

# Vendor Management Process Review



**November 2020**

**City of Durham  
Audit Services Department  
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## **Staff**

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## **AUDIT SERVICES**

CITY OF DURHAM

**Date:** November, 2020  
**To:** Audit Services Oversight Committee  
**From:** Germaine Brewington, Director of Audit Services  
**Subject:** Vendor Management Process Review Dated November 2020

The Audit Services Department staff completed the report for the Vendor Management Process Review. The objectives of this review were to review the vendor management process; and to review training provided to staff to keep them abreast of the changes made to the vendor management process.

This report presents the observations and results of the Vendor Management Process Review. One recommendation was proposed. In response to the recommendation by Audit staff, City Management concur with the recommendation made. The detailed Management Response to the recommendation is included with the attached report.

The Department of Audit Services staff would like to acknowledge the contributions of staff from the Finance Department.

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# Review Report Highlights

## Background

The Purchasing Division of the Finance Department is responsible for maintaining vendor files and accurate vendor information to ensure correct processing of vendor payments. The Accounts Payable staff are responsible for processing payments. In FY 2021, the City became a victim of accounts payable fraud. Fortunately, the City did not lose any money. The City made an electronic fund transfer (EFT) payment to a bank account which belonged to the perpetrator rather than the legitimate vendor. Fortunately, the account had a closed status so the payment automatically returned to the City. Secret Service was also watching the account for suspicious activity and they notified the City.

## Objectives

The objectives of this review were to: 1) Review the vendor management process; and 2) Review training provided to staff to keep them abreast of the changes made to the vendor management process.

## Why this review is important

No matter how big or small a company, every dollar spent by an organization is processed through accounts payable (AP). AP is one of the areas of the business most vulnerable to internal and external fraud. Between vendors, suppliers, payments to employees, and more, organizations need to be vigilant about monitoring their finances.

## Highlights

In FY 2021, the City became a victim of an accounts payable fraud. Fortunately, the City did not lose any money. Lack of following established procedures as well as not having a heightened awareness of red flags around purchasing fraud by the Finance Department staff enabled the fraudster to almost succeed. The City made an electronic fund transfer (EFT) payment to a bank account which belonged to the perpetrator rather than the legitimate vendor. Fortunately, the account had a closed status so the payment automatically returned to the City. The Secret Service was also watching the account of the fraudster for suspicious activity and they notified the City. The revised vendor management process if followed will ensure that vendor information is updated accurately. Requiring all vendors to use Vendor Self-Service to communicate with the City, ensures that change requests originate from the vendor themselves or someone who is privy to vendor access information. In addition, verification of banking and or other pertinent vendor information prior to creating and/or updating vendor information in MUNIS will ensure that the information is accurate. The Purchasing Manager/Team Lead are now responsible for updating/adding banking information to vendor accounts. Purchasing as well as Accounts Payable staff were trained on the revised procedures. Continuous training will be required to make the Purchasing Division staff aware of ways in which potential fraudsters can try to circumvent the vendor management processes and defraud the City.

# Audit Services Department

## Internal Audit

The Audit Services Department serves a three-fold role at the City of Durham. Our number one goal is to provide independent, objective assurance that City processes are working effectively. Secondly, we serve as internal fraud examiners when fraud, waste, or abuse is alleged against a City employee or department. Finally, in order to constantly foster high ethical standards, we provide in-depth ethical training to all City employees on a rolling basis. To learn more, visit our CODI site or our page on the [City of Durham's website](#).

## Audit Services Oversight Committee

In order to maintain its organizational independence, the Audit Services Department reports to the Audit Services Oversight Committee (ASOC) at a minimum of four times a year. The ASOC approves all proposed audit plans and completed audits prepared by Audit Services staff.

The Audit Services Oversight Committee is made up of six members: two City Council Members, three resident members, and one alternate City Council Member. The current members include one certified public accountant and persons with business experience. The City Manager is an ex-officio, non-voting member of the ASOC.

