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SPECIAL REPORT NO 28

PAYMENT OF ACCOUNTS IN GOVERNMENT AGENCIES

No. 4 of 1998 – November 1998

Presented to both Houses of Parliament in accordance with the provisions of Section 57 of the Financial Management and Audit Act 1990

By Authority:

G Priestley, Government Printer, Tasmania

6 November 1998

President
Legislative Council
HOBART

Speaker
House of Assembly
HOBART

Dear Mr President
Dear Mr Speaker

PERFORMANCE AUDIT NO 28 - PAYMENT OF ACCOUNTS IN GOVERNMENT AGENCIES

This report has been prepared consequent to examinations conducted under section 44 of the Financial Management and Audit Act 1990, for submission to Parliament under the provisions of section 57 of the Act.

Performance audits seek to provide Parliament with assessments of the effectiveness and efficiency of public sector programs and activities, thereby identifying opportunities for improved performance.

The information provided through this approach will, I am sure, assist Parliament in better evaluating agency performance and enhance Parliamentary decision making to the benefit of all Tasmanians.

Yours sincerely

A J McHugh
AUDITOR-GENERAL

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LIST OF ACRONYMS AND ABBREVIATIONS

ANAO	Australian National Audit Office
DCHS	Department of Community and Health Services (now Department of Health and Human Services)
DELM	Department of Environment and Land Management (now part of the Department of Primary Industries, Water and Environment)
DETCCD	Department of Education, Training, Community and Cultural Development (now the Department of Education)
DOJ	Department of Justice (now Department of Justice and Industrial Relations)
DOT	Department of Transport (now part of the Department of Infrastructure, Energy and Resources
DPAC	Department of Premier and Cabinet
DPIF	Department of Primary Industry and Fisheries (now part of the Department of Primary Industries, Water and Environment)
EDI	Electronic data interchange/interface
EFT	Electronic funds transfer
FTE	Full-time equivalent
FMAA	*Financial Management and Audit Act 1990*
GBE	Government Business Enterprise
GRN	Goods received notice
PI	Performance indicator
Police	Department of Police and Public Safety (now Department of Police)
TASINET	TASmanian (Government) Internal (telephone) NETwork
TDR	Tasmania Development and Resources (now part of the Department of State Development)
TGC	Tasmanian Government Credit card
TI	Treasurer’s Instruction
Treasury	Department of Treasury and Finance

LIST OF NEW AND FORMER STATE GOVERNMENT DEPARTMENTS

On 18 September 1998 the *Tasmanian State Service (Restructuring) Order (No. 2) 1998* came into effect, which amalgamated some agencies, and changed names of others as follows:

Old Agency	New Agency
Department of Community and Health Services	Department of Health and Human Services
Department of Education, Training, Community and Cultural Development	Department of Education
Department of Environment and Land Management	Department of Primary Industries, Water and Environment
Department of Police and Public Safety	Department of Police
Department of Premier and Cabinet	Department of Premier and Cabinet (no change)
Department of Primary Industry	Department of Primary Industries, Water and Environment
Department of Justice	Department of Justice and Industrial Relations
Department of Transport	Department of Infrastructure, Energy and Resources
Tasmania Development and Resources	Department of State Development
Tourism Tasmania	Department of State Development

INTRODUCTION

Under the provisions of section 44(b) of the *Financial Management and Audit Act 1990* the Auditor-General may

> "carry out examinations of the economy, efficiency and effectiveness of Government departments, public bodies or parts of Government departments or public bodies"

The conduct of such audits is often referred to as performance auditing.

This report relates to a performance audit carried out by the Tasmanian Audit Office during the period May to September 1998 of agencies' payment of accounts systems.

As part of a broader public sector reform trend to improve efficiency, effectiveness and economy as well as the decentralisation and delegation of financial management from the Department of Treasury and Finance, agencies have implemented their own financial management ledger systems as well as re-engineer their processes in this area.

To this end significant improvements in the payment of accounts process have occurred over the past ten years, combined with the increased use of technology in daily operations, such as electronic transfers of funds and 'just-in-time' stock re-ordering.

With such advances having been made, the Audit Office considered that this was an appropriate time to review the payment of accounts processes at Government agencies. The primary objectives of the audit were to assess the management and administration of the payment of accounts function, and to identify, develop and report better practices to promote overall improvements in this area.

This report presents the results from the performance audit as well as providing examples of better practice.

AUDIT OPINION

Report Title	Payment of Accounts at Government Agencies
Nature of the Audit	The objectives of this performance audit were to assess the management and administration of the payment of accounts function, and to identify, develop and report better practices to promote overall improvements in this area.
Responsible Party	The Head of Agency is charged with the responsibility to establish policies in relation to internal control which address the objectives of effectiveness and efficiency of operations, including those which relate to the payment of accounts, and ensuring that expenditure by the Agency is authorised and bona fide.
Mandate	This audit has been carried out under the provisions of Section 44(b) of the *Financial Management and Audit Act 1990* which provides that: *"The Auditor-General may carry out examinations of the economy, efficiency and effectiveness of Government departments, public bodies or parts of Government department or public bodies."*
Applicable Standards	This audit has been performed in accordance with Australian Auditing Standard AUS 806 "Performance Auditing" which states that: *"The objective of a performance audit is to enable the auditor to express an opinion whether, in all material respects, all or part of an entity's activities have been carried out economically*, *and/or efficiently and/or effectively."*
Limitation on Audit Assurance	Audit procedures were restricted to a review of documentary evidence provided by the survey approach adopted in conducting the audit, analytical procedures, and testing of a limited number of transactions at each agency. This provides less evidence than would be available by applying more extensive and comprehensive procedures. The evidence provided by these procedures restricts the audit assurance to a moderate level, as the evidence is persuasive rather than conclusive in nature.
Audit Criteria	The assessment of agencies' management and administration of the payment of accounts function was determined under the following categories: ▪ *Degree of integration of the creditors and general ledger systems;* ▪ *Electronic commerce usage;* ▪ *Cash management payment policies;* ▪ *Establishment and use of performance indicators to determine the efficiency and economy of processes/resources used; and* ▪ *Existence of key internal and management controls.*

