

**WESTERN ECONOMIC DIVERSIFICATION CANADA**

**FINAL REPORT  
AUDIT OF  
TRANSFER PAYMENTS (GRANTS, CONTRIBUTIONS AND OTHER  
TRANSFER PAYMENTS)**

**July 17, 2006**

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## **EXECUTIVE SUMMARY**

In August 2004, the Audit and Evaluation Branch of WD requested BMCI Consulting Inc. (BMCI) to conduct an audit of Transfer Payments (Grants, Contributions and Other Transfer Payments). The audit commenced with a Preliminary Survey on August 23, 2004 that included initial interviews and document reviews to identify focus areas for the audit. Detailed fieldwork was carried out early in 2005.

The objective of this audit was to conduct an assessment of transfer payments (grants, contributions and other transfer payments) to assess policies, practices and internal management controls applied. This was an audit of the management control framework and any files reviewed were for the purposes of assessing areas where improvements might be required to the policies, practices and internal management controls. The audit assessed compliance with Treasury Board policies and guidelines and WD policies. The universe for this audit was fiscal years 2002-03, 2003-04 and 2004-05 to September 2004.

The most significant issue found is that WD does not have a mechanism in place to demonstrate the degree to which it is open and transparent in selecting recipients for its contribution programs. According to the Treasury Board Policy on Transfer Payments, the type of transfer payment that a department uses to meet its program objectives is determined by the departmental mandate, business lines, clients and an assessment of risk. The Policy further states that all transfer payments are subject to public scrutiny and must be managed in a manner that is open and transparent to the public and with due regard to economy, efficiency and effectiveness. The Treasury Board Policy on Transfer Payments does not define openness and transparency. WD has not defined openness and transparency. In numerous audits over the years, the Office of the Auditor General of Canada has stated that the best way of achieving openness and transparency is through the use of the competitive process.

The Department has not identified the conditions under which it would be appropriate for specific programs or sub-programs to be exempt from the requirement to have participation from more than one organization or even go through a competitive, or request for proposals', process.

A competitive process is rarely used to invite project proposals from a number of potential applicants to be assessed against all proposals received. There is evidence that WD does consider using a Request for Proposal process for programs or subprograms. For example, for the latest Western Economic Partnership Agreement in Alberta, it was determined that a request for proposals' process would be more transparent and would result in the highest quality projects being funded. The other exception noted was the Softwood Industry Community Economic Adjustment Initiative.

The recommendations contained herein will enable the Department to demonstrate how projects that receive funding are selected and to demonstrate that the process is open and transparent.

It was determined that many projects are initiated by invitation from WD to the potential applicant. The Department does not have a system for documenting and summarizing how proposals are initiated. Documentation was not available to identify the objective criteria used to determine why a particular project was regarded as being best value and therefore selected to receive funding. In the case of the Western Diversification Program (WDP) for example, a Due Diligence Report (DDR) is completed for all projects prior to approval. The steps for completing the DDR are detailed in the Guidepost Manual available to all WD employees electronically. These reports were on the files reviewed. There was however, only limited other information on the files indicating the sources of the information used in compiling the DDR and in drawing conclusions.

WD's policies, procedures and processes are incomplete and not being fully and uniformly applied. WD was not able to provide a complete and current manual. In a number of instances, identifying existing policies and procedures was difficult or not possible. Furthermore, the policies, procedures and processes that were found were not in a standard format. An example of this is one policy was produced in the form of a "News Release". This News Release, dated February 28, 1995, is used to support the policy of denying grants and contribution funding for businesses. The News Release actually states that WD will no longer provide direct loans to businesses. Interviews with staff revealed that a number of policies, procedures and processes

were not documented. The Department acknowledges this situation and has accepted the BMCI recommendation to establish and implement a complete framework of policies, procedures and processes to support the transfer payments programs.

It was determined that WD had no way of assessing whether best value was being achieved in the projects funded through the contribution programs. This was principally because the contribution agreements did not require the recipients to demonstrate that best value was being achieved through the expenditures of taxpayer funds. It was determined that starting in 1995, agreements approved under the Western Canada Business Service Network suggested that recipients used the Treasury Board Travel Directive as a guide (not a requirement) to determining reasonable costs for reimbursement of travel expenses. It was determined that, starting in 2005, WD has a clause in all new contribution agreements requiring recipients to adhere to the Treasury Board of Canada Travel Directive for any travel expenditures under the agreement. This improvement is a step towards ensuring the attainment of value for money.

### **Management Response**

WD management accepts many of the observations and recommendations contained in this audit report. However, WD management is concerned that other observations and recommendations are not well founded. The basis of this concern is that the audit was conducted using a standard that applies to contracts for goods and services rather than to contributions. Unlike contracts, grants and contributions are used by departments to support recipients to carry out activities that help achieve both their objectives and the government's policy goals and objectives. Recipients of contributions must meet performance conditions specified in a contribution agreement to receive funding. Over the life of the agreement, recipients must show they are meeting these conditions in order to be reimbursed for specific costs. The government does not benefit directly when it awards a grant or contribution as it does when it pays directly for goods or services obtained through a procurement contract. This misapplication of the policy intended for procurement contracts to that of contributions has resulted in observations and recommendations regarding transparency and best value that are not necessarily appropriate for the sound management of grant and contribution programs.

It is managements position that:

1. There is no requirement to use a competitive process for transfer payments. An ongoing intake approach to contribution funding is open and transparent, is permissible within the Treasury Board Policy on Transfer Payments and is acceptable to the Office of the Auditor General.
2. The department does not administer any contribution programs or sub-programs where participation is limited to one organization.
3. The department's Due Diligence Report and supporting file documentation is adequate to support funding decisions. BMCI was unable to provide specific instances of files where documentation was not sufficient to support the selection of the project for funding.
4. In April 2006 the department provided comprehensive training to staff on WD's policies, procedures and processes for managing its contribution programs.
5. Other internal audit reviews and audits carried out by independent audit firms of WD's expenditure processes, including a January 2006 audit, found WD to have a diligent process in place for processing claims as required by the Policy on Transfer Payments.

## **1.0 INTRODUCTION**

### **1.1 Background**

Western Economic Diversification Canada (WD) was created in 1987 with a mandate to promote the development and diversification of the economy of Western Canada and to advance the interests of the West in national economic policy. Economic growth in Western Canada is uneven. Economic differences and opportunities exist among sectors, and geographically. Each province has unique challenges to address and opportunities to pursue. Differences exist among communities as well.

