THE USE AND ABUSE OF GOVERNMENT PURCHASE CARDS

HEARING

BEFORE THE

SUBCOMMITTEE ON GOVERNMENT EFFICIENCY, FINANCIAL MANAGEMENT AND INTERGOVERNMENTAL RELATIONS

OF THE

COMMITTEE ON GOVERNMENT REFORM

HOUSE OF REPRESENTATIVES

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THE USE AND ABUSE OF GOVERNMENT PURCHASE CARDS

WEDNESDAY, MARCH 13, 2002

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON GOVERNMENT EFFICIENCY, FINANCIAL MANAGEMENT AND INTERGOVERNMENTAL RELATIONS,
COMMITTEE ON GOVERNMENT REFORM,
Washington, DC.

The subcommittee met, pursuant to notice, at 9:58 a.m., in room 2154, Rayburn House Office Building, Hon. Steve Horn (chairman of the subcommittee) presiding.

Present: Representatives Horn and Schakowsky.

Staff present: J. Russell George, staff director and chief counsel; Bonnie Heald, deputy staff director; Justin Paulhamus, clerk; Michael Sazonoff, intern; David McMillen, minority professional staff member; and Jean Gosa, minority assistant clerk.

Mr. HORN. A quorum being present, the Subcommittee on Government Efficiency, Financial Management and Intergovernmental Relations will come to order.

I have long believed that oversight hearings, such as we are holding today, shed light on important issues that need attention, and that such light encourages those in charge to fix the problem. I am delighted that in the audience are a number of individuals, top executives, that are going into the purchasing acquisition for DOD. I am delighted to have you in the hearings. I hope we can learn something from this morning's hearing. We are delighted that you will look at those laws and make sure that they are put and implemented in all of the contracts, so that they understand how these laws are. I thank you very much for being here.

How many of you are here? Stand up, please, and see how many are in the class. Only one, two, three, four, five, six. I thought there would be about 30.

So thank you very much. I hope you enjoy it. Sometimes it isn't enjoyable, but we'll do it.

So I have long believed that these oversight hearings, such as we are holding today, shed light on important issues that need attention, and that such light encourages those in charge to fix the problem. In many cases, that has been a correct assumption, but you will hear today what, in part, dismisses congressional oversight as merely a nuisance that must be endured, but that can be ignored, is the attitude.

On July 30, 2001, this subcommittee held a hearing examining the government purchase card programs at two Navy units in San Diego, the Space and Naval Warfare Systems and the Navy Public

Works Center. Over the last few months, the General Accounting Office, which is the right arm of Congress for both programmatic review as well as fiscal review, the General Accounting Office auditors and investigators have examined recent card purchases at the two San Diego Navy units. One of the units, the Public Works Center, was cooperative in providing auditors with the documentation and information they needed to complete their job. Equally important, this unit is making a concerted effort to identify and eliminate abusive uses of the cards.

It is another story at the Space and Naval Warfare Systems Center. According to the General Accounting Office, the Systems Center provided information that was often misleading and conflicting. Whether it is an attitude of leadership or a pervasive culture throughout the unit, Space and Naval Warfare Systems Center employees, most of whom are civilians, have continued using their government-guaranteed cards to buy extravagant personal items—all at taxpayer expense.

It is about April 15th when people will be writing out the checks to give the Federal Government a revenue source for all that is going on with the war and with now getting Federal money for education throughout America, where we have a first-rate education program, and the money is needed. It should not be wasted, as it has been, for personal use. These items include designer briefcases, tote bags, and day planners from Louis Vuitton and Franklin Covey, as well as high-quality, $30 Bose headsets for listening to music.

This abuse is of special concern because of the desire by many to increase temporarily the existing transaction limit on most purchase cards from $2,500 per purchase to $25,000 per transaction. This increase would apply to purchases that relate to the war against terrorism or defending the homeland against terrorism. That is where the money should go. Undoubtedly, this streamlined purchasing power might be needed. But before we consider that decision, we must be certain that proper controls are in place to stop the abuse of public funds which occurs. It isn't their money; it is we the taxpayers' money.

That said, I welcome our witnesses, and we will start. The ranking member is here? If Ms. Schakowsky comes, she will have an opening statement.

[The prepared statement of Hon. Stephen Horn follows:]

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Opening Statement
Chairman Stephen Horn, R-CA
Subcommittee on Government Efficiency,
Financial Management and Intergovernmental Relations
March 13, 2002

A quorum being present, the Subcommittee on Government Efficiency, Financial Management and Intergovernmental Relations will come to order.

I have long believed that oversight hearings, such as we are holding today, shed light on important issues that need attention, and that such light encourages those in charge to fix the problem. In many cases, that has been a correct assumption. But you will hear testimony today that, in part, dismisses congressional oversight as merely a nuisance that must be endured, but can then be ignored.

On July 30, 2001, this subcommittee held a hearing examining the Government Purchase Card Programs at two Navy units in San Diego -- the Space and Naval Warfare Systems and the Navy Public Works Center. At that hearing, General Accounting Office (GAO) auditors reported that they had found numerous examples of egregious misuse and criminal fraud committed by employees who had used these government-guaranteed credit cards for personal gain.

At the conclusion of the hearing, I forewarned witnesses that we would be holding another hearing to examine their progress in reasserting control over these abuses of taxpayers' hard-earned money. Over the last few months, GAO auditors and investigators have examined recent credit card purchases at the two San Diego Navy units. One of the units -- the Public Works Center -- was cooperative in providing auditors with the documentation and information they needed to complete their job. Equally important, this unit is making a concerted effort to identify and eliminate abusive uses of the cards.

It is another story at the Space and Naval Warfare Systems Center. According to the GAO, the Systems Center provided information that was often misleading and conflicting. Whether it is an attitude of leadership or a pervasive culture throughout the unit, Space and Naval Warfare Systems Center employees, most of whom are civilians, have continued using their government-guaranteed cards to buy extravagant personal items -- all at taxpayer expense. These items included designer briefcases, tote bags and day planners from Louis Vuitton and Franklin Covey; as well as high-quality, $300 Bose headsets for listening to music.

This abuse is of special concern because of the desire by many to increase temporarily the existing transaction limit on most purchase cards from $2,500 per purchase to $25,000 per transaction. This increase would apply to purchases that relate to the war against terrorism or defending the homeland against terrorism. Undoubtedly, this streamlined purchasing power might be needed. But before we consider that decision, we must be certain that proper controls are in place to stop the abuse of public funds before it occurs, not afterwards.

That said, I welcome our witnesses. We will start with our first panelist, Senator Charles Grassley, who has worked diligently on this issue.

Mr. HORN. Is Senator Grassley here? All right, he will be here in 1 minute, I am told. So we will be in recess just waiting for the Senator. If not, we will go on with the other panel.

[Recess.]

Mr. HORN. Mr. Kutz, Mr. Ryan, Captain Barrett, Captain Miller, Deputy Under Secretary Jonas, accompanied by Deidre A. Lee, Director of Defense Procurement, and Danielle G. Brian. Let's just line up the way it is. That is the way we will take them, as on the agenda, and leave a seat in the middle for Senator Grassley.

[Witnesses sworn.]

Mr. HORN. The clerk will note that the witnesses have affirmed the oath.

We will now start. The ranking member is here and has an opening statement. So please start.

Ms. SCHAKOWSKY. Thank you, Mr. Chairman, for holding this hearing, and I join you in welcoming our witnesses this morning. I will address three points in my remarks this morning.

First, I am disappointed in the arrogance and disrespect for the American public shown by the Space and Naval War Center.

Second, I am disappointed in the personnel at Naval Public Works for the fraudulent use of purchase cards. GAO reports that Public Works is making a serious effort at reform.

Finally, I believe that the problems we will address today are not unique to these organizations, but rather are symptomatic of the acquisition culture at the Department of Defense. There is an attempt to return the Defense Department to the era of the $600 hammers and $3,000 toilet seats.

GAO will report today on widespread abuse of the purchase card system at the Space and Naval Warfare Center. Purchase cards are used to buy luxury items like designer bags, personal digital assistants, and high-priced clothes. Purchase limit regulations were circumvented by splitting purchases to get below the limit. It would be an understatement to say that the program was managed badly at the Warfare Center. Management completely abdicated its responsibilities. This supposedly elite research center even tried to justify buying Lego robots from Toys R Us as a research expenditure.

Those, however, are not the worst of the offenses. The personnel at SPAWAR argued first that these purchases were justified. Then they told the GAO that it didn't matter if digital cameras and clothes and luggage disappeared because naval regulations said they didn't have to account for items that are easily pilfered. In other words, if something is easily stolen, the problem is solved by not keeping track of those things.

This morning the commander who testified last July is not here. The former commander retired. That, in and of itself, would not be noteworthy. However, the events surrounding this retirement are disturbing. The commander retired after refusing drug testing, refusing to have his car searched when he was selected for a random search, and for trying to get two of his subordinates to lie. For those abuses, the punishment was a $1,000 fine and retirement. The rumor is that, once Congress looks away, he will be back at work as a contractor—probably paid by a purchase card.

What we have here is an organization that is completely out of control. There is no respect for laws or regulations. There is no accountability for fraud and abuse. When caught, they try to justify abusive purchases. Unfortunately, the departmental response to these problems has been weak.

Last week Congressman Davis held a hearing on a proposal to raise the purchase limit on these cards to $25,000 per purchase. That proposal came from the Defense Department and those outside the government who provide goods and services. That would eliminate from competitive bidding 99.5 percent of the purchases made by the Federal Government.

We have seen this program badly abused by the two units here today. I suspect that when GAO reports back to us this summer on its examination across the whole Defense Department we will see similar abuse.

The Defense Department has not been a good steward of Federal funds. We should not put into their hands the tools to further abuse the public trust.

There is, however, another question that must be addressed before we expand the use of purchase cards. These cards make purchasing more convenient for the government, but no one has actually looked at the cost of using these cards. Much of what is purchased with these cards could be purchased using the GSA schedule, a program where GSA negotiates lower prices because of the volume of government purchases.

GAO has told us that purchase cards will account for nearly $20 billion in purchases this fiscal year or next. If there is a 5 percent waste in these purchases, that is $1 billion of waste.

I am requesting, and I hope that the chairman will join me in this request, the GAO look at the purchases made using these purchase cards: How many of those items could have been purchased from the GSA schedule? Did the agency pay more or less using the purchase card than it would have going through the GSA?

This program is 10 years old, and GSA has never done a careful examination of the program. Before we expand the use of purchase cards, we should have some facts about how the system is working today.

Again, I thank you, Mr. Chairman, for calling this hearing, and I look forward to the testimony of our witnesses.

[The prepared statement of Hon. Janice D. Schakowsky follows:]

**STATEMENT OF THE HONORABLE JAN SCHAKOWSKY
AT THE HEARING ON
PURCHASE CARD ABUSE**

March 13, 2002

Thank you Mr. Chairman for holding this hearing, and I join you in welcoming Senator Grassley. I will address three points in my remarks this morning. First, I am disappointed at the arrogance and disrespect for the American public shown by the Space and Naval Warfare Center. Second, while I am disappointed in the personnel at Naval Public Works for the fraudulent use of purchase cards, GAO reports that Public Works is making a serious effort at reform. Finally, I believe that the problems we will address today are not unique to these organizations, but rather are symptomatic of the acquisition culture at the Department of Defense. There is an attempt to return the Defense Department to the era of $600 hammers and $3000 toilet seats.

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Those, however, are not the worst of the offenses. The personnel at Space War, argued first, that these purchase were justified. Then they told GAO that it didn't matter if digital cameras and clothes and luggage disappeared because Naval regulations said that they didn't have to account for items that are easily pilfered. In other words, if something is easily stolen, the problem is solved by not keeping track of those things.

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program badly abused by the two units here today. I suspect that when GAO reports back to us this summer on its examination across the whole Defense Department, we will see similar abuse. The Defense Department has not been a good steward of federal funds. We should not put into their hands the tools to further abuse the public trust.

There is, however, another question that must be addressed before we expand the use of purchase cards. These cards make purchasing more convenient for the government, but no one has actually looked at the cost of using these cards. Much of what is purchased with these cards could be purchased using the GSA schedule, a program where GSA negotiates lower prices because of the volume of government purchases.

GAO has told us that purchase cards will account for nearly $20 billion in purchases in this fiscal year or the next. If there is 5% waste in these purchases that is a billion dollars of waste. I am requesting, and I hope that the Chairman will join me in this request, that GAO look at the purchases made using these purchase cards. How many of those items could have been purchased from the GSA schedule? Did the agency pay more or less using the purchase card than it would have going through GSA? This program is 10 years old, and GSA has never done a careful evaluation of the program. Before we expand the use of purchase cards, we should have some facts about how the system is working today.

Thank you Mr. Chairman for calling this hearing, and I look forward to the testimony of our witnesses.

Mr. HORN. I thank you for your statement. Please work with the staff director and the deputy staff director, Ms. Heald, on what you have just asked. We will be glad to ask GSA and others about that.

Now is Senator Grassley here anywhere? OK, well, we are going to start then. Oh, here we are.

Senator Grassley, we've got a seat for you right there. It isn't as comfortable as Senate chairs, but it's the House. We are delighted to have you here.

STATEMENT OF HON. CHARLES E. GRASSLEY, A U.S. SENATOR FROM THE STATE OF IOWA

Senator GRASSLEY. Am I sitting with friends or enemies? [Laughter.]

These folks in the defense of our country are not enemies. These folks ought to be congratulated for what they do at this particular time.

Mr. HORN. Yes, they have been sworn under oath. So we thought we would put you in the middle there. You have done a great job on this particular issue, just as you have done on many other things.

Senator GRASSLEY. Thank you very much.

First of all, let me apologize for being late. I had a group of college kids that I got too late. I thought if we had 30 kids come from Iowa that wanted to ask their Senator a few questions, I ought to do that. That is the reason I am late. Thank you, Mr. Chairman.

Mr. HORN. Yes, well, bring them here, if you would like. [Laughter.]

By the way, there are 30 people here in the Executive Procurement Acquisition for DOD. They are in a course, and your testimony, mine, and the ranking member's testimony will, we hope, get through to them, because that is the first class that has ever been in a hearing here. We are delighted to have them.

Senator GRASSLEY. Yes. Mr. Chairman, I am here to share my views on the latest results of our ongoing oversight of abuse of the Department of Defense credit card. This is a joint effort that we have been supported by the General Accounting Office. It is an honor and privilege for me to team up with you on such important oversight work.

What we are doing today is putting a spotlight on a problem. In a bureaucratic place like the Pentagon, the glare of public spotlight is never welcome, but shedding light is the heart and soul of oversight generally, and particularly of congressional oversight. Exposure is a great remedy enhancer.

Every time I peer into the inner recesses of the Department of Defense credit card account, I see more abuse and more fraud, and that makes me ask myself, how bad can it be? So we need to keep the spotlight on full power and the beam focused on the problem until we get to the bottom of the pit and figure out what needs to be done.

Today there are 1.7 million Department of Defense credit cards in circulation that generate over $9 billion in expenditures annually. There are two types of cards, the purchase card and the travel card. Most are travel cards. This is 1.4 million versus 200,500 pur-

chase cards. Most of the dollars are for purchase card transactions, $6.1 billion per year versus $3 billion for the travel cards.

A credit card is a financial instrument. It is a license to spend money. And every shred of evidence that I have seen says that the internal controls at the Pentagon are weak or nonexistent. Credit cards is a zero control environment, and in this environment it is a very dangerous one. That means that there is an army, 1.7 million strong, authorized to spend money with no checks and balances. The potential for abuse and fraud is virtually unlimited.

Now I understand the thinking behind the credit cards, and the thinking is very, very good. Unfortunately, we see the bad in the execution of a very good policy. We want the men and women serving in the Armed Forces to have the tools that they need to carry out their duty. A credit card is one of those modern devices that is supposed to make it better and easier for them to get the job done quickly and effectively without a whole lot of wasteful paperwork.

In simplifying the travel and purchase processes, each cardholder is given authority to spend money. The authority to spend money in the name of the taxpayer is obviously an awesome responsibility. That authority carries heavy responsibilities. Unfortunately, this awesome responsibility is not taken very seriously at the Pentagon. The criticism is not directed at Secretary Rumsfeld, because he is trying hard to cleanup a longstanding financial mess.

My criticism is directed at those employees who are supposed to oversee the program. Department of Defense credit cards are issued willy-nilly with no credit checks. The results are predictable then. The cards are being abused with impunity. Department of Defense credit cards are being taken on shopping sprees, and the cardholders think they are immune from punishment, and they are, Mr. Chairman.

We have zero accountability with purchase cards, zero accountability with travel cards until recently. That is the root cause of the problem. That is why we are having this hearing today, because of the lack of accountability. If there was accountability, it is obvious that this stuff would not be going on.

In a moment the General Accounting Office will be telling you just how bad it really is. The General Accounting Office has examined 300 transactions at two Navy offices in San Diego. Despite a small sample, Mr. Chairman, the General Accounting Office has uncovered extensive fraud and abuse, and more is being found each day. We are looking at the tip of an iceberg.

Here's a sample of some credit card abuse: in bars, strip joints, gambling casinos; for large cash withdrawals from ATM machines; clothing at upscale department stores like Macy's and Nordstrom's; designer leather goods and expensive luggage; gift certificates, $1,500 each; $200 robots at Toys R Us; groceries, kitchen appliances, home computers, and even a breast enlargement operation.

So you name it; these cards are used for it, and it is all personal business. If they need it, they buy it with Department of Defense plastic and keep it; no questions asked.

Now there is a proposal to raise the purchase limit from $2,500 to $25,000. If it goes up, new cars and homes might be next. The General Accounting Office's 300 transaction sample yielded over a

half million dollars in fraudulent and abusive purchases. Either the taxpayers or the bank gets stuck with the bill, depending on which card is used. In either case, it is bad.

For shopping done with a purchase card, the government is responsible for paying the bill, and most bills are paid promptly; no questions asked. With purchase cards, the taxpayers are the ones that get shafted, and get shafted right up front. To my knowledge, the government has never asked anyone to return an unauthorized purchase or repay the money, even when abuse is known to authorities.

Travel card expenses, by comparison, are the responsibility of individual cardholders. The taxpayer is out of the loop, at least up front. When the cardholder incurs legitimate travel expenses, that person is supposed to file a travel voucher, get reimbursed, and then pass the money onto the bank, in this case, Bank of America. All too often, cardholders simply pocket the money, tax dollars, leaving the bank holding the bag. When the travel card is used to cover personal expenses, what happens with alarming regularity, those bills are paid late, very late, and sometimes never. With no interest charges, obviously, abusers get a free ride.

The bank has equipped the Pentagon with an anti-fraud detection system. It is called EAGLS, acronym E-A-G-L-S. It gives agency program coordinators an online capability to detect unauthorized transactions on any account. It only takes a second to determine if a trooper is getting cash at the local ATM machine without orders, but nobody seems to be minding the store.

As I said at our hearing in July, Mr. Chairman, if the Pentagon knows this stuff is happening, and if the Pentagon does nothing, then that makes the Department of Defense party to bank robberies, and the robbery is still in progress. The bank is sustaining unacceptable losses, and in the end we all pay higher prices, and the taxpayers get shafted as well. When the bank has to write-off bad debts, tax revenues are lost.

So, Mr. Chairman, the bank has reached a breaking point. It is losing too much money. So, on February 11, 2002, the bank fired a warning shot across the bow. The bank is turning up the pressure. It has declared its intent to cancel the U.S. Army account, 413,029 cards, at midnight, March 25th, this month. That has really gotten somebody's attention, and in a hurry, and so there are now negotiations in progress.

Mr. Chairman, there then is a glimmer of hope on the horizon. The reason for hope comes from a brand-new Department of Defense policy called salary offsets. Before I explain the new policy, it is important to understand why the Department of Defense travel card program is teetering on the brink of disaster. As of November 2001, 46,572 Department of Defense personnel had defaulted on more than $62 million in official travel expenses, and the bad debt was growing at the rate of $1 million per month, making the Department of Defense default rate six times the industry average.

For a business interested in profits, a pile of bad debt with no accountability made for an intolerable situation, obviously. So something had to give. In October 2001, the bank and the Department of Defense agreed to take action. The salary offset program

then was born. There are now 31,579 accounts enrolled in the offset program. So far, offset payments total $5.2 million.

As a garnishment, the salary offsets provide some measure of accountability, but actually have limitations. For one, the money was taken from the bank in big chunks, but it is repaid to the bank in small chunks over a long period of time. And there are loopholes. Ten percent of unpaid accounts will slip right through the net, due to retirements, bankruptcies, dollar offset limits.

The bank still expects about $2 to $4 million a year to fall through the cracks and be written off as bad debt. But that's considered better, and it is also consistent with the industry average.

In addition, most of the older accounts in default will never be captured by offsets. The bank will still have to eat $40 million of unrecoverable debt. Even though there isn't any hard data yet, the bank expects salary offsets to reduce the default rate to negligible levels. That's the good news.

There is still bad news. Salary offsets are having little or no effect on high delinquency rates. Delinquencies have actually risen with salary offsets. That is because offsets don't kick in until 120 days plus or 4 months past billing. Payments are due within 30 days of billing. Today the Department of Defense has outstanding balances of $370 million. About 30 percent of the dollars owed for official travel expenses are more than 30 days past due; 15.4 percent are 60 days past due. One in five Department of Defense accounts is overdue for payment. That is four to five times the industry average.

The 3-month gap between the payment due date and offsets means that the bank has to float a loan. It is a free loan for the Department of Defense abusers that costs the bank $4 to $5 million a year.

A prime driver behind delinquencies is the use of the card to cover personal expenses. So, Mr. Chairman, you may remember at the last hearing I mentioned several cases involving egregious use of credit cards. Just a few of them:

A marine sergeant, A. Lopez, who ran up a $19,581 bill for personal expenses and then left the service and the unpaid bills when his retirement was up.

A person by the name of P. Falcon, with an unpaid bill of $9,847, including $3,100 spent at a nightclub.

A dead sailor, T. Hayes, who spent $3,521.

Q. Rivera, Army Reserve, whose wife spent $13,000 on a shopping spree in Puerto Rico.

R. Walker, Air National Guard, with an unpaid balance of $7,428, including his wife's gambling debts.

In the past 8 months that have passed since the hearing, only one of these accounts has been paid off. P. Falcon paid his bill. Every expense posted to his account was personal. He is under investigation.

The others have the same large, unpaid balances that we saw last summer. Some are under investigation.

More aggressive offsets and late fees might help bring this kind of abuse to a screeching halt. Some real leadership at the top would also help. One of the most powerful elements of leadership

is setting an example of excellence. Setting a good example should include paying credit card bills on time.

Officers should always set the example. Unfortunately, there are 713 commissioned officers who have defaulted on $1.1 million in charges. All of these accounts are in charge-off status or unpaid for 7 months or more. Their ranks range from junior lieutenants up to senior colonels and a Navy captain. Individual unpaid balances top out at $8,000. Some of the charges on these accounts look suspicious and obviously need investigation. Commissioned officers who run up $1.1 million in bad debts set a terrible example for the rank-and-file.

Somebody in the Pentagon needs to come down hard on officer scoff-laws. Credit card abuse in the military will never stop until the officers cleanup their act. So, Mr. Chairman, I am presenting to you a list of 713 commissioned officers who defaulted on their accounts, along with unpaid bills for each officer. I would like to have the committee take this, and I ask that it be placed in a confidential record at today's hearing.

Mr. HORN. Without objection.

Senator GRASSLEY. Then I would also ask you, Mr. Chairman, to join me in a letter to Secretary Rumsfeld, because I would like him to see the list and determine what action should be taken in this matter.

Mr. HORN. I am delighted to join you in that letter.

Senator GRASSLEY. OK, thank you very much.

The General Accounting Office has uncovered a disturbing case involving alleged purchase and travel card fraud by one person, Ms. Tanya Mays. She was assigned to the Navy Public Works Department, San Diego. Ms. Mays took her purchase card Christmas shopping and in a few short days ran up a bill of $11,551 at Macy's, Nordstrom's, and Circuit City. She bought gift certificates worth $7,500, a Compaq computer, an Amana range—there's nothing wrong with Amana ranges, if you pay for them; they're made in Iowa—[laughter]—groceries and clothing, all at taxpayers' expense.

Mr. HORN. I'm a Target man.

Ms. SCHAKOWSKY. Actually, I have an Amana. [Laughter.]

Senator GRASSLEY. OK. She presented the bill to her Navy supervisor, who signed and certified it for payment, and it was paid in full. She also used her travel card to buy airline tickets for her son. The cost was $722. When Ms. Mays left the Public Works Department, she was allowed to keep her purchase card. I guess they figured that she needed help again, and they were right, she did, this time for a personal car rental, and Public Works gladly paid the bill.

So, Mr. Chairman, I find the Mays' case very troublesome. She has allegedly made a number of fraudulent purchases. Yet, there seems to be total disregard for accountability. Ms. Mays has not been asked to repay the money she allegedly stole. No disciplinary action has been taken. In fact, she was moved into a bigger job and has been given a promotion effective October 2001. She is now assigned to the Army's top-level Financial Management Office in the Pentagon, and I am told that she is in charge of cash integration.

So, Mr. Chairman, when you put one of these cases under a microscope, it seems like the whole problem comes into much sharper focus. The Tanya Mays case is not unique, and I can guarantee that. Here's another.

A Department of Defense employee by the name of Somchart "Nick" Fungcharoen, he used his travel card exclusively for personal expenses. Over a period of 2 years he charged nearly $35,000, including medical expenses, $4,016. On the surface, it appears as if he spent most of the money romancing a waitress he met at the Hooters' Bar and Grill in Jacksonville, FL. Her name was Jennifer Gilpin.

Mr. HORN. Senator, I'm going to have to interject for a minute. I've got a journal call on the floor. When you are done with that statement, if you would come up here, and we will have Mr. Kutz start his testimony——

Senator GRASSLEY. OK.

Mr. HORN [continuing]. And then you will have a chance to dialog with GAO.

Senator GRASSLEY. OK.

Mr. HORN. Then I will be back within the time.

Senator GRASSLEY. This gentleman used his travel card exclusively for personal expenses. Over a period of 2 years he charged nearly $35,000, including medical expenses of $4,016. On the surface, it appears that he had used this to romance a waitress.

After they got to know each other, she asked him for money to have a breast enlargement operation. He agreed and took her to a surgeon, Dr. John J. Obi, M.D. Dr. Obi performed the operation and Fungcharoen used his Department of Defense credit card to pay the bill.

When the relationship soured, the case ended up in small claims court, and the military man had retired on disability and wanted his money back. The judge became alarmed that Fungcharoen testified proudly that he had used his government-issue credit card to pay the doctor. Fungcharoen whipped out the card in the courtroom and showed it to the judge. The judge examined the card and read on the inscription, "For official government travel only."

The judge stated, in total disbelief, "You paid for this breast enlargement with a government credit card?" After the revelation, the judge said, "Let's not go there."

This case is unique. It is unique because the cardholder paid his bill, though not always on time.

I have two problems with the case. First, Fungcharoen used his card exclusively for personal business. Had he used the standard commercial card, he would have incurred stiff interest charges and penalty. He used the Department of Defense plastic to avoid costs that the rest of us have to pay. He got a free loan from the bank without asking. That is just one small step away from other worse forms of abuse.

Second, the case underscores the total lack of oversight by the EAGLS crew. They were asleep at the switch, and a quick EAGLS check would have shown that he was making extensive unauthorized purchases around his home in Florida.

And why did he have a card after retirement is obviously an important question. Like Ms. Mays, I guess he figured out that he needed it again.

So, Mr. Chairman, accountability is the key. With no accountability, we can look forward to more egregious credit card abuse, relentless abuse. It will go on and on and on with impunity. A person who holds up a liquor store and takes $500 in cash can go to jail for 15 years. If he used Department of Defense plastic to steal $12,000 with DOD plastic, like Tanya Mays allegedly did, you get a promotion, and that just doesn't seem to be right.

People who abuse their government credit cards have to pay a price. Heads have to roll. When the price is right, the abuse then will end. If the abusers are forced to repay the money with penalties, the stealing will stop.

I thank you very much, Mr. Chairman.

[The prepared statement of Senator Grassley follows:]

TESTIMONY: DOD Credit Card Abuse
By Senator Chuck Grassley
Ranking Member
Senate Finance Committee

Before

Subcommittee on Governmental Efficiency, Financial Management
And Intergovernmental Relations
Committee on Governmental Affairs
U.S. House of Representatives

March 13, 2002

Mr. Chairman, I am here to share my views on the latest results of our ongoing oversight investigation of Department of Defense (DOD) credit card abuse. This is a joint effort supported by the General Accounting Office (GAO). It is an honor and privilege for me to team up with you on such important oversight work. What we are doing today is putting the spotlight on a problem. In a bureaucratic place like the Pentagon, the glare of the public spotlight is never welcome. But shedding light is the heart and soul of oversight. Exposure is a great remedy enhancer.

Every time I peer into the inner recesses of a DOD credit card account, I see more abuse and more fraud. That makes me ask myself: How bad can it be? So we need to keep the spotlight on full power and the beam focused on the problem until we get to the bottom of the pit and figure out what needs to be done. Today, there are 1.7 million DOD credit cards in circulation that generate over 9 billion dollars in expenditures annually. There are two types of cards: 1) Purchase cards; and 2) Travel cards. Most are travel cards -- 1.4 million -- versus 200,500 purchase cards. Most of the dollars are for purchase cards transactions -- 6.1 billion dollars per year versus 3 billion dollars for travel cards.

A credit card is a financial instrument. It is a license to spend money. And every shred of evidence I have seen says that internal controls at the Pentagon are weak or nonexistent. Credit cards in a zero control environment are dangerous. That means there is an Army -- 1.7 million strong -- authorized to spend money with no checks and balances. The potential for abuse and fraud is virtually unlimited.

Now, I understand the thinking behind the credit cards. The thinking is good. Unfortunately, execution is poor. We want the men and women serving in the Armed Forces to have the tools they need to carry out their duties. A credit card is one of those modern devices that is supposed to make it easier for them to get the job done quickly and effectively without a whole lot of wasteful paperwork. In simplifying the travel and purchase processes, each cardholder is given authority to spend money. The authority to spend money in the name of the taxpayer is an awesome responsibility in my book. That authority carries heavy responsibilities.

