



**Internal Audit Report**  
**Payroll Follow Up**  
**Date: June 2018**

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### Background and Context

Payroll is a key financial system and subject to annual audit review – as a minimum through key control testing. Payroll delivery is managed by the Council through LCC People Management.

There have been significant issues with Payroll since the implementation of Agresso in April 2015, and whilst there has been rectification work and improvement, problems that impact on pay and GL posting accuracy continued into 2017/18. The audits completed on Payroll, HR Admin and Pension Contributions during 2015/16 and 2016/17 all received a **Low Assurance** opinion.

In June 2017 following the completion of the 2016/17 payroll audit, a decision was taken by People Management and Internal Audit to issue the draft audit report to Serco but not to seek a detailed management response and immediate action to address the recommendations made on system functionality and the control environment. It was agreed that Serco's priority had to be a number of other projects including Pay Statements and the upgrade to Business World On. An update on progress with implementing all outstanding management actions was received from the Serco People Service Manager on 21 December 2017, and since that date Serco has held regular meetings with LCC People Management to monitor and agree progress in addressing the points raised in our draft report.

In October Serco appointed an experienced Payroll & Pensions Manager, who commenced in role from 6<sup>th</sup> November and has led work to more clearly define and improve processes and document controls within Serco's Payroll function. Consultants have also been engaged to progress a number of work 'packages' and some fixes to system configuration have already been made. Rectification work continues into 2018/19 in agreement with LCC People Management.

In parallel to Business as Usual, the work to identify and address the pay, pensions and general ledger errors that occurred in 2015/16 and 2016/17 continues in the Pay Statement project. Given the delays, this work has also been extended to cover 2017/18 payments. During this 3 year period, 2020 overpayments have been identified: £1.122m has been recovered and £564k remains

outstanding. A protocol has been agreed between the Council and Serco on the recovery of outstanding overpayments for 2015/16 and 2016/17.

During 2018/19 Internal Audit plans to undertake counter fraud work on salary overpayments using data analysis techniques.

Two other key projects have been in progress to address issues from payroll reports: the variable payments project has concluded leaving agreed exceptions that need further work – including a more robust solution to entering Retained Firefighter payments. At present we understand the Starters, Movers, Leavers' project is currently on hold pending the outcome of Serco's 'Operational Excellence' review over a number of people management projects. The outcome is expected in June 2018.

### Scope of Work

It is known that progress to address control issues and payroll system functionality has been impacted by priority given to other projects during 2017/18. The focus of our audit review has therefore been to follow up, evidence and evaluate the implementation of management actions on outstanding recommendations from the audit reports issued since 2015.

In seeking to provide assurance from our follow up work we have considered the following potential risks:

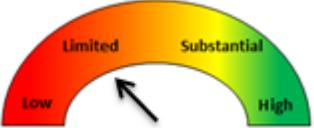
- Staffing resources are insufficient; do not have the necessary skills, knowledge, training or guidance
- Exception reporting to detect payroll errors is not effective
- System access permits improper use
- Overpayments are incomplete / inaccurate or not recovered
- Additions / Changes to employee data are fraudulent or incorrect
- Advances are not recovered
- Payments to employees are fraudulent or incorrect
- Third party payments / deductions and information is not provided to statutory agencies as required

## Background and Scope

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We utilised data analytics to identify a sample of pay and expense claims and allowances that had not been approved through workflow (manager authorisation within Business World On) for substantive testing.

## Executive Summary

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|  | <h3>Limited Assurance</h3> <p><b>Our critical review or assessment on the activity gives us a limited level of confidence on service delivery arrangements, management of risks, and operation of controls and / or performance.</b></p> <p><b>The controls to manage the key risks were found not always to be operating or are inadequate. Therefore, the controls evaluated are unlikely to give a reasonable level of confidence (assurance) that the risks are being managed effectively. It is unlikely that the activity will achieve its objectives.</b></p> |
|---|--|

| Risk   | Rating (R-A-G) | Recommendations |           |
|--|----------------|-----------------|-----------|
|  |                | High            | Medium    |
| Staffing resources are insufficient, do not have the necessary skills, knowledge, training or guidance | Medium         | 1               | 0         |
| Exception reporting to detect payroll errors is not effective  | Medium         | 0               | 2         |
| Systems access permits improper use  | Medium         | 0               | 1         |
| Overpayments are incomplete / inaccurate or not recovered  | Medium         | 0               | 1         |
| Additions / Changes to employee data are fraudulent or incorrect                                       | Medium         | 0               | 3         |
| Advances are not recovered   | Low            | 0               | 0         |
| Payments to employees are fraudulent or incorrect  | High           | 7               | 8         |
| Third party payments / deductions and information is not provided to statutory agencies as required    | Medium         | 0               | 2         |
| <b>TOTAL</b>   |                | <b>8</b>        | <b>17</b> |

## Executive Summary

### Key Messages



Our discussions and testing performed has demonstrated some level of improvement in Payroll processes and controls particularly since December 2017. In February 2018 there were 157 open management actions in relation to previous audit reports. 58% have now been closed and of the remainder 16% individual actions are addressed by the Pay Statements project.

