



MIAMI BEACH

BUDGET AND PERFORMANCE IMPROVEMENT
Internal Audit Division

INTERNAL AUDIT REPORT

TO: Jorge M. Gonzalez, City Manager
VIA: Kathie G. Brooks, Budget and Performance Improvement Director
FROM: James J. Sutter, Internal Auditor

DATE: April 21, 2008

AUDIT: Employees' Usage of Leave Hours to Purchase Pension Time

PERIOD: January 1, 2006 through December 31, 2007

This report is a byproduct of our regularly scheduled payroll processing audit. This area was selected for audit after initial testing revealed several material inaccuracies as to the calculation or omission of charging leave hours adjustments for purchasing pension time and 401 migrations into the City's pension plan. Therefore we tested all transactions occurring between 01/01/06 and 12/31/07 whereby City employees used leave hours to purchase pension time.

INTRODUCTION

The City Commission ratified Ordinance Number 2006-3504 on 03/08/06 to reform the pension system. Among other items, it merged the general and unclassified retirement systems, implemented the 2003-2006 collective bargaining agreement between the City and the Communications Workers of America and amended provisions of the retirement plan applicable to non-bargaining unit and unclassified employees.

In accordance with Florida Statute section 112.65, it also allowed vested employees the opportunity to purchase up to two years of creditable service under the pension plan. Similarly, City employees participating in the 401A plan were able to migrate into the pension plan. Acceptable payment methods for these two benefits included personal check, 401A and/or 457 plan rollovers, accrued sick and annual leave, etc.

Accrued sick leave may be used at a rate of two hours of accrued sick leave for the value of each hour used toward the purchase, provided that the participating employee retains at least 120 hours of accrued sick leave after the purchase. Meanwhile, annual leave may be used at the rate of one hour of accrued annual leave for the value of each hour used toward purchase.

Ordinance Number 2006-3530 was subsequently adopted on 09/21/06 to amend Ordinance Number 2006-3504 as to the definition of earnings, death benefits after retirement, the early retirement incentive program, etc. It also included an amendment of section 4.05 which discussed the purchase of credited service by certain employees who previously had creditable service under the Classified Plan. This purchase of probationary time or the first six months of classified employees' tenure is necessary as these individuals pay into Social Security and are not part of the City's Pension System during this period (not including Fraternal Order of Police and International Association of Fire Fighters unions covered employees, who contribute to Deferred Compensation in lieu of Social Security). At the end of their probationary period, the applicable classified employee may or may not be retained. Retained employees must participate in one of the City's retirement programs and no longer remit Social Security.

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When able, these now permanent employees may elect to use personal check, sick and annual leave, etc. to purchase their probationary period and have those months count as creditable service toward their pension. However, sick and annual leave may both be used at the rate of one hour of accrued time for the value of each hour used toward purchase thereby differing from the aforementioned two year and 401 migration pension buy back plans.

OVERALL OPINION

The Pension Office, Finance's Accounts Payable Section and the Human Resources' Compensation Division worked diligently and expeditiously to implement the desired pension reforms and to answer employee questions. Somewhere in their haste, deficiencies occurred in interdepartmental communication and implementation resulting in incorrect or omitted leave time deductions. The following shortcomings were noted during testing:

- Although tested employees were properly granted additional pension time after City checks were issued to the Pension Office, employee leave balances were not reduced accordingly by a total of \$225,716.95. The Compensation Division has since prepared leave adjustments for all identified active employees recovering \$202,057.71 for the City. The \$23,659.24 balance has not been collected as the affected employees no longer work for the City.
- Breakdowns in the overall process by which pension time is purchased with leave hours helped allow inaccurate or omitted leave transfers to go undetected.
- Payroll codes were not consistently and exclusively used for leave transactions to reduce the possibility of future confusion/disagreements and making mistakes, as well as hindering the audit trail.

PURPOSE

To determine the efficiency and effectiveness of the overall leave transfer process, were leave hours properly deducted from employees' balances in accordance with the amount of pension time granted, were City issued checks correctly prepared for all tested employees, and were transactions accurately recorded in the City's Financial System.

SCOPE

1. Confirm that tested employees' leave hours were deducted in accordance with the amount of pension time granted by the Pension Office.
2. Confirm that the designated process works properly and has the necessary safeguards and controls to help ensure that tested transactions are accurately completed.
3. Confirm that tested transactions were properly recorded in the City's Financial System.
4. Confirm that tested files and records are adequately secured, neatly organized and properly maintained.
5. Confirm that the Finance Department issued checks to the Pension Office in the correct amount for all tested employees.