Unfortunately, this awesome responsibility is not taken very seriously at the Pentagon. That criticism is not directed at Secretary Rumsfeld. He is trying hard to clean up a long-standing financial mess. My criticism is directed at the bureaucrats who are supposed to oversee the program. DOD credit cards are issued willy-nilly with no credit checks. The results are predictable: The cards are being abused with impunity. DOD credit cards are being taken on a shopping spree, and the cardholders think they are immune from punishment. And they are, Mr. Chairman.

We have zero accountability with purchase cards. Zero accountability with travel cards -- until recently. That's the root cause of the problem. That's why we are having this hearing today -- a lack of accountability. If there was accountability, this stuff would not be going on. In a moment, the GAO will be telling you just how bad it really is. The GAO has examined 300 transactions at two Navy offices in San Diego.

Despite such a small sample, the GAO has uncovered extensive fraud and abuse, and more is being found each day. We are looking at the tip of the iceberg. Here's a sample of how credit cards are abused:

–In bars, strip joints and gambling casinos
–For large cash withdrawls at ATM machines
--Clothing at upscale department stores like Macy's and Nordstrom
--Designer leather goods and expensive luggage
--Gift certificates - $1,500 each
--$200-dollar robots at Toys R Us
--Groceries, kitchen appliances, home computers
–Even a breast enlargement operation

You name it. They do it. And it's all personal business. If they need it, they buy it with DOD "plastic" and keep it. No questions asked. Now, there is proposal to raise the purchase limit from $2,500 to $25,000. If it goes up, new cars and homes are next, Mr. Chairman. The GAO's 300-transaction sample yielded over a half a million dollars in fraudulent and abusive purchases. Either the taxpayers or the bank get stuck with the bill -- depending on which card is used. For shopping done with the purchase card, the government is responsible for paying the bill, and all those bills are paid promptly -- no questions asked. With purchase cards, the taxpayers get shafted right up front.

To my knowledge, the government has never questioned a purchase card transaction nor asked anyone to return an unauthorized purchase or re-pay the money even when abuse is known to authorities. Travel card expenses, by comparison, are the responsibility of the individual cardholder. The taxpayer is out of the loop -- at least up front. When the cardholder incurs legitimate travel expenses, that person is supposed to file a travel voucher, get reimbursed, and then pass the money on to the bank -- the Bank of America. All too often the cardholder simply pockets the money -- tax dollars -- leaving the bank holding the bag. And when the travel card is used to cover personal expenses, which happens with alarming regularity, those bills are paid late -- very late -- and sometimes never. With no interest charges, abusers get a free ride.

The bank has equipped the Pentagon with an anti-fraud detection device. It's called EAGLS. It gives agency program coordinators an on-line capability to detect unauthorized transactions on any

account. It only takes a second to determine if a trooper is getting cash at the local ATM machine without orders. But nobody's minding the store.

As I said at our hearing in July, if the Pentagon knows this stuff is happening and if the Pentagon does nothing, that makes DOD party to a bank robbery, and the robbery is still in progress. The bank is sustaining unacceptable losses, and in the end, we all pay higher prices -- and the taxpayers get shafted, too. When the bank has to write off bad debt, tax revenues are lost. Mr. Chairman, the bank has reached a breaking point. It's losing too much money. So on February 11, 2001, the bank fired a warning shot "across the bow." The bank is turning up the pressure. It declared its intent to cancel the U.S. Army account -- 413,029 cards -- at midnight on March 25, 2002. That got somebody's attention in a hurry. Negotiations are in progress.

Mr. Chairman, there is a glimmer of hope on the horizon. The reason for hope comes from a brand new DOD policy called "salary offsets." Before I explain the new policy, it's important to understand why the DOD travel card program is teetering on the brink of disaster. As of November 2001, 46,572 DOD personnel had defaulted on more than 62 million dollars in "official" travel expenses. And the bad debt was growing at the rate of one million dollars per month, making DOD's default rate six times the industry average.

For a business interested in profits, a pile of bad debt with no accountability made for an intolerable situation. Something had to give. In October 2001, the bank and DOD agreed to take action. The salary offset program was born. There are now 31,579 accounts enrolled in the offset program. So far, offset payments total 5.2 million dollars. As a garnishment, salary offsets provide some measure of accountability but have limitations. For one, the money was taken from the bank in big chunks. But it's repaid to the bank in small chunks over a long period of time. And there are loopholes. Ten percent of unpaid accounts will slip right through the net -- due to retirements, bankruptcies, dollar offset limits.

The bank still expects about 2 to 4 million dollars a year to fall through the cracks and be written off as bad debt. But that's considered better. It's consistent with the industry average. In addition, most of the older accounts in default will never be captured by offsets. The bank will still have to eat 40 million dollars of unrecoverable debt. Even though there isn't any hard data yet, the bank expects salary offsets to reduce the default rate to "negligible" levels. That's the good news. There is still more bad news. Salary offsets are having little or no effect on high delinquency rates. Delinquencies have actually risen with salary offsets

That's because offsets don't kick in until 120 days plus -- or four months -- past billing. Payments are due within 30 days of billing. Today, DOD has outstanding balances of 370 million dollars. About 30 percent of the dollars owed for "official" travel expenses are more than 30 days past due. 15.4 percent are 60 days past billing. One in five DOD accounts is overdue for payment. That is 4 to 5 times the industry average. The 3-month gap between the payment due date and offsets means the bank has to float a loan. It's a free loan for DOD abusers that costs the bank 4 to 5 million dollars a year. A prime driver behind delinquencies is the use of the card to cover personal expenses.

Mr. Chairman, you may remember at the last hearing that I mentioned several cases involving egregious abuse of DOD credit cards. These were as follows:

The case of the Marine Sergeant [--] who ran up a $19,581.64 bill for personal expenses and then left the service - and the unpaid bill - when his enlistment was up;

--[--] - Army - with an unpaid bill of $9,847.49, including $3,100 spent at a nightclub;

--The dead sailor - [--] who spent $3,521.28;

--[--] - Army Reserve - whose wife spent $13,011.18 on a shopping spree in Puerto Rico;

--and [--] - Air National Guard - with an unpaid balance of $7,428.21, including his wife's gambling debts.

In the eight months that have passed since the hearing, only one of these accounts has been paid off. [--] paid his bill. Every expense posted to his account was personal. He is under investigation.

The others have the same large, unpaid balances we saw in July 2001. More aggressive offsets and late fees might help to bring this kind of abuse to a screeching halt. Some real leadership at the top would also help. One of the most powerful elements of leadership is setting an example of excellence. Setting a good example should include paying credit card bills on time. Officers should always set the example.

Unfortunately, there are 713 commissioned officers who have defaulted on 1.1 million dollars in charges. All these accounts are in "charge-off" status or unpaid for 7 months or more. Their ranks range from junior lieutenants up to senior colonels and a Navy captain. Individual unpaid balances top out at 8,000 dollars. Some of the charges on these accounts look suspicious and need investigation. Commissioned officers who run up 1.1 million in bad debt set a terrible example for the rank and file.

Somebody over in the Pentagon needs to come down hard on the officer scoff-laws. Credit card abuse in the military will never stop until the officers clean up their act. Mr. Chairman, I have a list of the 713 commissioned officers who defaulted on their accounts, along with the unpaid balance for each officer. I now present this file to the Committee and ask that it be placed in a confidential record of today's hearing. Mr. Chairman, I ask that you join me in a letter to Secretary Rumsfeld. I want him to see the list and determine what action should be taken in this matter.

The GAO has uncovered a particularly disturbing case involving purchase and travel card fraud by the one person - [--]. She was assigned to the Navy Public Works Department in San Diego. [--] took her purchase card Christmas shopping and in a few short days ran up a bill for $11,551.24 at Macy's, Nordstrom, and Circuit City. She bought gift certificates worth $7,500, a Compaq computer, Amana range, groceries and clothing - all at the taxpayers' expense. She presented the bill to her Navy supervisor who signed and certified it for payment. And it was paid in full. She also used her travel card to buy airline tickets for her son. That cost another $722.00 dollars.

When [--] left the Public Works Department, she was allowed to keep her purchase card. I guess they figured she might need it again. And they were right. She did - this time for a personal car rental. And Public Works gladly paid the bill. Mr. Chairman, I find the [--] case very troublesome. She has allegedly made a number of fraudulent purchases. Yet there seems to be total disregard for accountability. [--] has not been asked to re-pay the money she allegedly stole. No

disciplinary action has been taken. In fact, she was moved into a bigger job and given a promotion in October 2001. She is now assigned to the Army's top-level financial management office in the Pentagon. I am told she is in charge of "cash integration." Mr. Chairman, when you put one of these cases under the microscope, it seems like the whole problem comes into much sharper focus.

The [–] case is not unique. I guarantee it. Here's another: a DOD employee by the name of Somchart "Nick" Fungcharoen. He used his travel card exclusively for personal expenses. Over a period of two years, he charged nearly 35,000 dollars, including medical expenses of $4,016.46. On the surface it appears as if he spent most of the money romancing a waitress he met at the Hooters Bar and Grill in Jacksonville, Florida. Her name was Jennifer Gilpin.

After they got to know each other, she asked him for money to have a breast enlargement operation. He agreed and took her to a surgeon, Dr. John J. Obi, MD. Dr. Obi performed the operation, and Fungcharoen used his DOD credit card to pay the bill. When the relationship soured, the case ended up in small claims court. Fungcharoen had retired on disability and wanted his money back. The judge became alarmed when Fungcharoen testified proudly that he had used his "government-issued credit card to pay the doctor."

Fungcharoen whipped out the card in the courtroom and showed it to the judge. The judge examined the card and read the inscription on it: "for official government travel only." The judge stated in total disbelief: "you paid for this breast enlargement with a government credit card." After that revelation, the judge said: "let's not go there." This case is unique. It is unique because the cardholder paid his bill, though not always on time. I have two problems with this case.

First, Fungcharoen used his card exclusively for personal business. Had he used a standard commercial card, he would have incurred stiff interest charges and penalties. He used DOD "plastic" to avoid costs that the rest of us have to pay. He got a free loan from the bank without asking. That is just one small step away from other worse forms of abuse. Second, the case underscores the total lack of oversight by the EAGLS crew. They were asleep at the switch. A quick EAGLS check would have shown he was making extensive unauthorized purchases around his home in Florida. And why did he have a card after retiring? Like [–], I guess he figured he might need it again.

Mr. Chairman, accountability is the key. With no accountability, we can look forward to more egregious credit card abuse. Relentless abuse. It will go on and on and on with impunity. A person who holds up a liquor store and takes 500 dollars in cash can go to jail for 15 years. If you use DOD "plastic" to steal 12,000 dollars with DOD "plastic" - like [–] allegedly did, you get a promotion. That's not right. People who abuse their government credit cards must pay a price. When the price is right, the abuse will end. If the abusers are forced to repay the money with penalties, the stealing will stop.

Senator GRASSLEY. I will do as the chairman suggested. I will be right up there.

We would now call upon Mr. Kutz, the Director of Financial Management and Assurance at the General Accounting Office. Mr. Kutz.

STATEMENTS OF GREGORY D. KUTZ, DIRECTOR, FINANCIAL MANAGEMENT AND ASSURANCE, U.S. GENERAL ACCOUNTING OFFICE, ACCOMPANIED BY JOHN RYAN, SPECIAL AGENT, ASSISTANT DIRECTOR, OFFICE OF SPECIAL INVESTIGATIONS, U.S. GENERAL ACCOUNTING OFFICE; CAPTAIN JAMES M. BARRETT III, CIVIL ENGINEER CORPS, U.S. NAVY, AND COMMANDING OFFICER, NAVY PUBLIC WORKS CENTER, SAN DIEGO, CA; CAPTAIN PATRICIA A. MILLER, COMMANDING OFFICER, SPACE AND NAVAL WARFARE SYSTEMS CENTER, SAN DIEGO, CA; TINA W. JONAS, DEPUTY UNDER SECRETARY FOR FINANCIAL MANAGEMENT, DEPARTMENT OF DEFENSE; DEIDRE A. LEE, DIRECTOR OF DEFENSE PROCUREMENT, OFFICE OF THE UNDER SECRETARY OF DEFENSE FOR ACQUISITION, TECHNOLOGY AND LOGISTICS, DEPARTMENT OF DEFENSE; AND DANIELLE G. BRIAN, EXECUTIVE DIRECTOR, PROJECT ON GOVERNMENT OVERSIGHT

Mr. KUTZ. Senator, good to see you chairing a House hearing here. Good morning.

Senator GRASSLEY. I can't believe it. [Laughter.]

Mr. KUTZ. It is a pleasure to be here to testify on our audit of Navy purchase cards. With me this morning is Special Agent John Ryan from our Office of Special Investigations.

Purchase cards were introduced to the government in the 1980's primarily to streamline the acquisition process for small purchases. Usage of purchase cards has grown quickly in the Federal Government, increasing from about $2 billion in 1995 to nearly $14 billion in 2001.

The Department of Defense purchase card activity was about $6 billion in 2001. With 230,000 purchase cards in the hands of DOD employees, effective internal controls are necessary to protect the government from fraud, waste, and abuse.

Senator, I have a purchase card in my hand here that is also displayed on the monitor. As you can see, it looks like a normal credit card and can generally be used wherever Mastercard is accepted. However, notice, as you mentioned on the travel card, this one says, "For official government purchases only."

Today I will discuss our followup audit of fiscal year 2001 purchase card activity at two Navy units in the San Diego area, SPAWAR Systems Center, which I will refer to as SPAWAR, and the Navy Public Works Center, or Public Works. These units of primarily civilian employees serve critical roles in supporting DOD's mission.

Our audit focused on implementation of the purchase card program, not its design. As you mentioned, Senator, used and controlled properly, the purchase card can benefit the Federal Government. The bottom line of my testimony this morning is that for fiscal year 2001 we again found significant breakdowns in internal controls over purchase cards at the two Navy units. These break-

downs contributed to fraudulent and abusive purchases and theft and misuse of government property.

My testimony has three parts: first, the overall purchase card internal control environment; second, the effectiveness of key internal controls, and, third, examples of fraudulent, improper, and abusive purchases.

First, our work has shown that the lack of a strong internal control environment leads to the risk of improper behavior. For fiscal year 2001, the control environment at both SPAWAR and the Public Works was ineffective. However, improvements were made by both units, including significant reductions in the number of cardholders, increased focus on training, and reductions in credit limits.

A key factor impairing the control environment at SPAWAR was the management tone at the top. The former commanding officer testified last July that the purchase card program at SPAWAR had effective management controls. By denying before this subcommittee, and later to his staff, that there was a problem, he effectively supported the status quo.

We are encouraged by the commitment of Captain Miller, the new commanding officer, to ensure that an effective, well-controlled purchase card program is implemented at SPAWAR. However, we are concerned that there will be significant cultural resistance to change. For example, through the end of our audit, SPAWAR continued to rationalize many improper, abusive, and questionable purchases.

A key factor in the improvements at the Public Works is the consistently proactive attitude demonstrated by Captain Barrett and his staff.

Second, basic internal controls over the purchase card program remain ineffective during 2001 at both units, including independent documentation of receipt of goods and services and independent review and certification of the monthly credit card bill. Public Works' failure rate of 16 percent for receipt and acceptance was a significant improvement from the 47 percent failure rate in 2000.

I will use the posterboard to illustrate how fraud can occur when these two key internal controls fail. As you can see, this excerpt from a purchase card bill is similar to a normal credit card statement. Most taxpayers closely review their monthly credit card bill to ensure that all the charges are appropriate.

This extreme example is the December 1999 credit card bill that you mentioned, Senator, for a fraud case that Agent Ryan investigated. As you can see, somebody went on a Christmas shopping spree. This bill, which includes over $11,000 in fraudulent charges, was approved and paid for by the Public Works. Consistent with our 2001 findings, both controls failed, as the government never received these goods, and the bill was paid with no review. Fortunately, over a year later, the government got this money back. However, I think you will agree this is no way to handle taxpayer money.

Third, given the weak controls, it is not surprising, especially for SPAWAR, that we identified potentially fraudulent, improper, and abusive purchase card transactions in 2001. Examples of actual and potential fraud include 1,914 compromised Navy accounts that were previously reported that were used to purchase jewelry, pizza,

flowers, and tires; over $10,000 of charges by a safety product vendor that SPAWAR paid, despite the fact that no goods were received, and $164,000 of purchases from another SPAWAR vendor with no documentation that any goods or services were received.

We have provided the listing of compromised accounts, which includes 78 SPAWAR and 10 Public Works accounts that were active to the Navy in January, and these accounts were finally canceled earlier this month. The two vendor cases I mentioned have been referred to Agent Ryan for investigation of fraud and abuse.

We also identified the improper purchases at both SPAWAR and Public Works. Some of these purchases represented disbursement of government funds that have not authorized by law. Examples of improper purchases included food, clothing, and the rental of luxury automobiles.

SPAWAR also improperly wrote 30 convenience checks over the $2,500 limit, for a total of $347,000. After we identified wasteful and improper usage, the Navy canceled SPAWAR's convenience check privileges.

In addition to fraudulent and improper charges, we identified a number of abusive or questionable purchases by SPAWAR. These represent purchases that were at excessive cost, of questionable government need, or both.

For example, as shown on the posterboard, we found purchases at SPAWAR including Louis Vuitton $250 day planners, which are also shown on the monitor; $195 leather tote handbags, again shown on the monitor; abusive and wasteful usage of cell phones; luggage such as wallets, passport holders, and backpacks that were given away; computer bags purchased in Italy and from Sky Mall for as much as $250 each; four sets of Lego toy robots that you mentioned, Senator, costing $200 each, none being in possession of the government; clothing, including the $140 jacket, which is also shown on the monitor; a $300 Bose headset that was used primarily to listen to music, and a questionable trip for 30 to Bally's Paris Casino in Las Vegas, at a cost to the taxpayer of $15,000 to $20,000.

Consider this: For 2001, we audited less than 200 transactions and found these abusive items, along with potentially fraudulent and improper purchases. In contrast, SPAWAR's stand-down review looked at 16,000 transactions, and, Senator, guess what they found—nothing. No fraudulent, improper, or abusive charges.

In summary, the findings today reflect what can happen when financial management is broken and accountability is lost. These purchase card control weaknesses are reflective of the broader financial management problems facing DOD. It is interesting to note that there have been limited consequences for individuals that have misused the government purchase card.

In light of the events of September 11th, and the Federal Government's short and long-term budget challenges, it is more important than ever that DOD get the most from every dollar spent. Secretary Rumsfeld has noted that billions of dollars of resources could be freed up for national defense priorities by eliminating wasteful

spending. The purchase card abuse I have just described is a small example of what he is talking about.

Senator, this concludes my testimony. Mr. Ryan and I are available for questions after the other statements.

[The prepared statement of Mr. Kutz and Mr. Ryan follows:]

United States General Accounting Office

GAO

Testimony

Before the Subcommittee on Government Efficiency, Financial Management and Intergovernmental Relations, Committee on Government Reform, House of Representatives

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PURCHASE CARDS

Continued Control Weaknesses Leave Two Navy Units Vulnerable to Fraud and Abuse

Statement of Gregory D. Kutz
Director, Financial Management and Assurance

Statement of John J. Ryan
Assistant Director, Office of Special Investigations

Mr. Chairman, Members of the Subcommittee, and Senator Grassley:

I appreciate the opportunity to present follow-up information on our previous testimony[1] on internal control weaknesses related to use of the government purchase card at two Navy units. The Navy reported that it used purchase cards—Citibank MasterCards issued to civilian and military personnel—for more than 2.8 million transactions valued at $1.8 billion in fiscal year 2001. As we previously reported, the Department of Defense (DOD) has increased the use of purchase cards with the intention of eliminating the bureaucracy and paperwork long associated with making small purchases and intends to expand the use of purchase cards over the next several years.

However, the benefits of the purchase card may be substantially reduced if controls are not in place to ensure its proper use. As the comptroller general testified[2] on March 6, 2002, following the events of September 11, reducing fraud, waste, and abuse is even more imperative to ensure that DOD's resources are available to meet national priorities such as homeland security and the war on terrorism. We believe that DOD, with its long-standing problems in financial management, must take steps to ensure the proper stewardship of the increasing amounts of taxpayer dollars devoted to its vital missions. Careful examination of the controls over the purchase card program is one aspect of ensuring that DOD is getting the most from every dollar.

At this subcommittee's July 30, 2001, hearing, we testified on the results of our audit of key internal controls over purchase card activity at two Navy units based in San Diego—the Space and Naval Warfare Systems Command (SPAWAR) Systems Center and the Navy Public Works Center (NPWC).[3] Overall, we found a significant breakdown in internal controls over $68 million[4] in fiscal year 2000 purchase card transactions, leaving these two units vulnerable to fraudulent, improper, and abusive purchases and theft and misuse of government property. We also reported that weak internal controls contributed to five recent cases of alleged purchase card fraud related to Navy purchase card programs in the San Diego area and investigated by the Naval Criminal Investigative Service (NCIS) and other cases that we referred to our own Office of Special Investigations for further review.

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[1]U.S. General Accounting Office, *Purchase Cards: Control Weaknesses Leave Two Navy Units Vulnerable to Fraud and Abuse*, GAO-01-995T (Washington, D.C.: July 30, 2001).

[2]U.S. General Accounting Office, *DOD Financial Management: Integrated Approach, Accountability, Transparency, and Incentives Are Keys to Effective Reform*, GAO-02-497T (Washington, D.C.: Mar. 6, 2002).

[3]SPAWAR Systems Center and the Navy Public Works Center are working capital fund activities. SPAWAR Systems Center performs research, engineering, and technical support, and the Navy Public Works Center provides maintenance, construction, and operations support to Navy programs. Both of these Navy programs have locations throughout the United States. Our review focused on the purchase card program at the San Diego units only. For SPAWAR, this included SPAWAR Headquarters, which is located in San Diego, and SPAWAR Systems Center San Diego, which we will refer to collectively as SPAWAR Systems Center.

[4] SPAWAR Systems Center and NPWC made about $75 million in fiscal year 2000 purchase card transactions. We audited the $68 million of those purchases made by SPAWAR Systems Center and NPWC cardholders located in San Diego.

Our July 2001 testimony was followed by a report[5] in which we summarized our findings and offered 29 recommendations for improving Navy purchase card controls. We will report to you separately on the status of these 29 recommendations as part of our ongoing audit of the Navy's fiscal year 2001 purchase card activity.

The subcommittee and Senator Grassley asked us to perform a follow-up audit at the two Navy units and discuss the status of corrective actions. In addition, we were asked to follow up on the status of fraud cases that we reported on in July 2001 and any other fraud cases we identified as part of this follow-up audit. Today, I will discuss the results of our follow-up work, including (1) the purchase card control environment at the two Navy units' San Diego activities for fiscal year 2001 including any implemented or planned improvements, (2) the results of our test work on statistical samples of purchase card transactions at the two Navy units for the fourth quarter of fiscal year 2001, which identified continuing weaknesses in two critical areas, and (3) potentially fraudulent, improper, and abusive or questionable transactions made by the two Navy units during fiscal year 2001. In this testimony, we also report on the status of two cases investigated by our Office of Special Investigations as a result of our audit of NPWC and SPAWAR Systems Center purchase card activity for fiscal year 2000. Background information on the Navy purchase card program is included in appendix I.

Summary

For fiscal year 2001, internal controls at SPAWAR Systems Center and NPWC continued to be ineffective, leaving both units vulnerable to fraudulent, improper, and abusive purchases and to theft and misuse of government property. Both units had made some improvements in the overall control environment, primarily after the end of fiscal year 2001. Key improvements included reductions in the number of cardholders, an increase in the number of approving officials, an overall decrease in the aggregate monthly credit limits, and a decrease in purchase card usage.

At the same time, serious weaknesses remained in three key control environment areas, particularly at SPAWAR Systems Center. First, while both SPAWAR Systems Center and NPWC have taken steps to implement our recommendations regarding cardholder training and proper documentation of training, SPAWAR Systems Center still needs to do more to make sure all cardholders receive required training and to document the training taken by cardholders. For example, as of January 21, 2002 there was no documentation demonstrating that 146 cardholders had taken certain required training. As of February 15, 2002, SPAWAR Systems Center had suspended the accounts of only 5 of the cardholders who had not taken the required training. In contrast, NPWC has taken steps to provide cardholders and approving officials the necessary training and to assure itself that untrained personnel do not remain purchase card holders. On October 26, 2001, NPWC cancelled the cards of its 15 employees who had not complied with training requirements.

Second, both SPAWAR Systems Center and NPWC have recently made some efforts to implement new policies directed at improving internal review and oversight activities, which, as

[5]U.S. General Accounting Office, *Purchase Cards: Control Weaknesses Leave Two Navy Units Vulnerable to Fraud and Abuse*, GAO-02-32 (Washington, D.C.: Nov. 30, 2001).

we previously testified, had been ineffective. Both units performed a Navy-mandated "stand-down" review of purchase card transactions, but neither performed an in-depth analysis of the selected transactions. We question SPAWAR Systems Center's results in particular because it reported that it reviewed about 16,000 transactions and ultimately identified only one purchase that was not for a legitimate government purchase—a case in which the cardholder accidentally used the purchase card instead of a personal credit card. By comparison, our follow-up work identified numerous examples of potentially fraudulent, improper and abusive or questionable transactions that occurred in a similar time frame.

Third, we identified a significant impairment of management "tone at the top" at SPAWAR Systems Center during the last quarter of fiscal year 2001. The former commanding officer testified at the July 30, 2001, hearing before this subcommittee that the purchase card program at SPAWAR Systems Center had effective management controls and indicated that the trust SPAWAR Systems Center management had in its staff was an acceptable substitute for a cost-effective system of internal controls. Following the hearing, for the most part, the "tone at the top" at SPAWAR Systems Center was "business as usual." In contrast, the commanding officer at NPWC was proactive in addressing the weaknesses we identified and took immediate action to address any improper or prohibited uses of the purchase card. In December 2001, the former SPAWAR Systems Center commanding officer was relieved of duty for findings of dereliction of duty and conduct unbecoming an officer in matters unrelated to the purchase card program.

We are encouraged by the commitment of the new commanding officer to ensure that an effective, well-controlled purchase card program is implemented at SPAWAR Systems Center. However, we remain concerned that there will be significant cultural resistance to change in the internal control environment. For example, up to the time we completed our fieldwork in February 2002, some cardholders and managers continued to rationalize the questionable purchases we brought to their attention—including expensive laptop carrying cases, Lego robot kits, clothing, food, and designer day planners—as discussed later in this statement. Such an attitude perpetuates an overall environment that tacitly condones possibly fraudulent, wasteful, abusive, or otherwise questionable spending of government funds.

The two basic internal controls over the purchase card program that we tested remained ineffective during the last quarter of fiscal year 2001 at the two units. Specifically, SPAWAR Systems Center did not have independent, documented evidence that it received and accepted items ordered and paid for with the purchase card for about 56 percent of its fourth quarter fiscal year 2001 transactions. NPWC significantly improved its adherence to this internal control, although its 16 percent failure rate is still too high. The improved results for NPWC are the result of management attention to this important control and increased training for cardholders. We again tested independent, documented certification of monthly purchase card statements and found that for the fourth quarter of fiscal year 2001, the two units continued to pay the monthly credit card bills without any independent review prior to payment to ensure transactions represented valid, necessary government purchases.

In addition, we attempted to test whether easily pilferable or sensitive items were being recorded in the units' property records to help prevent and detect theft, loss, and misuse of government assets. Our previous work showed that this was a serious problem. However, we were unable to

perform those tests as part of our follow-up work because SPAWAR Systems Center, in accordance with a Navy policy change, recently revised its policy and no longer maintains accountability over easily pilferable items such as personal digital assistants and digital cameras. We disagree with the Navy and SPAWAR Systems Center policy and believe that property that is pilferable and easily converted to personal use should be accounted for. NPWC generally does not use purchase cards to buy pilferable items, and our statistical sample at NPWC did not identify any accountable property items.

In our June 30, 2001, testimony, we identified a number of potential fraud cases related to the two San Diego Navy units. We followed up on two of those cases, which highlighted the major role that poor internal control plays in fraud. In one case, we investigated about $12,000 of potentially fraudulent fiscal year 2000 transactions related to the purchase card of a former NPWC employee. The purchases—made between December 20 and 26, 1999—included an Amana range, Compaq computers, gift certificates, groceries, and clothing. The cardholder's supervisor approved the purchase card statement that included these charges without reviewing it. NPWC also did not properly cancel this purchase card account after the cardholder had moved on to another organization within the Navy, and the cardholder subsequently used the purchase card for a personal car rental that was approved for payment by NPWC. This individual now works at the Pentagon.

We also followed up on the previously reported compromise in September 1999 of up to 2,600 purchase card accounts assigned to Navy activities in the San Diego area. Immediate cancellation of these accounts was imperative, especially since the weaknesses in controls over receipt and acceptance and certification of monthly statements at SPAWAR Systems Center and NPWC would severely hamper the detection of fraudulent purchases associated with compromised accounts. We reported that Navy investigators were only able to identify a partial list consisting of 681 compromised accounts. In December 2001, Navy notified us that all 681 compromised accounts identified in the July testimony were cancelled, including 22 active SPAWAR Systems Center accounts. However, no other action was taken by the Navy to identify or cancel the remaining over 1,900 compromised accounts. Our investigators subsequently identified the source of the compromised accounts as the database of a Navy vendor. In January 2002, the vendor provided our investigators with the entire listing of the 2,595 compromised accounts. We provided this list to the Navy and recommended that it immediately cancel the remaining 1,914 compromised account numbers. Included on the list were 78 SPAWAR Systems Center and 10 NPWC accounts that were active as of December 2001.

The specific internal control weaknesses at SPAWAR Systems Center and NPWC contributed to additional purchases during fiscal year 2001 that we believe are fraudulent, improper, abusive, or otherwise questionable. Most of the problem transactions were at SPAWAR Systems Center and had been approved and represented to us as being appropriate, proper uses of the purchase card. The number and severity of the problems we identified at NPWC were substantially less than at SPAWAR Systems Center. In addition, rather than dispute our findings on each transaction, NPWC showed a proactive response and not only concurred with our findings but immediately took action to help prevent future fraudulent, improper, or abusive transactions from occurring.

