July 31, 2014

Dr. Daniel, President

Ms. Lisa Choate, Chair of the Audit and Compliance Committee,

We have completed an audit over the expenditure process as part of our Fiscal Year 2014 Audit Plan, and the report is attached for your review. The audit was conducted in accordance with the Institute of Internal Auditors’ *International Standards for the Professional Practice of Internal Auditing*. The objectives of the audit were to provide assurance that adequate controls exist over the expenditure process, including payables and receiving.

Overall, we found that adequate controls exist over the expenditures process. Opportunities exist, however, to improve internal controls over the payables and receiving processes, as outlined in the attached detailed report.

Management has reviewed the recommendations and has provided responses and anticipated implementation dates. Though management is responsible for implementing the course of action outlined in the response, we will follow up on the status of implementation subsequent to the anticipated implementation dates. We appreciate the courtesies and considerations extended to us during our engagement. Please let me know if you have any questions or comments regarding this audit.

Toni Stephens
Executive Director of Audit and Compliance

*UT Dallas Responsible Parties:*
Mr. Pete Bond, Assistant Vice President for Procurement Management

*Members of the UT Dallas Audit and Compliance Committee:*
External Members:
Mr. Bill Keffler
Mr. Ed Montgomery
Ms. Cynthia Trochu
Dr. Hobson Wildenthal, Executive Vice President and Provost
Dr. Calvin Jamison, Vice President for Administration
Mr. Terry Pankratz, Vice President for Budget and Finance
Dr. Andrew Blanchard, Vice President for Information Resources and Chief Information Officer, Dean of Undergraduate Studies
Dr. Bruce Gnade, Vice President for Research
Dr. Darrelene Rachavong, Vice President for Student Affairs
Mr. Timothy Shaw, University Attorney

*The University of Texas System:*
Dr. Pedro Reyes, Executive Vice Chancellor for Academic Affairs
Mr. Alan Marks, Assistant Vice Chancellor of Academic Affairs and Athletics Counsel
Mr. J. Michael Peppers, CIA, CRMA, CPA, FACHE, Chief Audit Executive
Ms. Moshmee Kalamkar, CPA, CIA, Audit Manager

*State of Texas Agencies:*
Legislative Budget Board
Governor’s Office
State Auditor’s Office
Sunset Advisory Commission

AN EQUAL OPPORTUNITY/AFFIRMATIVE ACTION UNIVERSITY
Executive Summary

*Expenditure Process, Report No. 1416*

**Audit Objective and Scope:** The objectives of the audit were to provide assurance that adequate controls exist over the expenditure process, including payables and receiving. The scope of the review was fiscal year 2013 to present.

**Audit Results:**
The audit resulted in no priority recommendations to University operations; however, we offer the following recommendations to strengthen and enhance operations and internal controls.

<table>
<thead>
<tr>
<th>Recommendation</th>
<th>Estimated Implementation Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1) Enhance Monitoring Procedures over Vouchers</td>
<td>August 31, 2014</td>
</tr>
<tr>
<td>(2) Enhance Use of Electronic Payment Methods</td>
<td>September 30, 2014</td>
</tr>
<tr>
<td>(3) Implement Desktop Receiving</td>
<td>August 31, 2015</td>
</tr>
<tr>
<td>(4) Enhance Monitoring over Applied Invoices</td>
<td>December 15, 2014</td>
</tr>
<tr>
<td>(5) Enhance Monitoring over Open Purchase Orders</td>
<td>August 31, 2014</td>
</tr>
<tr>
<td>(6) Enhance Monitoring over Duplicate Invoices</td>
<td>September 30, 2014</td>
</tr>
</tbody>
</table>

**Conclusion:** Overall, we found that adequate controls exist over the expenditures process. Opportunities exits, however, to improve internal controls over the payables and receiving processes.

**Responsible Vice President:**
Mr. Terry Pankratz, Vice President for Budget and Finance

**Responsible Party:**
Mr. Pete Bond, Assistant Vice President for Procurement Management

**Staff Assigned to Audit:**
Dylan Becker, CPA, CIA, Senior Auditor, In-Charge Auditor
Hiba Ijaz, Student Intern
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Background

Expenditure processes are administered by Procurement Management for all departments at UTD. SciQuest is the purchasing software that is used to record all requisitions and purchase orders issued to outside vendors. The workflow established in SciQuest that is used to facilitate the purchasing process helps ensure proper segregation of duties, proper approvals for purchases are documented, and a detailed audit trail exists. A total of approximately 38,100 payments were made for approximately $340 million during Fiscal Year 2013.

Procurement Management reports directly to the Vice President of Budget and Finance and has a total of 48 employees, including 26 full-time employees and 22 part-time employees. Procurement Management consists of different functions that work to ensure the payables and expenditures processes are properly administered and accurate and timely payments are made to vendors. The primary functions include accounts payable, purchasing, and facilitating the pay cycle. Accounts Payable is also responsible for administering the receiving process for certain items and only active vendors are eligible to receive payments.

