



THE OFFICE OF THE INDEPENDENT PERFORMANCE AUDITOR

December 17, 2021

Chair Zito,
SANDAG Audit Committee

Dear Chair Zito:

Subject: Testing Results on Corrective Action Plan – Salary and Compensation Performance and Compliance Audit Items due as of September 30, 2021

Background

The SANDAG Office of the Independent Performance Auditor (OIPA) completed a Salaries and Compensation Performance and Compliance Audit (audit) in August 2020. In November 2020, the Board of Directors at the recommendation of the Audit Committee, approved a Corrective Action Plan (CAP) to address audit recommendations relating to the Salaries and Compensation Compliance Audit conducted by the OIPA. As part of the OIPA's roles and responsibilities, quarterly reviews are performed on all CAP's that resulted in an audit finding.

Objective

The objective of this review to ensure that the Corrective Action Plan items approved by the Board of Directors that were due by September 30, 2021 have been implemented and are consistently followed and to ensure that the finding identified in the audit has been corrected.

As stated by Management, there were two action items from the CAP that were due to be completed by September 30, 2021. Both items - *Action V1.2 – To strengthen procedures for awarding compensation adjustments to employees and Action V1.3 – to provide training for completing performance evaluations and preparing and approving compensation recommendations* have been completed. Additionally, testing for proper documentation and consideration on salary increases and lump sum performance bonuses for both FY21 and lump sum merit pay for FY22 was performed.

The CAP includes actions that management are to undertake in response to the recommendations noted in the audit. The OIPA's responsibility is to review the CAP on a quarterly basis for actions that are due based on time commitments that were provided by management.

The review consists of applying the following actions:

1. Vouching that the time commitment was accomplished.
2. Testing the outcomes/outputs (e.g., policies, procedures, tracking sheets, system controls, or

other tangible outputs) exists, are reviewed and to ensure that the matter addresses specific findings and the related causes and effects; and

3. That testing is performed on the action items to ensure that the actions have been successfully implemented, enforced, are sufficiently documented, and that it has corrected the matter in an efficient and effective manner.

It is important to note that testing on a quarterly basis is not the only involvement that the OIPA has in the implementation of the CAP and board approved action items. The OIPA and Management are working proactively and collaboratively on a continuous basis to ensure the success of the CAP implementation.

This review of two action items was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants.

These procedures do not constitute an audit, and we do not express an opinion on the specified elements, accounts, or items. In addition, we have no obligation to perform any procedures beyond those listed in the report that were designed to address the action items requested by the Board in the form of an approved CAP for the Salaries and Compensation Audit.

Action Items and Results

The procedures performed and the results are as follows:

Action Item V1.2:

Recommendation. To strengthen procedures for awarding compensation adjustments to employees:

- ✓ The Performance Management Program policy, which is part of the Employee Handbook, was updated in January 2021 to include a new Performance Rewards section. In summary, this section defines the types of performance rewards available to employees, eligibility criteria, performance standards, the recommendation and approval processes, and program controls.
- ✓ A new Human Resources policy/procedure guide, pertaining to Employee Performance Rewards, has been developed and implemented. This describes and documents existing procedures and practices and incorporates administrative and process improvements designed to ensure compensation decisions are consistent, fair, and defensible, and that appropriate oversight, management, and controls are in place.

OIPA Results – In regard to the two actions above, the OIPA noted the following:

- A Review of the Performance Management Program policy - The OIPA reviewed the documents provided by Human Resource (HR) titled **Performance Management Program Policy**, which is incorporated into the Employee Handbook and noted that the policy includes sufficient detail regarding the types of rewards (merit increases and /or one time performance bonus) that are available to employees, stated criteria, standards and the approval process and program controls that will be implemented to help ensure fairness of treatment within the process.

The policy is divided into four elements which includes the need for both the reviewer and the employee to first define performance expectations, the next an ongoing, frequent and continuous basis, have check-

in conversations to assess if defined expectations are being achieved, and making adjustments as needed. The third element addresses the area of employee's growth and development which involves the employer encouraging and supporting the employee to develop and set professional goals (e.g., develop and improve professional skill sets) that will help to carry the employee into the future and create possibilities for more opportunities. Finally, the fourth discusses the type of rewards which are obtainable to the employee which include merit increase and/or one time performance bonuses.

Based on our review, the OIPA determined that the level of detail provided is sufficient to help guide both the employer and the employee in applying effective tools to support the success around employee performance while ensuring proper documentation and consistent methods in the performance evaluation process.

