Tempe
Internal Audit

# Memorandum

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|---|---|
| TO: | Lara Calder, Financial Services Director |
| | Rebecca Strisko, Human Services Director |
| THRU: | Bill Greene, City Auditor (X8982) |
| FROM: | Jacqueline Gerald, Sr. Auditor |
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| | Kara Stanek, Sr. Assistant City Attorney |
| | Anthony Butch, Assistant Fire Chief |
| | Darrell Duty, Interim Fire Chief |
| | Kathy Ferguson, Payroll Supervisor |
| DATE: | January 30, 2025 |
| SUBJECT: | FINAL REPORT: PAYROLL OVERTIME AUDIT |

Attached is our final report on the subject audit. Copies of this report will be distributed to the mayor and council and posted to the Internal Audit Office website.

Thank you and your staff for your cooperation during this project.

# Citywide Overtime

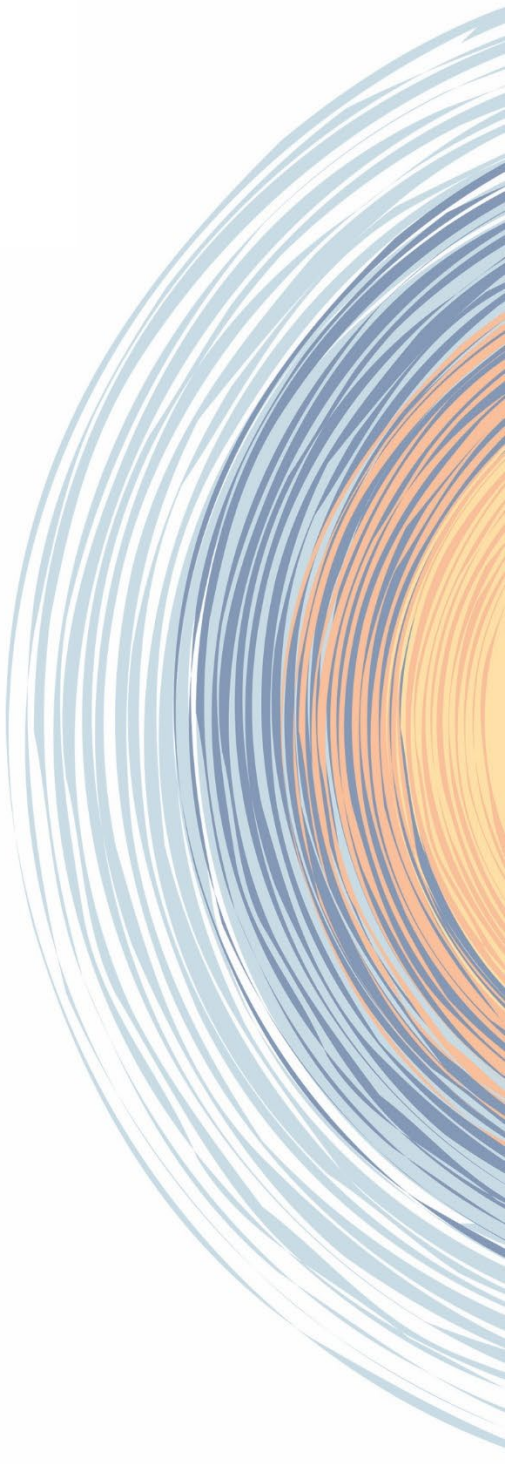
January 30, 2025


Project Team:

Bill Greene, City Auditor
Jacqueline Gerald, Sr. Auditor


Mission Statement

To enhance and protect organizational value by providing high-quality, objective, risk-based audit and consulting services to assist the City in accomplishing strategic priorities, goals, and objectives.




Tempe
Internal Audit

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## Executive Summary

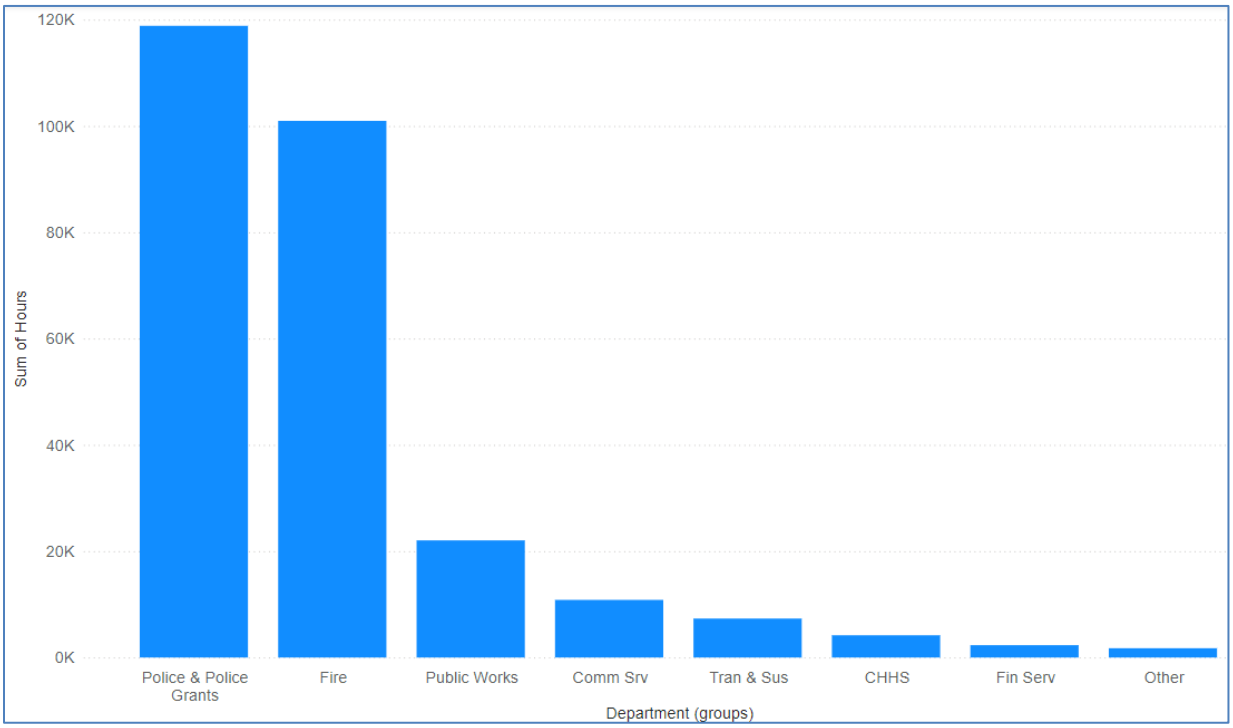
We assessed whether the internal controls over overtime reporting are sufficient to ensure that overtime pay is:

- Accurately calculated, processed, and reported,
- Compliant with applicable laws and regulations, and
- Aligned with the organization's established policies and procedures.

