

OFFICE OF THE CITY CONTROLLER



**ADMINISTRATION AND REGULATORY AFFAIRS DEPARTMENT
STRATEGIC PURCHASING DIVISION**

**INFORMATION TECHNOLOGY
AND PERFORMANCE AUDIT OF
VENDOR MASTER FILE (LIMITED SCOPE)**

Ronald C. Green, City Controller

David A. Schroeder, City Auditor



**OFFICE OF THE CITY CONTROLLER
CITY OF HOUSTON
TEXAS**

RONALD C. GREEN

June 30, 2011

The Honorable Annise D. Parker, Mayor
City of Houston, Texas

SUBJECT: 2011-06 ADMINISTRATION AND REGULATORY AFFAIRS DEPARTMENT, STRATEGIC PURCHASING DIVISION, INFORMATION TECHNOLOGY AND PERFORMANCE AUDIT OF THE VENDOR MASTER FILE (LIMITED SCOPE)

Mayor Parker:

The Controller's Office, has completed an Information Technology and Performance Audit of the Vendor Master File. The primary objectives of the audit were to determine if:

- Adequate controls exist over the vendor setup, validation, and maintenance processes to ensure that vendor information is valid, reliable, and accurate;
- SPD has current operational policies and procedures for vendor master information;
- Vendor accounts in the vendor master file are not a duplicate of another vendor account for the same company; and
- Transaction activity within the vendor master accounts, including one-time vendors, is reviewed periodically and the accounts are updated appropriately.

The detailed results are provided in the attached report which consisted of four issues. One item of significant concern was the existence of duplicate vendor records. Responsible management provided prompt and sufficient responses to those issues.

We appreciate the overall cooperation we received from the Administration and Regulatory Department and the related Strategic Purchasing Division.

Respectfully submitted,

Ronald C. Green
City Controller
Houston, Texas

xc: City Council Members
Waynette Chan, Chief of Staff, Mayor's Office
Alfred Moran, Director, Administration and Regulatory Affairs Department
Calvin Wells, Deputy Director, Administration and Regulatory Affairs Department, Strategic Purchasing Division
David Schroeder, City Auditor

TABLE OF CONTENTS

Transmittal Letter	i
Executive Summary.....	1
Background	1
Audit Objectives.....	1
Audit Scope	2
Audit Scope Modification	2
Audit Methodology	2
Procedures Performed.....	2
Summary Conclusions, Significant Issues, and Recommendations	3
Detailed Findings, Recommendations, and Management Responses	4-7
Memorandum from Responsible Management	8

EXECUTIVE SUMMARY

BACKGROUND INFORMATION

The Audit Division (AD) has completed a limited scope performance audit of the Vendor Master File (VMF). The VMF contains account records and information about entities that enable them to engage in contracts, orders, deliveries and payments for purchases of goods and services to the City of Houston (COH). An important internal control to ensuring safeguarding of COH resources over the Accounts Payable process is to have mechanisms in place that support the assertion that valid vendors exist, provide quality goods and services at advantageous prices in a timely manner that are needed to meet stated business objectives of the various Department(s)/Division(s).

A substantial portion of activities related to the VMF is the responsibility of the Strategic Purchasing Division (SPD) of the Administrative and Regulatory Affairs Department (ARA).¹ The Vendor Master Group (VMG) in SPD has the responsibility to create, delete (block) purchasing activity, and to perform some maintenance functions on the vendor master accounts in SAP (the enterprise-wide financial accounting system used by the City of Houston (COH), which was officially implemented in July 2006).² The VMG, which consists of one supervisor and two administrative assistants, report to the Deputy Assistant Director over SPD. As of February 01, 2011, there were 36,227 general vendors in the VMF.

