
Internal Audit Report

Staff HR Compensation Process

Report No. SC-22-03
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I. EXECUTIVE SUMMARY

Audit and Management Advisory Services (AMAS) has completed a review of the Staff HR Compensation unit's classification review, stipend review and Staff Appreciation and Recognition (STAR) award payments for adequacy of internal controls, effectiveness and efficiency of operations, compliance with established University policies and procedures and prudent business practices. We also reviewed the first-year implementation of the Three-year Equity Compensation program for non-represented staff. This audit was included on the campus FY 2021-22 internal audit plan.

Overall, based on the results of work performed within the scope of the audit, we found that current processes ensure unit responsibilities are carried out properly in regards to classification, STAR award and stipend processes. However, there are opportunities to strengthen STAR award and stipend approval processes to ensure compliance with UC policies and campus procedures.

We reviewed the first year (FY2021-2022) implementation of the Three-year Equity Compensation Program for non-represented staff and found that the results match with program parameters. However, we observed that, approximately 81% of the employees who received equity increases through the program are still under the 25th percentile of the Career Tracks Salary Ranges (Effective 4-1-2021) after their equity increase.

As an important component of the equity program, all new hires in non-represented roles made on or after November 1, 2021 are expected to be hired no lower than the 25th percentile of their salary grades. We observed that, unless moving a current employee's salary at or over the 25th percentile, a new hire would be receiving a higher salary than an employee who is currently working below the 25th percentile in the same salary grade.

The following observation requiring management corrective action were identified:

A. Exception to Policy Approvals

We found that some instances of stipend payments that exceed stated limits under PPSM-30 Compensation policy were not approved explicitly as exceptions.

B. Routing for Approvals

We identified opportunities to strengthen internal controls to ensure STAR award and Stipend reviews are routed for necessary approvals.

Agreement was reached with management on the recommended actions to address the risks identified in this area. The observations and the related management corrective actions are described in greater detail in section III.

II. INTRODUCTION

Purpose

The purpose of this audit was to evaluate the Staff HR Compensation department's processes for adequacy of internal controls and compliance with relevant UC policies and the procedures. This audit was included on the campus FY 2021-22 internal audit plan.

Background

The Staff HR Compensation unit provides services to the campus in the following areas:

- Compensation planning, development and administration
- Classification and reclassification of positions
- Implementation of wage changes
- Salary administration and awards
- Fair Labor Standards Act Implementation and training
- Collection and distribution of salary survey data

Beginning in October 2019, Staff Human Resources, in full partnership with Information Technology Services, has launched digital Employee Action Request (EAR) processes. These EAR processes include stipends, equities, job description updates, and classification reviews, which were previously supported by a paper workflow. By this digital transformation, Staff HR aimed to introduce transparency and accountability into the processes by giving requesting units visibility to see their requests move through the process, as well as enhance the efficiency of the process by reducing errors and route approvals quickly.

Staff HR Compensation unit functions relevant to this audit include:

Classification Review: The classification review process is designed to ensure positions are clearly and properly classified in relation to the career track or represented job classification standards. A reclassification is a change in classification that occurs due to changes in duties and responsibilities of the position.

The classification review process addresses incumbent-held positions only; new or vacant positions are initiated via a Position Control Request.

UC- Policy PPSM-36 and relevant Collective Bargaining Agreements (CBAs): Classification of Positions describes how a position is classified and the availability of a classification review. The Staff HR Compensation unit website provides detailed guidelines to the campus regarding classification review.

Salary Stipend Review: An administrative stipend is a temporary pay action that an employee receives when they are temporarily assigned an increased responsibility, such as:

- Significant additional duties or short-term projects not currently a part of the employee's regular position
- Duties of a position in a higher grade or classification which would result in an upward reclassification if permanently assigned or out of classification assignment as defined within collective bargaining agreements.

Permanent increases in responsibility are addressed through the reclassification or equity process.

For non-represented staff, the stipend amount and duration must be in accordance with PPSM-30 Compensation policy. Represented staff are eligible for stipends only as outlined in the respective collective bargaining unit agreements. We limited the scope of our review to policy-covered employee's stipend payments.

PPSM-30 Compensation states that

- The stipend amount cannot exceed 25 percent of the employee's base salary.
- The payment of administrative stipends is intended to be temporary and generally should not exceed 12 months; however, if necessary, one extension of up to an additional 12 months may be approved in accordance with Section IV.C.1 of this policy.
- An extension of an administrative stipend beyond 24 months is an exception to this policy.

Staff Appreciation and Recognition (STAR) Plan: The purpose of the STAR Plan is to recognize and reward employees in accordance with the performance standards, such as, exceptional performance, creativity, organizational abilities, work success, exhibiting extraordinary commitment to promoting and protecting principals of community and teamwork.

The following limits apply to STAR Plan cash awards.

- Cash awards of up to \$10,000 or 10% of annual base salary, whichever is less, may be granted to an eligible employee.
- An employee may receive a combination of awards providing that the cumulative amount does not exceed the maximum allowable limit for the fiscal year of \$10,000 or 10% of annual base salary, whichever is less, prorated to appointed time.

