

INTERNAL AUDIT



The Honorable Mayor Kim McMillan
City Council Members
Audit Committee Members
Clarksville, Tennessee 37040

Executive Summary of City General Payroll Audit

The following is an executive summary of the findings and management's comments in response to the findings related to the internal audit report on the City General Payroll Audit. The full audit report is attached and contains additional details about the findings and recommendations as well as background information.

The objectives of the audit were to:

- Report on City General payroll activity from January 2011 through June 2012.
- Determine compliance with Federal and State payroll-related law related to compensation and payroll records.
- Determine compliance with City Code and City Human Resources policy.
- Determine whether Fox Lawson & Associates pay study scales were properly implemented.
- Evaluate payroll-related local policy and procedures (City Code and City Human Resource Policy) for compliance with the Fair Labor Standards Act (FLSA) requirements.
- Evaluate the design and effectiveness of internal controls over the payroll process during the audit period.

Our audit revealed the following results related to our original objectives:

- Based on our statistical sample of 259 payroll transactions out of a total population of 34,198 transactions during the period January 2011 through June 2012, we are 95% confident (3% tolerable error) that all transactions are accurately calculated and properly supported.
- Our testwork revealed the following in regard to compliance with Federal and State payroll-related laws:
 - Supporting documentation required by the Employee Retirement Income Security Act of 1974 is not being maintained for the 5 retired employees that are paid directly by the City under the old retirement system.
 - Supporting documentation required by the Tennessee Lawful Employment Act is missing in 17 out of 30 files tested for compliance with the Act.
- Our testwork revealed the following in regard to compliance with City Code and City Human Resources policy:
 - Required annual evaluations are missing for either 2011 or 2012 in 44% of the personnel files.
 - Standard City procedures were not followed in promoting an HR employee.

One Public Square / Suite 315 / Clarksville, TN 37040
(931) 648-6106 / Fax (931) 645-7408
www.lynn.stokes@cityofclarksville.com
www.jim.mcnaughton@cityofclarksville.com
www.robin.manley@cityofclarksville.com

- Based on our testwork regarding the implementation of the Fox Lawson & Associates study, we are 95% confident that City General employees were paid in accordance with the FLA study during the period tested.
- Our testwork revealed the following in regard to City policy and procedures related to the requirements of the Fair Labor Standards Act:
 - Some departments don't require full time, regularly scheduled, non-exempt employees to document their hours as mandated by the Act.
 - Some departments have policies related to paid overtime and comp time that put the City at risk for being out of compliance with the Act.
- Our evaluation of the design and effectiveness of the internal controls surrounding the payroll process revealed the following:
 - In general, internal control procedures are adequately designed and operating effectively. However, we found two significant deficiencies in control procedures related to the following:
 - Two employees have payroll functions that are not sufficiently segregated. They have authority to both process payroll and/or set up new employees and/or change pay rates.
 - Thirteen employees are currently identified in Munis software as payroll superusers. Superusers are granted broad permissions in the payroll module. These employees' access is restricted by the screens they are able to view instead of restricted by permissions to certain payroll functions.

During the conduct of the audit, the auditors became aware of several situations or procedures that prompted them to make three additional recommendations to management.

- A change from semi-monthly to bi-weekly payroll periods and the adoption of a five business day payroll lag time would create a number of efficiencies in the payroll process;
- The creation of a system to document and retain management position papers related to policy interpretations would help eliminate confusion over past interpretations and decisions;
- Tracking and analyzing paid overtime and comp time by the departments on a systematic basis would facilitate sound business decisions in regard to the use of those payment options as opposed to hiring temporary or seasonal employees.

Management agrees with all of the findings and recommendations set forth by the auditors in the report. Full details can be read in the complete report.

Internal Audit would like to thank Human Resources and the various other departments for their assistance during the conduct of the audit. We received willing support on every level.

If you have any questions about the audit, the findings, or the recommendations please contact me at 648-6106.

Respectfully,



Lynn Stokes
Director of Internal Audit

cc: Debra Frazier, Interim Director of Finance
Will Wyatt, Director of Human Resources



INTERNAL AUDIT REPORT

AUDIT TITLE:	PAYROLL AUDIT
DEPARTMENT:	CITY GENERAL
AUDIT PERIOD:	JANUARY 2011 THROUGH JUNE 2012

CITY OF CLARKSVILLE

CITY GENERAL

PAYROLL AUDIT
AUDIT # 1305



Auditor



Audit Director

April 16, 2013

Date

**CITY OF CLARKSVILLE
INTERNAL AUDIT REPORT**

City General Payroll Audit

Table of Contents

Origin of Audit.....	1
Audit Objectives.....	1
Scope and Methodology of Audit.....	1
Statement of Auditing Standards	2
Background	2
Internal Controls and Compliance with Regulations.....	3-9
Results of the Audit	
Findings.....	10-18
Other Recommendations.....	19-20
Conclusion.....	20-21

Internal Audit Report

Origin of the Audit

The Internal Audit department reviewed the City of Clarksville's General Fund (City General) payroll to provide assurance and advisory services related to payroll. This audit was included in the FY 2013 Audit Plan approved by the Audit Committee.

