

WASCO STATE PRISON— RECEPTION CENTER

Audit Report

PAYROLL AUDIT

August 1, 2015, through July 31, 2018



BETTY T. YEE
California State Controller

December 2020



BETTY T. YEE
California State Controller

December 10, 2020

John Sutton, Warden
Wasco State Prison–Reception Center
Post Office Box 8800
Wasco, CA 93280

Dear Mr. Sutton:

The State Controller’s Office audited the Wasco State Prison–Reception Center’s (WSP-RC) payroll process and transactions for the period of August 1, 2015, through July 31, 2018. WSP-RC management is responsible for maintaining a system of internal control over the payroll process within its organization, and for ensuring compliance with various requirements under state laws and regulations regarding payroll and payroll-related expenditures.

Our audit determined that WSP-RC did not maintain adequate and effective internal controls over its payroll process. WSP-RC lacked adequate segregation of duties and compensating controls over payroll transactions that resulted in improper separation lump-sum and overtime payments and improper holiday credits. WSP-RC also granted inappropriate keying access to the State’s payroll system.

In addition, WSP-RC did not implement controls to limit the accumulation of vacation and annual leave credits, resulting in liability for excessive balances. WSP-RC also did not always promptly collect salary advances from its employees.

If you have any questions, please contact Andrew Finlayson, Chief, State Agency Audits Bureau, by telephone at (916) 324-6310, or by email at afinlayson@sco.ca.gov.

Sincerely,

Original signed by

JIM L. SPANO, CPA
Chief, Division of Audits

JLS/as

cc: Ericka Clark, Institution Personnel Officer
Wasco State Prison–Reception Center
Kathleen Allison, Secretary
California Department of Corrections and Rehabilitation
Jennifer Barretto, Undersecretary of Administration
California Department of Corrections and Rehabilitation
Katherine Minnich, Deputy Director of Human Resources
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Audit Report

Summary

The State Controller’s Office (SCO) audited the Wasco State Prison–Reception Center’s (WSP-RC) payroll process and transactions for the period of August 1, 2015, through July 31, 2018. WSP-RC management is responsible for maintaining a system of internal control over the payroll process within its organization, and for ensuring compliance with various requirements under state laws and regulations regarding payroll and payroll-related expenditures. We completed our audit fieldwork on June 10, 2020.

Our audit determined that WSP-RC did not:

- Maintain adequate and effective internal controls over its payroll process. WSP-RC lacked adequate segregation of duties and compensating controls over payroll transactions that resulted in improper separation lump-sum and overtime payments and improper holiday credits. WSP-RC also granted inappropriate keying access to the State’s payroll system;
- Implement controls to limit the accumulation of vacation and annual leave credits, resulting in liability for excessive balances; and
- Promptly collect salary advances from its employees.

Background

In 1979, the State of California adopted collective bargaining for state employees. This created a significant workload increase for the SCO’s Personnel and Payroll Services Division (PPSD), as PPSD was the State’s centralized payroll processing center for all payroll related-transactions. PPSD decentralized the processing of payroll, allowing state agencies and departments to process their own payroll-related transactions. Periodic audits of the decentralized payroll processing at state agencies and departments ceased due to the budget constraints in the late 1980s.

In 2013, the California State Legislature reinstated these payroll audits to gain assurance that state agencies and departments maintain adequate internal control over the payroll function, provide proper oversight of their decentralized payroll processing, and comply with various state laws and regulations regarding payroll processing and related transactions.

Audit Authority

Authority for this audit is provided by California Government Code (GC) section 12476, which states:

The Controller may audit the uniform state pay roll system, the State Pay Roll Revolving Fund, and related records of state agencies within the uniform state pay roll system, in such manner as the Controller may determine.

In addition, GC section 12410 stipulates that:

The Controller shall superintend the fiscal concerns of the state. The Controller shall audit all claims against the state, and may audit the disbursement of any state money, for correctness, legality, and for sufficient provisions of law for payment.

Objectives, Scope, and Methodology

We performed this audit to determine whether WSP-RC:

- Maintained adequate and effective internal controls over its payroll process;
- Processed payroll and payroll-related disbursements and leave balances accurately and in accordance with collective bargaining agreements and state laws, regulations, policies, and procedures; and
- Administered salary advances in accordance with collective bargaining agreements and state laws, regulations, policies, and procedures.

The audit covered the period from August 1, 2015, through July 31, 2018.

The audit population consisted of payroll transactions totaling \$384,415,770, as quantified in the Schedule.