FINDINGS, RECOMMENDATIONS AND MANAGEMENT RESPONSES

1. Finding: Incorrect or Omitted Leave Hour Deductions

Among other payment methods, City employees were given the opportunity to use accrued leave time (sick and vacation hours) to purchase pension time for the 401 migration, probationary time and up to two years for similar work experience. This area was selected for testing because of the large volume of recent transactions and the relatively high dollar amounts, as well as reported problems associated with the deducting of an employee's leave hours totaling \$14,391.10 more than one year after submittal only because of his insistence.

The discovery of other incorrect material leave adjustments resulted in the sample size being increased to include all applicable transactions occurring between 01/01/06 and 12/31/07. Any believed inaccurate or omitted transactions were collected and forwarded to the Human Resources Department's Compensation Division and/or Pension Office. Sufficient time was granted to review their records and disprove any identified transactions. Several meetings were held to discuss their findings and to determine where the breakdowns were occurring.

As a result, all parties agree that the leave hours listed below and in Exhibit A totaling \$225,716.95 were not properly deducted prior to Internal Audit's testing and subsequent notification. Corresponding payroll leave adjustments were prepared shortly thereafter to reimburse the City for amounts already paid to the Pension Office. A total of \$202,057.71 was recovered but the \$23,659.24 balance is still outstanding because the individuals have since left the City's employment.

Meanwhile, the table below shows the exceptions found for incorrect or omitted leave deductions by category, both in dollars and number of employees, in relation to the total population size tested:

Category	Dollar Amounts			Number of Employees		
	Exceptions Found	Total Population	%	Exceptions Found	Total Population	%
401 Migration	\$38,132.58	\$221,416.05	17.22%	8	36	22.22%
Two Year Buy Back	\$171,853.09	\$1,405,641.70	12.23%	23	160	14.38%
Probationary Time	\$15,731.28	\$263,469.07	5.97%	4	86	4.65%
Total	\$225,716.95	\$1,890,526.82	11.94%	35	282	12.41%

The root cause of the incorrect leave adjustments was found to be in the following order from most to least common:

- a. the departmental payroll coordinators unaware that the Compensation Division had entered leave adjustments, intentionally zeroed them out in Quick Entry believing most likely that they had inadvertently made an incorrect entry (15/35 = 42.86%),
- b. employees' leave transfer contracts were apparently not received by the Compensation Division which except for in two instances could not be disproved by Internal Audit (13/35 = 37.14%),

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- c. the Compensation Division incorrectly entered the payroll leave adjustment by adding leave hours rather than subtracting them, not halving sick hours, etc. ($6/35 = 17.14\%$),
- d. the Pension Office provided incorrect calculations on the Request for Direct Payment and/or Leave Request Transfer forms ($1/35 = 2.86\%$).

Finally, review of employee identification number 12180's two year buy back found that he was incorrectly credited with two years of pension time when he only purchased 1.76 years. The Pension Office quickly corrected the error and said that it most likely would have been caught during final retirement calculations as all figures are thoroughly reviewed at that time.

Recommendations:

The implementation of the following recommendations should help prevent the identified root causes from reoccurring:

- a. The Compensation Division should enter the leave adjustment with a prior date not occurring in the pay period to prevent departmental payroll coordinators from making future unauthorized changes. This practice has already been adopted by the Compensation Division.
- b. The overall leave transfer process should be amended as discussed further in finding 2.
- c. Human Resources Department management should routinely review leave adjustments completed to help ensure their accuracy. The Compensation Division has now implemented this practice to help ensure that only correct payroll adjustments are processed.
- d. Pension Office management should review and approve all calculations prior to the employee leaving the City's employment to help correct any identified errors prior to receiving their leave settlement.
- e. Collection efforts for the remaining balances due from the separated employees should attempted.

Management Responses:

The Finance Department will pursue the collection of these outstanding monies.

The Human Resources Department has already implemented the applicable recommendations as noted above, and coupled with the newly defined payment process listed in finding #2, should help reduce the possibility of future errors.

The Pension Office agrees with the finding and recommendation listed above.

2. Finding: Process Deficiencies

Initially, the Pension Office would prepare the employees signed transfer contract and the Request for Direct Payment (D.P.). The transfer contract would be sent by interoffice mail to the Compensation Division while the D.P. was sent simultaneously to the Finance Department's Accounts Payable Section. Known problems occurred as Accounts Payable Section received this mail and accurately prepared City checks but the Compensation Division claimed that they did not always receive this documentation. Internal Audit's efforts to substantiate this claim were unsuccessful except for two City employees (identification numbers 15906 and 17597).

