

CITY OF ALBANY

Office of Audit and Control

Report on the 2012 Accounts Payable Audit Process

**Audit Report
May 2013**

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Executive Summary

This report provides a synopsis and analysis of data collected during the Office of Audit & Control's 2012 Accounts Payable audit process. The City of Albany paid approximately 19,000 invoices during the audit period and the Office of Audit & Control (OAC) was tasked with examining those invoices prior to payment, and rejecting any that do not meet standards. In February, 2012, the Office of Audit and Control amended its ongoing accounts payable audit processes and procedures to function as a more formal audit process.

While the vast majority of vouchers and invoices proceed through the process without issue, during the year it became clear that certain problem issues needed to be addressed.

Payments to vendors were, at times, delayed for excessive amounts of time. At times delaying payments can be acceptable, such as when a vendor fails to properly complete the City's order, or when vendors improperly bill the City and adjustments must be made. Unnecessary delays at the Department level caused by closed Purchase Orders, lost paperwork, poor tracking, etc, are not acceptable. OAC staff found a disproportionate number of very lengthy payment delays from the Water Department and OAC has undertaken a full audit of the Water Department's Accounts Payable functions.

Unaddressed vendor pricing issues can waste taxpayer money. OAC found that some City departments had approved some payments for more than the contracted amounts. This was a result of a small number of vendors mischarging for goods or services. In each of the cases identified by OAC staff, the City either paid the correct amount or was credited for past overpayment.

Discussions with the Legal Department have lead to refinements to the contracting process that should help protect the City from some overcharges in the future. OAC will continue to intently watch for vendor overcharges in an effort to ensure all charges are warranted and valid.

Overall, the recorded trends show that the highest volume of problem invoices were sent to OAC during the first quarter of the year with significant declines after the 2011 invoices had all been processed. As this was the first year of data collection, any large scale trends or long-term effects of policy changes will not be seen in the data.

Many of the issues identified in the audit review process, and this report, could be corrected by more diligent tracking and recording of purchases, invoices, and expenditures at the department level. Additional issues could be addressed with a periodically updated Purchasing Manual. The current manual dates to 1995.

Background

This ongoing audit was initiated because the City Charter instructs the Office of Audit and Control (OAC) to "warrant as valid all accounts payable and claims prior to payment". While OAC has continuously performed this duty, and the Comptroller's Office did so previously, it wasn't until February 2012 that the task was converted into a more formal audit process.

This new audit process focuses on the tracking and analysis of audited invoices, and therefore provides OAC with the required data to quantify and address problems as they're uncovered. OAC also uses the process, and the data it outputs, as a risk assessment tool to aid in the planning of future audits.

An intended effect of the new process is a greater level of accountability – be it from its vendors, departments, or city staff. It is also intended to function as a management tool for individual departments to improve performance and compliance citywide.

OAC must, as per government auditing standards, mitigate impairments to its independence – in this case, by performing this required audit process while remaining separate from the City's management functions. To address this, OAC has taken steps to ensure this audit function is separate. The Office:

- Does not alter or edit documentation submitted to it by the Departments unless in the case of minor typographical errors or omissions; these changes must not directly affect the substance of the invoice/voucher.
- Returns all non-compliant documentation to the Departments or Purchasing for correction or administrative approval of issues that cannot be corrected.

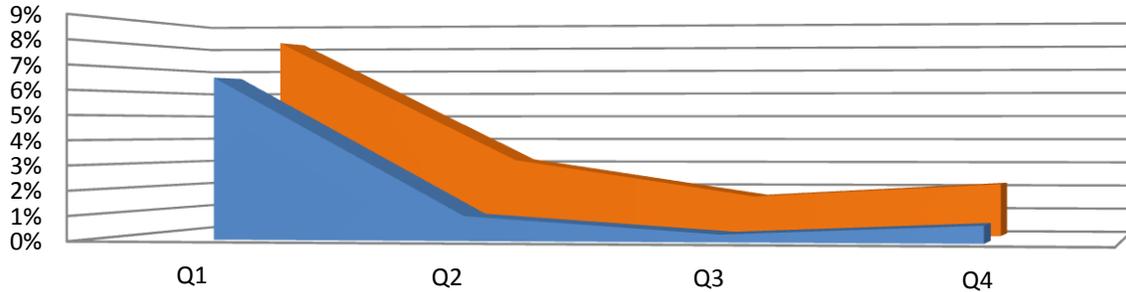
With this being the first year of this new audit process, we are confident that our staff did not identify every exception in the approximately 19,000 invoices that were manually audited. We do have confidence that by following a consistent methodology, we found a very large and representative sample of the exceptions. Audit staff was able to utilize the City's financial computer system to identify nearly all of the invoices that arrived at OAC over four months after the invoice date.