To achieve our audit objectives, we:

- Reviewed state and WSP-RC policies and procedures related to the payroll process to understand WSP-RC's methodology for processing various payroll and payroll-related transactions;
- Interviewed the WSP-RC payroll personnel to understand WSP-RC's methodology for processing various payroll and payroll-related transactions, determine employees' level of knowledge and ability relating to payroll transaction processing, and gain an understanding of existing internal control over the payroll process and systems;
- Selected transactions recorded in the State's payroll database using statistical sampling, as outlined in the Appendix, and targeted selection based on risk factors and other relevant criteria;
- Analyzed and tested the selected transactions and reviewed relevant files and records to determine the accuracy of payroll and payroll-related payments, accuracy of leave transactions, adequacy and effectiveness of internal control over the payroll process, and compliance with collective bargaining agreements and state laws, regulations, policies, and procedures; and
- Reviewed salary advances to determine whether WSP-RC administered and recorded them in accordance with collective bargaining agreements and state laws, regulations, policies, and procedures.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, 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.

Conclusion

Our audit determined that WSP-RC:

- Did not maintain adequate and effective internal controls over its payroll process.¹ We found the following deficiencies in internal control over the payroll process that we consider to be material weaknesses:
 - Inadequate segregation of duties and a lack of compensating controls over payroll transactions (see Finding 1);
 - Inappropriate keying access to the State’s payroll system (see Finding 2);
 - Failure to implement controls to ensure that WSP-RC adhered to the requirements of collective bargaining agreements and state regulations to limit the accumulation of vacation and annual leave credits, resulting in liability for excessive balances (see Finding 3);
 - Inadequate controls to ensure that separation lump-sum payments were calculated correctly and paid in a timely manner, resulting in improper, questioned, and late payments (see Finding 4);
 - Inadequate controls to ensure that overtime payments were calculated correctly and granted to eligible employees, resulting in improper payments (see Finding 5);
 - Inadequate controls to ensure that salary advances were collected in a timely manner, resulting in failure to recover outstanding amounts (see Finding 6); and
 - Inadequate controls to ensure that holiday credits were granted to eligible employees and supported with documentation, resulting in improper and questioned credits (see Finding 7);
- Did not process payroll and payroll-related disbursements and leave balances accurately and in accordance with collective bargaining agreements and state laws, regulations, policies, and procedures. We found the following instances of noncompliance with the requirements of collective bargaining agreements and state laws, regulations, policies, and procedures:

¹ In planning and performing our audit of compliance, we considered WSP-RC’s internal control over compliance with collective bargaining agreements and state laws, regulations, policies, and procedures to determine the auditing procedures that were appropriate under the circumstances for the purpose of providing a conclusion on compliance, and to test and report on internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this footnote; it was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. As discussed in this section, we identified certain deficiencies in internal control over compliance that we consider to be material weaknesses.

A deficiency in internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with provisions of laws, regulations, or contracts on a timely basis. Control deficiencies, either individually or in combination with other control deficiencies, may be evaluated as significant deficiencies or material weaknesses. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with provisions of laws, regulations, or contracts will not be prevented, or detected and corrected, on a timely basis. A significant deficiency over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with provisions of laws, regulations, or contracts that is less severe than a material weakness, yet important enough to merit attention from those charged with governance.

- Excessive vacation and annual leave balances with a value of at least \$2,061,192 as of July 31, 2018 (see Finding 3).

Although an October 20, 2020 directive from California Department of Human Resources (CalHR) does not affect the dollar value of this finding, we are disclosing this directive because it affects our recommendation. CalHR has directed departments to immediately suspend policies that require leave balances to be reduced below the limit, and that require employees to implement leave-reduction plans. This suspension will be in effect until the 2020 Personal Leave Program (2020 PLP) ends or July 1, 2022, whichever is sooner;

- Improper and late payments made for employee separation lump-sum pay (see Finding 4), improper payments made for overtime pay (see Finding 5), and improper and questioned holiday credits (see Finding 7), costing an estimated net total of \$629,855; and
- Did not administer salary advances in accordance with collective bargaining agreements and state laws, regulations, policies, and procedures. Five salary advances, totaling \$4,284, remained outstanding as of July 31, 2018, due to WSP-RC’s noncompliance with the State’s collection policies and procedures (see Finding 6).

Follow-up on Prior Audit Findings

The California Department of Corrections and Rehabilitation’s Office of Audits and Court Compliance issued a report in September 2016 for its Business Services Review of WSP-RC from August 22, 2016, through August 25, 2016. The Business Services Review report included findings regarding inadequate documentation for separation lump-sum payments and uncollected salary advances. Based on the work performed during our current audit, we noted similar findings (see Findings 4 and 6).

Views of Responsible Officials

We issued a draft audit report on September 23, 2020. John Sutton, Warden, responded by letter dated October 1, 2020 (Attachment), acknowledging the findings and indicating that WSP-RC has taken steps to correct the noted deficiencies. This final audit report includes WSP-RC’s response.

Restricted Use

This audit report is solely for the information and use of WSP-RC, the California Department of Corrections and Rehabilitation, CalHR, and the SCO; it is not intended to be and should not be used by anyone other than these specified parties. This restriction is not intended to limit distribution of this audit report, which is a matter of public record and is available on the SCO website at www.sco.ca.gov.

