

Citywide Payroll Process

Internal Audit Report

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**Carson City, Nevada**

**Submitted By**

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## Executive Summary

Eide Bailly LLP (“We”, or “Our”) performed an independent citywide assessment of Carson City’s (“City”) payroll process to ensure that payroll is processed accurately, completely, and timely. Additionally, this review evaluated the adequacy of the related internal controls, the functionality of the current payroll system, and related IT controls. During the assessment, we identified three (3) findings and present recommendations to improve existing processes and minimize risks associated with payroll.

## Background Information

The City’s payroll is managed by the Finance Department by both the Payroll Administrator and Payroll Accounting Manager. New hires, terminations, and employee changes such as salaries, benefits, and deductions are entered by the Human Resources (HR) Department into Munis ERP (the financial system of record) and reviewed and posted in the system by the Payroll Administrator. Utilizing system workflow approvals in Munis, employee changes go through appropriate channels of review and approval from appropriate HR and Finance personnel.

The City uses three timekeeping systems including *ExecuTime* for the majority of City employees, *TeleStaff* for Sherriff’s Office and Fire Department, and *WendelWorks* for employees in Parks & Recreation Department. The individual department supervisors review and approve time entries each pay cycle which are validated by the Payroll Administrator. All calculations including any changes to the payroll are reviewed in detail by the Payroll Accounting Manager before finalizing each payroll period. The Payroll Administrator processes payroll for approximately 770+ employees during each payroll cycle; there are 26 pay periods in a calendar year. Please refer to **Appendix A** for the detailed list of internal controls and primary control activities.

## Objective & Scope

The objective of this project was to evaluate: 1) Whether internal controls and policies and procedures governing the City’s payroll processes provide reasonable assurance that payroll is processed accurately, timely and in the proper period; 2) Assess the adequacy and functionality of the current payroll system and related IT controls; 3) Identify opportunities for improving payroll controls, including recommendations for addressing control gaps and ineffective control design or operation; 4) Determine cause or contributing factors, as well as impact, for any identified deficiencies, where applicable; and 5) Determine whether improvements already planned by management are sufficient to address issues.

The scope of this audit was to review and evaluate the citywide payroll process and internal controls for fiscal year 2021 ending on June 30, 2021.

We conducted this audit in accordance with the International Standards for the Professional Practice of Internal Auditing. Those standards require that we plan and perform the audit to obtain sufficient and 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. Our work was limited to those areas specified in the "Audit Objective, Scope, and Methodology" section of this report.

## Methodology

We performed the following procedures to complete this audit. Our procedures were organized in the following five (5) categories and comprised of specific and detailed audit procedures described below.

### 1. General Procedures:

- Gained an understanding of and evaluated the general payroll process through process walkthroughs, documentation review, data and information gathering, including discussions with Payroll Administrator and Payroll Accounting Manager, and Business Systems Analyst as needed.

- Gained an understanding of federal and state payroll-related laws as they apply to minimum wages, overtime laws, and payroll recordkeeping policies to identify key compliance risks or known issues, if any.
- Identified and evaluated if adequate internal controls were in place to ensure proper review and approval of timesheets in timekeeping systems and proper segregation of duties in calculating bi-weekly payroll.
- Identified internal controls and primary control activities performed by management including HR, Finance, and IT.
- Inspected internal documentation for general payroll process including a summary of the payroll process, payroll processing checklist, payroll processing schedule, and examples of payroll reports.
- Designed and built a payroll process flowchart to identify internal controls and control activities and confirmed the accuracy of those controls with the Payroll Administration. Note: a copy of the flowchart was shared with the Payroll Administration. See **Appendix A** for a complete list of internal controls.

## **2. Timesheet Testing:**

- Reviewed a sample of payroll weeks / dates from fiscal year 2021 (FY21) to verify that payroll was processed accurately to account for regular pay, overtime pay, sick leave, taxes, and deductions (pre-tax and post-tax).
- Inspected the roster of employees in the payroll module of Munis to ensure completeness and accuracy of employee records against the records maintained by HR.
- Verified accuracy and completeness of hours worked for a sample of employees that were included in payroll process for the dates selected; 11/13/20, 03/05/21 and 05/28/21. We reviewed 12 employees from each of the 3 pay periods selected for a total of 36.
- Verified labor hours entered in Munis matched timesheets from the various time reporting systems, where applicable.
- Inspected employee timesheets for appropriate supervisor approvals in the applicable time keeping systems.
- Verified the completeness and accuracy of payroll uploads to Munis by reconciling Time Entry summary reports (timesheets) to Hours Proof Report from Munis.

## **3. Federal Income Tax (FIT) Withholding Testing:**

- Evaluated internal processes and procedures for reviewing and updating federal income tax rate tables and updating the procedures for any changes in tax laws.
- Verified accuracy of the federal income tax withholdings for payroll dates selected for. We utilized IRS tax calculators with appropriate data parameters in the validation process.