The impact of the new Payroll and Pensions Manager is visible. He has worked with the team to introduce strengthened payroll processes and controls and continues to do so, resulting in improvements in the payroll control environment. The improvements observed include:

- more detailed and consistent checking arrangements
- completion and signing of monthly payroll check lists
- the detailed recording of overpayments
- checking on maternity and sickness cases
- reporting to detect potential errors in pension deductions
- greater focus on staff training and improved staff retention

In the last few months there have also been system configuration improvements (to address 19 reported issues ready for 2017/18) and since April 2018 the introduction of additional 'workarounds' and reporting to detect issues in activities where errors are known to occur.

At the time audit work was completed many of the improvements visible had only been in place for a short time and we therefore did not have the opportunity to review sufficient months' evidence of revised process and controls in practice. Further review over these process improvements and workarounds is planned and it is essential that Serco continue in the positive direction that is now visible in order to continue to improve the payroll control environment and overall assurance. Given

## Executive Summary

### Key Messages



the improvement in control design our assurance opinion has moved to **Limited Assurance**.

The majority of issues reported previously impacted on employee pay and pension contributions. These errors were to be more fully identified and corrected through the 'Pay Statements' project. There have been significant delays in delivery of this project and changes to the planned outcomes. The Council and Serco have defined governance arrangements in place and need to continue to work together positively to drive this project to a conclusion. It is essential that employee underpayments, overpayment recovery plans and rectification through the ledger and with pension providers are completed in this financial year to protect the integrity of Business World On going forward. This also applies to the work on Equated Pay that People Management is currently scoping with Serco.

Whilst improvements have been made there remain a number of areas where work is still needed to address the issues raised in audit reports. The key points include:

**Access:** there are outstanding recommendations relating to system access within the HR / Payroll and Support teams to ensure adequate segregation of duties is in place. Recently there have also been wider questions around access to employee information. At present we understand there is a review ongoing that includes all access to and roles in Business World On. This review needs to ensure that the arrangements for Serco operational and support teams are appropriate and that other access is compliant with Data Protection requirements.

**Exception reporting:** Prior to December 2017 there was no evidence of any review of items on exception reports. This has since been introduced but spot quality checks performed by the Payroll & Pensions Manager still need to be evidenced. The system Error and Warnings report is still not user friendly and includes unnecessary items. Serco need to look at the value and relevance of the Errors

## Executive Summary

### Key Messages



and Warnings report entries and checks performed to identify whether there are other areas which might provide increased value.

Additional exception reports have been introduced to identify issues which can lead to errors in Local Government Pension Scheme (LGPS) deductions. Review of these reports highlighted occasions where pension deductions were still incorrect (missing months / incorrect schemes on employee records). Serco management need to ensure that the full impact of entries on these reports is considered when the teams complete checks. We recommend management complete spot checks on all pension reports used to detect potential errors to confirm that any issues have been dealt with fully and correctly.

**Management of overpayments:** The layout of the Overpayment Tracker has significantly improved with more information recorded and supporting documentation retained on file. It shows that during the 3 years from April 2015 to March 2018 2020 overpayments were identified of which £1.122m has been recovered and £564k remains outstanding.

The Tracker is reported to LCC People Management each week, however during the audit we identified a second tracker (from February 2018) which was not being reported. This includes numerous overpayments where recovery action is not yet in progress (including £56,133 from April & May 2018). The two documents should be combined to provide a complete and single picture. LCC People Management and Serco need to urgently agree an approach to these overpayments, specifically where these have occurred in 2017/18 and 2018/19. Without prompt action there is a risk that overpayments will not be recovered.

There was no evidence that checks had been performed by the senior payroll administrators /

## Executive Summary

### Key Messages



manager on the accuracy of overpayment calculations included in the Tracker. As there have been errors historically, it is important that a validation check is completed and evidenced.

**Starters / Movers / Leavers (SML):** Some of the previous findings were due to be addressed by the SML project, but this has been put on hold at present pending review of People Management projects by Serco. If the SML project is not completed the Council and Serco need to ensure appropriate controls are in place, including

- Evidence of appropriate management authorisation
- Completion of Position fields needing to be mandatory on forms,
- Cross checks to be performed between HR starters and leavers and Payroll for completeness assurance,
- Leavers with multiple positions of employment or zero hours contracts being identified to allow payroll to only close down the correct positions

**Maternity pay calculations:** review of a sample of maternity cases identified that employees have not been receiving the increases to the Statutory and Occupational payments that they are entitled to when there is a pay increase due to a pay award or increment that occurs when they are on maternity leave. We also identified occasions when back pay had been incorrectly processed as if the employee were at work. Payroll staff needs to be provided with clear guidance on requirements to review and recalculate payments when pay increases occur and we suggest this is built into the timetable of annual tasks alongside pay awards. New forms have been introduced for maternity calculation and management need to ensure these fully evidence second checks on calculations as well and for input to Business World On.

