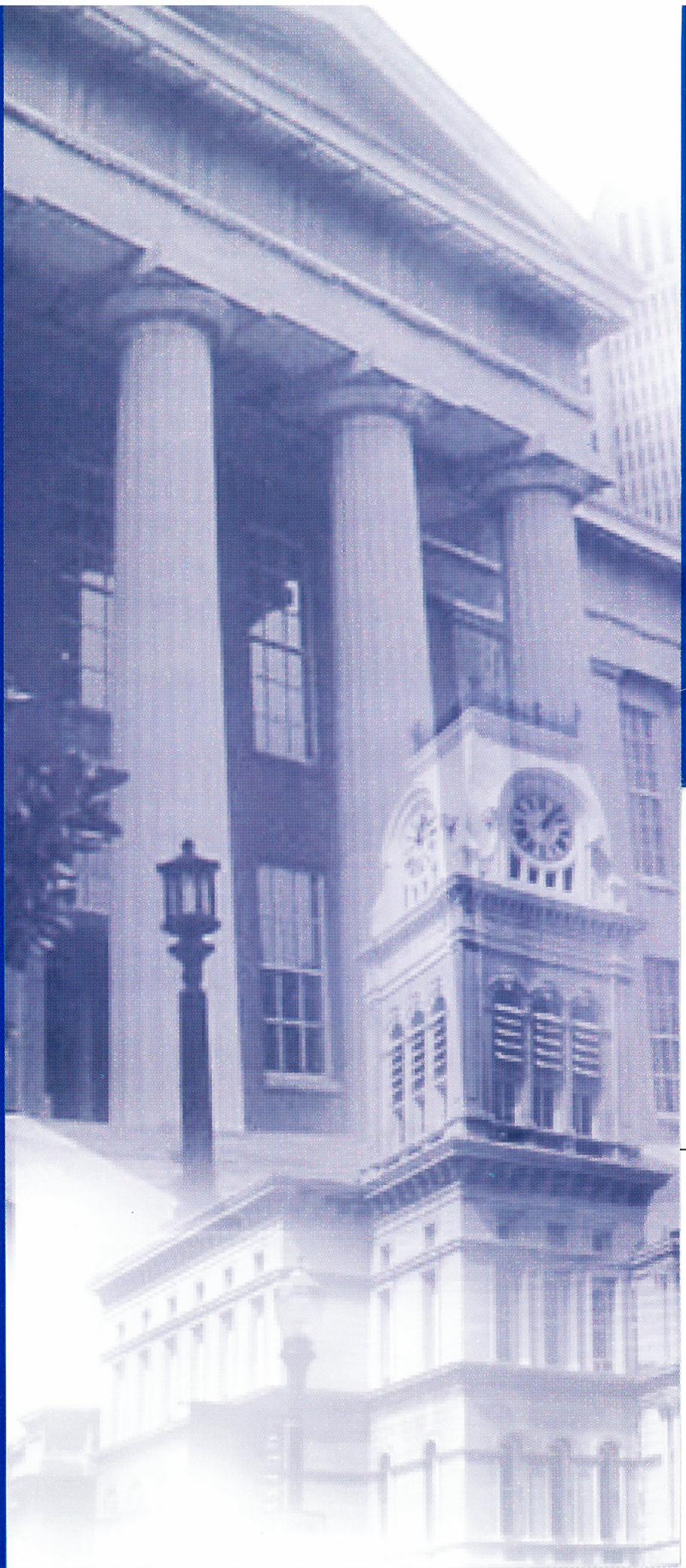




Greg Fischer
Mayor

Louisville Metro Council

The Office of Internal Audit provides independent, objective assurance and consulting services that adds value to and improves Louisville Metro Government.



Office of Internal Audit

Louisville Metro Government

2013 Payroll Activity

Audit Report

Louisville Metro Government

2013 Payroll Activity

July 2014



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Executive Summary

PROJECT TITLE

Louisville Metro Government - 2013 Payroll Review

OBJECTIVE AND SCOPE

The objective was to obtain assurance that payroll activity was processed appropriately and internal controls were effective in mitigating certain risk. The primary focus of the audit was high level reviews and analysis of payroll data, covering highest gross and key personnel earnings, use of earn codes, vacation pay at termination and worker's compensation.

