



Negotiated Employee Salary Increases

Audit Report

August 30, 2016



INTERNAL AUDIT DIVISION
SANTA BARBARA COUNTY AUDITOR-CONTROLLER

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ATTACHMENTS:

- Attachment A – Auditor-Controller Payroll Response to Audit Report
- Attachment B – Human Resources Response to Audit Report

Overview

Negotiated Employee Salary Increases

Introduction

The Internal Audit Division of the County of Santa Barbara (County) Auditor-Controller's Office performed an audit of employee salary increases negotiated into the County's memorandum of understanding (MOU) with the Services Employees International Union, Local 620 (Local 620). Our work was limited to the area specified in the Objective, Background, and Scope below. We believe the evidence we obtained provides a reasonable basis for the findings in this report.

Objective, Background, and Scope

The objective of our audit was to identify changes to the County's MOU with Local 620 that could be difficult for the County to implement correctly. Our audit was performed to determine whether these changes were made properly.

Local 620 is the County's largest recognized employee organization, representing approximately 48% of the County's workforce. In September 2011, the Board of Supervisors approved an MOU with Local 620 that placed a freeze on all merit increases for the term of the agreement. Although that MOU expired in June 2013, a successor MOU did not take effect until February 2014. This new MOU included the following provision:

"Effective with anniversary months beginning in October 2013, employees in job classifications represented by the union are eligible for merit increases."

Human Resources (HR) identified 206 employees from 18 County departments potentially affected by this MOU change and provided a list of these employees to Auditor-Controller Payroll (A/C Payroll). As this MOU provision became effective retroactively, Internal Audit identified this as an MOU change that could be difficult for the County to implement correctly. As such, the scope of our audit included all employees represented by Local 620 that should have received salary increases retroactively under the MOU. Our testing covered the period of February 17, 2014 through June 22, 2014.

Conclusion

Enacting pay-related MOU provisions retroactively for employees from multiple departments is a complicated and time consuming process that is susceptible to errors, omissions, and inconsistent execution. We also identified opportunities to increase operational efficiencies. We recommend that HR and A/C Payroll implement the recommendations in the report.

Findings and Recommendations

Negotiated Employee Salary Increases

Finding 1 – MOU with Retroactive Pay Provision

The Employee Relations Division of HR negotiates the County's MOUs with its recognized employee organizations. Negotiations with Local 620 for the successor MOU began in March 2013 but were not completed when the existing MOU expired in June 2013. Negotiations were eventually completed and the new MOU became effective in February 2014.

The new MOU included a provision allowing for merit increases effective retroactively back to October 2013 that potentially affected over 200 employees from 18 County departments. As demonstrated in this report, implementing retroactive pay provisions for hundreds of employees across multiple County departments is a complicated and time consuming process that is susceptible to errors, omissions, and inconsistent execution.

Recommendation 1: HR should avoid MOU provisions that grant retroactive pay.

Finding 2 – Decision to Revise Anniversary Months not Formally Documented

Local 620 and HR identified 26 Step A employees that were hired during the merit freeze and decided their anniversary months should be revised by six months to provide a merit increase sooner under the new MOU. Although the communicated intent was to follow Civil Service Rule 409 and allow these employees to receive a merit increase within six months instead of 12 months, this agreement was not formalized.

Recommendation 2: Agreements between the County and recognized employee organizations involving employee compensation should be formalized.

Finding 3 – Procedure for Determining All Employees Affected by MOU Changes

We received a list from A/C Payroll of employees identified by HR as potentially affected by the retroactive merit increases. We determined that the list did not include everyone affected and was not generated using current payroll information. No formal procedure is in place for accurately identifying all employees affected by MOU changes.

Recommendation 3: HR and A/C Payroll should develop a formal procedure for accurately identifying all employees affected by MOU changes and determining changes have been properly executed for all employees identified.

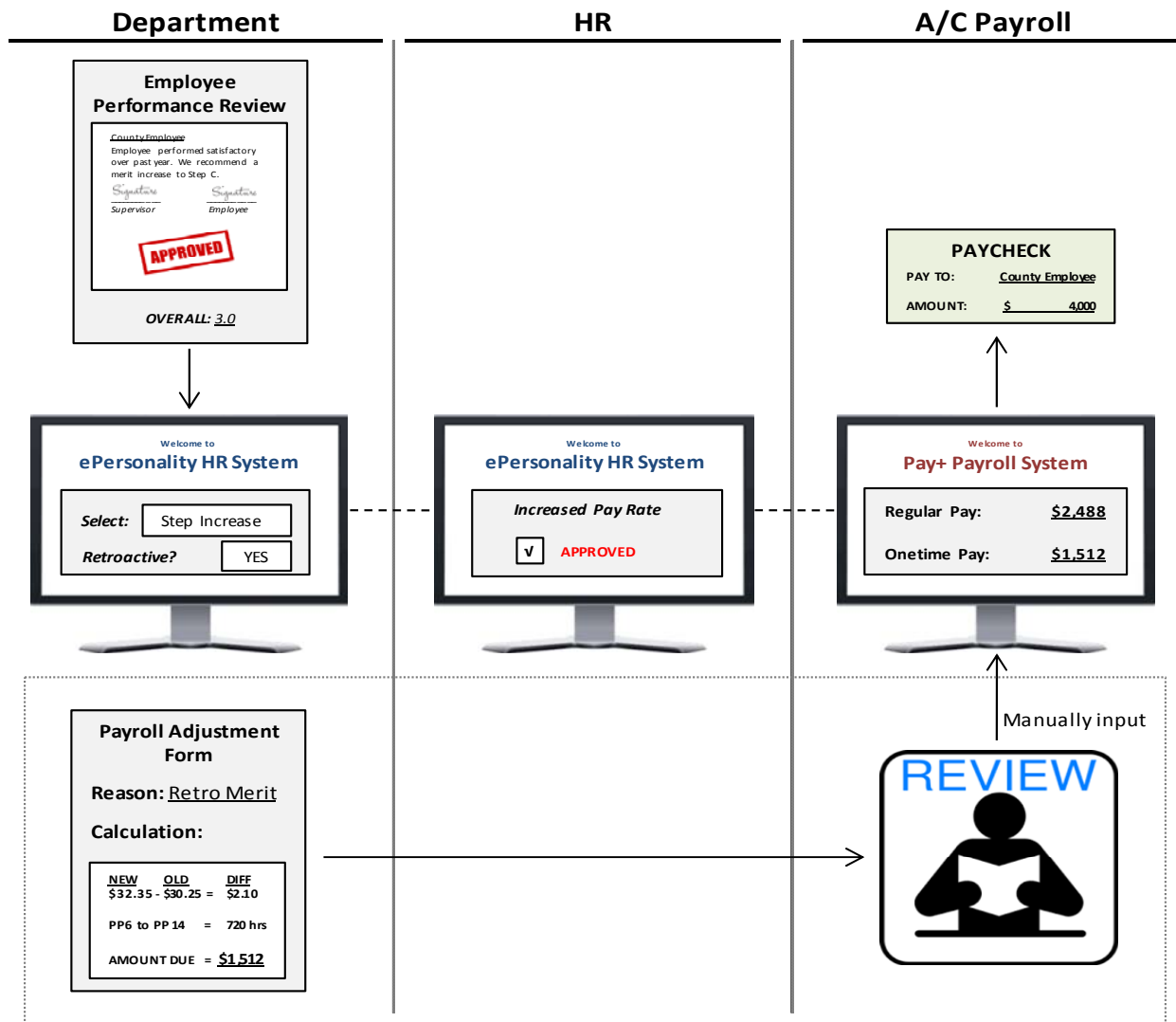
Findings and Recommendations

Negotiated Employee Salary Increases

Finding 4 – Errors Executing Retroactive Merit Increases

Executing a merit increase retroactively involves two separate processes:

1. Department enters a merit increase into HR system retroactively based on an Employee Performance Review (“EPR”) then submits transaction and EPR to HR for approval.
2. Department calculates the pay owed to the employee using a Payroll Adjustment Form and sends to A/C Payroll for review, input, and payment to the employee.



Both of these processes must be completed for an employee to receive a onetime payment.

Findings and Recommendations

Negotiated Employee Salary Increases

While departments occasionally may need to process payroll adjustments, it is not a routine process that department payroll clerks perform regularly. Calculating payroll adjustments for merit increases granted retroactively can also be complicated by cost-of-living adjustments, overtime, unpaid leave, and allowances. Further, A/C Payroll is not staffed to process a high volume of these adjustments. As a result, there is a high risk that errors could be made that go undetected and uncorrected.

A/C Payroll did not develop guidance for departments to follow in order to properly perform the payroll adjustments for retroactive merit increases. There also was no timeline or strategy established for receiving and processing the adjustments for each department. As a result, the payroll adjustments were prepared inconsistently and submitted sporadically by departments.

We examined the list of employees potentially eligible for a retroactive merit increase and determined it had various inaccuracies. We created a revised list using current payroll information and additional information from HR that had 156 employees. We selected 22 employees that had received a payroll adjustment and 11 employees that had not received a payroll adjustment for further examination.

Out of the 22 employees selected for examination that received a payroll adjustment during the period of February 17, 2014 through June 22, 2014, we identified the following errors:

| Description of Error | Employees | Department | Amount |
|---------------------------------------|------------------|------------------------|-------------------|
| No retroactive increase granted | 1 | District Attorney | \$ (840) |
| Calculation did not include allowance | 3 | Auditor-Controller | \$ (125) |
| Calculation used incorrect pay rate | 1 | Planning & Development | \$ (160) |
| | 1 | Public Works | \$ (39) |
| | * | Auditor-Controller | \$ (16) |
| | 1 | Public Health | \$ 188 |
| Employees with Errors | <u>7</u> | Underpayments | <u>\$ (1,180)</u> |
| Percentage Tested with Errors | 32% | Overpayments | <u>\$ 188</u> |

** Employee is already counted as one of the three Auditor-Controller employees above.*

Out of the 11 employees selected for examination that had not received a payroll adjustment during the period of February 17, 2014 through June 22, 2014, we identified 4 employees (36%) that should have received a payroll adjustment for a retroactive merit increase but had not.

Findings and Recommendations

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In addition, we examined the 26 Step A employees that HR determined should have their anniversary months revised by six months in order to provide a merit increase sooner under the new MOU, noting the following errors:

- 7 employees (27%) did not have their anniversary month revised. Instead, the employees received a merit increase on or after their original anniversary month.
- 2 employees (8%) had their anniversary months revised and a step increase was granted retroactively in the HR system, however no payroll adjustment for the retroactive increase was processed and paid to the employees.
- 3 employees (12%) received a promotion but remained at Step A. These employees received a step increase six months after their promotion date.
- 7 employees (27%) separated from employment. No revisions to their anniversary months were made and no merit increases were granted prior to their separation.

Recommendation 4: A/C Payroll should develop and distribute guidance to departments when an MOU change that requires payroll adjustments occurs. A/C Payroll should also establish a timeline for receiving payroll adjustments from departments to ensure sufficient resources are available to review and process the adjustments. An assessment should also be performed to determine if all employees that should have received a retroactive merit increase actually received one. All errors and omissions identified should be corrected.

Findings and Recommendations

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Finding 5 – Areas for Improvement in Payroll Adjustment Process

A/C Payroll is responsible for reviewing Payroll Adjustment Forms completed by departments and processing the resulting payments to employees. We identified the following areas for improvement in A/C Payroll’s process for reviewing and processing these onetime payments:

| Areas for Improvement | Instances | Recommendations |
|---|------------------|---|
| A/C Payroll changed department's Payroll Adjustment Form to correct errors. In 3 instances A/C Payroll used incorrect rates. | 12 | Errors identified by A/C Payroll on Payroll Adjustment Forms should be sent back to the department to correct and resubmit. |
| A/C Payroll generated timecard reports to verify hours on department's Payroll Adjustment Form and corrected hours if needed. | 21 | Departments should review hours worked during the adjustment period and provide the timecard report to A/C Payroll. |
| A/C Payroll made a keying error when entering the payroll adjustment in the payroll system. | 2 | Payroll adjustments should be reviewed by a second employee prior to processing to ensure transaction is entered correctly. |
| Completing the payroll adjustment form is a manual process that is subject to input and calculation errors. | All | Explore the cost-benefit of creating a payroll adjustment application to automate the process using data from the payroll system. |

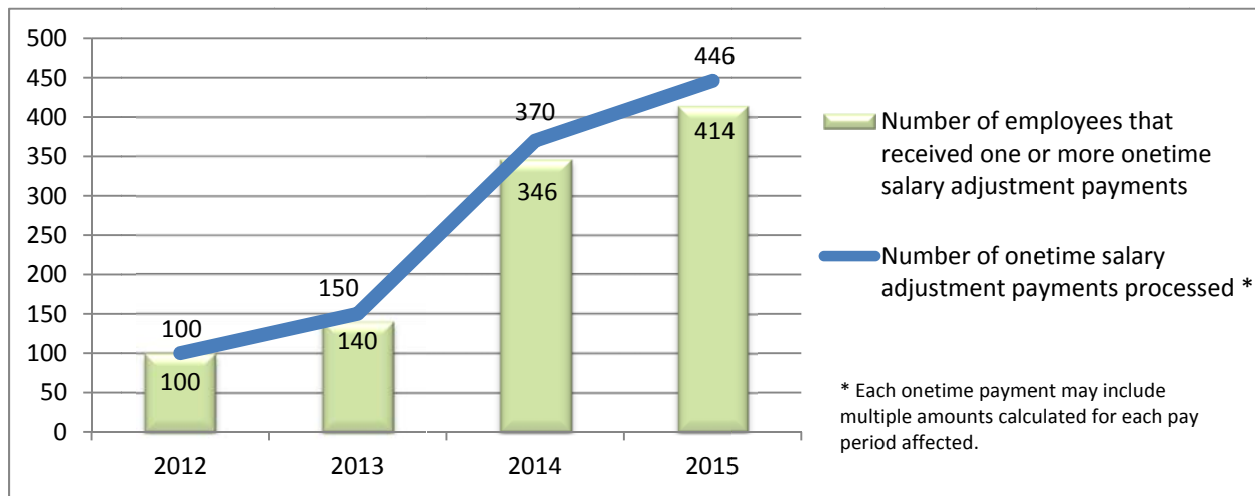
Recommendation 5: A/C Payroll should consider the recommendations above.

