

Saskatchewan Environment
**Internal Audit Report
and Recommendations**

June 7, 2005





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Over the last two years Saskatchewan Environment has undertaken significant change to improve its effectiveness and accountability.

Since May 2003, a comprehensive organizational change effort has been underway to increase management accountability. It introduced a new operational structure and strategic planning process. At the same time, there has been a need to increase respect and accountability between employees in the aftermath of a high profile sexual harassment case.

The new operational design was introduced in February 2004 along with the department's new strategic plan with improved reporting requirements. The change eliminated the five regional management units and required direct reporting into our four operational divisions. As such we dismantled a complex matrix organization with many shared responsibilities to establish "line-of-sight" reporting and accountability to senior management and the executive management team. We reduced the department's management team by one third and ensured all senior managers were informed of their oversight obligations. In June 2004, we introduced a new delegation of signing authority, which reduced the number of employees authorized to approve expenditures and ensured separation between initiating and approving payments.

These changes improved segregation of duties, reinforced specific managerial accountability and clarified administrative processes.

Other changes to improve accountability include consolidating financial processing from 16 sites across the province to four. We increased our internal audit capacity. We have expanded financial management training for all staff. These improvements resulted in a department employee, on December 4, 2004, expressing concerns about a number of financial transactions within the Resource Stewardship Branch. Management confirmed evidence of suspicious payments. Immediately, an employee was suspended and subsequently terminated, security measures were undertaken, the department began an investigation aided by the SPMC Investigation Unit. In addition the Provincial Auditor and the Provincial Comptroller were notified and an RCMP investigation was launched and is still underway.

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The department undertook a comprehensive audit and investigation of the department's financial transactions and internal controls spanning the period of investigation. The audit was carried out with internal audit resources seconded within government and contracted external auditors. The audit plan was reviewed by the Provincial Comptroller and the Provincial Auditor; both concurred with the plan. The findings of the audit have been provided to the Provincial Auditor, the Provincial Comptroller and the RCMP and forms the basis of the Provincial Auditor's report issued June 7, 2005.

The following department report summarizes in detail the activities undertaken by the department's audit team to address the allegation of financial irregularities in Saskatchewan Environment. It also outlines the actions the department has taken to address this serious issue.

At Saskatchewan Environment we have over 1,700 dedicated employees working hard on a daily basis to earn the public's trust. As with the general public, our staff feel a deep sense of betrayal when it appears a professional and public trust has been broken.

As deputy minister the responsibility for rebuilding that trust and public confidence is ultimately mine. Since coming to Environment, we have improved the performance of our organization across many areas of service delivery including financial accountability, and that effort will continue as we strive to be efficient and accountable in carrying out our mandate.

A handwritten signature in black ink that reads "Lily Stonehouse". The signature is written in a cursive, flowing style.

Lily Stonehouse
Deputy Minister

Audit Team

SE seconded two internal auditors from Finance and two internal auditors from Industry and Resources.

SE also engaged senior management and junior audit staff resources from auditing firm Meyers, Norris and Penny.

Department staff, seconded staff and third party resources have spent direct time in excess of 2,200 hours as of May 31, 2005.

The Provincial Comptroller's staff and the Provincial Auditor's staff have completed detailed reviews of all our working paper files.

Audit Scope

SE developed an audit plan for the internal review. The purpose was to:

- isolate the amount of money misappropriated from the department by the identified employee;
- assess which internal controls were absent or circumvented to allow the misappropriation to occur and to recommend changes;
- assess possible existence of similar misappropriation within the department by other employees and to recommend additional work as necessary; and
- assess the system of internal controls for the department's expenditure processes and recommend changes.

The audit plan included a thorough review of all non-salary payments made over a seven-year period for the three branches where the employee worked and had access to generate and/or approve expenditures, along with a random sample of payments from throughout the department.

The transactions were broken into three categories for audit purposes:

- High risk payments - cheques returned to the department for distribution and all payments made to known false vendors, including all non-salary payments to the employee;
- Moderate risk payments - code 2 to 9 payments excluding other government and crown corp payments; and
- Low risk payments - SPMC, and crown corporation utility invoices.

The Provincial Comptroller's office and the Provincial Auditor reviewed the audit plan; both concurred with the plan.

