Vendor Master File Audit

ASSURANCE • INSIGHT • OBJECTIVITY

Final Report
Audit Plan Code: 20-10

We identified seven employees with improper access to the Vendor Master File (VMF). We also noted instances where the controls to manage the VMF were not present or did not function as intended.

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Abbreviations

AP	Accounts Payable
CAP	Corrective Action Plan
EPISD	El Paso Independent School District
FASRG	Financial Accountability System Resource Guide
IIA	Institute of Internal Auditors
IRS	Internal Revenue Service
IT	Information Technology
SAM	System for Award Management
SFO	School Funds Online
SOP	Standard Operating Procedures
TEA	Texas Education Agency
TIN	Tax Identification Number
VMF	Vendor Master File

We have completed the audit of the Vendor Master File (VMF). The objectives of the audit were to:

1. Determine whether sufficient controls exist for the management of the VMF and if controls are operating effectively.

2. Determine if security roles of individuals who have access to modify the VMF are aligned to their job descriptions and if proper segregation of duties exist.

The Executive Summary provides, on a summarized basis, the findings discussed throughout the body of the detailed Internal Audit Report that follows. The Internal Audit Report includes background information and detailed findings, recommendations, and observations.

Summary of Results

We would like to acknowledge the following positive results:

- We did not identify any exceptions when we evaluated a sample of 28 vendors with activity above $50K, from July 1, 2019, to February 25, 2020, to determine whether there was a bid/co-op for each vendor.

- We selected a sample of 45 vendors with PO Boxes and verified the existence of 44; the last vendor had been acquired by another company.

The summaries of the audit findings and observations are as follows.

1. We identified seven employees (within and outside of Procurement) who have improper access to the VMF. Improper access to the VMF creates a risk that access is used intentionally or accidentally to make inappropriate changes to vendor information. This may create issues with segregation of duties where there is no oversight or where errors are not prevented or detected and corrected timely. Procurement does not have a process in place to periodically evaluate the access level by role/position to the VMF.

2. As of February 25, 2020, we noted 35.8% of the vendors in the VMF had not been used in more than two years, and 30.5% had no activity in Frontline or School Funds Online (SFO). Also, the remaining vendors that had activity in the last 24 months had instances of duplicates or data integrity issues such as missing or incorrect information. Having these issues can increase (i) the risk of not identifying fictitious vendors, (ii) the risk of making incorrect payments to vendors, (iii) the time spent by employees to process accurate Forms 1099-MISC Miscellaneous Income (Forms 1099), and (iv) the risk of reporting incorrect expenditures by vendor.

3. Some vendors were <u>added</u> to the VMF without the required forms, incompletely, or inaccurately. If a vendor is missing the required forms, there is no evidence the vendor was created legitimately or that the external verification was performed. Incomplete or inaccurate information might cause issues such as checks delivered to incorrect addresses, or Forms 1099 issued to incorrect Tax Identification Numbers (TIN).

4. Some <u>changes</u> to the VMF did not have appropriate supporting documentation in Frontline or were not entered accurately or completely. We found no evidence that changes are reviewed or that vendors were contacted to verify the legitimacy of the change requests. This is a potential weakness in the process as it could lead to fraudulent changes being taken as legitimate requests and cause payments to be redirected to incorrect remit-to addresses. In addition, there is no audit change log in Frontline to help research and detect unauthorized or fraudulent modifications to the VMF.

5. We identified one vendor that is not part of the VMF. Having vendors that are not part of the VMF increases the risk of (i) understating expenditures and revenues, (ii) not filing all the Forms 1099 that should be filed according to the IRS guidelines, or (iii) failing to comply with regulations such as CHE(Local) or section 22.0834 of the Texas Education Code.

6. Campuses issued checks to 25 vendors with holds through SFO in the 12-month period tested, as the interface between Frontline and SFO does not transfer the holds. Therefore, the campuses could be using vendors identified as having issues or being out of compliance.

We also identified four observations as follows.

1. On April 13, 2020, 5,314 vendors were inactivated without inactivating the company. Using the Frontline testing environment, Internal Audit verified that by not inactivating the company, a vendor can be added to an active company without requiring approval. In addition, we noted 31 vendors that were inactivated in Frontline were used on SFO after the inactivation.

2. The W9 in the vendor packet and online is outdated. New vendors should fill out the most current version of the W9 form because the information requested has changed.

3. Vendors added as part of lawsuit settlements (one-time vendors) or garnishment of wages have different supporting documentation than the standard forms. Neither the Procurement Manual nor the New Vendor Set Up Procedures provides information on the documentation required for adding these types of vendors and when to inactivate them. Lack of documented procedures might lead to (i) inadequate retention of forms that contain important information to support the purpose of adding the vendor and (ii) the accumulation of one-time vendors.

4. Written notifications of bad performance have not been sent to vendors that received an unsatisfactory vendor performance form as outlined in the Procurement Manual. Not sending notifications to the vendors will enable problems with vendors to continue uncorrected.

Management's Corrective Action Plan

District management and leadership submitted a Corrective Action Plan (CAP) outlining 17 activities to be implemented. All 14 recommendations made by Internal Audit were incorporated into the CAP. The CAP appears to be sufficient to address the findings and observations outlined in this report. Internal Audit will conduct follow-up reviews to validate CAP activities have been implemented.

