



INTERNAL AUDIT

**Follow-up of the Limited Scope Assessment of the Vendor Master
File Review**

R-23-05

September 3, 2024

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Rating Matrix

Descriptor	Guide
High	Matters considered being fundamental to the maintenance of internal control or good corporate governance. These matters should be subject to agreed remedial action within three months.
Medium	Matters considered being important to the maintenance of internal control or good corporate governance. These matters should be subject to agreed remedial action within six months.
Low	Matters considered being of minor importance to the maintenance of internal control or good corporate governance or that represents an opportunity for improving the efficiency of existing processes. These matters should be subject to agreed remedial action and further evaluation within twelve months.

Distribution List

Title	For Action ¹	For Information	Reviewed prior to release
Audit Committee		*	
Executive Director		*	*
Chief Financial Officer	*	*	
Comptroller		*	
Deputy Comptroller		*	
Accounting Supervisor		*	

¹For Action indicates that a person is responsible, either directly or indirectly depending on their role in the process, for addressing an audit finding.

Executive Summary

Introduction

The Audit Committee directed Internal Audit (“IA”, alternatively referred to as “we”) to conduct an engagement over the Vendor Master File to determine whether controls are designed to effectively manage vendor payments and reduce the likelihood and impact of fraud, waste, and abuse. We completed the initial phase in May 2023 but did not publicly release the report because of security concerns. We completed the follow-up phase on June 25, 2024 and conducted it in accordance with the International Standards for the Professional Practice of Internal Audit, published by the Institute for Internal Auditors.

Background and Overview

A vendor master file (“VMF”), for purposes of this report, refers to the database of vendor information used by the Accounts Payable team (“AP”) as the list of vendors approved for payments. While AP are the users of the VMF, the Accounting team (“Accountants”) enters information into the database as a function of separation of duty (“SOD”). A well-controlled and managed VMF is essential for accurate and timely payments, and for reducing fraudulent abuse of the accounts payable system.

Objectives and Scope

Initial Phase Scope:

This engagement had two primary objectives: 1) Determine the existence and strength of control activities around the VMF 2) Determine the validity of existing data in the VMF.

The VMF has 23 types of records for different purposes, such as payments to payroll vendors, pension, claims, etc. This engagement was focused on type “V” which are the typical suppliers paid by AP. Transactions reviewed were focused on payment batches approved between 1/1/2021 – 1/31/2023.

Follow-up Phase Scope:

We reviewed management’s progress on action plans during the follow-up phase of the engagement. We tested key VMF data, such as attribute completeness. We hired a consultant, Greenskies Analytics, to test UTA data against the Internal Revenue Service (“IRS”) database for accuracy of vendor’s taxpayer identification numbers (TIN) and entity names. Finally, we performed a stress test to determine if AP could detect a false invoice and false vendor.

Summary

Initial Phase Summary:

The Accounting department needs to implement a more clearly defined and controlled process over the VMF. This need is shown by inaccurate information in the database, control gaps that expose the organization to fraud, and a generally informal approach to adding new records and managing existing records.

A significant SOD violation was noted and resolved. A particular user in the Accounting department could add and edit vendors and add and approve payments. This issue was brought to management’s attention, and they promptly changed the user’s access rights. It must be emphasized that there is no evidence that the employee inappropriately abused this access.

Management is committed to addressing the record and control issues noted in the engagement. IA would like to thank them for their diligence and attention completing the engagement.

Follow-up Phase Summary:

Management implemented new procedures to vet vendors and verify accuracy of TIN, and we believe these procedures are well designed and sufficient. We tested compliance with these procedures and found that they are not always followed for new vendor additions. We do not have high present concern over these results given that new processes take time to mature and become habits to the employees performing them. We encourage management to continue to emphasize these processes and measure success.

We found that the VMF still has data consistency issues, such as missing contact information and duplicate vendors. Our most significant concern was that 526 vendors did not have any transactions from 1/1/2023 – 1/9/2024. We recommend that management request complete contact information from active vendors and deactivate vendors that have not had transactions in the past year.

We performed a stress test of management’s current procedures by submitting a fake invoice for a fake vendor. The AP team successfully detected the invalid transaction and stopped the process.

Management demonstrated significant improvement to the control environment in this follow-up phase from the initial phase. We commend their efforts and dedication and invite them to continue to implement meaningful action plans. We will keep the initial phase action plans open with a status of “pending remediation” and will follow-up on progress in two years.

Initial Phase Issue Status

Criteria

The Committee of Sponsoring Organizations of the Treadway Commission (“COSO”) publishes an integrated framework to guide organizations on best practices for internal controls. Component Three: Control Activities, Principle 12 of this framework, states:

The organization deploys control activities through policies that establish what is expected and procedures that put policies into action.

The Points of Focus for Principle 12 further elaborates:

Management establishes control activities that are built into business processes and employees’ day-to-day activities through policies establishing what is expected and relevant procedures specifying actions.

Condition

The Accounting department has not developed sufficient processes to ensure the accuracy and validity of vendor information in the VMF.

Cause

- a. The Accounts Payable team has historically operated lean and lacked the resources to develop and maintain a robust control process. The team is currently at six and now better resourced to implement controls.
- b. Roles and responsibilities between the Accounts Payable team and Accountants was unclear.
- c. A former employee performed, or was believed to have performed, certain tasks to validate new vendors. These tasks were not communicated to the successor.
- d. New hires to the Accounts Payable team did not receive sufficient training or instruction on properly validating new vendors.

