



OFFICE OF THE CITY AUDITOR
COLORADO SPRINGS, COLORADO

13-06
Colorado Springs
Utilities Payroll Audit

April 2013



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Purpose

The purpose of the audit was to perform a review of payroll and contractor pay that ensured an adequate internal control environment, accurate and timely payments, and compliance with policies and procedures. Our scope included policy compliance for additional compensation such as standby pay.

Highlights

We concluded that overall, the internal control structure was adequate, and transactions were being processed accurately. Monitoring requirements by management and Human Resources were generally being followed. Some policies and related compliance enforcement should be strengthened. During the course of the audit we identified four observations and have listed our recommendations in the attached report.

- 1) Administrator user access—Administrators for the Human Resources and Payroll Systems could modify any data in the system without another user's involvement. Reports of administrator actions were not in place.
- 2) Exempt employee standby pay— Criteria or guidance for justification of standby pay eligibility for exempt employees was not well-defined. Policy did not require monitoring by Human Resources. Employees were limited to an additional 25% of base pay and labor was subject to budgetary controls. The immediate supervisor approved standby pay.
- 3) Approval of payroll hours—Supervisors were not approving time promptly to allow timely processing of payroll, which increased risk of errors and administrative burden.
- 4) Agency Contract Personnel (ACP) - Assignment extensions over 12 months were not approved by senior management for two contract

(Continued on page 2)

Management Response

Management was generally in agreement with our recommendations. Responses can be found in the attached report.

Recommendations

1. A process should be developed to monitor transactions entered into the Payroll and Human Resources system under administrator access.
2. We recommend Colorado Springs Utilities develop a well-defined policy that defines circumstances under which exempt employees may receive standby pay. Policy should include frequency of approval, and justification and monitoring requirements.
3. Performance criteria should be put in place to ensure Supervisors perform their time reporting responsibilities and held accountable for noncompliance.

A policy should be put into place requiring payroll adjustments be submitted within a reasonable time period.

(Continued on page 2)

13-06 Colorado Springs Utilities Payroll Audit

April 2013

(Highlights continued from page 1)

employees tested. We understand this occurred due to information technology issues which have since been corrected.

Some ACP assignments were greater than one year. The Monthly Usage Report dated June 30, 2012 indicated 57% had been ACP over 12 months and 39% had been ACP over 24 months.

(Recommendations continued from page 1)

4. We recommend increased compliance with ACP extension approval requirements. Workforce Planning should define the frequency for auditing approvals of extensions and develop procedures to strengthen enforcement of compliance with policy requirements that ACP do not work more than 30 days past the assignment end date.



Office of the City Auditor

Colorado Springs Utilities Payroll Audit

Date: April 3, 2013

To: President Hente, President Pro-Tem Martin, and Members of City Council

Re: 13-06 Colorado Springs Utilities Payroll and Related Activities Audit

We conducted an audit of the Colorado Springs Utilities payroll and payroll related functions covering the months from January 1, 2012, to June 30, 2012.

The purpose of this audit was to perform a review of payroll and related activities to ensure an adequate internal control environment as well as accurate and timely payments to employees, and compliance with policies and procedures. The review centered on the payroll function and the financial processing system, which is used to make payments to employees. Additionally, we reviewed for compliance with policy requirements related to contract labor and additional compensation such as standby pay. A risk assessment was performed to determine audit procedures and focused on areas of highest risk.

We concluded that overall the internal control structure was adequate, transactions were being processed accurately, and the key policies and procedures were being followed. We did find oversight, authorization, and policy enforcement for standby pay and contract labor could be strengthened. We identified four observations, which are listed in the attached report.

As always, feel free to contact me if you have any questions.

Sincerely,

A handwritten signature in black ink, appearing to read "Denny Nester".