IPA follow-up Recommendation: Recently there has been a shift in SANDAG's performance review process that moves away from a quarterly formal and documented review to a more informal continuous ongoing process with an annual formal and documented performance review. The OIPA agrees with SANDAG management regarding this change because annual reviews are typically viewed as a more effective and efficient method of performing employee's performance reviews. However, the OIPA suggested that the following recommendations be considered:

1. The policy be updated to reflect the changes in process and the employees be formally noticed.
 2. SANDAG's management are encouraged to actively communicate on an informal basis regarding employee's growth and development and also properly document any areas that require improvements or where work performed is above normal and or outstanding.
 3. SANDAG management ensure proper documentation exists that support the percentage of annual merit increases and bonus and are consistent with merit increases and performances of others with similar successes.
 4. SANDAG management ensure proper documentation exists when employees that are underperforming and expectations are not being achieved.
 5. All documentation should be contemporaneous.
- A Review of the new Human Resources policy/procedure guide, pertaining to Employee Performance Rewards, has been developed and implemented. The OIPA reviewed the document provided by Human Resource (HR) titled **Employee Performance Rewards**. Based on the OIPA review the document clearly defines the roles and responsibilities of those assigned. Additionally, the policy provides detail information on the steps required to be performed by the department, documentation and timelines that the assigned tasks are to be performed. Further, the policy provides additional detail information on other types of pay increases and/or adjustments available that are outside that of merit and performance bonuses that where employee's performance is not a factor.

IPA follow-up Recommendation: Recently there has been a shift in SANDAG's performance review process that moves away from a quarterly formal and documented review to a more informal continuous ongoing process with an annual formal and documented performance review. The OIPA agrees with SANDAG management regarding this change because annual reviews are typically viewed as a more effective and efficient method of performing employee's performance reviews. In addition to the noted changes recommended on the previous policy, OIPA suggest the document reflect similar changes in regard to the

quarterly vs. annual basis for performance reviews, where applicable.

Action Item V1.3:

Recommendation. To provide training for completing performance evaluations and preparing and approving compensation recommendations strengthen procedures for awarding compensation adjustments to employees:

- ✓ According to SANDAG management - An 'Overall Performance Rating' procedure (HR Guidelines – Overall Performance Rating document was provided to the OIPA) was designed and implemented in Spring 2021 as part of enhancing existing tools and practices. This is essentially a "calibration" process that provides Directors an opportunity to normalize any discrepancies or inconsistencies in goal rating scores derived from the quarterly Performance Check-ins by assigning one of six performance levels to each team member. As part of assigning an Overall Performance Rating, Directors must prepare summary documentation that justifies and supports the rating. The process was used to prepare compensation recommendations for distribution of the 2% Compensation Adjustment Pool approved by the Board in early 2021 and will be used again in the upcoming preparation of performance rewards.
 - One of the controls introduced with the Overall Performance Rating process, was to establish an expected distribution of ratings. The range widths recognize SANDAG's high-performance culture where many employees are regarded as going 'above and beyond' in achieving one or more of their goals in the performance period. The distribution ranges serve as a guide for Directors in assigning ratings and reinforce the importance of differentiating the performance levels of employees within the department.
 - Another control measure introduced with the Overall Performance Rating process ensures consistency in compensation adjustments provided to the employees within a department who have demonstrated similar levels of performance. This was accomplished by setting minimum and maximum performance reward amounts (as a percentage of base pay) and requiring that all employees with the same Overall Performance Rating receive the same performance reward. This process also supports consistency in rewards between departments.
 - A summary report compiled from the Department Compensation Recommendation spreadsheet demonstrates overall consistency in performance rewards was provided to the OIPA. The summary was reviewed by the Senior Leadership Team (among other documents) in their overall review and approval of the compensation recommendations.
- ✓ According to SANDAG Management, with respect to training, Human Resources facilitated several group discussions with Directors in Spring 2021 at the onset of the compensation recommendation cycle, and when the Overall Performance Rating process was introduced, to provide training and answer questions. A version of the 'Overall Performance Rating' procedure was provided as a resource, and the Manager of Human Resources provided one-on-one consultations with Directors as needed. This document was provided to the OIPA for review.

OIPA Results – The OIPA reviewed the HR Guidelines – Overall Performance Rating document and determined that the document provided significant details and guidance regarding the process for Management to score and rate employees. The document provides step by step guidance on the scoring process to help ensure consistency and fairness to the performance review and merit increase process. The document provides further guidance based on a 4-point rating scale with both a narrative

explanation and summarized matrix to simplify the guidance. From an audit perspective, the document was impressive, providing ease of understanding and form. Additionally, it further re-enforced the importance of proper documentation in supporting the scores provided.

The OIPA was provided a compiled spreadsheet consisting of scoring by each department regarding the percentage of score rankings that was supportive of the evaluators (directors, managers, supervisors) understanding and demonstrating consistent employee behavior from SANDAG's total employee population with a majority of the scores between 3.0 and 3.25 (*A 3.25 Overall Performance Rating means an employee has gone above-and-beyond in achieving at least one significant assigned goal in the performance period. A 3.0 Overall Performance Rating means an employee has achieved the goals assigned to them during the performance period*).

