



Internal Control and Organizational Performance

Accounts Payable Audit

Operating Unit: Niagara Region

Date of Audit: November 2018 to January 2019

Auditors: MNP LLP

Distributed To: Niagara Region Audit Committee
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EXECUTIVE SUMMARY

BACKGROUND

In accordance with the 2018 Audit Plan, Internal Control and Organizational Performance (ICOP) contracted MNP LLP (MNP) to perform a comprehensive review of the internal controls surrounding Niagara Region's Accounts Payable process.

The purpose of the audit was to assess the control framework in place to ensure appropriate, accurate, timely and efficient processing of Niagara Region's vendor payables in accordance with its policy and legislative requirements.

The audit methodology used by ICOP included a review of relevant documentation, analysis of payment transaction data, and interviews with key individuals involved in the process. The period covered by the audit was July 1, 2016 to October 31, 2018.

Appendix II identifies further background information related to Niagara Region's Accounts Payable processes and other relevant information for readers of this report.

SCOPE

The scope of the audit focused on assessing the following:

- Adequate controls in place to process payments in an efficient, accurate, complete and timely manner;
- Review of accounts payable transactions for duplicate payments to vendors and/or unusual activities;
- Invoices paid to vendors in accordance with Regional payment strategy;
- Adequate controls in place to determine that supplier management is adequately achieved; and,
- Physical security of cheques.

A sample of 80 payment transactions were selected and reviewed in detail from the full payment population of 229,520 for the period of July 1, 2016 to October 31, 2018. In addition, the vendor master file containing 8,221 vendors as at October 31, 2018 was reviewed.

Areas that were out of scope of this audit included:

- Accounts Payable transactions related to:
 - Niagara Regional Housing;
 - Niagara Regional Police Services; and,
 - Ontario Works.
- Employee reimbursements;
- Period and year end accruals;
- Information technology general controls and information technology application controls; and,
- Purchases made using a Niagara Region Purchasing Card (PCard).

INTERNAL AUDIT FINDINGS

While there are areas for improvement, the overall internal control environment is effective. The following areas were found to be strengths of the accounts payable process and controls:

- There is an appropriate segregation of duties between the Purchasing and Accounts Payable functions;
- There is an automated three-way match (for goods) between a purchase order, receipt of goods, and invoice; and a two-way match (for services) between a purchase order and invoice before a payment can be made within the system;
- The Region has safeguards in place for the physical security of manual cheque stock; and,
- Performance measures/metrics for Niagara Region accounts payable are comparable, and sometimes better, when assessed against other municipalities' performance measures/metrics as reported within Municipal Benchmarking Network (MBN) Canada Performance Measurement Reports/data.

The listing below provides a summary of the observations and areas of improvement. Detailed observations and recommendations can be found in the next section of this report.

- 1) Maintenance and review of vendor master file information.
- 2) System logging and reporting of delegation of authority.

ICOP and MNP appreciate the assistance and co-operation from the staff in the Enterprise Resource Management Services department during the audit.

OBSERVATIONS AND RECOMMENDATIONS

The following are all the observations from the audit along with recommendations and Management's Action Plans to address these issues. See Appendix I for the risk ranking justification.

Observation #1 – Maintenance and review of vendor master file information	
Risk Ranking	LOW
<p>During the audit, various analyses were performed on the vendor master file¹ to assess: (1) if the information contained within the PeopleSoft system is complete; (2) if there are duplicate vendors contained in the master file; and (3) if there are instances where vendor and employee addresses are the same. The following provides a summary of the details of the analysis conducted and results of the analysis for each of these areas:</p> <p><u>Incomplete and/or missing information</u></p> <p>An analysis of the vendor master file was conducted to determine if the information contained within the PeopleSoft system is complete. Queries were performed to determine the type of information missing, such as postal codes, telephone numbers, and payment information. The PeopleSoft system requires that the name and address of a vendor be entered during vendor set-up.</p> <p>Our analysis found the following information missing from the vendor master file:</p> <ul style="list-style-type: none">• Eight vendors did not have a postal code;• 3,397 vendors did not have a telephone number; and,• 161 vendors did not have the method of payment. <p>In addition to the above queries, further analysis was conducted, and it was found that 429 vendors have P.O. Box addresses.</p> <p><u>Duplicate vendors</u></p> <p>An analysis of the vendor master file was conducted to determine the number of duplicate vendors within the master file. Queries were performed to determine if there are:</p> <ul style="list-style-type: none">• Vendors with the same ID#, same name and same address;• Vendors with the same ID#, same name but different address; and• Vendors with different ID#, but with same name and same address. <p>Our analysis found the following:</p> <ul style="list-style-type: none">• 56 instances of vendors with the same ID#, same name and same address – from reviewing the results, the PeopleSoft system contains 56 instances of duplicate information, having records with the same vendor ID# twice (three times for two instances), same vendor name and same address within the vendor master file.• 148 instances of vendors with the same ID#, same name but different address – from reviewing the results, the PeopleSoft system contains 148 instances of vendors	