Denny Nester, MBA, CPA, CIA, CGFM, CFE, CGAP

City Auditor

Cc: Jerry Forte, Chief Executive Officer
Carl Cruz, Chief Customer and Corporate Services Officer
Bill Cherrier, Chief Planning and Financial Officer
Dede Jones, General Manager, Financial Services
Sandi Yukman, General Manager, Human Resources
Sonya Thieme, Manager, General Accounting
Melissa Kellione, Manager, Talent Acquisition, Planning, and Rewards
Dan Noble, Manager, Workforce Operations and Management
Dave Maier, Manager, Enterprise Risk Management
Patricia Van Meter, Senior Analyst, Enterprise Risk Management



Office of the City Auditor

Colorado Springs Utilities Payroll Audit

Report Details	1
Purpose and Scope	1
Background	1
Commendable Practices	2
Conclusion	3
Observations, Recommendations and Responses.....	4
Observation 1 - Insufficient monitoring of administrator actions and user access levels.....	4
Observation 2 – Exempt standby pay policy eligibility criteria was not well defined and monitoring by Human Resources was not in place.....	5
Observation 3 - Supervisors were not approving employee time promptly to allow timely processing of payroll ..	7
Observation 4 – Contract extensions for agency contract personnel were not monitored sufficiently	9



REPORT DETAILS

PURPOSE AND SCOPE

The purpose of the audit was to perform a review of payroll and contractor pay that ensured an adequate internal control environment, accurate and timely payments, and compliance with policies and procedures. The review centered on the payroll function and the financial system, which was used to make payments to employees. Our scope included policy compliance for additional compensation such as standby pay.

In addition, we reviewed policy compliance regarding contract labor employees. Consulting services were not included in this review. We did not examine regulatory compliance with Federal and Colorado laws. We also reviewed trend data related to payroll and contractor pay, for 2006 through the most recent period available during our audit, which was December 31, 2011 or June 30, 2012 in some instances.

A risk assessment was performed which determined audit procedures and focused efforts on areas of highest risk. Our audit period was January 1, 2012 through June 30, 2012.

BACKGROUND

Process Background

The Colorado Springs Utilities payroll function was centralized and responsible for processing all employees' pay every two weeks. Colorado Springs Utilities Payroll Department reported to the Customer and Corporate Services Division from 2005 through our audit period. Effective October 1, 2012, the department reported to the Planning and Finance Division. The department consisted of four full-time employees to process over 1800 employee paychecks. Each employee that was not a direct charge employee was responsible for entering reported hours electronically through a resource management system for approval by their supervisor. Employees that were classified as direct charge employees were required to enter exception time only, such as vacation or sick leave, for supervisor approval. Payroll personnel conducted several data verification steps on the approved time as part of payroll processing.