Conclusions

Based on the evidence collected, I conclude that:

- There is a satisfactory degree of integration of the creditors and general ledger;
- Agencies are still in the process of increasing efficiency through the adoption of electronic commerce, due to the variation among agencies in using electronic funds transfers compared to cheques in paying accounts;
- Improvements in cash management aspects of the payment of accounts are possible at several agencies;
- Only two agencies currently have performance reporting systems in place for accounts payable processes; and
- With minor exceptions, satisfactory controls over the payment of accounts process were in place at all agencies.

SUMMARY OF AUDIT RECOMMENDATIONS

Where agencies charge other agencies on a 'user pays' basis, the Audit Office encourages compliance with the Guidelines issued under Treasurer's Instructions on cash management by adopting a commercial approach to receivables collection.

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Agencies should address delays in processing payments brought about by late forwarding of authorised invoices by increasing awareness of the importance of cash management to officers in non-finance areas.

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Agency management should carry out a cost benefit analysis to determine whether efficiency gains are possible if payments were to be logged on the payments/purchasing system to ensure payment within the terms of trade, as well as the ability to take a discount if applicable.

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The Audit Office considers that agencies should investigate whether efficiency gains can be made by enhancing the automated payment of accounts.

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Agencies should monitor and report on performance indicators as an aid to identifying further areas for improvement, and thus increase the efficiency of processing accounts payable.

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AUDIT OBJECTIVES, APPROACH AND COST

Audit Objectives

The objectives of the performance audit were twofold: firstly within each agency we assessed the management and administration of the payment of accounts function with regard to the following criteria:

- Degree of integration of the creditors and general ledger systems;
- Electronic commerce usage;
- Cash management payment policies;
- Establishment and use of performance indicators to determine the efficiency and economy of processes/resources used; and
- Existence of key internal and management controls.

Secondly we wished to identify, develop and report better practices to promote overall improvements in public sector management in regard to the above areas.

Scope of the Audit

The scope of the audit was restricted to an examination of the payments of accounts processes, and cash management practices as they applied to the payment of accounts for goods and services. Thus the Audit Office did not examine procurement and purchasing practices or salary payments. As well, while there was a review of the impact of the introduction of the Tasmanian Government credit card on the payment function, the Audit Office did not examine other aspects of controls surrounding credit card transactions.

The audit focused primarily on the following topics:

- Cash management policies and practices for payments;
- Degree of risk management and key controls present over the payment of accounts process;
- Maximisation of information technology in payments processing to ensure value for money; and
- The use of performance indicators by management to monitor and improve accounts payable processes.

As part of the testing, the Audit Office examined transactions for the 1997-98 financial year.

The following agencies, as they existed at that time, were reviewed during the audit:

- Department of Community and Health Services
- Department of Education, Training, Community and Cultural Development
- Department of Environment and Land Management
- Department of Justice
- Department of Police and Public Safety
- Department of Premier and Cabinet
- Department of Primary Industry and Fisheries
- Department of Transport

- Department of Treasury and Finance
- Tasmania Development and Resources
- Tourism Tasmania

Audit Methodology

The following methods were used during the course of the audit to gather evidence from which conclusions were drawn:

- Discussion with managers responsible for accounts payable operations at each agency in regard to the overall functioning of the area;
- Detailed testing of 80 transactions to establish adequacy of controls in place, whether payments were within terms of trade, and to ascertain the manner of payment (electronic transfer versus cheque);
- Perusal of departmental accounting policy documentation;
- Comparison of management of the payment of accounts processes at each agency with Treasury guidelines, Treasurer's Instruction's, Agency's own policies, as well as the Australian National Audit Office's Better Practice Guide; and
- Perusal of any performance indicators used and verification of a portion of underlying data.