¹ The vendor master file contained 8,221 commercial suppliers/vendors as at October 31, 2018. Rent supplement program clients were removed when conducting the analyses since Niagara Regional Housing transactions are not within the scope of the audit.

that have the same ID# and same name, but different address. It is our understanding that the practice of having multiple vendors with the same ID is acceptable within the system, as there are vendors that the Region uses that have different locations and addresses, which the system is able to accommodate.

- **7 instances of vendors with different ID#s, but with the same name and same address** – from reviewing the results, there are 7 instances which have the same vendor name and address, however, have been set up within the PeopleSoft system with different vendor ID#s (totalling 20 different vendor ID#s).

Vendor and employee addresses

Our analysis between the Niagara Region's employee listing and vendor master file as at October 31, 2018, identified 23 instances where employees and vendors share the same addresses. The 23 instances were investigated further by ICOP and Human Resources and their review did not identify any non-compliance.

Implication

Having current and complete master vendor list facilitates timely and efficient payments to vendors, as well as aids in communicating with vendors.

Having duplicate vendors within the master vendor list may lead to double payments or could indicate fictitious vendor set-up (and lead to potential fraud).

Other fictitious vendor "red flags" include use of P.O. Box addresses and vendors which have been set-up with employee addresses.

Recommendation

- 1) Maintenance should be conducted on the master vendor file on a regular basis (i.e. at least annually). This would include the following activities to ensure completeness and accuracy:
 - a) Review and update the vendor master information.
 - b) Obtain missing or incomplete data such as missing telephone numbers, postal address, complete name, and emails.
 - c) Update any out of date information.
 - d) Determine if there are any vendors (i.e. duplicate vendors) that should be removed from the master file.
 - e) Archive inactive vendors which have had no business activity for a certain amount of time (i.e. for over 18 months). If the vendor is archived, their information can be easily accessed for reinstatement, if needed. By removing inactive vendors, the list becomes leaner and records are easier to access, increasing employee productivity through reduced processing time.

Maintenance activities should include department representatives (in addition to Finance staff), if possible, as they may have insight into information that is old, missing or incorrect.

The Region should also consider if any of the master vendor file review or maintenance activities can be automated as some cleanup activities lend themselves well to automation. In addition, the Region may want to consider the use of a vendor self-service portal where individual vendors can update their information.

- 2) On a regular basis, conduct analysis and further review on areas which may uncover fictitious vendors, such as comparing vendor and employee addresses and vendor use of P.O. Box addresses.

Management Action Plan

Person(s) Responsible	Director, Procurement & Strategic Acquisitions	Completion Date	11/30/2019
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1. While maintenance on the master vendor file including the activities identified in the recommendation is not currently an established process, Procurement is in agreement with the audit recommendation that it should be.

Procurement (Strategic Acquisitions, specifically Strategic Sourcing) with assistance from the ERP Support team will develop a new process (completed annually) for the Supplier Administration function which gives due consideration to the activities/requirements identified above.

Process considerations for initial update and ongoing maintenance could include: Procurement seeking assistance from ERP Support team to extrapolate the vendor data from PeopleSoft Financials and then in conjunction with Finance identify the priority data fields which are omitted/important. Supplier Admin would obtain the missing information or out of date information for the purposes of updating the master vendor file, seeking assistance from the Client Department on an as and when required basis.

With regards to the automation of the master vendor file review or maintenance activities, Procurement will coordinate with the ERP Support team to explore this but it is our understanding that this would not be possible without customization of the PeopleSoft Financials.

