General Ledger Accounting Procedures – Journal Voucher Review

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Introduction

The General Ledger Accounting Procedures – Journal Voucher review was included as a carry-forward project in the Office of the City Auditor's 2003 Annual Work Plan.

In 1996, the City of Edmonton's financial management and procurement systems were converted to SAP. SAP is a large integrated data processing system that provides information to support the various business processes for the City. The City of Edmonton upgraded to SAP Version 4.6 in April of 2001.

The City of Edmonton's general ledger is part of the financial accounting module of SAP R/3. The general ledger serves as a complete record of all business transactions. It is the centralized, up-to-date reference for entering and display of financial transactions conducted by the City.

Journal vouchers are normal transactions used by accountants to update the general ledger. They may be postings of original transactions to accounts or adjustments and corrections to previously recorded transactions. For example:

- Allocating a corporate expense to operational business areas for items such as desktop software contracts.
- Allocating monthly telephone or utility charges to responsible departments or branches.
- Entering payroll information generated by the City's HR system (PeopleSoft) to SAP.
- Correcting an error or adjusting a previous allocation that was disputed.
- Posting year-end adjustments to the general ledger as recommended by the External Auditors.

SAP's general ledger software allows users to review individual transactions at any time by displaying the original transaction documents (including the ID of the person who entered the transaction), detailed line items, and transaction values at various levels of detail. Effective documentation supporting the nature, extent, and timing of all journal vouchers is a critical internal control in financial accounting environments.

High-quality financial information that is relevant and useful is necessary to support effective departmental and corporate decision-making, to prepare the City's summary financial statements, and to report to Council and to the public the full cost of delivering City programs and operations. Departmental managers use this financial information in

their day-to-day management of the City's operations. Managers' involvement as reviewers of financial reports is a key control in financial accounting environments.

The SAP General Ledger has the following features:

- Financial data can be viewed at a program, department, or corporate level.
- Automatic and simultaneous updating of sub-ledgers (e.g., listing of assets, customer accounts owing, etc.) occurs in the appropriate general ledger accounts.
- Simultaneous updating of general ledger and department cost centers is conducted without user intervention.
- Real-time evaluation and additional analysis of and reporting on current accounting can be conducted on data that will be contained in the financial statements.

Journal Vouchers are a vital component of all general ledger accounting systems, providing accountants the flexibility required to account for unusual, non-recurring and non-system transactions or events. This flexibility also introduces additional risks since management's internal control systems can be circumvented using journal vouchers. Because of the manual nature of journal vouchers, accuracy and propriety risks are also increased. Proper documentation, approval, and verification of accuracy of direct general ledger postings are key controls in general ledger accounting.

Objective

The OCA's objective was to assess and test the controls surrounding the preparation and documentation of general ledger journal vouchers. Selected journal vouchers were tested for completeness, accuracy, and authorization.

Methodology and Scope

The scope of the audit included all journal voucher postings to the general ledger for the year 2001 (the last full accounting period available at the time of the data analysis). The OCA used data analysis software to extract all journal vouchers for the year. There were 22,543 journal vouchers that created 131,484 separate general ledger account postings with a total value of $7.8 Billion. This amount seems higher than expected because of the 'double entry' nature of accounting where a single item is recorded as both a positive (debit) and negative (credit) amount. In addition, a single item can be allocated or adjusted many times. Therefore a single economic event can result in cumulative transaction values significantly in excess of the actual transaction amount.

The OCA then used data analysis software to categorize all the journal vouchers created in the City's general ledger during 2001 by City departments and to summarize them according to their nature, type, purpose and magnitude. For each type of journal entry summarized, a sample was taken and provided to each of the departmental senior accountants. Each senior accountant was then asked to provide documentary and

authorization evidence to support the journal voucher entries made. During this phase, the following journal voucher entry types were identified:

- System generated journal vouchers: These are journal vouchers that are created internally by SAP.
- Recurring journal vouchers: These are typically used to allocate costs on a periodic basis.
- Reversing journal vouchers: These are journal vouchers that are used to reverse previous period estimates.
- Manual direct-entry journal vouchers: These are used when no other form of entry to the general ledger is available.

