

The Auditor-General
Audit Report No.25 2001–2002
Assurance and Control Assessment Audit

Accounts Receivable

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Canberra ACT
11 December 2001

Dear Madam President
Dear Mr Speaker

The Australian National Audit Office has undertaken an across agency Assurance and Control Assessment audit in accordance with the authority contained in the *Auditor-General Act 1997*. I present this report of this audit, and the accompanying brochure, to the Parliament. The report is titled *Accounts Receivable*.

Following its tabling in Parliament, the report will be placed on the Australian National Audit Office's Homepage—
<http://www.anao.gov.au>.

Yours sincerely



P. J. Barrett
Auditor-General

The Honourable the President of the Senate
The Honourable the Speaker of the House of Representatives
Parliament House
Canberra ACT

AUDITING FOR AUSTRALIA

The Auditor-General is head of the Australian National Audit Office. The ANAO assists the Auditor-General to carry out his duties under the *Auditor-General Act 1997* to undertake performance audits and financial statement audits of Commonwealth public sector bodies and to provide independent reports and advice for the Parliament, the Government and the community. The aim is to improve Commonwealth public sector administration and accountability.

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Abbreviations/Glossary

ACA	Assurance and Control Assessment
Accounts Receivable	Amounts owed for goods or services provided on credit.
ANAO	Australian National Audit Office
APS	Australian Public Sector
CEO	Chief Executive Officer
CSA	Control self assessment
Debt	Another term used for accounts receivable.
FMIS	Financial management information system
Fraud control plan	A plan devised to protect the revenue, expenditure and property of an organisation from any attempt, either by members of the public, contractors, sub-contractors, agencies, intermediaries or its own employees to gain by deceit financial or other benefits. This policy is designed to protect public money and property, protect the integrity, security and reputation of our public institutions and maintain a high level of services to the community consistent with the good government of the Commonwealth.
GST	Goods and Services Tax
Internal control framework	Management's philosophy and operating style, and all the policies and procedures adopted by management to assist in achieving the entity's objectives. It comprises the interrelated components of risk assessment, control environment, control activities, monitoring and review processes, and information and communication processes.
IT	Information Technology
MAB-MIAC	Management Advisory Board—Management Improvement Advisory Committee
Other Charges	Charges for items other than the sale of goods and services.
Trade Debtor	Debtor that relates to amounts owed for the sale of goods and services.

Summary and Recommendations

Summary

Background

1. Accounts receivable make up a significant proportion of the Commonwealth's financial assets at any point in time. Accounts receivable represent highly liquid assets that have a direct impact on the Government's cashflow and financial position.

2. At 30 June 2001, total accounts receivable amounted to \$36 billion of taxes, advances and loans and other receivables owed to the Commonwealth. This Assurance and Control Assessment (ACA) audit¹ related to \$18.3 billion² of other receivables in the 'general government sector'³. The scope of the audit covered the following types of accounts receivable:

- trade debtors—charges for goods and services;
- other charges—miscellaneous charges;
- recoveries from the overpayment of benefits—the audit only included the recovery process not how it had been established that an overpayment had occurred; and
- recoveries from staff.

3. The audit was undertaken in eight Commonwealth organisations. At the time of the audit the total amount of other receivables owing to these organisations was \$44.6 million⁴.

¹ ACA audits are undertaken under the general performance audit provisions of the *Auditor-General Act 1997*. They examine common business activities and processes that are not specifically covered by financial statement or other performance audits. The report to Parliament is generally aimed at improving administration across the Commonwealth public sector. The findings of these audits are indicative, rather than representative, given the relatively small number of agencies involved.

² These amounts have been calculated from the working papers of the Consolidated Financial Statements and include balances for the Sale of Goods and Services, recoveries of benefits payments and other receivables.

³ General Government Sector is a term used in the Consolidated Financial Statements of the Commonwealth Government of Australia. It includes government organisations other than Public Trading Enterprises and Public Financial Enterprises.

⁴ This amount was calculated by totalling the receivables amounts recorded by the audited organisations in their financial records at the time of the audit.

Audit objectives

4. The objectives of the audit were to:

- assess whether the processing, collection and overall management of the accounts receivable function was being performed in accordance with applicable legislation, government policy and applicable internal controls;
- identify better practices in accounts receivable activities; and
- as necessary, recommend improvements in the controls and practices relating to accounts receivable.

Previous audit coverage

5. In 1997–98, the ANAO performed a financial control and administration audit of the *Management of Accounts Receivable*⁵ across a number of Commonwealth organisations. The main objectives of the audit were to assess the cost-effectiveness of the management and administration of the accounts receivable function in the ‘general government sector’ and to identify, develop and report better practice in the management of accounts receivable.

6. The major audit findings were that, at both the strategic and operational level, improvements could be made in the management and administration of the accounts receivable function. These findings included the following:

- The direct labour costs associated with the accounts receivable function in the Commonwealth were estimated to be significantly higher than those of the private sector.
- In most agencies managers responsible for service delivery had no responsibility for management of the debt arising from the services. This was the role of Corporate Services. It was considered that improvements could be achieved in debt management by removing this separation of responsibility.
- Some agencies had not developed written accounts receivable policies and those policies that were in place did not effectively address all aspects of the management of the function.

⁵ ANAO Audit Report No.29 1997–98, Financial Control and Administration Audit, *Management of Accounts Receivable*, Canberra.

- Agencies had not undertaken risk assessments of either their revenue collection or accounts receivable functions, and, as a result, were not in a position to manage these risks.
- Current management performance reporting mechanisms did not enable management to exercise ongoing control over the accounts receivable function.

7. The major recommendations made in the 1997–98 audit included that the management and organisational framework could be improved by:

- establishing a comprehensive and clear policy framework which has been endorsed by executive management;
- identifying, analysing and assessing risks to revenue collection;
- transferring responsibility for strategic decision making in relation to debtor management to program managers; and
- strengthening management reporting and performance measurement.

8. These findings and recommendations were taken into account in this audit.

Audit conclusion

9. The ANAO concluded that Commonwealth organisations audited were generally processing, collecting and managing the accounts receivable function in accordance with applicable legislation, Government policy and applicable internal controls. The ANAO nevertheless considered that improvements could be made to achieve more effective control in the accounts receivable function. The key areas where improvements could be made included the following:

- Specific control activities should be introduced to ensure the completeness of revenue and accounts receivable balances. In particular, controls should be established to better manage the distribution of saleable data and information external to the organisation via e-mail and the recording of related revenue and accounts receivable.
- Financial Management Information Systems (FMIS) should be used to the full extent of their capabilities to facilitate the streamlined processing of revenue and accounts receivable.
- Appropriate monitoring and review procedures should be put into place to assess ongoing performance.

10. The audit also identified examples of sound and better practices currently used by the organisations reviewed. These included:

- risk assessment processes at the strategic level being incorporated into the business planning cycle;
- comprehensive guidelines supporting the accounts receivable functions having been developed and implemented;
- invoices being processed directly from FMISs; and
- performance measures being established and regularly reported on.

11. The results of the 2001 audit are consistent with the findings of the 1997–98 audit⁶. The opportunities for improvement provided in the better practice guide⁷ published at the same time as the 1997–98 audit are still relevant.

Key findings

12. The main findings arising from the audit were as follows:

- *Risk assessment*—All organisations had completed risk assessments at the organisation level, although these were not being reviewed on a regular basis. All but one had completed fraud risk assessments and prepared fraud control plans. However, formal process level risk assessments of the accounts receivable function had only been conducted in three of the organisations reviewed noting that two other organisations considered the accounts receivable function immaterial to the organisation as a whole.
- Control environment:
 - *Process*—Organisations have developed policies and procedures to support the accounts receivable function. However, organisations need to improve both the access to, and cross-referencing of, policies and procedures. Policies and procedures were appropriately detailed and provided useful guidance for staff members.
 - *Personnel*—Organisations have appropriately qualified and trained staff to perform accounts receivable processes. Induction training programs have been implemented in all of the organisations. However, in one organisation the program was not sufficiently comprehensive to instruct staff of their responsibilities.

⁶ *ibid.*

⁷ ANAO 1997–98, Better Practice Guide *Management of Accounts Receivable*, Canberra.

- *Structure*—Responsibilities and the relevant delegations, for accounts receivable tasks, have been appropriately allocated within organisations, and have been adequately documented.
- *Technology*—General and application IT controls are generally being utilised in the majority of organisations. These controls need to be monitored to ensure that the systems and data stored in them remain secure.
- *Control activities*—Limited controls are used in three organisations to ensure that accounts receivable balances are complete. In particular, an emerging issue was identified whereby saleable data and information can be e-mailed external to an organisation without being easily detected. This requires new types of IT controls. Other significant control issues identified were that:
 - three organisations were not performing debt management procedures as required by their procedural documents;
 - reconciliations were either not performed, or not documented, in a way by which it could be determined that they had been performed in a timely manner; and
 - the accounts receivable process could be improved by the greater use of available FMIS functionality.
- *Information and communication*—The audit found that organisations had generally implemented effective processes to provide financial and operational reporting to management. In some organisations, operational and financial reporting could be improved through additional analysis of the data and by correcting reporting deficiencies.
- *Monitoring and review*—Organisations had underestimated the importance of monitoring and review. Only three organisations had developed performance indicators as well as mechanisms to report against them regularly. Only two organisations had performed reviews of the accounts receivable process.

Sound and better practices

13. The audit identified examples of sound and better practices in place in several organisations. While many of the sound practices would be expected to be applied in all organisations reviewed, this was not the case. To provide some insight into approaches being taken in various organisations, details of the sound practices observed have been included in the Report in addition to identified better practices. A summary of the sound and better practices is provided in Table 1.

Table 1**Sound and better practices observed in accounts receivable**

Control framework component	Sound and better practices
Risk assessment	<ul style="list-style-type: none"> • Risk assessment processes at the strategic level were incorporated into the business planning cycle. • Fraud Control Plans highlighted the risk areas relating to accounts receivable from the point of view of fraud. The plans also included proposed specific actions aimed at addressing those risks.
Control environment	<ul style="list-style-type: none"> • Comprehensive guidelines supporting the accounts receivable functions have been developed and implemented. • Use of Intranet and other technological means have been developed to promulgate and distribute policies and procedures. • Staff involved in debt recovery activities are required to receive training in debt recovery and client relations. • Induction, formal and one-off training programs have been used effectively. • Job description documentation has been put in place within the accounts receivable area to identify tasks and responsibilities. • Financial and other delegations are distributed to staff via the Intranet and other technological means such as e-mail. • Personnel sections distribute a regular report to IT sections to advise when staff leave the organisation. • Automated checking of computer passwords for obvious or common passwords is undertaken.
Control activities	<ul style="list-style-type: none"> • The checking of credit worthiness has been established as a primary control. • External collection agents have been engaged to follow up outstanding debts. • A code of conduct has been established for external collection agents. • Invoices are processed directly from the FMIS and as a result, cost efficiencies have been achieved. • Electronic receipts are issued wherever possible.
Information and communication	<ul style="list-style-type: none"> • User feedback has been obtained to identify possible improvements in financial reports.
Monitoring and review	<ul style="list-style-type: none"> • Internal audit reviews of the accounts receivable and associated functions are undertaken on a periodic basis. • Performance measures were established and regularly reported on.

Recommendations

The recommendations set out below are based on the findings made in the agencies reviewed but should have relevance to all Commonwealth agencies and have been framed accordingly.

Risk assessment

Recommendation No.1
Para 2.16 The ANAO *recommends* that organisations, which have not recently done so, undertake a process level risk assessment of the accounts receivable function. This risk assessment should have regard to the significance and materiality of the accounts receivable function to the organisation as a whole.

