

# **ORGANIZATIONAL DEVELOPMENT AND HUMAN RESOURCES**

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## **Compensation and Benefits**

**Audit Report No. ODHR0108**

**June 6, 2008**



**MENTAL HEALTH MENTAL RETARDATION  
AUTHORITY OF HARRIS COUNTY**

**Internal Audit Report**

**AUDITOR'S REPORT**

**Organizational Development and Human Resources**

**Compensation and Benefits**

**Harris County, Texas**

**Internal Audit Report**

**June 6, 2008**

**Henry E. Webb, CFE**

**Internal Auditor**





June 6, 2008

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Executive Director  
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Re: HR / Employee Deductions Audit (Report No. ODHR0108 )

## **BACKGROUND**

The Mental Health and Mental Retardation Authority of Harris County (MHMRA) has formal policies and procedures designed to ensure compliance with the Federal Fair Labor Standards Act (FLSA). The FLSA, first enacted in 1938, establishes minimum wage, overtime pay, record keeping, and child labor standards affecting full-time and part-time workers in the private sector and in federal, state, and local governments. These standards affect more than 100 million workers. The act stipulates that all non-exempt workers in the United States be paid overtime when they work more than 40 hours in a week and also defines which conditions must be met to be exempted from the terms of the law. FLSA is a dynamic instrument, and many of the requirements have been enacted over the years through judicial challenges.

The Act applies to enterprises with employees who engage in interstate commerce, produce goods for interstate commerce, or handle, sell, or work on goods or materials that have been moved in or produced for interstate commerce. For most firms, a test of not less than \$500,000 in annual dollar volume of business applies (i.e., the Act does not cover enterprises with less than this amount of business).

However, the Act does cover the following regardless of their dollar volume of business: hospitals; institutions primarily engaged in the care of the sick, aged, mentally ill, or disabled who reside on the premises; schools for children who are mentally, or physically disabled or gifted; preschools, elementary, and secondary schools and institutions of higher education; and federal, state, and local government agencies.

The Act exempts some employees from its overtime pay and minimum wage provisions, and it also exempts certain employees from the overtime pay provisions alone. The Act does not limit the number of hours in a day or the number of days in a week that an employer may require an employee to work, as long as the employee is at least 16 years old. Similarly, the Act does not limit the number of hours of overtime they may be scheduled. However, the Act requires employers to pay covered employees not less than one and one-half time their regular rates of pay for all hours worked in excess of 40 in a workweek, unless the employees are otherwise exempt.

Employers must keep records on wages, hours, and other information as set forth in the Department of Labor's regulations. Most of this data is the type that employers generally maintain in ordinary business practice.

## Health Care Industry

Hospitals and other institutions “*primarily engaged in the care of the sick, the aged, or the mentally ill*” are covered employers under Section 3(s)(1)(B) of the FLSA. Thus, hospitals, residential care establishments, skilled nursing facilities, nursing facilities, assisted living facilities, residential care facilities, and intermediate care facilities for mental retardation and developmentally disabled must comply with the minimum wage, overtime, and youth employment requirements of the FLSA.

Non-exempt employees must be paid at least time-and-one-half their “regular rate” of pay for all hours worked over 40 in a workweek. The “regular rate” includes an employee’s hourly rate *plus* the value of some other types of compensation such as bonuses and shift differentials. The only remuneration excluded from the regular rate under the FLSA are certain specified types of payments like discretionary bonuses, gifts, contributions to certain welfare plans, payments made to certain profit-sharing and savings plans, and pay for foregoing holidays and vacations.

Under section 7(j) of the FLSA, hospitals and residential care establishments may utilize a fixed work period of fourteen consecutive days in lieu of the 40 hour workweek for the purpose of computing overtime. To use this exception, an employer must have a prior agreement or understanding with affected employees before the work is performed. This eight and eighty (8 and 80) exception allows employers to pay time and one-half the regular rate for all hours worked over eight in any workday and eighty hours in the fourteen-day period.