Due to its makeup and size, WD is in essence a strategic, pragmatic, responsive and flexible Department that is able to look for and create opportunities that a larger entity could not achieve. The Department is often asked to deliver national programs to western Canadians on behalf of other Federal departments. WD is a catalyst for collaboration and leveraging financing together with other governments, small start-up firms, universities, research institutes and large established enterprises.

In August 2004, the Audit and Evaluation Branch of WD requested BMCI Consulting Inc. (BMCI) to conduct an audit of Transfer Payments (Grants, Contributions and Other Transfer Payments). The audit commenced with a Preliminary Survey on August 23, 2004 that included initial interviews and document reviews to identify focus areas for the audit. These interviews included individuals in the Audit and Evaluation Branch, Headquarters, and in all Regions. Audit and Evaluation specifically excluded the Softwood Industry Community Economic Adjustment Initiative, as it was to be the subject of a separate project. Detailed fieldwork was carried out early in 2005.

### **1.2 Objectives**

The objective of this audit was to conduct an assessment of transfer payments (grants, contributions and other transfer payments) to assess policies, practices and internal management

controls applied.

This was an audit of the management control framework and any files reviewed were for the purposes of assessing areas where improvements might be required to the policies, practices and internal management controls.

### **1.3 Scope**

The audit assessed compliance with Treasury Board policies and guidelines and WD policies. The Softwood Industry Community Economic Adjustment Initiative Program was specifically excluded by Audit and Evaluation. This program was to be the subject of a separate Audit and Evaluation project. In particular, the report covers the following areas:

- Demonstration of due diligence;
- Providing sound administration;
- Providing strong follow-up; and
- Performance measurement and reporting.

## **2.0 APPROACH AND METHODOLOGY**

BMCI followed the methodology prescribed by the Treasury Board and the IIA Standards for the Government of Canada. Consequently, the audit was conducted using the following phased approach:

<p><b>Phase I: Planning and Survey</b></p> <ul style="list-style-type: none"><li>- Preliminary Research and Planning</li><li>- Preliminary Survey</li><li>- Detailed Work Program</li></ul>
<p><b>Phase II: Verification (Conduct)</b></p> <ul style="list-style-type: none"><li>- Detailed Analysis</li><li>- Compilation and Testing</li></ul>



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| <ul style="list-style-type: none"><li>- Working Paper File Documentation</li><li>- Register of Findings</li><li>- Debriefing Sessions</li></ul>                                      |
| <p><b>Phase III: Reporting</b></p> <ul style="list-style-type: none"><li>- Debriefing Sessions</li><li>- Draft Report</li><li>- Management Response</li><li>- Final Report</li></ul> |

**Phase III: Reporting**

- Debriefing Sessions
- Draft Report
- Management Response
- Final Report

*Phase I: Planning and Survey*

The universe for this audit was fiscal years 2002-03, 2003-04 and 2004-05 to September 2004 (approximately 30 months). It is important to note that the data BMCI received from WD to use for sampling purposes included expenditures of only approximately \$158 million incurred during the 30-month period. If actual expenditures were used for 2002-03 and 2003-04, and an estimate made for the six months ended September 2004, the amount for expenditures would be approximately \$560 million. This means that the data provided to BMCI represents only slightly more than 25% of actual expenditures for the period. In December 2004 and a number of times over the ensuing months BMCI questioned whether or not the listing of files was complete and requested Audit and Evaluation to investigate. When BMCI had the opportunity to raise this issue directly with Corporate Finance and Programs the missing data was promptly provided. BMCI is of the opinion that the data initially not provided does not materially impact the audit of procedures and processes but notes that all comments are related to the sample of \$158 million in expenditures.

- The scope of the universe was identified in terms of the numbers of transfer payments, by dollar value, by program and by region.
- BMCI conducted a preliminary review of the management of transfer payments (grants, contributions and other transfer payments) at WD, including a review of Treasury Board Secretariat and Departmental policies and requirements related to transfer payments. This served to develop an understanding regarding the use of transfer payments. BMCI reviewed documented processes at Headquarters and in the British Columbia Region.

- BMCI undertook a preliminary investigation to identify the management control framework for transfer payments as well as to identify potential other focus areas for the audit. Interviews were conducted with individuals in the Audit and Evaluation Branch, program and policy areas at Headquarters, and program and policy areas in the British Columbia Region. Individuals interviewed represented all levels from the working level to Assistant Deputy Ministers.
- BMCI identified lists of those organizations that applied for a transfer payment in the time period indicated in the Scope section of this report. It is important to note that the lists were based on the original data representing \$158 million in expenditures. This list was used to select some stakeholders who received a transfer payment and some who did not.

#### *Phase II: Conduct and Analysis Phase*

- This phase of the audit was completed in June 2005.
- BMCI designed tests based on the results of the Preliminary Survey phase. These included detailed file reviews, interviews, etc. and covered all regions. A judgemental sample of 80 projects (20 from each region) was selected representing a variety of WD programs. This sample was designed to enable overall conclusions on how the Department managed its grants, contributions and transfer payments programs. The sample was not intended to enable BMCI to draw conclusions on a specific WD program.
- Interview guides were tested in the British Columbia Region and adjusted as necessary before continuing with the audit.
- BMCI also interviewed a number of stakeholders.
- BMCI conducted file reviews and interviews to verify the functioning of the management control framework.

### **3.0 TREASURY BOARD POLICY ON TRANSFER PAYMENTS**

In order to facilitate understanding and interpretation of the findings of this report, the key requirements of the Treasury Board Policy on Transfer Payments are stated below.

“Transfer payments are transfers of money, goods, services or assets made from an appropriation to individuals, organizations or other levels of government, without the federal government directly receiving goods or services in return. Payments that are made in exchange for goods or services are contracts and are subject to the Government Contract Regulations, Trade Agreements and the Contracting Policy.”<sup>1</sup> This section of the Policy makes it clear that while the objectives of the government are expected to be furthered through transfer payments, the government itself cannot receive a direct benefit in return. There are no reports to the government of a consulting nature nor does the government receive another service or good. This does not mean that the recipient of a transfer payment does not receive a direct benefit. The key difference between a transfer payment and a contract is who receives the good or service. The government indeed, expects recipients of transfer payments to directly benefit in some way.