The Chancellor must approve awards above \$5,000, including combined awards that exceed \$5,000.

Starting from FY 21-22, the central contribution toward STAR awards was changed to support the three-year equity program. This meant that beginning in FY 21-22 the STAR Plan was funded by the department or division and central funding was not provided.

Units will need to follow appropriate fund usage and/or restrictions. For example, general funds may not be used for non-general funded positions/functions. Federal funds are generally not allowed for awards, unless specifically approved by the granting agency.

Three-year Equity Compensation Program for non-represented staff:

In 2018, a Campus Welfare Committee was formed to research and analyze relevant data and make recommendation regarding employees' dissatisfaction with base compensation and related administration. One of the key findings of the committee was a significant amount of UCSC staff were paid below the market rate of their roles.

In 2021, at the request of the Chancellor and the Campus Provost and Executive Vice Chancellors, Staff HR formed another task force and updated the 2018 Campus Welfare Committee's report regarding the compensation philosophy.

In September 2021, the Chancellor shared the new compensation philosophy and the decision to implement specific changes to staff compensation practices for non-represented staff. The principles of the new compensation policy include recruiting, developing and retaining a well-qualified and engaged workforce and being as competitive as possible relative to the market.

In accordance with the philosophy, UC Santa Cruz decided to invest \$5.5 million over three years FY21-22, FY22-23, and FY23-24, in a salary equity program to align non-represented staff salaries closer to the market. As a first step the program targets everyone who was below the 25th percentile pay grades 15 to 30. For the five highest salary grades (26-30), there were no salary adjustments in the first year of this program for employees who are now at or above the 25th percentile.

Eligibility criteria:

- Non-represented career, partial career and contract employees
- Employees who have a "met expectation" performance rating or above for 2020-2021
- Employees hired before November 1, 2021.

According to the compensation philosophy, as a new practice, all hires in non-represented roles will have their starting salaries set at no lower than the 25th percentile of their salary grade.

Scope

Our review consisted of four topic areas: Classification, Stipends, Staff Appreciation and Recognition (STAR) award processes and the first year implementation of the Three-year Equity Compensation Program for non-represented staff. We conducted this audit by means of following:

- Reviewed UC and UC Santa Cruz policies, guidelines, best practices relevant to classification and compensation.
- Reviewed audit reports conducted at UC campuses related to classification and compensation.
- Reviewed UCSC Campus Welfare Committee Compensation Philosophy report (2018) and 2021 Compensation Philosophy Update to the 2018 report.
- Reviewed the emails from the Chancellor's and Associate Vice Chancellor Staff HR, regarding the Three-year Equity Compensation Program for non-represented staff.
- Interviewed Staff HR personnel to gain an understanding of overall processes and procedures for classification and compensation actions.

- Performed and documented a risk assessment based on the results of our preliminary work, such as interviews, review of documentation, and other observations.
- Obtained classification review, salary equity review, stipend review request from July 1, 2020 to February 28, 2022 documentation.
- Detailed testing included an evaluation of:
 - Classification review process
 - Administrative stipend review process
 - STAR award process
 - The first year (FY 2021-22) implementation of the Three-year Equity Compensation Program for non-represented staff.

For additional details, please see Appendix A. Summary of Work Performed and Results.

III. OBSERVATIONS REQUIRING MANAGEMENT CORRECTIVE ACTION

A.	Exception to Policy Approval	
We found that some instances of stipend payments that exceed stated limits under PPSM-30 Compensation policy were not approved explicitly as exceptions.		
Risk Statement/Effect		
Without a clear process for obtaining exception to policy approval, the senior managers may not be informed explicitly that approval request is for a policy exception.		
Agreement		
A.1	The SHR will establish a step in the process that separates exception to policy approvals from the approvals exceed delegated authority limit.	Implementation Date
		10/01/2022
		Responsible Manager
		Manager of Compensation, Policy, Operations & CruzPay

A. Exception to Policy Approval- Detailed Discussion

Overall, we found that the Compensation unit has appropriate control over the stipend approval process. However, we found opportunities exist to improve exceptions to policy approvals.

Per PPSM-30 Compensation policy, the stipend amount cannot exceed 25 percent of the employee’s base salary and an extension of an administrative stipend beyond twenty-four months is an exception to this policy. These salary actions must be approved as exceptions.

Per SHR practice, administrative stipends above 25% or exceeding one year require the approval of a principal officer. This approval is captured by Service Now (Employee Action Request System) or obtained as an email attachment.

This practice does not provide clarity about whether a principal officer’s approval is required for a salary action exceeds delegated authority limits or for an exception.

For example, a stipend payment over 12 months is not an exception to policy, but it requires the principal officer’s approval and cannot be re-delegated. However, an administrative stipend beyond 24-months or

exceeding 25 percent of base salary requires policy exception approval. Per SHR practices, the principal officer’s approval is being obtained in the same way for both cases.

