



**Internal Audit Review on the Payroll system.
Payroll final report 2012/13**

C3 / 11

Assurance Level	Good
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June 2013

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1. Background

- 1.1 The Payroll section is responsible for the management of payments to employees. The Payroll section is within the Financial Management section. Two reports have been produced for this audit to clearly record the roles and responsibilities of Payroll and Human Resources (HR). This also will help to clearly report the responsibility of the issues raised during this review.

In 2012/13 the average number of permanent and casual employees (including members), paid each month was 293. The average gross pay per month for 2012/13 was £522,674.03.

- 1.2 The Payroll audit is a fundamental review, which is audited on an annual basis. For the 2011/12 audit, the Payroll audit was awarded a **Good** level of assurance in respect of the key controls tested and 6 recommendations were made.

- 1.3 The Payroll section acts upon notifications received from Human Resources (HR), Line Management and employees. Notifications could be received to request deductions from an employee's salary, such as union membership, or to temporarily increase an employee's salary for additional duties.

- 1.4 This audit reviewed the key controls of the payroll system. Changes to employee data and payments are automatically calculated by iTrent or can be manually input by Payroll. Audit testing and observation was undertaken to ensure that the controls were operating as intended. The following areas was reviewed:

- New starters
- Leavers
- Monthly BACS
- Monthly Errors and Warnings
- Travel and Subsistence
- Car loans
- Honoraria
- Maternity
- Sickness
- Mileage and lump sum payments
- Auto enrolment
- Real time Information (RTI)

- 1.5 Internal Audit utilised the IDEA (Interactive Data Extraction and Analysis) software to conduct a variety of tests to provide full assurance that the data and controls within the Payroll system are accurate. A series of tests was performed on 100% of Payroll data to ensure that there are no duplicate records/claims, to confirm the accuracy of calculations and to highlight unusual trends in data.

- 1.6 This review has been conducted by Tom McIntosh (Internal Auditor). Internal Audit wishes to thank all staff for their full co-operation during their interviews, which has

allowed this report to be produced.