Original signed by

JIM L. SPANO, CPA
Chief, Division of Audits

December 10, 2020

**Schedule—
Summary of Audit Results
August 1, 2015, through July 31, 2018**

Audit Area Tested	Method of Selection	Number of Units of Population	Dollar Amount of Population	Number of Selections Examined	Selection Unit	Dollar Amount of Selections Examined	Total Dollar Amount of Known and Likely Issues	Finding Number
Segregation of duties	N/A	N/A	N/A	N/A	N/A	N/A	N/A	1
System access	Targeted	27	N/A	27	Employee	-	-	2
Excess vacation and annual leave	Targeted	73	\$ 2,061,192	73	Employee	\$ 2,061,192	\$ 2,061,192	3
Regular pay	Statistical	52,405	325,970,691	77	Transaction	-	-	
Separation lump-sum pay	Targeted	236	6,829,047	102	Employee	5,272,822	195,163	4
Overtime pay	Statistical and targeted	26,945	43,879,716	165	Transaction	397,928	342,974	5
Salary advance	Targeted	21	42,822	8	Transaction	11,562	4,284	6
Holiday credit	Targeted	8,909	3,629,355	338	Transaction	119,894	91,718	7
Uniform allowance	Targeted	2,993	2,002,947	2,993	Transaction	-	-	
			<u>\$ 384,415,770</u>			<u>\$ 7,863,398</u>	<u>\$ 2,695,331</u>	

Findings and Recommendations

**FINDING 1—
Inadequate
segregation of
duties and lack of
compensating
controls over
payroll
transactions**

WSP-RC lacked adequate segregation of duties within its payroll transactions unit to ensure that only valid and authorized payroll transactions were processed. WSP-RC also failed to implement other controls to compensate for this risk.

GC sections 13400 through 13407 require state agencies to establish and maintain internal controls, including proper segregation of duties and an effective system of internal review. Adequate segregation of duties reduces the likelihood that fraud or error will remain undetected by providing for separate processing by different individuals at various stages of a transaction and for independent reviews of the work performed.

Our audit found that WSP-RC payroll transactions unit staff performed conflicting duties. Staff members performed multiple steps in processing payroll transactions, including entering data into the State's payroll system; auditing employee timesheets; reconciling payroll, including reconciling system output to source documentation; reporting payroll exceptions; and processing adjustments. For example, staff members keyed in regular and overtime pay and reconciled the master payroll, overtime, and other supplemental warrants. WSP-RC failed to demonstrate that it implemented compensating controls to mitigate the risks associated with such a deficiency. We found no indication that these functions were subjected to periodic supervisory review.

The lack of adequate segregation of duties and compensating controls has a pervasive effect on the WSP-RC payroll process, and impairs the effectiveness of other controls by rendering their design ineffective or by keeping them from operating effectively. These control deficiencies, in combination with other deficiencies discussed in Findings 2 through 7, represent a material weakness in internal control over the payroll process such that there is a reasonable possibility that material noncompliance with provisions of laws, regulations, or contracts will not be prevented, or detected and corrected, on a timely basis.

Good internal control practices require that the following functional duties be performed by different work units, or at minimum, by different employees within the same unit:

- *Recording transactions* – This duty refers to the record-keeping function, which is accomplished by entering data into a computer system.
- *Authorization to execute* – This duty belongs to individuals with authority and responsibility to initiate and execute transactions.
- *Periodic review and reconciliation of actual payments to recorded amounts* – This duty refers to making comparisons of information at regular intervals and taking action to resolve differences.

Recommendation

We recommend that WSP-RC:

- Separate conflicting payroll function duties to the greatest extent possible. Adequate segregation of duties will provide a stronger system of internal control whereby the functions of each employee are subject to the review of another.

If it is not possible to segregate payroll functions fully and appropriately, WSP-RC should implement compensating controls. For example, if the payroll transactions unit staff member responsible for recordkeeping also performs a reconciliation process, then the supervisor should perform and document a detailed review of the reconciliation to provide additional control over the assignment of conflicting functions. Compensating controls may also include dual authorization requirements and documented reviews of payroll system input and output; and

- Develop formal procedures for performing and documenting compensating controls.

**FINDING 2—
Inappropriate
keying access to the
State’s payroll
system**

WSP-RC lacked adequate controls to ensure that only appropriate staff had keying access to the State’s payroll system. WSP-RC inappropriately allowed seven employees keying access to the State’s payroll system. If not mitigated, this control deficiency leaves payroll data at risk of misuse, abuse, and unauthorized use.

The SCO maintains the State’s payroll system. The system is decentralized, thereby allowing employees of state agencies to access it. PPSD has established a *Decentralized Security Program Manual* that all state agencies are required to follow in order to access the State’s payroll system. The program’s objectives are to secure and protect the confidentiality and integrity of payroll data against misuse, abuse, and unauthorized use.

