



City of Peekskill Internal Controls Over Leave Accruals

Report of Examination

Period Covered:

January 1, 2010 — June 3, 2011

2011M-234



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

February 2012

Dear City Officials:

A top priority of the Office of the State Comptroller is to help local government officials manage government resources efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support government operations. The Comptroller oversees the fiscal affairs of local governments statewide, as well as compliance with relevant statutes and observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations and City Council governance. Audits also can identify strategies to reduce costs and to strengthen controls intended to safeguard local government assets.

Following is a report of our audit of the City of Peekskill, entitled Internal Controls Over Leave Accruals. This audit was conducted pursuant to Article V, Section 1 of the State Constitution and the State Comptroller's authority as set forth in Article 3 of the General Municipal Law.

This audit's results and recommendations are resources for local government officials to use in effectively managing operations and in meeting the expectations of their constituents. If you have questions about this report, please feel free to contact the local regional office for your county, as listed at the end of this report.

Respectfully submitted,

*Office of the State Comptroller
Division of Local Government
and School Accountability*

Introduction

Background

The City of Peekskill (City) is located in Westchester County and has a population of approximately 23,600. The City is governed by the City Council (Council) which comprises seven elected members. The Council is responsible for the general management and control of the City's financial affairs. The appointed City Manager is responsible for the day-to-day management of the City's operations and financial resources under the direction of the Council.

The City Comptroller (Comptroller), appointed by the City Manager, is responsible for managing the City's finances. The Comptroller works under the supervision of, and reports to, the City Manager. The City provides various services to its residents including highway, parks, and general government support. These services are financed primarily by real property taxes, sales tax, and State aid. Budgeted expenditures for the 2011 fiscal year for the general fund were approximately \$34.7 million.

Objective

The objective of our audit was to assess internal controls over leave accruals. Our audit addressed the following related question:

- Are internal controls over leave accruals appropriately designed and operating effectively to adequately safeguard City assets?

Scope and Methodology

We examined internal controls over leave accruals for the period January 1, 2010 to June 3, 2011.

We conducted our audit in accordance with generally accepted government auditing standards (GAGAS). More information on such standards and the methodology used in performing this audit are included in Appendix C of this report.

Comments of City Officials and Corrective Action

The results of our audit and recommendations have been discussed with City officials and their comments, which appear in Appendix A, have been considered in preparing this report. City officials disagreed with certain aspects of our findings and recommendations in our report, but indicated that they planned to implement some of our recommendations. Appendix B includes our comments on the issues raised in the City's response letter.

The Council has the responsibility to initiate corrective action. A written corrective action plan (CAP) that addresses the findings and recommendations in this report should be prepared and forwarded

to our office within 90 days, pursuant to Section 35 of the General Municipal Law. For more information on preparing and filing your CAP, please refer to our brochure, *Responding to an OSC Audit Report*, which you received with the draft audit report. We encourage the Council to make this plan available for public review in the Clerk's office.

Leave Accruals

A good system of accounting for employee leave time (vacation, sick, etc.) includes comprehensive policies and procedures that provide for periodic independent reviews of leave time accrual records and balances throughout the year. It is important for procedures to be designed to ensure that leave time is earned in accordance with City policies, collective bargaining agreements and/or Council resolutions, and that days used are properly deducted from employee leave time accruals.

The City did not have comprehensive written policies and procedures for leave time. As a result, 12 employees had negative leave time balances, two employees used leave time to which they were not entitled, and seven employees earned leave time that was not added to their balances. In addition, 33 employees who left the City were not deactivated in the payroll system, increasing the risk they could receive payments for leave time they are not entitled to.

Once a year, the data entry clerk enters time balances into the payroll system from the information provided by the Human Resources Department (HR). Subsequently, the clerk receives bi-weekly payroll reports from department heads that include leave time usage. Because the payroll system does not automatically accrue leave time earned or deduct leave time used, the clerk has to manually enter this information. However, there is no process to review the clerk's entries for accuracy. In addition, HR gets monthly reports of leave time usage from department heads and keeps manual records for each employee's leave time balances. However, the monthly reports and the HR records are never compared to the information the clerk enters into the payroll system to ensure accuracy of the information.