Control environment

Recommendation No.2
Para 3.14 The ANAO *recommends* that:

- organisations include items identified as Better Practice in the ANAO's Better Practice Guide on Accounts Receivable⁸ in their policies and procedures for the accounts receivable function; and
- policy and procedural documents be maintained in a manner that allows them to be easily identified and accessed.

Recommendation No.3
Para 3.23 The ANAO *recommends* that organisations conduct both induction and refresher training programs to ensure that all staff who are appointed to the accounts receivable function are fully aware of their responsibilities and daily tasks.

Recommendation No.4
Para 3.37 The ANAO *recommends* that organisations ensure that appropriate general and application IT controls are in place to provide adequate security for their systems and accounts receivable data.

⁸ *ibid.*

Control activities

Recommendation No.5 The ANAO *recommends* that, in relation to the accounts receivable process, organisations:

Para 4.38

- review the adequacy of controls surrounding the completeness of the relevant balances; and
- assess the performance of their FMIS on a regular basis to ensure that it is meeting the needs of the organisation and that the capabilities are being utilised cost-effectively.

Information and communication

Recommendation No.6 The ANAO *recommends* that organisations provide appropriate analysis of the financial results,

Para 5.11

including accounts receivable, to help users better understand and make use of the financial reports.

Monitoring and review

Recommendation No.7 The ANAO *recommends* that organisations:

Para 6.17

- establish appropriate performance indicators for the accounts receivable function;
- provide performance information against these indicators in their regular management reports; and
- implement regular monitoring and review procedures to measure performance against the indicators put in place.

Responses to the recommendations by organisations included in the audit

15. A similar grouping of recommendations was made in a detailed report to each of the organisations covered by the audit. The recommendations varied according to the adequacy of the individual internal control framework operating within the organisation. Organisations agreed with the recommendations and a number indicated that corrective action had been undertaken before the audit was completed.

Audit Findings and Conclusions

1. Introduction

Background

What is accounts receivable?

1.1 Accounts receivable is an accounting term used to describe amounts owed for goods or services provided on credit. As soon as credit is provided, an accounts receivable or debt, is incurred. The debt becomes overdue if not paid within the agreed terms of trade. Effective management of the accounts receivable function ensures that an organisation's cashflow is maximised and its accountability responsibilities⁹ to recover all debts are met.

Financial significance and environmental change

1.2 Accounts receivable makes up a significant proportion of the Commonwealth's financial assets at any one point in time even though it only represents a median of 3.6 per cent of the total finance budget and between 0.002 and 0.293 per cent of total organisational expenditure¹⁰. Accounts receivable represents highly liquid assets which have a direct impact on the Government's cashflow and financial position.

1.3 At 30 June 2001, total accounts receivable amounted to \$36 billion of taxes, advances and loans and other receivables owed to the Commonwealth. This audit did not examine processes related to taxes, advances and loans but concentrated on other receivables that included sale of goods and services, overpayment of benefits and other charges. In the Commonwealth, as at 30 June 2001, other receivables accounted for \$18.3 billion¹¹.

⁹ For example for agencies under the *Financial Management and Accountability Act 1997*, section 47 makes a Chief Executive responsible for pursuing the recovery of each debt owing to the Commonwealth for which the Chief Executive is responsible unless the debt has been written off, or the debt is not legally recoverable, or it is not economical to pursue recovery of the debt.

¹⁰ ANAO Audit Report No.25 2000–2001, *Benchmarking the Finance Function*, p. 61.

¹¹ *op. cit.*, p. 11, *Footnote 2*.

1.4 The Commonwealth environment has undergone significant changes in recent years that have impacted on the accounts receivable function. These changes include:

- new technology which has increased opportunities for automation of processes and procedures;
- the introduction of cost recovery to a number of Commonwealth organisations which has resulted in the need to develop invoicing processes and the associated management of accounts receivable;
- new agency funding arrangements which require organisations to place more emphasis on the management of cashflows;
- the introduction of the Goods and Services Tax (GST) legislation in 2000 which has increased the need for agencies to have efficient accounts receivable processes, especially in a climate where agencies can invest surplus cash balances;
- the implementation of accrual budgeting and reporting which requires agencies to identify and record current and future accounts receivable activity; and
- the introduction of the *GovernmentOnline* strategy which requires organisations to assess new electronic means for receiving monies and communicating with their debtors.

The accounts receivable process

1.5 The accounts receivable process is the set of activities comprising the recording of revenue (issue of the invoice) and accounts receivable (recognising the debt) and the collection of the relevant amounts. For most organisations, the accounts receivable process has three distinct parts:

- generating a debt—the recording of the debt as well as ensuring that the debtor is made aware of the amount and terms of the debt;
- receipting—the recording of the payment of the debt; and
- debt recovery—the procedures used by the organisation to recover the overdue debts.

1.6 These processes are graphically represented at Appendix 5.

1.7 In addition, the accounts receivable process can involve the checking of the customer's credit risk, dealing with customer complaints, and identifying future cash inflows.

1.8 The quality of the design of the accounts receivable process and how well the organisation executes the process has an impact on customer relationships¹² and sound cash management. An organisation that knows and can meet its customers' service expectations enhances the productive relationship it has with its customers. An organisation that manages its accounts receivable process effectively makes a positive contribution to its cash flow.

Audit objectives and coverage

1.9 The objectives of the audit were to:

- assess whether the processing, collection and overall management of the accounts receivable function was being performed in accordance with applicable legislation, Government policy and applicable internal controls;
- identify better practices in accounts receivable activities; and
- as necessary, recommend improvements in the controls and practices relating to accounts receivable.

1.10 This audit covers four types of accounts receivable, namely:

- trade debtors—debts incurred from the sale of goods and services;
- other charges—any other ad hoc activity that results in a debt;
- recoveries of overpayments of benefits—an overpayment to a recipient of a Government program which is recovered as a debt rather than by reducing the recipient's future payments¹³; and
- recoveries of overpayments to staff—overpayments generally of travel allowances and salaries.

¹² In organisations where the debts are mainly the recovering of overpayments from administered programs, this function will also be important for supplier relationships.

¹³ The audit only included the recovery process not how it had been established that an overpayment had occurred.

1.11 The audit was undertaken in eight Commonwealth organisations; some of these organisations are subject to the *Financial Management and Accountability Act 1997* (FMA Act) while others are subject to the *Commonwealth Authorities and Companies Act 1997* (CAC Act). These organisations were:

- Army and Air Force Canteen Service;
- Australian Bureau of Statistics;
- Australian Institute of Health and Welfare;
- Department of Education, Training and Youth Affairs;
- Department of Employment, Workplace Relations and Small Business;
- Department of Health and Aged Care;
- Royal Australian Mint; and
- Therapeutic Goods Administration.

1.12 At the time of the audit, the total amount of other receivables, referred to earlier, which was owed to these organisations was \$44.6 million¹⁴.

Audit evaluation criteria

1.13 This audit is one in a series of Assurance and Control Assessment (ACA)¹⁵ audits looking at business and financial processes in the Commonwealth. Other audits include *Audit Report No.52 Payment of Accounts 2000–01*, *Audit Report No.8 Disposal of Infrastructure Plant and Equipment 2001–02*, *Audit Report No.10 Agency Banking 2001–02* and *Audit Report No.19 Payroll Management 2001–02*.

1.14 The audit criteria for these audits were based on the internal control framework detailed in the ANAO's *Better Practice Guide to Effective Control, Control Structures in the Commonwealth Public Sector: Controlling Performance and Outcomes*¹⁶ and consist of:

- risk assessment;
- control environment;
- control activities;
- information and communication; and
- monitoring and review.

¹⁴ op. cit., p. 11, *Footnote 4*.

¹⁵ A description of ACA and the performance information related to this audit is contained in Appendix 1.

¹⁶ ANAO 1997, *Controlling Performance and Outcomes, Better Practice Guide to Effective Control*, Canberra.

1.15 The internal control framework can be described as follows:

The control environment is the foundation for the effectiveness of all the other components. It reflects management's commitment and attitude to establishing an effective control structure. It is sometimes referred to as the "tone at the top" and is dependent on firm leadership and clarity of direction from the governing body.

Risk assessment and control activities include identification, analysis and assessment of risks to achieving objectives and the design of control policies and procedures to manage those risks, focussing on those that have potential for more significant exposures and are critical to the business.

Regular and relevant information needs to be collected and communicated to enable performance to be monitored and reviewed. The effectiveness of the control structure also requires on-going monitoring and review.¹⁷

Detailed criteria

1.16 The above audit criteria have been adapted and expanded to take account of the diverse risks and operations of an accounts receivable function. Development of the criteria also considered better practice in both the business and government sectors' accounts receivable functions.

1.17 Table 2 shows the audit evaluation criteria mapped against the components of the internal control framework. Each organisation's management of the accounts receivable process was assessed against those criteria.

¹⁷ *ibid.*

Table 2**Audit evaluation criteria**

<i>Risk assessment</i>	
<p>Each organisation would be expected to have completed a risk assessment at both the organisational level (agency, program) and process level (function, task) including one for the accounts receivable process.</p> <p>The assessment would be expected to have covered the sources of revenue, potential for non-collection of debt including non-payment, loss and theft, potential for non-recognition of revenue and existing controls.</p> <p>The assessment would be expected to complement the fraud risk assessment, and any weaknesses requiring management attention would be identified and action taken.</p>	
<i>Control environment</i>	
<p>Management demonstrates commitment to ensuring well controlled business operations, including the following:</p>	
Process	Organisations would be expected to have accounts receivable policies and documented procedures for the management of accounts receivable.
Personnel	Organisations would be expected to have engaged appropriately qualified staff and arranged for training of relevant staff.
Structure	Organisations would be expected to have determined responsibility for all associated functions and provided the appropriate delegations.
Technology	Organisations would be expected to have implemented appropriate general IT controls.
<i>Control activities</i>	
<p>Organisations would be expected to have specific controls to ensure the validity, completeness and accuracy of accounts receivable amounts including appropriate general and application IT controls.</p> <p>Controls would cover all elements of the process including granting credit, recording sales, recording credits, processing remittances, debt management, and management reporting.</p> <p>Controls would also be expected to be efficient.</p>	
<i>Information and communication</i>	
<p>Organisations would be expected to have in place systems/reports to identify outstanding debts by age and debtor as well as debtors exceeding their credit limits.</p> <p>There would be an expectation of a close link between the accounts receivable accounting module and the general ledger to ensure efficient report generation and minimise the possibility of data errors.</p> <p>It would be expected that the agency would have regular two-way information flows between accounts receivable staff and management.</p>	
<i>Monitoring and review</i>	
<p>Organisations would be expected to have regular monitoring and review processes in place to ensure that policies and procedures are adhered to and properly applied.</p> <p>There would also be an expectation that processes would exist so that required changes and weaknesses in the operating environment could be identified; this might be achieved by reporting against performance measures and through internal checking and auditing processes.</p> <p>The results of this process would then be input into the next round of strategic planning and risk assessment performed by the organisation.</p>	

Previous audit coverage

1.18 In 1997–98, the ANAO reported a financial control and administration audit of the *Management of Accounts Receivable*¹⁸ across a number of Commonwealth organisations. The main objectives of the audit were to assess the cost-effectiveness of the management and administration of the accounts receivable function in the ‘general government sector’¹⁹ and to identify, develop and report better practice in the management of accounts receivable. The major audit findings were that at both the strategic and operational level, improvements could be made in the management and administration of the accounts receivable function.