AUDIT OBJECTIVES

The initial audit objectives were stated in the Audit Notification letter distributed to the Department Director, the Mayor, and City Council members and were based on the 2011 Audit Plan. The initial audit objectives were broadly defined and meant as a starting point for the engagement. The preliminary objectives of the audit were to determine that:

1. Adequate controls exist over the vendor setup, validation, and maintenance processes to ensure that vendor information is valid, reliable, and accurate;
2. SPD has current operational policies and procedures for vendor master information;
3. Vendor accounts in the vendor master file are not a duplicate of another vendor account for the same company;
4. Transaction activity within the vendor master accounts, including one-time vendors, is reviewed periodically and the accounts are updated appropriately; and
5. The total amounts paid to vendors, including those with multiple locations, are monitored on a regular basis.

¹ The VMF in SAP includes other types of payees (non-procurement) that were previously recorded and stored separately. The responsibility of the VMF is segregated primarily by general vs. non-procurement payees. General payees are created and managed by SPD, while non-procurement vendor accounts are created and managed by the Payroll Division of ARA.

² When SAP was implemented, the responsibility of the VMF was transferred from the Controller's Office, which was previously responsible for all VMF activity.

AUDIT SCOPE

The scope for the audit included: general vendors from the VMF as contained in SAP as of February 01, 2011; relevant historical vendor account information back to July, 2006; purchasing functions that affect the VMF; vendor account information; previous audit reports and SPD's procedures.

AUDIT SCOPE MODIFICATION

After review of SPD policies, procedures and responsibilities, in conjunction with information obtained through interviews with key SPD personnel, audit objective #5 was deemed to be out of the intended scope of this project.

AUDIT METHODOLOGY

We conducted this performance audit in accordance with generally accepted government auditing standards and the International Standards for the Practice of Internal Auditing as promulgated by the Institute of Internal Auditors. 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.

The scope of our work did not constitute an evaluation of the overall internal control structure of the Division. Department management is responsible for establishing and maintaining a system of internal controls to ensure City assets are safeguarded, financial activity is accurately reported and reliable, and management and their employees are in compliance with laws, regulations, and policies and procedures. The objectives are to provide management with reasonable, but not absolute, assurance that the controls are in place and effective.

PROCEDURES PERFORMED

Some of the key audit procedures performed to meet the audit objectives and provide a basis for our conclusions were as follows:

- Obtained and reviewed policies and procedures, relevant City Ordinances and Charter Articles, financial data, and organizational charts;
- Conducted interviews with SPD personnel to obtain an understanding of the vendor master set-up;
- Evaluated risks associated with the vendor creation process;
- Reviewed the systems developed to interface vendors with the VMF; and
- Used Audit Control Language (ACL) to perform various analyses of the VMF.

SUMMARY CONCLUSIONS, SIGNIFICANT ISSUES, AND RECOMMENDATIONS

Based on the evidence obtained as a result of the audit procedures performed to meet our audit objectives, the summary conclusions and significant issues are listed below.

CONCLUSION 1

While some internal controls exist to verify reasonableness and accuracy of vendor account creation and validation, internal controls were not in place to adequately identify and resolve the existence of duplicate vendor records and the maintenance of the VMF including inactive accounts. (**Audit Objectives 1, 3 & 4**)

RECOMMENDATION 1

SPD should investigate and coordinate the involvement of other departments as necessary to review vendor accounts and put purchasing blocks on those identified as duplicates and those considered inactive.

CONCLUSION 2

SPD has procedures in place related to most VMF activity; however, some improvement could be made to clarify and delineate inactivity and define rules for archiving and periodic review. (**Audit Objectives 2 & 4**)

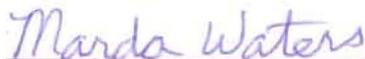
RECOMMENDATION 2

SPD should:

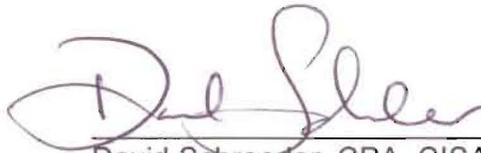
- Develop and implement data archiving rules in collaboration with the Controller's office;
 - Determine what specific vendor information should be reviewed on a regular basis and develop a method to obtain the information from SAP.
-

ACKNOWLEDGEMENT

The audit team would like to thank SPD's VMG for their professionalism and cooperation in providing us with the required documentation on a timely basis. We also acknowledge SPD management for their responsiveness to the issues identified by providing specific commitment for resolution.