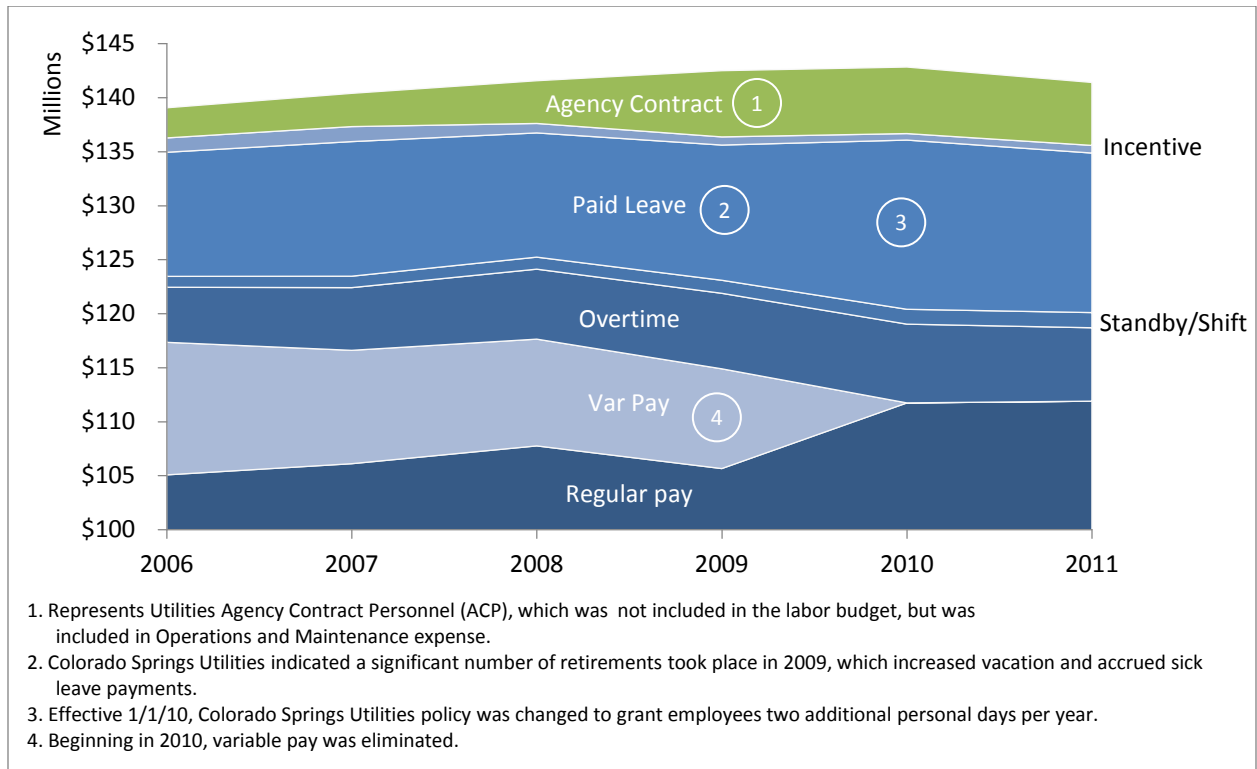
Colorado Springs Utilities Agency Contact Personnel (ACP) policy guidance stated that ACP were utilized as a cost effective means of meeting the labor needs where the nature of the work is short/limited term. Human Resources Workforce Planning Department was responsible for centralized management of ACP for Colorado Springs Utilities. We conducted a limited review of Colorado Springs Utilities usage of ACP. The scope of our review did not include agency contract procurement or compliance, nor did we analyze the efficiency or effectiveness of contract labor utilization.



The Human Resources Compensation Unit performed oversight and monitoring of additional compensation such as standby pay.

Trend Data

The following chart details payroll and ACP expenses by year. Trends indicate gross payroll has remained flat from 2006 through 2011. **Please note the chart begins at \$100 million.**



Source: Colorado Springs Utilities General Ledger System

COMMENDABLE PRACTICES

We noted improvements made by Colorado Springs Utilities Payroll since the last audit report issued in 2009. Improvements were noted in increased segregation of duties, supervisory time approvals, and review of account reconciliations.

Additionally, we noted strengthening of employment processes administered by Human Resources and Payroll including:

- Creation of an Agency Contract Personnel database and centralized management of ACP was implemented in 2010.



Office of the City Auditor Colorado Springs Utilities Payroll Audit

- Development of position management processes which ensure consistent creation, administration and review of all positions.
- A comprehensive I-9 review was in progress in 2012 to ensure federal compliance.
- Financial payroll processing system had improved user access due to custom set-up of users by need with the new security upgrade.
- Automation and improved employee features in the payroll financial system to reduce time spent by payroll on administration, communication and correction of errors.

CONCLUSION

We concluded that overall, the internal control structure was adequate, and transactions were being processed accurately. Policies and procedures in key areas were generally being followed. Some policies and compliance should be strengthened. During the course of the audit we identified four observations and have listed our recommendations in the attached report.



OBSERVATIONS, RECOMMENDATIONS AND RESPONSES

OBSERVATION 1 - INSUFFICIENT MONITORING OF ADMINISTRATOR ACTIONS AND USER ACCESS LEVELS

- Business Application Administrators in Human Resources and Accounting had the ability to modify any data within the system without another user's involvement, creating a segregation of duties concern.
- Reports were not in place to monitor transactions entered by the Business Application Administrators.

Business Application Administrators (BAA) in Human Resources and Accounting have security access to most functions and screens in the financial modules. The administrator access level provided the user with the ability to modify any data within the system (e.g. add employees, update payroll taxes and calculation information, make salary changes) without the segregation of duties provided by another user's involvement.

