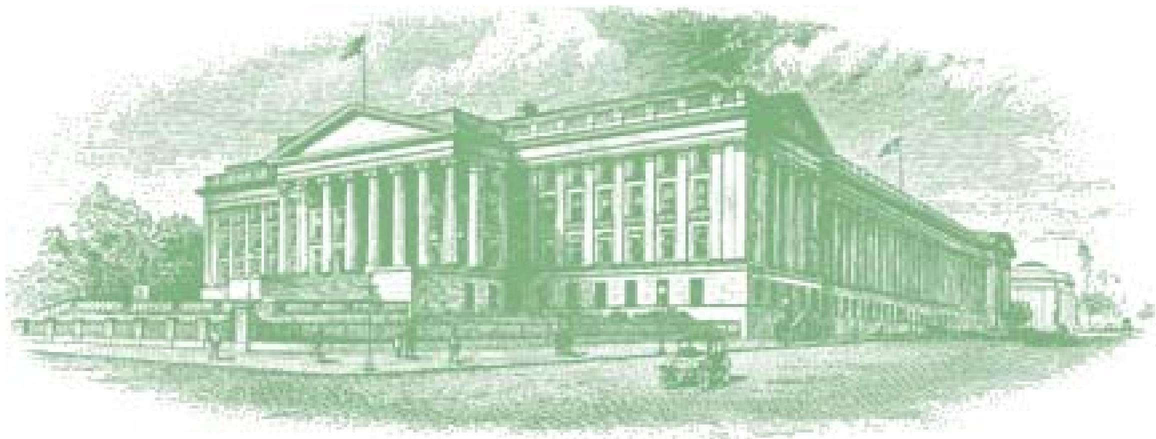
Audit Report



OIG-07-016

GOVERNMENT-WIDE FINANCIAL MANAGEMENT: FMS Policy to Charge Agencies for Plastic Card Network Costs Has Been Developed But Not Yet Implemented (Corrective Action Verification on OIG-03-088)

November 30, 2006

Office of Inspector General

Department of the Treasury

Contents

Appendices

Abbreviations

CAV	Corrective Action Verification
FMS	Financial Management Service
JAMES	Joint Audit Management Enterprise System
OIG	Office of Inspector General
PCA	Planned Corrective Action
PCN	Plastic Card Network

November 30, 2006

Kenneth R. Papaj
Commissioner
Financial Management Service

This report presents the results of our review of corrective action taken by the Financial Management Service (FMS) in response to one of the recommendations we made in our July 2003 report on the Plastic Card Network (PCN).[1] We recommended that the FMS Commissioner and the Fiscal Assistant Secretary jointly consider having PCN member agencies pay their own transaction fees and charges for PCN services. We estimated that implementation of this recommendation could yield a monetary benefit to the federal government of $797 million, the amount of FMS's projected PCN costs over 5 years. In October 2004, FMS closed the recommendation in the Department of the Treasury's Joint Audit Management Enterprise System (JAMES), indicating that corrective action had been taken.

In brief, we found that in July 2004, FMS's Assistant Commissioner of Federal Finance approved a policy for charging agencies for PCN costs in limited circumstances that would be effective with the next rebid of PCN services scheduled for fiscal year 2005. This did not occur until August 28, 2006, and has yet to be implemented. Therefore, no participating federal agencies have been charged for PCN costs. We also found that FMS is considering a different approach for administering the collection services it provides federal agencies. If implemented, this new approach would effectively supersede the July 2004 policy. Under

[1] Finding 1, Recommendation 3, in *Government-Wide Financial Management Services: Additional Control and Oversight Needed to Reduce Costs and Improve the Plastic Card Network*, OIG-03-088 (July 11, 2003).

the new approach, FMS would provide agencies, at no charge, collection services including PCN that it has determined it can provide most cost-effectively. FMS would charge an agency for collection services only if they elected to use services considered less efficient. A timeline has been established for conducting a pilot test of the approach, but we noted that an overall timeline for completing the approach design, finalizing agreements with agencies, and obtaining the pilot test results has not been established. While we concluded that FMS met the intent of our recommendation to consider charging agencies for PCN costs, it is too early to assess FMS's planned new approach. We will continue to monitor FMS's development of this approach and will plan audit work as appropriate.

