

Draft Report by the Director of Audit  
on the Audit of the Severance Payments Funds  
Ministry of Labour



National Audit Office  
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## Executive Summary

The National Audit Office and the Internal Audit Unit within the Accountant General's Department conducted an audit of the Severance Payments Fund for the period January to June 2020. The audit focused on the payments made from the Fund for Severance and Long Service Gratuities.

The main objective of the audit was to determine whether the payments made from the Fund complied with the requirements of the Protection of Employment Act Cap 18.27. We also looked at the sustainability of the Severance Payments Fund.

We concluded that all the requirements of the Protection of Employment Act Cap 18.27 were not being followed and this conclusion is based on the findings noted below.

### What we found

1. Over \$128,000 paid out to claimants who did not qualify to receive benefits

1. \$4,500 was overpaid in severance benefits and \$24,000 underpaid in long service gratuities because the Department of Labour is not calculating benefits based on 52 weeks before the termination date

1. Errors in computation led to the overpayment of over \$25,000 in benefits

1. Long Service Gratuity is not being calculated on the larger of the average wage or the last wage

To address the non-compliance with the Protection of Employment Act Cap 18.27, we recommend the following:

### What we recommend

- The Department of Labour should recoup the funds paid out to individuals who did not qualify to receive the benefits from the Severance Payments Fund.
- The Department of Labour should train its staff to correctly compute total wages based on the 52-week period immediately before the date of termination.
- Every benefit computation must be verified by a designated officer within the Department of Labour.
- The Department of Labour needs to determine both the average wage and the last wage when computing Long Service Gratuity benefits. The larger of the 2 figures should be used.

## **PART ONE**

### **Background**

The Severance Payments Fund was established by the Protection of Employment Act Cap 18.27.

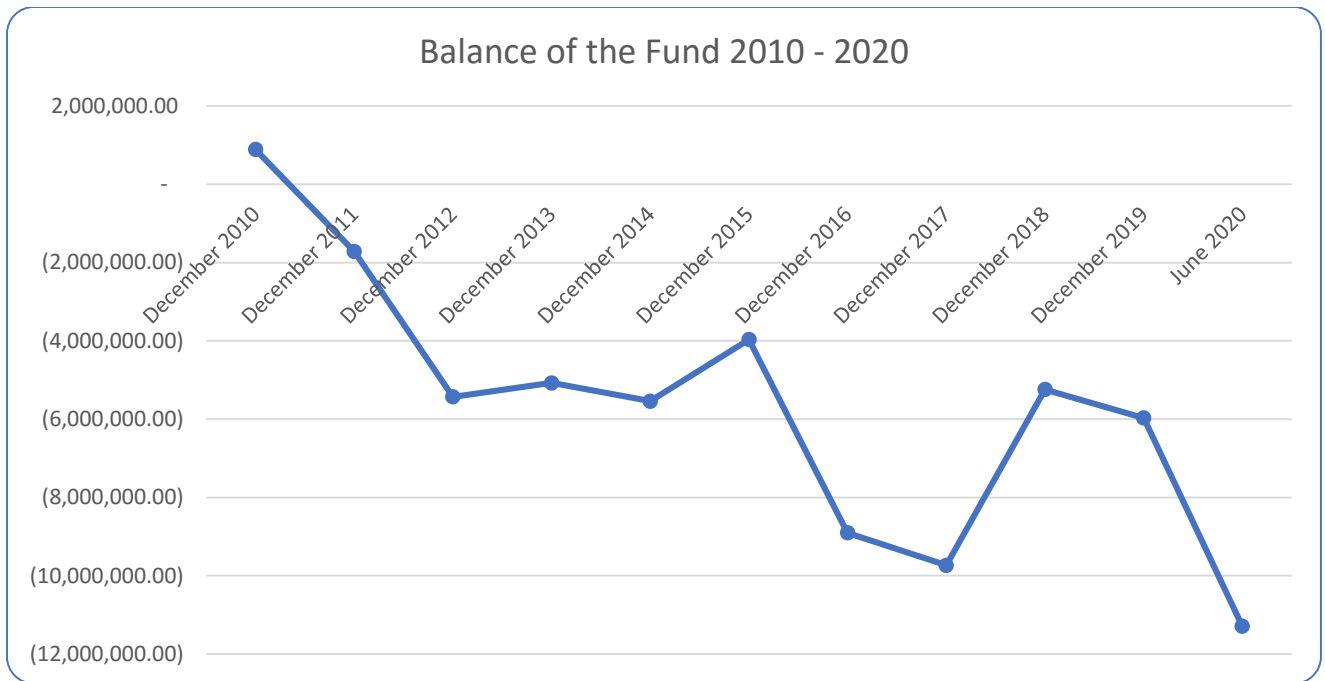
In accordance with the Act, a contribution equal to one percent (1%) of the wages of employees is payable by employers to the Government of St. Kitts and Nevis. The Social Security Board collects this contribution on behalf of the Government of St. Kitts and Nevis and then passes on the contribution to the Department of Labour monthly.

