



**CHARLOTTE**<sup>SM</sup>

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**INTERNAL AUDIT**

**Audit Report  
CATS Bus Operations – Imprest Account  
For Fiscal Year 2017  
October 26, 2017**

**City Auditor's Office  
Gregory L. McDowell, CPA, CIA**

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**Purpose and Scope**

The purpose of this audit was to determine whether the City has reimbursed the bus operations management company accurately and the funds have been disbursed properly. The City's outside auditor, Cherry Bekaert LLP (CB), performs agreed-upon procedures related to the Bus Operations Division (BOD). The work performed by Internal Audit is provided to CB for its review.

The City contracts with a management company, McDonald Transit Associates, Inc. (McDonald) to manage bus operations, known as Transit Management of Charlotte, Inc. (TMC). TMC sends reimbursement requests to the Charlotte Area Transit System (CATS) for operating expenses, except bus parts for which the City pays directly to suppliers. The City wire transfers the reimbursements into an imprest bank account in the name of TMC, from which BOD issues checks for operating expenses.

Auditors reviewed the operations and specific transactions for the fiscal year ended June 30, 2017. Tests were designed to determine whether:

- Internal controls over the transactions handled through the bus transit imprest fund, including payroll, are adequate,
- Wire transfers to the CATS Bus Transit Payroll Imprest Account are accurately recorded;
- BOD's reimbursement requests are adequately supported, and
- Bus operations employees' wages comply with union agreement terms.

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

This report is intended for the use of the City Manager's Office, City Council, CATS, and the City's external auditor Cherry Bekaert.

**Conclusion**

CATS has established adequate internal controls to ensure expenditures from the imprest fund are timely and accurate. Improvement has been made in the documentation of employee benefit elections.

### **Summary Recommendations and Actions – 2017**

The following findings are detailed, beginning on page 4:

1. TMC should continue improving benefit election documentation and annually updating employee personnel files.
  - In the most recent enrollment period tested, the non-union dues exception rate improved to 3% (down from 13%).
2. TMC should maintain United Transportation Union (UTU) membership authorization forms and require a monthly written certification of membership from the UTU.
  - An itemized report has been developed for the UTU representative to certify monthly a list of union members and their deductions.
  - TMC will ensure that a signed authorization form is retained for every union member.

### **Background**

McDonald Transit Associates, Inc. (McDonald) began providing transit management services for CATS' Bus Operations Division (BOD) in September 2003. Additional contract awards and extensions have resulted in McDonald providing continuous service to the City, with the current contract valid through at least 2017. (Available contract options could be exercised to remain in effect until February 2019.)

McDonald is responsible for managing day-to-day operations and maintenance of CATS' largest bus fleet (other fleets include Special Transportation Services and Lynx Blue Line light rail). CATS engages a transit management firm in this capacity because North Carolina law prohibits governmental entities from managing and collectively bargaining with unions. Bus drivers, maintenance staff, and parts room workers are employed by the private company Transit Management of Charlotte, Inc. (TMC), which is managed by McDonald under its contract with the City. McDonald and TMC employees work at the Davidson Street and the Tryon Street facilities.

The City is fully responsible for the finances of the BOD and is contractually required to pay all operating expenses. TMC is required to maintain an imprest account through which the following expenses are paid: wages and salaries of all TMC employees, the employer's share of payroll taxes and benefits, employer contributions to the pension plan, all payments made in settlement of claims or satisfaction of judgment incurred in the operation of the public transportation system, all general and miscellaneous expenses for BOD, all expenses for liability insurance, workers' compensation and tort claims, and all expenses for materials and supplies (excluding bus parts).

The individual payroll checks for the employees of TMC are prepared by Ceridian. In addition, Ceridian calculates and deposits payroll withholding and the employer's share of the taxes. Each week, the payroll administration staff for TMC prepares a report based on printouts from

Ceridian listing the amount and the account to be charged for payroll. This report is then forwarded to the accounting specialist for inclusion in the request for payment from the City. Also included in the request are any other miscellaneous payroll-related expenses to be paid.

Each week, TMC requests payment for itemized expenses and documents the request by providing copies of invoices. The request for funds is reviewed by CATS administration and the City's Finance staff. Upon approval, a wire transfer of the funds is made by the City and TMC issues the checks the following day. TMC's accounting specialist writes the checks using Quicken software and they are forwarded to the general manager for his signature. The checks are then given to the financial support clerk who prepares the envelopes and mails the checks. The payroll/finance administrator is responsible for reconciling the imprest account on a monthly basis.

### **Prior Year Update**

For FY16, CATS and TMC addressed findings and recommendations satisfactorily, except as noted under Recommendation #2A below.

**Recommendation #1:** CATS should update its approval process to include the following procedures: (1) Ensure the designated backup(s) are aware of the procedures to approve expenses when the CATS Chief Operations Planning Officer (COPO) is unavailable; (2) Print a copy of the email sent to AP to include with the detailed backup file. The purpose of this email would be to confirm, via the timestamp, that the CATS approval occurred prior to the wire transfer.

- A new position, General Manager of Bus Operations (GM), was created and filled in August 2016. The GM has since replaced the COPO as the primary approver for all payment requests; the COPO is the designated back-up for the GM. Approval guidelines have been established, and a written procedure is in place to ensure consistency and accuracy within the approval process. Testing indicates the new procedures are working as designed.

**Recommendation #2A:** TMC should annually update all employee benefit folders with signed authorization forms, including waivers of coverage, union dues, and AFLAC elections. For the years following FY17 open enrollment, a signed acknowledgement form should be obtained even if an employee elects to roll forward coverage from a prior year.

- TMC has refined the process of collecting enrollment forms from all employees; however, documentation for certain deductions can be improved. See FY17 audit findings for further details regarding the most recent open enrollment process.

