



**August 8, 2012**

**To:** Finance and Administration Committee  
**From:** Will Kempton, Chief Executive Officer  
**Subject:** Orange County Employees Retirement System: Review of Orange County Transportation Authority Payroll Transmittals

**Overview**

The Internal Audit Department of the Orange County Employees Retirement System has completed a review of the Orange County Transportation Authority's payroll transmittals. The audit found that the Orange County Transportation Authority has generally adequate controls to ensure complete, accurate, efficient, and timely transmittal of payroll data. Two recommendations were offered. Management has responded, and the Orange County Transportation Authority Internal Audit Department agrees, that implementing these recommendations does not add value or enhance controls.

**Recommendation**

Receive and file an audit completed by the Internal Audit Department of the Orange County Employees Retirement System: Review of the Orange County Transportation Authority Payroll Transmittals.

**Background**

The Orange County Transportation Authority (OCTA) is one of fifteen plan sponsors that submit employer and employee payroll contributions, as well as member information, to the Orange County Employees Retirement System (OCERS) for administration of its pension fund.

Despite the planned implementation of a new pension administration system next year, OCERS Internal Audit Department (OCERS Internal Audit) notified OCTA of their intent to perform an audit of the current process for OCTA payroll transmittals.

The audit was conducted and results were presented to staff at an exit meeting held on July 17, 2012. Subsequent to the exit meeting, additional audit

fieldwork was conducted and the draft report was revised. A final report was forwarded to OCTA on July 24, 2012.

### ***Discussion***

OCERS Internal Audit tested 40 of 113 pay periods between January 2008 and April 2012 for accuracy and completeness and found no exceptions. In addition, OCERS Internal Audit tested 200 member records of OCTA employees to determine if payroll data for these employees was transmitted accurately and completely. Again, no exceptions were noted. Finally, OCERS Internal Audit assessed the adequacy of internal controls at OCTA to ensure the accuracy of biweekly payroll data and found these to be effective; however, two recommendations related to documentation were offered.

OCERS Internal Audit recommended that OCTA payroll staff provide additional evidence of their review of bi-weekly transmission data and retain the evidence for one year. Management disagreed with the recommendation and explained that the validity check being performed was initially developed to ensure accurate reporting after implementing the payroll system in 2004. Since that time, staff has continued to perform the system validity check on a bi-weekly basis; however, no error has ever been identified, and the system continues to operate accurately. In addition, OCTA management pointed out in their response that both the transmitted file data and the validity check can be replicated.

In addition, OCERS Internal Audit recommended that OCTA payroll staff maintain a record of the exceptions and related resolution of those exceptions that appear on a report that is generated from the OCERS Pension Gold system. The observation points out that OCERS' staff maintains a record of the exceptions noted and the disposition of those exceptions. In some cases, OCERS' staff will forward to OCTA staff a Notification of Change in Member Account to authorize a change to the OCTA payroll system. In those instances OCTA maintains the authorizing document in the respective employee file. OCTA management responded that maintaining a duplicate log of OCERS' system exceptions and resolutions would not add value or controls to the current process.

OCTA's Internal Audit Department has reviewed the observations and recommendations by OCERS Internal Audit and agrees with OCTA's management responses.

***Summary***

The OCERS Internal Audit has completed a review of OCTA's payroll transmittals. The audit found that OCTA has generally adequate controls to ensure complete, accurate, efficient, and timely transmittal of payroll data. Two recommendations were offered. Management has responded, and OCTA's Internal Audit Department agrees, that implementing these recommendations does not add value or enhance controls. The detailed audit scope and results are included in the audit report at Attachment A.

***Attachment***

- A. Review of OCTA Payroll Transmittals by the Orange County Employees Retirement System Internal Audit Department

**Approved by:**



---

Janet Sutter  
Executive Director, Internal Audit  
714-560-5591



## **Review of OCTA Payroll Transmittals**

**Report Date: July 24, 2012**

### **Internal Audit Department**

**Director of Internal Audit: David James, MBA, CPA, CIA**

**Temporary Internal Auditor: Vinh Pham, CPA**

**Orange County Employees Retirement System**  
**Internal Audit Department**  
**Review of OCTA Payroll Transmittals**  
**July 24, 2012**

**Table of Contents**

Conclusion.....	1
Objective, Scope, and Methodology.....	1
Background.....	2
Discussion.....	4
Observations, Recommendations, and Management Responses.....	6

## **Conclusion**

The Internal Audit Department (Internal Audit) has completed an independent review of the procedures for transmitting and processing payroll data between Orange County Transportation Authority (OCTA) and Orange County Employees Retirement System (OCERS). Based on the review, Internal Audit has determined that OCTA has adequate controls to ensure complete, accurate, efficient and timely transmittal of payroll data to OCERS. Also based on the review, Internal Audit has determined that OCERS has adequate controls in place to prevent inaccurate or erroneous data from being imported into its pension administration system, Pension Gold. Internal Audit has recommendations for OCTA to 1) increase the retention period of records pertaining to its review of transmittal file data, and 2) improve the documentation regarding the resolution of exceptions noted by OCERS during the transmittal process.

