



An Audit Report on

Financial Processes at the Pension Review Board

August 2016

Report No. 16-038



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Overall Conclusion

In fiscal year 2015, the Pension Review Board (Agency) had significant weaknesses in succession planning, cross-training, and policies and procedures that put its financial operations at risk. Specifically, when the **Agency's** only accountant left employment in May 2015, the Agency had neither the staff nor the policies and procedures necessary to enable it to continue processing its payroll and non-payroll expenditures without assistance. However, it is important to note that the payroll expenditures that auditors tested at the Agency complied with state statutes and rules. In fiscal year 2015, payroll represented 91 percent of the **Agency's total expenditures**.

To maintain its financial operations, in June 2015 the Agency requested that the former accountant provide training on financial processes to the executive director; the Agency later contracted with the former accountant for those services in July 2015. However, in contracting with that individual, the Agency (1) did not comply with statutory requirements regarding how soon an agency can contract with a former employee and (2) made \$16,400 in advance payments on the contract that were unallowable according to the *State of Texas Procurement Manual*. As of March 2016, the Agency had paid that individual a total of \$29,000 (which represented 21 percent of its \$137,928 in non-payroll expenditures from September 2014 through March 2016).

Although the Agency had controls over its purchasing process, it did not consistently (1) ensure that travel expenditures complied with the Office of the Comptroller of Public Accounts' **travel allowance and reimbursement rates** and (2) retain required documents to support non-payroll expenditures.

Background Information

The 66th Legislature created the Pension Review Board (Agency) in 1979 to oversee state and local government retirement systems. Seven board members (comprising five industry representatives, one contributing member of a public retirement system, and one member receiving retirement benefits from a public retirement system) govern the Agency.

For fiscal years 2015 and 2016, the Agency was appropriated \$1.76 million and authorized 15.0 full-time equivalent employees.

Sources: The Agency; Texas Government Code, Section 801.103; and the General Appropriations Acts (83rd and 84th Legislatures).

Table 1 presents a summary of the findings in this report and the related issue ratings. (See Appendix 2 for more information about the issue rating classifications and descriptions.)

Table 1

Summary of Chapters and Related Issue Ratings		
Chapter	Title	Issue Rating ^a
1	The Agency Should Improve Succession Planning, Cross-training, and Policies and Procedures for Financial Processes	High
2	The Agency Should Strengthen Certain Controls Over Financial Processes	Low
<p>^a A chapter is rated Priority if the issues identified present risks or effects that if not addressed could critically affect the audited entity's ability to effectively administer the program(s)/function(s) audited. Immediate action is required to address the noted concern and reduce risks to the audited entity.</p> <p>A chapter is rated High if the issues identified present risks or effects that if not addressed could substantially affect the audited entity's ability to effectively administer the program(s)/function(s) audited. Prompt action is essential to address the noted concern and reduce risks to the audited entity.</p> <p>A chapter is rated Medium if the issues identified present risks or effects that if not addressed could moderately affect the audited entity's ability to effectively administer program(s)/function(s) audited. Action is needed to address the noted concern and reduce risks to a more desirable level.</p> <p>A chapter is rated Low if the audit identified strengths that support the audited entity's ability to administer the program(s)/functions(s) audited or the issues identified do not present significant risks or effects that would negatively affect the audited entity's ability to effectively administer the program(s)/function(s) audited.</p>		

Auditors communicated other, less significant issues in writing to Agency management.

Summary of Management's Response

At the end of each chapter in this report, auditors made recommendations to address the issues identified during this audit. The Agency agreed with the **recommendations in this report, and management's response is presented in Appendix 4.**

Audit Objective and Scope

The objective of this audit was to determine whether the Agency has processes and related controls to help ensure that it administers financial transactions in accordance with applicable statutes, rules, and Agency policies and procedures.

The scope of this audit covered the Agency's expenditures and activities related to purchasing, travel, payroll, and the related information systems between September 1, 2014, and February 29, 2016. Additionally, auditors performed limited procedures on contracts with a former Agency employee through March 2016.