Audit Objectives

Our objectives for this audit were to:

- Report on City General payroll activity from January 2011 through June 2012.
- Determine compliance with Federal and State payroll-related law related to compensation and payroll records.
- Determine compliance with City Code and City Human Resources policy.
- Determine whether Fox Lawson & Associates pay study scales were properly implemented.
- Evaluate payroll-related local policy and procedures (City Code and City Human Resource Policy) for compliance with the Fair Labor Standards Act (FLSA) requirements.
- Evaluate the design and effectiveness of internal controls over the payroll process during the audit period.

Scope and Methodology of the Audit

Our audit scope included tests of payroll compliance related to compensation on the federal, state and local (City Code and City Human Resource policy) level.

The scope did not include an audit of benefits or payroll deductions.

Our audit scope included the City General internal control structure and the payroll transaction activity during the selected audit period (January 2011 through June 2012). We assessed the effectiveness of the controls by assessing the accuracy of the existing payroll process and structural adequacy and the sustainability of the internal control structure.

The audit scope included an evaluation of IT payroll permission controls, but did not include an evaluation of the financial systems or the adequacy or design of IT or financial systems.

Evidence to support our conclusions was gathered from direct inquiries of management and staff as well as observations of source documentation and tests of the controls surrounding the transaction approval, calculation, and record keeping requirements of the payroll process. From a population of 34,198 transactions, we randomly selected a sample of 259 transactions and 217 associated employee personnel

files (217 employees selected out of 1299 employees paid during the period) for review. We expanded our sample to include all Human Resources employees.

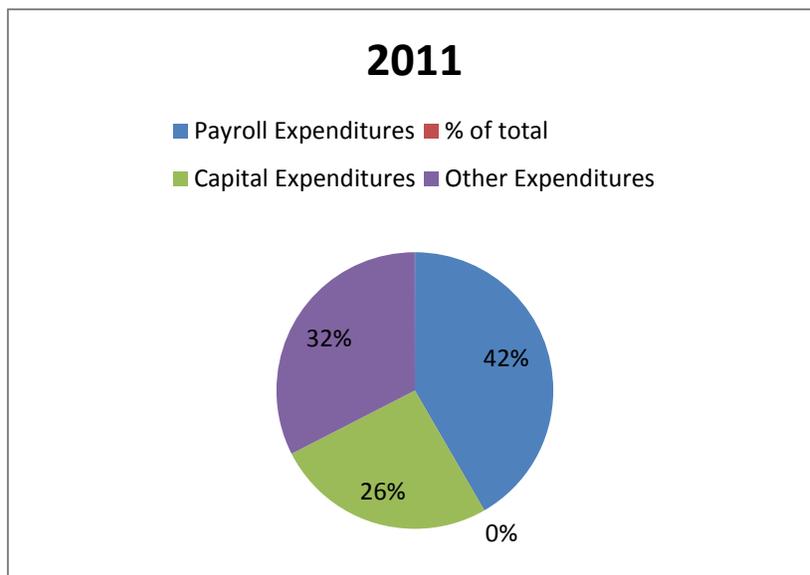
Statement of Auditing Standards

We conducted this audit in accordance with generally accepted government auditing standards as set forth in Governmental Auditing Standards issued by the Comptroller General of the United States, with the exception of the peer review. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

Reasons for inclusion in the Internal Audit plan:

In FY2011, payroll expense made up 42% of the City's total expenditures.



Source: Total and Capital Expenditures per CAFR for 2011 (Statement of Revenues, Expenditures and Changes in Fund Balance). Payroll and Other totals are from Munis (extracted and tied detail to total (+/- 1%))

In FY2011, payroll expense was \$46.8M which indicates an approximate 10.3% increase over the FY2010 expense. The main reason for the increase is the implementation of the Fox Lawson & Associates (FLA) pay study (phased in from 04/01/2011 through 5/31/2011). The FLA study reviewed all full time positions to determine the appropriate classification and pay grade for each position and employee. The implementation of the study aligns the labor rates for City employees with other municipalities in the region.

The City General payroll process:

Employee positions must be approved by Human Resources and supported by an approved City budget before they can be filled. When an employee fills a position, they are assigned a position control number (proves the position is budgeted), and an employee control number. After their employee number has

been assigned, their rate of pay, work schedule, pay schedule, and personal information are entered into the City's Munis payroll system.

Employees are paid on a semi-monthly schedule. There is no payroll time-lag for the City's full time employees so estimates are made for time worked at the end of each pay period. These estimates are reconciled to actual time worked in the follow-up pay period.

City payroll is approved at the department level, but processed centrally.

