



Fairfax County Internal Audit Office

**Department of Finance
Direct Pay Voucher Process Audit
Final Report**

January 2009

Background

A direct pay voucher is used to process a payment for a county expenditure or liability through the county's financial accounting system (FAMIS). Per the Accounting Technical Bulletin for FAMIS direct payments (ATB 60050), direct payment vouchers are used to pay non-recurring county obligations for which a procurement and/or encumbrance action is not required. ATB 60050 provides a list of allowable expenditure categories for which the direct pay process is appropriate, such as membership dues, professional certification fees, tuition reimbursement, and newspaper/publication subscriptions, among others. The Department of Finance (DOF), Accounts Payable Section has central oversight over the county's FAMIS direct pay process, but has delegated the primary responsibility for ensuring compliance with applicable county policies to the county departments. County policy requires that all direct pay transactions be routed to the Accounts Payable Section to perform a secondary review and approval before they are posted to FAMIS and paid. For fiscal years 2007 and 2006, the Accounts Payable Section reviewed approximately 14,619 direct payment vouchers totaling \$47.8 million and 14,702 direct payment vouchers totaling \$31.2 million respectively.

Executive Summary

Our audit focused on internal controls over the FAMIS direct payment process and a comprehensive review of selected direct payment transactions. The most critical objective of our audit was to determine if goods or services which should have been procured through the county's procurement system (CASPS) or other method were inappropriately paid through the FAMIS direct pay process. We found that the direct payments reviewed generally appeared to be an appropriate use of the direct pay process, with the exception of payments initiated by two of the departments in our sample. We also noted certain areas of control weaknesses which provide the following opportunities for improvement:

- The county's FAMIS direct pay policy document (ATB 60050) was not always clear or consistent. ATB 60050 included a table of allowable categories of payments which was not stated to be all-inclusive, but a subsequent section of the document stated that any exceptions to the categories listed in the table must be approved by the county's purchasing agent in writing. A substantial number of direct pay transactions from various departments were for types of disbursements that were not included in the county's list of approved categories, with no evidence of the required approval from the Department of Purchasing and Supply Management (DPSM) for most of these exceptions.
- There was no documented county policy or other guidance regarding the appropriate levels of approval for large direct payments, including payments exceeding \$1 million.
- Several examples of the inappropriate use of FAMIS direct payment vouchers for contracted goods or services were noted, and appeared to circumvent the county's procurement system control of automated routing to appropriate oversight departments for technical review. In some instances, the inappropriate use of the

direct pay process for consulting services and personal services could have resulted in a failure to comply with Internal Revenue Service regulations.

- The primary FAMIS system control designed to prevent duplicate payments was not robust, and relied on the comparison of vendor invoice number data, which is manually input by county staff without adequate guidance. This resulted in some inconsistencies which increased the risk of failure of FAMIS to detect and prevent a duplicate payment.
- There were at least ten examples of inappropriate use of 'one-time' (OT) vendor numbers. The use of OT vendor numbers increases the risk of fraudulent or erroneous payments because these vendors or payees do not go through the vendor name and taxpayer identification number verification process performed for the non-OT vendors.
- There were no standard FAMIS reports for direct pays available for management review and analysis.
- The supporting documents for several of the direct payment transactions we reviewed did not include any evidence of the initiating department's approval by supervisory staff other than the central administrative staff.

Scope and Objectives

This audit was performed as part of our fiscal year 2008 Annual Audit Plan and was conducted in accordance with generally accepted government auditing standards. Our audit covered only non-encumbered FAMIS direct payments with document numbers beginning with the "VP" prefix. We did not audit payments processed as FAMIS financial contracts, travel vouchers, change orders, or certain direct payments such as tax refunds, witness fees, debt service payments for county bonds, foreign transactions initiated by the Fairfax County Economic Development Authority, or payments posted to FAMIS through an interface process with another computerized system. The audit covered the period of July 1, 2006, through August 31, 2007, and the audit objectives were to determine if:

- Direct payment disbursements were properly authorized, and written prior approval was obtained from the county's purchasing agent for items not typically allowable by policy
- The direct payment voucher process controls were adequate to prevent the circumvention of required competitive bid and/or technical review processes
- The direct payment controls and procedures prevented duplicate payments to vendors

