

INTERNAL AUDIT REPORT

2019

# SCDOT EMPLOYEE BENEFIT CHANGES

An Assessment of:

- ✓ Risks
- ✓ Control Design Adequacy
- ✓ Control Operating Effectiveness



SOUTH CAROLINA OFFICE OF THE STATE AUDITOR

INTERNAL AUDIT SERVICES

May 22, 2019

# 2 EXECUTIVE SUMMARY

## EMPLOYEE BENEFIT CHANGES

### OBJECTIVE:

To determine whether internal controls are adequately designed and operating effectively for providing reasonable assurance that:

1. Employee benefit change transactions are processed accurately and timely and
2. The accumulator report used to detect benefit change errors is reconciled monthly to minimize accumulated benefit underpayments.

### BACKGROUND:

After the second payroll run of each month, the Public Employee Benefit Authority (PEBA) produces an accumulator report. This report is available to download and lists individual employees and dollar amounts where expected premium deductions for elected benefits does not match the actual SCEIS (South Carolina Enterprise Information System) deductions. Prior to May 2016, SCDOT did not have a process to review and clear discrepancies. At the end of fiscal year 2017, PEBA requested payment from SCDOT for an accumulated variance of approximately \$450,000, which SCDOT paid. To reduce the amount of such payments in the future, the Agency assigned a dedicated employee to review and clear entries. The outstanding variance dropped to approximately \$10,000 at the end of fiscal 2018, with the same balance projected for fiscal 2019.

### OBSERVATIONS ON INTERNAL CONTROLS:

None

Continued on next page

# EXECUTIVE SUMMARY *continued*

## PERFORMANCE OPPORTUNITIES:

### 1. Quality Assurance

*Opportunity:* Keying errors and missing documentation could go undetected until the staff review of the accumulator report takes place after month end. The Human Resources Division (HR) should establish a quality assurance review process to verify that key benefit information was entered into the data system correctly.

(See detailed Performance Opportunity 5.1 on page 10)

### 2. Timely Processing

*Opportunity:* The accumulator report is an effective detective control but includes a large number of entries that make the reconciliation time-consuming and prone to errors. The Operations, Benefits and Payroll divisions within HR should meet to discuss key processing dates and system lock out periods. In order to meet specific dates, all processing divisions should establish goals. The divisions should communicate instances where deadlines cannot be met.

(See detailed Performance Opportunity 5.2 on page 11)

### 3. Information Sharing and Communication

*Opportunity:* The Operations, Benefits, and Payroll divisions operate independently of each other but the action or inaction of each division may negatively impact the others if there is not mutual awareness. Periodic team meetings should be scheduled to share information, discuss risks and challenges, and brainstorm process improvements.

(See detailed Performance Opportunity 5.3 on page 12)

**Management Action Plans are included in Section 5 following each detailed Performance Opportunity as referenced above.**

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# 1 FOREWORD

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## **AUTHORIZATION**

The South Carolina Office of the State Auditor established the Internal Audit Services division (IAS) pursuant to SC Code Section 57-1-360 as revised by Act 275 of the 2016 legislative session. IAS is an independent, objective assurance and consulting function designed to add value and improve the operations of the South Carolina Department of Transportation (SCDOT). IAS helps SCDOT to achieve its objectives by bringing a systematic, disciplined approach to evaluating the effectiveness of risk management, internal control, and governance processes and by advising on best practices.

## **STATEMENT OF INDEPENDENCE**

To ensure independence, IAS reports administratively and functionally to the State Auditor while working collaboratively with SCDOT leadership in developing an audit plan that appropriately aligns with SCDOT's mission and business objectives and reflects business risks and other priorities.

## **REPORT DISTRIBUTION**

This report is intended for the information and use of the SCDOT Commission, SCDOT leadership, the Chairman of the Senate Transportation Committee, the Chairman of the Senate Finance Committee, the Chairman of the House of Representatives Education and Public Works Committee, and the Chairman of the House of Representatives Ways and Means Committee. However, this report is a matter of public record and its distribution is not limited.