## **4. Payroll Discharges Testing ('Terminations'):**

- Sample tested 3 out of 12 employees discharged in FY21 and performed a detailed review of supporting documentation to ensure completeness and appropriateness as follows:
  - Verified Personnel Action Forms (PAF) were submitted and approved timely and appropriately. Support included, but was not limited to, HR emails, Munis approval workflows, and Employment Termination Forms.
  - Verified system access for the discharged employees were inactivated in Munis and that the associated user ID was inactivated in the City's Active Directory (Office 365-Outlook) in a timely manner.

- Verified termination paperwork and calculations were prepared, and final checks were issued accurately and timely for each discharge.
- Verified that discharged employees were properly excluded from subsequent payroll.

#### 5. Munis User Roles and Permissions Testing ('System User Role Testing'):

- Evaluated system user access within Munis for both HR and Payroll Administration staff for proper segregation of duties based on user roles and permissions established in the system.
- Reviewed user access for former employees to ensure their access was properly inactivated in Munis.
- Identified and reviewed eleven (11) user roles and permissions within HR and Payroll Departments that were assigned payroll (PR) modules and verified proper segregation of duties within the City's payroll process system as follows:
  - Reviewed the User Role Access Reports and verified user access levels for HR and Payroll employees were assigned permissions that ensured proper segregation of duties based on their respective roles and responsibilities.
  - Reviewed Staff Directory for employee title and department to verify that user roles and PR modules were assigned appropriately based on roles and responsibilities.

## Testing Results

This section of the report provides a high-level description of the testing results and specific observations. The three findings and the associated recommendations are described in detail in the *'Findings and Recommendations'* section of the report and provide the city with opportunities for process improvement.

**Finding #1.** The City lacks a formalized process and mechanism for tracking and reviewing Citywide payroll related changes related to Federal and State regulatory updates.

**Finding #2.** The City lacks a citywide internal control to monitor user roles and permissions.

**Finding #3.** HR and Payroll user roles need to be re-evaluated to ensure proper segregation of duties based on functional responsibilities of each department.

## Conclusion

Carson City's Payroll Administration appears to have internal controls and policies and procedures governing the City's payroll processes to ensure that payroll is processed accurately, timely and in the proper period. No incorrect payments were noted during our procedures. The City could enhance its system to include better documentation of Federal and State regulatory changes and monitoring system user access to ensure proper access and segregation of duties. As such, we provided three recommendations for improving payroll controls that address the findings noted. We believe that evaluating and implementing these recommendations will strengthen the City's overall control environment and mitigate the risks associated with payroll. Risk ratings are all deemed low as there are internal controls in place to mitigate the risks.

## Findings & Recommendations

### Finding #1: Annual Assessment of Regulatory Changes in Payroll

**Risk Rating: Low**

There is a continuous internal communication between Finance and Human Resources Departments regarding implementing regulatory updates and changes related to payroll. However, there is not a formalized tracking mechanism and / or a formalized process for a periodic review and assessment of payroll related statutory changes (e.g., tax rates, minimum wage, overtime pay).

**Recommendation #1:**

We recommend that the Payroll Administration implement a tracking mechanism and an annual internal control with appropriate formal documentation on discussion and assessment of payroll related regulatory changes (e.g., an annual memo prepared by an Accounting Manager and reviewed and approved by CFO and Human Resources Director).

**Management Response:**

*Annually, the Accounting Manager will review and assess Federal and State regulatory changes necessary to the payroll system. A formal internal memo indicating the necessary changes and detailing the updates made to the payroll system will be created. The memo will be reviewed and approved by the Human Resources Director and Chief Financial Officer. The approved memo will be retained for seven years. This process will be implemented in December 2021 and performed each December thereafter.*

### Finding #2: User Access Update in Munis

**Risk Rating: Low**

Our audit identified two former employees who still appeared with system access in Munis. After further review, we confirmed that the risk was mitigated with proper inactivation in the City's Active Directory (Office365-Outlook). Munis user access reports were inconsistent with the City's Active Directory.

**Recommendation #2:**

We recommend that the City's IT Department establish an entity level internal control to ensure all former employees are "Disabled" in Munis as soon as User IDs are disabled in Active Directory to ensure Munis roles are assigned only to existing employees and ensure the accuracy and completeness of Munis User Access Reports for reliability.

**Management Response:**

*IT leadership has provided updated instructions involving the termination process for City employees. The new process will include auditing disabled Active Directory accounts for Munis access and ensuring the appropriate actions are taken to disable the account within Munis. For any approver role within Munis, the workflow queue will be passed to a primary and secondary Munis account within each Department. This process will occur on the same day that the IT Department receives the termination notice.*

### Finding #3: User Access Roles & Permissions in Munis

**Risk Rating: Low**

During the review of Munis user role and permission system reports, we noted that HR employees in user key roles "J\_HR\_APPROVAL\_MGR" and "J\_HR\_STAFF" have full access to payroll related functions in Munis including the role permissions in 'Pay Type Maintenance' and 'Projection run number Maintenance Access' functions. The permissions in these user roles are primarily related to Payroll Administration rather than Human Resources as defined below.