We examined the records of 27 WSP-RC employees who had keying access to the State’s payroll system at various times between August 2015 and July 2018. Of the 27 employees, seven had inappropriate keying access to the State’s payroll system. Specifically, WSP-RC did not immediately remove or modify keying access for six employees after the employees’ separation from state service, transfer to another agency, or change in classification. For example, a Personnel Specialist promoted to an ineligible classification on January 31, 2018; WSP-RC did not request to remove the employee’s access until April 3, 2018 (62 days later). In addition, one employee had keying access to the system while appointed to the Staff Services Analyst classification, which is ineligible to have keying access to the State’s payroll system without the required justification; WSP-RC could not provide the justification letter for this employee.

The *Decentralized Security Program Manual* states, in part:

The PPSD system contains sensitive and confidential information. Access is restricted to persons with an authorized, legal, and legitimate business requirement to complete their duties. . . .

Currently, PIMS, HIST, KEYM, PIP, LAS, MPC and/or ACAS applications are restricted to Personnel Specialists or Personnel Technician classifications because their need is by definition a function of their specific job duties and any change in those duties requires a reevaluation of the need for access.

If the employee's duties change, such that the need for access no longer exists, the access privilege MUST be removed or deleted immediately by a request submitted by the department/campus. . . .

A request to grant access to an individual in a classification other than in the Personnel Specialist/Payroll Technician series to access PIMS, HIST, KEYM, PIP, LAS, MPC and/or ACAS requires a written justification from the Authorizing Manager. The justification must describe the individual's specific job duties requiring the need to access system information (i.e., PIMS = Employment History, HIST=Payroll History, LAS=Leave Accounting System, etc.) as well as level of access to that application, in order to perform their regular daily duties. . . .

To prevent unauthorized use by a transferred, terminated or resigned employee's user ID, the Security Monitor must IMMEDIATELY submit all pages of the PSD125A to delete the user's system access. Using an old user ID increases the chances of a security breach which is a serious security violation. Sharing a user ID is strictly prohibited and a serious violation.

Recommendation

We recommend that WSP-RC:

- Update keying access to the State's payroll system immediately after employees leave WSP-RC, transfer to another unit, or change classifications; and
- Periodically review access to the system to verify that access complies with the *Decentralized Security Program Manual*.

FINDING 3— Inadequate controls over vacation and annual leave balances, resulting in liability for excessive balances

WSP-RC failed to implement controls to ensure that it adheres to the requirements of collective bargaining agreements and state regulations to limit the accumulation of vacation and annual leave credits. This deficiency resulted in liability for excessive leave balances with a value of at least \$2,061,192 as of July 31, 2018. We expect the liability to increase if WSP-RC does not take action to address the excessive vacation and annual leave balances.

Collective bargaining agreements and state regulations limit the amount of vacation and annual leave that most state employees may accumulate to no more than 80 days (640 hours). The limit on leave balances helps state agencies to manage leave balances and control the State's liability for accrued leave credits. State agencies may allow employees to carry a higher leave balance only under limited circumstances. For example, an employee may not be able to reduce accrued vacation or annual leave hours below the limit due to business needs. When an employee's leave accumulation exceeds or is projected to exceed the limit, state agencies should work with the employee to develop a written plan to reduce leave balances below the applicable limit.

Our examination of WSP-RC's leave accounting records determined that WSP-RC had 1,515 employees with unused vacation or annual leave credits at July 31, 2018. Of those employees, 73 exceeded the limit set by collective bargaining agreements and state regulations. For example, one employee had an accumulated balance of 2,400 hours in vacation, or 1,760 hours beyond the 640-hour limit.

Collectively, the 73 employees accumulated 29,504 hours of excess vacation and annual leave, with a value of at least \$2,061,192 as of July 31, 2018. This estimated liability does not adjust for salary rate increases and additional leave credits.² Accordingly, we expect that the amount needed to pay for this liability will be higher. For example, a WSP-RC employee separated from state service with 3,902 hours in leave credits, including 2,188 hours in annual leave. After adjusting for additional leave credits, the employee should have been paid for 4,658 hours, or 19% more.

We judgmentally selected 10 of the 73 employees for examination to determine whether WSP-RC complied with collective bargaining agreements and state regulations. We determined that WSP-RC could not demonstrate that it had complied with collective bargaining agreements and state regulations when allowing these employees to maintain excess vacation or annual leave balances. We also found that WSP-RC had no plans in place during the audit period to reduce leave balances below the limit.

If WSP-RC does not take action to reduce the excessive leave balances, the liability for accrued vacation and annual leave will likely increase because most employees will receive salary increases or use other non-compensable leave credits instead of vacation or annual leave, increasing their vacation or annual leave balances. The state agency responsible for paying these leave balances may face a cash flow problem if a significant number of employees with excessive vacation or annual leave balances separate from state service. Normally, state agencies are not budgeted to make these separation lump-sum payments. However, the State's current practice dictates that the state agency that last employed an employee pays for that employee's lump-sum separation payment, regardless of where the employee accrued the leave balance.