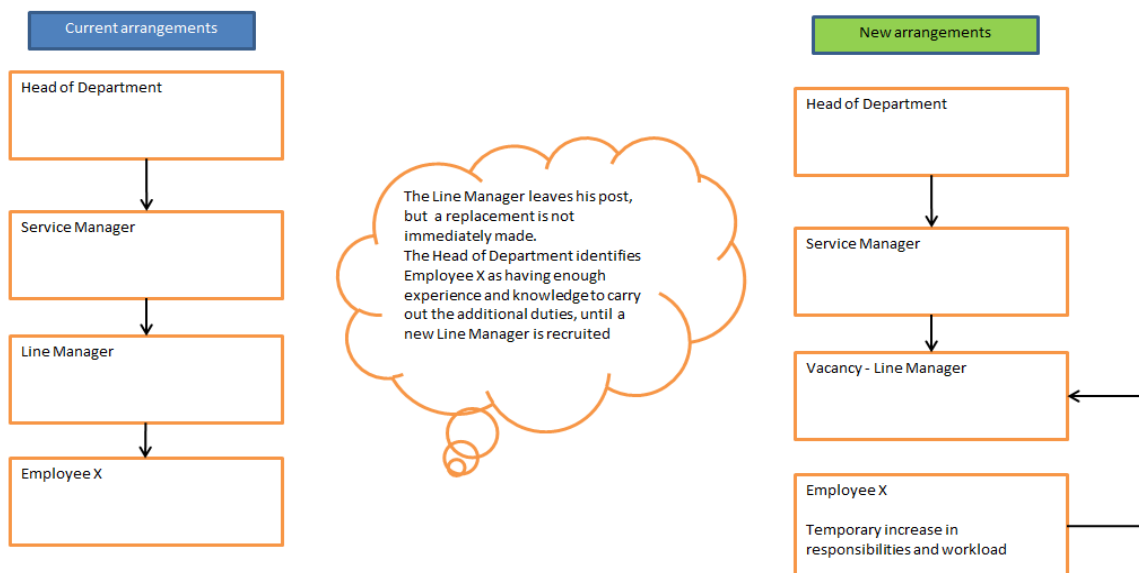
2. Internal Audit Opinion

- 2.1 Based on the interviews conducted, testing undertaken and observations made, it is our opinion that there is 1 fundamental issue that Payroll need to address in order to improve internal controls and processes:
- i. Honoraria payments should be shown as a separate element on iTrent
- 2.2 Control weaknesses have been identified that requires attention. Honoraria payments are additional payments to an employee's salary, for carry out additional duties, that are not part of their original job description, or to cover higher graded posts.
- 2.3 When employees are granted an honoraria, their salary is increased to the temporary salary, agreed by the Head of Service* and the Director. However, honoraria is an extra payment on top of the employee's original salary. The creation of a separate element would instantly identify employees in receipt of honoraria payments on iTrent. This would also improve the audit trail, to show when payments were made and will help when submitting returns to HMRC.
- 2.4 As part of this review, testing also identified an officer in receipt of an honoraria payment, which is not included on the Payroll monitoring spread sheet. There is a risk that employees are in receipt of honoraria payments, that are not known to Payroll. The monitoring spread sheet is not up to date and payments are made to employees that no longer require them and therefore not authorised.
- 2.5 There have been significant improvements to Payroll administration since the 2011/12 audit. Now that the Payroll is managed in house, controls and procedures have been adapted to ensure that key controls and checks are undertaken before, during and after each pay period. The Payroll Officer completes timely reconciliations of each payroll element before staff a paid.
- 2.6 Supporting evidence and reports from the payroll system are clear and accurate. The previous arrangements with North Yorkshire County Council (NYCC) required several amendments to be resolved before each pay run, but since the payroll administration has been brought back in house, accurate monitoring and reporting has led to accurate pay runs. During this review there have been no significant problems or issues with the pay runs, which confirms that the key controls are operating effectively and efficiently.

* Head of Service could be referred as the Corporate Head, Strategic Manager or Service Manager throughout this report.

3. Internal Audit Findings – Honoraria

3.1 Honoraria payments are for employees that carry out additional work/duties. Honoraria payments can be awarded to employees that have taken on additional duties, that is not within their current job description. For example, when staff leave or go on maternity, there may be sufficient skills, knowledge and capacity within the section to cover the post holders’ duties until an appointment is made. Payments can also be made if an employee is seconded to complete/manage a project or to cover duties undertaken by an employee who is on maternity leave.



3.2 An application must be completed for all Honoraria requests, detailing the reasons for the increase in payment and the duration the extra payment will be made. A standard calculation is applied ($\text{New salary} - \text{original salary} = (\text{the difference in pay}) \times \% \text{ of work to be carried out} = \text{total yearly payment} \div 12 = \text{monthly payment}$) to ensure that the employee is correctly paid, for the period that they are carrying out additional work/acting up duties.

3.3 Audit testing was undertaken to confirm that honoraria payments are correctly applied and an application exists for all payments. Information held by HR and Payroll was compared and examined to ensure employees pay has been correctly calculated and that the honoraria payments are valid. Audit testing was undertaken of 9 employees in receipt honoraria payments in 2012/13. This is a 100% sample check. For 2012/13, the value of honoraria payments was approximately £15k, which is around £1,650 per employee.

3.4 Applications for honoraria payments are made using the ‘Approval for acting up or honorarium payment’ form. The reason and details for the payment is recorded on this

form, including the period of the payment (start date and end date). This is signed by the Head of Service to agree the reason for the payment. Subsequent approval is received from finance, to confirm adequate budget is in place, Human Resources approval is required to review the job description and employee specification and to consider if there are any equality issues. Finally Director approval is required to approve the payment.

- 3.5 Audit testing was undertaken to confirm that there was an up to date and approved application. This test wanted to ensure that there was a clear audit trail in place for honoraria payments are awarded.

Audit testing found that, of the 9 honoraria applications reviewed, 7 honoraria start/end dates did not agree to the Payroll monitoring spread sheet. Upon review of all the applications held on the personal file, it could be determined that the start/end dates of honoraria payments did not agree to the monitoring spread sheet. The monitoring spread sheet should be up to date and accurate to provide an up to date record of employees in receipt of honoraria payments. There is a risk that payments continue to be paid once an employee returns to work and there is a risk that Payroll do not know who is in receipt of payments and what their original/contracted salary should be.

- 3.6 As part of the application process, the Head of Service is expected to clearly show the employee's original salary and the proposed honoraria/acting up salary. The difference between the monthly pay from the original grade to the new temporary grade is recorded on the spread sheet, but it would be good practice for Payroll to record the increase in payment figure on the application to show actual extra per month, the employee will receive. This would enable HR to formally notify the employee of the extra payment as well as document the start and end date of payment.