As discussed in appendix II, our work was not designed to identify, and we cannot determine, the extent of fraudulent, improper, abusive, or otherwise questionable transactions.

We found a number of improper purchases at SPAWAR Systems Center and NPWC that were not permitted by law, regulation, or DOD policy. For example, we identified about $8,500 in food and refreshments that should not have been purchased for SPAWAR Systems Center and NPWC employees. Without statutory authority, appropriated funds may not be used to furnish meals or refreshments to employees within their normal duty stations.[6] In most of these cases, it appears that the cardholders were aware of the prohibition on food purchases but made the purchases anyway. The monthly certification process failed to detect the improper food purchases. Moreover, while NPWC officials acknowledged the impropriety of the food purchases we identified, SPAWAR Systems Center officials indicated that most of the food purchases made by their cardholders were a legitimate government expense, a conclusion with which we disagree.

Further, we identified abusive or questionable purchases by SPAWAR Systems Center cardholders that were at an excessive cost, for a questionable government need, or both. For example, we identified purchases of day planners and calendars from commercial vendors, including calendar refills and designer leather holders purchased from Louis Vuitton and Franklin Covey. With the cost of a single Louis Vuitton day planner cover at about $250, the issue of excessive cost and abuse is clear. Further, by law, government agencies are directed to purchase certain products, including day planners and calendars, from certified nonprofit agencies that employ people who are blind or severely disabled. The most expensive day planner available from these agencies costs about $40. In addition, we identified about $33,000 of abusive or questionable purchases from Franklin Covey of designer and high-cost leather briefcases, totes (purses), portfolios, Palm Pilot carrying cases, and wallets. Other examples include abusive and wasteful usage of cell phones, a trip for about 30 staff for an organizational meeting in Las Vegas, and clothing. We also identified abusive and possibly fraudulent purchases of luggage, Lego robot kits, and high-cost computer bags that were given away by SPAWAR Systems Center employees. Only one of the cardholders referred to in this testimony or our July 30, 2001, testimony had formal disciplinary action—in the form of removal of the purchase card—taken against them.

Scope and Methodology

We conducted our audit work from November 2001 through February 2002 in accordance with U.S. generally accepted government auditing standards, and we performed our investigative work in accordance with standards prescribed by the President's Council on Integrity and Efficiency. We briefed officials from the Department of Defense Purchase Card Program Management Office, Naval Supply Systems Command (NAVSUP), assistant secretaries of Navy for financial management (comptroller) and research development and acquisition, SPAWAR Systems Center, and NPWC on the details of our audit, including our objectives, scope, and methodology and our findings and conclusions. We referred instances of potentially fraudulent transactions that we identified during our work to our Office of Special Investigations for further investigation. Our control tests were based on stratified random probability samples of 50

[6] 72 Comp. Gen. 178, 179 (1993); 65 Comp. Gen. 508, 509 (1986).

SPAWAR Systems Center purchase card transactions and 94 NPWC transactions. We also reviewed a nonrepresentative selection of transactions using data mining intended to identify potentially fraudulent, improper, abusive, or otherwise questionable transactions. In total, we audited 161 SPAWAR Systems Center and 145 NPWC fiscal year 2001 transactions. Our work was not designed to identify, and therefore we did not determine, the extent of fraudulent, improper, or abusive transactions and related activities. Further details on our objectives, scope, and methodology are included in appendix II.

Some Improvements to Purchase Card Control Environment but Weaknesses Remain

In our follow-up audit, we found that both units had made some improvements in the overall control environment, primarily after the end of fiscal year 2001. However, the control environment at SPAWAR Systems Center continued to have significant weaknesses, while NPWC had made major strides towards a positive control environment. *GAO's Standards for Internal Control in the Federal Government* (GAO/AIMD-00-21.3.1, November 1999) state that, "A positive control environment is the foundation for all other standards. It provides discipline and structure as well as the climate which influences the quality of internal control." Our previous work found that a weak internal control environment at SPAWAR Systems Center and NPWC contributed to internal control weaknesses and fraudulent, improper, and abusive or questionable activity. In July 2001, we testified that the specific factors that contributed to the lack of a positive control environment at these two units included a proliferation of cardholders, ineffective training of cardholders and certifying officers, and a lack of monitoring and oversight. The following sections provide an update on the status of these conditions as well as information on several additional factors that affected the overall control environment at these Navy units.

Number of Cardholders Reduced but Significant Financial Exposure Continued

Although both units have reduced the number of cardholders, balancing the business needs of the unit with the training, monitoring, and oversight needed for a substantial number of cardholders remains a key issue. In October 2001, NAVSUP issued an interim change to its existing purchase card instructions to establish minimum criteria that prospective purchase card holders must meet before a purchase card account (including convenience check accounts[7]) can be established in the employee's name. The interim change issued by NAVSUP also established a maximum "span of control" of 5 to 7 cardholders to each approving official[8] and required that Navy activities establish local policies and procedures for approving and issuing purchase cards

[7]Convenience checks, also referred to as accommodation checks, are used for vendors that do not have the capability to accept payment by credit card. For the Navy, each unit generally has one individual authorized to write convenience checks.

[8]The approving official is responsible for reviewing and verifying the monthly purchase card statements of the cardholders under their purview. The approving official is responsible for verifying that all purchases were necessary and for official government purposes in accordance with applicable policies, laws, and regulations. Unless otherwise specified, the approving official must also be the certifying officer for his/her cardholders and in that capacity must certify that the monthly purchase card statement is appropriate and ready for payment.

to activity personnel. The Navy's span of control requirement reflects guidance issued by the Department of Defense Purchase Card Program Management Office on July 5, 2001, shortly before the Subcommittee hearing. The revised guidance stated that, generally, an approving official's span of control—cardholders per approving official—should not exceed a ratio of 7 to 1. Neither of the two units increased the number of approving officials to meet the suggested ratio until well after the start of fiscal year 2002. Table 1 summarizes the progress made by both units.

Table 1: Number of Cardholders and Approving Officials at SPAWAR Systems Center and NPWC

	SPAWAR			NPWC		
	9/21/00	**9/21/01**	**1/21/02**	**9/21/00**	**9/21/01**	**1/21/02**
Number of cardholders	1,153	950	793	292	226	185
Percent of employees who were cardholders	27%	22%	19%	17%	14%	12%
Ratio of cardholders to approving officials	1,153:1	950:1	4:1	42:1	32:1	4:1

Source: Citibank, SPAWAR Systems Center, and NPWC records.

The data in table 1 show that from September 21, 2000, to January 21, 2002, SPAWAR Systems Center had a net reduction in the number of cardholders of 360 (31 percent) and NPWC, 107 (37 percent). In addition, in fiscal year 2002, SPAWAR Systems Center increased the number of approving officials to 203 and NPWC, to 43. As a result, the approving official ratio for SPAWAR Systems Center and NPWC is now in line with DOD's criterion of no more that 7 cardholders per official. However, as of January 21, 2002, SPAWAR Systems Center still had 23 approving officials who were responsible for more than 7 cardholders and therefore did not comply with the DOD and Navy span of control requirements.

SPAWAR Systems Center records show that it significantly reduced the number of cardholders, primarily through canceling cards of those that did not need them and through employee attrition. According to SPAWAR Systems Center officials, some SPAWAR Systems Center purchase cards were canceled because of misuse; however, we were unable to determine from SPAWAR Systems Center records how many of the cards were canceled for this reason. We previously reported that SPAWAR Systems Center had a significant span-of-control issue with one approving official responsible for certifying monthly purchase card statements for all of its cardholders. According to Citibank and SPAWAR Systems Center records, effective for the billing period ending January 21, 2002, SPAWAR Systems Center increased from 1 to 203 the number of approving officials responsible for certifying monthly summary invoices. This change reduced SPAWAR Systems Center's average span of control to 4 cardholders to each approving official, which is in line with DOD and Navy guidelines. We did not perform any testing for fiscal year 2002 transactions to determine whether the approving officials were in place and performing effective reviews. SPAWAR Systems Center management told us that they are continuing to evaluate the number of cardholders and the impact any further cuts would have on management's ability to support operations and keep employees working efficiently.

NPWC reduced the number of its cardholders through employee attrition and by canceling the cards of individuals who no longer needed them, had not taken required training, or had misused the card. Specifically, on July 6, 2001, the agency program coordinator (APC) gave each business line manager an analysis of monthly purchase card usage data for each of the cardholders under his or her supervision. The business line managers were instructed to analyze cardholder monthly transaction volume and reduce the number of cardholders by eliminating those cardholders they believed no longer needed a purchase card. NPWC also recently increased its number of approving officials from 7 as of September 21, 2001, to 43 by January 21, 2002. This significant increase brought the ratio of cardholders to approving officials in line with DOD and Navy guidelines.

Another key factor in minimizing the government's financial exposure is assessing the monthly credit limits available to cardholders. The undersecretary of defense for acquisition and technology emphasized in an August 2001 memorandum to the directors of all defense agencies, among others, that not every cardholder needs to have the maximum transaction or monthly limit and that supervisors should set reasonable limits based on what each person needs to buy as part of his or her job. We concur with the undersecretary's statements and continue to recommend that cardholder spending authority be limited as a way of minimizing the federal government's financial exposure.

As shown in table 2, total financial exposure, as evidenced by monthly credit limits for SPAWAR Systems Center and NPWC cardholders, has decreased substantially.

Table 2: SPAWAR Systems Center and NPWC Total Cardholder Credit Limits

(Dollars in millions)		
Date	**SPAWAR**	**NPWC**
September 21, 2000	$56.9	$13.5
September 21, 2001	33.0	12.9
January 21, 2002	28.0	12.1
Total reduction	50.8%	10.4%

Source: Citibank, SPAWAR Systems Center, and NPWC records.

SPAWAR Systems Center reduced the overall credit limits of it cardholders by about $29 million primarily by (1) eliminating nearly $10 million of credit assigned to each of two cardholders and (2) reducing the net number of cardholders by 360. As we previously reported, most SPAWAR Systems Center cardholders had a $25,000 credit limit, and no cardholder had a credit limit of less than $25,000. We continue to believe that a $25,000 minimum credit limit is more than most SPAWAR Systems Center cardholders need to perform their mission. This point is best demonstrated by the fact that even when we used SPAWAR Systems Center's reduced number of cardholders, the average monthly purchase card bill in fiscal year 2001 would have been less than $5,000.

As shown in table 2, Citibank's records indicate that between September 21, 2000, and January 21, 2002, NPWC reduced its cardholder exposure from about $13.5 million to $12.1 million—a $1.4 million reduction. NPWC achieved this reduction primarily by reducing by 107 the number

of individuals who had purchase cards and by reevaluating cardholders' monthly credit limits. We previously reported that most NPWC cardholders were granted a monthly credit limit of $20,000. Currently, about 20 NPWC cardholders have a credit limit of less than $20,000, about 42 percent still have a $20,000 credit limit, and the remaining cardholders have higher credit limits to meet job needs. Further, the average monthly purchase card bill (using the reduced number of cardholders) in fiscal year 2001 for NPWC cardholders would have been about $11,500. On September 7, 2001, the NPWC agency program coordinator distributed spreadsheet analyses of individual cardholder actual monthly and average charges, along with suggested new monthly cardholder limits, to the respective cardholder's business line managers. The agency program coordinator required the business line managers to respond to the agency program coordinator with new limits for cardholders by the close of business on September 21, 2001. At the exit meeting we held with NPWC officials, NPWC provided Citibank records documenting that NPWC further reduced its cardholder credit limits to $5.6 million in February 2002.

In addition to the reductions in the number of cardholders and aggregate financial exposure, the dollar volume of transactions decreased significantly in fiscal year 2001 when compared to fiscal year 2000, as shown in table 3.

Table 3: SPAWAR Systems Center and NPWC Purchase Card Spending, Fiscal Years 2000 and 2001

Dollars in millions				
	FY 2000[a]	**FY 2001[b]**	**Reduction**	**Percent reduction**
SPAWAR	$45	$39	$(6)	13%
NPWC	$30	$25	$(5)	17%

[a] SPAWAR Systems Center and NPWC used the purchase card in fiscal year 2000 to make a total of about $75 million in acquisitions. About $68 million of those acquisitions were made by cardholders located in San Diego.
[b] SPAWAR Systems Center and NPWC used the purchase card in fiscal year 2001 to make a total of about $64 million in acquisitions. About $50 million of those acquisitions were made by cardholders located in San Diego.
Source: Citibank, SPAWAR Systems Center, and NPWC records.

The NPWC agency program coordinator attributed a portion of this decrease to increased controls over the use of purchase cards, resulting in a reduction in unnecessary and improper card usage. Other reasons were a reduction in the number of projects worked on during fiscal year 2001 and the use of more contracts for goods and services, which are paid by means other than the purchase card. The SPAWAR Systems Center senior military contracting official told us that SPAWAR Systems Center's reduction in purchase card use is a result of a decrease in workload and an increase in concern over purchase card controls brought on as a result of our audit and the congressional hearing.

Training of Cardholders

While both SPAWAR Systems Center and NPWC have taken steps to implement our recommendations regarding cardholder training and proper documentation of training, SPAWAR

Systems Center still needs to do more to make sure all cardholders receive required training and to document the training taken by cardholders. We previously reported that the lack of documented evidence of purchase card training contributed to a weak internal control environment at these two units. GAO's internal control standards emphasize that effective management of an organization's workforce—its human capital—is essential to achieving results and is an important part of internal control. Training is key to ensuring that the workforce has the skills necessary to achieve organizational goals. In accordance with NAVSUP Instruction 4200.94, all cardholders and approving officials must receive purchase card training. Specifically, NAVSUP 4200.94 requires that prior to the issuance of a purchase card, all prospective cardholders and approving officials must receive training regarding both Navy policies and procedures as well as local internal operating procedures. Once initial training is received, the Instruction requires all cardholders to receive refresher training every 2 years. Further, in response to our previous audit and the July 30, 2001, hearing, NAVSUP sent a message in August 2001 to all Navy units directing them to train all of their cardholders concerning the proper use of the purchase cards on or about September 12, 2001.

SPAWAR Systems Center training records indicated that as of January 21, 2002, 146 cardholders either had not completed the NAVSUP-mandated training or had not produced a certificate evidencing completion of the training. In addition, 13 active cardholders had not satisfied the requirement to take refresher training every 2 years. SPAWAR Systems Center officials told us that they intended to suspend the accounts of cardholders who had not taken the required training; however, as of February 15, 2002, the accounts of only 5 cardholders had been suspended.

NPWC has taken well-documented steps to provide cardholders and approving officials the necessary training and to assure itself that untrained personnel do not remain purchase card holders. As a result of our previous audit findings in this area, NPWC held mandatory cardholder training sessions in June 2001 and July 2001, which all cardholders and their supervisors attended. In addition, NPWC presented NAVSUP-prepared training for all cardholders and approving officials in September 2001. The mandatory NAVSUP training addressed the issues of receipt and acceptance, spending limits, accounting, unauthorized or personal use of the card, policies and procedures, improper transactions, NPWC internal procedures, other required training, the NAVSUP and Citibank Web sites, and our findings from the previous purchase card testimony and related report. All but 15 of NPWC's cardholders and approving officials attended the mandatory NAVSUP training, and on October 26, 2001, NPWC canceled the 15 remaining cardholder accounts for noncompliance with the training requirements.

Monitoring and Oversight

Both SPAWAR Systems Center and NPWC have recently made some efforts to implement new policies directed at improving internal review and oversight activities, which, as we previously testified, were ineffective. We also testified that the Navy's purchase card policies and procedures did not require that the results of internal reviews be documented or that corrective actions be monitored to help ensure that they are effectively implemented. While still relatively

ineffective, this area has great potential to strengthen the control environment at these two Navy units.

We also previously testified that, although the SPAWAR Headquarters Command inspector general (IG) reviewed purchase card transactions generated by Headquarter cardholders during fiscal year 2000 and prepared a draft report summarizing the results of this review, the final report had not been issued at the conclusion of our fieldwork for the July 30, 2001, testimony. The final report[9] of this review was issued on July 19, 2001, and identified many of the internal control findings discussed in our prior review; however, the IG's report did not identify the kind of abusive transactions we identified. Also, on August 13, 2001, the Command IG began a limited review of the 2 most recent months of purchase card activity for Headquarters cardholders. The summary findings, which were released in a report dated October 16, 2001, have many of the internal control findings discussed later in this statement and similarly point to the need for clear, comprehensive policies, procedures, and training to resolve many of the control weaknesses and instances of questionable transactions. The IG also reported that it found some "transactions that appeared to be either 'excessive' or may have been of questionable good judgment," but did not provide examples of these potentially abusive transactions. The IG also reported that several cardholders had stated that they felt uncomfortable making purchases, but did not want to tell their supervisor "no" and suffer potentially adverse career consequences.

At the July 30, 2001, hearing we reported that the Naval Audit Service had conducted an audit of the NPWC purchase card program for which a report had not been issued. The Naval Audit Service completed its audit in December 2000 and reviewed transactions primarily occurring from March 1999 through August 2000. The Naval Audit Service issued its report[10] over 1 year later, on January 10, 2002. Some of the Naval Audit Service findings are of the same nature and significance as the findings reported in our previous testimony, although the Naval Audit Service report did not identify the improper or abusive transactions we discussed. The Naval Audit Service concluded that management of the purchase card program at NPWC was not sufficient to ensure the integrity of the command's purchase card program and that NPWC's internal operating procedures did not clearly define duties and responsibilities or adequately control the various processes involved in purchase card transactions. Further, the Naval Audit Service reported that maintenance and repair services were obtained on a "piece-meal" basis instead of being aggregated and performed as entire projects, which resulted in NPWC not taking advantage of its buying power to obtain discounts on its recurring purchases.

Further, in August 2001, following the July 30, 2001, purchase card congressional hearing, NAVSUP directed all Navy units to review 12 months of purchase card transactions. In response to this requirement, both SPAWAR Systems Center and NPWC reviewed samples of transactions, although neither performed an in-depth analysis of the selected transactions. For example, SPAWAR Systems Center told us that it reviewed 16,393 of the 45,318 transactions for the 9-month period ended July 2001. According to SPAWAR Systems Center, its stand-down review identified 187 split purchases and 9 transactions that initially appeared questionable or

[9]SPAWAR Headquarters Command Inspector General, *Review of International Merchant Purchase Authorization (IMPAC) Card at SPAWAR*, 98-16 (San Diego, Calif.: July19, 2001).
[10]Naval Audit Service, *Management of Purchase Card Program at Public Works Center, San Diego, CA*, N2002-0023 (Washington, D.C.: Jan. 10, 2002).

suspicious. After completing their review, SPAWAR Systems Center officials concluded that only one of these nine transactions was not for a legitimate government purpose, because the cardholder in question accidentally used the purchase card instead of a personal credit card. However, we question whether the stand-down review was designed and performed to be a thorough and critical analysis of the nature and magnitude of the control weaknesses and the extent to which fraudulent, improper, or abusive transactions were occurring during the 9-month period reviewed. Our own statistical sample of 50 transactions from just the last 3 billing cycles of fiscal year 2001 found one potentially fraudulent and subsequently disputed purchase and a total of 11 abusive or improper transactions on the monthly statements for 9 cardholders. Furthermore, as detailed later, we found numerous examples of abusive and improper transactions occurring in the first nine billing cycles of fiscal year 2001.

NPWC's stand-down review subjected 9,099 transactions out of 50,850 for the 12-month period ended August 31, 2001, to a documentation review. The review identified several cases of potential improper use and 320 cases of potential split purchases. However, the primary finding related to the use of the card for prohibited acquisitions of "noncommonly used" hazardous materials. NPWC estimated that approximately 600 of the transactions reviewed violated the Navy's prohibition against using the purchase card to acquire noncommonly used hazardous materials. Specifically, Navy purchase card policies and procedures require that prior to acquiring potentially hazardous materials, cardholders must first determine that a requested purchase meets the definition of a commonly used hazardous material and that the materials are carried on the unit's Authorized Use List. If the requested purchase does not meet the "commonly used" definition, the hazardous materials are to be procured by other means that bring the hazardous material under the control of a Hazardous Substance Management System (HSMS). Compliance with these requirements would then help ensure the safe storage, use, and disposal of the hazardous materials.

NPWC found that cardholders were using the purchase card to acquire noncommonly used hazardous materials such as bacterial control agents and toxic, corrosive solvents used to descale and deodorize sewage systems. Such hazardous material purchases were not being subjected to the required controls and, consequently, NPWC had no assurance that the approximately 600 reported purchases were stored, used, and disposed of in a safe and environmentally acceptable manner. To alleviate this problem, NPWC is working with the Fleet Industrial Supply Service to coordinate the maintenance and control of Navy hazardous materials. NPWC's identification and proactive attitude towards resolving this matter again demonstrate a positive control environment.

Management "Tone at the Top" Was
Significantly Impaired at SPAWAR Systems Center

GAO's internal control standards[11] state that management plays a key role in demonstrating and maintaining an organization's integrity and ethical values, "especially in setting and maintaining the organization's ethical tone, providing guidance for proper behavior, removing temptations for unethical behavior, and providing discipline when appropriate." At the time we began our follow-up review, the SPAWAR Systems Center commanding officer not only did not demonstrate a commitment to improving management controls but openly supported the status quo. Consequently, the lack of a positive control environment continued. In contrast, the commanding officer at NPWC continued to support a proactive attitude in addressing the weaknesses we identified and took immediate action to address any improper or prohibited uses of the purchase card. It is not surprising that, given these differences in the management tone at the two units, we continued to find numerous examples of potentially improper, abusive, and otherwise questionable use of the purchase card at SPAWAR Systems Center, while we found few such cases at NPWC.

The former SPAWAR Systems Center commanding officer testified on July 30, 2001, that the purchase card program at SPAWAR Systems Center had effective management controls and an honest and trustworthy workforce. The commanding officer went on to incorrectly characterize our audit approach and findings by stating that there was not a pervasive and serious abuse and fraud problem at SPAWAR Systems Center and that over 99.98 percent of purchases made by cardholders were for legitimate government purposes. The commanding officer did not acknowledge that the serious weaknesses in SPAWAR Systems Center's system of internal controls over the purchase card program left SPAWAR Systems Center vulnerable to the types of abusive and improper transactions that we found and that such abuses could occur without being detected.

Upon his return to San Diego following the hearing, the commanding officer held an "all-hands" meeting at a SPAWAR Systems Center auditorium that cardholders, approving officials, and managers were particularly encouraged to attend "... to clarify the substantial differences between the perception of problems reported in the press and the reality of the situation." At the meeting, the commanding officer showed a videotape of the entire congressional hearing. By denying that these weaknesses resulted in undetected misuse of purchase cards, the commanding officer effectively diminished the likelihood that substantive changes would be implemented or, if implemented, taken seriously. The underlying message of his testimony, his subsequent "all hands" meeting, and his meetings with us, was that the trust SPAWAR Systems Center management had in its staff was an acceptable substitute for a cost-effective system of internal controls.

The commanding officer was relieved of duty in December 2001 for matters unrelated to the purchase card program. The admiral in charge of SPAWAR held a nonjudicial punishment hearing on December 8, 2001, and found that the commanding officer had violated two articles of the Uniform Code of Military Justice, including dereliction of duty and conduct unbecoming

[11]U.S. General Accounting Office, *GAO's Standards for Internal Control in the Federal Government*, GAO/AIMD-00-21.3.1 (Washington, D.C.: Nov. 1999).

an officer. The admiral issued the commanding officer a Punitive Letter of Reprimand, relieved him of his command at SPAWAR Systems Center, and endorsed his request for retirement from the Navy.

The new commanding officer at SPAWAR Systems Center now has an opportunity to set a "ton at the top" that reflects a true commitment to establishing a positive control environment. Basec on our discussions with the commanding officer and some of the actions we have observed, we are encouraged by her commitment to ensure that an effective, well-controlled purchase card program is implemented at SPAWAR Systems Center. At the same time, we remain concerned that there will be significant cultural resistance to change in the internal control environment. For example, up to the time we completed our fieldwork in February 2002, some cardholders an managers continued to rationalize the questionable purchases we brought to their attention—including expensive laptop carrying cases, Lego robot kits, clothing, food, and designer day planners—as discussed later in this statement. Such an attitude perpetuates an overall environment that tacitly condones possibly fraudulent wasteful, abusive, or otherwise questionable spending of government funds.

Critical Internal Controls Remained Ineffective

Basic internal controls over the purchase card program remained ineffective during the last quarter of fiscal year 2001 at the two units we reviewed. Based on our tests of statistical sample of purchase card transactions, we determined that the two key transaction-level controls that we tested were ineffective, rendering SPAWAR Systems Center and NPWC purchase card transactions vulnerable to fraudulent and abusive purchases and theft and misuse of government property. As shown in table 4, the specific controls that we tested were (1) independent, documented receipt and acceptance of goods and services and (2) independent, documented review and certification of monthly purchase card statements.

Table 4: Estimate of Fiscal Year 2001 Transactions That Failed Control Tests[a]

Navy units in San Diego	Breakdowns in key purchase card controls[a]	
	Independent, documented receipt of items purchased	Proper certification of purchase card statements for payment
	Percent failure	Percent failure
SPAWAR Systems Center	56%	100%[b]
NPWC	16%	100%[c]

[a]The numbers represent point estimates for the population based on our sampling tests. The confidence intervals for our sampling estimates are presented in appendix II of this testimony.
[b]For the last quarter of fiscal year 2001, SPAWAR Systems Center continued to have only one certifying officer for almost 1,000 cardholders. This unacceptable span of control led us to conclude that all transactions selected as part of our statistical sample were not properly reviewed and approved by a certifying officer.
[c]Our statistical testing identified one transaction that was reconciled by the cardholder and approving official prior to payment. The projected error rate was 99.9 percent, which we rounded to 100 percent.

In addition, we attempted to test whether the accountable items—easily pilferable or sensitive items—included in some of the transactions in our samples were recorded in the units' property records to help prevent theft, loss, and misuse of government assets. However, we were unable to perform those tests because SPAWAR Systems Center had recently changed its policy and no longer maintains accountability over easily pilferable items such as personal digital assistants and digital cameras. Further, our statistical sample at NPWC did not identify any accountable property items.

NPWC Made Significant Improvements in Independent Receipt and Acceptance, While SPAWAR Systems Center Results Were Unchanged

SPAWAR Systems Center did not have independent, documented evidence that they received and accepted items ordered and paid for with the purchase card, which is required by Navy policy. That is, they generally did not have a receipt for the acquired goods and services that was signed and dated by someone other than the cardholder. As a result, there is no documented evidence that the government received the items purchased or that those items were not lost, stolen, or misused. Based on our testing, we estimate that SPAWAR Systems Center did not have independent, documented evidence to confirm the receipt and acceptance of goods and services acquired with the purchase card for about 56 percent of its fourth quarter fiscal year 2001 transactions. We previously reported a 65 percent control failure rate for fiscal year 2000.

NPWC improved its adherence to the internal control of documenting independent receipt and acceptance of items acquired with a purchase card, although its 16 percent failure rate in this control technique remained unacceptable. We previously testified that NPWC generally did not

have documented independent receipt and acceptance for goods and services and reported a 47 percent control failure rate for fiscal year 2000. The improved results for NPWC are the result of management attention to this important control and increased training for cardholders.

Review and Certification of Monthly Purchase Card Statements Remained a Significant Weakness at Both Units

Throughout fiscal year 2001, SPAWAR Systems Center and NPWC still did not properly review and certify the monthly purchase card statements for payment. We previously reported that SPAWAR Systems Center and NPWC approving officials who certify the monthly purchase card statements for payment generally rely upon the silence of a cardholder to assume that all purchase card transactions listed on the monthly statements are valid government purchases. However, this process does not compensate for the fact that a cardholder might have failed to forward corrections or exceptions to the account statement in a timely manner or, even worse, may not have reviewed the statement. As a result of the breakdown of this control, for the fourth quarter of fiscal year 2001, SPAWAR Systems Center and NPWC were paying the monthly credit card bills without any independent review of the monthly cardholder statements prior to payment to verify that the purchases were for a valid, necessary government need.

Under 31 U.S.C. 3325 and DOD's *Financial Management Regulation,*[12] disbursements are required to be made on the basis of a voucher certified by an authorized agency official. The certifying official is responsible for ensuring (1) the adequacy of supporting documentation, (2) the accuracy of payment calculations, and (3) the legality of the proposed payment under the appropriation or fund charged. The certification function is a preventive control that requires and provides the incentive for certifying officers to maintain proper controls over public funds. It also helps detect fraudulent and improper payments, including unsupported or prohibited transactions, split purchases, and duplicate payments. Further, section 933 of the National Defense Authorization Act for Fiscal Year 2000 requires the Secretary of Defense to prescribe regulations that ensure, among other things, that each purchase card holder and approving official is responsible for reconciling charges on a billing statement with receipts and other supporting documentation before certification of the monthly bill.

We previously reported that NAVSUP policy is inconsistent with the purpose of certifying vouchers prior to payment and made recommendations to revise the policy appropriately. Navy agreed with our recommendations concerning the need to change this portion of the purchase card instruction.

For the last quarter of fiscal year 2001, SPAWAR Systems Center continued to have only one approving official to certify for payment the monthly purchase card statements of almost 1,000 cardholders. This unacceptable span of control led us to conclude that all transactions selected as part of our statistical sample were not properly reviewed and approved by a certifying officer. NPWC also continued to inappropriately certify purchase card statements for payment before receiving cardholder assurance that the purchases were proper. Our review of purchase card transactions disclosed that no significant change in this process had taken place during the fourth

[12]DOD *Financial Management Regulation*, Volume 5, Chapter 33, "Accountable Officials and Certifying Officers."

quarter of fiscal year 2001, and we therefore identified a 100 percent failure rate for this control at SPAWAR Systems Center and NPWC.

However, in keeping with its proactive attitude, instead of waiting for NAVSUP to issue its new purchase card payment certification procedures, the NPWC agency program coordinator issued local guidance in December 2001 that requires approving officials, prior to certifying their summary invoice for payment, to obtain notifications from cardholders that their statements do not include disputed items. The guidance also indicates that approving officials and cardholders should conduct ongoing reviews during the month of the transactions in their purchase card accounts using Citidirect online services. While this does not fully implement the recommendation that we made in our November 30, 2001 report,[13] this is a positive interim step. Given the significant reduction in individual approving officials' span of control this measure provides NPWC an opportunity to strengthen this control.