Analysis

The City of Albany processed approximately 19,000 invoices in 2012 from mid-February through December. Overall, of those invoices, 683 (3.64%) were aged 4 months or more and 289 (1.54%) were recorded as 'exceptions'. Invoices can, and do, end up on both lists.

Overall Trends for 2012- From Q1 to Q2, 2012, the percentage of invoices audited that qualified as aging and/or exceptions declined sharply, and then remained fairly level and low. This is to be expected, and follows the trend experienced in previous years by OAC staff, and the Comptroller's Office prior to that. Whether this drop is greater than in previous years is unknown because this is the first year that problematic invoices have been tracked in this fashion. Typically, first quarter invoice submissions include 'stragglers' from the prior year, invoices that were not submitted on time for various reasons. These late invoices are often tied to purchase orders (or budget lines/accounts) that have been completely expended or closed at year end.

Percentage of Audited Invoices in 2012 Flagged as Exceptions or Aged



	Q1	Q2	Q3	Q4
Exceptions	6.5%	1.0%	0.3%	0.7%
Aged	8.1%	3.1%	1.6%	2.2%

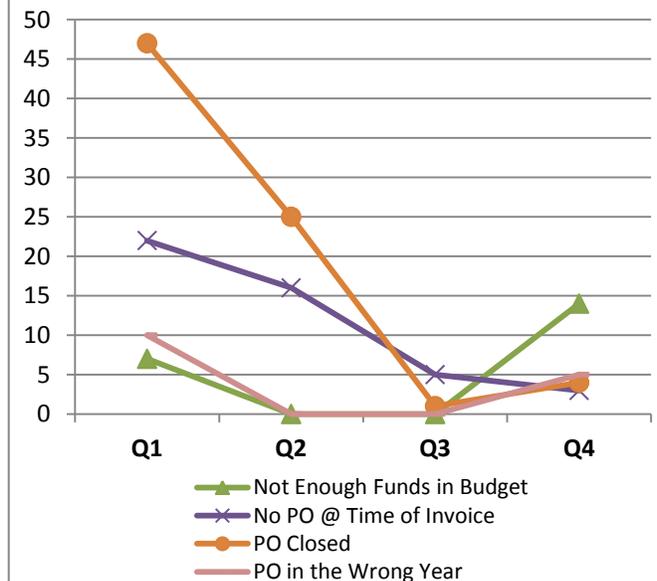
The influx of exceptions during the first and second quarter is reflected in the individual trends displayed on the following two graphs.

Exceptions due to purchase orders being closed, absent (No PO @ Time of Invoice), or those written for the wrong budget year were prevalent in Q1 of 2012.

The resurgence of these specific issues in Q4 was expected, as the problematic invoices begin to arrive at year-end as departments rush to clear up issues and get ready for the new year.

