Metro

Payroll:

Increased coordination and training needed

December 2017
A Report by the Office of the Auditor

Brian Evans
Metro Auditor

Angela Owens
Senior Management Auditor
Zane Potter
Senior Management Auditor

Knighton Award
for Auditing

Audit receives recognition

The Office of the Metro Auditor was the recipient of the "Distinguished Award" for Small Shops by Association of Local Government Auditors (ALGA). The winning audit is entitled "Community Planning and Development Grants: Performance measures and stronger controls needed to ensure results." Auditors were presented with the award at the ALGA conference in Atlanta, Georgia in May 2017. Knighton Award winners are selected each year by a judging panel of peers and awards are presented at the annual conference.

Metro Accountability Hotline

The Metro Accountability Hotline gives employees and citizens an avenue to report misconduct, waste or misuse of resources in any Metro or Metro Exposition Recreation Commission (MERC) facility or department.

The Hotline is administered by the Metro Auditor's Office. All reports are taken seriously and responded to in a timely manner. The auditor contracts with a hotline vendor, EthicsPoint, to provide and maintain the reporting system. Your report will serve the public interest and assist Metro in meeting high standards of public accountability.

To make a report, choose either of the following methods:

Dial 888-299-5460 (toll free in the U.S. and Canada)
File an online report at www.metroaccountability.org

Brian Evans

Metro Auditor

600 NE Grand Ave
Portland, OR 97232-2736
TEL 503 797 1892, FAX 503 797 1831

MEMORANDUM

December 20, 2017

To: Tom Hughes, Council President
      Shirley Craddick, Councilor, District 1
      Carlotta Collette, Councilor, District 2
      Craig Dirksen, Councilor, District 3
      Kathryn Harrington, Councilor, District 4
      Sam Chase, Councilor, District 5
      Bob Stacey, Councilor, District 6

From: Brian Evans, Metro Auditor *BE*

Re: Audit of Payroll

This report covers our audit of Payroll. Over the last 10 years, the Office of the Auditor has identified payroll weaknesses. Although Metro made efforts to improve, we found many of the findings identified in previous audits remained. The purpose of this audit was to determine if Metro addressed the root causes of ongoing payroll issues. The audit was included in the FY2016-17 Audit Schedule.

Lack of coordination and insufficient training were common root causes of the payroll issues we reviewed. As a result, there were ongoing errors and weak controls. Metro's approach to tracking errors was incomplete. Formal processes are essential for organizational learning and adaptability. In other organizations, payroll has been identified as a potential source of fraud, waste and abuse. A variety of controls are required in the payroll process to reduce the risk.

During our audit, Metro initiated another project focused on improvements. The project brought together the Deputy Chief Operating Officer and Department Directors to get the appropriate level of authority to address issues that cannot be resolved by the employees who process payroll. Moving forward, Metro will have to strengthen management so that the momentum of the latest improvement efforts can be sustained.

We have discussed our findings and recommendations with Scott Robinson, Deputy Chief Operating Officer; Tim Collier, Director of Finance and Regulatory Services; Mary Rowe, Director of Human Resources; and Rachel Coe, Director of Information Services. A formal follow-up to this audit will be scheduled within three years. I would like to acknowledge and thank all of the management and staff who assisted us in completing this audit.

Summary

Over the last 10 years, we identified weaknesses with Metro's payroll processes. A 2006 audit found internal controls could be improved. In 2010, we made recommendations for additional improvements including increasing department coordination, improving the use of software functionality, and implementing stronger controls to ensure data accuracy. In 2016, we were notified of errors related to payroll deductions and leave hours.

Since at least 2009, Metro has started projects to address payroll issues. Although some improvements were made, we found many of the findings identified in our previous audits remained. In February 2017, Metro started another payroll process improvement project. The goal of the project was to eliminate systemic and chronic pay and leave inaccuracies.

Based on the payroll issues we reviewed in this audit, lack of coordination and insufficient training were common root causes. To better understand how and why errors occurred, we reviewed six in depth. Although the total monetary amounts of the errors reviewed was relatively small, they may have had a larger impact on individual employees and trust in the payroll process.

Our 2013 follow-up audit found that Metro's approach to tracking errors was incomplete. The same was true during this audit. Without a formal approach to track errors, it can be difficult to find the source of the error, how it should be corrected, and who should correct it.

In other organizations, payroll has been identified as a considerable source of potentially fraudulent activity. A variety of controls are required to separate duties and limit access to data so that no individual employee can initiate and process payments. We found duties were not properly segregated and employees had access to data that appeared to be more than what they needed to perform their work. We also found that reconciliation of payroll accounts were not done timely last fiscal year, which may have reduced Metro's ability to detect potential fraud and waste.