Each City General department management team is responsible to (payroll specific):

- Account for the hours worked, overtime worked, and leave used by department employees
- Assign a department "time keeper" to enter approved overtime and leave (Munis workflow process)
- Review and approve/deny requests for overtime and leave submitted on leave slips
- Review and approve/deny overtime and leave amounts entered (Munis workflow process)
- Ensure that records of all time worked, overtime, and leave documentation are maintained
- Track banked compensatory, holiday, and leave time for all department employees
- Send documentation to central payroll in support of hours worked and rates to be paid for any employees that do not have default hours set up in Munis
- Reconcile time worked against time paid in the previous period and send adjustment information to central processing
- Perform an annual performance evaluation for each employee in the department and send a copy to Human Resources department for filing

Central payroll processing is responsible to:

- Enter any new employee data (after approval)
- Enter previous period adjustments
- Enter time and rates for non-hourly default employees
- Check that all expected workflow approvals occur
- Process the payroll
- Print and maintain payroll reports
- Maintain any documentation that has been sent up through department channels
- Request payroll related liability payments

Human Resource department is responsible to (payroll specific):

- Maintain personnel files that support employee setup, pay, and performance
- Provide guidance through Human Resource policy and procedure
- Assess compliance with City Code requirements
- Provide support for any benefits paid

Finance department is responsible to (payroll specific):

- Facilitate payroll check runs
- Manage the payroll funding
- Reconcile bank statement and other balance sheet payroll activity

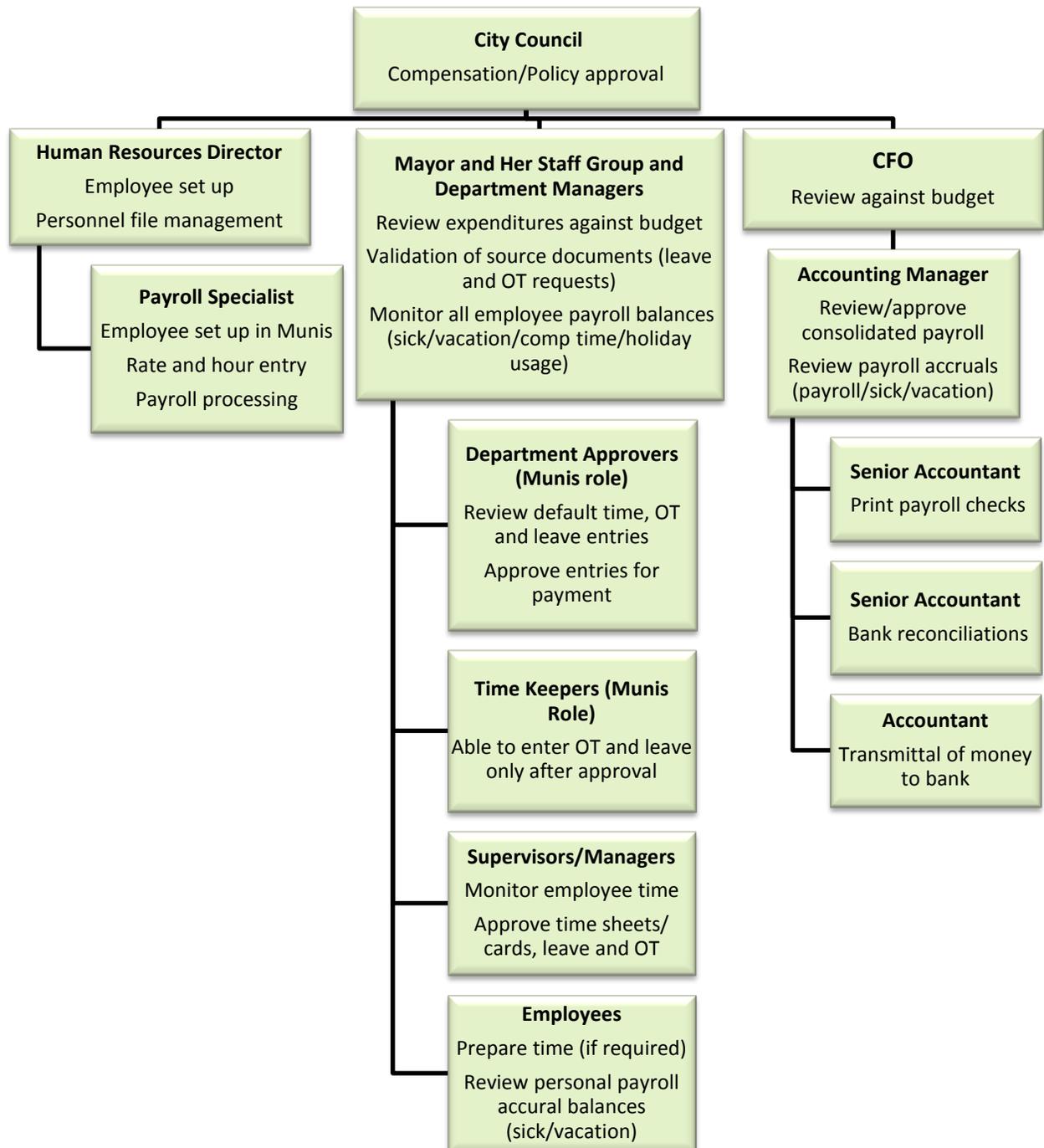
Information Technology is responsible to (payroll specific):

- Establish and maintain Munis workflow

In addition to the payroll transactions for regular employees, payroll transactions include incentive payments, longevity payments, and retiree benefits.

- Incentive payments are payments for meeting certain training or certification milestones are tracked by department management (fire and police).
- Longevity payments are annual payments made to each employee that has more than 6 years of service with the city. The amount paid is easily calculated (service years at a specified measurement date x specified rate).
- Retiree benefits are monthly payments to qualified retirees. The amount of these payments is constant during a given year. The amounts are impacted by cost of living increases (if approved in the annual budget process).