Although an October 20, 2020 directive from CalHR does not affect the dollar value of this finding, we are disclosing this directive because it affects our recommendation. CalHR has directed departments to immediately suspend policies that require leave balances to be reduced below the limit, and that require employees to implement leave-reduction plans. This suspension will be in effect until the 2020 PLP ends, or July 1, 2022, whichever is sooner.

² Most state employees receive pay rate increases every year pursuant to state laws and/or collective bargaining agreements until they reach the top of their pay scale, or promote into a higher-paying position. In addition, when an employee's accumulated leave balances upon separation are calculated for lump-sum pay, the employee is credited with additional leave credits equal to the amount that the employee would have earned had the employee taken time off and not separated from state service.

Recommendation

We recommend that, after the 2020 PLP ends, or July 1, 2022, whichever is sooner, WSP-RC:

- Implement controls, including existing policies and procedures, to ensure that its employees' vacation and annual leave balances are maintained within levels allowed by collective bargaining agreements and state regulations;
- Conduct ongoing monitoring of controls to ensure that they are implemented and operating effectively; and
- Participate in leave buy-back programs if the State offers such programs and funds are available.

**FINDING 4—
Inadequate
controls over
separation lump-
sum pay, resulting
in improper,
questioned, and
late payments**

WSP-RC lacked adequate segregation of duties within its payroll transactions unit, as noted in Finding 1, and lacked adequate controls over the processing of employee separation lump-sum pay. We identified \$202,413 in overpayments, \$10,845 in underpayments, and \$3,595 in questioned payments for separation lump-sum pay. We also found that WSP-RC did not make separation lump-sum payments to four employees in a timely manner. If not mitigated, these control deficiencies leave WSP-RC at risk of making additional improper and late separation lump-sum payments, noncompliance with agreements and laws, and liability for late payments.

GC section 19839 allows lump-sum payment for accrued eligible leave credits when an employee separates from state employment. Collective bargaining agreements include similar provisions regarding separation lump-sum pay.

Payroll records show that WSP-RC processed separation lump-sum payments, totaling \$6,829,047, for 236 employees between August 2015 and July 2018, as follows:

Separation Lump-Sum Pay Group	Unit	Amount
Section 7(k) employees (examined 100%)	93	\$ 3,917,551
Non-section 7(k) employees (examined nine highest payments)	143	2,911,496
Total population	236	\$ 6,829,047

* Amounts in this table are rounded to the nearest dollar.

We examined the separation lump-sum pay, totaling \$3,917,551, for all 93 employees who were covered by the provisions of Section 7(k) of the Fair Labor Standards Act. Of the 93 employees, 63 were overpaid by an approximate total of \$201,863 and two were underpaid by an approximate total of \$1,529. Our examination of lump-sum payments also showed a lack of supporting documentation for payments, totaling \$3,595, made to three employees. Without the required documentation, there is no record of calculation or approval of payments for separation lump-sum pay. Therefore, we could not determine the validity, accuracy, and propriety of the payment made to these employees. As a result, we questioned these payments.

Of the remaining 143 employees who were not covered by the provisions of Section 7(k) of Fair Labor Standards Act and granted separation lump-sum pay, totaling \$2,911,496, we selected nine employees who were granted the highest payments, totaling \$1,355,271. The payments for these selections represent 47% of the total separation lump-sum payments to non-Section 7(k) employees. Of these nine employees whose payments we examined, one was overpaid by approximately \$550 and six were underpaid by an approximate total of \$9,316.

Of the 102 employees whose separation lump-sum payments we examined, four were not paid in a timely manner, in violation of collective bargaining agreements and state laws, as summarized in CalHR's *Human Resources Manual*, section 1703.

The known overpayments to Section 7(k) employees were made because payroll transactions unit staff members miscalculated leave balances paid, and improperly included holiday credits that should not have been included when calculating employees' leave balances for lump-sum pay. The known underpayments to Section 7(k) employees occurred because the payroll transactions unit staff members miscalculated leave balances paid. The improper payments to non-Section 7(k) employees were made because Personnel Specialists miscalculated leave balances paid. WSP-RC also lacked adequate supervisory review to ensure accurate processing of separation lump-sum pay.

GC sections 13400 through 13407 require state agencies to establish and maintain internal controls, including an effective system of internal review.

Recommendation

We recommend that WSP-RC:

- Establish adequate controls to ensure accurate and timely separation lump-sum payments;
- Conduct a review of separation lump-sum payments made during the past three years to ensure that the payments were accurate and in compliance with collective bargaining agreements and state law; and
- Recover overpayments made to separated employees in accordance with GC section 19838 and *State Administrative Manual (SAM)* section 8776.6, and properly compensate those employees who were underpaid.

FINDING 5— Inadequate controls over overtime pay, resulting in improper payments

WSP-RC lacked adequate segregation of duties within its payroll transactions unit, as noted in Finding 1, and lacked adequate controls over the processing of overtime pay. We identified \$343,159 in overpayments and \$185 in underpayments for overtime, consisting of \$2,443 in overpayments and \$185 in underpayments based on actual transactions examined (“known”); and \$340,716 in overpayments based on the results of statistical sampling (“likely”). If not mitigated, these control deficiencies leave WSP-RC at risk of making additional improper overtime payments.