Testing included activity occurring during calendar year 2013 (January 1, 2013 to December 31, 2013). The details of the scope and methodology of the review are addressed in the Observations and Recommendations section of this report.

INTERNAL CONTROL ASSESSMENT

Satisfactory

RESULTS

- **Stipend Overtime Pay.** Louisville Fire Department employees obtaining certain accreditations are paid a stipend amount, typically \$1,000. Two employees were overpaid, resulting in a total overpayment of \$1,244.
- **Segregation of Duties.** In order to perform their job effectively, there are users who have access to job data, time and labor and paycheck data functions of the human resources and payroll system, PeopleSoft. This level of access creates a condition where a user could create a fictitious person on the payroll for the purpose of receiving pay fraudulently.



OFFICE OF INTERNAL AUDIT
LOUISVILLE, KENTUCKY

GREG FISCHER
MAYOR

INGRAM L. QUICK, CHIEF AUDIT EXECUTIVE

JIM KING
PRESIDENT METRO COUNCIL

Transmittal Letter

July 7, 2014

The Honorable Greg Fisher
Mayor of Louisville Metro
Louisville Metro Hall
Louisville, KY 40202

Subject: Audit of Louisville Metro Government's 2013 Payroll Activity

Introduction

In accordance with internal auditing best practices, an enterprise-wide review of 2013 payroll activity was performed. The objective was to obtain reasonable assurance that payroll activity was processed appropriately and that internal controls were effective in mitigating certain risks. This was achieved by performing high-level reviews and analyses of payroll data. Individual employee time records were not reviewed.

The audit was conducted in accordance with Government Auditing Standards issued by the Comptroller General of the United States and with the International Standards for the Professional Practice of Internal Auditing issued by the Institute of Internal Auditors.

As a part of the review, the internal control structure was evaluated. The objective of internal control is to provide reasonable, but not absolute, assurance regarding the achievement of objectives in the following categories:

- Achievement of business objectives and goals
- Effectiveness and efficiency of operations
- Reliability of financial reporting
- Compliance with applicable laws and regulations
- Safeguarding of assets

There are inherent limitations in any system of internal control. Errors may result from misunderstanding of instructions, mistakes of judgment, carelessness, or other personnel factors. Some controls may be circumvented by collusion. Similarly, management may circumvent control procedures by administrative oversight.

Scope

The review period covered calendar year 2013 (January 1, 2013 – December 31, 2013) and included the following areas:

- Highest Gross Earnings
- Key Personnel Earnings
- Earn Code Analysis
- Workmen's Compensation
- Vacation Pay at Termination
- Ghost Employees

Activity from each area was reviewed to ensure appropriateness. The details of the scope and methodology of the review will be addressed in the Observations and Recommendations section of this report. The audit would not identify all issues because it was based on selective review of data.

Opinion

It is our opinion that the internal control structure for Louisville Metro Government's payroll activity is satisfactory. The internal control rating for each area reviewed is on page 6 of this report. These ratings quantify our opinion and identifying areas requiring corrective action.

- **Stipend Overtime Pay.** Louisville Fire Department employees obtaining certain accreditations are paid a stipend amount, typically \$1,000. Two employees were overpaid, resulting in a total overpayment of \$1,244.
- **Segregation of Duties.** In order to perform their job effectively, there are users who have access to job data, time and labor and paycheck data functions of the human resources and payroll system, PeopleSoft. This level of access creates a condition where a user could create a fictitious person on the payroll for the purpose of receiving pay fraudulently.

Corrective Action Plan

The focus of this review was the Louisville Metro enterprise, not an individual department. Each Louisville Metro department is responsible for ensuring its payroll activity is appropriate. In addition, the Office of Management and Budget's (OMB) Payroll division and Metro Technology Services (MTS) are responsible for the accuracy and integrity of payroll expenditures for Louisville Metro Government. OMB and MTS were asked to provide a corrective action plan for the recommendations in this report. The corrective action plans are included in the Observations and Recommendations section of this report. We will continue to work with OMB and MTS to ensure the actions taken are effective to address the issues noted.