Contents

Detailed Results

Chapter 1	
The Agency Should Improve Succession Planning, Cross-training, and Policies and Procedures for Financial Processes	1
Chapter 2	
The Agency Should Strengthen Certain Controls Over Financial Processes.....	4

Appendices

Appendix 1	
Objective, Scope, and Methodology	6
Appendix 2	
Issue Rating Classifications and Descriptions.....	9
Appendix 3	
Summary of Agency Expenditures from September 2014 through February 2016.....	10
Appendix 4	
Management's Response	12

Detailed Results

Chapter 1

The Agency Should Improve Succession Planning, Cross-training, and Policies and Procedures for Financial Processes

Chapter 1
Rating:
High ¹

In fiscal year 2015, the Pension Review Board (Agency) had significant weaknesses in succession planning, cross-training, and policies and procedures that put its financial operations at risk. Specifically, when the Agency's only accountant left employment in May 2015, the Agency did not have staff with the necessary expertise, and the Agency's accounting policies and procedures did not contain sufficient detail to enable the Agency to process its payroll and non-payroll expenditures without assistance.

To maintain its financial operations, in June 2015 the Agency requested that the former accountant provide training on financial processes to the executive director; the Agency later contracted with the former accountant for those services in July 2015. From August 2015 through March 2016, the Agency paid the former accountant a total of \$29,000. However:

- The Agency contracted with its former accountant 11 months before the date that Texas Government Code, Section 2252.901, specifies an agency can hire a former employee as a contractor.
- The former accountant provided 104 hours of training before the initial contract was signed.
- In August 2015, the Agency paid the former accountant the full contract amount of \$15,000 for 300 hours of training when that individual had provided only 234 hours of training as of the time of that payment. As a result, \$3,300 of that payment was an unallowable advance payment, according to the *State of Texas Procurement Manual*.
- In September 2015, the Agency paid the former accountant an additional \$4,000 for 80 additional hours of training that the individual had not yet provided. In addition, the Agency had not formed a new contract for that payment.
- In March 2016, the Agency formed a new contract under which it paid the former accountant an additional \$10,000 for 200 additional hours of

¹ Chapter 1 is rated High because the issues identified present risks or effects that if not addressed could substantially affect the audited entity's ability to effectively administer the program(s)/function(s) audited. Prompt action is essential to address the noted concern(s) and reduce risks to the audited entity.

training when that individual had provided only 18 hours of training. As a result, \$9,100 of that payment was an unallowable advance payment, according to the *State of Texas Procurement Manual*.

In addition, the Agency processed payroll and non-payroll expenditures without appropriate separation of duties. Specifically, the Agency's executive director both entered and released the following transactions into the payroll and accounting systems:

- Six payroll transactions totaling \$147,508 for June 2015, December 2015, February 2016, and March 2016.
- Five non-payroll transactions totaling \$629 for June 2015 and July 2015.

As discussed further in Chapter 2, auditors did not identify errors in the payroll expenditures tested. Chapter 2 also discusses certain errors that auditors identified in the non-payroll expenditures tested, but those errors were not related to weaknesses in separation of duties. However, when a single employee has the ability to both enter and release financial transactions in an accounting or payroll system, that increases the risk of errors in financial transactions.

The Agency's policy also specifies that only the executive director can approve expenditures, and the executive director is the only individual at the Agency who can release payments in USAS. Not having a backup individual who could perform those duties in the executive director's absence could leave the Agency unable to process its expenditures.

To address succession planning, the Pension Review Board created a deputy director position in October 2015 to assist and back up the executive director. Auditors noted that the deputy director approved some expenditures during fiscal year 2016. Although the Agency has not had an accountant since February 2016, its staff services officer is receiving training on some financial processes and, according to the Agency, it has assigned other staff to perform as backups for key roles.

Recommendations

The Agency should:

- Continue to develop and implement a succession plan and cross-training for financial processes.
- Develop and implement policies and procedures for financial processes that contain sufficient detail to ensure that the Agency can maintain

financial processes without the need for additional training or substantial assistance.

- Develop and implement policies and procedures that address separation of duties for the entry and release of financial transactions.
- Update its policies to identify personnel other than the executive director who can approve expenditures in the executive director's absence, and update user access to USAS to ensure that those personnel can approve and release payments in the executive director's absence.

The Agency Should Strengthen Certain Controls Over Financial Processes

Chapter 2
Rating:
Low ²

The Agency had controls over its financial processes. The payroll expenditures that auditors tested at the Agency complied with state statutes and rules. However, the Agency did not consistently (1) ensure that travel expenditures complied with the Office of the Comptroller of Public Accounts' travel allowance and reimbursement rates, (2) retain required documents to support travel expenditures, and (3) update the authorized signers on its procurement cards.

