



# **Continuous Audit of Final Average Salary Calculations (Q1 2022)**

**Report Date: March 30, 2022**

**Internal Audit Department**

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**OCERS Internal Audit**  
**Continuous Audit of Final Average Salary Calculations (Q1 2022)**  
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## Audit Objective and Scope

The objective of this audit was to provide an independent review of Final Average Salary (FAS) calculations used in new benefit payments setup by OCERS' Member Services, on a continuous basis.

In response to Internal Audit's 2020 Audits of FAS Calculations, Member Services reorganized the Retirement Program Specialist Team and modified the FAS calculation process including an updated retirement transaction Excel spreadsheet as part of the Management Action Plan. The action plan was implemented in Q2 2021.

In this current audit's scope of Q1 2022, Member Services processed a total of 196 new service and disability retirement benefits. Internal Audit reviewed the FAS calculations for 50 of these benefits.

The audit was conducted in conformance with the International Standards for the Professional Practice of Internal Auditing issued by the International Internal Audit Standards Board.

## Conclusion / Executive Summary

**Opinion: *Opportunities for Improvement***

During our review, Internal Audit noted opportunities exist to improve Member Services' quality control review over FAS calculations.

We noted a 4.0% error rate (two errors) out of the 50 FAS calculations sampled from Q2 2022. The errors resulted in a change of \$35 in the monthly benefit payment for one member and a change of \$2.56 for the other member.

Management has agreed to our observation. See below for additional detail and Management's responses.

## Background

To finalize each retiree's FAS, Member Services uses a retirement transaction Excel spreadsheet. In the spreadsheet, Member Services inputs a preliminary FAS number calculated by the pension administration system (PAS) software after reviewing it, and also inputs other manually calculated pensionable pay amounts not captured or calculated by the PAS software. To calculate these amounts, the Retirement Program Specialist (RPS) must reference a variety of external data sources, such as hourly rate history, timesheet data, reciprocal salary data, and relevant Employer MOUs. A Member Services Quality Assurance team member then reviews the final FAS calculated by the RPS.

Internal Audit independently tested 50 (January and February) of the 196 FAS benefit calculations completed in the Q1 January through March 2022 benefit payroll period, and performed the following:

- Recalculated and traced the preliminary FAS used in the spreadsheet back to the preliminary FAS number calculated by the PAS software.
- Reviewed Member Service’s manual calculations of other pensionable pay item amounts (typically pensionable paid time off, or PTO) manually added to the preliminary FAS and the documentation used by Member Services to support their calculations.

Below is a summary of IA’s error rate noted in the current 2022 audit, plus error rates noted in prior 2020 and 2021 audits:

Quarter	Benefit Applications	Tested by Internal Audit (IA)	IA Error Count	IA Error Rate
Q1/2020	149	82	6	5.8%
Q2/2020	514	56	2	
Q3/2020	108	10	1	8.0%
Q4/2020	466	65	5	
Q2/2021	182	60	4	6.7%
Applications Processed Under the Revised FAS Calculation Procedure				
Q3/2021	75	75	6	8.0%*
Q4/2021	154	134	2	1.5%*
Q1/2022	196	50	2	4.0%*

\*Each of the quarters contained a month with 100% accuracy

Monthly Breakdown of Q1 2022 Quarter Testing				
Month	Benefit Applications	Tested by Internal Audit (IA)	IA Error Count	IA Error Rate
January	59	33	2	6%
February	57	17	0	0%
March	80	0	n/a	n/a

### Important Observation

1. **Internal Audit noted a 4.0% error rate (two errors) with the 50 FAS calculations sampled from the 1<sup>st</sup> quarter of 2022.** The first error occurred due to the erroneous manner in which the reciprocal salary data provided by another pension agency was formatted in Excel. This is a new type of error not found in prior FAS Calculation audits. This error resulted in a change of \$35 in the monthly benefit payment. The second error was due to a previously unknown

PAS software anomaly in which a pay item was incorrectly prorated. This error resulted in a change of \$2.56 in the monthly benefit payment.

In response to the observation, Member Services (M.S.) Management team investigated the first error and engaged CalPERS leadership on the formatting error. Additionally, M.S. Management confirmed other accounts with salary information from CalPERS were formatted and reported correctly. M.S. Management is also training the team to be aware of possible formatting errors from outside agencies using Excel to report data to OCERS.

Regarding the second error, M.S. Management team is working with the PAS software vendor to determine the reason for the error and fix the PAS software to ensure it is following the configuration settings properly. M.S. Management is querying the PAS software to see if this issue has impacted other accounts.

