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# THE USE AND ABUSE OF GOVERNMENT PURCHASE CARDS: IS ANYONE WATCHING?

## 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: IS ANYONE WATCHING?

**MONDAY, JULY 30, 2001**

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 10 a.m., in room 2154, Rayburn House Office Building, Hon. Stephen Horn (chairman of the subcommittee) presiding.

Present: Representative Horn.

Staff present: J. Russell George, staff director and chief counsel; Bonnie Heald, professional staff member and director of communications; Scott Fagan, assistant to the subcommittee; Chris Barkley, staff assistant; Davidson Hulfish, Samantha Archey, Fred Ephraim, and Christopher Armato, interns; David McMillen, minority professional staff member; and Jean Gosa, minority assistant clerk.

Mr. HORN. This hearing of the Subcommittee on Government Efficiency, Financial Management and Intergovernmental Relations will come to order. For the last 6½ years, I have chaired the subcomittee that ensures that taxpayer dollars are being used efficiently and effectively. Yet time after time this subcommittee has received reports that Federal departments and agencies have not been good stewards of billions of dollars provided by hard-working taxpayers. Sometimes the allegations have been attributed to poor accounting procedures. Other times they have been attributed to flagrant mismanagement. In the case of the Department of Defense, there seems to have developed a culture throughout previous administrations that encompasses both of these elements.

This is the second time in less than a week that representatives from the Department of Defense have appeared before this subcommittee to defend illegal or otherwise improper uses of its roughly $325 billion budget. Last week we learned that some Defense Department officials have been illegally tapping closed appropriations accounts despite a 10-year-old law that prohibits such actions.

Today we will examine the government's purchase card programs at two Navy units within the Department of Defense, the Space and Naval Warfare Systems Center and the Navy Public Works Center. Both are based in San Diego, CA. This investigation was initiated by our first witness, Senator Charles Grassley from Iowa. Our second witness will come from the General Accounting Office.

Last year the Department of Defense used purchase cards, MasterCards or VISA cards, for more than 10 million transactions valued at $5.5 billion. That figure represents more than one-third of the entire government's purchase card transactions, which totaled $15 billion in fiscal year 2000. Unlike the government's travel card program in which the cardholder pays the bill, the purchase card bills are paid by the Federal Government.

This credit card program was designed to save money by eliminating bureaucracy and paperwork associated with making small purchases. As defined by the General Services Administration, small purchases are those under $2,500. In addition, Federal agencies can receive rebates from the banks that issue the cards when the bills are paid promptly. Those benefits, however, do not consider the cost of fraudulent or improper use of the cards for personal expenses, and in the cases we will examine today, they fail to consider the cost of proper oversight and management of the programs. Most reasonable people would hardly construe these as legitimate and necessary government expenses, and all taxpayers would agree.

Senator Grassley and I have asked the General Accounting Office to expand its investigation of the government purchase card program as well as the travel card program. If the misuse and outright fraud found in these two Navy facilities are indicative of the governmentwide programs, then the cost of the programs may far outweigh its benefits.

Our witnesses today have been involved in the implementation and oversight of the government's purchase card program. In addition, we will hear testimony from witnesses who are responsible for the two Navy purchase programs audited by the General Accounting Office. We want to know how these abuses were allowed to occur and what is now being done to stop them.

I welcome all of you, and we now look forward to your testimony. We will start with the gentleman from Iowa, Senator Grassley, who is the one that first picked this up, and he's got a very good reputation for looking at misuse of the taxpayers' money. We are delighted to have him with an opening statement, and we would like him to come with us when that statement is over and join us here for the question period.

And it is a pleasure to have you here, Senator.

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

Senator GRASSLEY. Thank you, Mr. Chairman, and I want to compliment you for doing a thorough job of our Constitutional responsibilities of oversight to see that money is spent according to the Constitution and congressional policy, and to make sure that the laws are faithfully executed. I'm glad to join you in that effort. And so I thank you for inviting me to testify on credit card abuse. It's an honor and privilege to be here, and especially to work with you on a very important issue.

As the chairman knows, in recent years I have become increasingly concerned about the total breakdown of the internal financial controls at the Defense Department. My concerns are reinforced by the continuous stream of audits issued by the General Accounting

Office and the DOD's Inspector General. These audits consistently show that sloppy accounting and nonexistent internal controls leave the Department of Defense's financial resources vulnerable to theft and to abuse.

In 1997–1998, as chairman of the Judiciary Subcommittee on Administrative Oversight, I conducted my own review of internal controls at the Department of Defense. I issued a report and held a hearing. I came away from the experience convinced that there were no effective internal controls in place. Stealing money was a piece of cake. Fraudulent activity, if detected, was detected by chance and not, oddly enough, as a result of effective internal controls.

This work taught me one very important lesson about government bookkeeping. Bookkeeping is the key to controlling the money. If your books of account are accurate and complete, it's easy to follow the money trail, and that makes it hard then to steal money, and that's how it should be. By contrast, if your bookkeeping is sloppy and nonexistent, as it is at the Pentagon today, then there is no money trail, and that makes it easy to steal money. And that's exactly why I'm so concerned about the Pentagon's mushrooming credit card operation. Credit cards weaken controls, erase the audit trail.

Mr. Chairman, I'd like to focus on the dangers of credit card proliferation in what I will characterize as a zero-control environment. Today there are over 1.8 million Department of Defense cards in circulation that generate about $9 billion a year in expenditures. A credit card is a license to spend money. Any person with a credit card is authorized to spend money with no checks and balances. In the past, Department of Defense employees needed a phony invoice to trigger a fraudulent check, and getting a fraudulent Treasury check took some doing. Well, now that obstacle is gone. Credit cards then provide a shortcut to the cash pile. The Pentagon is giving everyone a big scoop shovel and telling them to rip into the national money sack and do it at both ends.

The Department of Defense created an army of spenders. With the Department of Defense credit card in hand, they have almost unlimited authority to spend money. There are no controls, no responsibilities, no accountability. If they want to spend money, they go to the nearest ATM machine or use a DOD convenience check to get cash, and they're doing it with alarming regularity. If they need a new computer or a Palm Pilot, they go to CompUSA and charge it and keep it. If they need something for the house, they go to Home Depot and charge it. If they feel like a night out on the town, they go to a night club and charge it. Pentagon credit cards are being taken on a shopping spree, and the taxpayers are footing the bill.

The General Accounting Office testimony today, I think, will clearly show that no one is minding the store. No one is checking to see if the goods and services charged to a purchase card account were received. And no one is checking to verify the charges if they were legitimate, and that is required by law.

The General Accounting Office reports that purchase cards are being used to buy expensive items for personal use with no accountable records. There were over 500 known purchase card fraud

cases in the last 2 years alone, and with just a small sample, the General Accounting Office found more. The worst part of it, Mr. Chairman, is no one seems to care. The Defense Finance and Accounting Service simply pays the bill in full, no questions asked.

Mr. Chairman, I know you have looked at the Department of Defense travel cards, and they remain a festering problem. They need more attention. And they offer us a rare glimpse at a root cause of the Department of Defense control problem. As I said, credit cards are a license to spend money, and they're being issued with no road test. They're being issued willy-nilly, with no credit checks.

Mr. Chairman, that may sound like that's got to be wrong, but that's true. There are no credit checks. Even purchase cards with a $100,000 limit are issued with no credit check. One credit card company, the Bank of America, identifies high-risk individuals, but the bank's appraisal in the case of the military is irrelevant. At the Pentagon, everyone gets a card.

This is a fatal flaw in the program. It leaves the door wide open to fraud and abuse. Military and civilian personnel who could never qualify for credit suddenly find themselves with unlimited credit on a government credit card.

The application form itself helps to set the stage for fraud and abuse. It's right up front on the application. No credit check is an option, and all the applicant has to do is check box B, "no credit check." When first-time cardholders see this, they must lick their chops, obviously.

No credit check is the same as no control. A "no credit check, everybody gets a travel card" policy is causing account delinquencies to go ballistic. As you know, Mr. Chairman, there are over 43,000 Department of Defense employees, civilian and military, who have defaulted on more than $59 million in charges for what is supposed to be authorized travel. This, of course, is a black mark on the Armed Forces. The Department of Defense is supposed to pay the cardholder, but the money doesn't always get to the bank. The government has no liability for unpaid balances, and the bank has no collection authority and earns no interest. The bank has to write off the delinquencies, thus take a loss, and the losses are mounting fast. They now exceed $200 million.

There is the case of the marine sergeant who ran up a $20,000 bill and then left the service and the unpaid bill when his enlistment was up. That case is not unique. There is a soldier who spent $3,100 in a night club, the dead sailor who spent $3,565, an Army reservist's wife who spent $13,053 on a shopping spree in Puerto Rico.

The marine sergeant, Sergeant X, was initially issued a restricted card in March 2000 because of a questionable credit record. The restricted status put the lid on Sergeant X's credit allowance, but not for long. On March 21st, the Marine Corps arbitrarily raised his credit limit from $2,500 to $10,000. The higher limit precipitated a spending spree. Then the alarm bells went off at the bank. There was a fraud alert on August 3rd due to, "unusual account activity."

Two weeks later Sergeant X got special permission to make charges on a blocked merchant category code [MCC], at a civilian clothes store like Macy's. The next day, August 18th, Sergeant X's

credit limit was raised again to $20,000. Then Sergeant X's account became past due and then delinquent.

Now, despite all the red warning flags, the Marine Corps raised Sergeant X's credit limit one last time, January 29, 2001. This time it went to $25,000.

In just one 2-month period, Sergeant X made cash withdrawals totaling $8,500. The bank thinks he was using the cash withdrawals to make payments on his credit card account. Finally, in February, Sergeant X's credit was revoked. Mr. Chairman, the Marine Corps was warned, but looked the other way while Sergeant X robbed the bank.

Mr. Chairman, I hope you will join me in asking the Inspector General to examine these cases and determine whether the Department of Defense is paying for unauthorized expenses and whether others could be involved in stealing money. The driver behind the delinquencies are cash withdrawals from the ATM machines for personal use. Over 20 percent of all Department of Defense travel card transactions are cash transactions. Now, this is five times the industry average. Most cash transactions go delinquent and are written off as bad debt.

Attempted access to blocked MCC codes like Sergeant X's case is a tip-off. It's the warning flag. Many MCCs are blocked, like online gambling casinos, Toys R Us and the like. The bank knows when a card is used to gain access to a blocked MCC code. The banks also know that an unsuccessful hit on a blocked MCC code is almost always followed immediately by a successful hit at the nearest ATM machine. ATMs are used to circumvent the blocked MCC code to make an unauthorized purchase.

Mr. Chairman, the bank gave the Pentagon an antifraud control device. It's called by the acronym EAGLS, E-A-G-L-S. It provides an online capability to detect suspicious account activity and delinquency; information needed to take corrective action, in other words. Daily account activities on EAGLS should be watched like a hawk. If Sergeant X was getting cash at the ATM machine without travel orders, his access to the cash machine should have been shut down. Unfortunately, EAGLS control is ignored. Nobody uses it.

The thinking behind the Department of Defense credit card explosion is good. Reduce the paperwork. Save money to streamline the process. Adopt best practices of the commercial sector. In the private sector credit cards are big business. That's because the control environment is good. Monthly bills are reconciled and are paid promptly. In corporate America, if you abuse your card, you lose it or you get fired.

In the Pentagon there is no accountability and no control. Trust and accountability are key ingredients in any credit card program. Trust and accountability go hand in hand because a credit card provides direct unrestricted access to cash. Credit cards create a low-control environment. The credit card environment requires a high degree and level of trust and accountability.

Mr. Chairman, the low-control credit card environment is incompatible with the zero-control environment at the Pentagon. Issuing credit cards willy-nilly with no credit checks in a zero-control environment is a recipe for disaster, and that's exactly where we are

today, Mr. Chairman, a disaster, and Bank of America is holding the bag, and the bank can only blame itself for being in such a predicament. The bank signed the contract. The bank agreed to assume all the risk and all the responsibility, but with absolutely no authority. All the authority rests squarely in the hands of the Pentagon. The contracts give the Department of Defense absolutely vital authority over the bank's decisions. On the most important decisions of all, whether to do credit checks, the Pentagon is forcing the bank to adopt worst business practices of the public sector. The contract mandates the policy. There shall be no control filter with credit checks. Everybody gets a card, even those with bad credit records.

Mr. Chairman, the "no credit checks, everybody gets a card" policy allows the abuser to rob the bank, and the Department of Defense is backing them up. That is causing the bank to sustain unacceptable losses. Bank of America's predecessor, American Express, endured the same fate. So something has to give. It seems like the current arrangement is very unworkable.

I know that the Department of Defense is trying to fine-tune the process, but recent improvements are very modest. The root cause of the problem remains untouched: no control and no credit checks. If the Department of Defense is serious about adopting the best practices of the commercial sector, then the Department of Defense has to do an about-face maneuver. The Department of Defense must give the bank authority to decide who can be trusted with a card and what the credit limit should be on each account. This rule should apply to travel as well as purchase cards. I think that this would solve the problem. I think that is the key, Mr. Chairman. Modify the contract to allow credit checks and regulate limits. It seems to be very simple.

In closing, Mr. Chairman, Secretary Rumsfeld has made a personal commitment to clean up the financial mess at the Pentagon. Obviously, he is just getting started, and we know how things take several years, and it may be that is true with Secretary Rumsfeld's best efforts before we see results. I support his efforts 100 percent and look forward to some very good results. So nothing I have said here today should be taken as criticism of Secretary Rumsfeld. The problems I have addressed are the result of decisions made in previous administrations and mainly by former Deputy Secretary of Defense Hamre.

I thank you, Mr. Chairman.

Mr. HORN. We thank you, Senator, and please join us here.

[The prepared statement of Senator Grassley follows:]

TESTIMONY:

# DOD Credit Card Explosion: Front Door at Pentagon Is Wide Open on Fraud and Abuse

By

Senator Chuck Grassley
Ranking Member
Senate Finance Committee

Before

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

July 30, 2001

Mr. Chairman, I would like to thank you for inviting me to testify on Department of Defense (DOD) credit card abuse. It is an honor and privilege to be here and to work with you on this very important issue.

As the Chairman knows, in recent years, I have become increasingly concerned about the total breakdown of internal controls at the Defense Department.

My concerns are reinforced by a continuous stream of audits issued by the General Accounting Office (GAO) and the Inspector General (IG).

These audits consistently show that sloppy accounting and nonexistent internal controls leave DOD's financial resources vulnerable to theft and abuse.

In 1997-1998, as Chairman of the Judiciary Subcommittee on Administrative Oversight, I conducted my own review of internal controls at DOD.

I issued a report and held a hearing.

I came away from the experience convinced that there were no effective internal controls in place. Stealing money was a piece of cake. Fraudulent activity - if detected - was detected by chance and not as a result of effective internal controls.

This work thought me one very important lesson about government bookkeeping: Bookkeeping is the key to controlling the money.

If your books of account are accurate and complete, it's easy to follow the money trail. That makes it hard to steal money. That's how it should be.

By contrast, if your bookkeeping is sloppy or nonexistent - as it is at the Pentagon today, then there is no money trail. That makes it easy to steal money.

And that is exactly why I am so concerned about the Pentagon's mushrooming credit card operation. Credit cards weaken controls and erase the audit trail.

Mr. Chairman, I would like to focus on the dangers of credit card proliferation in what I will characterize as a zero-control environment.

Today, there are over 1.8 million DOD cards in circulation that generate about $9.0 billion a year in expenditures.

A credit card is a license to spend money.

Any person with a credit card is authorized to spend money with no checks and balances.

In the past, DOD employees needed a phony invoice to trigger a fraudulent check, and getting a fraudulent Treasury check took some doing. Well, that obstacle is gone.