We recommended Metro improve coordination by creating a formal system to track errors. Initial and ongoing training were also needed to give employees the tools to complete their jobs. Finally, we recommended that Metro implement additional controls to reduce the possibility of fraud, waste, and abuse.

Background

The payroll process is an important part of Metro's internal business services. It impacts every department and employee. Timeliness and accuracy are key components of effective and efficient payroll administration. In Fiscal Year 2016-17, Metro's expenditures for gross pay totaled about $68.4 million. A total of 36,612 checks were processed or an average of 1,525 per pay period.

Payroll processing is commonly part of an organization's accounting function. This is to ensure separation between those charged with maintaining employee information and those who issue payments to employees. At Metro, the Payroll division has moved between Human Resources (HR) and Finance and Regulatory Services (FRS). Since 2015, it has been part of FRS.

The Payroll division consists of four employees. Since 2013, it has had four different supervisors. Other departments have a role in the payroll process. Information Services (IS) manages the systems used in the payroll process. HR sets up those systems with information so that employee pay can be calculated correctly. HR staff also manage employee job and benefits information. Timekeeping review and sign-off is done by department managers and Payroll staff.

Exhibit 1   **Many departments have a role in the payroll process**
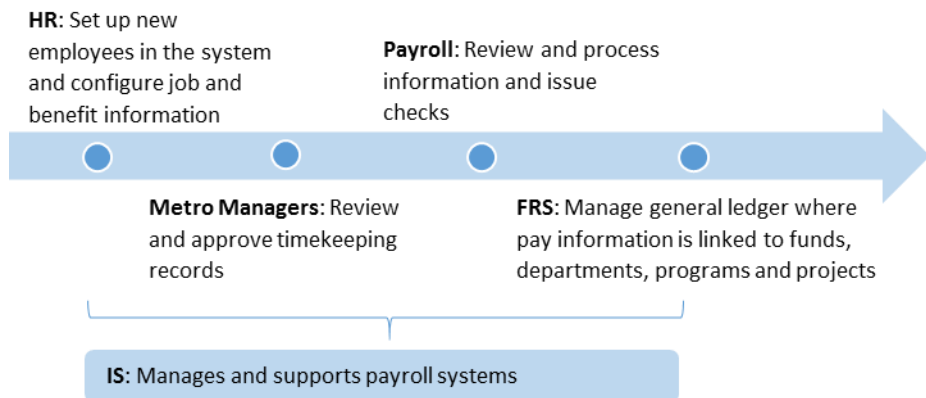
Source: Metro Auditor's Office analysis

There are three software systems used in the payroll process. Kronos is the timekeeping system. PeopleSoft Finance is the accounting system. FRS uses it to manage the general ledger where pay information is linked to funds, departments, programs, and projects. PeopleSoft HRIS is used by HR to manage employee information.

Over the last 10 years, the Office of the Metro Auditor (Office) has identified weaknesses with Metro's payroll processes. A 2006 audit found internal controls could be improved such as the proper segregation of duties. Four years later in 2010, our Office released another report that provided recommendations for additional improvements. These recommendations focused on:

- Increasing department coordination to clarify roles and responsibilities;
- Developing clear policies and procedures;
- Improving the use of software functionality to reduce manual processes; and
- Implementing stronger controls to ensure greater transparency and data accuracy.

In November 2012, Metro's accountability hotline received a report alleging several errors in payroll calculations, such as the amount of deductions taken from employee paychecks for health insurance and union dues. A follow-up audit was started in response to the allegations because the issues raised by the ethics reports were similar to the findings from the 2010 audit. The follow-up audit confirmed that all of the reported errors were valid and stronger controls were needed to ensure timely and accurate pay. In 2016, we were notified of payroll errors related to deductions and leave hours.

Since at least 2009, Metro has started improvement projects to address payroll issues. That year, Metro contracted with a firm who reviewed employee retirement contributions. The following year, Metro contracted with a consultant who made recommendations such as minimizing manual processes, and outlining roles and responsibilities. In 2013, Metro started an in-house project to address inaccuracies related to payroll configurations. The extent to which that project was completed was unclear. In February 2017, Metro started another payroll process improvement project. The goal of the project was to eliminate systemic and chronic pay and leave inaccuracies.

Results

Since 2006, our Office has identified issues with payroll accuracy, timeliness, and controls. Although some improvements were made, most of the payroll related recommendations from previous audits were not implemented. The overall process lacked an owner and the root causes of some reoccurring issues were not addressed. As a result, there were ongoing errors and weak controls.