We found that five of nine policy exception approvals were requested with a similar explanation that the salary action required the principal officer’s approval because it exceeded delegated authority limits. These approvals should have been requested explicitly as policy exceptions.

B.	Routing for Approval	
We identified opportunities to strengthen internal controls to ensure STAR award and stipend reviews are routed for necessary approvals.		
Risk Statement/Effect		
Noncompliance with the policy and campus procedures.		
Agreement		
B.1	The SHR will implement additional controls into their processes to ensure approvals are obtained.	Implementation Date
		10/01/2022
		Responsible Manager
		Manager of Compensation, Policy, Operations & CruzPay

B. Routing for Approvals – Detailed Discussion

Overall, we determined that the Compensation unit had effective controls over stipend review and STAR award payment processes and the unit responsibilities were carried out appropriately.

However, we found opportunities exist to improve the stipend and STAR award routing for approval step to ensure appropriate approvals are obtained in accordance with the UC policy and campus procedures.

When reviewing the stipend and STAR award processes, we found the following;

- We found 11 employees’ stipend payments were processed over 25% of their base salaries, while principal officers approved only nine of them.
- Eight employees’ stipend periods were more than 24 consecutive months, while the principal officer’s approvals were received for only seven of them. One employee’s stipend payment was

over 24 months, but had multiple stipends, which is why it escaped the principal officer's approval.

- We identified 13 employees whose STAR award payments exceeded \$5,000. The Chancellor approved 11 of them, but two were not submitted for her approval.

An effective internal control helps ensure that STAR award and stipend approvals are obtained in accordance with policy and reduces the risks of noncompliance with the policy and campus procedures.

During our review we found some award payments were made from federal awards. We also found payments from general funds for positions that were fully funded from fund sources different from general funds that included federal awards, private gifts, auxiliary enterprise funds, and recharge funds.

We did not extend our review to examine the appropriateness of these funds. However, our initial evaluation showed that there is an opportunity to strengthen the internal controls to help appropriate fund usage.

Although units are fully responsible for providing appropriate fund sources, SHR could request budget approvers to approve the appropriate funding by adding a check box in the "STAR award nomination spreadsheet." This will help mitigate the risk of using inappropriate funds.

APPENDIX A. SUMMARY OF WORK PERFORMED AND RESULTS

Preliminary Analysis	
Work Performed	Results
<ul style="list-style-type: none"> ● Reviewed UC and UC Santa Cruz policies and guidelines. 	<p>We identified the relevant policies and guidance:</p> <ul style="list-style-type: none"> ● University of California – Policy PPSM-30: Compensation ● University of California – Policy PPSM-36: Classification of Positions ● University of California – Policy PPSM-34: Incentive and Recognition Award Plans ● SHR Services Client Guide for IT Request
<ul style="list-style-type: none"> ● Reviewed audit reports conducted at UC campuses related to classification and compensation. ● Reviewed UCSC Campus Welfare Committee Compensation Philosophy report (2018) and 2021 Compensation Philosophy Update to the 2018 report. ● Reviewed the emails from the Chancellor’s and Associate Vice Chancellor Staff HR, regarding the Three-year Equity Compensation Program for non-represented staff. ● Interviewed Staff HR Compensation and Operations Manager. ● Reviewed UCSC Staff HR, UCOP and UC campuses web resources related to Classification and Compensation processes. 	<ul style="list-style-type: none"> ● Identified common issues from other campuses. ● Learned UCSC Three-year Equity Compensation program objectives, eligibility criteria and implementation. ● Gained an understanding of overall campus processes and procedures for classification and compensation. ● Developed a risk matrix and audit program to address the risk areas identified.

Fieldwork	
Work Performed	Results
<p>1. To evaluate the Classification review process for adequacy of internal controls and compliance with UC policies and the campus procedures. Performed the following;</p>	
<p>Obtained a list of Classification review requests that the SHR Compensation unit processed from July 1, 2020 to February 28, 2022.</p> <p>From the data, we judgmentally selected 11 completed reviews based on our initial analysis. We reviewed the sample for adequacy of internal controls and compliance with relevant policies and procedures.</p>	<p>Overall, we did not find any concerns related to the Classification review process.</p>
Work Performed	Results
<p>2. To evaluate Staff Appreciation & Recognition (STAR) award review process for adequacy of internal controls and compliance with UC policies and the campus procedures. We Performed the following;</p>	
<p>Independently obtained STAR award payments between July1, 2020-June 30,2021 from Infoview DOPE reports. We analyze the data;</p> <p>To determine whether the STAR award payment paid to each employee did not exceed the maximum allowable limit for the fiscal year of \$10,000.</p> <p>To determine whether the amount of STAR award payment paid to each employee did not exceed the employee`s 10% of annual base salary. From the data, judgmentally selected STAR award payments to 10 employees for detailed testing.</p>	<p>None of the STAR award payments exceeded \$10,000 during FY21.</p> <p>For all 10 samples, STAR award payments were under 10% of their base salaries.</p>