All contributions received by the Government of St. Kitts and Nevis are accounted for in a fund called the Severance Payments Fund which is managed by the Accountant General. The Government, through the Department of Labour, is responsible for paying severance payments out of this Fund to workers who are made redundant.

Long Service Gratuities are also paid from the Severance Payments Fund as provided by the Protection of Employment Act Cap 18.27. However, there are no contributions paid into the Fund on behalf of employees for this purpose.

The Severance Payments Fund has had a negative balance since July 2011, as the payments from the Fund continue to exceed the contributions to Fund. At January 1, 2020, the Fund had a negative balance of **(\$6)** million. By the end of June 2020, the negative balance in the Severance Payments Fund had increased to **(\$11.2)** million.

The illustration on the next page shows the balance of the Fund during the period December 2010 to June 2020.



The illustration below shows the three major events that have impacted the Severance Payments Fund over the past 10 year.



For the period under review, contributions into the Fund totaled \$1.8 million, while payments made from the Fund for Severance and Long Service Gratuities totaled \$7.2 million.

Annually, \$1.5 million was allocated to the Fund from the capital expenditure budget of the Ministry of Labour. That allocation has increased to \$7.2 million in 2021. The Fund also receives \$28,000 in annual interest revenue from a \$1.5 million investment in the Government of St. Kitts and Nevis Treasury Bills.

## **Audit Mandate**

The Audit Act of 1990, part 1, section 6 (1) states that:

“The Director of Audit shall make such examinations and enquiries of Public Bodies as he considers necessary to enable him to report as required by this Act.”

Section 76, subsection 2(a) of the Constitution of the Federation of Saint Christopher and Nevis states that:

“The Director of Audit shall:

- a) Satisfy himself that all moneys that have been appropriated by Parliament and disbursed have been applied to the purposes to which they were so appropriated and that the expenditure conforms to the authority that governs it.”

The Protection of Employment Act Cap 18.27 section 5 states that:

“The Director of Audit shall annually conduct an audit of the Fund and his or her annual report shall be laid before the National Assembly.”

## **Audit Objectives**

The main objective of this audit was to determine whether amounts paid from the Severance Payments Fund for the period January to June 2020 were accurate and complied with the requirements of the Protection of Employment Act Cap 18.27.

To carry out our audit, the main objective was divided into the following sub-objectives:

- Whether each computation had been verified by an officer of the Department of Labour.
- Whether normal wages were used to compute the severance and long service gratuity payments.

- Whether the 52-week period from the date of termination of services was used in the computation of benefits.
- Whether the correct rate of severance payment was used in the calculation of benefits.
- Whether the employee file contained adequate supporting documentation to verify that the employee had been made redundant or had offered his resignation from the employer.
- Whether all persons who received severance and long service gratuity payments were eligible to receive the benefits.
- Whether the long service gratuity is being calculated using either the average earnings or last drawn wage or salary, whichever is more beneficial to the employee.

### **Audit Scope**

The audit focused on the payments made from the Severance Payments Fund for the period January to June 2020. Four payments of severance benefits amounting to almost \$1.2 million were not included in this audit as they form part of a criminal investigation.

### **Audit Criteria**

The St. Christopher and Nevis Protection of Employment Act Cap 18.27 was used to conduct this audit.

### **Methodology**

To carry out this audit, we conducted meetings with staff of the Department of Labour and we recomputed the severance payments and long service gratuity payments made from the Fund.

## **PART TWO**

### **Findings**

**1. Over \$128,000 was paid out to claimants who did not qualify to receive benefits.**

Section 5 of the Protection of Employment Act Cap 18.27 mentions what is considered as termination of employment. Sections 26 and 27 of the Act also documents who has the right to receive severance payments. Section 3 of the Third Schedule of the Act also states that Long Service Gratuity only applies to the manufacturing and hospitality sectors.