The three types of transfer payments are grants, contributions and other transfer payments. During the period covered by the audit almost all of WD activity was the issuing of contributions. WD had one grant (\$27 million to the Friends of the Canadian Museum for Human Rights – see Appendix A) and no other transfer payments. The definitions for each type of transfer payment are listed below.

“**Contribution** (*contribution*) - is a conditional transfer payment to an individual or organization for a specified purpose pursuant to a contribution agreement that is subject to being accounted for and audited. Contributions would also include Alternate Funding Arrangements and Flexible Transfer Payments, which represent types of contributions that were developed for the Department of Indian and Northern Affairs to meet their unique program objectives.

**Grant** (*subvention*) - is a transfer payment made to an individual or organization, which is not subject to being accounted for or audited but for which eligibility and entitlement may be verified or for which the recipient may need to meet pre-conditions.

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<sup>1</sup> Policy on Transfer Payments, Treasury Board of Canada Secretariat, June 1, 2000, Section 2 Preface

**Other transfer payments** (*autres transferts*) — are transfer payments based on legislation or an arrangement which normally includes a formula or schedule as one element used to determine the expenditure amount; however, once payments are made, the recipient may redistribute the funds among the several approved categories of expenditure in the arrangement. Examples of other transfer payments are transfers to other levels of government such as Equalization Payments as well as Canada Health and Social Transfer Payments.”<sup>2</sup>

The Policy further clarifies that “All transfer payments are subject to public scrutiny and must be managed in a manner that is open and transparent to the public, and with due regard to economy, efficiency and effectiveness. Basic principles of parliamentary control, authority and accountability establish the boundaries within which decisions are made on the use and management of transfer payments.”<sup>3</sup>

“It is government policy:

- to make transfer payments to further approved federal government policy and program objectives;
- to manage transfer payments in a manner sensitive to risks, complexity, accountability for results and economical use of resources; and
- to require repayment of contributions made to a business which is intended to allow it to generate profits or increase the value of the business, unless otherwise approved by Treasury Board.”<sup>4</sup>

#### **4.0 FINDINGS and RECOMMENDATIONS**

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<sup>2</sup> Policy on Transfer Payments, Treasury Board of Canada Secretariat, June 1, 2000, Appendix A

<sup>3</sup> Policy on Transfer Payments, Treasury Board of Canada Secretariat, June 1, 2000, Section 2, Preface

<sup>4</sup> Policy on Transfer Payments, Treasury Board of Canada Secretariat, June 1, 2000, Section 5, Policy Statement

WD is organized with a Headquarters office in Edmonton, a Liaison Office in Ottawa, and four Regional offices located in Vancouver, British Columbia, Edmonton, Alberta, Saskatoon, Saskatchewan, and Winnipeg, Manitoba. The Regional offices and the Ottawa Liaison Office are managed by Assistant Deputy Ministers. BMCI found that each of these Offices operate independently in many ways. Accordingly, audit findings may not necessarily apply to all offices to the same degree.

The following table contains information extracted from the Departmental Performance Reports for the appropriate years. The percentage of total expenditures that are attributed to Operating Costs has decreased each year, declining from 17.9% in 2001-2002 to 16.7% in 2002-03 and then 13.0% in 2003-04. Coupled with the costs of Contributions to Employee Benefit Plans, the overall cost of operating the Grants and Contributions Programs of WD is significant.

#### Actual Expenditures 2001-02, 2002-03 and 2003-04 (millions)

Category	2001-02	2002-03	2003-04
Operating	\$45.1	\$41.1	\$41.0
Grants and Contributions	\$178.0	\$179.3	\$253.3
Obligations under the Small Business Loans Act	\$17.3	\$10.1	\$6.3
Obligations under the Canada Small Business Financing Act	\$6.4	\$9.1	\$10.6
Contributions to Employee Benefit Plans	\$4.7	\$4.2	\$4.5
Refunds of amounts credited to revenues in previous years	\$0	\$3.0	\$0
<b>Totals</b>	<b>\$251.5</b>	<b>\$246.8</b>	<b>\$315.7</b>

#### Management Response

*BMCI's calculated ratios fail to take into account that the Department's mandate includes representing western Canadian interests in national decision making and coordinating federal economic development in the west. These activities require the use of significant operating resources but little if any G&C resources. Consequently the cost of managing the G&C programs is significantly overstated by BMCI.*

#### 4.1 Transparency

***i) WD does not have a mechanism in place to demonstrate the degree to which it is open and transparent in selecting recipients for its contribution programs.***

According to the Treasury Board Policy on Transfer Payments, the type of transfer payment that a department uses to meet its program objectives is determined by the departmental mandate, business lines, clients and an assessment of risk. The Policy further states that all transfer payments are subject to public scrutiny and must be managed in a manner that is open and transparent to the public and with due regard to economy, efficiency and effectiveness. In addition to the Policy, basic principles of Parliamentary control, authority and accountability establish the boundaries within which decisions are made on the use and management of transfer payments.

BMCI found that the Treasury Board Policy on Transfer Payments does not define openness and transparency. WD has not defined openness and transparency. Furthermore, BMCI could not find definitions for these terms elsewhere within Government of Canada sources. In numerous audits over the years, the Office of the Auditor General of Canada has stated that the best way of achieving openness and transparency is through the use of the competitive process.

***Management Response***

*The Office of the Auditor General of Canada (OAG) reference cited by BMCI refers to transparency in contracting for goods and services and is not applicable to Grants and Contribution spending. Further, the OAG in a joint paper issued with Industry Canada February 2001 on the specific topic of G&C programs noted that either a request for proposals (batch) approach or ongoing intake approach is acceptable depending on the circumstances: “in some cases “batching” may be more appropriate”, but in other cases “timeliness of response can be a concern.” The Office of the Auditor General has not raised the use of a competitive process as a standard expected by the OAG in any of their audits of WD’s management of C&C programs. In our view WD is in full compliance with Sections 2.3 and 5.0 of the Policy on Transfer Payments.*

*By way of information, a separate audit conducted by BMCI of WD's contracting standards for the purchase of goods and services (report dated January 2004) found that the department required a competitive process that is more stringent than the Treasury Board contracting policy.*

BMCI is of the opinion that the Transfer Payment Policy implies that a key ingredient of a successful program is attainment of the expected level of participation from the target population. Ensuring available funds are allocated to the projects demonstrating best value would best be attained by encouraging as many applicants as possible from those eligible to do so. This can only be achieved by effective communication and promotional material for the target population. The material must clearly describe the purpose of the program, the types of projects that are eligible and the eligibility criteria for applicants. The evaluation, criteria for project proposals, also needs to be clearly communicated. Other information made available should contain details about the approval process, including any appeal process, the requirement for an agreement, the monitoring requirements, and how to apply.