Through its investigation SE reviewed all transactions in Sustainable Lands Management Branch (later the Resource Stewardship Branch) and Regional Services over the seven years under investigation. The investigation included random samples of payments for those years throughout the rest of the department (50 to 70 per year for a total of more than 400 payments throughout the department). This is in addition to the 8,945 transactions set out in the table on the next page.

The following is a summary of the SLMB, RSB, and Regional Services transactions (number and dollar value) individually reviewed for all years in question.

Summary Total		
	Number of Transactions	Dollar Value of Transactions
1998-99	663	\$ 295,366.77
1999-00	1,151	\$ 726,946.20
2000-01	1,180	\$ 860,278.91
2001-02	1,117	\$ 606,850.24
2002-03	1,124	\$ 724,971.61
2003-04	1,203	\$ 1,280,211.04
2004-05	2,507	\$ 5,301,968.49
Total	8,945	\$ 9,796,593.26

Audit Findings

The audit found a maximum of 556 payments were processed and are suspicious in nature. We have confirmed 200 payments as being a misuse of government funds. With assistance from the RCMP investigation, Saskatchewan Environment's internal review of the remaining payments will be completed.

The audit has identified the maximum loss of public money as \$ 511,394.10.

Summary of Suspicious Payments by Year		
Fiscal Year	Payments	Dollar Amount
1998-99	2	\$ 3,160.04
1999-00	28	\$ 29,996.51
2000-01	80	\$ 88,880.48
2001-02	89	\$ 71,389.65
2002-03	111	\$ 85,063.16
2003-04	138	\$ 130,335.61
2004-Dec 31, 04	108	\$ 102,568.65
Total	556	\$ 511,394.10

SE Actions Taken To Date

It is clear from a detailed review of the transactions that none of these individual transactions would have been easily detected through the internal controls in place at the time.

- The nature of the items being acquired individually seemed reasonable in light of the programs being delivered by the branch.
- Other legitimate transactions in the department were being handled the same way for vendor set up and code 1 special cheque handling.

The key detective control that appeared to be absent in this case was management review and oversight control.

The audit team did not find any evidence of similar fraudulent activities in the two branches that were reviewed, nor did any other incidents turn up on our random samples throughout the department.

Over the past year and a half, the department has implemented a range of initiatives as part of a new accountability regime. Initiatives have included:

- Dismantled a complex matrix organization and replaced it with direct, line of sight reporting to enable us to clarify expectations of management and their responsibilities.
- Revised the delegated signing authority to ensure that those approving expenditures are managers with budget responsibilities.
- Redirecting five positions to strengthen financial management and analytical capacity.
- Redirecting another four positions to supervisory roles in the Southern Support Services Unit to ensure each financial supervisor has a manageable span of control.
- Consolidating financial policy responsibilities with delivery of financial services and reducing the number of financial processing sites from 16 to four to increase consistency of application of financial policies.
- Reporting of progress on the department's operational plan on a quarterly basis.
- Evaluating all managers regarding financial control compliance through annual performance reviews.
- Adopting leadership accountabilities which articulate principles to guide manager behaviour.
- Surveying all employees for suggestions respecting cost-saving measures that could be considered during annual budget development cycles.

More specifically - the following internal controls have been put in place directly following this incident.

Vendor Policy

- SE has changed the vendor policy effective December 7, 2004 so that the addition of any new vendor or changes to any vendor addresses must be requested by a Branch Head prior to being approved by either a Support Services Manager or the Director of Finance and Administration. Third party verification of vendor authenticity is performed before new vendor is approved.

Cheque Handling Policy

- SE has set in place a policy with respect to requesting Finance generated cheques be returned to the Department.
- It will only be in rare and very exceptional circumstances that a cheque will be returned to SE and this must be requested from the Executive Director of a branch instead of a manager.
- A monthly report of special handling code 1 transactions is being reviewed by the Support Services Managers and the Director of Finance and Administration.

Delegated Signing Authority

- SE made significant changes to its delegated signing authority document on June 4, 2004
- These changes increased the level of authority required to approve expenditures.
- The delegated signing authority is reviewed by the Finance and Administration Branch and approved by the Deputy Minister on an annual basis (Reviewed 2005/06 Delegated Signing Authority with Senior Management Team on April 12).