Conclusion

We identified seven employees who have improper security roles, which include having the ability to modify the VMF. The employees' access may be incompatible with proper segregation of duties. We also noted issues that indicate some of the controls to manage the VMF were not present or did not function as intended. Such issues include (i) absence of an audit change log, (ii) vendors with incomplete or inaccurate data, (iii) vendors with missing supporting documentation in Frontline, (iv) vendors listed as active without activity, (v) duplicate vendors, and (vi) vendors with holds transferred to SFO as active.

Recommendations have been made in this report in an effort to assist Procurement to strengthen controls and access related to the management of the VMF. We recommend Procurement implements such recommendations and document them in their operating procedures to (i) reduce the risk of making incorrect payments to vendors and reporting incorrect expenditures by vendor, and (ii) improve tracking and monitoring of vendors and their data in Frontline.

Background

The Vendor Master File (VMF) is an essential part of the District's process of acquiring and paying for goods and services. The VMF includes information about vendors such as name, address (remit-to, order from), Tax Identification Number (TIN), contact, etc.

The Procurement and School Resources Department (Procurement) maintains the VMF. The Purchasing Specialist and an assigned Buyer, within Procurement, are involved in the process of adding new vendors and making changes to vendor information in the VMF. The VMF from Frontline had a total of 7,934 vendors as of February 14, 2020.

The District uses the data in the VMF to purchase goods and services from vendors through the ERP system Frontline. The Executive Director of Procurement estimates that about $200 million flow annually through the department. Also, campuses use the data in the VMF to issue checks to vendors through School Funds Online (SFO) using campus and student funds. For FY 2019-2020 (as of February 25, 2020), campuses had spent approximately $2,838,177 on campus and student funds.

The Board of Trustees approved the audit of the VMF as part of the 2019-2020 Internal Audit Plan.

Objective and Scope

The objectives of the audit were to:

1. Determine whether sufficient controls exist for the management of the VMF and if controls are operating effectively.

2. Determine if security roles of individuals who have access to modify the VMF are aligned to their job descriptions and if proper segregation of duties exist.

The audit scope included all vendors in the VMF as of and for the twelve-month period ended February 14, 2020, and security roles related to the VMF as of February 14, 2020.

Methodology

To achieve our audit objectives, we:

- Researched relevant federal/state laws and regulations, Board policies, and the Procurement and Campus Accounting manuals.

- Used pre-audit and internal control questionnaires and conducted meetings with Procurement, Information Technology (IT), Campus Accounting, Treasury, and Accounts Payable (AP).

- Performed a risk assessment based on our understanding of the VMF management process and controls in place.

- Performed walkthroughs to obtain an understanding of the processes that affect the VMF.

- Contacted vendors via email, instant message, or phone call. We also performed inquiry with a consulting firm that specializes in the System for Award Management (SAM) registration.

- Performed data analysis (analytical procedures) using different sets of vendor data.

- Selected random samples based on our sampling procedures, which were used in several procedures to perform tests of details.

Inherent Limitations

Because of the inherent limitations in a system of internal controls, there is a risk that errors or irregularities occurred and were not detected. Due professional care requires the internal auditor to conduct examinations and verifications to a reasonable extent. Accordingly, an auditor is able to obtain reasonable, but not absolute, assurance that procedures and internal controls are followed and adhered to in accordance with the federal, state, local policies, and guidelines.

The extent of our testing during the audit, as it pertains to modifications to the VMF, was limited given Frontline, the ERP system, does not maintain a log of all changes made to the VMF.

Acknowledgement

We would like to acknowledge and thank the staff in Procurement, Information Technology, Accounts Payable, Campus Accounting, and Treasury for their cooperation and assistance during the audit.

Results

We would like to acknowledge the following positive results.

- We did not identify any exceptions when we evaluated a sample of 28 vendors with activity above $50K, from July 1, 2019, to February 25, 2020, to determine whether there was a bid/co-op for each vendor.

- We selected a sample of 45 vendors with PO Boxes and verified the existence of 44; the last vendor had been acquired by another company.

Our testing procedures indicated that in some instances, controls within the vendor addition and change processes were missing or not operating effectively, and that some employees have improper access to the VMF. These instances are explained in detail in Findings 1 through 6.

Finding 1

We identified employees (within and outside of Procurement) who have improper access to the VMF. Improper access to the VMF creates a risk that access is used intentionally or accidentally to make inappropriate changes to vendor information. It can create issues with segregation of duties where there is no oversight or where errors are not prevented or detected and corrected timely. Procurement does not have a process in place to periodically evaluate the access level by role/position to the VMF.

1.1 Two Procurement employees can create vendors that are automatically approved. This level of access does not require approval of the vendor by another employee. Thus, it circumvents the review process, which is used as a safeguard to prevent errors or fraudulent vendors from being input to the VMF.

1.2 A third Procurement employee has the same Frontline security roles as the two employees referenced in 1.1, but in his/her case, the vendors are not automatically approved. IT could not ascertain what caused the difference in access, but they suggested the difference could be due to a workflow setting.

1.3 Five employees in the Financial Services Department can modify the vendor name, tax ID, and tax address. These fields are both essential and sensitive; access to these fields should be reserved for personnel responsible for maintaining the VMF.

1.4 Two of those five employees in the Financial Services Department can request vendors online. When a vendor is requested, a vendor is created, but it still must go through the approval process in Frontline. However, all vendors created are transferred to SFO and can be issued checks in SFO, even though they may not yet be approved.