<p>We identified STAR award payments over \$5,000 and obtained approval documents from SHR, to ensure the Chancellor’s approval was obtained for STAR award payments above \$5,000, including combined awards that exceed \$5,000.</p>	<p>13 employee award payments exceeded \$5,000. 11 of them were approved by the Chancellor. The other two were not submitted to the Chancellor’s approval.</p>
<p>We reviewed fund sources which STAR awards were paid to identify; Whether federal funds were used for awards. Whether General Funds were used for non-general funded positions.</p>	<p>We identified award payments from federal grants. We did not extend our review to check if the federal agency's approvals were received for those payments.</p> <p>We identified award payments made from General Funds (19900-19999) for the positions that were fully funded from fund sources different from 19900-19999. Those funds include federal awards, private gifts, auxiliary enterprise, recharge funds. We did not extend our analysis to determine if every position paid from those funds was eligible funds for payments.</p> <p>Our initial evaluation showed that there is an opportunity to strengthen the internal control to ensure appropriate fund usage.</p> <p>Although the requester unit is responsible for providing appropriate fund sources, the SHR could request budget approvers’ approval along with the “STAR award nomination spreadsheet” from units.</p>
<p style="text-align: center;">Work Performed</p>	<p style="text-align: center;">Results</p>
<p style="text-align: center;">3. To evaluate Administrative Stipend approval process for adequacy of internal controls and compliance with UC policies and the campus procedures. We Performed the following;</p>	
<p>Obtained a list of Stipend review requests that the SHR Compensation unit processed from July 1, 2020 to February 28, 2022. We analyzed the data;</p>	

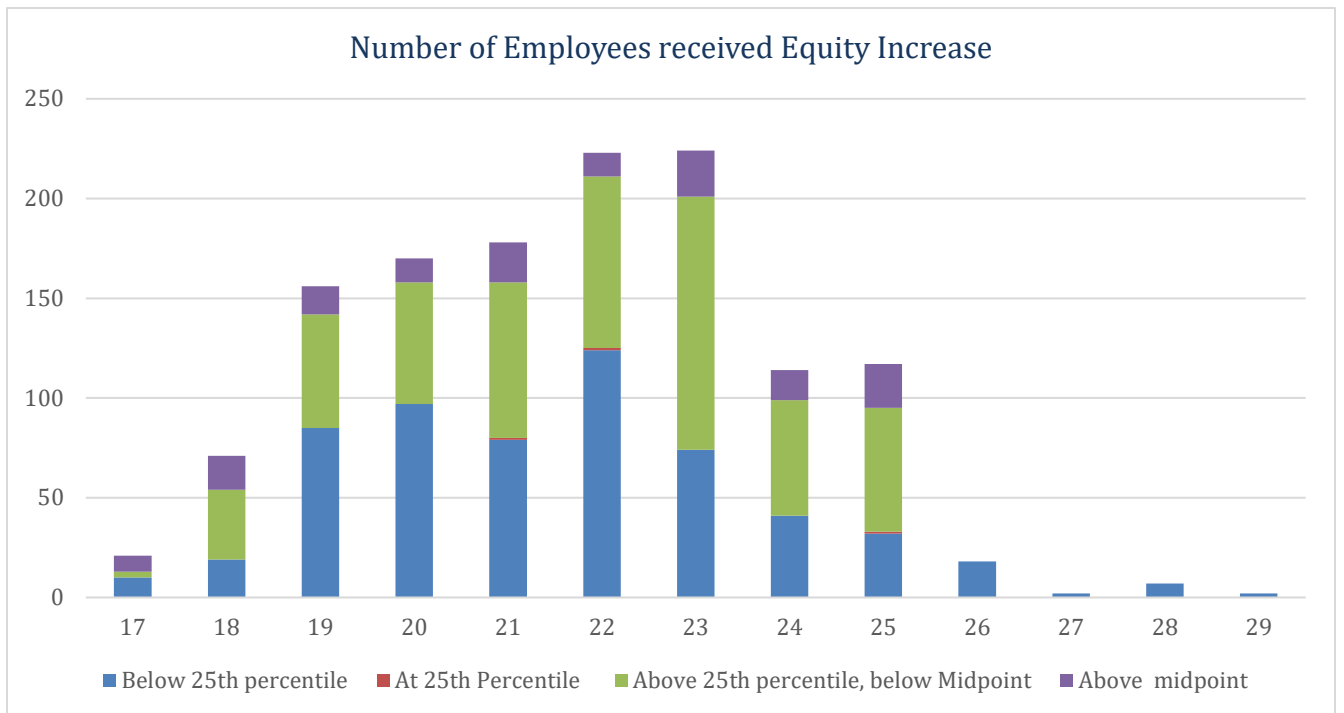
<p>Obtained the complete list of employees who received equity increase through the first-year implementation of the Three-year Equity Compensation Program and relevant data from Staff HR.</p> <p>We analyze the data in accordance with the program parameters below;</p> <p>For the highest salary grades (26-30) there are no salary adjustments in year one of this program for employees who are now at or above 25th percentile</p> <p>Salary increases will range from 0% to 6%</p> <p>About 82% of the approximately 1650 non-represented staff will receive an equity adjustment in the first year of the program.</p> <p>Based on the program parameters 71% of the funds will be distributed to employees at or below 25th percentile.</p> <p>Approximately 94% of the \$2.5 million will be distributed to the employees in grades 15 through 25.</p>	<p>In FY2020-2021, total \$2,408,552 fund was distributed through the program.</p> <p>No employee above 25th percentile received equity increase in the highest salary grades (26-30)</p> <p>Salary increases range applied from 0.24% to 6.37%</p> <p>1,303 employee received equity increase through the program in the first year.</p> <p>About 79% of approximately 1650 non-represented staff received an equity increase.</p> <p>Approximately 71% of the funds distributed to employees at or below 25th percentile.</p> <p>94% of the \$2.408,552 was distributed to employees in grades 15 through 25.</p> <p>Results of our analysis closely match with the program parameters.</p>
<p>We also analyze the data further to see the result of the first-year implementation of the program</p>	<p>590 Employees under 25th percentile and 3 employees at 25th percentile received equity increase in the first year of the program.</p> <p>After the equity increase, 476 employees stayed below 25th percentile. Approximately 81% of the employees in the list still under 25th percentile</p>