## Background

In fiscal year 2023-2024, City of Tempe (City) employees worked over 267,800 hours of overtime, totaling approximately $14.9 million dollars. The Police and Tempe Fire and Medical Rescue (TFMRD) departments incur most of the overtime (See following Table):

**Fiscal Year 2023-2024 Overtime Hours**



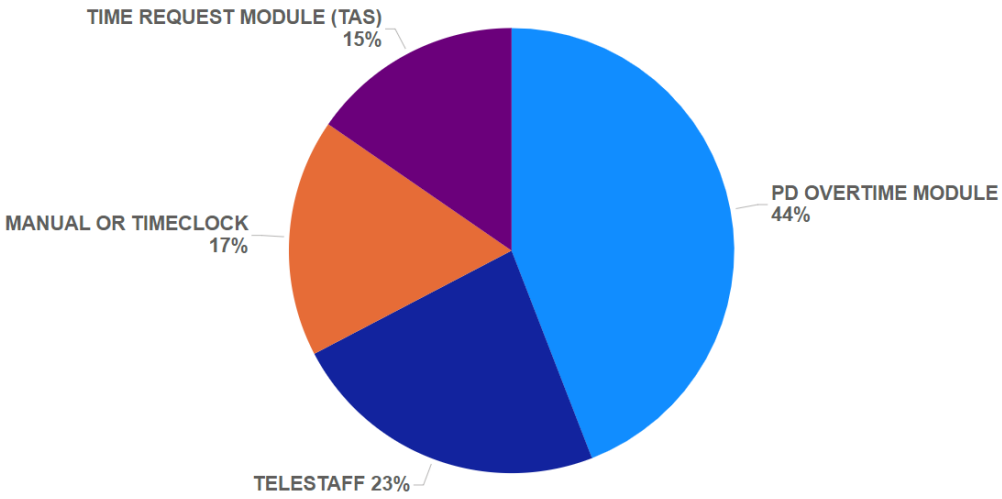

The City currently uses the PeopleSoft payroll system, which is scheduled for replacement within the next five years. PeopleSoft operates on an exception-based model, meaning only deviations from standard work schedules (such as overtime) require manual entry and approval each pay period. Given the City's large workforce, it is crucial to ensure accurate overtime calculations and compliance with Payroll policies, Memorandums of Understanding (MOUs), and the Fair Labor Standards Act (FLSA)[1].

[1] The FLSA is enforced by the Wage and Hour Division of the Department of Labor.

The FLSA mandates overtime pay at one and a half times the regular rate for hours worked beyond 40 per week, with exceptions for sworn firefighters who are paid overtime for hours worked over 105.76 per 14-day pay period.

In the City, there are four systems that employees use to report overtime hours worked (See Chart below). Each system has its own internal controls to ensure overtime is approved and accurately uploaded to PeopleSoft prior to the biweekly processing of payroll.

**Hours of Overtime Entered by System for Fiscal Year 2023-24**




Reporting errors and miscalculations can lead to financial penalties, legal issues, and damage to employee morale.

## Results in Brief

***Our audit identified several areas where City overtime calculations were not in alignment with FLSA requirements. A multi-departmental review and potential consultation with the U.S. Department of Labor (DOL) may be needed to address some of these issues.***

Some areas of noncompliance can be addressed through policy or procedural updates, while others are embedded within the PeopleSoft system, making them more complex and time-consuming to resolve. A comprehensive review by the Finance Department's Payroll Section, Human Resources, Legal Department, and the City Manager's Office will be required to assess risks and determine the best corrective actions. Payroll has previously flagged these issues, but challenges in identifying and implementing the solutions have persisted. For example:

- PeopleSoft's use of an 80-hour pay period, rather than 40-hour work week, can lead to incorrect overtime calculations for non-exempt employees, especially when they earn premium or bonus pay.

- PeopleSoft incorrectly calculates overtime pay when overtime hours are worked in one pay period but submitted for payment in a following period.

- The City offers many nonexempt employees the option of a 9/80 work schedule. To comply with FLSA, a 9/80 work schedule needs two pay periods with a 40-hour cutoff. PeopleSoft currently cannot accommodate this requirement. Strict monitoring is also necessary to avoid unintended overtime.

The upcoming PeopleSoft system replacement offers an opportunity to ensure full FLSA compliance. A well-planned requirements phase is essential to define the new system's capabilities and goals, including adherence to FLSA overtime regulations. This will also necessitate updating payroll policies and procedures to support compliance.

Our detailed report contains recommendations to improve internal controls and increase compliance with FLSA requirements, including a list of recommended capabilities that should be required when PeopleSoft is replaced.

## Department Responses to Recommendations

| | |
|---|---|
| **Rec. 1.1**: Payroll, HR, and the City Attorney's Office collaborate to develop a jointly agreed-upon recommendation to address work schedules that may result in FLSA non-compliance, such as the 9/80 schedule for nonexempt employees. The recommended plan should include mitigation strategies and a detailed transition roadmap and be presented to the City Manager's Office for review and approval, prior to implementation. Implementation should occur before migrating to the new ERP to avoid heavy customization. | |
| ***Response*:** All non-exempt staff on 9/80 schedule will be migrated to either 5/8, 4/10 or hybrid. | ***Target Date*:** 2/28/2025 |
| **Rec. 1.2**: Payroll, HR and IT collaborate to develop a jointly agreed-upon plan to address automated overtime calculations that result in FLSA non-compliance by the PeopleSoft system. If corrections cannot feasibly be programmed prior to the migration to a new ERP, then they should be included as standard requirements in the new system. | |
| ***Response*:** Accounting (Payroll) will work with the IT Peoplesoft Team to change the additional pay types, Bonus, Premium and DROP to be excluded Regular Rate Calculation, where appropriate in line with FLSA rules.<br>Accounting (payroll) will work with IT Peoplesoft team to configure Peoplesoft so it calculates on 40 not 80 hours. | ***Target Date*:** 6/30/25 |
| **Rec. 1.3**: Payroll work with HR and the Law Department to review the calculation of DROP payments in PeopleSoft and determine if modifications are needed. | |
| ***Response*:** Accounting (Payroll) will work with the IT Peoplesoft Team to change the DROP to be excluded Regular Rate Calculation.<br>Accounting (Payroll) will work with IT Peoplesoft team to configure Peoplesoft so it calculates on 40 not 80 hours.<br>Accounting (Payroll) will add to the requirements for the new ERP. | ***Target Date*:** 6/30/25 |
| **Rec. 2.1**: Payroll implement additional controls to reduce the risk of Timekeepers making changes to prior period exception pay during payroll processing. | |
| ***Response*:** Accounting (Payroll) will work with Peoplesoft IT Team to set cut off dates and enable retroactive payroll adjustments in order to handle changes to payroll hours by making adjustments to the appropriate historical period and including those adjustments in the current payroll period.<br>Accounting (Payroll) will add to the requirements for the new ERP. | ***Target Date*:** 6/30/25 |

| | |
|---|---|
| **Rec. 2.2**: For future paramedic hires, TFMRD should implement a weekly reconciliation process to ensure the amount of prepaid overtime can be determined upon employee shift change or separation from the City, and implement a policy of allowing paramedics to initially, and upon shift changes, join the pay equalization program only during a pay period with 96 or fewer hours followed by either 128 or 120 hours. | |
| ***Response*:** Upon the hiring of Paramedics and EMTs, OT will be paid based only on hours worked. Once the new hires enter a pay period with 96 or fewer hours followed by either 128 or 120 hours, they will enter the pay equalization program.<br><br>Staffing of the members for the initial placement will be made to place members on the needed shift in coordination with the request of the 96 or fewer hours followed by either 128 or 120. | ***Target Date*:**<br>02/01/2025 |
| **Rec. 2.3**: TFMRD consider the need to reconcile, and monitor going forward, prepaid overtime hours for all current paramedics who did not join the pay equalization program during a pay period with 96 or fewer hours followed by either 128 or 120 hours, or who have switched shifts in the past to determine their true prepaid overtime balance. | |
| ***Response*:** An audit of current members will be conducted to evaluate any pay issues based on the concerns outlined in the audit. | ***Target Date*:**<br>07/01/2025 |

