



Office of the City Auditor

Review of Manual Distribution of Checks

Report Date: April 13, 2012



Office of the City Auditor

"Promoting Accountability and Integrity in City Operations"

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Office of the City Auditor Transmittal Letter



Date: April 13, 2012
To: James K. Spore, City Manager
Subject: Review of Manual Distribution of Checks

I am pleased to present the report of our review of the Department of Finance's process whereby vendor (non –payroll) checks are picked up by the payee or his designee as opposed to the normal mailing process. The results of this review will be provided to City Council through the City's Audit Committee.

The results of our audit are provided in this report. Findings considered to be of insignificant risk have been discussed with management. We completed our fieldwork on March 12, 2012. It should be noted that while we found a few weaknesses that resulted in recommendations for improvement, this was not prompted by any known instances of fraud.

The Office of the City Auditor reports to City Council through the City's Audit Committee and is organizationally independent of all other City Departments. This report is intended solely for the information and use of the Audit Committee, City Council, City Manager, and appropriate management. It is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

We would like to commend personnel from the Department of Finance for their courtesy and cooperation extended to us during the review. It should also be noted that management agreed with our findings and recommendations and have promptly implemented most of them prior to the issuance of the report.

If you have any questions about this report or any audit-related issue, I can be reached at 385-5872 or via email at lremias@vbgov.com.

Respectfully submitted,

Lyndon S. Remias, CPA, CIA
City Auditor

c: City Council Members
Audit Committee Members
Dave Hansen, Deputy City Manager
Patti Phillips, Director of Finance



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Purpose

The purpose of this review is to document the process and related controls whereby vendor (non-payroll) checks are physically picked up as opposed to the normal mailing procedure. We will assess the design and test the compliance of those controls.

Scope and Objectives

The objectives of our review were:

- To document the procedures and related controls over the manual distribution of vendor (non-payroll) checks as opposed to the normal procedure of mailing of checks.
- To assess whether those controls are effectively designed to minimize risk of misappropriation.
- To test controls deemed to be designed effectively to assess whether they are operating as designed.
- Offer recommendations to improve ineffective controls to mitigate and reduce risk to an acceptable level.

The audit covered the fiscal year ending June 30, 2011 and the current fiscal year from July 1, 2011 through December 31, 2011

Methodology

To accomplish our objectives, we performed the following procedures:

- Interviewed appropriate personnel concerning the process by which vendor (non payroll) checks are picked up versus the normal check mailing procedure.
- Obtained written procedures and with information from interviews we documented the manual check process with the associated internal controls.
- Assessed effectiveness of the design of internal controls to reduce risks to an acceptable level.
- Tested compliance with those controls deemed to be designed effectively to reduce risk to an acceptable level.
- Obtained the manual check log books to verify if any checks listed in the logs as picked up had required signature by payee or designee.
- Examined the cancelled check and endorsement for consistency and support documents for the appropriateness of the expenditure for any unsigned manual check log book entries.



- Verified that checks designated as Priority 6 (Same day checks/emergency checks) were properly authorized.
- Verified through ComIT that Accounts Payable personnel authorized to enter invoices in InSITE could not also set up vendors in InSITE and vice versa.
- Made recommendations to improve controls and the process.

Standards

Our audit was conducted in accordance with generally accepted government auditing standards. The Office of the City Auditor reports to City Council through the Audit Committee and is organizationally independent of all City Departments. This report will be distributed to the City's Audit Committee, City Council, City Manager, and appropriate management within the City of Virginia Beach. This report will also be made available to the public.



Background

The City’s Finance Department regularly, with the aid of the City Treasurer, processes daily vendor (non-payroll) check runs for both the City and Schools. The various check runs are designated a “priority code” as to the type of checks being issued. The priority codes for City check runs are as follows:

Priority #	Type of Check Run
99	These are the vast majority of vendor checks that are batched and printed with the next business day date. After printing these checks are folded, sealed and locked in the safe until the mail room picks them up for mailing the following day.
1	These checks are batched and printed and <i>returned</i> to Accounts Payable staff for special handling one of two reasons: 1) the check must have an attachment sent with it – i.e. a registration form, 2) the vendor has made arrangements to come to Accounts Payable and pick up the check.
3	Election official checks (these are now processed as 99s).
4	Real estate refunds
5	Welfare checks
6	Same day checks/emergency checks requiring written authorization by the Financial Services Coordinator or the Comptroller.