1.5 Three of the five employees mentioned in 1.3 are also able to change the remit-to name and delete remit-to addresses. The three employees work in the AP unit of the Financial Services Department and may have security roles that are incompatible with proper segregation of duties. Those employees are able to process payments, change the name of the check recipient, and delete the address. As mentioned in Finding 4, changes are not subject to review. Therefore, inappropriate changes made by these employees might go undetected.

1.6 Two of the five employees from the Financial Services Department can inactivate vendors and add and remove holds. Unintended modification of

these fields might cause changes that might result in additional work for Procurement. For instance, inadvertent inactivations might lead to having to add new vendors or accidental removal of holds might lead to activity with vendors that have issues.

Finding 2

We identified vendors (i) that have not conducted business with the District (inactive) in two (2) to 15 years, (ii) without activity, (iii) that are duplicates, and (iv) with data integrity issues within the VMF. Having an unclean VMF can increase (i) the risk of not identifying fictitious vendors, (ii) the risk of making incorrect payments to vendors, (iii) the time spent by employees to process accurate Forms 1099, and (iv) the risk of reporting incorrect expenditures by vendor. Procurement does not have a process in place to "clean up" the VMF on a periodic basis.

2.1 <u>Inactive Vendors</u>

    2.1.1 As of February 25, 2020, 35.8% (2,839 of 7,934) of the vendors in the VMF had not conducted business with the District for more than two years. In addition, 30.5% (2,418 of 7,934) of the vendors had no activity recorded in Frontline or School Funds Online (SFO). Many of those vendors were transferred from the previous system (AS400) to Frontline (previously TEAMS) and were not used after the system implementation. See Chart 1 below for a depiction of the vendors in the VMF by last month of use.

Chart 1. Vendors by Last Month of Activity
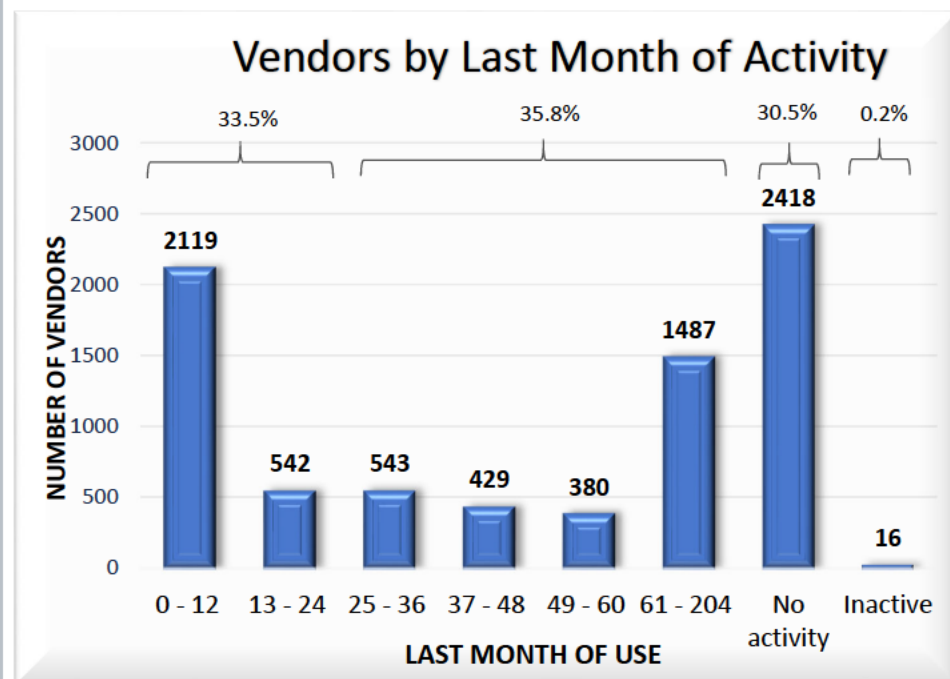
    2.1.2 Although there is no set criteria among standard-setting groups or in the Procurement Manual for when a vendor should be inactivated, best practice suggests inactivating vendors not used in 18 to 24 months. Per

discussion with the Executive Director of Procurement, a 24-month threshold could be used to inactivate vendors.

2.2 Duplicate Vendors

2.2.2 Out of the 2,661 vendors with activity in the last 24 months, we identified 226 active vendors (8.5%) that have the same TIN, vendor name, contact email, remit-to address, order-from address, or phone number of at least another vendor. Duplicate vendors increase the possibility of incorrect totals per vendor and the risk of making duplicate payments.

Inaccurate totals per vendor may lead to a vendor not receiving the Form 1099 because it appears not to meet the $600 threshold as actual total transactions are spread across different "vendors." In addition, Procurement may not be able to identify purchases above $50K from vendors that are not in a bid, cooperative, etc.

2.2.3 We noted that duplicate vendor records have been created due to the following:

a.   There is no standard naming convention. For instance, the VMF contains a vendor by the name of TASSP and a vendor by the name of Texas Association of Secondary School Principals. Both of them are the same institution.

b.   Requests for new vendors are not tracked. This has led to duplicate vendors that have been added to the VMF within a relatively short period of time. For instance, vendor Sun City Shredding was added twice to the VMF within 13 business days, and vendor Shyanne Damonique Murgoia was added twice within eight (8) business days. Although the duplicate records for the two vendors have not been approved (status is "Approval in Progress"), the duplicates have transferred to SFO and can be used by campuses.

c.   The Purchasing Specialist was not searching for possible duplicates using the TIN when adding a vendor to the VMF; s/he was searching only by name.