The Agency processed payroll and pay actions appropriately.

The Agency had processes and related controls to ensure that it made payroll expenditures in accordance with state statutes and rules. Specifically:

- The Agency appropriately paid payroll for all 20 active employees from September 2014 through February 2016.
- The Agency appropriately approved and supported all 39 employee pay actions tested. (Pay actions include one-time merits awards, promotions, and equity adjustments.)

The Agency should consistently comply with travel requirements.

The Agency made \$122,479 in non-payroll expenditures from September 2014 through February 2016. Auditors tested 28 of the non-payroll expenditures totaling \$40,393. Auditors identified no significant errors in the \$34,956 in non-travel expenditures in that sample. The travel expenditures in that sample totaled \$5,437, and auditors identified the following issues related to those travel expenditures:

- Four of the travel expenditures tested exceeded the maximum allowable lodging rate by a total of \$332. The Agency did not have a receipt for one of those expenditures.
- One of the travel expenditures tested was for a first-class flight that exceeded the cost of an alternative flight to and from the same city on the same day by \$378.

² Chapter 2 is rated Low because the audit identified strengths that support the audited entity's ability to administer the program(s)/function(s) audited or the issues identified do not present significant risks or effects that would negatively affect the audited entity's ability to effectively administer the program(s)/function(s) audited.

The Agency should ensure that individuals who are authorized to use its procurement cards are current employees.

The Agency made 27 purchases using procurement cards from September 2014 through February 2016 totaling \$8,870. The majority of those purchases were for travel-related expenses for the members of the Pension Review Board and Agency personnel. According to the Agency, the procurement cards are physically secured in a locked filing cabinet. In addition, auditors observed that the Agency reconciles procurement card transactions with an internal budget spreadsheet each month. However, individuals authorized to use the Agency's procurement cards were not always current employees. Specifically:

- The Agency's former accountant was still an authorized signer on the Agency's procurement cards until at least January 2016, more than seven months after that individual's last day of employment.
- As of June 2016, another former employee whose last day of employment was in February 2016 was still authorized to use the Agency's procurement cards. However, according to the Agency, it requested that authorization be revoked for that employee in March 2016.

Recommendations

The Agency should:

- Consistently ensure that travel expenditures do not exceed the maximum allowable travel rates and are the most cost-effective option available.
- Consistently retain receipts for all travel expenditures.
- Update and regularly maintain the list of authorized signers for its procurement cards to ensure that authorized signers are current employees.

Appendices

Appendix 1

Objective, Scope, and Methodology

Objective

The objective of this audit was to determine whether the Pension Review Board (Agency) has processes and related controls to help ensure that it administers financial transactions in accordance with applicable statutes, rules, and Agency policies and procedures.

Scope

The scope of this audit covered the Agency's expenditures and activities related to purchasing, travel, payroll, and the related information systems between September 1, 2014, and February 29, 2016. Additionally, auditors performed limited procedures on contracts with a former Agency employee through March 2016.

Methodology

The audit methodology included collecting information and documentation; interviewing Agency staff regarding financial and operational processes; testing documentation related to purchasing, travel, contracting, payroll, and leave accounting; and analyzing and evaluating the results of the tests.

Auditors used professional judgment to select samples of transactions related to purchasing, leave, and pay actions. The samples were not designed to be representative of the population, and results should not be extrapolated to the population. Auditors also tested 100 percent of the individuals the Agency employed during the scope of the audit to determine if those individuals were active employees and were paid appropriately based on their position classifications.

Data Reliability

Auditors used expenditure information in the Uniform Statewide Accounting System (USAS) and payroll data from the Uniform Statewide Payroll/Personnel System (USPS). To determine the reliability of data from USAS and USPS, auditors relied on previous State Auditor's Office work, and reviewed the data for accuracy and completeness by (1) reviewing data query criteria, (2) comparing the data with the Agency's Annual Financial Report, and (3) tracing a sample of selected detailed transactions from the data to source documents. Auditors determined that the expenditure and

payroll data from those systems was sufficiently reliable for the purposes of this audit.

Information collected and reviewed included the following:

- Agency policies and procedures.
- Expenditure data from USAS.
- Employee payroll and leave data from USPS.
- Invoices and supporting documentation for expenditures.
- Travel vouchers and supporting documentation.
- Employee personnel files and leave documentation.
- Supporting documentation for contracts.

