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HUMAN CAPITAL: Incentive Awards Were Appropriate, But Payment Controls Can Be Improved

Audit Report OIG-A-2015-009 | March 13, 2015

AMTRAK

NATIONAL RAILROAD
PASSENGER CORPORATION

Office of Inspector General

Memorandum

To: Alex B. Melnkovic
Executive Vice President, Chief Human Capital Officer

From: David R. Warren
Assistant Inspector General, Audits

Date: March 13, 2015

Subject: *Human Capital: Incentive Awards Were Appropriate, But Payment Controls Can Be Improved* (Audit Report No. OIG-A-2015-009)

The Board of Directors approved and Amtrak (the company) implemented the FY 2014 Short Term Incentive (STI) Plan. The Passenger Rail Investment and Improvement Act of 2008 encouraged the Board of Directors to develop an incentive pay program for management employees. The initial plan was developed and implemented in fiscal year (FY) 2013. The plan gives non-agreement employees the opportunity to receive monetary awards based on the company achieving pre-determined financial and customer service goals. The plan applies to all non-agreement employees hired on or before July 1, 2014, except employees of the Office of the Inspector General and the Northeast Corridor Advisory Commission. To be eligible for the awards, employees must have received a performance rating of "Met Goals "or higher for FY 2014. The STI award was to be paid no later than December 31, 2014.

The plan for FY 2014 had two components. The first component established a financial performance goal of an adjusted net operating loss of not more than $305 million. This goal had to be achieved before the second component could be considered. The second component set a Customer Satisfaction Index (CSI) goal of 84.25 percent, with a partial incentive payment for achieving a CSI of at least 83.5 percent.

The objective of this audit was to review the accuracy of the company's reported plan goal achievement and payments to employees.

Results

The company reported that it achieved its FY 2014 financial goal, but not its customer service goal. It made monetary award payments to employees for achieving the financial goal. We determined that the goal achievement reported by the company was accurate and was supported by its financial and customer service data. The payments made to employees in 98.4 percent of the cases were accurate. The relatively minor payment errors included $36,907 in overpayments, $2,389 in no payments, and $171 in underpayments. These errors were the result of weaknesses in controls for implementing the payment process. We also noted that these weaknesses led to inefficiencies in implementing the process. We discuss our specific results below.

The Financial Performance Goal Was Met. The company's unaudited FY 2014 financial data reported an adjusted net operating loss of almost $214 million, which was $91 million less than the $305 million financial performance loss goal. We reviewed the STI calculation performed by Finance department officials. The calculation reduced the net operating loss for certain non-cash and other balances to arrive at the adjusted net operating loss. We reviewed the methodology used to perform the calculation and traced the amounts to the company's trial balances. Our review showed that the calculation of the adjusted net operating loss was accurate and supported by the company's trial balance amounts. The majority of the award payments for achieving this goal were made on December 12, 2014.

The results of the FY 2014 financial statement audit, which had not been started as of March 13, 2015, may affect the amount of the adjusted net operating loss. However, it is unlikely that subsequent accounting or audit adjustments will affect the achievement of the goal, given the $91 million difference between the $305 million adjusted net operating loss goal and the reported adjusted net operating loss of almost $214 million.

The Customer Service Goal Was Not Met. Achieving the financial goal triggered consideration of the customer service goal. The company's actual CSI for FY 2014 was 81 percent, 2.5 percent below the minimum goal. As a result, no payments were made for this goal.

We reviewed the processes the company used to solicit and measure feedback through mailed customer surveys and to quantify the CSI results. We also tested the accuracy of three months of data from FY 2014 and found that the results were reliable.

The Payments Contained Minor Errors. Using a specialized data-analysis software tool, we analyzed 100 percent of the award payments made to eligible non-agreement employees.

The payments were accurate, with the exception of a minor number of overpayments and underpayments. The payment errors resulted from management control weaknesses in the award payment process.

The company made award payments totaling $11.2 million. We determined that 98.4 percent of eligible employees (2,831 out of 2,876) received the correct award payment. We also determined that 1.6 percent (45 employees) received an incorrect award payment. Overpayments totaling $36,907[1] were made to 32 employees. Payments totaling $2,389 were not made to 9 award-eligible employees, and 4 employees were underpaid by $171.[2] These errors resulted from using incorrect information for salaries, hire and rehire dates, transfer dates from union to management positions, and errors in calculating leave-of-absence days. This occurred because of the following:

- Some of the employee compensation information in the company's human capital and payroll system was inaccurate.
- The automated system used to calculate award payment amounts was not fully developed and tested prior to being used. As a result, all possible payment scenarios were not included in the system.
- Complex cases that were not automated required staff to make time-consuming manual calculations that resulted in errors.