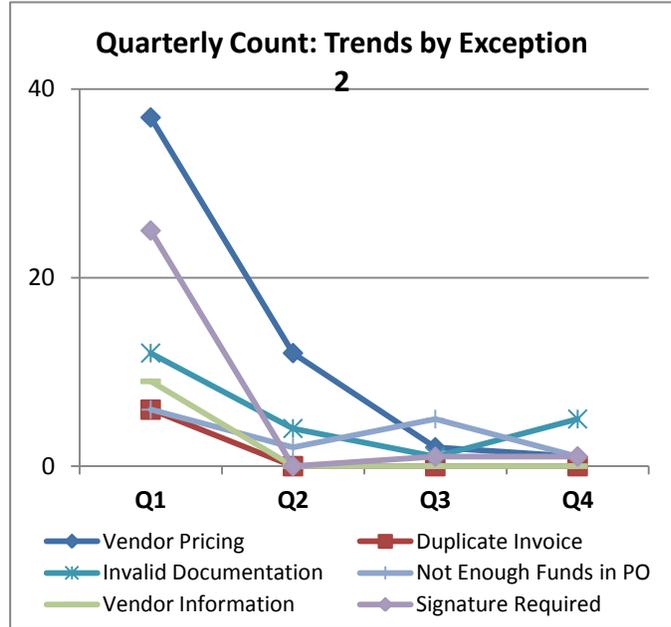
Vendor pricing exceptions were high at the start of 2012. OAC found that two vendors who supply the City with uniforms were, at times, improperly billing the city a rate higher than the agreed upon contract pricing. While the difference was minor per instance, the overcharging had been going on for some time, affected a large volume of invoice submissions, and therefore began to add up. Correcting the issue resulted in credit to the City's accounts for the overcharges. Since the correction, further significant issues with the two companies have not occurred.

Quarterly Count: Trends by Exception



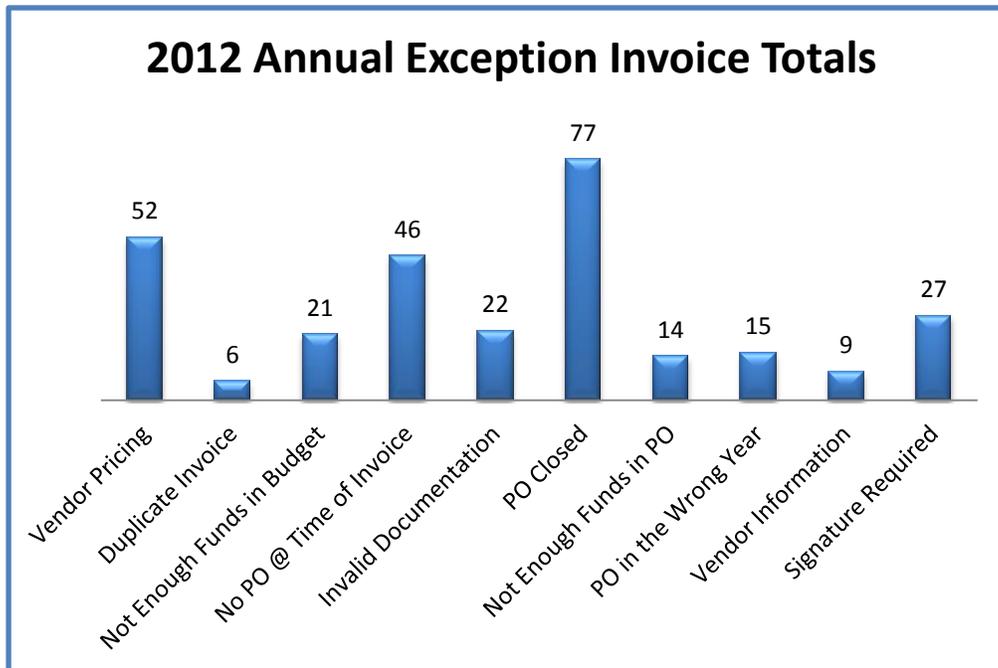
Those two vendors accounted for the vast majority of vendor pricing exceptions at the beginning of 2012. Therefore, after rectifying the issue with the vendors, the overall frequency of these exceptions declined sharply, and immediately.

An invoice from a parts supplier that charged the City a price higher than retail pricing found elsewhere, alerted OAC to an issue with some current contracts. Contracts are often written for specific items, and a discount rate is listed for any additional items not specified in the contract. Without some frame of reference, though, the City cannot accurately judge if they are receiving that discount.



After OAC's review, and discussions with the Law Department, the Law Department decided to adopt a new contracting strategy. Contracts referencing a discounted rate in the future will require some form of catalogue or pricing list from vendors, so the City can properly verify it is receiving the promised discount.