Audit Resources and Timing

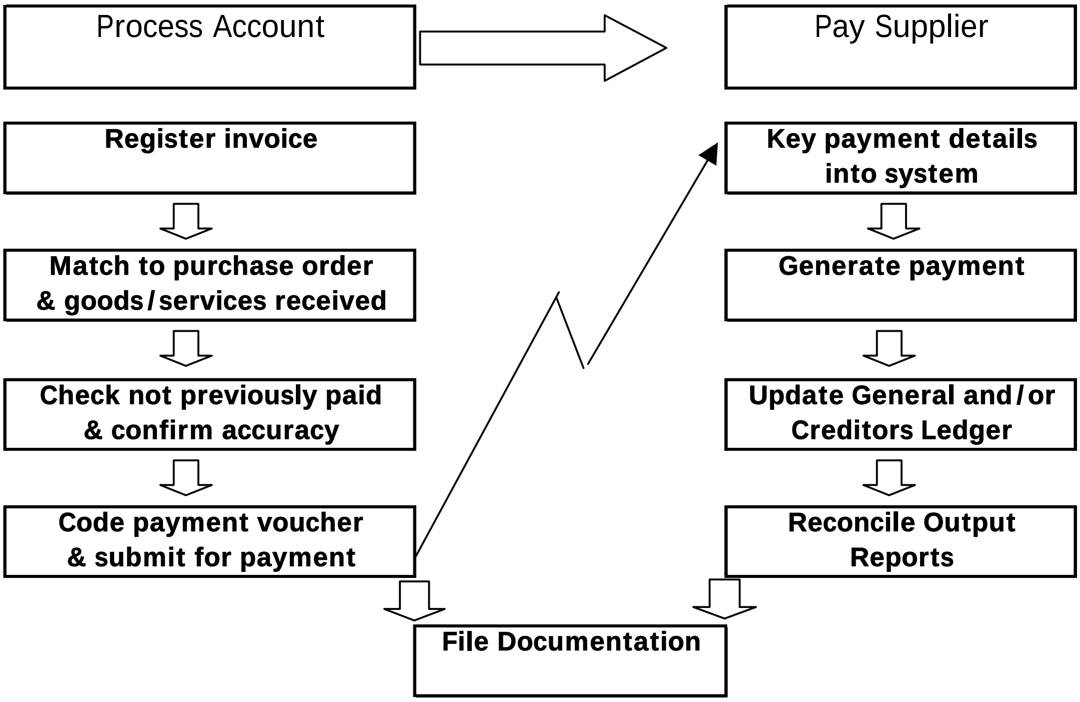
Planning for the performance audit commenced in April 1998. Testing at Agencies occurred in May through July 1998. The report was finalised in September 1998.

The total cost of the audit, including the cost of Tasmanian Audit Office staff is estimated as $25,000.

BACKGROUND

The Payment of Accounts Process

Traditionally, processing accounts to be paid comprised several steps, as outlined below. It commences with the receipt of an invoice and concludes upon payment to the supplier. However, with increasing computerisation of the accounting function in both the public and private sectors, these steps have become more automated, allowing staff to spend their time value-adding to the process and thus improving efficiency, effectiveness and economy as set out in the diagram below[1].



Importance of the Payment of Accounts System to Cash Management

Cash management involves the handling of receipts and payments in regard to the manner and timing of related transactions. Ultimately, good cash management can assist Treasury in minimising the Government's net cost of borrowing through improved timing of cash flows and management of cash balances[2].

In regard to disbursements of cash, good management of the payments of accounts system could include the following elements:

- Purchase supplies or services later without jeopardising agency objectives;

[1] ANAO. 1996b, p 3.

[2] ANAO. 1994, p 1.

- Negotiate more favourable purchase terms;
- Reduce inventory held; and
- Pay invoices only when they are due[3].

As well, in a small economy such as Tasmania's, late payment of creditors can have a profound effect on local small businesses, who in turn depend upon prompt payment by their creditors to enable them to continue operating soundly.

This audit only examined the payment of invoices aspect of the above elements.

Increased Devolution from Treasury to Agencies

A key aspect of the Department of Treasury and Finance's (Treasury) Financial Management Reform Strategy is the need for improved accountability for the use of scarce resources and the provision of better value for money in the delivery of services, by drawing on commercial best practice[4]. Consistent with contemporary management techniques, one way of achieving improvements in financial management has been by decentralising and delegating responsibility for managing payment processes to agencies, with Treasury continuing to manage the Government's overall cash resources.

Accordingly, from 1 July 1996 agencies have managed their own operating accounts and general ledger systems. Mandatory cash data is electronically transferred overnight to Treasury to replenish agencies' bank accounts.

With this framework in place, Treasury issued its *Guidelines for Effective Cash Management in Agencies* in May 1997. The Guidelines include recommendations in relation to the payment of accounts which are detailed later in this report.

Previous Reviews and Audits

In the Tasmanian Audit Office's No 1 Report of 1997, *Public Account 1996-97,* it was reported that the Department of Community and Health Services was able to spend within its cash budget due to, *inter alia*, considerable delays in payment of creditors by the former Regional Health Boards. As at 30 June 1997 out of a total $26.6M owing to creditors by DCHS (including debts assumed from the former Boards), some $6.8M had been owing for more than 60 days.

The Australian National Audit Office has also carried out reviews of cash management and payment of accounts practices, including two reports titled *Cash Management in Commonwealth Government Departments* published in 1993 and 1994, as well as its 1996 report *Payment of Accounts* and an accompanying Better Practice Guide.

Improvements in Processing of Transactions Efficiently with EFT

Besides the computerisation of the payment of accounts system, other enhancements available to agencies to enable further efficiencies and economies is the use of electronic funds transfer (EFT) instead of payment by printed cheque, and electronic data interchange (EDI) with suppliers.

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[3] ANAO. 1994, pp 1-2.

[4] Department of Treasury and Finance. 1997b, p 16.

Commencement of the Use of the Tasmanian Government Credit Card

Another facet of Treasury's Financial Management Reform Strategy has been the introduction of corporate credit cards for low value purchases, excluding hospitality and fuel purchases. Use of a card enables significant efficiencies through the rationalisation of ordering, authorisation, reconciliation and creditor payments procedures. To date the majority of agencies have implemented the cards, although to varying degrees[5].