Collective bargaining agreements, and state laws and policies, contain specific clauses regarding overtime pay. Payroll records show that WSP-RC processed 26,945 overtime pay transactions, totaling \$43,879,716, between August 2015 and July 2018, as follows:

Overtime Payment Type by Group	Unit	Amount
Work Week Group 2 and SE – Paid for less than 250 hours per transaction between August 2015 and June 2018 (statistically sampled)	26,885	\$ 43,648,502
Work Week Group 2 and SE – Paid for at least 250 hours per transaction between August 2015 and June 2018 (items examined 100%)	9	194,633
Work Week Group 2 and SE – Paid for in July 2018 (items examined 100%)	12	20,215
Work Week Group E (items examined 100%)	39	16,366
Total population	<u>26,945</u>	<u>\$ 43,879,716</u>

* Amounts in this table are rounded to the nearest dollar.

Of the 26,885 overtime pay transactions, totaling \$43,648,502, for Work Week Group (WWG) 2 and WWG SE employees who were paid for less than 250 hours of overtime per transaction between August 2015 and June 2018, we randomly selected a statistical sample (as described in the Appendix) of 105 transactions, totaling \$166,714. Of the 105 transactions, five were overpaid by approximately \$1,306. As we used a statistical sampling method to select the overtime pay transactions examined, we projected the amount of likely overpayments to be \$340,716. Therefore, the known and likely overpayments totaled approximately \$342,022.

The following table summarizes the results of our statistical sampling:

Known overpayments	\$ 1,306
Divide by: Sample	<u>166,714</u>
Error rate for projection (differences due to rounding)	<u>0.78%</u>
Population that was statistically sampled	43,648,502
Multiply by: Error rate for projection	<u>0.78%</u>
Known and likely overpayments (differences due to rounding)	342,022
Less: Known overpayments	<u>1,306</u>
Likely overpayments	<u>\$ 340,716</u>

* Amounts in this table are rounded to the nearest dollar.

We also examined all nine overtime pay transactions, totaling \$194,633, for WWG 2 and WWG SE employees who were paid for at least 250 hours of overtime per transaction between August 2015 and June 2018. Our examination of the transactions found no exceptions.

In addition, we examined all 12 overtime pay transactions, totaling \$20,215, for the pay period of July 2018. We examined these transactions due to a change in the calculation of an employee's regular rate of pay for overtime purposes effective July 1, 2018, pursuant to CalHR's *Human Resources Manual* section 1713. Of the 12 transactions, two were overpaid by \$359 and one was underpaid by \$120.

Furthermore, we examined all 39 overtime pay transactions, totaling \$16,366, for WWG E employees who are not eligible to receive overtime pay under normal circumstances. Of the 39 transactions, three were overpaid by a total of \$778 and one was underpaid by \$65.

The known improper payments were made because payroll transactions unit staff members miscalculated overtime hours worked or on-call/callback hours; paid for overtime hours worked at the straight-time rate instead of the time-and-a-half rate, or vice-versa; failed to verify whether employees were eligible for compensation of “travel time”; or incorrectly entered the overtime hours worked into the payroll system. Furthermore, WSP-RC lacked adequate supervisory review to ensure accurate processing of overtime pay.

GC sections 13400 through 13407 require state agencies to establish and maintain internal controls, including a system of policies and procedures adequate to ensure compliance with applicable laws and other requirements, and an effective system of internal review.

Recommendation

We recommend that WSP-RC:

- Conduct a review of overtime payments made during the past three years to ensure that the payments complied with collective bargaining agreements and state laws and policies; and
- Recover overpayments made to employees through an agreed-upon collection method in accordance with GC section 19838, and properly compensate those employees who were underpaid.

We further recommend that, to prevent improper overtime payments from recurring, WSP-RC:

- Establish adequate internal controls to ensure that payments are accurate and comply with collective bargaining agreements and state laws and policies; and
- Provide adequate oversight to ensure that payroll transactions unit staff process only valid and authorized payments that comply with collective bargaining agreements and state laws and policies.

FINDING 6— Inadequate controls over salary advances, resulting in failure to recover outstanding amounts

WSP-RC lacked adequate segregation of duties within its payroll transactions unit, as noted in Finding 1, and lacked adequate controls over salary advances to ensure that advances were recovered in accordance with state law and policies. Five salary advances, totaling \$4,284, remained outstanding as of July 31, 2018, due to WSP-RC’s noncompliance with the State’s collection policies and procedures. The oldest unrecovered salary advance was outstanding for nearly four years. If not mitigated, these control deficiencies leave WSP-RC at risk of failing to collect additional salary advances.

At July 31, 2018, WSP-RC’s accounting records showed 21 outstanding salary advances, totaling \$42,822, including eight balances, totaling \$11,562, which had been outstanding for more than 60 days. Generally,

the prospect of collection diminishes as an account ages. When an agency does not initiate collection within three years from the date of overpayment, the possibility of collection is remote.