1.19 Seven principles for the achievement of better practice were identified:

- a comprehensive and clear policy framework which has been endorsed by executive management should be established;
- risks to revenue collection should be identified, analysed and assessed;
- responsibility for strategic decision making in relation to debt management should be transferred to program managers;
- management reporting and performance measurement should be strengthened;
- sale and billing systems should be integrated;
- alternative payment options should be introduced; and
- a more structured approach to the recovery of debt should be developed.

1.20 Further details of the findings and recommendations of the 1997–98 audit are provided at Appendix 2. The appendix also includes a detailed analysis of the progress made on implementing the 1997–98 recommendations based on the findings of the 2001 audit. In summary:

- all organisations had implemented an FMIS with integrated sales and billing systems;
- the use of direct credit and credit cards has increased;
- all organisations except one had clear procedures documented for the recovery of debts;
- functional managers in all organisations had input into the debt recovery process;

¹⁸ op. cit., p. 12, Financial Control and Administration Audit, *Management of Accounts Receivable*.

¹⁹ op. cit., p. 11. *Footnote 3*.

- all organisations had polices for the management of accounts receivable in place;
- five out of the eight organisations had performance indicators; and
- all organisations had implemented some form of regular reporting mechanism.

Audit Methodology

1.21 The audit was undertaken in accordance with ANAO Auditing Standards during the period January to December 2001.

1.22 The audit process involved interviews with selected officers, the examination of files and records supporting the accounts receivable process, and general observation and inspection.

1.23 Research was also conducted into current better practices. Sources for this information included the New South Wales Audit Office and Arthur Andersen's Global Best Practices website at www.knowledgespace.com. This research provided the basis for the assessment of sound and better practices performed in this audit.

Structure of the remainder of the audit report

1.24 Chapters 2—6 discuss the findings and recommendations of the audit against each component of the internal control framework.

1.25 The ANAO's observations are presented in two distinct categories:

- *Audit findings* which detail control weaknesses contributing to a breakdown in both efficiency and effectiveness of the internal control framework; and
- *Sound and better practices* relate to business practices, which, if adopted, would strengthen the internal control framework and lead to improved effectiveness and efficiency of the accounts receivable process.

2. Risk Assessment

Introduction

2.1 Risk assessment is the starting point for evaluating the accounts receivable control framework, because, through a formal process, it provides the necessary information to properly design controls which are both complete and cost-effective. A sound risk assessment also provides the basis for ensuring responsibility for managing risks is appropriately allocated to managers who need to understand the risks and can be held accountable for its management through the operation of the control framework. Managers need to ensure complete and cost-effective accounts receivable control frameworks are put in place to properly support the organisation's objectives.

2.2 The assessment and management of risks in accounts receivable processes should aim to balance the cost of control against the likely benefits.

In managing the risk you need to strike a balance between the cost of managing the risk and the benefits to be gained. Recognising that a risk-free environment is impossible (if not uneconomic) to achieve, you need to decide what level of risk is acceptable²⁰.

Organisational and process level risk assessments

2.3 Risk assessments should be conducted at both *organisational* and *process* levels to assess whether organisations have properly applied the outputs of the process to the design of the control framework and related activity. Risk management activities generally commence with an organisational risk assessment that involves formally identifying risks within the context of the breadth of organisational activity. These risks would then be evaluated and sourced to activities or functions.

2.4 While the organisational risk assessment provides management with the necessary knowledge and understanding to manage risk, further development of risk assessment activity related specifically to the management of the accounts receivable function is required to fully understand the control requirements. Formal process level risk assessments provide managers with the requisite knowledge to manage the risks and associated opportunities. A better understanding of process level risks should lead to a better understanding of control issues.

²⁰ Management Advisory Board/Management Improvement Advisory Committee (MAB/MIAC) 1996, *Guidelines for Managing Risk in the Australian Public Service*, Report No.2, Canberra.

Fraud risk assessment

2.5 Fraud control is integral to internal control and central to good corporate governance. In the Commonwealth environment, organisations operating under the *Financial Management and Accountability Act 1997* are required to implement a Fraud Control Plan. The Commonwealth Fraud Control Policy requires Chief Executives to be responsible for:

*Fostering an environment within their agencies which makes fraud control a major responsibility for all public sector staff, for articulating clear standards and procedures to encourage minimisation and deterrence of fraud, and for the detection and prosecution of offences should they occur*²¹.

2.6 Fraud control policies should reflect an organisation's wider operating environment and be an integral part of the organisation's planning regime. Fraud control plans should, in turn, be linked to the broader objectives of an organisation as outlined in its corporate plan, the directions specified in its business plan and the activities of individual work areas. Importantly, the fraud control plan should be subject to regular review to take account of changing conditions.

Risk assessment of the accounts receivable function

2.7 Generally, the accounts receivable function in the Commonwealth is construed as a simple, low risk process. This is acceptable on one level—accounts receivable processes are routine and assumed to be well understood by staff. However, the accounts receivable function has risks warranting consideration, including risks to the organisation's reputation, efficiency, potential for fraud, and information risks as follows:

- Reputation risk: the risk to an organisation's reputation should receipts be misappropriated or debts not recovered.
- Efficiency risk: the risk that inadequate use of information systems in processing requires an unbalanced proportion of alternative scarce resources.
- Potential for fraud: the potential for fraud increases with the exposure of staff to cash and cheques.
- Information risk: the risk that management lacks adequate information on the performance of the accounts receivable function to make decisions about its future application in the organisation's governance arrangements.

²¹ Commonwealth Law Enforcement Board, 1994, *Best Practice for Fraud Control—Fraud Control Policy of the Commonwealth*, Canberra.

Business benefits of risk assessments

2.8 Formal organisational risk assessments, undertaken against an established risk framework that takes account of the costs and benefits of controls, assist an organisation to apply consistent and defensible approaches to the management of risks, including those risks associated with the accounts receivable function.

2.9 Process level risk assessments are the basis for the subsequent design of all aspects of the control environment, specific control activities, information and communication processes, and monitoring and review procedures. The process level risk assessment can enhance control structures, detect control weaknesses, prevent control breakdown and increase operational efficiency.

Audit findings and comments

Summary table

2.10 The following table summarises the risk assessment audit findings.

Table 3

Risk assessment

<i>Principle</i>	Implementation of an effective risk assessment framework is a central element of the management of accounts receivable.
<i>Audit evaluation criteria</i>	<p>Each organisation would be expected to have completed a risk assessment at both the organisational level (agency, program) and process level (function, task) including one for the accounts receivable process.</p> <p>The assessment would be expected to have covered the sources of revenue, potential for non-collection of debt including non payment, loss and theft, potential for non-recognition of revenue and existing controls.</p> <p>The assessment would be expected to complement the fraud risk assessment, and any weaknesses requiring management attention would be identified and action taken.</p>
<i>Audit findings</i>	<p>In relation to the eight organisations reviewed, the audit found:</p> <ul style="list-style-type: none"> • all organisations had implemented an organisational level risk assessment in some form; • most organisations had not conducted a formal process level risk assessment of the accounts receivable function; and • fraud control plans had been implemented in all but one organisation.
<i>Sound and better practices noted</i>	<p>The audit noted the following in some organisations:</p> <ul style="list-style-type: none"> • risk assessment processes were incorporated into the business planning cycle; and • fraud control plans highlighted the risk areas relating to accounts receivable from the point of view of fraud. The plans also included proposed specific actions aimed at addressing those risks.

Detailed findings

Organisational and process risk assessment

2.11 All organisations had implemented an organisational level risk assessment. Where the accounts receivable function was considered material to the organisation as a whole, the function's risks had been included and assessed.

2.12 Three of the organisations had undertaken process level risk assessment related to the accounts receivable function. Two of the organisations planned to conduct a process level risk assessment once they had conducted a restructure of the accounts receivable function. Two other organisations considered the accounts receivable function immaterial to the organisation as a whole. The final organisation was in the process of reviewing its risk assessment policies and, as a result, had not completed a process level risk assessment.

2.13 The ANAO also noted that where process level risk assessments had been completed, the risks and controls identified were not reviewed on a regular basis. In one instance, this situation resulted in controls identified as being relied upon not actually being performed, so that the organisation was not effectively managing its risks.

Fraud control plans

2.14 The audit found that in all but one organisation, fraud control plans had been developed and updated on a regular basis. The organisation that did not have a fraud control plan in place is an operating unit of a larger Department. Management of the organisation believed that they had been included in the Department's fraud control plan.

Conclusion

2.15 All organisations had completed risk assessments at the organisation level, although these were not being reviewed on a regular basis. All but one had completed fraud risk assessments and prepared fraud control plans. However, formal process level risk assessments of the accounts receivable function had only been conducted in three of the organisations reviewed noting that two other organisations considered the accounts receivable function immaterial to the organisation as a whole.

Recommendation No.1

2.16 The ANAO recommends that organisations, which have not recently done so, undertake a process level risk assessment of the accounts receivable function. This risk assessment should have regard to the significance and materiality of the accounts receivable function to the organisation as a whole.

3. Control Environment

Introduction

3.1 A critical component of an effective control environment is management's attitude and commitment to the implementation and maintenance of an effective internal control structure. The level of positive support by management strongly influences the design and operation of control policies and procedures.

Through their words and actions, management sets the tone of the organisation's workplace, its integrity, values and ethics²².

3.2 Without an effective control environment, managers will be unable to ensure the adequacy of the accounts receivable control framework. Organisations should establish a control environment that clearly sets out accounts receivable management responsibilities and promotes sound management principles, including continuous improvement. Comprehensive and up-to-date policies and procedures are fundamental to achieving such an environment.

Business benefits of an effective control environment

3.3 An effective control environment will ensure accounts receivable management policies, procedures and practices are aligned with overall corporate strategies and objectives. Such an environment establishes a control consciousness within which specific operational controls are applied. It provides the framework which supports management's ability to rely on the integrity of processing as well as the cost-effectiveness of that processing.

3.4 The nature of management's approach in this area clearly has an impact beyond the accounts receivable function. The words and actions of management establish the atmosphere for the implementation and maintenance of an effective control structure across financial management and operational activity—in effect enhancing the organisation's approach to risk management and corporate governance as a whole.

²² op. cit., p. 24, *Controlling Performance and Outcomes, Better Practice Guide to Effective Control.*

Audit findings and comments

3.5 The control environment relating to the accounts receivable function was examined under the following four main elements:

- process—the organisation’s policies and procedures should be complete and effectively communicated in order to reflect the organisation’s governance responsibilities;
- personnel—the need for high quality and experienced staff to be employed, with their responsibilities and accountability clearly defined, as well as promoting these through effective training and communications programs;
- structure—the structure of the function should relate to the organisation’s needs, and allow for clear responsibilities, accountabilities and transparency of process; and
- technology—the technology used within the function should be established to support all the elements of the established control environment.

3.6 The audit findings for each of the above elements are detailed below.

Control environment process

Summary table

3.7 The following table summarises the control environment process audit findings.

Table 4
Process

<i>Principle</i>	Effective policies and procedures provide all relevant personnel with access to a documented framework for the management of accounts receivable.
<i>Audit evaluation criteria</i>	Organisations would be expected to have accounts receivable policies and documented procedures for the management of accounts receivable.
<i>Audit findings</i>	In relation to the eight organisations reviewed, the audit found: <ul style="list-style-type: none"> • all organisations have issued policies and procedures for the accounts receivable function; • relevant policies and procedures were sometimes difficult to locate as they were stored in multiple places and were not cross referenced; and • some elements identified in the ANAO’s Better Practice Guide on Accounts Receivable²³ have not been included in policy and procedural documents.

continued next page

²³ op. cit., p. 12, Financial Control and Administration Audit, *Management of Accounts Receivable*.