*“No employer engaged in the operation of a hospital or an establishment which is an institution primarily engaged in the care of the sick, the aged, or the mentally ill or defective who reside on the premises shall be deemed to have violated subsection (a) {work week longer than forty hours unless such employee receives compensation for his employment in excess of the hours at a rate not less than one and one-half times the regular rate at which he is employed} if, pursuant to an agreement or understanding arrived at between the employer and employee before performance of the work, a work period of fourteen consecutive days is accepted in lieu of the workweek of seven consecutive days for purposes of overtime computation and if, for his employment in excess of eight hours in any workday and in excess of eighty hours in such fourteen-day period, the employee receives compensation at a rate not less than one and one-half times the regular rate at which he is employed.”*

An employer can use both the standard 40 hour overtime system and the 8 and 80 overtime system for different employees in the same workplace, but they cannot use both for a single individual employee.

An employer’s work period under 8 and 80 overtime system must be a fixed and regularly recurring 14-day period. It may be changed if the change is designed to be permanent and not to evade the overtime requirements. If an employer changes the pay period permanently, it must calculate wages on both the old pay period and the new pay period and pay the amount that is more advantageous to each employee in the pay period when the change was made.

Premium pay for daily overtime under the 8 and 80 system may be credited towards the overtime compensation due for hours worked in excess of 80 for that period.

## Penalties/Sanctions

The Department of Labor uses a variety of remedies to enforce compliance with the Act’s requirements. When Wage and Hour Division investigators encounter violations, they recommend changes in employment practices to bring the employer into compliance, and they request the payment of any back wages due to employees.

Willful violators may be prosecuted criminally and fined up to \$10,000. A second conviction may result in imprisonment. Employers who willfully or repeatedly violate the minimum wage or overtime pay requirements are subject to civil penalties of up to \$1,000 per violation.

## OBJECTIVES

The overall objectives of the audit were to determine whether the departments:

- Managed and used resources in an efficient, effective, and economical manner
- Administered funds in compliance with applicable laws, regulations, policies and procedures
- Implemented internal controls to prevent or detect material errors and irregularities

The specific objective in this audit was to:

- Determine whether departments are in compliance with the FLSA, and whether controls are in place to adequately govern administration of agency compensation and benefits to employees

## SCOPE

The scope of the work did not constitute an evaluation of the overall internal control structure of the units. The examination was designed to evaluate and test compliance with established policies and procedures and to test the internal control over tested areas and material. The audit scope was from September 1, 2007 through May 31, 2008.

Department management is responsible for establishing and maintaining a system of internal controls to adequately comply with approved policies and procedures. The objectives of an internal control system are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or theft, and that transactions are executed in accordance with management's authorization and are recorded properly.

Because of inherent limitations in any system of internal accounting control, errors or irregularities may occur and not be detected in a timely manner. Also, projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions, or that the degree of compliance with procedures may deteriorate.

The purpose of the audit report is to furnish management independent, objective analyses, recommendations, and information concerning the activities reviewed. The audit report is a tool to help management discern and implement specific improvements. The audit report is not an appraisal or rating of management.

Although due professional care in the performance was exercised, this should not be construed to mean that unreported noncompliance or irregularities do not exist. The deterrence of fraud is the responsibility of management. Audit procedures alone, even when carried out with professional care, do not guarantee that fraud will be detected. Specific areas for improvement are addressed later in this report.

Other minor findings, not included in this report, have been communicated to management and/or corrected during the audit process. Internal Audit would like to thank management and staff for their cooperation throughout the audit.

## METHODOLOGY

In order to meet the objectives, Internal Audit evaluated controls over the compensation and benefits division of Human Resources. This division is responsible for facilitating the Agency's Compensation and Benefits Administration for the agency personnel. This division serves as the point of contact for Agency personnel with questions regarding benefits and compensation (group health, dental, vision, life, long and short term disability, 403(b), 457, 401(a), and flexible spending account administration) and reviewed policies and procedures for compliance and completeness. MHMRA staff was interviewed and audit tests and procedures were conducted as considered necessary.