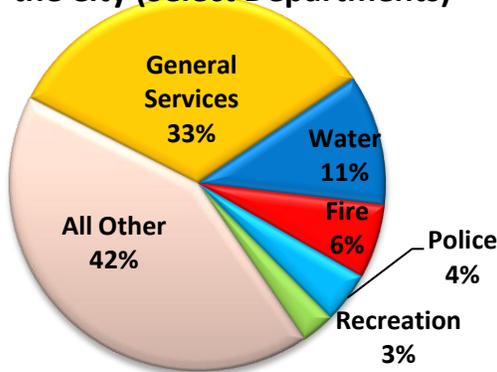
The large number of 'Signature Required' exceptions in the first quarter were attributed to new staff that had not yet been fully trained on purchasing procedures. Once addressed, those exceptions became nearly nonexistent.



Departmental Trends- It would be expected that the departments with the most invoices submitted for payment would have the larger number of problematic submissions. While this is generally true, there are obvious issues uncovered in the data.

The Department of General Services, while it makes up one third (33%) of invoices paid by the City, only comprised one quarter (25%) of the problem issues OAC reported on in 2012.

Percentages of Total Invoices Paid by the City (Select Departments)



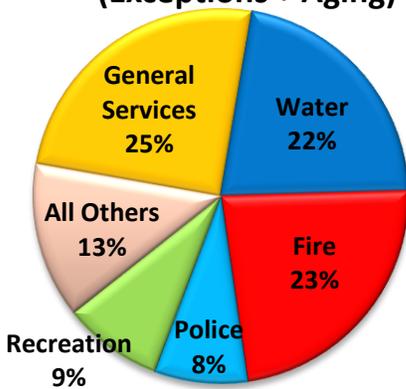
Comparatively, the Water and Fire Departments accounted for 11% and 6% of total invoices paid throughout 2012, respectively. Yet, these two departments accounted for nearly half of all problems uncovered (22% & 23% of issues).

These two departments, having far fewer total invoices, had nearly the same total number of problematic invoices as DGS.

Looking more deeply, OAC determined that the bulk of problematic Water Department invoices involved 'aging' issues. Of the total invoices OAC identified as 'aged', city-wide: 26% of those 5 months or older - increasing to 37% of all those aged 10 months or more - were attributed to the Water Department.

This data, combined with a growing frequency of vendor complaints regarding outstanding Water Department invoices gave cause for OAC to begin a more in-depth audit of the Water Department's Account's Payable process.

Percentages of Problem Invoices (Exceptions + Aging)



Percentages of a department's aging when compared to all aging:

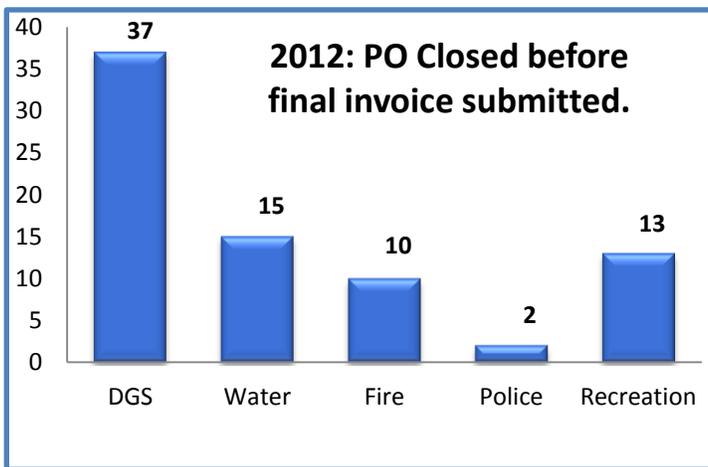
	5 Mo	6 Mo	7 Mo	8 Mo	9 Mo	10 Mo
Water	26%	30%	33%	34%	35%	37%
Recreation	11%	14%	14%	17%	20%	18%
Police	8%	7%	5%	5%	5%	6%
Planning	0%	0%	0%	0%	1%	0%
Mayor's	1%	1%	1%	1%	0%	0%
Law	3%	2%	2%	1%	2%	3%
Fire	25%	19%	16%	16%	17%	10%
DGS	20%	22%	23%	20%	16%	19%
Comm Dev	2%	2%	2%	3%	4%	6%
City Clerk	0%	0%	0%	0%	0%	0%
Buildings	3%	3%	2%	1%	1%	1%
Treasurer	1%	1%	1%	0%	0%	0%
Engineering	1%	0%	0%	0%	0%	0%

The Fire Department, while also showing a comparatively large number of problematic invoices, has requested a budget transfer at the beginning of the second quarter of each year to rectify 'aged' invoices attached to over-spent purchase orders or budget-lines. After this transfer, the

Department does not show any further, significant issues in those exception categories.