City General Payroll Role Chart



Internal Controls and Compliance with Federal and State Laws, City Code, and City Policies:

Relevant Procedures and Controls	Yes	No	Other	Status
Internal Controls: Do payroll procedures exist?	X			Procedures are not written. The procedures were determined through discussions with HR Payroll Specialist and department timekeepers and validated by observation, evidence in payroll backup, and evidence in personnel files.
Are the payroll process roles clearly defined and understood?	X			Roles are clearly defined and specific. The central role (Payroll Specialist) directs the process and monitors compliance.
Do procedures provide that all authorizations (new hires, status changes, separations) include Human Resource approval and document immediate transmittal to the payroll accountant?	X			Employee changes have to be signed by HR, department management, and the Mayor. Documented on status change forms. Authorization of default labor, OT and Leave is in workflow process. For non default employees timesheets or time cards document approval.
Segregation of Duties: Are key duties and responsibilities in authorizing, processing, recording, and reviewing transactions segregated?		X		Processing is centralized but fed by workflow approval, reporting is centralized, but reviewed by Accounting Manager. Check printing is performed by Accountant. Reconciliation is performed by Senior Accountant. Payroll Processing role and Employee Setup role assignment's back each other

Relevant Procedures and Controls	Yes	No	Other	Status
Does the software system access prevent any one employee from unilaterally changing payroll?		X		<p>up. Those roles need to be separated. No one should have access to both functions at the same time.</p> <p>IT(3), the Payroll Specialist, and 9 other employees have full payroll rights. Currently restricting views is the only means to control access. All changes are stamped with the identity of the initiator.</p>
Are controls in place to prevent the person who prepares the time sheets from changing the time after approval?	X			<p>Default time or time sheet time card approval. Once time cards are approved they are never sent back to employees for changes. Time is validated through Munis workflow. Any adjustments (after submission) are made after review and approval in a following period.</p>
Are overtime hours, standby time worked, detailed and approved prior to being paid (by someone other than who prepares payroll)?	X			<p>All timesheets, overtime and leave approvals are approved by the department management. They are included as support for the payroll in which they were paid (held by department).</p>
Are time sheets, overtime approvals, and leave form approvals documented and maintained?	X			<p>All have approval documented. Held at the department. Approval is also documented generally in the Munis workflow process.</p>
Is access to personnel files restricted?	X			<p>Held in HR. Locked room except during business hours when access to the room is monitored and restricted. Access restricted to auditors, those with payroll roles, and management as needed.</p>

Relevant Procedures and Controls	Yes	No	Other	Status
Is access to payroll files restricted?	X			Placed in cabinets in Payroll Specialist office. Office locked at night. Access provided on as needed basis for management and auditors.
Is Munis payroll system access restricted appropriately for those with payroll roles?		X		Full access for IT (3), Payroll Specialist, and 9 other employees have full payroll rights (only view restricted). Department Approver role has the rights to validate payroll entered by default and the timekeeper (workflow). Department Timekeeper role has the rights to enter approved OT and leave requests into Munis. Changes by any one individual are stamped with the EE's identifier. Access for those with full rights is restricted through the establishment of procedures not by system limitations.
Is Munis payroll system access confined to those with a payroll role?		X		IT (3) and Payroll Specialist have full rights and views, and there 9 other employees with full rights but limited views. Any activity is stamped with the EE's identifier.
Is check stock secured?	X			Finance controls check stock. They hold the stock in a fireproof bank type safe. The electronic signature thumb drive is secured in the same safe. An accountant monitors the safe access during the day. Checks are approved by Accounting Manager who receives the payroll support file. Once

Relevant Procedures and Controls	Yes	No	Other	Status
<p>Does the City maintain adequate bank account controls over payroll?</p> <p>Is the ability to transmit funds to the bank segregated from the ability to prepare payroll?</p>	<p>X</p> <p>X</p>			<p>printed, checks are sent to Human Resources for distribution.</p> <p>The City maintains a separate bank account for payroll clearing. The activity is nominal (bank transmittal, a handful of checks, and payments of payroll liabilities). The balance of the account once all checks, the transmittal and payroll liabilities clear is \$0.</p> <p>The preparer of payroll releases the payroll once it is determined to be supported and approved at all levels. The Accounting Manager reviews and gives final approval for the transmittal.</p>
<p>Procedures to ensure that payroll is properly calculated:</p> <p>Verify the time paid against supporting documents:</p> <p>a. Time sheets (Hourly and Salary NE)</p> <p>b. Default time</p> <p>c. Overtime (Hourly and Salary NE)</p> <p>d. Leave (vacation/sick/other)</p>	<p></p> <p>X</p> <p>X</p> <p>X</p> <p>X</p>	<p>X</p>		<p>Most full time non-exempt, all part time, and all seasonal employees fill out time sheets or time cards. However, there were 20/259 FT non-exempt employees who were paid on the basis of hours worked who did not have a time sheet or other validation to support their payments (managers/ supervisor review only).</p> <p>All FT start with the default and adjustments are made from there (OT, Leave, LWOP if applicable).</p>

