

Research Report

May 2001



Fully Re-engineered State Agency Purchasing Systems Can Save \$300 Million by 2004

In 1997, the country's first totally electronic system from point of sale through charge approval and bank payment was introduced by Florida's State Comptroller, Department of Banking and Finance (DBF) and Secretary of the Department of Management Services.

Florida's Purchasing Card program for state agencies replaces manual reviews and approvals with electronic routing and approval, it improves management reporting and it reduces the cost of making small dollar purchases by as much as 80% through elimination of requisitions, purchase orders and checks.

When introduced, DBF staff projected that fully implementing the purchasing card plus other paperless technology innovations and a change to random pre-audit of state purchases under \$1,000 would save the state and its vendors up to \$300 million in reduced staff time, paperwork and record keeping, increased vendor discounts and reduced late payment interest penalties. Exact savings would depend on how fully each state agency re-engineers its purchasing processes.

This *Research Report* describes advantages of the state purchasing card and the status of state agencies' transition to its full use.

Purchasing Card Pluses

Cost Savings. The purchasing card's biggest advantage is improved efficiency and reduced staff time which can save the state a DBF-estimated average of \$60 per purchase. However, this savings accrues only when the purchasing card is used in an agency's fully re-engineered procurement process. Fully re-engineering means substituting electronic preparation, approval, transmission and recording of transactions for labor intensive manual processes.

The following examples provide a hint of potential statewide manpower redirects and savings:

- One of four positions assigned to voucher processing at the Department of Banking and Finance has been vacated and not filled.

- The Department of Juvenile Justice has reassigned one purchasing position and five accounts payable positions because of its purchasing card program.
- Two positions at the Department of Revenue have been eliminated from the purchasing section and remaining staff have been assigned to more complex procurements.
- Positions in the Department of Transportation's disbursement operations and financial services units have been reassigned due to the time saved from using the purchasing card.
- The Department of Management Services plans to eliminate three vacant accounting positions due to efficiency savings realized through the of the purchasing card.

Vendor Discounts and Surcharge. Some vendors provide discounts to agencies using the purchasing card. Additionally, the state's purchasing card contract with Bank of America includes a vendor surcharge currently set at 42 basis points (.0042) on the net purchase volume. Since 1998, the Department of Management Services has received over \$1 million from this provision.

Improved Customer Service. The purchasing card enhances both internal and external customer service by getting requested services and products to employees faster and paying vendors within 48 hours versus 30 to 45 days under the manual warrant process. Productivity of the cardholder and staff are enhanced through the FLAIR Purchasing Card Module's elimination of unnecessary requisitions, purchase orders and multiple reviews and approvals.

Improved Accountability. The purchasing card system generates data for analysis of spending trends and purchasing activity, and it facilitates detection of any misuse by vendors or employees.

Improved Accounting and Auditing. The Purchasing Card Module streamlines both accounting and auditing functions. An electronic Purchasing Card Module in the Florida Accounting and Information Resource System (FLAIR) automatically adds information to transactions received from merchants' point of sale devices. Such information (i.e. appropriate accounting codes, the date goods are received and the traveler's social security number) formerly required labor intensive manual entry. The Purchasing Card Module also captures and makes available information provided by the Bank of America (the state's contractor) and agency processors through the FLAIR information warehouse.

Purchasing Card Complements Other E-Commerce Innovations

Florida's implementation of the purchasing card, which is considered an industry standard, is a critical component of a multi-year transition from manual to electronic processing of more than four million transactions annually. It is projected to save the state and vendors up to \$300 million. Other complementary e-commerce innovations include invoice tracking for high volume recurring vendor transactions and electronic funds transfers to vendors. The latter avoids the expense of having to archive hard copy records for a period of 20 years.

In tandem with the purchasing card program, a Department of Banking and Finance (DBF) policy change to statistically sample the 97% of state agency purchases of less than \$1,000 plus Electronic Data Interchange (EDI) have resulted in DBF authorizing payment of four- out-of- five invoices without going through the labor intensive manual pre-audit process. What this means is that 80% of all invoices are not pre-audited as a result of being sampled (purchases less than \$1,000) or being a load and post item (a purchasing card transaction or EDI transaction.) Of this 80% workload reduction, three-fourths is due to statistical sampling and one-fourth to the purchasing card.

Over the past three years, more than one million state payment transactions have been executed electronically. The conversion rate from manual to electronic processing increased from 8% of transactions in July 1999 to 21% in January 2001. Still, nearly eight in ten transactions are processed at least partially by hand. While total electronic processing is unattainable, a Florida TaxWatch suggested target of processing 90% electronically by 2004 was not challenged by knowledgeable staff in half a dozen state agencies that reviewed drafts of this *Research Report*.