Historically, the BAA users have been granted add/change/delete access to all screens so they may act as a liaison between Accounting, Human Resources and Information Technology to coordinate testing, implementation of system patches and upgrades. Information Technology did not have access to the payroll software system.

Without monitoring of transactions processed by those individuals with unlimited access, inappropriate or unauthorized transactions could go undetected. Reports should be in place and management should perform regular reviews to monitor administrator transactions to ensure administrators are not making updates that should be made by operations personnel, and identify any inappropriate transactions.

AUDITOR'S RECOMMENDATION

A process should be developed to monitor transactions entered under administrator access.

COLORADO SPRINGS UTILITIES RESPONSE

Colorado Springs Utilities agrees with the recommendation. The roles and responsibilities of the Business Application Administrators of Lawson/FHAS require total system access (driven primarily by the need to establish security access for all users). Increased monitoring of administrator actions enhances internal controls. The Lawson/FHAS Payroll System does not offer a monitoring mechanism; therefore, a process must be identified outside the system. We will explore potential solutions to monitor and track administrator actions including but not limited to other information technology solutions that can be applied to Lawson/FHAS. We commit to investigating the availability of monitoring tools that support definition of a process and reporting findings no later than August 1, 2013.



OBSERVATION 2 – EXEMPT STANDBY PAY POLICY ELIGIBILITY CRITERIA WAS NOT WELL DEFINED AND MONITORING BY HUMAN RESOURCES WAS NOT IN PLACE

- Under policy, written standby pay authorizations from senior management were required for exempt employees during our audit period, but in practice, the immediate supervisor had always approved standby pay each pay period in the resource management system. Effective October 15, 2012, the policy was changed to require immediate supervisor approval, consistent with practice.
- Criteria or guidance for determining exempt employees eligible for standby pay was not well defined by policy. Any exempt employee was eligible to earn standby pay, but managers were discouraged from earning exempt standby pay. The Personnel Policies Manual (PPM) did not include requirements to provide justifications to Human Resources for eligible classifications or for Human Resources to monitor standby pay. Employees were limited to an additional 25% of base pay and labor was subject to budgetary controls.

Standby pay was defined as time when the employee remained available to be called back to work on short notice to accommodate needs for emergency service. Exempt employees were not automatically eligible for standby pay. Standby pay rates per policy were as follows:

- Authorized exempt employees assigned standby duty on a day not regularly scheduled to work received up to six hours pay at 100% of their base pay rate.
- Non-exempt employees assigned to a standby schedule were compensated for off-duty hours spent on standby at a rate of 15% of their base hourly pay rate.

During our audit period January 1, 2012, through June 30, 2012, 416 employees had received standby pay for a total amount of \$632,948. Of those employees, 93 (22%) were exempt employees for a total compensation of \$286,697, or 45% of all standby pay.

As stipulated in the PPM, employees were limited to 25% of base annual salary in standby pay in a calendar year. An error report would be generated for review by the Payroll Department as a control if any employee exceeded the 25% limit. We verified the 25% policy limit was not exceeded for any employees during our audit period.

AUDITOR'S RECOMMENDATION

We recommend Colorado Springs Utilities develop and implement a well-defined eligibility policy that includes job classifications or circumstances under which an exempt employee is eligible to receive standby pay. The policy should include the following:

- Frequency of approval required
- An annual justification requirement for the need for standby pay for job classifications, as well as,



Office of the City Auditor Colorado Springs Utilities Payroll Audit

- Monitoring requirements by management and Human Resources to ensure compliance with well-defined policy.

COLORADO SPRINGS UTILITIES RESPONSE

Colorado Springs Utilities agrees with the recommendations. Standby pay eligibility and criteria could be further defined, particularly for exempt employees. We will partner with our leadership to more specifically define eligibility and update our Quality by Design document (# 11089, Standby and Emergency Call-Out) by August 1, 2013. This update will also include specifying the frequency of approval required. We will not define eligibility by classification, but rather by the specific situation. We only identify classification-based criteria for exempt overtime pay. We agree that increased monitoring of the newly defined criteria should occur, following the establishment and publication of the criteria. We will explore system solutions to monitor and track employees receiving standby pay. We commit to monitor this information periodically, with our first review to occur by December 1, 2013.



