classes that are conducted on a quarterly basis. Information Applications will modify the LGFS training manual to incorporate this information.

Responsible Department: Procurement/Information
Applications

Estimated Completion Date: April 30, 2001

Need For Written Procedures And Better Controls

There are no written procedures that outline how decentralized purchase orders are prepared and issued. This results in inconsistencies, particularly among the field stations, the primary users of decentralized purchase orders. Recognizing this confusion, Water Resources Operations drafted standard operating procedures⁶ that address how their field stations should perform decentralized purchasing. We found this document to be thorough, except that it does not provide for adequate segregation of duties between purchasing and receiving. We also found a similar lack of segregation of duties for centralized purchase orders where purchasers perform the receiving function as well. Not segregating purchasing from receiving increases the risk of asset misappropriation.

Good internal control practices dictate that approvals, record keeping, and asset custody be segregated to the extent possible. This is required in order to minimize the risk of asset misappropriation. A lack of segregation of duties increases the risk that a District employee could order merchandise and convert it for personal use. Both at our headquarters and field stations, storekeepers and other purchasers enter purchases into the system (initiate transactions), take physical custody of purchases, and enter the receiving (record keeping) into the system. While we understand that independent receiving is not always possible, especially when purchasing is done in the field, whenever possible the person acknowledging receipt should be someone other than the person that placed the order.

The lack of written procedures and requirements for processing and reviewing purchase orders also contributes to significant time delays between the placement of an order and receipt of the merchandise. The Procurement department used to routinely investigate open purchase orders; however, this is now performed only on an exception basis or near fiscal year end. We found that, as of March 31, 2000, there were 181 purchase orders worth \$1.4 million over 180 days old. In one case, the purchaser was not aware that decentralized purchase orders could be used for out-of-state purchases. Instead, a centralized purchase order

⁶ *Standard Operating Procedures for Storeroom Activities* address the purchasing function at the field stations. This is a very thorough and comprehensive document replete with flowcharts and narratives of the purchasing process. With added internal control features, this procedure would be a good model for the entire District to follow.

was issued for \$55, well below the \$750 decentralized purchase order maximum, to an out-of-state vendor. The centralized purchase order was issued in October 1999 the vendor invoice indicates that the order wasn't shipped until July 2000, over nine months after the purchase order was entered into the system.

In other cases there were inconsistencies in payment processing. Both the Miami Field Station and the Okeechobee Service Center use the same vendor for film processing but process their transactions differently. The Miami Field Station holds onto all their receipts while the Okeechobee Service Center sends the receipts to the Accounts Payable Section. Monthly, the vendor sends a combined statement to the Accounts Payable Section. The Accounts Payable Section sends the statement to the Miami Field Station who matches their receipts with the statement and then prepares a decentralized purchase order (after the fact). Conversely, the Okeechobee Service Center creates a single decentralized purchase order at the beginning of the year for their estimated annual purchases. Extra clerical work is created and Accounts Payable can only make partial/incomplete payments to the vendor. Written procedures would provide guidance on how to properly process transactions consistently.

Recommendations

8. The District should develop a Purchasing Manual.

Management Response: Management concurs with the recommendation. Procurement will develop a procedural instruction for decentralized purchase orders. In addition, the new procurement manual is in progress, which will contain a discussion on decentralized purchasing.

Responsible Department: Procurement

Estimated Completion Date: June 30, 2001

9. **Procurement should resume the practice of periodically following-up on open purchase orders.**

Management Response: Management concurs with the recommendation. Procurement will follow up on all purchase orders over 45 days late on a monthly basis.

Responsible Department: Procurement

Estimated Completion Date: January 30, 2001

10. **Strengthen internal controls over the purchasing function by segregating the purchasing and the receiving functions to the extent possible.**

Management Response: Management concurs with the recommendation. A District team is being formed to review the feasibility of separating these functions.

Responsible Department: Procurement/Information
Applications

Estimated Completion date: April 30, 2001

Procurement Card Polices Adequate But Program Is Underutilized

Procurement card purchases are being performed in accordance with District policy and are adequately controlled. The *Procurement Card Program Users Manual* is informative and comprehensive. In fact, the District's Procurement Card program comports with practices and controls recommended by the Government Finance Officers Association.