Relevant Procedures and Controls	Yes	No	Other	Status
<p>Verify rate paid is documented and validated in the personnel file</p> <p>Verify the Overtime is calculated correctly</p> <p>Verify Vacation /Sick/Holiday/Other Leave on the timesheet is supported by validated leave forms or holidays</p>	X			<p>Personal status changes are in the personnel file. Automatic pay adjustments (mass changes) are not but can be verified through documented City Council actions.</p>
<p>Payroll policy and practice in compliance with Federal and State of Tennessee laws and City Code and City Human Resource Policy:</p> <p>Payroll policy and practice is in compliance with the Federal (FLSA and ERISA), and State guidance (related to hours, compensation, and record keeping)?</p> <p>Payroll policy and practice is in compliance with City Code (related to hours, compensation, and record keeping)?</p> <p>Payroll policy and practice is in compliance with Human Resource policy (related to hours, compensation, and record keeping)?</p> <p>Is the compensation in accordance with the Fox Lawson & Associates pay study after the implementation?</p>				<p>Could be a potential issue due to some unsupported hours worked for non-exempt (FLSA) employees and lack of support for retiree benefits (ERISA).</p> <p>It is a violation of City Code to give pay increases without performance evaluations. No evidence of performance evaluations was found in 16% of 2011 and 44% of 2012 centrally located personnel files.</p> <p>Personnel files do not support compliance with policy 91-3 "Employee Performance Evaluation"</p>

Results of Audit:

Auditor testing and research revealed the following findings:

1. Key supporting documentation is not being maintained for retirement benefits paid directly by the City.

Criteria: According to Section 209 of the Employee Retirement Income Security Act of 1974, (ERISA), an employer must “maintain benefit records with respect to each of [its] employees sufficient to determine the benefits due or which may become due to such employees.” DOL proposed regulations suggest that records must be maintained for “as long as they may be relevant to a determination of benefit entitlements.”

Condition: Currently the City has 5 retired employees that it pays directly each month under the City’s Pension Plan (a City funded defined benefit plan). These retirement obligations precede the current TCRS retirement plan (Tennessee Consolidated Retirement Plan) where all retirement payment and obligation tracking is the responsibility of the State.

There is no evident ownership and tracking of these retiree obligations. The only evidence that the retirement obligation exists other than the fact that payments are consistently being made is held in the City Finance Department – a department that plays no role in the payment or calculation of the obligation.

Cause: There is no permanent file for these retired employees as they all retired before personnel files were maintained in the current format.

Effect: Without a way to validate the obligation, the terms of that obligation, and a means to monitor these obligations, the obligations cannot be effectively managed. Without a file that supports the benefit we are paying, we risk being out of compliance with ERISA by not having documentation for the retiree benefit expenditure.

Recommendation: The City Human Resource Department should create a retiree personnel file for each of these 5 retirees. The file should contain:

- a. A copy of the Pension Plan the employee retired under
- b. The ordinance authorizing payment (with reasoning if Plan eligibility criteria not met but Retirement Committee approved the retirement anyway)
- c. The details behind any annuity purchased to provide a portion of the benefit
- d. Any required payment adjustments (COLA, etc...)
- e. The end of obligation condition (i.e. termination upon death or spousal benefit).
- f. The progress of the repayment for any outstanding overpayment.
- g. Documentation of contacts made between the retirees/their representatives and the City.

Responsible Department: Human Resources

Management Comments: Management agrees that the files need to be brought up to date.

Agree X

Disagree _____

Corrective Action Plan: A benefit file will be created for each retiree and held in Human Resources to support each of the remaining obligations. These files will provide support for the obligations, the amounts being paid, and the current status of any employee receivables.

Projected Completion Date: June 30, 2013

Responsible Manager: Will Wyatt, Human Resource Director

2. One or more required annual performance evaluations are missing in 44% of tested personnel files.

Criteria: City of Clarksville Code (Section 1.5-801) and Human Resource Procedure 91-3 specify that:

- a. Employees should receive a performance evaluation at least annually.
- b. Employees should receive no salary adjustment “unless there is on file in the department of human resources a performance evaluation completed within the past 12 months”.
- c. Employees should receive no salary increase or longevity bonus without a current performance evaluation that demonstrates the employee meet or exceeds expectations.
- d. Department Heads should receive no salary increase until every employee in the department has a current evaluation completed.

Condition: After a review of the City employee files, it was determined that performance evaluations are either not performed or not documented in the personnel files. We reviewed 192 personnel files and found only 84% of those employees had an evaluation from FY2011 and only 56% had an evaluation covering FY2012. Additionally, we reviewed the personnel files of all 15 of the general fund Directors and discovered that only 1 (7%) had a performance evaluation dated after December 2010. All otherwise eligible employees received pay raises in this time period despite the lack of a centrally filed performance appraisal.

Cause: The performance evaluation process is not being managed at the Human Resources Department level. No central control activity is in place to ensure that Department Heads and employees receive the required performance evaluations before a pay raise is implemented. Evaluations are managed at the department level with no validation by Human Resources which is where pay raises are processed.

