



April 13, 2016

To: Finance and Administration Committee

From: Darrell Johnson, Chief Executive Officer
Janet Sutter, Executive Director
Internal Audit Department

Subject: Accounts Payable Controls

Overview

The Internal Audit Department has completed an audit of controls over the accounts payable function. Based on the audit, system assignments do not provide for adequate segregation of duties, and procedures for utilizing payment requests and invoice review are not consistently adhered to. In addition, Cofiroute USA, LLC, the contracted operator of the 91 Express Lanes, is not required to competitively procure goods and services on behalf of the Orange County Transportation Authority. The Internal Audit Department has made three recommendations to improve controls and enhance procedures.

Recommendation

Direct staff to implement three recommendations offered in the audit of Accounts Payable Controls, Internal Audit Report No. 15-513.

Background

Accounts Payable (AP) staff processes payments to Orange County Transportation Authority (OCTA) vendors and employees. Various policies exist related to these activities. Most payments are paid against a contract agreement or purchase order. For payments under \$2,500 to vendors not under contract, a Payment Request form is used. This form of payment is generally reserved for a one-time payment (or a series of payments) of \$2,500 or less.

The AP section supervisor oversees five accounting specialists who are collectively responsible for processing payments, validating Tax Identification Numbers for new vendors, and adding or editing vendors in OCTA's financial management system, Integrated Financial and Administrative Solution (IFAS).

Cofiroute USA, LLC (Cofiroute), the contracted operator of the 91 Express Lanes, also processes various payments to OCTA's IFAS system related to 91 Express Lanes operations, including, but not limited to, customer refunds, security services, collection services, equipment, maintenance, and other administrative expenses. These payments are entered into IFAS by Cofiroute employees and are processed on a weekly basis under a batch system. During the 18-month period reviewed, Cofiroute employees processed approximately \$7.2 million in payments.

Discussion

Three AP staff members and four Cofiroute staff members are assigned IFAS system access that allows for both the creation and/or edit of the vendor master file, as well as the ability to enter payments. This creates an environment in which a fictitious vendor could be created and a payment processed to that vendor with little possibility of detection. The Internal Audit Department (Internal Audit) recommended management either revise system access assignments to prevent staff from having the ability to both create and/or edit the vendor master file and enter payments, or develop and implement adequate controls to identify unauthorized payments and/or unauthorized changes to the vendor master file. Management agreed and indicated that detective measures will be implemented in order to identify unauthorized edits to the master vendor file. With respect to Cofiroute, management indicated that system access assignments will be revised to prevent staff from having the ability to both edit the master vendor file and enter payments.

Internal Audit identified instances whereby payments did not comply with policies, were not properly authorized, or did not evidence proper review as required. A recommendation was made that management provide training to ensure knowledge of, and consistent enforcement of, OCTA policies and procedures. Management agreed and stated they will include training on AP procedures and responsibilities in on-going bi-weekly staff meetings and communicate OCTA's Policies and Procedures to departments responsible for the related exceptions.

Internal Audit noted that, while Cofiroute routinely makes purchases on behalf of OCTA, Cofiroute's procurement rules are not consistent with OCTA procurement policies and procedures, which are designed to foster competition and ensure economical pricing for goods and services. As such, Internal Audit recommended management amend the agreement with Cofiroute to include procurement guidelines and implement monitoring controls to ensure compliance. Management agreed and indicated they will work with Cofiroute to

develop procurement guidelines and incorporate these guidelines in the operating agreement.

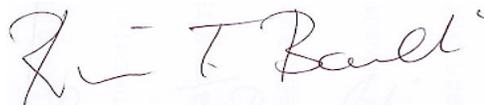
Summary

Internal Audit has completed an audit of accounts payable controls and has offered three recommendations for improvement.

Attachment

- A. Accounts Payable Controls, Internal Audit Report No. 15-513

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ORANGE COUNTY TRANSPORTATION AUTHORITY INTERNAL AUDIT DEPARTMENT



Accounts Payable Controls

Internal Audit Report No. 15-513

April 4, 2016



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Conclusion

The Internal Audit Department (Internal Audit) has completed an audit of controls over the accounts payable function. Based on the audit, system assignments do not provide for adequate segregation of duties and procedures for utilizing payment requests and invoice review are not consistently adhered to. In addition, Cofiroute USA, LLC (Cofiroute) the contracted operator of the 91 Express Lanes, is not required to competitively procure goods and services on behalf of the Orange County Transportation Authority (OCTA). Internal Audit has made three recommendations to improve controls and enhance procedures.

