Council Direction: Not applicable

Information: To ensure the efficiency and effectiveness of transaction processing through the disbursement process and the proper treatment of commodity taxes, management of Corporate Services have committed to having periodic external reviews performed every few years.

Two external consultants were engaged through the request for proposal process to review the years 2003, 2004 and 2005. The consultants reviewed transactions looking for overpayments, misinterpretations of legislation and incorrect calculations. The fee charged by both consultants is contingent upon recoveries received. If no monies are recovered then no fees are paid to them. The consultants report any systemic problems they encounter and make recommendations for improvements.

Their findings are positive as reflected by the small percentage of errors that they have uncovered in both areas.

Accounts Payable Review Results:
Recoveries were identified on 20 of 472,620 transactions reviewed. A transaction processing accuracy rate of 99.99 percent of transactions and 99.99 percent of the total dollars disbursed resulted. The recoveries totalled $59,350 out of over $1.98 billion in transactions processed. This translates to approximately $20,000 of overpayments per year of which all but the consultant’s percentage fees have been recovered. The consultant reports that the Accounts Payable processes were very well managed and controlled.

The overpayments have been summarized into four categories. Five overpayments totalling $13,096 were made when invoices submitted to Accounts Payable twice were...
keypunched to two different vendors. This occurs as either a careless error or because there are vendors set up in the system having very similar names. When this happens, the system does not identify the duplicate because it appears to be a unique payment as the vendors are different. Four overpayments totalling $8,195 were made when the same invoice was submitted twice for payment and a keypunch error occurred on the Invoice Number input. Again, the system sees this as two different invoices and does not flag the payment as duplicate. The first two categories become problems when operational staff approve and submit multiple copies of the same invoice. The third category occurred because the vendor submitted two unique invoices (different invoice numbers, different amounts) for the same goods but did not supply us with a credit note. There were 2 overpayments of this nature totalling $28,438. The last category contained 8 overpayments totalling $8,167. These overpayments relate to returned goods where a credit note was not submitted to Accounts Payable for the credit to be input.

One potential solution to minimize these errors would be to add one staff dedicated to independent proof reading and error detection. This would cost approximately $60,000. Due to the nature of the duplicate payments and the high volumes an extra body would not eliminate all overpayments. The projected savings of approximately $20,000 does not justify this cost. The consultant provided some recommendations for improvement as part of his report. These recommendations have either already been implemented or are being investigated. A copy of the consultant’s Accounts Payable Review Report is attached as Appendix A.

Commodity Tax Review Results:

The consultant reviewed the City’s commodity tax files for Employer Health Taxes ("EHT"), Ontario Retail Sales Tax ("ORST/PST"), Gasoline and Fuel Taxes and Goods and Services Tax ("GST"). His findings are broken down as:

<table>
<thead>
<tr>
<th>Recoveries</th>
<th>Tax Type</th>
</tr>
</thead>
<tbody>
<tr>
<td>$0</td>
<td>Employer Health Taxes (“EHT”)</td>
</tr>
<tr>
<td>$0</td>
<td>Ontario Retail Sales Tax (“ORST”)</td>
</tr>
<tr>
<td>$15,000</td>
<td>Gasoline Tax – Fire Services</td>
</tr>
<tr>
<td>$76,000</td>
<td>Goods and Services Tax (“GST”)</td>
</tr>
</tbody>
</table>

The consultant had no issues to report for Employer Health Taxes (“EHT”) on our filings of $7.3 million in 2005 and $7.1 million in 2004 and no issues with the City’s ORST claims of $623,000 in 2005 and $542,000 in 2004. The consultant will be completing gasoline tax rebate claims estimated at $15,000 for Fire Services for 2003 to 2005. Gasoline tax rebates are available for fuel purchased to power auxiliary equipment on vehicles and to power unlicensed non-recreation vehicles and equipment. Gas tax rebates for other City vehicles filed by Fleet Services average $55,000 per year. The consultant estimates additional fuel rebates of $5,000 per year for 2003 to 2005 for powering auxiliary equipment on vehicles used by Fire Services.
Procedures will be implemented by Fire Services to submit the required information to Fleet Service for the completion of the Gasoline Tax Rebate on an annual basis.