BMCI was informed that many projects are initiated by invitation from WD to the potential applicant. The Department does not have a system for documenting and summarizing how proposals are initiated. Furthermore, documentation was not available to identify the objective criteria used to determine why a particular project was regarded as being best value and therefore selected to receive funding. In the case of the Western Diversification Program (WDP) for example, a Due Diligence Report (DDR) is completed for all projects prior to approval detailing the Project Description, Project Costs, Eligibility, Viability, Funding, Benefits, Resources and Incrementality and any Special Considerations. The steps for completing the DDR are detailed in the Guidepost Manual available to all WD employees electronically. These reports were on the files reviewed. There was however, only limited other information on the files indicating the sources of the information used in compiling the DDR and in drawing conclusions.

The Department has not identified the conditions under which it would be appropriate for

specific programs or sub-programs to be exempt from the requirement to have participation from more than one organization or even go through a competitive, or request for proposals', process. A competitive process is rarely used to invite project proposals from a number of potential applicants to be assessed against all proposals received. There is evidence that WD does consider using an RFP process for programs or subprograms. For example, for the latest WEPA agreement in Alberta, it was determined that a request for proposals' process would be more transparent and would result in the highest quality projects being funded. The other exception noted was the Softwood Industry Community Economic Adjustment Initiative.

### ***Management Response***

*WD does not implicitly or explicitly limit its contribution programs or subprograms to one organization. Consistent with 2.3 and 5.0 of the Policy on Transfer Payments, when developing programs WD considers the best way to ensure effective, efficient and economical program delivery. In accordance with section 5.0 of the Policy on Transfer Payments, projects are selected based on their potential to contribute to the department's strategic objectives and specific regional business plan objectives.*

*The ongoing intake approach to program delivery used by WD is permissible within the Treasury Board's policy on Transfer Payments and is commonly used by many federal and provincial government departments to deliver G&C programs. Ongoing intake is defined as a process whereby clients submit applications for funding at their convenience and that are assessed on a case-by-case basis. The ongoing intake approach has a number of advantages including better client service and responsiveness by avoiding the artificial deadlines inherent in a Request for Proposal (RFP) type process. An ongoing intake approach is virtually essential in the cooperative (rather than competitive), partnership oriented approach WD and other departments use to work with communities, provincial governments and industry associations. As previously noted this approach is supported by the Office of the Auditor General of Canada.*

*Finally, during the period under review WD delivered eight major programs using either a competitive process or in a manner that ensured equitable access to funds for eligible recipients.*



*This is better explained by looking at each program as follows:*

- 1. Infrastructure Canada Program (ICP): Delivered in Western Canada by WD as part of a federal/provincial/municipal commitment to enhance municipal infrastructure in all communities across Canada. The West's share of federal program funding was determined by Infrastructure Canada using a formula based on provincial population and unemployment. Each western province formed management committees made up of federal, provincial and municipal representatives who ensured funding was distributed equitably to communities in each province.*
- 2. Women's Enterprise Initiative (WEI): Created by WD after extensive research and consultation with women entrepreneurs across western Canada resulting in funds committed equally to each western province to ensure all women entrepreneurs have access to business services and capital to successfully start or grow their business. Each provincial organization is required to set and report against annual targets for the level of participation from the target population.*
- 3. Community Futures Program (CFP): Delivered in western Canada by WD since 1995 to all rural communities in western Canada. After consultation with CFDCs funds are allocated to each of the 90 organizations with adjustments for northern/remote locations. This ensures that each community has access to funds for community economic development projects and that all rural entrepreneurs have access to services and capital to successfully start or grow their businesses. Each CFDC is required to set and report against annual targets for the level of participation from the target population.*
- 4. Loan Investment Fund Program (LIFP): Created by WD after research and consultation into gaps faced by western Canadian small and medium sized enterprises (SMEs) in obtaining access to capital. As gaps are identified contributions are made to existing capital providers such as Credit Unions and chartered banks to leverage their funds and ensure they are available on an application basis to all targeted high-risk clientele who would otherwise*

*have trouble accessing capital.*

- 5. Western Diversification Program (WDP): Created with the inception of the department to deliver on the mandate to develop and diversify the western Canadian economy. The program involves a number of subprograms and major initiatives created as a result of research and consultation with relevant community, stakeholders and/or provincial/municipal governments. Projects are selected based on an ongoing intake process or in accordance with a specific sub-agreement. For example, during the three fiscal years covered by the audit approximately \$50M of WD's G&C Western Economic Partnership Agreement (WEPA) approvals were done jointly by WD and provincial government officials pursuant to the priorities established for the federal/provincial WEPAs.*
- 6. Innovation and Community Investment Program (ICIP): This program was created by WD to support innovation and create new economic opportunities in western Canadian communities. The funding was allocated evenly between the four western provinces and to projects based on an ongoing intake process.*
- 7. Service Delivery Network Program (SDNP): Created by WD after research and consultation into gaps in financing and services facing western Canadian SMEs. Contributions are provided to community-based organizations throughout western Canada as gaps are identified. These organizations in turn make services and/or capital available to all targeted clients.*
- 8. Softwood Industry Economic Community Adjustment Program (SIECAI): Delivered in Western Canada by WD as part of a federal response to communities seriously impacted by reduction in softwood lumber activity due to the US import duties. The West's share of program funding was based on job losses. Individual communities were determined to be eligible based on Statistics Canada data that reflected the impact of the softwood lumber crises. Within impacted communities the program was delivered to eligible recipients using a fully competitive process.*