Central Receiving reports directly to the Vice President of Administration and administers the receiving function for all inventoried items, such as capital and controlled items. This process helps ensure accurate inventories and capital assets are properly recorded and received prior to impacting the financial statements. A total of 14 employees, including 11 full time and three part time employees, received a total of approximately 3,207 items for $29.6 million during Fiscal Year 2013. All items received by Central Receiving are received directly in PeopleSoft to ensure a three way match between the purchase order, invoice, and receipt exists before payments are authorized.

Audit Objective

The objectives of the audit were to provide assurance that adequate controls exist over the expenditure process, including payables and receiving.

Scope and Methodology

The scope of this audit was fiscal year 2013 to date, and our fieldwork concluded on June 10, 2014. To satisfy our objectives, we performed the following:

- Interviewed staff and observed documentation to gain an understanding of current operations and processes over accounts payables, receiving, PeopleSoft and Sciquest, and payments to vendors.
• Tested selected purchase orders to determine:
  o Proper matching of purchase orders to vouchers and receipts
  o The accuracy of payments to vendors
  o The payables and pay cycles followed established workflow
  o A proper segregation of duties existed
  o Purchase orders are closed in a timely manner
  o Encumbrances are released in a timely manner

• Reviewed selected payments made to determine:
  o Payment methods used to pay vendors
  o The likelihood and probability of duplicate payments

Where applicable, we conducted our examination in accordance with the guidelines set forth in The Institute of Internal Auditor’s International Standards for the Professional Practice of Internal Auditing. The Standards set criteria for internal audit departments in the areas of independence, professional proficiency, scope and performance or audit work, and management of the internal auditing department.

Audit Results and Management’s Responses

Overall, we found that adequate controls exist over the expenditures process. Opportunities exits, however, to improve internal controls over the payables and receiving processes. Our audit work indicated that the following controls currently exist:

• Workflow has been established in SciQuest to help facilitate the payables and pay cycles;
• Controls exist in PeopleSoft that identify and prevent payments of identical invoices from the same vendor;
• Receipt requirements for capital and controlled items are established;

A priority recommendation is defined as one that may be material to operations, financial reporting, or legal compliance. This would include an internal control weakness that does not reduce the risk of irregularities, illegal acts, errors, inefficiencies, waste, ineffectiveness, or conflicts of interest to a reasonable low level. We have no priority recommendations resulting from this audit; however, the following recommendations will help enhance financial reporting process and minimize the risk of material misstatements going undetected in a timely manner.
Audit Recommendations

(1) Enhance Monitoring Activities over Vouchers

Purchase orders that were used to procure goods or services represent open encumbrances against departmental budgets until they are invoiced. Once the invoice is received a payment voucher is issued and the expense is recorded. The payment vouchers should be tied to the purchase orders to ensure accurate and complete accounting and financial records are maintained and encumbrances are released in a timely manner.

We reviewed purchase orders that had an invoice date between August and December 2013 and noted there were 104 paid vouchers for approximately $364,000 that were not tied to the purchase orders that were used to order the goods or services. Best practices suggest that purchase orders should be tied to the vouchers that were used to make payments to ensure that encumbrance balances are accurate, budgeted funds are fully utilized, and the risk of duplicate payments is reduced. Insufficient monitoring procedures existed over vouchers. As a result, the risks were increased that encumbrances were not released in a timely manner, and that erroneous payments made to vendors were not detected in a timely manner.

Recommendation: Procurement Management should consider enhancing monitoring procedures to identify paid vouchers that were not tied to the purchase order used to order the goods or services and ensure encumbrances are released in a timely manner.

Management’s Response: Queries will be built to identify purchase orders that have not been fully liquidated in a timely fashion. The use of the existing encumbrance report that has been use for the past couple of months will continue to be of help for departments to identify encumbrances that should be fully liquidated. Enhancement of training information, including but not limited to the FAQ (ASKYODA) will give specific instructions on how to clean up stale encumbrances.

Estimated Date of Implementation: August 31, 2014

Person Responsible for Implementation: Pete Bond, Assistant Vice President for Procurement Management, for Division of Budget & Finance
(2) **Enhance Use of Electronic Payments to Vendors**

Payments to vendors from UTD are made by three primary methods; hard copy checks, electronic funds transfer (EFT) and wire transfers. To execute payments using the EFT or wire transfer method, it is necessary for UTD to have the bank account information from the vendors. Payments made with hard copy checks do not require bank account information and must be printed and mailed from UTD to the address on file for the vendor.

