Objective, Scope and Methodology

The objective of this audit was to determine the effectiveness of operations and internal controls to manage risk within the vendor maintenance process.

The scope of the audit was the review of the vendor maintenance process as it existed within the 2014-2015 school year, with testing samples identified on a judgmental basis. Testing and analysis was performed to determine if:

- Procedures were adequate, in writing, approved and communicated
- Vendor additions and changes were appropriately approved, were made in accordance with established procedures and best practices, and were processed in a timely manner.
- Appropriate documentation was in place to support the vendor additions and changes
- Ongoing and periodic vendor validation was effectively performed
- Sufficient internal controls had been implemented to limit exposure to unauthorized or inappropriate transactions

Executive Summary

Vendor maintenance is one of the functions performed within the Accounting Services area of the Financial Services Department. The vendor maintenance process includes receiving, reviewing and maintaining vendor related information within the vendor database (aka vendor master file) which is housed in the Oracle Financial Module. The vendor maintenance process is crucial in preventing the existence of fraudulent vendors and ensuring accuracy of vendor information.

The results of our audit determined that there are several areas for improvement that would increase the effectiveness of operations and internal controls over the vendor maintenance process. These areas include:

- Validating the legitimate existence of vendors prior to adding them to the database
- Requiring management to approve the action to add vendors and to make changes to vendors
- Sending confirmations to vendor documenting the addition and change actions performed in their name
- Deactivating inactive vendors
- Creating thorough written standard operating procedures which include effective internal controls
- Requiring procedures to be followed, re-training of staff and backups, as well as enhancing process monitoring by management

Observations, Recommendations and Management’s Action Plan

Issue 1: Vendor Validation Not Performed

Validating vendors (the action of confirming the legitimate existence of the business or person) through an external source prior to adding them to the district’s vendor database is an internal control designed to help ensure district expenditures are not made to fraudulent vendors. Accounting Services indicated they had not been validating vendors as they had been dependent upon the department requesting
that the vendor be added to the database to ensure the legitimacy of the vendor prior to submitting the request. However, best practice (Contract and Procurement Fraud Vendor Management – Association of Certified Fraud Examiners, 2012 and Managing Risks in Vendor Relations – Association of Certified Fraud Examiners, March 2012) calls for this task to be performed by Accounting Services staff as a defense against internal and external fraud, including erroneous or fraudulent payments.

Recommendation
Internal Audit recommends that the Director of Accounting Services immediately initiate a process to validate vendors through an external source prior to them being added to the vendor database. Internal Audit also recommends that Accounting Services validate all vendors currently in the vendor database and that all payments to vendors identified as non-legitimate be investigated.

Management Action Plan (MAP)
Accounting Services will implement a manual validation process of a Google search or telephone call prior to set-up in the Oracle Vendor Database. In addition, Accounting Services will utilize a 3rd party company to annually verify Tax Identification Numbers (TIN) and Social Security Numbers of active vendors, excluding employee iExpense and Workers Compensation vendors, in the Oracle vendor database and research the efficiency and feasibility of purchasing a software package or online subscription to a Tax ID verification system to validate vendors prior to them being added to the Oracle database.

Estimated Implementation Date
August 1, 2015

Identity, by Position Title, Person Responsible For Implementation of MAP
Accounting Services Director, Accounting Services Assistant Director, and Vendor Maintenance Specialist

Issue 2: Management Did Not Approve Addition of Vendors to Database
The current vendor maintenance process requires the receipt of a request from a district staff member to add a vendor to the database before the vendor will be added. The management of the department requesting a vendor be added to the database should approve the request prior to it being submitted to the vendor maintenance area. In addition, Accounting Service management should approve or authorize, post validation, the addition of a vendor to the vendor database. Management approval/authorization is an internal control designed to help deter the establishment of fraudulent vendors and disbursement schemes such as shell companies or personal purchases using district funds.

Analysis and testing resulted in determining that:

- Current procedure does not require management of the requesting department to approve the request or for management of the Accounting Services department to approve/authorize the addition, post validation
- Management of the requesting department did not consistently approve the request to add the vendors to the database
- Accounting Service management did not approve/authorize any of the additions tested.
Accounting Services indicated they had been depending upon the management of the department requesting that the vendor be added to approve the addition of the vendors to the vendor database and for Procurement Services to approve the “Awarded” vendors.

**Recommendation**
Internal Audit recommends that the Director of Accounting Services initiate action to require the management of the requesting department and management of Accounting Services to approve vendor additions and changes in the vendor database via an automated process. Accounting Services’ approval should occur post validation of the vendor.

**Management’s Action Plan:**
Accounting Services will modify the existing vendor set-up procedures and forms to require campus or departmental management level approval on non-awarded new vendor additions prior to them being added to the Oracle vendor database. Additionally, at the end of each period, the Director of Accounting Services or designee will review and approve a report of all new vendors added to the vendor database.