With regards to recommendation 1d), Procurement is in agreement that it is important to determine if there are any vendors (i.e. duplicate vendors) that should be removed from the master file but would add that the search would be for “true duplicates” as business decisions during the implementation of PeopleSoft Financials (Deloitte) gave due consideration the creation of duplicate vendor master files, specifically Yardi Landlords, differing currencies and utilities on case to case basis.

With regards to recommendation 1e), Procurement is appreciative of comment however at this time it would not be Procurements intent to create a separate process to

inactivate vendors (and subsequently re-activate them) as we do not envision a gain in efficiency vis a vis a direct correlation between the number of records, accessibility to data and efficiency/productivity. The database which resides within PeopleSoft Financials is solely maintained in an electronic format (no paper copies) and is both searchable by vendor name and exportable to Excel.

2. Procurement has established processes and oversight (separation/segregation between processor and approver) which gives due consideration to legitimacy of the vendor which is being set up in PeopleSoft Financials. Procurement will give further consideration to this recommendation as part of its response to MAP recommendation 1. Procurement will explore the feasibility of completing an annual analysis and review of vendor and employee address, however discussions with the Human Resources division would be required as part of completing the comparative as we suspect that employee information at Niagara Region would be treated as confidential.

Observation #2 – System logging and reporting of delegation of authority

Risk Ranking

LOW

It was noted that the PeopleSoft system is unable to capture and produce a report or log which provides the start and end dates of users who have delegated their authority for the approval of payments. Authority may be delegated within the system for when approvers of transactions and payments go on vacation or are on an extended leave of absence.

While the system is able to provide a report of who approved payments, the report does not include the start and end date of when any delegation of authority was active.

Implication

Reports and logs of approvals and other activities, such as delegation of authority, provide evidence of an audit trail of transactions within the PeopleSoft system.

A robust PeopleSoft report containing management delegated authority by user by date may improve the capability and efficiency of a reviewer to audit past delegated transactions.

Recommendation

- 1) Consider review of the PeopleSoft system to determine if the start and end dates of users who have delegated their approval authority can be captured within the system and reported on.

Management Action Plan

Person Responsible	Associate Director, Finance Operations and Systems	Completion Date	11/30/2019
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At this time, we do not have the capability in our current version of PeopleSoft Financials to audit the start and end dates of when users have turned on their delegated authority. Although a user can choose the start and end date when turning on the delegation function, the back end table in PeopleSoft Financials that tracks delegation is not effectively dated and therefore only records that the function was turned on (not as of/when). As such, we can run a report that shows everyone who has delegation turned on today, but cannot run an historical version of that report.

However, at any point in time, we can easily provide a history of when a delegation of authority was used to approve something (as we provided for the purpose of this audit). Every transaction records when it has been approved “on behalf of” someone else. For example:

- Director of Finance, Helen Chamberlain, turns on delegation of authority for March 4 – 8, 2019, assigning the Associate Director, Budget Planning and Strategy, Margaret Murphy, as her delegate.
- During that period, Margaret Murphy approves several purchase orders, travel and expense reports, and vouchers that would usually be approved by the Director role.
- PeopleSoft Financials records each of those transactions as “Margaret Murphy approved on behalf of Helen Chamberlain”.

If the delegator (Helen Chamberlain, in this example) would like to know what transactions were approved in her absence, PeopleSoft Financials is able to provide that information.

If the concern is that an employee could assign a delegate for the length of their employment and therefore never directly approve transactions, then the available report would show that the employee's user ID has never approved a transaction.

To our knowledge, there is no PeopleSoft Financials out-of-the-box audit logging process that shows effective dating for the delegation function. In theory, we could customize a solution; however, our system strategy is to minimize any customizations and use configuration where possible (to ensure system integrity and reduce opportunity for errors during patching and upgrades). Given that we are able to report on when delegation of authority has been used for approval, we do not perceive the inability to see the effective dates for delegation as a big risk to the reliability of the approval process.

As such, at this time, we are choosing not to proceed with investigating a customized option. Instead, we will agree to review the availability of this functionality within PeopleSoft Financials as we proceed with future upgrades (our next upgrade is scheduled to be completed in November 2019).