Credit cards provide a shortcut to the cash pile. The Pentagon is giving everyone a big scoop shovel and telling them to rip into the national money sack at both ends.

DOD has created an Army of spenders.

With a DOD credit card in hand, they have almost unlimited authority to spend money. There are no controls, no responsibilities, and no accountability.

If they want to spend money, they go to the nearest ATM machine or use a DOD convenience check to get cash. And they are doing it with alarming regularity.

If they need a new computer or "Palm Pilot", they go to CompUSA and charge it - and keep it.

If they need something for the house, they go to Home Depot and charge it.

If they feel like a night out on the town, they go to a nightclub and charge it.

Pentagon credit cards are being taken on a shopping spree, and the taxpayers are footing the bill.

GAO testimony today will clearly show that no one is minding the store. No one is

checking to see if the goods and services charged to purchase card accounts were received. No one is checking to verify if the charges were legitimate - **as required by law.**

The GAO reports that purchase cards are being used to buy expensive items for personal use -- with no accountable records. There were over 500 **known** purchase card fraud cases in the last two years alone. And with just a small sample, GAO found some more. And the worst part about it, Mr. Chairman, no one seems to care.

The Defense Finance and Accounting Service simply pays the bills in full - no questions asked.

Mr. Chairman, I know you have looked at DOD Travel Cards, but they remain a festering problem. They need more attention, and they offer us a rare glimpse at a root cause of a DOD control problem.

As I said, credit cards are a license to spend money, and they are being issued with no road test. They are being issued "willy nilly" with no credit checks. That's right, Mr. Chairman, DOD cards are issued with no credit check.

Even purchase cards - with their $100,000.00 limit -- are issued with no credit check.

One credit card company - Bank of America - identifies "high risk" individuals. But the Bank's appraisal is irrelevant. At the Pentagon, everybody gets a card. This is a fatal flaw in the program. It leaves the door wide open to fraud and abuse.

Military and civilian personnel who could never qualify for credit suddenly find themselves with unlimited credit on a government credit card.

The application form itself helps to set the stage for fraud and abuse. It's right up front on the application. No credit check is an option. All the applicant has to do is check Box B -" No credit check."

When first-time cardholders see this, they must lick their chops. Not credit check equals no control.

A no-credit-check-everybody-gets-a-travel-card policy is causing account delinquencies to go ballistic.

As you know, Mr. Chairman, there are over 43,000 DOD employees - civilian and military - who have defaulted on more than $59 million in charges for what is supposed to be authorized travel. This is a black mark on the Armed Forces.

DOD is supposed to pay the cardholder, but the money doesn't always get to the Bank.

The government has no liability for unpaid balances, and the bank has no collection authority and earns no interest. The bank has to write off the delinquencies and take the loss. And the losses are mounting fast. They now exceed $200 million.

There is the case of the Marine Sergeant who ran up a $20,000.00 bill and then left the service – and the unpaid bill – when his enlistment was up.

That case is not unique. There is the soldier who spent $3,100.00 at a nightclub; the dead sailor who spent $3,565.84; an Army Reservist's wife who spent $13,053.24 on a shopping spree in Puerto Rico.

The Marine Sergeant -- Sgt. X -- was initially issued a **restricted** card in March 2000 because of a questionable credit record. The restricted status put a lid on Sgt. X's credit allowance - but not for long. On March 21st, the Marine Corps arbitrarily raised his credit limit from $2,500.00 to $10,000.00.

The higher limit precipitated a spending spree. Then the alarm bells went off at the bank. There was a fraud alert on August 3rd due to "unusual account activity."

Two weeks later, Sgt. X got special permission to make charges on a blocked Merchant Category Code or MCC at a civilian clothes store like Macy's.

The next day - August 18th - Sgt. X's credit limit was raised again -- to $20,000.00.

Then Sgt. X's account became past due and then delinquent.

Despite all the red warning flags, the Marine Corps raised Sgt. X's credit limit one last time on January 29, 2001. This time it went to $25,000.00.

In just one two-month period, Sgt. X made cash withdrawals totaling $8,500.00. The bank thinks he was using the cash withdrawals to make payments on his credit card account.

Finally February Sgt. X's credit was revoked.

Mr. Chairman, the Marine Corps was warned but looked the other way while Sgt. X robbed the bank.

Mr. Chairman, I hope you will join me in asking the IG to examine these cases and determine whether DOD is paying for unauthorized expenses, and whether others could be involved in stealing money.

The driver behind the delinquencies are cash withdrawals from ATM machines for personal use. Cash withdrawals total $500 million per year.

Over 20 percent of all DOD Travel Card transactions are cash transactions. This is five times the industry average. Most cash transactions go delinquent and are written off as bad debt.

Attempted access to blocked MCC codes, like in Sgt. X's case, is the tip off. It's a red warning flag.

Many MCC's are "blocked" – like online gambling, casinos, and Toys-R-Us and the like.

The Bank knows when a card is used to gain access to a blocked MCC code. The Banks also knows that an unsuccessful "hit" on a blocked MCC code is almost always followed immediately by a successful "hit" on the nearest ATM cash machine.

ATM's are used to circumvent the blocked MCC code to make an unauthorized purchase.

Mr. Chairman, the Bank gave the Pentagon an anti-fraud control device. It called EAGLS. It provides an on-line capability to detect suspicious account activity and delinquencies -- information needed to take corrective action. Daily account activity on EAGLS should be watched like a hawk.

If Sgt. X was getting cash at the ATM machine without travel orders, his access to the cash machine should have been shutdown.

Unfortunately, EAGLS control is ignored. Nobody uses it.

The thinking behind the DOD credit card explosion is good -- Reduce paperwork and save money. "Streamline" the process. Adopt "Best Business Practices of the Commercial Sector."

In the private sector, credit cards are a big success. That's because the control environment is good. Monthly bills are reconciled and paid promptly.

In corporate America, if you abuse your card, you lose it or get fired.

At the Pentagon, there is no accountability and no control.

Trust and accountability must be key ingredients in any credit card program. Trust and accountability go hand-in-hand because a credit card provides direct – unrestricted -- access to cash. Credit cards create a low-control environment. The credit card environment requires a high level of trust and accountability.

Mr. Chairman, the low-control credit card environment is incompatible with the zero-control environment at the Pentagon.

Issuing credit cards "willy nilly" with no credit checks in a zero-control environment is a recipe for disaster.

And that's exactly where we are today, Mr. Chairman, a disaster.

And Bank of America is holding the bag.

But the bank can only blame itself for being in such a predicament. The bank signed the contract.

The bank agreed to assume all the risks and all the responsibility with absolutely no authority.

All the authority rests squarely in the hands of the Pentagon bureaucrats.

The contract gives DOD absolute veto authority over the bank's decisions.

On the most important decision of all - whether to do credit checks, the Pentagon is forcing the bank to adopt the worst business practices of the public sector.

The contract mandates the policy: There shall be no control filter with credit checks. Everybody gets a card - even those with bad credit records.

Mr. Chairman, the no-credit-check-everybody-gets- a-card policy allows the abusers to rob the bank. And DOD is backing them up. This is causing the bank to sustain unacceptable losses. Bank of America's predecessor -American Express - endured the same fate.

Something has to give. The current arrangement is just unworkable.

I know DOD is trying to fine-tune the process, but recent improvements are very modest. The root cause of the problem remains untouched: No control and no credit checks.

If DOD is serious about adopting the best practices of the commercial sector, then DOD has to do an about-face maneuver. DOD must give the bank authority to decide who can be trusted with a card, and what the credit limits should be on each account.

This rule should apply to travel and purchase cards.

I think that would solve the problem. That's the key. Modify the contract to allow credit checks and regulate limits. It's that simple.

In closing, Mr. Chairman, Secretary Rumsfeld has made a personal commitment to clean up the financial mess at the Pentagon. He is just getting started, so it will be several years before we begin to see results. I support his efforts one hundred percent and look forward to some good results.

So nothing I have said here today should be taken as criticism of Secretary Rumsfeld.

The problems I have addressed are the result of decisions made by the previous administration - and mainly former Deputy Secretary of Defense Hamre.

Mr. HORN. And we will now bring all of the witnesses and administer the oath, and also we will tell you about how this—I would like all of the assistants that will be whispering in various ears to also take the oath so I don't have to interrupt this testimony, and so just get them all, and the clerk will take the names. Please raise your right hands.

[Witnesses sworn.]

Mr. HORN. So I just want to make sure we have all the witnesses here, and the first will be Mr. Kutz of the U.S. General Accounting Office, accompanied by Robert Hast, Managing Director, Special Investigations, U.S. General Accounting Office; Captain Ernest L. Valdes, Commander, Space and Naval Warfare Systems Center in San Diego; Captain John E. Surash, the Commanding Officer, Navy Public Works Center, San Diego; and Vice Admiral Keith W. Lippert, the Director of the Defense Logistics Agency, former commanding officer, Naval Supply Systems Command, and he is accompanied by Larry Glascoe, Executive Director of the Navy Supply Systems Command; Jerry Hinton, Director of Finance, Defense Finance and Accounting Service; Patricia Mead, the Acting Deputy Assistant Commissioner, Federal Supply Service, General Services Administration, accompanied by Sue McIver, the Director, Services Acquisition Center, Federal Supply Service, General Services Administration; and we have Deidra Lee, Director of Defense Procurement, Department of Defense.

And we will now start with the gentleman with the U.S. GAO, General Accounting Office. That reports, for those of you that are not familiar with them, to the Comptroller General of the United States, and it is an arm of the Congress, the legislative branch, and they do excellent work, and we're both—Senator Grassley and I have certainly made great use out of the GAO in our years in the Congress.

So we will now start in with Mr. Kutz, the Director of Financial Management and Assurance.

**STATEMENTS OF GREGORY D. KUTZ, DIRECTOR, FINANCIAL MANAGEMENT AND ASSURANCE, U.S. GENERAL ACCOUNTING OFFICE, ACCOMPANIED BY ROBERT HAST, MANAGING DIRECTOR, SPECIAL INVESTIGATIONS, U.S. GENERAL ACCOUNTING OFFICE; ERNEST L. VALDES, COMMANDING OFFICER, SPACE AND NAVAL WARFARE SYSTEMS CENTER, SAN DIEGO, CA (SPAWAR); JOHN E. SURASH, COMMANDING OFFICER, NAVY PUBLIC WORKS CENTER, SAN DIEGO, CA; KEITH W. LIPPERT, DIRECTOR, DEFENSE LOGISTICS AGENCY, FORMER COMMANDING OFFICER, NAVAL SUPPLY SYSTEMS COMMAND (NAVSUP), ACCOMPANIED BY LARRY GLASCOE, EXECUTIVE DIRECTOR, NAVY SUPPLY SYSTEMS COMMAND; JERRY HINTON, DIRECTOR OF FINANCE, DEFENSE FINANCE AND ACCOUNTING SERVICE; PATRICIA MEAD, ACTING DEPUTY ASSISTANT COMMISSIONER, OFFICE OF ACQUISITION, FEDERAL SUPPLY SERVICE, GENERAL SERVICES ADMINISTRATION, ACCOMPANIED BY SUE McIVER, DIRECTOR, SERVICES ACQUISITION CENTER, FEDERAL SUPPLY SERVICE, GENERAL SERVICES ADMINISTRATION; AND DEIDRA LEE, DIRECTOR OF DEFENSE PROCUREMENT, DEPARTMENT OF DEFENSE**

Mr. KUTZ. Mr. Chairman and Senator Grassley, good morning. It's a pleasure to be here to testify on the results of our audit of Navy purchase cards. With me this morning is Bob Hast, Managing Director of our Office of Special Investigations and an expert in credit card security issues.

Purchase cards were introduced into the government in the 1980's primarily to streamline the acquisition process for small purchases. Usage of purchase cards is growing quickly in the Federal Government, increasing from about $2 billion in 1995 to about $12 billion in 2000. DOD purchase cards usage in fiscal year 2000 was about $5 billion.

With rapid growth in the usage of purchase cards, establishment of effective internal controls is critical to prevent fraud, waste and abuse. I have a purchase card in my hand here that Citibank was kind enough to provide for today's hearing. As you can see, it looks like a normal credit card. Navy's card is a MasterCard and can be used wherever MasterCard is accepted; however, notice that it says, "For official U.S. Government purchases only."

As requested initially by Senator Grassley, our audit focused on Navy purchase card activity in the San Diego area using a case study approach at SPAWAR Systems Center, or SPAWAR, and Navy Public Works Center, or Public Works. These two Navy activities, which provide goods and services to their Navy clients, had about $68 million of purchase card activity in fiscal year 2000.

The bottom line of my testimony this morning is that we found significant breakdowns in Navy purchase card controls in the San Diego area. These breakdowns contributed to fraudulent and abusive spending 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, fraudulent and abusive usage of purchase cards.

First, we found an ineffective overall internal control environment at SPAWAR and Public Works. Our work has shown that the lack of a strong internal control environment leads to the risk of improper behavior. For example, neither SPAWAR nor Public Works had effective policies over the issuance of purchase cards. Any employee having supervisor approval could basically get a purchase card. As a result, as shown on the posterboard, we found a proliferation of purchase cards, with 36 percent of SPAWAR and 16 percent of Public Works employees holding purchase cards. In contrast, we found that for six large defense contractors, no more than 4 percent of employees held purchase cards, and at GAO, about 2 percent of our employees hold purchase cards. This control breakdown resulted in over 1,700 cardholders, each with a monthly spending limit of over $20,000. We found no compelling reason why over 1,700 individuals were given the power to make purchasing decisions for the Federal Government.

We found other overall internal control weaknesses relating to rebate management, training, and the usage of internal audits. In fact, at SPAWAR, we found evidence that management ignored internal review results that demonstrated some of the very same problems that we found.

Second, with the ineffective overall control environment I just described, it is not surprising that the four basic controls we tested were ineffective. These controls include independent documentation of receipt of goods, independent certification of the monthly credit card bill, timely recording of purchases into the accounting records, and recording of property purchases into the property inventory records. These four controls are intended to provide reasonable assurance as to the integrity of purchase card transactions.

As shown on the posterboard, we estimate control failure rates of 35 to 100 percent for fiscal year 2000. The primary problem we found was that Navy employees were simply not following basic policies and procedures. For example, for 65 percent of SPAWAR and 47 percent of Public Works transactions, we found no evidence that a person independent of the cardholder validated that goods and services were received. This control is intended to minimize the risk, for example, of employees going on a personal shopping spree. Unfortunately, the high failure rate for fiscal year 2000 clearly shows that this control was ineffective.

In addition, SPAWAR and Public Works did not record property purchases in inventory records as required by Navy policy. When we asked to inspect 65 items from our sample, the two commands could not provide conclusive evidence that 31 items, including laptop computers and a digital camera, were in possession of the government. One of the 31 items was a video conferencing camera reported as stolen. For this item we found that the responsible Public Works employee had received and deposited in his personal checking account $2,500 from a personal insurance claim. Only after being confronted by our investigators did the employee reimburse the government with a personal check.

Third, we found fraudulent and abusive transactions involving Navy San Diego activities, including SPAWAR and Public Works. Weak internal controls contributed to five recent cases of alleged purchase card fraud related to Navy activities in the San Diego

area. Two of these related to Public Works. These purchase card fraud cases, which so far total over $660,000, involve numerous purchases of items for personal gain. Examples included home improvement items from the Home Depot, laptop computers, Palm Pilots, DVD players, an air conditioner, clothing, jewelry, eyeglasses and pet supplies. The control breakdowns related to these frauds were so pervasive that the total dollar amount could not be determined. One cardholder sentenced to 15 months in prison commented that illegal usage of the purchase card was "too easy."