- 'Pay Type Maintenance' function is used by Payroll to create pay codes.
- 'Projection run number Maintenance Access' function is used by Payroll to create payroll budget.

**Recommendation #3:**

We recommend that the City’s IT Department perform further review and modifications, where needed of Munis system functionality pertaining to user role and permissions granted to HR and Finance employees to ensure proper segregation of duties.

**Management Response:**

*The IT Application Team will work with the Finance and Human Resource Departments to test permission updates for existing HR roles in the Munis test environment. The roles will be tested against operational and Department responsibilities. The roles will be updated to comply with the principle of least privilege. The testing will begin immediately and should be completed no later than December 3<sup>rd</sup>, 2021. Once testing and verification is complete, the roles will be updated in the production Munis environment.*

## Appendix A – Internal Controls and Related Control Activities

We identified the following internal controls (IC) and/or management control activities as they relate to the City’s payroll process:

- IC1.** HR Director reviews and approves all employee changes to salary, benefits, deductions, new hires, and terminations.
- IC2.** Finance Department verifies the accuracy of HR personnel changes with secondary review by CFO and the final review by the Payroll Administrator including changes to salary, benefits, deductions, new hires, and terminations.
- IC3.** Department Supervisors review and approve time entries. The City uses three timekeeping systems including *ExecuTime* (City Employees), *TeleStaff* (Sherriff’s Office and Fire Department), and *WendelWorks* (Parks & Recreation Department).
- IC4.** Payroll Administrator prints Time Entry Proof Report from Munis (still in open payroll) and verifies all timesheets are accurate, complete, and approved before importing time entries to Munis. Timesheets without approval are not uploaded into the system until approval is received and documented. If errors are detected, the Payroll Administrator works with supervisors and department business managers to complete the corrections saving the documentation in the “Book” \*. Such corrections are processed in the “open/unposted payroll” before payroll is closed for the period. In addition, all employee’s time for the month is reviewed and verified when preparing the monthly PERS (Retirement Report).
 

\* “The Book” is a physical binder prepared by the Payroll Administrator consisting of different tabs that contain all the reports and calculation spreadsheets used in processing payroll. The Accounting Manager reviews each item in “the Book” and signs off on her review. “The Book” is stored in the Payroll Administrator’s drawer.
- IC5.** IT Controls in timekeeping systems. Timesheets in *Executime* cannot be edited after supervisor approval and after the time entry data has been imported to Munis. Any correction to time entered are re-entered and re-approved in the system. Executive also has a “lock pay period” function that is performed by the Payroll Administrator that prevents any changes. Telestaff system has automated scheduling and communication tools used by Sherriff’s Office and timesheet accuracy relies on Sheriff’s review and sign-off. *WendelWorks* is a clock-in and out system where only a supervisor could make a manual entry if an employee forgot to clock in and out for the day.
- IC6.** Payroll Administrator generates an “Error Report” from Munis that warns the user if an error occurred in the payroll and needed to be fixed. She reviews all employee changes and ensures all calculations are accurate. Munis system would not move on to the next step in the process until all errors are fixed.
- IC7.** Accounting Manager reviews and signs off on all calculations and payroll entries prepared by the Payroll Administrator. The Payroll Administrator generates the Final Proof Report after which changes can no longer be made in the system (Munis).
- IC8.** Direct Deposit and Positive Pay file are reviewed by the Treasurer before uploading to the bank. The Treasurer issues the printer key to the Payroll Administrator to print the signed checks. The checks will only print with signatures (Treasurer and CFO) if the key is inserted in the printer. The Payroll Administrator inputs the number of checks and amount that were printed to the Treasury log and the Treasurer confirms the information to the Final Proof Report.
- IC9.** Payroll Administrator calls bank to confirm direct deposit file upload as part of a two-step process from

the bank to confirm the upload.

- IC10.** Accounting Manager reviews and approves wire transfers prepared by the Payroll Administrator.
- IC11.** Deputy CFO reviews and approves wire transfers prepared by the Payroll Administrator.
- IC12.** Changes to staff listing used in payroll including terminations are processed through a “Personnel Action” that is reviewed and approved by HR Director, CFO, and payroll administrator, as documented in Munis workflow system. After a final check is processed, the payroll administrator posts the termination Personnel Action. This process removes the employee from the timekeeping and payroll systems. HR sends out a list to payroll and IT Department listing of all the terminations each pay period. Payroll Department confirms they have processed the final payments for all terminations listed and posted the Personnel Action. IT Department ensures that they have inactivated the respective employees from all other City system access including Active Directory (Office365-Outlook).
- IC13.** Annually, Payroll Administrator updates the tax rate tables as needed according to the most recent IRS Publication 15-T for the first paycheck in January. The tax table updates, if any, are reviewed and approved by the Payroll Accounting Manager.



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