<i>Sound and better practices noted</i>	<p>The audit noted the following in some organisations:</p> <ul style="list-style-type: none"> • use of Intranet and other technological means have been developed to promulgate and distribute policies and procedures; and • comprehensive guidelines supporting the accounts receivable functions have been developed and implemented.
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Detailed findings

3.8 The existence of policies and procedures is a key element for preventing possible control breakdown, should, for example, the organisation experience high turnover in personnel. These mechanisms include the use of Chief Executive's Instructions and procedures, as well as guidelines and detailed process descriptions.

3.9 Generally, the policies and procedures in the organisations provided sufficient guidance for staff to perform daily tasks in a controlled and consistent manner. Five organisations had formal documented policies and procedures approved by the organisation's Chief Executive. The remaining three organisations were in the process of updating procedural documents.

3.10 The ANAO *Management of Accounts Receivable* Better Practice Guide²⁴ provided guidance on items to be included in an accounts receivable policy document (refer Appendix 4). While organisations had included the majority of items in their guidance material, some items such as the treatment of dishonoured cheques had not been included. The ANAO considers that all items should be included in policy or procedure documents to ensure that accounts receivable staff have appropriate and sufficient guidance to cover potential issues that may arise.

3.11 Many organisations increasingly use Intranet functionality or other technology to communicate policies and procedures.

3.12 In some instances, not all of the relevant guidance material could be easily located by staff. In one organisation, policies and procedures were maintained on three databases without any internal links. In another two organisations, the policy and procedure documents were not cross-referenced to other guidance material. These situations resulted in staff, especially new members, having difficulty in finding all relevant guidance for performing their daily tasks.

²⁴ op. cit., p. 14, Better Practice Guide, *Management of Accounts Receivable*.

Conclusion

3.13 Organisations have developed policies and procedures to support the accounts receivable function. However, organisations need to improve both the access to, and cross-referencing of, policies and procedures. Policies and procedures were appropriately detailed and provided useful guidance for staff members.

Recommendation No.2

3.14 The ANAO recommends that:

- organisations include items identified as Better Practice in the ANAO's Better Practice Guide on Accounts Receivable²⁵ in their policies and procedures for the accounts receivable function; and
- policy and procedural documents be maintained in a manner that allows them to be easily identified and accessed.

Control environment personnel

Summary table

3.15 The following table summarises the control environment personnel audit findings.

Table 5

Personnel

<i>Principle</i>	Organisations employ high quality and experienced staff and through training and regular communication ensure all relevant personnel are aware of their responsibilities, policies and procedures.
<i>Audit evaluation criteria</i>	Organisations would be expected to have engaged appropriately qualified staff and arranged for training of relevant staff.
<i>Audit findings</i>	In relation to the eight organisations reviewed, the audit found: <ul style="list-style-type: none">• appropriately qualified and experienced staff have been employed to perform accounts receivable processes; and• although training programs are being used in most organisations, the thoroughness of induction programs in some organisations could be enhanced to ensure that staff are fully aware of all accounts receivable guidance material.
<i>Sound and better practices noted</i>	The audit noted the following in some organisations: <ul style="list-style-type: none">• staff involved in debt recovery activities are required to receive training in debt recovery and client relations;• induction, formal and one-off training programs have been used effectively; and• job description documentation has been put in place within the accounts receivable area to identify tasks and responsibilities.

²⁵ *ibid.*

Detailed findings

3.16 Organisations had engaged appropriately qualified and experienced staff to perform accounts receivable functions. The staff involved in accounts receivable functions ranged from processing staff to qualified accountants.

3.17 All organisations had job descriptions for each position involved in the accounts receivable function to ensure that current staff were aware of their responsibilities. These job descriptions were also used for developing selection criteria when hiring new staff.

3.18 All organisations had implemented formal and informal on-the-job training programs that varied in substance and areas covered. Formal training was generally organised and performed in an ad hoc manner. Four organisations had a program of planned training courses, but the majority identified training requirements as the need arose.

3.19 The majority of organisations trained staff in the accounts receivable function by on-the-job training and having experienced staff members offer guidance. One organisation had a requirement that staff responsible for debt recovery must receive formal training in this activity and client relations.

3.20 Organisations had also made use of one-off programs to communicate new and emerging issues. This was demonstrated by the amount of training performed on GST issues relating to accounts receivable.

3.21 On the whole, organisations made effective use of induction training, although one organisation's program could have been more thorough. The program did not cover all applicable policies and procedures nor did it include existing staff members starting work in the accounts receivable function. This resulted in processes being performed incorrectly as, initially, staff members were not aware of all of the relevant guidance material.

Conclusion

3.22 Organisations have appropriately qualified and trained staff to perform accounts receivable processes. Induction training programs have been implemented in all of the organisations. However, in one organisation the program was not sufficiently comprehensive to instruct staff of their responsibilities.

Recommendation No.3

3.23 The ANAO recommends that organisations conduct both induction and refresher training programs to ensure that all staff who are appointed to the accounts receivable function are fully aware of their responsibilities and daily tasks.

Control environment structure

Summary table

3.24 The following table summarises the control environment structure audit findings.

Table 6
Structure

<i>Principle</i>	Organisations structure the accounts receivable function to specify responsibilities and allow for transparency of processes.
<i>Audit evaluation criteria</i>	Organisations would be expected to have determined responsibility for all associated functions and provided the appropriate delegations.
<i>Audit findings</i>	In relation to the eight organisations reviewed, the audit found: <ul style="list-style-type: none"> • organisations had allocated responsibility for accounts receivable tasks; and • one organisation had not formally documented their delegations.
<i>Sound and better practice noted</i>	The audit noted in some organisations that financial and other delegations are distributed to staff via the Intranet and other electronic means such as e-mail.

Detailed findings

3.25 The Chief Executive Officer of most organisations had allocated the responsibility for the efficient, effective and ethical management of accounts receivable to the managers of finance areas. In most cases, responsibility was allocated through Chief Executive’s Instructions and procedural documents.

3.26 The majority of organisations had also appointed managers to be responsible for policy development, staff training, maintenance of accounting records, and other monitoring processes and financial and management reporting arrangements. In smaller organisations these responsibilities were assigned to one manager.

Delegations/authorisations

3.27 Delegates or authorised officers were appointed to: determine when to start debt recovery actions; receive public monies; approve credit limits; accept payment by instalments; and approve the use of external collection agents. Generally, the delegations/authorisations provided

authority to a range of officers commensurate with this level of responsibility. All except one organisation had formally documented the delegations/authorisations and distributed them to relevant staff members.

Conclusion

3.28 Responsibilities and the relevant delegations, for accounts receivable tasks, have been appropriately allocated within organisations, and had been adequately documented.

Control environment technology

Summary table

3.29 The following table summarises the control environment technology audit findings.

Table 7

Technology

<i>Principle</i>	Organisations use technology to support accounts receivable activities in a way that contributes to the organisation's strategic objectives as well as ensuring cost-effective and efficient processing.
<i>Audit evaluation criteria</i>	Organisations would be expected to have implemented appropriate general IT controls.
<i>Audit findings</i>	In relation to the eight organisations reviewed, the audit found: <ul style="list-style-type: none"> • general IT controls are in place, but are not being used to the full extent so as to maximise security over data and systems; • one organisation had the ability to cancel invoices without these actions being reviewed by management; and • one organisation did not have sufficient staff to implement a full segregation of duties.
<i>Sound and better practices noted</i>	The audit noted the following in some organisations: <ul style="list-style-type: none"> • Personnel sections distribute a regular report to IT sections to advise when staff leave the organisation; and • automated checking of computer passwords for obvious or common passwords is undertaken.

Detailed findings

3.30 General IT controls include, for example, unique identification log-ons and passwords controls that assist in ensuring the security of the computer system and environment. Application IT controls, such as hierarchical access, refer to controls that are used at the application level, that is, controlling individual items of software.

3.31 General and application IT controls are important for ensuring the validity, completeness and accuracy of accounting data. As more processes become automated, IT controls become increasingly important and management should implement and regularly monitor these controls to help ensure their ongoing validity.

3.32 All organisations have implemented FMISs with the majority of organisations fully implementing general and application IT controls. The controls still needing to be implemented in two organisations included the requirement for:

- passwords to be of a minimum length;
- passwords to be changed on a frequent basis;
- log-on identification to be restricted to one machine at any one time²⁶;
- user accounts to be disabled after a set number of failed attempts to logon; and
- the IT section to be advised when staff leave so their user accounts can be closed.

3.33 Staff in one organisation were able to cancel open or unpaid invoices without the action being reviewed by management. Although this practice had been accepted for operational purposes, it did increase the potential for fraudulent activity. In this instance, the ANAO recommended that a senior officer review the audit log of cancelled invoices on a regular basis and that the log be altered to include the reason for the cancellation.

3.34 One organisation also had a segregation of duties issue in relation to their system administrators. The ANAO acknowledges that where the section responsible is small, it is difficult to fully implement appropriate segregation of duties. Organisations, especially small ones, need to assess the risk associated with a lack of segregation of duties and design appropriate controls to compensate for this risk. Often, a simple change in the process can be affected whereby control is strengthened without requiring additional resources or placing onerous costs on the organisation.

²⁶ One organisation commented to the ANAO that *'the issue of staff having the capability to log on or to more than one machine at a time is not necessarily considered a significant risk (in their organisation) as all transactions processed by staff are logged. The more significant risk is that staff may leave their machine unattended for a period of time. Staff will be reminded that they should not leave sessions open when they are not using their machine in order to minimise the risk of other staff modifying records under their logon. In this context it needs to be noted that all the department's PC's have an automatic time out facility which requires a password to be entered if the machine is left unused for longer than 10 minutes.'*

3.35 Regular monitoring of IT controls would have identified these control weaknesses and allowed for corrective action to be taken by management.

Conclusion

3.36 General and application IT controls are generally being utilised in the majority of organisations. These controls need to be monitored to ensure that the systems and data stored in them remain secure.

Recommendation No.4

3.37 The ANAO recommends that organisations ensure that appropriate general and application IT controls are in place to provide security for their systems and accounts receivable data.

4. Control Activities

Introduction

4.1 Control activities are the specific practices, processes and methodologies that help an organisation ensure that:

- risks are reduced whilst opportunities for improvement are identified;
- irregularities are prevented or detected and addressed;
- assets are safeguarded; and
- financial records and relevant data are complete and accurately reflect the activities of the organisation.

Business benefits of control activities

4.2 An effective framework includes controls that minimise the impact of risks and contributes to the efficient and effective delivery of quality outputs and outcomes. It is only at this level of the overall control framework that specific internal controls operate. Control activities ensure integrity, accuracy and completeness of the accounts receivable process. The control activities' effectiveness is greatly enhanced by the surrounding pervasive controls, the control environment, and monitoring and reporting activities. However, their failure can create wide-ranging risks, including exposure to fraud. For this reason, emphasis should be more on preventative rather than detective controls.

Audit findings and comments

Summary table

4.3 The following table summarises the control activities audit findings.

Table 8

Control activities

<i>Principle</i>	The establishment of specific control mechanisms within accounts receivable related transactions.
<i>Audit evaluation criteria</i>	Organisations would be expected to have specific controls to ensure the validity, completeness and accuracy of accounts receivable amounts including appropriate general and application IT controls. Controls would cover all elements of the process including granting credit, recording sales, recording credits, processing remittances, debt management, and management reporting. Controls would also be expected to be efficient.