Another of the Navy purchase card fraud cases involved compromise of as many as 2,600 purchase cards for Navy activities in the San Diego area. Navy investigators were only able to obtain a partial list of 681 compromised accounts. The account numbers showed up on a computer printer at a community college library in San Diego in 1999. However, the Navy has not yet canceled the compromised accounts. Rather, they're only canceling the accounts as fraudulent activity is identified. Navy investigators estimated that as of January 2001, at least 27 alleged suspects used 30 of the compromised account numbers. These suspects made more than $27,000 in fraudulent purchases of pizza, jewelry, phone calls, tires and flowers.

With ineffective internal controls, preventing and detecting fraudulent purchases for compromised accounts will be virtually impossible. As of May 21, 2001, we identified 22 compromised SPAWAR accounts that are still active. We also found transactions at SPAWAR and Public Works that we believe are potentially fraudulent or abusive. As shown on the posterboard, the potentially fraudulent purchases include personal items such as cosmetics from Mary Kay, and gift certificates from Nordstrom. It is unclear whether these purchases were made by Navy employees, or were due to compromised accounts. The ineffective monthly certification control resulted in payment of these obviously unauthorized purchases. However, we found evidence that the Navy subsequently received credit from Citibank for these items.

We referred all potentially fraudulent transactions to Mr. Hast and his team for further investigation. The abusive purchases relate primary to SPAWAR and include items where the purchase was at an excessive cost, questionable government need, or both. For example, as shown on the posterboard, we found purchases of items such as flat-panel computer monitors costing from $800 to $2,500 each. We believe the cost of these monitors is excessive when compared to standard GSA monitors that cost about $300 each. In addition, we found items purchased that were of questionable government need, including Palm Pilots, designer Palm Pilot carrying cases, and a leather briefcase from the Coach store. Accessories were also purchased for the Palm Pilots, including keyboards, travel kits, additional memory, modems and belt clips. We found no documentation to justify these as valid government purchases. Rather, it appears that these purchases were often made to satisfy the personal preferences of purchase card holders.

In summary, we found that Navy's management of the purchase card program in the San Diego area is simply not acceptable. We found significant problems with every aspect of the program that

we reviewed. These problems contributed to fraudulent and abusive usage of purchase cards.

I testified before this subcommittee in May on the importance of fixing DOD's serious financial management problems. Last week we testified that DOD made $615 million of illegal and improper adjustments to closed appropriations accounts. Today, you see another example of what can happen when financial management is broken and accountability is lost.

The individuals here from the Navy appear to be very capable people who can fix these problems. To do so, they will need to demonstrate leadership in this area and establish accountability, proper incentives and consequences for their employees to ensure proper behavior. We will be issuing a report with recommendations after this hearing. We are available to work with the Navy to implement those recommendations.

Mr. Chairman, that ends my statement. Mr. Hast and I would be happy to answer questions after the others give their statements.

Mr. HORN. Well, thank you very much for that presentation. We have faith in the GAO and you just do a marvelous job. So thank you.

[The prepared statement of Mr. Kutz follows:]

GREG KUTZ - GAO 7-30-01

Subcommittee Copy

Mr. Chairman and Members of the Subcommittee, Good Morning. It is a pleasure to be here to testify on our audit of Navy Purchase Cards. (With me is Bob Hast, Managing Director of our Office of Special Investigations, and an expert in credit card security issues)

Purchase cards were introduced to the government in the 1980's, primarily to streamline the acquisition process for small dollar purchases. Usage of purchase cards is growing quickly in the federal government, increasing from $2 billion in 1995 to $12 billion in 2000. The Department of Defense purchase card activity was over $5 billion in fiscal year 2000. With rapid growth in purchase card usage, effective internal controls are needed to protect the government from fraud, waste, and abuse.

I have a purchase card in my hand that Citibank was kind enough to provide for this hearing. As you can see, it looks like a normal credit card. The card used by the Navy is a MasterCard and can generally be used wherever MasterCard is accepted. However, notice that it says "For Official US Government Purchases Only."

As requested initially by Senator Grassley, our audit focused on Navy purchase card activity in the San Diego area, using a case study approach at:

- SPAWAR Systems Center (SPAWAR); and
- Navy Public Works Center (Public Works).

These two San Diego locations—which provide goods and services to their Navy clients—had a combined $68 million of purchase card activity in fiscal year 2000.

The bottom line of my testimony this morning is that we found significant breakdowns in purchase card controls in the San Diego area. These breakdowns contributed to fraudulent and abusive spending, and theft and misuse of government property.

My testimony has 3 parts:

- First, the overall purchase card internal control environment;
- Second, the effectiveness of four key internal controls; and
- Third, fraudulent and abusive usage of purchase cards.

First, we found an ineffective overall internal control environment at SPAWAR and Public Works. Our work has shown that the lack of a strong internal control environment leads to the risk of improper behavior. For example, neither SPAWAR nor Public Works had effective policies over the issuance of purchase cards. Any employee having supervisor approval was able to get a card.

As a result, **as shown on the posterboard**, we found a proliferation of purchase cards, with 36% of SPAWAR employees and 16% of Public Works employees holding purchase cards. In contrast, we found that for 6 large defense contractors no more than 4% of employees held purchase cards. At GAO, about 2% of our employees have purchase cards.

This control breakdown resulted in over 1,700 cardholders, each with a monthly spending limit of $20,000 or more. We found no compelling reason why over 1,700 individuals were given the power to make purchasing decisions for the government.

We found other overall control weaknesses relating to rebate management, training, and usage of internal audit results. In fact, we found evidence that SPAWAR management ignored internal review results that demonstrated many of the serious problems we found.

Second, with the ineffective overall control environment I just described, it is not surprising that the four basic controls we tested were ineffective. These controls include

- independent documentation of receipt of goods;
- independent certification of the monthly bill;
- timely recording of purchase card transactions; and
- recording of property purchases in inventory records.

These four controls are intended to provide reasonable assurance as to the integrity of purchase card transactions.

**As shown on the posterboard**, we estimate control failure rates of 35 to 100 percent for fiscal year 2000. The primary problem we found was that Navy employees simply did not follow basic policies and procedures.

For example, for 65% of SPAWAR and 47% of Public Works transactions, we found no evidence that a person independent of the cardholder validated that goods and services were received. This control is intended minimize the risk, for example, of employees using the purchase card for a personal shopping spree. Unfortunately, the high failure rate for fiscal year 2000 clearly shows that this control was ineffective.

In addition, SPAWAR and Public Works did not record property purchases in inventory records, as required by Navy policies. When we asked to inspect the 65 property purchases from our sample, the two commands could not provide conclusive evidence that 31 of them—including laptop computers and digital cameras—were in the possession of the government.

One of the 31 items was a video conferencing camera reported as stolen. For this item, we found that the responsible Public Works employee had received and deposited in his checking account $2,500 from a personal insurance claim. Only after being confronted by our investigators did the employee reimburse the government with a personal check.

Third, we found fraudulent and abusive transactions involving Navy San Diego activities, including SPAWAR and Public Works. Weak internal controls contributed to five recent cases of alleged purchase card fraud related to Navy activities in the San Diego area. Two of these cases involved Public Works employees. These purchase card fraud cases, which so far total over $660,000, involved numerous purchases of items for personal gain.

Examples included home improvement items from The Home Depot, laptop computers, Palm Pilots, DVD players, an air conditioner, clothing, jewelry, eyeglasses, and pet supplies. The control breakdowns related to the frauds were so pervasive that the total dollar amount could not be determined. One cardholder sentenced to 15 months in prison commented that illegal use of the purchase card was "too easy."

Another of the Navy purchase card fraud cases involved the compromise of as many as 2,600 purchase cards for Navy activities in the San Diego area. Navy investigators were only able to obtain a partial list of 681 compromised accounts.

The account numbers showed up on a computer printer at a Community College library in San Diego in 1999. However, the Navy has not yet canceled all the compromised accounts. Instead, Navy is canceling accounts only after fraudulent transactions are identified.

Navy investigators estimated that as of January 2001, at least 27 alleged suspects used 30 of the compromised account numbers. These suspects made more than $27,000 in fraudulent purchases of pizza, jewelry, phone calls, tires, and flowers. With ineffective internal controls, preventing and detecting fraudulent purchases for compromised accounts will be virtually impossible. As of May 21, 2001, we identified 22 compromised SPAWAR accounts that were still open.

We also found transactions at SPAWAR and Public Works that we believe are potentially fraudulent or abusive. **As shown on the posterboard**, the potentially fraudulent purchases include personal items such as cosmetics from Mary Kay and gift certificates from Nordstrom. It is unclear whether these purchases were made by Navy employees or were related to compromised accounts.

The ineffective monthly certification control resulted in payment of these obviously unauthorized purchases. However, we found evidence that the Navy subsequently received a credit from Citibank. We referred all potentially fraudulent transactions that we identified to Mr. Hast and his team for further investigation.

The abusive purchases relate primarily to SPAWAR and include items where the purchase was at an excessive cost, or questionable government need, or both. For example, **as shown on the posterboard**, we found purchases for items such as flat panel computer monitors costing from $800 to $2,500 each. We believe the cost of these monitors is excessive compared to standard GSA schedule monitors costing about $300 each. In addition, we found items purchased that were of questionable government need, including:

- Palm Pilots
- designer Palm Pilot carrying cases, and
- a leather brief case from the Coach Store.

Accessories were also purchased for the Palm Pilots including keyboards, travel kits, additional memory, modems, and belt clips.

We found no documentation to justify these items as valid government purchases. Rather, it appears that these purchases were often made to satisfy the personal preferences of purchase card holders.

In summary, we found that Navy's management of the purchase card program in the San Diego area is simply not acceptable. We found significant problems with every aspect of management of this program that we reviewed. These problems contributed to fraudulent and abusive usage of purchase cards.

I testified before this Subcommittee in May on the importance of fixing the serious financial management problems facing DOD. Last week, we testified that DOD made $615 million of illegal and improper adjustments to closed appropriation accounts. Today, you see another example of what can happen when financial management is broken and accountability is lost.

The individuals here from the Navy appear to be very capable people who can fix these problems. To do so, they will need to demonstrate leadership in this area and establish accountability, proper incentives, and consequences for their employees to ensure acceptable behavior.

We will be issuing a report with recommendations after this hearing. We are available to work with the Navy in implementing these recommendations.

Mr. Chairman, this concludes my testimony. Mr. Hast and I would be happy to respond to any questions.

Mr. HORN. Our next witness is Captain Ernest L. Valdes, the Commander of the Space and Naval Warfare Systems Center in San Diego, otherwise known as SPAWAR.

Go ahead, Mr. Valdes.

Captain VALDES. Mr. Chairman, Senator Grassley, thank you for the opportunity to discuss the Navy purchase card program. I entered a full statement to the committee, and I'd like to provide a summary statement at this time.

Mr. HORN. Without objection, it's in the record. I might add, when you're called, the whole statement goes in automatically.

Captain VALDES. Thank you.

Mr. HORN. And we'd like you to summarize it.

Captain VALDES. Yes, sir.

Mr. HORN. Because the sooner we can summarize it and get into a dialog with Senator Grassley and myself and any others that want to appear, and so we want to get a positive way.

Captain VALDES. Thank you, Mr. Chairman.

I'm Captain Ernest Valdes, commanding officer, Space and Naval Warfare Systems Center, San Diego. It's my job to command an organization whose mission is to provide the joint warfighter with the technology to collect, process, display and transfer information necessary to conduct military operations.

My command is one of the many Navy activities that uses and relies on the government purchase card program. We are a major command within the Navy and employ a workforce of approximately 80 military and 3,400 civilian government personnel consisting primarily of scientists, engineers and computer specialists. My command manages more than 1,000 projects both large and small, in research and development, testing evaluation, installation and in-service engineering in support of the Navy and Marine Corps. For fiscal year 2000, SSC revenues were over $1.2 billion.

The Navy's purchase card program greatly facilitates the timely and efficient response to our fleet and customer needs and is crucial to fulfilling our mission in support of naval forces. For over 10 years, SSC San Diego has effectively managed the purchase card program that makes over 50,000 purchases a year valued at approximately $45 million per year. The success of our program is based upon effective management controls and in the trust we have in our cardholders, who are career Civil Service employees or Active Duty service members.

We firmly believe the purchases being made are for legitimate government purposes. For example, during an upgrade of the operations center of *USS Blue Ridge,* a command and control ship forward-deployed in Japan, our team of engineers and technicians found computer and local area network components requiring immediate replacement or repair. During this effort, which includes an installation of an entire network on board the command ship, and a major upgrade to its command and control system, we placed 30 people on board the *Blue Ridge* for over 3 weeks working around the clock to complete this effort. The use of the purchase card resulted in immediate government savings by allowing the team to quickly procure necessary items and contributed significantly to the successful upgrade of *Blue Ridge,* accomplished in time for an upcoming operational exercise.

In addition to the trust we place in our cardholders, we have management controls to oversee the program. These management controls include as a first line of defense responsibility of the cardholder to review and challenge any discrepancies on their monthly card statements. Approving officials then review their individual cardholder statements as a second line of review. My command's agency program coordinator further reviews a random sample of cardholder statements each month, contacting cardholders and their supervisors when deficiencies are noted, including taking the action of revoking the card for misuse or, in other areas, disciplinary action to the cardholder.

Given the significant size of this program, we conduct regular reviews that occasionally reveal misuse or compromise of the purchase card. For example, our internal review process disclosed an employee's misuse of a purchase card for personal items while on travel. In this and other similar cases, cardholder authority was revoked. We also rely on our workforce to do the right thing and report cases of purchase card abuse, either directly to their supervisor or through hotline calls.

We have seen a few cases that revealed compromise of a purchase card by third parties outside the Navy; that is, the card number was stolen. And this resulted in the purchase of cosmetics and items at a record music store. In these instances of compromise or stolen purchase cards, the affected cardholders immediately reported and disputed the charges, and the cases were resolved in favor of the cardholders. And I refer to the Mary Kay issue that the GAO discussed earlier. That was an incident of a stolen credit card number.

I will now address the specific GAO findings and address weaknesses in the program that merit attention and followup action. Our first action was to review the number of purchase cardholders at my command, and we have reduced the number of cardholders at the center by 18 percent. Our existing program is to require that all cardholders receive training prior to receiving the purchase card. We experienced a backlog in refresher training, and I intend to correct that problem by accelerating the training schedule to complete all training and refresher training by the end of the fiscal year.

SSC San Diego relies on the following procedure and management control to execute our program and combat vulnerability to abuse: First, a mandatory initial training program and following refresher training every 2 years—these are existing management controls at the Center; supervisory oversight of cardholders' use and need; cardholder review of their monthly statements; approving officials' review of the individual cardholder's statement.

We conduct random reviews every month by the agency program coordinator, and we have an aggressive action plan to correct deficiencies through counseling, retraining, and cardholder revocation for the serious cases. Mr. Chairman, we conduct formal investigations and pursue disciplinary action.

Finally, SSC San Diego has recognized that the purchase card program was a manual, paper-intensive process that would benefit from the employment of modern e-business solutions. My command recently implemented an enterprise resource planning system in-

corporating best commercial practices and utilizing commercial off-the-shelf software. This system will substantially improve our business processes at the command, including the purchase card program, and significantly improve our documentation issues that the GAO auditors highlighted.

In conclusion, Mr. Chairman, the purchase card program is vital to the successful implementation of SSC San Diego's mission to support our Navy and Marine Corps team. I also believe the implementation of enterprise resource planning will greatly improve the management tools available to oversee the program, while providing our workforce the necessary flexibility to accomplish the Center's mission in support of our Naval forces.

Mr. Chairman, Senator, thank you for giving me this opportunity to address the committee, and I'll address questions at any time, sir.