Effect: The City is not in compliance with City Code Section 1.5-801. Despite City Code guidance, employees without centrally documented evaluations that meet or exceed expectations are still receiving salary increases. Department heads that have either not performed or not forwarded evaluations to the Human Resources Department are receiving salary increases. Additionally, the lack of employee performance documentation at the organizational level puts the City at risk when employee actions are taken based on job

timekeeping system to document and maintain hours worked as required either through Munis software or the purchase of new timekeeping software.

Projected Completion Date: Email to department heads will be sent by May 31, 2013. The electronic timekeeping solution is projected to be implemented by December 31, 2013 (if Munis solution) or as soon as funding is available (non Munis).

Responsible Manager: Will Wyatt, Human Resources Director

4. **Some departmental policies regarding overtime and comp time for non-exempt employees put the City at risk for being out of compliance with the FLSA.**

Criteria:

FLSA legislation protects non-exempt employees by providing for overtime compensation at a premium rate if they work over a maximum number of hours. No state or local policy can diminish the rights granted on the federal level. Therefore, an employer cannot lessen a right granted by federal regulation by having a standing policy that no OT will be paid. Additionally, an employer cannot require an employee to use comp time instead of being paid OT without employee consent. Such requirements lessen the employee protections provided by the FLSA act.

Condition:

Overtime policy in 5 of 14 departments limits the employee's choice between OT and compensatory time without employee consent:

- a. 5 out of 14 departments give the impression that OT is prohibited in written policy (1) or in stated (4) department procedure (FLSA concern).
- b. 5 out of 14 departments dictate that comp time shall be taken in all OT cases (FLSA concern).

Cause: There is inconsistent overtime/ comp time policy direction across departments because the guiding Human Resource policy is very general (... "complies with FLSA...") and departments have been allowed to create their own overtime/ comp time procedure. As a result, some departments have developed procedures that might act to restrict an employee's rights.

Effect:

The City may not be in compliance with Section 207 (o) of the Fair Labor Standards Act (FLSA) for its non-exempt employees. This is due to the fact that a state or local entity cannot lessen a right granted by federal regulation. If City denies overtime or forces its employees to choose comp time over overtime even when the employee would prefer to be paid overtime, the rights of the employee are not being taken into consideration.

Recommendation:

Protections need to be incorporated into policy that ensure the FLSA rights of employees.

- a. **Pre-approval policy requirement:**
Although an employee may be restricted from using discretionary overtime, the employee's right to compensation for overtime worked cannot be reduced or eliminated by policy that requires pre-approval.

Departments should amend any written policy requiring pre-approval of overtime to include a statement that acknowledges the employee's right to OT compensation such as: "It is not management's intention to include tasks in any job that require overtime. Therefore, when a situation evolves that requires overtime, the overtime needs to be pre-approved before it is worked. However, if overtime is worked (without pre-approval), management reserves the right to reprimand the employee but will pay the overtime to the employee."

To minimize the chance of overtime, train manager's to:

- i. Ensure that there are no tasks that fundamentally require overtime
- ii. Ensure that there is no systemic imposition of overtime
- iii. Address with employees that discretionary overtime is not allowed
- iv. Have a process for employees seeking approval for overtime
- v. Modify and manage your employees' time and workloads effectively
- vi. Ensure that all employees that do work overtime have their time appropriately recorded (and paid or comped- if employee consents to comp time- at the appropriate rate)

b. Overtime payment method restrictions

Departments should amend policy that restricts the manner of overtime payment (i.e. comp time in lieu of OT). If comp time is used, the City must be able to demonstrate employee agreement about being paid comp time instead of overtime. This agreement should be reconfirmed at least annually and held on file with the department payroll records.

Responsible Departments: Human Resources

Management Comments: Departments have been given the freedom to determine their own overtime and comp time procedures with only general guidance ("must comply with FLSA"). Although it is acceptable to require preapproval of overtime, once worked, overtime cannot be denied. The general guidance provided by the City needs to be clarified so that both the City and the employees understand the overtime process and the rights of the employees.

Agree X

Disagree _____

Corrective Action Plan: Human Resources will develop a written policy for overtime and comp time to ensure that employee rights are protected. Human Resources will issue email guidance to clarify the policy requirements.

Projected Completion Date: June 30, 2013

Responsible Manager: Will Wyatt, Human Resource Director

5. Standard City procedures were not followed in promoting an HR employee.

Criteria: Per City Code Section 1.5-405 (e),(f) all promotion increases must be supported by a classification. And, any temporary job position assignment must be handled in a timely manner.

Condition: Our testwork revealed a situation where a promotion was initiated as a temporary out-of-class assignment. The position was not classified nor was the action finalized as of the date of this report, 15 months after the initiation of the action. The employee continues to be paid the out-of-class rate. City Code allows a maximum of six months for an employee to remain in a temporary position.

Management states that the employee is in the process of migrating to a new position. The new position has not been classified yet. Management further states that the current pay will be within the final position classification pay range.

Cause: In this case there was an immediate need for a position to be filled due to an employee vacancy in a key area. However, instead of hiring the position left by the employee vacancy, a new position was created that eliminated the temporarily assigned position and changed the responsibilities of the position the employee was promoted from. That left the temporary assignment individual without a home position to return to.