We found that there were 5 persons who were paid severance and long service gratuity but did not qualify to receive the benefits. This information is shown in the table below.

<b><u>Type of Benefit</u></b>	<b><u>Payment Amount</u></b>	<b><u>Reason for disqualification</u></b>
Severance	\$36,507.24	Claimant was still employed within the same company. Promoted with an increase in base pay plus commission.
Severance	\$1,651.48	Claimant was not employed for one full year. They did not meet the criteria to qualify for the benefit.
Severance	\$26,278.20	Claimant resigned.
Long Service Gratuity	\$33,810.92	Claimant was not continuously employed.

Long Service Gratuity	\$30,605.29	Claimant did not work within manufacturing or hospitality sectors.
<b>Total</b>	<b>\$128,853.13</b>	

We noted that 2 of these claims had been previously disqualified by the Labour Commissioner. Two of the claims were processed after the Department of Labour received communication from the claimant’s lawyers.

The Department of Labour is not adhering to the specifications of the Protection of Employment Act Cap 18.27 in terms of who can qualify for the right to these benefits.

Section 20 of the Protection of Employment Act Cap 18.27 mentions the right to appeal a decision of the Labour Commissioner to the Income Tax Commissioners. We note that this appeals process is not in place and the decisions on appeals were made by the Deputy Labour Commissioner during the period under review. We did not find any evidence that any of the cases mentioned above were referred to the Attorney General’s Office for a legal opinion on whether the claimant qualified under the provisions of the Act.

**Recommendation**

*The Department of Labour should recoup the funds paid out to individuals who did not qualify to receive the benefits from the Severance Payments Fund.*

*The Department of Labour should advocate for the appointment of Tax Commissioners in accordance with the Tax Administration and Procedures Act Cap 20.52 to allow for the appeals process that is required by the Protection of Employment Act Cap 18.27.*

**2. \$4,500 was overpaid in Severance benefits and \$24,000 was underpaid in Long Service gratuities because the Department of Labour is not calculating benefits based on the last 52 weeks before the termination date.**

Section 32 of the Protection of Employment Act Cap 18.27 states that “a week’s pay in the case of an employee not paid on a piece work basis, is equivalent to the aggregate of the employee’s normal wages for the fifty-two weeks immediately preceding the termination of employment divided by the number of weeks worked;”

We found that 30% of the files sampled were not correctly computed because the 52 weeks before the date of termination was not correctly accounted for. We found that when the date of termination was at the end of the month, the Department of Labour correctly calculated the total wages. However, if the termination date was a date other than the end of the month, the Department of Labour did not count 52 weeks from the date of termination. We found that the Department of Labour always started their calculation from the first of a month regardless of when the claimant’s job was terminated. However, if the claimant was made redundant or retired during a month, the calculation of 52 weeks requires that the wages be apportioned for the beginning and ending months. This was not done.

This led to an overpayment of severance benefits of \$4,500 and an underpayment of long service gratuity payments of \$24,000.

The staff at the Department of Labour has not been following the requirements of the Protection of Employment Act Cap 18.27. We noted that all computations were done in this manner and that the staff had not been trained on using the requirements of the 52 weeks correctly.

## **Recommendations**

*The provisions of the Protection of Employment Act Cap 18.27 must be adhered to. The Department of Labour should train the staff how to correctly compute total wages based on the 52-week period immediately before the date of termination.*

### **3. Errors in computation led to the overpayment of over \$25,000 in benefits.**

Section 30. (1-3) of the Protection of Employment Act Cap 18.27 states that: (1) The rate of severance payment shall be two weeks for each year of continuous service for a period of up to five years service, three weeks for a period of five years to ten years service and four weeks for any period of service in excess of ten years calculated backward from the date of the termination of employment, except in the case of seasonal workers, where the rate shall be one week's pay for each period. (2) Half of a year or more shall be counted as a full year and a period less than half of a year shall be ignored. (3) No employee shall be entitled to more than fifty-two weeks' severance payment.

We found that 23% of the files sampled had errors that could be categorized into 3 groups:

- Incorrect wage figures used – 11 severance and 7 long service gratuity files had errors in wages that led to an overall overpayment of more than \$10,000 of severance benefits and \$1,400 of long service gratuity benefits. We compared the wages used in the computations with those listed in the documents provided by the Social Security Board. We found differences in the amounts recorded. We noted that some wage figures were transposed and some figures were drastically different from those recorded in the documents received from the Social Security Board. We also noted differences in recorded wage amounts

which were taken from bank statements of claimants because they were recorded at net amounts instead of gross.

