



August 29, 2022

Benefit Payroll Process Audit

# City of Milwaukee Employees' Retirement System

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# Table of Contents

Background.....	3
Internal Controls Assessment Objectives and Scope .....	3
Procedures Performed .....	4
Audit and Assessment Results – Executive Summary .....	5
Observations, Recommendations, and Management Responses.....	7
Closing.....	8
Appendix .....	9



# Background

At the request and direction of the Administration and Operations (A&O) Committee, an audit of the Benefit Payroll Process and controls for the City of Milwaukee Employees' Retirement System (CMERS) was performed during the period from May 1, 2022 through June 30, 2022. The audit was requested to review, evaluate, and test the organization's Benefit Payroll process against leading practices, test controls and determine whether control deficiencies existed within the internal control environment or whether there were identified control design or operating deficiencies. This audit cannot be relied upon to disclose errors, fraud, or noncompliance with laws and regulations.

## Internal Controls Assessment Objectives and Scope

The objective of the Benefit Payroll Process Audit was to review, evaluate, and test processes and controls currently in place against leading practices and evaluate operating effectiveness. The focus of the assessment was to address the following risks:

1. Assess the suitability of the design for process and controls over Benefit Payroll Process, including the inherent risk of inaccurate payments.
2. Assess the governance and accountability over the Accounting and Financial Reporting process, as well as the inherent risks from misappropriation, fraud, and abuse.
3. Compare current state internal controls versus leading practices and test for operating effectiveness.
4. Propose future state changes that mitigate risk or enhance CMERS' internal control structure and outcomes.

*The following processes and sub-processes are in-scope, as well as segregation of duties in each area:*

The objective of the Benefit Payroll Process Audit included the review of processes and controls related to the design and test of operating effectiveness, including:

1. Benefit Payment Disbursement Process and Controls
  - a. Bank Authorization
  - b. Expected Changes Analysis
  - c. Benefit Participant Audit
  - d. Duplicate Payment Application Controls
  - e. Participant Death Notice Review
  - f. Benefit Payment Adjustments (COLA)
2. Benefit Payment Reconciliation and Approval Processes
  - a. Disbursement Reconciliations
    - i. Positive Pay
    - ii. ACH Balancing
    - iii. Manual Checks
  - b. Benefit Payment Approval Process
3. Compliance Reporting
  - a. Participant Withholding Taxes
  - b. 1099 Reporting
4. System Access Restrictions
  - a. User System Access Review and Approval
  - b. Physical Access Controls
  - c. Segregation of Duties
  - d. Policies and Procedures
5. Organizational Resilience
  - a. Review and Update of Standard Practice Instructions (SPIs)



## Procedures Performed

The Benefit Payroll Process Audit was performed in collaboration with members of CMERS.

As part of the audit, various techniques were used to audit and assess the effectiveness of the internal controls, including:

1. Interviewed members of CMERS
  - a. Dan Gopalan, Chief Financial Officer
  - b. Terry Siddiqui, IT Consultant
2. Gathered supporting documents describing current state processes (e.g., policies, procedures, screenshots, flowcharts, reconciliations, analyses, etc.)
3. Gathered evidence and tested CMERS processes and controls for the following functions;
  - a. Benefit Payment Disbursement Process and Controls
  - b. Benefit Payment Reconciliation and Approval Process
  - c. Compliance Reporting
  - d. System Access Restrictions
  - e. Organizational Resilience
4. Ranked current-state processes against five levels of maturity definition (1. Initial; 2. Repeatable; 3. Defined; 4. Managed; and 5. Optimized)

We would like to acknowledge and thank management with whom we interacted. The time, effort, and discussions they provided were instrumental in our understanding and provided the necessary information to complete our project. During our assessment and audit, management and personnel provided all the materials requested and answered all of our questions promptly. Below is the executive summary of our findings.