The OCA then reviewed the documentation provided by the departmental senior accountants to assess the overall propriety of the journal vouchers and whether they were properly documented and approved. Follow-up discussions were held with each of the senior accountants regarding those sample items that were not fully documented or authorized. Discussions were also held with the SAP Business System Support Team, to confirm that the SAP system configuration could be altered to accommodate additional accounting transaction types.

Observations

SAP Procedure for Journal Voucher Creation, Approval and Documentation

From a sample of 269 documents examined by the OCA, less than 50% were properly completed, authorized, and/or had sufficient documented support for the transaction amounts. Also noted were many instances where SAP information fields were either left blank or contained insufficient or incomplete information. The sample did not provide any evidence of inaccurate or improper entries. However, without proper journal voucher documentation and approval controls, errors or misstatements would be very difficult to identify. The difficulty arises because of both the sheer volume of journal vouchers and sometimes-incomplete information.

The City's accounting procedure for journal vouchers has not been updated since prior to the implementation of SAP in 1996. An SAP-specific accounting procedure is required so that business area accountants will know the nature and extent of additional documentary evidence that is required to support and supplement what is already contained in the SAP system. It will also allow for journal voucher approval to be aligned with SAP's internal user access and security system.

Recommendation 1:

That an accounting procedure be developed, communicated, and enforced to address the creation, authorization, accuracy, and support documentation requirements for SAP journal vouchers. In addition, SAP user access profiles should be reviewed/developed

for all existing and new journal voucher document types to ensure that the creation and posting functions are appropriate and consistent with proper segregation of duties.

Management Response:

Corporate Accounting, Budgets and Reporting will coordinate the development of an Accounting Procedure that will describe the requirements for creation, authorization and documentation for SAP Journal Vouchers. The procedure will provide guidance with respect to both the type and amount of information that is to be included in each SAP Document.

If new SAP journal voucher document types are developed, user access profiles will be evaluated against both existing and new journal voucher document types to ensure that appropriate segregation of duties for creation and posting functions is maintained.

SAP Document Types

Currently in SAP, journal vouchers are used to record manual direct-entry journal transactions, system-generated transactions, inter-departmental allocations, monthly recurring journal transactions and some other types of transactions and processes. As indicated above there were 22,543 journal vouchers posted in 2001. This quantity of transactions makes it difficult for business area accountants and auditors to easily distinguish between the different types of transactions flowing through their accounts. Some of these transactions require minimal monitoring (e.g., system-generated transactions), while others should be monitored regularly (e.g., manual direct-entry journal transactions). This makes the account analysis function performed by departmental accountants more difficult and less efficient than it needs to be.

Separate documents types should be developed in SAP and used to distinguish between different types of transaction sources and/or business processes. This will allow department managers and accountants to do more efficient and effective analysis of the transactions going through their accounts.

Recommendation 2:

That Corporate Services Department determine the nature and source of transactions currently recorded in SAP as a single type of journal voucher document to determine which additional document types should be developed for distinct types of business processes and/or transactions.

Management Response:

Corporate Services Department will review the nature and source of transactions currently included as SA document types to evaluate use of any additional document types to distinguish between such factors as system-generated and manual journal entries.

Conclusion

Corporate Services Department has agreed with these recommendations and has provided actions plans to address them. Implementation of Recommendation 1 is scheduled to be complete by June 30, 2004 and implementation of Recommendation 2 is scheduled to be complete by December 31, 2003. The OCA believes that the implementation plans will resolve the issues identified in this audit and will significantly enhance the overall SAP control environment at the City of Edmonton.

We would like to acknowledge the high level of cooperation and support we received from departmental and corporate accounting staff during this audit.