## **PERFORMED BY**

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## **REVIEWED BY**

Wayne Sams, CPA  
Director of Internal Audit Services

## **ACKNOWLEDGEMENT**

We wish to thank members of management and staff in the Human Resource and Payroll divisions for their cooperation in sharing their knowledge and experience and developing actions to improve internal control and enhance operating performance.



## 3 INTERNAL AUDITOR'S REPORT

May 22, 2019

Ms. Christy A. Hall, Secretary of Transportation  
and  
Members of the Commission  
South Carolina Department of Transportation  
Columbia, South Carolina

We have completed a risk and control assessment of the South Carolina Department of Transportation's (SCDOT's) Employee Benefits Changes Activity. The objective of this assessment was to contribute to the improvement of risk management by evaluating SCDOT's exposure to risks and the controls designed by Management to manage those risks. Our engagement included two aspects:

- Facilitation of Management's assessment of risks associated with processing employees' benefit changes
- Independent assessment of the design and effectiveness of internal controls to manage identified risks of the activity

We planned and performed the engagement with due professional care in order to obtain sufficient, appropriate evidence to provide a reasonable basis for our conclusions. We determined internal controls are adequately designed and are operating effectively. We noted no internal control observations.

While our engagement was primarily focused on risk management, we have identified other matters that may represent opportunities for cost savings, revenue enhancement, process improvement, strengthened control environment, or more effective performance. These matters are detailed in the *Performance Opportunities* section on page 9.

George L. Kennedy, III, CPA  
State

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## 4 ENGAGEMENT OVERVIEW

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### 4.1 BACKGROUND

When employees elect benefits, SCDOT staff key the information into the Public Employee Benefit Authority's (PEBA) Employer Benefits System portal. Each morning, PEBA sends a file to SCEIS (South Carolina Enterprise Information System) that includes changes, additions or terminations to employee benefit elections. Once a SCEIS employee reviews the file, it is uploaded into the SCEIS reporting system.

After the second payroll run of each month, PEBA produces an accumulator report that is available for agencies to download from PEBA's website. This report lists individual employees and dollar amounts where the expected premium deductions for elected benefits does not match the actual SCEIS deductions. Variances are listed by type of deduction (medical, dental, vision, etc.) and also by employee cost share and employer cost share. SCDOT staff research and clear the variances, if possible, via a SCEIS helpdesk ticket.

Prior to May 2016, SCDOT did not have a process to review and clear discrepancies. At the end of fiscal year 2017, PEBA requested payment from SCDOT for an accumulated variance of approximately \$450,000, which SCDOT paid. While it is not uncommon for State agencies to have variances, the differences are not typically that large. To reduce the amount of such payments in future years, the Agency assigned a dedicated employee within the payroll function to review and clear entries. Additionally, the payroll function was transferred to the Human Resources Division (HR). The Benefits and Operations Departments within HR were also assigned roles in this process. With these changes, we noted that the outstanding variance dropped significantly to approximately \$10,000 at the end of fiscal year 2018, with the same balance projected for fiscal year end 2019. Such balances are typical of other State agencies.



### 4.2 OBJECTIVES

Management's objective with employee benefit changes is to ensure that transactions are accurate and timely and the accumulator report is reconciled monthly to reduce the financial risk exposure for SCDOT. Our objective was to facilitate management's assessment of risks that threaten the achievement of its objectives and to assess the effectiveness of controls designed to manage those risks to an acceptable level.

### 4.3 SCOPE

The change in benefits activity is composed of the following six processes which are described in Appendix A:

	<b>Process</b>	<b>Responsible Division(s) within HR</b>
1	Onboarding	Benefits
2	Change of Life Status	Benefits
3	Open enrollment	Benefits
4	Termination of Benefits (Employee Terminated)	Operations/Benefits
5	Termination of Benefits (Death)	Operations/Benefits
6	Leave Without Pay	Benefits

### 4.4 METHODOLOGY

For the processes included in the engagement scope, we performed the following procedures:

1. We facilitated Management’s completion of a process outline that documented the steps in the process and the individuals responsible for those steps.
2. We facilitated Management’s completion of a risk and control matrix used to:
  - a. Identify risks which threaten process objectives;
  - b. Score the risks as to their consequence and likelihood of occurrence using the risk matrix in Appendix B;
  - c. Determine if controls are adequately designed to manage the risks to within the Agency’s risk appetite; and
  - d. Propose design improvements to controls when risks are not managed to within the Agency’s risk appetite.