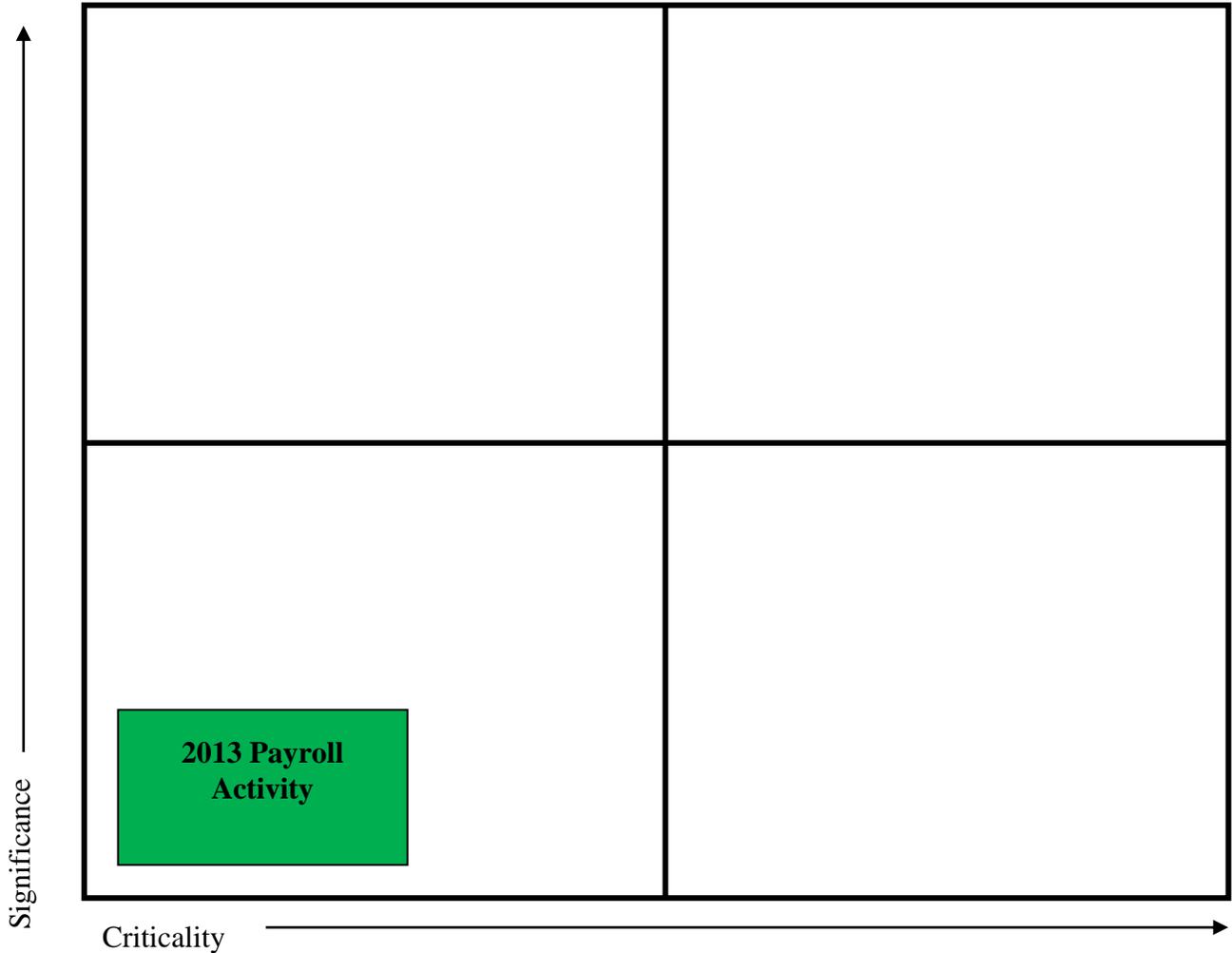
Sincerely,



Ingram Quick, CIA, CFE
Director of Internal Audit

cc: Louisville Metro Council President
Louisville Metro Council Government Accountability and Ethics Committee
Director of Office of Management and Budget
Director of Metro Technologies Services
Louisville Metro External Auditors

Internal Control Rating



<u>Legend</u>			
<u>Criteria Issues</u>	<u>Satisfactory</u> Not likely to impact operations.	<u>Needs Improvement</u> Impact on operations likely contained.	<u>Inadequate</u> Impact on operations likely widespread or compounding.
<i>Controls</i>	Effective.	Opportunity exists to improve effectiveness.	Do not exist or are not reliable.
<i>Policy Compliance</i>	Non-compliance issues are minor.	Non-compliance issues may be systemic.	Non-compliance issues are pervasive, significant, or have severe consequences.
<i>Image</i>	No, or low, level of risk.	Potential for damage.	Severe risk of damage.
<i>Corrective Action</i>	May be necessary.	Prompt.	Immediate.

