



**A Report to the
Audit Committee**

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Audit of Unusual Financial Related Transactions

September 22, 2014

Metropolitan
Nashville
Office of
Internal Audit

EXECUTIVE SUMMARY

September 22, 2014



Why We Did This Audit

The audit was initiated to analyze financial related transactions that look unusual. This analysis is an important part of financial transparency and stewardship over public funds.

What We Recommend

- Regular verification of vendors should be conducted to ensure only active vendors are maintained in vendor master file.
- Credit Card policies should be enforced to ensure that only valid and authorized purchases are made.

For more information on this or any of our reports, email Mark.Swann@nashville.gov

AUDIT OF UNUSUAL FINANCIAL RELATED TRANSACTIONS

BACKGROUND

The Metropolitan Nashville Government like any other organization is susceptible to errors, fraud, or inefficiencies. With an annual budget exceeding \$1.8 billion dollars, there are possible risks that include fraudulent financial reporting, misappropriation of assets, corruption, regulatory and legal misconduct, and public mistrust.

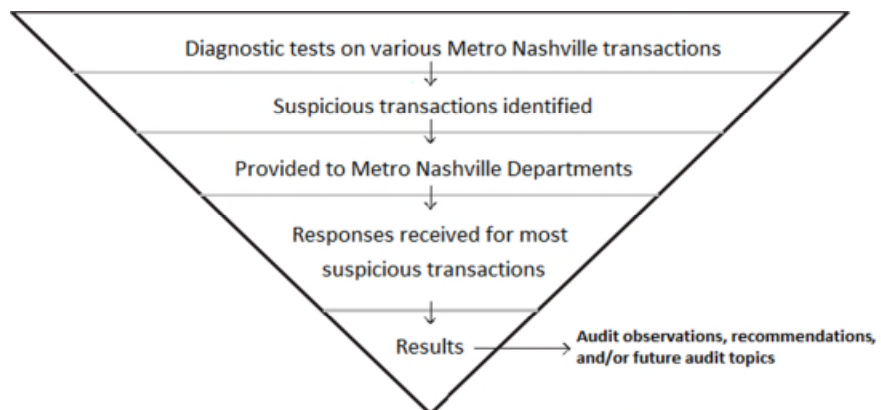
The ability to use analytical procedures helped the Metropolitan Nashville Office of Internal Audit identify unusual transactions or outliers. The review of those transactions will help ensure that Metropolitan Nashville Government service delivery purpose was conducted as intended.

OBJECTIVES AND SCOPE

The objectives of the audit were to:

- Determine if there were any unexplainable unusual expenditures.
- Determine if there were any unexplainable unusual payroll entries.
- Determine if there were any unexplainable additions, deletions, or changes made to the vendor and employee master files (EBS address book).

The audit scope included the three calendar years ended December 31, 2011, December 31, 2012, and December 31, 2013. Testing covered the Metropolitan Nashville general government except the Fire Department for payroll test. Fire Department payroll is scheduled for a separate future audit.



WHAT WE FOUND

We found there were controls in place to limit the risk related to unauthorized financial transactions. However, additional steps can be taken to strengthen processes around credit card review, address book maintenance, vendor verification, and employee benefit disclosures.

GOVERNANCE

The Metropolitan Nashville Charter outlines the director of finance's powers and duties. Under the general guidance of the Mayor, the director of finance is responsible for the administration of the financial affairs of the Metropolitan Nashville Government. The director of finance has final authority for all financial related decisions made on behalf of the Metropolitan Nashville Government.

OBJECTIVES AND CONCLUSIONS

1. *Were there any unexplainable unusual expenditures?*

Yes. Our conclusion was based upon evaluations of the following sub-objectives:

a) *Were duplicate payments made?*

Yes. Test results indicated that 40 (less than one percent) out of 54,854 payments that exceed \$5,000 were related to a duplicate payment. EnterpriseOne was configured to prevent the reuse of the same invoice number for the same vendor however, it did not check across multiple vendors or prevent the enterer from adding additional characters at the end of the original invoice number. (See Observation A.)

b) *Were there any employees and vendors with matching banking information?*

Yes. There were 29 instances where an employee and vendor had bank account and routing numbers that matched. However, after reviewing the payments made to both parties, there were no payments identified as invalid. The main two causes of match were:

- Employees conducting work outside of their normal duties and being paid as vendors. (See Observation C.)
- Vendors becoming employees after their work was complete.

c) *Were there any unusual credit card purchases?*

Yes. A review of 384 credit card purchases for purposefully selected vendors (see Appendix C) demonstrated a lack of compliance with Finance Department Policy #19. Credit card purchases could improve in the following areas:

- 14 purchases (3.6 percent) lacked sufficient explanation of business purpose.
- 10 purchases (2.6 percent) had missing receipts.
- 36 plus purchases (9.4 percent) were for items that Metropolitan Nashville Government has an active contract for.
- 14 purchases (3.6 percent) were for the purchase of gift cards (gift cards can be used as a form of cash advance which is prohibited by Finance Department Policy #19). (See Observation G.)

2. *Were there any unexplainable duplicate tax identification numbers in the vendor address book?*

Yes. Two reviews were conducted on duplicate tax identification numbers. The first review compared vendors to vendors. There were 2,161 tax identification numbers that had multiple active vendors (6,723 – vendors) associated with one of those numbers. Of those 6,723 vendors, 3,221 had not received a payment. (See Observation B.)

The second review compared vendors to employees. There were 660 tax identification numbers that had both a vendor and employee associated with them. Employees received employee related reimbursements through their vendor numbers, similar payments were made to both the vendor and employee numbers, and employees were hired in other departments as vendors causing the employee to receive an Internal Revenue Service Form W-2 Wage Tax Statement and Form 1099-MISC Miscellaneous Income from the same employer. (See Observation C.)

3. *Were there any unexplainable additions, deletions, or changes to the EnterpriseOne Address Book?*

Undeterminable. The audit trail function within EnterpriseOne was capturing additions, deletions, and changes to the address book. Even though it had been activated, it was not being utilized and therefore a lack of knowledge existed on how to comprehend the report. The report had not been formatted to readily identify what changes have occurred. (See Observation B.)

4. *Were there any unexplainable unusual fuel card transactions?*

Yes. A review was conducted of multiple fuel transactions in one day, transactions after normal business hours, and non-fuel transactions. The review of multiple transactions in one day found that 34 of 317 transactions (11 percent) were either duplicate transactions, compromised transactions, transactions that could not be explained by the department, or instances where a wrong card was used. Monitoring of fuel transactions could decrease the occurrence of these types of transactions. (See Observation D.) Reasonable explanations were received for all transactions after normal business hours and non-fuel transactions.

5. *Were there any unexplainable unusual payroll entries and transactions?*

Generally Yes. Our conclusion was based upon evaluations of the following sub-objectives.

a) *Were there any employees with excess overtime or comp time?*

Yes. For the departments reviewed, the lack of detailed documentation explaining the need for overtime or comp time was common throughout. (See Observation E.)

b) *Were there any departments or employees with excessive out-of-class pay?*

No. A review of out-of-class pay showed that departments were getting approval from Metro Nashville Human Resources or the Department of Finance prior to assigning the pay class to employees. The appropriate documentation was being maintained within each department documenting the eligibility for out-of-class pay.

c) *Were there any employees with unexplainable duplicate banking information with another employee?*

No. A review of banking information of employees demonstrated that there were employees with matching banking information. However, test results indicated reasonable explanations for the bank information to match.

6. *Were businesses complying with business license requirements?*

Generally Yes. A review of 75 vendors that conducted business with the Metropolitan Nashville Government between 2011 and 2013 demonstrated that most vendors were complying with business license requirements. There were 23 vendors (31 percent) that did not have a business license and appear not to be exempt from business license requirements. The Office of Internal Audit could only accurately identify two vendors that should have obtained a business license but

did not. Final determination of the exemption status of the remaining 21 vendors requires additional information not obtained because they were located out of county. (See Observation F.)