[5] Department of Treasury and Finance. 1997b, pp 35-36.

FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

Accounting Policies for Payment of Accounts

The advantages of having written accounting policies are to ensure standardisation of the approach taken in paying accounts, as well as provide an environment for comparable data which management can review in order to monitor performance.

Treasurer's Instruction (TI) 302(2) requires Heads of Agencies to include policies on the following matters in their accounting manuals:

- Reliability and integrity of information;
- Effectiveness and efficiency of operation;
- Preventing error and fraud in the financial transactions; and
- Ensuring that expenditure by the agency is authorised and bona fide.

In their *Guidelines for Effective Cash Management in Agencies*, Treasury also encourages agencies to apply the following guidelines systematically to their payment of accounts processes:

- Take discounts wherever a net advantage exists;
- Pay invoices within terms of trade;
- Negotiate more favourable purchase terms;
- Just in time purchase of supplies;
- Prescheduled payments of funds/grants to external organisations;
- Effective use of the Tasmanian Government Credit Card;
- Maximum use of electronic payment methods; and
- Integrated financial systems[6].

Testing Performed

As part of this audit, the Audit Office ascertained whether agencies had in place policies regarding the following aspects of the payment of accounts:

- ***Payment by due date:*** Is there a policy to pay creditors within the terms of trade, or is the payment of accounts driven by batch processing efficiencies?
- ***Maximisation of discounts:*** Are there special processes in place to ensure that accounts which offer discounts are 'fast-tracked' or specially noted to maximise savings? Depending upon economies of scale, such processes may be less cost efficient compared to batch processing advantages.
- ***EDI/EFT usage:*** Do agencies have policies in place to maximise use of EDI and/or EFT? Such policies would comprise circularisation of creditors to obtain bank account details so that a direct transfer can be made, and form design of grantee applications to capture such data.

[6] Department of Treasury and Finance. 1997a, pp 4-6.

- ***Petty cash:*** Are there established thresholds in place to ensure that petty cash floats are not used as advance accounts?
- ***Use of credit cards:*** In addition to agreements made with the credit card supplier, are there any additional guidelines set up by agencies to clarify instances where credit cards are to be used?
- ***Cash management:*** What procedures are in place to ensure that creditors are not paid unduly early?
- ***Risk management in verification of payments:*** Has there been any predetermined threshold established below which a higher level of risk is accepted, such as particular types of payments or monetary values? Alternatively a policy of zero risk may have been established.

Findings

In regard to ascertaining what accounting policies agencies had in place regarding the payment of accounts process, discussions were held with finance officers and accounting manuals were perused. The results are set out in Table 2.1 below.

Table 2.1: Agencies' Policies Regarding Payment of Accounts

Policy	DPAC	DoJ	Tourism	DELM	Treasury	DPIF	Police	DCHS	DETCCD	TDR	DoT
Due date	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Discounts	✓	✓	✓	✓	⁕	✓	✓	✓	✓	✓	✓
EDI/EFT	✓	✓	✓	✓	✓	✓	✓	☼	✓	✓	✓
Petty cash	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Credit cards	✓	✓	✓	✓	✓	✓	✓	❊	✓	✓	✓
Cash management	✓	✓	✓	✓	✓	✓	✓	✓	✓	✗	✓
Risk management	✓	✗	✓	✓	✓	✓	✓	✗	✓	✓	✓

Notes:

✓ Policy is in place

✗ Policy is not in place

❊ Not applicable—agency does not yet use credit cards

☼ Not applicable—the aging accounting system used by the Launceston General Hospital is not capable of making EFT payments. However, the accounting for all three major hospital systems is to migrate to the Finance One Statewide Financial System. Finance One presently processes payments for about 14,000 creditors with 52% being made by EFT.

⁕ Minimal discounts apply to agency, but they are taken where possible; there is no established policy per se.

As the table shows, for all agencies, the Audit Office found that satisfactory policies were in place regarding the payment of accounts processes with only a few exceptions.

Buyer / Supplier Relationships

As noted earlier in this report, Treasury encourages agencies to establish relationships with their suppliers in order to generate greater savings. The prime example found was agencies' travel agreements with either airlines or travel agents.

Another efficiency identified was at DCHS. A cooperative arrangement between Royal Hobart Hospital (RHH) and FH Faulding Pty Ltd (Fauldings), whereby Fauldings maintains an off-site store. This has saved the building of a new store and provided a one-off saving in stock levels.

Conclusion

Results for this area were satisfactory.

Testing of Policies

Testing was carried out to verify whether the above policies were operative in relation to the following areas:

- Payment by due date; (see pp 25)
- Maximisation of discounts; (see p 26)
- EDI/EFT usage; (see pp 28)
- Cash management with respect to payment of accounts; (see p 24) and
- Use of Tasmanian Government Credit Card (see p 29).

Results from Audit Office testing are summarised later in this report.

Core System Controls

What Are They?

In relation to the payment of accounts, the degree of validation and verification applied to each payment should be balanced with risk management principles.

The areas examined in this audit included the following:

- *Integration of creditors and general ledger*—this ensures that all changes made in one ledger are reflected in the other, such as raising an invoice or paying a statement.
- *Reports of rejected and suspended items are regularly produced and actioned*—the presence of such a control means that all payments, orders and invoices are recorded, ultimately ensuring accurate totals for all related items in the agency's financial statements.
- *A regular analysis of the age and amount of creditors occurs*—this control enables management to monitor the timeliness of payments made.
- *Existence of validation checks prior to approval for payment*—such a control includes checks of documentation attached to the invoice, authorisation for payment from the originating section, and ensuring that the information stated on the invoice matches the original order or contract.