Citing Policy Change, SPAWAR Systems Center Failed to Maintain Accountability for Pilferable Items

We disagree with a change in SPAWAR Systems Center policy that eliminated the accountability of certain property items considered to be pilferable. Recording items in the property records that are easily converted to personal use and maintaining serial number and bar code control is an important step in ensuring accountability and financial control over such assets and, along with periodic inventory, in preventing theft or improper use of government property. We previously testified that most of the accountable items—easily pilferable or sensitive items—in our samples for fiscal year 2000 were not recorded in property records.

On August 1, 2001, the Department of the Navy changed its definition for what constitutes pilferable property. Unlike the previous policy, which was prescriptive in identifying what was pilferable, the new policy provides commanding officers with latitude in determining what is and what is not pilferable. Specifically, the new policy defines pilferable to be an item—regardless of cost—that is portable, can be easily converted to personal use, is critical to the activity's business/mission, and is hard to repair or replace. Citing the "hard to repair or replace" criteria in the new policy, on November 1, 2001, SPAWAR Systems Center determined that only computer systems and notebook/laptop computers would be considered pilferable items. Thus, based on our fiscal year 2000 and 2001 audit work, SPAWAR Systems Center did not maintain accountability over numerous sensitive and pilferable items, such as digital cameras and personal digital assistants (PDA), leaving them subject to possible theft, misuse, or transfer to personal use.

SPAWAR Systems Center's new commanding officer and executive director told us that they do not believe that it is cost beneficial to account for and track these assets, but instead rely on supervisory oversight and personal employee trust to provide the necessary accountability of these assets. The commanding officer and the executive director stated that SPAWAR Systems Center is a diversified organization in which its scientists and engineers are working on as many as 1,000 different projects at any one time, which would make it difficult to keep track of these lower cost items. We acknowledge the important mission that SPAWAR Systems Center serves,

[13]GAO-02-32.

but we also believe that the diverse nature of its operations is one of the key reasons why SPAWAR Systems Center needs to maintain accountability of its pilferable items. As discussed later in this testimony, we believe that SPAWAR Systems Center's lack of accountability over items that are pilferable contributed to several abusive and questionable purchases.

Although NPWC also had the opportunity to redefine what constitutes pilferable property, NPWC did not institute a similar policy change. Unlike SPAWAR Systems Center, NPWC generally does not use the purchase card to buy property items that are pilferable or easily converted to personal use. As a result, our sample of fourth quarter fiscal year 2001 NPWC transactions did not include any accountable items.

Status of ERP Implementation at SPAWAR Systems Center

SPAWAR Systems Center officials stated that they have implemented a new Enterprise Resource Planning (ERP) system that is designed to address most of the weaknesses that we identified in our July 2001 testimony. Once effectively implemented, the ERP system would facilitate on-line review, reconciliation, and monitoring of credit card activity. The system would also result in reduced storage needs because ERP requires receipt and acceptance documentation to be scanned into a database storage container. However, our limited assessment of the control environment identified several weaknesses. Although the new system has the stated capability to address the weaknesses we identified in the purchase card program, until it is effectively implemented and individuals comply with purchase card policies and procedures, SPAWAR Systems Center has little assurance that the weaknesses we previously identified will be corrected or mitigated.

For example, the implementation of the ERP system at the time of our review did not provide for an adequate separation of duties or proper certification of purchase card transactions for payment. Specifically, a systems administrator with high-level administrative access privileges on the system performed both cardholder and approving official duties. In addition, the administrator pushed transactions through the system as an approving official without the required cardholder reconciliation or any knowledge of the transactions. Further, the administrator, who performed approving official duties, did not review the transactions to determine if they complied with Navy policies and procedures. That responsibility remained with the existing approving official; however, as we previously testified about the manual process, we found no evidence that the approving official verified compliance. SPAWAR Systems Center officials stated that by the end of February 2002, the administrator should no longer have these duties because all of the newly designated approving officials will have completed the required ERP training. We have not verified this corrective action or whether the approving officials are properly performing their duties.

In assessing the control environment, we attempted, but were unable, to obtain documentation such as (1) the DOD Information Technology Security Certification and Accreditation Process (DITSCAP)[14] for the system and (2) formal procedures on granting and removing access to the

[14]DOD Instruction 5200.40, December 30, 1997, and OPNAV Instruction 5239.1B, November 9, 1999, requires any DOD system that collects, stores, transmits, or processes unclassified or classified information to comply with the DITSCAP process to establish a more secure system operations.

ERP. First, SPAWAR Systems Center officials stated that the certification and accreditation for the ERP system was not complete and that it was currently operating under interim authority. The DITSCAP would give an indication as to whether SPAWAR Systems Center had established its information security requirements and whether the system implementation meets the established security requirements. Second, although SPAWAR Systems Center had an informal process for granting and removing system access, these procedures had not yet been formally documented. Establishing such formal control procedures helps ensure that authorized users have the appropriate access to perform their job duties.

Potentially Fraudulent, Improper, Abusive, and Questionable Transactions

We identified numerous examples of improper, abusive, or questionable transactions at SPAWAR Systems Center during fiscal year 2001. Given the weaknesses in the overall internal control environment and ineffective specific internal controls, it is not surprising that SPAWAR Systems Center did not detect or prevent these types of transactions. In fact, most of the transactions that we identified as improper, abusive, or questionable at SPAWAR Systems Center were approved and represented to us as being an appropriate, proper use of the purchase card. In contrast, using the same data mining techniques at NPWC, the number and severity of the problems we identified were substantially less than at SPAWAR Systems Center. In addition, rather than dispute our findings on each transaction, NPWC showed a proactive response and not only concurred with our findings but immediately took action to prevent future improper or abusive transactions from occurring. As discussed in appendix II, our work was not designed to identify, and we cannot determine, the extent of fraudulent, improper, and abusive or otherwise questionable transactions.

Further, our review of SPAWAR Systems Center and NPWC transactions for potentially fraudulent, improper, and abusive or otherwise questionable purchases was limited and not intended to represent the population of SPAWAR Systems Center and NPWC transactions. Specifically, we reviewed a total of 161 SPAWAR Systems Center and 145 NPWC fiscal year 2001 transactions and performed additional analysis of related activity at three specific vendors as discussed in appendix II. To test those transactions and related activity, we examined all available documentation supporting the transactions, and when necessary we interviewed NPWC and SPAWAR Systems Center staff. To put the number of transactions that we reviewed into perspective, during fiscal year 2001 SPAWAR Systems Center and NPWC processed a total of about 83,000 transactions. Thus, the potentially fraudulent, improper, and abusive or questionable transactions we identified relate to the 306 transactions and associated activity we reviewed. We cannot project the extent of potentially fraudulent, improper, or abusive transactions for SPAWAR Systems Center or NPWC to the entire population of fiscal year 2001 transactions. See appendix II for a more detailed discussion of our objectives, scope, and methodology.

Potentially Fraudulent Transactions

We considered potentially fraudulent purchases to include those made by cardholders that were unauthorized and intended for personal use. Some of these instances involved the use of

compromised accounts, in which an actual Navy purchase card or an active account number was stolen and used to make a fraudulent purchase. Other cases involved vendors charging Navy purchase cards for unauthorized transactions.

Both SPAWAR Systems Center and NPWC had policies and procedures that were designed to prevent the payment of fraudulent purchases; however, our tests showed that although both units made some improvements, particularly NPWC, they did not implement the controls as intended. For example, as discussed previously, controls were ineffective for independent verification of receipt and acceptance and proper review and certification of monthly statements prior to payment. Fraudulent activities must therefore be detected after the fact, during supervisor or internal reviews, and disputed charge procedures must be initiated to obtain a credit from Citibank. Table 5 shows examples of potentially fraudulent transactions that we identified at SPAWAR Systems Center. Using the same audit techniques, we did not find documented evidence of potentially fraudulent NPWC transactions for fiscal year 2001. However, as noted previously, our tests were not designed to identify all fraudulent transactions, and considering the control weaknesses identified at SPAWAR Systems Center and NPWC, and the substantial number of compromised accounts discussed later, fraudulent transactions may have occurred during fiscal year 2001 and not have been detected.

Table 5: Examples of Potentially Fraudulent Purchase Card Transactions at SPAWAR Systems Center

Type of items purchased	Vendor	Total amount	Source
Car rentals	Dollar Rent a Car	$338	Cardholder
Unknown	Kids R Us	$826	Compromised account
Phone calls	800-Collect	$516	Compromised account
Unknown	Car Club	$9,486	Compromised account
Adult entertainment, other Internet purchases	Paycom.net, Ibillcs.com	$285	Unknown
Unknown	Safety product vendor	$10,600	Vendor

The fact that all of the unauthorized transactions in table 5 were authorized for payment by SPAWAR Systems Center clearly demonstrates the lack of an effective review and monthly certification process. SPAWAR Systems Center officials told us that they were aware of all of these potentially fraudulent transactions and eventually received a credit from either the vendor or Citibank or reimbursement from the cardholder, but in some cases after many months. For example, the car rental transaction related to a SPAWAR Systems Center employee who stated that she had inadvertently used the purchase card rather than a personal credit card. However, it took the employee 5 months to reimburse the government for this personal and unauthorized charge. Three of the examples in table 5 relate to the 2,595 Navy purchase card compromised accounts discussed below. The card numbers used to make the internet purchases were not on the list of compromised accounts. These cardholders reported to Citibank that the transactions were unauthorized, and Citibank provided credits to their accounts for disputed amounts up to three months after SPAWAR Systems Center paid the bill. The $10,600 of potentially fraudulent

charges represent numerous unauthorized charges, many of which were about $500 each, during fiscal year 2001 by a safety product vendor that SPAWAR Systems Center paid despite the fact that no goods were received. As of January 21, 2002, SPAWAR Systems Center had not received a credit from the bank or the vendor for about $3,100 of the unauthorized charges.

In our July 2001 testimony, we identified about $12,000 in potentially fraudulent fiscal year 2000 transactions on the purchase card of a former NPWC employee. NPWC Command Evaluation staff researched the potentially fraudulent charges, and NPWC eventually disputed them and recovered the full amount from the bank. Our Office of Special Investigations conducted an investigation of the suspect employee to determine if these transactions were indeed fraudulent. This investigation identified the following.

- The purchases occurred primarily between December 20 and 26, 1999, and included an Amana range, Compaq computers, gift certificates, groceries, and clothes. Based on our research, most of the merchants noted that these were not phone orders and someone presented the purchase card in question to make the purchases.
- The cardholder brought the January 2000 credit card statement, with the above charges on the bill, to her supervisor for his approval and signature. According to the supervisor, the cardholder told him that she needed the statement signed immediately because she was late in processing it. The supervisor signed the credit card statement without reviewing it.
- The cardholder claims to have disputed the charges on January 31, 2000. Citibank indicated that it did not receive the dispute documentation until August 23, 2000, and the bank did not credit the Navy for these charges until April 2001.
- Based on an examination of the handwriting specimens by the U.S. Secret Service Forensic Services Division, the fraudulent purchase receipts were probably signed by someone other than the cardholder and all appear to have been signed by the same individual.
- The Amana range was bought with a gift card that was purchased in the name of the cardholder's alleged ex-boyfriend's mother.
- The cardholder left NPWC to work for the U.S. Pacific Fleet from June to November of 2000 and now works at the Pentagon. After leaving work on her last day at NPWC, the cardholder improperly used the NPWC purchase card—which should have been canceled—for a personal automobile rental that was initially paid by NPWC and subsequently reversed through a credit from Citibank. The cardholder was supposed to, but has not yet, repaid Citibank the $358 owed.
- The cardholder also misused a government travel card by purchasing three airline tickets for personal use. The cardholder partially repaid the cost of the tickets but had a remaining balance of $379. The Bank of America has written off the balance of the cardholder's account.

The facts of this case demonstrate a complete breakdown in internal controls, particularly in the area of proper review and certification of monthly statements. The individual who approved the payment to Citibank for these fraudulent charges told us that he signed off on the January 2000 statement without reviewing it to determine if the transactions were valid. It is unclear whether the credit NPWC ultimately received was the result of the Citibank investigation of the case or NPWC's determining some time after payment of the bill that the charges were fraudulent.

NPWC also did not properly cancel the purchase card account of this cardholder after the cardholder had moved on to another organization within the Navy. Further, NPWC paid the purchase card bill that included this cardholder's personal automobile rental, a clear indication that the monthly review and certification of bills was not being done. Finally, as of February 6, 2002, no disciplinary actions had been taken against this cardholder. Our Office of Special Investigations referred this case back to the Naval Criminal Investigative Service for further investigation and, if warranted, prosecution.

We also followed up on the previously reported September 1999 compromise of up to 2,600 purchase card accounts assigned to Navy activities in the San Diego area. We reported that Navy investigators were able to identify only a partial list consisting of 681 compromised accounts. We recommended that the Navy act immediately to cancel all known active compromised accounts. In December 2001, Navy notified us that all 681 compromised accounts we identified in the July testimony were cancelled, including 22 active SPAWAR Systems Center accounts. However, no other action was taken by the Navy to identify or cancel the remaining nearly 2,000 accounts that were compromised in September 1999. Our investigators subsequently identified the source of the compromised accounts as the database of a Navy vendor, which provided NCIS with the names of its former employees who were possible suspects in the theft of data. In January 2002, the vendor provided our investigators with the entire list of the 2,595 compromised accounts. We provided this list to the Navy and recommended that it immediately cancel the remaining 1,914 compromised account numbers. We found that 78 SPAWAR Systems Center and 10 NPWC compromised accounts were active as of December 2001. As noted previously, 3 of the examples of potentially fraudulent SPAWAR Systems Center activity reported in table 5 involved these compromised accounts.

As we reported in our previous testimony, as of January 2001, at least 30 of the nearly 2,600 compromised account numbers were used by 27 alleged suspects to make more than $27,000 in fraudulent transactions for pizza, jewelry, phone calls, tires, and flowers. However, with the lack of effective controls over independent receipt for goods and services and proper review and certification of purchase card statements for payment that we identified at the two units, it will be difficult, if not impossible, for the Navy—including SPAWAR Systems Center and NPWC—to identify fraudulent purchases as they occur, or to determine the extent of the fraudulent use of compromised accounts. On December 11, 2001, the NCIS case on the compromised Navy purchase card numbers was presented to the U.S. Attorney's Office, Southern District of California, San Diego, for prosecution. The U.S. Attorney's Office declined prosecution of the case due to the low known dollar loss of $28,734. The NCIS case was closed on December 20, 2001.

The following are other cases of potential fraudulent activity.

- A fraud hotline call alerted NPWC to a case involving two NPWC employees, an air conditioning equipment mechanic—who was a purchase card holder—and his supervisor. The alleged fraud includes the element of collusion, which internal controls generally are not designed to prevent. However, adequate monitoring of purchase card transactions, along with the enforcement of controls—such as documentation of independent confirmation of receipt and acceptance and recording of accountable items in property records—will make detection easier. In this case, the cardholder allegedly made

fraudulent purchase card acquisitions during the period of April 1999 through December 1999 to obtain electronic planners, leather organizers, a digital camera, a scanner/printer, and various cellular telephone accessories for himself and his supervisor. These items totaled more than $2,500. NPWC initiated administrative action and gave a notice of proposed removal to the cardholder on August 15, 2000, and to the supervisor on August 1, 2000. Both employees resigned after they had repaid the Navy nearly $6,000 but before formal removal. Criminal actions were not taken against the individuals.

- SPAWAR Systems Center's Command Evaluation is currently investigating purchases made by cardholders in one of SPAWAR Systems Center's divisions. This is an ongoing investigation focused on transactions made during the period August 2000 through April 2001. Preliminary findings resulted in a request from Command Evaluation to the SPAWAR Systems Center agency program coordinator to suspend purchase card authority for all cardholders and approving officials in the affected division until the investigation is completed.
- Our Office of Special Investigations is conducting a further investigation of about $164,000 in transactions during fiscal year 2001 between SPAWAR Systems Center and one of its contractors for potentially fraudulent activity. The SPAWAR Systems Center division responsible for these purchase card transactions is the same department that SPAWAR Systems Center's Command Evaluation is currently reviewing, as discussed in the previous bullet. This case is discussed in more detail in the following section on improper purchases.

Improper Transactions

We identified transactions for SPAWAR Systems Center and NPWC that were improper, including some that involved the improper use of federal funds. The transactions we determined to be improper are those purchases intended for government use, but are not for a purpose that is permitted by law, regulation, or DOD policy. We also identified as improper numerous purchases made on the same day from the same vendor that appeared to circumvent cardholder single transaction limits. *Federal Acquisition Regulation* and NAVSUP Instruction 4200.94 guidelines prohibit splitting purchase requirements into more than one transaction to avoid the need to obtain competitive bids on purchases over the $2,500 micropurchase threshold or to circumvent higher single transaction limits for payments on deliverables under requirements contracts. We identified these improper transactions as part of our review of about 161 SPAWAR Systems Center and 145 NPWC fiscal year 2001 transactions and related activity. We identified most of these transactions as part of our data mining of transactions with questionable vendors, although several were identified as part of our statistical sample.

Transactions Not Permitted by Law, Regulation, or DOD Policy

The *Federal Acquisition Regulation*, 48 C.F.R. 13.301(a), provides that the governmentwide commercial purchase card "may be used only for purchases that are otherwise authorized by law or regulations." Therefore, a procurement using the purchase card is lawful only if it would be lawful using conventional procurement methods. Under 31 U.S.C. 1301(a), "[a]ppropriations shall only be applied to the objects for which the appropriations were made . . ." In the absence of specific statutory authority, appropriated funds may only be used to purchase items for official

purposes, and may not be used to acquire items for the personal benefit of a government employee. As previously discussed NPWC identified approximately 600 transactions that violated the Navy's prohibition against using the purchase card to acquire noncommonly used hazardous materials. As shown in table 6, we found examples of purchases that were not authorized by law, regulation, or policy.

Table 6: Transactions Not Permitted by Law, Regulation, or Policy

Type of items purchased	Unit	Example vendors	Nature of improper transaction	Total transacti amount
Food and refreshments	Both	Admiral Kidd Catering, Omni Hotel, Expressly Gourmet, Dave's Snack Bar, Embassy Suites	Not authorized by law	$ 8,
Clothing	SPAWAR	Sport Chalet, Twig's Alaskan Gifts	Not authorized by law; see additional clothing in table 8	$
Luxury rental cars (e.g., Lincoln Town Car)	NPWC	Enterprise, Courtesy, Fuller	Not in accordance with DOD policy; abusive	$7,
Contracted services	SPAWAR	Telecommunications contractor	Not in accordance with Navy policy; potentially fraudulent	$164,
Convenience check	SPAWAR	U.S. Postal Service	Not in accordance with DOD policy; abusive	$347,
Printing services	SPAWAR	Kinko's	Not in accordance with policy to use the Defense Automated Printing Service	$3,
Sales tax	SPAWAR	Numerous	Not authorized by law	$

Food. We found a number of purchases of food at SPAWAR Headquarters, SPAWAR Systems Center and NPWC that represent an improper use of federal funds. Without statutory authority, appropriated funds may not be used to furnish meals or refreshments to employees within their normal duty stations.[15] Free food and other refreshments normally cannot be justified as a necessary expense of an agency's appropriation because these items are considered personal expenses that federal employees should pay for from their own salaries.[16] In January 2000, the General Services Administration (GSA) amended the government travel regulations to permit agencies to provide light refreshments to employees attending conferences involving travel. In response to GSA's action, DOD amended the Joint Travel Regulation (JTR) and Joint Federal Travel Regulation (JFTR) to permit similar light refreshments for DOD civilian employees and military members. In April 2001, DOD clarified the JTR/JFTR rule to permit light refreshments only when a majority of the attendees (51 percent or more) are in travel status.[17] The following food purchases should not have been paid for with appropriated funds.

[15] 72 Comp. Gen. 178, 179 (1993); 65 Comp. Gen. 508, 509 (1986).

[16] 65 Comp. Gen. 738, 739 (1986).

[17] For purposes of this testimony, we determined a purchase of food to be improper if it did not comply with the JTR/JFTR light refreshment rule. However, we have some questions about the validity of this rule and therefore do not necessarily conclude that food purchases in accordance with this rule are proper. We are currently working on a legal decision concerning the validity of the GSA and DOD light refreshment policies.

- Three instances in which NPWC purchased primarily meals and light refreshments for employee-related activities, including team meetings, at a cost of about $4,100. The supporting documentation we were provided initially by NPWC showed these purchases to be the rental of rooms for meetings. However, after our further inquiry of the Admiral Kidd Catering Center we found that a large portion of the purchases were related to food and refreshments including luncheon buffets. Officials from the Admiral Kidd Catering Center indicated that the invoices for these events do not show the food purchases because they knew that the Navy is not allowed to pay for food at these conferences.
- Five instances in which SPAWAR Headquarters or Systems Center cardholders purchased primarily light refreshments for employee team meetings or training sessions when less than a majority of the attendees were on travel, at a total cost of about $1,000.
- One transaction in which a SPAWAR Headquarters program management office had a 2-day off-site meeting at a San Diego hotel for about 20 staff, and SPAWAR Headquarters provided all participants with lunch and refreshments. The cardholder provided us with documentation indicating that SPAWAR Headquarters spent $2,400 to rent a room at the hotel where the meeting was held. The assistant program manager told us that the $2,400 charge was just for the meeting room rental. However, we obtained documents directly from the hotel, which were signed by the assistant program manager, that prove that SPAWAR Headquarters paid about $1,400 for lunch and refreshments for both days. Furthermore, by comparing the hotel's copy of the event confirmation form with the copy of the same form provided by SPAWAR Headquarters, it appeared that the form had been altered to indicate that the $2,400 was only for rent. After briefing SPAWAR Headquarters and System Center management of our findings, the SPAWAR Headquarters inspector general opened an investigation of this matter that is still ongoing.

Clothing. We identified several purchases of clothing by SPAWAR Systems Center employees that should not have been purchased with appropriated funds. According to 5 U.S.C. 7903, agencies are authorized to purchase protective clothing for employee use if the agency can show that (1) the item is special and not part of the ordinary furnishings that an employee is expected to supply, (2) the item is essential for the safe and successful accomplishment of the agency's mission, not solely for the employee's protection, and (3) the employee is engaged in hazardous duty. Further, according to a comptroller general decision dated March 6, 1984,[18] clothing purchased pursuant to this statute is property of the U.S. government and must only be used for official government business. Thus, except for rare circumstances in which a clothing purchase meets stringent requirements, it is usually considered a personal item that should be purchased by the individual.

For the transactions that we tested, we found that several SPAWAR Systems Center employees had purchased clothing, such as a lightweight hooded jacket, long pants, and a shirt that should have been purchased by the employees with their own money. One of the cardholders told us that he believed his purchases of clothing were appropriate because other SPAWAR Systems Center employees were also purchasing clothing. As a result of this statement, we expanded our analysis and found that during fiscal year 2001 SPAWAR Systems Center cardholders purchased

[18] 63 Comp. Gen. 245, 247 (1984). In requesting the comptroller general's approval of the purchases, the agency represented that "the parkas would be labeled as [agency] property, centrally controlled, and issued and reissued to employees only for job requirements." SPAWAR Systems Center officials have not made a similar representation.

about $4,400 worth of socks, gloves, parkas, jackets, hats, shirts, and sweatpants from REI and Cabela's that appear to also be improper. Because we did not test each of these transactions to determine if they were adequately justified, we included the $4,400 as questionable clothing purchases in table 8.

Luxury car rentals. We identified 34 fiscal year 2001 purchases totaling $7,028 in which NPWC could not support the representation that rentals of Lincoln Town Cars or similar luxury cars were for individuals authorized to obtain a luxury car. DOD policy provides that only four-star admirals and above (or equivalent) qualify to rent such luxury vehicles. Our analysis of NPWC's fiscal year 2001 purchase card transactions for rentals of commercial vehicles disclosed 42 instances of rentals of luxury vehicles (e.g., Lincoln Town Cars and Cadillac DeVilles). NPWC cardholder documentation showed that only 8 of the 42 rentals were for four-star admirals. In the other 34 instances, cardholder documentation either disclosed that a rental of a Lincoln Town Car or similar vehicle was for a Navy captain or lower-ranking admiral, or the documentation was insufficient to determine who rented the automobile. As a result of its inappropriately renting the Lincolns and other luxury cars, we estimated that NPWC spent about $2,000 more than it would have if NPWC had rented an automobile that was consistent with DOD policy. Consistent with NPWC's proactive approach, the day after we brought this issue to management's attention, controls and procedures were put in place to resolve this issue. Because these purchases were at an excessive cost, they also fall under the definition of abusive transactions.

Prepayment of goods and services. We also identified 75 SPAWAR Systems Center purchase card transactions, for about $164,000 with a telecommunications contractor, that appear to be advance payments for electrical engineering services. Section 3324 of title 31, United States Code, prohibits an agency from paying for goods or services before the government has received them (with limited exceptions). Further, Navy purchase card procedures prohibit advance payment for goods and services, except in cases such as subscriptions and post office box rentals. SPAWAR Systems Center project managers gave us with several conflicting explanations of the nature of the arrangement with the contractor, first indicating that the charges were for time and materials and later stating that each purchase was a fixed-fee agreement. No documentation was provided to support either explanation. We were also told by SPAWAR Systems Center employees that the purchase card was used to expedite the procurement of goods and services from the contractor because the preparation, approval, and issuance of a delivery order was too time-consuming in certain circumstances.

For all 75 transactions, we found that the contractor's estimated costs were almost always equal or close to the $2,500 micropurchase threshold. Because we found no documentation of independent receipt and acceptance of the services provided or any documentation that the work for these charges was performed, these charges are also potentially fraudulent. We therefore referred the SPAWAR Systems Center purchase card activity with this contractor to our Office of Special Investigations for further investigation.

Convenience checks. We found that SPAWAR Systems Center improperly used convenience checks in fiscal year 2001, which ultimately resulted in NAVSUP canceling the use of these checks at SPAWAR Systems Center in November 2001, after we made inquires concerning the

number of SPAWAR Systems Center convenience checks issued that exceeded the $2,500-per-check limit. Convenience checks are charged directly to the government purchase card account and are used to pay vendors and other government agencies that do not accept the purchase card. According to the SPAWAR Systems Center agency program coordinator, two Citibank convenience check accounts were established in December 1998, presumably before NAVSUP changed its policy allowing only one account per unit. The SPAWAR Systems Center head of supply and contracts canceled one of these accounts on November 15, 2001, after we made inquires concerning SPAWAR Systems Center's convenience check usage.

We found that the two employees responsible for these two accounts had issued 187 checks during fiscal year 2001, 30 of which were in excess of the $2,500 limit for individual checks, for a total of over $347,000. The checks that exceeded the $2,500 limit were issued to pay for postage meter charges, various services to vendors who were sole source providers, and training. After we made inquires to the DOD Purchase Card Program Office regarding the propriety of SPAWAR Systems Center's writing convenience checks in excess of $2,500, NAVSUP canceled SPAWAR Systems Center's convenience check privileges on November 20, 2001. We also believe the use of convenience checks for over $2,500 purchases is not economical because of the 1.25 percent fee charged per transaction. For example, SPAWAR Systems Center used convenience checks to make one purchase of $10,000 for postage, which resulted in a fee of $125.

Printing. In addition, we identified several instances in which SPAWAR Systems Center did not adhere to DOD's policy to use the Defense Automated Printing Service (DAPS) to perform all printing jobs. Further, the Navy's purchase card list of prohibited or special-approval items states that cardholders are prohibited from buying printing or duplication services from entities other than DAPS. In two of the transactions that we audited, SPAWAR Systems Center paid about $3,800 to Kinko's for printing manuals.

Sales tax. We identified eight instances of sales taxes paid on SPAWAR Systems Center purchases. Payment of sales tax for the purchase of goods and services for the government is not authorized by law. According to SPAWAR Systems Center employees, these sales tax payments generally occurred when the vendors did not know how to process a nontaxable transaction.

Split Purchases

Our analysis of the population of fiscal year 2001 transactions made by one or more cardholders on the same day from the same vendor, which appeared to circumvent cardholder single transaction limits, identified about $7.5 million in SPAWAR Systems Center potential split purchases and nearly $3 million in NPWC potential split purchases. The *Federal Acquisition Regulation* and Navy purchase card policies and procedures prohibit splitting a purchase into more than one transaction to avoid the requirement to obtain competitive bids for purchases over the $2,500 micropurchase threshold or to avoid other established credit limits. Once items exceed the $2,500 micropurchase threshold, they are to be purchased in accordance with simplified acquisition procedures, which are more stringent than those for micropurchases.

Our analysis of the population of fiscal year 2001 SPAWAR Systems Center and NPWC transactions identified a substantial number of potential split purchases. To determine whether these were, in fact, split purchases, we obtained and analyzed the supporting documentation for 30 potential split purchases at SPAWAR Systems Center and 20 potential split purchases at NPWC. We found that in many instances, cardholders made multiple purchases from the same vendor within a few minutes or a few hours for items such as computers, computer-related equipment, cell phone services, and small contracts that involved the same, sequential, or nearly sequential purchase order and vendor invoice numbers. Based on our analyses, we concluded that 13 of the 30 SPAWAR Systems Center and 10 of the 20 NPWC purchases that we examined were split into two or more transactions to avoid micropurchase thresholds. Table 7 provides several examples of cardholder purchases that we believe represent split purchases intended to circumvent the $2,500 micropurchase limit or other cardholder single transaction limit.

Table 7: Examples of Potential SPAWAR Systems Center and Navy Public Works Center San Diego Split Purchases

Navy unit	Vendor	Date	Charge	Items purchased	Cost of items	Indicator of split purchase
SPAWAR	Nextel Wireless	7/17/2001	10 charges	Cell phone service	$24,482	10 separate charges of about $2,500 each to pay July monthly bill
SPAWAR	World Wide Technology	9/05/2001	1	Computer equipment	$1,938	Computer equipment resides within the cabinet
			2	Cabinet	$2,214	
SPAWAR	CompUSA	9/11/2001	1	Software	$2,240	Orders placed only minutes apart for similar products
			2	Software	$1,160	
NPWC	Construction Fence Rental	7/12/01	1	Security fence	$2,442	Rental of security fence on the same day for the same construction project
			2	Security fence	$2,310	
			3	Security fence	$75	
NPWC	Comlogic NCC Computers	9/17/2001	1	Computer	$2,495	Multiple charges on the same day for items listed on the same authorization
			2	Computer parts	$1,401	
			3	Computer software	$149	
NPWC	Union Electric Motors	7/5/2001	1	Custom control panel and components	$2,485	Purchases were on the same day and vendor invoice was sequentially numbered; vendor said transactions were part of single sale
			2	Additional component for control panel	$885	

Note. All cardholders making these transactions had $2,500 single-transaction limits.