Procedures and tests conducted included the following:

- Interviewed Agency staff to identify financial and operational processes, including financial and administrative controls.
- Tested documentation related to purchasing to determine compliance with the Agency's policies and procedures and state laws and regulations.
- Tested a sample of Agency salary expenditures, employee pay actions, and leave transactions for appropriate documentation and required approvals.
- Analyzed selected contract expenditures to determine whether the Agency made contract expenditures in compliance with state laws and regulations.

Criteria used included the following:

- The salary schedules in the State's Position Classification Plan for fiscal years 2015 and 2016.
- The Agency's employee manual.
- The Agency's accounting policies and procedures
- Texas Government Code, Chapters 403, 660, 661, 659, and 2252.
- The General Appropriations Acts (83rd and 84th Legislatures).
- Office of the Comptroller of Public Accounts' travel guidelines.

- *State of Texas Procurement Manual.*
- Title 34, Texas Administrative Code, Chapters 5 and 20.

Project Information

Audit fieldwork was conducted from March 2016 through June 2016. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The following members of the State Auditor's staff performed the audit:

- Hillary Eckford, CIA (Project Manager)
- Link Wilson (Assistant Project Manager)
- Mary Anderson
- Michelle Rodriguez
- Anca Pinchas, CPA, MACy, CIDA, CISA (Quality Control Reviewer)
- Angelica M. Ramirez, CPA (Audit Manager)

Issue Rating Classifications and Descriptions

Auditors used professional judgement and rated the audit findings identified in this report. Those issue ratings are summarized in the report chapters/sub-chapters. The issue ratings were determined based on the degree of risk or effect of the findings in relation to the audit objective(s).

In determining the ratings of audit findings, auditors considered factors such as financial impact; potential failure to meet program/function objectives; noncompliance with state statute(s), rules, regulations, and other requirements or criteria; and the inadequacy of the design and/or operating effectiveness of internal controls. In addition, evidence of potential fraud, waste, or abuse; significant control environment issues; and little to no corrective action for issues previously identified could increase the ratings for audit findings. Auditors also identified and considered other factors when appropriate.

Table 2 provides a description of the issue ratings presented in this report.