Treasurer's Instruction (TI) 302(1) sets out Government policy in relation to risk management and internal control, which applies to agencies' payment of accounts processes:

> When specifying procedures, processes and practices in Agency Accounting Manuals, Head of Agencies are to exercise effective risk management which involves reducing the potential for loss through the implementation of adequate preventative measures while providing scope for improved resource management strategies.

Findings at agencies

Integration of creditors and general ledger

All agencies had integrated creditors and general ledgers.

Reports of rejected and suspended items

In regard to rejected and suspended items, there was a variety of approaches taken to implementing this control. Some agencies relied upon a control in their ledger which did not process a batch unless it balanced. This forces the accounts officer to immediately follow up any rejected and suspended items. Other agencies produced reports containing rejected and suspended items each month, and followed up such items then. One agency had a system which suspended all batches entered in a session until a second (independent) officer reviewed the batches and then processed them.

Validation checks prior to payment

All agencies had controls in place during the year which checked documentation, authorisation and agreement to purchase order prior to certification and processing.

Analysis of the age and amount of creditors

There was considerable variance in regard to creditor analysis. During the period examined, the Department of Transport was paying its creditors as invoices were presented to the Finance section for processing; accordingly, there were no outstanding creditors to verify. However, from 1 July 1998 the agency has begun logging payments by due date onto its ledger to ensure better cash management, and a monthly report detailing outstanding creditors for longer than 60 days will be reconciled and actioned.

Analysis of outstanding payments was found to be carried out at least once a year at the Departments of Justice, Primary Industry and Fisheries, Police and Public Safety, Education Training Community and Cultural Development, Tourism Tasmania and Tasmania Development and Resources.

Similar to Transport, the Departments of Premier and Cabinet and Environment and Land Management do not carry out any creditor analysis, as they both pay outstanding invoices as they are received by their Finance sections.

The Department of Treasury and Finance relies upon a review of expenditure from its management reports for this control. Treasury stated that a reconciliation of the control account to the subsidiary creditors ledger will be undertaken monthly in line with other balance sheet information, and a review of the outstanding amounts in the creditor subsidiary ledger will be undertaken monthly by the Accountant. A review of old and unused creditor accounts will be followed up in September 1998 and then annually.

At DCHS, it was found from the testing of the Hospitals and Ambulance Division in Launceston that while an 'Accrual Journals Unmatched Goods Received Notice' (GRN) report is produced by the ledger each month, it is not actioned. As well, according to DCHS the general ledger system used by the three Tasmanian public hospitals is not capable of deleting obsolete goods received notices automatically. This is a manual task which is resource-intensive and has not been undertaken since December 1997. DCHS stated that the report will be reviewed immediately and any backlog of obsolete GRNs will be deleted as soon as possible. Action will also be taken on a monthly basis in respect of any older invoices appearing on the Creditors' Trial Balance Report.

For the DCHS creditors paid through Finance One aging and payment of creditors is a system parameter. The system calculates the payment date, based on invoice date, and the number of days before payment is due, i.e., 7, 14, 30 or 45.

Conclusion

Satisfactory controls were in place at all other agencies and in DCHS' Corporate Office for core controls, with the exception of DCHS' lack of creditor analysis in Launceston.

Cash Management Controls

The *Guidelines for Effective Cash Management in Agencies* issued under Treasurer's Instructions encourages agencies to take advantage of discounts for early payment where offered by the supplier. The Audit Office considers that ideally, in these circumstances payment should be made toward the end of the discount period, i.e. not paid too early, for cash management purposes.

While no standard terms of trade apply to all government purchases, the *Guidelines* recommend that payment be made within the supplier's terms. If no term is specified 'the account should generally be paid at 30 days'[7] (i.e. within 30 days of the receipt of the goods or services supplied). In the long term paying accounts on a timely basis provides an ability for an agency to negotiate more favourable terms of trade. Treasury supports the notion of agencies' pro-actively developing closer relationships with their suppliers, and the formation of strategic alliances or partnerships is also included in the ANAO's *Better Practice Guide*[8].

Interest Charged on Inter-Agency Accounts

Paragraph 4.3 of the *Guidelines for Effective Cash Management in Agencies* encourages agencies to adopt a commercial approach to revenue collection by charging interest on overdue accounts, provided that debtors are made aware of such charges beforehand.

TI 515(2) specifically addresses agencies which charge interest on overdue accounts from other agencies:

> In circumstances where inter-agency charging occurs (i.e. user pays), and agencies charge interest on overdue accounts, such interest is payable in accordance with the terms specified....

Although the charging of interest on overdue accounts is a revenue collection issue, the matter was examined during this audit to ascertain the level to which this TI was being complied with by both examination of any inter-agency creditors in the transactions selected as well as discussions with each agency's finance officers to ascertain their own policies on charging other debtor agencies.

The charging of interest on inter-agency debts is considered to have the effect of encouraging the debtor agency to pay such invoices within terms of trade, instead of seemingly giving priority to 'external', that is non-agency, creditors. Two groups of 40 transactions for the 1997-98 financial year were examined for each agency to determine whether interest was being charged.