Despite the increases in credit card usage since the program began in FY98, we found that the program is underutilized. The stated goal of the program is to "become the preferred alternative to purchase small dollar items." Since its inception in FY98, the program has been making steady strides towards this end. In FY00, credit card purchases represented 27% of the total purchase transactions under \$500.⁷ However, given that decentralized purchase orders still represent 62% of the purchases under \$500, the Procurement Card has not realized its potential.

There are numerous benefits of a purchasing card program. The cardholder/employee can conveniently make purchases, without a purchase order, from an expanded merchant base, in a more timely manner. This simplified purchasing process provides more information on purchasing histories, and enables better control through purchasing dollar limits. Vendors benefit through expedited payments and reduced paperwork.

There are still many purchases that could have been made more efficiently using a credit card. For example, in FY00, there were 9,752 decentralized purchase orders issued that were less than \$500. This represents over 91% of the decentralized purchase orders issued during the year. Further, there were 1,719 centralized purchase orders under \$500 for which a credit card could have been used. Use of the credit cards could reduce the number of man-hours devoted to clerical tasks associated with purchasing.

The major reason that procurement cards are not being used more often, is that the expenditures are not automatically charged to specific enough account codes in the accounting system. For a business group like Water Resources Operations, the intended primary beneficiary of the Procurement Card program, this is unacceptable. They need to account

⁷ The limit for Procurement Card transactions is \$499.99. Purchases under price agreements, petty cash and check requests were not included in this calculation.

for all the costs associated with their activities. To accurately classify credit card purchases would require an additional manual procedure. Instead, it is easier for them to continue to use decentralized purchase orders. An automated distribution system that will address this problem has been developed and is currently being tested. If successful, we would anticipate a dramatic increase in credit card usage. We recommend that the testing of the distribution system be completed expeditiously and implemented.

Recommendation

- 11. Complete the testing of the Procurement Card Distribution System and make it available District-wide. Continue to monitor and encourage Procurement Card usage.**

Management Response: Management concurs with the recommendation. The testing of the Procurement Card Distribution System is in process and estimated to be completed in February 2001. Subsequently, it will be made available District-wide.

Responsible Department: Procurement/Information
Technology

Estimated Completion Date: April 30, 2001

Controls Over Price Agreements Are Inadequate For Inventory Items

As stated in the background, a price agreement with a vendor is established to obtain the best available price for commonly purchased goods and services for a specific period of time. We found that inventory items under price agreement can be purchased from vendors other than the vendor named in the price agreement. This occurs because there are inadequate controls in place to ensure that price agreements for inventory items are being taken advantage of. As a result, the District may be paying too much for certain commodities.

Commodity codes⁸ are flagged in the accounting system to alert users to the existence of a price agreement that should be used. When a purchaser enters the flagged commodity code on a requisition or a decentralized purchase order, the system notifies the purchaser that the commodity is under price agreement. This feature does not work, however, when the commodity ordered is an “inventory item.”

Purchasers do not always use centralized purchase orders for inventory items as is the recommended practice. Commodity codes for the District’s inventory system are set up differently than commodity codes for non-inventory items. The inventory system uses a sub-code with additional digits. These sub-codes prevent the commodity code flagging that otherwise alerts users to the existence of price agreements, which may result in the use of another vendor at a higher price. For example, the District paid \$4.90 each for rain gear that was under price agreement for \$4.45. If a centralized purchase order had been used, as is recommended for inventory items, the Purchasing Agent would have used the price agreement. However, when a decentralized purchase order is used, as was the case with the rain gear, the additional review by the Purchasing Agent does not occur. Changes to the inventory system would not be cost beneficial at this time. However, inventory system commodity code refinements should be considered when the District acquires a new accounting system.

⁸ A commodity code is an eleven digit number used by the accounting system to identify the various goods and services provided by vendors.

Recommendation

- 12. Purchasers should order inventory items through the centralized purchase order system in order to take advantage of price agreements.**

Management Response: Management concurs with the recommendation. This instruction will be emphasized in the new procedural instructions for decentralized purchase orders. Procurement will closely monitor award of decentralized purchase orders via LGFS Report DISTP003.