In 1995 DBF, which pays all state agencies' bills, assigned about 75 pre-audit positions to examination of agencies' manually processed purchases. Following implementation of the purchasing card plus other paperless technology innovations and a change to random pre- audit of state purchases under \$1,000, there are 43 pre-audit positions.

At the Department of Corrections, the combined impact of implementing the purchasing card, requiring the card's use for purchases of less than \$2,500, making larger quantity purchases on fewer purchase orders and consolidating 60 business offices into four service centers has resulted in reducing the purchasing staff from 166 to 79.

Automating Travel Transactions

When state agencies began using the purchasing card in 1997, they focused on small dollar purchases (less than \$1,000) which represented approximately 97% of the state's total state transactions. Department of Banking and Finance staff say that the next area for increasing use of the purchasing card is employee travel. Purchasing card benefits to agencies and traveling employees include:

- taking advantage of pre-booked discounts;
- savings through sales tax avoidance from direct billing to tax exempt agencies;
- elimination of corporate credit cards for travel;
- paying for travel expenses as they are incurred rather than requiring travelers to use their personal funds up front; and
- more information to track travel expenses electronically.

State Agencies' Experience With The Purchasing Card

Forty-four agencies including 25 constitutionally authorized departments, the legislative and judicial branches, the 10 state universities, several commissions, boards and offices and the Florida School for the Deaf and Blind are participating in the voluntary purchasing card program.

A recent Corporate Purchasing Card Benchmark survey administered by Washington University's Olin School of Business in St. Louis lists five levels of purchasing card experience: pilot program, early roll-out, middle of roll-out, full roll-out and mature. Florida Department of Management Services purchasing card staff suggest that:

- four Florida agencies have reached "maturity" of at least three years' experience with the purchasing card;
- fourteen agencies have between two and three years of experience and are in the middle to full rollout stage;
- eighteen agencies have between one and two years of experience and are in the early to middle rollout stage; and
- eight agencies have less than one year of experience and are in the pilot to early roll out stage.

The following list groups agencies by level of experience and notes the number of transactions they submitted to the Department of Banking and Finance in FY1999-2000.

Mature Agencies (429,955 Transactions)

Banking & Finance (16,041)

Management Services (53,833)

Juvenile Justice (128,582)

Transportation (231,499)

Middle to Full Roll Out Agencies

(1.6 Million Transactions)

Citrus (10,711)

Law Enforcement (35,810)

Community Affairs (10,288)

Legislature (N/A)

Environmental Protection (156,244)

Revenue (45,712)

Health (718,407)

Florida Atlantic University
(57,170)

Highway Safety (80,342)

Florida International University
(85,256)

Insurance (18,595)

University of Central Florida
(71,988)

Justice Administrative Commission
(NA)

University of Florida (383,908)

Early to Middle Roll Out Agencies

(1.3 Million Transactions)

Administrative Hearings (1,373)

Lottery (11,576)

Children & Families (443,380)

Military Affairs (15,438)

Corrections (385,233)

Parole Commission (3,445)

Elder Affairs (10,299)

Public Service Commission
(N/A)

Executive Office of the Governor
(5,830)

State (9,977)

Florida State University (120,507)

State Courts (18,026)

Fish & Wildlife Commission (78,913)

University South Florida
(132,823)

Health Care Administration (35,364)

Veterans Affairs (8,334)

Legal Affairs (41,389)

Business & Professional
Regulation (22,890)

Pilot to Early Roll Out Agencies

(922,876 Transactions)

Agriculture & Consumer Services
(115,239)

Education (21,796)

Workforce Innovation (673,504)

Florida A & M University (31,716)

Florida Gulf Coast University
(16,825)

Florida School for Deaf & Blind
(9,509)

University of North Florida
(28,928)

University of West Florida
(25,359)

Purchasing Card Best Practices

The Washington University/Olin School of Business survey cited above, plus material from Visa Card research on "best practices" of 18 corporations, suggest the following considerations for state agencies re-engineering their purchasing systems to initiate and improve purchasing card programs:

- Develop a purchasing card policy that describes allowable purchases; spending limits; use enforcement; user procedures; advantages of use; and restricted purchases. One hundred percent of the best practices companies contacted by Visa have a separate policy for their purchasing card programs;
- develop a written plan with objectives and performance measures, steps, milestones and timetables;
- create a cross-functional planning team that includes card users;
- develop a training program for rollout and continuation;
- use lessons learned from piloting the program to modify the purchasing card policy during roll-out;
- where possible, mandate use of the purchasing card for all allowable purchases;
- the unit responsible for the purchasing card program should track usage on a person-by-person basis and contact individuals who are not using the card; and
- perform cost analysis comparisons between traditional and new processes.