Marda Waters, CPA
Auditor-in-charge



David Schroeder, CPA, CISA
City Auditor

DETAILED FINDINGS, RECOMMENDATIONS, AND MANAGEMENT RESPONSES

1. DUPLICATE VENDOR MASTER RECORDS

BACKGROUND: Audit Control Language (ACL) analytics include queries that analyze vendor master data for duplicate vendors. The ACL analytics use same vendor name, similar vendor name, same address, similar address, and same Federal Tax ID Number in various combinations to determine the possibility of duplicate vendors.

The audit team downloaded the City of Houston vendor master file as of February 1, 2011 using ACL Direct Link. The vendor master file contained a total of 47,387 records, of which 36,227 were designated as general vendors (ZVND.)

We excluded the records that had one or more blocks or flags that would limit purchasing or payment capability and then used the ACL Duplicate function on the Employer Identification Number (EIN) or the Social Security Number (SSN,) as applicable (*See result #1 in Table 1 below*). We then narrowed our criteria and analyzed the data for vendor records that have the same tax identification number and the same physical address (*See Result #2 in Table 1 below*). In performing the procedures noted above, we also identified vendor records that had no Tax Identifying information (*See Result #3 in Table 1 below*). The results of both analyses are summarized as a finding below:

FINDING:

Results	Based on EIN/SSN	on	Based on EIN/SSN and Address
(#1) Number of Duplicate Records	8,596		2,295
(#2) Number of Duplicate Entities	2,941		776
(#3) Number of blank EINs/SSNs	1,469		300

RECOMMENDATION: We recommend the Vendor Master Group investigate the identified vendor accounts and put purchasing blocks on those identified as duplicates.

MANAGEMENT RESPONSE: *“The Strategic Purchasing Division (SPD) agrees with the audit recommendation. SPD, in collaboration with the City Controller’s Office, will determine which vendors need to be blocked and marked for deletion. Duplicate vendor numbers with no activity pending will be blocked/marked for deletion in SAP. SPD’s targeted date for beginning dialogue with the affected agencies to address this audit finding/recommendation is July 11, 2011.”*

2. VENDOR MASTER DATA ARCHIVING

BACKGROUND: The SAP Account Payable Business Blueprint states under the Archive section in 3.1.1.1 “Purge criteria is determined jointly by Controller and Strategic Purchasing.” An early version of the Blueprint had stated “inactive vendor master records should be maintained in the production system for a period of three years, if the vendor has no open Purchase Orders, no scheduled payables and no retainage against it.” However, the current Blueprint does not state any criteria for archiving.

When the City began using SAP on July 5, 2006, there were approximately 16,700 vendor accounts in the Vendor Master File (VMF). Since that time, the following number of accounts has been added to the file:

FY07 – 3,112
FY08 – 7,182
FY09 – 3,850
FY10 – 3,880
FY11 – 2,626 (up through 02-01-11)

The VMF at the date we pulled the data contained a total of 47,387 accounts. Of this total, 36,227 were identified as general vendors (4,744 of these were blocked from purchasing activity). The remaining 11,160 accounts in the VMF were identified as non-general vendors, which includes examples such as employee expense reimbursements, health benefits, Combined Municipal Campaign organizations, and governmental agencies.

FINDING: Vendor Master Records are not getting purged; the blueprint is not current and does not define criteria for archiving. As the number of vendor accounts continues to increase, the performance of the ERP system degrades³.

RECOMMENDATION: SPD management should develop and implement data archiving rules in collaboration with the Controller’s office. Through the implementation of data archiving rules, (which may include marking the respective accounts for archiving or deletion) the inactive vendor master records can be removed or set aside from the active vendor master records thereby enhancing the efficiency, reliability, and accuracy of the VMF.