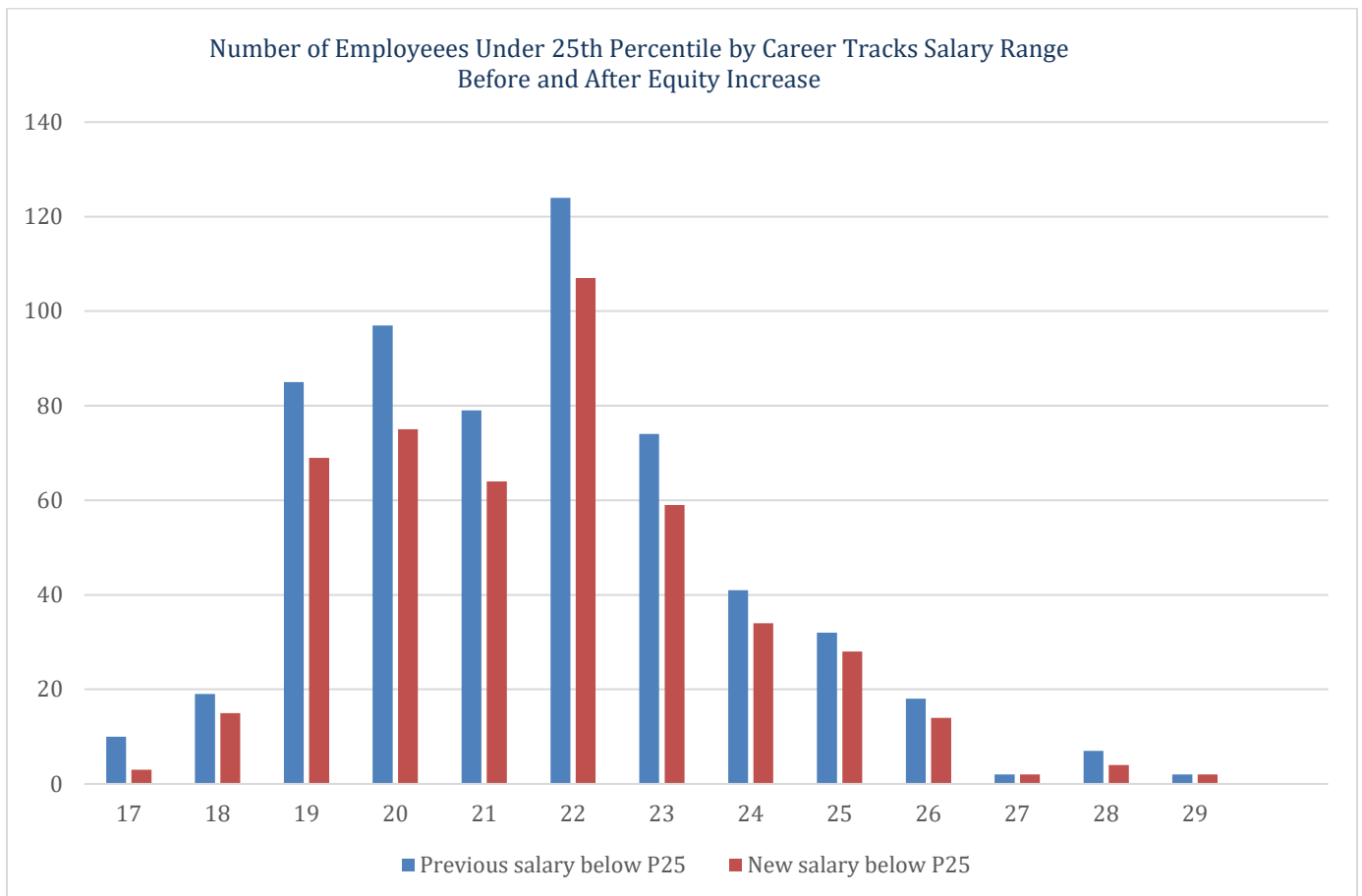
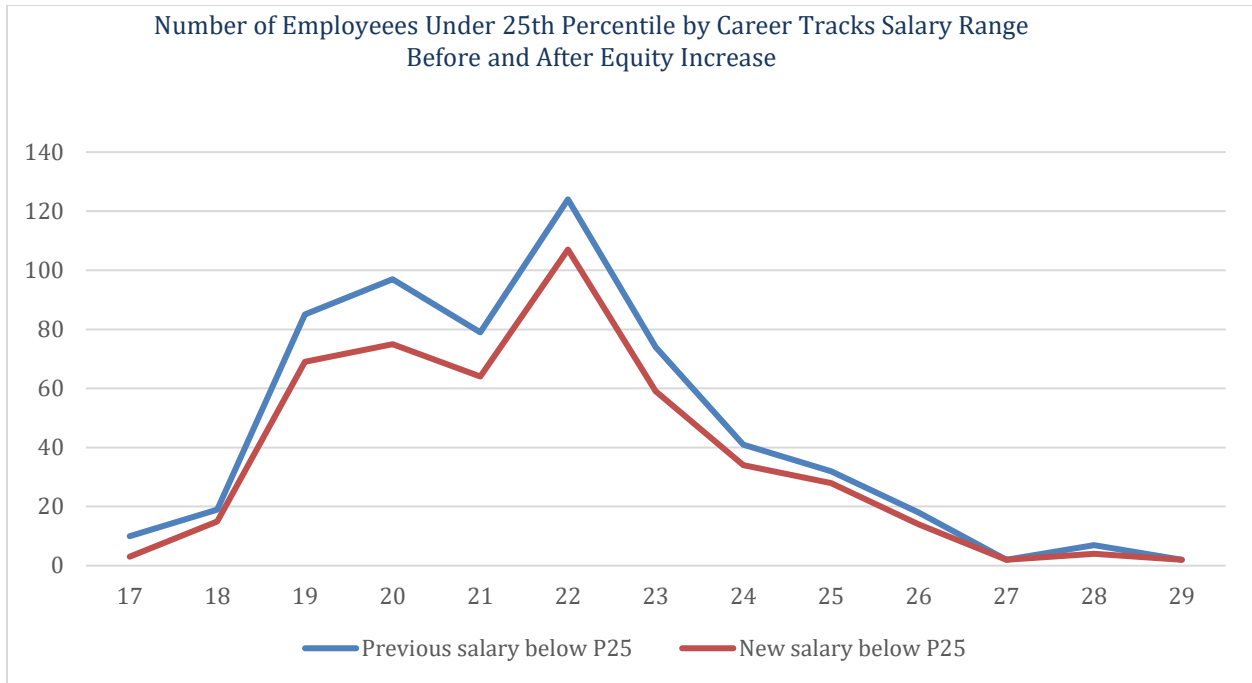
	<p>For the new compensation practices, "All new hires in non-represented roles will have their starting salaries set at no lower than the 25th percentile of their salary grades."</p> <p>According to this practice, a new hire will have a higher salary than an employee currently working at below 25th percentile in the same salary grade.</p>																									
<p>We performed analysis to see the results with quartile ranges.</p>	<p>Fund distribution percentages per quartiles;</p> <p>P0-25 70.8 % P25-42 22.8 % P42-58 5.8 % P58-75 0.6 %</p> <p>Number of employees in each quartile before and after equity increase and percentage of changes;</p> <table border="1" data-bbox="808 884 1356 1058"> <thead> <tr> <th></th> <th>Q1</th> <th>Q2</th> <th>Q3</th> <th>Q4</th> </tr> <tr> <th></th> <th><u>P0-25</u></th> <th><u>P25-42</u></th> <th><u>P42-58</u></th> <th><u>P58-75</u></th> </tr> </thead> <tbody> <tr> <td>Before</td> <td>590</td> <td>413</td> <td>244</td> <td>56</td> </tr> <tr> <td>After</td> <td>476</td> <td>489</td> <td>275</td> <td>63</td> </tr> <tr> <td>Change%</td> <td>-19%</td> <td>18%</td> <td>13%</td> <td>13%</td> </tr> </tbody> </table> <p>This analysis showed that, the number of employees in P0-25 ranges dropped by 19%, and P25-42, P42-58, P58-75 increased by 18%, 13%, 13% respectively.</p> <p>Per 2021 Compensation report, in order to actualize the compensation philosophy, UCSC practices require most of employees to be paid at or within an appropriate deviation around the midpoint of salary ranges. In other words, most employees would be expected in the second or third range quartiles.</p> <p>The result of analysis showed that, 19% of employees in Q1 moved towards or above midpoint. However, the number of employees in Q4 increased by 13%, while one of the main expectations from the program to see the most employees in Q2 and Q3.</p>		Q1	Q2	Q3	Q4		<u>P0-25</u>	<u>P25-42</u>	<u>P42-58</u>	<u>P58-75</u>	Before	590	413	244	56	After	476	489	275	63	Change%	-19%	18%	13%	13%
	Q1	Q2	Q3	Q4																						
	<u>P0-25</u>	<u>P25-42</u>	<u>P42-58</u>	<u>P58-75</u>																						
Before	590	413	244	56																						
After	476	489	275	63																						
Change%	-19%	18%	13%	13%																						