The most significant benefits reported by best practices companies were cost reduction, process improvement and less paperwork. Annual transaction costs were reduced by a reported 73 percent, saving approximately \$60 per purchase for average annual savings of \$4.1 million per company.

Recommendations

The following recommendations are based on Florida TaxWatch's review of state purchasing card practices and state agencies' experience with the card over the past four years:

1. The Governor and Cabinet should set a target of electronically processing 90% of the state's four million plus annual transactions by 2004.
2. State purchasing statutes and rules should be modified to require or encourage;
 - use of the purchasing card for all purchases under \$1,000 and most eligible purchases up to \$2,500;
 - agencies to seek vendor discounts for using the purchasing card;
 - reduction of non-eligible purchasing card transactions such as traveling employees' meals, payments to state government entities, utility payments and health benefit claims, where possible;
 - use of the purchasing card to take advantage of pre-booked travel discounts and to avoid payment of sales tax via direct billing to tax exempt agencies; and
 - reduction of the number of "do's and don'ts" that prompt agency staff to seek clarification before using the card.
3. Explore the economic feasibility of negotiating a provision in future bank contracts for purchasing cards to have a unique numbering system so vendors can program their computer systems to automatically not charge sales tax to purchases made with those cards.

State Agency Experiences With The Purchasing Card

Department of Banking and Finance

In 1996, the year before the purchasing card was introduced, the Department of Banking and Finance (DBF) manually processed 1,400 intra agency purchases. By 1999-2000, that number dropped to 400, and the value of DBF's internally processed purchasing card transactions grew by 700% (from \$1.4 million to \$17 million). One of the four positions assigned to voucher processing has been vacated and not filled.

DBF compared the traditional manual payment process to the purchasing card process for handling its internal purchases in Fiscal Year 1997-98. This analysis identified the various tasks and their direct costs associated with the traditional manual process of obtaining and paying for non-contract and non-travel

commodities of less than \$1,000 and compared them against the tasks and costs associated with use of the purchasing card. Indirect costs for management, rent, utilities, etc. were not included in the analysis because using the state purchasing card would not alter them. This analysis showed that the purchasing card process costs an average of \$48.00 per transaction less than the manual process, plus a \$12 savings from not pre-auditing, for total savings of \$60.

Department of Juvenile Justice

Between July and December 2000, the Department of Juvenile Justice (DJJ) used the purchasing card for 51% of its purchases (31,834 out of 61,951). This included 92% of purchases from frequently used suppliers, 65% of purchases from regularly used suppliers and 36% of purchases from infrequently used suppliers. DJJ has reassigned one purchasing position and five accounts payable positions because of its purchasing card program.

DJJ's use of the purchasing card for travel provides a convenience for employees by eliminating their having to advance personal income for payment of official business expenses. It also facilitates getting new employees some have not yet received a paycheck into training without having to issue and reconcile travel advances. Formerly, when a new employee departed abruptly (sometimes within days of starting training), trying to regain any monies given in advances resulted in varying degrees of success.

Due to the ease with which the purchasing card handles payments for new trainees and employees who travel for extended periods of time, DJJ's travel office has not issued a travel advance during the past year. The time freed from this time-consuming process has been re-assigned to the more comprehensive travel auditing.

DJJ's experience with the purchasing card is that there are significant savings when purchasing goods and services, but managing travel thoroughly and accurately requires the same audit process used prior to the purchasing card. Additionally, matching purchasing card transactions with information contained in the reimbursement request increases audit workload in the travel office.

Department of Management Services

The Department of Management Services (DMS) implemented the purchasing card system in January 1998. Its purchasing office now processes 56% fewer purchase orders than prior to implementation of the program.

In FY1999-2000, DMS processed 59% (32,906 of 55,870) of eligible transactions via the purchasing card. The dollar value of these transactions was \$8.5 million with an average purchase cost of \$259. From July 1, 2000 through January 31, 2001 it processed 14,886 transactions totaling \$4.3 million. Non-eligible transactions represent items such as payroll, payments to state government entities, utility payments and health benefit claims. The Department encourages but does not require use of the purchasing card for travel.

The Bureau of Financial Management Services plans to eliminate three vacant accounting positions due to efficiency savings realized through the use of the purchasing card

Department of Transportation

Since implementing the purchasing card in 1998, field purchase orders for small dollar items and services have decreased from 4,000 to 800 annually. This, in turn, has decreased the number of warrants issued for these purchases as they are now paid electronically. Positions in the Disbursement Operations and Financial Services units have been reassigned due to time saved from using the purchasing card.

The Department is currently re-engineering its travel system reconciliation process for full use of the purchasing card by the end of 2001. A decision to not use the purchasing card for travel during the start-up years was based on a concern about lack of accountability and because the processes of paying travel expenditures and reimbursing employees for travel expenditures are not integrated.