MANAGEMENT RESPONSE: *“The Strategic Purchasing Division agrees with the audit recommendation. Members of SPD met with the ERP Team in September 2010 to discuss the implementation of a vendor archiving process. In view of the audit finding/recommendation, SPD will accelerate this process and work collaboratively with ERP, City Controller’s Office and the Office of Business Opportunity (M/WBE vendors) to develop a standard operating procedure for archiving vendors. SPD’s targeted date for beginning dialogue with the affected agencies to address this audit finding/recommendation is July 11, 2011.”*

³ This was confirmed by the ERP Manager.

3. VENDOR MASTER FILE PURCHASING BLOCKS

BACKGROUND: The SAP Account Payable [sic] Blueprint states that “Vendor Records will be set up and maintained by the Strategic Purchasing Division (SPD.)” In reviewing the monitoring associated with VMF maintenance, we identified vendor accounts⁴:

- With no purchasing activity since July 1, 2008 and;
- That did not have either a “posting block” or “total function block” on them.⁵

FINDING: The VMF had 9,065 inactive vendors (24% of the total number of accounts identified as general vendors). 6,380 were created prior to the implementation of SAP and 2,685 were created since.

RECOMMENDATION: SPD management should review all vendor accounts for inactivity and put a total function block and a posting block on those that have not had any activity for a pre-determined length of time, consistent with the archiving rules.

MANAGEMENT RESPONSE: *“The Strategic Purchasing Division agrees with the audit recommendation and has been proactive in this area. Members of SPD met with the ERP Team in September 2010 to discuss the implementation of a vendor archiving process. In view of the audit finding/recommendation, SPD will accelerate this process and work collaboratively with ERP, City Controller’s Office and the Office of Business Opportunity (M/WBE vendors) to develop a standard operating procedure for archiving vendors. SPD’s targeted date for beginning dialogue with the affected agencies to address this audit finding/recommendation is July 11, 2011.”*

⁴ We reviewed a report generated from SAP that shows inactive vendors

⁵ A “posting block” will prevent payments to the vendor while the “total function block” prevents any purchasing activity on the vendor account.

4. MANAGEMENT REVIEW

BACKGROUND: Management overview of processing activity works as a preventive and detective control. The Vendor Master Group in SPD is tasked with creating and maintaining vendor accounts in the Vendor Master File. This includes placing and removing various blocks and flags on individual accounts.

FINDING: There is no procedure currently in place to review and monitor activity related to all changes in the VMF, including when blocks were added or removed from an account.

RECOMMENDATION: We recommend that SPD management determine what information should be reviewed on a regular basis and develop a method to obtain the information from SAP. Ideally, management should review activity on a monthly basis. Furthermore, we recommend SPD add this to their Policy and Procedures.

MANAGEMENT RESPONSE: *“The Strategic Purchasing Division agrees with the audit recommendation, with the exception of the monthly reviews. SPD will develop a policy/procedure requiring the Vendor Master Team leader to provide to management, on a quarterly basis, a vendor activity report that contains at the minimum: 1) number of vendors created; 2) list of vendors blocked/marked for deletion; and 3) list of vendor records that were modified. SPD’s targeted date for beginning dialogue with the affected agencies (ERP) to address this audit finding/recommendation is July 11, 2011.”*



Memorandum from Responsible Management
Memorandum

To: Ronald Green
City Controller

From: Alfred J. Moran, Jr., Director
Administration & Regulatory Affairs

Date: June 28, 2011

Subject: SPD Vendor Master File Audit

Controller Green,

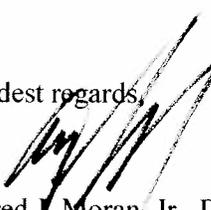
In regards to the audit conducted by the Controller's Office on Materials Management aspects of the SAP database, we have reviewed the following audit findings:

- Duplicate Master Vendor Records
- Vendor Master Data Archiving
- Vendor Master File Purchasing Blocks

We recognize the nature of these discrepancies and their impact on the business process. We will work with your office and the ERP team to resolve these issues beginning July 11, 2011. Please see our expounded management responses contained in the audit report for our plan of action.

Thank you for bringing these matters to our attention.

Kindest regards,



Alfred J. Moran, Jr., Director
Administration & Regulatory Affairs

Cc Jessica Vardar