2.2.4 Neither the Procurement Manual nor the New Vendor Set Up Procedures have guidelines or a checklist of all the steps to perform prior to creating a vendor, such as searching for duplicates by the TIN and by the vendor name, in different ways.

2.3 Data Integrity

2.3.2 We performed analytical procedures over the 2,661 vendors (33.5%) used in the last 24 months (see Chart 1) to identify vendors with missing, incomplete, or incorrect information on file. According to the Procurement Manual, Procurement will "provide a complete and functional list of approved vendors." We noted the following:

a.   Two (2) vendors (0.1%) with zip codes with four digits.

b.   Ten (10) active vendors (0.4%) with no remit-to address. Four vendors are from EPISD, and the remaining six are other entities.

c. Four (4) vendors (0.2%) with Tax ID numbers with eight (8) digits. Every TIN, social security number (SSN), and employer identification number (EIN) should be nine (9) digits long.

d. Six (6) vendors (0.2%) who have TINs that don't seem to be legitimate due to the sequence of digits used (e.g., 999999999).

e. Ninety (90) vendors (3.4%) with no tax ID.

2.3.3 Information that is incomplete or inaccurate may cause issues such as delays due to incorrect information printed on purchase orders, problems sending payment to the incorrect addresses, and issuing Forms 1099 that are inaccurate.

2.3.4 Of those 90 vendors without a TIN, 70 appear to be tax-exempt entities such as public schools, public universities, colleges, and other governmental institutions. Although Forms 1099 are not issued to government agencies or other schools, per inquiry with the AP Manager, all vendors should have a TIN if only to have complete vendor information.

2.3.5 The VMF contains incorrect TINs. In October 2019 and October 2018, the Internal Revenue Service (IRS) sent CP-2100A Notices to the District related to the 2018 and 2017 tax years reporting the following issues:

a. Two (2) TINs reported on Forms 1099 had not been issued by the IRS.

b. Ten (10) Forms 1099, issued by the District, had names or TINs that did not match the IRS records.

As of June 15, 2020, the District had not received a CP-2100A Notice for the 2019 tax year.

2.3.6 We identified three causes of incomplete or inaccurate data.

a. The TIN field in Frontline is not a required field and does not include validation rules. As such, Frontline allows TINs that are null or that have less than nine digits or alphanumeric characters.

b. Addresses are not required fields either, and zip codes with less than five digits are allowed by Frontline.

c. It appears that the current review process is not functioning as intended as it has allowed incomplete information to be recorded in the VMF. See Finding 3 for more details of the review process.

Finding 3

We noted instances where vendors were <u>added</u> to the VMF incompletely, inaccurately, or without the required forms. To create a vendor in Frontline, a Packet that includes four forms must be submitted to Procurement. The forms are (i) Vendor Request Form, (2) IRS Form W9 Request for Taxpayer Identification and Certification, (iii) Contractor Certification form, and (iv) Conflict of Interest Questionnaire (CIQ). In addition to those forms, Procurement attaches to Frontline

IRS and SAM verification printouts. However, neither the Procurement Manual nor the New Vendor Set Up Procedures provides the specific steps on how to review vendor data for completeness/accuracy and the required retention of vendor forms.

In the period between February 15, 2019, and February 14, 2020, 311 new vendors were added to the VMF. We inspected a sample of 60 vendors to verify whether supporting documentation to create a vendor was in Frontline, and vendor data entered in the VMF was complete and accurate. We noted the following (results are summarized in Table 1):

Table 1. Results of Procedure Performed over New Vendors

	Original Results - # of Forms Missing or with Exception	Subsequently Provided - per Request	Total Forms Missing or with Exception	%
Incomplete Packet	51	33	18	30.0%
Vendor Request Form Not Retained	50	37	13	21.7%
W9 Not Retained	4	2	2	3.3%
CIQ Not Retained	15	5	10	16.7%
Contractor Certification Not Retained	15	3	12	20.0%
Missing All Packet	1	-	1	1.7%
Forms Retained Not Properly Filled Out	27	N/A	27	45.0%
Not Entered Complete/Accurate	20	N/A	20	33.3%
Lack Evidence Review	49	N/A	49	81.7%
IRS Verification Not Retained	9	N/A	9	15.0%
SAM Verification Not in Frontline	50	N/A	50	83.3%

3.1 One (1.7%) vendor was added to the VMF without a Packet. The forms in the Packet are necessary to obtain all the relevant information to create the vendor. The forms must be filled out and signed by the vendors as evidence that the information provided is correct. According to Procurement, the Packet is reviewed and attached to Frontline. If a vendor is missing all documents on Frontline, there is no evidence that the vendor was created legitimately.

3.2 Fifty-one (85.0%) vendors were missing one or more of the required forms in Frontline. Procurement provided additional documents not originally in Frontline after our request. The documents are needed for reasons described in 3.2.1 through 3.2.4.

   3.2.1 The Vendor Request Form provides the physical and remit-to addresses, which might be different from the address on the W9.

   3.2.2 The W9 is required as it provides the TIN, tax classification, and tax return name. This information is necessary to identify whether the funds paid to the vendor must be reported to the IRS and to verify the legitimacy of the vendor by searching for the TIN and the tax return name in the IRS database. Also, if the TIN is not provided, the District might need to withhold tax (i.e., backup withholding) from the payments to the vendor.

   3.2.3 The Local Government Code, Section 176.006, indicates that a Conflict of Interest Questionnaire is required for "a person who is both a local government officer and a vendor of a local governmental entity [… who] enters or seeks to enter into a contract" with the District. In addition, CHE(Local) and the Procurement Manual indicate that "Every

individual or entity who contracts or seeks to contract with the District […] shall file a completed conflict of interest questionnaire."

    3.2.4 Section 22.0834 of the Texas Education Code requires that the District obtains a certification from its contractors regarding their criminal history. This was instituted to keep students safe. Currently, the District meets this requirement by obtaining the Contractor Certification form when a new vendor is added.

3.3 Vendor data information entered in Frontline was incomplete or inaccurate for 20 (33.3%) vendors. Some inaccuracies may stem from not verifying illegible information or abbreviations.

    3.3.1 To maintain a vendor list that is "complete and functional," vendor information must be entered in Frontline completely and accurately.

    3.3.2 Incomplete or inaccurate data can create problems when searching for a vendor (i.e., the vendor name is wrong) that could lead to creating duplicate vendors.

    3.3.3 Other issues due to incomplete or inaccurate vendor data include, but are not limited to, delivering checks to incorrect addresses, issues with vendors who receive payments late, returned checks, etc.

3.4 There was no evidence of review documented for 49 (81.7%) vendors. Furthermore, there are discrepancies between the process documented on the Procurement Manual and the current practice as it pertains to vendor review. Currently, the Procurement Manual indicates that the "Executive Director of Procurement Services will […] review the vendor setup for completeness and approve or deny the new vendor." However, the review of the vendor setup is generally performed by a Buyer.

3.5 The IRS verification was not performed or retained for 9 (15.0%) vendors. The IRS verification is necessary to confirm that the TIN provided by the vendor belongs to them. There was no evidence that the SAM verification was performed for 50 (83.3%) of the vendors. The SAM verification is necessary to ensure that federal funds are not disbursed to vendors who are not eligible for them. The District relies on these two verifications to validate the legitimacy of vendors added to the VMF. If the appropriate documents are not attached to Frontline, there is no evidence that the verification was performed.

3.6 The Procurement Manual refers to three other forms needed to add a vendor that are not used in current practice: Vendor Acknowledgement Form, Purchasing Checklist Category Form, and the Suspension and Debarment Form. However, it does not list the "Contractor Verification" as a form that new vendors must fill out. Also, the "Vendor Request Form" is listed as "New Vendor Form" in the Procurement Manual. These discrepancies between the Procurement Manual and current practice may cause confusion as to what is necessary to become a vendor or what must be retained and attached to Frontline.

Finding 4

We noted requests for <u>changes</u> to vendor information in the VMF that (i) did not have appropriate supporting documentation in Frontline, (ii) had not been entered, or (iii) were requests to fix a prior change that had been entered incorrectly. We performed different procedures over changes to the VMF. The combined results are summarized in Table 2.

Table 2. Results on Testing over Changes

Condition	Average Results in %
Support not retained on Frontline	50.4%
Change input inaccurate	27.0%
No change entered	20.0%
Support does not include evidence from vendor	16.9%
Request to fix prior data entry	14.3%
Change input incomplete	8.6%

After requesting support for the changes that did not have it, Procurement provided support for some changes. Those pieces of support are not reflected on the table.

4.1 The Purchasing Specialist is responsible for making the changes in Frontline and uploading supporting documentation for the change. Changes to vendor information are not reviewed or approved by another person.

4.2 We found no evidence that the current process to make changes involves reaching out directly to vendors to confirm the change or performing any verification. This is a potential weakness in the process as it could lead to fraudulent changes being taken as legitimate requests and cause payments to be redirected to incorrect remit-to addresses.

    4.2.1 Contacting vendors is particularly important because the majority of change requests (97.1% according to one of our procedures) are sent to Procurement by other EPISD departments. Without confirming the change requests with the vendors, the District could be subject not only to external, but also internal attempts to deviate payments.

    4.2.2 Also, obtaining written support from the vendor for every change is essential to verify that only legitimate information is entered in the VMF as well as to minimize the opportunity to enter errors. For example, a Vendor Request Form that AP sent to Procurement incorrectly listed the new remit-to address as 5753 Hwy 83 N instead of the correct address of 5753 Hwy 85 N (i.e., typo). These errors can be minimized by obtaining the updated information directly from documents provided by the vendor.

4.3 There is no audit log in Frontline of changes made (i.e., modifications) to the VMF. A change audit log is an essential tool for identifying modifications made to a vendor, including when, and by whom. It also helps research and detect unauthorized or fraudulent modifications to the VMF. The change log, in the District's case, is especially important because there is no review or approval performed for changes to the VMF.

    4.3.1 For example, one of our procedures identified three vendors that show the same addresses as two Procurement employees that routinely

modify the VMF in the "tax address line 2" field. The employees indicated that they are not associated with the vendors and do not know why their addresses are part of the vendors' information. We observed one of the employees entering a new vendor and noted that his/her address popped up. Although it appears that the employees' addresses might have been entered when the vendors were created, we were unable to corroborate that hypothesis due to the lack of a change log.

4.3.2   The current settings on Frontline record the time stamp (date and time) and the user who entered the last modification for limited information (in the Company tab). However, this information is overwritten each time there is a change, and Frontline does not indicate what fields were changed. In other words, an unauthorized modification could be entered and used, and then the change could be overwritten by entering once again the legitimate information. In such a case, Frontline would not provide any information on the unauthorized modification, and the change could go undetected.

4.3.3   Frontline does not track any changes for other information, including the remit-to address section. Inappropriate changes to the remit-to address present a risk to the District as resources could be deviated.

Finding 5

We identified one vendor that is not part of the VMF: Auctions Unlimited. This vendor receives District funds in a way that does not follow the traditional procurement process. Auctions Unlimited receives a 10.0% fee on the proceeds from the auctions. As such, it has not been captured in the VMF.

Having vendors that are not part of the VMF increases the risk of understating expenditures and revenues, as well as the risk of not filing all the Forms 1099 that should be filed according to the IRS guidelines. Finally, if vendors are not added to the VMF, Procurement cannot ensure all documents required (Packet) are collected and reviewed. Procurement does not have the Packet for Auctions Unlimited. As such, there is no CIQ on file, and the District cannot determine compliance with the conflict of interest requirements outlined in CHE(LOCAL).

Finding 6

We identified 25 vendors with holds in Frontline that were used by campuses through SFO. We tested all vendors used in the last 24 months that have holds for requisitions and holds for payments. Our testing indicates that about $172,011 was disbursed to the 25 vendors in the period between February 14, 2019, and February 25, 2020. Vendor Sam's Club Direct accounts for 81.9% ($140,939) of the total amount. That amount includes both campus and student activity funds disbursed.

According to IT, the nightly interface between Frontline and SFO does not transfer the holds. According to Campus Accounting, entering manual holds to SFO would be impractical as they would be overwritten by the interface each night. As such, any vendor that is on the VMF, with or without holds, is transferred to SFO and is available for issuing checks.

Frontline holds are added to prevent the acquisition of goods and services and/or payment to certain vendors that have issues. The campuses could be using vendors identified as having issues. See the summary of the hold reasons for the 25 vendors in Table 3.

Table 3. Summary of Hold Reasons

Summary of Hold Reasons		
Vendor Not On Bid/Contract	7	28%
Inactive, Use other vendor	4	16%
Pending Review	3	12%
Unapproved Vendor	2	8%
User Other Vendor	2	8%
Does Not Accept Purchase Orders	2	8%
Debit Card Use Only Vendor	2	8%
Out of Business	1	4%
Missing CIQ	1	4%
Failure to supply HB1295	1	4%
Total	25	100%

Observations

While conducting this audit, some observations were made that were outside of our original scope and objectives. These observations do not violate local, state, or federal guidelines, and as such, were not included as findings in the Vendor Master File Audit Report. However, we felt the items noted or observed were worthy of informing you as the data owner/expert, in order for you to make the determination as to whether they should be addressed.

Observation 1

On April 13, 2020, 5,314 vendors were inactivated without inactivating the company (in Frontline, a company is like an "umbrella" that contains the vendors and can have multiple vendors). Using the Frontline testing environment, Internal Audit verified that by not inactivating the company, a vendor can be added to an active company without requiring approval. In addition, we noted that 31 vendors that were inactivated in Frontline were used on SFO after the inactivation.

Observation 2

The W9 in the Packet (including the W9 listed on the EPISD website) is the 2014 version, which is outdated. The most current version of the W9 was issued in October 2018. Although W9s received from vendors do not expire, new vendors should fill out the most current version of the W9 form because the information requested on the form has changed.

Observation 3

We noted that vendors added as part of lawsuit settlements (one-time vendors) or garnishment of wages have different supporting documentation than the one in the Packet, and in some instances, the documentation is not in Frontline. The Procurement Manual does not provide information on the documentation required for adding these types of vendors and when to inactivate them. Lack of documented procedures might lead to (i) inadequate retention of forms that contain important information to support the purpose of adding the vendor and (ii) accumulation of one-time vendors.

Observation 4

According to the Buyer and Purchasing Specialist involved in maintaining the VMF, they have not sent written notifications of bad performance to vendors that received an unsatisfactory vendor performance form. The Procurement Manual states that "The vendor will be sent a written notification from the Procurement Services Department stating the problem, the corrective action required and that the vendor's failure to correct the problem could result in a loss of future business with the district." Not sending notifications to the vendor will enable the problems to continue uncorrected.

Recommendations and Management Response

A CAP outlining 17 activities to be implemented and signed by District management and leadership was submitted to Internal Audit. All 14 recommendations made by Internal Audit were incorporated into the CAP. The CAP appears to be sufficient to address the findings and observations outlined in this report.

1

We recommend Procurement develops a process to evaluate the access level by role/position to the VMF. Procurement should ensure proper segregation of duties and controls are considered during the evaluation. Along with department heads, Procurement should determine if the access aligns to the employee's job responsibilities, and request access changes if necessary. If access is not necessary to perform the employee's job responsibilities, the access should be removed.

Management and Leadership Response: Agreed with our recommendation and incorporated into the CAP as activities one (1) and 17.

Person(s) Responsible: Executive Director of Procurement & School Resources, Executive Director of Financial Services, and Chief Information Officer.

Implementation Dates: 11/30/2020; 6/30/2021

2

We recommend Procurement works with IT to revise the access security role that allows the two employees in Procurement to enter a vendor and approve it automatically. This will assist in establishing segregation of duties where the person entering a vendor is not approving it.

Management and Leadership Response: Agreed with our recommendation and incorporated into the CAP as activity two (2).

Person(s) Responsible: Executive Director of Procurement & School Resources and Chief Information Officer.