Findings at agencies

Overall, the Audit Office found that only three agencies charge interest on overdue inter-agency accounts. These included the Departments of Premier and Cabinet (for TASINET/Technology Management Division charges), Treasury (for all inter-agency charges), and Primary Industry and Fisheries (all charges).

The Audit Office noted that one significant inter-agency creditor, the Department of Environment and Land Management, which charges all agencies rent for premises, does not charge interest on overdue accounts. The agency has stated that this area will be reviewed

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[7] Department of Treasury and Finance. 1997a, p 4.

[8] ANAO. 1996b, pp 5-6.

as part of the business process review to be undertaken as part of the Prophecy (general ledger) Open implementation.

It should be noted that not all agencies will have the occasion to charge other agencies for services in a user pays environment, due to the nature of each agency's individual core business.

Recommendation

Where agencies charge other agencies on a user pays basis, the Audit Office encourages compliance with Treasury's Guideline on cash management by adopting a commercial approach to receivables collection.

Timeliness of Payments

As described earlier in this report, cash management controls of the payment of accounts should address three issues: not paying accounts unduly early, nor outside of the terms of trade, and to take advantage of discounts where possible. Two sets of 40 transactions over the 1997-98 financial year were used to review timeliness of payments. As well as being used to determine the presence of any inter-agency charging, one set of transactions was used to examine the effectiveness of any discounts taken, and the other set was tested to review the timeliness of payments of the accounts.

Unduly Early

Treasury recommends that '[w]here discounts are not available, payments should be made only when due'[9].

Some agencies pay invoices in order of receipt, instead of logging them into their ledgers by due dates to ensure that payment is made within terms of trade and any discounts offered by suppliers are taken. In a number of cases, this approach was found to have the effect of paying some suppliers unduly early, according to the results from the Audit Office's transaction sampling.

However, finance officers from these agencies considered that the efficiencies brought about through batch processing on prescheduled days (usually once a week) outweighed any cash management advantages which could apply, due to the low value of the discounts applicable and the resources required to stagger payment of invoices on various days. Agencies that adopted this approach included the Departments of Premier and Cabinet, Environment and Land Management, Transport, and Tasmania Development and Resources.

As noted above, from 1 July 1998 DOT now logs on its invoices by due date, to better manage its cash flow.

The former Department of Education, Training, Community and Cultural Development (DETCCD) has an arrangement to pay certain suppliers early in order to retain good relationships with them.

Late Payment

Treasury recommends payment of all accounts within the terms of trade specified by the supplier, and at 30 days where no terms are specified[10].

[9] Department of Treasury and Finance. 1997a, p 4.

[10] Department of Treasury and Finance. 1997a, p 4.

For all agencies except DCHS, a number of payments were found to have been paid late due to the finance sections receiving the invoice concerned late from the officer in the operational area who had approved it for payment. This was seen as a major gap in the efficient processing of payments.

In regard to DCHS, the Audit Office understands that for smaller suppliers a maximum of 30 days for default terms of trade, and for larger creditors a period of 45 days is used. However, even with a longer period of time, the Audit Office still found 8 payments made in excess of 45 days. However the agency considers that this is due to situations where a goods received notice has been raised prior to the receipt of an invoice, thus creating a delay longer than 30 days between receipt of goods and payment of the supplier.

As noted above, the selected transactions were taken from the 1997-98 financial year. However, over the last two months of the financial year DCHS introduced a creditor policy which took place from 1 July 1998.

As Treasury notes in its guidelines, although it may appear to an agency that a benefit is gained by paying its creditors late[11], in the longer term such an approach can cause commercial relations between the supplier and the agency to deteriorate, as well as affect the supplier's cash flow, particularly small businesses. Conversely, timely payment of invoices enables an agency to develop strategic alliances with suppliers with a view to being able to negotiate more favourable terms of trade[12].

Discounts Taken

From the Audit Office's testing at agencies for transactions which could give rise to a discount, it was noted that such transactions were rare; usually only one or two suppliers offered discounts to agencies. Where discounts were offered, however, as with normal invoices, quite often the saving was missed, due to late remission of the invoice from the operational section to the finance section. This occurred at DPAC, DELM, DPIF, Police, DCHS, DETCCD and TDR. As well, due to oversight in some instances at TDR, discounts were not claimed for a number of invoices paid within the discount period.

For agencies such as TDR which use batch processing, officers have advised the Audit Office that they consider the efficiency gains made from batch processes to outweigh the cash advantages from taking discounts in the situations the Audit Office found.

Better Practice Examples

Despite the problem at Police and DPAC with delays in receiving invoices authorised for payment, it was noted that where invoices were received within the discount period, such invoices were specifically noted to ensure payment is made within the discount period.

From the Audit Office's testing of both Treasury and Transport invoices which had discounts applicable, all were taken.

Recommendations

Agencies should address delays in processing payments brought about by late forwarding of authorised invoices by increasing awareness of the importance of cash management to officers in non-finance areas.

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[11] Department of Treasury and Finance. 1997a, p 4.

[12] Department of Treasury and Finance. 1997a, p 4.

It is considered that due to varying economies of scale at different agencies, management should carry out a cost benefit analysis to determine whether efficiency gains are possible if payments were to be logged on to the payments/purchasing system to ensure payment within the terms of trade, as well as the ability to take a discount if applicable.

Conclusion

Improvements in cash management aspects of the payment of accounts are possible at several agencies, due to delays in payment and unduly early payments.