APPENDIX B. THREE -YEAR EQUITY COMPENSATION PROGRAM- FIRST YEAR IMPLEMENTATION

NUMBER OF EMPLOYEES RECEIVED EQUITY INCREASE -FIRST YEAR

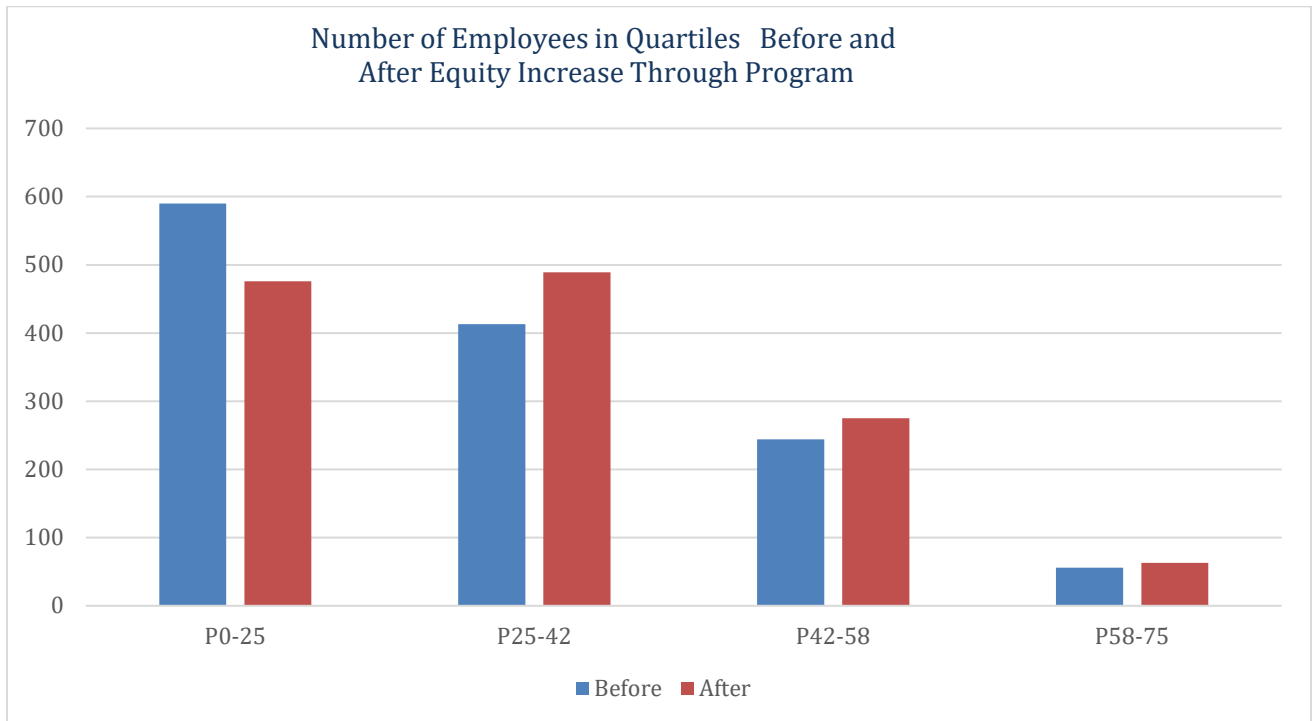
Career Track Salary Ranges	Previous salary below P25	Previous salary at P25	Previous salary above P25, below Midpoint	Previous salary above midpoint	Total	New salary below P25
17	10	0	3	8	21	3
18	19	0	35	17	71	15
19	85	0	57	14	156	69
20	97	0	61	12	170	75
21	79	1	78	20	178	64
22	124	1	86	12	223	107
23	74	0	127	23	224	59
24	41	0	58	15	114	34
25	32	1	62	22	117	28
26	18	0	0	0	18	14
27	2	0	0	0	2	2
28	7	0	0	0	7	4
29	2	0	0	0	2	2
Total	590	3	567	143	1,303	476





Number of Employees in Each Quartile before and after Equity increase

	Q1 P0-25	Q2 P25-42	Q3 P42-58	Q4 P58-75
Before	590	413	244	56
After	476	489	275	63
Change %	-19%	18%	13%	13%