*A specific example of a successful sub-program delivered using a collaborative ongoing intake delivery model is the award winning Vancouver Agreement (funded under the WDP), where governance and decision-making is by a joint federal-provincial-municipal management committee with critical input from diverse community groups in Vancouver's troubled Downtown East Side. In fact, in its November 2005 Report, the Office of the Auditor General stated that the Vancouver Agreement had a promising governance model with provincial, municipal, and federal governments working together to meet the needs of the community.*

*WD disagrees with the observation that there is only limited information in files supporting the information in the DDRs. A review by management of some of the files reviewed by BMCI suggests that this observation is not supported by evidence on the files. Application information was on all of the files reviewed by management along with other documentation to support the application such as audited financial statements, project budgets and cash flow projections, letters of support, Gantt Charts and detailed project proposals. WD will engage in independent auditor to review this further.*

*Further to the issue of transparency the department notes that in 2005 WD proactively began posting all transfer payments to recipients on its web site to further improve transparency of contribution management.*

BMCI found that WD's transfer payment programs had clearly stated objectives and eligibility criteria, which are outlined in the terms and conditions, thus enabling program staff to be confident as to whether or not a particular project proposal could be funded by the program. It is important to note, however, the objectives of the Western Diversification Program (WDP) and the eligibility criteria outlined in the terms and conditions are stated in a broad manner.

For example the following is a list of organizations that are eligible to receive contributions under the WDP:

- non-profit organizations
- post secondary institutions
- hospitals and regional health care centres, for purposes of undertaking research and development of new technologies
- co-operatives
- small and medium sized commercial, legally incorporated for profit enterprises
- indian bands, as represented by their chief and council
- federal Crown corporation
- Provincial Government Departments, Agencies and Crown Corporations such as provincially owned telecommunication companies
- Municipal Governments and organizations created by them

The following are examples of eligible activities for grants and contributions under the WDP:

- enhanced technology commercialization and adoption
- linkages among innovation system players (such as communities, firms, research facilities, and/or educational institutions, etc.)
- applied research and development leading to commercialization
- community innovation (planning studies, which look at a community's capacity, and are based on a knowledge infrastructure or technology focus, such as cluster studies or competitive studies, and initiatives which build capacity in a community, based on a knowledge generator such as a university or key industry, or create receptor capacity)
- improving business productivity (i.e. new machinery, training, business information)
- developing markets (supplier, domestic, international)
- addressing systemic business issues
- industry collaboration
- increasing participation in international markets
- attracting investment to western Canada
- supporting the viability of the local economy and increasing the participation of

community members

- supporting community adjustment to economic realities (for example, mine closures)
- promoting community planning and strategies
- supporting the creation of physical assets (for example, buildings and equipment)
- conducting economic and business research
- supporting investment in skills, knowledge and competencies development in support of the department's strategic objectives
- supporting recipients to convene conference and offer co-ordination and collaboration
- otherwise increasing the development and diversification of the Western Canadian economy

In all instances proposed projects are to be assessed on the degree to which they contribute to current WD program objectives and strategic directions. These objectives and strategic directions are described in WD literature, on the WD web site and in such important government accountability documents as the Departmental Performance Reports and the Departmental Reports on Plans and Priorities.

BMCI expected the WD web site would be easy to use and that members of the target audience for WD programs could easily identify the eligibility criteria for the various programs and sub-programs. This would have been consistent with the Preface to the TB Policy on Transfer Payments states that “All transfer payments are subject to public scrutiny and must be managed in a manner that is open and transparent to the public, and with due regard to economy, efficiency and effectiveness.” Furthermore, based on the foregoing statement, BMCI also expected that WD would be taking steps to increase the likelihood that the best possible projects were in fact selected for funding, possibly by identification of projects through a competitive process somewhat similar to the request for proposals process used when contracting for goods or services.

BMCI reviewed the WD web site and concluded that:

- the information on all programs was available for the target population for WD

programs;

- the site could be made easier to use i.e. potential project applicant could have difficulty determining whether or not their organization is eligible under a WD program, which program or sub-program might be most appropriate and what criteria is used to assess potential projects for each WD program or sub-program.
- it is not clear what a potential project applicant is expected to provide in a proposal for funding. It is possible that some potential project applicants do not seek funding because the web site is unclear about what proposals might be eligible for funding. This is largely because the WD web site emphasizes current departmental strategic thrusts more than the specific programs under which projects would be funded. The web site outlining the type of data that is required to substantiate project proposals is lacking as to format and content and WD staff must be contacted to determine proposal requirements. Information found on WD's web site is not user friendly nor specifically identifies the information required to submit proposals. Service to potential project applicants could be improved and workload reduced at WD by making improvements to the web site. For example, the web site could include guidelines and templates for the submission of proposals, application forms, the terms and conditions for the various programs as well as the current priorities being pursued by WD and/or the Regions.

### ***Management Response***

*As the BMCI audit points out, the objectives and eligibility criteria under the WDP closely parallel WD's strategic objectives pertaining to Sustainable Communities, Entrepreneurship and Innovation. We agree with BMCI that these objectives are consistently described in WD literature, the WD web site and documents such as the Report on Plans and Priorities and Departmental Performance Report. WD and specifically WDP criteria are therefore transparent and consistent. Furthermore, the DDR and Guideposts manual discussed above ensures projects are assessed against their fit with these strategic objectives and their potential to deliver benefits or results.*

The majority of funding is allocated to a modest number of organizations. BMCI's analysis of

the transfer payments approved during the period under audit revealed that there were 100 projects funded at more than \$200,000. These 100 projects represent 4.5% of the 2,228 projects approved; they were sponsored by 67 different organizations and received 74.6% of the funding. Details of this analysis can be found in Appendices B and C. BMCI is not drawing any conclusions as to whether this is desirable. The information is simply provided to add context for the reader.