GC section 19838 and SAM sections 8776 and 8776.7 describe the State's collection policies and procedures, which require WSP-RC to collect salary advances in a timely manner and maintain proper records of collection efforts.

We examined the eight salary advances that had been outstanding for more than 60 days. Based on this examination, we noted that WSP-RC did not comply with the State's collection policies and procedures for five salary advances, totaling \$4,284. WSP-RC did not send collection notices promptly, or did not send the notices at all. For example, in January 2018, WSP-RC issued a salary advance to a separating employee, and then improperly issued the separation lump-sum pay, resulting in an overpayment. WSP-RC sent the first collection letter in March 2018, about two months later.

The lack of adequate controls over salary advances reduces the likelihood of collection, increases the amount of resources expended on collection efforts, and negatively impacts cash flow.

Recommendation

We recommend that WSP-RC ensure that it recovers salary advances in a timely manner, pursuant to GC section 19838 and SAM sections 8776 and 8776.7.

FINDING 7— Inadequate controls over holiday credit transactions, resulting in improper and questioned credits

WSP-RC lacked adequate segregation of duties within its payroll transactions unit, as noted in Finding 1, and lacked adequate controls over the processing of holiday credit transactions. We identified approximately \$1,825 in improper holiday credits and \$89,893 in questioned holiday credits. If not mitigated, these control deficiencies leave WSP-RC at risk of granting additional improper holiday credits.

GC section 19853 specifies the compensation that an eligible employee is entitled to receive when required to work on a qualifying holiday. Collective bargaining agreements between the State and Bargaining Units 6, 15, 18, and 19 include similar provisions regarding holiday credit and holiday pay for represented employees.

Leave accounting records show that WSP-RC processed 8,909 accrual transactions of holiday credit. We examined 65 of these transactions, with an estimated value of \$30,001, because they involved unusual credits. Of the 65 transactions, nine involved improper credits, with an estimated value of \$1,825. The improper holiday credit transactions were made because payroll transactions unit staff members granted holiday credits to employees during pay periods with no holidays. WSP-RC also lacked adequate supervisory review to ensure proper and accurate processing of holiday credits.

We also examined an additional 273 holiday credit transactions, with an estimated value of \$89,893, because they appeared to be holiday credits granted to ineligible employees. We requested supporting documentation to determine whether these holiday credits were allowable compensation that had been misclassified in the State's payroll system. For example, employees may be eligible for a personal holiday or holiday pay (instead of holiday credit). WSP-RC failed to provide the requested supporting documentation. Without the required documentation, there is no record of the nature or approval of these holiday credits. Therefore, we could not determine the validity, accuracy, and propriety of the holiday credits made to the employees. As a result, we questioned these 273 holiday credit transactions.

GC sections 13400 through 13407 require state agencies to establish and maintain internal controls, including an effective system of internal review.

Recommendation

We recommend that WSP-RC:

- Conduct a review of holiday credits granted during the past three years to ensure that credits are properly supported with documentation, and complied with collective bargaining agreements and state law;
- Correct any improper holiday credits in the State's leave accounting system; and
- Establish adequate controls to ensure that holiday credits granted are valid and comply with collective bargaining agreements and state law.

Appendix— Audit Sampling Methodology

We used attributes sampling for tests of compliance. The sample design was chosen because:

- It follows the American Institute of Certified Public Accountants (AICPA) guidelines;
- It allows us to achieve our objectives for tests of compliance in an efficient and effective manner; and
- Audit areas included high volumes of transactions.

The following table outlines our audit sampling application for all audit areas where statistical sampling was utilized:

Audit Area	Type of Test	Population (Unit)	Population (Dollar)	Sampling Unit	Sample Selection Method	Confidence Level	Tolerable Error Rate	Expected Error (Rate) ^a	Sample Size ^b	Results Projected to Intended Population	Finding Number
Regular pay	Compliance	52,405	\$325,970,691	Transaction	Computer-generated simple random	90%	5%	1 (1%)	77	Yes	
Overtime pay (Work Week Groups 2 and SE)	Compliance	26,885	43,648,502	Transaction	Computer-generated simple random	90%	5%	2 (1.75%)	105	Yes	5

^a Pursuant to the AICPA's *Audit Guide: Audit Sampling* (May 1, 2017 edition), pages 131-133, the expected error is the expected number of errors planned for in the sample. It is derived by multiplying the expected error rate by the sample size. The expected number of errors in the sampling tables on pages 135-136 was rounded upward, e.g., 0.2 errors becomes 1.0 error.

^b For populations of 250 items and above, we determined the sample size using a calculator that utilizes a binomial distribution. As stated in *Technical Notes on the AICPA Audit Guide: Audit Sampling* (March 1, 2012), page 5, although the hypergeometric distribution is the exactly correct distribution to use for attributes sample sizes, the distribution becomes unwieldy for large populations unless suitable software is available. Therefore, more convenient approximations are frequently used instead.