Staff Training and Communication

- All Finance and Administration processing staff and managers have been advised of the importance of following the proper protocols and that proper documentation is critical.
- All branch heads (senior management) were trained on the importance of internal controls as well as various aspects of fraud at a January 11, 2005 meeting of senior management.
- All Finance and Administration staff were trained on the importance of Internal Controls as well as various aspects of fraud (training provided to entire branch on January 25, 2005)
- All managers have been advised through training sessions, the purpose of the financial processes and procedures and the resulting risk of not following them diligently - Spring Training was provided in April and May 2005

Qualified Financial Resources

- There were five additional financial positions created in the 2004-05 budget year (two Financial Consultants, two Senior Financial Managers and one Internal Auditor)
- These positions are targeted for individuals with accounting designations and are in the process of being staffed.

Saskatchewan Environment

Response to the Provincial Auditor's 2005 Spring Audit Recommendations

Recommendation

1. We recommend the Department of Environment properly segregate the duties of the employees responsible for collection, receipt, disbursement, or expenditure of public money.

2. We recommend the Department of Environment clearly communicate to its employees its operating policies and ensure that its employees understand the reasons for the policies.

3. We recommend the Department of Environment train its employees to help establish a culture of fraud awareness.

Response

The department implemented a new delegated signing authority in June 2004 that resulted in segregating approval for payments from those who initiate payments. This new delegated signing authority along with the department's 2004 reorganization contributed to the department discovering this loss of public money.

The department will continue to strengthen its segregation of duties and other internal controls throughout the department.

Other payment process controls implemented include establishing a higher level of authority for approving new vendors for set-up on the financial payment system and establishing a higher level of authority for requesting cheques to be returned to the department prior to delivering to suppliers. Support staff can no longer initiate these activities. Branch Head approval is now required.

In addition, the department will complete its review of internal controls by the end of June. Provincial Auditor and Provincial Comptroller will review the results of the review and the department will implement any additional changes over the coming months.

The department financial policies require Branch Heads to review monthly forecasts including monthly listing of payments charged to the branch. As part of an annual performance review, every manager will be evaluated to ensure compliance with this policy.

In April and May 2005 the department initiated training for employees. This training focused on financial operating processes and procedures as well as the delegated signing authority standards within the department. Training sessions were held in Swift Current, Saskatoon, Regina, Prince Albert, Meadow Lake and La Ronge. The department will continue to deliver this training to ensure all employees are included and will also deliver additional training for managers.

At monthly Senior Management Forums, Branch Heads receive regular briefings on the internal control review and the department audit. Managers are briefed on existing and new controls to ensure compliance with policies and operating procedures regarding financial management.

The department delivered fraud awareness and internal control training in January 2005 to the Senior Management Group (all department Branch Heads) and the entire Finance and Administration Branch. This fraud awareness and internal control training was also provided to the Parks Branch in April 2005 and will be delivered to all branches in the department during the remainder of 2005-06.

Recommendation

4. We recommend the Department of Environment assess if the Government's standard blanket fidelity bond (insurance) coverage reduces its risks of loss to an acceptable level.

5. We recommend the Department of Environment assess the risk of loss of public money by employees in positions of trust (responsible for collection, receipt, disbursement, or expenditure of public money) and reduce the risk to an acceptable level (e.g., increasing insurance coverage or requiring criminal record checks).

Overseeing Operations

While there were no new recommendations made, the Auditor continued to recommend (from 1998) that SE "define and document its compliance reporting needs."

Response

The department concurs with the Auditor's recommendation and will be working with Finance and PSC to assess the Government's standard blanket fidelity bond (insurance) coverage in light of the risk of financial loss within the department.

The department concurs with the Auditor's recommendation and will be assessing the risk of loss of public money by employees in positions of trust and have been implementing policies and procedures to reduce this risk to an acceptable level.

We have reviewed all functions on the financial system and have removed all instances where one employee can initiate purchases, and approve transactions for payment.

We have elevated the level of authority required for adding or changing vendors and for requesting cheques be returned to the department for handling.

We have briefed all purchase card holders and have ensured their transactions are approved by supervisors with budgetary responsibilities in agreement with the new designated signing authority.

We have increased our internal audit capacity and have added a position to ensure the appropriate internal controls and monitoring are in place and followed.

We have expanded training for all department staff with responsibility for financial management to further improve compliance with internal controls.

Managers, through annual performance reviews, will be evaluated on compliance with our improved financial controls. The detailed review performed by the internal audit committee has resulted in a process to report on compliance.

In addition, the Provincial Auditor acknowledged that our improved authority grid, introduced in June 2004, clearly sets out who has the authority to initiate and approve payments and the maximum amount and the nature of transactions they can approve.