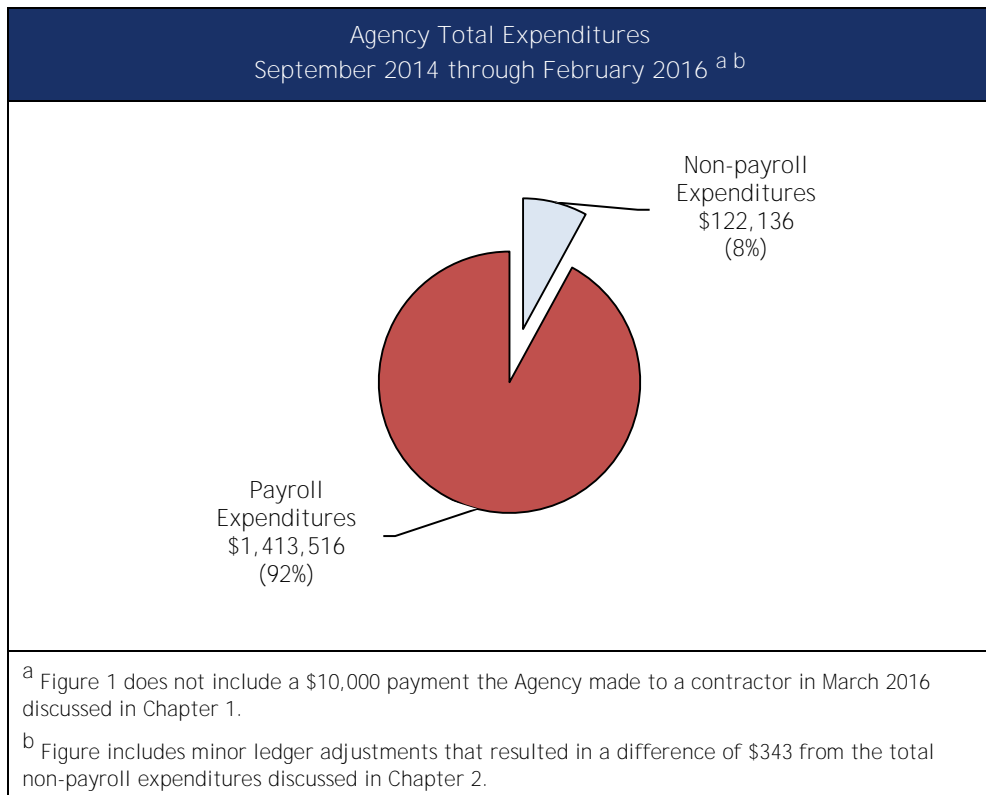
Table 2

Summary of Issue Ratings	
Issue Rating	Description of Rating
Low	The audit identified strengths that support the audited entity's ability to administer the program(s)/function(s) audited <u>or</u> the issues identified do not present significant risks or effects that would negatively affect the audited entity's ability to effectively administer the program(s)/function(s) audited.
Medium	Issues identified present risks or effects that if not addressed could <u>moderately affect</u> the audited entity's ability to effectively administer program(s)/function(s) audited. Action is needed to address the noted concern(s) and reduce risks to a more desirable level.
High	Issues identified present risks or effects that if not addressed could <u>substantially affect</u> the audited entity's ability to effectively administer the program(s)/function(s) audited. Prompt action is essential to address the noted concern(s) and reduce risks to the audited entity.
Priority	Issues identified present risks or effects that if not addressed could <u>critically affect</u> the audited entity's ability to effectively administer the program(s)/function(s) audited. Immediate action is required to address the noted concern(s) and reduce risks to the audited entity.

Summary of Agency Expenditures from September 2014 through February 2016

Figure 1 shows the Pension Review Board's (Agency) total expenditures from September 2014 through February 2016.

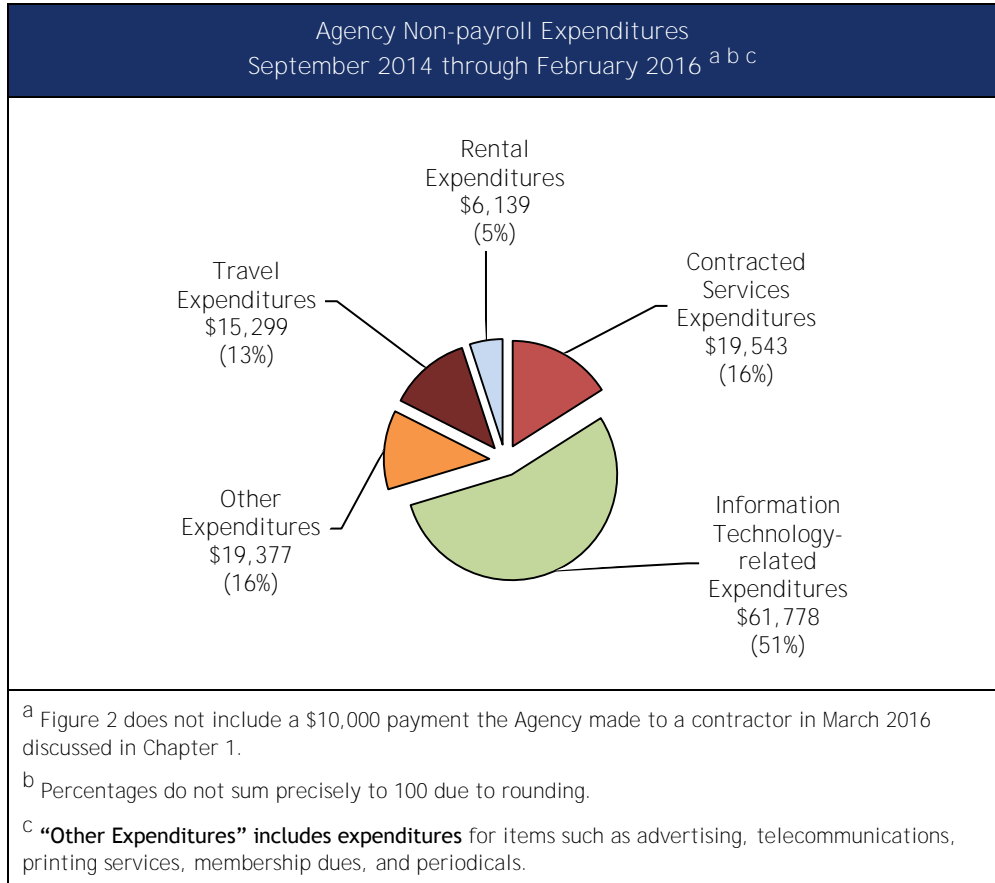
Figure 1



Source: Created by auditors from the Agency's expenditure data in the Uniform Statewide Accounting System.

