



## Accounts Payable – A Goldmine for You and Your Clients

In this article we will show how you can use IDEA - or even train your clients in its use - to increase the value of your engagements.

Purchases and payables is the most common transaction generating misstatements - deliberate or inadvertent. Some of the possibilities are dummy invoices for fictitious suppliers, splitting invoices to avoid approval thresholds and the most common, duplicate payments. Data analysis can also detect inefficiencies in systems (e.g. large number of small cheques), budget manipulation (e.g. large purchases made just before or just after a quarter or year end date), process improvements (e.g. elimination of employee advances through use of corporate credit cards) and provide useful information for your client on purchasing patterns and cash flow requirements.

### Review of Planning Considerations

Before undertaking an engagement, accountants should include as part of their planning, consideration as to whether IDEA would be a suitable tool for a particular engagement or client. Success factors include:

- Sufficient transaction volume and detail. For Accounts Payable, the IDEA Workbook recommends a minimum of 2,500 transactions.
- The ability to easily acquire copies of the client data. IDEA comes with a number of tools to assist the user in acquiring appropriate data including direct import of popular small business accounting packages such as Simply Accounting and QuickBooks. For larger systems, you would look for files or tables containing Supplier Master information, Payment History and Purchases Ledger.
- Properly trained and equipped staff. While IDEA is consistently rated highly for its ease of use, it is recommended that staff participate in either a 2-day introductory course or complete the self-study program in the IDEA Workbook.

If these success factors are present, IDEA can help you improve the quality and efficiency of your work, and add value to your work for your client.

### Some Examples

Here is a brief selection of tests and procedures that can be used to identify anomalies and errors.

#### 1. Looking at the digits - Benford's Law

In the 1920's, a physicist at GE Research Laboratories, Frank Benford, noticed that his log table books were more worn in the first section (logs of numbers with low first digits) compared to the last section (logs of numbers with high first digits). He concluded that he was looking up logs of numbers with low first digits, because there were more of them. He tested his theory against available lists of naturally generated numbers and used mathematical models to calculate expected frequency of the occurrence of digits, now known as Benford's Law. The law states that the digit "1" occurs more frequently than any other as the first digit of a number (about 30%) declining through to "9" which occurs about 5% of the time.

Auditors and analysts can use Benford's Law to identify numbers in a data set which do not conform to the expected frequency. However, you should note that numbers which are assigned, such as invoice or cheque number, will not comply, nor will data files with prescribed minimums or maximums. IDEA contains built-in Benford's Law functions, allowing users to compare client files against expected outcomes for first, first two, first three and second digits. In the example below, the first two digits of "79" appear abnormally frequently. This situation should be checked against internal procedures - for instance there may be an approval threshold at \$80,000 or \$8,000.

#### 2. Other Digital Analysis

Another common indication of fraud or error in purchases is the occurrence of round numbers. To search for round numbers using IDEA, you need to understand the term "modulus". The "MOD" button on IDEA's equation editor is the modulus function. This gives the remainder when dividing one numeric expression by another. When you click the MOD button, a "%" sign is entered into the equation. Thus, to find all the round thousands simply build an equation as follows: **AMOUNT % 1000 = 0**. This equation will generate a file of all records where the amount, divided by 1000 yields a remainder equal to zero.

### 3. Basic Analysis

The File Statistics available for an IDEA file can contain some useful basic information which could lead you to alter your test plan. For instance, auditors have reported finding 2 zero items in payables files. If this happens at one of your clients, you should inquire as to how that could have occurred and based on the response possibly change your audit plan.

### 4. More Analysis

File Stratification is a powerful feature which provides you significant insight into purchasing patterns. For instance, you can stratify the payments file on the Amount field, to determine the number of transactions in each of your specified bands. This could show a large number of small payments, leading to a recommendation to management to consolidate vendors.

### 5. Some More Basics

Routine tests that should be included in your accounts payable work include:

- comparing the total of the file with the amount shown in the general or sub ledger
- joining the transaction file with the supplier master file and then searching for transactions with no authorized supplier
- testing for gaps in cheque number sequence, summarize payments by supplier to identify purchasing patterns and compare to previous year as well as highlighting unusual items such as a one-off large payment to a supplier
- selection of large balances and a statistical sample of others for confirmation.

### 6. Process Improvements

In a recent audit, using the Payments file, we created a Virtual Field called "Days to Pay", by calculating the difference between the date of the supplier invoice and the date it was paid. Our client had a policy of paying invoices within 25 days of receipt. We summarized our file on Days to Pay. The results show good compliance with the 25-day rule, but also show a number of unusual exceptions including invoices paid before the invoice date! An improvement to this payment process would be an appropriate recommendation to management.

### 7. Management Analysis

You can use Pivot Tables to easily create analysis for management that may not be available from conventional reporting. Other similar analysis can be created on the fly from huge data files.

### 8. Duplicate Payments

We saved the best for last. Searching and identifying duplicate payments is a powerful, valuable client service. Some planning and thought is required to search effectively. While most accounts payable systems have controls to prevent duplicate payments, they are often easily overridden or by-passed by staff. The simplest test would be to use IDEA's "Duplicate" task to identify items with duplicate Supplier Number and Amount. This could generate items which are merely recurring payments, so you might want to add Invoice Date or Invoice Number to the duplicate requirements. You could also try search for Duplicate Amounts and Invoice Number allowing different Supplier Numbers. This could uncover invoices paid twice but to different vendors.

One IDEA user in internal audit found that duplicate payment testing had such a high payback that he added one of the company's accounts payable clerks to his audit team and trained her to use IDEA. Within a short time period, the clerk identified a number of questionable payments. The happy clerk received a bonus scaled to recoveries!

The Accounts Payable clerk subsequently trained the Accounts Payable department to conduct "self audits". The AP department now audits their own work, and identifies errors and irregularities before they reach Internal Audit.

If any of your clients have high numbers of purchase transactions, you should consider proposing a "Duplicate Payments" review. If your review results in significant findings, consider adopting this user's plan - train your client's staff to use IDEA to build an internal system of continuous monitoring.

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