Modes of Payment

With a view to increasing the efficiency and cost-effectiveness of payment processing, Treasury has issued both Treasurer's Instructions and Guidelines on the area of the method of payment. The Guideline issued in TI 511 encourages agencies to pay via electronic means rather than by cheque. In regard to inter-agency payments, TI 515 requires all such payments to be electronic rather than by cheque, 'unless special circumstances arise'.

Several agencies now use the Tasmanian Government Credit Card, which Treasury considers to increase efficiency by reducing paperwork. TI 520 sets out circumstances where the card can be used; this includes purchases costing less than $2,000 per transaction which do not relate to hospitality, petrol or motor oil. Cash management advantages can also be gained as there is an interest-free period of 27 to 63 days, depending on the billing cycle[13].

Efficiencies can also be gained by using electronic certification for matched purchase orders and invoices, goods received and authorised payments[14].

Findings at Agencies

Usage of direct credits, EFT and EDI vs cheques

To gauge the extent of electronic funds transfers (EFT), the Audit Office selected transactions over the 1997-98 financial year and compared EFT payments to cheque payments.

Based on the Audit Office's testing results, use of EFT varied considerably between agencies:

Table 5.1: Use of EFT in proportion to total payments made for 1997-98

Agency	EFT Proportion
Tourism Tasmania	97%
Primary Industry and Fisheries	90%
Education, Training, Community and Cultural Development	90%
Justice	65%
Transport	63%
Treasury and Finance	47%
Environment and Land Management	45%
Tasmania Development and Resources	39%
Police and Public Safety	38%
Community and Health Services*	N/A
Premier and Cabinet	0%

* *Testing was carried out at the Hospitals and Ambulance Service Division of DCHS located in Launceston. As indicated earlier, DCHS stated that it cannot make EFT payments through the Homer system used in hospitals, but 52% of creditors paid through the Finance One system are by EFT.*

For those agencies with less than less than 60% EFT usage, discussions with finance officers confirmed that low usage was due to few direct payment details for creditors being available when their general ledger systems were first implemented.

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[13] Department of Treasury and Finance. 1997a, p 5.

[14] Department of Treasury and Finance. 1997a, p 6; ANAO 1996b, pp 7-8.

There were no inter-agency payments present in the transactions selected for this procedure, so the Audit Office could not draw any conclusions in relation to whether agencies are complying with that particular TI.

TDR is currently implementing changes to its grants processing which should increase EFT payments by 50% over the next 12 months. TDR has estimated that its current proportion of EFT payments is approximately 45.5%, excluding grant payments.

Better Practice Examples

Overall, those agencies with the highest rates of electronic payment versus cheques have brought this about by frequent circularisation of direct payment detail requests for their creditors, as well as re-engineering their processes. It is understood that Transport now has a policy to request direct payment details from all new creditors.

In addition to EFT, the Audit Office notes that Treasury used electronic data interface (EDI) to pay Telstra and TASINET (TASmanian Govt Internal telephone NETwork) invoices.

Impact of the Tasmanian Government Credit Card

All agencies except DCHS use the American Express Tasmanian Government Credit Card (TGC). The agencies that do use TGC have only done so since 1997-98; accordingly the impact of TGC transactions compared to EFT and cheques has varied between agencies as their officers are still in the process of increasing card use. For example, DELM charged only $4486 on the TGC in July 1997, but by April 1998 the monthly charge had increased to $28,550. As set out in the table below, there has been an increasing trend to use TGC for paying accounts.

Table 5.2: Agencies' Monthly Expenditure via TGC

Agency	**As at February 1998 $**	**As at June 1998 $**
Tourism Tasmania	7,131	16,807
Primary Industry and Fisheries	18,186	16,928
Education, Training, Community and Cultural Development	43,800	47,473
Justice	6,484	9,014
Transport	6,909	9,393
Treasury and Finance	6,750	12,890
Environment and Land Management	10,734	29,061
Tasmania Development and Resources	11,138	54,653
Police and Public Safety	2,130	661
Community and Health Services*	N/A*	N/A*
Premier and Cabinet	212	2,409
TOTAL	**115,472**	**199,289**

* DCHS was not using the TGC during the 1997-98 year.

The Audit Office considers that in regard to those agencies using the TGC, efficiencies in transaction processing are being brought about through steadily increased card use, together with increased use of EFT instead of payments by cheque. A quantified example of such efficiency was the reduction in accounts processing resources by 1 FTE at TDR.

DPIF, DETCCD and DELM considered that they had also experienced increased efficiencies, which had not been quantified; these included the savings in time and resources in having cheque runs, and carrying out reconciliations of unpresented cheques.

However, Police believes that since it has been contracting out cheque printing and using technology as an integral part of its payment of accounts processes, there have been minimal efficiencies gained over the past few years.

System Capabilities/Automated Functions

The highest levels of automated processing of payments were found at DPIF, DCHS, DETCCD, Transport and Tourism Tasmania. Remaining agencies had not purchased the corresponding module of which would integrate payments and purchases processing. At Treasury, a total review of its accounts payable/receivable procedures is currently under way, and this has resulted in some procedural changes being implemented to date and may also result in further operational changes occurring.

Recommendation

The Audit Office considers that agencies should investigate whether efficiency gains can be made by enhancing the automated payment of accounts.

Conclusion

Overall, it is considered that agencies are still in the process of increasing efficiency through transaction processing of accounts payable. This is evident in the variation of EFT used compared to cheques, automation of the certification process, and use of the TGC.