# 1 – Overtime Accuracy and Compliance with FLSA

## Background

As a municipal employer of a large work force, it is important that the City accurately calculate overtime and adhere to the Fair Labor Standards Act (FLSA). The FLSA is recognized as one of the foundations of U.S. labor law. It establishes protections for workers including mandating a minimum wage and overtime pay. Per the DOL website, the goal of the FLSA is to protect and enhance the welfare of the Nation's workforce.

While overtime is typically calculated as one and one-half times the employee's regular hourly wage, the FLSA outlines specific exemptions which can complicate some calculations. The FLSA also provides a strict definition of employees' regular hourly wages and mandates how to calculate them. Per the Enforcement section of the Reference Guide to the FLSA available on the DOL website, miscalculations in overtime pay can lead to significant financial repercussions, including back wages, penalties, and legal fees. Additionally, our research, based on articles by subject matter experts, found a strong consensus that FLSA compliance is crucial for maintaining ethical labor practices, boosting employee morale, and preventing costly legal disputes.

According to the FLSA, all employees must be paid at least one and one-half times their regular rate of pay for all hours worked over 40, except for sworn firefighters. Firefighters must be paid at least one and one-half times their regular rate of pay for all hours worked over 212 hours per The City's designated 28-day pay period (106 hours per pay period). The City's official workweek starts on Monday at 12:01 AM and ends on the following Sunday at midnight with two work weeks per pay period.

## Approach

To determine whether overtime is being calculated accurately and in compliance with FLSA regulations, we performed the following:

- Research of FLSA regulations: researched the Department of Labor website, which is the primary source of information on FLSA regulations. This website included a regulatory library, interpretive guidance, resources for employers, links to other helpful sites, fact sheets and frequently asked questions and answers regarding the calculation of overtime.
- Document Review: examined payroll policies and procedures relevant to the calculation of overtime and employee handbooks to ensure they align with FLSA regulations.
- Expert Consultations: consulted with the City's Payroll and Human Resource (HR) professionals, who are knowledgeable about The City policies and practices concerning FLSA compliance, particularly regarding overtime.
- Employee interviews: conducted interviews with department timekeepers to assess their understanding of overtime policies and timekeeping practices.

- System review: we evaluated PeopleSoft's overtime configuration and import controls as they related to overtime.
- Data analysis: utilized data analytic tools to identify patterns, anomalies, and trends in overtime hours and payroll data.
- Sample testing: recalculated samples of overtime pay to determine accuracy and compliance with FLSA.

## Results

***Overtime was calculated accurately when employees earned no premium or bonus pay in addition to their regular base pay.***

We reviewed paycheck information for 2,335 employees paid during the sample pay period ending August 11, 2024. Of the 807 employees who received overtime under the pay code "OT", we focused on those without premium or bonus pay. For all 293 employees in this group, overtime calculations were correct. We could not verify overtime accuracy for the remaining 514 employees due to system complications involving premium and bonus pay as discussed below.

***A multi-departmental review, along with potential consultation with the DOL, is needed to assess several possible areas of misalignment with FLSA overtime pay calculation requirements.***

We noted several areas where City practices do not conform to FLSA guidance:

- Calculation of the regular rates not consistent with FLSA - PeopleSoft calculates non-exempt employees' regular rate of pay based on an 80-hour pay period rather than 40-hour pay week as required by FLSA. This will lead to an incorrect calculation of overtime in many cases where the employee earned premium, or bonus pay during the pay period in addition to regular pay.

| Overtime Calculation Example | | | | | |
|---|---|---|---|---|---|
| Per FLSA Regulations | | | | Per PeopleSoft | |
| | Week 1 | Week 2 | Total Pay | Total Pay | Difference |
| Regular hours | 40 | 40 | | 80 | |
| Overtime | 10 | 0 | | 10 | |
| Total Hours | 50 | 40 | | 90 | |
| Hourly Rate | $20.00 | $20.00 | | $20.00 | |
| Reg Pay | $1,000.00 | $800.00 | | $1,800.00 | |
| Bonus Pay | $50.00 | $0.00 | | $50.00 | |
| Total Wages | $1,050.00 | $800.00 | | $1,850.00 | |

| | | | | | |
|---|---|---|---|---|---|
| Regular Rate | $21.00 | $20.00 | | $20.56.00 | |
| Additional 50% Hrly Overtime Pay | $10.50 | $0.00 | | $10.28 | |
| Additional OT Pay | $105.00 | $0.00 | | $102.78 | |
| **Total Pay** | $1,155.00 | $800.00 | **$1,955.00** | **$1,952.78** | **-$2.22** |

Additionally, PeopleSoft incorrectly calculates overtime pay when overtime hours are worked in one pay period but submitted for payment in a following period. The system bases overtime rates on the regular pay of the pay period in which the overtime is submitted, not the pay period when the overtime was worked. This leads to underpayment for employees who earned additional premium or bonus pay in the pay period when the overtime was earned but not when it was submitted. Likewise, overpayments can occur when employees earn additional premium pay in the pay period that overtime was submitted but not when it was earned. Ideally, the system should be able to determine the correct overtime by calculating a new regular rate for the pay period in which the overtime was worked, and then roll forward any adjustments to the current pay period as needed.

- Totaling bi-weekly hours for flexible work schedules - The City offers many nonexempt employees the option of a 9/80 work schedule, which consists of four nine-hour days and one eight-hour day in the first work week, followed by four nine-hour days in the second work week of the pay period. Employees effectively work one 44-hour week and one 36-hour week within each pay period, totaling 80 work hours for the pay period. While this schedule does not violate FLSA regulations for exempt employees, nonexempt employees must be paid overtime for hours worked over 40 per work week.

  We identified 140 nonexempt employees working a 9/80 schedule, which, if calculated as specified by *FLSA Fact Sheet 56A: Overview of the Regular Rate of Pay Under the FLSA* (12/2019), resulted in approximately 14,560 hours of overtime not being paid at an overtime rate. The potential overtime cost component of these hours to the City is approximately $374,000 per year (See following Table).