AUDIT OBSERVATIONS

Internal control helps entities achieve important objectives and sustain and improve performance. The Committee of Sponsoring Organizations of the Treadway Commission (COSO), *Internal Control – Integrated Framework (2013 Framework)*, enables organizations to effectively and efficiently develop systems of internal control that adapt to changing business and operating environment, mitigate risks to acceptable levels, and support sound decision making and governance of the organization. The audit observations listed are offered to assist management in fulfilling their internal control responsibilities. A summary of *Internal Control – Integrated Framework (2013 Framework)* components and principles can be seen in Appendix B.

Observation A - Duplicate Payment Preventive Controls

Duplicate payments continue to be a challenge to minimize due to several factors that have contributed to the processing of duplicate payments. Those factors included but were not limited to:

- Address Book Maintenance – The vendor address book contains multiple entries for the same vendor which may lead to confusion on which vendor record should be selected for payment (see Observation B for additional detail).
- Payment Services Personnel – EnterpriseOne, the accounting software utilized by the Metropolitan Nashville Government, was configured to prevent the reuse of the same invoice number for the same vendor. However, test results indicated that personnel attached a letter to the end of the invoice number to avoid the configuration in place to prevent duplicate invoices from being processed. For example, invoice number “1234” would be entered the second time as “1234A”, which would not be flagged as a duplicate invoice.

Criteria:

The Committee of Sponsoring Organizations of the Treadway Commission, *Internal Control – Integrated Framework (2013 Framework)*, Control Activities – Principle 12

Recommendation for management of the Finance Department to:

1. Run periodic reports to check for duplicate payments. This report may be coded to flag for duplicate invoice numbers across multiple vendors.
2. Provide additional training and guidance for invoice enterers on how to handle duplicate invoice number error codes within EnterpriseOne to prevent duplicate payments.

Observation B - Address Book Maintenance

Duplicate and Out-of-Date Vendors Maintained in Address Book

By maintaining multiple records for the same vendor, the risk of duplicate or fraudulent payments increases dramatically. Duplicate vendors were maintained within EnterpriseOne, the official accounting system for the Metropolitan Nashville Government. The vendor master file (address book) is

a critical part of the procurement and accounts payable control environment, and a well-maintained file helps prevent control failures, inefficient processing, and inaccurate management reporting.

Active entries should be reserved for vendors that have recently conducted business with the Metropolitan Nashville Government. There were several active vendors that had not received payments from the Metropolitan Nashville Government in the last seven years. It becomes more difficult to select legitimate vendor records when a large volume of unnecessary vendor entries exist.

Unused and Ineffective Audit Trail Function

The “Audit Trail” report (implemented in 2010) was cumbersome to determine the exact change that occurred. In order to efficiently utilize the audit trail function it should allow the user to easily identify the specific information related to the change that occurred.

Criteria:

The Committee of Sponsoring Organizations of the Treadway Commission, *Internal Control – Integrated Framework (2013 Framework)*, Information and Communication – Principle 13

Recommendation for management of the Finance Department to:

1. Develop regular verification procedures to assure records are current and accurately reflect Metropolitan Nashville activity with its vendors.
2. Simplify the current audit trail function to capture only prudent information to allow for the changes to be readily identifiable.

Observation C – Disclosure Requirements for Employees Paid as Vendors

Active employees paid as vendors have not fully complied with Metropolitan Nashville Procurement Code, Ethic in Public Contracting disclosure requirements. These requirements state employees benefiting from Metropolitan Nashville Government contracts should report such benefits to the Metropolitan Nashville Procurement Appeals Board. There were no disclosures filed with the Board.

Criteria:

- The Committee of Sponsoring Organizations of the Treadway Commission, *Internal Control – Integrated Framework (2013 Framework)*, Control Environment – Principle 1
- Metropolitan Nashville Code of Laws § 4.48.060, Employee Disclosure Requirements

Recommendation for management of the Finance Department to:

Ensure employees serving as active vendors are notified of Metropolitan Nashville Procurement Code disclosure requirements.

Observation D - Monitoring of Fuel Card Transactions

A review of fuel card transactions for a single day identified 34 unauthorized transactions out of 317 transactions that should have been discovered by monitoring activities in the responsible departments. In addition, a limited survey of fleet coordinators indicated that some of the responding departments had no formalized department level monitoring process.