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<i>Audit findings</i>	<p>In relation to the eight organisations reviewed, the audit found:</p> <ul style="list-style-type: none"> • several organisations had inadequate controls for the complete and proper recording of revenue and accounts receivable transactions; • some organisations' debt management procedures were not always conducted in accordance with stated policies; • reconciliations were either not performed or not documented in a way to determine that they had been done in a timely manner; and • FMISs are either not capable or not being used to their full capabilities to ensure efficiency of processes.
<i>Sound and better practices noted</i>	<p>The audit noted the following in some organisations:</p> <ul style="list-style-type: none"> • the checking of credit worthiness has been established as a primary control; • external collection agents have been engaged to follow up outstanding debts; • a code of conduct has been established for external collection agents; • invoices are processed directly from the FMIS and as a result, cost efficiencies have been achieved; and • electronic receipts are issued wherever possible.

Detailed findings

4.4 To consider the control activities relevant to accounts receivable, the function has been separated into the following sub-processes:

- granting of credit—the assessment of potential debtors' ability to pay;
- generation of a debt—the procedures to ensure that all debts are recorded accurately;
- debt management—the procedures used to monitor debt and ensure maximum recovery of debts;
- receipts—the processing of receipts to ensure that monies payed are banked and recorded accurately; and
- reconciliations—the performance of regular reconciliations of bank accounts as well as the accounts receivable subsidiary ledger to the general ledger.

4.5 Although the use of IT is not a sub-process of the accounts receivable function, it does impact on each of the sub-processes identified. The use of IT is discussed at the end of this chapter.

Granting of credit

4.6 Organisations must ensure that credit is granted only to parties that are in a position to repay the debt as the subsequent recovery of unpaid debts are a cost to an organisation. Possible controls include, but are not limited to, a review of the potential customer's current and past financial positions, reference checks from other creditors and the appointment of an appropriate delegate to grant credit.

4.7 Organisations used a variety of methods to check the credit risk of private sector organisations including a search of the Australian Securities and Investment Commission's website, requests for recent financial data from the customer and obtaining credit ratings from independent rating organisations. One organisation also specified credit limits. To ensure these credit limits were not exceeded, the organisation circulated lists of customers internally, who had reached their limit and were not to be granted any more credit. This list also included individuals who had a history of not paying invoices in accordance with the established terms of payment.

4.8 Organisations that dealt with other Commonwealth organisations used mechanisms such as contracts, memoranda of understanding and other agreements, to formalise what services were to be supplied, and when payment was due. Commonwealth organisations do not have a high credit risk and therefore checking of credit risk was not considered necessary.

Generation of a debt

4.9 Organisations must ensure that accounts receivable processes are able to capture and record all debts accurately and in a timely manner. The recording of these debts is referred to as the generation of a debt. Where accounts receivable are not effectively recorded the organisation may not receive the monies owed to it. This can impact on future operations and also on management's ability to discharge their accountability responsibilities for the recovery of debts.

4.10 The majority of accounts receivable considered within the scope of this audit were incurred from the sale of goods and services. Organisations that sell goods have processes that calculate and manage the cost and subsequent sale of these goods. Organisations that sell services have implemented project costing systems that enables the calculation of staff time and other costs incurred in providing the service. These systems are used to calculate ongoing work-in-progress balances and assist in determining when a debt needs to be generated.

4.11 The production processes and project costing systems assist organisations in controlling the accounts receivable function. However, there are still some significant risks existing in organisations. One significant and emerging risk is the ability for staff in organisations to e-mail data and information stored electronically to external parties without easy detection. There should be controls in place to ensure that a debt is generated every time saleable information or data is provided to external parties. One organisation advised the ANAO in November 2001 that:

The most significant finding from the review of our agency relates to the need to provide controls of the electronic transmission of saleable data to ensure all such transmissions result in a sale being recorded. This is a new and emerging issue with the shift to this form of dissemination of our data products and poses control issues for the future. We have instituted a preliminary review to identify the potential scope of this issue. While we anticipate that we have a low risk exposure, we will ensure that as processes and systems are redeveloped controls are put in place, where appropriate, to ensure that all data transmissions result in the appropriate charging for the data provided. The issue will be considered as part of a risk assessment audit. The first step will be to improve our Chief Executive's Instructions in this area advising staff that they are not to forward chargeable products. All requests for free distribution of chargeable products, based on our community service obligations, would then be channelled through a central point. We wish to emphasise here that there are strict controls around confidential unit record data and pre-release commercially sensitive data and that this audit finding relates only to the transmission of data products developed for dissemination to the public and available to the public over the internet.

4.12 This risk is also significant for information considered sensitive or confidential. Access to data should be restricted to ensure that the organisation is not subject to fraud or the unauthorised disclosure of sensitive information.

4.13 In two organisations, existing systems were not adequate to ensure that all debts were recorded. The risks of this occurring were when:

- the services provided are of such a small value that contracts and agreements are not developed between the parties. A debt may not be generated because there is no control in place to ensure that work completed is invoiced; and
- there is no control in place to ensure that travel acquittals are completed when staff do not complete travel arrangements in accordance with the approved itinerary.

4.14 Seven organisations processed invoices directly from their FMIS. In the majority of cases, the accounts receivable subsidiary ledger was interfaced with the general ledger.

Invoice design

4.15 The design and the information included on each organisation's invoices were compared to better practice²⁷. The majority of organisations' invoices met most of the identified better practices although there were some common omissions such as the inclusion of a contact name or position title and phone number of the contact person; the accepted modes of payment; and the highlighting of the actual due date of payment. The ANAO considers the adoption of these better practices would improve the user friendliness of organisations' invoices. A list of better practices related to the design of invoices has been included in Appendix 4.

Debt management

4.16 Organisations need to ensure that appropriate processes and controls are in place to identify and manage overdue debts. The processes should ensure that debts are followed up in a timely and effective manner to maximise cash inflows and minimise the risk of non-payment. Processes should also include establishing when a debt is irrecoverable and when recovery action should cease. The performance of these processes should be properly documented.

4.17 All organisations used aged debtor reports²⁸ to identify overdue debts. These debts were followed up by staff contacting the debtor by telephone, e-mail and reminder letters. Where debts were being recovered from staff, one organisation made arrangements with the staff members to deduct amounts from future salary payments.

4.18 Three organisations were not performing debt recovery procedures in accordance with their stated policies and procedures. The reasons for this included lack of resources and a lack of awareness of the procedures.

4.19 The debt recovery procedures of one organisation did not provide staff with sufficient guidance and, as a result, procedures were applied in an ad-hoc manner.

²⁷ The Audit Office of New South Wales 1998, *Guide to Better Practice Debtors Administration*, Sydney.

²⁸ An Aged Debtor Report is a schedule that shows the amount due from a debtor by the length of time the balance has been unpaid. The aging categories are generally current, 30 days, 60 days and 90+ days. When a debt has terms of trade of 30 days, the current category refers to debts still in the initial 30 days period, whereas the 30 days category refers to debts past this time and so on.

4.20 Where organisations were performing debt recovery in accordance with detailed procedures, all but one documented the performance of these procedures by, for example, recording the details of telephone conversations or retaining copies of reminder letters.

4.21 The audit found three organisations accepted payment by instalment, when debtors were able to demonstrate financial hardship. However, in one organisation, these payment arrangements were not being monitored.

4.22 Three organisations used the services of external collection agents. The audit found only one organisation had provided agents with a code of conduct to guide the performance of their activities undertaken on behalf of the Commonwealth. None of the organisations was reviewing the performance of the agents although one planned to as part of a future selection process.

Reminder Letters

4.23 Reminder letters were generally of a high standard when compared to current better practice.²⁹ However, the standard reminder letter of two organisations could be improved through the inclusion of a contact name and phone number and details of the nature of the debt.

Receipts

4.24 Receipting of the payment of monies is the culmination of the accounts receivable process. It involves the custody, banking and recording of the monies received.

4.25 The receipting process requires a degree of segregation of duties to minimise the opportunities for error and misappropriation of monies. In particular, the person who records the receipts should not bank the monies. Seven of the organisations had appropriate segregation of duties in the receipting process. One organisation had a small accounts receivable section, making it difficult to achieve appropriate segregation. The organisation was planning to re-assess its receipting controls as part of a process level risk assessment.

4.26 All organisations had the functionality within their FMIS to match debtors' receipts to the relevant invoices.

²⁹ op. cit., p. 46, Guide to Better Practice Debtors Administration.

4.27 Organisations increasingly receive payments in electronic form. For outstanding debts from large organisations, the majority of payments were received in electronic form. Where debts were owed by small organisations and individuals, the majority of payments were made by cash and cheque. Many organisations were investigating further use of electronic receipts such as Bill Pay³⁰ and on-line credit card facilities.

4.28 The ANAO considers that organisations should continue to encourage the use of electronic forms of payment to reduce the risks and costs arising from the handling of cash.

Reconciliations

4.29 Reconciliations are a control mechanism for confirming the validity and accuracy of recorded transactions. Reconciliations should be performed on a timely and regular basis and should be reviewed by a responsible officer to ensure they are properly prepared.

4.30 The audit found one organisation had not performed reconciliations of the accounts receivable subsidiary ledger with the general ledger or bank accounts for the majority of 2000–2001. As a result, the risk associated with the collection of revenue to the organisation was also increased as the person preparing the receipts was also responsible for banking the money, and management had no mechanism in place to ensure all monies received were recorded accurately. One result of the completion of these reconciliations subsequent to audit fieldwork was that unbanked monies were identified.

4.31 In addition, five organisations were not performing formal reconciliations of the accounts receivable subsidiary ledger with the general ledger. This resulted in one organisation's ledgers not being in balance for nine months. The organisations considered that there was no need for formal reconciliations to be conducted as their FMIS had an automated interface between the two ledgers, that is the data entered into one ledger was automatically included in the other. However, an automated process (ie. the recording of data) is not the same as an automated control (ie. the verification of data). As there was no automated control, reconciliations were still necessary.

4.32 Three organisations did not evidence the date of the preparation or approval reconciliations and, therefore, it was not possible to determine whether the reconciliations had been performed or reviewed on a timely basis.

³⁰ Bill Pay is a centralised electronic bill payment service. The service is offered by financial institutions whereby their customers can use the phone or Internet to pay bills from their credit card, savings or cheque accounts.

Use of IT

4.33 FMISs offer organisations the opportunity of making their processes more efficient, as well as providing increased access to the data for performance reporting purposes.

4.34 The audit found that three organisations' FMIS were not capable of performing certain accounts receivable procedures (for example inaccurate reports were produced) or their capabilities were not being fully used (for example, the automatic reminder letters function was not being used).

4.35 In addition, three FMISs had been implemented without adequately considering the supporting databases and systems necessary to effectively manage the accounts receivable function. As a result, FMISs did not provide for:

- screen copies of invoices to be accessed by staff in a reasonable amount of time when responding to customer inquiries which meant that invoices had to be photocopied and used as a reference copy;
- debtor's credit limits to be automatically checked;
- client accounts to be checked as to whether they are in credit, prior to an invoice being generated and sent;
- GST to be calculated correctly; and
- debts to be aged correctly.

Conclusion

4.36 Limited controls are used in three organisations to ensure that accounts receivable balances are complete. In particular, an emerging issue was identified whereby saleable data and information can be e-mailed external to an organisation without being easily detected. This requires new types of IT controls.

4.37 Other significant control issues identified were that:

- three organisations were not performing debt management procedures as required by their procedural documents;
- reconciliations were either not performed, or not documented, in a way by which it could be determined that they had been performed in a timely manner; and
- the accounts receivable process could be improved by the greater use of the available FMIS functionality.

Recommendation No.5

4.38 The ANAO recommends that, in relation to the accounts receivable process, organisations:

- review the adequacy of controls surrounding the completeness of the relevant balances; and
- assess the performance of their FMIS on a regular basis to ensure that it is meeting the needs of the organisation and that the capabilities are being utilised cost-effectively.