- Incorrect period/years used - A small number of files had incorrect computations that resulted in an overpayment of over \$13,000 in benefits due to errors in the benefit period used. We found that the number of years served was rounded up to the next full year even though the period was less than half of a year. Errors made in this category resulted in large differences in the computations as the benefits increase with the number of years served.
- Incorrect weeks used – We found errors in this category resulted from the incorrect calculations of the number of weeks in particular months. The number of weeks in a month is determined by the number of Mondays in that month. We found that errors resulted when the Department of Labour listed a month as containing 5 weeks when it should have been 4 and vice versa. This led to an underpayment of severance benefits of \$1,200 and an overpayment of long service gratuity of \$1,300.

Errors in these 3 groups resulted in the government paying out over \$25,000 more than it should have.

The main cause of most of these errors is the lack of verification by the Department of Labour. Errors such as transpositions, incorrect recordings, incorrect weeks during a month and the incorrect calculation of benefit periods should be rectified by a verification process.

As it pertains to the incorrect wages, we noted that when contributions have not been paid by the employer to the Social Security Board, the Department of Labour seeks to obtain information from other sources including bank statements of the applicant. However, the amount deposited to a claimant's bank account will be the net amount and not the gross. Using the net amounts of wages

in a computation will lead to an incorrect benefit calculation. We also noted that the Department of Labour contacts the Social Security Board by telephone to obtain wage information. However, when this was pointed out to us, the wages used in the computation was different from the wages figure in the data provided by the Social Security Board.

### **Recommendation**

*Every benefit computation must be verified by a designated officer within the Department of Labour.*

*The Department of Labour should use documents from the Social Security Board to compute wages. A copy of all contribution filings is sent to the Department of Labour monthly. The Department of Labour should ensure that a filing and record system is in place to ensure that this information can be accessed when needed.*

*Requests made to the Social Security Board for wage information and the response should be documented.*

*In cases where employers have not paid their contributions, the Department of Labour should seek alternative methods of obtaining the correct information.*

#### **4. Long Service Gratuity is only being calculated on the average wage and not on the larger of the average wage or the last wage.**

Section 8 of the Third Schedule of the Protection of Employment Act Cap 18:27 states that; (1) Long service gratuity shall, as provided by section 35A.(1) of the Act, be calculated at the same rate as severance payment. (2) Without prejudice to the generality of sub-regulation (1) in calculating long service gratuity the average earnings or last drawn wage or salary, whichever is more beneficial to the employee, shall be used.

In a sample of 28 long service gratuity files, we found that the Department of Labour used the average wage for all computations of the long service gratuity benefits. We found that the last wage was higher than the average wage for 17 of those files. We noted however that most of the last wages of the claimants were significantly higher than the average wage because the last wage included other payments by the employer to the employee.

This resulted in the government underpaying claimants of long service gratuity by \$369,000.

This occurred because the Department of Labour did not compare the last wage with the average wage to determine which is greater and therefore more beneficial to the claimant.

### **Recommendation**

*The Department of Labour needs to determine both the average wage and the last wage when computing Long Service Gratuity benefits. The larger of the 2 figures should be used.*

#### **5. Only 36% of the files had been signed as having been verified.**

The Processing Form should be signed by the person computing the benefits and the person verifying the claim.

In a sample of 108 severance files, only 39 files or 36.1% had been signed at the back cover as having been verified by the Head of the Verifications Unit. Most of those that had been signed as verified were done during the first quarter of the year.

We noted that the staff of the Department of Labour worked from home during the second quarter of 2020 due to the pandemic. We could not determine if the balance of the files had been verified.

We did note however that the balance of the Processing Form folders was complete.

Not verifying the computations could lead to incorrect calculations, errors and the processing of claims for which persons are not qualified. It could also lead to fraudulent activity as a critical step in the internal control process is being bypassed.