Recommendations

- The Payroll honoraria monitoring spread sheet should be updated to show all employees in receipt of honoraria payments and should record accurate start and end date of payments.
- The financial breakdown of the additional monthly payment should be recorded on the application form to inform budget holders of their responsibility for the additional payment.
- Honoraria payments should be shown as a separate element on iTrent

Target date: July 2013

Responsible Officer: VFM and Improvement Manager

4. Internal Audit Findings – other audited areas

- 4.1 As part of this audit review, testing was undertaken on the other key controls for the Payroll system. A walkthrough of each key control was undertaken, to confirm that the controls operated as intended.
- 4.2 A review of the new starter process was undertaken to ensure that the key controls had been followed when setting up a new employee. When a new employee is selected for appointment, HR create a personal file which contains the contract of employment, identification, tax notification (P45 or P46), qualification evidence (linked to the post), new starter form and correspondence to confirm the employee in the post.
- 4.2.1 The new starter form is a key document as the information included on this form, is used by Payroll to set up the employee on iTrent. The employee's bank details are recorded, including salary details, start date, allowances (essential user, standby allowance etc.), National Insurance number and job location/site. These details are input onto iTrent to create the employee record and the employee is now active and can be paid.
- 4.2.2 Testing was undertaken to ensure that key documents are received prior to the start date, a completed new starter form is on file and these details have been transferred accurately onto iTrent. Craven District Council had 45 new starters in 2012/13, of which, a sample of 5 (11% of new starters) were selected for testing.
- Audit found, for 100% (5 out of 5) that the information recorded on the new starter form, agreed to details held on iTrent. A new starter form was present on all employees' personal files in HR.
- 4.3 A review was undertaken of Council Leavers. There is a process in place to close down employee records, when they inform the Council that they are leaving. A resignation letter is received from the employee, or a termination notification from Management, informing HR/Payroll of their last working day. Checks are then undertaken to confirm that the outstanding leave figure (as this may need to be paid or recovered) and are there any outstanding loans or professional fees that need to be repaid.
- 4.3.1 A leavers form checklist is completed by the Line Manager and passed to HR to record and carry out their own checks before the employee leaves. Upon completion of all the checks, it is passed to Payroll to action on the iTrent system. The final pay figure is calculated by iTrent, when the leaving date is entered and the Payroll Officer will check the final pay figure for reasonableness and to ensure that any entries that need to be recovered are taken from their final salary.
- 4.3.2 Audit testing was undertaken to confirm that the above process had been followed.

A sample of 5 (17%) leavers was selected to review out of 29 leavers in 2012/13.

100% (5 out of 5) the correct process was followed, to close down an employee's record. Testing also confirmed that all employees selected, were marked as a leaver on the iTrent system, providing assurance that they have been correctly closed down and will not be included in any future pay runs.

- 4.4 Monthly BACS arrangements were checked and the summary totals and number of payments from the Payroll payment file through to BACS payment were agreed for all of 2012/13 payment runs. Testing was also undertaken to ensure that checks are undertaken by Senior Management prior to the pay run, as well as ensuring that there was an adequate separation of duties from preparing the payroll file, checking the payment value and number payments at the BACS machine and submitting the file to the bank to pay Craven District council employees.
- 4.4.1 Leading up to the pay run, notifications and requests can be made by the employee, Line Manager, Senior Management or external agencies (HMRC etc.) to amend the payment for the current pay period. For example, an employee may request for deductions to be made for gym membership at Craven Pool and Fitness Centre or union membership subscription. Line Management or Senior Management may agree to a temporary increase in salary if the employee is carrying out additional duties or approve an overtime claim and finally notifications can be received from HMRC to amend employee tax codes.
- 4.4.2 A cut off for payroll changes is applied so that the process of reconciling each payroll element can be started, in preparation for the pay run. Each payment and deduction is agreed to supporting monitoring spread sheets. Reports are produced from iTrent to agree the totals as recorded on the spread sheet.
- 4.4.3 Before each pay run the net pay control report is passed to a Senior Officer in Finance to review the salary payments and to check the payments to HR staff and the Payroll Officer to confirm that these agree to their usual salary payment. The pay run reconciliation summary is signed to confirm the check has been completed and this is retained with the supporting iTrent reports and monitoring spread sheets for the relevant pay run. The iTrent payroll file is then sent to the BACS box/machine in preparation for final checks/agreement. This file is sent by the Payroll Officer or the Creditors Modern Apprentice.
- 4.4.4 The iTrent payroll file is reviewed on the BACS box/machine by an officer independent of the payroll process. Checks are made to confirm that the Payroll total value and number of payments agree to the totals on the BACS screen. These totals are agreed before the officer approves the file and sends to the bank for payment. A BACS submission summary report is printed to confirm the value of the payroll and the number of payments made. This report also identifies the officer who sent the file, the date and time.
- 4.4.5 Audit testing was undertaken to ensure that the total value and number of payments for all 2012/13 (April 2012 – March 2013) pay runs agreed from the iTrent payroll report, to the BACS submission and to Agresso. Also, testing was undertaken to confirm that there was an adequate separation of duties from