Implementation Date: 11/30/2020

3

We recommend that Procurement performs a periodic cleanup of the VMF. The cleanup process should include consolidating and inactivating duplicate vendors, reviewing whether the active vendors' information in Frontline is current and accurate, filling-in missing information, obtaining and uploading missing documents, and resolving issues causing holds. Procurement could involve other stakeholders such as Accounts Payable to determine the extent (all vendors or only certain vendors) of the cleanup.

There are several risk factors Procurement could consider in prioritizing the order to clean vendor data in the VMF, such as:
- Vendors with issues documented in the CP-2100A IRS notices,
- Vendors with duplicates,
- Vendors with holds,
- Vendors with incomplete information,
- Vendors who share TIN, email, address or phone number with current employees,
- Vendors with missing documents, and
- Vendors with PO Boxes as remit-to addresses,

To aid in the process of identifying vendors missing attachments, Procurement could work with IT to create a query that pulls only the vendors used in the last 24 months that do not have attachments.

The cleanup process should be clearly documented in the operating procedures or the Procurement Manual.

Management and Leadership Response: Agreed with our recommendation and incorporated into the CAP as activities three (3) and 17.

Person(s) Responsible: Executive Director of Procurement & School Resources and Chief Information Officer.

Implementation Dates: 05/31/2021; 6/30/2021

4

To facilitate the search of vendors on Frontline and reduce the number of duplicates created, we recommend Procurement institutes the use of a naming convention. The naming convention could cover guidance on using:
- Acronyms as the vendor name (IRS or Internal Revenue Service)
- Commas and periods in the name (Vendor Co, Inc. or Vendor Co Inc)
- Ampersands or "and" in vendor name (Vendor & Vendor or Vendor and Vendor)
- Spaces between initials (A B C Vendor or ABC Vendor)
- Abbreviations for states or the United States (Texas Landscaping or TX Landscaping)
- Names of natural persons (Daniel David Martinez Mc Adams; Daniel D Martinez McAdams; Daniel D. Martinez; Daniel Martinez; Martinez, Daniel D; McAdams, Daniel)
- Abbreviations for cardinal directions (Southwest Vendor or SW Vendor)
- Articles such as "a," "an" and "the" (The Vendor or Vendor)
- Salutations or professional credentials (*Mrs*. Daniella Martinez, *MD*; Daniella Martinez *M D*; Daniella Martinez*, MD*; etc.)
- Numbers (1 or one) and using ordinal numbers (1st or First).
- Apostrophes (I'm O'Hara Vendor or Im OHara Vendor)
- Special characters (such as dashes "-," at symbols "@," number symbols "#")
- Abbreviations for other words such as Board, Association, Business, Center, Corporation, National, American, Street, Road, etc. (American Association, Am Assoc or Am. Assoc.)

The naming convention should be documented in the New Vendor Set Up Procedures or the Procurement Manual.

Management and Leadership Response: Agreed with our recommendation and incorporated into the CAP as activities four (4) and 17.

Person(s) Responsible: Executive Director of Procurement & School Resources

Implementation Dates: 11/30/2020; 6/30/2021

5

We recommend Procurement updates and expands upon the written operating procedures for adding, changing, and inactivating vendors. The updated procedures should cover the following:

- Adding a New Vendor
  - Searching for duplicates.

- o Using a naming convention. See Recommendation 4.
- o Handling vendors disbarred in SAM.
- o Rejecting a vendor.
- o Selecting whether a vendor is subject to 1099-MISC and/or backup withholding.
- o Handling vendors that require supporting documentation different from the Packet, such as vendors for garnishment of wages, lawsuits settlements, etc.
- o Reviewing the Packet for completeness.
- o Reviewing the new vendor and verifying that the supporting documentation was attached to Frontline.

- Changing Vendor Information
  - o Validating a request to change vendor information. See Recommendation 7.
  - o Determining when it is appropriate to create a new vendor instead of changing the information of an existing vendor and what documents must be obtained (e.g., a TIN change request results in a new vendor instead of an update.)
  - o Reactivating vendors.
  - o Adding or removing holds.

- Inactivating vendors
  - o Handling one-time vendors (e.g., employee settlements).
  - o Handling vendors created for garnishment of wages.
  - o Inactivating duplicate vendors that have not been approved within a period of time.

These operating procedures can also be used for training new and back-up employees.

We recommend Procurement implements a checklist delineating the steps to perform to add a new vendor so that no steps are missed. The checklist should include review of the documents in the new vendor packet.

Also, we recommend Procurement institutes a tracking mechanism so that requests to add vendors and requests for changes are not missed or entered twice (in the case of adding vendors).

Management and Leadership Response: Agreed with our recommendation and incorporated into the CAP as activities five (5) and 17.

Person(s) Responsible: Executive Director of Procurement & School Resources

Implementation Dates: 05/31/2021; 6/30/2021

6

We recommend Procurement updates the Procurement Manual to reflect current practices for adding new vendors to the VMF. The updated procedures should clearly identify the position that will have the responsibility of reviewing and approving new vendors and the documents required as part of the new vendor packet.

Management and Leadership Response: Agreed with our recommendation and incorporated into the CAP as activities six (6) and 17.

Person(s) Responsible: Executive Director of Procurement & School Resources

Implementation Dates: 05/31/2021; 6/30/2021

7

We recommend that additional verification steps are implemented prior to <u>adding</u> a vendor to ensure that the vendor is legitimate.

We recommend Procurement implements a validation process to follow prior to making a <u>change</u> in vendor information. Direct communication with the vendor will not only serve as a confirmation to Procurement that the change request is legitimate, and the new information is correct, but it will also serve as a notification to the vendor that the change has been made.