Criteria:

- The Committee of Sponsoring Organizations of the Treadway Commission, *Internal Control – Integrated Framework (2013 Framework)*, Monitoring Activities – Principle 16
- Metropolitan Nashville General Services Department Administrative Order Number 39 – Fuel Program

Recommendation for management of the General Services Department to:

Reiterate to department heads that fuel card usage should be monitored by their departments. Monitoring should include verifying odometer readings, fuel type, location and time of purchase, quantity of fuel, who fueled the vehicle, purchases of non-fuel services or items, and multiple transactions in one day for the same fuel card.

Observation E – Overtime and Comp time Approval

Long hours can detrimentally affect workers, their co-workers, their families, and the public. When individuals routinely work overtime, it may in the long term create harm to the organization by decreasing quality, increasing mistakes, and reducing productivity. The standard work week for most Metropolitan Nashville employees is 40 hours per week. Some employees in police and water services were averaging in excess of 60 work hours per week. Civil Services Rules Section 5.7, Special Pay Provisions, state that “It is the policy of Metropolitan Nashville that overtime shall not be worked unless essential to the public interest or to preserve public health and safety.”

Criteria:

The Committee of Sponsoring Organizations of the Treadway Commission, *Internal Control – Integrated Framework (2013 Framework)*, Control Environment – Principle 4, Control Activities – Principle 12

Recommendation for management of the Police Department and Metro Water Services to:

Decide if a workload study will be beneficial to identify potential areas that may need to be addressed further related to prolonged overtime requirements.

Observation F - Conducting Business with Unlicensed Vendors

The Metropolitan Nashville Government paid approximately \$400 thousand to two businesses that failed to comply with the business license requirements. There were potentially 21 other vendors that did not obtain a business license but should have. Those 21 vendors were located out-of-county or out-of-state. Determination of their exemption status requires additional information not available in the vendor files. Identification of unlicensed vendors becomes problematic because of the numerous exceptions granted to different business types. The current process of vendor verification only includes requiring a tax identification or employer identification number and requiring a valid bank account to be deemed legitimate.

No person shall conduct business in Tennessee without first acquiring the appropriate business licenses required. In order to maintain the licenses, businesses are required to file a business tax return and remit the amount of tax due.

Criteria:

- The Committee of Sponsoring Organizations of the Treadway Commission, *Internal Control – Integrated Framework (2013 Framework)*, Risk Assessment – Principle 6
- Tennessee Code Annotated § 67-4-701 Business Tax Act

Recommendation for management of the Finance Department to:

Add an additional step in the vendor verification process to verify the vendor has a current and valid business license to conduct business in the state of Tennessee or is exempt from business tax.

Observation G - Credit Card Usage

A review of 384 credit card purchases purposefully selected based on vendor name (see Appendix D) demonstrated a lack of compliance with Finance Department Policy #19. Credit card purchases could improve in the following areas:

Purchasing Contracted Items

Metropolitan Nashville Government has entered into contracts with various suppliers for a wide range of items from office supplies to computer equipment. Each department was required to sign a Notice of Delegation of Purchasing Agent's Authority which prohibits the purchase of contracted supplies or services from non-contracted firms. There were 36 identified purchases (9.4 percent) where the items that were purchased had a valid contract to purchase from.

Lack of Documentation

Section six of Metropolitan Nashville Government's Credit Card Policy requires each cardholder to ensure sufficient documentation to support all charges and payments made with their credit card exists. It also requires departments to maintain this documentation in a central location in the event of an audit or review. Fourteen purchases (3.6 percent) lacked sufficient explanation of business purpose and ten purchases (2.9 percent) were missing receipts. Without the proper supporting documentation, it is very difficult to ensure that only valid and authorized purchases were made. Documentation also provides management with the necessary support to identify fraudulent or personal items being purchased.

Gift Cards

Gift card purchases were difficult to review because receipts were not consistently provided for the actual items purchased with the gift card. There was a transaction showing where the gift card was received but nothing to show how the gift card was actually used. Metropolitan Nashville's Credit Card Policy prohibits the use of cash advances. Gift cards can be used as a form of cash advances because you place a predetermined cash amount on the card for future use. Documentation provided showed that 14 purchases (3.6 percent) were for the purchase of gift cards.