preparing the payroll, agreeing the payroll file and approving the payroll payment via BACS.

- 4.4.6 Audit testing found that 12/12 (100%) of payroll values and number of payments sent to BACS, agreed to supporting iTrent payroll reports. Audit testing found that there was a clear separation of duties at each stage of the payroll process.
- 4.5 Errors and warnings reports are produced before each pay run, to identify payments that are significantly different (+ and -) from the previous pay run. The report is used to show any unusual payments that may not be normally picked up as part of the reconciliation process.
 - 4.5.1 Common entries on the errors and warning report include casual staff that gets paid one month, but not the next.
 - 4.5.2 Testing was undertaken to confirm that the errors and warning report was produced before each pay run. This test also wanted to confirm that each entry on the report was checked and a reason was given to why the employee appeared on the report.
 - 4.5.3 12 out of 12 (100%) errors and warnings report reviewed found that they were produced before each pay run. A review of the report also found that each entry was checked and a legitimate reason was given for why they appeared on the report.
- 4.6 The audit also conducted a review of car loans provided to staff by Craven District Council. Car loans are offered to employees who are either essential user status or official casual user status. Loans are charged at 4% and payment is taken direct from the employees salary.
 - 4.6.1 In order to obtain a loan, the employee must complete an application form. A supporting invoice is required from the car dealer to show the loan amount required. The employees Service Manager and the Head of Finance is required to review and approve the loan, before it is passed to payroll to include the deduction to their salary.
 - 4.6.2 Craven District Council have 3 active car loans in 2012/13. This generated income of approximately £8k (£7.5k principle and £600 interest).
 - 4.6.3 Testing covered the application process, to ensure that loans were correctly applied for, that supporting evidence from the car dealer agreed to the loan amount paid and that the loan was approved by the Head of Finance before the balance was paid to the car dealer.
 - 4.6.4 Audit testing found that a car loan application was completed for 100% of all active loans. The correct loan and interest repayments were calculated by the Payroll Officer. All loans were approved by the Corporate Head (Financial Management) before the balance was paid to the car dealer.

- 4.7 A walkthrough of an employee on maternity was tested, to ensure the statutory and key procedures had been followed. The Council is required have clear arrangements in place for dealing with employees that may go on maternity. Employees who are about to go on maternity are entitled to maternity pay that can be paid for first 39 weeks (classed as ordinary maternity leave) or up for a year (also called additional maternity leave). The first 6 weeks, maternity pay is 90% of the employees salary, from week 7, statutory maternity pay applies.
- 4.7.1 Testing reviewed the formal notification of a pregnancy (MATB1) and that the correct Statutory Maternity Pay (SMP) was correctly calculated and communicated to the relevant employee.
- 4.7.2 Audit testing of one employee on maternity found that the MATB1 was retained and the expected due was clear and the SMP calculations were provisionally calculated on this date. Testing also identified that the calculations for 39 week and 1 year maternity pay were accurate. Evidence of the options available to the employee were clearly recorded and in discussion with the Payroll Officer, these were communicated to the employee by Payroll and by HR. The correct procedure was followed and supporting evidence was correctly obtained.
- 4.8 A walkthrough of sickness was undertaken. This test was to ensure that sickness was correctly and accurately recorded on iTrent. Craven District Council sickness policy allows up to the first 6 months of sickness on full pay and after 6 months, then the employee goes down to half pay. After a year, all payments cease.
- 4.8.1 A random employee that had taken sick leave was selected to test. Sickness details were obtained and these were confirmed to iTrent. Audit testing found that the correct absence dates were applied on iTrent. The relevant pay slip also showed the sickness element. The employee provided a valid 'fit note' that showed the period of sickness and their expected return to work date.
- 4.9 Mileage and lump sum rates for all employees changed on the 1st January 2013. There was originally 3 mileage and lump sum rates, depending on the size of the claimants car engine size. On the 1st January 2013, Craven District Council agreed to put all claimants onto the middle band, regardless of the engine size.
- 4.9.1 Mileage claims are made using a mileage claim form, and these are manually input into a spread sheet by the Creditors MA and the input is checked by the Payroll Officer. The spread sheet is uploaded into the iTrent system prior to each pay run and is reconciled before each pay run (iTrent report and monitoring spread sheet).
- 4.9.2 Lump sum payments are manually input onto the same spread sheet. These rarely change and lump sum payments are only made if this is stated in the employees contract of employment, as a requirement of their job.
- 4.9.3 Testing was undertaken of January claims; to confirm that the new mileage and lump sum rates had been applied. Testing found that a majority of claims had been changed to the new rates. There were 10 claims that were paid at the old rate, but in discussion with the Payroll Officer, these claims were paid at the different rate as the mileage was made in December, so the old rates applied the mileage