There are many internal controls and procedures governing the various processes involved with:

- Setting up vendors in InSITE;
- Entering, reviewing and batching invoices for payment;
- Working with the City Treasurer to process the various check runs.

This review is specifically focused on the instances whereby a vendor check is removed from the normal mailing process and picked up by the vendor (non-payroll) or designee at Accounts Payable.

In Accounts Payable (AP), there are two types of staff members, each having separate responsibilities in InSITE for control purposes. The two types of AP staff members are as follows and will be referred to as such in the following process narrative:

- AP(1)- These account clerks audit and key vendor invoices into InSITE and *cannot* set up vendors.
- AP(2)- These account clerks set up vendors in InSITE, batch checks for printing, process voids and 1099s and *cannot* enter vendor invoices for payment.



Office of the City Auditor Review of Manual Distribution of Checks

After the various check runs are completed, batch information verified and given to the Treasurer's Office, Priority 1 checks are released to AP(1) staff members to match with copies of the vouchers that state for them to hold for pickup or to include an attachment for mailing with the check. After AP(1) staff members have completed this, all checks with their appropriate backup documentation are locked in the safe for next day mail or pickup. Priority 1 checks are also locked in the safe at the close of business each day.

Priority 6 checks are same day checks/emergency checks which are also picked up by the payee or designee. To be processed as a Priority 6 check, an authorization form must be completed by AP staff member, initialed by the AP Supervisor and routed to the Financial Services Coordinator or the Comptroller for authorization. There are not many Priority 6 checks.

The signed Priority 6 authorization form is put into PDF format and attached to the payment details in InSITE by the AP(1) and the original given to AP(2) to process. The original hard copy Priority 6 form is filed by AP(2) with the check batching documents and maintained for 5 years.

The Priority 1 and 6 checks given to the AP(1) staff for pickup are signed for in the log book by the payee or designee after showing identification. The AP staff member distributing the check initials the log as well. There is now only one log book but prior to July 1, 2011 there were two log books—one for supplier checks and one for employee checks.

Finance has developed a policy whereby they can charge the payee a \$15 fee for manual check pickup, which is indicated in the log book as well.

Any checks not picked up at the close of business are returned to the safe until the next day.

One critical control within Finance and the AP division in particular, is the segregation of the ability to set up vendors in the vendor file and the ability to audit, process and enter invoices. The AP staff is segregated with five staff members that can only enter vendor invoices and two that can only set up vendors in InSITE. We verified the segregation of duties by requesting the InSITE "*Active Users and Responsibilities Report*" from ComIT. This report identifies what duties and abilities InSITE users have access to. We found that all of the AP staff members had the proper levels of authorization and separation of duties.



Results

The internal controls are well designed to minimize the risks of misappropriation of manually distributed vendor (non-payroll) checks and while we noted some areas of noncompliance with those controls, improvements have been made and compliance in the current fiscal year is excellent. We followed up on the areas of noncompliance and noted no instances of fraud or misappropriation. We also offered some recommendations to improve controls and in one area where there could be an opportunity for improved efficiency.

Findings and Recommendations

Finding 1:

We reviewed the Department of Finance Accounts Payable Division's Supplier Log book (07/01/10-06/30/11), Employee's Log book (07/01/10-06/30/11), and Combined Log book (07/01/11-10/31/11), each set up for documenting the manual pick up of vendor (non-payroll) checks. From the three logs we noted 29 checks out of approximately 1,660 that were listed as picked up but did not have a signature from the payee or his/her designee. It should be noted that these were from the supplier and employee log books through June 30, 2011 and no exceptions were noted in the July 1, 2011 combined log book. The new log book is much improved and facilitates compliance by having instructions and the various signature areas blocked off. The signatures were missing for a number of reasons:

- checks were picked up as a group (such as for a real estate closing) but were only signed for on one line and did not indicate where the group of checks picked up ended;
- the signature *appears* to be on the wrong line (the new form helps prevent this);
- AP staff members simply failed to obtain the required signature.