In a memorandum dated November 17, 2006 (Appendix 1), responding to our draft report, FMS agreed with our conclusion, and identified several initiatives that will improve the efficiency of its revenue collections generally and card collections specifically.

Background

Office of Management and Budget Circular No. A-50 Revised, *Audit Followup*, states that audit follow-up is an integral part of good management and a shared responsibility of management and auditors. Each agency should establish an audit follow-up system to assure the prompt and proper resolution and implementation of audit recommendations. Treasury Directive 40-03, *Treasury Audit Resolution, Follow-Up, and Closure*, requires bureau staff to ensure that (1) audit recommendations are resolved on a timely basis; (2) resolved audit recommendations (i.e., those agreed to by bureau/Departmental Offices management) are promptly acted upon and that progress with respect to proposed and ongoing corrective actions is adequately monitored; and (3) statistical information and other data are appropriately reported pursuant to all statutory and regulatory requirements, including section 5 of the Inspector General Act of 1978, as amended.

At a department level, the status of audit recommendations is tracked in JAMES, an interactive system accessible by bureau management, which contains tracking information on audit reports from issuance through completion of all actions related to the findings and recommendations and provides the status of audit recommendations. At the bureau level, FMS uses an internal tracking system, the Audit Monitoring System, which provides more flexibility and detailed day-to-day information.

FMS's Management Control Branch, in the Program Integrity Division, coordinates the development of FMS responses to audit findings and recommendations, including the preparation of planned corrective actions (PCA), and ensures the proper recording, tracking, monitoring, and completion of PCAs. The Management Control Branch also prepares a Management Control Program Report that includes the status of open PCAs every month. This report is provided to the FMS Executive Board monthly by electronic mail and is presented at least once every other month at Executive Board meetings. Revisions to agreed-upon target dates for completion of PCAs require the written approval of the FMS Commissioner or Deputy Commissioner.

Our July 2003 recommendation that FMS consider having PCN member agencies pay their own transaction fees and charges was based on our analysis that this change would save the federal government an estimated $797 million in PCN operating costs from 2003 through 2007. Our assumption was that agencies – if they were charged for PCN services – would pass the costs on to the buyers of their goods and services in the form of increased prices. FMS concurred with the recommendation. FMS reported actual PCN costs for fiscal year 2003 of $80.2 million, for fiscal year 2004 of $74.7 million, and for fiscal year 2005 of $77.8 million.

FMS closed the recommendation in JAMES on October 25, 2004, with a PCA that stated "FMS's Emerging Technology Division will evaluate an agency's paying for their own respective transaction fees and charges."

Objective, Scope, and Methodology

The objective of this corrective action verification (CAV) was to determine whether FMS management has taken corrective action that is responsive to the intent of our recommendation to consider having PCN member agencies pay for their own transaction fees and charges. The scope of the CAV was the corrective action associated with recommendation 3 of finding 1 in our July 2003 report.[2]

We met with a manager from FMS's Program Integrity Division to obtain an understanding of the process used to monitor the status of recommendations. We discussed the status of the recommendation and details of the corrective actions with the Assistant Commissioner for Federal Finance. We reviewed an FMS-commissioned study, "Summary and Evaluation of Card Acceptance," dated January 14, 2004, as well as other papers that supported the proposed policy change. We reviewed the logs in FMS's Audit Monitoring System and the supporting documents provided. We requested follow-up information from managers and staff of Federal Finance to review more specifically the PCA on the recommendation. We queried JAMES to review the historical status of the recommendation.

We conducted our review during August 2006 at FMS in Washington, D.C., in accordance with generally accepted government auditing standards.