By circumventing the competitive requirements of the simplified acquisition procedures, we believe that in many instances SPAWAR Systems Center and NPWC may not be getting the best prices possible for the government. As a result, these split purchases are likely increasing the cost of government procurements using the purchase card and, thus, at least partially offsetting its benefits.

Abusive and Questionable Transactions

We identified numerous examples of abusive and questionable transactions at SPAWAR Systems Center during fiscal year 2001. Several of the improper transactions for NPWC discussed previously are also abusive or questionable; however, we found no other abusive items related to NPWC in our statistical sample or data mining. We defined abusive transactions as those that were authorized, but the items purchased were at an excessive cost (e.g., "gold plated") or for a questionable government need, or both. Questionable transactions are those that appear to be improper or abusive but for which there is insufficient documentation to conclude either. For all abusive or questionable items, we concluded that cardholders purchased items for which there was not a reasonable and/or documented justification.

Many of the purchases we found to be abusive or questionable fall into categories described in GAO's *Guide for Evaluating and Testing Controls Over Sensitive Payments* (GAO/AFMD-8.1.2, May 1993). The guide states: "Abuse is distinct from illegal acts (noncompliance). When abuse occurs, no law or regulation is violated. Rather, abuse occurs when the conduct of a government organization, program, activity, or function falls short of societal expectations of prudent behavior." Table 8 shows the potentially abusive and questionable transactions we identified at SPAWAR Systems Center for fiscal year 2001.

Further, several of these items fall into the category of pilferable items, which, as discussed previously, SPAWAR Systems Center no longer records in its property records and therefore does not maintain accountability over them. For example, the cell phones and headset are items that could easily be converted to personal use without detection as they are not subject to bar coding and periodic inventory. In addition, items that may have limited use on one project could be made available for use on other projects, if their existence and location were recorded in centralized property records. Such visibility could serve to avoid duplicative purchases as well as provide the control needed to help prevent misuse of government property.

Table 8: Abusive and Questionable Transactions at SPAWAR Systems Center

Type of items purchased	Example vendors	Nature of transaction	Abusive/ questionable	Total amount
Room rental and refreshments	Bally's in Las Vegas	Organization meeting for about 30 staff members in Las Vegas	Questionable	$2,308
Cellular phones and services	Nextel, SprintPCS, AT&T Wireless	Abusive and uneconomical procurement, physical control, and usage of services	Abusive and questionable	$74,936
Clothing (see also table 6)	Cabela's, REI, Sport Chalet	Purchase of personal items such as socks, gloves, parkas, jackets, hats, shirts, and sweatpants	Questionable	$4,668
Luggage	The Luggage Center	Numerous wallets, passport holders, backpacks, neck pouches, and other items given away	Abusive	$775
Designer leather goods	Louis Vuitton, Franklin Covey	Purchase of designer and high-cost leather briefcases, totes, portfolios, day planners, palm pilot cases, wallets, and purses	Abusive and questionable; improper for nonmandatory source of supply	$33,054
Computer bags	SkyMall	Purchase of computer bags at an excessive cost, two given away	Abusive	$731
Headset	Bose	High-cost headset purchased, questionable need	Abusive	$299
Lego "Mindstorm" robots	Toys R Us	Four computer robot kits given away or at employee's home	Abusive	$800

Room rental and refreshments. We identified meeting room rental and refreshments at Bally's, a hotel and casino in Las Vegas, which is a questionable transaction. This charge was related to a trip for about 30 staff members from SPAWAR Headquarters. SPAWAR officials told us that the trip was an organizational meeting to work out the details of a planned merger of two program management working groups. According to SPAWAR Headquarters officials, the staff members who attended the organizational meeting spent the first morning of the 3-day trip at Nellis Air Force Base discussing issues related to an ongoing project involving a test and evaluation squadron. The cost of the transaction we reviewed was about $2,300, and we estimate the total cost of the trip was between $15,000 and $20,000. For the specific transaction we reviewed, we found that the same control weaknesses we reported earlier applied, including lack of independent receipt of goods and proper certification of the monthly bill. There was no documentation showing that this transaction had been authorized in advance or that management had fully considered the cost of this trip and potentially less costly alternatives.

GAO's *Guide for Evaluating and Testing Controls Over Sensitive Payments* notes the importance of the control environment and the need for effective controls related to sensitive

payments. A trip for about 30 employees to a Las Vegas hotel and casino for 3 days at a significant cost to the government is clearly sensitive and should be subjected to a high level of scrutiny, with clear documentation and approval in advance of the event. We would expect to see authorization in advance of the procurement by someone at a higher level than the most senior individual involved in the event—in this case, a captain. We found no documented justification to indicate a valid need for this 3-day meeting to be held in Las Vegas nor did we find an evaluation of the cost-benefit of having the meeting in Las Vegas versus alternative sites. Thus, we question whether the entire cost of the trip was a prudent expenditure of government funds. We did not review the travel vouchers and related documentation for the other component costs of the trip such as airfare, rental cars, or hotel bills; however, in estimating the total cost of the trip, we reviewed available documentation related to travel card usage from Bank of America.

Cell phone usage. We found significant breakdowns in controls at SPAWAR Systems Center over the use of cell phones and related services, resulting in abusive and wasteful expenditures of government resources. In addition, we found a proliferation of cell phone agreements, with the purchase card being used to purchase equipment and services from more than 40 different cell phone companies at a total cost of $341,000 for fiscal year 2001. According to SPAWAR Systems Center management, they have a master cell phone contract with AT&T Wireless. However, lack of management oversight and a large number of available purchase cards has resulted in individuals with purchase cards or their supervisors deciding who needs a cell phone, which cell phone company to use, and what type of calling plan to purchase. For all but one of the transactions that we audited, we did not find any evidence that the monthly cell phone bills had been independently reviewed to ensure the transactions were reasonable and for valid government purposes.

In the large case we audited, we identified a $24,000 monthly bill for about 200 Nextel cell phones and related services that were acquired to provide a voice communication system for coordination and control among various groups during a demonstration and test of a military wide area relay network. The Nextel phones were selected for evaluation as an alternative not for their standard cellular phone-to-phone capability, but for their "group-talk" feature, which provides a wireless "walkie-talkie" like capability for preprogrammed work groups. One of the key control failures with this cell phone procurement was related to SPAWAR Systems Center's handing out cell phones to project team members and government contractors without keeping an inventory of who had each cell phone. Contractors that used these government cell phones told us that SPAWAR Systems Center officials brought a box of 60 or 70 cell phones to a meeting and handed them out to contractors that were part of the team. The contractors told us that SPAWAR Systems Center provided them with no instructions on proper use of the cell phone. The approximately 200 cell phones were not physically controlled and SPAWAR Systems Center did not have a list of who had the cell phones. Based on further investigation, we found that these contractors were using the cell phones to call friends and family and to conduct other personal business. Based on our review of the bills for this Nextel account—which totaled about $74,000 during fiscal year 2001—we estimated that about $9,200 was spent on long distance and other local telephone calls, which was not the primary intended purpose of these cell phones.

In addition to the Nextel contract, we also identified cell phone contracts with large monthly fees for phones that were either used infrequently or not at all. For example, we audited one account with five cell phones. The service for each phone included 500 minutes of airtime, and the basic service cost of each cell phone was $50 a month. For the 3 months of activity we audited, we found that three of the five phones had either no voice activity or very little. For example, one of these cell phones had only 2 minutes of calls during a month that we audited. This is the equivalent of the government paying $25 per minute for airtime.

We identified a number of other abusive and questionable charges including the following.

- One cardholder purchased $775 of luggage including wallets, passport holders, backpacks, neck pouches, and other items. The cardholder told us that these items were used to carry or ship equipment to universities for outreach activities. At the end of the events, the individual told us that the items were given away. There is no documentation available showing the authorization and need to purchase this luggage for purposes of carrying or shipping equipment. This purchase appears abusive because a valid government need is neither apparent nor documented, particularly since the cardholder gave away government property that could easily be converted to personal use.
- As part of our data mining, we identified purchases of day planners from commercial vendors, including calendar refills along with designer leather holders purchased from Louis Vuitton. By law, government agencies are directed to purchase certain products, including day planners and calendars, from certified nonprofit agencies that employ people who are blind or severely disabled. This program is referred to as the Javits-Wagner-O'Day (JWOD) program, which is intended to provide employment opportunities for thousands of people with disabilities to earn good wages and move toward greater independence. In addition, DOD's policy requires the use of JWOD sources, whether or not the procurement is made using a purchase card, unless the central JWOD agency specifically authorizes an exception. In this year's audit, we found that SPAWAR Systems Center employees had purchased three Louis Vuitton calendar refills for $27 each, and we identified three purchases of Louis Vuitton calendar holders at a cost of $255 each in fiscal year 2000. The most expensive JWOD calendar holders—specifically designed for DOD—cost about $40.
- In addition, we identified about $33,000 in purchases from Franklin Covey of designer and high-cost leather briefcases, purses (totes), portfolios, day planners and refills, palm pilot cases, and wallets. For example, we found leather purses costing up to $195 each and portfolios costing up to $135 each. Many of these purchases are of a questionable government need and should be paid for by the individual. To the extent the day planners and calendar refills were proper government purchases, they were at an excessive cost and, as with the Louis Vuitton day planners, should have been purchased from a JWOD source at a substantially lower cost. Circumventing the JWOD requirements and purchasing these items from commercial vendors is not only an abuse and waste of taxpayer dollars, but shows particularly poor judgment and serious internal control weaknesses.
- We identified the purchase of three computer bags from SkyMall at a cost of $161 each, and another purchase of a computer bag at a store in Italy for almost $250. All three computer bags were purchased by employees who were traveling on SPAWAR Systems Center business. The cost of these computer bag purchases is excessive compared to other standard bags we found purchased for $25. In addition, the cardholder who purchased the SkyMall

bags told us that one of the two bags, along with another bag purchased in a separate transaction, was given to non–SPAWAR Systems Center government employees working on the project.

- We identified the purchase of a Bose headset at a cost of $299. The cardholder told us that the headset was originally purchased for a project but had never been used on the project. The cardholder stated that he has used the headset to listen to music on official government travel aboard airplanes.
- We identified four Lego "Mindstorm" computer robot kits that were purchased at Toys R Us at a total cost of $800. The SPAWAR Systems Center employee who requested that these robots be purchased initially told us that they were purchased as a learning tool for new professionals and junior engineers to learn cooperative behavior between robots and to conduct robotic research. However, during our interview, this SPAWAR Systems Center employee stated that at the time of these purchases his division did not have any new professionals scheduled to rotate through his assignment. Within 6 weeks of purchasing the kits, the employee removed all four from SPAWAR Systems Center, brought two of them to a local elementary school where he mentors an after school science club, and brought two to his home. We believe this purchase is abusive because there does not appear to be a valid government need for the purchase, and because the cardholder effectively gave away government property that could easily be converted to personal use. As part of the NAVSUP mandated stand-down transaction review, SPAWAR Systems Center also reviewed the transactions for the Lego robot kits and initially questioned their propriety. However, contrary to our conclusion that these purchases were abusive, SPAWAR Systems Center ultimately considered the Lego kits to be a valid government purchase.

Disciplinary Action Seldom Taken Against Cardholders Who Made Abusive Purchases

In our November 30, 2001, report[19] on the purchase card controls at SPAWAR Systems Center and NPWC, we recommended that action be taken to help ensure that cardholders adhere to applicable purchase card laws, regulations, internal control and accounting standards, and policies and procedures. Specifically, we recommended that the commander, Naval Supply Systems Command, revise NAVSUP Instruction 4200.94 to include specific consequences for noncompliance with purchase card policies and procedures. DOD did not concur with that recommendation and stated that existing Navy policy clearly identifies consequences for fraud, abuse, and misuse. We continue to believe that Navy needs to establish specific consequences for these purchase card problems because the Navy policy does not identify any specific consequences for failure to follow control requirements. Enforcement of the consequences is also critical. For example, only one of the cardholders referred to in this testimony or our July 30, 2001, testimony had formal disciplinary or administrative action—in the form of removal of the purchase card—taken against them.

Thus, we reiterate our previous recommendation that the Navy enforce purchase card controls by establishing specific formal disciplinary and/or administrative consequences—such as withdrawal of cardholder status, reprimand, suspension from employment for several days, and, if necessary, firing. Unless cardholders and approving officials are held accountable for

[19]GAO-02-32.

following key internals controls, the Navy is likely to continue to experience the types of fraudulent, improper, and abusive and questionable transactions identified in our work.

Conclusions

The weaknesses identified in the purchase card program at these two Navy units are emblematic of broader financial management and business process reform issues across DOD. The comptroller general testified on March 6, 2002, before the Subcommittee on Readiness and Management Support, Senate Committee on Armed Services, on the major challenges facing the department in its business process transformation efforts.[20] In light of the events of September 11, and the federal government's short- and long-term budget challenges, it is more important than ever that DOD get the most from every dollar spent. As Secretary Rumsfeld has noted, billions of dollars of resources could be freed up for national defense priorities by eliminating waste and inefficiencies in existing DOD business processes. The cultural issues we identified at SPAWAR Systems Center— such as the failure to acknowledge significant control weaknesses in the purchase card program, the parochial approach to program management without regard to broader Navy and DOD initiatives, and the lack of consequences on a personal or organizational level for failure to adhere to controls—are a major impediment to the improvements that are needed to stop wasteful and abusive purchases and ensure that taxpayer dollars are spent where national priorities dictate. In response to requests from this Subcommittee and Senator Grassley, we have ongoing audits related to the purchase and travel card programs at the Army, Navy, and Air Force and plan to offer additional recommendations to strengthen the controls over these programs.

Contacts and Acknowledgments

For future contacts regarding this testimony, please contact Gregory D. Kutz at (202) 512-9095 or *kutzg@gao.gov* or John J. Ryan at (202) 512-9587 or *ryanj@gao.gov*. Individuals who made key contributions to this testimony include Beatrice Alff, Cindy Brown-Barnes, Bertram Berlin, Sharon Byrd, Lee Carroll, Douglas Delacruz, Francine DelVecchio, Stephen Donahue, Douglas Ferry, Kenneth Hill, Jeffrey Jacobson, Kristi Karls, John Kelly, Yola Lewis, Stephen Lipscomb, Scott McNulty, Sidney Schwartz, and Jenniffer Wilson.

[20]U.S. General Accounting Office, *DOD Financial Management: Integrated Approach, Accountability, Transparency, and Incentives Are Keys to Effective Reform*, GAO-02-497T (Washington, D.C.: Mar. 6, 2002).

Appendix I

Background

The Navy's purchase card program is part of the Governmentwide Commercial Purchase Card Program, which was established to streamline federal agency acquisition processes by providing a low-cost, efficient vehicle for obtaining goods and services directly from vendors. According to GSA, DOD reported that it used purchase cards for more than 10.7 million transactions, valued at $6.1 billion, during fiscal year 2001. The Navy's reported purchase card activity—MasterCards issued to civilian and military personnel—totaled about 2.8 million transactions, valued at $1.8 billion, during fiscal year 2001. This represented nearly 30 percent of DOD's activity for fiscal year 2001. According to unaudited DOD data, SPAWAR Systems Center and NPWC made about $64 million in purchase card acquisitions during fiscal year 2001. Because these two units have cardholders located outside the San Diego area, we limited our testing to only those SPAWAR Systems Center and NPWC cardholders who are located in San Diego, California. Those cardholders accounted for about $50 million of SPAWAR Systems Center and NPWC's $64 million in purchase card transactions.

SPAWAR Systems Center and NPWC are both working capital fund activities. SPAWAR Systems Center performs research, engineering, and technical support, and NPWC provides maintenance, construction, and operations support to Navy programs. Both of these Navy programs have locations throughout the United States. Our review focused on the purchase card program at the San Diego units only. For SPAWAR Systems Center, this included SPAWAR Headquarters, which is located in San Diego, and SPAWAR Systems Center San Diego.

Governmentwide Purchase Card Program Guidelines

Under the Federal Acquisition Streamlining Act of 1994, the *Defense Federal Acquisition Regulation Supplement* guidelines, eligible purchases include (1) micropurchases (transactions up to $2,500, for which competitive bids are not needed); (2) purchases for training services up to $25,000; and (3) payment for items costing over $2,500 that are on the General Services Administration's (GSA) preapproved schedule, including items on requirements contracts. The streamlined acquisition threshold for such contract payments is $100,000 per transaction. Accordingly, cardholders may have single-transaction purchase limits of $2,500 or $25,000, and a few cardholders may have transaction limits of up to $100,000 or more. Under the GSA blanket contract, the Navy has contracted with Citibank for its purchase card services, while the Army and the Air Force have contracted with U.S. Bank.

The *Federal Acquisition Regulation*, Part 13, "Simplified Acquisition Procedures," establishes criteria for using purchase cards to place orders and make payments. U.S. Treasury regulations issued pursuant to provisions of law in 31 U.S.C. 3321, 3322, 3325, 3327, and 3335, govern purchase card payment certification, processing, and disbursement. DOD's Purchase Card Joint Program Management Office, which is in the office of the assistant secretary of the army for acquisition, logistics, and technology, has established departmentwide policies and procedures governing the use of purchase cards.

Navy Purchase Card Acquisition And Payment Processes

The NAVSUP is responsible for the overall management of the Navy's purchase card program, and has published the NAVSUP Instruction 4200.94, *Department of the Navy Policies and Procedures for Implementing the Governmentwide Purchase Card Program.* Under the NAVSUP Instruction, each Navy Command's head contracting officer authorizes purchase card program coordinators in local Navy units to obtain purchase cards and establish credit limits. The program coordinators are responsible for administering the purchase card program within their designated span of control and serve as the communication link between Navy units and the purchase card issuing bank. The other key personnel in the purchase card program are the approving officials and the cardholders.

Approving Officials

If operating effectively, the approving official is responsible for ensuring that all purchases made by the cardholders within his or her cognizance were appropriate and that the charges are accurate. The approving official is supposed to resolve all questionable purchases with the cardholder before certifying the bill for payment. In the event an unauthorized purchase is detected, the approving official is supposed to notify the agency program coordinator and other appropriate personnel within the command in accordance with the command procedures. After reviewing the monthly statement, the approving official is to certify the monthly invoice and send it to the Defense Finance and Accounting Service for payment.

Cardholders

A purchase card holder is a Navy employee who has been issued a purchase card. The purchase card bears the cardholder's name and the account number that has been assigned to the individual. The cardholder is expected to safeguard the purchase card as if it were cash.

Designation of Cardholders

When a supervisor requests that a staff member receive a purchase card, the agency program coordinator is to first provide training on purchase card policies and procedures and then establish a credit limit and issue a purchase card to the staff member.

Ordering Goods and Services

Purchase card holders are delegated limited contracting officer ordering responsibilities, but they do not negotiate or manage contracts. SPAWAR Systems Center and NPWC cardholders use purchase cards to order goods and services for their units as well as their customers. Cardholders may pick up items ordered directly from the vendor or request that items be shipped directly to end users (requesters). Upon receipt of items acquired by purchase cards, cardholders are to record the transaction in their purchase log and obtain documented independent confirmation from the end user, their supervisor, or another individual that the items have been received and

accepted by the government. They are also to notify the property book officer of accountable items received so that these items can be recorded in the accountable property records.

Payment Processing

The purchase card payment process begins with receipt of the monthly purchase card billing statements. Section 933 of the National Defense Authorization Act for Fiscal Year 2000, Public Law 106-65, requires DOD to issue regulations that ensure that purchase card holders and each official with authority to authorize expenditures charged to the purchase card reconcile charges with receipts and other supporting documentation before paying the monthly purchase card statement. NAVSUP Instruction 4200.94 states that upon receipt of the individual cardholder statement, the cardholder has 5 days to reconcile the transactions appearing on the statement by verifying their accuracy to the transactions appearing on the statement and notify the approving official in writing of any discrepancies in the statement.

In addition, under the NAVSUP Instruction, before the credit card bill is paid the approving official is responsible for (1) ensuring that all purchases made by the cardholders within his or her cognizance are appropriate and that the charges are accurate and (2) the timely certification of the monthly summary statement for payment by the Defense Finance and Accounting Service (DFAS). The Instruction further states that within 5 days of receipt, the approving official must review and certify for payment the monthly billing statement, which is a summary invoice of all transactions of the cardholders under the approving official's purview. The approving official is to presume that all transactions on the monthly statements are proper unless notified in writing by the purchase card holder. However, the presumption does not relieve the approving official from reviewing for blatantly improper purchase card transactions and taking the appropriate action prior to certifying the invoice for payment. In addition, the approving official is to forward disputed charge forms to the unit's comptroller's office for submission to Citibank for credit. Under the Navy's contract, Citibank allows the Navy up to 60 days after the statement date to dispute invalid transactions and request a credit.

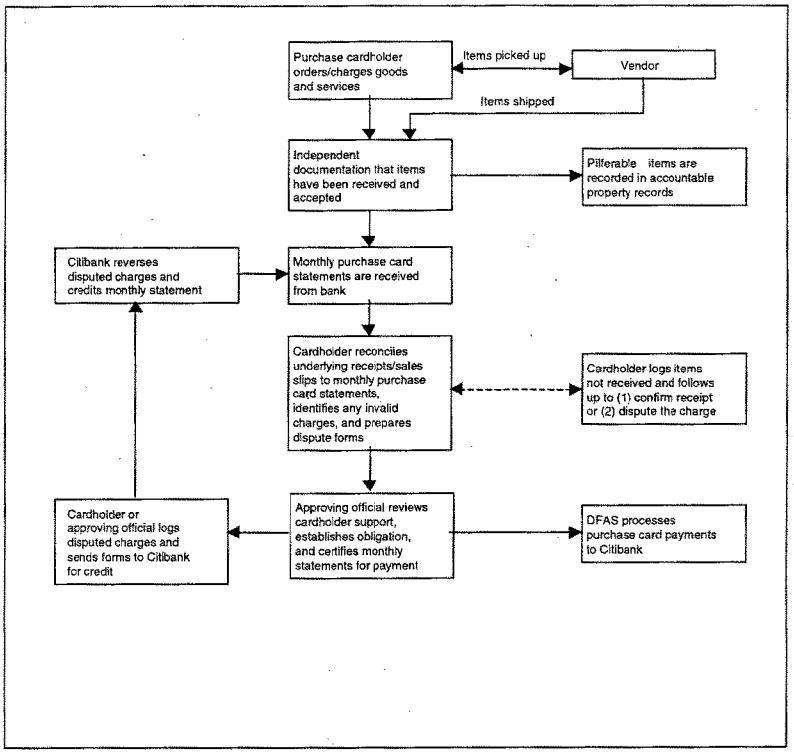
In our November 30, 2001, report[21] we recommended that the Navy modify its payment certification policy to require (1) cardholders to notify approving officials prior to payment that purchase card statements have been reconciled to supporting documentation, (2) approving officials to certify monthly statements only after reviewing them for potentially fraudulent improper and abusive transactions, and (3) approving officials to verify, on a sample basis, supporting documentation for various cardholder transactions prior to certifying monthly statements for payment. DOD concurred with this recommendation and stated the Navy would modify its payment certification procedures; however, as of February 26, 2002, Navy had not yet issued those changes to its procedures.

Upon receipt of the certified monthly purchase card summary statement, a DFAS vendor payment clerk is to (1) review the statement and supporting documents to confirm that the prompt-payment certification form has been properly completed and (2) subject it to automated and manual validations. DFAS effectively serves as a payment processing service and relies on the approving-official certification of the monthly payment as support to make the payment. The

[21]GAO-02-32.

DFAS vendor payment system then batches all of the certified purchase card payments for that day and generates a tape for a single payment to Citibank by electronic funds transfer. Figure 1 illustrates the current design of the purchase card payment process for SPAWAR Systems Center and NPWC.

Figure 1. SPAWAR and Navy Public Works Center Purchase Card Process



Appendix II

Scope and Methodology

We reviewed purchase card controls for two Navy units based in San Diego, SPAWAR Systems Center and NPWC, and assessed changes that these two units made to their control environment since we notified the units of the problems with their respective purchase card programs in early June 2001. In addition we followed up on the status of fraud cases that we reported on in July 2001, and any other fraud cases we identified as part of this follow-up audit. Specifically, our assessment of SPAWAR Systems Center and the NPWC purchase card controls covered

- the overall management control environment, including (1) span of control issues related to the number of cardholders, (2) training for cardholders and accountable officers,[22] (3) monitoring and audit of purchase card activity, and (4) management's attitude in establishing the needed controls, or "tone at the top;"
- tests of statistical samples of key controls over fourth quarter fiscal year 2001 purchase card transactions, including (1) documentation of independent confirmation that items or services paid for with the purchase card were received and (2) proper certification of the monthly purchase card statement for payment;
- to the extent feasible, substantive tests of accountable items in our sample transactions to verify whether they were recorded in property records and whether they could be found;
- data mining of the universe of fiscal year 2001 transactions to identify any potentially fraudulent, improper, and abusive or questionable transactions;[23]
- analysis and audit work related to invoices and other information obtained from three vendors—Cabela's, REI, and Franklin Covey—from which, based on interviews with cardholders and our review of other transactions, we had reason to believe that SPAWAR Systems Center had made significant improper and abusive or questionable purchases during fiscal year 2001; and
- analysis of the universe of fourth-quarter fiscal year 2001 purchase card transactions to identify purchases that were split into one or more transactions to avoid micropurchase thresholds or other spending limits.

In addition, our Office of Special Investigations worked with DOD's criminal investigative agencies, Citibank, and credit card industry representatives to identify known and potentially fraudulent purchase card scams. Our Office of Special Investigations also investigated potentially fraudulent or abusive purchase card transactions that we identified while analyzing SPAWAR Systems Center and NPWC fiscal year 2001 purchase card transactions.

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[22]We also tested statistical samples of transactions to determine whether the two units had documented evidence that cardholders had received required purchase card training.

[23]We considered potentially **fraudulent** purchases to include those made by cardholders that were unauthorized and intended for personal use. The transactions we determined to be **improper** are those purchases intended for government use, but are not for a purpose that is permitted by law, regulation, or DOD policy. We also identified as improper numerous purchases made on the same day from the same vendor that appeared to circumvent cardholder single transaction limits. Many of the purchases we found to be **abusive or questionable** fall into categories described in GAO's *Guide for Evaluating and Testing Controls Over Sensitive Payments* (GAO/AFMD-8.1.2, May 1993). The guide states that "Abuse is distinct from illegal acts (noncompliance). When abuse occurs, no law or regulation is violated. Rather, abuse occurs when the conduct of a government organization, program, activity, or function falls short of societal expectations of prudent behavior."

We used as our primary criteria applicable laws and regulations; our *Standards for Internal Control in the Federal Government;*[24] and our *Guide for Evaluating and Testing Controls Over Sensitive Payments.*[25] To assess the management control environment, we applied the fundamental concepts and standards in the GAO internal control standards to the practices followed by management in the four areas reviewed.

Statistical Sample of Internal Control Procedures

To test controls, we used a two-step sampling process for purchase card transactions that were recorded by Navy during the fourth quarter of fiscal year 2001. At SPAWAR Systems Center, we selected stratified random probability samples of 50 purchase card transactions from a population of 7,267 transactions totaling $5,919,635. Because the majority of SPAWAR Systems Center transactions failed the control test we did not have to expand our sampling size. At NPWC, we initially selected a sample of 50 purchase card transactions from a population of 11,021 transactions totaling $6,030,501. In light of NPWC's improvements in the area of documenting independent receipt and acceptance, we increased our sample size of NPWC transactions to 94 to generate a more accurate assessment of the control failure rate at NPWC.

We stratified the each of the samples into two groups—transactions from vendors likely to represent purchases of computer equipment and other vendors. With this statistically valid probability sample, each transaction in the population had a nonzero probability of being included, and that probability could be computed for any transaction. Each sample element was subsequently weighted in the analysis to account statistically for all the transactions in the population, including those that were not selected. Table 10 presents our test results on three key transaction-level controls and shows the confidence intervals for the estimates for the universes of fiscal year 2000 purchase card transactions made by SPAWAR Systems Center and NPWC.

[24] *Standards for Internal Control in the Federal Government* (GAO/AIMD-00-21.3.1) was prepared to fulfill our statutory requirement under the Federal Managers' Financial Integrity Act to issue standards that provide the overall framework for establishing and maintaining internal control and for identifying and addressing major performance and management challenges and areas at greatest risk of fraud, waste, abuse, and mismanagement.

[25] *Guide for Evaluating and Testing Controls Over Sensitive Payments* (GAO/AFMD-8.1.2) provides a framework for evaluating and testing the effectiveness of internal controls that have been established in various sensitive payment areas.

Table 9: Estimate of Fiscal Year 2001 Transactions That Failed Control Tests[a]

Navy units in San Diego	Breakdowns in key purchase card controls	
	Independent, documented receipt of items purchased	**Proper certification of purchase card statements for payment**
	Percent failure	Percent failure
SPAWAR Systems Center	56% (39-72%)	100%[b]
Navy Public Works Center	16% (9-27%)	100%[c] (93-100%)

[a]The projections represent point estimates for the population based on our sampling tests at a 95-percent confidence level.
[b]For the last quarter of fiscal year 2001, SPAWAR Systems Center continued to have only one certifying officer for almost 1,000 cardholders. This unacceptable span of control led us to conclude that all transactions selected as part of our statistical sample were not properly reviewed and approved by a certifying officer.
[c]Our statistical testing identified one transaction that was reconciled by the cardholder and approving official prior to payment. The projected error rate was 99.9 percent, which we rounded to 100 percent.