As shown on the Risk Scoring Matrix in Appendix B, risk significance is rated on a scale of 1 (lowest) to 25 (highest) and is the product of the risk consequence score (1 to 5) multiplied by the risk likelihood score (1 to 5). Risk appetite is the amount of risk exposure Management is willing to accept in pursuit of its objectives. Executive Management has set various risk appetites by risk type as shown in Appendix C. Risks scoring below Management’s risk appetite require no further risk management. Controls determined to be inadequate in design or ineffective in operation result in risk exposure to the Agency if risk scores exceed risk appetite.



3. We observed the discussion by key process owners and other subject matter experts performing the steps in procedure two above.
4. We evaluated Management's assessment to determine if it is reasonable and comprehensive.
5. We tested key controls for risks with inherent scores of 9 and above [scale of 1 (low) to 25 (high)] to determine if the controls are operating effectively. Testing may include inquiry, observation, inspection of documentation, and re-performance of process steps. We determined that the accumulator report is the primary control for detecting and preventing entry errors. Our testing therefore focused on the causes for entries appearing on the accumulator report. We selected report entries that included the following:
  - Employees who separated from SCDOT
  - Employees who did not separate from SCDOT
  - Entries that were deemed uncollectable
6. We developed, as needed, observations based on the assessments of controls which are not adequately designed and/or operating effectively.
7. We collaborated with Management to develop action plans to improve control design and/or operating effectiveness.
8. We collaborated with Management to identify opportunities and develop action plans for improving performance.

## 4.5 CONCLUSION

In our opinion, based on the testing performed, the revised processes to reduce the large benefit variance payments are working as intended and the accumulator report is an effective detective control. We noted that the accumulator report includes a large number of entries that makes the reconciliation time-consuming and prone to error. We therefore identified opportunities that could reduce the number of entries thereby promoting the control's ongoing success.

## 4.6 DEVELOPMENT OF MANAGEMENT ACTION PLANS

We will follow up with Management on the implementation of the proposed actions on an ongoing basis to ensure they are effectively and timely implemented. We will provide the Commission and Senior Management with periodic reports on the status of management action plans and whether those actions are effectively and timely implemented.

# 5 PERFORMANCE OPPORTUNITIES

While our engagement was primarily focused on risk management, we have identified other matters that represent opportunities for cost savings, revenue enhancement, process improvement, strengthened control environment, or more effective performance.

## Performance Opportunity 5.1 Quality Assurance

**Processes Affected:** (See process descriptions in Appendix A on page referenced below)

Process 1 – On Boarding, Change of Life Status, Open Enrollment or Leave without Pay (page 12)

Process 2 – Termination of Benefits (page 12)

**Keying errors and missing documentation could go undetected until the staff review of the accumulator report takes place after month end.** A quality assurance (QA) process could reduce the number of entries on the accumulator report that are caused by keying errors. The QA would help ensure:

- employee benefits are correct
- the necessary supporting documents are provided
- the appropriate premiums are being deducted from the employee’s paycheck

**Recommendation:** We recommend that HR establish a QA process to verify that key information was entered correctly. This could be a checklist completed by someone independent from the employee who keyed the information. In addition, the HR-1 Human Resources Separation Form, the HR-4 Leave Without Pay Form and any other form that would be applicable should be reviewed and updated to verify that all the necessary information was included on each form. A shared spreadsheet with “missing” or needed documents should also be developed.

## Management Action Plan (MAP) 5.1

Benefits manager will develop a spreadsheet upon which benefits consultants will record all transactions with sufficient data to identify the employee, the action, the processing date, and whether the action will affect payroll deductions. This spreadsheet can be compared to the HR-1 and HR-4, as well as existing SCEIS reports to ensure data is accurately keyed. Combination of this spreadsheet, and the adoption of benefits e-forms based on existing HR-2 and HR-7, and implementation of a regular, weekly coordination meeting between the SCDOT Benefits Manager, Payroll Manager, and Operations Manager should be sufficient to reduce errors or omissions that will result in additions to the accumulator report.

MAP Owner:	Benefits Manager
Division:	Human Resources
Scheduled Date:	July 1, 2019

## Performance Opportunity 5.2 Timely Processing

**Processes Affected:** (See process descriptions in Appendix A on page referenced below)

Process 1 – On Boarding, Change of Life Status, Open Enrollment or Leave without Pay (page 12)

Process 2 – Termination of Benefits (page 12)

**We determined that the accumulator report is an effective detective control but includes a large number of entries that make the reconciliation time-consuming and prone to errors.** There are numerous entries on the monthly accumulator report that could be avoided with more timely processing of approvals and keying of information that occur in multiple areas (districts, Operations Division, and Benefits Division). Analysis of documentation indicated that there is a wide range in the number of days between when a form requesting a change in benefits is received and when the required entries are completed. During our review, we noted instances where the DEA (District Engineering Administrator) approval, Operations Division data entry and Benefits Division data entry all happened on the same day or within two or three days. However, our review also noted instances where there were 30 days or more between transactions being processed.

**Recommendation:** Operations, Benefits and Payroll divisions should meet to discuss key processing dates and system lock out periods. Transactions are required to be keyed into the Employer Benefits System (EBS) by a specific date or they will appear on the accumulator report. In order to meet this specific date, all processing divisions should establish goals to meet that deadline. Divisions should communicate instances where deadlines cannot be met to aid the Payroll Division in clearing items from the accumulator report.

### Management Action Plan (MAP) 5.2

The SCDOT Benefits Manager, Payroll Manager and Operations Manager will meet weekly to compare transactions, discuss issues, and identify topics for dissemination to their respective staffs.

MAP Owner:	Director of Human Resources
Division:	Human Resources
Scheduled Date:	June 3, 2019

### Performance Opportunity 5.3 Information Sharing and Communication

**Processes Affected:** (See process descriptions in Appendix A on page referenced below)  
Process 1 – On Boarding, Change of Life Status, Open Enrollment or Leave without Pay (page 12)  
Process 2 – Termination of Benefits (page 12)

**The Operations, Benefits, and Payroll divisions operate independent of each other but the action or inaction of each division may negatively impact the others if there is not mutual awareness.** We noted limited information sharing or communication among the three divisions. A global understanding of the entire Employee Benefits Changes activity does not exist among process owners making it difficult for them to understand how their work affects each other. The Payroll Division is physically separate from the other two divisions which may hinder effective communication.

**Recommendation:** A broad description of the activity should be documented and shared allowing employees involved in processing benefit changes to gain a better understanding of process goals. Periodic team meetings should be scheduled to share information, discuss risks and challenges, and brainstorm process improvements. Relocating payroll employees to HR may promote more effective communication and collaboration with the other HR divisions.

#### Management Action Plan (MAP) 5.3

Weekly, after the meeting between SCDOT Benefits Manager, Payroll Manager and Operations Manager, the three managers will discuss with their respective staff any issues that arose out of the meeting and general topics of mutual information identified at the meeting.