**Potential Financial Impact of 9/80 Schedules for Non-Exempt Employees**

| | Estimated Value |
|---|---|
| Hours Not Paid at Overtime Rate | $1,122,000 |
| Leave Hours Not Taken | $ 748,000 |
| Net | $ 374,000 |

To comply with FLSA regulations, a nonexempt employee's 9/80 work schedule would need to be structured across two pay periods. The first pay period would end precisely at 40 hours (typically noon on Friday). The second pay period then begins immediately after (at noon on the same Friday). This arrangement effectively transfers four hours from one pay period to the next. However, PeopleSoft cannot

currently accommodate the splitting of a workday into separate pay weeks. In addition, strict monitoring and record-keeping would be essential. Any schedule adjustments, such as changing the flex day or lunch hour, could unintentionally change work week hours and thus create a need for overtime pay.

Our review of the 140 nonexempt employees on 9/80 schedules showed that all workweeks began on Monday, with alternating 44- and 36-hour weeks. Payroll staff confirmed that the City does not currently adhere to the required 40-hour workweek split and has previously raised concerns about this.

A survey of four neighboring municipalities showed that all allowed the traditional 9/80 schedule for exempt employees only. However, some offered an alternating 4/10 and 5/8 bi-weekly schedule for nonexempt employees, which provides a similar benefit without FLSA compliance issues.

- Prepayment overtime plan: Paramedics generally work 24-hour shifts that result in highly fluctuating paychecks. To address this, TFMRD implemented a prepayment pay equalization program. Under this plan, paramedics receive a consistent paycheck comprising 40 hours at their regular rate and 16 hours at the overtime rate. When working less than 56 hours in a week, the pay difference is considered an advance against future overtime hours. According to the City's Equalized Payroll Agreement for Civilian Paramedics, overtime shall be reconciled at the end of each bi-weekly pay period to ensure that all overtime hours worked in each individual week have been compensated at the overtime rate, and at the end of employment any advanced overtime is to be deducted from their final paycheck.

  The Department of Labor's Opinion letter regarding prepayment plans dated January 7, 2005, listed two requirements for a prepayment plan to comply with FLSA:
  - The use of a system whereby the employer can maintain a running account for each employee of the amount to the employer's credit.
  - At no time may the employer owe the employee overtime compensation. In any workweek in which the prepayment credits are not sufficient to equal the additional overtime due the employee, the difference must be paid on the next payday.

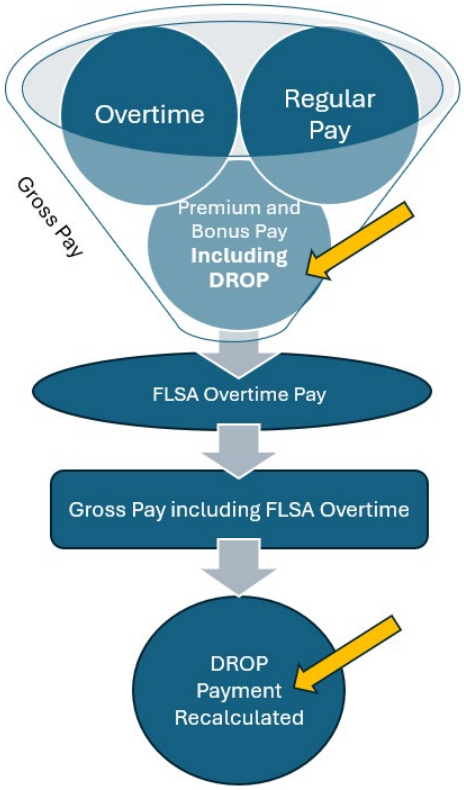
  The TFRMD Equalized Payroll Agreement, while designed to align with FLSA regulations, is currently not being fully implemented. Prepaid overtime for paramedics is not reconciled week-to-week meaning Payroll staff are likely not withholding the correct amount of prepaid overtime from the final checks of some civilian paramedics terminating employment. This discrepancy suggests a potential violation of FLSA regulations. This program is discussed in further detail in Observation 2.

  Also, because civilian paramedics do not qualify for premium pay such as shift differentials or technical rescue pay, the pay equalization program currently does not appear to interfere with the accurate calculation of the regular rate of pay for overtime. However, future pay changes are anticipated and could include premium

pay. Calculating overtime pay in accordance with FLSA under this prepayment plan will be much more complicated.

- Overstated DROP payments: The Deferred Retirement Option Plan (DROP) is a retirement benefit specifically designed for members of the Public Safety Personnel Retirement System (PSPRS) that allows eligible police officers to receive a cash payment each pay period based on the number of years they work past their official retirement age. Due to a calculation loop programmed in PeopleSoft, the final actual DROP payment is greater than 24.21% of total pay because it is first included in gross pay when calculating FLSA overtime, then, PeopleSoft re-calculates a higher DROP payment based on the total pay, which includes FLSA overtime pay. We estimate that this calculation error caused an estimated total overpayment of $14,400 to employees in the DROP program during the time period included in our audit scope (from January 1,2023 through June 30, 2024). See below for flowchart of DROP payment process:

**DROP Payment Loop Overpayment**




FLSA Guidance we reviewed was unclear regarding whether the additional pay not included in the FLSA calculation caused by the inflated calculation of DROP payments would be in violation of FLSA regulations.

Noncompliance with FLSA overtime regulations could lead to financial loss, penalties, and legal liabilities for the City. Payroll has highlighted these areas in the past, but challenges in PeopleSoft programming and in coordinating necessary changes have persisted. Due to the large number employees who earn premium or special pay and

the many earning codes in PeopleSoft for the different kinds of pay, we were unable to reasonably estimate the amount of over or underpayments to employees annually.

## Recommendations

1.1 Payroll, HR, and the City Attorney's Office collaborate to develop a jointly agreed-upon recommendation to address work schedules that may result in FLSA non-compliance, such as the 9/80 schedule for nonexempt employees. The recommended plan should include mitigation strategies and a detailed transition roadmap and be presented to the City Manager's Office for review and approval, prior to implementation. Implementation should occur before migrating to the new ERP to avoid heavy customization.

1.2 Payroll, HR and IT collaborate to develop a jointly agreed-upon plan to address automated overtime calculations that result in FLSA non-compliance by the PeopleSoft system. If corrections cannot feasibly be programmed prior to the migration to a new ERP, then they should be included as standard requirements in the new system.

1.3 Payroll work with HR and the Law Department to review the calculation of DROP payments in PeopleSoft and determine if modifications are needed.