Responsible Department: Procurement

Estimated Completion Date: May 31, 2001

Commodity Codes Not Being Effectively Used

Our testing revealed that District purchasers change the product descriptions for commodity codes. This results in District purchasers using commodity codes that were not intended for the actual purchases. For example, the commodity code 63057220000 is for “Paint Enamel, High Performance, Acrylic, Gray Primer.” However, the description had been changed, by District purchasers, to reflect a wide variety of other paint products such as safety yellow. But safety yellow has its own unique commodity code that is not always used when it is purchased. Changing commodity codes weakens accountability by eliminating the means to track commodity purchases and may result in higher costs.

A decentralized purchase order included the purchase of a 3-gallon water cooler, used to store ice and water in the field. The District paid \$22.45 for this item using a commodity code intended for an electric water cooler, the type that dispenses bottled water. The purchaser changed the commodity code description on the purchase order to reflect an item substantially different from what the commodity code was established for. Had the correct commodity code have been selected, it would have been discovered that there is a price agreement for three gallon water coolers at \$17.78.

Sometimes it is not always clear which commodity code should be used. For example, we noted an instance where a field unit issued several decentralized purchase orders for welding gasses using what appeared to be an appropriate commodity code. Like the example above, this resulted in not taking advantage of a price agreement. A price agreement stipulates a cost of \$4.29 for a 124 cubic foot cylinder of oxygen welding gas. What was actually purchased was oxygen in a 141 cubic foot tank for \$5, at a minor additional cost of \$0.01/cubic foot. The commodity code that was used was unaltered by the purchaser and was for “oxygen welding gas.” The purchaser apparently knew that there was a price agreement for the welding gasses but chose to use another vendor for convenience. Doing so was made easier because of the generic commodity code that was already in the system. To remedy this, any purchasing procedures that are developed should address exceptions to using price agreements and commodity codes should be as specific as possible.

Commodity codes, if used correctly, can provide the District with valuable data that would enhance accountability. For example, commodity codes are used to identify products that are under price agreement or that may require resource manager approval. Commodity codes can be used to identify vendors in order to obtain quotes or send out bids. After the purchase has been made, commodity codes can provide the District with a commodity history including how much of a commodity was purchased, by whom, from whom, and for how much. This type of purchasing history will allow the District to make better informed procurement decisions. Allowing purchasers to change the product description of the commodity code greatly diminishes their value and reduces accountability. Instead, each commodity should be assigned a unique commodity code and the accounting system should be modified to prevent changing commodity code descriptions by District purchasers.

Recommendation

- 13. When practical, each good and service purchased should have a unique commodity code.**

Management Response: Management concurs with the recommendation, however, the clean up and modification of the commodity table in LGFS will require many weeks of labor hours. This is a manual task that has not been done since the inception of LGFS in 1991. The LGFS software is likely to be replaced in the next few years. Based on these considerations the significant labor cost does not warrant the reworking of the commodity code system at this time.

Responsible Department: N/A

Estimated Completion Date: N/A

Need To Strengthen Controls Over Vendor Database

The process for adding new vendors to the vendor database is weak and informal. Security over access to the database needs to be strengthened. Also, information in the vendor database is incomplete. Most notably there was a high percentage of vendors without either a required Federal ID or Social Security Number. Currently, there is an unacceptable risk that the District could do business with undesirable vendors.

Adding a vendor to the District's vendor database is as simple as calling the Procurement Department and requesting that a new vendor be added to the database. Procurement inscribes the name of the vendor in a manual log, assigns a vendor number, and adds the new vendor to the database. This enables staff to commence transacting business with the vendor. Procurement follows up later with the *Vendor Information Form* to obtain additional vendor history.

There is no approval process in place to formally document the inclusion of the vendor in the database, an otherwise commonly recognized internal control feature. A good control process would ensure that fictitious vendors and others who should not be doing business with the District are precluded from getting established in the system. Taken further, the approval process should prevent vendors who have a documented history of inappropriate or illegal activity from doing business with the organization.

While we did not identify fictitious vendors in the database, there were 32 instances where current, former, and temporary or leased employees were in the database as vendors. It does not appear that any of these 32 vendors' IDs were established for inappropriate purposes, as we tested for potential conflicts of interest.⁹ We were able to conclude that only a few were established during their time of employment and only one received a payment as a contractor during the period of their employment. We did observe an entry in the vendor database that clearly identified one active vendor as an employee. Two employees that we contacted were surprised to learn that they were in the vendor database because they never requested to be established as vendors. Procurement could not explain

⁹ The Ethics Policy precludes District employees from doing business with the agency in a private capacity.

how, contrary to their practices, employees were established as vendors in the database.