[The prepared statement of Captain Valdes follows:]

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HOUSE GOVERNMENT
REFORM COMMITTEE

STATEMENT OF

CAPTAIN ERNEST L. VALDES

COMMANDING OFFICER

SPACE AND NAVAL WARFARE SYSTEMS CENTER SAN DIEGO

SPACE AND NAVAL WARFARE SYSTEMS COMMAND

BEFORE THE HOUSE COMMITTEE ON GOVERNMENT REFORM

GOVERNMENT EFFICIENCY, FINANCIAL MANAGEMENT AND

INTERGOVERNMENTAL RELATIONS SUBCOMMITTEE

HEARING ON

NAVY PURCHASE CARD PROGRAM

JULY 30, 2001

NOT FOR PUBLICATION UNTIL
RELEASED BY THE
HOUSE GOVERNMENT
REFORM COMMITTEE

## INTRODUCTION

Mister Chairman and distinguished members of the Committee, thank you for the opportunity to discuss the Navy's Purchase Card Program. I am Captain Ernest Valdes, Commanding Officer, Space and Naval Warfare Systems Center San Diego (SSC San Diego). It is my job to command an organization whose mission is to provide the joint warfighter with the technology to collect, process, display and transfer information necessary to conduct military operations. Recently, the General Accounting Office (GAO) conducted an audit, number 918994/924012, of the Navy's Purchase Card Program at SSC San Diego. I am submitting this statement concerning the findings of the GAO audit.

## SSC SAN DIEGO'S MISSION

In order to place the GAO findings in perspective, it is important to understand the mission of SSC San Diego. SSC San Diego provides integrated Command, Control, Communications, Computers and Intelligence, Surveillance and Reconnaissance (C4ISR) systems for warrior information dominance. We are a major command within the Navy, and employ a workforce of approximately 80 military and 3,400 civilian government personnel, consisting primarily of scientists, engineers and computer specialists. SSC San Diego manages more than 1,000 projects, both large and small, for research and development, test and evaluation, installation and in-service engineering in support of the Navy and Marine Corps. The Center is a Navy Working Capital Fund (NWCF) activity, which means we do not receive an annual appropriation -- but instead receive revenues from various engineering and Fleet support projects. Last year, for fiscal year 2000, SSC San Diego revenues were over $1.2 Billion dollars. Our scientists, engineers and staff that support our command mission -- and ultimately our nation's warfighters -- travel to and perform work at many worldwide locations, including assignments in support of forward-deployed ships and submarines. The Navy's Purchase Card Program greatly facilitates the timely and efficient response to these Fleet and customer needs, and is crucial to fulfilling our mission in support of Naval Forces.

**PURCHASE CARD PROGRAM**

For over ten years, SSC San Diego has effectively managed a Purchase Card Program that makes over 50,000 purchases a year valued at $45 million. The success of our Program is based upon effective management controls and in the trust we have in our cardholders, who are career civil service employees or active duty service members. We firmly believe the purchases being made are for legitimate government purposes and ultimately benefit our customers, including the Fleet and our C4ISR programs.
For example, during an upgrade to the Operations Center of the USS BLUE RIDGE (LCC 19), a command and control ship forward-deployed in Japan, an installation team of SSC San Diego engineers and technicians were aboard and found computer and local area network components requiring replacement or repair. During this installation effort, the use of the Purchase Card resulted in immediate government savings by allowing SSC San Diego employees to quickly procure necessary items and thus avoid an extension of their foreign travel that might have ensued while waiting for goods and materials acquired through other procurement avenues. The purchase cards were used to procure items from the Navy Exchange in Yokosuka Japan, and some items were purchased in San Diego and express mailed directly to the ship while inport Japan. The purchase card program contributed significantly to a successful upgrade to the USS BLUE RIDGE -- accomplished in time for an upcoming operational exercise.

In addition to the trust we place in our cardholders, we have management controls to oversee the Program. These management controls include, as a first line of defense, responsibility of the cardholders to review and challenge any discrepancies on their monthly credit card statements. Approving Officials then review their individual cardholders' statements as a second line of review. The SSC San Diego Agency Program Coordinator further reviews a random sample of cardholder statements each month, contacting cardholders and their supervisors when potential deficiencies are noted.
The Agency Program Coordinator at my Command will revoke cards for misuse, when warranted. Furthermore, our management controls require initial supervisor approval of each cardholder and then again upon completion of the mandatory training before a card is issued.

Given the significant size of this Program, SSC San Diego management and cardholders conduct regular reviews that occasionally reveal misuse or compromise of the purchase cards. As an example of how our internal reviews are working to combat misuse and fraud, the internal process disclosed an employee's misuse of a purchase card for personal items while on travel. In a separate case, there were inappropriate purchases of office furniture and appliances for the workplace. In both of these cases, cardholder authority was revoked. We also rely on our workforce to do the right thing and report cases of purchase card misuse. As an example of this, we saw a few cases that revealed compromise of a purchase card by third parties outside of the Navy – that is, the card number was stolen – and this resulted in the purchase of cosmetics and items purchased at a record music store. In these instances of compromised or stolen purchase cards, the affected cardholders immediately reported and disputed the charges and the cases were resolved in favor of the cardholders.

So despite the unique challenges of the purchase card program, the card allows our scientists, engineers and staff to quickly and efficiently make purchases that in the past required a cumbersome and intensive purchasing process.

**GAO FINDINGS**

I will now address the specific GAO findings at SSC San Diego, and address the weaknesses in the Program that merit attention and follow-up action. Changes are being implemented at SSC San Diego to improve the Purchase Card Program. During the audit, GAO stated the number of cardholders at SSC San Diego appeared excessive. We have reviewed the number of purchase cardholders for use and need and reduced the number of cardholders at SSC San Diego by 18 percent. I intend to conduct a second review within the next year to determine if further reductions are warranted. The GAO audit found deficiencies in the training of cardholders at SSC San Diego. Our existing program and policy is to require that all proposed cardholders receive the one-day training prior to receiving the purchase card and contracting officer's warrant – and we have an excellent track record in meeting this policy by conducting initial training for all of our cardholders. However, the backlog in refresher training increased when the Navy requirement for refresher training changed from three to two years. SSC San Diego

intends to comply with the refresher training requirements by accelerating the training schedule to complete the refresher training for all cardholders by the end of this fiscal year. So I can state that we have a sound training program, and every cardholder at the command has been trained at least once in order to be authorized to participate in the Purchase Card Program.

GAO also found deficiencies in receipt and acceptance of cardholder purchases. Our current policy requires cardholders to document receipt and acceptance of purchases made. In those instances where the cardholder is also receiving the end items, the Approving Official's approval is required on the purchase requisition prior to initiating the transaction. In those urgent situations when approval cannot be obtained, verbal approval must be obtained and noted when the purchase requisition is later completed.

A fourth finding by GAO involved split purchases, which are multiple purchases made by a single cardholder to avoid the micro purchase limit. In those instances where split purchases were found, the facts were gathered and appropriate action was taken, including the counseling and/or re-training of cardholders or the revocation of their purchase card authority.

The last GAO finding I would like to address involved property management and the accountability of purchases made with the Purchase Card. GAO's finding relates to the definition, interpretation and application of accounting for government property in a property management system – and the key issue is the control of pilferable items. We need to look at this issue carefully because I feel it is important to start with the premise that we have an honest and professional government workforce. For the isolated cases, my command has a number of measures to deter the pilfering of government property and classified material. These measures include day-to-day supervisory oversight and controls; established physical security measures such as locked and alarmed buildings, offices, and laboratory spaces; a compound that has restricted access to authorized personnel only; roving security patrols; and random inspections of individuals, briefcases, containers and vehicles leaving the Command. I am reviewing the application of Navy policy to the property management program in place at SSC San Diego to determine if any changes and stricter controls are warranted. It is important to note that for every item identified in the review during the GAO audit, each item was personally sighted and

accounted for at SSC San Diego -- which to me reflects the basic honesty and integrity of our civilian workforce.

In summary, SSC San Diego management controls do exist to combat our vulnerability to fraud. To review SSC San Diego's management controls and program execution, we rely on the following:

- A mandatory initial training requirement and follow-on refresher training every two years
- Supervisory oversight of cardholder use and need
- Cardholder review of their monthly statements
- Approving officials review of their individual cardholders' statements
- Random reviews conducted by the SSC San Diego Agency Program Coordinator
- Aggressive action to correct deficiencies through counseling, re-training and/or card revocation.

Finally, SSC San Diego recognized that the Purchase Card Program was a manual, paper intensive process that would benefit from the employment of modern e-business solutions. My command recently implemented an Enterprise Resource Planning (ERP) system, incorporating best commercial business practices and utilizing commercial off-the-shelf software, to provide our workforce with an integrated data environment and improved workflow and management processes. The Enterprise Resource Planning system has fundamentally changed, and will substantially improve, our business processes, including the Purchase Card Program. Enterprise Resource Planning will also significantly improve our documentation in most areas that the GAO auditors highlighted. Specifically, receipt and acceptance of goods and materials, separation of function from the cardholder to the receiver and property management will all be enhanced as a result of the software management tools under ERP.

**CONCLUSION**

In conclusion, the Purchase Card Program is vital to the successful implementation of SSC San Diego's mission to support our Navy and Marine Corps team. I feel that we have adequate management controls in place and a roadmap to further improve our existing controls. I also firmly believe that the implementation of

Enterprise Resource Planning will greatly improve the management tools available to oversee the Purchase Card Program, while providing our workforce the necessary flexibility to accomplish SSC San Diego's mission and support of our Naval forces.

Mr. Chairman, Thank you for giving me this opportunity to address the committee. I am ready to respond to any of questions at this time.

Mr. HORN. I think at this point we're going to yield to Senator Grassley, because he has another appointment coming, and he'll question you and some of the others, even though you haven't had a chance to give your testimony at this point.

Senator GRASSLEY. I have my questions of the General Accounting Office, but I hope that before the day is over, we hear that part of the solution to the issues that we have before us is that we are going to give the normal commercial way of checking credit for the issue of the credit cards to have the authority to issue credit cards to those that have good credit risk as opposed to everybody. And I hope the Defense Department would look to the banks for that normal commercial way of doing business.

Mr. Kutz, in 1997–1998, you provided extensive support for my review of internal controls at the Department of Defense. We discovered that supporting documentation like receiving reports simply did not exist. At the conclusion of that review, which was in September 1998, Mr. Hamre launched the purchase card initiative. Purchase cards eliminate the need for receiving reports.

Do you think that the Department of Defense answers to the internal control problems that we uncovered in 1998?

Mr. KUTZ. I believe most of the problems we found were actually implementation of policies and procedures. As part of this study, we found certain flaws in policies and procedures, but for the most part, the controls that we looked at were adequate. The issue was that the employees were either not doing the control or not leaving a documentation trail that shows that they did the control. We believe that the problems that we found are for the most part the employee following mostly valid policies and procedures.

Senator GRASSLEY. OK. The General Accounting Office has documented extensive misuse of purchase cards. To what extent have you checked the Department of Defense payment records to verify that taxpayer dollars have been used to cover unauthorized purchases?

Mr. KUTZ. As part of this review, we audited the underlying records for these two locations. We're doing a DOD-wide purchase card review for you and Chairman Horn, as was discussed earlier today. So beyond what we found at these two locations, as you mentioned in your opening statement, we're aware that for the 2-year period there are 500 or so potential frauds DOD-wide. But beyond these two locations, we really can't speak to other findings or issues with respect to the purchase card program at DOD.

Senator GRASSLEY. Has anyone examined the Department of Defense payment records to determine if the Department of Defense is using tax dollars to cover unauthorized charges on travel card accounts? And this is in regard also to my asking the internal—or the Inspector General to do an examination of the most egregious cases, like Sergeant X that I talked about in my opening comments.

Mr. KUTZ. We're doing a DOD-wide audit of travel cards for you and Chairman Horn. And again, beyond that, I know Chairman Horn had a hearing on that in the spring, and the issues with respect to the delinquency of the Department were discussed extensively. Beyond that, we're in the middle of putting a plan together to look at this DOD-wide, and we will look at all aspects of man-

agement of the travel card program at the Department and hopefully report back to you and Chairman Horn in the Spring.

Senator GRASSLEY. And, Mr. Chairman, that will be the last of my questioning, but, once again, I want to thank you for your leadership in this area and would pledge to continue to work with you.

Mr. HORN. Well, it's always a pleasure to work with you. When I was a Senate staff member in the early 1960's, there was Senator Williams of Delaware, and he was the one that really looked after all this, and I'm glad to see that your fine work goes in Senator Williams doing it. And they woke up when he came in asking questions, and I think that hopefully they will get your questions and get the point.

In the group 2 days ago, I said we're going to have another hearing in 3 months. We're not going to just let this drift. And we're going to do that until the Pentagon gets organized and starts doing what any corporate group would do. So we need to get you on track. And when the Bank of America came in to see me, I said, goodbye, folks. Don't even talk to me about it; that, you know, you've taken that risk, and you should have—you should have done just what the Bank of America would have done to its own people. So thank you.

So we'll go down the line now and get everybody's testimony then. I've got a whole series of questions.

So Captain John E. Surash, the commanding officer for the Navy Public Works Center in San Diego.

Captain SURASH. Good morning, Mr. Chairman. I'm Captain Jack Surash, commanding officer of Navy Public Works Center in San Diego. Sir, we provide the full range of Public Works services to the Navy and Marine Corps activities in the San Diego area. These services are provided to over 3,000 buildings on seven major bases, as well as military family housing located at several off-base sites. These commands and activities, including support for the many ships at the waterfront in San Diego Bay, consist of over 400 clients located in a 200-square-mile area. We must operate our business with the same price, quality, customer service and competitiveness issues that challenge and motivate all commercial businesses.

The Public Works Center employs a workforce consisting of 14 military and approximately 1,700 civilian and contractor personnel. Prior to the introduction of purchase cards, we obtained materiel requirements through a central procurement office. Frankly, this was a very cumbersome, bureaucratic, expensive and slow procedure.

The purchase card plays a critical role in handling our daily operations in support of the Navy fleet and Marine Corps. During fiscal year 2000, my cardholders made over 56,000 purchase card transactions valued at approximately $30 million. The purchase card replaced a procurement system that was not cost or time-effective for small dollar purchases.

Mr. Chairman, in 1999 my command's internal review process uncovered several areas of concern. To determine whether these concerns were unique or systemic, we took the rather extraordinary step of requesting a review of our purchase card program by the Naval Audit Service. The auditors periodically updated me on these

findings, and, based on their updates, I directed a number of changes be put in place.

In September 2000, we published a completely reviewed purchase card instruction which strengthened internal control procedures. I instructed my agency program coordinator to conduct stand-down training for all cardholders, supervisors and approving officials. Purchase cards were suspended for any employee who did not attend this training. I also required my agency program coordinator to conduct refresher training on an annual basis for all cardholders, supervisors and approving officials. We reviewed the number of purchase cardholders, resulting in an approximate 30 percent reduction from about 360 down to 247 cardholders.

As a part of our new process, we now require the cardholder, the supervisor and the approving official to sign a certification on each monthly cardholder statement. I tasked my supervisors to review the cardholder package and provided them with a checklist to aid their review. I directed that all original purchase card documents be maintained in one central location, so that if the need arose, all documents could be easily retrievable. I also strengthened internal controls for the dispute process.

GAO's audit covered fiscal year 2000. Mr. Chairman, I would point out that this is approximately the same period that the Naval Audit Service was conducting their review of my command. However, based on the GAO review, I learned there were a couple of areas that still needed to be addressed, so as a result of their investigation, I took the following action: A key issue was ensuring separation of functions between the person ordering material and the person receiving and accepting it. Our program had allowed cardholders to order and receive materials and services so long as someone else had made the original request for the material. I have now issued a revision to that policy that strictly requires that someone other than the cardholder accept and receive material and services.