Findings and Recommendations

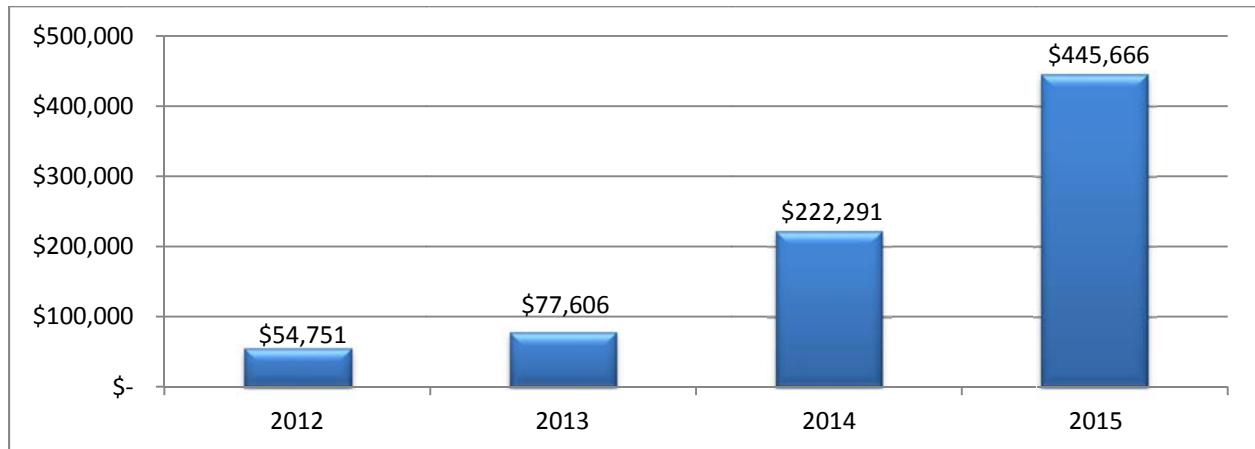
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Finding 6 – Overtime Salary Adjustment Payments to Employees

Overtime salary adjustment payments to employees are made when merit increases are granted retroactively or processed late, employees complete their timesheets late or incorrectly and are owed additional pay, or for other special circumstances. These payments must be calculated and recorded for each pay period affected in order to correctly calculate pensionable salary amounts. The number of employees that received one or more salary adjustment payments and the total number of these payments processed in 2012 through 2015 is as follows:



The dollar amount of these payments made during these years is as follows:



As shown by the charts above, the number and dollar amount of overtime salary adjustment payments to employees increased significantly after the Local 620 MOU became effective in February 2014. These payments continued to increase in 2015 as employees and managers from other bargaining groups became eligible for post-recession salary increases.

Findings and Recommendations

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While it may not be practical to eliminate all situations that require onetime salary adjustment payments, there may be opportunities to improve County processes to reduce the need for these payments. For example, we identified various instances during our audit where a onetime salary adjustment payment was made because a department granted a merit increase but processed the employee's EPR late. Department payroll clerks are responsible for determining, tracking, and notifying supervisors of EPR deadlines. The processes, tools, and expertise for carrying out these responsibilities vary by department and, as a result, produce varying outputs. A uniform EPR tracking system for use by all departments that utilizes automated capabilities could help reduce the number of late EPRs processed in the County.

Recommendation 6: HR should evaluate the cost-benefit of implementing an automated EPR tracking system to accurately and efficiently determine and notify supervisors of EPR deadlines to reduce the frequency of late EPRs. A/C Payroll should review the reasons for onetime salary adjustment payments and determine if there are other opportunities to improve County systems and processes in order to reduce the need for these payments.

Acknowledgement

Negotiated Employee Salary Increases

The responses from A/C Payroll and HR to the findings, conclusions, and recommendations included in this report, as well as any planned corrective actions, are presented as attachments to this report. We have not evaluated the validity of these comments.