The sample size and selection were statistically generated using a desired confidence level of 95%, expected error rate of 5%, and a desired precision of +/-5%. Statistical sampling was used in order to infer

the conclusions of test work performed on a sample to the population from which it was drawn and to obtain estimates of sampling error involved. When appropriate, judgmental sampling was used to improve the overall efficiency of the audit.

### **STATEMENT OF AUDITING STANDARDS**

The audit was conducted in accordance with generally accepted government auditing standards (GAGAS). Those standards require that Internal Audit plan and perform the audit to afford a reasonable basis for the judgments and conclusions regarding the organization, program, activity, or function under audit. An audit also includes assessments of applicable internal controls and compliance with requirements of laws and regulations when necessary to satisfy the audit objectives. An audit also includes assessing the estimates, judgments, and decisions made by Agency management. It is believed that this audit provides a reasonable basis for the findings, conclusions, and recommendations.

### **RESULTS**

As a result of the audit procedures and surveys conducted, it was determined that controls over Agency compensation and benefits administration are not adequate. Various internal controls need to be strengthened. These and other items are discussed below.

### **FINDING**

Policy and procedures are not in place to guide Human Resource employees through the process of setting up Agency employee deductions for specific benefits, resulting in multiple errors in the employees selected benefits.

### **RECOMMENDATION**

- It is recommended that Human Resource personnel develop and implement policy and procedures for compensation and benefits selection.

### **Management Response**

*“Management agrees with the need for the documentation of policies and / or procedures to maintain consistency in operations.”*

### **FINDING**

Prior to October 2007, invoices for employee benefits were paid without reconciling benefit amounts from vendor to Agency listing.

### **RECOMMENDATION**

- It is recommended that the division review and reconcile vendor invoices on an on-going basis to ensure accuracy of payments.

### **Management Response**

*“Management agrees with the need for regular reconciliations and is developing enhanced processes for those reconciliations.”*

### **FINDING**

During Agency Open Enrollment, the benefits selected by employees were “finalized” on a daily basis as opposed to the end of the enrollment period.

**RECOMMENDATION**

- \* It is recommended that benefits are “finalized” only when Open Enrollment has closed.

**Management Response**

*“Management agrees with the need for closing enrollment only at the end of the official enrollment period, and is working with vendors, both Empath and Choicelinx to achieve this.”*

**FINDING**

Agency personnel make requests in writing when changes to either increase or decrease a particular payroll deduction, stipulating an effective date and on several occasions; the change date was after the requested effective date.

**RECOMMENDATION**

- It is recommended that requests by Agency personnel to either increase or decrease particular payroll deductions should be completed in a timely manner and document any reasons for variance.

**Management Response**

*“Management agrees with the need for timely entry of employees’ savings requests. However, to many variables may impact that date of actual receipt of employees’ request as compared to the date of entry. Management will develop forms and processes which clearly delineate effective dates of requests.”*

**FINDING**

Due to the large workload in the Compensation and Benefits Division, the department clearly could benefit from an additional FTE. The direct benefit would be seen in Agency customer care.

**RECOMMENDATION**

- It is recommended that the division analyze the ability to fund an additional FTE during the Agency budget cycle.

**Management Response**

*Management agrees and will make appropriate efforts during the budget process for additional staff. This request must be balanced against other needs within the HR department, such as those functions currently supporting the Agency’s wellness program.”*

**FINDING**

Liability accounts, i.e., dental, tax, credit union, and payroll accounts are not being reconciled.

**RECOMMENDATION**

- It is recommended that all liability accounts are reconciled on a regular basis.

**Management Response**

*“Management agrees with the need for the reconciliation and will use any new staff to better distribute the workload to accomplish this task.”*

**FINDING**

The current payroll system, EMPATH, has not been upgraded to allow the Agency to fully utilize the technology available.

**RECOMMENDATION**

- It is recommended that management explore the full functionality of EMPATH to better serve Agency personnel.