From the start of fiscal year 2013 to April 30, 2014 (20 accounting periods), approximately 84% of all payments issued to vendors were made with hard copy checks. Additionally, we identified that 263 vendors received between 11 and 19 checks, and 213 vendors received at least 20 checks during the period reviewed. A summary of the frequency of payments methods is below:

<table>
<thead>
<tr>
<th>Frequency of Types of Transactions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Type</td>
</tr>
<tr>
<td>Check</td>
</tr>
<tr>
<td>EFT</td>
</tr>
<tr>
<td>WIRE</td>
</tr>
<tr>
<td>TOTAL</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Frequency of Checks to Same Vendors</th>
</tr>
</thead>
<tbody>
<tr>
<td>No. of Checks Issued</td>
</tr>
<tr>
<td>----------------------</td>
</tr>
<tr>
<td>10-19</td>
</tr>
<tr>
<td>&gt; 20</td>
</tr>
</tbody>
</table>
Increasing the use of electronic payment methods, such as EFT and wire transfers, help reduce errors, expedite payments, create an enhanced audit trail and reduce costs. Approximately 1% of all approved vendors, as of April 30, 2014, had their bank account information on file with UTD. As a result, the risk of untimely payments is increased, errors could go undetected in a timely manner, and the cost of issuing payments is increased.

**Recommendation:** Procurement Management should consider requesting information necessary to establish electronic payment processes from vendors that have received multiple payments from UTD.

**Management’s Response:** Procurement Management will semi-annually run a vendor query identifying the University’s primary vendors not on EFT payment method. Initial communication will begin September 30, 2014. From this we will pass on information on how to be paid electronically on future transactions. We are currently setting up vendors who put EFT instructions on their invoices. For new vendors, information will be given at time of set-up in the system on how the University expects to pay its vendors and pass that information on to vendor at that time. The University is also looking at banking solutions to take on the payment function for the University.

**Estimated Date of Implementation:** September 30, 2014

**Person Responsible for Implementation:** Pete Bond, Assistant Vice President for Procurement Management, for Division of Budget & Finance

(3) **Implement Desktop Receiving**

The SciQuest system is used to document the receipt of goods purchased that are not required to be received by Central Receiving and have met certain criterion. Purchase orders that are less than $500 or contain office supplies do not require a receipt to be documented in SciQuest prior to payment. Items that are considered capital assets or controlled items are inventoried by UTD and must be received by Central Receiving before payments can be authorized.

During the audit, we noted that Procurement Management was responsible for indicating receipt of non-capital and non-controlled items in SciQuest. Additionally, reliance was placed on emails from the departments to confirm that goods or services were actually delivered. Procurement Management requested to be responsible for the receiving function when SciQuest was implemented to help prevent untimely receipt of goods and services and to minimize the risk of delayed payments. A proper segregation of duties suggests that the same function that administers the pay cycle should not be responsible for the receiving function.
A desktop receiving function exists in SciQuest to allow departmental users to document the receipt of goods purchased. Implementing this function would enhance segregation of duties and eliminate the need and time spent for Procurement Management employees to email departments to verify receipt of goods.

**Recommendation:** Procurement Management should consider implementing desktop receiving for non-capital and non-controlled items.

**Management’s Response:** We will assign a team to begin a project plan for implementing departmental desktop receiving in early FY15. Initially we will roll out to a pilot group and expand to select users in all departments. The project will involve developing procedures, workflow and training. We anticipate implementing desktop receiving for the pilot group by December 2014 and to entire campus by summer 2015.

**Estimated Date of Implementation:** August 31, 2015

**Person Responsible for Implementation:** Pete Bond, Assistant Vice President for Procurement Management, for Division of Budget & Finance

(4) **Enhance Monitoring Activities Over Applied Invoices**

Purchase orders can have multiple line items if different types of items have been ordered. Each line item on the purchase order contains the amount, quantities, and cost of the items ordered. PeopleSoft has been established to apply the line items of the invoice to the line items of the purchase orders. For example, line one of the invoice will be applied to line one of the purchase order, and line two of the invoice will be applied to line two of the purchase order. When invoices are received from vendors, they are initially entered into SciQuest by Procurement Management and may contain an equal number of line items as the purchase order, or a single line item that consolidates the total amount of the items delivered to UTD.

During the first quarter of fiscal year 2013, we noted there were 38 purchase orders where the quantities and amounts contained on the line items of the invoice was incorrectly applied to the amounts and quantities on the line items of the purchase order. The total variance between the line items of the purchase orders and the applied line items of the invoices was approximately $646,000. To pay the difference between the line items of the purchase order where the invoice was applied, and the total invoiced amount, funds were expensed directly from the department’s budget rather than from the funds that had already been reserved as an encumbrance from the departmental budget for payment. As a result, encumbrances and fund balances were not accurate during Fiscal Year 2013, and an enhanced risk existed that budgeted funds were not fully utilized.
**Recommendation:**  Procurement Management should consider reviewing the pay cycle to help ensure that the invoices are appropriately tied to the purchase order.