Although our cardholders had received the required training, I issued contracting warrants based upon the training they took. The training records were discarded at the time we issued the new instruction, and we conducted stand-down training. I have now directed that all future training and contracting warrants be maintained for historical audit purposes. In addition, I've added another person to my command's internal review staff and initiated a program where they independently perform a review of the purchase card program every month.

The GAO presented a list of 39 questionable purchases. Mr. Chairman, we were already aware of 20 of these, all from three cardholders, as a result of our normal internal investigations. All 20 transactions were being handled through appropriate means involving our internal review office, consultation with the Naval Criminal Investigation Office and our own legal counsel.

Research on the additional 19 transactions, 12 were, in fact, proper; 2 were disputed, and credits were received; and 2 involved cardholders using the wrong card by mistake. The final three were valid official requirements; however, the purchase card was the incorrect procurement tool to use. In addition, the General Accounting Office identified 21 purchases that had been improperly spread

to stay under purchase card thresholds. Further research shows that 12 were, in fact, split purchases.

Mr. Chairman, however, much of the work at the Public Works Center is task-oriented. Purchases are made based on requirements that are known at a specific point in time. As work progresses, similar requirements may become evident, and purchases are made to fulfill the additional requirements. In these cases it may appear that purchases have been split to circumvent the purchase limits, when, in fact, the purchases were made based on requirements as they were known at the time. However, this is an area that we know we have to continually watch, and I have directed my people to do so.

In summary, Mr. Chairman, we have previously recognized that management and control of our purchase card program required increased attention. The General Accounting Office pointed out some additional areas where revisions to the program were needed, and we are quickly making those changes.

The purchase card program provides my command a flexible and powerful procurement method, one I truly believe makes us more responsive and cost-effective in meeting Navy and Marine Corps requirements. I fully recognize that proper controls are a key element, and I am committed to ensuring these controls are in place.

This concludes my summary statement, Mr. Chairman.

Mr. HORN. Thank you very much.

[The prepared statement of Captain Surash follows:]

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HOUSE GOVERNMENT
REFORM COMMITTEE

STATEMENT OF

CAPT J. E. SURASH, CEC, USN

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

FISCAL YEAR 2000 GOVERNMENT PURCHASE CARD

JULY 30, 2001

NOT FOR PUBLICATION UNTIL
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HOUSE GOVERNMENT
REFORM COMMITTEE

**INTRODUCTION**

Mister Chairman and distinguished members of the Committee, I am Captain Jack Surash, Commanding Officer of the Navy Public Works Center, San Diego (PWCSD). I am here today to address the Navy Purchase Card Program at my command.

PWCSD provides the full range of public works services to Navy and Marine Corps activities in the San Diego area. 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, 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. We charge for our services rather than receive an annual appropriation. Therefore, we must 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. My team provides these services through over 35 Product/Service Lines organized into five Business Lines: Facilities Engineering & Acquisition, 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 Naval Supply Systems Command.

## BACKGROUND

Prior to the introduction of purchase cards, PWC San Diego obtained it's material requirements through a central procurement office. Frankly, this was a very cumbersome, bureaucratic, expensive, and slow procedure. The Purchase Card plays a critical role in handling our daily multifaceted operations in support of the Fleet and Marine Corps. During FY 2000, my cardholders made 56,700 purchase card transactions valued at $29.7 million. The Purchase Card replaced a procurement system that was not cost or time effective for small dollar purchases. Our experience is that the purchase card provides a more efficient and effective method of procurement, and enables us to be more responsive to Fleet and Marine Corps clients. We believe in the program but we also fully understand that proper controls and procedures must be employed.

## BENEFITS OF THE PURCHASE CARD PROGRAM

The Purchase Card offers substantial benefits for making small dollar purchases under the $2,500 micro-purchase threshold by streamlining the procurement process. The concept of the purchase card program is "just-in-time." You will get what you need when you need it. It provides fast payment to vendors and allows the Navy to make single monthly payments rather than thousands of individual payments.

## RECOGNIZED PROBLEMS

In 1999, our internal review process uncovered several cases of potential fraud. To determine whether these problems were unique or systemic, we took the extraordinary step of requesting an audit of our Purchase Card Program by the Naval Audit Service.

The audit started in January 2000 and continued through December 2000. The auditors periodically updated me with their findings and weaknesses in my program. During the interim briefings, the auditors stated they did not uncover systemic fraud; however, the auditors did point out weak areas in our program. Based on these updates, I directed that the following changes be put in place:

In September 2000 we published a completely revised Purchase Card instruction which strengthened internal control procedures. I instructed my Agency Program Coordinator (APC) to conduct mandatory stand-down training for all cardholders, supervisors, and Approving Officials. Purchase cards were suspended for any employee who did not attend this mandatory training. I also required my APC to conduct refresher training on an annual basis for all cardholders, supervisors, and Approving Officials. We reviewed the number of purchase card holders, resulting in a 31 percent reduction -- from 359 to 247. I directed my managers to look at the number of cardholders on an annual basis. The current review is underway, and is scheduled to be completed by 31 July 2001. As part of our new process, we now require the cardholder, the supervisor and the Approving Official (AO) to sign a certification on each monthly cardholder statement. I tasked my supervisors to review the cardholder package and provided them with a checklist to aid their review. I feel the supervisors have the most direct knowledge of the numerous ongoing jobs and are in the best position to know if the material procured was required for the job. I directed that all original purchase card documents be maintained in one central location so that if the need arose, all documents would be easily retrievable. I also asked my people to strengthen internal controls for the dispute process by having the AO submit the dispute form to Citibank vice the cardholder. This adds a "separation of function" for this important part of the process. These changes were in place prior to GAO's audit. We are continuing to look for every opportunity to improve controls in our Purchase Card Program.

**GAO FINDINGS**

GAO's audit covered fiscal year 2000. I would point out that this is approximately the same period that the Naval Audit Service audit covered. Based on the GAO outbrief, I learned there were areas that still needed to be addressed. I again took action to correct the problems, including:

A key issue was ensuring separation of function between the person ordering material and the person receiving and accepting it. Our program had allowed cardholders to order and receive material and services, so long as someone else had made the original request for material. We frankly had misread the guidance. I have now issued a revision to our policy that strictly requires that someone other than the cardholder accepts and receives material and services.

Although our cardholders had received the required training and I issued warrants based upon the training they took, the training records were discarded at the time we issued the new instruction and conducted the stand-down training. I have now directed that all future training and warrants be maintained for historical/audit trail purposes.

GAO noted that the required semi-annual reviews of the program had not been conducted. Although my APC had performed various types of reviews, he did not retain documentary evidence of those reviews. I have directed that all future reviews (whether they be daily, monthly, or quarterly) and actions taken as a result of those reviews, be maintained for historical/audit purposes and the results be incorporated into the formal semi-annual review. In addition, I have added another person to my Command Evaluation staff and have initiated a program where they independently perform a review of the purchase card program every month.

GAO presented a list of 39 "Questionable Purchases." We were already aware of 20 of these – all from three cardholders -- as a result of internal "hot line" investigations. All 20 transactions were being handled through appropriate means, involving our internal review office, consultation with the Navy Criminal Investigation Office (NCIS) and our own Legal Counsel.

Research on the additional 19 transactions revealed 12 were proper charges, two were disputed and credits were received, two involved cardholders using the wrong card by mistake (they notified the APC), and three were for a valid, official requirement, but the purchase card was not the correct procurement tool.

GAO identified 21 potential purchases that may have been improperly split in order to stay under purchase card dollar thresholds. Further research shows that 12 were split purchases. However, much of the work at PWC is task oriented – purchases are made based on requirements that are known at a specific point in time. As work progresses, similar requirements may become evident and purchases are made to fulfill the additional requirements. In these cases, it may appear the purchases may have been split to circumvent the purchase limits, when in fact, the purchases were made based on requirements as they were known at the time. This is an area we know we have to continually watch and I have directed my people to do so.

Finally, a stand-down was conducted with mandatory attendance by all cardholders and AO's, providing training on these changes and reemphasizing their responsibility.

**CONCLUSIONS**

In summary, we had previously recognized that management and control of our purchase card program required increased attention. GAO pointed out some additional areas where revisions to the program were needed and we are quickly making those changes. The purchase card program provides my Command a flexible and powerful procurement method – one I truly believe makes us more responsive and cost effective in meeting Navy and Marine Corps requirements. 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. This concludes my statement. I am prepared to respond to your questions.

Mr. HORN. And we now go to Vice Admiral Keith W. Lippert, Director of Defense Logistics Agency, former commanding officer, Navy Supply Systems Command.

Admiral LIPPERT. Mr. Chairman, thank you for the opportunity today to discuss the Department of the Navy Purchase Card Program. I am Vice Admiral Keith Lippert, currently serving as the Director of the Defense Logistics Agency. I took over on July 20th. I previously served as the Commander of Naval Supply Systems Command, or NAVSUP, from August 1999 to July 11, 2001.

NAVSUP is the Department of the Navy's purchase card program manager, and in this capacity we are responsible for the establishment of Navy and Marine Corps policies and procedures for use of the purchase card and the management of purchase card services provided by Citibank. I am aware that there are issues surrounding the purchase card program. The Department of the Navy is addressing these issues, and I am confident that the policies, procedures and metrics that are in place to manage this 12-year-old purchase card program are adequate and comparable to the best practices of private industry. However, there can be improvements.

The General Accounting Office noted during their outbrief to the Department of the Navy that its written purchase card policies and procedures are generally adequate. The Department of the Navy recognizes that program execution is not always perfect. Oversight procedures, however, exist to identify and address areas of concern.

The Department of the Navy's Purchase Card Program is very successful overall and represents a significant business revolution in how the Department of the Navy purchases supplies and services. The card allows the purchase of commercially available supplies and services without the delay incident to the traditional purchasing process. The purchase card also reduces costs by consolidating transactions into a single monthly invoice for payment.

The Department of the Navy's reliance on the purchase card continues to grow. Today the Department of the Navy buys 99 percent of all requirements valued at $2,500 or less through the purchase card. And throughout the Navy and Marine Corps and in every commanding activity, there are more than 30,000 purchase cards with 9,100 approving officials and 1,800 agency program coordinators providing management and oversight.

The Department of the Navy purchase card policy establishes the structure and procedures used to manage the card program. The Department of the Navy's purchase card policy is available in hardcopy and on the Naval Supply Systems Command Web site, making it readily accessible to all. The Department of the Navy's policy establishes controls for the oversight and management of the program from the Department of Navy's major command level to the local activity cardholder. The controls cannot completely eliminate the occurrence of misuse. They can, however, deter and identify misuse.

The greatest strength of the system is employee honesty. The workforce is relied upon to properly use the card and to report misuse. The Department of the Navy's Purchase Card Program is structured in a way to place responsibility and accountability at

the lowest possible level, and the Department of the Navy trusts that its employees will execute these responsibilities with integrity.

There are three separate processes that provide checks and balances. The first is the establishment of accountability at the various levels of the program. The program establishes oversight responsibility for each level of the subsequent levels below them. This structure is similar to that used by Citibank for its corporate customers and creates a multitiered network of oversight.

The first tier, is the agency program coordinator, establishes cardholder limits and restricts vendor lists and conducts a semiannual review of purchase card use. Also resident at the local level is the approving official, who certifies all purchase invoices prior to payment.

Another level of oversight is performed by the Department of the Navy's contracting personnel. Contracting personnel approve and monitor execution of purchase card activities. Financial management policy also establishes procedures for funds control. Additional reviews are also conducted by the Navy and DOD Inspector General and audit services.

And finally, CitiBank, the Department of the Navy's bank card contractor, constantly monitors purchase card transactions. Since the inception of the purchase card contract with Citibank in November 1998, the Department of the Navy has made over 7 million credit card transactions. It is interesting to note that the commercial benchmark for vendor fraud and compromised card activity is 0.06 percent to 0.09 percent of the total dollar value spent. The Department of the Navy's rate is less than half of the commercial benchmark. One measure of the effectiveness of our oversight is that since November 1998, only 38 cases of fraudulent activity have been reported by the Naval Criminal Investigative Service.

I would like now to address some of the Department's initiatives to improve our purchase card program.

First, the Department of the Navy is in the process of moving from a manual purchase card process to a fully automated purchase card system, such as the Enterprise Resource Planning System.

Second, the Department of the Navy has increased training of the Department of the Navy's employees to reinforce proper purchase card usage.

And finally, the Department of the Navy is implementing electronic management tools such as Citibank's newly fielded dynamic reporting system that will permit it to better analyze purchase card transaction data.

In conclusion, the purchase card is a vital acquisition tool for its service members and civilian employees. I commend the General Accounting Office audit team for identifying opportunities for the Department of the Navy to improve an extremely complex program. The Department of the Navy has taken actions to improve its existing program.

This concludes my statement, and I am readily available to answer your questions, sir. Thank you very much.

Mr. HORN. We thank you very much.

[The prepared statement of Admiral Lippert follows:]

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COMMITTEE

STATEMENT OF

VICE ADMIRAL KEITH LIPPERT, SC, USN

DIRECTOR, DEFENSE LOGISTICS AGENCY

BEFORE THE HOUSE GOVERNMENT REFORM COMMITTEE

SUBCOMMITTEE ON GOVERNMENT EFFICIENCY

FINANCIAL MANAGEMENT AND INTERGOVERNMENTAL RELATIONS

HEARING ON THE

NAVY

PURCHASE CARD PROGRAM

JULY 30, 2001

NOT FOR PUBLICATION UNTIL
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HOUSE GOVERNMENT REFORM
COMMITTEE

**INTRODUCTION**

Mr. Chairman and distinguished members of the Committee, thank you for the opportunity today to discuss the Department of Navy Purchase Card Program. I am Vice Admiral Keith Lippert, currently Director of the Defense Logistics Agency. I previously served as Commander, Naval Supply Systems Command (NAVSUP) from August 1999 through July 2001. NAVSUP is the Department of the Navy purchase card program manager. In this capacity, NAVSUP is responsible for establishment of Navy and Marine Corps policies and procedures for use of the purchase card and management of purchase card services provided by CitiBank.

I am aware that there are issues surrounding the purchase card program. The Department of the Navy is addressing these issues. I am confident the policies, procedures and metrics that are in place to manage the 12 year old purchase card program are adequate and comparable to best practices of private industry; however, there can be improvements. The General Accounting Office noted during their outbrief to the Department of the Navy that its written purchase card policies and procedures are generally adequate. The Department of the Navy recognizes that program execution is not always perfect. Oversight procedures, however, exist to identify and address areas of concern.

**PROGRAM ASSESSMENT**

The Department of the Navy's purchase card program is very successful overall and represents a significant business revolution in how the Department of the Navy purchases supplies and services. The card allows the purchase of commercially available supplies and services without the delay incident to the traditional purchasing process. The purchase card also reduces costs by consolidating transactions into a single monthly invoice for payment.

The Department of the Navy's reliance on the purchase card continues to grow. Today, the Department of the Navy buys 99 percent of all requirements valued at $2,500 or less using the purchase card. Throughout the Navy and Marine Corps, in every command and activity, there are more than 30,000 purchase cards with 9,100 approving officials and 1,800 agency program coordinators providing management and oversight.

The Department of the Navy purchase card policy establishes the structure and procedures used to manage the card program. The Department of the Navy's purchase card policy is available in hard copy and on the NAVSUP Systems Command website, making it readily accessible to all.

The Department of the Navy policy establishes controls for the oversight and management of the program from the Department of the Navy major command level to the local activity cardholder.