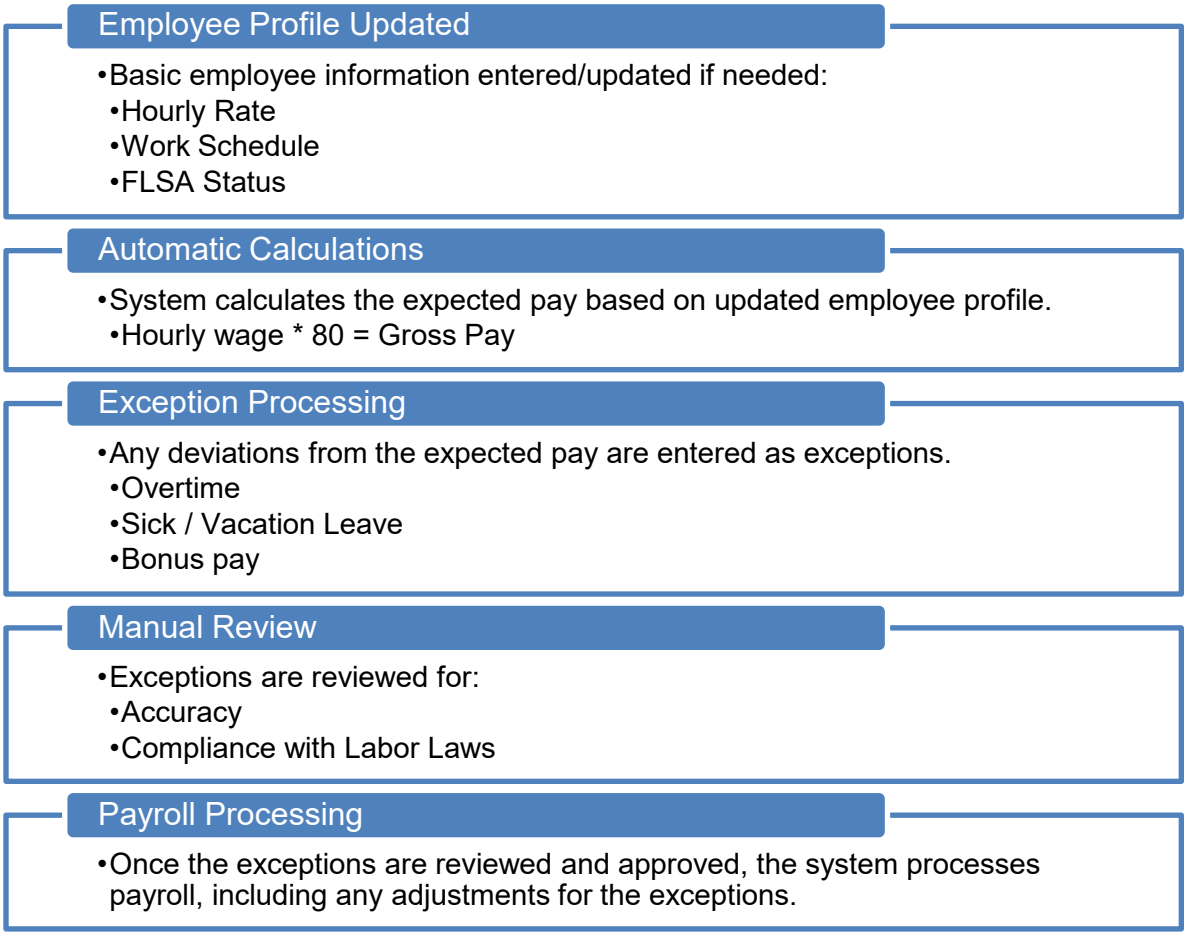
## 2 – Oversight and Monitoring for Timekeeping Systems

### Background

The City's payroll system, PeopleSoft, is expected to be replaced within the next 5 years, but the project will not begin until the replacement of the City's financial system is complete. The financial system replacement project is currently in the requirements gathering and vendor selection phase.

PeopleSoft is an exception-based payroll processing system, not a time and labor system. This means only deviations from the standard or expected pay need to be entered, approved, and processed. Instead of manually entering time and attendance data for every employee, the system assumes that employees are working their regular schedules and will pay accordingly unless there's an exception. This is the opposite of a time and labor system, which is used to record and track employee work hours and attendance and calculates payroll biweekly based on hours worked.

**Exception Based Payroll Processing**



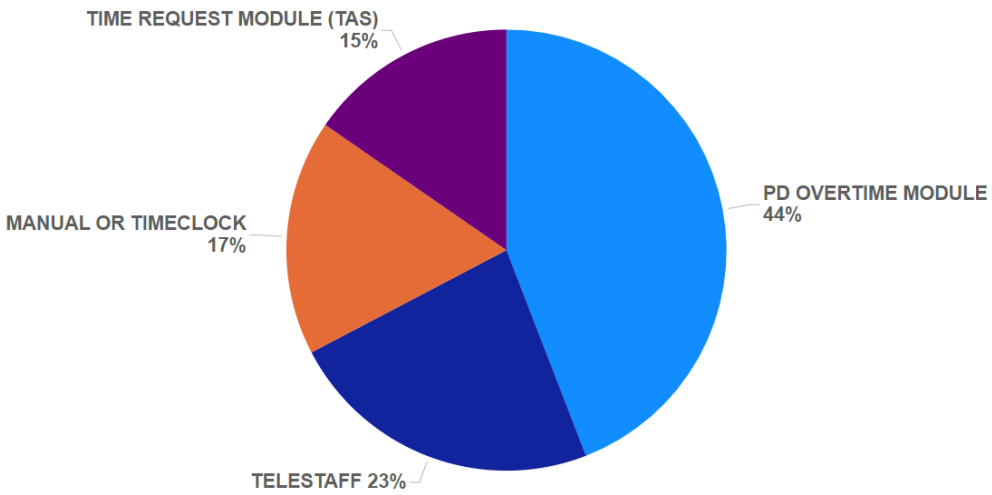

Exception based payroll systems require less ongoing work for employees than time and labor systems but depend heavily on frontline supervisors to monitor employees'

hours and approve any exceptions entered. Various pay codes are used to report exception pay, including 17 codes for different types of overtime. At the City, overtime exceptions are generally entered into one of the following systems depending on the department:

- **Time Request Module (TAS)** – a module within PeopleSoft implemented in June 2021 that allows Timekeepers to set up employees' work schedules and allows employees to directly enter their leave time and overtime hours. TAS's workflow process notifies the employee's supervisor of any overtime pay request. The supervisor generally reviews and approves the request electronically. At the end of each pay period, designated Timekeepers in each department review all approved overtime pay requests for errors. Final approval occurs on the Timesheet Entry Report and is approved by the designated authorized signer. Once supervisors approve TAS hours, the timekeeper prints Timesheet Entry Report, reviews report, obtains final approval from authorized signer and sends report to payroll.
- **Police Overtime (OT) System** – The Police OT system is a separate module in PeopleSoft that tracks the hours and reasons for overtime worked by police officers. Every pay period, all approved overtime hours are exported to Excel spreadsheets and reviewed for errors or inconsistencies. Corrections are entered before the data is imported into the payroll system. After the import, a report is generated to identify any records that were not successfully loaded. Police staff then make manual corrections directly in PeopleSoft.
- **Timeclock** – Some departments with a large number of part-time employees use a separate timekeeping system that offers multiple entry methods, including a mobile app and phone reporting. Timekeepers generate a file from this system containing approved work hours and upload it to PeopleSoft each pay period. While this system doesn't track overtime hours separately, timekeepers run a PeopleSoft report to identify employees who worked over 40 hours per week, obtain the employee's supervisor's approval and manually code the overtime accordingly.
- **Telestaff** – This is a specialized workforce management software designed for public safety organizations to automate scheduling and track time and attendance. Each pay period, time and attendance data are exported from Telestaff and uploaded to PeopleSoft. After the upload, TFMRD staff review an error report to identify any issues and make necessary corrections.

