PAYROLL & INTERNAL CONTROLS

HIGHLIGHTS

- ► Internal Controls over payroll
- ▶ Procedures
- ▶ Documentation
- ► Responsibilities
- ► Reporting
- ► Payroll issues and concerns

INTERNAL CONTROLS

- Objectives
- ► Control Environment
- Risk Assessment
- Control Activities
 - ► Examples of internal control procedures in Part 2, Section 2 of the Uniform Internal Control Standards Manual on our website www.in.gov/sboa
- ▶ Information and Communication
- ▶ Monitoring

OBJECTIVES

- Operations Effectiveness and efficiency of operations.
 - Processing of payroll from start to finish
 - ► Accuracy of hours, pay rates, check/deposit amounts, timeliness of payment, authorizations, financial reporting (correct funds/accts)
- Reporting Reliability of reporting for internal and external use.
 - ▶ Internal Accounting records, financial reports, payroll reports, grants
 - ► External Monthly, quarterly, yearly reports to IRS, DOR, DWD, etc Form 100R to State Board of Accounts
- Compliance Compliance with applicable laws and regulations.
 - ► Federal and State laws and regulations, local ordinances & policies, and Uniform Compliance Guidelines

CONTROL ENVIRONMENT

- Overall structure of the organization and sets the tone.
- Includes oversight by governing body.
- ▶ Outline of specific duties within the organizational structure.
- Creating job descriptions and determining skills necessary to perform jobs.
- ▶ Designation of responsible persons for each part of the payroll process.
- ▶ Documentation of internal control procedures over specific payroll areas, including communication and monitoring.
- Correlation of assigned responsibility and authority to entity objectives.
- Establishing a confidential reporting system for individuals to report suspected fraud and abuse of local policies.

RISK ASSESSMENT

- ▶ Identify, analyze, and manage potential risks
- Complexity of the activity itself or the calculations for the activity.
- Susceptibility of the activity to fraud or misappropriations.
- ▶ Extent of judgment involved for the activity.
- Size and volume of individual items comprising the activity.
- Organizational structure # employees, experience of staff, etc
- ▶ New technology
- New or amended laws or regulations

CONTROL ACTIVITIES

- ▶ Detect, prevent, or reduce the identified risks
- Designed to achieve objectives
- ► Includes the detailed processes & procedures of the control structure
- Examples:
 - ► Reconciliations
 - ► Authorizations
 - ► Approval processes
 - ▶ Performance reviews
 - ► Verification processes

CONTROL PROCEDURES

- ➤ Salaries and wage rates are verified by someone outside of the payroll process.
- ▶ The responsibilities for hiring, terminating, and approving promotions are segregated from those preparing payroll transactions or inputting data.
- ▶ The responsibilities for approving time sheets are segregated from those for preparing payroll transactions or inputting data.
- Payroll adjustment reports are reviewed by someone outside of the payroll process.
- Employees' time and attendance records are approved by their supervisors.

CONTROL PROCEDURES (Continued)

- Corrections to recorded time and attendance records are approved by the employee's supervisor and authorized by management.
- ▶ Procedures are in place to ensure that changes in employment status are promptly reported to the payroll processing unit.
- ► Payroll disbursements are reviewed and approved by an authorized individual prior to payment.
- Access to payroll applications is appropriately controlled by user logins and passwords. Permissions can be set that allow only certain users to perform certain tasks.
- ► Changes to a payroll disbursement are approved by an individual other than the ones authorized to make the changes.

CONTROL PROCEDURES (Continued)

- ▶ Payroll checks are accounted for in numerical order and reconciled to the payroll check register.
- ► Access to the signature stamp used to sign payroll checks is adequately controlled.
- ► Payroll checks/stubs are periodically distributed by someone outside the normal payroll distribution function.
- Unclaimed payroll checks/stubs are returned to an individual other than those involved with the payroll process.
- ► Employees are cross-trained on the payroll process; those assigned to payroll take mandatory vacations.

INFORMATION & COMMUNICATION

- Identification, capture, and exchange of information within the entity and external parties.
- ➤ The form of communication and documentation of internal communications between offices, departments and the oversight body is established and communicated to employees.
- ▶ Procedures to ensure that the communication requirements are being followed and necessary information is being communicated properly.
- Procedures for feedback on and clarification of the information provided.
- Internal memos and reports are maintained to document communication. Logs are kept for information provided verbally.
- Procedures are established to retain public documents.

MONITORING

- ▶ Periodic checks are performed to determine if controls are in place and working effectively.
- ► Control activities are reviewed to determine if the actual activities are in compliance with established procedures.
- Deficiencies in the internal control process are documented and remediation is quickly completed to address any deficiencies.
- ▶ Management and the oversight body meet regularly to discuss controls, weaknesses and corrective action plans.