If there are any questions, please contact us at (805) 568-2100.

Respectfully Submitted,

A handwritten signature in blue ink that reads "Heather Fletcher". The signature is written in a cursive, flowing style.

Heather Fletcher, CPA
Audit Manager

NEGOTIATED EMPLOYEE SALARY INCREASES AUDIT 2016

RESPONSE: AUDITOR-PAYROLL DIVISION

FINDING 4

Auditor-Payroll recognizes the complexity and infrequency of departments having to calculate payroll adjustments. Improved forms were designed and implemented (including live department clerk training) in August 2015 to assist department personnel with accuracy, completeness and authorization of the adjustment.

Auditor-Payroll recognizes the need for direct instruction to departments in major adjustment events, and has improved and increased training capabilities and departmental communication.

Auditor-Payroll has worked with Employee Relations to obtain specific identification of employees impacted by negotiated changes, in order to assess accuracy in implementation of pay changes.

Auditor-Payroll will establish a project with Application Development staff to identify and correct retroactive increase errors and omissions.

FINDING 5

Auditor-Payroll conducted live training and made available example templates, including specified instructions and backup requirements.

Payroll Adjustment Forms with errors are now returned to departments for correction, no corrections made by AC/Payroll staff.

Supervisorial review of data entry now occurs on every payroll adjustment entered.

Auditor-Payroll is included in notification of board letters at the time of docketing for negotiations involving pay changes.

AC is working to develop automation of payroll adjustments through the timekeeping system to reduce human errors.

FINDING 6

Auditor Payroll is reviewing reasons for past onetime payroll adjustments to address where improvements to processes can be made to reduce the number of such adjustments.

Human Resources Response to Audit Report on Negotiated Employee Salary Increases

Recommendation 1: HR should avoid MOU provisions that grant retroactive pay.

Response: Partially agree. HR agrees that where possible it is preferable to avoid retroactive pay adjustments. However, in the arena of collective bargaining retroactive changes are sometimes necessary and appropriate in the interests of coming to agreement. Further, any retroactive provisions of a labor agreement would have the prior approval of the Board of Supervisors before being proposed at the bargaining table. HR looks forward to working in partnership with the Auditor Controller's Office to ensure successful implementation of MOU provisions that affect employee compensation and benefits.

Recommendation 2: Agreements between the County and recognized employee organizations involving employee compensation should be formalized.

Response: Partially agree. HR agrees that to the extent possible the intent of both parties in regards to changes in employee compensation and benefits should be included in the formal MOU document. However, in actual practice there are often unforeseen conditions or events that were not specifically addressed at the bargaining table. In those cases, it is up to the parties to identify the original intent of the agreement and to apply that as closely as possible to the unforeseen condition. It is not practical or necessary to make on-going revisions to the adopted MOU for every possible contingency. Again, HR anticipates working in partnership with Auditor Controller Payroll to address unique pay and/or benefit situations as they arise.

Recommendation 3: HR and A/C Payroll should develop a formal procedure for accurately identifying employees affected by MOU changes and determining changes have been properly executed for all employees identified.

Response: Agree. HR agrees that it is prudent to have a set procedure that will allow Human Resources and Auditor Controller Payroll to work in partnership to accurately identify employees affected by retroactive pay adjustments and developing procedures for validating that the changes have been made correctly. HR would like to note that in the particular event covered by this audit that great effort was taken to accurately identify affected employees. As part of the Audit, the Auditor-Controller's Office found 60 instances of employees who were not included on the original list that Human Resources provided to the Auditor's Office. Human Resources reviewed these 60 employees and came up with the following results. Twenty of the people on the Auditor's list were for some reason not included on the list from Human Resources, but HR verified that all twenty received the appropriate retroactive pay increase. Nine of the employees were either at E-step or Y-rated during the Merit Freeze and were therefore ineligible for Merit Increases. Finally, thirty one of the employees had an event prior to the end of the Merit Freeze that pushed their Anniversary Month outside of the retroactive period and therefore no retroactive pay increase was necessary for those employees. HR feels confident that we worked collaboratively with departments and SEIU Local 620 to ensure that we did not miss any affected employees.

Recommendation 6: HR should evaluate the cost-benefit of implementing an automated EPR tracking system to accurately and efficiently determine and notify supervisors of EPR deadlines to reduce the frequency of late EPRs.

Response: Partially agree. While HR does not believe that this would completely resolve the issue, we agree that it would be a helpful tool. In addition, HR feels that the development of an EPR system would be a Countywide effort that would require the participation of a variety of partners to be successful.