The Controls Over the Payment Process Were Weak. Controls over the incentive payment process—including policies and procedures—were not fully developed and documented before the payments were processed. As a consequence, award-payment policies and procedures for certain cases were developed as the process was being implemented. These decisions were not adequately documented and could not be verified without discussion with program officials. This weak control environment creates the risk of inconsistent decisions and inaccurate payments.

An incentive committee of senior executives was established to administer the program. However, the only formal information on how the payment process would be implemented was the *Guide to the 2014 Amtrak Short-Term Incentive Plan*, *Frequently Asked Questions and Answers*, and *The 2014 Manager Toolkit–Performance Merit and STI*—documents that were available on the company's Intranet and the Benefits websites. Although useful, this information did not address all aspects of the rewards plan and its implementation policies and procedures. As we performed our review, it became necessary for us to obtain

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[1] These do not include three overpayments of $10,610 that were later recovered.
[2] These do not include one underpayment of $100 that was paid later.

information from Human Capital staff on the policies and procedures they developed as the process was being implemented. For example, policies and procedures were not documented to account for:

- exclusion of Northeast Corridor Advisory Commission members from the plan
- eligibility of employees on military leave of absence
- eligibility of employees who did not return from leave
- approvals for deviations from the plan
- assurance that the employee compensation information in the company's human capital and payroll system is accurate and complete before payments were calculated
- verification that performance ratings used to determine eligibility were completed and finalized

Conclusions and Recommendations

The STI Plan goal achievement was accurately presented, and the overwhelming majority of incentive payments were accurate. However, there were some errors in the payments, and the payment process was more labor intensive than necessary. This resulted from data-system weaknesses and the untimely development of the payment software.

Further, the absence of formal policies and procedures for making award-payment decisions creates a weak control environment and enhances the risk of inaccurate and inconsistent award payments. Because STI payments could be approved in FY 2015 and beyond, addressing these control weaknesses early in the fiscal year could help avoid payment errors and strengthen the integrity and transparency of the process. Therefore, we recommend that the Chief Human Capital officer (1) collect FY 2014 overpayments and make payments to the employees who were inappropriately underpaid. We also recommend the following actions relative to the STI Plan and process for future fiscal years:

(2) Create an official policy documenting the established rules governing the plan and develop procedures for approving and documenting the exceptions. The incentive committee should approve these documents.
(3) Before the incentive payments are calculated, establish and document policies for updating the payroll system with correct employee compensation information and for finalizing performance ratings.
(4) Allow sufficient time to develop and test the automated system for calculating incentive payouts to help ensure that the actual calculations are correct and comply with the established policies and procedures.

Management Comments and OIG Analysis

In his response to a draft of this report, the company's Chief Human Capital Officer (CHCO) agreed with three of our recommendations and partially agreed with the fourth. He also provided action plans and estimated dates. His response is stated below:

> **Recommendation (1)** The Chief Human Capital Officer and Incentive Committee, once formally established, will oversee the Short-Term Incentive plan processes and will approve or disapprove any recommendations and exceptions as deemed appropriate. After an in-depth review of STI processes conducted during FY14, Amtrak management opted not to collect overpayments; however, payments were made to employees who were underpaid.
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> **Recommendation (2)** Management agrees with the recommendation. The Chief Human Capital Officer will direct the SVP, Total Rewards and Director, Compensation to organize a formal Incentive Committee by June 30, 2015. The Chief Human Capital Officer and the Incentive Committee will oversee the plan processes and will approve and/or disapprove any recommendations and exceptions as deemed appropriate. In collaboration with key stakeholders the SVP, Total Rewards and Director, Compensation will be responsible for developing and documenting the established rules governing the Short-Term Incentive Plan and will monitor their effectiveness. The CHCO and the Incentive Committee will conduct a final review of the governing plan rules and provide final approval before the payout, if any. The STI Plan Rules are subject to change at Amtrak's discretion.
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> **Recommendation (3)** Management agrees with the recommendation. The SVP, Total Rewards and Director, Compensation will be responsible for creating an action plan to manage related processes to ensure the successful administration of the STI plan. The action plan will be developed by June 30, 2015. The SVP, Total Rewards and Director, Compensation will:
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> - Identify critical areas of impact/stakeholders and assign roles and responsibilities.
> - Identify critical milestones, timelines, and deliverables.
> - Ensure deliverables effectively address deficiencies highlighted in the STI Plan Payout Audit
> - Provide timely updates to the CHCO and the Incentive Committee.

Recommendation (4) Management agrees with the recommendation. The FY15 STI Process action plan will include scheduled timeframes for system enhancements and testing requirements to ensure compliance with established plan rules, guidelines, and/or procedures.

As discussed above, the company agreed with recommendations two through four. The planned actions they cited are consistent with the intent of our recommendations. With regard to recommendation one, they noted that payments were made to employees who were underpaid. The company further responded that after review, management opted not to collect overpayments. We understand management decided to accept this risk and we will close that part of the recommendation as unimplemented.