# Audit and Assessment Results – Executive Summary

All the established processes and controls that were assessed during the audit were rated as Defined Maturity\*: Management has established defined and documented formalized processes, procedures, and transaction flows that are regularly updated. This level of maturity is considered suitable for these control environments by management and internal audit.

PROCESS MATURITY DEFINITIONS				
*DEFINED MATURITY	Policies and processes are established and are reviewed and updated as needed, e.g., annually to reflect changing business needs; preventive and detective controls are employed but are primarily reliant on manual activities; performance monitoring is performed using a mix of manual and automated processes. <i>See Appendix for all Maturity Definitions.</i>			
Processes	Control Description	Control Deficiency?	Issues Identified	Process Maturity Level
<b>Benefit Payment Disbursement Process and Controls</b>	Wells Fargo Bank Signatories are regularly reviewed and updated. Annually the Signatories list is approved by CMERS A&O Committee.	No	None	<b>Defined</b>
	Every month, CMERS will prepare the <u>Expected Changes Spreadsheet</u> that details retiree activity, e.g., deaths, new retirees, recalculations, etc. The spreadsheet creates a comparison between the actual activity recorded in MERITS and the changes expected by management. All variances between expected and actual changes are investigated and explained every month. Once the spreadsheet has been prepared, it is reviewed and approved by management.	No	None	
	As part of management’s monthly benefit payment process, Management will perform an independent audit through MERITS workflow to ensure that all changes to member records and payment files are accurate and valid. If during the audit a participant’s records are identified with an issue, Management will investigate the issue and determine the corrective actions.  Corrective actions to participant records can only be accomplished with two ERS employees, one to make the change and another employee to approve the change.	No	None	
	The MERITS system will not allow a Duplicate Payment to be made to a plan participant.	No	None	
	CMERS has established procedures to proactively identify deceased retirees and prevent erroneous	No	None	



	<p>retiree payments. Using Lexis-Accurint, a search tool, management will search for deceased retirees every month. In the event a retiree is identified as being deceased, the retiree’s death notice is reviewed by management to determine if the benefit payment should be returned. If it is determined that the benefit payment is to be refunded to CMERS, management approves the creation of the receivable, and it is recorded by CMERS in the Receivable Log. The Receivable Log is reviewed monthly by management.</p> <p>At the time the receivable is established, the deceased retiree’s benefits are halted and a lock on the deceased retiree’s benefit payments is created in MERITS to prevent future payments.</p>			
	<p>Cost of Living Adjustment (COLA) table/schedules are used in MERITS to calculate increases in Participant Benefit Payments. COLA adjustments are reviewed every year and updated appropriately. Any change to the COLA table/schedule must be properly supported and approved by an individual who was independent and knowledgeable of the process.</p>	<b>No</b>	<b>None</b>	
<b>Benefit Payment Reconciliation and Approval Processes</b>	<p>Every month, ERS will reconcile the benefit payment records that were made using Positive Pay, ACH, and Manual Checks and Check Stock to the supporting disbursement records. The reconciliation is prepared by Pension Analyst and is approved by the Pension Accounting Manager. Once the reconciliation is complete, it is incorporated into the Monthly Funds Transfer Package.</p>	<b>No</b>	<b>None</b>	<b>Defined</b>
	<p>Once the Benefit Payment records have been reconciled, the reconciliation and the supporting documents are accumulated into the Monthly Funds Transfer Package and is submitted to the CFO and Executive for review and approval Director for review and approval. Once the Funds Transfer package is approved the monthly benefit payments are distributed to the benefit participants.</p>	<b>No</b>	<b>None</b>	
<b>Compliance Reporting</b>	<p>Federal and State withholding taxes are calculated using withholding tables/schedules used within MERITS. These tables are updated annually and are reviewed by an individual independent and knowledgeable of the process.</p> <p>After the withholding taxes have been prepared, the calculations and supporting documentation are then reviewed and approved by management.</p>	<b>No</b>	<b>None</b>	<b>Defined</b>



