

Western Australian Auditor General's Report



Audit of Payroll and other Expenditure using Data Analytic Procedures



Report 6: May 2016

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WESTERN AUSTRALIAN AUDITOR GENERAL'S REPORT

**Audit of Payroll and other Expenditure using
Data Analytic Procedures**

Report 6
May 2016



**THE PRESIDENT
LEGISLATIVE COUNCIL**

**THE SPEAKER
LEGISLATIVE ASSEMBLY**

**AUDIT OF PAYROLL AND OTHER EXPENDITURE USING DATA ANALYTIC
PROCEDURES**

This report has been prepared for submission to Parliament under the provisions of section 25 of the *Auditor General Act 2006*.

Our audit analysed large volumes of agency expenditure and payroll data to identify potential fraud, errors or omissions. We found no evidence of fraud from our tests. However, we did identify errors including overpayments and a need for improved controls at half the agencies tested.

I wish to acknowledge the cooperation of the staff at the agencies included in this audit.

A handwritten signature in black ink, appearing to read 'C. Murphy'.

COLIN MURPHY
AUDITOR GENERAL
10 May 2016

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Audit of payroll and other expenditure using data analytic procedures

Background

Tens of millions of state government financial transactions occur each year. Agencies are required to maintain suitable policies and financial controls to ensure that these transactions are justified and approved.

However, policies, controls and well-trained staff do not guarantee that these transactions will not involve errors or fraud. They just reduce the probability of occurrence.

Our normal testing of controls and transactions during our annual financial audits aims to identify 'material' errors. That is, an error that would cause a line item in a financial statement to be materially misstated. So, while our sampling of transactions supports the material accuracy of the financial statements and gives an understanding about the reliability of controls, its purpose is not to specifically test for fraud.

In this audit, we have used data analytics to test for fraud or errors.

Data analytics can be used to search large volumes of transactions and data for unusual items, patterns and events that could indicate fraud. We then further investigate the items or events to identify errors or potential fraud.

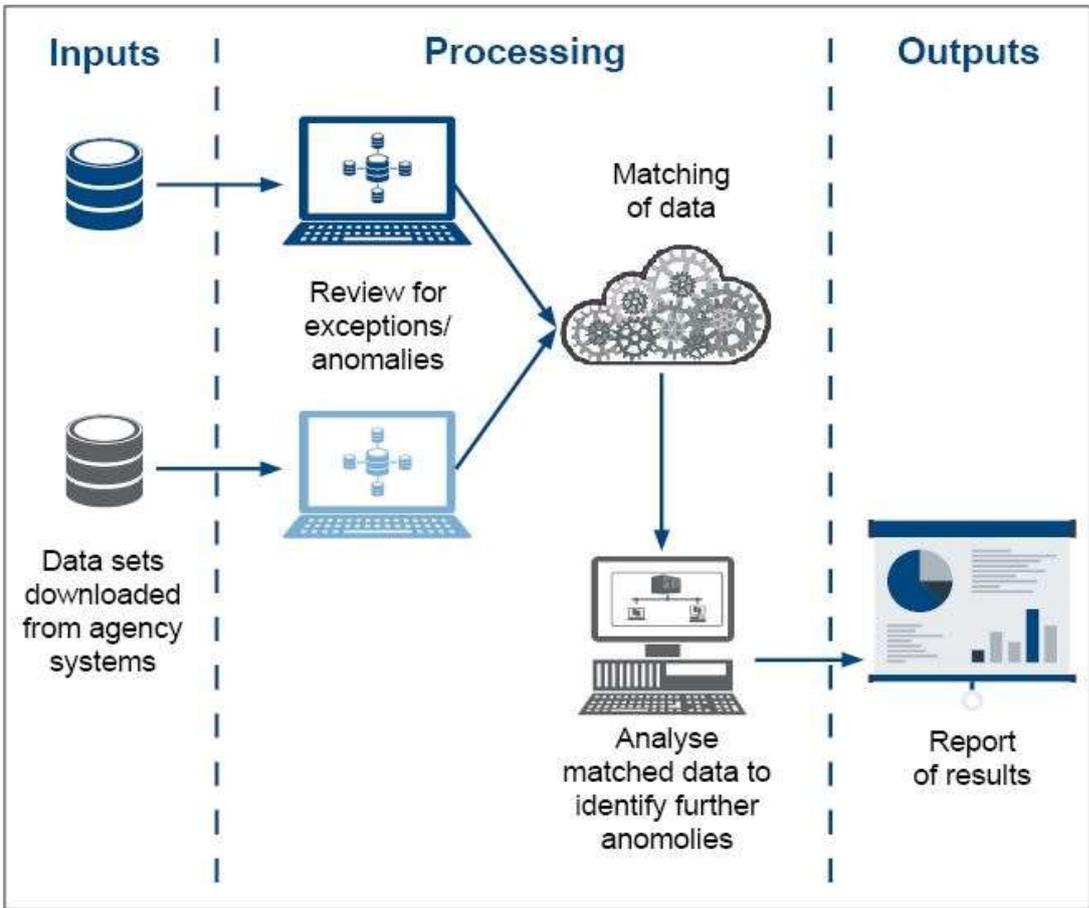


Figure 1: Simplified illustration of data analytics

What we did

Our objective was to analyse agency expenditure and payroll data to identify potential fraud, errors or omissions. We downloaded and analysed 4 million transactions totalling over \$7.5 billion from the systems of 12 agencies. Our audit techniques included the matching of data between agency systems, and the interrogation of databases. We have not disclosed all of our audit tests in this report; however, they included identifying:

- supplier invoices that may have been paid twice
- officers approving payments that were above their delegation limits
- 'splitting' of invoices into smaller amounts to circumvent system delegation limits
- purchases from suppliers associated with agency staff, which may indicate undue favouring of a supplier
- government purchasing cards used while the relevant officer was on leave
- unusual payments or payments with inadequate descriptions, which may indicate fraud
- payments approved by only 1 officer
- payments to non-approved suppliers
- large payroll payments which may indicate overpayments
- payment of allowances beyond their approved period
- employees paid after they ceased work at the agency.

Our testing included payroll expenses totalling \$4.1 billion and other expenditure totalling \$3.4 billion. Some audit procedures enabled 100% testing for anomalies, whereas other tests involved identifying potential anomalies, which we investigated on a sample basis. We audited the agencies listed in Table 1 for the period 1 July 2014 to 30 April 2015.

Agency	Payroll transactions tested \$m	Other expense transactions tested \$m
Child Protection and Family Support	262	334
Commerce	70	71
Corrective Services	436	313
Department of Planning	50	34
Education	2,417	1,778
Fisheries	42	42
Parks and Wildlife	101	104
Regional Development	13	103
Treasury	25	69
Police Service	687	478
WA Land Information Authority (Landgate)	61	139
Workcover	12	10

Table 1: Value of payroll and other expenditure audited

Unfortunately, we were unable to perform all of our tests at all agencies because of the unavailability of suitable data in some instances. For example, some agencies hold key information as manual records or in unsuitable formats meaning data matching was not feasible. We reveal in the Findings section which tests we could not perform at all agencies.

We conducted this narrow scope performance audit under section 18 of the *Auditor General Act 2006* and in accordance with Australian Auditing and Assurance Standards.

Conclusion

We found no evidence of fraud from our tests at any of the 12 agencies. However, we did identify errors including overpayments and a need for improved controls at 6 agencies, and in particular, at the Department of Corrective Services. Without improved controls, there is a heightened risk of fraud or error occurring.

What did we find?

We found a range of errors and a need for improved controls, though we found no significant errors or non-compliance. The following is a summary of our findings:

Suppliers paid twice for the same services

Two agencies made 10 duplicate payments totalling \$51,545. The agency or vendor detected 4 of the duplicate payments totalling \$43,754 after the agency made the second payment, while the others, totalling \$7,791 were detected by our audit. Overpayments totalling \$6,875 are yet to be recovered.

Preventing duplicate payments should be a fundamental prerequisite of any payment system. The 10 duplicate payments occurred due to a failure of 1 or more control procedures. Specifically:

- processing payments based on copies of invoices rather than originals
- multiple entries for the same supplier in the agency's supplier listing, resulting in undetected duplicate payments
- paying through the accounts payable system after it had already been paid by purchasing card.

Invoice splitting and exceeding delegation limits

We found 9 instances at the Department of Corrective Services of invoice 'splitting'. The relevant payments totalled \$174,275.

One way in which an employee can approve payments above their delegated limit, is to split the total owed into smaller payments within their limit. Invoice splitting can assist persons with fraudulent intent to reduce the likelihood of fraudulent payments being detected.

While we do not believe that fraud was involved in these instances, it did mean that the payments were not properly authorised. This in itself is a serious matter. Authorisation of payments aims to ensure that senior management are aware of purchased services and supplies and helps ensure that those services and supplies are warranted and consistent with the agency's mandate and purpose.

We only checked for invoice splitting and exceeding of delegation limits at 2 agencies. This was because the other 10 agencies do not keep an electronic record of the officer who approved each payment in a format that enables reliable data matching.

Payments to companies that are associated with an agency employee

In this analysis, we used a database of the Australian Securities and Investments Commission (ASIC) to identify payments made by agencies to companies that were associated with employees of the agencies. We then assessed whether the agency had recognised the potential for corruption or conflict of interest.

At 2 agencies, we identified 13 payments totalling \$10,985 made to companies associated with an employee and an advisory board member. Neither agency could demonstrate that they had recognised the risks. One of the agencies documented and formally considered the risk only when we reported the matter to them. Subsequently, both agencies were able to provide sufficient evidence to remove our concern about potential corruption or conflict of interest.