### **Recommendation**

*We recommend that that every computation for benefits be verified by an authorized person within the unit before payment is processed. This also has the added control of holding someone accountable for errors.*

#### **6. Documentation needed to calculate benefits were missing from the files.**

The Processing Claim file should contain adequate documentation to allow for the processing of benefits for the claimant. The Department of Labour's Severance Processing Checklist details the type of documents that need to be presented to the Department of Labour for a claim to be processed. These include a letter from employer, identification, residency documents, completed Claim Form, Social Security contribution sheets and data from Social Security C3 records.

We found that the Social Security Contribution sheets which show the period for which the claimant worked for a particular company was missing from most of the records. This piece of information is important as it shows whether the employment has been continuous and it supports the number of years worked that is listed on the claim form. We also found fewer instances of missing letters of redundancy from the employer and missing identification.

The Department of Labour is not ensuring that all files are complete before they are processed. This could lead to a reliance on information provided by the employer which could be incorrect.

## **Recommendation**

*The Department of Labour should ensure that files are complete before claims are processed.*

### **7. Most of the claims paid by the Department of Labour took between 3 to 6 months to process.**

Section 7 of the Third Schedule of the Protection of Employment Act Cap 18.27 states that ‘...the Commissioner....shall ensure that the payment is made within sixty days...’

According to section 28 of the First Schedule of the Protection of Employment Act Cap 18.27, claims should not exceed three months.

We looked at the time taken to process claims by the Department of Labour by comparing the date the claim forms were received by the Department to the date the payment was approved. From a sample of 157 files, we found that most (36%) of the claims were processed over a three to six-month period. The results are shown in the graph on the next page.



The graph also shows that 83% of the files sampled were processed more than three months after the Department of Labour received the claim form.

We noted letters on files to claimants informing them of additional internal checks that needed to be completed. The letters noted were issued more than three months after the claims were received.

### **Recommendation**

*The Department of Labour needs to analyze and assess their process in the payment of claims to see where bottlenecks exist so that the Department can comply with the provisions of the Act and make the payments in a timely manner. Where additional steps need to be taken or investigations carried out, the Claimant should be informed before the deadline is reached.*

## **8. Legislative reform is needed for the Fund to be sustainable.**

While the focus of the audit was largely on compliance with the Protection of Employment Act Cap 18.27 in terms of payments from the Fund, it is noted that the Fund has not been able to adequately provide for the payments since July of 2011.

The introduction of Long Service Gratuity in 2014 further increased the negative balance of the Fund as payments were being made from the Fund for this benefit, but no monies were being received into the Fund.

The COVID – 19 pandemic and the resulting job losses have placed a greater demand on the Severance Payments Fund and have underscored the fact that the framers of the Act had not envisioned the likes of a pandemic and its impact on such a Fund.

There are several other reasons why the Fund balance is still negative.

All employers who should be contributing to the Fund are not. However, employees should not be penalized from accessing the Fund if their employer did not contribute.

During the audit, we noted that the last 52 weeks of total wages of several claimants were high when compared to previous years or when compared to their normal monthly wage/salary. We noted that many claimants received some sort of extra payment usually during the last month or week of employment in the form of holiday, bonus and terminal grant.

The Protection of Employment Act Cap 18.27 defines “normal wages” as ‘includes any salary or money contracted to be paid or required by law to be paid or given as a recompense, reward or remuneration for any services, work or labour done or to be done.’

This definition of wages is not clear and as of right now, the figure being used by the Department of Labour for wages is whatever is reported as being paid to the claimant. As benefits are paid to claimants based on the average of the last year of wages, a large payment made during the 52-week period before termination will significantly increase the benefits to be paid to the claimant. One percent (1%) of a large one – time payment paid by the employer to the government cannot pay for the benefits that the government must pay out on the inflated figure.

The results of the audit for Long Service Gratuity showed a large difference in the amount that should have been paid to claimants if the last wage was used. Of the 17 files whose last pay was greater than the average wage, 6 of these files had large lump sum payments included in the last pay. This resulted in a difference of over \$260,000 underpaid in long service gratuity payments for those 6 claimants.

### **Recommendations**

*The sustainability of the Severance Payments Fund needs to be taken into consideration. The Fund needs legislative reform that will address how the Fund will function. A clear definition of what constitutes wages, eligibility to receive benefits, provisions of the Fund in times of natural disasters and pandemics, and limits on contributions into and payments out of the Fund may have to be considered.*

### **Conclusion**

The findings of the report indicate that the Department of Labour is not in compliance with the provisions of the Protection of Employment Act Cap 18.27 in terms of payments of benefits from the Severance Payments Fund.