Management states that the employee is in the process of migrating to a new position. The new position has not been classified yet. Management further states that the current pay will be within the final position classification pay range.

Effect: Management has not addressed the classification supporting a promotion to a new position and has not resolved the temporary out-of-class promotion in a timely manner. Therefore, this employee does not have a position classification supporting the rate of pay being received.

Recommendation: Management should create a new position based on the employee's new job description, have the position classified, and seek permanent assignment of the employee to the position as soon as possible.

Responsible Department: Human Resources

Management Comments: This out-of-class adjustment was unique in that the position the employee left changed. In hindsight, instead of an out-of-class adjustment this employee's new responsibilities should have been classified and a permanent position should have been created so the employee could be appointed to the new position.

Agree _____ Disagree _____

Corrective Action Plan: This employee is no longer receiving out-of-class pay. The employee has been placed into a new classification and assigned to a permanent position.

Projected Completion Date: Completed April 1, 2013.

Responsible Manager: Will Wyatt, Human Resources Director

6. Some personnel files (53% of tested files) are lacking documentation required under the Tennessee Lawful Employment Act.

Criteria: Per TN Code Annotated § 50-1-703 (a) (3) [Tennessee Lawful Employment Act] employers must validate the lawful employment status of their employees. To prove lawful employment was validated, employers need to request and maintain eligibility verification documents as outlined in the Act.

Condition: Only 17 of 30 (53%) employee personnel files sampled had the required documentation.

Cause: The regulations surrounding documentation requirements relating to lawful employment have changed over time. The Tennessee Lawful Employment Act which went into effect on January 1, 2012, created the updated standard but efforts have not been made in the City to bring all employee files up to the new standard as of the audit report date.

Effect: The City is not in compliance with the Tennessee Lawful Employment Act. The City could be added to a published list of offenders and possibly subjected to fines if a complaint is filed and the City is found to be in noncompliance with the validation requirements.

Recommendation: Human Resources Department needs to initiate steps to ensure the required Tennessee Lawful Employment Act actions are taken and that the resulting documents are obtained and maintained in each employee's personnel file.

Responsible Department: Human Resources

Management Comments: The lack of documentation is most likely missing in the older personnel files. Current procedure requires that all new employees provide the required proof of work eligibility. Copies of the Federal I-9 form and the documents that are provided by the employee are filed in each personnel file. To ensure that we are compliant, we are considering a move to E-verify as our verification tool going forward. A copy of the E-verify report in each employee file meets the employment validation requirement.

Agree _____

Disagree _____

Corrective Action Plan: Human Resources will begin using E-verify to validate employability for all new employees. For existing employees Human Resources plans on re-certifying one department each month until all departments have been processed to ensure that employment validation documents exist in all personnel files.

Projected Completion Date: E-Verify in place for new employees (July 1, 2013) and re-certification of all existing employees (June 30, 2014).

Responsible Manager: Will Wyatt, Human Resources Director

7. Payroll access in Munis and payroll functions performed by employees are not properly segregated.

Criteria: Access to payroll should be restricted to the work required by the role each individual holds. Payroll roles should be properly segregated to reduce the risk of payroll fraud. No individual should be able to both set up a new employee and also process payroll. Likewise no individual should be able to change payroll rates and also process payroll.

Condition: Currently 13 employees have super user rights to the payroll module. These employees are only restricted by limiting their ability to view certain screens. In addition, two of the individuals have the capability to set up new employees, change pay rates and also process payroll.

Cause: In the past it was considered easier to assign full rights and limit access by restricting views. Also, as duties have shifted in some cases the segregation of payroll duties was not reviewed.

Effect: The current payroll access configurations increase the City's exposure to payroll fraud. The current method of control relies too heavily on trusting employees to restrict their system interaction.

Recommendation: The IT Department should work with Finance and HR to define specific roles within the payroll process. Then the system access for each of these roles should be defined to restrict access to each job function. Once roles have been created and defined, they can be issued to each individual so they can perform only the tasks they have been assigned in the payroll process. Proper segregation of duties should always be reviewed when responsibilities shift from one employee to another.

Responsible Department: IT and Human Resources

Management Comments:

Human Resources Response: Human Resources will be working with the IT Department to ensure a role based access system is in place. Going forward, we will ensure employees do not have access to payroll processing functions at the same time they have the capability to set up new employees or change employee pay.

Agree _____

Disagree _____

Corrective Action Plan:

Human Resources Response: Human Resources will work with IT and Finance to develop formal limited access Human Resources and Payroll roles. All roles will be reviewed to ensure no one individual has both payroll processing capability and employee setup or pay change capability in any given payroll. Some temporary access may be needed in certain situations due to limited backup personnel.

IT Response: IT will update the permissions in Munis based on defined roles from Finance and HR.