Background

The Accounts Payable section (AP) is part of the Accounting and Financial Reporting Department in the Finance and Administration Division.

The AP supervisor oversees five accounting specialists who are collectively responsible for processing payments, validating Tax Identification Numbers for new vendors, and adding or editing vendors in OCTA's financial management system, Integrated Financial and Administrative Solution (IFAS).

AP processes payments to OCTA vendors and employees. Various policies exist related to these activities, including the Accounts Payable Invoice Review Policy, Vendor Payment Policy, Payment Authorization Policy, Payment Request Policy, and the Check Signature Policy. The majority of payments processed are disbursed via paper checks; however, payments processed electronically such as wire transfers, Automated Clearing House transactions, and ePayables have increased over the last couple of years.

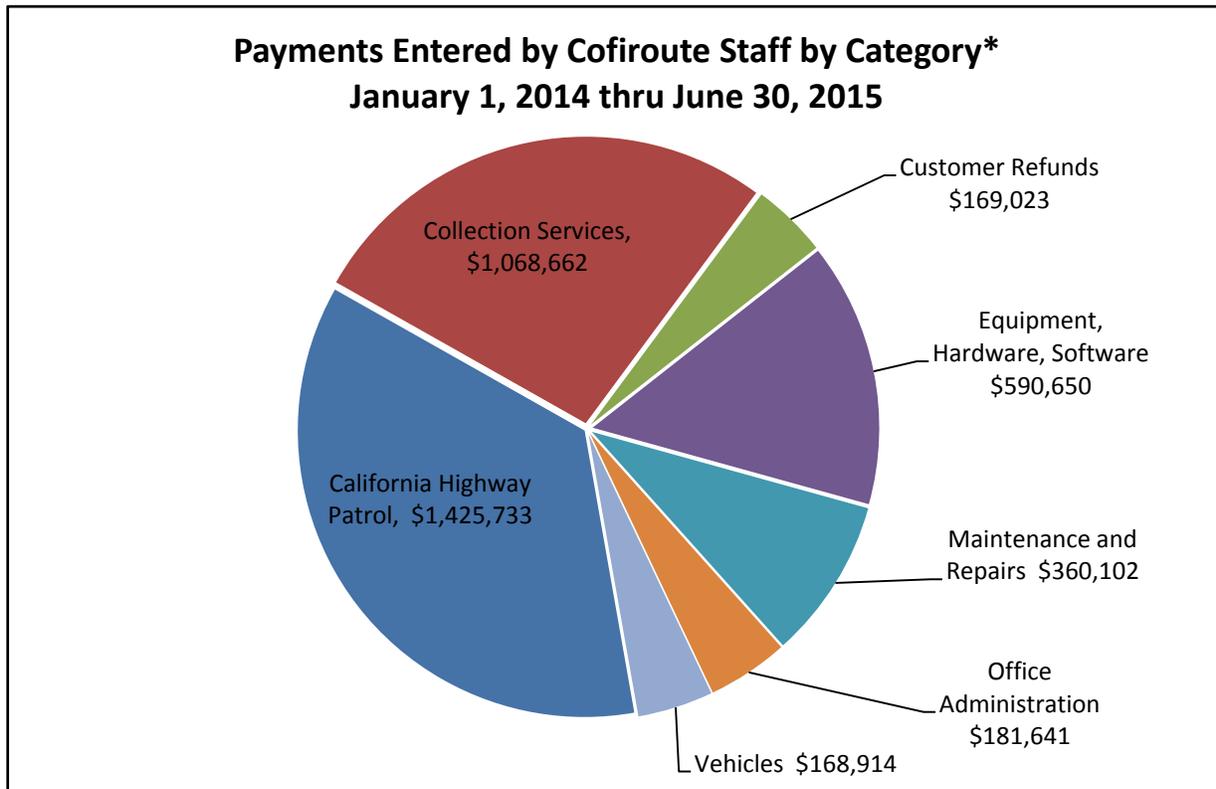
Most payments are paid under a contract agreement or purchase order (PO). For payments under \$2,500 to vendors not under contract, payment requests are used. The Payment Request Policy states that all payments that do not reference a PO, contract agreement, cooperative agreement, or expense report shall be submitted for payment using a Payment Request Form. This form of payment is generally reserved for a one-time payment (or a series of payments) of \$2,500 or less. However, certain types of payments above \$2,500 are allowable if they fit into an approved category. Some of the approved categories are payroll disbursements, judgments and settlements, refunds, utility payments, membership dues, conferences and training, payments to other governmental units, real estate purchases, investment fees, and miscellaneous payments charged to the 91 Express Lanes. Additionally, payment requests are not to be used for goods or services that are covered by a current contract or PO, or as a means to avoid amending a contract.