## **Objective, Scope, and Methodology**

The objective of the review was to determine the completeness, accuracy, efficiency, and timeliness of the processes for transmitting and processing OCTA payroll data between OCTA and OCERS. The scope of the review included pay periods between January 2008 and April 2012. The methodology included, but was not limited to, the following:

- Review of OCERS policies and procedures for the payroll transmittal process.
- Interviews of management and staff of OCERS and OCTA involved in the payroll transmittal process to obtain an understanding of the process in place, identify existing controls, and determine the efficiency of the process.
- Review of a sample of transactions in OCTA payroll data files transmitted to OCERS and other pertinent payroll records to verify controls in place and determine the completeness, accuracy, and timeliness of the process.
- Review of a sample of records in Pension Gold to verify controls in place and determine the accuracy of data imported into the OCERS pension administration system.
- Reconciliation of a sample of records between the OCTA payroll system and OCERS Pension Gold to determine the completeness and accuracy of OCTA payroll data in Pension Gold.

We planned and performed this review to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our review objectives. We believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our review objectives.

## Background

OCERS provides retirement, disability, death, and survivor benefits to its members in accordance with the County Employees Retirement Law of 1937. OCTA is one of fifteen plan sponsors that submit employer and employee contributions and other pertinent members' information and payroll data to OCERS for the administration of its pension fund.

OCTA is a multi-modal transportation agency serving Orange County. OCTA, which began in 1991 with the consolidation of seven separate transportation agencies, directs countywide bus and paratransit service, Metrolink rail service, the 91 Express Lanes toll facility, freeway, street and road improvement projects, motorist aid services, and regulation of taxi operations.

### Payroll Transmittals

The communication of biweekly payroll data between OCERS and OCTA must be complete, accurate, efficient, and timely. The calculation of employee and employer contribution amounts, pension amounts, and funding of future liability by OCERS are dependent on members' information such as years of service, age, and pensionable earnings. Therefore, it is crucial that members' information and payroll data are accurately recorded in the pension administration system.

Every pay period, the fifteen plan sponsors electronically transmit files to OCERS that contain active members' payroll data. The transmittal file layout contains information such as members' pensionable salary rate, employee and employer contributions for the pay period, and the status of the member (active, inactive, on leave). OCERS Information Technology (IT) staff downloads and reviews the transmittal file for data integrity.

For 2010, OCTA's employer contribution was over \$16 million, and its employee contribution was over \$8.5 million.

There are two plans for OCTA employees (Rate Group #5):

Tier	Plan	Number of Members
Tier 1	Plan A – 2%@57 – 1 year monthly pay	55
Tier 2	Plan B – 1.667%@57-½ – 3 year monthly pay	1,492

The employee contribution rates vary depending on the entry age of the member, with the contribution rates increasing as the entry age increases. For example, for Plan B the rate for entry age 21 is 6.20%, and the rate for entry age 45 is 9.72%.

OCTA's employer contribution rate has increased during the review period as follows:

<b>Effective Date</b>	<b>Normal Contribution</b>	<b>UAAL</b>	<b>Employer Contribution Rate</b>
7/1/11	11.11%	9.28%	20.39%
7/1/10	11.32%	5.94%	17.26%
7/1/09	11.26%	3.76%	15.02%
7/1/08	11.25%	4.77%	16.02%
7/1/07	11.36%	3.60%	14.96%

### **OCTA Biweekly Payroll and Transmittal Process**

OCTA uses the Lawson / Infor software for its payroll (ERP) system. On a biweekly basis, OCTA runs its payroll, calculating the gross pay, pensionable pay, and contribution amounts according to formulas provided by OCERS. After payroll closes, OCTA creates a transmittal file with that pay period's employee information regarding contributions and other employee data. OCTA queries their database for total liability of employee and employer, buyback, total subject wages, pensionable hours, including sick leave, and compares these control totals to those in the transmittal file. OCTA includes premium pay items in its transmittal for inclusion as part of pensionable pay. OCTA then sends the encrypted file to OCERS.

The employer contributions are prepaid by OCTA at the beginning of each calendar year for use in the upcoming fiscal year. OCERS Finance staff and OCTA track the prepayment balance. OCTA is in contact with OCERS staff periodically throughout the fiscal year to ensure the prepaid balance agrees with what OCERS has on file. OCTA has had sufficient funds in the prepaid account to cover the expected employer contribution during the review period.