Criteria:

- The Committee of Sponsoring Organizations of the Treadway Commission, *Internal Control – Integrated Framework (2013 Framework)*, Monitoring Activities – Principle 16
- Notice of Delegation of Purchasing Agent's Authority

- Metropolitan Nashville Government’s Finance Department, Treasury Policy #19 Credit Card

Recommendation for management of the Finance Department to:

1. Reiterate to department heads that items that are under contract should be purchased from one of Metropolitan Nashville Government’s contracted firms through the iProcurement system.
2. Reiterate to department heads and cardholders the importance of maintaining the proper supporting documentation for all credit card purchases.
3. Reiterate to department heads that if exceptions to portions of the Credit Card Policy are needed, a request to the Finance Director for approval should be submitted.

GOVERNMENT AUDITING STANDARDS COMPLIANCE

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 observations and conclusions based on our audit objectives.

METHODOLOGY

To accomplish our audit objectives, we performed the following steps:

- Interviewed key personnel within various departments.
- Reviewed and analyzed documentation for compliance with the Tennessee Code Annotated, Metropolitan Nashville Code of Laws, and other applicable laws, regulations, and policies.
- Evaluated internal controls currently in place.
- Reviewed sample selections to determine the effectiveness of internal controls.
- Reviewed financial related transaction files using audit analytic software.
- Considered risk of fraud, waste, and abuse.
- Considered information technology risks.

AUDIT TEAM

Mark Swann, CPA, CIA, CISA, Metropolitan Auditor

Tracy Carter, CFE, In-Charge Auditor

Seth Hatfield, CPA, CIA, Auditor

Lauren Riley, CPA, Senior Auditor

APPENDIX A – MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN



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MAYOR

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September 10, 2014

Mr. Mark Swann
Metropolitan Auditor
Office of Internal Audit
1417 Murfreesboro Road
Nashville, TN 37217

Dear Mr. Swann: *Mark*

This letter acknowledges the Finance Department's receipt of the audit of unusual transactions. We have reviewed the findings and recommendations and have incorporated our responses in Appendix A to the attached report.

We appreciate the work you have done to help us improve our processes and internal controls, and we appreciate the professionalism of the Internal Audit staff in conducting the work.

Sincerely,

Richard M. Riebeling
Director of Finance

Attachment

Copy: Kim McDoniel
Tom Eddlemon
Jeff Gossage

APPENDIX A – MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN

We believe that operational management is in a unique position to best understand their operations and may be able to identify more innovative and effective approaches and we encourage them to do so when providing their response to our recommendations.

