



Procurement Cards

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Typically, small routine purchases make up only 5% to 10% of a company's total purchasing spend. Yet whether the item purchased is a \$10 stapler or a \$5 million data management system, the internal cost to process and document the transaction ranges from \$80 to \$150 or more.

A procurement card program offers a simplified, streamlined procedure for making and documenting routine, low-cost purchases. A procurement card (P-card) is essentially a corporate credit card that allows employees to purchase designated products and services without going through the company's purchasing department and all of its pre-approval procedures and paperwork requirements.

A procurement card program can be structured in various ways and tailored to meet a company's individual purchasing needs and patterns. Card users are generally designated and approved by the program manager and given a spending limit. Expanded purchasing limits require the approval of higher levels of company managers. P-card use can be limited to approved vendors or certain types of goods. They may be limited by dollar amount, by store type, by SIC type, by geography, or by number of uses per day/month.

The benefits of P-card programs include:

- **Efficiency:** The purchasing process is simplified and streamlined. Fewer people are involved and less time is expended. Paperwork is reduced so internal handling costs go down.
- **Convenience:** All monthly P-card purchases are summarized on a card statement, eliminating the need for multiple invoices from or multiple payments to the same vendor.
- **Rebates:** Companies can receive rebates of up to 1.5% back from the card issuer. .

At the end of each month, the card issuer provides a statement summarizing purchases made with each P-card. The statement goes to the cardholder, who reviews, reconciles and approves it prior to forwarding it to accounting to be processed. The itemized statement resembles an individual credit card statement and gives information on each transaction.

A statement's level of detail is dependent on the merchant's point-of-sale system, and these systems can be grouped into the following three levels¹:

Level 1

The basic information provided includes the name of the cardholder, the purchase amount, the purchase date, as well as the name, city and state of the merchant.

Level 2

Level 1 information is included. Additional information can include sales tax, point-of-sale code (the cardholder provides a reference number during the purchase), and minority/women-owned or 1099 information.

Level 3

Level 1 and Level 2 information is included. Additional information can include line-item data like a description, quantity and amount. Level 3 detail requires that merchants must be using more advanced systems rather than credit card terminals. Examples are electronic cash registers or PC-based systems.

Card statements are available electronically, as well as in hard-copy format, making it easy for data to be automatically imported and posted to the appropriate GL account. Many card companies will also code accounts to facilitate posting of purchases to internal GL accounts. The statements provide sufficient line item detail for management to track the type, quantity, frequency, date, and location of purchases and thus monitor cards for possible overuse or inappropriate use by employees.

For example, an employee may be authorized to purchase plumbing parts up to a given dollar amount from Lowe's stores within specified zip codes. If charges for other types of products – say, paint, power tools or lawn care products – appear on the card, they will be immediately obvious.

These benefits are clear and compelling; however, there are also drawbacks to procurement card programs. Firstly, there are the obvious concerns about potential abuse and/or misuse of P-cards. Strong internal oversight is essential, with strict spending limits imposed on each card. Prior to issuing cards to employees, management should clearly stipulate how, when and where the cards can be used and specify penalties for misuse, abuse, fraud or payment delinquency. Some firms require employees to undergo a credit review before issuing them company P-cards.

Another potential negative has to do with the amount of detail provided in the card program documentation. In most jurisdictions, businesses are expected to collect sales taxes from consumers and remit them to the appropriate taxing authority. Businesses also are required to assess a use tax on their own non-taxed purchases and remit these amounts as well. However, monthly P-card statements generally do not contain the level of detail required to accurately calculate and substantiate sales/use tax figures. Thus, companies may be unable to make informed decisions regarding monthly accruals and accurately report use tax on non-taxed purchases. Large companies with locations in numerous tax jurisdictions often face complex issues with regard to sales/use tax, and this situation can be further complicated by use of procurement cards. There are also questions relating to the documentation of deductible business expenditures and information reporting requirements with P-cards.

These issues would clearly be problematic if a taxing authority were to come calling with an audit notice. Thus a review of internal recordkeeping policy is in order prior to implementation of a corporate procurement card program to ensure that card purchases are properly analyzed for monthly use tax accrual and reporting purposes and properly documented for later review in the event of an audit.

To prevent compliance problems and defend against audit challenges, companies must put procedures in place to accrue and record use tax on a frequent, regular basis. Monthly card statements and appropriate backup documentation should be catalogued and archived for audit purposes.

It is also important to ensure adherence to internal procedure so that cardholders provide the necessary tax information and transaction documentation in a timely manner. For these reasons, it is imperative that companies dedicate appropriate resources to the organization's tax reporting and internal audit functions.

Supporting documentation that should be maintained includes:

- Any and all vendor issued receipts or statements giving amounts purchased, purchase dates, general ledgers being charged and sales tax paid/charged.
- Cancelled checks and other bank records regarding purchases.
- Computations of self assessed use tax accruals.
- Records of where, when and how goods or services are used or consumed.
- Data in support of any claimed exemptions.

Sales/use tax auditors in state and local jurisdictions have become more sophisticated and more aggressive with regard to corporate taxpayers. As procurement card programs become more common, they will likely come under greater scrutiny by these taxing authorities. Companies will need to weigh the obvious benefits of P-card programs against the possibility of fines, penalties, interest assessments as well as the corporate and personal liability associated with non-compliance and strengthen their P-card program documentation procedures.

While P-card programs involve some upfront expense and may require review and adjustment of internal policy and/or procedural methods, they offer significant savings in terms of efficiency and convenience. These benefits far outweigh the costs and risks incurred with such a program. Moreover, if a business is challenged to dedicate the resources to setting up a P-card program, processes can be put in place by an outsource provider with the capacity and expertise to implement a successful, effective, money-saving P-card program.

¹ Materiel Management Guidebook; University of California Riverside; <http://purchasing.ucr.edu/purchasing/procurement/guidebook.html>

About CFO Edge

CFO Edge is a leading Southern California provider of interim CFO services. Based in Los Angeles, we are a group of experienced chief financial officers who engage with CEOs and CFOs on demand to address strategic planning, business management, and day-to-day financial operations challenges. Our seasoned professionals deliver services as interim CFOs, part-time CFOs, project-based CFOs, recruitment-to-permanent CFOs and interim-to-permanent CFOs. At CFO Edge, we're passionate about helping our clients create, grow and sustain value. For more information, visit www.cfoedge.com or call 626.683.8840.