APPENDIX I - RATING SCALE

Rating	Definition
CRITICAL	Requires immediate action by Corporate Leadership Team to avert a severe/disastrous risk event in the near-term. Internal controls are deemed to be ineffective, absent or poorly designed. Management Actions Plans (MAP's) are to be implemented immediately to mitigate risk of substantial financial losses, business interruption, loss of reputation and/or environmental, public health & safety risk.
HIGH	Requires prompt action by Management to avert, reduce or transfer a major risk event. Internal controls are deemed to be ineffective, absent or poorly designed. MAP's should be implemented to mitigate the risk of financial losses, loss of reputation, address fraud issues or legal/regulatory non-compliance.
MEDIUM	Requires timely actions by Management to reduce risks to a low level. Internal controls are deemed to be ineffective or poorly designed. Management action is required, but is not immediate. Moderate financial losses, temporary/minor reputational impairment, lesser potential for fraud or regulatory non-compliance may occur without timely MAP's.
LOW	Management actions are recommended to address the weaknesses identified. Internal controls are operating effectively or partially address the control objective; however they may be poorly designed and/or operational inefficiencies exist which may result in an opportunity for improvement. Low risk events may cause operational inconvenience or minor financial losses.

APPENDIX II – ACCOUNTS PAYABLE BACKGROUND INFORMATION

Niagara Region changed its financial accounting and procurement processes and converted from Smartstream to Oracle's integrated PeopleSoft Financials system in February 2016 resulting in the conversion of 2,428 purchase orders to the new system. The Purchasing module of the PeopleSoft system manages the purchase of goods/services from suppliers, allowing:

- ✓ All employees to create requisitions online to order goods and services; and
- ✓ Users to create receipts of goods online to ensure end-to-end processing.

The Accounts Payable module of the PeopleSoft system facilitates matching and triggers payment to suppliers by enabling:

- ✓ The creation of payment vouchers for all invoices; and
- ✓ Making payments to suppliers based on selected payment methods (i.e. cheque or electronic funds transfer).

At a high level, the following process steps are followed for making payments through the PeopleSoft system:

- An online purchase requisition is originated by a requestor and approved, which in turn, causes the creation of a purchase order that is approved and sent to a supplier.
- When goods are received by a requestor, a receipt is created, and the system automatically matches this receipt to the purchase order and supplier's invoice.
- Upon receipt of a supplier's invoice, an invoice voucher is created in the system that is matched automatically to the receipt.
- Vouchers and invoices are reviewed and approved online.
- Once matching occurs (three-way (i.e. Purchase Order-Invoice-Receipt) for goods and two-way (i.e. Purchase Order-Invoice) for services), the system triggers a payment to the supplier either by cheque or electronic funds transfer.

The following table provides details of the data that was reviewed during the accounts payable audit:

Item	Qty	\$
Total Population of Transactions for July 1, 2016 to October 31, 2018	229,520	\$1.6 billion
Total Transactions Sampled	80	\$57 million
Errors Noted	0	0
Number of vendors in Master Vendor File	8,223	-
Number of Employees	3,610	-
Average Purchases over five years (2013 to 2017)	-	\$385 million

Niagara Region is part of, and contributes data to, the 16-member Municipal Benchmarking Network (MBN) of Canada. MBN Canada collects the data and calculates selected performance measures to indicate how a municipality is performing, comparative to other municipalities within the network, in a variety of different areas (including accounts payable).

Five years (from 2013 to 2017) of the Niagara Region's results for eight accounts payable measures (which were provided to and compiled by MBN Canada for each year's Performance Measurement Report) were analyzed during the audit and compared to the other MBN member municipality results, as reported in MBN Canada Performance Measurement Reports.

The analysis of the eight accounts payable measures are listed in the table below. Upon review, Niagara has performed comparably well, and better in some cases, in the accounts payable measures:

#	Item	Niagara Region	Median of other member Municipalities
1	Number of invoices processed per \$1-m of purchases	248	248
2	Operating cost to process an invoice	\$5.51	\$5.91
3	Number of invoices processed by each accounts payable staff	12,708	13,159 (Note 1)
4	Percent of invoices paid within 30 days	82%	73%
5	Percent of payments that are electronic	67%	58%
6	Total purchases	\$385 million	\$503 million
7	Percent of goods and services purchased (Operating and Capital) through a centralized procurement process	60%	59%
8	Operating costs for centralized purchasing per \$1,000 municipal purchases (Operating and Capital) through a procurement process	\$2.60	\$5.36

Note 1 – Other municipalities include P-Card and Expense Statement transaction data in this calculation while Niagara Region does not.