Methodology

Our audit approach included reviewing the policies and procedures for FAMIS direct pay vouchers, and interviewing the management and staff of the Department of Finance and other selected departments to obtain an understanding of the requirements for the direct

pay process. We performed analytical procedures on the audit population data, and identified potentially higher risk sub-populations of direct payment transactions for which we planned and conducted specific audit tests. We also obtained samples of direct pay supporting documents, contracts, and request for proposal documents for our review. Our audit did not examine the system controls over the county's financial system (FAMIS). Our transaction testing did rely on those controls; however, this was not a scope limitation. The potential impact of this circumstance on our findings was that some portion of transaction data from FAMIS may have been erroneous, but this would not have affected the conclusions of the audit.

The Fairfax County Internal Audit Office is free from organizational impairments to independence in our reporting as defined by generally accepted government auditing standards. We report directly and are accountable to the county executive. Organizationally, we are outside the staff or line management function of the units that we audit. We report the results of our audits the county executive and the Board of Supervisors, and reports are available to the public.

Findings and Recommendations

1. **Appropriate Use of FAMIS Direct Pay Process**

The FAMIS direct payment function was being used to process payments for goods and services which should have been paid through the county's purchasing system (CASPS). Nearly 10 percent (9 of 100) of direct payment transactions randomly chosen from all county departments for review appeared to be an inappropriate use of the direct pay process. Examples included payments for professional consulting contracts, performing artist contracts, recreational class instructors, and cell phones. These types of purchases should be processed in CASPS, which allows for the automated routing of transactions to the appropriate oversight agencies for technical review.

The majority of transactions which were inappropriately paid through the direct pay process were related to the Reston and Mclean Community Centers. Therefore, we chose an additional audit sample for the Reston and Mclean Community Centers and found a significant misuse of the direct pay process. We noted that the Reston Community Center had received retroactive approval from DPSM for the use of the direct pay process as a temporary remedy for previously established contracts that had inappropriately been processed in FAMIS rather than CASPS. However, these contracts did not receive the technical review required of the purchasing department (DPSM) and/or Department of Human Resources (DHR). This was due to the fact that FAMIS did not have the same system controls as CASPS to automatically route such contracts to the appropriate agencies for technical review.

Recommendation: We recommend that the DOF accounts payable staff more closely review the supporting documents for direct pay transactions for propriety, and not approve direct payments which are clearly not permissible. DPSM approval

should be obtained for transactions that appear to be an appropriate use of the direct pay process but were not listed as an allowable type of expenditure in the ATB 60050.

Management Response: DOF accounts payable had implemented a voucher review check list as of January 2008. This check list is being used by accounts payable voucher processors to address compliance with Direct Pay requirements. In addition, a draft procedural memorandum (PM) was prepared the by the Department of Human Resources as of March 28, 2007, with input from DOF and DPSM. The PM requires agencies to get approval from DHR on requests to hire individuals for personal services. DHR will determine whether these qualify as independent contractors or if they need to be treated as employees.

2. Direct Pay Policies and Procedures

The county's direct pay policy document (ATB 60050) was not always clear or consistent as to the allowable categories of expenditures or other payments for the direct pay process. For example, Table 1 on page 2 identifies two types or categories of approved direct pay expenditures, and for each category there is a header followed by a detailed list of specific types of approved or mandated direct pay expenditures. The table column headers are worded so as to suggest that the detailed lists are representative examples, rather than an all-inclusive list. However, page 3 says that "exceptions to the conditions listed in Table 1 will require the initiating department to obtain written approval from the County Purchasing Agent."

IAO noted several types of direct payments that could have been appropriately included in the list of allowable categories, but were not. Examples of these types of payments were revenue refunds, the return of developer performance deposits, interest payments, and court ordered payments for legal support services. Many of the direct payments we reviewed were for these types of disbursements, but we noted that in most cases approval had not been obtained from the county's purchasing agent, as required by county policy. Forty one of 100 direct payment transactions randomly chosen for review were in this category of exceptions, as were three of 15 transactions subjectively chosen from the sub-population of "held check" payments, and three of 15 and one of 15 transactions subjectively chosen from the Mclean and Reston community centers, respectively. Written policy documents need to be clear and concise to effectively communicate the requirements to county departments. A lack of clearly defined county policy regarding approved categories of expenditures and other payments may result in inconsistent application of the intended policy and procedure requirements.