**Sickness absence payments:** the team has introduced manual workarounds to monitor and check

## Executive Summary

### Key Messages



long term absences, including since February 2018 a more proactive approach utilising the Absence Transfer report to identify employees affected. Manual calculation is still required to check long term absences as the system does not always pay correctly and does not assess teachers' sickness entitlement in accordance with their scheme. We also established that the approach taken to manual calculation of SSP still differs from that built in Business World On and local terms and conditions. At present there is no second check on these calculations – we recommend that at least a sample check is completed to confirm accuracy and compliance with conditions of service.

Overpayments are still being generated by delays in managers and schools entering sickness absences into Business World On. This also impacts on reporting of sickness absence statistics. The Council and Serco need to continue to work on ways to reinforce the message on the importance of the timeliness of absence entry and the impact this has.

**Teachers' Pensions:** we have previously reported that in some circumstances the requirements of the Teachers' Pension scheme are not been applied correctly (% banding applied where there is back pay or a reduction in pensionable pay due to sickness or maternity absence). Whilst we understand work is in progress to test a system fix for back pay, there is no manual 'workaround' in place at present and pension deductions are not checked / adjusted for this issue when processing maternity and long term sickness absences. Additional checks need to be introduced in these cases if there is to be assurance that pension contributions taken in 2018/19 are correct.

**Monthly reporting to West Yorkshire Pension Fund (WYPF):** discussion determined that manual intervention is still necessary to provide all the details required on the Contributions report to WYPF on the LGPS each month. This creates significant work and introduces an increased risk of error. Serco should look to engage expertise to review and revise the Contributions report to minimise the manual work involved.

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### Key Messages



**Payslips:** Improvements are needed to employee payslips to ensure employees are able to confirm their payments and deductions (particularly for multiple jobs) are correct and data included is complete. Serco and LCC People Management need to agree a timescale for this work as the current payslips will not meet statutory requirements from April 2019.

## Executive Summary

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### Areas of Good Practice



There are a number of areas where improvements have and continue to be made in the processes and controls for HR Admin and Payroll:

- An initial staff skills review was completed by the previous Interim Payroll Manager and is to be reviewed by the current Payroll & Pensions Manager. Training needs have been identified through this assessment and appraisals. Training Plans are to be finalised early in 2018/19 and training has already been arranged / delivered through team meetings, sessions delivered by subject experts (e.g. HR Advisors) and professional bodies including the Chartered Institute of Payroll Professionals (CIPP). The two senior payroll administrators are now studying for CIPP.
- Basic reports have been built on Amendment Logging to allow the HR / Payroll Business World On Support team to review system changes. These include changes to the resource master file and show what changes have been made, when and who by. The reports are used to review and investigate changes where issues / errors have occurred and to share learning.
- Improved consistency, coverage and timeliness of checks over the Errors and Warnings report performed since December 2017. Other reports have also been introduced / utilised more consistently to detect potential errors and highlight these for correction
- Introduction of comprehensive monthly payroll check lists which are signed off by the Payroll & Pensions Manager.
- Workarounds have been introduced for calculating, checking and amending maternity and sickness absence payments where errors are known to occur

## Executive Summary

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### Areas of Good Practice



- The Variable Payments project has identified agreed exceptions to self-service for pay and expense claims. The self-service message for other users, including schools has been reinforced. The Payroll & Pensions Manager has confirmed that either he or Payroll Seniors screen any manual claims received.
- For schools no amendments to pay will be processed without the approval of the Headteacher. Schools have access to Gross Pay and Employee Costs reports to check payroll payments each month
- Information included within the record of overpayments is more comprehensive, including the cause of the error and detailed supporting documents and forms are now held on file for all overpayments processed
- A sound process is in place for making and recovering pay advances and the sample we tested had all been recovered through payroll
- Payroll is now reconciled to the monthly HMRC Real Time Information submission and the Finance Team reconciles payroll and the general ledger each month.

We would like to thank staff in Serco Payroll and HR Admin teams and LCC People Management for their time and assistance during the audit.

## Executive Summary

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### Managing your risks



During our audit we identified one risk that should be considered for inclusion in your service Operational Risk Register:

- payments to employees are fraudulent or incorrect

## Management Response

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### Management Response



#### **Serco Management Response:**

This is a fair audit and we thank you for your support to work in partnership to produce the action plan for the Internal Audit report. It is encouraging to see that the assurance has moved from "low" to "limited" in recognition of the improvements made during the last 12 months. The aim is for the Council and Serco partnership to achieve "substantial" assurance in September 2018.