The controls cannot completely eliminate the occurrence of misuse; they can, however, deter and identify misuse.

The greatest strength of the system is employee honesty. The workforce is relied upon to properly use the card and to report misuse. The Department of the Navy purchase card program is structured in a way to place responsibility and accountability at the lowest possible level; and the Department of the Navy trusts that its employees will execute these responsibilities with integrity.

There are three separate processes that provide checks and balances. The first is the establishment of accountability at various levels of the program. The program establishes oversight responsibility for each level over the subsequent levels below them. This structure is similar to that used by CitiBank for its corporate customers and creates a multi-tiered network of oversight. The first tier, the Agency Program Coordinator, establishes cardholder limits and restricted vendor lists, and conducts semi-annual reviews of purchase card use. Also, resident at the local levels is the Approving Official who certifies all purchase card invoice prices prior to payment.

Another level of oversight is performed by the Department of the Navy's contracting personnel. Contracting personnel approve and monitor execution of purchase card activities. Financial management policy also establishes procedures for funds control.

Additional reviews are also conducted by Navy and DoD Inspectors General and audit services.

Finally, CitiBank, the Department of the Navy's bankcard contractor, constantly monitors purchase card transactions. Since the inception of the purchase card contract with CitiBank in November 1998, the Department of the Navy has made over seven million credit card transactions. It is interesting to note that the commercial benchmark for vendor fraud and compromised card activity is .06 to .09 percent of total dollars spent. The Department of the Navy's rate is less than half of this commercial benchmark. One measure of the effectiveness of our oversight is that since November of 1998, only 38 cases of fraudulent activity have been reported by the Naval Criminal Investigation Service.

**OPPORTUNITIES TO IMPROVE**

I would now like to address some of the Department of the Navy's initiatives to improve our purchase card program.

First, the Department of the Navy is in the process of moving from a manual purchase card process to a fully automated purchase card system such as an Enterprise Resource Planning System.

Second, the Department of the Navy has increased training of the Department of the Navy employees to reinforce proper purchase card usage.

Finally, the Department of the Navy is implementing electronic management tools such as CitiBank's newly fielded Dynamic Reporting system that will permit it to better analyze purchase card transaction data.

**CONCLUSION**

In conclusion, the purchase card is a vital acquisition tool for our service members and civilian employees. I commend the General Accounting Office audit team for identifying opportunities for the Department of the Navy to improve an extremely complex program. The Department of the Navy is taking actions to improve its existing program.

This concludes my statement. I would also like to introduce the Executive Director of Navy Supply Systems Command, Larry Glasco. We will be glad to answer your questions.

Mr. HORN. We now go to Jerry Hinton, the Director of Finance for Defense Finance and Accounting Service.

Mr. HINTON. Good morning, Mr. Chairman. My name is Jerry Hinton, and I'm the Director of Finance for Defense Finance and Accounting Service. I welcome the opportunity to discuss with you the responsibilities for paying purchase card bills at DFAS.

DFAS purchase card payment process is in accordance with the DOD Financial Management Regulation and DOD policy memorandum. Specifically, DFAS performs a prepayment audit review or audits before charge card payments are made. Their prepayment review includes checking for the procurement identification number [PIN], and, if needed, the subprocurement instrument identification number [SPIIN]. We check for the payees' names and addresses. We check that the invoice date is later than the purchase order date, that the invoice is originally invoiced, that the estimated pay date is correct, that the appropriate payment office is identified by the line of accounting reference, that the prompt payment or certification is provided, that the correct amount is being paid to include interest where applicable, and that only the charge that is certified by the approving official is being paid.

In the case of the Navy, the entitlement system, which is called the Standard Accounting and Reporting System [STARS] One Pay, automatically schedules the payment through a disbursing module to make the payment when required.

Now I would like to address the GAO draft that discussed duplicate payments for charge card invoices. We have confirmed some duplicate charge payments were made at DFAS San Diego during the period covered by the audit. Most of these payments were caused by Citibank error. Shortly after the duplicates were discovered, Citibank systemically corrected the problem that had contributed to the duplicate payments. All duplicate payments identified were recovered from Citibank.

Mr. Chairman, that concludes my remarks, and I'll be happy to answer any questions.

Mr. HORN. Thank you.

[The prepared statement of Mr. Hinton follows:]

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Reform

STATEMENT OF JERRY S. HINTON

DIRECTOR OF FINANCE

DEFENSE FINANCE AND ACCOUNTING SERVICE

BEFORE THE

U.S. HOUSE OF REPRESENTATIVES

COMMITTEE ON GOVERNMENT REFORM

SUBCOMMITTEE ON GOVERNMENT EFFICIENCY, FINANCIAL MANAGEMENT AND

INTERGOVERNMENTAL RELATIONS

ON

OVERSIGHT HEARING ON USE AND ABUSE OF GOVERNMENT PURCHASE CARDS

JULY 30, 2001

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Committee on Government Reform

Good morning, Mr. Chairman, Congresswoman Schakowsky and members of the Subcommittee. My name is Jerry S. Hinton and I am the Director for Finance, Defense Finance and Accounting Service. I welcome the opportunity to discuss with you DFAS' responsibilities for paying Purchase Card bills.

I would like to start by giving you a general picture of the size of our responsibility and operations. DFAS is the largest finance and accounting operation in the world. Our mission is to provide responsive, professional finance and accounting services for the Department of Defense. On an annual basis we pay approximately 5.4 million military members, civilians, retirees, and annuitants; issue approximately $288 billion in disbursements; execute some 100 million accounting transactions; pay approximately 14 million invoices and over 5 million travel payments. During FY2000, DFAS paid approximately 10 million Chargecard transactions totaling $5.5 billion.

The DFAS Purchase Card payment process is in accordance with the DoD Financial Management Regulation and DoD policy memorandums. Specifically, DFAS performs a pre-payment review or audit before Chargecard payments for paper invoices are made. The pre-payment review or audit includes checking: (1) For the Procurement Instrument Identification Number (PIIN), and, if needed, the Sub-Procurement Instrument Identification Number (SPIIN); (2) For Payees' names and addresses; (3) That the invoice date is later than the purchase order date; (4) That it is the original invoice, and that the invoice number and date are correct; (5) That the estimated pay date is correct; (6) That the appropriate paying office is identified by the line of accounting referenced; (7) That the Prompt Pay or other Certification is provided; (8) That the correct amount is being paid to include interest where applicable, and (9) That only charges certified by the approving official are being paid. The entitlement system, Standard Accounting

and Reporting System (STARS) One Pay, automatically schedules the payments through a disbursing module (ADS) to make the payments when required.

Now I'd like to address the GAO draft that discussed duplicate payments for Chargecard invoices. We have confirmed some duplicate Chargecard payments were made at DFAS San Diego during the period covered by the audit. Most of these duplicate payments were caused by Citibank errors. Shortly after the duplicate payments were discovered, Citibank systemically corrected the problem that had contributed to the duplicate payments. One duplicate payment was caused by ship error; we have instituted internal controls to guard against a repetition of this type of error. All duplicate payments identified were recovered from Citibank.

Mr. Chairman and Congresswoman Schakowsky, that concludes my remarks and I will be happy to answer your questions.

Mr. HORN. And we now have Patricia Mead, the Acting Deputy Assistant Commissioner, Office of Acquisition, Federal Supply Service, General Services Administration.

Ms. MEAD. Good morning, Mr. Chairman and members of the subcommittee. I am Patricia Mead, Acting Deputy Assistant Commissioner, Office of Acquisition of the Federal Supply Service. I am pleased to be here on behalf of the General Services Administration to discuss the governmentwide purchase card program.

GSA has been responsible for contracting for purchase card services since 1989. The most recent purchase card contracts were awarded in 1998 to five banks as part of the GSA Smart Pay Program. The purchase card was initially adopted as a management tool. The purchase card replaced the paper-based, time-consuming purchase order process for small dollar procurements.

Now, as the primary payment and procurement method for purchases under $2,500, the purchase card currently saves the government approximately $1.2 billion annually in administrative costs. In addition to these administrative savings, the government received refunds from GSA contractor banks in excess of $50 million last year based on total purchase card charges of $12 billion.

Because the GSA Smart Pay Program was designed as a managerial tool, agencies have numerous tools for oversight of the program. GSA mandated that contractors provide electronic reports to agency managers. These reports are secure and easy to access via the Internet. Agencies use these reports to assist in the identification of questionable transactions; for example, split purchases, improper cardholder limits exceeding the cardholder's contract warrant authority, and fraudulent activity.

While all payment mechanisms are subject to a certain degree of risk, GSA has built safeguards and systematic controls into the program designed to minimize risk. For example, when accounts are set-up, agencies determine what limits to set on each transaction. They are able to set limits by dollar amount per transaction, number of transactions per month, total per month and the types of businesses at which the purchase card may be used.

In addition, the agency decides to whom a purchase card should be issued; any limits on the use of the card; approval procedures; roles and responsibilities; and degree of agency program oversight. Most agencies establish their operating procedures at the Department level with further refinements in the field locations.

The controls GSA established in the contracts with the banks operate at multiple levels. Each cardholder with account activity in a given billing cycle receives a statement from his or her bank at the end of the cycle. This statement is a critical control. The cardholder receives training to understand the importance of promptly reviewing and approving the accuracy of the statement in accordance with agency policy. Operationally, after the cardholder reviews the statement, it is routed to an approving official or certifying official who approves the statement. This review is intended to validate all transactions as proper. Training has been established for all reviewing officials, emphasizing the need to report suspected card misuse to the agency program coordinator or to the Inspector General for further action.

Liability for transactions made by authorized cardholders rests with the government. If the card is used by an authorized cardholder to make an unauthorized purchase, the Government is liable for payment, and the agency is responsible for taking appropriate action against the cardholder.

The contract provides for agency program coordinators to oversee the program. The role of the agency program coordinator includes ensuring that cardholders properly use the card and monitor account activity. Because GSA Smart Pay is a critical managerial tool, agency program coordinators receive numerous reports on cardholder activity from the banks. To simplify the oversight process, transactions can be segregated by dollar amount, merchant type and frequency of transactions with specific merchants. Although reports can be helpful in identifying questionable purchases, reviewing and approval of transactions at the local level continues to be our most effective control mechanism.

GSA recognizes that cardholder training is essential to ensuring proper use of the card. GSA provides online cardholder training free to all purchase cardholders. The training discusses how to make purchases with the card, roles and responsibilities of cardholders and ethical conduct. Many agencies choose to supplement this training with written, oral or online training of cardholders on agency procedures.

GSA requires that all contractors participate in an annual training conference for purchase card program coordinators. Subjects of the annual training conference include electronic reporting tools, industry best practices, fraud monitoring and card management controls. The contractors are also required to provide onsite training to agency program coordinators. Written training materials provided by the contractors include cardholder guides and agency program coordinator guides. These address authorized uses of the card and responsibilities of the cardholder and the agency program coordinator.

As part of a continuing effort to improve the card program, GSA has recently formed a purchase card roundtable comprised of 25 agencies, which will address issues of concern, including fraud and program audits. This is an opportunity for agencies to share experiences and learn from each other.

Finally, there is a full electronic record of all transactions under the GSA Smart Pay Program. This electronic footprint makes fraud or misuse far easier to detect than any paper-based environment. A strong training program, state-of-the-art tools and a detailed review structure give Federal agencies all the tools and internal controls necessary to effectively run the purchase card program.

But as stated in the recent GAO Report on Strategies to Manage Improper Payments, people make internal controls work, and responsibility for good internal controls rests with all managers. Agencies must use the tools GSA has made available. GSA will continue to work with our industry partners and our customer agencies to minimize risk to the Government and ensure proper use of the cards.

Mr. Chairman, that concludes my prepared remarks today. I would be happy to answer any questions you may have. Thank you.

Mr. HORN. Thank you.

[The prepared statement of Ms. Mead follows:]

STATEMENT OF

PATRICIA MEAD

ACTING DEPUTY ASSISTANT COMMISSIONER

OFFICE OF ACQUISITON

FEDERAL SUPPLY SERVICE

U.S. GENERAL SERVICES ADMINISTRATION

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The purchase card was initially adopted as a management tool. The purchase card replaced the paper-based time-consuming purchase order process for small dollar procurements. Now, as the primary payment and procurement method for purchases under $2,500 (often referred to as micro-purchases), the purchase card currently saves the Government approximately $1.2B annually in administrative costs. In addition to these administrative savings, the Government received refunds from GSA contractor banks in excess of $50M last year based on total purchase card charges of $12B.

Because the GSA SmartPay program was designed as a managerial tool, agencies have numerous tools for oversight of the program. Realizing the need for the most current and complete data available, GSA mandated that contractors provide electronic reports to agency managers. These reports are secure and easy to access via the Internet. Agencies use these reports to assist in the identification of questionable transactions, split purchases (improperly splitting a single purchase into two or more micro-purchases to avoid otherwise applicable competition requirements), improper cardholder limits exceeding a cardholder's contract warrant authority, and fraudulent activity.

While all payment mechanisms are subject to a certain degree of risk, GSA has built safeguards and systematic controls into the program designed to minimize risks. For example, when accounts are set up, agencies determine what limits to set on each transaction. They are able to set limits by dollar amount per transaction, number of transactions per month, total per month, and the types of businesses at which the purchase card may be used. In addition, the agency decides to whom a purchase card should be issued, any limits on use of the card, approval procedures, roles and responsibilities, and degree of agency program oversight. Most agencies establish their operating procedures at the department level with further refinements in the field locations.

The controls GSA established in the contracts with the banks operate at multiple levels. Each cardholder with account activity in a given billing cycle receives a statement from his or her bank at the end of the cycle. This statement is a critical control. The cardholder receives training to understand the importance of promptly reviewing and approving the accuracy of the statement in accordance with agency policy. Operationally, after the cardholder reviews the statement, it is routed to an approving official or certifying official who approves the statement. This review is intended to

validate all transactions as proper. Training has been established for all reviewing officials emphasizing the need to report suspected card misuse to the agency program coordinator or Inspector General for further action. Criminal investigation of fraudulent transactions is generally conducted by the Inspector General's office in each agency. The banks routinely provide detailed data to assist the Inspector General office in performing the investigation.

Liability for transactions made by authorized cardholders rests with the Government. If the card is used by an authorized cardholder to make an unauthorized purchase, the Government is liable for payment and the agency is responsible for taking appropriate action against the cardholder. Use of the card by a person, other than the cardholder, who does not have authority and for which the Government does not receive any benefit, is not the liability of the Government. The Government's liability for transactions involving a lost or stolen card is limited to a maximum of $50. Historically, all liability for lost or stolen card transactions has been assumed by the GSA SmartPay® banks.

All GSA SmartPay® banks maintain a sophisticated fraud detection system to identify fraudulent activity and reduce risk. These systems have, in many cases, successfully deterred or prevented fraudulent activity by outside parties, not necessarily Government employees. In those instances where fraud is suspected, the contractor will notify the agency and begin the account cancellation process, after which a new card will be issued.

The contract provides for agency program coordinators to oversee the program. The role of the agency program coordinator includes ensuring that cardholders properly use the card and monitoring account activity. Because GSA SmartPay is a critical managerial tool, agency program coordinators receive numerous reports on cardholder activity from the banks. To simplify the oversight process, transactions can be segregated by dollar amount, merchant type and frequency of transactions with specific merchants. Although reports can be helpful in identifying questionable purchases, review and approval of transactions at the local level continues to be our most effective control mechanism.

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GSA requires that all contractors participate in an annual training conference for purchase card program coordinators. Subjects of the annual training conference include electronic reporting tools, industry best practices, fraud monitoring and card management controls. The contractors are also required to provide on-site training of agency program coordinators. Written training materials provided by the contractors include cardholder guides and agency program coordinator guides. These guides

address authorized uses of the card and responsibilities of the cardholder and the agency program coordinator.