**It is recommended that the:**

**Deputy Minister initiates steps to identify how the Department knows that it is achieving an expected level of participation among qualified applicants.**

**Deputy Minister have criteria developed to judge which contribution programs may benefit from increasing the level of participation among qualified applicants and which programs are best served through an ongoing intake process. The rationale for decisions made using the criteria should be documented.**

**Director General, Corporate Finance and Programs set yearly performance goals for the funding of projects, which would require a defined level of participation among qualified applicants.**

**Director General, Corporate Finance and Programs take steps to ensure that the web site clearly indicates, for each program: guidelines and templates for the submission of proposals, eligibility criteria, terms and conditions for the programs, and the current criteria against which applications will be assessed.**

### ***Management Response***

*The department accepts these recommendations for programs or sub-programs where this is not the case now. Note that by design many WD programs are systemic in nature and provide*

*support to recipients who in turn are responsible for seeking a high level of participation from a wide range of qualified applicants who make up the targeted population. For example, during the period under review, WD provided \$54.8M under the Community Futures Program to 90 community based non-profit organizations covering all of rural western Canada that provide business advisory and capital support to all entrepreneurs in their communities.*

*WD has taken steps to ensure that the department's web site clearly indicates terms and conditions for programs and the current criteria against which projects will be assessed.*

***ii) WD and the potential recipients may not fully understand the level of risk assumed if projects are not approved.***

BMCi noted a number of instances where the start date (the date set out in the Statement of Work as the earliest date on which the recipient can begin incurring eligible costs) of a project under a contribution agreement preceded the date of approval. WD procedures are to have the start date correspond closely to the date that initial contact was made (normally in writing). In BMCi's opinion, having a project start date that is earlier than the date of approval of any transfer payment agreement could potentially be an area of concern. One such concern could be that the WD officer (or the Minister), with the appropriate approval authority, may feel that an effective verbal contract is already in place and as such may feel undue pressure to approve the project. Furthermore, since funds are not committed until the date of approval, there is no assurance that money will be available.

If a contribution agreement is approved with a project start date that has already past, the approving authority is essentially authorizing retroactive expenses for the project. If, for operational reasons, expenses need to be incurred by the potential transfer payment recipient prior to approval of the agreement, the potential recipient must request that such expenses be included as eligible expenses. If the project is not approved, this practice may cause an unexpected financial burden on the organization. BMCi is concerned that potential recipients



requesting the inclusion of retroactive expenses are not informed in writing of the risk they are assuming. Potential recipients must clearly understand that WD may not approve the inclusion of retroactive expenses. It is also possible that WD may not approve the project at all. Additionally, without a formal contract in place, there could be a misunderstanding as to what expenses are considered appropriate.

**It is recommended that the:**

**Director General, Corporate Finance and Programs take the necessary steps to ensure that where the start date is earlier than the approval date the reasons are documented in the DDR as well as the nature and amount of any retroactive expenses.**

**Director General, Corporate Finance and Programs establish a policy requiring that where the start date precedes the approval date, the recipient be advised in writing about the risk that they are assuming.**

### ***Management Response***

*The Department accepts these recommendations. WD will consult with the Department of Justice to determine the appropriate way to advise clients of the risk they are assuming.*

## **4.2 Economy**

***i) BMCI found that WD's policies, procedures and processes incomplete and are not being fully and uniformly applied.***

BMCI expected to find a complete framework of policies, procedures and processes for the management of the transfer payment programs. However, WD was not able to provide a complete and current manual. In a number of instances, identifying existing policies and procedures was difficult or not possible. Furthermore, the policies, procedures and processes

that were found were not in a standard format. An example of this is one policy that could only be produced in the form of a “News Release”. This News Release, dated February 28, 1995, is used to support the policy of denying grants and contribution funding for businesses. The News Release actually states that WD will no longer provide direct loans to businesses. Interviews with staff also revealed that a number of policies, procedures and processes were not documented.

Without complete and uniform policies:

- decisions made are not always supportable by written policies, procedures and processes.
- WD’s credibility could be compromised; some staff advised BMCI that they cannot easily document the justification for turning down requests for contributions. Furthermore, interviews with staff showed that there was not a common understanding of the current policies, procedures and processes.
- WD management lacks the tools to hold staff accountable for decisions made and for measuring the openness and transparency of the process of managing the transfer payments programs.

**It is recommended that the:**

**Director General, Corporate Finance and Programs establish and implement a complete framework of policies, procedures and processes to support the Transfer Payments Programs.**

### ***Management Response***

*The Department accepts this recommendation.*

In a review of how various delegated authorities under the Financial Administration Act are exercised, BMCI found that they have been exercised appropriately. BMCI also noted that the Quality Assurance Review Forms and the Risk Based Audit Framework (RBAFs) for the

respective programs do detail the procedures to be followed. The Financial Administration Act Section 34 states that “(1) No payment shall be made in respect of any part of the public service of Canada unless, in addition to any other voucher or certificate that is required, the deputy of the appropriate Minister, or another person authorized by that Minister, certifies a) in the case of a payment for the performance of work, the supply of goods or the rendering of services, (i) that the work has been performed, the goods supplied or the service rendered, as the case may be, and that the price charged is according to the contract, or if not specified by the contract, is reasonable, ...b) in the case of any other payment, that the payee is eligible for or entitled to the payment.”

The appropriate steps may have been taken, however there was little documentation on the files reviewed indicating the process and procedures followed and to support the decision for the final signature under Section 34 confirming compliance with the terms and conditions of the specific contribution agreement.

The focus of the Monitoring and Payments Function is on obtaining data to support the claim with little documentation on the files indicating the process and procedures followed and to support the decision for the final signature under Section 34 confirming compliance with the terms and conditions of the specific contribution agreement. In one case, the assessment officer when questioned indicated that the deliverable – a structure – had been met since he drove by the site daily on his way to work. He like most other assessment officers did not consider this part of their job description. In fact, assessment officers, in most cases, considered their job complete once the approval had been obtained. From there on it was considered to be the responsibility of payment and monitoring people to ensure all requests for funds were appropriately supported. Furthermore, the files did not reflect what action had been taken where necessary over and above the receipts for various expenditures to indicate that the deliverable had been met.