Data Mining

In addition to selecting statistical samples of SPAWAR Systems Center and NPWC transactions to test specific internal controls, we also made nonrepresentative selections of SPAWAR Systems Center and NPWC transactions based on data mining of fiscal year 2001 transactions. The purpose of the data mining procedures was twofold. Specifically, we conducted separate analysis of acquisitions that were (1) potentially fraudulent, improper, and abusive or otherwise questionable and (2) split into multiple transactions to circumvent either the micropurchase or cardholder transaction thresholds.

Our data mining for potentially fraudulent, improper, and abusive or questionable transactions was limited to cardholders who worked in San Diego and covered 36,216 fiscal year 2001 transactions totaling about $26.1 million at SPAWAR Systems Center, and 46,709 fiscal year transactions totaling about $23.9 million at the NPWC. For this review, we scanned the two units' San Diego-based activities for transactions with vendors that are likely to sell goods or services (1) on NAVSUP's list of prohibited items, (2) that are personal items, and (3) that are otherwise questionable. Our expectation was that transactions with certain vendors had a more likely chance of being fraudulent, improper, abusive, or questionable. Because of the large number of transactions that met these criteria we did not look at all potential abuses of the purchase card. Rather, we made nonrepresentative selections of transactions based on transactions with the vendors who fit these criteria. For example, we reviewed, and in some cases made inquires, concerning 162 transactions and other related transactions on the same monthly purchase card statement with vendors that sold such items as sporting goods, groceries, luggage, flowers, and clothing. While we identified some improper and potentially fraudulent and abusive transactions, our work was not designed to identify, and we cannot determine, the extent of fraudulent, improper, and abusive or questionable transactions.

Our data mining also included nonrepresentative selections of acquisitions that SPAWAR Systems Center and NPWC entered into during the period June 22, 2001, through September 21, 2001, that were potentially split into multiple transactions to circumvent either the micropurchase competition requirements or cardholder single transaction thresholds. We limited our data mining to this period because senior SPAWAR Systems Center and NPWC officials acknowledged to us in early June 2001 that cardholders had made split transactions and that they would attempt to correct the problem. Therefore, to allow the two units an opportunity to resolve this issue, we limited our review to transactions that occurred subsequent to SPAWAR Systems Center and NPWC's acknowledging a problem with splitting purchases.

We briefed DOD managers, including officials in DOD's Purchase Card Joint Program Management Office, and Navy managers, including NAVSUP, SPAWAR Systems Center, and NPWC officials, on the details of our review, including our objectives, scope, and methodology and our findings and conclusions. Where appropriate, we incorporated their comments into this testimony. We conducted our audit work from November 2001 through February 2002 in accordance with U.S. generally accepted government auditing standards, and we performed our investigative work in accordance with standards prescribed by the President's Council on Integrity and Efficiency.

(192046)

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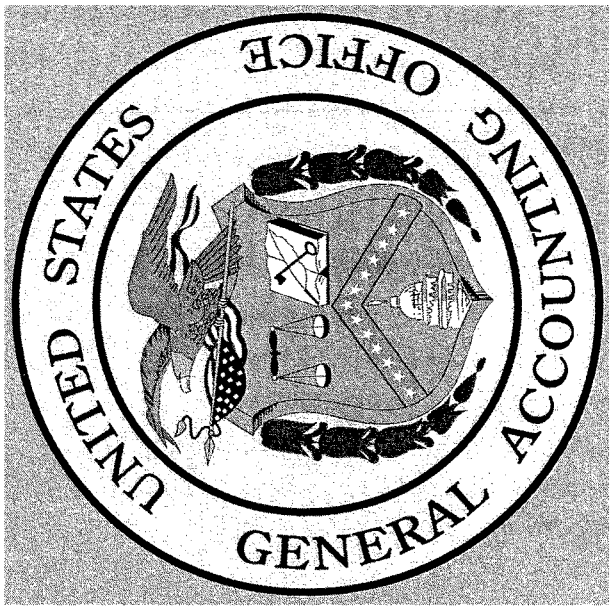
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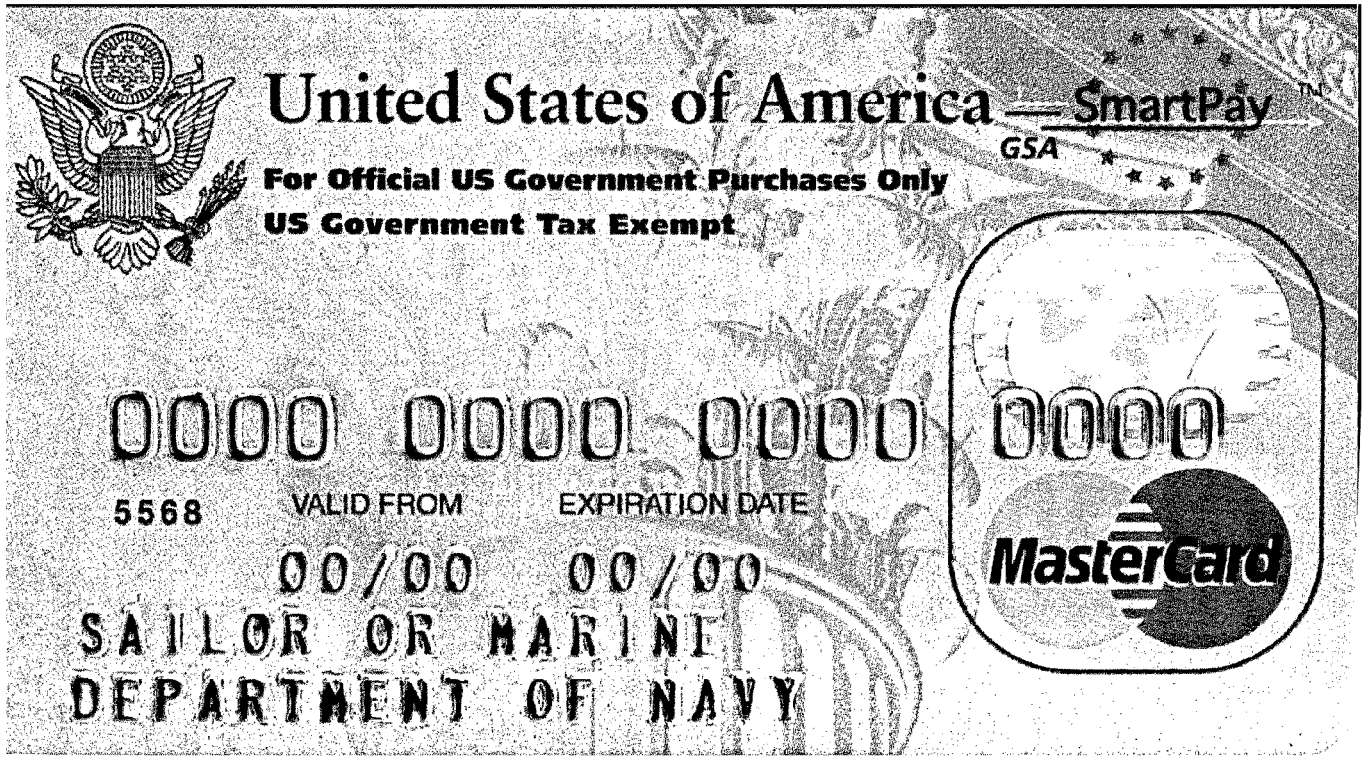
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SAILOR OR MARINE
DEPARTMENT OF NAVY
MasterCard

GAO Accountability * Integrity * Reliability

Selected Purchase Card Statement Items

Monthly Detail		
SalesDate	**Vendor**	**Amount**
12-20	Macy's West	1,500.00
12-20	RobinsonMay Gift Cards	1,500.00
12-20	Nordstrom	1,500.00
12-20	Circuit City	2,392.00
12-22	RobinsonMay Gift Cards	500.00
12-22	Lees Men's Wear	167.01
12-22	Foot Locker	53.85
12-23	RobinsonMay Gift Cards	1,500.00

Louis Vuitton Day Planner--$250

Franklin Covey Tote (Purse) $195

REI Jacket $140

Senator GRASSLEY. It is now my privilege to invite Captain James M. Barrett, Commanding Officer, Navy Public Works Center, San Diego, to testify. Welcome.

Captain BARRETT. Thank you, Senator. Good morning.

As you mentioned, I am Captain Jim Barrett, Commanding Officer of the Navy Public Works Center in San Diego. I assumed command of the Center on August 24, 2001. I have submitted my written testimony statement for the record.

In testimony before this subcommittee on July 30, 2001, my predecessor stated, "I fully recognize that controls are a key element." He was committed to ensuring those controls were put in place. I am here to assure you that I have continued to address that commitment since taking command of the Public Works Center, San Diego.

Prior to, during, and as a result of GAO's initial audit, PWC, San Diego, has worked tirelessly to improve the internal control environment of our purchase card program. As Mr. Kutz has mentioned, we have significantly reduced the number of cardholders; we have significantly reduced the credit limits of our purchase cardholders; we have greatly increased the number of approving officials that allows a more effective oversight for those cardholders.

We have published supplemental guidelines and issued a revised command instruction on purchase card procedures. We have held numerous training sessions to address the issues raised by GAO during their initial audit. We have also held training sessions to address Navy policy changes resulting from GAO's audit.

Mr. Chairman, I believe we have improved dramatically, and we are continuing our work to get better. That concludes my summary statement, subject to any questions you or the other committee members may have. Thank you, Mr. Chairman, for the opportunity to appear today.

[The prepared statement of Captain Barrett follows:]

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RELEASED BY THE

HOUSE GOVERNMENT REFORM COMMITTEE

STATEMENT OF

CAPT JAMES M. BARRETT III, CIVIL ENGINEER CORPS, UNITED STATES NAVY

COMMANDING OFFICER, NAVY PUBLIC WORKS CENTER,

SAN DIEGO BEFORE THE HOUSE GOVERNMENT REFORM COMMITTEE

SUBCOMMITTEE ON GOVERNMENT EFFICIENCY

FINANCIAL MANAGEMENT AND INTERGOVERNMENTAL RELATIONS

HEARING ON

FOLLOW-UP AUDIT OF GOVERNMENT PURCHASE CARD

MARCH 13, 2002

NOT FOR PUBLICATION UNTIL

RELEASED BY THE

HOUSE GOVERNMENT REFORM COMMITTEE

INTRODUCTION

Good morning, Mr. Chairman. I'm Captain James Barrett, Commanding Officer of the Navy Public Works Center in San Diego (PWCSD). I assumed Command of the Center on 24 August 2001. PWCSD provides the full range of public works services to Navy and Marine Corps activities in the San Diego area. PWCSD is a Navy Working Capital Fund (NWCF) activity, which means we charge for our services rather than receive an annual appropriation. We operate our businesses with the same cost, price, quality, customer service and competitiveness issues that challenge and motivate all commercial businesses. PWCSD employs a work force of 14 military and 1,700 civilian and contractor personnel. Our annual business volume exceeds $300 million per year. Services are provided for over 3,000 buildings on 7 major industrial bases and military family housing units located at various off-base sites. These commands and activities, including fleet support for the many ships berthed at the waterfront in San Diego Bay, consist of over 400 clients located in a 200 square mile area. In addition to the typical services associated with public works (maintenance, utilities, and transportation), PWCSD owns and operates a dry dock at the 32nd Street Naval Station, and also provides specialty services including a high-tech machine shop, environmental lab services, and wireless communications. My team provides these services through over 35 Product/Service Lines organized into five Business Lines: Facilities Engineering, Maintenance, Utilities, Transportation, and Environmental. PWCSD is under the control and direction of Commander, Navy Region Southwest (CNRSW). PWCSD also receives guidance and policy on technical and financial issues from Commander, Naval Facilities Engineering Command (NAVFACENGCOM). We receive purchase card authority from the Commander, Naval Supply Systems Command (NAVSUP) through the Fleet and Industrial Supply Center, San Diego.

In testimony before this subcommittee on 30 July 2001, my predecessor, CAPT Jack Surash, stated: "I fully recognize that proper controls are a key element – controls that balance risk and degree of oversight – and I am committed to ensuring these controls are in place." I am here to assure you that I have continued to address that commitment since taking command of the PWCSD.

Control Environment.

During and as a result of GAO's initial audit, PWCSD has worked tirelessly to improve the internal control environment of our purchase card program. We have reduced the number of cardholders from 292 in September 2000 to 173 as of March 2002. We also increased the number of Approving Officials (AO's) from 6 in July 2001 to 47 as of March 2002. The AO ratio is now in line with DOD's criteria of no more than 7 cardholders per official and at PWCSD the ratio is generally 4 to 1.

Again, with the intent of strengthening the internal control environment, we reduced the credit limits of our purchase cardholders from approximately $14M in September 2000 to approximately $5.5M as of March 2002, which is significant. We developed a process for assessing proper credit limits for each cardholder and will continue to assess the credit limits on a recurring basis.

PWCSD has always viewed cardholder and AO training as a critical control element. Based on GAO status updates during the initial audit, we held cardholder stand down training for all cardholders, their supervisors, and AO's in June and July 2001 to address the GAO issues. In September 2001, we required all cardholders, supervisors and AO's to attend mandatory NAVSUP training. Cards were suspended for 15 cardholders who didn't attend the training.

Additionally, when PWCSD increased the number of AO's, we required the new AO's to attend purchase card training, which was held in December 2001 and January 2002. Documentation of all training is maintained by the APC for audit purposes.

Monitoring and Oversight.

The Naval Audit Service published their Purchase Card Program audit report of PWCSD on 10 January 2002. Based upon the periodic briefings by NAVAUDSVC while the review was ongoing, PWCSD promptly took action to correct many of the deficiencies. As a result, the published report showed that PWCSD had completed action on 16 of the18 recommendations. We just completed a "Tiger Team" review of our entire procurement process. One of the benefits of this review will result in the establishment of new contracts as well as utilizing existing contracts to get a bigger 'bang for the buck' in obtaining maintenance and repair services and materials. This will also reduce the number of purchase card transactions.

When NAVSUP directed all Navy units to review 12 months of purchase card transactions, we identified a problem with purchase of hazardous materials. To correct this problem PWCSD will utilize our two prime vendors (Napa and Graybar) for some of the hazardous material purchases. These prime vendors maintain inventories of maintenance and automotive materials (hazardous and non-hazardous) throughout the San Diego region. The PWCSD Executive Steering Committee has recently approved the process of having all PWCSD purchases of non-commonly used hazardous material forwarded to the PWCSD APC. The APC will make a determination whether to send the requirement to FISCSD for procurement or obtain the requirement from one of the PWCSD Prime Vendors. The policy and practice for PWCSD is to only procure quantities of hazardous material that will be completely used on the existing

requirement, to the maximum extent possible. For quantities of hazardous material that is not completely used, PWCSD has hazardous waste sites at all bases where the hazardous waste materials are maintained and disposed of through the PWCSD Environmental Department.

Independent Receipt of Items Purchased

GAO initially pointed out that we had a problem with receipt and acceptance. We implemented process changes and within a very short time period, we were able to improve from a 47% failure rate to a 15.5% failure rate. Although this is better, we believe we can do more. We will continue to train our people and monitor their performance in this key control area.

Certification of Monthly Purchase Card Statements.

We have emphasized to our cardholders that they are to review their accounts on-line with Citibank throughout the month. We have directed that our AO's, prior to certifying their summary invoice for payment, require written notification from each cardholder that their statements do not include disputed items. Our new AO structure now provides a reasonable span of control that will allow proper certification.

Potentially Fraudulent Transactions

GAO provided three case studies related to potential fraud. Two of those cases relate to purchase cardholders at PWCSD. The other case involves the compromise of 2600 purchase card accounts in the western United States.

Regarding the two cases involving PWCSD employees, I am very pleased with the investigative work performed by the PWCSD staff and their efforts to obtain restitution for the

Government. After the PWCSD staff determined early on during both investigations that there was potential fraud, they immediately referred both cases to The Naval Criminal Investigative Service (NCIS). Because NCIS was backlogged, the PWCSD staff sought and obtained permission from NCIS to gather part of the evidence necessary to seek an indictment from the Assistant U.S. Attorney (AUSA) if the AUSA decided to prosecute the cases. The evidence gathered by my staff was provided to NCIS. The AUSA declined prosecution of both cases.

TM - $12,000 Case

While the case was in the hands of NCIS, the subject transferred to the Department of the Army in Washington D.C. NCIS then returned the case to PWCSD because subject was no longer under their jurisdiction. At this time the Command Evaluation Officer and Legal Counsel again spent many hours aggressively pursuing restitution to the Government. Their efforts included writing letters to Citibank officials, obtaining affidavits from the subject, and providing information to Citibank's investigative personnel. The end result was Citibank provided credits to PWCSD in the amount of about $12,000.

I believe we have improved upon the internal control procedures that may have contributed to this abuse back in 1999 and early 2000. Some examples of how we have strengthened our internal controls since then include:

. We added a cardholder and supervisor certification to the monthly Citibank statement that requires them to certify that these purchases were not for personal use.

. We added an additional 'separation of function' element by having the AO vice the credit cardholder, fax the copy of the cardholder dispute to Citibank.

. We now have AO's in the cardholder's chain of command. The AO's are aware of what the material requirements are.

. We added purchase card turn-in to the check-out paperwork for all employees who leave PWCSD.

A/C Mechanic and Supervisor

In GAO's second case study, two PWCSD employees were involved in possible purchase card fraud totaling about $2,500. The PWCSD staff conducted the preliminary investigation and referred it to NCIS when fraud was suspected. When NCIS declined to pursue the case, PWCSD initiated administrative action to remove these two individuals. When given notices of proposed removal, both left the Command. However, before their departure, the PWCSD staff convinced the two individuals to make restitution to the Government in the amount of nearly $6,000 (part of the reimbursement was for the suspected purchase card fraud; the remainder was for misconduct issues not related to the purchase card).

2600 Compromised Cards

In GAO's third example of 2,600 compromised government purchase cards, my staff took immediate action to cancel the compromised cards when GAO provided the cardholder names to PWCSD.

Improper Transactions (Splits).

I'd like to address the area of splitting transactions. GAO's follow-up did find instances of splitting. They identified 20 potential splits and of these 10 turned out to be actual splits. This is an area that we are constantly watching and training our cardholders in the rules and regulations. As an example, two of the splits discussed by GAO involved a cardholder in our IT

department. These split transactions were identified by the cardholder's AO during the monthly review of that cardholder's statement. The APC immediately suspended the cardholder's account until a meeting was held between the cardholder, cardholder's entire chain of managers, the AO, and the APC. The circumstances of the transactions were completely discussed and the rules and regulations were explained and reinforced to all concerned. After this retraining session, the cardholder's account was reinstated.

Transactions Not Permitted by Law, Regulation, or DOD Policy

Food

Another area that I would like to address is the issue of food, which was served to employees during day-long meetings. One of those occasions related to a conference sponsored by the Public Works Field Support Office. Two occasions related to strategic planning sessions involving personnel of PWCSD and our customer commands. We have reviewed the circumstances and concur with GAO. The food items served at the Public Works Field Support Office personnel conference were the types of items that are listed as allowable by ASN FM&C letter 7150 FMB-56 of 31 May 2000 (muffins, cookies, bagels, coffee, juice.) Although these items are allowable as "light refreshments", they were selected from the hotel's "Breakfast Menu" which gave the appearance of being inappropriate. In the other two instances, a "Fast Track" lunch (cold-cut sandwiches, potato salad, chips, and soda) was served during a working lunch. I believe those violations grew out of a lack of understanding of the rules. The general understanding in PWCSD was that the provision of meals is permissible when employees are engaged in all day sessions off-site and when allowing those employees to leave during the day would be unduly disruptive to the end purposes of the conference. The staff now understands

that meals can be provided only in the context of training or externally-sponsored conferences. We have developed a PWCSD Notice on the circumstances where it permissible to pay for employee meals while in a travel status attending meetings, conferences, and while attending training sessions. Once this clear guidance is in place, and with our current controls, I do not expect this to happen again. This notice will be released this month.

Luxury Vehicles

GAO is correct that my Transportation personnel did rent Class IV vehicles for individuals not authorized to obtain these cars. GAO pointed out this problem on 12 December 01. This systemic problem was caused by a lack of communication and understanding of flag ranks in our work reception. The very next day, procedures were in place to ensure that the class of vehicle rented is commensurate with the rank of the individual using the vehicle.

Senator GRASSLEY. Thank you very much for your testimony.

I now would call Captain Patricia A. Miller, Commanding Officer, Space and Naval Warfare Systems Center, San Diego. Welcome, Captain.

Captain MILLER. Good morning. Thank you, sir. Good morning, Senator Grassley.

As you said, I am Captain Patricia Miller, Commanding Officer, Space and Naval Warfare Systems Center, San Diego. I assumed command on December 8, 2001. Senator Grassley, I have prepared a written statement, which I request be submitted for the record.

Senator GRASSLEY. It will be received.

Captain MILLER. Thank you, Senator. I will now briefly summarize my statement.

First, I sincerely appreciate GAO's thorough and candid assessment in their recently completed command audit. As I told Mr. Kutz, I am personally committed to changing the culture at my command to permanently improve this important and vital program.

As you know, the GAO found both continued weakness and significant improvements in our program. We agree there was a command climate that permitted these abuses. We agree there were several employees who used poor judgment in making purchases, and we did not serve our employees well by providing proper oversight to prevent these abuses.

In summary, we agree with GAO's findings. We have made significant changes to correct these deficiencies and are working hard to implement GAO's recommendations.

For example, we have reduced the number of cardholders by more than 30 percent. We have dramatically increased the number of approving officials, and are now far below the recommended Department of Defense cardholder-to-approving-official ratio. We have ensured these approving officials are personally accountable for statements submitted for payment and the cardholders under them.

All approving officials and cardholders have received detailed training on appropriate purchasing behavior. We have strengthened our internal controls by implementing a process to randomly review purchase card transactions. We have implemented a semiannual command evaluation review to look at our processes and procedures to identify potential problems early. In addition, GAO has reviewed the Enterprise Resource Planning [ERP], System, and we have implemented their recommendations.

Senator, I am personally committed to increasing our management oversight, training employees to establish a greater awareness of ethical and prudent purchases, and changing the command climate to ensure every single employee understands their ethical and fiduciary responsibilities. We are fully engaged in making the necessary changes to ensure that you and the public have trust and confidence in my command.

Senator Grassley, I appreciate the committee giving me the opportunity to address this important issue, and I am now prepared to respond to any questions you may have. Thank you.

[The prepared statement of Captain Miller follows:]

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HOUSE GOVERNMENT
REFORM COMMITTEE

STATEMENT OF

CAPTAIN PATRICIA A. MILLER

COMMANDING OFFICER

SPACE AND NAVAL WARFARE SYSTEMS CENTER SAN DIEGO

BEFORE THE

HOUSE GOVERNMENT REFORM COMMITTEE

GOVERNMENT EFFICIENCY, FINANCIAL MANAGEMENT AND

INTERGOVERNMENTAL RELATIONS SUBCOMMITTEE

ON

NAVY PURCHASE CARD PROGRAM

13 MARCH 2002

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HOUSE GOVERNMENT
REFORM COMMITTEE

Mister Chairman and distinguished members of the Committee: Thank you for the opportunity to discuss our execution of the Navy's Purchase Card Program. I am Captain Patricia A. Miller, Commanding Officer of Space and Naval Warfare Systems Center San Diego (SSC San Diego). SSC San Diego is the Navy's full spectrum research, development, test and evaluation, engineering and fleet support center for command, control and communication systems and ocean surveillance. In that role, the Center provides information technology to the nation's warfighters, principally of the Navy and Marine Corps, but, increasingly, of the joint services, to collect, process, display and transfer information to support them in their requirements to execute their military and humanitarian missions effectively.

SSC San Diego is headed by a Navy Captain and a Senior Executive Service civilian, with a workforce of 3,450 civilians and 80 military personnel. More than half of our workforces are scientists and engineers, primarily in the computer science, computer engineering and electronic engineering fields. Another 20 percent of the employees are technicians and technical specialists. We have a highly educated and highly skilled workforce. More than 2,500 of our employees have four-year degrees; 900 have advanced degrees, and more than 200 of those have doctorates. Our products in support of our customers are advanced, cutting-edge technologies, and we have the state-of-the-art laboratories and equipment, including four of the most advanced supercomputers available anywhere, to continually push the envelope of those technologies. In the critical areas of research and development, we procure high-technology hardware and software items to support experimentation, with potential important application for meeting emerging Fleet requirements. One method of procurement is the Navy purchase card.

Our most important customer is in fact the Fleet, but in serving that customer SSC San Diego is funded for its 1,000-plus technical programs by all three of the Navy's major

acquisition commands; the Office of Naval Research; and the Defense Advanced Research Projects Agency, which is our second largest sponsor after our headquarters, Space and Naval Warfare Systems Command (SPAWAR). We are also funded by various agencies of the Department of Defense and other federal agencies; and by the Army, the Air Force and the Coast Guard.

Recently the General Accounting Office (GAO) completed audit number 192046 of the Navy's Purchase Card Program at SSC San Diego. This audit was conducted between November 5, 2001 and mid-February 2002. It is important for me to state that this purchase card program is critical to the success of SSC San Diego for research and development, test and evaluation, installation and in-service engineering in support of the fleet and the nation's military services.

Before I address the actual audit findings, I would like to express my appreciation to the General Accounting Office for their very detailed look into our Purchase Card Program. No one likes to be audited, particularly if there is a potential expectation that unfavorable things will be found during the audit. However, the value in a case like this is that an objective outside organization is able to provide insight into problems and weaknesses that have been missed by internal checks, plus recommend appropriate steps for dealing with those problems and effecting cultural change. There has been a very respectful and cordial relationship between GAO and SSC San Diego personnel involved in this audit since last fall, and I believe this spirit of cooperation has contributed to the value of the final audit report being provided today to your committee.

I also want to discuss briefly what the Purchase Card Program means to SSC San Diego and, by extension, to our Fleet customers. It is an understatement to say that this program has

favorably improved our efficiency in procuring material to support our customers. It provides a responsiveness and flexibility unheard of in the long history of Navy procurement. What once took weeks if not months to purchase now can take as little as a few hours. The lengthy, and costly, process of submitting requirements through a centralized procurement office has been reduced to making a reasonable judgment on an appropriate source, quality and cost of a required item, and calling up a vendor to order it, or driving to a nearby store to pick it up. For SSC San Diego personnel, the program allows "just in time" delivery of supplies and laboratory equipment, minimizing costly storage of these items. Our forward-deployed technology teams can respond rapidly to emerging requirements of the Fleet around the globe.

I'd like to share several more significant examples of the value of the Purchase Card Program from our recent experience with Navy ships:

- USS Barry (DDG-52) lost all of its data link capability, a critical item in the ship's ability to pass tactical data essential to its operations and mission fulfillment. SSC San Diego personnel responding to the casualty report determined the cause was a non-functioning microprocessor card. The ship was unable to obtain a replacement card through the supply system in a timely manner. An SSC San Diego purchase card was used to procure a replacement quickly, and the ship's data links were returned to fully operational condition in very short order.
- USS Blue Ridge (LCC 19) was participating in network upgrades when it was determined that copper-based network interface cards (NICs) rather than fiber-based NICs had been shipped for installation. The correct NICs had to be procured on site to ensure usability of the affected workstations for COMSEVENTHFLT staff and the ship's crew.

- Multiple Forward Deployed Naval Forces (FDNF) ships were commencing Automated Digital Networking System (ADNS) installations to allow off-ship classified and unclassified network connectivity. These installations were some of the first-ever in the U.S. Navy and supporting tool kits had not yet been provisioned to FDNF sites. The purchase card was used to allow immediate procurement of the kits, which contained special-purpose tools required to complete the installations.

- An urgent requirement from the U.S. Department of State and U.S. Navy regional commanders was received for the installation of coalition networks on Japanese Maritime Self-Defense Force ships. Network routers, network hubs, and support materials were procured via the purchase card to complete installations in support of the ships' operational schedules, allowing coalition operations in support of Operation Enduring Freedom.

- A computer security firewall failed at a site in the Far East that was providing protection to the Forward Deployed Naval Forces (FDNF) Amphibious Readiness Group (ARG). An urgent trip to the site revealed failed components in the computer providing the firewall protection. Spare components had not been provisioned, so the purchase card was used to allow the immediate restoration of the firewall protecting the FDNF ships.

These are only recent examples of many instances in which the ability to use a purchase card directly at a convenient vendor has allowed SSC San Diego personnel to be responsive to urgent fleet requirements.

I will now address the GAO's audit findings. GAO noted both significant improvement and continued weaknesses in SSC San Diego's Purchase Card Program. Please be assured that I

am absolutely committed to improving the management controls and command climate for this essential program. I have already taken several significant steps in this direction, including:

- Achieving greater than a 30 percent reduction in the number of purchase card holders as of 1 March
- Increasing the number of approving officials providing purchase oversight and accountability to 228
- Achieving a resulting ratio of cardholders to approving officials well within Department of Defense guidelines of 7:1

The GAO audit report emphasizes training as essential to program success, and I agree with that, to the point that not one new purchase card will be issued to an employee before his or her initial training in proper card use is completed and documented. We held a general information session for several hundred Center management officials on this subject last summer. During this gathering, a detailed plan of action and milestones (POA&M) was introduced, outlining Center actions to address deficiencies in the program. As part of this POA&M, SSC San Diego established an IPT to study the Purchase Card Program. This group, representing all our technical and administrative groups and headquarters, wrote an official SSC San Diego instruction to document proper purchase card use procedures and developed an aggressive training program. The first Navy stand-down training for several hundred Center cardholders and approving officials was scheduled for September 12, 2001. Like a multitude of plans short-circuited by the tragedy of September 11, the purchase card training schedule was put on hold temporarily. In October 2001, however, the first Navy-mandated purchase card stand-down training sessions were held, with additional classes in January 2002. Cardholders were trained in acceptable purchase practices to ensure they understood them; for

those who failed to attend the required training, we have taken appropriate action and suspended or cancelled their cards. All approving officials received training concerning the importance of their oversight and reconciliation role in the purchase card process as well as the potential for personal liability.

We will continue to refine and update our training program and emphasize the absolute necessity of attending the required refresher training every two years. Our next efforts are intended to reach all Center employees, many of whom are not formally involved in the Purchase Card Program but still impact it. These are the several thousand employees who are neither cardholders nor approving officials, but they may request the cardholder in their branch to use the card to purchase something. I have already addressed these folks in an early March all-hands e-mail in which I stated the substantial value of this program to the Center and the absolute requirement that all employees support it by ensuring it is used ethically and prudently. In the near future, all SSC San Diego employees will receive training to ensure they understand the rules, especially the fundamental rule that the purchase card is used only to satisfy real, and realistic, government requirements.