MAP Owner:	Director of Human Resources
Division:	Human Resources
Scheduled Date:	June 3, 2019

## PROCESS DESCRIPTIONS

### Process 1 On Boarding, Change of Life Status, Open Enrollment or Leave without Pay

On boarding, change of life status, open enrollment and leave without pay may require documentation to support enrollment/changes to dependent coverage. New employees have thirty days from their hire date to enroll in the various benefit plans offered by the State. Their employment date dictates when they become eligible for benefits. If they start on the first working day of the month, they are eligible for the benefits starting that month. If they start on any other day of the month, they are eligible for benefits starting the first of the following month. SCDOT employees are paid twice a month. Time worked from the 2<sup>nd</sup> of the month through the 16<sup>th</sup> of the month is paid on the first of the following month. Time worked from the 17<sup>th</sup> through the 1<sup>st</sup> of the next month is paid on the 16<sup>th</sup> of the following month. Benefit premiums are paid in advance with equal amounts being deducted from each paycheck. Premiums for coverage from the 1<sup>st</sup> to the 15<sup>th</sup> of the month is deducted from the paycheck received on the 2<sup>nd</sup> of the month. Premiums for the 16<sup>th</sup> to the end of the month are deducted from the paycheck received on the 16<sup>th</sup>. Coverage ends on the last day of the month regardless of the employees last day of employment. Change of life status requests must be entered within thirty days of the event. Failure to timely provide the documents to PEBA could result in missed or inaccurate premiums being deducted from the employee's paycheck.

The objective of this process is to ensure that requests are processed timely and accurately and that the appropriate deductions are collected.

### Process 2 Termination of Benefits

Benefits are to be terminated within thirty days of the employee's last working day or immediately in the event of the death of an employee. The process starts with the completion of an on-line form. This form is electronically routed for approval by the DEA/Director. Once it is approved, the form is electronically routed to the Operations Division which keys information into SCEIS. The Benefits Division receives notification once the Operations Division has completed its process. Benefits Division employees key the information into PEBA's EBS. Once PEBA completes the termination process, it sends a file to SCEIS for uploading.

The objective of this process is to terminate employees benefits within thirty days of their last day worked or immediately in the event of the death of an employee.

# APPENDIX B

## RISK SCORING MATRIX

Risk significance is rated on a scale of 1 (lowest) to 25 (highest) and is the product of the risk consequence score (1 to 5) multiplied by the risk likelihood score (1 to 5). The following matrix provides a color scale corresponding to risk significance scores.

<b>Likelihood</b>	Frequent or Almost Certain	3-4 Low	9-13 Medium	14-17 Med-High	18-21 High	22-25 Extreme
	Likely	3-4 Low	5-8 Med-Low	9-13 Medium	14-17 Med-High	18-21 High
	Possible	3-4 Low	5-8 Med-Low	5-8 Med-Low	9-13 Medium	14-17 Med-High
	Unlikely	1-2 Minimal	3-4 Low	5-8 Med-Low	5-8 Med-Low	9-13 Medium
	Rare	1-2 Minimal	1-2 Minimal	3-4 Low	3-4 Low	3-4 Low
		Incidental	Minor	Moderate	Major	Extreme
		<b>Consequence</b>				

# APPENDIX C

## RISK APPETITE

Risk appetite is defined as the amount of risk the Agency is willing to accept in the pursuit of its objectives. Management’s goal is to manage risks to within the appetite where mitigation is cost-beneficial and practical. Management has set the Agency’s risk appetite by risk type using scoring methodology consistent with the Risk Scoring Matrix shown in Appendix B. Risk appetites by risk type are as follows:

RISK TYPE	EXAMPLES	RISK APPETITE SCORE 1 = Minimal Risk 25 = Extreme Risk (See Scoring Matrix in Appendix B)
<b>Safety</b>	Employee and Public Well-Being	<b>2</b>
<b>Ethical</b>	Fraud, Abuse, Mismanagement, Conflict of Interest	<b>2</b>
<b>Financial</b>	Funding, Liquidity, Credit, Reporting	<b>4</b>
<b>Strategic</b>	Resources not Aligned, Unclear Objectives	<b>4</b>
<b>Reputational</b>	Unintentional Unwanted Headlines	<b>4</b>
<b>Operational</b>	Delays, Cost Overruns, Waste, Inefficiency	<b>6</b>
<b>Regulatory</b>	Non-Compliance	<b>6</b>
<b>Legal</b>	Lawsuits	<b>10</b>