Moving forward, Metro will have to strengthen management between the three departments involved in the payroll process. To ensure accurate pay, better coordination and training is needed to address the root causes of payroll issues so that the momentum of the latest improvement efforts can be sustained.

Despite previous efforts, some payroll issues remained

Metro made efforts to improve the payroll process. It changed management structures and moved tasks across and within departments. It also initiated projects that focused on technological and software enhancements to ensure accuracy, and reduce the need for manual changes to data. Positive outcomes included a better understanding of the software systems and some increased automation and efficiency.

During our audit, Metro initiated another project focused on improvements. Metro reported that early phases resulted in increased efficiency, and some technical changes were in process. A limited duration project manager was hired to document the process as a whole and ensure the project's completion. The project brought together the Deputy Chief Operating Officer and Department Directors to get the appropriate level of authority to address issues that cannot be resolved by the employees who process payroll.

We did not evaluate the results of the project as part of this audit. However, some project updates to employees indicated the need for improved communication to strengthen trust. For example, one update noted a part of the project was completed when it was not. Another update promised employees that a question and answer session would be recorded for those that were unable to attend, but it was not.

Even though Metro made efforts to improve the payroll process, we found many of the findings identified in our previous audits remained.

Exhibit 2   Audits identified ongoing issues

Findings	Previous Audits		
	2006	2010	2013
Payroll errors		X	X
Lack of error tracking		X	X
Duties not adequately segregated	X	X	X
Employees have more access to data than what may be necessary for their job	X	X	X
Untimely reconciliations		X	X

Source: Metro Auditor's Office reports

These issues continued because Metro had not addressed their root causes. For example, a direct cause of an error may be entering incorrect information for a deduction. The root cause could be that training was not in place to help employees understand how the deduction should be calculated. Based on the ongoing payroll issues we reviewed, lack of coordination and insufficient training were common root causes.

Exhibit 3   Addressing root causes would help resolve issues

Root cause:	Criteria:	Why it is important:	Improvement could:
Lack of coordination	• Strong understanding of roles and responsibilities • Good communication within and between departments	Metro's payroll process doesn't have a single owner, so success depends on employees across multiple departments working together to achieve accurate and timely pay	Help employees understand: • Why issues happened • How to resolve them • How to avoid them in the future
Insufficient training	• Initial and ongoing training • Documented policies and procedures	Employees need to have the tools necessary to be successful at their work	• Increase engagement and morale • Provide stability in the event of turnover • Prevent issues from occurring in the first place

Source: Metro Auditor's Office analysis of management literature

Case studies show more work was needed to address root causes of errors

We found errors continued to happen because coordination and training needs were not addressed. Metro is responsible for timely and accurate pay. It must adhere to applicable laws, collective bargaining agreements, and other employment policies. There are several types of payroll errors and several places in the process where they can happen. Some examples include:

- The information in Kronos and PeopleSoft may not be correct and result in inaccurate calculations of time and pay data;
- Supervisors may not provide a thorough review of employee timesheets and employees may not always accurately track their time and leave information; or
- Language in collective bargaining agreements could be ambiguous or not followed exactly, resulting in inaccurate payments or leave hours.

To better understand how and why errors occurred, we reviewed six in depth. We determined that two errors (incorrect sick leave hours and vacation misalignment) were handled together. For the two errors related to union dues, we were only able to get limited information.
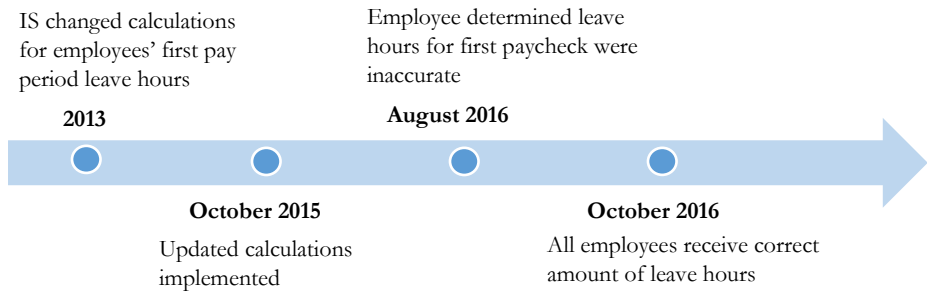
Although the monetary amounts of the errors reviewed was relatively small, they may have had a larger impact on individual employees and trust in the payroll process. The errors demonstrated that Metro's quality control processes were underdeveloped and highlighted the need to address root causes.

In August 2016, an employee determined that they did not receive vacation or sick leave hours for their first paycheck in 2015. The following month a union filed a grievance related to this error. After the grievance was filed, HR reviewed vacation and sick leave hours and determined that hours were accurately calculated beginning in October 2015. This meant that prior to October 2015, all employees likely did not get vacation and sick leave hours for their first paycheck unless they started on the first day of the pay period.