OBSERVATION 3 - SUPERVISORS WERE NOT APPROVING EMPLOYEE TIME PROMPTLY TO ALLOW TIMELY PROCESSING OF PAYROLL

- We reviewed a sample of 46 employees to ensure time was properly approved and matched the employee's time in the payroll system. We found that two of the 46 employee time entries were not properly approved during the pay period.
- Payroll Department personnel estimated that an additional 34.3 hours per month were required to process late time entries, which averaged 781 entries per month.
- Pay adjustments were processed up to one year after the date the time was submitted.

Supervisors were responsible for understanding and complying with policy in place to ensure accurate and timely approved employee time, including follow-up of late time submittals. Payroll hours must be reported and approved by a specified time after the end of the pay period. All supervisors were to run a report that indicated all unapproved time in the resource management system prior to the deadline.

The Payroll Department ran a report of unapproved time during the pay week and email notices were sent to the employee and their supervisor to request time approval. When a supervisor did not approve reported hours by the cut-off date, the Payroll Department adjusted the time to generate a full paycheck.

After the pay period, the Payroll Department continued contacting supervisors until approvals were entered. Once the time was approved, Payroll personnel reviewed to ensure consistency with what was paid, and made adjustments for discrepancies as needed. This manual process increased administrative burden and risk of errors. Adjustments to time reported were not required to be processed within a given time period, only by year-end.

AUDITOR'S RECOMMENDATION

- Performance criteria should be put in place to ensure Supervisors perform their time reporting responsibilities and are held accountable for noncompliance.
- Policy should be strengthened to require payroll adjustments be submitted within a reasonable time period.

COLORADO SPRINGS UTILITIES RESPONSE

Colorado Springs Utilities agrees with the recommendations. We agree supervisors are responsible for understanding and complying with policy to review and approve non-exempt employee time, exempt employee exception time and any time entry associated with work management tracking. The timely review and approval of these time records is action that directly supports the reduction in required payroll adjustments. We will partner with our leadership to specifically define accountability mechanism(s) which will include utilizing our corrective action process in support of accountability for



Office of the City Auditor Colorado Springs Utilities Payroll Audit

noncompliance. We will also explore additional process improvements that impose reasonable time limits to make payroll adjustments associated only with work management tracking. We commit to implementing an action plan no later than December 31, 2013.



OBSERVATION 4 – CONTRACT EXTENSIONS FOR AGENCY CONTRACT PERSONNEL WERE NOT MONITORED SUFFICIENTLY

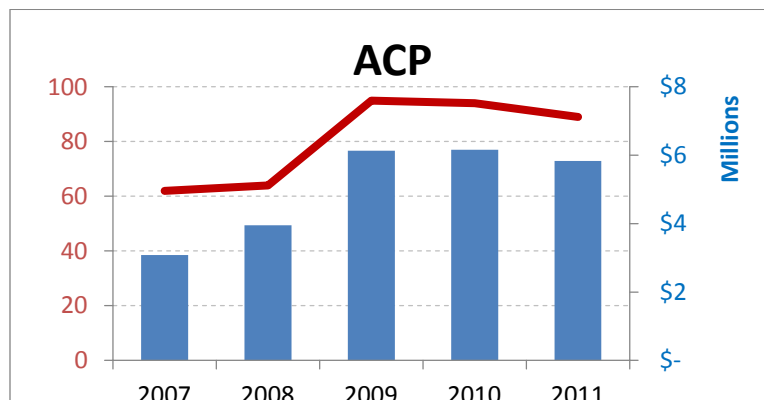
- Policy guidance stated Agency Contract Personnel were to be utilized in a short term/limited or temporary capacity, but this term was not clearly specified. As of June 30, 2012, the full time equivalent (FTE) for 124 ACPs was 79 employees as most ACP were not utilized on a full-time basis. The Monthly Usage Report dated June 30, 2012 indicated some ACP had been working for the contract terms shown below:
 - 71 (57 %) had been ACP for over 12 months in their current assignment
 - 48 (39 %) of those workers had been ACP for over 24 months in their current assignment
- Policy for ACP assignments over 12 months required extension approval by senior management. Policy further indicated if extension approval was not obtained within 30 days, the ACP should be released from assignment. In our testing, two of the five ACP continued employment without extension approvals. We understand that this occurred because notifications were not generated due to information technology issues which have since been corrected.