## **Audit Services Oversight Committee Members**

### **Chair:**

Maticia Sims, CPA, CIA, CRMA  
*Resident Member*

### **Vice-Chair:**

Nicolas Long  
*Resident Member*

### **Committee Members:**

Steve Schewel  
*Mayor*  
*City Council Member*

Jillian Johnson  
*Mayor Pro-Tempore*  
*City Council Member*

Shanell Frazer  
*Resident Member*

Charlie Reece  
*Alternate*  
*City Council Member*

### **Non-Voting Member:**

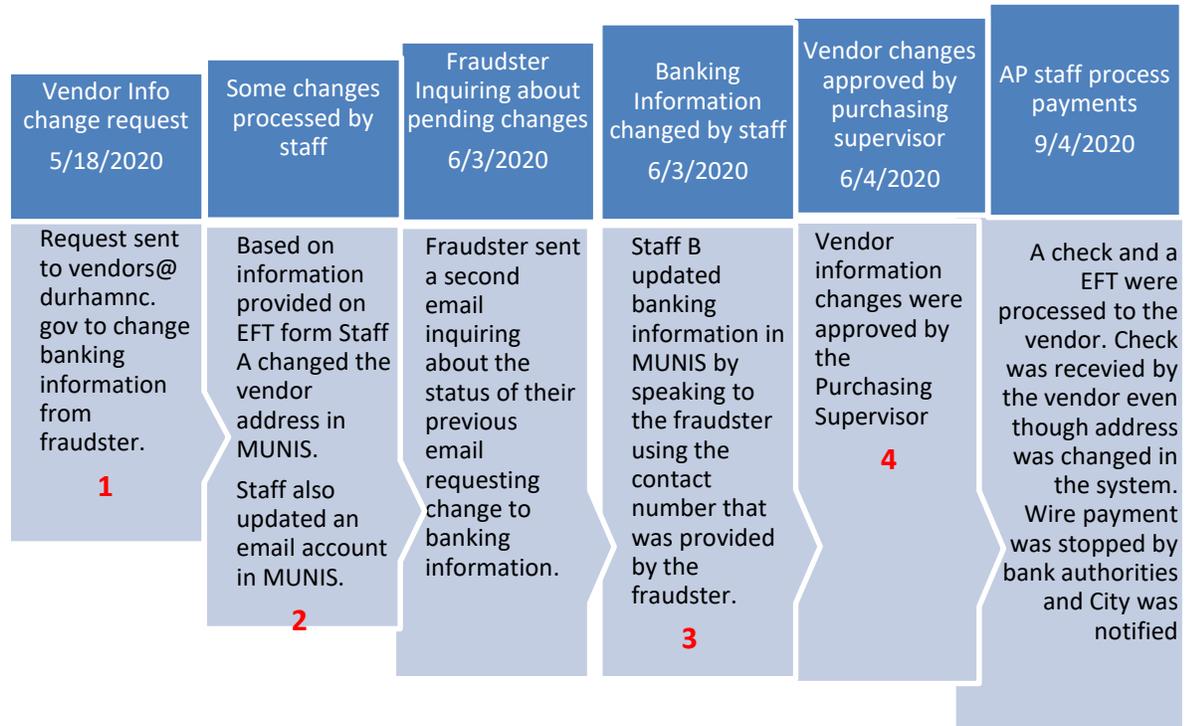
Wanda Page  
*Interim City Manager*

## Background

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No matter how big or small a company, every dollar spent by an organization is processed through accounts payable (AP). Because of this, AP is one of the areas of the business most vulnerable to internal and external fraud. Between vendors, suppliers, payments to employees, and more, organizations need to be vigilant about monitoring their finances. Although accounts payable fraud is an unavoidable risk that comes with doing business, there are several steps organizations can take to protect themselves and limit their financial loss. Accounting professionals play a key role in this process, as they must have the skills and knowledge to recognize the red flags of fraud when processing payment requests. The Purchasing Division of the Finance Department is responsible for maintaining vendor files and accurate vendor information to ensure correct processing of vendor payments. The Accounts Payable staff are responsible for processing payments. In FY 2021, the City became a victim of an accounts payable fraud. Fortunately, the City did not lose any money. The City made an electronic fund transfer (EFT) payment to a bank account which belonged to the perpetrator rather than the legitimate vendor. Fortunately, the account had a closed status so the payment automatically returned to the City. The Secret Service was also watching the account for suspicious activity and they notified the City.