Most union contracts required Metro to conduct a look back from when an error was discovered. The look back period was two years. Metro reviewed employees impacted by the error from October 2013 to October 2015. Based on this review, HR determined the error impacted 131 represented and non-represented employees. The amounts were small because the sick leave and vacation hours were only for an employee's first pay period. The error was corrected in September 2016 for non-represented employees, and in October 2016 for union members.

The error was caused by a lack of coordination between Payroll and IS. In 2013, IS changed how an employee's first pay period leave hours were calculated. IS assumed the changes were tested for accuracy by Payroll before being put into use. It took almost two years to ensure employees' first pay period leave hours were accurately calculated.

Exhibit 4 **Almost two years passed before employee first paycheck leave hours were accurate**

IS changed calculations for employees' first pay period leave hours

2013

Employee determined leave hours for first paycheck were inaccurate

August 2016

October 2015

Updated calculations implemented

October 2016

All employees receive correct amount of leave hours
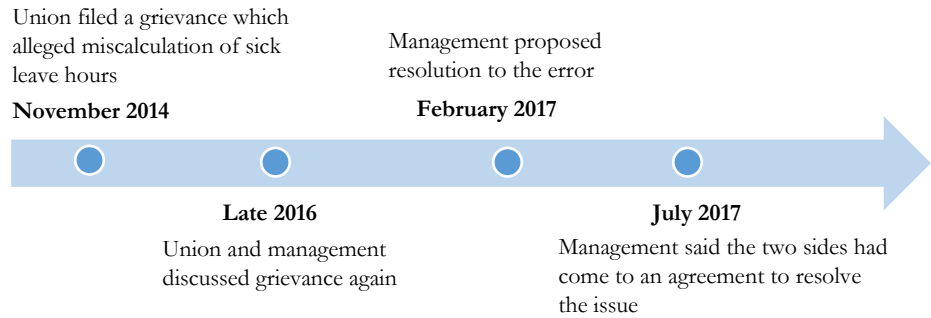
Source: Metro Auditor's Office analysis

In November 2014, a union filed a grievance because a member did not receive the correct amount of sick leave hours. Due to a misalignment between language contained in the bargaining agreement and what was setup in PeopleSoft, some employees were awarded sick hours for time they did not work while others were not awarded sick leave hours for time worked such as overtime. Metro did not know when the incorrect setup began. When the grievance was filed and negotiations to correct the error between management and the union started, management brought up a vacation misalignment related to a separate agreement with union members. This was a misalignment that allowed union members to incorrectly receive additional vacation hours.

Over two years passed and in late 2016 the union and management discussed the grievance again. Management and the union gave different explanations for the delay in resolving the grievance. Management stated that the sick leave misalignment was not addressed because the two sides never came to an agreement. The union stated that in order to reach an agreement management required a resolution for both misalignments.

In February 2017, Metro proposed crediting employees impacted by the error. Based on its review, 53 employees were impacted and were owed a total of 245 sick leave hours. The proposal also allowed employees to retain the sick leave earned for hours they did not work. The proposal made no mention of the misalignment related to vacation hours. In July 2017, management said the two sides agreed to the proposed resolution. In short, almost three years passed until an agreement was reached to correct the sick leave misalignment.

The error was caused by a lack of coordination between HR and Payroll. This was because the language that was agreed to in the contract was not setup correctly in PeopleSoft. Because of the misalignment, some employees did not receive accurate and timely sick leave hours for nearly three years, and some employees received more hours than they should have.

Exhibit 5   Almost three years passed before an agreement was reached to correct leave hours

Union filed a grievance which
alleged miscalculation of sick
leave hours

November 2014

Management proposed
resolution to the error

February 2017

Late 2016

Union and management
discussed grievance again

July 2017

Management said the two sides had
come to an agreement to resolve
the issue

Source: Metro Auditor's office analysis

In July 2016, an employee emailed Payroll staff to tell them there was an error related to a sick leave donation made by the employee. Payroll staff determined that sick leave donations were incorrectly calculated for four months. The error caused sick leave hours to be added instead of being deducted from employees making donations. Payroll staff reviewed who was impacted and determined that 24 employees were given a total of 605 additional sick hours in error. Payroll employees were unsure how to address the issue and asked Labor Relations how they wanted to handle it. It was determined that since the amounts of additional sick leave were so high for some employees, a correction should be made.

The error was caused by lack of written procedures and training for Payroll staff. A new employee was hired around the time the initial error occurred and was tasked with calculating sick leave donations. However, the employee was not given training nor were there procedures to follow. This error highlights the importance of ensuring that new staff are given the tools to correctly do their job. Inaccuracies occurred because these tools were not present.

Metro did not accurately deduct union dues for some employees. We identified two different errors related to union dues. We were unable to find out how many employees were affected by one of the errors. The error may have impacted any employee that moved from a represented to a non-represented position. For the other error, related to dues for temporary employees, we received limited information.

Dues for temporary employees were deducted when a member turned in their membership card to Metro. Some membership cards were not being turned in, so Metro was not deducting the dues. Metro determined since at least the summer of 2016 that it was legally obligated to deduct dues for temporary employees even if they did not turn in their membership cards. However, we were told in June 2017 that union dues were not deducted for some unions until a membership card was received. In July 2017, Metro staff said that a full review of temporary union dues for one union will be initiated.

This issue was caused by a lack of coordination between Payroll, Office of the Metro Attorney, and HR. If one department decides a particular change is needed within the payroll process, it is incumbent upon that department to inform the other departments. Errors occurred because this did not happen.

Metro lacks a formal way to track payroll errors

Our Office's 2013 follow-up audit found that Metro's approach to tracking errors was incomplete. The same was true during this audit. Formal processes are essential for organizational learning and adaptability. These processes include gathering and analyzing information. For payroll, this would mean tracking as well as analyzing errors. Without a formal approach to track errors, it can be difficult to find the source of the error, how it should be corrected, and who is responsible for the correction.

Limited information about errors can make it difficult for the departments to have a common understanding of an error and how to correct it. In the past, some new errors occurred because of changes made to correct another error.

The error related to employees' sick leave hours was due to a lack of coordination between departments. This error may have been prevented if Metro had a formal way to track errors. Instead, at least two years passed before the solution was implemented and it was unclear who ultimately implemented it.

Without having a formal process to track payroll errors across departments, Metro may have missed an opportunity to more efficiently determine where challenges occurred during the payroll process. Error tracking could help determine where resources should be directed to improve the process. For

Underdeveloped controls continued to present an opportunity for fraud, waste, and abuse

In other organizations, payroll has been identified as a considerable source of potentially fraudulent activity. A variety of controls are required at key points in the payroll process. Previous audits consistently identified challenges with ensuring duties were segregated, access to data was appropriate, and reconciliations were timely. Better coordination, and increased training were necessary to manage fraud, waste, and abuse risks at Metro.

Metro made incremental improvements over the years to address some risks. These included increased automation for some data calculations, removing some manual processes, improvements in security monitoring, and reorganizing payroll processing to improve segregation of duties. More recently, Metro was working on a list of potential safeguards to address payroll risks. However, more work was needed to address them.

Duties were not segregated to fully minimize risk

Segregation of duties ensures that no one person or department can perform the functions needed to carry out the critical processes of a transaction. Increased coordination and training were needed to ensure segregation of duties was maintained across the payroll process as a whole. Without proper segregation of duties, there was an increased risk that Metro

could pay employees who aren't real (ghost employees). There was also a risk Metro could pay for work that was not actually done. These risks increase when there are group timecard signoffs and relaxed reviews of employee timesheets.

For payroll, maintaining personnel data (e.g. adding a new employee, or changing salary information), approving employee time, and processing paychecks should be segregated.

Exhibit 6   Segregate duties to reduce risks

Source: Metro Auditor's Office analysis of control best practices

Duties were not properly segregated. An analysis by IS showed that, of the employees who could create a new employee in PeopleSoft, some could also add to or approve employee timesheets. This increased the risk of creating a ghost employee and approving their time. Additionally, Payroll and HR employees had the ability to add or change some of the same data, even though activities performed by those groups should be segregated.

There were other scenarios we heard of during the audit that increased the risk a terminated employee could be improperly kept on the payroll as their pay is diverted. In one scenario, HR staff responsible for inactivating an employee in the system may not learn about a termination until after a final paycheck is created. In another, HR staff may have to reach out to supervisors about temporary employees who have not worked in a year.

For some parts of the payroll process, duties were not segregated but other safeguards were in place to reduce risk. For example, multiple supervisors or managers were involved in generating the data used to add employees to the system. They could also change employee hours and approve timesheets. Having supervisors and managers in both of these roles likely provided convenience for some new employees, even though ideally these positions should be segregated. HR processed background checks for employees and required a copy of photo identification, which acted as a safeguard. This made it more difficult to create a ghost employee and then approve their time. We reviewed a selection of employee files and found the mitigating controls were being followed.