PAYROLL ISSUES & CONCERNS

- ▶ Compensation
 - ► Establishing salaries and wages
 - ▶ Payment
 - ► Election Workers
- ▶ Record of Hours Worked
- Benefits
- Withholdings

COMPENSATION

- ► Establishing Salaries & Wages:
 - ▶ All compensation and benefits must be included in the labor contract, salary ordinance, or resolution approved by the County Council or specifically authorized by statute. (IC 36-2-5-3 and 3.5)
 - ▶ A salary ordinance is separate from the budget ordinance. The Form 144 completed as part of the budget process is not the salary ordinance. The salary ordinance is a separate and distinct ordinance that should not be combined or confused with the ordinance for appropriations. (IC 36-2-5-11(c))

COMPENSATION (Continued)

Payment:

- ▶ All compensation should be paid through payroll claims (including additional pay, such as on-call or per call pay, shift premiums, stipends, bonuses, etc)
- ▶ Items not considered compensation for personal services and not payable through payroll claims (paid through regular county claims):
 - ► Mileage & travel expenses
 - ▶ Per diem of jurors, compensation of pauper attorneys (unless serving as an officer or employee of the court), and witness fees
 - ► Compensation of precinct election boards
 - ▶ Payments to attorneys, engineers, and other professionals, when serving on a contractual basis
- Method of payment Check or Direct Deposit
 - ▶ Payment manner must be authorized by the County Executive (IC 36-2-8-2).
 - ▶ Mandatory Direct Deposit? IC 36-1-3 provides commissioners with home rule powers which would allow a policy to be established, however it becomes a legal matter to determine if you can enforce such a policy

COMPENSATION (Continued)

- Payment (Continued):
 - ► Compensation may not be paid in advance (IC 5-7-3-1)
 - ➤ Compensation should be paid in a manner that complies with the way the salary ordinance is written (annual, bi-weekly, hourly, etc)
 - ▶ Years with 27 pays If salary ordinance establishes salaries on a bi-weekly or hourly basis then no need to do anything different. If salary ordinance establishes an annual salary, then annual salary would need to be divided by 27 bi-weekly pays instead of 26 bi-weekly pays.
 - ► However salaries are established, adequate appropriations should be included in the budget to cover the planned disbursements

COMPENSATION (Continued)

- Election Workers:
 - ▶ Election wages are excluded from federal income tax withholding
 - ▶ Election wages paid to a county employee should be through payroll
 - ▶ Election wages paid to a non-employee worker should be paid through payroll if the wages are anticipated to be more than \$600 for the calendar year because W-2 reporting will be required.
 - ▶ Although Form W-2 is not required to be issued for amounts less than \$600, election wages are taxable. The worker is to include the election wages on their income tax return.
 - ▶ Review IRS publications on paying election workers at <u>www.irs.gov</u> or contact IRS, Federal ,State, and Local Government Specialist for Indiana for more information on reporting and withholding requirements

RECORD OF HOURS WORKED

- ► Federal Fair Labor Standards Act (FLSA) requires that records of wages paid, daily and weekly hours of work, time and day of week when employee's workweek begins be kept for each covered, non-exempt worker
- ► The following State Board of Accounts prescribed forms or alternatives can be used to meet these requirements:
 - ► Form 99A, Employee's Service Record
 - ► Form 99B, Employee's Earnings Record
 - ► Form 99C Employee's Weekly Earnings Record (required only for employees non-exempt from FLSA & not on fixed work schedule & not paid weekly)
- ▶ Visit Department of Labor website at <u>www.dol.gov</u> for more information on required documentation and to determine whether an employee is exempt or non-exempt

BENEFITS

- ▶ All types of employee benefits should be detailed in a written policy
 - ▶ Policies should be established by the governing body
 - Negotiated labor contracts approved by governing body are considered written policies
 - ▶ Policy should conform to requirements of federal and state regulatory agencies
- ► Examples of benefits:
 - ▶ Sick , vacation, personal, and any other type of special leave
 - ► Fringe benefits take home vehicle, free use of property or services, etc
- Contact the IRS for proper tracking, valuation and reporting of benefits

WITHHOLDINGS

- ► All withholding should be tracked and remitted to appropriate agencies in a timely manner
 - ► Taxes, insurance premiums, garnishments, other authorized withholdings
- Withholdings funds should be monitored and reconciled to the unpaid amounts on hand

OUTSOURCING PAYROLL

- ▶ Management decision
- Consider the risks
- ► County still responsible for information, accuracy, compliance, and reporting of payroll
- ▶ Still need internal controls in place
- Understand outsourced functions, responsibilities, reporting, communication, documentation
- Manual versus automated process integration

IMPORTANCE OF CONTROLS

- ▶ Payroll transactions are significant as a major expense
- Susceptible to fraud
 - Especially to smaller units with less segregation of duties
- Highly automated
 - ▶ Less human involvement
 - ▶ See less of detail so errors or fraud could go unnoticed
- Financial Impact
 - ▶ Noncompliance could results in penalties and additional charges
 - ► Affect accuracy of financial records and reporting
- Personally responsible for losses or additional expenses

NEW OVERTIME RULE

- ▶ Elected officials, policymaking appointees, and their personal staff and legal advisors who are not subject to civil service laws
- ► Consult your human resources department, legal counsel, and AIC additional assistance on the new rules
- ▶ Visit the Department of Labor website at www.dol.gov/featured/overtime