	Benefit Payment Participant 1099's are properly supported, reconciled, and reviewed by management before they are mailed to the IRS and the State of Wisconsin Department of Revenue. This work is done in a timely manner to ensure that 1099 mailing deadlines were met.	<b>No</b>	<b>None</b>	<b>Defined</b>
<b>System &amp; Physical Access Controls</b>	Employee access to CMERS systems is reviewed by management twice a year to ensure that ERS's employees and business partners have the appropriate system access, and that no "high-risk" Segregation of Duties conflicts exist.	<b>No</b>	<b>None</b>	
	Participant Files containing sensitive member information are secured in locked filing cabinets in the filing room at the end of each day. The filing room is also locked at the end of each day to further ensure the security of the files.  In addition, internal organization policies and system controls are in place that guide and control employee access to member Personal Identifiable Information (PII) that are regularly reviewed and monitored by CMERS management.	<b>No</b>	<b>None</b>	
<b>Organization Resilience</b>	Standard Practice Instructions (SPIs) are regularly reviewed and updated by management to reflect current processes and controls.	<b>No</b>	<b>None</b>	<b>Defined</b>
	Management regularly cross trains and evaluates department personnel as to their ability to competently perform duties outside of the employee's current role and responsibilities.	<b>No</b>	<b>None</b>	

*Following the conclusion of our testing of CMERS Internal Control Environment, we identified No Internal Control Deficiencies.*

## Observations, Recommendations, and Management Responses

None.



# Closing

We wish to extend our appreciation to management and staff for their timely cooperation and assistance during the project.

\* \* \* \* \*

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# Appendix

## Maturity Definitions

Capability Level	Capability Description	Capabilities Attribute
<b>5. Optimized</b>	Policies and processes are continuously reviewed and improved within a highly automated control environment.	<ul style="list-style-type: none"> <li>• Processes and controls are continuously reviewed and improved</li> <li>• Preventive and detective controls are highly automated to reduce human error and cost of operation.</li> <li>• Comprehensive, defined performance metrics exist, with extensive automated performance monitoring.</li> <li>• Extensive use of best practices, benchmarking, and/or self-assessment to continuously improve process.</li> </ul>
<b>4. Managed</b>	Policies and processes are documented, standardized, regularly updated and controls increasingly use automation.	<ul style="list-style-type: none"> <li>• Procedures and controls are well documented and kept current.</li> <li>• Preventive and detective controls are employed, with greater use of automation to reduce human error.</li> <li>• Many metrics are used with a blend of automated and manual performance monitoring.</li> <li>• Best practices and/or benchmarking are used to improve process</li> </ul>
<b>3. Defined</b>	Policies and processes are established, are reviewed, and updated as needed (e.g., annually) to reflect changing business needs; preventive and detective controls are employed but are primarily reliant on manual activities; performance monitoring is performed using a mix of manual and automated processes.	<ul style="list-style-type: none"> <li>• Procedures are well documented, but not kept current to reflect changing business needs.</li> <li>• Preventive and detective controls are employed, still reliant on manual activities.</li> <li>• Some metrics are used, but performance monitoring is still manual and/or infrequent.</li> <li>• Generally occurs during periodic (e.g., annual) policy and procedure renewal.</li> </ul>
<b>2. Repeatable</b>	Some standard processes are defined, and success depends largely on "tribal knowledge" and detective controls.	<ul style="list-style-type: none"> <li>• Some standard procedures exist, relies on "tribal knowledge."</li> <li>• Mostly detective are in place, minimal preventive controls, and highly manual.</li> <li>• Few performance metrics exist, thus performance monitoring is inconsistent or informal.</li> <li>• Most likely in reaction to audits or service disruptions.</li> </ul>
<b>1. Initial</b>	Few processes are defined, and success depends on individual effort and heroics.	<ul style="list-style-type: none"> <li>• No formal procedures exist.</li> <li>• Controls are non-existent or primarily in reaction to a "surprise."</li> <li>• There are no metrics or performance monitoring.</li> </ul>