The consultant’s review of GST was much more comprehensive and time consuming. He reviewed over 459,000 accounts payable transaction lines for 2003 through 2005 totalling approximately $2 billion. GST adjustments of $76,000 have been made related to mileage, parking, and training courses. This represents 0.26% on the City’s 2005 GST rebate of $29.7 million. The majority of the GST adjustments required in 2003 were not available in 2004 and 2005 due to the change in the municipal GST rebate. The change in the municipal GST rebate from 57.14% to 100% on February 1, 2004 made for less decision making on payment processing and provided less recovery opportunities.

The consultant’s findings will be discussed with staff across the Corporation to improve their education and understanding of GST.

_______________________
Joseph L. Rinaldo
General Manager
Finance and Corporate Services
May 4, 2006

City of Hamilton
71 Main Street West
Hamilton, Ontario
L8P 4Y5

Attention: Ms. Jane Hartwell, Manager of Business Applications Support & A/P

Dear Ms. Hartwell,

A Disbursement Audit was performed by BGI Benchmark Group International at the City of Hamilton during the period January through April 2006. The purpose of the audit was to identify disbursement errors and the associated control weaknesses which may have caused the errors. The period reviewed included disbursements from January 2003 through November 2005.

For this 35-month period, BGI reviewed approximately 472,620 transactions totaling over $1.98 billion. As of the report date, we identified recoveries on 20 items totaling $59,350.28. The recoveries consisted of the following:

<table>
<thead>
<tr>
<th>Type of Error</th>
<th>Number of Items</th>
<th>Amount of Item</th>
<th>Percent of Item</th>
</tr>
</thead>
<tbody>
<tr>
<td>Duplicate Paid - Different Supplier #</td>
<td>5</td>
<td>25.0%</td>
<td>13,096.90</td>
</tr>
<tr>
<td>Duplicate Paid - Altered Invoice #</td>
<td>4</td>
<td>20.0%</td>
<td>8,195.35</td>
</tr>
<tr>
<td>Duplicated Billing</td>
<td>2</td>
<td>10.0%</td>
<td>28,437.64</td>
</tr>
<tr>
<td>Sub-Total Duplicate Payments</td>
<td>11</td>
<td>55.0%</td>
<td>49,729.89</td>
</tr>
<tr>
<td>Unprocessed Credits</td>
<td>8</td>
<td>40.0%</td>
<td>8,167.25</td>
</tr>
<tr>
<td>Other Miscellaneous Overpayments</td>
<td>1</td>
<td>5.0%</td>
<td>1,453.14</td>
</tr>
<tr>
<td>Totals</td>
<td>20</td>
<td>100.0%</td>
<td>59,350.28</td>
</tr>
</tbody>
</table>

Overall, 99.996 percent of the transactions and 99.997 percent of the total dollars disbursed were processed correctly. Our review indicated that the accounts payable area was very well managed and controlled.
A summary of validated recoveries is included with this report and includes details of the individual recovery items and the causes for the errors.

Our review did indicate that there were opportunities for improvements in operational efficiencies as well as control issues that should be addressed. A discussion of each of these issues is included in the "Observations and Recommendations" section of this report.

BGI very much appreciates the assistance and cooperation of City of Hamilton personnel and management during this review and would welcome the opportunity to conduct another review in the near future.

Sincerely,

Alan Myers
Senior Accounts Payable Specialist
Observations and Recommendations

A. Enter Correct Invoice Details

System controls are circumvented when incorrect invoice numbers or dates are entered into the accounts payable system. There were 4 recoveries totaling $8,195.35 that were attributable to this type of inconsistency. The following table lists examples of invoices entered into the accounts payable system with altered invoice numbers:

<table>
<thead>
<tr>
<th>Supplier Name</th>
<th>Item Number</th>
<th>Invoice Number</th>
<th>First Payment</th>
<th>Second Payment</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Addmore Office Furniture</td>
<td>HAM11</td>
<td>D42268</td>
<td>87826</td>
<td></td>
<td>$1,242.00</td>
</tr>
<tr>
<td>Allturf Ltd.</td>
<td>HAM14</td>
<td>129806</td>
<td>0000129806</td>
<td></td>
<td>$696.90</td>
</tr>
<tr>
<td>Cayuga Materials</td>
<td>HAM19</td>
<td>401168780</td>
<td>701168780</td>
<td></td>
<td>$4,899.84</td>
</tr>
</tbody>
</table>

Recommended Action

A1. Guidelines should be included in written accounts payable procedures to promote consistency in the entering of invoice information. These guidelines need to be communicated to all branches and areas that have involvement in entering invoices for payment into the system so as to ensure consistency throughout the company (See Appendix 1 - Suggested Procedures for Entering Supplier Invoices).