Each pay period, OCTA transfers employee contributions to OCERS' bank account within five days from the end of the pay periods and is considered timely. OCERS Finance staff verifies that the contribution amounts on OCTA payroll reports match the contribution amounts recorded in OCERS' pension administration system on a biweekly basis. OCERS Finance staff also performs a biweekly reconciliation of OCTA payroll reports to amounts received at the bank.

### **OCERS Biweekly Payroll / Transmittal Import Process**

Data transmissions are encrypted for protection during the file transfer process from OCTA to OCERS. The encrypted files are transmitted to OCERS using File Transfer Protocol process software. OCERS IT downloads the files' data into Pension Gold using a process that checks for data exceptions.

Some exceptions are "fatal" such as incorrect salary and contribution amounts, and they must be resolved before the transmittal can be processed. Other exceptions are "informational" such as new members not yet inputted to OCERS' system, excess of 80 hours worked, birth date, and social security number. Pension Gold generates an exception report listing the "informational" exceptions. OCERS Member Services staff



works with OCTA staff to resolve these exceptions, and corrections are made in the next pay period's transmittal. Member Services management reviews a Change Report generated by Pension Gold whenever a change or correction is made in the system.

## **Discussion**

OCERS IT and Member Services divisions have adequate procedures in place to effectively detect and correct possible exceptions transmitted to prevent inaccurate member data, payroll data, and contribution amounts from being imported into the OCERS pension administration system. These procedures also include effectively communicating with OCTA Payroll staff to make adjustments to data as needed.

OCTA has effective internal controls in place to ensure a review of biweekly payroll data before transmittal to OCERS. However, we have made some recommendations to improve the documentation of the process in the section "Findings and Recommendations" below.

### **Completeness and Accuracy of Employee Payroll Records**

In our testwork of completeness of employee payroll records, no exceptions were noted. We randomly selected 40 pay periods out of 113 from the review period of January 2008 to April 2012. This gave a 95% confidence level with a 5% sampling error rate. We traced key data in Pension Gold such as total number of records in a pay period, employer contribution rate used, subject wages, employer contributions, and employee contributions to various source records for accuracy and completeness.

### **Member Records Testwork**

We tested 200 OCERS member records of OCTA employees to determine if the payroll data for individual employees were transmitted accurately and completely to the Pension Gold system. This randomly selected sample size gave a 95% confidence level with a 5% sampling error rate that our results reflected the population of 192,000 records. We used records from transmittal files received by OCERS from OCTA during January 2008 to the April 2012, OCTA payroll records, and information in OCERS' pension administrative system. We compared key information that affects the contribution amounts, verified contribution rates, and recalculated contribution amounts.

It is not unusual for transmittal files to contain some data that were different than expected, but the variances were consistently identified in the data verification performed by OCERS staff using Pension Gold. The variances were noted and resolved. We found that OCERS records from the transmittals were substantially accurate and complete.

## **Transition to the V3 Pension Administration System**

In late 2013, OCERS is scheduled to transition (go live) from Pension Gold to the V3 pension administration system. The current process of plan sponsors transmitting payroll data to OCERS will also change significantly with the new system. With the new system, the plan sponsors will be required to take a more active role in the biweekly transmittal process. Instead of simply transferring the transmittal files to OCERS IT staff, plan sponsors will access the V3 system via the internet and directly submit their biweekly payroll information and adjustments to V3. The new system will generate exception reports that will be used by the plan sponsors to make adjustments to their submitted records as needed. The plan sponsor cannot release data into the V3 system until they have cleared all exceptions. With the new process, more staff time may be required by OCTA and other plan sponsors to correct data exceptions in a timely manner.

OCTA Payroll staff and OCERS staff have held meetings to prepare for this transition to the new system. Plan sponsor have been given the specifications of the new file format so they could submit a test transmittal file to OCERS.

Prior to the implementation of the new transmittal process, OCTA and OCERS should continue to communicate regularly to ensure clear understanding of the new procedures and a smooth transition to ensure accurate, complete, and timely payroll data submissions under V3.

## **Observations and Recommendations**

### **Observation #1: OCTA Transmittal File Review**

According to OCTA, after it completes its download of biweekly payroll data generated from Lawson / Info to the transmittal file, a Payroll staff member reviews the file for completeness and accuracy of the data prior to submitting the file to OCERS. We observed that there were tick marks on the transmittal summary reports as evidence of such review. OCTA retains those reviewed reports for six months after the data have been transmitted to OCERS.

### **Recommendation #1:**

We recommend that the records of this review of transmittal files prior to their submission be retained for at least one year. Because OCERS submits data to the actuary on a yearly basis, it would be prudent to retain these reports for one year in case OCERS and OCTA need to reconcile any discrepancy or exception during the actuarial reporting process.