Background

Personnel costs are normally one of the largest operating budget items for departments. It is imperative that proper controls are in place to provide accountability for the funds expended. In accordance with internal auditing best practices, routine reviews of payroll activity can help in obtaining reasonable assurance that payroll activity is processed appropriately and that internal controls are effective in mitigating certain risks.

This was a scheduled audit.

Summary of Audit Results

I. Current Audit Results

See Observations and Recommendations section of this report.

II. Prior Audit Issues

The Office of Internal Audit performed a prior review of Louisville Metro 2012 payroll activity and issued the results in August 2013. Unless otherwise noted, all prior issues have been satisfactorily addressed.

III. Statement of Auditing Standards

The audit was performed in accordance with Government Auditing Standards issued by the Comptroller General of the United States and with the International Standards for the Professional Practice of Internal Auditing issued by the Institute of Internal Auditors.

IV. Statement of Internal Control

An understanding of the internal control structure was obtained in order to support the final opinion.

V. Statement of Irregularities, Illegal Acts, and Other Noncompliance

The audit did not disclose any instances of irregularities, any indications of illegal acts, and nothing was detected during the examination that would indicate evidence of such. Any significant instances of noncompliance with laws and regulations are reported in the Observations and Recommendations section of this report.

VI. Views of Responsible Officials / Action Plan

A draft report was issued to the Office of Management and Budget and Metro Technology Services on June 11, 2014. It was determined that a formal exit conference was not necessary.

The views of OMB were received on June 30, 2014 and the views of Metro Technology Services were received on July 1, 2014 and are included as corrective action plans in the Observations and Recommendations section of the report. The plans indicate a commitment to addressing the issues noted.

LMCO §30.36(B) requires Louisville Metro Agencies to respond to draft audit reports in a timely manner. It specifically states that

“The response must be forwarded to the Office of Internal Audit within 15 days of the exit conference, or no longer than 30 days of receipt of the draft report.”

The Office of Management and Budget and Metro Technology Services’ response was provided within this required timeframe.

Observations and Recommendations

Scope

An enterprise-wide review of Louisville Metro Government's 2013 payroll activity was performed. The objective was to obtain reasonable assurance that payroll activity was processed appropriately and that internal controls were effective in mitigating certain risks. This was achieved by performing high-level reviews and analyses of summarized payroll data. Individual time records were not reviewed. The review would not reveal all issues because it was based on selective review of data.

The review period covered calendar year 2013 (January 1, 2013 – December 31, 2013). The population for each area reviewed was as follows.

- **Earn Code Analysis.** The population was all earn codes as noted on an earn code listing/report obtained through a PeopleSoft query. A sample of 5 earn codes were judgmentally selected for review to ensure appropriateness of activity.
- **Vacation Pay at Termination.** Data for employees who received compensation for accrued unused vacation leave at the time of their termination of employment with Louisville Metro was obtained. Per Metro Personnel Policies, an employee can be compensated for up to 40 days of accrued unused vacation leave upon separation from Louisville Metro Government employment.
- **Ghost Employees.** All employees who were active at the end of the calendar year were examined. The universe of employees examined was 5,558. They were reviewed for evidence of being fictitious through examination of matching checking account numbers, social security numbers or names.
- **Highest Gross Earnings.** Data for employees with \$100,000 or more in gross earnings for the year was obtained. There were a total of 60 employees identified with gross earning greater than \$100,000. A sample of 10 employees was judgmentally selected for review to ensure appropriateness of activity.
- **Key Personnel Earnings.** Data for gross earnings for key personnel was obtained. This included Office of Management and Budget, Human Resources, and Information Technology employees whose job function allows the high-level access to the payroll system. There were a total of 19 employees identified as key personnel. A sample of 6 employees was judgmentally selected for review to ensure appropriateness of activity.
- **Workman's Compensation.** All employees who were active at the end of the calendar year were examined. Those employees' records were reviewed to determine that they were assigned a workman's compensation classification code.