Recommendation: DOF should work with DPSM and update ATB 60050 to clarify allowable expenditures and other payment types. Any lists of allowable categories should be updated on at least an annual basis. If the list of allowable payment categories is not meant to be restrictive, then DOF should remove the contradictory requirement at page 3 of ATB 60050 that says if a payment type is not on the approved list, then it must be approved by DPSM. If DOF and DPSM prefer a restrictive list, then the two departments should consider establishing a dollar

threshold for DPSM approval, under which DOF Accounts Payable Section management approval would suffice.

Management Response: DOF has coordinated with DPSM to review allowable direct payments. DOF will modify the appropriate accounting technical bulletin and inform agencies accordingly, with a projected completed date of May 2009. In the interim, DOF will initiate a quality review program to independently check approved vouchers on a sample basis.

3. Approval Levels for Large Direct Pay Transactions

There were three VP direct pay transactions greater than \$1 million during the audit period, of which only one was authorized by the DOF accounts payable manager. One was authorized by the accounts payable supervisor accountant III and the other was authorized by the accounts payable administrative associate. The administrative associate performed both the 500 level and the 700 level DOF approvals, which circumvented the additional FAMIS separation of duties control for separate approvals. Additionally, 12 of 15 transactions greater than \$100,000 were approved by administrative staff rather than a professional accountant. While there was a FAMIS system control which required both a 500 level and 700 level approval by DOF for direct pay transactions greater than \$1 million, there was not written policy defining DOF approval authority for transactions greater than \$100,000. DOF also had not established any countywide policy for departments addressing the minimum level of initiating department's supervisory approval for direct pays. Optimal internal control practices would normally require senior management level approval of large transactions, especially transactions which have not been subject to the system controls of the county's purchasing system (CASPS). There were 148 direct pay transactions between \$100K and \$500K totaling \$30.3 million; five direct pay transactions between \$500K and \$1 million totaling \$3.5 million; and three direct pay transactions greater than \$1 million totaling \$4.4 million.

Recommendation: We recommend DOF implement an internal policy requiring direct payments over certain threshold amounts be reviewed by DOF management. The thresholds and approval levels should be in line with other county procurement and/or disbursement policies. DOF should also address in ATB 60050 the approval requirements for county departments initiating large direct pay transactions over \$100,000, and should consider changing the FAMIS document approval routing process to require that the initiating department perform a second, 700 level FAMIS approval by at least a division chief before the transaction is routed to DOF for final approval.

Management Response: DOF will establish a section in the policy regarding approval authority for high dollar direct payment transactions. The anticipated completion date for revising the ATB is May 2009.

4. Sufficient Supporting Documentation

We noted nine direct pay transactions for which the supporting documents received

by DOF did not include any evidence of the initiating department's approval by supervisory staff that should have adequate knowledge of the operations. The nine transactions were for refunds of developer performance deposits. DOF accounts payable staff did verify that the developer deposits were in the county's financial system prior to approving the refunds to developers, but they did not receive documented approval from staff with on-site knowledge of program operations sufficient to determine if the developers had completed all the necessary requirements to warrant the return of their performance deposits. Two other performance deposit refunds we reviewed did have evidence of appropriate approval which included the signatures and dates of two levels of field staff and/or supervisors.

Good internal control practices should require that refunds of performance deposits be authorized by supervisory staff that has adequate knowledge of the operations. Supporting documents for most other types of direct payments include an invoice with indication of management approval. Even though invoices were not typically prepared for developer deposit refunds, there should be some other documentation indicating management's approval of the release of funds. Refunds of developer performance deposits represented a substantial portion of the total population of direct payment transactions, in terms of both transaction volume and dollar amount. Failure to properly verify approvals from program or field staff with direct knowledge of the performance requirements could result in the inappropriate release of funds.

Recommendation: DOF should revise the ATB 60050 direct pay policy to provide sufficient guidance to county departments regarding the appropriate department approval of direct pay transactions. Due to the relatively high volume and total dollar value of direct pay transactions related to developer deposits, DOF accounts payable staff should require that the initiating department include evidence of approval by program or field staff in the supporting documents forwarded to DOF for review.