We have strengthened and improved our internal controls by ensuring more timely review of monthly purchase card transactions by the Agency Program Coordinator. We also report the results of these reviews to Center top management officials for action. This provides an improved opportunity to detect unauthorized purchase card buys made either consciously or accidentally, identify purchase trends, and implement corrective actions in a timely manner. At the highest level, the command review level, we have also implemented semi-annual reviews of the Purchase Card program.

I have taken the findings of the GAO audit just concluded, conducted internal investigations of potential abuses of the purchase card program, and taken appropriate action against offenders, including procedural reminders, cancellation of cards and disciplinary actions.

I want to mention one other SSC San Diego initiative that has both positive and negative potential in our planned efforts to initiate the GAO recommendations for improvement in our Purchase Card Program. Enterprise Resource Planning (ERP) refers to commercially available business software solutions that enable organizations such as SSC San Diego to:

- Automate and integrated business processes
- Share common data and processes across the entire organization
- Produce and access information in a near real-time environment
- Provide consistent information for timely decision making and performance measurement

Through ERP, SSC San Diego plans to reduce process cycle times, create a more efficient and effective team, and provide consistent, accurate and timely information.

The Center's ERP effort is one of four Navy pilots in the use of commercial software to provide more effective financial management capabilities. It was the first of the pilots to "go live"; in fact, at this time it is the only one that has done so. That occurred in July 2001, which regrettably was the same period selected for the recent GAO audit sample period. It is certainly not intended as an excuse, but the substantial attention required to real-time implementation of ERP was one of the many obstacles that diverted attention from a more robust and effective response to Purchase Card Program deficiencies. The good news is that ERP, now that the Purchase Card Program documentation process has been incorporated into it, provides a very substantial tool in our intended effort to strengthen internal controls on card purchases.

Although ERP alone will not solve all of the management control issues noted by GAO, it will, in time, provide a seamless and efficient tool to further ensure that purchase card buys are appropriate, cost effective and well-documented. GAO has acknowledged improved supporting documentation related to the purchase card program improved as implementation of the ERP tools progressed.

I'd like to conclude this statement in a vein similar to the manner in which I started. No one likes an audit, and it is sometimes difficult to accept criticism, especially when you know that the large majority of your employees really are doing their very best to honestly fulfill their responsibilities as public servants. Some of them have failed, and that negatively impacts this valuable Navy program. SSC San Diego as an organization, despite some recognizable improvements in accountability and oversight and some substantial efforts to do even better, still has a lot of progress to make. GAO has noted an uncomfortable number of control weaknesses and questionable purchase card transactions in its review of our FY01 purchases. We appreciate their thoroughness in identifying problems in execution of the Purchase Card Program and agree that additional improvement is needed to ensure that public funds are spent responsibly and prudently to meet the government's minimum needs.

In conclusion, the GAO audit has provided SSC San Diego with an opportunity to improve and correct deficiencies in the Purchase Card Program. Although improvements have been made in virtually every area of the program, we recognize that more needs to be done, including a first critical step toward cultural change among the workforce. I am personally committed to establishing the oversight and management controls required to make this an effective program. It is vital that the purchase card be available as an essential tool in meeting emerging commitments and threats to homeland defense and national security.

Mr. Chairman, thank you for giving me this opportunity to address the committee, and I welcome your questions.

Senator GRASSLEY. I want to thank you for the responsible attitude toward change and correcting the problem, for both of our Captains in command there in San Diego. Thank you very much.

It is now my pleasure to invite Tina W. Jonas, Deputy Under Secretary for Financial Management at the Department of Defense. Ms. Jonas.

Ms. JONAS. Thank you, Senator. I am glad to be here this morning to talk about this issue.

At the outset, let me say that the Department's senior leadership is seriously concerned about purchase card problems that are the focus of this hearing this morning. We will not tolerate failure to comply with established policies and procedures such as occurred with the purchase cardholders at some locations. We understand that, even if instances of fraud and abuse are caught early, they reveal a lapse in internal management controls, and such lapses cannot be allowed in so serious a business as America's national defense.

For purchase cards, the most important role of my organization, the Comptroller's Office, is to strengthen all internal management controls, not merely those controls relevant to purchase cards. We are doing this as part of an unprecedented overhaul of the Department's financial management.

Our efforts include both long-term and short-term initiatives. Long-term we are streamlining and standardizing the Department's financial and non-financial systems, transforming them into an integrated set of systems that will enable DOD leaders to get the timely, accurate, and complete financial information that is essential to strong internal controls.

Short-term we are taking action to address immediate problems to facilitate our long-term initiatives and to work with the Department's senior leadership to overcome purchase card problems. For example, the Under Secretary of Defense Comptroller, Dr. Zakheim and the Under Secretary of Defense for Acquisition, Technology and Logistics, Pete Aldridge, recently issued a joint memorandum directing all components to ensure compliance with published purchase card and internal controls.

These controls are consistent with the General Accounting Office's standards, and they include a maximum dollar limit for any single purchase, a maximum dollar limit for the cumulative value of all purchases made during the monthly billing cycle, limitations on the cards used to categories of merchants, if appropriate, or to a single merchant.

It also includes requirements for the supervisor to receive, review, and, as necessary, question and adjudicate billing differences with each subordinate cardholder. I think this was one of the key faults that happened at the Navy, and we are working decisively on that problem. When implemented properly, these controls minimize losses from waste, fraud, or abuse.

In addition, in the Department's internal management control program, we are making the purchase card program an area of special emphasis. This will force DOD components to review their internal controls for their purchase cards and report on the adequacy of those controls. I assure you that we will review those reports

very carefully and followup with specific actions necessary to correct problems.

We are also working with the audit community and subject matter experts, and we have identified potential fraud indicators for this program. For example, if the same person that makes a purchase also approves the bill for payment, this would be a red flag, and these types of indicators are being developed and software is being used to identify suspect transactions.

We are also building a front-end edit that the purchase card contractors will use to flag suspect transactions for review before transactions are authorized. This is the same concept used by major credit card companies, but it is tailored to the DOD business model.

Beyond the specific purchase card emphasis, the scope of our management controls extends to every activity an area of responsibility within the Department and its components, and our procedures apply to all financial, administrative, and operational controls.

This past year the Comptroller implemented the first phase of an initiative to ratchet-up the management control program. In cooperation with the Assistant Inspector General for Auditing, we identified major areas that other senior leaders in the Department evaluated for coverage in the Annual Statement of Assurance in the Reporting Cycle.

Also, this past year, for the first time, we required components to identify the cost to correct material and systemic weaknesses, and we required the components to specify performance metrics to gauge success in resolving identified weaknesses. This year, again, we will work with the Inspector General to identify issues and trends that need to be addressed by the DOD senior leadership, and we conduct periodic visits to component Headquarters' internal review organizations to ensure that they are appropriately resourced and effectively performing their missions.

In closing, Mr. Chairman, the Department takes the matter of internal control seriously, and our most senior leadership will manage from the top-down and ensure the correction of those deficiencies identified by the General Accounting Office and the Office of the Inspector General.

Thank you. I would be happy to take any questions.

Mr. HORN. Thank you very much.

We now have Deidre A. Lee, the Director of Defense Procurement, Office of the Under Secretary of Defense for Acquisition, Technology and Logistics, Department of Defense. Ms. Lee.

Ms. LEE. Good morning, Chairman Horn. I'm a last-minute addition to this hearing, to affirm Defense Procurement's commitment to properly manage the defense purchase card program. You and I had a brief discussion during a hearing last week, and I just wanted to appear before you today and affirm again that commitment.

The purchase card program is very important to the Department. As you know, we use it for a variety of methods. It has saved transaction costs, and it has in many cases put the purchaser closer to the requirements and shortened that timeframe. But it must be properly managed.

As noted, the Public Works has an improvement program and has made some progress. The current situation at SPAWAR is unacceptable. We are working with Captain Miller and she has certainly stepped up-to-the-plate, starting in December, to try to remedy these situations.

We have a two-prong approach. The first is to address the problems at SPAWAR, and the Department has taken the following actions: The purchase cards at SPAWAR have been suspended at the bank—that is not just through the user, but at the bank—effective immediately. We then are going to reinstate a handful of the purchase cards to support mission-critical and essential fleet needs, and they will be reviewed by the local commander. The program office will monitor the transactions through the bank. We can actually go through the bank and see when those cards are used and what is turned back on, and we will do that.

Then the cards will remain suspended until Captain Miller puts in her what we call a multi-step program, making sure people are trained, educated, understand the commitment, understand their responsibility. Then, little by little, with confirmation through senior leadership, we will reinstate that program and manage it very aggressively.

We also have a training program that she has put in place, and everyone gets remedial training. They will be reminded of their duty to buy only minimum requirements, instead of, unfortunately, some of these luxury items we talked about. They will be reminded of their obligation to purchase through NIB/NISH, the blind, the handicapped, the Federal Supply Schedules.

We will also identify the review and certification process, that billing officials must be connected to the cardholder and know what they're purchasing and whether or not it applies to their job.

We also have put in place a property accounting system. So when purchases are made, there's a matchup: Are they there? Do we have them?

Then there also will be a very clear statement of what the situation is for violations of using that card. We are working with SPAWAR to do all of that.

I am very serious about remedying the situation, and I intend to personally verify the situation improvements and report back to you by the end of May.

Shifting to the departmentwide program, because, as GAO mentioned, we are also concerned, let's make sure we are doing this right across the Department, and with you, Mr. Chairman, I note that we have the Executive Contracting Course here. I am glad for them to hear this discussion, so they know how serious we are about improving this program.

We have taken an approach across the Department as well. We have identified many activities, but mainly leadership, internal controls, and common sense are needed to use this program properly.

We are going to review all the approval and certification procedures for officials. They have been instructed to do that. We've also reviewed how we appoint billing officials, how we appoint certification officials, the span of control.

We are reviewing the establishment for account establishment: Who should have a card? Why? For what purpose? To what amount? And that includes the limits.

We have instructed the card managers to review the flexibilities within the card. Can they block certain codes, certain merchant codes, certain vendors? And they have been reminded to do that.

We are also making sure that appropriate resources are allocated. You can't just handout the cards and then not have the resources allocated to do the oversight. So we are focusing on that as well.

We are going to have training for all purchase card accounts and also to emphasize leadership and oversight responsibilities. We have also partnered with DCAA, Defense Contract Audit Agency, the Inspector General, and have several things going on there, including an online training course that will be available by the end of the year which specifically addresses some of the things highlighted in GAO. We are using a software program where we can have oversight of the purchases.

We have also put in place some additional—I have asked the IG to do an across-the-Department look. They now coordinate all purchase card reviews with the various inspector units and give us a quarterly report on what they've found. We will track down those trends and implement it across the Department program, not just at SPAWAR or Public Works.

We also have an online software program where the cardholder is going to have to click on each transaction. The transaction then goes to the oversight, so that it has to follow the process of having appropriate review.

So, Mr. Chairman, we are painfully aware of the issues with purchase cards, and I am here to personally commit that we will make sure these cards are used appropriately and make sure that our people understand their responsibilities, and we all live up to our commitment to the taxpayer.

[The prepared statement of Ms. Lee follows:]

STATEMENT OF
DEIDRE A. LEE

DIRECTOR, DEFENSE PROCUREMENT

OFFICE OF THE UNDER SECRETARY OF DEFENSE FOR ACQUISITION,

TECHNOLOGY & LOGISTICS

BEFORE THE

SUBCOMMITTEE ON GOVERNMENT EFFICIENCY, FINANCIAL MANAGEMENT AND INTERNATIONAL RELATIONS
OF THE
HOUSE GOVERNMENT REFORM COMMITTEE

MARCH 13, 2002

Army - Card - transactions? → travel cards.

Mr. Chairman and Members of the Committee:

Mr Chairman — I am a last minute addition to this hearing -- to affirm Defense Procurement's commitment to properly managing the purchase card program.

I appreciate the opportunity to come before you and discuss the Defense Department's implementation of the Governmentwide purchase card program. Defense procurement is the manager of the Defense Department's ~~Governmentwide purchase card program. In this capacity,~~ I am ~~we are~~ responsible for providing overarching policy for use of the card. The implementation of the program is handled through the program management office and by the individual services and defense agencies.

During fiscal year 2001, Department of Defense personnel made over 10.7 million purchaseswith the purchase card valued at over $6 billion

The Governmentwide purchase card program has allowed the Department of Defense to significantly streamline the acquisition process, has provided administrative ~~real-~~

savings to the taxpayer and increased the ability of Department of Defense field activities to support their customers.

The purchase card program is very important to the Department of Defense—it must be properly managed. As noted, the management of cards at Public Works is improving. The situation at SPAWAR is unacceptable. We have taken steps to remedy the situation and emphasize oversight of the purchase card program as part of a two prong approach.

First, to address the problems at SPAWAR, The Department of Defense has taken the following actions:

The purchase card program at all SPAWAR locations has been suspended at the bank. A handful of purchase cards will be reopened to support critical mission essential needs of the fleet. Purchases under those accounts

require review by the local commander. In addition, the program office will monitor, thru the bank's on-line system, each purchase under those accounts. Other purchases must be made through other contracting procedures such as purchase orders.

All other SPAWAR purchase cards will remain suspended until I and other senior management at the Office of the Secretary of Defense and the Navy are satisfied that appropriate controls are in place and cardholders understand their duties and accountability to the taxpayer. The plan of action includes—

A phased approach for selective reinstatement of purchase cards. The first phase is mission essential with Commander's review to meet immediate critical needs. This will be followed by a review of how many cards and what types of limits are needed to support normal

operations. SPAWAR will establish reasonable limits on individual purchases that more closely align with normal cardholder usage over the past year.

In conjunction with this review, cardholders and billing officials must receive remedial training on—

The proper procedures for review and certification of monthly purchase card transactions. -- Billing officials must verify that the Government received the item or service and that it was appropriate for the cardholder to obtain the item or service, given the mission of the activity and the cardholder's job description.

The duty to buy only minimum requirements instead of luxury items.

The order of priority for acquisition sources, including NIB NISH, Federal Supply Schedules.

The procedures for ensuring that expensive, easily pilferable items are entered on government property rolls.

The consequences of violating the purchase card policies and procedures, including the range of possible outcomes for adverse behavior.

Mr. Chairman, I am serious about remedying this clearly unacceptable situation. I intend to personally verify that the situation has improved and report findings to you by the end of May.

Shifting focus to the Department-wide program, the second prong of our approach addresses concerns expressed by the subcommittee and other members of Congress about the Department of Defense Governmentwide purchase card program as a whole. Many

significant steps have been taken over the past year to strengthen internal controls.

The Department of Defense Governmentwide purchase card program management office and I have made it clear to senior command authorities within the Department of Defense that leadership, strong internal control practices, and common sense are essential to provide the level of quality control needed to meet our fiduciary responsibility to the taxpayer. The General Accounting Office has noted several times that the written purchase card policies and procedures are generally adequate – it is our compliance and oversight that must improve. Focusing on these areas, the program office and I have emphasized the following issues over the past year--

- Review, approval, and certification procedures for billing and approval officials.

- Appointment of billing officials. Billing officials should be first-level supervisors whenever possible and cardholders cannot be their own billing officials.
- Criteria for establishing accounts. Cardholders must have a continuing need to purchase goods or services and individual purchase limits must be based on what the cardholder needs to buy as part of his or her job.
- Establishing limits on merchant categories to block certain merchant categories, such as jewelry store and dating services, in accordance with Department-wide policy.
- Allocation of adequate resources to the program at the field locations to support the required levels of review and oversight.
- Training for all purchase card participants

- Leadership oversight and responsibilitly

To strengthen internal controls, we have engaged our partners through out the Department. The Inspector General of the Department of Defense, and the Directors of the Defense Finance and Accounting Service, and the Defense Manpower Data Center have redirected the Department's internal purchase fraud detection program to focus on purchase card acquisitions.

To further improve internal controls, I have engaged the Department's internal audit and inspection activities, under the leadership of the Inspector General. The Inspector General will serve as the central clearing house of Department-wide purchase card audit activities and be a central repository of audit findings. This allows increased visibility of fraud and misuse trends.

Mr. Chairman, we use the Department's audit and inspector general functions as an additional internal control under the purchase card program. We send them out to verify that the local programs are implemented according to applicable policies and that they have appropriate internal controls.

The program office has established a partnership with the Defense Acquisition University to develop on-line cardholder and billing official training modules incorporating lessons developed by the program manager and defense components. The on-line tutorial is expected to be available as a training tool sometime this summer. The training specifically addresses issues raised by the GAO.

The program management office, the Inspector General, the Service audit agencies, and the Defense

Finance and Accounting Service have established a partnership to exploit data mining techniques. This project is in its infancy, but we anticipate substantial improvement in our ability to detect high risk situations in the future.

A final on-going project that is expected to provide improved internal controls is the implementation of on-line statement review, approval, and certification. In addition to speeding bill payment, reducing delinquencies, and increasing rebates earned, the project includes improvements to internal controls. Card holders must "click" on each transaction on their bills to approve the bill for transmittal to the billing official for payment. This forces cardholders to review their bills. As the billing official cannot certify the bill for payment absent the cardholder review and approval, this drives adherence to the Department of Defense certification policy. The system

also allows visibility into real-time transactions by the billing official or the program office. This allows continuous review of cardholder purchases throughout the month, thereby reducing the risk of fraud.

In closing, I would like to affirm my commitment to improve the Governmentwide purchase card procurement process, have ~~appropriate oversight, and provide the tools needed for the defense workforce to obtain the goods and services they need.~~

Thank you. I would be glad to take any questions you might have.

Mr. HORN. Well, I thank you for your statement. You mentioned accountability. Now that accountability will come up the service line or the civilian line, or both?

Ms. LEE. Both, sir, and including the financial side, Ms. Jonas, as well as the policy side from a procurement-specific standpoint, myself.

Mr. HORN. Because there are also Inspectors General in the services.

Ms. LEE. Yes, sir. We have asked the DOD Inspector General to coordinate all their audit reports and kind of look across the Department, what did each Inspector General at each service find, coordinate that and show us any trend data, any systematic problems.

Mr. HORN. So we've got now a program that relates to education of these in terms of both the civilian and the service line?

Ms. LEE. Yes, sir.

Mr. HORN. Now I would like to know, what, if anything, has been done in terms of the court martial part, and is there anything to do with this type of bad behavior? Is there anywhere in the court martial situation, in the code of military justice, that one can be brought before on court martial? Otherwise, they are just laughing.

Ms. LEE. Sir, if you are talking about the removal of the commander from SPAWAR, that was for a variety of actions. I understand it was not specifically the purchase card, but we have all kind of talked about the attitude or tone at the top that seemed to be underlying that situation, and that was one of the issues.

Mr. HORN. Well, it's been about 30 years since I have looked at the court of military justice, when that was put out mostly in the Eisenhower administration. The question is, is there language in that one can violate and be brought up on that?

Ms. LEE. I am not personally familiar with it.

Mr. HORN. Now our last presenter is Danielle G. Brian, the executive director of Project on Government Oversight [POGO]—nothing to do with the comic "Pogo," but sometimes things seem that way. [Laughter.]

Ms. BRIAN. Mr. Chairman, thank you for inviting me to testify at this hearing. As usual, this subcommittee is performing the very important job of overseeing the workings of the Federal Government. If only more committee chairmen and members of committees took that part of their job as seriously as you do.

I am the director of the Project on Government Oversight [POGO]. Our organization investigates, exposes, and seeks to remedy systemic abuses of power, mismanagement, and subservience by the Federal Government to powerful special interests. Founded in 1981, POGO is a politically independent, non-profit watchdog that strives to promote a government that is accountable to the citizenry.

Today we are talking about waste, fraud, and abuse of the Department of Defense, the agency that can't account for $1 in $4 it spends. I know defenders of DOD accounting procedures claim this is an unfair criticism, that the missing $1.1 trillion is only a paper transaction. In these days of Arthur Andersen accounting, a firm, I might add, that continues to consult for nearly every Federal agency, my response is, show me the money.

We have found that Federal agencies are loath to admit they're making a mess of things. The Pentagon must be forced to account for its expenditures of taxpayer dollars. I am particularly impressed when government officials such as those at the Navy Public Works put their energy into fixing a problem rather than denying or covering it up.

Thanks to the work of Senator Grassley and his staff, Chairman Horn, and the GAO, we have been made aware of the abuses of Federal purchase cards, one of many Federal dollar sink holes at DOD. The GAO found that these purchase cards, as we have been hearing, have been used to buy personal items at two San Diego Navy installations. Despite the Pentagon's best efforts to pretend these were localized abuses, however, it is clear this is a systemic problem. Across the country and in a different service, this time the Army, similar abuses have been uncovered.

In January 2000, two enterprising reporters at the Fayetteville Observer sent Freedom of Information Act requests for the receipts of more than 330,000 government credit card purchases by Fort Bragg cardholders. Among many others, they found charges of, for example, $981 for Atlanta Braves baseball tickets, $235 for Six Flags Magic Mountain tickets, and my personal favorite, $111 at Victoria's Secret.

Some may say that those who would commit fraud will do so regardless, but creating a system where the oversight is largely the honor system is asking for trouble. One cardholder indicted for making over $17,000 in fraudulent personal transactions commented that illegal use of the credit cards was too easy, and that she was the sole authorizer of card purchases.

We believe that for the most part the problem is not created by the existence of the purchase cards themselves, but with the reduced financial oversight that comes with what are called micro-purchases of $2,500 or less for each transaction. However, most of these unaccountable micro-purchases are made through the use of these credit cards.

According to the Federal Acquisition Regulation, micro-purchases may be awarded without soliciting competitive quotations if the contracting officer considers the price to be reasonable. A system that allows for non-competitive purchases without checks and balances is simply a bad idea. Allowing hundreds of thousands of government cardholders to make these purchases is lunacy.

In addition to the outright fraud committed with the use of these purchase cards, a more damaging problem is the overcharging that also flies below the micro-purchasing radar screen. A 2001 DOD IG audit of micro-purchases at the Defense Supply Center in Philadelphia found that overcharging occurred in no fewer than 42 percent of the audit sample. Among the most egregious cases of overcharging was a $409 sink that should have been purchased for $37.

Not surprisingly, both the GAO and the DOD IG have recommended strengthened internal controls to prevent such overcharging and outright fraud. But when Uncle Sam is paying the credit card bill, there are currently far too few deterrents to keep a credit cardholder from misusing these purchase cards.

Incredibly, in the face of these findings, another subcommittee under Government Reform, the Subcommittee on Technology and

Procurement Policy, held a hearing just last week on proposed legislation that would increase tenfold the micro-purchase threshold from $2,500 to $25,000 with no additional financial oversight, which is section 221 of the Services Acquisition Reform Act. I can imagine the headlines that will soon follow if this bad bill becomes law.

This proposal to increase the government purchase card micro-purchasing threshold is simply a continuation of the efforts by acquisition reform lobbyists to reduce financial oversight and limit the ability of competition and free market forces to lead to smarter government spending. We have found that so-called acquisition reforms, which have gained currency in the past decade, have repeatedly been detrimental to oversight and accountability of Federal procurement and have resulted in increased expense to taxpayers. Who benefits? The contractors who have drafted this legislation.

In our recent report, "Pickpocketing the Taxpayer: The Insidious Effects of Acquisition Reform," we cite numerous findings by government auditors that show these reforms have, in fact, been deforms which limit competition and pretend prices for government purchases are determined by commercial forces when they are not.

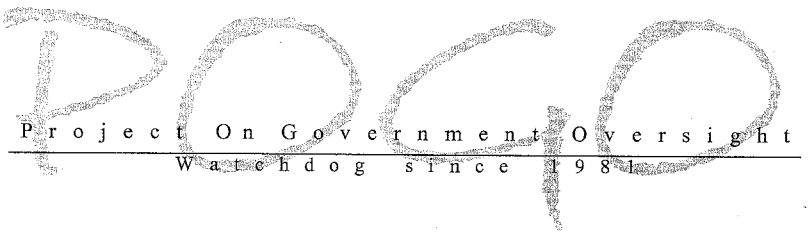
Mr. Chairman, I simply do not understand how we have come to a point where the founding principles of the American economy, free market forces and fair and open competition, are valued only when they don't apply to the government.

The downward spiral away from competitive purchasing and toward more acquisition from the few remaining giant defense contractors is exacerbated by the use of government credit cards. The Office of Advocacy of the U.S. Small Business Administration is currently studying the effects of the use of government credit cards on small businesses.

They have already concluded, "Prior to acquisition reform, micro-purchases of $2,500 or less were reserved exclusively for small businesses." Today these purchases are no longer reserved for small businesses because many of these purchases are being acquired through the use of the government credit card. Nearly one-half million Federal employees may use the government credit card with any authorized merchant. There are few, if any, acquisition controls on the use of the card. Other than convenience, there is very little data to reveal that the government is getting the best price with the use of the credit card.

In conclusion, Mr. Chairman, I hope you are successful in persuading your colleagues that reduced procurement and financial oversight at the Pentagon is not in the American public's best interest. Thank you.

[The prepared statement of Ms. Brian follows:]



Written Testimony of Danielle Brian
Executive Director
Project On Government Oversight
March 13, 2002
before the
House Subcommittee on Government Efficiency,
Financial Management, and Intergovernmental Affairs

Mr. Chairman. Thank you for inviting me to testify at this hearing. As usual, this Subcommittee is performing the very important job of overseeing the workings of the federal government. If only more Committee Chairmen took that part of their job as seriously as you do.

I am the Executive Director of the Project On Government Oversight or POGO. Our organization investigates, exposes, and seeks to remedy systemic abuses of power, mismanagement, and subservience by the federal government to powerful special interests. Founded in 1981, POGO is a politically-independent, nonprofit watchdog that strives to promote a government that is accountable to the citizenry.

Today we are talking about waste, fraud, and abuse at the Department of Defense – the agency that can't account for one in four dollars it spends. I know defenders of DOD accounting procedures claim that this is an unfair criticism – that the missing $1.1 trillion is only a paper transaction. In these days of Arthur Anderson accounting – a firm, I might add that continues to consult for nearly every federal agency – my response is "show me the money." We have found that federal agencies are loathe to admit they're making a mess of things. The Pentagon must be forced to account for its expenditures of taxpayer dollars.

Thanks to the work of Senator Grassley, Chairman Horn, and the GAO, we have been made aware of the abuses of federal purchase cards, one of many federal dollar sinkholes at DOD. The GAO found that these purchase cards have been used to buy pizza, jewelry, personal phone calls, tires, and flowers at two San Diego Navy installations.

Despite the Pentagon's best efforts to pretend these were localized abuses, however, it is clear this is a systemic problem. Across the country, and in a different service – this time the Army – similar abuses have been uncovered. In January 2000, two enterprising reporters at the *Fayetteville Observer* sent Freedom of Information Act requests for the receipts of more than 330,000 government credit card purchases by Fort Bragg card holders. Among many others, they found

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charges of $981 for Atlanta Braves baseball tickets, $235 for Six Flags Magic Mountain tickets, and my personal favorite, $111 at Victoria's Secret.

Some may say that those who would commit fraud will do so regardless, but creating a system where the oversight is largely the honor system, is asking for trouble. One cardholder indicted for making over $17,000 in fraudulent personal transactions commented that illegal use of the credit cards was "too easy," and that she was the sole authorizer of card purchases.

We believe that, for the most part, the problem is not created by the existence of the purchase cards themselves, but with the reduced financial oversight that comes with "micropurchases" of $2,500 or less. However, most of these unaccountable micropurchases are made through the use of these credit cards. According to the Federal Acquisition Regulation "micro-purchases may be awarded without soliciting competitive quotations if the contracting officer . . . considers the price to be reasonable." A system that allows for non-competitive purchases without checks and balances is simply a bad idea. Allowing hundreds of thousands of government card holders to make these purchases is lunacy.

In addition to the out-right fraud committed with the use of these purchase cards, a more damaging problem is the overcharging that also flies below the "micropurchasing" radar screen. A 2001 DoD IG audit of micropurchases at the Defense Supply Center in Philadelphia found that overcharging occurred in no fewer than 42% of the audit sample. Among the most egregious cases of overcharging was a $409 sink that should have been purchased for $37. Not surprisingly, both the GAO and the DoD IG have recommended strengthened internal controls to prevent such overcharging and fraud. When Uncle Sam is paying the credit card bill, there are currently far too few deterrents to keep a credit card holder from misusing these purchase cards.

Incredibly, in the face of these findings, another subcommittee of House Government Reform, the Subcommittee on Technology and Procurement Policy, held a hearing just last week on proposed legislation that would increase ten-fold the micro-purchase threshold from $2,500 to $25,000 with no additional financial oversight – section 221 of the Services Acquisition Reform Act. I can imagine the headlines that will soon follow if this bad bill becomes law.

This proposal to increase the government purchase card micropurchasing threshold is simply a continuation of the efforts by acquisition reform lobbyists to reduce financial oversight and limit the ability of competition and free market forces to lead to smarter government spending. We have found that so-called acquisition reforms, which have gained currency in the past decade, have repeatedly been detrimental to oversight and accountability of federal procurement – and have resulted in increased expense to taxpayers. Who benefits? The contractors who have drafted this legislation.

In our recent report "Pick Pocketing the Taxpayer: The Insidious Effects of Acquisition Reform," we cite numerous findings by government auditors that show these reforms have in fact been de-forms which limit competition and pretend prices for government purchases are determined

by commercial forces when they are not. Mr. Chairman, I simply do not understand how we have come to a point where the founding principles of the American economy – free-market forces and fair and open competition – are valued only when they don't apply to the government.

The downward spiral away from competitive purchasing and toward more acquisition from the few remaining giant defense contractors is exacerbated by the use of government credit cards. The Office of Advocacy of the U.S. Small Business Administration is currently studying the effects of the use of government credit cards on small businesses. They have already concluded,

> "(P)rior to acquisition reform, micro-purchases of $2,500 or less were reserved exclusively for small businesses. Today, these purchases are no longer reserved for small businesses because many of these purchases are being acquired through the use of the government credit card. Nearly one-half million Federal employees may use the government credit card with any authorized merchant. There are few if any acquisition controls on the use of the card. Other than convenience, there is very little data to reveal that the Government is getting the best price with the use of the credit card."

