



CITY OF HAMILTON
CITY MANAGER'S OFFICE
Office of the City Auditor

TO:	Chair and Members Audit, Finance and Administration Committee
COMMITTEE DATE:	August 13, 2020
SUBJECT/REPORT NO:	Special Audit Respecting Case Number 2019-013 (AUD20005) (City Wide)
WARD(S) AFFECTED:	City Wide
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SUBMITTED BY:	Charles Brown CPA, CA, CPA (Illinois) City Auditor Office of the City Auditor
SIGNATURE:	

Discussion of Confidential Appendix “A” and “B” to this report in Closed Session, would be pursuant to Section 8.1, Sub-section (a) of the City's Procedural By-law 18-270, as amended, and Section 239(2), Sub-section (a) of the Ontario Municipal Act, 2001, as amended, as the subject matter pertains to the security of the property of the municipality or local board.

RECOMMENDATIONS

- (a) That the Management Action Plans as detailed in Confidential Appendix “B” of Report AUD20005 be approved;
- (b) That the Executive Director of Human Resources and the General Manager of Finance and Corporate Services be directed to instruct the appropriate staff to

have the Management Action Plans (attached as Confidential Appendix “B” to Report AUD20005) implemented; and

- (c) That Confidential Appendices “A” and “B” to Report AUD20005, Special Audit Respecting Case 2019-013 remain confidential.

EXECUTIVE SUMMARY

As a result of a recent investigation reported to the Audit, Finance and Administration Committee (AF&A) (Case 2019-013), the City Auditor chose to carry out a targeted audit of payroll process, as well as vendor payment changes, to identify gaps that expose the City to unnecessary risks.

Recommendations were made to strengthen controls and increase process efficiencies for payroll and vendor banking changes in order to reduce the risk of occurrence of fraud and error in these processes.

The results of this targeted audit are presented in a formal report containing our findings, conclusions, recommendations and management responses. This audit report is attached as Confidential Appendices “A” and “B” to Report AUD20005.

Alternatives for Consideration – Not Applicable

FINANCIAL – STAFFING – LEGAL IMPLICATIONS

Financial: None.

Staffing: None.

Legal: None.

HISTORICAL BACKGROUND

On June 24, 2020, Council directed the City Auditor to implement a policy on City Auditor Reporting of Serious Matters to Council. Under this policy, timely disclosure to Council is called for in situations that:

- Pose a security threat (e.g. cybersecurity exposure) to the organization's information systems/hardware/software applications or involves major privacy breach
- Threaten public safety
- Involve potential fraud over \$100,000
- Could have a significant adverse impact on the City's vulnerable populations
- Result in investigation by the Office of the City Auditor (OCA) and referral to the Police
- In the judgement of the City Auditor are deemed to be of a significant risk to the Corporation.

This is a follow-up to one of two previous reports of a serious matter made to AF&A under the new policy. The criterion applied and met was that the matter resulted in an investigation by the OCA and referral to Hamilton Police Service. The incident that was investigated led to a targeted audit of payroll and other processes being undertaken, and recommendations being made for observed control weaknesses that arose in the course of the audit.

The scope of the audit focused on several payroll processes, including how changes are made to an employee's payroll method or direct deposit information. Due to a widespread occurrence of vendor-related fraud in municipalities, the OCA also took this opportunity to review processes surrounding changes to vendor payment details. The results of this audit are attached as Confidential Appendix "A" of Report AUD20005.

The Audit, Finance and Administration Committee receives and approves audit reports as part of its responsibilities for the oversight of governance.

POLICY IMPLICATIONS AND LEGISLATED REQUIREMENTS

None.

RELEVANT CONSULTATION

Confidential Appendix "B" to Report AUD20005 includes action plans which reflect the responses of the following management groups responsible for overseeing employee records, payroll, vendor payments and IT security:

- Human Resources Division in the City Manager's Office;
- Information Technology Division in the Corporate Services Department; and
- Financial Services and Taxation Division in the Corporate Services Department.

ANALYSIS AND RATIONALE FOR RECOMMENDATIONS

The OCA carried out the following analyses related to payroll processes and vendor payment changes to identify gaps that expose the City to unnecessary risks:

- 1) Assessed processes and controls in place for payroll changes:
 - Adding employees (new, temporary)
 - Removing employees (retirement, terminations, temporary)
 - Pay rate changes (cost of living adjustments, merit, position changes)
 - Changes in payment method or information (direct deposit, cheque)
 - Adding and removing employees on salary continuance

This work included documenting processes, performing process review, identifying both manual and automated/system access controls in place, and testing to determine those control operating effectively.

- 2) Assessed processes related to disclosing employee information to third parties.
- 3) Assessed processes in place for manual payroll cheques and testing related controls.
- 4) Assessed controls in place to prevent payments to ghost employees and evaluating if there are any ghost employees currently on the payroll.
- 5) Evaluated if HR employees have received adequate training to be knowledgeable of fraud, phishing or social engineering scams.
- 6) Evaluated processes and testing controls for vendor banking changes to determine operating effectiveness.

The OCA made 15 recommendations to strengthen controls and increase process efficiencies for payroll and vendor banking changes. These recommendations can be found in the Confidential Appendix “B” to Report AUD20005.

Management agreed with all fifteen recommendations and provided management action plans for implementation. The implementation of the action plans is anticipated to be completed by Q3 2022.

Under the current Council approved policy an Annual Report of case intake and resolution regarding the Fraud and Waste Hotline will be issued publicly. The investigation matter referred to above, which provided cause for the audit of payroll processes and reporting of attendant weaknesses will be included in that Annual Report.

ALTERNATIVES FOR CONSIDERATION

Not applicable.

ALIGNMENT TO THE 2016 – 2025 STRATEGIC PLAN

Our People and Performance

Hamiltonians have a high level of trust and confidence in their City government.

APPENDICES AND SCHEDULES ATTACHED

Confidential Appendix “A” to Report AUD20005.

Confidential Appendix “B” to Report AUD20005.