As part of a continuing effort to improve the card program, GSA has recently formed a purchase card round table comprised of twenty five agencies which will address issues of concern including fraud and program audits. This is an opportunity for agencies to share experiences and learn from each other.

Finally, there is a full electronic record of all transactions under the GSA SmartPay program. This electronic footprint makes fraud or misuse far easier to detect than in a paper-based environment. A strong training program, state of the art tools, and a detailed review structure gives Federal agencies all the tools and internal controls necessary to effectively run the purchase card program. As stated in a recent GAO report on "Strategies to Manage Improper Payments, Learning from Public and Private Sector Organizations," "people make internal controls work, and responsibility for good internal controls rests with all managers".[1] Agencies must use the tools GSA has made available. GSA will continue to work with our industry partners and our customer agencies to minimize risk to the Government and ensure proper use of the cards.

Mr. Chairman, that concludes my prepared remarks for today. I would be happy to answer any questions that you or members of the subcommittee may have. Thank you.

[1] Strategies to Manage Improper Payments, Learning from Public and Private Sector Organizations, May 2001, page 8..

Mr. HORN. Our last presenter is Deidra Lee, Director of Defense Procurement for the Department of Defense. And I gather you do not have a written statement because you have been out of town, and you came back for this hearing, so thank you for coming.

Ms. LEE. Good morning, Mr. Chairman. It's a pleasure to see you again. We have worked together on some other issues. I do not have a written statement for the record, as you mentioned, but I am here to tell you that I would like to assure you that the Department of Defense takes financial responsibility very, very seriously. We will look into these issues regarding the purchase card and other financial issues that have been raised. And I certainly look forward to working with GAO, the services, and this committee to make sure we have demonstrated to the taxpayer that we are spending their dollar wisely.

Mr. HORN. We thank you for that, and we'll now go to questions. And let's start with Mr. Kutz.

You have heard this testimony. Do you think they'll solve the problem, or is this just talk?

Mr. KUTZ. As I said earlier, I know Captain Valdes mentioned his enterprise resource system off-the-shelf package that's being implemented. I think that will certainly help automate some of the processes. But what we're talking about here, Mr. Chairman, is a people issue, a leadership issue and an accountability issue, and I think they have clearly the capability to do it. I have read the backgrounds of these folks. They have done fine service to our country, and I certainly don't have any doubt that they can fix the problems, but it's going to take attention and, you know, some of their precious time. And I'm sure they are busy with lots of things in the positions that they're in, but they are going to have to spend probably a little bit more time on this type of issue to make it happen.

Mr. HORN. What do you think we should do, have a 3-month rule for this group also, and will you be doing a check and repeating what you have already done, put in your blue cover, and see if the recommendations are being implemented; or is this——

Mr. KUTZ. We could certainly do that. As we said earlier, we are looking at this issue beyond these two locations for you in a broader study of DOD purchase card usage. But certainly we would hope to work with these folks to deal with the recommendations and find valid ways to implement them. And if you would like us to report back to you this fall on that, we would be happy to do that.

Mr. HORN. Let's get it done by November 1. And then in the meantime, you are going through two more operations, I take it.

Mr. KUTZ. We'll probably look beyond that. We had not looked at the Army or the Air Force, So we will probably take a look at Army and Air Force. I think of the 500 potential frauds that Senator Grassley mentioned, I believe 322 of them, based on my notes, are Army-related. So probably Army is the place that we will focus some case studies on in the immediate or short term.

Mr. HORN. Admiral Lippert, it's your responsibility, I take it, now throughout the Defense Department, and you would have the same policies for the Navy that you will for the Army and the Air Force?

Admiral LIPPERT. From NAVSUP's perspective, we set the policy for the Navy, and now as Director of the Defense Logistics Agency, I will be setting the policies within the Defense Logistics Agency, which is separate from the rest of the Department of Defense.

Mr. HORN. But that is the right button to press if something happened?

Admiral LIPPERT. Yes, sir.

Mr. HORN. So I'm sure you will solve that problem.

Mr. Kutz, in Admiral Lippert's testimony, he said the Navy rate of vendor fraud and compromised card activities is less than half of the commercial benchmark. Given your findings, do you think he is correct?

Mr. HAST. Mr. Chairman——

Mr. HORN. Mr. Hast is assistant to Mr. Kutz.

Mr. HAST. In listening to the Vice Admiral's testimony, he stated that commercial fraud at Citibank is between 6 and 9 percent.

Admiral LIPPERT. That was 0.06 and 0.09 percent.

Mr. HAST. Actually, it's 0.006 and 0.009. Those are basis points. And the credit card industry is running fraud at about 6 to 9 basis points. We did not check to see whether the Navy's was half of that, but if they are 0.04, that would be significantly higher than what the credit card industry is, which is 0.006 to 0.009.

Admiral LIPPERT. The numbers I was quoting were correct. As I said, it's 0.06 percent, which is not 6 percent, but 0.06 of 1 percent. And the numbers that we got are quoted from Citibank.

Mr. HORN. What's the best thing GAO can give to the Admiral that is the most important thing for him to look at in the next 3 months?

Mr. KUTZ. Probably reducing the number of purchase cards or taking a long hard look at why there are this many purchase cards out there. It does appear for the Navy that there's 47,000 or 48,000 purchase cards based on what we found in the records. I think there needs to be a look to see if that is something that is really controllable, or is that just way too many purchase cards to control.

So I think the first line of defense here would be looking to make sure that we have the right number of cardholders, because the more cardholders you have, the harder it's going to be to train them, to monitor them, to review their transactions, etc. So, again, I would recommend that as the first thing to take a look at here.

One other thing, and Mr. Hast can probably expand on this, is that those compromised accounts that I mentioned are still live out there, and I think somebody needs to immediately cancel those accounts.

And, Bob, do you want to add to that?

Admiral LIPPERT. Could I address that point, Mr. Chairman? The accounts he is referring to were identified by us in the Naval Criminal Investigative Service, and they asked us to keep those accounts open while they are doing an investigation. So why they are still open is, based upon their suggestions and direction to us, is that it's an ongoing investigation.

Mr. HORN. Any comment?

Mr. HAST. I understand that law enforcement would need some of those accounts to stay open, but when you have 2,600 accounts open, you have the vulnerability of almost $230 million worth of

fraud if they got into the wrong hands and someone was able to exploit that. I think that's an awful lot of vulnerability to leave sitting out there.

Mr. HORN. Well, I must say it seems to be that they're getting very high priced items, computer hand-held this and that, and they can go out and just simply say, Well, we needed it for whatever we did, and instead, they are making a few bucks on the side. Is that what you saw in some of this?

Mr. HAST. Yes. Those were some of the types of cases that we reviewed.

Mr. HORN. And if you were in the Admiral's place, what would you do? Would you just say, look, you are doing it for the Navy or the Army or the Air Force, we expect you to use that card in that way and not go out and make yourself a fortune.

Mr. HAST. I am sure those controls are in place and those expectations are in place. I think that working with the credit card industry—and as I said, they are—working with Citibank on the front-end-loaded software that recognizes abnormal purchases and recognizes fraud is really the way to go. The credit card industry, when they found fraud creeping up, put a lot of money into research and development and developed front-end-loaded fraud control, and they have been successful since 1984 until the present in lowering fraud from close to 30 basis points down to 7 or 8 basis points.

So I do believe that technology and working with the industry on the front-end-loaded system are the way to go.

Mr. HORN. When the GIA started looking at this, did they have any reports from the Inspector General of the Navy or Defense or Army or Air Force? Where are the Inspectors General on these?

Mr. KUTZ. The DOD Inspector General is doing a Department-wide study that has not been released. There were several Naval Audit Service audits done of the Public Works, and I don't know if they were requested by the captain or not. It sounds like they maybe were. One of those was issued in December 1999 and had some of the issues that we found for 2000. The other one was done for fiscal 2000. And I believe that the captain was briefed on that, and we do not know the results. So he may be able to elaborate on what the Naval Audit Service found with respect to Public Works.

Mr. HORN. Admiral, when the GAO noted that 2,600 purchase card accounts were compromised, and many of these accounts had been hit for items such as jewelry, pizza and other inappropriate purchases, why hasn't the Navy canceled those accounts and just let them work their way back?

Admiral LIPPERT. Mr. Chairman, that is the direction that we have from the Naval Criminal Investigative Services, to keep those accounts open while they are doing an ongoing investigation for fraud. So that's why we haven't canceled those immediately.

Mr. HORN. So that service of the Navy is working on this?

Admiral LIPPERT. Yes, sir. Yes, sir.

Mr. HORN. And then I guess, Mr. Hast, why did the Office of Special Investigations get involved in the compromised card number case? Did you develop information that would help to identify the source of the compromised numbers or what?

Mr. HAST. Yes. As part of GAO's review of the Navy Purchase Card Program, the Office of Special Investigations was asked to review ongoing Naval Criminal Investigative Service investigations. One investigation was the one with the 2,600 cards, and we are especially interested in that because that seemed to have the greatest vulnerability. While NCIS initiated an investigation with a Secret Service task force, we conducted an investigation in which we developed information to help NCIS identify the source of the 2,600 numbers. Specifically, we are able to identify that the addresses on the list were shipping addresses, and they were a number of merchants that kept this type of information. NCIS has now identified that merchant who has verified that the list came from their data base and that two former employees were targets.

Mr. HORN. Ms. Lee, as the Director of Defense Procurement, tell me how your office can solve this problem, and do you have ground rules?

Ms. LEE. Yes, sir, we do. We have Department-wide policy, Department of Defense-wide policy on how the purchase card is to be used. As was discussed by GAO and others, we set the Department-wide policy, which is then implemented at the various services, at the various units. It certainly does run along these lines, which is make sure that people that need the card have the card; that their supervisor is aware of it; review of their purchases; and overall review of the system. And we will certainly take a look at where, if anything, we need to strengthen those policies, including training for both the individuals and the supervisors, to make sure we are protecting the cards.

Mr. HORN. Had you had any knowledge of what was going on here in the last couple of months?

Ms. LEE. Yes, sir, I was aware there was a review ongoing at those particular units. I was also aware that we have various IG looks periodically, and also that our regular procurement reviews that the services conduct of their various units, they look at their purchase card programs.

Mr. HORN. Well, did you call in the various service IGs, the very service—people on the financial side? How do you operate on behalf of the Secretary of Defense?

Ms. LEE. Periodically, certainly as these kind of issues arise or as we find them from our normal review process, we try to put out—and we discussed that I have an interdepartmental staff where all the services come together, and we talk about these kinds of issues and what they're doing at each service level. I also meet with the other defense agencies, who do, although not represented by the major services—we have a good number of people out there in that area as well. We look at what our overall policies are and periodically put out updates, reminders, and additional information to the whole Department for the purchase card program.

Mr. HORN. Do you have other situations like this, and if so, what are you going to do about it?

Ms. LEE. Mr. Chairman, we certainly are going to make sure that every time in every instance when there is a purchase card issue or a perceived issue that we investigate the appropriate circumstances and take the appropriate action. As has been men-

tioned here, the purchase cards are a valuable tool. We just want to make sure people are using them correctly.

Mr. KUTZ. Mr. Chairman, last week, just for your information, GAO testified on purchase card problems at the Department of Education. And so that is another place that we are aware of that has some of the same types of issues as we reported on here.

Mr. HORN. Well, I thank you on that.

Captain Valdes, going back to your computer purchases, you told GAO that the acquisition of flat panel monitors, which cost between $800 and $2,500, that that was justifiable because they use less energy than the traditional 17-inch monitors, which cost approximately $300. Could you share with the subcommittee the study showing that the savings in electricity offsets the additional cost of a flat panel monitor?

Captain VALDES. Yes, Mr. Chairman. The benefits are in power savings. We have seen numbers upwards of 75 percent, And the recent Consumer Reports indicates such. But it's not just an electricity savings. That is important in California, as you might imagine. But it's just not——

Mr. HORN. I advise people to take a candle to California.

Captain VALDES. I've got one in my briefcase.

We buy these flat panels for shipboard use. We put a whole network of ultrathin monitors on board *USS Coronado,* the flagship for the Third Fleet, and the purpose there was to save space, reduce the heat on board the ship, and to maximize the efficiency of the space that's available to the crew members, which already are very tight quarters.

So there's a number of benefits to the flat panel display. The price is coming down significantly, and we feel in many areas with power savings—it's also fairly immune—well, it is immune to electromagnetic radiation effects. So if you have a CRT, and you are a high-powered transmitter, for example, you will see distortion with a standard CRT. With a flat panel you won't.

So from a military point of view and from a space, electricity and weight point of view, it becomes very important for the Marine Corps. We use vans for radar air traffic control—these are very small vans, Mr. Chairman. And we use flat panels to save limited space in those vans.

I'm also prepared to discuss some of the GAO findings as they relate to fraud if you feel it's necessary.

Mr. HORN. Do you think the computers should be bought one, two at a time, or do you think the Navy should buy computers in bulk like other government agencies in order to get the best prices?

Captain VALDES. That is a valid point, Mr. Chairman. I am going to look into how we might improve our procurement process with respect to bulk versus individually. Right now we buy these systems by project because that's the way the accounting works in the Navy Working Capital Fund Command. And I have over 1,000 different projects at the Command. So the challenge there is going to be to align the dollars with the project to make it work. But I'll look into that.

Mr. HORN. How many Palm Pilots did you have to give away, as it seems to be?

Captain VALDES. Sir, we have used Palm Pilots, just like most folks in business do, to improve the efficiency and effectiveness of the worker.

Mr. HORN. And what do you find that does for you?

Mr. VALDES. Well, what it does is it allows people to manage their time effectively. It allows them to retrieve data fairly quickly. I use it personally to be able to manage my time during the day.

Mr. HORN. Well, is it everybody that has to have one?

Captain VALDES. No, sir.

Mr. HORN. I see some of that here, too. But it just seems to me that not everybody has to carry one of these around. There can be a scheduler that does that.

Captain VALDES. That is a valid point. For all purchases, we require that the supervisor or approving official approve the purchase. And so if an engineer or a scientist feels he needs a Palm Pilot, or one of our legal or professional staff members, then the supervisor will make that determination, sir.

Mr. HORN. Now you haven't had that up to now, so is this a new policy?

Captain VALDES. No, sir. We have always had the policy where the approving official makes a determination on every purchase. That's been a long-standing policy at the Center and in accordance with Navy and DOD policy.

Mr. HORN. Who has to sign-off on a Palm Pilot?

Captain VALDES. The supervisor and approving official.

Mr. HORN. And what rank would that be?

Captain VALDES. A typical supervisor is an engineer, roughly at what we call the DP–3 level, DP–4 level. So it is a senior supervisor engineer with typically 10 to 15 years of experience in government service. So that's really the level of approval that occurs.

Mr. HORN. So this is in the senior Civil Service?

Captain VALDES. Yes, sir. It is individuals who have seniority within Navy.

Mr. HORN. How about the uniformed?

Captain VALDES. Well, it's a similar approval. We only have 80 military personnel, so it's typically a smaller group of people, but it's a senior-level person. In the case of if a lieutenant needs a Palm Pilot, it will be his or her supervisor.

Mr. HORN. What did they do before they had a Palm Pilot?

Captain VALDES. They carried a lot of paper.

Mr. HORN. Are you thinking of a slide rule?

Captain VALDES. Slide rules and paper.

Mr. HORN. Seems to me you have got to make some tough judgments, and these are little toys for a lot of people. And gee, you know, I am at such and such a level, and look, I've got a Palm Pilot.

Captain VALDES. Mr. Chairman, I'm going to look into it within my command.

Mr. HORN. Meanwhile the taxpayers are making out their 1040's and all.