We followed up on each of those 29 checks and examined the endorsements to determine if they were reasonable and we noted no exceptions. We also reviewed the supporting documentation for the appropriateness of those checks and noted no exceptions.

Recommendations

- 1.1 We recommend reinforcing to AP staff members the importance of this control especially for outside vendors.
- 1.2 Though the new combined supplier and employee log format is much improved we recommend the following:



- i) Number the pages of the combined log book. This would help show whether a page has been removed.
- ii) Add a column to the combined log book to show that identification was verified by AP staff member disbursing the check.

Finding 2:

We downloaded all of the checks that had been coded as a Priority 6 (same day pickup) from July 2011 through December 2011. We noted nine instances where the authorized approval form was not *electronically* attached in InSITE as required. We did however research and found all nine of those *hardcopy* Priority 6 approval forms that are attached to the payment batch sheets and are filed with other AP documents for the fiscal year end. We also noted one Priority 6 authorized approval form *did not* have the reason for the emergency check noted on the form but it was approved by the appropriate personnel.

Recommendation

- 2.1 We recommend that Finance ensure all Priority 6 approval forms are electronically stored in InSITE to ensure that it can be readily available for review.

Finding 3:

During the course of our field work, we noted one area where there could be an opportunity for increased efficiency. At the current time, AP is required each month to manually key in over a hundred water bills for *City* facilities and then issue *individual* checks to the City Treasurer to have them posted to the *individual* accounts in Banner, the Public Utilities billing system. Finance indicated they previously inquired about the possibilities of an upload or other mode for these transactions to be processed but was told by Public Utilities it was not possible at that time.

Recommendation

- 3.1 We recommend the appropriate personnel from Public Utilities and Finance meet to streamline the procedure for processing and paying water bills for city facilities.

Finding 4:

We found the safe containing the printed checks does not have controlled access as all AP(1) and AP(2) employees have access to the printed checks at all times. Controlled access had been a control in the past but is not currently being enforced for efficiency purpose (processing Priority 1 and 6 checks).



Recommendation

- 4.1 We recommend Finance reinstitute controlled access to the safe containing the printed checks. Even though the AP staff is properly segregated as to who can set up vendors and who can enter invoices, controlling access to the printed checks is an important control.

Conclusion

Based on our review of the controls over the manual distribution of checks, the controls are effectively designed to limit risk to an acceptable level. We noted some instances of non-compliance with those controls but no instances of fraud or misappropriation. We offered some recommendations for improvements to the controls and in one area where there could be an opportunity for improved efficiency.

Acknowledgements

We would like to thank the personnel from the Department of Finance for their cooperation and responsiveness to our requests during the review and their receptiveness to our questions, recommendations and suggestions.



City of Virginia Beach

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INTER-OFFICE MEMORANDUM

DATE: April 19, 2012

TO: Lyndon Remias, City Auditor

FROM: Patricia A. Phillips, Director of Finance 

SUBJECT: Review of Manual Distribution of Checks

Thank you for your review of the check distribution process. I am pleased that the audit reported that our internal controls are well designed to minimize risk and that no instances of fraud or misappropriation were found.

Based upon the findings, Finance has already reinforced the importance of obtaining signatures for each and every individual check that is manually picked up, regardless of whether one check or a group of checks is involved. In addition, pages have been numbered in the log book and a Y/N column has been added to indicate that identification was verified. Furthermore, we have reinforced that all priority 6 approval forms are scanned and attached electronically to the invoice record in InSITE.

Finance has long been a proponent of eliminating checks written to the Treasurer in payment of City water bills for City departments. As far back as 2003 with the implementation of Banner, to the more recent implementation of Energy CAP, Finance has met with representatives of Public Utilities to request this change and we will continue to request this change to enhance efficiency. As you know, we cannot make this a priority at this time due to other major commitments that require the dedication of all available resources.

Regarding your recommendation for more controlled access to the safe where checks are stored prior to distribution, we are in general agreement. However, we will need some time to analyze the impact on our business processes and our ability to service our customers before implementation is accomplished.

We noted that the audit had few and mostly procedural findings. We have always emphasized the importance of reinforcing and strengthening control procedures to safeguard the City's assets.