Effect

1. The current VMF contains inaccurate, incomplete, or missing information, including:
 - Tax identification number (“TIN”) is missing on 311 vendors.
 - The TIN for 25 vendors are not valid within the database of the Internal Revenue Service (“IRS”).
 - The name and TIN combination for 148 vendors do not match IRS records.
 - Duplicate or similar names existed for 46 vendors.
 - 964 vendors do not have a phone number on file.
 - 710 vendors do not have an email address.
 - IA reviewed a sample of 25 vendors added or edited since 2021. Four of the vendors had no attachments, indicating that there is no W-9 on file.

- IA reviewed a sample of the name, address, and phone number data for 179 VMF records against an internet search engine and found the following inaccuracies¹:
 - 29 incorrect names
 - 30 incorrect addresses
 - 2 with no address listed
 - 44 incorrect or missing phone numbers
- 2. Low or no use vendors with an active profile have a higher risk of being “hijacked” by an employee with access to the information without detection. Analysis of transactions per supplier from the approximate range of 1/1/2021 – 1/31/2023 showed a high rate of low to no use vendors with active profiles:
 - 13% of active vendors (163/1,238) had zero transactions during the 25-month period reviewed.
 - 54% (671/1,238) had between one and ten transactions during the 25-month period reviewed.
 - 20% (252/1,238) had between 11 and 50 transactions during the 25-month period reviewed.
- 3. Fraud and abuse are more likely to occur if proper vendor validating does not occur. IA demonstrated this by successfully submitting a fake invoice to Accounts Payable. The invoice was stopped at a point planned by the auditor (no funds were paid out), but it went far enough in the process to show that the current controls are insufficient to prevent fraud and abuse.
- 4. Inaccurate or incomplete TIN may cause compliance failures with 1099 tax reporting requirements.

Recommendation

1. A formal process should be developed to validate new vendors.
2. Roles and responsibilities between the Accounts Payable team and Accountants should be clearly defined and documented.
3. An IRS TIN match should be performed for new vendors additions.
4. Existing data errors should be investigated and resolved.

Management Response and Action Plan

- The AP team had a preliminary meeting with the Accountants to discuss a plan.
- The Accounting Supervisor met with the Enterprise Systems and Records departments to ensure data security and compliance with vendor sensitive information.
- The Accounting Supervisor is putting together a Laserfiche form that AP and anyone that is needing a Vendor added, updated, or amended fills out.
- The form will then route to a second individual who will then call the vendor and do an internet search on the address to confirm the information to be accurate.
- The form will then route to a special Laserfiche bucket for the Accountants where they will then do an IRS TIN check to ensure the name and TIN match.
- The Accountants team will then perform the requested addition, update or amendment as requested, when the search comes back confirming TIN and name match.
- The Accounting Supervisor and the AP will be performing a review and research the existing Vendor list and request W9s or inactivate the unused vendors if applicable.
 - Note: We are not able to inactivate vendors if there is an outstanding PO (Purchase order) that still has funds on it. Even if it has been more than two years since their last payment.

Target Completion Date

- Completed: Preliminary meeting (AP) with Accountants to discuss a plan.

¹ This test should be understood as an informal demonstration that potentially inaccurate information persists in the VMF. If management elects to validate and correct existing information they should do so through formal sources, preferably confirming with the vendor directly.

- Completed: The Accounting Supervisor has met with the Enterprise Systems and Records departments for first steps on new form.
- June 1st, 2023: New Laserfiche form draft submitted to Enterprise Systems to create.
- July 1st, 2023: Testing of completed form in Laserfiche.
- August 1st, 2023: Training of purchasing and all parties on the new form completed and start using form.
- August 1st, 2023: Have access and go live on the new form and the IRS Website (Accountants).
- December 31st, 2023: Review of all outstanding old vendors cleaned up and accurate for daily business needs.

Follow-up Phase Issue Status

Current Status

Pending Remediation

Management implemented a new checklist form with actions for employees to perform to verify the legitimacy of new vendors. They also validate vendor provided TIN against IRS records. We believe these are strongly designed and properly measured controls. We tested a sample of 25 new vendors added to the VMF to verify the rate these new procedures are followed. Management did not document the checklist for eight of the vendors and did not retain evidence of TIN match for 14 of the vendors. Management should continue to mature these procedures.

We analyzed the fidelity of VMF data and found opportunities for management to clean existing records. For example, 1,321 vendor records do not have a phone number; 936 do not have an email address; 14 vendor names were exact or near duplicates; 158 had a mismatch of name and TIN; six had an invalid TIN. Our most concerning find in the data was that 526 vendors did not have a transaction from 1/1/2023 – 1/9/2024. We recommend that management request complete contact information from active vendors and deactivate vendors that have not had transactions in the past year.

We performed a stress test of management’s current procedures by submitting a fake invoice for a fake vendor. The AP team successfully detected the invalid transaction by following the newly designed checklist procedures. Their success in this stress test is a strong indication that management’s new processes, when followed, are a strong control.

Overall, we recognize that management has made significant and well-designed changes to improve the internal controls of the VMF. We will keep the status as “pending remediation” but follow-up will be in two years instead of the typical one year.

Management Response and Action Plan

Accounting management is aware of the need to improve consistency with the new procedures. We will continue to focus on training and accuracy when inputting new vendors into the VMF database. As encouraged, we will continue to emphasize these processes and measure success. As to the most concerning finding of 526 inactive vendors, we will work with IT staff to identify and confirm vendors with no transactions and provide information to Procurement to coordinate so that purchase orders can be closed out where appropriate. We will then be able to close vendor records that are currently inactive but open due to purchase order balances.

Target Completion Date

December 31, 2024