Figure 2 shows the Agency’s non-payroll expenditures from September 2014 through February 2016.

Figure 2



Source: Created by auditors from the Agency’s expenditure data in the Uniform Statewide Accounting System.

Management's Response



PRB
Texas
Pension
Review
Board

Joshua B. McGee
Chair
Keith Brainard
Vice Chair
Andrew W. Cable
Stephanie V. Leibe
J. Robert Massengale
Robert M. May
Ernest Richards, Esq.

Anumeha "Anu"
Executive Director

Mailing Address:
P.O. Box 13498
Austin Texas 78711-3498

Telephone:
(512) 463-1736
(800) 213-9425

Fax:
(512) 463-1882

Web Site:
www.prb.state.tx.us

Email:
prb@prb.state.tx.us

August 5, 2016

State Auditor's Office
Attn: Hillary Eckford
P.O. Box 12067
Austin, TX 78711-2067

On behalf of the Pension Review Board (PRB), I thank the State Auditor's Office (SAO) audit team for their professionalism and thorough review of our financial processes.

The PRB views these findings as important to continue to establish effective and efficient financial operations that safeguard taxpayer money and serve the public interest of overseeing Texas public retirement systems. We acknowledge our responsibility to comply with all statutory requirements and regulations and agree to implement the auditor's recommendations.

The PRB is proud that the agency's payroll, which represented 91 percent of total expenditures in FY 2015 complied with laws and regulations and no errors were found. The PRB's situation during fiscal years 2015 and 2016 was critical. We are a small agency of fourteen employees. In FY 2015, we had an employee turnover rate of 36 percent, including our only accountant. I was appointed executive director in July 2015 and took actions necessary to sustain critical functions including processing the agency's payroll and invoices.

The PRB is committed to taking all necessary steps to continue to strengthen financial controls and prevent the prior year's issues from reoccurring.

Sincerely,

Anumeha
Executive Director
State Pension Review Board

Attachment



Joshua B. McGee
Chair
Keith Brainard
Vice Chair
Andrew W. Cable
Stephanie V. Leibe
J. Robert Massengale
Robert M. May
Ernest Richards, Esq.

Anumeha "Anu"
Executive Director
Mailing Address:
P.O. Box 13498
Austin Texas 78711-3498
Telephone:
(512) 463-1736
(800) 213-9425
Fax:
(512) 463-1882
Web Site:
www.prb.state.tx.us
Email:
prb@prb.state.tx.us

Management's Response

Chapter 1:

We agree with the findings and have taken the following steps to implement the recommendations:

-- Recognizing the critical need for succession planning, cross-training, and separation of duties, the agency created the deputy director position in October 2015 to assist and backup the executive director. Also, the agency now has two accounting positions.

-- The agency is in the process of updating its financial policies and procedures with detailed and more efficient processes.

-- In June 2016, the agency updated its policies to reflect its current practice of the deputy director approving expenditures. The deputy director has access to the necessary budget and payroll systems and has been approving expenditures since August 2015.

Responsible parties: Executive Director, Deputy Director, Accountant, and Accounting Technician

Implementation date: September 30, 2016

Chapter 2:

The PRB agrees with the findings and will provide staff with additional training on travel requirements. The agency updated the list of procurement card administrators, created an online account to keep the list current, and updated its employee exit checklist to remove administrators from the list when they leave the agency.

Responsible parties: Executive Director, Deputy Director, Accountant, and Accounting Technician

Implementation date: August 31, 2016

Copies of this report have been distributed to the following:

Legislative Audit Committee

The Honorable Dan Patrick, Lieutenant Governor, Joint Chair

The Honorable Joe Straus III, Speaker of the House, Joint Chair

The Honorable Jane Nelson, Senate Finance Committee

The Honorable Robert Nichols, Member, Texas Senate

The Honorable John Otto, House Appropriations Committee

The Honorable Dennis Bonnen, House Ways and Means Committee

Office of the Governor

The Honorable Greg Abbott, Governor

Pension Review Board

Members of the Pension Review Board

Mr. Josh B. McGee, Chair

Mr. Keith Brainard, Vice Chair

Judge Andrew W. Cable

Ms. Stephanie V. Leibe

Mr. J. Robert Massengale

Mr. Robert M. May

Mr. Ernest Richards

Ms. Anumeha, Executive Director



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