Details of how the potential fraud happened are outlined below in Figure 1:



**Figure 1:** Details of the potential fraud

**Note:** A description of what enabled the fraudster to almost succeed in their plan of defrauding the City is described below.

- 1** A Vendor Information Change request was submitted to [Vendors@Durhamnc.gov](mailto:Vendors@Durhamnc.gov). Anyone with knowledge of this email address can submit an information change request. Risk can be mitigated by ensuring that all change requests are submitted via the Vendor Self-Service platform. Access to information in the Vendor Self-Service account may not be readily available to individuals outside of the vendor’s organization. A fraudster should not be able to submit a change request unless they are privy to Vendor Self-Service account information.
- 2** Prior to updating the vendor file the staff should verify name, address, FID# using <https://www.irs.gov/tax-professionals>. Staff did not perform this procedure as required. Staff A updated the address from 601 Jack Enders Blvd, Berryville VA, 22611 to 601 Enders Blvd, Berryville VA, 22611 and an email address was added isy.giuliani@am-linereastinc.com. The email

address was different than the current valid email on file in MUNIS. ([ex.MARTIN@AMLINEREAST.COM](mailto:ex.MARTIN@AMLINEREAST.COM)). If the verification process was followed, staff would not have changed the physical address and should have recognized the red flag of fraud.

- 3** Staff B updated the banking information which was fraudulent. Staff B should have had the Purchasing Supervisor review the vendor file contacts, and should have reviewed invoice history and contacted the vendor's Finance office to validate the banking information before updating the vendor profile in MUNIS as required by Standard Operating Procedures. Instead, Staff B requested a contact number by emailing the fraudster that initiated the change request. The fraudster replied to the inquiry by sending a contact number. Staff B unaware that they were speaking with the fraudster posing as the President of the company accepted the verification. If verification steps were followed as established, staff would have identified the fraud.
- 4** The changes were approved by the Purchasing Supervisor without review and verification of banking prior to setup.

On 9/4/2020 an EFT payment in the amount of \$304,456.93 was sent to the fraudulent account. On 9/8/2020, the AP Fiscal Analyst was contacted by the Finance Director with the details from the Secret Service and the Finance Director asked the AP Fiscal Analyst to contact the vendor. The AP Fiscal Analyst immediately put a stop on the vendor record and removed the EFT information. The bank account was frozen by the bank and returned back to the City on 9/10/2020. The Finance office of AM Liner East Inc. was contacted and the AP Fiscal Analyst spoke with the Payroll Manager and Assistant to the CFO. The AM Liner East, Inc. staff verified that the check number in the amount of \$553,390 was received. A follow up email was sent with the Vendor Self Service link to the vendor to enable the AM Liner East, Inc. staff to register their organization and make updates. On 9/11/2020, a replacement paper check #853663 in the amount of \$304,456.93 was reissued and mailed on 9/11/20 to 601 Jack Enders Blvd Berryville, VA 22611. Purchasing staff were coached and reprimanded for not performing the procedures as designed.

## Objectives

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The objectives of the review were to:

- 1) Review the vendor management process; and
- 2) Review training provided to staff to keep them abreast of the changes made to the vendor management process.

## Scope, Methodology, and Compliance

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### Scope

The scope of the Agreed Upon Procedures review included examining practices surrounding the vendor management process.

### Methodology

Audit Services Department staff performed the following procedures to accomplish the objectives of the review. Audit staff:

1. Reviewed the revised vendor management process;
2. Interviewed staff responsible for processing changes to vendor information and setting up vendors in the Purchasing Division;
3. Interviewed Accounts Payable staff; and
4. Reviewed documents to support the request to change the AM Liner East, Inc. vendor information in question.

During the audit, Audit Services Department staff also maintained awareness to the potential existence of fraud.

### Compliance

Audit Services staff conducted this Agreed Upon Procedures review in accordance with generally accepted government auditing standards. Those standards require that Audit Services staff plan and perform the review to obtain

sufficient and appropriate evidence to provide a reasonable basis for our findings and conclusions based on the review objectives. Audit Services staff believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our review objectives.