Projected Completion Date: December 31, 2013

Responsible Manager: Will Wyatt, Human Resource Director, and Amie Wilson, Information Technology Director

Other Recommendations:

Although not considered findings, auditor testing revealed some inefficient policies. We suggest that management consider the following recommendations:

1. **Recommendation: Improve the efficiency of payroll processing by creating a payroll lag and moving to a bi-weekly payroll.**

The following efficiencies could be gained by such a move:

- No reconciliations of assumed work activity versus actual work activity are required (currently required each pay period).
- Standard deadlines create less confusion about payroll cutoff.
- End of the work week cutoff simplifies OT calculations.
- Possibility of overpayment to employees as they terminate is reduced or eliminated.
- More time is available to review payroll activity which reduces errors.

After reviewing case studies, the auditors believe implementation of a payroll lag and a bi-weekly payroll system can be accomplished with minimum impact to employees. Please contact the audit team for some specific examples.

Management Comments: The Human Resource Director agrees that a move to a payroll lag and a bi-weekly payroll would be a more efficient payroll process for the City. He suggests that the Directors of Finance and Human Resources meet to review the available options and make a decision about whether to proceed on this initiative.

2. **Recommendation: Create a system to document and retain City of Clarksville management position decisions (management interpretations of policy).**

The auditors recommend that each department document and retain position papers that demonstrate how management has interpreted legislation, regulation (including City Code) and how management's position was approved.

Currently, there is no formal means to capture management positions on policy so reviewers after the fact are unsure if the positions are supported and approved.

After a time there is no known justification for how or why transactions are handled in a certain way.

Management Comments: The Mayor and City Attorney will discuss the need for the documentation and maintenance of management interpretations. After their review of the options, the Mayor will provide guidance to the Directors.

3. Recommendation: Departments should track and periodically analyze the efficiency of paid overtime and compensatory time activity.

In order to facilitate sound business decisions in regard to paid overtime and compensatory time, the auditors recommend that departments track on a monthly basis the accrual of paid OT and comp time for each functional area within the department.

- Monthly information should be graphed on an annual basis to highlight seasonal accruals or other trends that would suggest that seasonal or part time employees would be more economical.
- Any position that results in paid overtime or comp time on a regular basis should be supported by an efficiency analysis. Finance has volunteered to help departments develop a decision model.
- Comp time impacts productivity instead of the bottom line. Currently the loss of productivity is hidden because it's not part of the financial analysis.

Management Comments: The Mayor will discuss the tracking of comp time and overtime at the department level at a future Department Head meeting with emphasis on tracking and analyzing paid overtime and comp time on a systematic basis. Discussion will include the use of the information as a decision making tool in staff make up (the use of temporary or seasonal employees as opposed to full time employees).

Conclusion:

Our audit of City General's payroll process revealed the following results related to our original objectives:

- Based on our statistical sample of 259 payroll transactions out of a total population of 34,198 transactions during the period January 2011 through June 2012, we are 95% confident (3% tolerable error) that all transactions are accurately calculated and properly supported.
- Our testwork revealed the following in regard to compliance with Federal and State payroll-related laws:
 - Supporting documentation required by the Employee Retirement Income Security Act of 1974 is not being maintained for the 5 retired employees that are paid directly by the City under the old retirement system.
 - Supporting documentation required by the Tennessee Lawful Employment Act is missing in 17 out of 30 files tested for compliance with the Act.
- Our testwork revealed the following in regard to compliance with City Code and City Human Resources policy:
 - Required annual evaluations are missing for either 2011 or 2012 in 44% of the personnel files.
 - Standard City procedures were not followed in promoting an HR employee.
- Based on our testwork regarding the implementation of the Fox Lawson & Associates study, we are 95% confident that City General employees were paid in accordance with the FLA study during the period tested.

- **Our testwork revealed the following in regard to City policy and procedures related to the requirements of the Fair Labor Standards Act:**
 - **Some departments don't require full time, regularly scheduled, non-exempt employees to document their hours as mandated by the Act.**
 - **Some departments have policies related to paid overtime and comp time that put the City at risk for being out of compliance with the Act.**
- **Our evaluation of the design and effectiveness of the internal controls surrounding the payroll process revealed the following:**
 - **In general, internal control procedures are adequately designed and operating effectively. However, we found two significant deficiencies in control procedures related to the following:**
 - **Two employees have payroll functions that are not sufficiently segregated. They have authority to both process payroll and/or set up new employees and/or change pay rates.**
 - **Thirteen employees are currently identified in Munis software as payroll superusers. Superusers are granted broad permissions in the payroll module. These employees' access is restricted by the screens they are able to view instead of restricted by permissions to certain payroll functions.**

During the conduct of the audit, the auditors became aware of several situations or procedures that prompted them to make three additional recommendations to management.

- **A change from semi-monthly to bi-weekly payroll periods and the adoption of a five business day payroll lag time would create a number of efficiencies in the payroll process;**
- **The creation of a system to document and retain management position papers related to Human Resources policy interpretations would help eliminate confusion over past interpretations and decisions;**
- **Tracking and analyzing paid overtime and comp time by the departments on a systematic basis would facilitate sound business decisions in regard to the use of those payment options as opposed to hiring temporary or seasonal employees.**

The auditor would like to thank Human Resources, the departmental management and the departmental staff for their help and support during the performance of this audit. Their positive attitude facilitated the conduct of the audit and provides the necessary environment for process improvements to take place.

If further information about this audit is desired please contact Internal Audit at 931-648-6106.