**Management’s Response:**  The Inventory and Fixed assets group is current notifying Purchasing and AP when line items are altered in PeopleSoft so that AP Specialist can pay the invoice against all lines directly in PeopleSoft rather than in SciQuest. This should eliminate hanging encumbrances on the additional lines. In addition, the open encumbrance report that is being distributed to end users and being reviewed by Procurement will help identify issues like this in a timely manner so that hanging encumbrances can be cleared quickly.

**Estimated Date of Implementation:**  December 15, 2014

**Person Responsible for Implementation:**  Pete Bond, Assistant Vice President for Procurement Management, for Division of Budget & Finance

**Enhance Monitoring over Open Purchase Orders**

Open purchase orders are encumbered from departmental budgets until they invoiced. Once the purchase order has an invoice applied, the encumbrance is released and a liability is recorded in PeopleSoft.

We reviewed purchase orders that had one invoice applied during fiscal year 2013 and noted that purchase orders were not closed in a timely manner. The average number of days to enter an invoice was 18, but the average number of days that a purchase order remained open was 131. Additionally, the average number of days to close the purchase order after an invoice was recorded was 111.

See tables below for a summary of fiscal year 2013 purchase orders:

<table>
<thead>
<tr>
<th>Days to Enter Invoice (Days Encumbered)</th>
<th>No. Days</th>
<th>PO Count</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>0-30</td>
<td>16,993</td>
<td>$ 22,596,155</td>
<td></td>
</tr>
<tr>
<td>31-60</td>
<td>978</td>
<td>$ 6,165,662</td>
<td></td>
</tr>
<tr>
<td>61-120</td>
<td>669</td>
<td>$ 7,376,982</td>
<td></td>
</tr>
<tr>
<td>121+</td>
<td>426</td>
<td>$ 3,893,559</td>
<td></td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td>19,066</td>
<td><strong>$ 40,032,358</strong></td>
<td></td>
</tr>
</tbody>
</table>

Avg = 18 Days

<p>| Total Days to Close (Days PO Remained Open) | |
|-------------------------------------------|---|---|---|</p>
<table>
<thead>
<tr>
<th>No. Days</th>
<th>PO Count</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>TOTAL</td>
<td>19,066</td>
<td><strong>$ 40,032,358</strong></td>
</tr>
</tbody>
</table>
Closing purchase orders in a timely manner helps ensure budgeted funds are effectively utilized, the risk of duplicate payments is reduced, and encumbrances are released in a timely manner.

**Recommendation:** Procurement Management should consider enhancing monitoring procedures over open purchase orders.

**Management’s Response:** Monthly distribution of the open encumbrance report will be sent to each cost center manager with step by step instructions on how to clean up invalid encumbrance balances.

**Estimated Date of Implementation:** August 31, 2014

**Person Responsible for Implementation:** Pete Bond, Assistant Vice President for Procurement Management, for Division of Budget & Finance

(6) **Enhance Monitoring over Duplicate Invoices**

A feature within PeopleSoft was recently turned on that effectively identifies duplicate invoices from the same vendors and prevents payments without additional authorization.
This feature does not, however, prevent payments against invoices that are similar but not identical from the same vendor. During fiscal year 2013, we identified a total of 4,053 invoices from the same vendors that were at least 98% similar. Monitoring invoices that are similar, but not identical, helps identify additional potential duplicate payments and enhances existing internal controls.

One way to prevent monitoring of similar invoices from the same vendor would be to use fuzzy logic functionalities in Excel. Internal Audit shared this logic with Procurement Management as an option to consider.

**Recommendation:** Procurement Management should consider implementing additional monitoring procedures to further enhance the risk of duplicate payments.

**Management’s Response:** We have obtained the file from Internal Audit that provides a methodology for applying “fuzzy logic” to invoice numbers and amounts that will help identify possible duplicate payments. We will review this process as well as research other tools including audit software, queries, or PeopleSoft provided reports to help identify similarities that could be potential duplicates. In addition, departmental reconcilers help identify duplicates so they can be resolved in a timely manner. We will also expand training to Accounts Payable staff to improve consistency in data entry processes to become more consistent in invoice number format so that the system can help identify duplicates before they happen.

**Estimated Date of Implementation:** September 30, 2014

**Person Responsible for Implementation:** Pete Bond, Assistant Vice President for Procurement Management, for Division of Budget & Finance

**Conclusion**

Overall, we found that adequate controls exist over the expenditures process. Opportunities exist, however, to improve internal controls over the payables and receiving processes.

We appreciate the courtesy and cooperation received from the management and staff of the Procurement Management office during this audit.