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IFAS System Access Rights

While over one hundred OCTA employees have access to the IFAS system, the majority are limited to view, or read only, access rights. At the time of the review, all AP personnel had the ability to process payments in the system and three staff also had the ability to add or edit vendors in the IFAS system. AP has an informal policy that prohibits staff responsible for setting up vendors in the system from also processing payments to the vendor.

Cofiroute processes various payments to OCTA's IFAS system related to 91 Express Lanes operations, including but not limited to, customer refunds, security services, collection services, equipment, maintenance, and other administrative expenses. These payments are entered into IFAS by Cofiroute employees and are processed on a weekly basis under a batch system. During the 18-month period reviewed, payments processed by Cofiroute employees totaled approximately \$7.2 million. Of that amount, about \$3.2 million consisted of payments made to other tolling agencies for tolls levied against 91 Express Lanes customers using their facilities. The breakdown of the remaining payments* processed by Cofiroute employees is illustrated in the chart below:



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Objectives, Scope, and Methodology

The objectives were to determine whether payments are processed in accordance with relevant policies and procedures and to assess the adequacy of internal controls over payment processing, including system access controls within the financial management system, IFAS.

The methodology consisted of a review of controls over payment processing including IFAS system access assignments. Payments to vendors not under contract were reviewed for evidence of compliance with relevant OCTA policies and procedures. Additionally, numerous analytical tests were performed on IFAS system data to assess system controls and compliance with OCTA policies and procedures with respect to payment processing. Items tested were selected judgmentally with a bias toward characteristics of the attributes to be tested. As such, results cannot be projected to the population.

The scope was limited to payments processed from January 1, 2014 through June 30, 2015. The scope excluded certain non-routine or low risk payments such as scholarship awards, wire transfers, wage garnishments, e-payables, and various payments made to governmental agencies and utility companies. The scope also excluded payments related to corporate card expenses, wire transfers, and electronic payments due to coverage in other audits.

We conducted this performance audit in accordance with generally accepted government auditing standards. 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.

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Audit Comments, Recommendations, and Management Responses

System Access Assignments Should Enforce Segregation of Duties

Three AP staff members and four Cofiroute staff members are assigned system access that allows for both the creation and/or edit of the vendor master file, as well as the ability to enter payments. This creates an environment in which a fictitious vendor could be created and a payment processed to that vendor with little possibility of detection.

Although OCTA's AP has an informal policy barring staff from creating and/or editing a vendor and posting payments to that vendor, Internal Audit identified multiple instances of payments posted by the same staff member that created the vendor. The same condition was observed with regard to Cofiroute payments.

In light of this internal control weakness, Internal Audit performed additional test work to identify inappropriate payments and none were identified. However, these tests could not have detected all possible means of processing a fraudulent payment.

Recommendation 1:

Internal Audit recommends management either revise system access assignments to prevent staff from having the ability to both create and/or edit the vendor master file and enter payments, or develop and implement adequate controls to identify unauthorized payments and/or unauthorized changes to the vendor master file.

Management Response:

Management concurs. We have assigned two AP staff members the ability to create and modify vendors in IFAS. Due to limited staff resources, changes in vendor responsibility, employee vacancies, etc.... there may be times when a staff member is responsible for data entry of an invoice for a vendor that they previously set up/modified. Staff will implement detective measures in order to identify unauthorized changes to the vendor master file. The Accounting Operations Section Manager will begin reviewing on a weekly basis a new vendor report and a log of any changes made to existing vendors and will compare critical information to the invoice packet. Additionally, the Accounting Operations Section Manager will review on a weekly basis a report showing all new vendors, payments, and related staff to ensure that staff are not setting up and paying the same vendor.