In two instances, we found other evidence that indicates that the vendor was added to the database during District employment. In these cases, the companies' initial filing with the State of Florida, Department of State, Division of Corporations, occurred during the time that the employee/owners were employed with the District. Further, we found another vendor/employee was paid for a commodity while the District employed the owner. This happened one time and was for an insignificant amount. The employee did not appear to have any knowledge of the transaction because he is removed from the day-to-day operation of the business. Further, the person who made the purchase did not appear to be aware that the vendor was also a District employee.

We discovered that numerous individuals have read/write access to the vendor database including Accounts Payable, Procurement, Equity in Contracting, and Information Applications Division programming staff. We also found that there was one individual with read/write privileges who is in an unrelated department. This employee was previously employed in Supplier Diversity (the predecessor to Equity in Contracting) but has not worked there in over three years. Failure to remove database authorization privileges when employees move within the District was also noted in the "IS Security Audit." Steps are being taken to establish a process to reevaluate system access authorization requirements for employees who transfer to another unit.

In addition to the results of our testing above, our review of the vendor database indicates that it is incomplete. Procurement staff indicated that, at a minimum, they require a Federal ID Number or a Social Security Number for vendors to be included in the database. However, there are no controls (such as required fields) in place that would prevent adding a vendor to the database without this information. Our review of 100 vendors in the database revealed that 24 had been established without either a Federal ID or Social Security Number.

One additional observation made about the vendor database is that it does not flag vendors who have been unresponsive to District solicitations. This is reflected in the low response rate¹⁰ for District

¹⁰ The response rate is the sum of the number of responses to solicitations received, and no-bids received, divided by the total number of solicitation packages mailed out.

solicitations. During FY00, the District mailed out 2,321 solicitation packages (56 individual bids) but only received 251 responses and 127 no-bids, a response rate of 16%. The Procurement Department could save considerable administrative time and mailing costs if they used the system's capability of tracking non-responsive vendors.

The bid response rate could also be improved with greater use of the Internet. Internet procurement allows organizations to create a better market, reaching a much larger group of vendors. The city of Dallas has shown an increase in the bid response rate since it started using the Internet. They now receive 17 to 20 bids on some requests, which used to get only two or three. Similarly, Orange County, California, used to get seven or eight bids per solicitation; however, since using the Internet they have increased their response rate ten-fold.

A larger pool of vendors, drawn from a wider geographical area, increases competition, which usually results in lower cost. Private sector firms that have switched to Internet procurement report savings of up to 70 percent. Given the success of Internet procurement else where, the District should consider trying it on a test basis.

Given the control weakness that we noted, a formal vendor approval process should be adopted. This approval process should include:

- documenting who requested the vendor,
- completion of the *Vendor Information Form* by the vendor,
- verifying that the vendor is registered with the state and is licensed to perform the service that they provide,
- requesting a list of officers and registered agents to identify possible conflicts of interest,
- having the vendor sign an affidavit attesting that he/she understands the District's conflict of interest policy,
- creating and maintaining a hard copy vendor file that includes all of the above documentation,
- requiring that a Procurement official verify that all steps in the process are complete and authorize entering the vendor into the database, and
- designating certain fields in the vendor database as "required fields" (e.g. the Federal Identification Number) meaning that a vendor can not be added to the database without data being entered into this field.

Recommendations

14. **Procurement should develop a formal vendor approval process.**

Management Response: Management concurs with the recommendation. A team will be formed to develop criteria and implement a formal vendor approval process.

Responsible Department: Procurement

Estimated Completion Date: May 31, 2001

15. **The feature in the vendor database that tracks vendor solicitation responsiveness should be used.**

Management Response: Management concurs with the recommendation. A team will develop criteria for removal of unresponsive vendors from the bid database and implement a formal process.

Responsible Department: Procurement

Estimated Completion Date: June 30, 2001

16. **Procurement should increase the use of the Internet as a means to increase the bid response rate.**

Management Response: Management concurs with the recommendation. A calendar of current and upcoming solicitations is currently posted on the District x-web. As of October 1, 2000, vendors can download any of these solicitations from the x-web. Procurement will monitor the bid responsiveness rate and if necessary consider posting solicitations on other web sites.