It is important to note that our testing did not include matching to other government databases or bank records, which could be performed in a more detailed investigation, for example where there is a strong indication of fraud or conflict of interest.

Payments to a family member

We tested payments made outside the payroll system into the bank accounts of employees to ensure that employees with capacity to authorise payments were not paying into their own accounts or colluding to pay into the accounts of other employees.

At the Police Service, we identified a payment of \$1,400 into an employee's bank account for services provided by a relative of the employee. We found that the employee who received the payment also authorised the payment.

After we reported the issue, the agency commenced an internal investigation on the conduct of the individual. They found that the payment was for valid services and recommended that no criminal charges be pursued. However, management considered that there was a clear conflict of interest involved and advised that the matter is now being investigated in accordance with the Public Sector Management Act.

Using a purchasing card while the cardholder was on leave

Our analysis included \$197 million in payments using government purchasing cards. During our analysis, we noted 45 purchasing card payments at Department of Corrective Services and Department of Treasury totalling \$82,769 where the cards were used by other employees while the cardholder was on leave. Although all these payments were for legitimate purposes, the use of another employee's purchasing card is not appropriate as it can make accountability for financial transactions difficult to determine.

At the Department of Education, our testing detected a purchasing card used to purchase alcohol while the cardholder was on leave. This card had been stolen and used for payments totalling \$1,928. Although the Department reported the theft and the bank made reimbursement for the illegal payments, the cardholder was not requested at the time to complete a statutory declaration in relation to the circumstances. A statutory declaration was provided during our audit.

Government purchasing cards used on personal PayPal accounts

Agencies sometimes use PayPal as a method of payment. We identified 4,926 payments at 12 agencies totalling nearly \$1.2 million that used the PayPal payment method.

While this may be convenient, it does carry the risk of inadvertent use of government purchasing cards for private purposes if employees link the government card to their personal PayPal account. We identified 3 private payments made in this manner, though the cardholders had already reimbursed all 3 payments. Only the Department of Parks and

Wildlife and Department of Education had PayPal policies to identify the circumstances where this payment method can be used and to help manage the risk.

Lack of clear reason for some payments

The Treasurer's Instructions set out fundamental requirements to be met before an agency's incurring and certifying officers can authorise a payment. These include the need for sufficient description of the reason for a payment in order for them to be satisfied that the payment is appropriate.

Our analysis included sample testing of the adequacy of descriptions used to explain the reason for payments. Although the vast majority of payments contained sufficient explanation of the reason for payment, 12 of 51 payments at Department of Corrective Services lacked adequate detail. We therefore could not confirm that the payments were appropriate.

Examples included:

- travel costs incurred on purchasing cards that significantly exceeded the daily public service allowances. We expected to see clear explanations to demonstrate the need for the excess expenditure
- purchases made from a hardware chain with no explanation of their purpose
- no explanation of the reason for payment of private school fees
- supporting documentation for purchase of mobile phone accessories that was inconsistent with receipts for tie down straps for a car trailer.

The Department advised that it is investigating the transactions.

Some tests found no errors

Some of our data analytics tests found no errors, which indicated that the related system controls were sound at these agencies:

- Overpayments of temporary salary allowances – we found no instances at any of the 12 agencies of temporary salary allowances (Temporary Special Allowance or Higher Duties Allowance) continuing after the employee ceased to perform the relevant duties.
- Payments approved by only 1 officer – the Treasurer's Instructions and better practice requires at least 2 officers approve payments to minimise the risk of fraud. We tested 2 agencies and found no non-compliance. We were unable to test the other 10 agencies because they did not hold this information in a format that enabled reliable data matching.

Recommendations

1. All agencies should ensure that they maintain the integrity of their financial control environment and their key financial and operational databases by:
 - a) periodically reviewing and updating policies and procedures, and communicating these to staff
 - b) periodically reviewing the adequacy of their controls that prevent, and detect the types of control weakness identified in this report
 - c) monitoring compliance with policies, including through analysis of transactions and databases.

Use of data analytics – guidance to all agencies

Data analytics is a technique that all agencies can use to gain assurance about the reliability of their data and efficiency of their operations. In particular, we recommend that agencies consider its use:

- when wanting their internal auditors to provide assurance about agency functions that can be measured through interrogation of data. Such analysis would be especially warranted if there are known problems that can be understood by in-depth analysis
- after a new system or procedure has been implemented, or after key controls have been modified to achieve efficiencies. This testing can detect fraud or errors that may be a result of gaps in the new/revised controls.

Auditor General's Reports

Report No.	Reports 2016	Date Tabled
5	Audit Results Report –Annual 2015 Financial Audits – Universities and state training providers – Other audits completed since 1 November 2015; and Opinion on Ministerial Notification	10 May 2016
4	Land Asset Sales Program	6 April 2016
3	Management of Government Concessions	16 March 2016
2	Consumable Stock Management in Hospitals	24 February 2016
1	Health Department's Procurement and Management of its Centralised Computing Services Contract	17 February 2016

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