Because there were three departments involved in setting up payroll information, efforts to ensure certain duties were appropriately segregated needed to be coordinated. Without coordination, there was an increased risk of gaps. Each department brings different expertise and authority to impact

the overall process. Ensuring proper segregation of duties for the payroll process requires stronger understanding of what ought to be, what people across the agency can do in the software, and what role they have in the process. If changes occur in roles or software permissions, they need to be evaluated to determine their effect on segregation of duties.

Metro employees had more access to data than necessary to complete their work

Employees had access to data that appeared to be more than what they needed to perform their work. In some cases, understanding of the extent of that access was limited. Access should be restricted to only what employees need to complete their jobs. Too much access can impact data integrity and increase the risk for fraud or abuse. Increased coordination between IS, payroll, and HR could improve understanding of staff access. Training could also help employees understand what data they, and their direct reports, can access.

Nine people in HR could add a new employee to the system. We were told there would not be a time when nine people would need to do this. One position had the primary responsibility of entering new employees into the system. Twice a year there may have been a need for others to perform this duty. This meant for the majority of the year, there were up to eight extra people in HR who could add a new employee to the system. It may have been appropriate to increase access, but there should have been a process to ensure that once the business need was met, access aligned with actual responsibilities.

Several employees in HR and Payroll had access to make changes through "correction mode." This access overwrites data when it is changed. Its use is discouraged because of the risk it presents to data accuracy. We were told that correction mode was mostly used to make certain changes or fix data entry errors. We were also told that a report existed that could show some changes made in correction mode, but it was not regularly used. Even though previous audit recommendation identified the need to properly define the function and educate users on its use, there were no formal guidelines or policies in place on how to use correction mode, or other ways to evaluate or approve its use.

There was also overlap in access to data among HR employees. For example, employees that could enter employee job and salary information also had access to employee benefit data, even though a different unit in HR handled benefit information. Likewise, employees in Benefits had access to other, unrelated, employee personnel data. In some cases there may not have been a business need for this access. In others, access may not have been updated as employees moved between different units in HR. As access expands over time there is a risk it could negate other controls in place, such as segregation of duties. It could also provide unnecessary access to personal information.

Payroll staff had access to a large amount of timesheet and payroll data. Some of this access was required to process payroll. Some was needed because of limitations in software or Metro's payroll process. Information

was transferred from Kronos in a text file that could be changed manually. Changes to data were made in PeopleSoft throughout payroll processing. High levels of access to manually change data was necessary to ensure accurate pay, but increased the risk of fraud and abuse.

In payroll processing, some controls were in place to mitigate high levels of access. For example, Payroll ran reports that would show large adjustments to employee pay. We were told that all changes made during the payroll process were reviewed and approved. However, we found reviews of changes and reports were inconsistently documented and therefore could not conclude on their effectiveness.

Employee direct deposit data also existed in a file that was editable, and there was a group login to access the payroll bank account. According to management, the bank did not allow more than one login for the account. Monthly bank reconciliations were in place to ensure there were no inappropriate edits to direct deposit information. However, shared login access posed a risk. It reduced Metro's ability to determine who logged in to the bank account and tie transactions to the individual who carried them out. It should be avoided when possible.

Regular security reviews were cited as ensuring employee access to data was appropriate. However, our observations showed it may not have provided the assurance people believed it did. The annual security reviews did not always give the information necessary for managers and lead employees to make informed decisions about the access their employees had. In some cases, employees continued to have high levels of access to data because efforts were not coordinated to limit it. We were told that, in one department, it was not on anyone's radar to alert IS to change access levels when employees change roles.

The timeliness of reviews was also an issue. When we first began the audit, there had not been a security review of PeopleSoft HRIS access for two years. A review was supposed to take place annually. Management stated this was due to a software upgrade. There were no formal reviews of access to Kronos, the time keeping system.

Reconciliations were not timely

Metro did not reconcile some payroll accounts in a timely manner. Reconciliation is the process of matching one set of records with another set of records and identifying, explaining, and correcting any difference. For example, matching the total amount withheld for taxes with the individual amounts withheld from each paycheck. Reconciliations serve as a key element of internal control and should be done on a timely and routine basis.

Payroll staff were responsible for reconciling 14 accounts related to employee deductions such as income tax withholdings, union dues, payroll taxes, and garnishment deductions. These accounts totaled about $23.3 million reconciled in FY 2016-17. Of the 14 accounts, 12 were supposed to

be completed on a monthly basis. According to FRS data, these were only completed about 50 percent of the time from July 2016 through April 2017. These accounts represented about 98 percent of the total amount that is reconciled by Payroll staff. Two accounts (the remaining two percent) were supposed to be done on a quarterly basis. These were only completed a third of the time during the same time period.