**Management Response**

*“Management agrees will the need for better use of the EMPATH system and has recently engaged in both teleconferences and face-to-face meeting with EMPATH. Areas of change that will have the greatest impact on operations at this early stage appear to be in the use of multiple positions, the improved use of global positions, and the use of benefits enrollment.”*

**FINDING**

The division has not been able to plan the work flow of the division due to the workload. Most of the work is done in a “crisis” setting.

**RECOMMENDATION**

- It is recommended that management make an assessment on the day-to-day functions and develop a work flow plan to better serve the Agency.

**Management Response**

*“Management agrees wholeheartedly with this finding. With the recent filing of the long-vacant Director of HR position, the department is now able to focus on larger process issues to facilitate work flow, workload, accuracy, and timeliness.”*

**FINDING**

A review of employee relief timesheets demonstrated that the timesheets are not being reviewed for accuracy prior to submittal for payment to Payroll, differential pay for staff is not consistent across-the-board for staff that meet differential pay standards, Payroll is paying off an faxed time sheets, and timekeepers are not attending mandatory training.

**RECOMMENDATION**

- It is recommended that all relief timesheets are reviewed for accuracy prior to payment.
- It is recommended that the differential pay policy should be revised to be consistent across the board.
- The policy should be reinforced that only original relief timesheets should be sent to payroll.

**Management Response**

*“Management agrees with the need for training and increased focus by the supervisors and timekeepers of relief timesheets. Recently conducted training was well-attended by timekeepers. Management is also in the process of developing a master document to better document the use of differential pay.”*

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Henry E. Webb

-S-

Michele Johnson

Cc: Rose Childs, MSW, CSWM, Deputy Director, Mental Health Division  
Kenneth Collins, LMSW, Deputy Director, Mental Retardation Division  
Barbara Dawson, MSE, Deputy Director, Comprehensive Psychiatric Emergency Program Division  
Daryl Knox, MD, Medical Director, Comprehensive Psychiatric Emergency Program Division  
Sarah Flick, MD, Medical Director, Mental Retardation Services  
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Tom Pederson, CPA, External Audit Firm  
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Tom Hamilton, Ph.D. (Chairman)  
Jane B. Cherry  
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Charles O. Buckner, CPA  
Vicki S. Raynold, CPA  
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**ATTACHMENT A**  
**SUMMARY OF RECOMMENDATIONS**  
**June 6, 2008**

Unit: (ALL) HR / Employee Deductions		
Area: Procedural Audit		
Inherent Risk:      Low <b>Moderate</b> High	Control Environment:    Well Controlled Acceptable <b>Poorly Controlled</b>	Overall Risk:      Low Moderate <b>High</b>
Type of Procedures: <b>Audit</b>		
Scope: * Using Internal Control Evaluation (ICEs) forms, documented internal controls * Conducted a preliminary survey reviewing applicable policies and procedures, etc. * Interviewed various staff, obtained understanding of management controls * Examined detailed receipts, vouchers, and supporting documentation		
Priority Rating: 1 1 1 1 1 1 1 1 1	Audit Recommendations: Develop P&P for Compensation and Payroll Reconcile invoices prior to payment Consult EMPATH/Choicelink for enrollment advice Make timely changes to employees selected benefits Need for additional FTE may be warranted Develop a work flow process for division Ensure relief timesheets are processed properly: original signatures & differential pay (standard) Reconcile liability accounts Upgrade EMPATH functionality	
Follow-up: Six Months		

**Priority Rating**

1. Implement immediately (30 - 90 days) - Serious internal control deficiencies or recommendations to reduce cost, maximize revenues, or improve internal controls that can be easily implemented.
2. Work towards implementing (6 - 18 months) - Less serious internal control deficiencies or recommendations that can not be implemented immediately because of constraints imposed on the unit (i.e., budgetary, technological constraints).
3. Implement in the future (2 - 3 years) - Recommendations that should be implemented but that can not be implemented until significant and/or uncontrolled events occur (i.e. legislative changes, buy and install major systems, requires third party cooperation).