Responsible Department: Procurement

Estimated Completion Date: April 30, 2001

OPPORTUNITIES TO INCREASE COMPETITION

The final objective of our audit was to determine whether current practices ensure that the District is obtaining competitive prices. Our testing did not reveal any departures from the District's Standards of Competition for purchases greater than \$5,000. However, for procurements of \$5,000 or less,¹¹ for which there are no standards of competition, the District may not be getting the most competitive prices. This is because District purchasers tend to use favored vendors.

Our testing revealed that certain vendors are favored and we found instances where this resulted in increased cost to the District. The favoring of vendors raises the question as to whether District purchasers are making sufficient efforts to identify alternative suppliers or if they are just routinely using familiar vendors.

We analyzed purchasing patterns for the six month period ending on March 31, 2000 and think that District staff could do more to spread the work and save money.

Example 1; Welding Wire:

For the first half of FY2000 there were 11 purchases made for welding wire. Eight of the purchases were from the same vendor, while the remaining three were from two other vendors. Seven of the purchases were for .035 weight welding wire and two were for .030 weight welding wire. The remaining two purchases were for other types of welding wire. A significant price difference was noted for a one pound spool of 4043 Aluminum .030 welding wire. The invoice from the favored vendor indicates a unit price of \$7.90 compared to \$4.00 from another vendor. The same was noted for .035 welding wire, \$7.15 compared to \$6.00. The vendor with the better prices is located in Belle Glade; so it is not practical for all of the field stations to use them. However, it does indicate that it might be beneficial for the other field stations to do some comparative shopping instead of relying solely on one vendor.

Example 2; Communications Equipment:

A vendor that provides mobile communications equipment under a price agreement appears to be favored for other commodities and services not covered under the price agreement. We selected six of the most

¹¹ Representing approximately \$8 million in procurements.

frequently used commodity codes associated with this vendor and discovered that no other vendors were used for five of them. However, for the remaining commodity code for “Radio Repair, GE Mobile” there was one other vendor used. The purchasing data reveals that this other vendor performed repairs on mobile radios and has sold ancillary equipment such as antennas, phone mounts and coaxial cable to one of the field stations throughout the year.

Further, we noted that the favored vendor charges \$150 to install a radio where the alternative vendor charges \$125. Additionally, the price agreement lists several other factory authorized service representatives in the area who could install these radios, however, none were used. Staff explained that the favored vendor has a history of providing quality workmanship and responsiveness to the District.

Example 3; Auto Parts:

With few exceptions, one vendor, was preferred over all other auto parts vendors for purchases of auto parts. This vendor was used more than 60% of the time. This does not appear to be fair to the rest of the vendor community. In addition, other vendors may have better prices, for example two other vendors had lower prices for brake cleaner.

We discussed vendor selection with the Storekeepers at the various field locations. They cited the following factors that they consider when selecting a vendor:

- availability of vendors (a major consideration in the more remote areas that the District serves),
- quality,
- price,
- merchandise availability,
- responsiveness and reliability of the vendor, and
- willingness of the vendor to accept District purchase orders.

Favoring certain vendors has both positive and negative aspects. High volume use of a particular vendor usually results in increased responsiveness of that vendor to customer needs. Preferred customers tend to get a level of service that the infrequent customer may not receive. Conversely, consistently using one vendor may not be appropriate in a

public procurement setting.¹² District purchasers should be constantly seeking out and spreading the work to new vendors regardless of whether the standards of competition require them to do so. This is now especially true since the threshold for requiring three price quotes has increased from \$5,000 to \$10,000.

Recommendation

- 17. District purchasers should be encouraged to use more than one source of supply for their needs.**

Management Response: Management concurs with the recommendation. The need for competition will be emphasized in the new procedural instructions for decentralized purchase orders. It should be noted that due to price, quality, delivery and utilization of local and M/WBE sources, it is not always in the best interest of the District to change vendors on all transactions.

Responsible Department: Procurement

Estimated Completion Date: May 31, 2001

¹² According to the Office of Supplier Diversity and Outreach, the District has fallen far short of its goals in the area of purchasing commodities from M/WBE vendors. In FY99 utilization was only 3.3%.