Although, the OIPA was not provided support such as training sign-in sheets or name logs identifying managers or directors that attended training, the results of the compensation scoring sheet by department demonstrates that there was sufficient understanding of the guidelines provided to the evaluators.

IPA follow-up Recommendation: Recently there has been a shift in SANDAG's performance review process that moves away from a quarterly formal and documented review to a more informal continuous ongoing process with an annual formal and documented performance review. Once the annual performance process is finalized and established any changes that would impact these guidelines should be revised to reflect the annual performance review process and additional training should be provided. Additionally, a sign-in log should be maintained that supports training effort.

Follow-up Testing on FY21 and FY22 compensation awards:

The OIPA performed testing over final pay increases and lump sum performance bonuses for FY21 and FY22 salary adjustments as a result of documented performance reviews. Additionally, the OIPA performed testing over increases and salary adjustments due to other events that were not based on an employee's performance. The OIPA's tests included a review over the methods used to evaluate other adjustments not based on employee's performance to ensure consistency in the process and that the method and results applied were properly documented and supported adjusted salaries.

OIPA Results:

- ✓ The OIPA reviewed salary increases for FY21 to determine if the methodology, process and practices were properly documented and stated guidelines were consistently followed. Additionally, the OIPA reviewed the payroll salary adjustments for all employees to determine if the percentage increases were consistent with the board approved Compensation Adjustment Pool of 2% awarded by the Board in early 2021 and if those percentages awarded were consistent and fairly distributed.

Based on our review SANDAG employees were compensated and within the percentage range allotted by the Board.

- ✓ The OIPA reviewed FY22 salary pay increases for both performance-based merit increases, lump sum merit increases, and for other pay type adjustments that were not based on a performance

review.

Background – the board awarded a 3% of salary and benefits for merit pay increases plus additional funds for market adjustments based on the recent salary range study that was performed in early 2021 and other considerations. The following pay type adjustments were available for consideration.

1. Merit Increase – based on employee performance reviews
2. Market Adjustments – based on the salary range study that was completed in early 2021
3. Flex Promotion – based on an employee’s progression through the entry levels of their position classification (step increases within their classification)
4. General Pay – based on various considerations that were given to bring employees that are currently working for SANDAG to parity within their range and for the level of effort.

Based on discussions with Human Resources and a review of the methodology and the itemized pay type adjustments calculated by department and for each employee, the OIPA found the adjustment to be sufficiently documented, itemized, and supported with the board approved salary range study. Based on a review of all departments and salary adjustments for each employee within a department, the OIPA reports the following results.

1. Merit Increases – based on the OIPA’s review, a majority of SANDAG staff received merit pay increases, based on performance reviews, between 3% to 7.5% with an average of 5% increase, with some employees receiving less and others more: however, still within a the provided overall board approved increase. As a result, there are a total of 306 employees that received merit pay increases.
2. Market Adjustments – Employees whose classifications were identified in the salary range study received pay adjustments that were reflective of the study results. As a result, there are 79 employees that received adjustments. The percentage increase varied and was based on the board approved salary range study.
3. Flex Promotion – Employees in various classifications were considered for pay step increases based on the employee’s progression of time with SANDAG. As a result, there were 26 employees that received step increases. The percentage increase varied by employee, based on the employees next step in their classification.
4. General Pay – Some employees received additional percentages from 1.5% up to 10% in addition to other pay type adjustments to provide a parity within their range. Employees considered for this adjustment were employees that had been working for SANDAG, providing a higher level of effort and a higher level of performance and commitment to their assigned task. Additionally, the process included additional justification by a member of the SANDAG Management team with a final approval by the SANDAG Leadership team. The increase was based on the belief that the employee should receive additional compensation in order to reach a fair and equitable salary (parity) within their range. As a result, there are 89 employees that received this adjustment.

It should be understood that all employees were eligible, and some did receive more than one pay adjustment type as described above. However, in no case did an employee receive all pay adjustment type increases. The highest percentage pay increase was 25.54% however,

with the exception of three employees that fell within the 20% or higher percentage range, these increases resulted from a mixture of pay type adjustments and a promotion.

The OIPA noted that a number of employees received increases that included receiving a combination of a Merit, Market and General pay adjustment type; the percentage increase ranged between 7.5% and 19% with three employees receiving an increase of 22.7%, 23% and 24.17%.

In regard to the performance-based merit increases, based on the support provided, a larger percentage of employees received an overall performance rating of 3.75 with an average merit increase of 5% with some employees receiving additional pay percentage adjustment types. Based on the OIPA's review of the methodology and other documents provided, it was determined that the salaries increases were sufficiently supported with adequate justification. The items due as of September 30, 2021 have been successfully accomplished and considered closed for further review by OIPA.

The OIPA would like to thank the Executive Director, Hasan Ikhata and SANDAG management and staff for their professionalism, responsiveness, and cooperation during this inquiry.

If you have additional questions, please contact me at (619) 595-5323 or mary.khoshmashrab@sandag.org.

Respectfully,



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