Exhibit 7   Timeliness of reconciliation varied from July 2016 through April 2017

Account	FY 2016-17 amount	Percent completed on time (July 2016 - April 2017)
Federal income tax withholding	$7,682,538	60%
Federal Insurance Contributions Act tax withholding	$5,058,223	20%
Federal Insurance Contributions Act tax payable	$5,058,223	60%
State income tax withholding	$4,114,864	60%
Tri-Met payroll tax	$491,174	33%
Union dues	$331,759	30%
Garnishment deductions	$185,114	50%
Union dues	$182,697	70%
Union dues	$66,960	20%
Parking deduction	$52,183	60%
Worker's compensation	$32,005	33%
Union dues	$30,218	60%
Union dues	$28,896	70%
Union dues	$9,083	70%

Source: Metro Auditor's Office analysis of FRS and PeopleSoft data

This may have been caused, in part, by turnover within Payroll. We were told Payroll staff who were hired within the last year were not trained to complete reconciliations and may not have had time to complete them. By not completing the reconciliations, Metro may have reduced its ability to detect potential fraud and waste.

Scope and methodology

The purpose of this audit was to determine if Metro addressed the root causes of ongoing payroll issues. The audit had two objectives:

- Determine reasons for continued errors in the payroll process.
- Determine if adequate controls were in place to reduce the potential for fraud, waste, and abuse.

To accomplish our objectives, we interviewed Metro management and employees involved in the payroll process. Those included employees from Human Resources, Finance and Regulatory Services (FRS), and Information Services. We observed many tasks of the payroll process, including changes to set-up tables, timekeeping, payroll calculation and payments. We also observed some quality control procedures, such as completion of end-of-year checklists and reports that checked for errors or anomalies.

We reviewed previous Metro audits related to payroll, as well as audits of other agencies. To better understand the topic of payroll and internal controls, we reviewed literature from various sources, including, American Payroll Association, ISACA (previously the Information Systems Audit and Control Association), the Institute of Internal Auditors, and the Association of Certified Fraud Examiners.

A payroll process improvement project was initiated during our audit. We reviewed that project's charter, objectives, and communication to employees, as well as its planned tasks and deliverables. We also reviewed documentation related to Metro's previous improvement efforts, annual budgets, and Council meeting minutes.

To determine the reason for continued payroll errors, we reviewed case study literature about the design and selection of case studies. Based on this review, we selected six payroll errors to understand what caused them.

To determine whether adequate controls were in place, we conducted additional interviews with employees throughout the payroll process. To select which controls to review, we conducted a risk assessment using guidelines from best practices, previous payroll challenges, current processes, and the potential for the current improvement project to address the risk area. Specific risk areas we chose to review included segregation of duties, access to data, and reconciliations.

We reviewed PeopleSoft and Kronos security settings and roles to identify issues related to data access and segregation of duties. To review reconciliations, we conducted additional interviews with employees and reviewed account tracking information from FRS employees.

This audit was included in the FY 2016-17 audit schedule. We conducted this performance audit in accordance with generally accepted government auditing standards. 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.

Recommendations

To improve coordination, Metro should:

1. Create a formal system for tracking errors that:
   a. involves each department in the payroll process,
   b. tracks the source of the error,
   c. how it should be corrected; and
   d. who is responsible for the correction.

To ensure employees have the tools necessary to do their job, Metro should:

2. Provide timely initial training;
3. Assess training needs, and provide ongoing training as necessary.

To better align the payroll process with best practices to reduce the risks of fraud, waste, and abuse, Metro should:

4. Segregate duties across all aspects of the payroll process. When not possible, ensure mitigating controls are in place, used, and documented.
5. Limit employee access to only data necessary to perform job duties. When high levels of access are necessary, establish safeguards to ensure proper use.
6. Assign roles, responsibilities, and authority for ensuring proper access and segregation of duties across the payroll process.
7. Conduct regular reviews of employee access to Kronos and PeopleSoft. Ensure reviews provide the information necessary to make informed decisions about employee access.

Management response

Memo

Metro
600 NE Grand Ave.
Portland, OR 97232-2736

Date: December 19, 2017

To: Brian Evans, Metro Auditor

From: Tim Collier, Director, Finance and Regulatory Services
            Rachel Coe, Director, Information Services
            Mary Rowe, Director, Human Resources
            Scott Robinson, Deputy Chief Operating Officer

Subject: Management Response – 2017 Payroll Audit

Thank you for the opportunity to respond to your audit of Metro's payroll process. Ensuring that our employees are paid timely and accurately is Metro's highest priority. Your recap and summary of previous audits and recommendations reinforce the important work that is already underway as part of the agency payroll process improvement project that started in January of 2017. While the current work effort was not reviewed or included in the current audit, management believes that significant progress has been made in the areas you have recommended.