A review of the number of hours entered by system shows Police and TFMRD account for almost 70% of overtime hours in total (See following chart).

**Overtime Hours Entered January 1, 2023 through June 30, 2024**
**by Timekeeping System**




## Approach

To determine if overtime was properly authorized and accurately recorded in PeopleSoft, we performed the following for each timekeeping system:

- Reviewed overtime reporting and approval controls, verifying that overtime must be properly approved prior to processing regardless of the system it was entered.
- Conducted sample testing to verify appropriate approvals were obtained for overtime transactions recorded in each system.
- Verified the procedures in place to upload overtime transactions from each system to PeopleSoft, including steps for reconciliation and error correction between systems, were being followed.
- Performed reconciliation of overtime entries reported in each system versus PeopleSoft for the following sample of pay periods:

| System | Sample PPE |
|---|---|
| Timeclock | February 25, 2024 |
| Telestaff | January 14, 2024 |
| Police OT System | February 25, 2024<br>April 7, 2024<br>June 2, 2024 |

- Performed data analysis to identify and test high risk overtime transactions including:
    - Potential duplicate overtime payments.

- Overtime taken while sick or on vacation.
- Self-approved overtime.
- Overtime processed without approval.
- Overtime not paid at one- and one-half regular rate.
- Overlapping off-duty overtime with regular overtime.

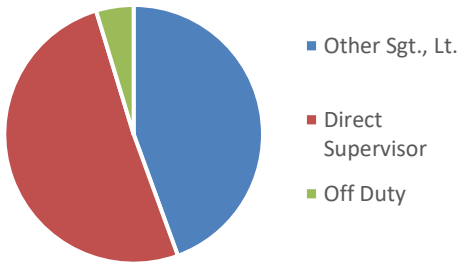
## Results

***Procedures are in place in each of the City's time reporting systems to ensure overtime transactions are properly approved and accurately uploaded but there are some opportunities to strengthen controls.***

In our review of payroll records from January 1, 2023, through June 30, 2024 we noted the following:

- **Police OT System** –
  - Our review of more than 15,000 overtime transactions in 2024 confirmed that all were approved by a direct supervisor, a supervisor at the same or higher level, or an off-duty coordinator as required by Section 203A of the City's Personnel Rules.

**2024 Overtime Transactions by Approver Type**

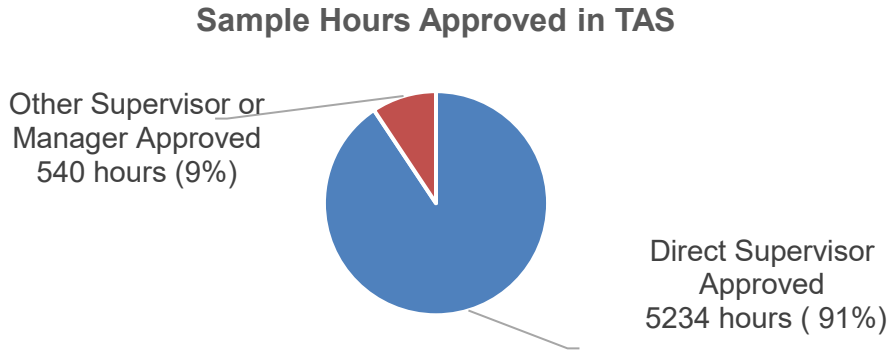



  - We traced three pay periods of overtime hours (approximately 22,000 hours) across PeopleSoft, the Police OT system, and the Off-Duty OT system. Our reconciliation found no errors, unauthorized Police overtime, duplicate payments, or self-approved overtime.
  - We verified that a sample of 44 overtime hours worked by 7 officers on days when they were also on full vacation or sick leave were approved and supported by valid reasons.
  - For a sample of 14 officers who worked a total of 119 hours of off-duty overtime on days they also worked regular overtime or standby (totaling 170 hours), we verified that there was no overlap in the work hours.
- **Telestaff** –
  - All 8,228 overtime hours per Telestaff for one sample pay period agreed to overtime reported by PeopleSoft, except for 1,496 hours of overtime associated

with the Equalized Payroll Agreement, which is entered directly into PeopleSoft. The Equalized Payroll Agreement is for nonsworn paramedics and other emergency transportation workers who work alongside sworn firefighters and is discussed in more detail below.

- Unscheduled overtime for a sample of 6 pay periods, totaling 482 overtime hours, were properly approved by a direct supervisor or another supervisor equal to or higher in the chain of command as required by Personnel Rule 203A.
- We found no instances of duplicate overtime payments or self-approved overtime.

- **Timeclock** –
  - The upload from the Timeclock system to PeopleSoft each pay period does not distinguish overtime hours from regular hours. Timekeepers must review the hours in PeopleSoft and enter adjustments to move hours worked over 40 from regular hours (coded RG) to overtime hours (coded OT).
  - We reviewed the hours reported by Timeclock for one pay period for department 3281, Diablo Stadium, and found that all 73 overtime hours were properly identified and re-coded as OT in PeopleSoft.
- **TAS** –
  - We reviewed the employee master file of active full-time employees in PeopleSoft on August 27, 2024. No employees had a user profile that could allow approval of their own overtime. All regular employees had a supervisor on file for the approval of overtime and leave requests, except for City Council members and the City Manager.
  - From the population of active full-time employees who worked 16,315 overtime hours between January 1 and June 30, 2024 (totaling 4,522 overtime entries), we selected a sample of 1,948 overtime entries (43% of the total). This sample was comprised of employees who had reported at least 50 overtime entries. All were either approved by the supervisor on record in PeopleSoft or by another higher-ranking supervisor or management level staff as required by Personnel Rule 203A (See following chart).




  - Timekeepers are expected to review and verify exception pay and forward department head approval of TAS timesheets to Payroll, via either email or hardcopy. Payroll tracks department approvals but have found that Timekeepers

are not always catching errors such as use of incorrect pay codes and overuse of available hours for paid time off. This causes additional review time by Payroll staff each pay period and increases the risk of errors going undetected. This issue was addressed in our prior audit report dated March 21, 2024. Payroll is working with HR to develop a comprehensive payroll policy that will govern the responsibilities of Payroll and HR, including controls over payroll processing, with a target completion date of June 30, 2025.

- Once all exception pay in all systems has been approved and uploaded, central processing takes several days. During this time, department staff are instructed to contact Payroll before making any changes or corrections in PeopleSoft to avoid timing issues. This includes changes to prior pay periods. During our analytic review of overtime hours earned between January 1, 2024, and June 30, 2024, we identified 5 employees that were paid twice in TAS for 12 hours of overtime (60 hours total) due to an attempt to correct an associated cost center while payroll was in a partially processed state. The total of the overpayments was $2,264. Additional controls to reduce the risk of duplicate payments of overtime to employees should be considered, including:
    - reminding all Timekeepers of the importance of not making payroll entries during payroll processing,
    - a procedure to review TAS entry identification numbers (id's) and dates worked after payroll is processed to ensure they do not match TAS ids in prior pay periods, and
    - reducing the significant timing gap between payroll confirmation and when rows are marked as "Processed".