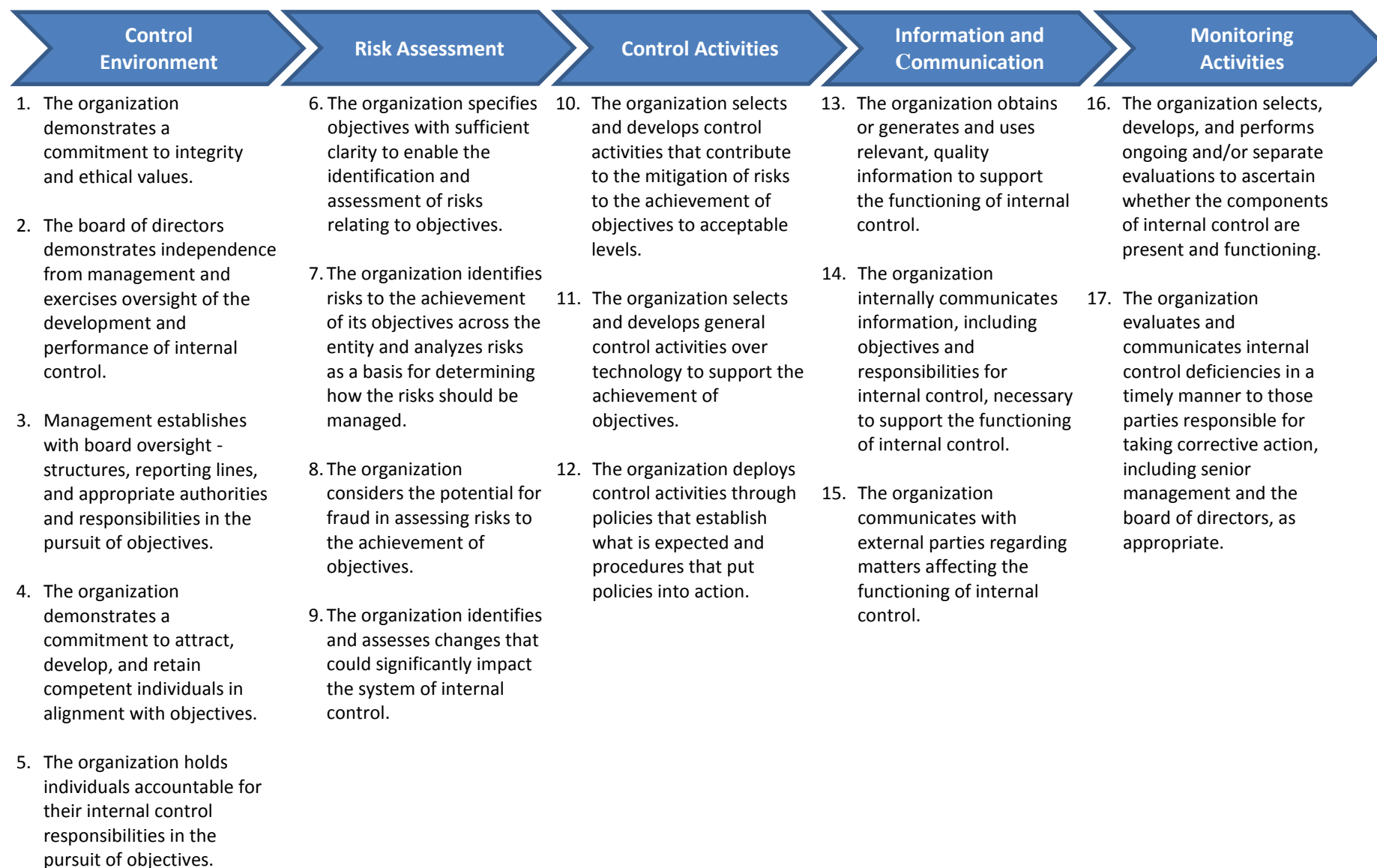
Recommendations	Concurrence and Corrective Action Plan	Proposed Completion Date
Management of the Finance Department should:		
<p>A1. Run periodic reports to check for duplicate payments. This report should be coded to flag for duplicate invoice numbers across multiple vendors.</p>	<p>Agree – The Finance Department processes over 300,000 payments annually. Of the potential duplicate payments found by Internal Audit over a 3 year period, 7 were not duplicates, 2 are in the process of being resolved, and the rest were detected and resolved by Departmental and/or Finance staff before the audit. We will work with ITS staff to develop a report that detects payments of the same amount with the same invoice number for different vendors.</p>	<p>December 31, 2014.</p>
<p>A2. Provide additional training and guidance for invoice enterers on how to handle duplicate invoice number error codes within EnterpriseOne to prevent duplicate payments.</p>	<p>Agree – Additional guidance has been provided to the Accounts Payable staff.</p>	<p>Completed.</p>
<p>B1. Develop regular verification procedures to assure records are current and accurately reflect Metropolitan Nashville activity with its vendors.</p>	<p>Agree – There are valid business reasons for one vendor having multiple vendor numbers - for different locations and business lines, as examples. We will begin to more regularly run reports for vendor tax identification numbers that have not been issued payments for an extended period of time.</p>	<p>March 31, 2015.</p>
<p>B2. Simplify the current audit trail function to capture only prudent information to allow for the changes to be readily identifiable.</p>	<p>Partially Agree – There are strong mitigating controls in place to prevent unauthorized changes to the address book, and a review of all changes would not likely detect problems. We will work with ITS staff to develop a report that detects changes to the address book records that correlate to other records in EBS that should be flagged for further follow up.</p>	<p>December 31, 2014.</p>
<p>C. Ensure employees serving as active vendors are notified of Metropolitan Nashville Procurement Code disclosure requirements.</p>	<p>Agree – We will enhance our procedures to ensure that any additions of vendors who are current employees are approved by Purchasing after they review for possible violations of the procurement ethics code. Additionally, Purchasing will review the specific instances noted to determine whether further action is needed.</p>	<p>December 31, 2014.</p>