Supervisors were required to approve ACP timesheets each pay period according to policy.

Examples in the policy included coverage during an outage, technical support in executing major capital projects, to support seasonal increases in work requirements, and provide knowledge transfer in the case of a retiree with required expertise on a short term basis.

We noted that in the last several years, systems and processes have been improved to require justification and senior management approval of use of ACP personnel at least annually, and to increase enforcement of assignment end dates.

Trend data related to ACP is presented below:



Source: Contractor count: provided by Workforce planning, represents number of full-time equivalents (fte)
Dollar amount: general ledger



AUDITOR'S RECOMMENDATION

- Colorado Springs Utilities should ensure policy guidance clearly reflects the organization's objectives related to contract labor utilization and that practices conform to policy guidelines.
- We recommend increased compliance with ACP extension approval requirements.
- Workforce Planning should increase monitoring efforts to ensure compliance with policy requirements that ACP do not work more than 30 days past the assignment end date.

COLORADO SPRINGS UTILITIES RESPONSE

- 1) Colorado Springs Utilities agrees, in part, with the first recommendation. Human Resources (HR) was actively monitoring extension approval requirements from 2010 until January, 2012 when a technology failure prevented us from receiving notifications about assignment end dates. Once HR became aware of the problem, management was contacted and approvals were received or assignments were terminated. As of October 31, 2012, all extension requests for assignments exceeding 12 months had been approved or assignments ended. To strengthen controls in the event of a future system failure, HR agrees further action is warranted. See response #2 that follows.
- 2) Colorado Springs Utilities will increase monitoring efforts by creating a review process outside of the ACP database. A semi-annual internal audit will be established to review upcoming end of assignment dates and extension request compliance. This separate process will provide Human Resources information about when an assignment will exceed the 30 day grace period in order to end the ACP assignment per established guidelines. With support from internal resources, the process is expected to be developed by June 30, 2013.

CITY COUNCIL'S OFFICE OF THE CITY AUDITOR

COLORADO SPRINGS, COLORADO

About our Office

The mission of the Office of the City Auditor is to provide City Council with an independent, objective and comprehensive auditing program for operations of the City. Our auditing program includes:

- Evaluating the adequacy of financial controls, records and operations
- Evaluating the effectiveness and efficiency of organizational operations
- Providing Council, management and employees objective analysis, appraisals, and recommendations for improving systems and activities

The Office of the City Auditor is responsible for auditing the systems used by the City of Colorado Springs and its enterprises, including Colorado Springs Utilities and Colorado Springs Airport. We perform a variety of audits for these entities, including financial audits, performance audits, contract audits, construction audits, and information system audits. We also perform follow-up on a periodic basis to monitor and ensure management actions have been effectively implemented.

Authorization and Organizational Placement

Our audits are conducted under the authority of Chapter 1, Article 2, Part 7 of the Colorado Springs City Code, and more specifically parts 703, 705 and 706 of the Code. The Office of the City Auditor is structured in a manner to provide organizational independence from the entities it audits. This independence is accomplished by the City Auditor being appointed by and reporting directly to the City Council.

Audit Standards

The audit was conducted in a manner that meets or exceeds the International Standards for the Professional Practice of Internal Auditing, a part of the Professional Practices Framework promulgated by the Institute of Internal Auditors, with the exception of the requirements under standards 1312 and 1321 to obtain an external quality assurance review once every five years. We do not believe this non-compliance impacted the quality of our audit.

The audit included interviews with appropriate personnel and such tests of records and other supporting documentation as deemed necessary in the circumstances. We reviewed the internal control structure and compliance tests. Sufficient competent evidential matter was gathered to support our conclusions.