

H. CARL McCALL  
STATE COMPTROLLER



A.E. SMITH STATE OFFICE BUILDING  
ALBANY, NEW YORK 12236

STATE OF NEW YORK  
**OFFICE OF THE STATE COMPTROLLER**

October 4, 2001

Mr. Peter Kalikow  
Chairman  
Metropolitan Transportation Authority  
347 Madison Avenue  
New York, New York 10017

Re: Report 2001-F-23

Dear Mr. Kalikow:

Pursuant to the State Comptroller's authority as set forth in Article X, Section 5 of the State Constitution, we have reviewed actions taken by officials of the Metropolitan Transportation Authority's affiliate – New York City Transit – as of September 7, 2001, to implement recommendations contained in our report *Metropolitan Transportation Authority, New York City Transit, The Automated Fare Collection Program Administering Out-of-System Sales* (Report 96-S-65) issued on February 4, 1999. In that audit we examined if New York City Transit (Transit) established an accounting system and controls to enable it monitor MetroCard sales and revenue transaction outside of its network of token booths and other Metropolitan Transportation Authority (MTA) controlled fare collecting facilities. We also explored whether Transit should continue to contract with an independent sales organization to solicit potential MetroCard merchants or perform this function in-house.

**Background**

The Metropolitan Transportation Authority (MTA) is a New York State-chartered public benefit corporation created by the Legislature in 1965 to deliver transportation services in the New York area and is governed by a Board whose 17 members are appointed by the Governor. In 1991, the MTA began to implement the Automated Fare Collection (AFC) program, a computerized fare management and marketing system that would allow riders to use a swipe card (MetroCard) instead of a token as payment of fare. In 1992, the MTA established a subsidiary, known as the Card Company. One of the missions of the Card Company was to develop a comprehensive system for selling the MetroCard to out-of-system retail locations. Developing an out-of-sales system was crucial since many passengers only use Transit's buses and are not proximate to a fare booth located in a subway station. In May 1996, the MTA decided to

“mothball” the Card Company and assigned the responsibility for developing an out-of-system sales network to New York City Transit – the affiliate that operates the subways and buses.

Our prior audit concluded that Transit lacked the procedures and controls required to adequately account for its out-of-system sales and revenue transactions. We found that many of the record-keeping procedures in place were not being followed. Without proper controls, the risk existed that not all receivables were collected and that merchant accounts were credited, accordingly. In general, the audit found a host of identified problems including poor inventory accountability, inadequate record keeping, inability to produce such basic documents as merchant files, and poorly trained and supervised employees.

### **Summary Conclusions**

Since issuing the prior audit report, the out-of-system sales network has been renamed the MetroCard Extended Sales Network and a Department of MetroCard Operations (Department) was established. With the introduction of 1-day, 7-day and 30-day unlimited ride MetroCards, Transit officials report the following achievements in sales, customer convenience and accountability:

- Total MetroCard sales to retail vendors in 2000 was approximately \$224 million; a 26.5 percent increase from 1999;
- In 2000, about 15 percent of daily MetroCard trips were sold through the Extended Sales Network; and
- Approximately 10.7 percent of all fares (MetroCards and tokens) collected by Transit were sold through the Extended Sales Network.

In addition, comprehensive monthly reports on extended sales are issued and Kable News Company (Kable) is the contractor responsible for MetroCard accounting records and delivery operations for transactions between merchants and Transit. There are periodic MetroCard inventory counts by a sub-contractor, monthly financial status reports issued to the Controller’s Department, internal audits done by the MTA’s Office of the Auditor General and Department staff do on-site reviews of Kable’s operations.

### **Summary of Status of Prior Audit Recommendations**

Of the 18 recommendations contained in the prior audit report, 14 were implemented, 2 were partially implemented and 2 were not implemented.

### **Follow-up Observations**

#### **Recommendation 1**

*Use Transit’s Encoding Facility records to reconstruct all private transaction conducted by the former manager who operated without supervision. Investigate all unresolved and questionable transactions.*

Status – Not implemented

Agency Action – In its response to our prior report Transit officials indicated this recommendation was completed in the first quarter of 1998. However, in our follow-up review Transit officials could not provide corroborating evidence that this recommendation was implemented in the first quarter of 1998. They advised us that the control environment has changed and responsibilities sufficiently segregated so that no one individual can order, approve and receive a delivery of MetroCards.

### **Recommendation 2**

*Establish controls over the MetroCard order forms by requiring, for example, the use of two signature forms, multiple copies, a log book, and sequentially-numbered forms corresponding to log numbers. Reconcile these forms periodically to copies maintained at Transit's encoding facility.*

Status – Implemented

Agency Action – Transit officials provided documents indicating that current policy requires the use of a standard form to order stock from Transit's High Production and Encoding Machine (HPEM) facility. Official also provided documentation indicating to order stock the form must be authorized by two individuals. Copies of the approved orders for the unit are maintained on file by the HPEM facility and their office. Officials indicated that orders are tracked and compared against the actual amounts shipped to Rapid Armored Corporation (Kable's sub-contractor for warehouse and delivery operations). Officials indicated that all variances are investigated and accounted for. Officials provided documents showing MetroCards shipped by their carrier (Rapid Armored Corporation with a date received, a Manifest number, and an HPEM number).

### **Recommendation 3**

*Establish a log for the recording and tracking of all merchant credits.*

Status – Implemented

Agency Action – In response to our prior report, Transit officials indicated that all credits are reviewed and processed daily, and are captured in the Sales Order Module of MAS 90 – software that tracks merchant, sales orders, accounts receivable, and general ledger information. The credits are reconciled monthly, and are included in the monthly reports submitted to the Controller's Department. Furthermore, information from this file is captured in a separate Crystal Report. Transit officials provided documentation that they introduced a MetroCard Return Request form that is sent to the Director of Retail Sales MTA-NYC Transit. An MTA-NYC Transit official approves the listing of the account number, the batch number, and the value of the MetroCard (\$4, \$6, \$15, \$17, \$50) returned. Most of the returned items were for expired MetroCards. They provided evidence that the credits are included in the monthly report submitted to the Controller's Department.

#### **Recommendation 4**

*Investigate and resolve the \$128,000 in overpayments claimed by a former sales organization, so that merchant accounts can be adjusted accordingly.*

Status – Implemented

Agency Action – Officials indicated they made several requests of the sales organization to supply documentation supporting this claim. Transit officials provided documentation of its August 2000 decision to reject the sales organization's claim.

#### **Recommendation 5**

*Establish procedures for verifying that missing batches are reduced before a credit or replacement batch is issued.*

Status – Partially implemented

Agency Action – Officials indicated and produced documents showing that order shipment data is summarized in an Oracle database (Database of Shipments and Summaries). The database that is summarized by batch number and is used to control the shipment and receipt of inventory is used as the primary tool to investigate missing batches. All cards are checked for usage in the AFC System prior to a credit being issued. Transit explained all cards of returned batches are rendered useless before a replacement batch is issued. The information provided did not conclusively prove missing batches are reduced before a credit or replacement batch is issued.

#### **Recommendation 6**

*Inform all merchants of the \$50 minimum balance requirement, document in the appropriate record the reasons for rejecting merchant applications and notify the merchant in writing of the decision.*

Status – Implemented

Agency Action – Transit officials indicated they now require a merchant have a bank account balance containing at least three figures because the minimum dollar amount of card stock that can be ordered is \$200. Transit notifies all merchants in writing when an application is rejected. To document this process is in effect, Transit officials provided a copy of a letter informing a merchant his application was rejected was because the bank referral they requested on several occasions was not received as well as a listing of merchants whose applications were rejected in the Year 2000.

#### **Recommendation 7**

*Reassess its decision to contract with a sales firm for services that could be performed by well-trained and adequately supervised in-house staff. In addition, determine what oversight and*

*monitoring will be necessary to provide reasonable assurance that the vendor is performing its duties according to contract terms.*

Status – Implemented

Agency Action – Transit reassessed its decision and continues to use an outside firm. Transit is in the third year of a five-year contract with Kable. Their oversight of Kable operation is achieved through daily, and monthly analysis of order processing which includes a review of inventory, accounts receivable, sales and cash balances. All discrepancies are investigated immediately. Transit performs on-site reviews at Kable’s main offices periodically to ensure data integrity. Transit provided copies of an on-site review of Kable’s facilities. The review was rather comprehensive indicating which areas of Kable’s operations required further strengthening.

### **Recommendation 8**

*Require that Merchant Services employees have adequate data-entry and bookkeeping skills and are supervised properly.*

Status – Partially Implemented

Agency Action – Transit officials indicated they have direct involvement in the hiring process to ensure appropriate Kable employees hired to work on its account have relevant accounting and finance experience. In addition, all Kable employees are subject to annual performance evaluations. Transit provided the job qualifications for the data control position that required a two-year degree or equivalent actual experience in accounting. However, documents provided for our review stated that for the period 8/24/00 – 10/31/00, “Specifically we identified input errors, omissions, miscalculations, and failure to process transactions timely. This generally demonstrates inadequate staff training, and lack of supervisory oversight pertaining to daily operations.”

### **Recommendation 9**

*Install computer edits and protected cells to prevent data manipulation and minimize data-entry errors. Periodically audit the database to assess its integrity.*

Status – Implemented

Agency Action – Officials indicated several controls have been implemented over the order input process to minimize the errors. For example, drop-down menus containing active inventory numbers in the sales order screen, as well as the use of a feedback loop that checks the item ordered against inventory, are used to prevent input errors and to prevent the backordering of inactive items. In addition, orders that exceed a predetermined credit limit are placed on hold and subject to managerial review before they are processed. This prevents the processing of duplicate orders. The customer service representative that inputs the data is prohibited from setting up new accounts. Furthermore, Transit provided a recent internal audit report where MTA’s Auditor General

concluded the accountability of MetroCards had improved based on sampling a sample of 50 batches and that all invoices for the selected batches were correctly posted in the system. They also reconciled the on-hand Metrocard inventory to the perpetual records.

### **Recommendation 10**

*Take a more active role in the supervision and direction of employee activities to verify that procedures are followed and that all work is documented properly.*

Status – Implemented

Agency Action – Transit officials indicated that the batch of orders received for the day is subject to managerial review and sign off before processing and before the MAS90 system is updated. Transit provided a copy of Day End – Check and Reconcile Reports for May 21 to 25, 2001. This document includes a checklist of procedures that need to be followed and a comparison of the number of batches issued for each MetroCard fare type to the dollar value of the batches issued.

### **Recommendation 11**

*Complete database postings in a timely manner and that Unit supervisors review them for accuracy.*

Status – Implemented

Agency Action – Transit officials indicated that the batch of orders received for the day is subject to managerial review and sign off before the MAS 90 system is updated. All ACH (Automated Clearing House) postings are done automatically when Chase Bank confirms the receipt of the funds. Inventory, cash, sales, account receivable balances are reconciled daily and monthly and reported regularly in the monthly submission to the respective parties. Transit provided us with its April 2001 Monthly Controller's Report that details accounts receivable, sales, inventory, cash balances and inventory withdrawals from the HPEM Unit. This information is prepared by the MetroCard Extended Sales and submitted to Transit's Controller.

### **Recommendation 12**

*Require that Merchant Service officials produce reports that are timely and accurate and that they are distributed to other Transit Units in a timely manner.*

Status – Implemented

Agency Action – Transit officials provided a monthly report that summarized the results of its operations. The report for a given month is provided to the Controller's Department by the last day of the following month. In addition, various other members of Transit's senior

management are on the distribution list for the report. Transit, provided the lead page of the monthly controller's report from July 2000 to April 2001.

### **Recommendation 13**

*Take periodic inventory counts at the contractor's warehouse facility, and reconcile them with the balances maintained by Merchant Services. Investigate and resolve all discrepancies.*

Status – Implemented

Agency Action – Transit officials indicated that inventory is reconciled daily and tied out to the General Ledger. Their contractor, Rapid Armored, is responsible for the physical custody of the inventory and performs a weekly count to ensure completeness. They note that title and risk of loss passes to Rapid Armored upon delivery. The Monthly Controller's Report includes an inventory tracking system, a record of inventory returned, activated and resold, inventory destroyed and a HPEM Reconciliation Report.

### **Recommendation 14**

*Credit merchant accounts at the point of collection.*

Status – Implemented

Agency Action – Transit officials indicated that as part of the ACH process the MAS 90 system automatically posts the payment to the correct merchant account. In addition, the accounts receivable and cash balances are reviewed and reconciled both daily and monthly to ensure completeness. Transit provided an aged accounts receivable ledger that lists a merchant's balance, current balance, and receivables that are 30 days, 60 days, 90 days, and over 120 days old. Under the past practice merchant accounts were automatically credited because the contractor fronted the money to Transit.

### **Recommendation 15**

*Block all merchant accounts after two unsuccessful collection attempts*

Status – Implemented

Agency Action – Transit officials indicated they have a procedure in place that calls for the blocking of a merchant account after one unsuccessful attempt. Transit provided a copy of MetroCard Operations Procedure 5.8 Processing Non-Payments – “The first rejected payment is noted in the system by setting the ‘Credit Hold’ flag. This action prevents the merchant from ordering a new supply of cards until the outstanding balance is paid via a second debit through ACH.”

**Recommendation 16**

*Reconcile all collections with merchant accounts to determine that no account is lost.*

Status – Implemented

Agency Action – Transit officials indicated accounts receivable and cash balances are reviewed and reconciled on a daily and monthly report. Transit provided its April 2001 Monthly Controller's Report which has an accounts receivable section including a control schedule, aged accounts receivable, and an inter-company activity report. After adjustments, the accounts receivable balance of the control schedule equaled the balance of the aged accounts receivable schedule and the subsidiary ledger aggregating all individual merchant accounts receivable.

**Recommendation 17**

*Maintain detailed and accurate merchant records and resolve problems promptly.*

Status – Implemented

Agency Actions – Transit officials indicated a detailed customer order/payment history is maintained on MAS90. All disputes are documented and the information is contained in the merchant's file. Transit provided its May 31, 2001 Accounts Receivable Aged Invoice Report aging the receivable balance of each individual vendor. In addition, Transit provided an Invoice History Report listing the type of fare cards purchased, the discounts offered, and the items returned.

**Recommendation 18**

*Review the consultant's support for its findings and, if warranted, seek reimbursement or ask that the work be redone.*

Status – Not implemented

Agency Actions – Transit officials indicate they believe the consultant performed appropriately and delivered a report that addressed the scope of work.

The major contributor to this report was Abraham C. Markowitz.

We would appreciate your response to this report within 30 days, indicating any additional actions planned to address the recommendations discussed in this report. We also thank the Metropolitan Transportation Authority and the New York City Transit management and staff for the courtesies they extended during our review.

Very truly yours,

Carmen Maldonado  
Audit Director

cc: Deirdre Taylor, DOB  
Paul Spinelli, MTA