**Estimated Implementation Date**
July 1, 2015

**Identity, by Position Title, Person Responsible For Implementation of MAP**
Accounting Services Director, Accounting Services Assistant Director, and Vendor Maintenance Specialist

**Issue 3: Confirmation of Addition or Change Not Sent To Vendors**
Vendors should be sent a confirmation of the action taken whenever they are added to the vendor database or when their information is changed within the database. This allows the vendor an opportunity to review the changes for accuracy and to question unauthorized actions that may lead to fraudulent or erroneous payment of district funds.

Analysis and testing determined that the current vendor maintenance process does not include sending a confirmation to the vendor notifying them of the actions taken in their name. Accounting Services indicated that lack of staffing required to perform this manual function has contributed to not distributing confirmations.

**Recommendation**
Internal Audit recommends that the Director of Accounting Services begin sending system generated confirmation to vendors whenever they are added to the vendor database or when changes to an existing vendor’s information occur. Address changes for existing vendors should be sent to both the new and old addresses.

**Management’s Action Plan:**
Accounting Services currently sends a reply email confirmation for vendor additions and changes submitted via email. Requests submitted via fax or mail do not receive a confirmation response. It is not cost effective to the District to send out two letters via US mail every time address updates/changes are made on a supplier’s account. Accounting Services will send email confirmations for all addition and change requests submitted to the Oracle Supplier Maintenance team. Accounting Services will log a service ticket with Information Technology to investigate the possibility of having automatic email
alert notifications sent to vendors whenever updates or changes are made to their account information. The notification would alert the vendor to contact the DISD Vendor Maintenance department if they did not initiate or authorize the changes/updates made to their account.

Estimated Implementation Date
July 1, 2015

Identity, by Position Title, Person Responsible For Implementation of MAP
Accounting Services Director, Accounting Services Assistant Director, and Vendor Maintenance Specialist

Issue 4: Vendor Deactivation Process Not Effective

Periodic deactivation of non-active vendors within the vendor database is a common internal control used to prevent fraudulent or erroneous payments from being created. Not performing an effective deactivation process leaves inactive vendors in the vendor database and available for processing of erroneous or fraudulent payments. Testing confirmed that a deactivation process is periodically performed by Accounting Services and was last performed on July 12, 2014, using vendor data as of May 28, 2014.

Testing of the deactivation process identified 19 of 25 (76%) judgmentally selected active vendors met the criteria for deactivation. Research initiated by Accounting Services resulted in identifying two "script bugs" within the process run by Information Technology to identify vendors that met the deactivated criteria. The "script bugs" included: 1) skipping records where no “Vendor Type” was defined in the applicable database field, and 2) skipping records where “quotes” were read as open Purchase Orders.

Recommendation
Internal Audit recommends that the Director of Accounting Services enhance the periodic deactivation process to ensure all vendors meeting the deactivation criteria are deactivated, including working with Information Technology to remove the identified "script bugs". In addition, Internal Audit recommends that all blank “Vendor Type” fields within the database be populated.

Management’s Action Plan:
As of May 5, 2015, there are no current active suppliers in the Oracle Vendor database that do not have a valid vendor type populated. Accounting Services has worked with Information Technology to correct the “script bugs” in the end of year deactivation process. A service ticket has been submitted to run the process as of May 25, 2015. When the data is provided, Accounting Services will validate the data, and deactivation process will be completed by July 31, 2015.

Estimated Implementation Date
July 31, 2015

Identity, by Position Title, Person Responsible For Implementation of MAP
Accounting Services Director, Accounting Services Assistant Director, and Vendor Maintenance Specialist
**Issue 5: Vendor Maintenance Procedures Do Not Include Sufficient Detail**

Written standard operating procedures are created to ensure compliance, to address operational needs, to manage risk, for continuous improvement, and as a training media for new and back-up staff. The effect of not documenting the vendor maintenance standard operating procedures in detail places the district in a position of not having assurance that needed internal controls exist or that staff is aware of all actions that they should perform.

Testing determined that the two written vendor addition and change procedures did not detail all of the actions performed by staff throughout the performance of the vendor addition or change processes. Accounting Services indicated that limited oversight has been directed toward the vendor maintenance function since its move from Procurement Services to Accounting Services in 2012. The staff person performing the vendor maintenance process moved with the function and continued the process that was in place at the time of the move.

**Recommendation**

Internal Audit recommends that the Director of Accounting Services ensures vendor maintenance standard operating written procedures are enhanced to include all steps that should be taken during the performance of the vendor maintenance tasks and include internal controls designed to limit exposure to unauthorized or inappropriate transactions, as discussed throughout the audit.