Due to the lack of controls, we reviewed the employee benefit report for the most current report (June 21, 2011) and found that 12 of the 275 employees on the report had negative leave time balances. For example, one employee had a negative 24 hour balance. We checked the employee's time records and found that the employee should have had a negative balance of eight hours because he had earned 16 hours of vacation time that had not been entered into the system.

In addition, we selected 15 additional employees¹ for review (for a total of 27) to determine whether their leave time was earned in accordance with the City's personnel policy or collective bargaining

¹ The 15 employees were selected using a random number generator.

agreements, and whether time used was properly deducted from their balances. Two employees used 24.8 hours of leave time valued at \$1,200 to which they were not entitled. In addition, seven employees earned 61.3 hours of leave time valued at \$2,400 that were not added to their balances. During our testing, we also identified 33 employees who were not deactivated in the payroll system even though they were no longer employed by the City. Although they did not receive payments for the remainder of our audit period, they should be deactivated to ensure this could not occur.²

The clerk told us that she was never trained on how to set up the leave time accruals. We brought the deficiencies to the attention of City officials, who had the software vendor update the system to prevent the clerk from entering leave time usage when employees do not have adequate balances.

As a result of the deficiencies, the City could lose money if employees use or get paid for leave time that they do not have, and there is an increased risk that employees will not receive the leave time benefits to which they are entitled.

Recommendations

1. The City should develop comprehensive policies and procedures for leave accrual balances and appoint someone independent of the maintenance of leave time records to periodically review the accrual records and balances for accuracy.
2. The clerk should correct the leave accrual records for the employees identified in this report.
3. The clerk should ensure that all individuals that are no longer employed by the City are deactivated from the payroll system.

² The employees were deactivated from the program tab that generates paychecks but not from program tab that generates reports. As a result, there is an increased risk that they could be inadvertently reactivated to receive paychecks and receive payments to which they are not entitled.

APPENDIX A

RESPONSE FROM CITY OFFICIALS

The City officials' response to this audit can be found on the following pages.



City of Peekskill
Finance Department

Charles Emberger
Comptroller

Jessie Boyd
Deputy Comptroller

Office of the State Comptroller
33 Airport Center Drive Suite 103
New Windsor, NY 12553

Dear [REDACTED],

We disagree with the auditor's report. Employees who retire from the City employment are paid out for their accruals so it may appear they were over paid, however they were not. The only benefit that is accrued on a monthly basis is sick time an employee earns one sick day per month. Compensation time is calculated on a weekly basis as employees work overtime. Vacations are posted in the beginning of the year and are not accrued automatically; however when someone retires the vacation time accrued is paid at time of separation. Also if an employee takes vacation the last week of the year and they get paid in January the vacation time shows up in the new year. This would appear an employee was overpaid but they are not. We received a list of employees from the auditors but no explanation of the problem. The list had twelve names and six were separated from the City. So we assume they were paid out accrued time, because the report is not available, the remaining six were still active. The State Comptroller's office refers to "leave time" we do not have a benefit defined as leave time; because the report is unclear we cannot respond. We have compensation time, vacation time, or sick time without knowing what the Comptroller's Office is depicting as "leave time" we cannot agree with their findings. We have controls in place to review on a monthly basis checking employees benefit time. Department heads send a monthly report to the Human Resource department and that report is checked against payroll records.

See
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Again we find the Comptroller's report inaccurate when it says an employee earned additional vacation time in the middle of the year. We post vacation time in January; we do not do mid-year adjustments. The time the employee accrues for vacation in the prior year is posted in January of the following year. Employees remain active in the system because if we deactivate them and they had earnings in the current year, the system will not produce a W2 because they are inactivated. So if an employee retired in the end of 2010 but their final check was paid in 2011 they must remain active for the year to produce a W2. We did find out after talking to the software company, there are several areas where you must

enter a termination date to remove employees from the active file. This would explain why retired or terminated employees remained on the reports.

In conclusion we have checks and balances in place so employees are not overpaid. We have made software changes to address the deactivation of employees and tighten up controls on submitting time sheets to payroll. We also have a "lock on benefits" no one can override or change other than human resources and payroll.