## **Results and Findings**

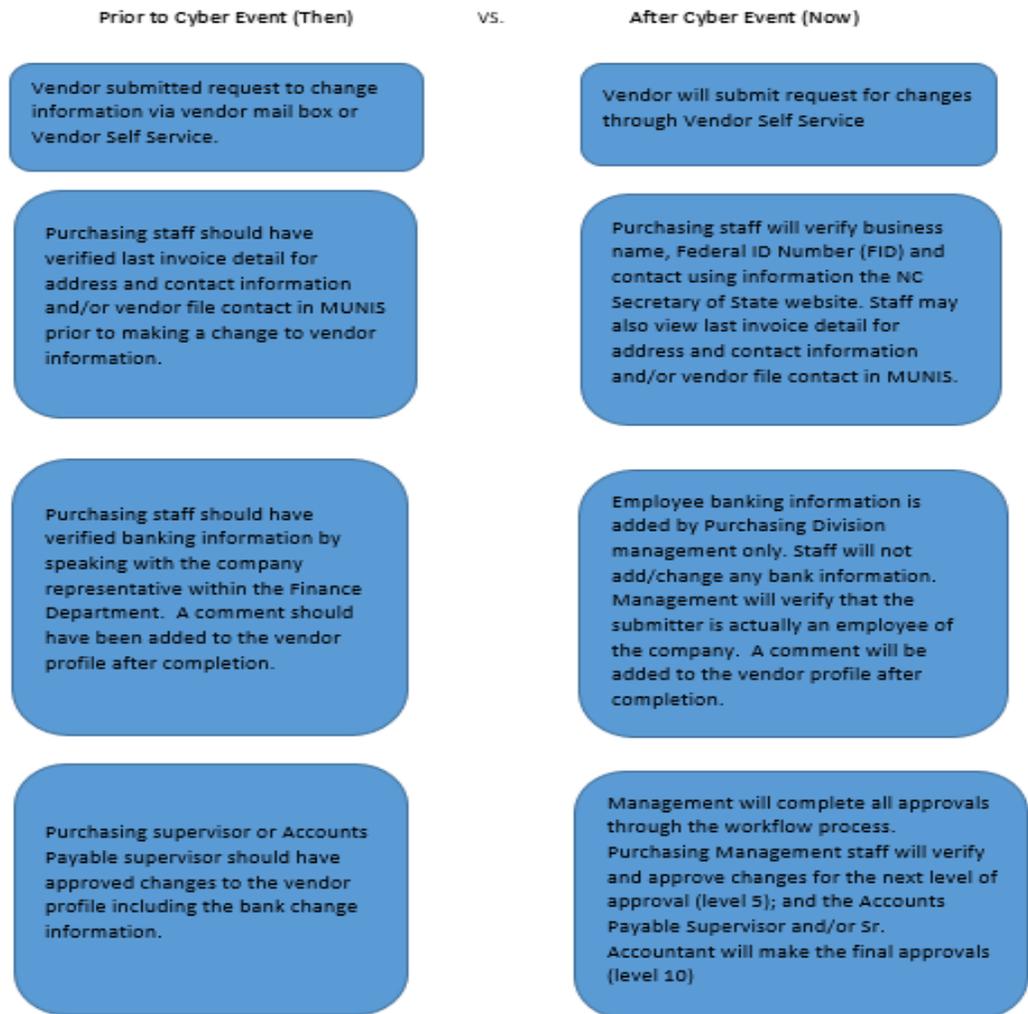
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### **Objective 1 Results Summary**

#### **REVIEW THE REVISED VENDOR MANAGEMENT PROCESS**

The revised vendor management process if followed will ensure that vendor information is updated accurately. Requiring all vendors to use the Vendor Self-Service portal to communicate with the City ensures that change requests originate from the vendor themselves or someone who is privy to vendor access information. In addition, verification of banking and or other pertinent vendor information prior to creating and/or updating vendor information in MUNIS will ensure that the information is accurate. The Purchasing Manager/Purchasing Team Lead are now responsible for updating/adding banking information to vendor accounts. This responsibility originally resided with the Purchasing Division staff. Given this recent incident the Purchasing staff are no longer tasked with adding/updating any banking information for any vendor in MUNIS. An additional layer of approval has been added such that the Accounts Payable Manager will sign off on all changes to vendor accounts. The following Figure 2 outlines the process before and after the incident.