undertaken.

- 4.10 Auto enrolment is a scheme the Government has introduced to help employees to start saving for their future. Every employer is required by law to auto enrol employees to a pension scheme, but employees have a right to opt-out. The Pensions Regulator is responsible for checking that employers are complying with the scheme. The Pension Regulator web site has clear and detailed guidance to help business and employees, to understand the impact of auto enrolment.
- 4.10.1 Craven District Council has submitted a report to Corporate Leadership Team (CLT) outlining the new auto enrolment process. A flow chart explaining how to determine eligible and non-eligible employees was provided as an appendix to the report. The report was to provide Management with the details of the scheme and to obtain 'buy in/support' about how the scheme is going to operate. The report also details the potential financial impact on the Council by auto enrolling employees that are not part of the current pension scheme. Craven District Councils staging date (start date) is February 2014. In discussion with the VFM and Improvement Manager (22/05/2013), CLT have agreed to defer auto enrolment of existing eligible staff from February 2014 – to 217 – currently 37 employees.
- 4.10.2 Craven District Council have worked closely with North Yorkshire County Council (NYCC) to adopt a consistent approach to communicating and applying the new auto enrolment scheme. NYCC manage the Local Government Pension Scheme (LGPS) that employees will be auto enrolled into.
- 4.10.3 On inspection of the auto enrolment requirements, the evidence and documentation provided, shows that Craven District Council has a plan in place to implement the Auto enrolment requirements. There is still work to do prior to the staging date, but regular meetings and a clear project plan should ensure that the Payroll section is prepared for the changes.
- 4.11 Real Time Information (RTI) is a requirement from HMRC for the Council to provide employee information after each pay run. A payroll file is produced before each pay run, which is reconciled to supporting payroll information.
- 4.11.1 The file is sent via a secure connection to HMRC.
- 4.11.2 Requirements of the RTI scheme, required Craven District Council to produce a payment file into a format requested by HMRC. The key details need to be aligned with HMRC information to ensure that the file would be accepted. Also, by providing real time information, HMRC confirmed that there is no longer a requirement to submit the year end P35 and P14 return. CDC do not need to send HMRC a completed P45, only the employee receives this now.
- 4.11.3 The first RTI submission was made in April 2013. In discussion with the Payroll Officer, HMRC confirmed that there were no issues with the file and that the file was in the correct format.

4.12 IDEA (Interactive Data Extraction and Analysis) was used to conduct the following tests:

Test details	Risk / reason for test	Results
Duplicate pay reference used	To ensure that the same pay reference is not used for more than one employee	Nil results.
Duplicate National Insurance Number (NINO) on iTrent	To determine if the same NINO is used for more than one employee	Nil results.
NINO is in the correct format	To ensure that NINOs are in the correct format, as expected by HMRC	Nil results. NINO for all employees is in the correct format.
Duplicate post number used	To ensure that only post number is used for each post.	Nil results. There are no duplicate post numbers used on iTrent.

4.12.1 It is hoped that in the 2013/14 Payroll audit, to be able to request more detailed reports so that more complex and targeted testing can be presented, to be able to provide further assurance that the iTrent system is accurate and there are no fraudulent records or transactions.