Appendix A

SCOPE AND METHODOLOGY

This report provides information on the FY 2014 Short Term Incentive (STI) Plan, including STI payments made to non-agreement employees. Our objective was to review the accuracy of the STI Plan goal achievement and payments to employees. The scope of our work was confined to these issues. We did not review other aspects of the STI Plan. We met with officials from the departments of Human Capital, Finance, and Marketing and Sales.

Our methodology for assessing STI goal achievement included interviewing company officials responsible for the design and implementation of the STI Plan, and reviewing the methodology the company used to determine the achievement of the financial and customer service targets. We also performed limited testing of the underlying financial and customer service data to determine the reasonableness of the reported goal achievement.

Our methodology for assessing the accuracy of STI award payments included using data-mining software to test 100 percent of the STI payments proposed by the Human Capital Compensation (HCC) team. For eligibility requirements and computation guidelines, we relied on three documents: *Guide to the 2014 Amtrak Short-Term Incentive Plan*, *Frequently Asked Questions and Answers*, and *The 2014 Manager Toolkit–Performance Merit and STI*. HCC provided additional guidelines for plan exceptions and interpretation of award pay decisions.

Using the data-mining tool, we downloaded the employee master data file from the company's SAP database. We also obtained from the Human Capital Technology group an electronic report on the performance-rating information maintained in the Success Factors software. Using this information, we calculated the STI payments that should have been made to the eligible employees based on the established eligibility requirements and STI guidelines, and we reconciled our results with the STI calculation files prepared by HCC for payment. For unreconciled amounts, we did the following:

- We compared the employee number, salary, band and zone, hire/rehire date, separation date, and leave of absence days against HCC's STI calculation file, and we noted exceptions.
- We compared the performance ratings HCC used to determine STI eligibility against the performance-rating information maintained in the Success Factors system, and we noted exceptions.

- To validate the exceptions we noted, we presented our findings to HCC and obtained clarification.

To ensure that STI payments were made accurately, we compared the STI calculation file from HCC with the STI payment file received from the company's Payroll department.

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 objective. We performed our work from November 2014 through March 2015 in Washington, D.C.

Internal Controls

We focused our control work on assessing the adequacy of policies and procedures for implementing the STI Plan goal achievement and incentive payments. During our interviews with company officials from Human Capital, Finance, and Marketing and Sales we discussed payment procedures to understand how the STI Plan was implemented and how payments were calculated. We did not review the entire system of controls for the overall STI Plan. This report identifies opportunities for improving internal controls for the incentive payment process.

Use of Computer-Processed Data

To achieve the audit objective, we relied on computer-processed data in SAP and on Success Factors—the employee performance evaluation system.

- To obtain reasonable assurance that we had accurately downloaded SAP data and correctly interpreted it for our analysis, we used our SAP access to view the source data and verify the validity of many of our identified exceptions.
- To ensure that the performance rating information we used for STI calculation was accurate, we collected the ratings maintained in the source system, Success Factors. Because management could not provide us with electronic access to the Success Factors system, we relied on the electronic report obtained from the Human Capital Technology group. We compared the performance ratings in the report with the ratings used by HCC for STI calculation, and we found that the ratings matched for almost all employees. Any deviations we found are noted in this report.

Based on these tests, we concluded that the data were sufficiently reliable to be used in meeting the audit objective.

Prior Reports

None were identified.

Appendix B

ACRONYMS AND ABBREVIATIONS

CHCO	Chief Human Capital Officer
CSI	Customer Satisfaction Index
FY	fiscal year
HCC	Human Capital Compensation team
OIG	Amtrak Office of Inspector General
STI	Short Term Incentive
the company	Amtrak

Appendix C

OIG TEAM MEMBERS

Earl Hedges	Senior Director, Audits
Vijay Chheda	Senior Director, Audits
Alejandra Rodriguez	Senior Audit Manager
Joseph Zammarella	Senior Auditor, Lead
Juan Morales	Consultant

OIG MISSION AND CONTACT INFORMATION

Amtrak OIG's Mission	The Amtrak OIG's mission is to provide independent, objective oversight of Amtrak's programs and operations through audits, inspections, evaluations, and investigations focused on recommending improvements to Amtrak's economy, efficiency, and effectiveness; preventing and detecting fraud, waste, and abuse; and providing Congress, Amtrak management, and Amtrak's Board of Directors with timely information about problems and deficiencies relating to Amtrak's programs and operations.
Obtaining Copies of OIG Reports and Testimony	Available at our website: www.amtrakoig.gov
To Report Fraud, Waste, or Abuse	Report suspicious or illegal activities to the OIG Hotline (you can remain anonymous): Web: www.amtrakoig.gov/hotline Phone: 800-468-5469
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