***The amount of prepaid overtime withheld from the final checks of civilian paramedics upon termination or when leaving the Paramedic Equalized Payroll program may likely be incorrect.***

Under the Equalized Payroll Agreement, civilian paramedics receive a consistent paycheck comprising 40 hours at their regular rate and 16 hours manually entered in PeopleSoft at the overtime rate. When working less than 56 hours in a week, the pay difference is considered an advance against future overtime hours. According to the agreement, overtime shall be reconciled at the end of each bi-weekly pay period to ensure that all overtime hours worked in each individual week have been compensated at the overtime rate. At the end of employment, any advanced overtime is to be deducted from the employee's final paycheck.

However, a reconciliation of prepaid overtime for paramedics is not performed week-to-week. TFMRD staff instead use the predictable pattern of paramedics' weekly work schedules shown in Chart 1 below to estimate the balance of prepaid overtime at the end of each pay period. This calculation is based on an employee's assigned shift. The Equalized Payroll Agreement for Civilian Paramedics provides an example outlining how to determine the prepaid overtime balance for any of the nine pay periods within a repeating cycle. The provided example chart accurately calculates prepaid overtime

only if an employee begins the equalized pay program during a pay period with 96 or fewer hours followed by either 128 or 120 hours.

**Chart 1 - Example Reconciliation as Provided in Equalized Payroll Agreement**

| Pay Period | Number of Shifts | Hours Worked | Paid Regular Hours | Paid OT Hours | Difference Between OT Hours Paid and OT Hours Worked | Balance of Pre-Paid OT Hours |
|---|---|---|---|---|---|---|
| Equalized Pay Cycle Begins | | | | | | |
| 1st 2-week pay period | 4 shifts | **96** | 80 | 32 | 16 | 16 |
| 2nd 2-week pay period | 5 1/3 shifts | *128* | 80 | 32 | (16) | 0 |
| 3rd 2-week pay period | 4 shifts | 96 | 80 | 32 | 16 | 16 |
| 4th 2-week pay period | 5 shifts | 120 | 80 | 32 | (8) | 8 |
| 5th 2-week pay period | 4 2/3 shifts | 112 | 80 | 32 | 0 | 8 |
| 6th 2-week pay period | 4 1/3 shifts | 104 | 80 | 32 | 8 | 16 |
| 7th 2-week pay period | 5 shifts | 120 | 80 | 32 | (8) | 8 |
| 8th 2-week pay period | 4 shifts | 96 | 80 | 32 | 16 | **24** |
| 9th 2-week pay period | 5 2/3 shifts | 136 | 80 | 32 | (24) | 0 |

In the above chart, a Paramedic who started the Equalized Payroll Program during a 96-hour period and subsequently terminated employment after eight weeks would have a prepaid balance of 24 hours of overtime pay that would need to be withheld from their final paycheck.

However, If a paramedic's enrollment in the program starts with a different number of hours worked, the prepaid overtime balance at termination per the example chart above will not be accurate and must be determined by recalculating the difference between hours paid and hours worked since the paramedic's entrance into the program.

For example, if the same paramedic started the Equalized Payroll Program during a 136-hour pay period and still terminated employment after eight weeks, they would be owed 16 hours of overtime. As Chart 2 below shows, the balance of prepaid overtime would be negative for the entirety of the employee's 16-week employment. And because the pay period schedule repeats every nine weeks, the City would consistently owe the employee up to 24 hours of overtime regardless of how long their employment, which is against FLSA regulations.

**Chart 2 - Example Reconciliation Under Other Than 96-hour Shift**

| Pay Period | Number of Shifts | Hours Worked | Paid Regular Hours | Paid OT Hours | Difference Between OT Hours Paid and OT Hours Worked | Balance of Pre-Paid OT Hours |
|---|---|---|---|---|---|---|
| Equalized Pay Cycle Begins | | | | | | |
| 1st 2-week pay period | 5 2/3 shifts | **136** | 80 | 32 | -24 | -24 |
| 2nd 2-week pay period | 4 shifts | 96 | 80 | 32 | 16 | -8 |
| 3rd 2-week pay period | 5 1/3 shifts | 128 | 80 | 32 | -16 | -24 |
| 4th 2-week pay period | 4 shifts | 96 | 80 | 32 | 16 | -8 |
| 5th 2-week pay period | 5 shifts | 120 | 80 | 32 | -8 | -16 |
| 6th 2-week pay period | 4 2/3 shifts | 112 | 80 | 32 | 0 | -16 |
| 7th 2-week pay period | 4 1/3 shifts | 104 | 80 | 32 | 8 | -8 |
| 8th 2-week pay period | 5 shifts | 120 | 80 | 32 | -8 | **-16** |
| 9th 2-week pay period | 4 shifts | 96 | 80 | 32 | 16 | 0 |

As there is no directive to enroll paramedics into the program during a pay period with 96 or fewer hours followed by either a 128- or 120-hour pay period, and TFMRD staff are relying on the example reconciliation provided in Equalized Payroll Agreement (Chart 1) to determine the balance of prepaid overtime each pay period, Payroll staff are likely not withholding the correct amount of prepaid overtime from the final checks of some paramedics when terminating employment. Out of four paramedics' schedules we reviewed, two started the pay equalization program in a 120-hour pay period. This resulted in a repeating nine pay period cycle where the City owed the paramedics up to 16 hours of overtime in over half of the pay periods.

Additionally, if a paramedic started the Equalized Payroll Program at the start of the 96-hour pay period but later changed shifts at some point while in the program, Chart 1 would still not lead to accurate reconciliation of prepaid overtime each pay period. There are three possible shifts for paramedics. If a paramedic switches shifts while in the Equalized Payroll Program, TFMRD must adjust the prepaid overtime balances accordingly going forward or ensure that the paramedic's prepaid overtime balance is settled and the paramedic is started back into the program under the new shift at the start of a 96-hour schedule.

## Recommendations

2.1 Payroll implement additional controls to reduce the risk of Timekeepers making changes to prior period exception pay during payroll processing.

2.2 For future paramedic hires, TFMRD should implement a weekly reconciliation process to ensure the amount of prepaid overtime can be determined upon employee shift change or separation from the City, and implement a policy of allowing paramedics to initially, and upon shift changes, join the pay equalization

program only during a pay period with 96 or fewer hours followed by either 128 or 120 hours.

2.3 TFMRD consider the need to reconcile, and monitor going forward, prepaid overtime hours for all current paramedics who did not join the pay equalization program during a pay period with 96 or fewer hours followed by either 128 or 120 hours, or who have switched shifts in the past to determine their true prepaid overtime balance.

# 3 –Considerations for New Payroll System Implementation Project

## Background

A well-planned system requirements phase will be critical to the success of the PeopleSoft replacement project. This process establishes the project's groundwork by clearly defining what the new payroll system needs to do, how it should function, and the specific goals it aims to achieve.