The payroll project includes membership from all three departments (IS, HR, FRS) involved in the processing of payroll and a formal steering committee that is made up of the three department directors and the Deputy Chief Operating Officer. With the help of external consultants, the project team has extensively reviewed pay rules, system configurations, and processes in both PeopleSoft and Kronos. We have developed a priority list from those reviews and from issues found in previous payroll runs. Many improvements have already been completed as part of that project.

To address earlier, outstanding audit issues and other improvements identified from the payroll project work, the team has put together a formal list of changes and are systematically working to complete that project list. A measured approach to implementing changes is necessary to avoid creating new issues and other unintended consequences. The payroll project team has now been chartered and formally charged as an ongoing team with the Payroll Supervisor being the business process owner and team lead. The steering committee remains in place to support the improvement process, provide project prioritization, and policy guidance.

We also believe that context is important. Payroll is an extremely complicated process, particularly with eight different unions and non-represented employees. The few errors that have been found have been corrected as quickly as possible and impacted employees have been notified. Again, ensuring the timeliness and accuracy of employee's payroll is of extreme importance for our agency and we will continue to improve to meet our high standards.

Recommendations:

To improve coordination, Metro should:

1. Create a formal system for tracking errors that:

>*a. involves each department in the payroll process,*

>*b. tracks the source of the error,*

>*c. how it should be corrected; and*

>*d. who is responsible for the correction.*

We agree that a more formal process should be developed.   The payroll project team, which is made up of individuals across all three departments, will be the place that these systemic errors are discussed, correction assigned, and resolution reported and documented.

To ensure employees have the tools necessary to do their job, Metro should:
2. Provide timely initial training;

We believe this was a temporary issue due to the change of payroll from HR to FRS and personnel turnover. Even so, we have worked to document all of our processes and brought in external consultants and trainers to work with staff to improve knowledge of the system. We agree that training is important and continues to be a primary focus of the current payroll supervisor. With the new position in payroll that was approved in November, we will ensure that this emphasis on training and documentation continues. In addition, a training program has been developed to improve the consistency and accuracy of the timekeeping process across the agency. This program will be deployed in the next couple months.

3. Assess training needs, and provide ongoing training as necessary.

As part of our current payroll process improvement project, employee training needs were surveyed, and training materials are in the final stage of development. In addition, as we continue to improve our documentation and review current responsibilities, we will assess our payroll training needs. One area of particular focus will be cross-training staff on the roles across payroll, ensuring Metro will always be able to deliver paychecks on payday regardless of the circumstances (building closure, employee sickness, etc.). We have dedicated funding for training in the payroll area to ensure staff will continue to be updated on the newest issues in payroll and have the skills necessary to be successful.

To better align the payroll process with best practices to reduce the risks of fraud, waste, and abuse, Metro should:
4. Segregate duties across all aspects of the payroll process. When not possible, ensure mitigating controls are in place, used, and documented.

Segregation of duties is of the utmost importance in any payroll operation. However, in a payroll shop the size of ours it is difficult to have total segregation of roles. People must cover for other people on extremely short notice and we have seasonal hiring that requires additional assistance. Metro's external auditors review system security, including in the payroll area, during their annual review; we have not had an external auditor comment that this is an issue. However, as a result of the audit, we have reviewed the

security roles of HR and Payroll staff and have made some adjustments. We have also made some changes in the way security is granted. Exceptions will be completed in writing and accompanied by a start and end date. We will continue to review our processes and duties on an ongoing basis.

5. Limit employee access to only data necessary to perform job duties. When high levels of access are necessary, establish safeguards to ensure proper use.

We agree, access for job duties is a key to segregation of duties and ensuring proper use. However, being a smaller payroll shop multiple people, at times, must be able to have access to the data to ensure that jobs can be completed in a timely manner (especially around the beginning of the year and with large projects). We do currently have internal controls that help mitigate risk and we will continue to ensure that we only allow access to those that it is necessary to complete all of the work.

6. Assign roles, responsibilities, and authority for ensuring proper access and segregation of duties across the payroll process.

We agree, with the new payroll position being hired we are doing a detailed review of current responsibilities and how the roles in payroll are distributed. As we review that work, we will look at access and additional documentation.

7. Conduct regular reviews of employee access to Kronos and PeopleSoft. Ensure reviews provide the information necessary to make informed decisions about employee access.

We agree, timely reviews of employee access are a necessary action for strong internal controls. We currently do this annually in all systems. When individuals leave employment, automatic notifications to terminate access to the network, email, and software systems are distributed from the HRMS system. We will continue to document accordingly.