**Recommendation #2B:** TMC should research all BOD employees' benefit elections and resolve any incorrect deductions by either refunding the employees or obtaining a signed election form indicating the deductions are correct.

- The Operations Analyst, at the General Manager's direction, has conducted reviews of the medical and dental benefit programs in response to the City audit report. Output from the Ceridian payroll system was compared with insurance carrier billings to find any individual employee payroll deductions that did not match the dollar amount for the same employee on the insurance bill. All non-matching entries were forwarded to the TMC benefits department for their investigation and response. This exercise was performed with the December 2016, January 2017, and March 2017 billings. The same review is being performed with the new insurance policies effective April 2017 and will continue periodically throughout the year. CATS personnel have periodically conducted random sampling of employee benefit enrollment forms against actual benefit deductions to verify accuracy of deductions. Results indicate an improvement in benefit input accuracy since the prior year audit. See FY17 audit findings for further details.

***Recommendation #2C:*** TMC should consider an online open enrollment process that could reduce the occurrence of manual entry errors.

- A new payroll system, Paylocity, was implemented in August 2017. This new system has web access that will allow direct input of benefits as employees make their elections. During a preliminary review of administrative staff pay changes, auditors noted the new system has expanded capabilities. These include online employee access to elected benefit information for monitoring, and a workflow for pay change approvals. Further testing of the new payroll system will take place during the FY18 audit.

### **Audit Findings and Recommendations – 2017**

**1. TMC should continue improving benefit election documentation and annually updating employee personnel files.**

Open enrollment for benefits such as medical, dental, life, short-term disability, and supplemental insurance occurs annually in March. Employees are strongly encouraged to attend open enrollment, but are not required. If employees fail to make elections during the open enrollment period, current elections are automatically rolled over into the new policy year. Whenever there is a change in the medical insurance carrier, attending open enrollment is mandatory in order to receive those benefits. The risks resulting from a non-mandatory open enrollment have been outlined in prior years' audits. These risks are mitigated by TMC's substantial efforts to have every employee make yearly elections. Prior to the most recent open enrollment period, notices were sent to all employees outlining the necessity of participating. Flyers and posters were distributed throughout the facilities and inactive employees were sent letters. For any employees unable to attend in person, a call center option was made available on four days. After all contact methods were exhausted, only one employee failed to enroll this period and this employee was on military leave.

Auditors tested two FY17 pay periods – one in the prior open enrollment period, March 2016, and one in the most recent election period, March-April 2017. Seventy-four of the 461

deductions tested had exceptions (16.1%). The majority of these errors involved documentation for bus operator union dues. Excluding the union dues errors (outlined in more detail in Finding #2), 24 of the 31 exceptions were in the prior enrollment period (77%). Errors found in the prior enrollment period are consistent with those seen in prior audits.

Exception Error Rate (excluding Union Dues)			
Pay Period	Exceptions	Deductions	Error Rate
07/28/16	24	201	11.9%
06/22/17	7	217	3.2%
<b>Totals</b>	<b>31</b>	<b>418</b>	<b>7.4%</b>

The majority of exceptions were due to manual entry errors and missing authorization forms. The reduced exception rate in the current enrollment period is due to new staff making a concerted effort to improve procedures as well as the added emphasis TMC has placed on document retention.

The following non-union dues exceptions were found during the current review:

- Two employees (of 40 sampled) with incorrect deductions taken from their prior enrollment period paychecks required reimbursements. No such exceptions were found in the most recent enrollment period sample.
- The remaining 29 exceptions were due to missing or unsigned authorization forms, coverage selected but not deducted, or other recordkeeping errors.

**Recommendation:** TMC should continue to annually update all employee benefit folders with signed authorization or acknowledgement forms. Employees that were incorrectly charged for unauthorized deductions should be refunded.

**Actions Taken:** Corrections have been made to the employee benefit deductions with refunds issued to the two affected employees.

**CATS/TMC Response:** CATS and TMC staff agree with the recommendation and will change operating procedures to reflect the recommendation. Effective immediately, TMC will update employee benefit deduction folders with signed authorization and acknowledgement forms. Every employee that has benefits will be required to view and sign the required forms.

2. **TMC should maintain United Transportation Union (UTU) membership authorization forms and require a monthly written certification of membership from the UTU.**

Auditors did not test deductions related to union dues in FY16. TMC staff noted they no longer receive the authorization forms and the UTU representative emails a list of any changes. This is still the case in FY17. Therefore, auditors were unable to verify whether deductions were authorized by the employees. As noted in both labor agreements (Article

III-B of the Operations Agreement and Article III-A of the Maintenance Agreement), TMC is required to have written consent on file for each employee who chooses to participate in the UTU. Additionally, the local union is contractually obligated to certify in writing each month an itemized statement of its members and their dues. As agreed to after the prior year's audit, these consent forms were to be kept in the personnel folders.

No authorization forms were found for members of the UTU. These errors make up the majority of the exceptions found during testing.

Deduction Type	07/28/16	06/22/17	Total
Total Exceptions	43	31	74
Union Dues	19	24	43
Union Dues %	44.2%	77.4%	58.1%

**Recommendation:** TMC should annually update all employee benefit folders with signed authorization forms, including union dues and waivers of coverage. TMC should enforce the contract language stating a certification of UTU members is to be provided monthly.

**Actions Taken:** TMC and the UTU representative have developed an itemized report showing current UTU members and their respective deduction amounts. Delivery of this report was started in September of 2017.

**CATS/TMC Response:** CATS and TMC staff with the recommendation of having the authorization forms signed by the employees. These forms will be maintained and kept in the benefits file room and a separate copy will be placed in the employee's personnel records.