A primary goal of any new payroll system should be the ability to ensure full compliance with all FLSA regulations, even with the complexities of public sector payroll.

Some of the complexities with City payroll processing include:

- Alternative workweeks and work periods permitted.
- Various pay types such as bonuses, shift differentials, standby pay, and more.
- Drastically different job classifications, work hours and compensation.
- Multiple collective bargaining agreements with various stipulations.

The inability of payroll programs to accurately calculate overtime for safety employees has forced some employers to perform manual FLSA overtime calculations. Governments that do not independently investigate and ensure the FLSA compliance of their payroll system put their agency at risk of liability if targeted for overtime lawsuits.

## Approach

To provide guidance on issues with FLSA compliance and potential factors to consider when developing criteria and requirements for the new payroll system, we performed the following:

- Researched FLSA requirements specifically for the accurate calculation of overtime by reviewing information from the Department of Labor (DOL) and the US Office of Personnel Management (OPM) including:
  - Section 778 of the FLSA Regulations,
  - DOL and OPM Fact Sheets,
  - FLSA Updates,
  - DOL Opinion Letters,
  - Other legal articles published on the topic of FLSA in the Public Sector.
- Met with Payroll staff to understand how the PeopleSoft system currently manages FLSA requirements, including the areas it is unable to meet.
- Reviewed the PeopleSoft Payroll Processing Manual, all collective bargaining agreements, and Personnel rules at the City.

## Results

***The following is a list of some of the requirements a public payroll system should have to meet FLSA requirements:***

1. If allowing 9/80 schedules, the payroll system must be able to split hours worked in a day into two separate workweeks.

   Since the FLSA designated workweek for an employee on a 9/80 schedule will stop and start in the middle of a workday, the employee will work hours in two different FLSA workweeks on the same day. Therefore, the payroll system will need to be able to split the hours worked on that day into two different FLSA workweeks and calculate overtime based on those FLSA workweeks.

2. The payroll system will need to be able to track FLSA workweeks over multiple pay periods.

   As pay periods typically do not stop and start in the middle of a workday, an exception-based payroll system is especially problematic as it does not account for changes in the start or stop times of the workday or changes in the employee's day off, all of which could lead to increased FLSA overtime liability.

3. The payroll system will need to be able to calculate overtime based on both the requirements of the collective bargaining agreement and on the separate FLSA requirements.

4. The payroll system should allow the inclusion of flat amounts for on-call or standby pay in the calculation of the regular rate of pay.

5. The payroll system must be able to convert special pay that is paid on a bi-weekly or monthly basis that does not correspond to the employee's FLSA workweek in the calculation of the regular rate of pay.

6. For annual bonuses, the payroll system should be able to recalculate the employee's regular rate of pay for each workweek in the preceding year to account for the bonus amount and pay any extra FLSA overtime amounts owed as a result.

7. The payroll system should be able to calculate FLSA overtime based on a blended rate for multiple positions.

   The hours worked at each of the rates should be combined to determine a weighted average rate of pay. The employee is then paid overtime at time and one-half that weighted average for all overtime hours worked.

8. The payroll system should be able to base FLSA overtime calculations on a work period of up to 28 days.

   Most public agencies have bi-weekly, or 14 day pay periods. Often the work period for safety employees will be longer than 14 days. Computation of FLSA overtime for

those safety employees requires that the payroll system calculates the hours worked over multiple pay periods to determine whether any FLSA overtime is owed. Payment becomes more complex when the work period does not neatly overlap with the pay period, such as for a 27-day work period.

9. The payroll system must be able to pay firefighters based upon the actual hours worked in the FLSA work period, not an average of the hours worked.

   The assumption that a firefighter works an average of 56 hours per week will result in underpayment of FLSA overtime for some pay periods and overpayment for other periods. The FLSA strictly prohibits the averaging of FLSA overtime over work periods, and the DOL has specifically prohibited this practice regarding firefighters.

10. The payroll system should be able to calculate the regular rate of pay for safety employees based upon the compensation for the work period, not the workweek potentially requiring the allocation of bonuses or special pay to be allocated across multiple pay periods and multiple work periods.

11. The payroll system should be able to distinguish FLSA from non-FLSA Compensatory Time Off (CTO).

    An inability to distinguish non-FLSA CTO from FLSA CTO means having to treat all CTO as FLSA CTO which will allow more employees to be taking time off on a more frequent basis. It can also create additional overtime liabilities, as the DOL does not permit an agency to deny a request to use compensatory time off simply because it would have to backfill the position on an overtime basis.

12. The payroll system must be able to pay accrued CTO at the appropriate regular rate of pay. The City is obligated to cash out CTO upon termination of employment at the higher of:

    - The employee's regular rate of pay as of termination; or
    - The average regular rate during the last three (3) years of employment.

13. The payroll system should have a mechanism that prohibits suspension of exempt employees other than on a weekly basis to prevent a finding that exempt employees are really non-exempt.

14. The payroll system should recognize when employees have exceeded caps on working a certain number of hours per day or workweek.

    If the payroll system cannot meet all requirements, alternative ways to meet the requirements should be fully explored to understand the implications and risks of any "work around" prior to selecting a noncompliant system.

## Recommendations

3.1 Payroll, HR and IT consider including FLSA specific requirements in the RFP for the City's PeopleSoft system replacement project and assess them in the City's vendor selection process.

# Scope, Methods, and Standards

## Scope

The scope of this audit included overtime transactions during the period from January 1, 2023, through August 2024 recorded under the following earning codes:

| Earn Code | Descr |
|---|---|
| CBK | Call Back |
| FHW | Fire Holiday Overtime Worked |
| FLS | FLSA Hours |
| FOP | Fire OT- Spec Event 3rd Party |
| FOT | Fire Overtime - Special Events |
| FSN | Fire OT Spec Event Non Reimb. |
| FSP | Fire Special Events 3rd Party |
| FSR | Fire Spec Events 3rd Pty Ret |
| OT | Overtime |
| TD6 | Fire-TD/OT BLS Engineer |
| TD7 | Fire-TD/OT ALS Engineer |
| TD8 | Fire-TD/OT BLS Captain |
| TDB | Fire-TD/OT Acting Capt +5% |
| TDC | Fire-TD/OT ALS Captain |
| TDD | Fire-TD/OT Deputy Chief |
| TDF | Fire-TD/OT Acting Engineer +5% |
| WOT | Water OT Per Schedule Plant Op |

## Methods

We used the following methods to complete this audit:

- Research of FLSA regulations
- Document review
- Expert consultations
- Employee interviews
- System review
- Data analysis
- Sample testing
- Review of overtime reporting and approval controls
- Sample testing of approvals
- Verification of upload procedures and controls
- Reconciliation of overtime transactions
- Data analysis

Unless otherwise stated in the report, all sampling in this audit was conducted using a judgmental methodology to maximize efficiency based on auditor knowledge of the population being tested. As such, sample results cannot be extrapolated to the entire population and are limited to a discussion of only those items reviewed.