FMS's Corrective Action

As of October 25, 2004, the date the recommendation was closed in JAMES, FMS had developed a short-term policy that set forth limited circumstances in which FMS would charge agencies for PCN service fees and charges: (1) if the collection is related to a non-statutory/convenience product or service, (2) if an agency can support the collection by funding the costs associated with the collection through an appropriation, or (3) if an agency collection benefits the agency alone and does not result in overall government efficiency and cost savings.

[2] *Government-Wide Financial Management Services: Additional Control and Oversight Needed to Reduce Costs and Improve the Plastic Card Network*, OIG-03-088 (July 11, 2003).

The policy was to have been effective with the next rebid of PCN services, which was initially scheduled for fiscal year 2005. The rebid was completed on August 28, 2006, and the policy has been effective since that date, when the financial agent agreement with the selected new PCN service provider was signed. However, according to FMS, the policy has not been implemented.

FMS commissioned an independent study to evaluate its overall federal payment collection. The study, which was completed in January 2004, recommended, among other things, that FMS establish a collection-mix strategy, analyze agency-payment strategy, and investigate moving to a convenience fee structure. These recommendations, in part, are reflected in a new FMS "holistic" collection approach under development, as well as the above-mentioned policy that was to have taken effect in fiscal year 2005. The "holistic" approach refers to an FMS long-term collection strategy that would involve design of a collection mix for each agency. The approach is aimed at lowering transaction costs for each agency, thereby lowering overall costs to the federal government.

In the past, FMS provided several different options to the agencies, but without considering cost efficiency for the agency's overall revenue collections. Under the "holistic" approach, however, FMS plans to achieve cost efficiency by using the most cost-effective collection methods for each agency. The approach considers tiering the agencies, developing "a rate card" for each agency to use to determine whether it has reached the intended cost efficiency, and requesting reimbursement from an agency when it does not reach the intended level of performance at the end of the year. In accordance with the new approach, FMS has developed a draft plan for achieving maximum cost-efficiency. However, this plan has not been finalized. FMS plans to conduct a pilot test of the approach with Tier 1 agencies – a group of federal agencies selected by FMS to test the "holistic" approach – in a phased-in manner during calendar year 2007.

Conclusion

FMS generally complied with the intent of our recommendation. FMS internally reviewed its existing policy of paying for agency credit and debit card fees and charges, assessed various alternatives to this policy, commissioned an independent study to evaluate its payment collection system, and developed a policy for agencies to pay for PCN service fees and charges in limited circumstances. In addition, FMS has designed the new "holistic" approach as a long-term solution to improve collection efficiency and save operating costs.

To date, however, FMS has not required any member agency to pay PCN service fees and charges. PCN costs for fiscal year 2005 were $77.8 million. The policy, if implemented in fiscal year 2005 as planned, would have saved a portion of those costs, as well as the costs incurred in fiscal year 2006. Although FMS has been developing the "holistic" approach as its new collection strategy, no agency agreements have been completed.

FMS should expedite the implementation of its policy on acquiring fees as outlined in its July 2004 policy document and establish a timeline specifying the approximate dates for completing the "holistic" approach design; finalizing agreements with agencies; initiating a pilot program, if planned; and analyzing pilot program results.

Management Response

Management agreed with the conclusion and its response reiterated several initiatives that it expects to improve the efficiency of its revenue collections generally and card collections specifically. Among the initiatives cited are the July 2004 policy for charging card acquiring fees to federal agencies, a limitation on the transaction amount of card collections, the selection of a new credit card acquiring service provider, and the "holistic" approach intended to increase the percentage of collections processed electronically and move agencies from high cost to lower cost collections mechanisms. The approach includes several mechanisms for charging agencies that continue with inefficient practices.

In addition, FMS stated that it and the new credit card acquiring service provider reengineered the invoice reconciliation procedures and developed a process to manage interchange rates on a per transaction basis, resulting in potential annual savings of $15 million on acquiring fees. In summary, management stated that it has reduced card acquiring fees and analyzed options for charging federal agencies for the fees, and expressed confidence that the actions completed and those in progress will address the recommendations in the audit report.