APPENDIX A – MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN

Recommendations	Concurrence and Corrective Action Plan	Proposed Completion Date
<p>F. Add an additional step in the vendor verification process to verify the vendor has a current and valid business license to be conducting business in the state of Tennessee or is exempt.</p>	<p>Agree – Purchasing will begin requiring copies of business licenses, where required, prior to issuing new contracts. Additionally, Purchasing will review the specific instances noted to determine whether further action is needed.</p>	<p>December 31, 2014.</p>
<p>G1. Reiterate to department heads that items that are under contract should be purchased from one of Metropolitan Nashville Government’s contracted firms through the iProcurement system.</p>	<p>Agree – The related portion of this audit report will be provided to all Department Heads for their consideration.</p>	<p>October 31, 2014.</p>
<p>G2. Reiterate to department heads and cardholders the importance of maintaining the proper supporting documentation for all credit card purchases.</p>	<p>Agree – The related portion of this audit report will be provided to all Department Heads for their consideration.</p>	<p>October 31, 2014.</p>
<p>G3. Reiterate to department heads that if exceptions to portions of the Credit Card Policy are needed, a request to the Finance Director for approval should be submitted.</p>	<p>Agree – The related portion of this audit report will be provided to all Department Heads for their consideration.</p>	<p>October 31, 2014.</p>
<p>Management of the General Services Department should:</p>		
<p>D. Reiterate to department heads that fuel card usage should be monitored by their departments.</p>	<p>Agree - General Services agrees to reiterate to department heads that fuel card usage should be monitored by their departments. Revised Office of Fleet Management Administrative Orders, to be issued on October 1, 2014, clearly state the responsibilities of Agency Fleet Coordinators, including detailed responsibilities for managing and monitoring the agency’s use of fuel keys and fuel cards.</p>	<p>October 1, 2014.</p>
<p>Management of the Police Department should:</p>		
<p>E2. Decide if a workload study will be beneficial to identify potential areas that may need to be addressed further related to prolonged overtime requirements.</p>	<p>Agree - This analysis, as it pertains to the Metropolitan Nashville Police Department, has been given, and will be given, all appropriate and due consideration.</p>	
<p>Management of Metro Water Services should:</p>		
<p>E2. Decide if a workload study will be beneficial to identify potential areas that may need to be addressed further related to prolonged overtime requirements.</p>	<p>Disagree – Metro Water Services tracks overtime and are well within accepted industry standards.</p>	

APPENDIX B – THE FIVE COMPONENTS OF INTERNAL CONTROL AND RELATED PRINCIPLES

Source: The Committee of Sponsoring Organizations of the Treadway Commission, *Internal Control – Integrated Framework (2013 Framework)*



APPENDIX C – TOP UNUSUAL VENDOR PAYMENTS

Vendor	Amount	Number of Transactions
Walmart	\$118,843.94	579
Amazon Mktplace Pmts	99,525.84	797
Carl Black Chevrolet	37,080.14	56
Kroger	30,375.54	467
Sir Speedy Church Street	7,153.10	19
Publix	5,646.70	82
Target	3,309.98	42
Hobby Lobby	2,284.44	16
Save a Lot	2,000.00	2
Dick's Sporting	1,409.65	8
Shell Oil	1,364.36	36
Mapco Express	826.87	18
Big Lots	789.20	9
Petsmart Inc	685.08	8
Dollar General	596.71	14
Toys r Us	471.09	3
Chevron	341.67	8
Bed Bath Beyond	338.95	4
Spirit Halloween c	225.98	1
Z Mart	223.71	5
Dollar Tree Comm	213.84	1
Trader Joe's	197.89	3
Fat Brain Toys	138.39	1
Nashville Pet Products	136.91	2
Belk	130.00	2
Shell Oil qps	114.48	2
Halloween Costumes	107.97	1
Family Golf Center	92.00	1
T J Maxx	74.88	1
Classy Clips Pet Salon	43.29	1
Family Dollar	34.62	2

Vendors were selected by auditor as unusual. Data from EBS for January 1, 2012 through April 30, 2014