## Process to Change Vendor Information



**Figure 2:** Process before and after the incident.

Purchasing as well as Accounts Payable staff were trained on the revised procedures. Continuous training will be required to keep Purchasing staff aware

of ways in which potential fraudsters can try to circumvent the vendor management process and defraud the City.

## Objective 2 Results Summary

### REVIEW TRAINING PROVIDED TO STAFF

Training provided to Finance Department staff currently is focused on making staff aware of the revised standard operating procedures. Training is not designed to help them understand how the new procedures when applied, will mitigate fraud or develop employee skills and knowledge to recognize the red flags of fraud in the accounts payable area. Research from the premier fraud organization-The Association of Certified Fraud Examiners has identified that “a 14% frequency of frauds originate in the Accounting department” (Association of Certified Fraud Examiners Inc., 2020, pg. 40). This percentage is second only to Operations departments that saw a 15% frequency rate in the occurrence of fraud (Association of Certified Fraud Examiners, Inc., 2020). Accounting professionals play a key role in this mitigation process, and they must have the skills and knowledge to recognize the red flags of fraud when processing payment requests.

Reference: Association of Certified Fraud Examiners, Inc. (2020). *Report to the nations: 2020 Global study on occupational fraud and abuse*. Retrieved from: [2020 ACFE Report to the Nations](#)

#### Finding 1

##### **Audit Services staff found:**

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*Training provided to staff should focus on enhancing staff's ability to recognize red flags of fraud.*

After this incident Purchasing staff and Accounts Payable staff were trained on the revised standard operating procedures. At present, training is not focused on developing staff's skills of recognizing fraud. Developing this skill set will help mitigate the risk of fraud.

## Conclusion

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In FY 2021, the City became a victim of accounts payable fraud. Fortunately, the City did not lose any money. Lack of following established procedures as well as not having a heightened awareness of red flags around purchasing fraud by the Finance Department staff enabled the fraudster to almost succeed. The revised vendor management process if followed will ensure that vendor information is updated accurately. Requiring all vendors to use Vendor Self-Service to communicate with the City ensures that change requests originate from the vendor themselves or someone who is privy to vendor access information. In addition, verification of banking and or other pertinent vendor information prior to creating and/or updating vendor information in MUNIS will ensure that the information is accurate. The Purchasing Manager/Team Lead are now responsible for updating/adding banking information to vendor accounts. Purchasing as well as Accounts Payable staff were trained on the revised procedures. Continuous training will be required to keep Purchasing staff aware of ways in which potential fraudsters can try to circumvent the vendor management process and defraud the City.

# Recommendation

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## Recommendation 1

The Finance Department staff should provide ongoing training to all staff involved in the accounts payable process. Training should focus on developing skills needed to identify red flags of fraud in the Accounts Payable area in addition to training on current established procedures.

**Value Added:** Risk Reduction

### Value Added Legend



To learn more, visit our website at: [durhamNC.gov/audit](http://durhamNC.gov/audit)

## Management Response

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Memo to: Dr. Germaine F. Brewington, Director of Audit Services  
From: David Boyd, Finance Director  
Date: December 14, 2020  
Subject: Management's Response to Recommendations Vendor Management Process Review December 2020

The following is the management's response to the Budget Measures Performance Audit dated June 2020.

**Recommendation 1:**

The Finance Department staff should provide ongoing training to all staff involved in the accounts payable process. Training should focus on developing skills needed to identify red flags of fraud in the Accounts Payable area in addition to training on current established procedures. Insert text here.

**Management's Response:**

We concur. Management is in full agreement with the recommendation.

The Purchasing Division's desk procedures were revised by the Purchasing Manager, Procurement Admin and Fiscal Analyst, Sr and distributed to all staff prior to the October 12<sup>th</sup> training. Additional trainings have been scheduled for quarterly trainings beginning on April 12, 2020. Along with our scheduled trainings, Audit Service's staff has agreed to conduct trainings on fraud awareness and the identification of red flags, particularly in the purchasing arena. Dates to be determined.

Implementation was completed on October 12, 2020 during training.

## Distribution of Report

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