Performance Management

Treasury recommends the use of performance indicators (PIs) to monitor effective cash management within agencies[15]. Besides allowing management the opportunity to gauge progress over a period of time, a well-rounded PI suite can also enable agencies to benchmark between themselves and other sectors. Examples of suggested performance indicators for the payment of accounts system as set out in *ANAO's Paying Accounts—Better Practice Guide* have been reproduced in an appendix to this report.

Findings at Agencies

Use of Benchmarks/Better Practice Examples

From the Audit Office's discussion with finance officers and perusal of documentation, it was found that only two agencies, Treasury and Transport, use PIs.

Treasury uses the following PIs:

- Payment performance against due date;
- Average cost per payment;
- Number of invoices processed;
- Number of errors detected (such as incorrect payments, double payments); and
- Number of key strokes (wrong cost code entered).

The indicators are collated on a quarterly basis, and have critical variance points that trigger follow-up action to be undertaken by the finance section.

Transport has been participating in Austroads Corporate Activities Benchmarking Project with other State transport agencies for the past three years. The project concerns various aspects of finance activities, including the following components of the payment of accounts system:

- Number of transactions;
- Total cost of accounts payable administration;
- Cost per transaction;
- FTEs for payment of accounts;
- Transactions per FTE;
- % EFT payments; and
- Credit cards issued to agency officers.

Indicators are collected by each agency and forwarded to Austroads for collation and cross-agency analysis.

Reporting progress/Better Practice Examples

As only two agencies currently collect information on PIs, this aspect of performance management applied solely to them.

[15] Department of Treasury and Finance. 1997a, p 9.

At Treasury, PIs are reported to the Executive, Corporate Management Group and to the Quality Assurance Committee on a quarterly basis. The reports compare PI results to the targets, with explanations provided for material variances. Critical action points have been set for a 1% variance from the target. The reports also outline current strategies in place to increase quality and efficiency in the payment processing function.

To date, Treasury's performance management system has already resulted in changes in its payment of accounts system to improve efficiency, such as the use of a single order book.

Transport distributes results from benchmarking to all Finance and Facilities staff along with the agency's business plans. Reporting is also carried out by Austroads to all other agencies. Transport considers that participation in the benchmarking project has lead to increased efficiencies in its processing of the payment of accounts.

DCHS is working towards the introduction of key performance indicators across the Agency, including the Finance Branch.

Recommendation

Agencies which do not currently monitor and report upon performance indicators should consider doing so, as PIs provide an effective method to increasing efficiency of payment of accounts processing.

Conclusion

As only two agencies currently have performance reporting systems for accounts payable processes, it is considered that further improvements in this area are possible for all other agencies.

This is consistent with the Audit Office's findings in relation to overall PI collection and reporting by agencies as set out in the Audit Office's 1997 Special Report Number 24, *Further Review of Performance Indicators in Government Departments*. In that report the Audit Office found that the majority of agencies did not yet have mature systems of performance monitoring[16].

[16] Tasmanian Audit Office. 1997, p 30.

Overall Conclusion

The Audit Office found a variety of results across the areas covered in this performance audit. Overall it is considered that with the recent decentralisation and delegation of the area of payment of accounts to agencies from Treasury, considerable progress has been made by individual agencies to bring about the efficient, effective and economical payment of accounts, but there is room for improvement in varying degrees across agencies, and they have acknowledged this.

As all agencies had fully integrated creditors and general ledger systems, this criteria was found to have been fulfilled.

In regard to key internal and management controls relating to payment of accounts system, most agencies had policies in place over all of the areas examined. Exceptions were that Justice did not have a risk management policy in place and TDR lacked a cash management policy.

For accounts paid through the hospitals' Homer system because of the time-consuming manual work involved, creditor analysis at DCHS in Launceston was in arrears. It is, however, in place for accounts paid through the Finance One system of DCHS. As indicated in the body of the report, the Homer accounting functions are to be migrated to the Finance One system. Satisfactory core controls were found to be in place at all other agencies, based upon the results of the Audit Office's transaction sampling.

As the Audit Office found some delays in the payment of creditors and instances of unduly early payments at several agencies, it is considered that improvements in cash management aspects of paying accounts are possible at a number of agencies.

In regard to electronic commerce usage, the Audit Office found that agencies are currently increasing efficiency through in their accounts payable processes, as shown by the variation of EFT used compared to cheques, credit card usage and automated certification of payments.

Only two agencies currently have performance reporting systems in place for accounts payable processes.

APPENDIX: SUGGESTED PEFORMANCE INDICATORS

In its publication *Paying Accounts – Better Practice Guide*[*], the Australian National Audit Office sets out the following suggestions for performance indicators to enable management to monitor the payment of accounts process:

Efficiency Indicators

- Total accounts payable full-time equivalent (FTE) staff resources;
- Invoices processed annually per accounts payable FTE;
- Accounts payable staff cost per invoice;
- Total processing cost per invoice; and
- Cost of accounts payable to total administrative costs.

Effectiveness Indicators

- Number of active suppliers;
- Percentage of payments made by EDI/EFT;
- Percentage of payments by direct credit;
- Cycle time to schedule a payment;
- Percentage of payments made with automated matching;
- Percentage of payments made using evaluated receipts;
- Percentage of payments made in error;
- Percentage of late payments; and
- Number of supplier-generated queries per 1000 payments.

[*] ANAO. 1996b, p 16.

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