Consequently, internal reviews were conducted to determine which employees did not have

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their leave balances properly reduced. Corresponding payroll adjustments were made and the process was changed. Late summer 2007, the Pension Office began scanning and e-mailing the transfer contract to six designated Human Resources Department employees to help ensure receipt and proper processing. Furthermore, the Accounts Payable Section supervisor brings a copy to a Human Resources Department employee, independent of the Compensation Division, before processing. These procedures are inefficient as there is a duplication of work and still three leave adjustments tested during this time period were not properly prepared.

Finally, the Finance Department did not ensure that the employee's leave balance was properly reduced before issuing the City check. They also commingled all employees participating in the tested pension buy back plans into one vendor account numbered 000410 thereby making it difficult to distinguish between the three.

Recommendations:

The process by which pension time is purchased with leave hours has evolved over the two year sampled period. Although it has improved as 24/35 or 68.57% of the identified inaccurate transactions occurred during the 2006 calendar year, there is still room for improvement. Therefore, the following processes are recommended to help ensure that future transactions are properly completed:

- The Pension Office completes the transfer hours' contract in accordance with the employee's request and prepares an invoice to the City for the amount due.
- The contract with invoice should be forward to the Compensation Division's Human Resources Administrator I for assignment to one of her staff.
- The corresponding leave adjustment should be timely completed by the assigned employee. A print screen of the leave adjustment should be generated and attached to the documentation.
- The Compensation Division's Human Resources Administrator I should review the documentation to ensure that the transfer was done and sign off on the invoice.
- The Compensation Division's Human Resources Administrator I should forward the documentation and invoice to either the Human Resources Director or Assistant Director for approval.
- The invoice with the supporting documentation attached should be forwarded to the Finance Department's Accounts Payable Section for processing.
- Documentation should be reviewed by Finance for approvals to ensure that the transfer has been made. A check payable to the City of Miami Beach General Employees Retirement System should be prepared in the next batch of processed checks.
- The issued check should then be delivered to the Pension Office so that the matching pension time can be added to the employee's record.

Management Responses:

The Human Resources and Finance Departments are agreeable to this amended process formulated at our exit conference. In addition the Finance Department believes that the new work flow will eliminate the disconnect that existed between the issuing of the check and the deduction of the hours.

The Pension Office will adhere to this newly created process.

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3. Finding: Payroll Codes or Ben/deds
Ben/deds (benefit deductions) are line items that appear on employees' paychecks that show either the inflow or outflow of monies. Testing showed that the leave hours deducted by the Compensation Division for the three pension buy back plans were charged to either s2bb (sick time / 2 year buyback) or sicb (adjustment to sick leave bank) for sick hours and v2bb (vacation time / 2 year buyback) or vacb (adjustment to vacation leave bank) for vacation hours. However, consistency was found to be lacking. For example, instances were noted whereby sick hours used in the 401 migration were charged to s2bb, other times to sicb and still others where they were initially charged to sicb and then later converted to s2bb through payroll adjustments. Additional payroll adjustments were also found to have used these aforementioned ben/deds for such unrelated reasons as United Way contributions, donated time, planning day payouts, etc.

Recommendations:

Separate ben/deds should have been created and used exclusively for each of the three pension buy backs tested to help avoid possible confusion/disagreements, reduce the likelihood of making mistakes and improve the audit trail.

Management Responses:

Ben/ded codes s2bb and v2bb are now being used exclusively for the 2 year buy back, as they affect the employee's leave payout at time of separation. Sicb and vacb are being used for any other type of adjustment to the respective leave banks, as they do not affect the employee's leave payout at the time of separation.

Human Resources' management is reviewing the use of these ben/ded codes every pay period.

EXIT CONFERENCE

An exit conference was held on March 20, 2008 in the Office of Budget and Performance Improvement. Participants included Ramiro Inguanzo (Human Resources Director), Kristin Tigner (Assistant Director of Human Resources), Georgie Eckert (Assistant Finance Director) and James Sutter (Internal Auditor). All parties were in agreement as to the contents of this report. Management responses were solicited and included in our report.