In conclusion, Mr. Chairman, I hope you are successful in persuading your colleagues that reduced procurement and financial oversight at the Pentagon is not in the American public's best interest.

Mr. HORN. Thank you very much. I am going to ask a few questions going this way this time [indicating].

Ms. Lee, I am wondering, what about the young woman who allegedly went on a pre-Christmas shopping spree using her government credit card? Was she reprimanded? According to the General Accounting Office, she has moved from a government salary grade of 11 to a grade 12. Where is she working now?

Ms. JONAS. Mr. Chairman, the woman that you are talking about currently works for the Army, as I understand it. I have personally spoken to the Army Comptroller about this case. I have been advised that the case was under investigation, and she has assured me that they are checking with the General Counsel as to what disciplinary action can be taken.

I also have spoken personally with the Navy Comptroller, Mr. Aviles, about this case because, apparently, if I've got the case right, a number of the abuses happened when this woman was with the Navy. The NCIS investigated the case. The assistant U.S. attorney was asked to look into it. I guess they have declined.

I would like to submit the facts for the record, if you don't mind, because I'm doing this almost entirely from my memory.

[The information referred to follows:]

Subcommittee on Government Efficiency, Financial Management and Intergovernmental Relations
Hearing Date: March 13, 2002
Subject: The Use and Abuse of Government Purchase Cards
Congressman: Stephen Horn
Insert: Page 66, Line 1280

(The information follows):

On November 19, 2000, Ms. Tanya Mays entered on duty with the Department of the Army by accepting a temporary appointment, not to exceed one year, as a Budget Analyst, GS-11, in the Office of the Assistant Secretary of the Army (Financial Management and Comptroller) (OASA(FM&C)). Prior to joining the Army, Ms. Mays worked for the Department of the Navy as a Budget Analyst, GS-11, in San Diego, California. Ms. Mays was competitively selected for the temporary appointment. She subsequently competed and was selected for a permanent GS-12 Budget Analyst position in October 2001. The selecting official was unaware of any allegations of charge card abuse/misuse by Ms. Mays.

Senior Army officials first learned of allegations of Ms. Mays'credit card abuse/misuse from inquiries by the Office of the Secretary of Defense and Senator Grassley's Office during the week of March 4, 2002. Currently, Department of the Army officials are reviewing documentation related to the allegations of credit card abuse/misuse. In the event that this review discloses any misconduct, civilian personnel and legal officials will advise management on the range of administrative actions available to them.

Ms. JONAS. But the assistant U.S. attorney apparently declined to prosecute, and I am uncertain at this moment—you know, I've heard two different facts on this, but I don't know whether it was because of the threshold or whether it was because of a lack of facts.

But I am very concerned about that case. I know Sandra Pack, who is the Army Comptroller, who is new to the building, also just found out about this case. So we are very well aware of that case. We are trying to look into that and see what we can do.

Mr. HORN. Well, I am sort of bemused that the Navy got away with passing off some of its people on the Army. I can't imagine the Army doing that and accepting it, but they probably didn't know a thing about it.

Ms. JONAS. Right, yes, Mrs. Pack recently came into this job and it is one of the things that she inherited, but she is very well aware of it and personally assured me that she is talking with her General Counsel on ability to act against this person.

Mr. HORN. Mr. Kutz and Mr. Ryan, who is the special investigator, do you have any comments on this situation?

Mr. RYAN. The case was originally investigated by NCIS and presented to the U.S. attorney. They declined prosecution.

Mr. HORN. Now which U.S. attorney was this?

Mr. RYAN. The one in San Diego.

Mr. HORN. San Diego. Now do they have some sort of dollar equivalent? I have seen that with some U.S. attorneys, "Oh, we can't be bothered with this." I mean, what do we have to do, let somebody steal $2 million? I mean it all adds up when you've got little things going. But you need to have an example.

Mr. RYAN. Well, they have prosecutive decisions and they make——

Mr. HORN. What was their criteria for not taking the case?

Mr. RYAN. I don't know. They just decided that they weren't going to prosecute the case. I think we would have to ask the U.S. Attorney's Office in San Diego to explain their decision.

Mr. HORN. And I would like the staff to deal with the Attorney General on this and see what the criteria is and why they're not doing something about it. Do we have any of these cases anywhere else in the United States where a U.S. attorney has been given it and has just said, "Sorry, I've got other things to do?"

Mr. RYAN. Decisions on prosecution in judicial districts is a decision that is made by the U.S. attorney. The investigators present the facts, and a decision to prosecute is left with the Department of Justice. Each judicial district, from my experience, being an agent with Secret Service for over 20 years, makes up their own mind, have their own criteria, and they decide whether or not they are going to prosecute or not prosecute. It really lies with the Department of Justice.

Mr. HORN. Mr. Kutz, when the General Accounting Office discovers some of these things, and it isn't just this case, but it is all over the country, does the GAO turn it over to the U.S. attorney?

Mr. KUTZ. We oftentimes refer it to Agent Ryan, who does further investigative work, and also will work up a case and then forward it to the Navy Criminal Investigative Service or another investigative group in the Department of Defense, who would then

present it to the U.S. attorney for prosecution. That is, indeed, what happened with the case you just described, Mr. Chairman.

Mr. HORN. How many cases have you referred to Mr. Ryan?

Mr. RYAN. Since I've been at GAO?

Mr. HORN. Yes, and how many are accepted?

Mr. RYAN. I really can't give you a number on the number we referred. We get a lot of information sent to GAO's BroadNet, allegations of fraud and abuse. We look at them. We interview the people making the allegations. We will build a case to a certain level, pass it onto the investigative body, either within the military or in the Executive side, the FBI or the Secret Service, for them to followup on the cases also.

Mr. HORN. So you expect the Department of Defense in this case or the Department of the Navy to put those papers before the U.S. attorney?

Mr. RYAN. I believe that's the best way to present it, yes.

Mr. HORN. Does anybody in GAO say, "We don't want to be bothered with that?" Or do they let you do what you think your conscience does——

Mr. RYAN. GAO is very proactive, ever since I have been at GAO, in pursuing, building-up these type of cases, developing the information, and making sure that the investigative bodies are fully aware and briefed. We make all our work papers and all our interviews available to the investigative bodies.

Mr. HORN. Captain Miller, you have been put on this job. What day did you take over?

Captain MILLER. Sir, I assumed command on Saturday, December 8, 2001.

Mr. HORN. Did you know what you were getting into? [Laughter.]

Captain MILLER. Unfortunately, yes, sir.

Mr. HORN. I'm curious, could you explain what the GAO found where you got a highly sophisticated staff of scientists using four toy robots to assist them in their work, and I'm just curious, are they toys? They cost the taxpayers $800, I believe. Are they in the Navy's possession? Do they have a use for whatever the Navy is working on?

Captain MILLER. Mr. Chairman, the items in question, the purchaser felt that they had a valid government use. I personally can't see that. That, to me, is one of those cases of poor judgment. But the bottom line is we did not have good management controls in place, and we did not have proper oversight, or that purchase would never have been made.

Mr. HORN. What about the various items of clothing and expensive handbags and daybook holders that the GAO put up on the charts? Are they listed in your inventory and are they under your control? Can other employees use them?

Captain MILLER. No, sir, they cannot use them. Those were purchased for personal reasons. I acknowledge the GAO's findings on that. Again, it boils down to poor management controls and poor oversight. We have taken positive steps, I believe, since December 8th to ensure that our training has been completed. All cardholders and approving officials understand their responsibilities, and I believe that we should see improvements.

Mr. HORN. Captain Barrett, do you and Captain Miller work out some of the things that need to be done in both those commands, or are we doing it each separately in terms of accountability, in terms of inventory, in terms of following-up on this kind of thing?

Captain BARRETT. Mr. Chairman, it has been a relatively separate effort on our behalf. Our problems tend to be internal in nature. I won't argue that there are opportunities for lessons learned, and we will see if we can't increase that dialog in the future.

Mr. HORN. Mr. Kutz, what would happen if someone in the private sector misused or fraudulently used their corporate card in this manner? Do you know any cases, any contractors, so forth?

Mr. KUTZ. No. What we did look at was for your hearing last summer in July, we looked at the number of cardholders or percentage of employees that held purchase cards at private sector corporations and found no more than 4 percent in large defense contractors. Now, again, they do different business than someone like SPAWAR, who has a lot of small projects. So I can see SPAWAR probably needing more credit cards, but I think that the industry standard is certainly that there are a lot less credit cards in the hands of people, and that was one of the things I will acknowledge that the Navy took significant action on since your last hearing.

They had, at the beginning of 2001, 47,000 Navy purchase cards outstanding, and as of September 30, 2001, they were down to 27,000. So I think the recommendations we had and the hearing you had had a positive impact on Navy, and they took that issue seriously.

I certainly believe that you would find stronger internal controls in the private sector over the usage of credit cards, and probably the disciplinary actions would be more swift and significant than what we have seen at the Department of Defense.

Mr. HORN. Ms. Jonas, in your role as Deputy Under Secretary for Financial Management, the Department of Defense has begun offsetting wages to repay delinquent travel card bills. That is correct, is it?

Ms. JONAS. That is correct, yes.

Mr. HORN. Would it be possible to have a similar salary offset for the purchase card program for cases in which the government has inadvertently paid the bill for personal items?

Ms. JONAS. That might be very appropriate in this case. If I can get back to the committee, we will look into it, and if that is appropriate. I will say the offset program for the travel card we hope to have a very beneficial effect. So far, we have collected about $21 million.

In this we think it will be a significant deterrent, and we have to do more to deter people, send the signal from the various high levels that this is not going to be acceptable, and if you abuse a card, whether it be a travel card or a purchase card, we will be there and you will be paying for these things out of your own pocket, not out of the government's pocket.

[The information referred to follows:]

Subcommittee on Government Efficiency, Financial Management and Intergovernmental Relations
Hearing Date: March 13, 2002
Subject: The Use and Abuse of Government Purchase Cards
Congressman: Stephen Horn
Insert: Page 73, Line 1466

(The information follows):

Salary offset is a process applicable to travel charge cards, where any debt incurred is a debt of the individual, not the government. Salary offset allows a travel charge card issuing bank to collect those private debts incurred on a government travel charge card by deduction from the cardholder's pay.

Under the government purchase card, however, the government generally is liable for purchases made by an authorized cardholder. Use of a government purchase card for a private purpose constitutes a misuse of the card, and their exist a variety of methods, criminal, civil, and administrative, through which the Department can seek restitution.

As an additional deterrent, new legislation currently in the FY 2003 Defense Authorization Bill passed by the House of Representatives and also contained in the Senate Armed Services Committee Report, will allow the Department to designate purchase cardholders in writing as accountable officials. As such, purchase cardholders will have pecuniary liability for errors, omissions, or untruthful statements related to their monthly purchase card statements.

Mr. HORN. I am going to yield now 10 minutes to the ranking member for questioning.

Ms. SCHAKOWSKY. Thank you, Mr. Chairman. I want to just say that Americans right now have, correctly, a very high regard for the men and women in our Armed Services, the efforts by our military to protect us against terrorist attacks and now with Homeland Security. It would seem to me that this would be a special time of obligation on the part of every person associated with our Defense Department to make sure that not any of that money is squandered.

We are now going to be considering a budget that requests an unprecedented increase in the defense budget. I think that it is only appropriate that we scrutinize every dollar, every million dollars, every billion dollars. I think it was pointed out by Ms. Ryan that the financial disarray within the Defense Department has been criticized repeatedly. She mentioned the recent report. The DOD Inspector General found that in fiscal year 2000 alone $1.2 trillion in Department-level accounting entries "were unsupported because of documentation problems or improper because the entries were illogical or did not follow generally accepted accounting principles."

When we talk about the abuses today, it seems to me that we are talking about a culture, not just a problem here or there, but a culture that has to be changed. I am so grateful to my chairman for continuing and following-up on that July hearing and finding out exactly what has happened since then.

That is why I wanted to ask Ms. Lee, the pattern of abuse that we heard about today at SPAWAR was evident at our hearing last summer. Why did the Department do nothing to curb this abuse between last July and today? I mean, you sound very determined; everything is going to be changed. You had a lot of time to do that.

Ms. LEE. Yes, Ma'am. The Navy had committed to doing some particular changes. There was a change in command, as you know, from that timeframe. That does not make it acceptable. We have to be more vigilant both at the specific site level, but at the oversight level to make sure that this time we truly deliver those changes.

Ms. SCHAKOWSKY. I know you have detailed some things, and I hope that those will be sufficient, so that when we come back, Mr. Chairman, and look again, that something has really happened. Repeatedly, the Department has failed to meet the financial muster. So this is not the first time that we have heard things will be better. I guess I don't know any other way but to say firmly we absolutely expect them to be better.

I wanted to ask Ms. Jonas, according to officials at SPAWAR, items like digital cameras and personal digital assistants don't have to be put on an inventory, and there's no need to account for them if they are lost or stolen. Is that Navy or DOD policy?

Ms. JONAS. I believe that may be a Navy regulation. I will have to check our regs. But, in any circumstance, that is not acceptable. It is government property. Whether it is $1 or whether it is $2,500, it must be accounted for.

I know that in the Department we have little barcodes for all the equipment in our offices, etc., and people are responsible for those inventories. So I will get with the Navy Comptroller to look at their regulations, and we will review our own regulations on accounting for property.

[The information referred to follows:]

Subcommitee on Government Efficiency, Financial Management, and Intergovernmental Relations
Hearing Date: March 13, 2002
Subject: The Use and Abuse of Government Purchase Cards
Congressman: Stephen Horn
Insert: Page 76, Line 1530

(The information follows):

Department of Defense (DoD) policy establishes a dollar threshold for property accountability of $5,000, unless the item is classified or sensitive (in which case a property accountability record is mandatory). The DoD Components are permitted to establish accountability controls for other property costing less than $5,000, if deemed appropriate for property management purposes or for property that is considered pilferable. Pilferable items are defined as those that have a ready resale value or application to personal possession and which are, therefore, especially subject to theft. It is not strictly mandatory for all pilferable items to be placed on property records.

Department of the Navy (DON) policy, which was revised on August 1, 2001, requires that all pilferable items be recorded and tracked in a compliant personal property system approved by the DON. Pilferable personal property is defined in DON policy as an asset, regardless of cost, that is portable, can be easily converted to personal use, is critical to the activity's business/mission, and is hard to repair or replace. This revised policy is not prescriptive in identifying what is pilferable but rather provides commanders latitude in determining what is and what is not pilferable.

Citing the "hard to repair or replace" criteria in the new policy, the Space and Naval Warfare (SPAWAR) Systems Center San Diego (SSC SAN DIEGO) developed and issued, on November 1, 2001, internal command guidance on property accountability. This guidance states that only computer systems and notebook/laptop computers, which are considered to be critical to fulfilling the activity's mission/business objective and are hard to repair or replace, be reported as pilferable items in the property records. Based on this determination, SSC SAN DIEGO no longer considers items such as cell phones, pagers, digital cameras, tools, and personal digital assistants (PDAs) to be considered pilferable. The General Accounting Office (GAO) believes this policy subjects such items to possible theft, misuse, or transfer to personal use. SSC SAN DIEGO's new Commanding Officer and Executive Director told GAO that they do not believe that it is cost beneficial to account for and track these assets, and rely on supervisory oversight and personal employee trust for the necessary accountability for such items.

The local policy at SSC SAN DIEGO contains a category of "sub-minor" property. These are items below the $5,000 threshold not meeting the pilferable criteria or that have a recovery period of less than 24 months. The local policy lists personal printers, scanners, cameras, TVs/VCRs, test equipment, and PDAs as examples of sub-minor property. Such property, although not recorded in property accountability records, is required to be labeled with a "Navy Property" sticker. This practice is intended to serve as a constant reminder to employees that these items are for official government use only and remain the property of the federal government.

Ms. SCHAKOWSKY. Because officials are using that as an excuse for the loss of these items. So are you saying that policy doesn't exist, that it will be changed, what?

Ms. JONAS. I will look into it to review Navy regulations, and my own personal view on this is that there is no excuse whatsoever, none.

Ms. SCHAKOWSKY. Does DOD have any regulations or guidance, something in writing, that would make it clear to employees that the purchase of luxury items like Coach briefcases is inappropriate?

Ms. JONAS. I believe Dee Lee, who is here with me, can discuss the specifics of what they put out on the purchase card. I don't know if you were here—well, I discussed in my testimony, but Dr. Zakheim and Under Secretary Aldridge have recently put out a letter on this, and what appropriate use of cards is, and strict guidance. We expect at the very top that be carried out.

Ms. SCHAKOWSKY. I mean, it would seem obvious that one doesn't use a government card for breast enhancement or Hooters, or whatever. So I don't know how one would actually state that, but are you saying to me that, until now, it hasn't been made explicit, that there have not been guidelines, Ms. Lee?

Ms. LEE. Purchase of personal items is never acceptable. It is not acceptable now.

Ms. SCHAKOWSKY. Has that been written?

Ms. LEE. Yes.

Ms. SCHAKOWSKY. Has that been in guidelines?

Ms. LEE. They are for, as it shows on the card, "For official government purposes only." Purchasing any kind of personal item is not acceptable.

Ms. SCHAKOWSKY. So, in other words, no one should have been confused about that. So then nothing was in place to make sure that was carried out? Is that what you are basically——

Ms. LEE. The oversight was lacking. We certainly should——

Ms. SCHAKOWSKY. Or absent?

Ms. LEE. Or absent. We should have had a billing official who was looking at each individual's card and saying, "What are you buying? Why are you buying this?"—and taking immediate action.

Mr. KUTZ. Representative, we made a recommendation, based on the hearing last summer, that the Department come out with specific guidance on prohibited items, and they disagree with our recommendation. Ms. Lee is the one who signed that letter back to us.

So there was a specific recommendation by the General Accounting Office that they list out specifically prohibited items, because I think their guidance is very, very general now, and you could drive an aircraft carrier through it. I think that they need to have very specific guidance on some of these items that it is prohibited to buy. I don't think it would hurt to do that, but they did disagree with that recommendation.

Ms. SCHAKOWSKY. And, Ms. Lee, could you comment on that? Why would you disagree with that?

Ms. LEE. Well, we will certainly relook at that, but our general guidance was personal items are never acceptable. So if we need to be more specific on what is a personal item, we certainly will look at that.

Ms. SCHAKOWSKY. Well, obviously, someone was not getting it.

Ms. LEE. Yes, Ma'am.

Ms. SCHAKOWSKY. So I think that the imagination of those using the cards may make it hard to specifically list everything, because who "wudda thunkit" on some of these items that were purchased. Nonetheless, to reject as unnecessary on its face was patently untrue. Clearly, something was necessary. There must be something going on. The people feel that with impunity they can charge these things.

So I would hope that you would relook at that since it was a specific recommendation, and I appreciate your bringing that to my attention. I would hope that, rather than sending another letter declaring it unnecessary, that instead you would figure out the comprehensive list.

Let me ask you, I guess earlier you dealt with the issue of the former commander refusing a drug test and refusing a random car search, and trying to get, as I said in my opening statement, two subordinates to lie for him, and the fine was a $1,000 fine and he was allowed to retire. I am just wondering if this is typical punishment for someone who refuses a drug test in the Navy, Ms. Jonas.

Ms. JONAS. The Secretary of the Navy, obviously, you know, he has control over the civilians and the military. I certainly, if I were in his shoes, would be personally looking into this. I have talked to the Assistant Secretary for Research and Development, who is one of the senior officials in the Department of the Navy, about the specific case and expressed my concern. I have also personally talked numerous times to the Navy Comptroller on this. I think they are both very concerned about it.

In part, that concern led to the new direction, the new guidance, that Secretary Aldridge and Under Secretary Zakheim just put out. We are very concerned about this. I cannot explain to you how concerned we are about it. But I think with respect to specific actions taken by the Navy, I mean that is not within my purview, but if I were in his shoes, I would have no tolerance for that.

Ms. SCHAKOWSKY. Fortunately, the Secretary of Defense has invited the Illinois delegation to meet with him tomorrow, and these are some questions that I can bring up.

Let me, in the little time remaining, Ms. Lee, I have heard that you hold yourself out to the rest of the Federal agencies as leaders in providing business to the JWOD, the disabled vendors' support. I am wondering how you can hold yourself in the Department out as leaders when units like SPAWAR haven't even heard of JWOD and aren't using the—there's an example of that day planner there.

Ms. LEE. They're Javits-Wagner-O'Day, and we call them NIB NISH, National Institute for the Blind and National Institute for the Severely Handicapped, and do have products that are mandatory source or at least first preference for the government to buy certain items. Among them are such things as day planners, pencils, pens, etc.

That is being addressed again in our training program. Our contracting folks here know that. Again, SPAWAR is an unacceptable situation, and we have to remedy it.

Ms. SCHAKOWSKY. Mr. Chairman, if I could just make one more remark—in addition, as part of our budget, we are also going to be

looking at the reauthorization of the TANF or welfare program. I would guarantee that we are going to spend more time looking at every nickel that is spent that may be overpaid to a welfare mom out there trying to raise a couple of kids, and I am not excusing fraud or abuse anywhere, but it just seems to me, then, when we look at a department that has asked for $400 billion, more than $1 billion a day, to be spent, then we had better pay attention to make sure, especially at a time when our Nation is threatened, to look at every single penny. Thank you.

Mr. HORN. I thank the ranking member.

Let me note—which one do you think, because we are going to close it down soon? But, Mr. Kutz, Senator Grassley and the subcommittee have asked you to broaden your examination of government purchase cards to other areas of the Department of Defense. I would not ask you to discuss this work in any particular detail. However, I will ask you whether you are finding similar misuses or fraudulent use of purchase cards in other areas of the Department of Defense or in other Cabinet departments.

Mr. KUTZ. Within the Department of Defense, I think, as you see today, the actual rubber hits the road far, far outside the Beltway. So the policy memos that come out from Headquarters oftentimes are not that well-distributed or known by people. So I think you are going to see, I guess, inconsistent application and inconsistent controls across. Some will be doing well and others are going to be more like SPAWAR. I think we are going to see a lot of interesting things in upcoming reports.

Again, you are talking about 230,000 people holding purchase cards, and as Senator Grassley talked about, almost 2 million people holding travel cards. That is a large program to control. Again, one of the things that we are looking at for both of those programs is controlling the number of cardholders out there, and particularly with respect to the travel card, looking at the issue of the credit checks, because really the credit checks is a key control in looking at travel cards.

Mr. HORN. Well, the purchase card is certainly different than the card that any of us as government officials use in our travel for the actual ticket of the airplane and based on the per diem limits. One can eat anywhere they want for lunch, breakfast, you name it. That, to my knowledge, doesn't get really very exposed one way or the other, and it is nobody's business where they eat. So that is not the problem. But can they use that interest credit card to substitute for the ones we change and have in our wallet?

Mr. KUTZ. They look just like—I mean, I showed you earlier this card here. This is the purchase card. I have a travel card myself that I am supposed to use when I am on government travel. They just look like a normal credit card. So you could actually easily make a mistake if you pulled it out of your wallet and inappropriately use it without intentionally misusing it.

But it is accepted at many vendors. One of the things that the Department has done and the banks have done is used what is called the MCC codes to block certain vendors. That is a control that is limited, but it is sometimes effective, preventing people from going to certain stores and types of vendors.

But, again, the travel card you are talking about, there's actually two types of travel card. There's the individually billed card like the one that I have, where the bill comes to my home and I pay it myself, and then there's also centrally billed accounts, which large plane tickets are put on and other travel is put on. So that is a lot more like the purchase card, and we are actually looking at those two programs separately.

Mr. HORN. In our case here in the Congress, we might use that or our own different one, Mastercard. Now the one the Congress has is the Visa card. We file the papers that we took the plane thing and the food, and all that, and that goes back through our Office of Finance. If there's something screwy about it, they let us know. Sometimes it happens where one of your staff members does that, but they certainly don't get into this business of the interest cards that we are talking about with the Navy here.

Do we know there is that type of abuse throughout part of the executive branch or what? How is GAO dealing with it?

Mr. KUTZ. The other agency we have looked at comprehensively is the Department of Education, but their program is extremely small compared to the Department of Defense. The whole Department of Education's program would be about the same as each one of the Navy units we are talking about here. But there were significant findings of fraud and abuse that the General Accounting Office reported out of the Department of Education.

We are planning to look for this subcommittee at several other executive branch agencies, and we will report back on what we find in other agencies.

Mr. HORN. I think the Education Committee certainly has looked at this in terms of the debt that has been created in education.

Mr. KUTZ. They were planning a hearing today actually, and it has been postponed, but they are going to have another one on their purchase card at Education.

Mr. HORN. Now listening to all this, do you think that the transaction level ought to move from $2,500 to $25,000, which is in a bill of my colleague, Mr. Davis? Ms. Lee was one of the witnesses, and so forth. We raised these questions in that particular area. What would GAO recommend?

Mr. KUTZ. I don't think it would be necessary to give all 230,000 purchase cardholders at the Department of Defense a $25,000 micro-purchase limit. That does not seem to be reasonable. Would it make sense to have a small group of tightly controlled cards have that? Yes, that might make sense for the war on terrorism or whatever need they may have to have the larger micro-purchase limit. But I would express significant caution to the subcommittee and the Congress with respect to just doing this, giving the DOD a blanket 230,000 cards with a $25,000 micro-purchase limit.

Mr. HORN. Well, I would think that those that have to—we used to say, if the officers didn't get a good Master Sergeant, they didn't get very far. Those that are in supply and procurement, when they need to do something on the military side, then, obviously, that level would be maybe not enough. But somehow it ought to be with a signoff of somebody when they review the paper.

Mr. KUTZ. The Department currently has some cards that have $25,000 single transaction limits to pay for things such as training,

and they also have some $100,000 cards that are used for small purchases on contract basically. So there is currently a procedure where they have certain cards with higher limits. Now, again, that is a little bit different than what you are talking about, which it sounds like it is giving the entire Department a $25,000 micro-purchase for all the cards.

Mr. HORN. So what are you going to do with that, Ms. Lee? If the bill goes through, Mr. Davis', are there going to be blanket $25,000 cards?

Ms. LEE. If the bill passes, obviously, we will have to put it in place with strong oversight and make sure that we do all these things we talk about for the cards, regardless of the limit.

Mr. HORN. Well, that is good to know, but we will just have GAO looking every other month, right?

So are there any other things you would like to say, any of you presenters, on the record? Please tell us. If you say something's hogwash, I would like to clarify it. So any of you want to? GAO, any comments? Navy?

Captain BARRETT. No, sir.

Mr. HORN. Department of Defense?

Ms. JONAS. Mr. Chairman, I would just like to say a lot of people say they don't want to come up and testify, but this sunshine really does help us. I mean, as you notice and as the Congressman noted, it is a big cultural change for the Department. There is a lot of education that has to go on. A lot of people really truly don't understand what the responsibilities are of having a card. We need to get the message down to the very lowest levels. As Greg mentioned in his testimony, sometimes it is very hard to get the message out from the highest levels to the lowest levels, but we are committed to doing that. We really appreciate your work here at this committee, and we will do our level best to try to correct many of these problems.

Mr. HORN. Yes, I got a bill through on transitions between Presidencies, and they have various types of material that they bring to not just the Cabinet members, but also the various 300 to 3,000 Presidential appointees, especially Assistant Secretaries, and so forth. So they would be looking at the ethics, which has bogged down every administration, because it takes so long to fill out the forms and all the rest of it. But somehow we've got to get that into those that get these very honored appointments.

Yes?

Ms. SCHAKOWSKY. Ms. Jonas, I just want to respond to what you said, that it is clear that there are too many people who don't understand how those cards can be used. I think they understand perfectly. I think what they understand is that they can get away with these kinds of purchases. I don't think that anyone in their right mind would think that they could take a government card and purchase these luxury items. What they think is that I can do it and I can get away with it. I think there has to be a much harsher approach to this, that it is fraud and it is abuse, and it has to stop. If they don't understand, then they have no place in our Armed Services, in our Defense Department.

Ms. JONAS. I would agree. I didn't mention this in my testimony. One of the things that we are looking at, and are in discussions

with OMB, is a legislative proposal to hold accountable officials financially liable. We hope to be sending that over to you. But I think that would be another significant deterrent, including the offset. I apologize if I—I think my comments were meant to intend that we need to do a very good job at letting every individual in the Department, every military officer, every civilian who has this privilege know exactly, clearly, unambiguously, what the responsibilities are with the card.

Ms. SCHAKOWSKY. And what the consequences will be.

Ms. JONAS. Absolutely, yes.

Ms. SCHAKOWSKY. Thank you.

Mr. HORN. That's good news. It looks like you are getting things done. I have great affection and feelings for the Secretary of the Navy. He is a first-rate person. Does he know about all this? Anybody in Defense, DOD, say, "Mr. Secretary, you ought to know what's going on in your Navy?"

Ms. LEE. We have been talking with John Young, who is the AT&L for the Secretary. I don't know his personal conversations——

Mr. HORN. Stop the bureaucracy bit. ATL?

Ms. LEE. Oh, Acquisition, Technology and Logistics.

Mr. HORN. Yes. Well, we humans up here don't always know this stuff, and we know the rigmarole that tries to get past us. [Laughter.]

But that is why I stop on everything——

Ms. LEE. Been here too long already, huh, Mr. Chairman?

Mr. HORN. Yes. Stovepipe is my other beef in the bureaucracy.

But, anyhow, I think the Deputy Under Secretary has got it moving in the right place, but I would think the Secretary of the Navy ought to know this is going on and not be blindsided when he comes up here for the Armed Services or whatever.

I thank you very much for that.

I am going to thank the following people who put together this interesting hearing: J. Russell George is the staff director and chief counsel, right behind me; Bonnie Heald, to my left, is the deputy staff director, that put the hearing together. Justin Paulhamus is the majority clerk, and Michael Sazonoff is the subcommittee intern. We have our court reporter, Joan Trumps. We thank you all for helping us on this.

Ms. SCHAKOWSKY. And we thank David McMillen for his help.

Mr. HORN. Thank you. With that, we are adjourned.

[Whereupon, at 11:45 a.m., the subcommittee was adjourned, to reconvene at the call of the Chair.]

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