**Attachment—
Wasco State Prison—Reception Center’s
Response to Draft Audit Report**

WASCO STATE PRISON-RECEPTION CENTER

P.O. Box 8800
701 Scofield Avenue
Wasco, CA 93280-8800



October 1, 2020

Mr. Andrew Finlayson, Chief
State Agency Audits Bureau
State Controller's Office, Division of Audits
P.O. Box 942850
Sacramento, CA 94250

Dear Mr. Finlayson,

This letter is in response to the draft report issued by the State Controller's Office (SCO) on September 23, 2020 regarding the Payroll Process Review of Wasco State Prison-Reception Center (WSP-RC) covering the period of August 1, 2015 through July 31, 2018. WSP-RC acknowledges the numbers reflected in this audit, and some improvements have already been made to existing processes.

The following is in response to the findings and recommendations contained in this report:

Finding #1 – Inadequate segregation of duties and lack of compensating controls over payroll transactions.

Response: Since the audit, the WSP-RC transaction unit underwent training and went over the payroll transactions procedure to ensure that levels of responsibility were understood. We have implemented separation of duties by having Personnel Supervisor I and/or Personnel Supervisor II verify daily payroll transactions in SCO. In addition, Personnel Supervisor I and Personnel Supervisor II review and approve all documents prior to submission or keying.

Finding #2 – Inappropriate keying access to the State's payroll system.

Response: WSP-RC has established a more efficient tracking system for individuals designated and approved to have system keying access. Current Security Authorization Listing PSD 125A has been updated and submitted to the Decentralized Security Administration. The Associate Warden-Business Services and Senior Personnel Specialist review and authorize keying access to the SCO payroll system.

Finding #3 – Inadequate controls over vacation and annual leave balances, resulting in liability for excessive balances.

Response: To ensure that employees' balances are below the Memorandum of Understanding (MOU) cap, employees were required to submit CalHR 138 Leave Reduction Plan form to their Supervisor.

Personnel retains a copy of the approved reduction plan in the Official Personnel File (OPF).

Finding #4 – Inadequate controls over separation lump-sum pay, resulting in improper, questioned, and late payments.

Response: To ensure compliance with collective bargaining unit agreements, state law, and accurate processing of separation transaction—especially lump-sum pay—WSP-RC reviewed and updated process according to the new rules.

Personnel Specialists were provided training regarding separation process and lump-sum calculation. To ensure accuracy of lump-sum calculation PIB#2018-001, Lump Sum Calculation for Rank-and-File Bargaining Unit 6 Employees in Posted Position Issue Date January 9, 2018 was reviewed and 7K Lump Sum Calculator has been updated.

Personnel Supervisor I and/or Personnel Supervisor II review and approve separation documents to ensure accurate processing of lump-sum pay prior to keying. Actual payments that were issued will be reconciled and adjusted immediately to resolve any differences. If it is not feasible to provide employee with an SCO warrant within 72 hours, a Salary Advance will be provided.

Findings regarding late payments were due to CalPERS's late confirmation of approved retirement dates.

Finding #5 – Inadequate controls over overtime pay, resulting in improper payments.

Response: Since the audit, the Personnel Supervisor I and/or Personnel Supervisor II review CDCR Form 998 in conjunction with bargaining units and Work Week Group overtime rules, calculation worksheet, and 672 prior to the Personnel Specialist keying pay.

Overpayment – For all the overpayments within the 3-year statute of limitations, the overpayment letter was mailed, and the collection process was initiated.

Underpayments – STD. 674 was processed and submitted to SCO, requesting a payment adjustment.

Finding #6 – Inadequate controls over salary advances, resulting in failure to recover outstanding amounts.

Response: WSP-RC has implemented daily monitoring of outstanding salary advances to ensure that items are addressed timely. A salary advance tracking sheet is routed daily to the staff. Comments and updates are reviewed by the Supervisor for approval or direction if additional time is needed.

Since the audit, WSP-RC is more efficiently tracking records of outstanding salary advances and documents sent to SCO to request pay. Our outstanding salary advances have been reduced and well-managed.

Finding #7 – Inadequate controls over holiday credit transactions, resulting in improper and questioned credits.

Response: WSP will conduct a review of holiday credits to ensure they are properly supported with documentations and comply with the MOU. We will correct the Leave Accounting System transaction as necessary.

WSP-RC welcomes insights provided by the auditors and would like to thank SCO for its work on this report. WSP-RC takes its responsibilities seriously to ensure effective payroll processes are in place and is committed to continually improving those processes. WSP-RC continues to place importance on the quality of work of the Personnel Office and is looking forward to continued improvement. We will take corrective action as necessary to address the issues identified in the report.

Should you have any questions, please contact Ericka Clark, Staff Services Manager I, at (661) 758-8400, extension 5181, or at ericka.clark@cdcr.ca.gov.

Sincerely,



John Sutton
Warden
Wasco State Prison - RC

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