We would like to make the following points:

**Process improvements ready for re-test:** a number of process improvements were completed and 3 months evidence available for testing. Audit will be re-testing August 2018.

**Variable payments project:** whilst concluded in its previous format, this is ongoing as a Variable Pay Joint Working Group. The Council require some manual payments to continue in respect of Music Support, and School Crossing staff. The partnership aim is to ensure that all Council claims are submitted electronically, to mitigate against fraud and manual errors, the continued support of the Council to achieve this would be welcomed. The working group are currently discussing with the Council an alternative solution to entering Retained Firefighter payments. Continued manual entry into the HR system is resource intensive and we will be raising this shortly for discussion with the Council.

**Access review:** Access to BW ON! is owned by the Council Finance department, we welcome the access review and look forward to working with the Council to achieve "adequate segregation of duties" via revised access controls.

**Management of overpayments:** From April 2017 obvious overpayments continued to be recovered in

## Management Response

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### Management Response



agreement with line managers. The Council instructed Serco in December 2017/January 2018 not to recover any overpayments (except in cases where the employee wished to make payment) until the outcome of the Pay Statement project was known. A separate tracker was created to record overpayments that were "on stop" in respect of recovery. On 8<sup>th</sup> June 2018 the Council communicated to Serco that recovery of overpayments could proceed, immediately following this Serco merged the ongoing and "on stop" overpayment trackers, this is provided to the Council on a weekly basis.

**Sickness absence payments:** A high percentage of errors occur as a result of managers not entering data in the HR system in a timely manner. Serco have produced statistics on the scale and nature of "dirty data" and this is expected to be presented to CMB during July 2018. Serco will work with the Council to provide information that will enable the Council to communicate with managers the importance of entering data correctly and on time into the HR system. By working together as a partnership we will be reviewing the HR Hierarchy build which will improve access by the Manager to team data.

**Pension reporting:** Serco have engaged expertise to review and revise the pension reports. The review commenced June 2018.

An action plan based on all other audit recommendations has been formulated and Serco will be pressing forward to address all of the points raised.

In the meantime we look forward to working with you progressively through to our target date of September 2018 and I would ask that this is given some priority by the Council.

### Management Response



#### LCC Management Response

The Council Management accepts the findings of the Audit Report. As outlined in the Serco response, the aim is for the Council and Serco partnership to achieve "substantial" assurance in September 2018 through improvements in the payroll control environment. This is the single highest priority for the People Management Service.

The Council Management is committed to ensuring resources are allocated to enable the necessary governance and oversight that the identified improvement actions in this report are implemented in a timely way. In particular the continued focus to ensure the satisfactory conclusion of the Pay Statement Project including resolving the Equated Pay inaccuracies is vital given that 16% of the remaining 2015/16 & 2016/17 Audit actions will be addressed by the Pay Statements project.

In addition, as outlined in the Audit Report, other key areas of focus which will require the Council to play a key role include:

**Variable Payments Project** – supporting changes with service areas to current processes so that if possible, all Council claims are submitted electronically, to mitigate against fraud and manual errors.

**Itemised Pay Slip** – ensuring client business needs are specified as part of the Improvements needed to employee payslips to ensure employees are better able to confirm their payments and deductions (particularly for multiple jobs.) An immediate action has been to agree a timescale for the payslip display to be updated so that it meets the new legislation requirements from April 2019. The Council has requested revisions to the payslip display since 2015, however we have agreed with Serco that other system rectification priorities have had to take higher priority.)

## Management Response

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### Management Response



**Starters, Mover Leavers Project.** This is currently on hold pending the outcome of Serco's 'Operational Excellence' review. Once the outcome of this review is concluded, expected in June 2018, The Council will work with Serco to ensure effective implementation, in particular through communication with Managers to implement the revised e-forms used for these processes. .

**Late/Incomplete or Inaccurate Data from Managers.** The Client People Management Team will engage with all Council Managers to ensure the necessary changes to reduce the errors in data on the forms which are submitted to payroll by Managers. These are currently averaging at 50%. This will enable the Service to operate more efficiently and will ensure an improved employee experience. A key area is improving system usability and ensuring that process guidance for Managers and employees is clear and easy to follow.

**Pension reporting –** Serco have made improvements to the pensions reporting process and have future improvements planned. Updates have been provided to the Pension Boards on the resolution of issues and backlogs of processing and the progress has been noted as satisfactory.

Overall, the responsiveness of the Serco Payroll Manager (appointed in November 2017) to requests made by the Council and the positive relationship he has with the LCC Pay and Reward Lead has made a marked difference to the progress of resolution of problems. There is a greater understanding of the ownership of actions and a joint commitment to complete these as a priority.



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