**Management’s Action Plan:**

Accounting Services will consolidate and update written procedures for the Vendor Maintenance Specialist role.

**Estimated Implementation Date**

August 15, 2015

**Identity, by Position Title, Person Responsible For Implementation of MAP**

Accounting Services Director, Accounting Services Assistant Director, and Vendor Maintenance Specialist

**Issue 6: Procedures or Internal Controls Not Consistently Followed or Performed**

Written standard operating procedures should be followed to ensure compliance, to address operational needs (consistency in performing a process), and to manage risk (internal controls). The effect of not following established procedures or establishing effective controls could include, among other adverse actions led to remittance information not being sent to vendor, delay of payments, payments being mailed to wrong address, inability to contact vendor, inability to prove who requested vendor be added, and inability to prove e-payable payment method was established.

Testing determined that the following procedure steps and expected internal controls were not consistently followed or performed during the vendor addition and change processes:

- Action to add/change vendor not occurring within 72 hours of receipt of request
- Vendor application and change forms received date not documented
- Verification of existence of P1-C, service or term agreement/contract not performed
- Request from district staff member to add vendor is missing or vendors name and identity of product or service is missing from request
• Required information missing from the applications: i.e., vendor contact title, remittance e-mail, payment option, felony statement, and certifying title
• Vendor changes made based upon receipt of e-mails and invoice, rather than vendor change form
• Manually entered and defaulted information missing or incorrect within the database; i.e., “General Comments” section not populated with date and name/initials of person performing the addition/change, Phone Numbers, Banking Information, Contact Information, Enforce Ship To, Receipt Routing, Quantity Received Tolerance, Quantity Received Exceptions, Days Early Receipt Allowed/Days Late Receipt Allowed, Allow Substitutions, Receipt Date Exception, Invoice Currency, and Payment Currency
• Required supporting documentation missing and/or not effectively secured: i.e., copy of staff request to add vendor, W9/Social Security Card, copy of checks for ACH set up and E-payable set up confirmation

Accounting Services indicated that limited management oversight has been directed toward the vendor maintenance function since its move from Procurement Services to Accounting Services in 2012.

Recommendation
Internal Audit recommends that the Director of Accounting Services enhance written standard operating procedures to address all steps/actions that should be taken by vendor maintenance staff, provide staff additional training, work with Information Technology to ensure default fields within the vendor database populate correctly, and document and perform a periodic management monitoring process of the vendor maintenance functions.

Management’s Action Plan:
Accounting Services will consolidate and update written procedures for the Vendor Maintenance Specialist role. Training for existing staff and back-up staff will be presented on the updated and consolidated procedures. Accounting Services will partner with Information Technology to validate the rules and conditions for various default fields to ensure that they populate correctly. The Assistant Director of Accounting Services has requested the creation of custom vendor maintenance transaction reports that will be used to monitor activity.

Estimated Implementation Date
September 31, 2015

Identity, by Position Title, Person Responsible For Implementation of MAP
Accounting Services Director, Accounting Services Assistant Director, and Vendor Maintenance Specialist

Issue 7: Focused Analysis of Vendor Database Identified Issues
The vendor database is the repository of a considerable amount of information about an organization's vendors. Maintaining a clean and error free vendor database is an internal control designed to manage risk as it has a direct correlation to the accuracy of payment transactions. The effect of not maintaining a clean and error free vendor database could result in false vendors, erroneous or duplicate payments, and a delay of payments among other adverse consequences.

A test of the vendor database determined issues within the data as follows:
• Vendors could not be verified as legitimately existing
Employees received pay as a vendor, while employed with the district - employees included in the database as an Employee vendor type and as either a Services, Other, or Athletic Official vendor type

- Taxpayer IDs were missing from the database or were incorrect within the database
- The same Taxpayer IDs was assigned to more than one vendor record
- Employees with Workers Compensation vendor types were not identified in the appropriate fields as employees, nor were their employee numbers included in the applicable field

Accounting Services indicated that limited oversight has been directed toward the vendor maintenance function since its move from Procurement Services to Accounting Services in 2012.

**Recommendation**
Internal Audit recommends that the Director of Accounting Services initiate a project to clean up of the vendor database.

**Management’s Action Plan:** Accounting Services will partner with Information Technology to scrub the current vendor database records and make appropriate corrections for identified items 2, 3, 4 and 5 listed below. Item number 1 will be addressed as part of the Tax Identification Number (TIN) validation being completed in response to Issue number 1 – Vendor Validation not Performed.

**Estimated Implementation Date**
September 30, 2015

**Identity, by Position Title, Person Responsible For Implementation of MAP**
Accounting Services Director, Accounting Services Assistant Director, and Vendor Maintenance Specialist