5. Information and Communication

Introduction

5.1 An organisation's information and communication arrangements are fundamental to ensuring the achievement of organisational objectives. Effective arrangements provide a solid foundation for informed decision making and performance reporting. Information and communication arrangements will differ depending on the size, structure and geographical distribution of the organisation. The arrangements will also involve manual and computerised systems.

5.2 Performance measurement is also integral to any internal control environment. When monitored consistently, performance measures help an organisation identify process problems as they occur, often well before problems adversely affect outputs and outcomes.

Business benefits of effective information and communication

5.3 Effective information and communication helps organisations establish whether resources are being directed towards the achievement of desired outputs and outcomes in the most efficient, effective and ethical way. It also enables organisations to fulfil their accountability obligations in providing data for financial and other reporting obligations.

5.4 Performance reporting assists organisations understand whether the accounts receivable function is meeting the needs of the organisation. It contributes to continuous improvement and enables staff to undertake and monitor their own operational activities, which can also be used as a tool in building staff confidence and morale.

Audit findings and comments

Summary table

5.5 The following table summarises the information and communication audit findings.

Table 9**Information and communication**

<i>Principle</i>	Information systems are in place to provide relevant information for financial and management reporting purposes to the right people at the right time.
<i>Audit evaluation criteria</i>	Organisations would be expected to have in place systems/reports to identify outstanding debts by age and debtor as well as debtors exceeding their credit limits. There would be an expectation of a close link between the accounts receivable accounting module and the general ledger to ensure efficient report generation and minimise the possibility of data errors. It would be expected to have regular two-way information flows between accounts receivable staff and management.
<i>Audit findings</i>	In relation to the eight organisations reviewed, the audit found: <ul style="list-style-type: none"> • organisations have implemented some form of financial reporting, but analysis of the results was limited; • operational reporting was being performed, but some improvements could be made; and • organisations were making extensive use of a variety of communication methods.
<i>Sound and better practices noted</i>	The audit noted that user feedback has been obtained to identify possible improvements in financial reports.

Financial reporting

5.6 All organisations prepared some form of financial reports on a regular basis, usually monthly, for the use of senior management. The reports generally were in the form of brief financial statements, and, in most cases, the processes used to generate them were effective including generation directly via the organisation's FMIS using accrual accounting information. One organisation requested feedback from the report users to determine how the reports could be improved.

5.7 Although this audit concentrated on the accounts receivable function, it noted that analysis of financial information in the financial reports was generally limited. This was particularly true of accounts receivable information as three organisations considered accounts receivable to be a low risk area not warranting much management attention. In two organisations where accounts receivable was material, the base data provided in the reports was not sufficient to provide senior management with a full understanding of the organisation's performance.

Operational reporting

5.8 All of the organisations could effectively produce reports that identified outstanding debts and the age of these debts. In two organisations, these reports required improvement as:

- one organisation's aged debtor report was produced in two parts—

the first showed the outstanding debt, but the amounts were not aged and there was no overall total. The second part of the report showed the ageing, but did not take into consideration partial payments; and

- the second organisation's report did not age debts correctly due to limitations of the existing FMIS.

5.9 Exception reports were also used in most organisations to determine whether transactions had been processed correctly within the system.

Conclusion

5.10 The audit found that organisations had generally implemented effective processes to provide financial and operational reporting to management. In some organisations, operational and financial reporting could be improved through additional analysis of the data and by correcting reporting deficiencies.

Recommendation No.6

5.11 The ANAO recommends that organisations provide appropriate analysis of the financial results, including accounts receivable, to help users better understand and make use of the financial reports.

6. Monitoring and Review

Introduction

6.1 Monitoring and review is the final component of an effective control framework. It is a key element of an organisation's continuous improvement process that helps ensure the organisation implements effective processes and tools to monitor and review relevant data. An effective monitoring and review environment includes use of both periodic reviews, such as those undertaken by internal audit and external consultants, as well as in-built review mechanisms.

6.2 Performance measurement is widely recognised as a key tool by which organisations can monitor performance. One of the main advantages of performance measurement is that it enables organisations to express the results of a business process in quantitative, not qualitative, terms.

6.3 By providing reliable, quantifiable data to evaluate business processes, performance measurement allows organisations to provide feedback about current performance and to set relevant, identifiable goals (targets) for future improvement. Moreover, it has long been acknowledged that, in general, 'what gets measured gets done'. That is, the practice of measuring a task or activity focuses direct attention on it, and as a result, people will naturally strive to improve the result. It is therefore integral to any continuous improvement environment. Performance measurement is also integral to the internal control environment as it helps an organisation identify process problems as they occur, often well before the problems adversely affect outputs and outcomes.

6.4 In addition to the monitoring of performance measures, the effectiveness of the control structure itself also needs to be monitored and reviewed. Control monitoring and review can be undertaken in various ways, including by:

- on-going monitoring which is an inherent part of the process, such as control self assessment, and by encouraging staff to identify breakdowns, redundancies, duplications and gaps in control procedures; and
- separate periodic reviews and evaluations, such as internal audit or process reviews. These reviews look at the effectiveness of control structures from another perspective and often provide the opportunity for on-going monitoring procedures to be revisited.

6.5 The scope and frequency of monitoring and review activities will depend primarily on an assessment of risks and the effectiveness of on-going monitoring. The greater the on-going monitoring, the less need there will be for separate evaluations. It is also important to note that the effectiveness and appropriateness of the control framework can change as the environment changes.

Business benefits of monitoring and review

6.6 Monitoring and review provides assurance and feedback on whether program objectives are being achieved efficiently and effectively. The component also provides an on-going check on the effectiveness of the internal control framework. Activity in this area significantly impacts continuous improvement. Periodic monitoring and review is often aligned with the sharing of ideas, both across the organisation and externally. This is associated with the benefits of obtaining independent and objective views. In-built monitoring and review mechanisms encourage ownership of controls as well as enhancing the internal control framework.

Audit findings and comments

Summary table

6.7 The following table summarises the monitoring and review audit findings.

Table 10

Monitoring and review

<i>Principle</i>	Monitoring and review takes place on an appropriate periodic basis that enables the organisation to check the internal control framework and help ensure the organisation's strategic objectives are being achieved.
<i>Audit evaluation criteria</i>	Organisations would be expected to have regular monitoring and review processes in place to ensure that policies and procedures are adhered to and properly applied. There would also be an expectation that processes would exist whereby required changes and weaknesses in the operating environment could be identified; this might be achieved by reporting against performance measures and through internal checking and auditing processes. The results of this process would then be input into the next round of strategic planning and risk assessment performed by the organisation.
<i>Audit findings</i>	In relation to the eight organisations reviewed, the audit found: <ul style="list-style-type: none"> • six of the organisations had not identified performance measures for the accounts receivable function; and • seven of the organisations do not use control self assessment as a monitoring and review tool.

continued next page

<i>Sound and better practices noted</i>	<p>The audit noted the following in some organisations:</p> <ul style="list-style-type: none"> • internal audit reviews of the accounts receivable and associated functions are undertaken on a periodic basis; and • performance measures were established and are regularly reported on.
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6.8 The audit found that organisations had scope to improve the monitoring and review of the accounts receivable function to ensure both organisational and control objectives were being achieved efficiently and effectively. In particular, this could be achieved through the introduction of monitoring and review of performance measures, and through the use of control self assessment.

Performance measurement and reporting

6.9 Performance measures provide management with sufficient knowledge to make informed decisions on the performance of the function. The development of performance information is particularly important as organisations begin to market test³¹ their corporate functions. Examples of potential performance measures and existing benchmarks for accounts receivable are detailed in Appendix 3.

6.10 The audit found three organisations were regularly reviewing performance indicators for the accounts receivable function. The indicators were quantifiable, for example, the level of current debt versus overdue debt, and were reported on a monthly basis to operational management.

6.11 The remaining five organisations had not identified any performance measures for the accounts receivable function or investigated how the data might be collected for reporting purposes.

Monitoring and review of the control structure

6.12 While the governing body of an organisation is responsible for the control framework, individual senior and line managers can facilitate operational improvement through taking responsibility for the framework within the areas of their control.

6.13 The ANAO has identified control self-assessment as a better practice in monitoring and review activity.³² Control self assessment is a reporting process where managers are actively responsible for developing, assessing, maintaining and monitoring the controls within their own areas of responsibility. This usually involves the completion of self-assessment

³¹ Process whereby Commonwealth organisations compare the efficiency and effectiveness of services performed internally to what could be provided by an external organisation.

³² op. cit., p. 24, *Controlling Performance and Outcomes, Better Practice Guide to Effective Control*.

checklists to confirm that control processes and procedures are clearly understood, implemented and are operating effectively. The checklist data can be collated along with other financial and operational performance data into reports.

6.14 Seven of the organisations had not adopted formal control self-assessment processes in the accounts receivable function as a mechanism to build-in regular monitoring and review. However, one of these organisations did have a quality assurance package but it did not focus on the controls used within the accounts receivable process.

6.15 Two organisations had used the internal audit function to monitor the accounts receivable and associated functions by undertaking compliance reviews, and to assess the controls included within the processes and procedures. The other organisations did not conduct any formal reviews to ensure compliance with the policies and procedures of the organisation or to assess the adequacy of these guidelines.

Conclusion

6.16 The audit highlighted that organisations had underestimated the importance of monitoring and review. Only three organisations had developed performance indicators as well as mechanisms to report against them regularly. Only two organisations had performed reviews of the accounts receivable process.

Recommendation No.7

6.17 The ANAO recommends that organisations:

- establish appropriate performance indicators for the accounts receivable function;
- provide performance information against these indicators in their regular management reports; and
- implement regular monitoring and review procedures to measure performance against the indicators put in place.



Canberra ACT
11 December 2001

P. J. Barrett
Auditor-General

Appendices

Appendix 1

About this audit

1. Assurance and Control Assessment (ACA) audits are undertaken under the general performance audit provisions (section 18) of the *Auditor-General Act 1997*. They examine the internal control frameworks supporting common business support activities and processes that are not specifically covered by financial statement or other performance audits. Audit evaluation criteria are based on the five interrelated components of the internal control framework³³, namely:

- risk assessment;
- control environment;
- control activities;
- management information and communication processes; and
- monitoring and review processes.

Performance information

Timeframe

2. Planning for this audit commenced in January 2001 with research into accounts receivable practices and private industry experience. Audit work was undertaken as follows:

- understanding and research—January and February 2001;
- in-depth fieldwork—March to June 2001; and
- reporting—July to December 2001.

3. The ANAO provided a report on the results of the audit to each organisation reviewed. The reports included a number of specific recommendations relevant to those organisations.

4. The elapsed time from the commencement of the audit to tabling this Report was eleven months and the cost was \$235 100.

³³ op. cit., p. 24, *Controlling Performance and Outcomes, Better Practice Guide to Effective Control*.

Appendix 2

1997–98 FCA Audit and Better Practice Guide— Management of Accounts Receivable

Background

1. In 1997–98, the ANAO undertook a financial control and administration audit of the accounts receivable function across a number of Commonwealth organisations³⁴.

2. The report tabled in Parliament on 23 December 1997, concluded that at both the strategic and operational level improvements could be made in the management and administration of the accounts receivable function in the general government sector. The ANAO recommended that improvements could be made by:

- establishing a comprehensive and clear policy framework which has been endorsed by executive management;
- identifying, analysing and assessing risks to revenue collection;
- transferring responsibility for strategic decision making in relation to debtor management to program managers;
- strengthening management reporting and performance measurement;
- integrating sale and billing systems;
- introducing alternative payment options; and
- developing a more structure approach to the recovery of debt.