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Audit Committee Members

Observation Details	Management Action Plan (MAP) /MAP Responsible Party / Completion Date
<p data-bbox="415 277 737 310" style="text-align: center;"><b>Important Observation</b></p> <p data-bbox="216 329 957 440"><b>1. Internal Audit noted a 4% error rate (two errors) with the 50 FAS calculations sampled from the 1<sup>st</sup> quarter of 2022.</b></p> <p data-bbox="262 483 957 979">In the first item, a reciprocal agency (CalPERS) provided salary data to OCERS in an Excel format that merged cells erroneously. Because of the merged cells, when Member Services summed this salary data, the summation formula used did not pick up 84 rows of premium pay item data out of a total of 129 rows of data. This resulted in \$17k out of \$24k of premium pay being excluded in the FAS calculation. Member Services was not previously aware of this CalPERS formatting error. This is a new type of error not found in prior FAS Calculation audits. This error resulted in an increase of \$35.43 to a reciprocal monthly benefit payment.</p> <p data-bbox="262 1024 957 1247">For the second item, the error occurred when the PAS software automatically pro-rated a pensionable pay item that was not configured to be prorated by the PAS software. This is a PAS software error. This error resulted in an increase of less than \$3 to the monthly benefit payment.</p> <p data-bbox="262 1292 957 1365">The details of the two errors are noted in the FAS Calculation Summary table below.</p>	<p data-bbox="978 329 1854 829"><b>Management Action Plan:</b> Member Services (M.S.) Management team investigated the first error reported by Internal Audit for this quarter, and we determined that the original data came to OCERS from CalPERS in an Excel spreadsheet that contained improper formatting for the salary records. M.S. management has engaged the leadership team at CalPERS for the department that prepares this information to inform them of the formatting error. We have also reviewed additional member accounts for which we had received salary information from CalPERS to determine if any other accounts had a similar issue. All of the other accounts we reviewed contained spreadsheets that contained merged fields similar to this account, but they were formatted properly and correctly reported final average salary. We are also training our staff to be aware of the possibility of formatting errors from any outside agency using Excel to report data to OCERS.</p> <p data-bbox="978 898 1854 1097">Regarding the second account with an error, M.S. Management team is working with ViTech to determine the reason for the error and fix the PAS software to ensure it is following the configuration settings properly. We are also working to query the PAS software to see if there are any other accounts that may have been affected in a similar way to this account.</p> <p data-bbox="978 1182 1818 1247"><b>Management Action Plan Responsible Party:</b> Jeff Lamberson, Director of Member Services</p> <p data-bbox="978 1317 1493 1349"><b>Completion Date:</b> December 31, 2022</p>

Observation Details	Management Action Plan (MAP) /MAP Responsible Party / Completion Date
<p><b><u>Risk:</u></b> Improperly formatted Excel data from external sources can lead to errors in the monthly benefit paid to OCERS members. A PAS software anomaly can also lead to errors in the monthly benefit paid to OCERS members.</p>	

### Internal Audit - FAS Calculation Summary (Q1 2022)

Sample	Nature of FAS Error	Monthly FAS Error	Monthly Benefit Payment Error	Months With Error
1	<p><u>CalPERS spreadsheet error</u></p> <p>A reciprocal agency (CalPERS) provided salary data to OCERS in an Excel format that merged cells erroneously. Because of the merged cells, when Member Services summed this salary data, the Excel summation formula used did not pick up 84 rows of premium pay item data out of a total of 129 rows of data. This resulted in \$17k out of \$24k of premium pay being excluded from the FAS calculation. Member Services was not aware of this CalPERS formatting error.</p> <p>Cells merged erroneously within a spreadsheet can give the false impression to a user that rows or columns of data are captured by a formula inserted by the user. However, identifying and re-formatting merged cells can help avoid this error.</p>	Original monthly FAS of \$6,218.83 understated by \$479.50.	Original monthly benefit of \$459.57 <b>underpaid by \$35.43.</b>	1 month
2	<p><u>Pension Administration System (PAS) software error</u></p> <p>The error occurred when the PAS software automatically pro-rated a pensionable pay item that was not configured to be prorated by the PAS software. This particular premium pay item is paid as a lump sum amount per pay period and should not get prorated when the FAS is calculated, as compared to premium pay items paid hourly and which should be prorated.</p>	Original monthly FAS of \$14,280.06 understated by \$4.15.	Original monthly benefit of \$8,825.93 <b>underpaid by \$2.56.</b>	1 month



### **Categories of Observations (Control Exceptions):**

#### **Priority Observations:**

These are observation(s) that represent critical exceptions to the audit objective(s) and/or business goals. Such conditions may involve either actual or potential large dollar errors or be of such a nature as to compromise OCERS' reputation or integrity. Management is expected to address Priority Observations brought to its attention immediately.

#### **Important Observations:**

These items are important to the process owner and they do impact the control environment and/or could be observations for improving the efficiency and/or effectiveness of OCERS' operations. Management is expected to address within six to twelve months.

### **Management's Responsibility for Internal Control**

Management has primary responsibility for establishing and maintaining the internal control system. All levels of management must be involved in assessing and strengthening internal controls. Control systems shall be continuously evaluated by Management and weaknesses, when detected, must be promptly corrected. The criteria for evaluating an entity's internal control structure are the Committee of Sponsoring Organizations of the Treadway Commission (COSO) Internal Control – Integrated Framework. Our Internal Control Audit enhances and complements, but does not substitute for department management's continuing emphasis on control activities and self-assessment of control risks.

### **Internal Control Limitations**

Because of inherent limitations in any system of internal control, errors or irregularities may nevertheless occur and not be detected. Specific examples of limitations include, but are not limited to, resource constraints, unintentional errors, management override, circumvention by collusion, and poor judgment. 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 the degree of compliance with the procedures may deteriorate. Accordingly, our audit would not necessarily disclose all weaknesses in the department's operating procedures, accounting practices, and compliance with OCERS' policies.

### **Audit Report Opinions:**

#### **Satisfactory:**

No issues or a limited number of “Important Observations” (typically no more than two Important Observations).

#### **Opportunities for Improvement:**

Multiple issues classified as “Important Observations” (typically two or more Important Observations) with no more than one “Priority Observations”.

#### **Inadequate:**

Usually rendered when multiple issues are classified as “Priority” ” (typically one or more Priority Observations), together with one or more other issues classified as “Important Observations”. The Priority Observations identified have a major effect on processes, plan sponsors/members, financials, and/or regulatory requirements.