### ***Management Response***

*WD does not agree with this observation. Again, it appears that the observation is based on the*

*policy for contracts rather than the policy for contributions. In accordance with the Policy on Transfer Payments, payments are to be based on the reimbursement of eligible expenses incurred and paid by the recipient. Certification under Section 34 of the Financial Administration Act for Grants and Contributions requires that the delegated signing authority certify that the payee is eligible for or entitled to the payment. This means that in addition to the requirement to incur and pay eligible expenses, recipients must also be in compliance with the contribution agreement terms and conditions. This is unlike operating contracts, which, under Section 34 of the Financial Administration Act require certification that work has been performed, or goods supplied or services rendered, as these contracts are to benefit the government directly.*

*Program terms and conditions vary greatly and as a result so do the nature of the projects being carried out which in turn impacts the types of expenditures incurred by project funding recipients. Accordingly, documentation in support of payments and compliance to terms and conditions varies. Processes and procedures to be followed for each program are documented in the Risk Based Audit Framework (RBAF) approved for each program by Treasury Board. WD's regional ADMs are responsible for ensuring that payment files contain adequate documentation to support certification under Section 34 of the Financial Administration Act as required by the program RBAFs. The relative role of assessment versus monitoring and payments officers is not relevant to Section 34 certification and it is unclear why BMCi has included this reference in the audit report.*

*The most recent audit by the Office of the Auditor General that included a review of WD's financial management was the 2001 audit of the Community Futures Program. In the 2001 Report of the Office of the Auditor General, Chapter 5 Voted Grants and Contributions – Program Management, Financial management and Control, the Auditor General found that WD exercised adequate control over G&C disbursements to CFDCs for operating costs. During the period audited by BMCi contribution expenditures for CFDC operating costs was 54.8M.*

**It is recommended that the:**

**Director General, Corporate Finance and Programs ensure that there is appropriate documentation for all authorizations under the Financial Administration Act.**

***Management Response***

*The department accepts the recommendation and will ensure that files are adequately documented to demonstrate that contribution funding recipients are eligible for or entitled to the payment.*

An Audit and Evaluation report on "Risk-Based Review of the Projects Monitoring and Payment Function" was dated November 28th, 2003. The report included a number of audit observations that BMCI found had not yet been addressed. BMCI could not find an action plan to address the recommendations of this Review. The more significant of these are:

- "... the differences among the regional M&P functions do not reflect significant differences in their operating environments - there is no compelling reason to have such differences among regions."
- "... responsibility for measuring and tracking project outcomes has not been formally assigned within WD."
- "... M&P has not maintained and updated policies and procedures governing the M&P function."

**It is recommended that the:**

**Director, Audit and Evaluation ensure that the Deputy Minister has appropriate information to meet the Treasury Board Policy on Internal Audit which requires that a management action plan adequately addressing the recommendations has been prepared and that there is the required reporting on the status of the recommendations.**

**Director General, Corporate Finance and Programs ensure that measuring and tracking**

**project outcomes is assigned to the Monitoring and Payments Function and carried out.**

**Director General, Corporate Finance and Programs ensure that the policies, procedures and processes for the Monitoring and Payments Function are updated where appropriate and then maintained.**

### ***Management Response***

*The department accepts the recommendations and notes that following the completion of the report on “Risk-Based Review of the Projects Monitoring and Payment Function” a management action plan was developed to address the recommendations. The status of the recommendations is updated regularly with the most recent update occurring December 2005. This status report has been provided for inclusion in the appendices. Work as outlined in the Action Plan for the Monitoring and Payments Function and Quality Assurance Review Process developed in July 2004 is near completion.*

*Furthermore, WD remains committed to measuring project outcomes at all levels of the organization. For G&C projects specifically, the Due Diligence Record (DDR) documents expected project outcomes and measures. Where payment is dependent upon meeting performance objectives compliance is monitored by the Monitoring and Payments group and is verified in support of the Section 34 Authority. Where project outcomes occur some time after project funding has been completed responsibility for monitoring is assigned to the regional Directors General and will be carried out by the Monitoring and Payments officers and the Assessment officers. Performance measurement also occurs as part of the program and sub-program evaluation work that is undertaken by WD’s internal Audit and Evaluation group.*

***ii) Contribution agreements do not include clauses requiring the recipient to ensure that value for money is achieved.***

Throughout the period covered by the audit (April 2002 to September 2004) BMCI found that

WD had no way of assessing whether best value was being achieved in the projects funded through the contribution programs. This was principally because the contribution agreements did not require the recipients to demonstrate that best value was being achieved through the expenditures of taxpayer funds. Contribution agreements generally do not require that the recipients demonstrate that best value has been achieved. In most cases, file documentation and contribution agreements do not demonstrate and/or require that the recipients demonstrate that best value has been achieved. BMCi was informed that starting in 1995; agreements approved under the WCBSN suggested that recipients used the Treasury Board Travel Directive as a guide (not a requirement) to determining reasonable costs for reimbursement of travel expenses. BMCi has also been informed that, starting in 2005, WD has a clause in all new contribution agreements requiring recipients to adhere to the Treasury Board of Canada Travel Directive for any travel expenditures under the agreement. This is a commendable improvement and a step towards ensuring the attainment of value for money. Nonetheless, BMCi has been informed that some organizations (e.g., City of Vancouver,) have more restrictive travel rules than those of the federal government.

**It is recommended that the:**

**Director General, Corporate Finance and Programs change the policy requiring contribution agreement recipients to adhere to the Treasury Board Travel Directive to allow for recipients to adhere to their own policy when it is more restrictive than the federal government requirements.**

***Management Response***

*The Department accepts this recommendation.*

In its review of project files, BMCi noted that contribution recipients often enter into contracts for goods and services with other organizations as part of fulfilling their obligations under the contribution agreement. WD does not require the recipients to demonstrate that they are achieving best value in these transactions. BMCi understands that the primary criterion for

selecting a project is its potential to deliver results supplemented by other factors such as leveraging, management/technical expertise, accessibility and long term sustainability. Expenditures taken toward the attainment of these criteria would be considered best value as would the obvious attainment of an item at least cost elsewhere.

**It is recommended that the:**

**Director General, Corporate Finance and Programs establish a policy requiring that all project funding be expended in a manner that clearly indicates that the best value was achieved in making the particular spending decisions and a clause to this effect be required in each new contribution agreement.**

*Management Response*

*WD's project assessment process as described in the Guidepost manual requires that projects be approved with the minimum amount of government assistance required to complete a project to ensure the best value for money. The importance of this requirement will be reinforced through training of all project officers and managers in early 2006.*

BMCI also noted that the Monitoring and Payments Function desk reviews of claimed expenditures submitted by recipients made various arbitrary adjustments that were not supported by the wording in the agreements. The same situation exists for the audits performed under contract for the Monitoring and Payments Function. Furthermore, BMCI found that the benefit of these reviews and audits under current conditions is questionable since the findings are rarely significant and there is no requirement to look at the claimed expenditures from a value for money perspective. If the desk reviews and audits were being performed from a best value point of view, there could be lessons learned to better define allowable expenditures in future agreements.