OIG Comment

Although FMS discussed the development of the "holistic" approach, no specific timeline was provided for completing the design, finalizing agreements with agencies, and conducting planned pilots. With respect to the potential annual savings of $15 million on acquiring fees cited by FMS, the reengineered and new processes that are the basis for the potential savings are new, and we did not review the support for the potential savings as part of our work. We will monitor the status of FMS's initiatives and plan audit work as appropriate.

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We would like to extend our appreciation for the cooperation and courtesies extended to our staff during the review. If you have any questions, please contact me at (202) 927-6512. The major contributor to this report was Myung Han, Management Analyst.

Donald R. Kassel
Director, Fiscal Service Audits

DEPARTMENT OF THE TREASURY
FINANCIAL MANAGEMENT SERVICE
WASHINGTON, D.C. 20227

COMMISSIONER

November 17, 2006

MEMORANDUM FOR DONALD R. KASSEL
DIRECTOR, FISCAL SERVICE AUDITS

FROM: KENNETH R. PAPAJ *Kenneth R. Papaj*

SUBJECT: Government-wide Financial Management Service: Financial Management Service Policy to Charge Agencies for Plastic Card Network Costs Has Been Developed But Not Yet Implemented (Corrective Action Verification on OIG-03-088)

Thank you for the opportunity to comment on the October 20, 2006, draft audit report entitled "Government-wide Financial Management Service: Financial Management Service Policy to Charge Agencies for Plastic Card Network Costs Has Been Developed But Not Yet Implemented (Corrective Action Verification on OIG-03-088)".

The Financial Management Service (FMS) understands and agrees with the Inspector General's draft audit report. As indicated in your report, FMS complied with the intent of the finding related to charging Federal agencies for credit and debit card acquiring fees. FMS is pleased to report several initiatives that will improve the efficiency of our revenue collections generally and our card collections specifically. Among these initiatives are the following:

- In July 2004, the Assistant Commissioner for Federal Finance approved a "Policy on the Payment of Credit and Debit Card Acquiring Fees Associated with Federal Collections." This Policy outlined principles for charging card acquiring fees to Federal agencies.

- In February 2005, the Commissioner for FMS published in the Treasury Financial Manual (Bulletin Number 2005-03) instructions to Federal agencies to limit their card collections to cashflows that consist of individual transactions less than or equal to $99,999.99. This policy caps the size of our acquiring fees and promotes an efficient and cost effective means for collecting large dollar transactions via wire or Automated Clearing House (ACH) debits/credits.

- Effective August 28, 2006, FMS selected a new credit card acquiring service provider. FMS and the new service provider reengineered the invoice reconciliation procedures and developed a process to manage interchange rates on a per transaction basis. This will result in potential annual savings of $15 million on acquiring fees for the Federal Government. On October 24, 2006, the first transaction was conducted using the new service provider.

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- Federal Finance developed a new long-term solution for promoting efficiency and reducing overall costs to the Federal Government called the "holistic approach." Under the "holistic approach", FMS and each Federal agency will agree to a strategic plan for increasing the percentage of collections processed electronically and for moving from high cost to lower cost collections mechanisms, such as the Internet. The approach includes several mechanisms for charging agencies that continue with inefficient practices.

In summary, since completion of the original audit, FMS has reduced card acquiring fees to the Federal Government and analyzed options for charging Federal agencies for these fees. We are confident that the actions completed and those in progress will address the recommendations in the final audit report.

cc: Donald V. Hammond

Department of the Treasury

Fiscal Assistant Secretary
Deputy Chief Financial Officer
Office of Strategic Planning and Performance Management
Office of Accounting and Internal Control

Financial Management Service

Commissioner
Assistant Commissioner of Federal Finance
Audit Liaison

Office of Management and Budget

OIG Budget Examiner