Additionally, management should consider enhancing its documentation of the review being performed of the transmittal file prior to their submission to OCERS by noting the signature, date, and description of tick marks on the transmittal summary report for a clearer evidence of if, when, and by whom such procedure was performed for a better audit trail.

### **OCTA Response**

OCTA believes that its current practices are adequate to ensure that information transmitted to OCERS is complete and accurate. OCTA staff developed the query to validate numbers in the transmission file as part of its Lawson Payroll System implementation in 2004. Since that time, no error has ever been identified in the OCERS' transmission file.

If a discrepancy or error must be reconciled during OCERS actuarial reporting process and more than six months has elapsed, OCTA's payroll system is able to replicate the transmittal file and the balancing query that was run."

### **Comments on the OCTA Response**

As stated in the "Conclusion" section of this report on page 1, Internal Audit concurs with OCTA that it has adequate controls to ensure complete, accurate, efficient, and timely transmittal of payroll data to OCERS. The fact that no error has been identified in the transmittal files during our review period is an indication that OCTA has adequate controls in place.

We concur with OCTA's response that its payroll system is able to replicate the transmittal file should there be a discrepancy or error that must be reconciled beyond the six-months record retention period, and that there is a mitigating control in place to address such potential occurrence. We believe that extending the record retention period by six more months will be an enhancement to a control that is already in existence. As stated above in our recommendation, doing so would add to the audit

trail since the original document would include hand-written notes or documentations made during the initial reconciliation process that the recreated document may not provide, and may facilitate an easier and more expedient error resolution. We believe the added benefit to OCERS outweighs the additional administrative duties this would impose upon OCTA and would not require OCTA to significantly amend its current process should OCTA choose to implement our recommendation.

## **Observation #2: Exceptions Log**

Pension Gold generates an Exception Report when the transmittal file is imported from OCTA. The Exception Report lists “informational” exceptions that require correction. OCERS notifies OCTA of the exceptions that need to be researched.

In certain cases when OCERS makes corrections to an employee’s records, OCERS sends to OCTA a form “Notification of Change in Member Account,” which OCTA includes in their employee’s records. OCTA does not maintain a log of the exceptions.

OCERS maintains a log of these exceptions and their resolutions. We reviewed a sample of transactions on OCERS exception logs and found that all exceptions were resolved.

## **Recommendation #2**

We recommend that OCTA create a log of exceptions notified it by OCERS by also including the resolution of each exception to ensure that all exceptions have been properly corrected in its records. Maintaining such an exception log would allow OCTA management to identify any systemic problems, patterns of exceptions, root causes, and help ensure that all necessary corrections are being made to their records. Although OCERS maintains their own log of exceptions and their resolutions, OCTA should also maintain a similar log because the some of the necessary adjustments need to be posted by OCTA. We believe taking this additional step would help further ensure that data transmitted to OCERS are accurate and complete, and allow OCERS to best serve OCTA and its employees.

## **OCTA Response**

OCTA does not believe that maintaining a mirror image of the OCERS’ error log and adding a notation of the resolution adds any value or control to current processes. The types of errors identified in the log are not of a systemic nature. The errors that require correction by OCTA are specific to issues related to rehires that have cashed out their OCERS accounts and employees who require new contribution rates due to reciprocity. If for some reason a correction was not made, it would continue to appear on OCERS’ exception log in following pay periods until the correction is made. Documentation of the resolution is maintained in the respective employee’s personnel file.

## **Comments on the OCTA Response**

We concur with OCTA that the types of exceptions noted above require correction by OCTA. We note that there are other types of exceptions that occur regularly, such as, an employee’s status needing to be changed from “active” to “active on leave” when salary and contribution amounts are \$0; and when an employee reports over 80 hours

in the period with excess of 80 hours needing to be reclassified to pay items such as unscheduled overtime, scheduled overtime, travel time, etc.

We concur with OCTA that an error not corrected would continue to appear on OCERS' exception log. Although it serves as a mitigating control, we believe having a mechanism in place to track the total population of exceptions, for example, a log, would provide a greater assurance that an error does not go uncorrected. If OCTA maintained its own log of exceptions, their resolution would be an enhancement to the detective controls that are already in place in OCERS' pension administration system and its exception resolution process by providing another layer of controls to complement the existing systems controls should OCTA implement our recommendation.

With the changes in the payroll transmittal process that would occur with OCERS' planned implementation of a new pension administration system, V3, in late 2013 as discussed on page 7 of this report, we believe that OCTA maintaining its own log of exceptions would be moving toward the new direction of the plan sponsors having to take a more active role in the biweekly transmittal and exception resolution processes.