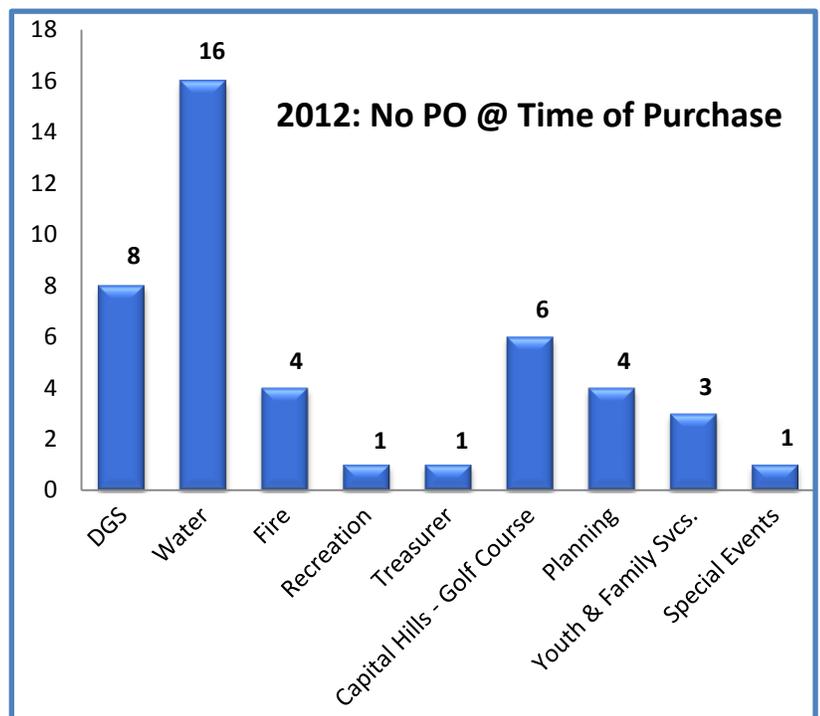
As a budget is a 'plan' for how to spend allotted funds, budget transfers through the City's Board of Estimate and Apportionment process are expected. OAC recommends, though, that the departments follow proper procedure and file for the transfers in a timely fashion – for example, as soon as it is realized that the department is likely to overspend a budget line.

The issue at the Fire Department is identifiable and revolves around untimely budget transfers and overspent Purchase Orders. Once the Fire Department's year-end budget transfer is made, it appears to pay all of its outstanding bills. OAC staff members are more concerned about the Water Department because OAC received reports from vendors of significant outstanding balances that were well over a year old that had not yet arrived at OAC for auditing.



Closed Purchase Order exceptions comprised 77 of the exceptions recorded in 2012. DGS was the originator of 37 of those exceptions. DGS being the largest share was not unexpected - as shown above DGS is responsible for 1/3rd of the City's invoices.