With respect to the 91 Express Lanes, management will revise IFAS system access assignments to prevent Cofiroute staff members from having the ability to both create and/or edit vendor files and enter payments.

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Payment Request and Invoice Review Policy Violations

The Accounts Payable Invoice Review Policy states that AP staff shall review all invoices for accuracy, reasonableness of documentation, compliance with applicable OCTA policies, practices, and procedures and proper authorization prior to payment. During the 18 month period audited¹, violations of OCTA policies were identified, as follows:

- Ten payment requests, totaling \$16,730, were processed for a vendor with an active blanket purchase order (BPO) in the amount of \$250,000. The payments violated the Payment Request Policy and, more importantly, these activities circumvented OCTA procurement policies and procedures that require Board of Directors' approval of contracts exceeding \$250,000. Total payments made to the vendor amounted to \$262,228.

These conditions should have been identified by AP staff, as invoices from the vendor under both the BPO and payment request method were processed together.

- AP staff processed 126 invoices, totaling \$23,512 to one vendor. The Payment Request Policy states that payment requests are to be used for one-time miscellaneous payments or a series of payments to a single vendor that totals \$2,500 or less in a rolling 12-month period. Payment requests should not be used in lieu of creating a contract or PO.
- Two invoices, totaling \$147,240, were processed without proper signature authorization. Both invoices reflected signatures for authorization; however, one invoice exceeded the signer's dollar authority and the other was charged to an area outside the signer's assigned responsibility.
- Two invoices, totaling \$79,811, lacked evidence that the rates were reviewed by AP staff. The Invoice Review Policy requires AP staff to verify billing rates on the first invoice against billing rates in the contract and initial to evidence this review.

Recommendation 2:

Internal Audit recommends management provide training to ensure consistent enforcement of policies and procedures by AP staff and advise department staff responsible for the exceptions of OCTA's policies and procedures.

¹ Testing performed involved judgmental sampling with a bias toward certain characteristics of the attributes to be tested. As such, the results cannot be projected to the population of transactions.

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Management Response:

Management concurs. The AP supervisor meets bi-weekly with staff and has included training on AP procedures and responsibilities and has/will communicate to departments responsible for the related exceptions as to OCTA's Policies and Procedures.

Strengthen Procurement Requirements at Cofiroute

In its capacity of providing operational and management services of the 91 Express Lanes, Cofiroute routinely makes purchases on behalf of OCTA and is provided access to the IFAS system for the purpose of entering payment transactions. Cofiroute procurement rules are not aligned with OCTA procurement policies and procedures, which are designed to foster competition and ensure economical pricing for goods and services.

Cofiroute purchases equipment, hardware/software, vehicles, administrative supplies, and professional services necessary for the operation of the 91 Express Lanes. During the 18 month period reviewed, these purchases totaled approximately \$1.3 million. These purchases undergo multiple levels of review by Cofiroute management and are generally pre-approved by OCTA Toll Roads management via email communications. Cofiroute purchasing procedures require completion of a Purchase Requisition form, a Purchase Order form, and a Vendor Selection Justification (VSJ) form; however, procedures do not address vendor selection.

The VSJ form reflects whether the goods and services were acquired from a preferred vendor, through competitive selection, or as a sole source. For nearly every transaction, the VSJ form indicated the procurement was not competitive. The VSJ form often indicated "vendor offers the best price and service" without additional documentation.

Agreement No.C-5-0300 (Agreement) between OCTA and Cofiroute requires Cofiroute to maintain policies and procedures that cover all processes of every kind and nature necessary for the performance of the contract. The Agreement goes on to identify 21 functional areas requiring policies and procedures; however, procurement is not included. In Section A.2.8, Contract Administration, the Agreement states that Cofiroute shall administer contracts in accordance with guidelines provided to them by OCTA; however, no guidelines have been provided to Cofiroute.

Recommendation 3:

Internal Audit recommends that management amend the Agreement with Cofiroute to include procurement guidelines and implement monitoring controls to ensure compliance. These guidelines should be consistent with OCTA's procurement policies and procedures.

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Management Response:

Management concurs and will work with Cofiroute to develop procurement guidelines and incorporate these guidelines in the operating agreement.