INTERNAL AUDIT

Payroll
Audit Report

November 18, 2019

Report Number: 2019-AUD-01 Payroll

AUDIT REPORT

Table of Contents

Report Number: 2019-AUD-01 Payroll

Executive Summary

Background

The Payroll function (Payroll) within the Human Resources division consists of two employees who are responsible for processing the biweekly payroll and disbursements for approximately 1,051 employees. Payments for contract and contingent staff are not included in the payroll totals as they are processed in accounts payable.

In December 2017, Centerpoint Human Capital Management (HCM) replaced the Kronos Workforce Payroll/HRIS system to handle the complete employee lifecycle from onboarding to retirement. The HCM module was implemented to automate and streamline current payroll processes, strengthen controls, and enhance operations with tools that produce reports and generate data for enhanced decision making. The HCM module within Centerpoint is used to enter, process and manage payroll; benefits; time and labor; compensation; absence management; and talent management for Citizens.

As a part of the Centerpoint implementation, Citizens began using a payroll vendor, Automatic Data Processing, Inc. (ADP) for W-2 preparation, tax preparation and filings to federal, state and local taxing authorities and the remittance of garnishment payments.

Audit Objectives and Scope

The objective of this audit was to evaluate whether key controls related to the payroll processes are adequate and ensure that authorized payroll transactions are processed in a complete, accurate, and timely manner within applicable laws, regulations and company policies.

The audit focused on the following areas:

- New Hires and Terminations
- Time Capture
- Absence Management
- Segregation of Duties
- Payroll Calculation and Processing
- Payroll Disbursements
- Third-Party Payments
- Post-Payroll Review

The scope of this audit did not include areas such as General Ledger Posting and Reconciliation; HCM User Access; Unclaimed Payroll Checks; and Security of Confidential Data

Management's Assessment on Reporting Controls

Internal Audit (IA) provided Payroll an opportunity to share known control weaknesses and their plans to remediate them. This process is intended to foster an environment whereby management and staff conduct periodic proactive reviews of controls and are aware of the risks to the business. It also enables us to focus our audit efforts on areas where it can add value to the organization.

At the start of the audit, payroll management self-identified areas where additional controls should be designed, these include:

Report Number: 2019-AUD-01 Payroll

Executive Summary

- **Payroll is sometimes unable to rely on system calculations resulting in manual intervention to ensure the payroll calculations are accurate.**

  - The final paychecks for terminated employees are not accurately calculated by the payroll system. HRIM and IT management identified an issue where the system overstates the terminated employee's accrued vacation and sick leave balances when termination pay is calculated through the payroll system. To date a solution has not been identified to resolve this issue in Centerpoint. In the interim, the Payroll Administrator manually calculates the terminated employee's accrued vacation and sick leave, and manually enters the final pay in the payroll system. The final pay for terminated employees is revalidated by the Payroll Manager during the Post-Payroll review before the payroll run is finalized. A manual calculation is time consuming and could be prone to errors.

  - Citizens' policies currently require non-exempt employees to take meal breaks of at least 30 uninterrupted minutes each day. However, Supervisors may give non-exempt employees explicit written approval to work through a scheduled meal break to make up time missed due to appointments, absences, or to meet critical business need; therefore, the meal break is considered compensable work time. Currently, the payroll system does not have the functionality to automatically pay non-exempt employees who take meal breaks that are less than 30 minutes. The Payroll Administrator generates a report called "Meal Breaks" to identify non-exempt employees who took meal breaks 29 minutes or less. The Payroll Administrator manually creates "Lunch Break Paid" element in the payroll system for each employee to ensure employees are paid in accordance with the Fair Standards Labor Act (FLSA). Manually changing payroll data could lead to unauthorized changes and inaccuracies.