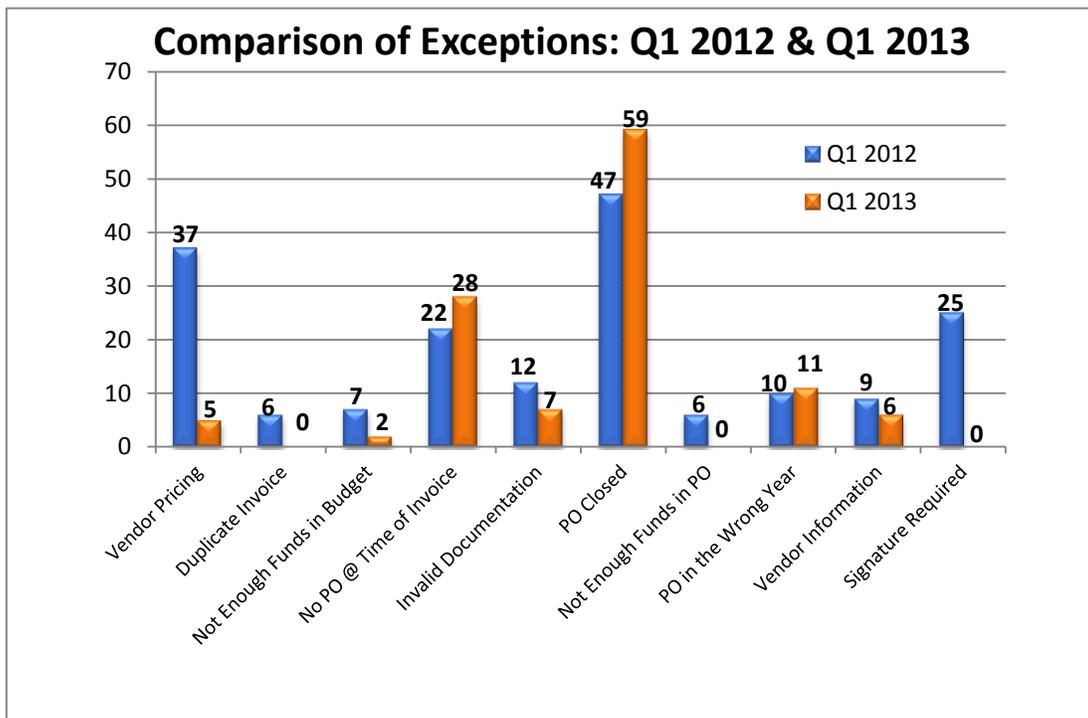
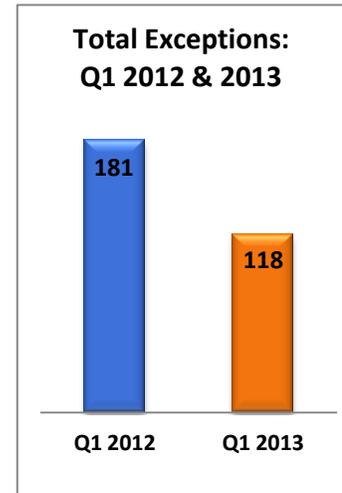
Purchases made without a valid Purchase Order accounted for 47 exceptions in 2012, the Water Department being responsible for the largest number of these issues. This fact was also taken into consideration when deciding to go forward with an audit of that department.



Comparing Total Exceptions from Q1 2012 & Q1 2013

Positive trends continue into the new year. A look at the exceptions identified in first quarter 2013 shows an overall decrease in total exceptions (181 in 2012; 118 in 2013), with an across the board decrease in any non-PO related exceptions. The slight increase in those PO related exceptions are not unexpected.

Vendor pricing, duplicate invoice, and signature exceptions all decreased sharply when compared to Q1 2012, suggesting the steps taken to address those issues may have been fruitful.



Recommendations

Some departments already put the first three recommendations into practice. These recommendations are general statements about practices that all departments should adopt if they have not done so already.

1. All departments should carefully track their budget lines, Purchase Orders, individual purchases and invoices.
 - Lax tracking leads to overspent accounts, overspent purchase orders, and/or the failure to properly account for and pay for invoices in a timely fashion.
2. Departments should verify that the prices listed on invoices, for contract items, are in line with contract pricing. (Some departments do a better job of this than others.)
 - Periodically checking the prices on invoices will help find price mistake issues, and correct them, early.
3. Departments should process invoices as close as possible to the receipt of goods or service. Promptly submit all required paperwork to the Purchasing Department, for payment purposes.
 - The longer a department holds off on processing and submitting the paperwork, the greater the chance for paperwork to be misplaced and the less likely employees will be familiar with the delivery of the purchased good or service.
4. Management should update the city-wide Purchasing Manual should be updated and distribute it to the City's departments.
 - An up-to-date Purchasing manual can be used as a reference by City departments and allow for greater accountability. There are significant gaps in the current manual that leave the City operating on past practice rather than written policy.
5. Purchasing should hold training sessions for department-level purchasing liaisons. Use the seminars to educate liaisons on matters such as: purchasing policies; invoice & supporting documentation requirements; purchasing best practices; budget tracking and how best to handle inevitable problems that arise in the purchasing process.
 - Sessions could also be used to gather feedback to help in periodically updating the Purchasing Manual.