3. The findings of the report are summarised below:

- based on available data, the ANAO estimated that the direct labour costs associated with the accounts receivable function in the Commonwealth are significantly higher than those of the private sector;
- in most organisations managers responsible for service delivery had no responsibility for management of the debt arising from the services. This was the role of Corporate Services. It is considered that improvements can be achieved in debt management by removing this separation of responsibility;
- some organisations had not developed written accounts receivable policies and those in place did not effectively address all aspects of the management of the function;

³⁴ op. cit., p. 12, Financial Control and Administration Audit, *Management of Accounts Receivable*.

- organisations had not undertaken risk assessments of either their revenue collection or accounts receivable functions. They therefore were not in a position to manage these risks;
- current management performance reporting mechanisms do not enable management to exercise ongoing control over the accounts receivable function; and
- in relation to debt owed by one Commonwealth organisation to another, through increased use of direct credit arrangements, cost savings from reduced debt follow-up action could be achieved.

Assessment of progress

4. Based on the recommendations made in the 1997–98 report, an assessment was made to determine what progress had been made in the eight agencies involved in the current audit.

<i>Recommendations</i>	<i>Progress since December 1997</i>
Management control and performance measurement	
Organisations integrate their sales and billing systems and extend their business systems to decentralised operations that generate significant revenues and debtors.	All organisations had implemented FMIS that had integrated sales and billing systems. One organisation's FMIS was unable to be made accessible to decentralised operations. This organisation was in the process of replacing its system for one that included this feature.
Investigate the use of alternatives to managing debt arising from credit sales, including promoting payment by direct credit of bank accounts, credit card and through agents.	Commonwealth organisations are making greater use of direct credit and credit cards where their debtors have been receptive to the idea. Where a Commonwealth organisation's average debtor is a small organisation or an individual the adoption of direct credit or credit cards has been slower than where the debtor is a large organisation. Three organisations have external collection agents for recovery action on old debts.
Adopt a structured approach to the recovery of debts, including the use of specialist debt collection staff, more timely identification of overdue debts and improved criteria against which write off or waiver of debts can be tested.	One agency required additional detail for its debt recovery procedures. The other organisations had clear procedures on what action was to be taken to recover a debt and, therefore, what information was required to determine if it should be written off. All agencies had employed specialised debt collection staff and had a structured approach to identifying overdue debts in a timely manner.
Review functional responsibilities of managers with the aim of linking the responsibilities of program and service delivery and accounts receivable management, where programs and services result in revenue generation.	In all organisations, functional managers had input to the debt recovery process. Only in one organisation was the functional manager specifically responsible for accounts receivable management. The other organisations found it more effective to retain the management of accounts receivable centrally and consult with the functional managers on a case by case basis.

continued next page

Recommendations	Progress since December 1997
Policy framework	
Organisations review policies for the management of accounts receivable to ensure that all key elements, including modes of payment, strategies for the collection of debt, handling of customer inquiries and credit management are addressed.	All organisations had policies for the management of accounts receivable in place. As noted below, three were in the process of being updated. As noted in Chapter 4 of this report, a number of key elements/better practice items had not been included in all policy documents.
Obtain approval of the accounts receivable policy by executive management prior to promulgation to staff.	Three organisations were in the process of updating their policies. The majority of these policies were being updated as a result of changes to systems. The changes to systems had resulted in changes in procedures that were already being performed, although executive management had not specifically approved the new policy.
Make existing and potential credit customers aware of the key elements of the accounts receivable policy prior to any sale taking place.	The majority of organisations included in this review have existing customer bases. New customers, when identified, are made aware of key elements of accounts receivable policy prior to sales taking place.
Risk Assessment	
Organisations monitor and regularly review debt outstanding in excess of 90 days with a view to seeking, where appropriate, approval to write the debt off.	Debt management activities always result in an assessment of whether attempts should continue to recover debts or whether writing the debt off would be more efficient. All organisations except one, monitored their debts on a regular basis. The one exception had resourcing problems and therefore, actions were not up to date. The organisation was in the process of removing the backlog.
Establish credible performance indicators for measuring the effectiveness and efficiency of the accounts receivable function.	Performance indicators have not been identified for the entire accounts receivable function in five out of the eight organisations audited.
Develop regular reporting mechanisms for monitoring actual performance against the indicators and clear procedures for actioning the related reports by executive management.	All organisations had developed some form of regular reporting mechanism. However, as performance measures have not been identified in the majority of organisations audited, reporting against these has not occurred.
Inter-agency transactions	
Where practicable, all inter-agency payments should be made by way of direct credit, immediately following any verification process.	Inter-agency payments are generally being made by direct credit in line with <i>GovernmentOnline</i> requirements.

Better Practice Guide 1997–98

5. Following the audit conducted in 1997 the ANAO prepared and published an accompanying Better Practice Guide³⁵. This guide intended to “provide an overview of the current trends and better practice approaches that are being adopted by organisations in managing accounts receivable. The guide highlighted the following items as the trends and better practices:

- Organisational culture—management attitudes need to support practices for minimisation of debt.
- Use of:
 - Centralised processing—this provides a number of benefits for the organisation including the achievement of a high degree of specialist expertise in the function supported; the establishment of centres of excellence that develop and enforce common practices and standards; and the achievement of cost efficiencies through the co-locating of systems and staff.
 - Standing payments—this is an alternative payment approach for organisations that deliver services on a regular basis resulting in recurring invoicing and receipting cycles. The customer can make standing payments that are reconciled to services provided on an annual or bi-annual basis. This approach reduces costs through the removal of the need for an invoicing and debt collection function, and more timely receipt of revenues.
 - Alternative payment options—organisations have a number of modern payment methods available to them that provide for added customer service, reducing remittance processing costs and improving cash flow through faster debtor turnover. These methods include direct debit, integrated voice response, outsourced agency collection, lock box processing and data kiosks.
 - Payment incentives—discounting can be used as an incentive for customers to pay upon receipt of services, and avoiding the use of credit terms. In addition to developing a range of incentives for early payment organisations should consider the imposition of penalties on late payment.
 - Case management approach—under this approach all aspects of the agency-customer relationship are drawn together including debt management. The increased knowledge of the customer that

³⁵ op. cit., p. 14, Better Practice Guide, *Management of Accounts Receivable*.

derives from the adoption of the case management approach can assist in the design of strategies for the prompt repayment of debt.

- Risk assessment of debt management processes—risk assessment is a major component in the establishment of an effective control structure. Once risks have been properly identified, controls can be introduced to either reduce risks to an acceptable level or to eliminate them entirely. A proper risk assessment also creates opportunities for freeing processes from inefficient practices.
- Use of advanced technology:
 - Systems integration—the major benefit of having the revenue and accounts receivable systems integrated is the necessity to download and re-key data is avoided;
 - Electronic commerce—electronic commerce is a term applied to the use of computer and telecommunications technologies, particularly on an inter-organisational basis, to support trading in goods and services. It uses technologies such as electronic data interchange (EDI), electronic mail, electronic funds transfer (EFT) and electronic catalogue systems to allow the buyer and supplier to transact business by exchanging information between computer applications systems. This achieves cost savings by removing the need for direct negotiation between the parties.
- Streamlined debt collection process—this ensures that only necessary processes are undertaken to ensure that outstanding amounts are minimised.
- Regular performance measurement—organisations should develop a suite of indicators that will measure progress over time. The effectiveness of the accounts receivable process as a whole should be measured as well as the effectiveness of specific debt collection techniques.

6. These trends and better practices are still relevant in the current environment.

7. Appendix 4 details the better practice policy document and recommended contents developed as part of the 1997–98 Better Practice Guide.

Appendix 3

Performance Measures³⁶

1. To ensure that management receive constant feedback throughout the business process, organisations can use performance measures. These allow management to determine whether an organisation is or is not performing in accordance with expectations. To do this, organisations can split performance measures into the three following measures:

- Key objectives—to articulate the performance results the company expects from the business process.
- Outcome measures—to determine whether the company has reached the key objectives. The outcome measures are usually chosen based on the organisation's overall business goals and are intended to demonstrate the impact of a process on the organisation's finances, efficacy, and efficiency. Senior management analyses outcome measures to keep score on organisation performance and to help control and allocate resources for improvements.
- Activity measures—to monitor the performance of those activities that are instrumental in reaching the key objectives. Activity measures detail the journey along the path toward the outcome measures by tracking improvements in process-specific activities over a period of time. Activity measures address issues of concern to the individuals in charge of carrying out those process-specific activities.

³⁶ Global Best Practices www.knowledgespace.com – Andersen GBP

Key Objective	Outcome Measures	Activity Measures
Reduction of bad debt	Bad debt write-offs as a percentage of total sales	<ul style="list-style-type: none"> • Anticipated amount of uncollected invoices over 60 days past due, by account, by month • Number of invoices and percentage of funds over 180 days past due and number of unapplied credit memos over 180 days old • Top ten list of the ten worst paying accounts, by month • What is the number of account write-offs? • Percentage of bad debt in Accounts Receivable. • How much bad debt does the organisations write off, calculated as a percentage of sales? • What is the average days past due?
Accelerated cash flow	Days' Sales Outstanding	<ul style="list-style-type: none"> • Percentage of receivables over 30, 60 and 90 days past due • Percentage of balance due collected, by month • Forecast of funds to be collected before the end of the month • Percentage of invoices containing errors each month • What is the number of and dollar amount of on-time, full pay accounts? • How much cash was collected in excess of organisational goals?
An accounts receivable process that enhances good customer relationships	The number of customer complaints the company receives regarding credit applications and invoices in a month	<ul style="list-style-type: none"> • The number of overdue invoice balances associated with customer dissatisfaction • The average length of time it takes to resolve customer invoice and payment disputes • The average length of time it takes to process credit applications • Percentage of invoices containing errors each month • Average number of customer complaints per month.

Key Objective	Outcome Measures	Activity Measures
Low cost to collect receivables	Total accounts receivable cost per full-time equivalent employee	<ul style="list-style-type: none"> • The percentage of accounts receivable transactions (including invoices, payments, shipment tracking and proofs of delivery) that move electronically, such as via EDI or the Internet • “Hit rate”—the percentage of payments an automated cash application system is able to match to invoices without employee intervention • Number of days or hours of processing float; that is, the length of time between receipt and posting of payment • Percentage of payments with errors
	Average of amount collected per credit and collections representative	<ul style="list-style-type: none"> • Number of active accounts per credit and collections representative • Percentage of time credit and collections representatives spend on the telephone with customers • Average number of days within which past due accounts receive a telephone call • The percentage of customer promises kept regarding payment per credit and collections representative • How many days lapse between the receipt of payments and the posting of payments? • How much cash was collected in excess of individual goals? • By what percentage did each collection agent reduce the balance due in the agent’s account portfolio?

Appendix 4

Better Practice Contents of Policy or Procedure Documents for the Accounts Receivable Process

This information was first published by the ANAO as part of the Management of Accounts Receivable Better Practice Guide in 1997.

1. The policy is endorsed by an Executive Officer.
2. The policy is based on a risk assessment of the agency and its customers. This is recognised in the document by stating the risk factors.
3. The policy:
 - Explains the nature of debts and debtors.
 - Outlines the agency's rights and duties with debtors; and legal consequences.
 - Details the terms of trade and circumstances when a delegate may change the terms of trade.
 - Identifies other related procedures manuals, legislation that can guide processing of debts.
 - Outlines mode of payment accepted and under what conditions (eg any transaction less than \$1000 must be by credit card).
 - Identifies mechanisms for reviewing requests from debtors.
 - Outlines general procedures for handling unusual requests or events.
 - Outlines who is responsible for debt collection.
 - States how and when to communicate with a debtor regarding an overdue amount.
 - States procedures to recover debts from employees.
 - Lists options for recovering an overdue debt (eg allow instalments).
 - Describes the use of commercial debt collection agencies.
 - Identifies who has the authority for determining the mode of collecting an overdue debt (eg. instalments) and identifies circumstances to guide the decision.
 - Identifies when to record a debt as overdue (including whether a period of grace applies).
 - Details procedures for imposing charges.
 - Details the preparation of and requirements for certain report production.
 - Identifies means of monitoring debts.