    IA noted that it appears to be standard practice within certain areas for non-exempt staff to work during part of their meal breaks. It is difficult for payroll staff to confirm that these shortened breaks were authorized by the supervisors and manually process payments to ensure compliance with FLSA. This practice could lead to abuse and IA suggests that consideration be given to a system change that prohibits staff processing meal breaks less than 30 minutes without management approval within Centerpoint HCM.

- **Due to system and workflow design limitations, some payroll processes have not been fully automated and result in time-consuming and inefficient manual intervention.**

  - Payroll is unable to lock the bi-weekly pay cycle to prevent changes during the payroll run. This creates challenges with timing of absence approvals, time entry and approvals, and retro processing.

    The current system design does not prevent changes to the payroll supporting documentation while the final payroll run is in progress. IA suggests that management consider changing system configuration so that there are clear input restrictions that will protect the integrity of the data supporting the payroll calculations.

  - There are sporadic instances where the Time and Labor module of the system does not allow management to edit, save, and/or approve employees' timecards prior to the payroll run. It is currently unclear why this error occurs and there is no identified system solution.

Report Number: 2019-AUD-01 Payroll

Executive Summary

In the interim the payroll administrator unilaterally approves all unapproved timecards prior to the payroll run, without input from management, to ensure that all staff receive a paycheck in the pay cycle. This could lead to unapproved time entries and errors that need to be corrected in a future pay cycle or it could lead to errors that go undetected.

- **Limited access to data on the Oracle platform prohibits adequate monitoring and exception reporting. This negatively impacts Payroll's ability to perform appropriate oversight of the whole payroll process.**

  o Time and attendance reports as well as exceptions reports are not available to identify and investigate anomalies that may occur in the payroll run and to ensure that corrections are made prior to finalizing payroll. Furthermore, retroactive pay reports (i.e. reports that note all payroll changes affected after the payroll run) are not available to enable Payroll to validate the accuracy and appropriateness of salary adjustments and payments made retroactively.

- **Citizens Payroll is managed by two staff, a Payroll Manager and a Payroll Administrator. Individuals designated as back-up resources for key personnel have not been sufficiently cross-trained.**

  o Citizens heavily relies on key personnel with specialized experience to perform the payroll process. The complexity of the payroll process requires qualified professionals with substantial experience to properly execute the payroll processing functions. Given that Payroll is limited to two employees, plus an IT support person, Payroll will be in a challenging position should one of the employees become unavailable to perform their duties. As a result, one person within HR and one in IT were identified as back-up to ensure the continued processing and monitoring of the payroll process. The HR person is currently undergoing training to be a qualified back-up.

Audit Opinion

Human Resources implemented the Centerpoint Human Capital Management (HCM) system to replace disparate human resources technologies that relied heavily on manual processes and controls. The HCM system allowed HR to automate and integrate the majority of its business processes to provide greater access to HR and Payroll information and to enhance the user experience. However, the implementation of the Centerpoint HCM system, specifically payroll, has created some unique challenges and it has not achieved all the benefits envisioned by HR management given the level of manual intervention and oversight required to ensure that payroll payments are accurate and timely.

Human Resources management has initiated a solicitation to procure a vendor for professional consulting services to address the ongoing issues with Centerpoint. Two vendors have been selected to complete proof of concepts as a part of the solicitation to determine which vendor will be selected for the contract.

Executive Summary

In the future when the Oracle contract comes up for renewal, it is recommended that Citizens explore products and/or services that would either replace or improve existing time and absence management functionality.

In addition to self-reported concerns, management is encouraged to consider the following improvement to controls:

- Consider developing key performance indicators (KPIs) to measure the efficiency and effectiveness of the payroll operations. KPIs such as Cost of Payroll, Time to Run Payroll, Timecard Approval, Days to Resolve Payroll Issues, and Payroll Processing Accuracy Rate could help the Payroll Department to provide a comprehensive view of the payroll overall performance and identify areas for improvement. Baselines should be established for each KPI.

We would like to thank management and staff for their cooperation and professional courtesy throughout the course of this audit.

Appendix 1

Distribution

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