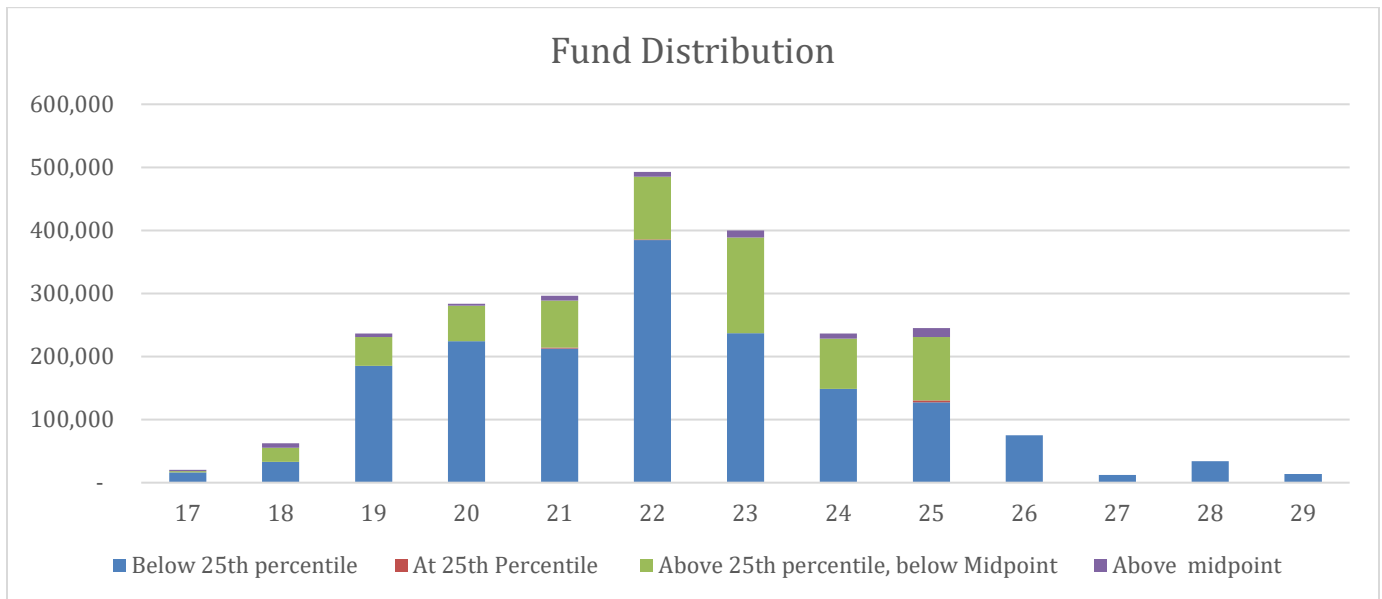
SALARY CHANGE PERCENTAGE

Career Track Salary Ranges	Lowest change %	Highest change %
17	0.24%	4.78%
18	0.24%	4.78%
19	0.24%	6.37%
20	0.24%	6.37%
21	0.24%	6.37%
22	0.24%	6.37%
23	0.24%	6.37%
24	0.24%	6.37%
25	0.24%	6.37%
26	3.19%	4.78%
27	3.19%	6.37%
28	1.59%	4.78%
29	4.78%	4.78%

FUND DISTRIBUTION BY SALARY RANGES (\$)

Career Track Salary Ranges	Below 25th Percentile	At 25th Percentile	Above 25th Percentile, below Midpoint	At or Above Midpoint	Total	%of fund distributed at or below 25th Percentile
17	16,152	0	2,112	2,202	20,466	79%
18	33,272	0	22,308	6,984	62,564	54%
19	185,477	0	45,267	5,862	236,606	79%
20	224,180	0	56,357	3,168	283,704	77%
21	212,613	1,716	74,383	7,537	296,249	72%
22	384,525	962	99,768	7,425	492,680	78%
23	237,087	0	151,586	11,104	399,777	59%
24	148,589	0	80,016	7,695	236,300	63%
25	127,558	2,650	100,688	14,215	245,111	55%
26	75,060	0	0	0	75,060	100%
27	12,147	0	0	0	12,147	60%
28	34,271	0	0	0	34,271	100%
29	13,616	0	0	0	13,616	100%
Total	1,704,547	5,328	632,484	66,193	2,408,552	
Percentage in total	70.8%	0.2%	26.3%	2.7%		

	Distributed Fund (\$)	% of total distribution	# of Employee
Increase in grades 15 through 25	2,273,458	94.39%	1,274
Increase in grades 26 through 29	135,094	5.61%	29



FUND DISTRIBUTION BY QUARTILES (\$)

Career Track Salary Ranges	P0-25	P25-42	P42-58	P58-75	Total
17	16,152	1,200	1,488	1,626	20,466
18	33,272	17,070	10,102	2,119	62,564
19	185,477	38,560	11,793	776	236,606
20	224,180	48,199	9,418	1,908	283,704
21	212,613	66,050	15,441	2,145	296,249
22	384,525	89,307	17,684	1,164	492,680
23	237,087	127,192	33,590	1,908	399,777
24	148,589	68,248	18,150	1,313	236,300
25	127,558	92,830	22,635	2,088	245,111
26	75,060				75,060
27	12,147				12,147
28	34,271				34,271
29	13,616				13,616
Total	1,704,547	548,656	140,301	15,047	2,408,552
<i>Percentage in total</i>	70.8%	22.8%	5.8%	0.6%	