Could you give us some examples where you feel the organization's purchase card program was effectively managed, and what are you going to do about it, real fast?

Captain VALDES. Yes, sir. Our management is, as I mentioned, at various different levels. We have management controls across the command. I mentioned the approval authority. I mentioned the supervisory controls. My plan is to reduce the number of cardholders. I've already reduced it by 18 percent. I intend to approve training. We currently train every cardholder before the card is issued, and we have a very good track record in making sure that every cardholder gets training before the card is issued.

What we need to improve on is refresher training, and I'm going to work to improve that posture in my command.

Mr. HORN. When was that training implemented?

Captain VALDES. We've always had that policy at the command.

Mr. HORN. Well, if you've had that policy, and we've got fraud, I don't know why we can't get a new system.

Captain VALDES. Yes, sir. When the GAO came to my command, they looked at all the folks that were carrying cards, and we provided them with assurances and documentation that they're all trained. Where we're weak is on some of the documentation to prove that the individual is trained. But all of the members of my command are trained prior to receiving a card.

The other areas are refresher training—it's required every 2 years. And we will work hard to catch up in that area.

Mr. HORN. For those that seem to be mall happy, do we just take the scissors and cut the card in half? It would save a lot of taxpayers' money.

Captain VALDES. Yes, sir. In the cases that GAO has highlighted and other cases that I'm aware of from our own internal controls, we revoke the card immediately.

Mr. HORN. Mr. Kutz, is there anything you want to add?

Mr. KUTZ. I am sure what Captain Valdes said about the flat panel monitors is probably accurate, but I would note that we found them in the accounting department and with secretaries also. So I am not sure how that relates to the mission he was talking about.

Captain VALDES. That was the power savings aspect.

Mr. KUTZ. And I did read the same Consumer Report in July, and I think according to that report, the entire cost of operating a normal computer for 5 years is about $57. So I would like to see his study that demonstrates the cost benefit of the electricity savings.

But I do think the Navy needs to look at what they're buying with the purchase card. If we are going out and buying one and two computers at a time, are we paying full retail, and are we getting the full benefit of having the—or are we outweighing the savings that we've got from the streamlined acquisition process? The same thing with Palm Pilots. Whether they are a valid Government item or not, I am not certain. I know a lot of people that have them, and I'm not sure of anyone I know in the government or the private sector that has actually paid for them.

So you need to take a hard look at what is actually being purchased and if the purchase card is the right vehicle for it, because my understanding is that buying computers in bulk results in substantial savings. And I know at GAO, we buy them 400, 500 at a time.

Captain VALDES. Right now, our numbers show that roughly 10 percent of our total computer buys is flat panels. So it is not a pervasive issue throughout the command. It's roughly 10 percent. But I'll look into decreasing that number.

Mr. HORN. Captain Surash, the General Accounting Office noted that one of your employees effectively stole $2,500 by accepting a personal reimbursement from an insurance claim for stolen government property. Now, what action has the Navy taken against this individual for pocketing the reimbursement that belonged to the government?

Captain SURASH. Mr. Chairman, we were aware of a number of the issues that GAO had discovered. That one, though, was one we were not aware of, and I've disciplined—administrative discipline is quite possible. That is currently under review. We just found out about that a very short time ago, sir.

Mr. HORN. Was it just one case, or do you know about more cases?

Captain SURASH. That is the only case with those particulars that I'm aware of, sir.

Mr. HORN. Now, some of your employees were buying at Macy's, Nordstrom and Sam Goody. I don't know who Sam Goody is, so enlighten me.

Captain SURASH. Sir, the Nordstrom buy was actually safety shoes. We provide our—we're mainly a blue collar workforce. Our 1,700 folks for the most part are blue collar and not white collar and out maintaining bases, and a lot of our folks need safety shoes, and we pay for their safety shoes. In this particular case, we had one of my female employees purchase a set of safety shoes at Nordstrom for $99.95, sir.

Mr. KUTZ. We were talking about three gift certificates for $1,500. We are OK with the safety boots. We didn't question the safety boots.

Captain SURASH. On that, sir, there is a case the General Accounting Office discovered seven purchases that sparked their interest all from the same individual. Actually, there were a total of 22 transactions that we were already aware of and taking action on this individual.

The action we took was we referred this case to the Naval Criminal Investigative Service. That—I do not have the final outcome of that particular investigation.

At my command, sir, we have canceled 54 cards. Some of that was because we had some employees leave, but it was also because of misuse. I currently have 30 cards suspended as of the close of business Friday, and these were because our internal review process now has found things that we don't like are going on. There are three individuals that misuse was so serious that essentially I tried to fire them. In the Civil Service system, I issued a notice of proposed removal. And one individual was, in fact, fired, one resigned, and one was able to retire before I could complete administrative action on him, sir.

Mr. HORN. Well, thank you. And that started last Friday? Nothing like a good old congressional hearing for some action.

Captain SURASH. That is not—those aren't actions since last Friday. The actions that I'm talking about are within the last year, sir.

As I mentioned in my testimony, we did a major overhaul at my command effective in the fall of 2000. And unfortunately, the GAO review of things at my command was essentially before my major changes were put in place. I don't want to sit here to tell you that I've got a perfect running process, but it is much improved from what GAO saw during their onsite last year.

Mr. HORN. Mr. Hinton, you've paid the bills. Do you have some kind of auditing control that would send up a red flag if a bill came through with large purchases made at Macy's or Nordstrom?

Mr. HINTON. The way the system works today, we see the bills, but not the details behind it, we do not have the details available to us. We rely on the process that the Department has in place, that the certifying official, those people that have signed-off on these purchases, have looked at them and reviewed them.

Mr. HORN. Wouldn't common sense in your organization say, wow, there's a real red light here? DFAS, what good is it? I mean, if you can't look at the check and say, good heavens, $2,500 for this? And, you know, especially when you see Macy's and Nordstrom.

Mr. HINTON. As I said earlier, we cannot see that as Macy's. We receive a certification from the particular service that says—under the Certifying Officers Act, that responsibility rests with the person that does the certification. We have attempted to go in and look at some merchant category codes. We did a study—we have an operation to go in and look at some of the transactions, but they are normally after the buys and more after the fact as opposed to before the payment is made.

Mr. HORN. Well, when you get that—it's really a purchase order of sorts, isn't it?

Mr. HINTON. Yes, sir.

Mr. HORN. Or are they paying it out-of-their-pocket and then turning it in? I don't think so.

It just seems to me, DFAS is—you know, they've fouled things up for the last 10 years that I know about in Columbus where that place was just a mess. Now, I know you've improved that. And they were knocking off $1 million checks to people. And when they threw up their hands and said, I didn't have that contract, I mean, good heavens.

What can your operation do, and why can't it do something?

Mr. HINTON. Well, thanks Mr. Chairman, for recognizing some improvements in Columbus. I would just like to say just like the people mentioned at the table, DFAS is a part of the Department and will look at ways we can also improve our processes as well.

Mr. HORN. Well, that's where I raised the flag of why the Inspectors General didn't check this sooner. And it seems to me we put them in there so they can get at things like this. So good old General Accounting Office comes in and does it.

Mr. Kutz, anything you want to add to this?

Mr. KUTZ. With respect to preventing the payments of vendors like Nordstrom, Macy's, etc., the key control there is the monthly certification, which doesn't take place at DFAS. That takes place

at the activity. And that's why it is important that each month, before the bill is paid, things like the Nordstrom, Macy's, etc., get flagged so you don't pay them. Rather than the pay-and-chase type of situation where you pay it, and then you go back and try find out later whether you had overpaid for things that weren't yours or were improper purchases. So that is the key control to making sure that you don't pay improper payments.

Mr. HORN. And, Ms. Mead, does GSA have this problem throughout the Federal Government, or what's your reading on this?

Ms. MEAD. We're not aware of it going on unless an agency reports it to us.

Mr. HORN. So you've setup a training program?

Ms. MEAD. We have a training program, and we have extensive electronic reports that enable the agencies to make their controls work. The data is available and very visible.

Mr. HORN. Well, are you sure that those training exercises are being done?

Ms. MEAD. I am sure they are being done. We're not sure that the things that people are learning are being put into effect.

Mr. HORN. Well, what would you do about it? Can you help them? I mean, you're putting training in, and then it seems to me that every agency has an Inspector General. And I can certainly ask, is the training being done? Now, is that training by GSA, or is it by the agency?

Ms. MEAD. GSA makes training available on a Web site, and the contract requires that the banks provide training to the agencies. So we do know people who attend the training once a year at the annual training conference.

Mr. HORN. OK. So, could they find whether training has occurred or not just by asking the question?

Ms. MEAD. Of each of the Department agencies?

Mr. HORN. Each Department. You're there because centralization and the Hoover Commission said, hey, we can save money for the taxpayers. Now that we find it, nobody seems to care much about it. And GSA ought to. You've got a very fine Administrator there, and I would think he would get at this.

Ms. MEAD. We see our role as putting the tools in the hands of the agencies so that they can have effective controls.

Mr. HORN. So you've got a model training program; is that it?

Ms. MEAD. We think we have a good training program.

Mr. HORN. Could you file for us at this point in the record just to see what it's like? Give it to the staff and we will put that in the hearing record. Thank you.

Anybody else want to make any points on this that we haven't asked? This is your chance.

Mr. KUTZ. Mr. Chairman, there are two more I would make. One other thing that Senator Grassley pointed out is management of the issue of credit limits for individual employees on a monthly basis. That's something that the Navy probably needs to take a look at from the standpoint of should everybody have a $20,000 or $25,000 limit, or are there some that maybe could get by with a couple thousand dollars a month limit, which, as Mr. Hast said earlier, reduces your exposure?

The other idea that was raised, and I'll let Mr. Hast expand on it, is the issue of credit checks, which probably does have some merit, because some of the frauds that we have seen are for people that had prior credit problems that were then given a government credit card and then committed frauds.

Mr. HORN. Mr. Hast.

Mr. HAST. I agree. I think it would be prudent that prior to giving someone a government credit card with a very high credit limit on it, we would check their credit and make sure that they behave responsibly in their personal life. I think someone who doesn't behave responsibly in their private life is much more likely not to behave responsibly with the public's money.

Mr. HORN. Who do you see should do that credit check? Is it the bank? Is it the Navy or the Army or the Air Force?

Mr. HAST. Whoever is issuing those cards. Whichever command is actually giving out the cards should set up a mechanism that they're able to do credit checks, and they're very easily done now by computer. They don't take a long time, and they are not very expensive.

Mr. HORN. Well, is it easy for them to get the check? And if so, do they have to pay a fee for it?

Mr. HAST. They would have to pay a fee for it.

Mr. HORN. What is the fee?

Mr. HAST. I would have to look. I'm not positive.

Mr. HORN. Well, perhaps Captain Surash and Captain Valdes would know.

Captain SURASH. I'm not familiar with a fee for credit check.

Mr. HORN. Well, maybe that's because nobody's ever done it. But let's look into that, and we ought to check on people's credit.

Captain VALDES. Mr. Chairman, I would like to briefly discuss the abuse issue, with your permission.

The GAO came to audit my command in August of last year. They spent 10 months. The total period of the audit was 10 months long. During that time they looked at 50,000 transactions, and they used an automated tool for that, which we are trying to get from them, on how to automatically review 50,000 transactions. But they started with Citibank data, from what I understand. And they found 78 cases of suspicious vendors—what they term suspicious vendors; 78 cases out of 50,000. Now we have—of those 50,000 transactions, they resulted in 6,000 vendors, and then they looked at each vendor to determine whether or not it was a suspicious case or suspicious transaction.

I had our legal inspector general look at the GAO list, and they found the following: Of the 78 vendors and transactions that were suspicious from the GAO's point of view, the vast majority, 62 cases on the list, were for legitimate government purchases and transactions. There were six cases of stolen cards or third-party fraud. There were five cases in the GAO list that we found through our Inspector General and legal to be cardholder misuse; not fraud, but misuse. The total value of that misuse was $2,107. Every dollar is important. I take this seriously. But just to put it in perspective, it's $2,107 out of $45 million in transactions. There were four cases of erroneous use of the card, and there was one possible billing error.

In summary, out of 50,000 transactions, a total of $45 million, GAO data itself revealed five cases of cardholder misuse for a total of $2,107.

I'm taking action, and I've already taken action on many of these cases, and I am going to pursue it. But I just wanted to make sure we put it in perspective, because I do not feel we have a problem—a serious abuse and fraud problem. In fact, I'm pretty proud of our workforce. I'm proud of their honesty and integrity. Over 99.98 percent of our purchases are for legitimate government use.

Thank you, Mr. Chairman.

Mr. HORN. Mr. Kutz, do you want to comment?

Mr. KUTZ. We only looked at supporting documentation for the two commands now for 400 to 500—or 4/10 to 5/10 of 1 percent of the transactions. What the captain is talking about are our automated tools where we downloaded information from Citibank into our system to scan it for obviously abusive-type things, such as the Coach store, which popped out when we did that. We didn't look at 50,000 transactions. We scanned through for obviously fraudulent or improper types of things. So to say that we looked at 50,000 transactions and have no problem with anything but what we found is a mischaracterization of our findings.

Captain VALDES. Sir, I did not say they looked at every transaction. What I said is that they scanned 50,000 transactions for all vendors. From that, they were able to pull 6,000 vendors that our command uses. And from that, they looked at 6,000 vendors and determined that there were 78 suspicious vendors or transactions. And that's the methodology that they used.

Mr. HORN. And that is the one that you are using, too; is that correct?

Captain VALDES. What I would like to do with that automated tool—right now, we do all this by hand. It's a manual process. I mentioned the Enterprise Resource Planning will help me automate that process, but I am also interested in tools to detect abuse, and whatever tools I can be provided with, I will use.

Mr. HORN. Is GAO able to transfer that material?

Captain VALDES. They have given us enough information to be able to find that tool, yes, sir.

Mr. HORN. Any other comments?

Well, Captain, this is the last comment I'll ask. Your staff justified the purchase of a leather briefcase from the Coach Store as being more durable and thus less expensive in the long run than other briefcases. Do you believe the Federal Government should be buying all of its employees briefcases from the Coach Store?

Captain VALDES. No, sir. That was abuse of a purchase card. I have written a letter of caution to the employee, and she's a good employee, Mr. Chairman. She probably made an honest mistake and happened to be at Nordstrom and purchased that bag, and I think she'll do better next time.

Mr. HORN. I won't comment on that.

Let's see. In closing, we will check back 3 months from now, just as we're doing with the last group from the Pentagon this last week. With the advent of the new administration, we anticipate the type of problem we have been discussing today will be resolved. Secretary Rumsfeld has been very clear in his desire to make the

Department of Defense accountable for the money it spends, and I want to be equally clear in my endorsement of that policy. The examination of government-issued purchase cards has only just begun.

I want to thank all of our witnesses today. I am sure there are ways you would have preferred to spend this morning. Let's hope there won't be need for another hearing on these two programs.

I would like to thank the staff who put this hearing together, and this is on our side and the minority: J. Russell George behind me, staff director/chief counsel; Bonnie Heald, to my left, your right, professional staff member and director of communications; Scott Fagan, assistant to the subcommittee; Chris Barkley, staff assistant; Davidson Hulfish, intern; Samantha Archey, intern; Fred Ephraim, intern; Christopher Armato, intern.

Minority staff: David McMillan, minority professional staff member; Michele Ash, minority counsel; Jean Gosa, minority clerk; and Christina Smith, Nancy O'Rourke and Lori Chetakian, our court reporters.

So we will have a hearing where we can go over these things about 3 months from now. So we will be looking for that. So with that, we're adjourned.

[Whereupon, at 12 noon, the subcommittee was adjourned.]

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