We previously reconciled all accruals on an annual basis we will step it up to a quarterly basis. We are currently implementing a written policy establishing a standard operating procedure for balancing benefit accruals.

Sincerely,

A handwritten signature in cursive script, appearing to read "Charles Emberger".

Charles Emberger

City Comptroller

APPENDIX B

OSC COMMENTS ON THE CITY'S RESPONSE

Note 1

The City's response indicates that sick time is accrued monthly, compensatory time is accrued when earned, and that vacations are posted at the beginning of the year. However, this does not address the audit finding. We identified employees who had negative vacation, sick and personal leave balances on the employee benefit report as of June 21, 2011. The concern is not when leave time is credited to the accounting records; it is that some employees use their leave time faster than they earn it based on the terms of the City's personnel policy or collective bargaining agreements.

City officials also indicate that if an employee were to retire mid-year, the vacation time (credited for an entire year) would be prorated downward to correspond to the amount of time during the year that the employee actually worked. Again, this does not address the audit finding. Contrary to the City's response, our report did not identify concerns with employee pay outs at retirement, or the impact of employees taking vacation the last week of the year before the accrual was posted to the accounting records. Our audit found that the City did not monitor accrual usage and balances to ensure employees did not receive leave time benefits to which they were not entitled. The findings in our report are based on the employee benefit report provided by the payroll clerk as well as employee records maintained by the Human Resources Department.

Note 2

We met with City officials during the audit and provided them with specifics on our findings. We also met with them at the end of the audit and provided them with our findings and spreadsheets including the names and discrepancies for each of the employees, and the balances identified on the employee benefit report provided by the payroll clerk. We conveyed our findings, in detail, using the leave time categories as defined by City officials.

Note 3

City officials represent that the Department heads send monthly reports to the Human Resources Department and that the Human Resources Department checks the reports against payroll records. This control, if performed, was not effective because it did not detect the discrepancies between the records kept by the Human Resources Department and the records maintained by the payroll software that we discussed in the report.

Note 4

The report indicates that the employee should have had a negative balance of eight hours because he had earned 16 hours of vacation time that had not been entered into the system. The employee cited left the City in September 2009, nearly two full years prior to the conclusion of fieldwork. Furthermore it is makes no differences whether he was supposed to be credited with vacation time at

the start of 2009, or credited with vacation time earned during 2009. All time earned was supposed to be entered into the system by September 2009, which it was not. All time still had not been entered into the system through June 3, 2011.

Note 5

Twenty-three of the 33 employees identified left the City prior to January 1, 2010 and, therefore, should have been deactivated early in 2011 after the W-2s were produced, given the software weakness that existed at the time. The remaining 10 employees retired during 2011 but were still active due to the same software weakness which could have resulted in them receiving payments to which they were not entitled. We commend City officials for making the software changes necessary to address this control weakness.

APPENDIX C

AUDIT METHODOLOGY AND STANDARDS

Our overall goal was to assess the adequacy of the internal controls put in place by officials to safeguard City assets. To accomplish this, we performed an initial assessment of the internal controls so that we could design our audit to focus on those areas most at risk. During the initial assessment, we interviewed City officials, performed limited tests of transactions, and reviewed documents such as City policies and procedures, Council minutes, and financial records and reports.

After reviewing the information, we determined where weaknesses existed, and evaluated those weaknesses for the risk of potential fraud, theft and/or professional misconduct. We then decided upon the reported objective and scope by selecting for audit those areas most at risk. We selected leave accruals for further testing. We performed the following procedures:

- We interviewed officials to gain an understanding of the internal controls over leave accruals.
- We reviewed City policies and collective bargaining agreements to identify how accruals were earned by employees.
- We reviewed Human Resources records and payroll records and reports to determine if the accrual information maintained by the Human Resources Department matched the information maintained by the Payroll Department
- We reviewed employee accrual information to determine if employees were paid, or could be paid, for leave time to which they were not entitled, and if they received the leave time to which they were entitled.

We conducted this performance audit in accordance with generally accepted government auditing standards (GAGAS). 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 objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

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Steven J. Hancox, Deputy Comptroller
Nathalie N. Carey, Assistant Comptroller

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