JJS:MC:mc

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(audit performed by Mark Coolidge, Senior Auditor)

cc: Ramiro Inguanzo, Human Resources Director
Patricia Walker, Chief Financial Officer
Rick Rivera, Pension Administrator

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EXHIBIT A - LISTING OF INCORRECT OR OMITTED PENSION LEAVE DEDUCTIONS BY ROOT CAUSE

ID NUMBER	REASON FOR LEAVE HOURS TRANSFERRED	DIRECT PAYMENT DATE	CMB DOLLARS OWED	CORRECTED AMOUNT	CORRECTED PAY PERIOD DATE
<u>PAYROLL COORDINATORS' ADJUSTMENTS:</u>					
14134	401 MIGRATION	09/19/06	\$23,112.53	\$23,112.53	02/03/08
15168	401 MIGRATION	12/18/06	\$2,713.06	\$2,713.06	02/03/08
17008	PROBATIONARY	11/15/06	\$2,789.22	\$2,789.22	02/17/08
10731	PROBATIONARY	01/11/07	\$869.15	\$0.00	N/A *
14243	PROBATIONARY	07/11/07	\$7,924.09	\$7,924.09	02/17/08
16509	TWO YEAR	09/06/06	\$4,185.91	\$4,185.91	02/03/08
16694	TWO YEAR	03/13/07	\$2,656.23	\$2,656.23	03/02/08
17306	TWO YEAR	03/13/07	\$2,116.01	\$0.00	N/A *
15846	TWO YEAR	12/11/06	\$6,761.92	\$6,761.92	02/03/08
16429	TWO YEAR	01/22/07	\$5,645.48	\$5,645.48	02/17/08
12492	TWO YEAR	04/18/07	\$10,524.34	\$10,524.34	02/03/08
14160	TWO YEAR	08/28/06	\$18,616.52	\$18,616.52	02/03/08
13145	TWO YEAR	05/15/06	\$7,935.08	\$7,935.08	02/03/08
SUBTOTAL			\$95,849.54	\$92,864.38	
<u>LEAVE TRANSFER CONTRACTS NOT RECEIVED:</u>					
15195	401 MIGRATION	11/02/06	\$4,931.04	\$4,931.04	03/02/08
15854	401 MIGRATION	11/02/06	\$2,030.02	\$2,030.02	02/17/08
17713	401 MIGRATION	06/26/06	\$685.32	\$685.32	02/17/08
17597	401 MIGRATION	06/21/06	\$1,990.17	\$1,990.17	02/03/08
15572	401 MIGRATION	11/02/06	\$1,640.99	\$1,640.99	02/03/08
15107	TWO YEAR	04/27/07	\$9,728.13	\$9,728.13	02/03/08
13915	TWO YEAR	10/11/07	\$5,742.52	\$5,742.52	02/17/08
15906	TWO YEAR	03/15/07	\$9,038.81	\$9,038.81	02/03/08
16306	TWO YEAR	10/27/06	\$6,767.66	\$6,767.66	02/03/08
10909	TWO YEAR	12/10/07	\$8,796.26	\$8,796.26	02/03/08
15051	TWO YEAR	07/27/06	\$1,740.47	\$1,740.47	02/03/08
13947	TWO YEAR	05/19/06	\$18,061.52	\$0.00	N/A *
16780	TWO YEAR	10/11/07	\$5,647.25	\$5,647.25	02/17/08
14287	TWO YEAR	08/03/06	\$3,979.27	\$3,979.27	02/03/08
16994	TWO YEAR	05/19/06	\$18,057.21	\$18,057.21	02/03/08
SUBTOTAL			\$98,836.64	\$80,775.12	
<u>INCORRECT LEAVE ADJUSTMENTS:</u>					
18090	401 MIGRATION	10/25/06	\$1,029.45	\$0.00	N/A *
15297	PROBATIONARY	07/11/06	\$4,148.82	\$4,148.82	02/17/08
15297	TWO YEAR	08/24/06	\$5,430.28	\$5,430.28	02/17/08
16462	TWO YEAR	12/11/06	\$10,505.04	\$10,505.04	02/03/08
15818	TWO YEAR	10/02/06	\$3,197.27	\$3,197.27	02/03/08
15841	TWO YEAR	11/20/06	\$5,136.80	\$5,136.80	03/02/08
SUBTOTAL			\$29,447.66	\$28,418.21	
<u>PENSION OFFICE MISCALCULATIONS:</u>					
11551	TWO YEAR	05/02/06	\$1,583.11	\$0.00	N/A *
SUBTOTAL			\$1,583.11	\$0.00	
GRAND TOTAL			\$225,716.95	\$202,057.71	

* These monies appear to be uncollectible since the employees left the City's employment prior to identifying the exception's existence.