A.2. Accounts payable processors should carefully review their data input to ensure that the correct invoice information is entered into the system.

B. Improve Supplier Master File Maintenance

The supplier master file contains over 30,200 records and is generally well maintained. However, there are several suppliers who have more than one supplier record and/or have been inactive for some time.

Duplicate payment system controls are circumvented when a payment references a different supplier record. There were 5 recoveries totaling $13,096.90 that were attributable to this type of inconsistency. The following table lists examples of invoices entered into the accounts payable system using two different supplier numbers:

<table>
<thead>
<tr>
<th>Supplier Name</th>
<th>Item Number</th>
<th>Invoice Number</th>
<th>Supplier Number</th>
<th>First Payment</th>
<th>Second Payment</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bloomco</td>
<td>HAM09</td>
<td>0002732</td>
<td>08892</td>
<td>51388</td>
<td></td>
<td>$2,000.00</td>
</tr>
<tr>
<td>Wolseley Canada</td>
<td>HAM10</td>
<td>3694866</td>
<td>35963</td>
<td>42730</td>
<td></td>
<td>$2,357.50</td>
</tr>
<tr>
<td>CHML/CJXY</td>
<td>HAM16</td>
<td>27628</td>
<td>18271</td>
<td>00320</td>
<td></td>
<td>$2,856.90</td>
</tr>
</tbody>
</table>
Recommended Action

B.1. The supplier file should be periodically reviewed to identify duplicate and/or inactive supplier records and consideration should be given to marking them as inactive.

B.2. Accounts payable processors should carefully review their data input to ensure that the vendor name on the computer is identical to the name on the invoice.

C. Forward Approved Invoices and Credits to Accounts Payable

City of Hamilton personnel who review and approve invoices for payment do not always promptly forward them to Accounts Payable. As a result, suppliers often inquire about past due invoices and fax or mail invoice copies for payment which, combined with the control weaknesses identified in A. and B. above, can lead to duplicate payments.

Recommended Action

C.1. All City of Hamilton departments should be reminded of the importance of forwarding approved invoices to accounts payable for timely processing.

D. Review Supplier Statements

Accounts Payable does not consistently review many of the supplier statements received and does not always account for all supplier issued credits. We reviewed accounts receivable aging statements from selected suppliers and recovered 8 unprocessed credits totaling $8,167.25. These credit memos were addressed to departments outside of Accounts Payable and were apparently never forwarded to Accounts Payable for processing.

Recommended Action

D.1. Accounts Payable should review selected supplier statements on a monthly basis. Supplier selection should be based on the volume of transactions, dollars, and returns activity. Items over 90 days should be researched and cleared promptly.

D.2. Suppliers should be notified that under no circumstances are they to unilaterally apply duplicate payments or overpayments. A duplicate payment or overpayment should be shown as a credit until taken and unpaid invoices or other charges should be recorded separately.

D.3. City of Hamilton personnel who have knowledge of credits for services or returned goods and receive credit notes directly from suppliers should be educated by accounting department staff to immediately inform Accounts Payable of these credits and forward the relevant paperwork in order to avoid overpayments.
E. Request Suppliers Submit Only One Invoice

Two instances were found where a supplier sent out an original invoice and a corrected invoice with no indication that the second invoice was a correction. See Schedule A, item numbers HAM01 and HAM02. We recovered 2 duplicate payments totaling $28,437.64 because of this situation.

Recommended Action

E.1. Suppliers who submit two original invoices should be contacted and requested to discontinue this practice. City of Hamilton should consider charging a handling charge to suppliers who submit two original invoices.