**It is recommended that the:**



**Director General, Corporate Finance and Programs establish a policy that in future the desk reviews and audits are to also include an assessment of whether or not the recipient is achieving best value in the expenditures under the agreement.**

**Director General, Corporate Finance and Programs ensure that future contribution agreements have clauses that reflect any lessons learned that result in best value being achieved.**

### ***Management Response***

*Desk reviews will confirm compliance with the terms and conditions of contribution agreements including the requirement to procure significant capital assets and/or services through a competitive process and comply with travel cost requirements.*

## **4.3 Efficiency**

***i) WD has funded some programs as contributions that may be more appropriate as grants.***

A good example of an initiative that might be more appropriately funded as a grant rather than a contribution is conference support. This is a sub-program of the Western Diversification Program. . The 538 contributions made under this program during the period audited averaged approximately \$6,000. More detail on this program can be found in Appendix E. Funding these projects as contributions requires the Monitoring and Payments Function to review all expenses of the conference to ensure that they are supportable before providing the WD support payment. If the funding were provided as a conditional grant, the only verification necessary by WD would be to confirm that the conference actually took place and, as an example, confirm that the required number of participants attended.

**It is recommended that the:**

**Director General, Corporate Finance and Programs take the necessary steps to have the conference support sub program identified as a grant subject to certain conditions such as**

**that the conference takes place and a defined number of individuals participated**

***Management Response***

*The Department will consider using grants under programs similar to the Conference Support Program.*

WD had two other sub-programs that would also be more efficiently delivered as conditional grants rather than contributions. One was the First Jobs in Science and Technology sub-program. The average contribution was \$21,039 for the 393 projects funded during the period covered by the audit. Additional details on the First Jobs in Science and Technology sub-program can be found in Appendix F. The second was the Export Readiness Program. The average contribution was \$17,148 for the 196 projects funded during the audit. Additional details on the Export Readiness sub-program can be found at Appendix G. Both of these programs were essentially tied to one deliverable. Subsequent to the audit, these programs began winding down and the final date for accepting applications was April 1, 2005 and the final date for approval of projects was May 31, 2005.

**It is recommended that the:**

**Director General, Corporate Finance and Programs ensure that in the future similar programs and sub-programs be established as grants.**

***Management Response***

*The Department will consider using grants under programs similar to the First Jobs in Science and Technology and Export Readiness Programs.*

**4.4 Effectiveness**

***i) Inaccurate and incomplete information on requests withdrawn or declined may be impacting management decision-making on projects to be considered for approval.***

BMCI expected to find that WD had a management reporting system, incorporating appropriate financial and non-financial information to provide management with timely, accurate and useful information. In the database of information provided to BMCI for review, only 85 projects were recorded as withdrawn by the applicant or rejected by WD. Many proposals are worked on by WD staff and are not entered into Departmental systems. These tend to be projects that are not carried forward for potential approval. There is no requirement for Development and Assessment Officers to record the process used in declining applicants. This situation has a number of potential impacts:

- The number of rejected proposals is understated;
- The number of withdrawn proposals is understated;
- Inconsistent application of justification for not accepting a proposal;
- No record of justification used;
- No documentation to substantiate that the rejection of the proposal was in accordance with the terms and conditions of the various programs and/or WD priorities;
- Development and Assessment Officers lack historical data to help them in making recommendation on other proposals;
- Workload measures are inaccurate and incomplete;
- Inability to establish meaningful performance and service standards;
- Openness and transparency are potentially reduced due to a lack of sufficient information supporting the decision making process for not funding proposals;
- The lack of a full history of past proposals hampers the ability of WD to identify potential development opportunities to be pursued in the future;
- The workload of WD staff is not recorded; and
- The same project, or a similar one, may be dealt with by another WD officer and that officer, not being aware that it has been reviewed and rejected, may forward it for approval this time. This could result in inconsistencies in dealing with clients.

WD officers told BMCI that due to work pressures, some milestone dates for agreements are

being entered well after the date occurred. This results in information not being accurate, complete and timely. The Department must have an information system that provides management with timely, accurate, complete and useful information of both a financial and non-financial nature on the transfer payment programs.

**It is recommended that the:**

**Director General, Corporate Finance and Programs ensure that all proposals received are documented in the appropriate WD information systems including the rationale for acceptance or rejection.**

**Director General, Corporate Finance and Programs ensure that training for Development and Assessment Officers covers all policies, procedures and processes of WD.**

**Director General, Corporate Finance and Programs ensure that there is a process for consistently evaluating proposals for funding under each WD program.**

**Director General, Corporate Finance and Programs establish and publish service standards for each WD program.**

### ***Management Response***

*The Department accepts these recommendations for the Western Diversification Program and has implemented an initial project assessment process to document and track all project proposals including reasons for project rejections or recommendations for further assessment.*

*The department's project approval process and Guidepost Manual is intended to ensure that proposals are fairly and consistently assessed. Tracking of project proposals will be strengthened to improve documentation of proposals that are not approved and training will be*

*provided to all project officers to increase consistency and quality of project due diligence in early 2006.*

*The Department will consider implementing additional service standards where appropriate and meaningful.*

## **5.0 CONCLUSIONS**

BMCI has reached the following principle conclusions:

- The Department needs to be better able to demonstrate that it manages its transfer payment programs in a manner that is open and transparent to the public and with due regard to efficiency, effectiveness and economy;
- Steps are also required to complete the Department's framework of policies, procedures and processes and then to ensure that they are fully and uniformly applied; and
- Additional initiatives are necessary to ensure that recipients of contribution funding can demonstrate that best value is being attained for money spent.



**APPENDICES**

**Appendix A – WD Grants and Contribution Expenditures for 2003-2004**

**Appendix B – Contributions over \$200,000**

**Appendix C – Transfer Payments April 2002 to September 2004**

**Appendix D – Requests Withdrawn or Declined**

**Appendix E – Conference Support**

**Appendix F – First Jobs**

**Appendix G – Export Readiness**

**Appendix H – News Release February 28, 1995**

**Appendix I – Interviews from Preliminary Survey**

**Appendix J – Project Monitoring and Payments Audit Follow-up, December 2005**