Overall, the Department is pleased with the purchasing card because it allows for improved monitoring and greater accountability; electronic data generated by the purchasing card system is used to monitor spending volumes and transactions for small dollar purchases on a daily basis; and purchasing card data is easily accessible to run minority spending reports and evaluate purchasing trends.

Department of Corrections

The Department of Corrections implemented its purchasing card program in the Spring of 2000, coinciding with a reorganization that consolidated 60 business offices into seven service centers during 1999-2000 and into four service centers in the fall of 2000. Centralization enables employees located throughout the state to purchase immediately needed goods and services with fewer purchasing staff and without delays resulting from off-site purchasing.

The purchasing card, which is mandatory for purchases of less than \$2,500, has improved payment compliance ratios, and financial staff now spend more time on their invoice-paying duties because they spend less time responding to vendor inquiries.

The Department's purchasing staff has been reduced from 166 to 79, but the impact of the purchasing card on this reduction is difficult to segregate from reorganization and other consolidation benefits such as larger quantity purchases on fewer purchase orders issued.

Prior to the advent of purchasing card, an estimated 75,000 purchase orders were issued annually. Since implementation of the purchasing card and centralization of purchases, the Department annually issues an estimated 18,000 purchase orders and makes 10,000 purchasing card purchases.

Department of Environmental Protection

The Department of Environmental Protection, which initiated its Department-wide purchasing card program in July 1999, has issued more cards (1,945) than any agency except the University of Florida. Its web-based training on the intranet and internet has reduced the requirement for Tallahassee staff to travel and present purchasing card training on a statewide basis. The Card has shifted work resources in some areas of Purchasing and Finance & Accounting. However, since state agencies must do a quality assurance check and post payment review of procurements made utilizing the purchasing card, resources have had to be redirected to that effort.

Five suggested ways to reduce workload incurred with utilization of the purchasing card are:

1. expand the area in the Flair Purchasing Card Module to allow users to put a more detailed description of what was purchased in the state's accounting system Flair Purchasing Card Module;
2. make the Flair Purchasing Card Module internet-accessible without having to go through the state's Metropolitan Area Network (MAN). Making the module accessible on the Internet would allow the staff of the Department in locations that do not have access to the Department's network to enter their information directly into the module and not have to send the paper work to another location to be entered;
3. make the module more user friendly. Staff that are entering information into the module are not accountants and the module, as designed, is for accountants to enter the required information;
4. when future bids are requested for the program, the specifications need to include a requirement that the bank furnishing the Purchasing Cards issue them with a unique numbering system so that the corporations, companies etc. can program their computer system to automatically not charge sales tax to a purchase made with a state purchasing card;
5. the Purchasing Statutes and Rules need revising so that the utilization of the purchasing card can be simplified. There are too many do's and don'ts now with the card and staff have to continually call the Purchasing Card Administrator to get clarification on a purchase before using the card. The Department began voluntary use of the card for travel in March 2000 and is mandating its use, effective July 2001. The Department's experience is that while there are cost savings associated with use of the card for travel, it is the area of least workload reduction because the card cannot be used to buy meals and therefore employees still must be reimbursed for this expense.

Department of Health

The Department of Health (DOH) implemented the purchasing card program in January 1999, and, since January, 2000, it has been mandatory for all purchases of commodities and services (with certain exemptions) under \$1,000. Some vendors' county health departments do business which give a discount for using the card.

DOH recently began piloting the use of the purchasing card for travel and found that, if cardholders provide a copy of the tax exemption certificate, most rental car companies, hotels and motels in Florida do not charge for the sales or room tax.

DOH staff say there is more control and accountability with the purchasing card than with purchase orders, which have decreased by 55% since February 2000. While purchasing volume has increased in the last two years, no additional staff have been hired to handle the increased workload.

Department of Revenue

The Department of Revenue (DOR), which began using the purchasing card on February 28, 1998, is known to have progressive training and management support. Purchasing card activity increased from 3,322 transactions between July 1, 1999 and March 13, 2000 to 8,035 between July 1, 2000 and March 13, 2001. During the same period, purchase orders decreased from 4,464 to 2,653, and purchases of \$1,000 or less decreased from 3,043 to 1,387. The number of purchasing cards issued increased from 140 in May, 2000 to 500 in March, 2001.

Procurements previously made by purchasing agents have been delegated to cardholders, two positions have been eliminated from the purchasing section and remaining staff have been assigned to more complex procurements and providing consulting to cardholders to help ensure compliance with state statutes and agency rules and procedures.

About 30 months after implementing its purchasing card program, DOR decided to allow use of the card for travel and to require its use for transactions of \$2,500 or less wherever feasible.

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