Observations

The internal control structure is satisfactory. Some minor issues were noted with the administration of payroll activity. As a result the internal control structure needs improvement. Opportunities noted to strengthen the controls are as follows.

Earn Code Analysis

- **Stipend Overtime Pay.** Fire employees obtaining certain accreditations are paid a stipend amount, typically \$1,000. Per the Bargain Letter Agreement this stipend should have been added to gross pay for overtime calculations. The expected use of this earn code is to allow a small premium per hour to be paid to qualifying employees. However, there are 2 instances (out of 2,826 such payments) where employees were paid a substantially larger amount than what is appropriate.
 - The Office of Internal Audit calculated the hourly wage that was paid to each employee using the code STO in 2013. Substantially all employees were paid at a rate of \$0.721 per hour. Two employees were paid at rates of \$17.88 or \$14.66 per hour instead, resulting in a total overpayment of \$1,244.

Vacation Pay at Termination

- There were no issues noted with regard to vacation pay at termination.

Ghost Employees.

- **Segregation of Duties.** In order to perform their job effectively, there are users who have access to job data, time and labor and paycheck data functions of the human resources and payroll system, PeopleSoft. This level of access creates a condition where a user could create a fictitious person on the payroll for the purpose of receiving pay fraudulently.

Highest Gross Earnings

- There were no issues noted with regard to highest gross earnings.

Key Personnel Earnings

- There were no issues noted with regard to key personnel earnings.

Workman's Compensation

- There were no issues noted with regard to workman's compensation.

Recommendations

Appropriate personnel should take corrective action to address the issues noted. Specific recommendations include the following.

Stipend Overtime Pay

- ✓ Metro Payroll should carefully monitor any pay adjustments (e.g., stipend overtime pay) made to employees during the normal payroll process. Procedures should be in place to verify that the pay is calculated appropriately.

Segregation of Duties

- ✓ Ideally, segregation of duties should be incorporated into human resources and payroll system, PeopleSoft. A single individual should not have access to enter a person along with access to enter time for such person. In situation where there is some overlap, stronger compensating controls should be practiced (e.g., supervisory review, monitoring).
- ✓ The importance of reviewing timecard reports for appropriateness and completeness should be stressed to all supervisors. Supervisory review should include ensuring that persons listed on the timecard report are actual employees of Louisville Metro Government.

Highest Gross Earnings

- ✓ No recommendations needed at this time.

Key Personnel Earnings

- ✓ No recommendations needed at this time.

Workman's Compensation

- ✓ No recommendations needed at this time.

Office of Management and Budget's Corrective Action Plan

Stipend Overtime Pay

In order to address this issue, Metro Government has written a query that will pull the employees being paid STO to evaluate the rate of pay and ensure that it is being calculated correctly. The report for this query will be run any time that there is STO paid. The stipend in question for this audit report will be ending on June 30, 2014, however the query can be modified to include other pay types if and when they are needed based upon union contracts or other employee programs.

Metro Technology Services' Corrective Action Plan

Segregation of Duties

PeopleSoft team will create a process or query, or series of queries, which can provide compensating controls to test for ghost employees. The target group is the super users who have the ability to create Job Data AND create time or payroll activity. The super users are those persons on the PeopleSoft team, including current contractors with Admin rights and Chris Luse (HR Consultant).

The PeopleSoft team can create the query but will need to have someone else review the resulting output. It has been suggested that IT Security could fill that role. The query could be looking at the following:

If a super user EVER created a job data entry (creates an employee) and have they ever created a time entry resulting in a paycheck for someone other than themselves. The query will also need to test for "Pay Line" entries. The query will also need to check history to test in case the employee account was created in a different pay period than the time entry resulting in a payroll event. It would be ideal if this could run automatically and be emailed to IT Security.

This will need to be tested in PSOFT Test Environment to make sure we are capturing the desired data. This has been discussed this with IT Security and they are aware that this could be coming their way.



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Name of Report: Louisville Metro Government – 2013 Payroll Activity

How do you rate this report?			
	Beneficial	Somewhat Helpful	Needs Improvement
Background Information	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Details	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Length of Report	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Clarity of Writing	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Potential Impact	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Suggestions, comments, ideas, thoughts: _____

Office of Internal Audit

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