Management Response: DOF will include documentation requirements in the revised direct payment policy. The anticipated completion date is for policy updates is May 2009.

5. Duplicate Payment Controls

There was a lack of consistency related to departments' data input of vendor invoice numbers in between the asterisks in the transaction description field in FAMIS used to detect duplicate payments. Twelve of 100 randomly chosen transactions did not have the vendor invoice number properly input into the FAMIS transaction description field. The DOF accounts payable manager confirmed that the DOF accounts payable staff are not required to match the invoice number per supporting documents to the invoice number input between the asterisks before approving a direct pay. FAMIS does not have all the system controls that are available in CASPS, and original documents are not required for payment. The county's main system control for preventing duplicate direct payments in FAMIS is a system control which compares vendor invoice data input between the asterisks in the

transaction description field. When input data is inconsistent or erroneous, the potential for duplicate payments increases.

Recommendation: DOF should establish a vendor invoice data entry standard and communicate the requirements to the county departments. Data entry requirements for vendor invoice numbers should also be specified in the ATB 60050 policy document. For payments which do not have an invoice number to reference, the ATB should include requirements for information that should be included in the transaction description field. A/P staff should verify the accuracy and consistency of invoice number data input between the asterisks in the FAMIS transaction description field before approving the payment.

Management Response: DOF will inform agencies by year-end 2008 that invoice numbering standards required for CASPS also apply to direct payments. The invoice numbering standards have now been posted on DOF's website. Finally, the standards will be incorporated in the new EAPS non-purchase order training and rollout which is anticipated to be completed by July 2010.

6. Inappropriate Use of One-Time (OT) Vendor Numbers

There were at least ten examples of inappropriate use of one-time vendor numbers for direct pay transactions. The vendors or payees were either already established with regular vendor numbers in FAMIS, or were not established in the FAMIS vendor file but should have been because multiple payments were made to the vendor throughout the audit period. The use of OT vendor numbers increases the risk of fraudulent or erroneous payments because these vendors or payees do not go through the taxpayer identification number verification process performed for the non-OT vendors. In that process, accounts payable staff utilizes the Internal Revenue Service's Web site to verify the vendor's name and taxpayer identification number provided to the county on an IRS W-9 form.

Recommendation: We recommend that DOF limit the use of OT one-time vendor numbers, and document the permitted uses in a policy document. Once a policy has been established, DOF accounts payable staff should review the appropriateness of the use of OT one-time vendor numbers before approving a FAMIS direct payment voucher.

Management Response: DOF has already incorporated one time vendor allowable use into the current draft version of the ATB-033 (DFN 60040.01). This ATB was circulated for agency comments in April 2008. The anticipated completion date is January 2009.

7. Standard System Reports

There were no standard FAMIS reports available for direct pay transactions to be reviewed on a regular basis, although we did note that accounts payable management had the capability to run ad hoc reports as needed. Effective management controls include adequate managerial oversight through periodic

review of management reports. The lack of regularly scheduled monitoring of standard direct pay reports could result in management not being aware of problems or irregularities with the direct pay process in a timely manner.

Recommendation: DOF should run management reports for direct pay transactions on a quarterly basis, at a minimum, for review of unusual or questionable activity. Suggested examples of information to be included in these reports are year-to-date payments to vendors subtotaled by vendor and agency (used to monitor the circumvention of competitive procurement thresholds); and the summary of amounts by selected expenditure subobject codes such as professional fees, consulting services, information technology, capital expenditures, etc. (reviewed to determine if the payments were an appropriate use of the direct pay process). DOF may want to consider applying dollar thresholds to aggregate payments to vendors. However, for subobject codes requiring technical review, a report should be run without thresholds and all exceptions should be reviewed. If there appears to be a pattern of abuse, DOF will consult with the applicable oversight department such as Department of Purchasing and Supply Management (DPSM), Department of Human Resources (DHR), or Department of Information Technology (DIT), and take action as applicable.

In addition to DOF's periodic review, DPSM has agreed to include direct pay transactions in its Procurement Assistance and Compliance (PAC) review process. DPSM will work with DOF to develop standard DART reports to be available to the PAC team for their reviews.

Management Response: DOF will develop a DART report and implement a quality review process. The anticipated completion date is February 2009.