5. Summary of Recommendations

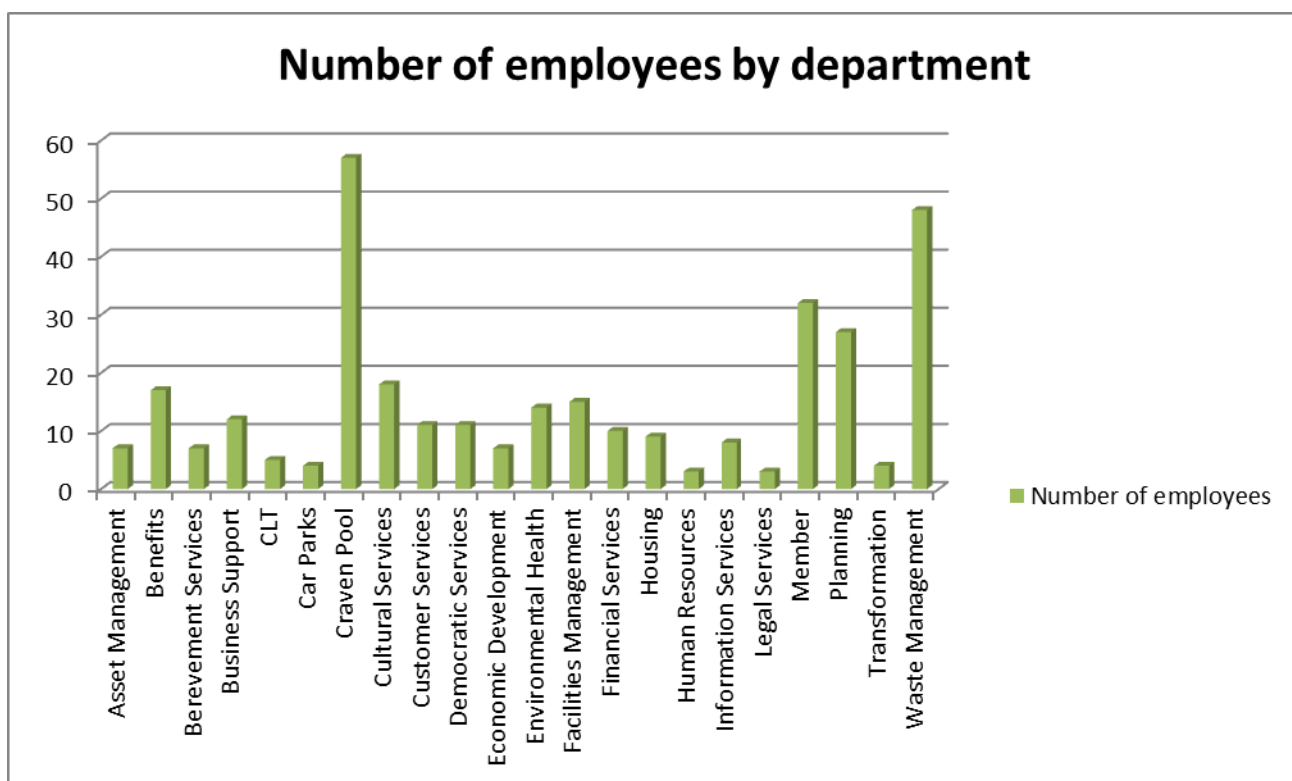
Reference	IA Recommendation	Responsible Officer	Priority	Implementation date
1	The Payroll honoraria monitoring spread sheet should be updated to show all employees in receipt of honoraria payments and should record accurate start and end date of payments.	VFM and Improvement Manager	Priority 3	October 2013
2	The financial breakdown of the additional monthly payment should be recorded on the application form and the monitoring spread sheet.	VFM and Improvement Manager	Priority 3	October 2013
3	Honoraria payments should be shown as a separate element on iTrent	VFM and Improvement Manager	Priority 1	August 2013

6. Payroll profile

For information purposes.

Below is a selection of charts showing the composition of the Payroll system. Details are provided under each chart to explain what it is showing. The data was extracted from the iTrent system, which was used to conduct the audit testing and IDEA review.

Craven District Council pay run has on average 293 members of staff per month. These employees are split over 22 departments. Below is a chart to show the number of employees in each department:



IDEA was used to determine the make-up of contracted employees and casual staff. Casual staff are set up on iTrent with 0 (zero) hours. Contracted staff have their hours specified on iTrent e.g. 37 hours (full time) or 22 hours (3 day week). Below is a chart showing the make-up of employee contracts:

