

Accounts Payable Audit:
Continue Improvements

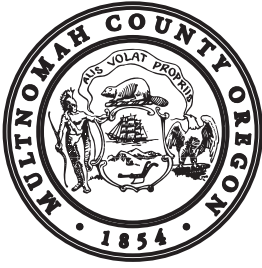
June 2010



Steve March
Multnomah County Auditor

Audit Staff
Judith DeVilliers

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.



Office of Multnomah County Auditor

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Date: June 28, 2010

To: Jeff Cogen, Multnomah County Chair
Commissioners Kafoury, Willer, Shiprack, and McKeel

From: Steve March, Multnomah County Auditor
Re: Accounts Payable: Continue Improvements

Policy makers and the public tend to focus on what major projects and services the county is providing or buying, but a critical element of the system is paying for what goods or services we purchase. In the county that responsibility is shared between the departments broadly, as the purchasers, and centrally by Accounts Payable (AP) within the Department of County Management, which oversees all payments including check printing and electronic payments. Overall, we believe the county's accounts payable are well-managed, based on our review of best practices literature.

Our audit focused only on accounts payable and the data reviewed included over 450,000 invoices totaling nearly \$2 billion from 2005 through 2009. The county has made great progress in converting to electronic payments and the use of purchase cards and we believe the county should continue these efforts which reduce costs and the number of checks that have to be written. We found no duplicate payments, payments on time per county criteria, and no gaps in check numbers. Specific recommendations and data have been provided to AP to help them continue improvements.

We want to thank the various departments and staff who provided assistance and cooperation in this audit and in particular the Interim Director of the Department of County Management, both the current and former Directors of Finance & Risk Management, as well as all of those in Accounts Payable; their response is included at the back of this audit. Part of this audit includes a supplementary report, "Accounts Payable Audit – Supplementary Trends and Charts," with charts and details from our analysis of accounts payable and check register data. Both reports can be found on our web page at www.co.multnomah.or.us/auditor.

CC: Mindy Harris, Interim Department of County Management Director & Chief Financial Officer; Mark Campbell, Interim Director Finance & Risk Management; Satish Nath, Accounts Payable Manager

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Accounts Payable Audit

Introduction

Changing technology has created opportunities to find greater efficiencies and improve controls in how an organization's bills are paid. The county has continued to adopt best practices for accounts payable with use of electronic payments, purchase cards, and other means of improving the efficiencies of the payment process.

Our objectives for this audit were to analyze accounts payable data in order to (1) perform some standard accounts payable tests, (2) provide management with a trend analysis of accounts payable invoices and payments, and (3) to identify possible areas of risk that would warrant additional review.

This report provides a summary of the work we did, what we found, and recommendations for improvements. In addition to this report we provided management with a supplementary report, "Accounts Payable Audit – Supplementary Trends and Charts," with charts and details from our analysis of accounts payable and check register data.

Background, Scope and Methodology

Accounts payable is managed on both department and centralized levels. Departments enter purchasing and invoice data into the county's enterprise system (SAP). The Department of County Management's Accounts Payable Unit centrally oversees all payments including check printing and electronic payments for all accounts payable activities. The division of responsibility between department and central accounts payable and the additional monitoring done by central accounts payable provide necessary accounting controls in prevention of errors or fraud in the county's payment system.

The primary guideline for the accounts payable function is found in the county's Administrative Procedure FIN-1 "Accounts Payable." The county's internal website (MINT) page for

accounts payable contains a wealth of information for county users with rules, guidelines, and forms. County users can also find help and instructions from the SAP Support site on the MINT and from classes and trainings. The county's Finance User's Group MINT site and monthly meetings also provide updates and information relating to accounts payable.

Our scope included only accounts payable and did not include employee compensation or property tax distributions to county jurisdictions. The accounts payable data we reviewed included over 450,000 invoices totaling nearly \$2 billion over a five-year period from fiscal year 2005 through 2009. We used ACL analytics software, which allowed us to easily obtain large amounts of data from SAP. ACL also has functions to test for duplicate records, missing numbers, stratification, summaries and crosstabs, Benford's analysis, and other tests. We performed many traditional accounts payable tests such as those done in recovery audits for duplicate payments, looked at the data for compliance with county policy and guidelines, and evaluated possible areas of internal control risks.

We also interviewed county employees, and observed central accounts payable weekly payment process and check printing. We researched best practices for managing accounts payable and for fraud prevention and detection.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Audit Results

Overall, we believe the county's accounts payable are well-managed, based on best practices literature we reviewed. Our analysis and summary of trend data for the five year period from fiscal year 2005 through fiscal year 2009 shows that the county follows best practices for accounts payable in many areas which

result in efficiencies for the county as well as benefits to vendors. The county has made great progress in its efforts to convert vendors to electronic payment methods and in its use of purchase cards. We believe the county should continue those efforts. We also found the county needs to review guidelines for direct pay and one-time vendors, clean up the vendor master records, review and improve controls for some areas of risk.

Target efforts to convert vendors to electronic payments

The county's increased use of purchase cards and electronic payment methods has reduced the number of checks written, which in turn reduced administrative costs and improved controls. Electronic payment methods are also beneficial to vendors. The number of accounts payable checks decreased 16% from 50,318 in fiscal year 2005 to 42,499 in 2009. The number of electronic payments, which include use of credit cards, ACH, and wire transfers, increased by 233% from 5,245 in fiscal year 2005 to 17,484 in 2009. 142 vendors used some form of electronic payment in fiscal year 2009.

Thirty-five percent of the checks written in fiscal year 2009 required some type of special handling, such as enclosures to be sent with the checks or distribution to departments for handling and mailing. We recommend the county focus on converting these vendors to electronic payment methods, which would result in greater efficiencies by reducing workload for both central AP and departments. We also believe the county should target its efforts to convert vendors who have a large number of payments. We have provided management with a list of vendors that fit these categories.

Clean up vendor master files

Vendor master records are a key internal control for accounts payable in preventing duplicate payments, errors or fraud. Risks for duplicate payments due to vendors with multiple entries in the vendor master file were noted in an accounts payable recovery audit by a consultant in April, 2003; and again in a report from our office, "County Payment Transactions" issued in March 2006. Our review of the vendor master file found the same problems previously noted in both of these reviews. Master files have duplicates for vendor names, and addresses, and show as "active" some vendors that have not had accounts payable activity for

over five years. Some of the risks associated with these problems include the risk of duplicate payments for vendors with multiple vendor numbers, and accurately reporting on vendors that require 1099 reporting for the IRS, and risk of fraud. We provided management with a list of duplicates we found in the vendor master files.

Monitor and revise guidelines for direct pay and one-time vendors

Payments identified as “direct pay” are made to vendors for purchases that do not require competitive solicitation, and are limited to a maximum of \$5,000. Central accounts payable staff review weekly check runs for large dollar payment such as these. According to management, they refer any questionable payments to the county’s contracting office for further review. 476 vendors were paid \$5,000 or more by direct pay in FY 2009, with a total dollar amount over \$117 million. Because the \$5,000 limitation is on the “division” level within a department and because some types of vendors are exempted from this limitation we could not determine how many, if any, of these vendors might be exceptions to the policy limitations outlined in Administrative Procedure FIN-16. Details necessary to evaluate if invoices meet requirements are in paper form and only available at department locations because at this time the county’s SAP does not use the imaging option. We provided a list of these vendors to management for additional review.

The use of one-time vendors allows payments for which setting up a vendor number in the vendor master file is not practical. An example of some of these are small payments to individuals for specific department programs such LIEAP (for energy assistance payments to individuals) or WITNESS (for District Attorney’s witness fee payments). One-time vendors are also used by all departments in some categories such as dues, publications, registrations, and miscellaneous. The county has guidelines for the non-program-specific categories for one-time vendors with limitations, such as for products only, and with some dollar limitations.

Departments are not following the guidelines for one-time vendors as follows: (1) 42% of payments for memberships were over \$100; (2) 74% of the payments for registrations were over \$75;

and (3) we found the guidelines for “products only” are not being followed, nor are those for reimbursing county employees for “things such as the purchase of supplies.” We recommend that management revise the guidelines to better meet county needs. We provided management with a list of the exceptions to one-time vendor guidelines for further review.

We also recommend that management monitor direct pay invoices and the use of one-time payments to maintain good internal controls and monitor compliance with county guidelines and rules. According to management, lack of imaging and work flow in the SAP enterprise system makes monitoring and reviewing payables time consuming for both departments and central accounts payable. We believe imaging and work flow would provide additional controls and efficiencies for managing accounts payable.

Results of accounts payable tests

We performed a number of other traditional AP post audit tests for accounts payable as listed below with references to any recommendations. We also conducted a trend analysis and other summaries of the accounts payable data. A supplementary report with details of these tests was provided to management in a separate report which can be found on our website. See www.co.multnomah.or.us/auditor.

- Invoices to Checks – ratio reflects best practices, no recommendations
- Stratification – trend does not reflect significant drop in small dollar checks, recommend increasing the use of purchase cards (Recommendation #1- b)
- Days to Payment – meets county criteria, no recommendation
- Top 100 Vendors – list may provide additional information on purchasing practices, information only, no recommendation
- Benford’s Analysis – reveals areas of risk where payment amounts are the same, thus greater risk of duplicate payments, also re-occurring payments are at greater risk for errors, recommend additional reviews may be needed

- Duplicate Payments – We tested SAP system controls and found no duplicate payments. Departments can and do bypass the SAP system controls, which increases the risk for duplicate payments. Duplicate payment risks also exist because a vendor may be paid on several vendor numbers, as a one-time vendor, or on a credit card. We recommend that departments review and document internal controls that would prevent duplicate payments (Recommendation #4)
- Sequence Gaps – we found no gaps in check numbers, no recommendation
- Lost Discounts – controls for taking available vendor discounts are at the department level. The ability to review or monitor discounts would be enhanced with SAP imaging. (Recommendation #5)
- Analytics revealed some higher risk areas that require additional study for both controls and possible cost savings. We have provided a list of these for management and may consider some of the areas for future audit projects.

Recommendations

- 1) Central accounts payable should continue efforts to convert vendors to electronic payments as follows:
 - a) Focus efforts on vendors that require additional check handling and those that have a high volume of payments.
 - b) Review use of P-cards and expand to the fullest extent possible.
- 2) Central accounts payable should work with purchasing and departments to better manage and clean up vendor master files including removal of duplicate vendors and unused vendors.
- 3) The county's chief finance officer and accounts payable manager should review the use of direct payment invoices and contracting rules and one-time vendors to:
 - a) Revise guidelines for one-time vendors and clarify contracting rules and exceptions for use of direct pay invoices.
 - b) Increase monitoring compliance with the county's rules and guidelines for direct pay invoices and one-time vendors.

- 4) Department management should review and document their processes and internal controls.
 - a) For check handling and disbursement and the need for inserts mailed with checks.
 - b) That would prevent duplicate payments.
- 5) The county should consider and evaluate the costs and benefits of SAP imaging and workflow to improve controls and provide efficiencies in processing contracts and invoices.



Response to Audit





Department of County Management

MULTNOMAH COUNTY OREGON

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To: Steve March, County Auditor
Judith DeVilliers, Principal Auditor

From: Mindy Harris, Interim Department Director & Chief Financial Officer
Mark Campbell, Interim Director Finance & Risk Management

Date: June 16, 2010

Re: Final Draft of the Accounts Payable Audit

The Department of County Management, and the Finance and Risk Management Division appreciate the time that you and your staff have invested in the review of the County's Accounts Payable operation. We would like to thank you for the thoughtful recommendations and thorough audit. We appreciate the opportunity to comment on your findings and recommendations.

Finance and Risk Management is continuing to pursue several initiatives that will address the recommendations noted in your report. Specifically, the Accounts Payable Manager will be assigned the ownership of vendor master data and associated business process to maintain the data. However, to preserve segregation of duties and best practices, the day-to-day vendor maintenance will be performed outside of accounts payable. A more detailed plan addressing some of the concerns noted in the report regarding the clean-up of vendor data is available for further review. Vendor data clean-up will begin in July, 2010, and should be completed by the end of the year.

The Finance and Risk Management Team will also continue to strengthen compliance on one-time vendors and direct pay type invoices by performing periodic reviews and follow-up discussions with Purchasing Section and appropriate department staffs involved. We will also review and update the Administrative Procedures and other operating procedures to reflect the changes in one-time vendor payment thresholds. Draft changes will be shared with the auditor's office for feedback before implementation.

The management supports your recommendation to implement imaging and business workflow to improve controls and efficiency. We will be discussing this recommendation with Information Technology and determine the next steps.

I agree with the recommendations and appreciate the time and effort taken to compile this report. These recommendations will assist us in improving and strengthening the County's payable processes. We would be happy to provide your office with progress updates or check-ins as we address and implement the recommendations.

cc: Satish Nath, AP Manager