- Outlines the process of managing dishonoured cheques.
- Lists circumstances when debts no longer need to be pursued and who has the authority to decide not to pursue a debt.
- States clear and comprehensive standards of performance (including the desired relationship with the customer) and targets for the timing of debt collection (eg. 80 per cent within 30 days from date of invoice).
- Details the requirements to review the policy and procedures—when, by whom.

Better Practice Items for Invoices

This information was published by the New South Wales Audit Office as part of the Guide to Better Practice Debtors Administration in 1998.

- Is the invoice clearly addressed?
- Does it provide enough information for the individual to understand why payment is being requested?
- Does the invoice avoid jargon that may be unfamiliar to the reader, particularly if English is not their first language? Does the invoice avoid extraneous detail that may distract the reader?
- Does the invoice clearly stipulate who is exempt from the charge or eligible for a reduced charge and the procedure for substantiating this status?
- Is the due date highlighted?
- Is any essential reference number highlighted?
- Is a contact name and telephone number given for inquiries?
- Are penalties for late payment stated?
- Does the same customer always have the same customer code?
- Does the invoice contain a tear-off remittance advice with clear instructions that this should be submitted with payment?
- Does the invoice make clear that a receipt will not necessarily be issued for non-cash payments? Does it contain a facility so that customers can indicate if they require a receipt?
- Does the invoice clearly indicate the type of payments accepted (cheque, credit card) and methods that can be used (telephone, agencies, personal payment, bank transfers, etc)?

Appendix 5

The accounts receivable process

1. The following three flow charts detail the activities undertaken as part of the accounts receivable process. For ease of use, the process has been separated into three distinct parts—generating a debt, receipting and debt recovery.

Figure 1

Process for generating a debt

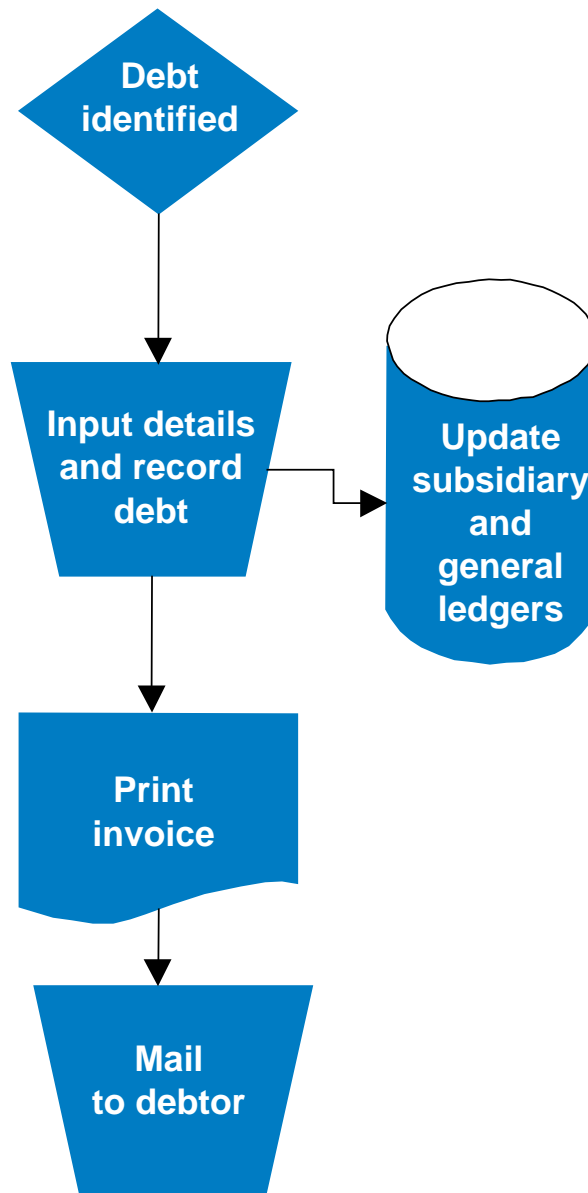


Figure 2
Receiving process

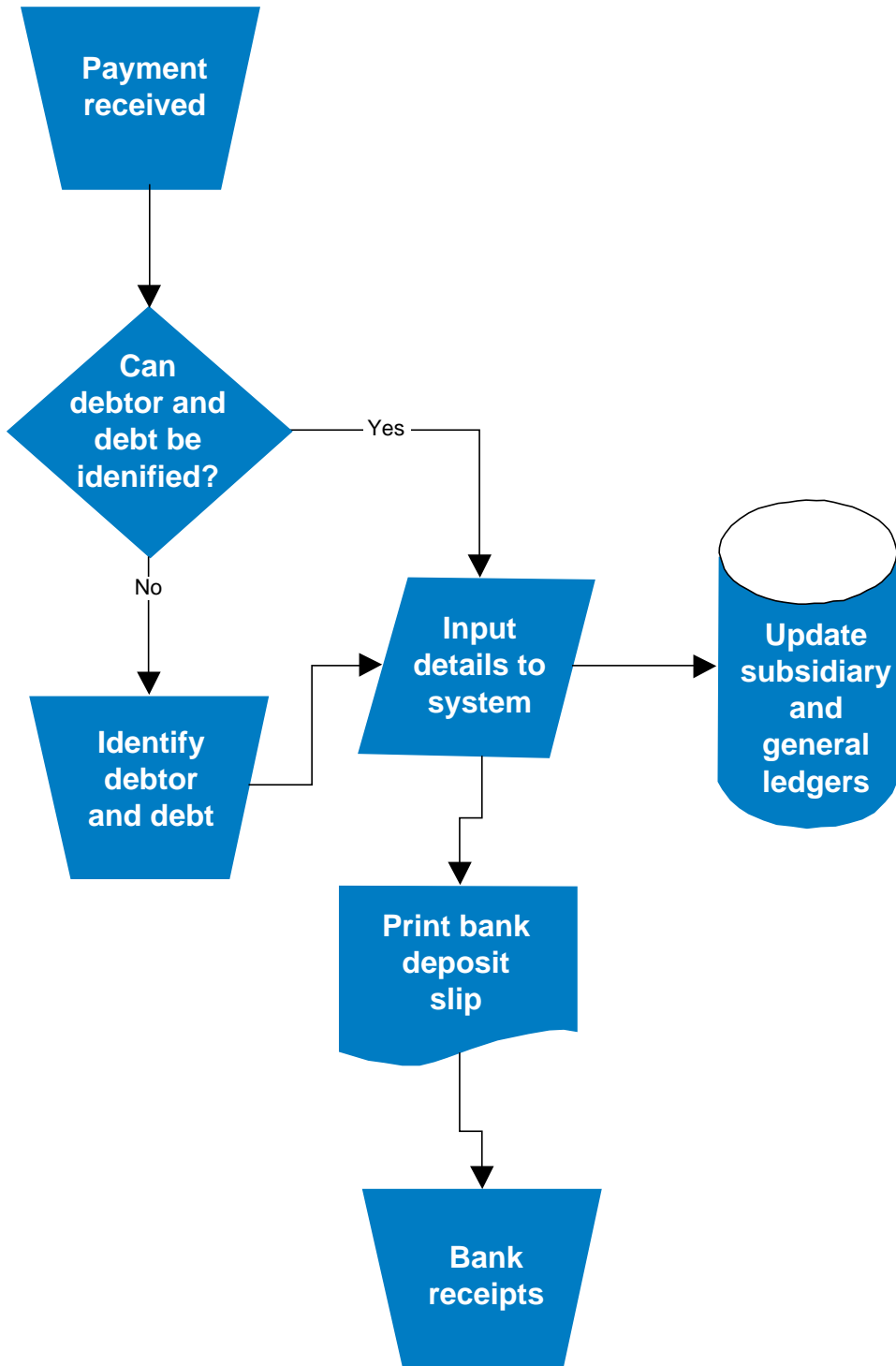
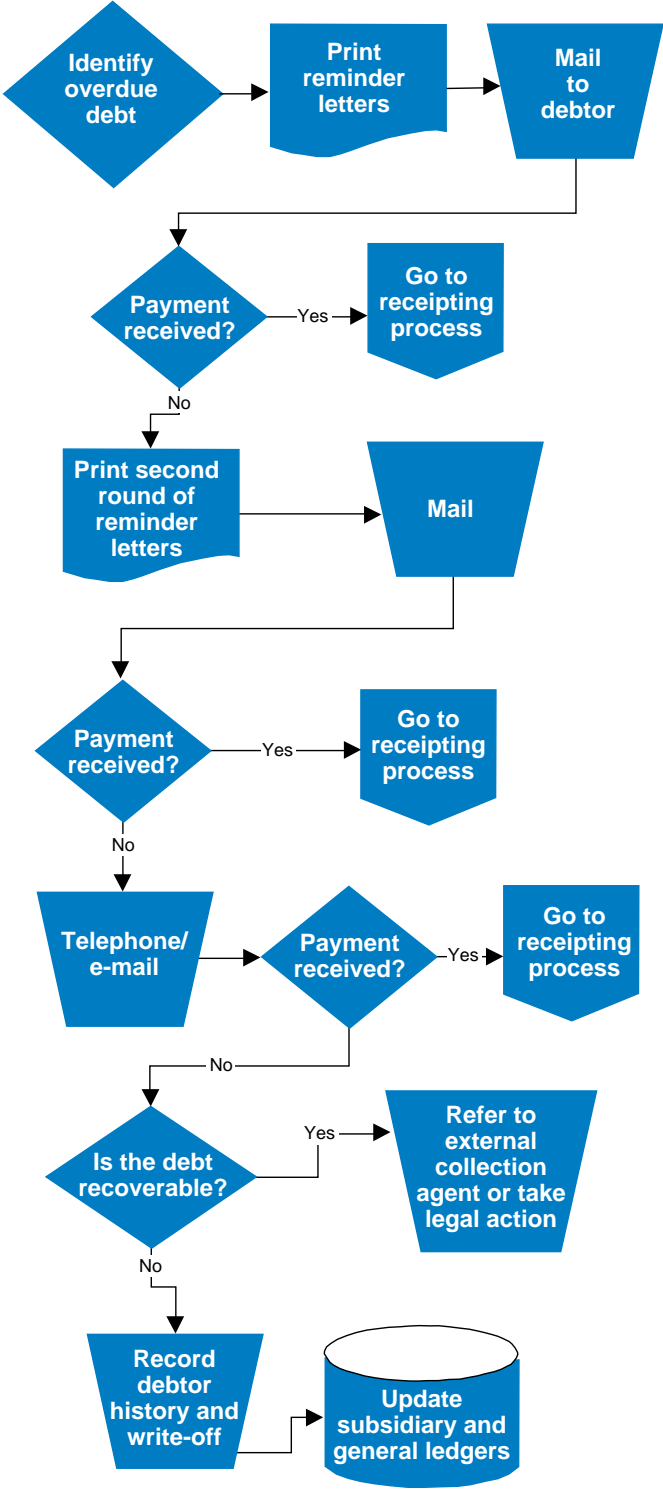


Figure 3
Process for managing overdue debts



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