Management and Leadership Response: Agreed with our recommendation and incorporated into the CAP as activities seven (7) and 17.

Person(s) Responsible: Executive Director of Procurement & School Resources

Implementation Dates: 05/31/2021; 6/30/2021

8

We recommend Procurement works with IT to set up a change log for the VMF. The change log should include, at a minimum, the following fields:
- Date and time of the change,
- Related Vendor ID and Company ID,
- Modified by (the user who made the change),
- Name of the field changed,
- Old value, and
- New value.

Given that there are no controls associated with changes to the VMF, a review process over the change log could be used as a mitigating control. The control could consist of periodically inspecting the change log to verify that all changes have appropriate supporting documentation from the vendor attached to Frontline (i.e., the legitimacy of change), and the changes were made accurately and completely. The review control should be assigned to an employee who is not involved in making the changes. This process should be clearly documented in the operating procedures or the Procurement Manual.

Management and Leadership Response: Agreed with our recommendation and incorporated into the CAP as activities eight (8), nine (9), and 17.

Person(s) Responsible: Executive Director of Procurement & School Resources and Chief Information Officer.

Implementation Dates: 05/31/2021; 6/30/2021

9

We recommend Procurement obtain the required documents (Packet) to add Auctions Unlimited to the VMF. In addition, Procurement should consult with Accounts Payable to determine if this vendor should be issued a 1099.

We also recommend Procurement determines whether (i) there are other vendors who do not follow the traditional procurement process, (ii) those vendors need to be added to the VMF, and (iii) they require a 1099. In addition, Procurement in consultation with Financial Services shall determine the documentation process for vendors who will not follow the traditional procurement process.

Management and Leadership Response: Agreed with our recommendation and incorporated into the CAP as activities 10, 11, and 17.

Person(s) Responsible: Executive Director of Procurement & School Resources, and Executive Director of Financial Services

Implementation Dates: 01/31/2021; 6/30/2021

10

We recommend Procurement works with IT to determine the best feasible solution to ensure vendors with holds or a status of "Approval in Progress" are not transferred from Frontline to School Funds Online (SFO).

Management and Leadership Response: Agreed with our recommendation and incorporated into the CAP as activity 12.

Person(s) Responsible: Executive Director of Procurement & School Resources, and Chief Information Officer

Implementation Date: 01/31/2021

11

We recommend Procurement performs an analysis to determine the pros and cons of inactivating vendors but not the companies. Other stakeholders, including Accounts Payable and Campus Accounting, should be involved in the process of conducting the analysis. If the decision is that inactivating vendors is not sufficient, we recommend Procurement and IT run a test to determine whether inactive companies can be issued checks on SFO, just like inactive vendors. If inactivating companies does not prevent vendors from being used on SFO, we recommend that Procurement and IT collaborate to find a feasible solution. If inactivating both vendors and companies produces the results desired, we recommend that Procurement works with Campus Accounting to determine whether the companies of the vendors inactivated on April 13, 2020, should be inactivated as well.

We also recommend Procurement works with IT and Campus Accounting to determine the feasibility of creating a computer script that will automatically inactivate the vendors/companies not used in 24 months while also retaining vendors used on SFO but not Frontline.

Management and Leadership Response: Agreed with our recommendation and incorporated into the CAP as activity 13.

Person(s) Responsible: Executive Director of Procurement & School Resources, Executive Director of Financial Services, and Chief Information Officer

Implementation Date: 01/31/2021

12

We recommend Procurement updates the IRS W9 form used to the most current IRS form in the Packet and online at https://www.episd.org/Domain/198.

In addition, we recommend Procurement periodically (e.g., twice a year) checks the W9 form on the IRS website to verify the Packet includes the most current version. The process should be documented in the operating procedures or the Procurement Manual.

Management and Leadership Response: Agreed with our recommendation and incorporated into the CAP as activities 14 and 17.

Person(s) Responsible: Executive Director of Procurement & School Resources

Implementation Dates: 09/30/2020; 6/30/2021

13   We recommend Procurement collaborates with other departments, such as Legal or AP, to establish an efficient process to manage one-time vendors added for special purposes (e.g., settlements). The process should establish (i) when to add one-time vendors, (ii) what supporting documentation should be collected, and (iii) when to inactivate the vendors. We recommend inactivating one-time vendors as soon as the vendor is paid. This prompt action will minimize the accumulation of one-time vendors and will reduce the possibility of unauthorized payments being issued. In the case of settlements, the Legal Department could provide the date the vendor should be inactivated.

Management and Leadership Response: Agreed with our recommendation and incorporated into the CAP as activities 15 and 17.

Person(s) Responsible: Executive Director of Procurement & School Resources, Executive Director of Financial Services, and General Counsel - Legal

Implementation Dates: 12/31/2020; 6/30/2021

14   We recommend Procurement enforces the requirement to send a written notification when a vendor has bad performance as outlined in the Procurement Manual. We also recommend Procurement promote that only vendors with outstanding service and ethical conduct are maintained as District vendors and encourage users to fill out vendor performance reviews. Otherwise, the District could be using vendors who under-deliver or who fail to meet responsibilities, etc.

Management and Leadership Response: Agreed with our recommendation and incorporated into the CAP as activity 16.

Person(s) Responsible: Executive Director of Procurement & School Resources

Implementation Date: 09/30/2020

EL PASO INDEPENDENT
SCHOOL DISTRICT