

**CROWN CORPORATION GOVERNANCE AND
ACCOUNTABILITY FRAMEWORK:
A REVIEW OF RECENTLY PROPOSED REFORMS**

**Tara Gray
Economics Division**

16 March 2006

The Parliamentary Information and Research Service of the Library of Parliament works exclusively for Parliament, conducting research and providing information for Committees and Members of the Senate and the House of Commons. This service is extended without partisan bias in such forms as Reports, Background Papers and Issue Reviews. Analysts in the Service are also available for personal consultation in their respective fields of expertise.

**CE DOCUMENT EST AUSSI
PUBLIÉ EN FRANÇAIS**

TABLE OF CONTENTS

	Page
INTRODUCTION	1
OVERVIEW	1
CURRENT GOVERNANCE AND ADMINISTRATIVE FRAMEWORK	2
RECENT REVIEWS OF THE GOVERNANCE FRAMEWORK.....	4
NEW RECOMMENDATIONS.....	9
A. Gomery Commission – Phase 2 Report.....	9
B. Accountability Act Proposals	9
REFERENCES	11



CANADA

LIBRARY OF PARLIAMENT
BIBLIOTHÈQUE DU PARLEMENT

CROWN CORPORATION GOVERNANCE AND ACCOUNTABILITY FRAMEWORK: A REVIEW OF RECENTLY PROPOSED REFORMS

INTRODUCTION

Crown corporations are distinct legal entities established by the government to pursue public policy and commercial objectives. The current legislative framework for governance and accountability of Crown corporations has been in place since 1984. Pressure to reform the existing regime has grown following the release of the Auditor General of Canada's November 2003 report, entitled *Government-Wide Audit of Sponsorship, Advertising, and Public Opinion Research*. The report scrutinized the governance and activities of six Crown corporations, and it instigated a major review of Crown corporation governance by the federal government that resulted in a report tabled in 2005.

This discussion focuses on the proposals relating to Crown corporation governance contained in the prospective Federal Accountability Act as outlined by the Conservative Party of Canada's 2006 election platform,⁽¹⁾ and the related recommendations included in the Gomery Commission's Phase 2 report, *Restoring Accountability: Recommendations*. The proposals are compared to the substantive recommendations recently put forward both by the federal government in its 2005 review and by the Auditor General in a series of reports on Crown corporation governance. The paper begins with a brief overview of the current governance and accountability framework.

OVERVIEW

Federal Crown corporations are legal entities established by the government as instruments of public policy. Unlike private-sector corporations, of which the main objective is the maximization of shareholder value, many Crown corporations operate in an environment where they pursue multiple and sometimes conflicting operational goals such as financial

(1) The present publication was prepared prior to the introduction of Bill C-2 on 11 April 2006, and will be updated in the near future.

self-sufficiency and fulfilling certain public policy objectives.⁽²⁾ They operate in diverse sectors of the Canadian economy including financial services, culture, transportation, agriculture and fisheries, energy and resources, and government services.

There are currently 43 federal Crown corporations (not including subsidiaries), employing over 73,000 people.⁽³⁾ As such, they account for a significant portion of government activity. Together, they received \$5.2 billion in parliamentary appropriations in 2003-2004.⁽⁴⁾ While not all Crown corporations receive appropriations, 25 of the 43 did so in that year.

CURRENT GOVERNANCE AND ACCOUNTABILITY FRAMEWORK

Crown corporations are created either by an individual Act of Parliament or by articles of incorporation under the *Canada Business Corporations Act*. The enabling legislation sets out the corporation's mandate, powers and objectives.

Corporate governance refers to the process and structure for overseeing the direction and management of a corporation so that it carries out its mandate and objectives effectively. The legislative framework for the governance and accountability regime of most federal Crown corporations is set out in Part X of the *Financial Administration Act* (FAA). Some Crown corporations operate at a greater distance from the government. For these, the governance and accountability regime is set out in their enabling legislation.⁽⁵⁾ Regardless of where the legislative authority is situated, the goal is to provide the corporation with sufficient autonomy in day-to-day activities and operations while at the same time allowing the government an appropriate level of direction and control. In addition to the legislative requirements, governance principles and practices for Crown corporations are contained in various other government documents such as governance policies, guidelines, and practices

-
- (2) House of Commons, Standing Committee on Public Accounts, Report 15, on Chapter 18 of the December 2000 Report of the Auditor General of Canada, "Governance of Crown Corporations," 1st Session, 37th Parliament, February 2002.
 - (3) Treasury Board Secretariat, *Annual Report to Parliament: Crown Corporations and Other Corporate Interests of Canada*, 2004.
 - (4) Auditor General of Canada, 2005 Status Report, Chapter 7, "Governance of Crown Corporations."
 - (5) Of the 43 Crown corporations, 9 are exempt from Part X of the FAA. While those corporations are subject only to their individual Acts, these Acts often reflect the governance regime provided by the FAA. The most common departure from the FAA is to exclude the Crown corporation from the obligation to submit an annual corporate plan for government approval.

issued by the Treasury Board Secretariat, the Department of Finance, and the Privy Council Office. In many cases, individual Crown corporations have also established their own internal policies and practices on governance, consistent with government guidelines.

The majority of Crown corporations are subject to the FAA. For these, Part X of the Act places the board of directors at the centre of the governance regime. The board of directors oversees the management of each Crown corporation and holds management responsible for the company's performance. In turn, the board of directors is accountable to Parliament through its responsible minister.⁽⁶⁾ As set out in the FAA, the principle of ministerial accountability has not been interpreted to mean that ministers are accountable for the day-to-day management and operations of Crown corporations in their portfolio. Rather, the government has found ministers accountable at a *systemic* level. For example, ministers are responsible for ensuring that the right individuals are appointed to the board of directors, that the right framework, legislation, and corporate plan are in place, that the organization has received policy direction consistent with its mandate, and that the organization delivers on its mandate.⁽⁷⁾

The federal government retains influence, and in some cases control, over Crown corporations through several mechanisms: the appointment and remuneration of directors and the chief executive officers (CEOs); the approval of corporate plans and budgets; and the approval and guarantee of borrowings. Furthermore, the legislation governing some Crown corporations empowers the minister to issue directives that allow the government to intervene in the management of the corporation by directing the board to follow a particular course of action.

Most Crown corporations subject to Part X of the FAA must submit annually, for government approval, a corporate plan and a capital budget and operating budget, as well as prepare an annual report. The annual report is the primary mechanism by which Crown corporations are made accountable to Parliament and Canadians. The FAA requires that the annual report include a Management's Discussion and Analysis section, and audited financial statements. The annual report, as well as summaries of plans and budgets, is tabled in Parliament by the responsible minister. Parliament also receives a consolidated report on Crown corporations by the President of the Treasury Board.

(6) The principle of accountability is set out in section 88 of the FAA: “[e]ach Crown corporation is ultimately accountable, through the appropriate Minister, to Parliament for the conduct of its affairs.”

(7) *Governance in the Public Service of Canada: Ministerial and Deputy-Ministerial Accountability*, Government Response to the Tenth Report of the Standing Committee on Public Accounts (tabled on 17 August 2005), http://www.tbs-sct.gc.ca/report/gr-rg/2005/0817_e.asp.

All Crown corporations must maintain proper financial statements that are subject to annual audits. The Auditor General is the appointed auditor for most, but not all, Crown corporations. Regardless, the audit provisions for all Crown corporations are the same. They include an annual audit opinion on the fairness of the presentation of the financial statements and on compliance with authorities, and a provision to raise other matters as the auditor considers appropriate. Since 1984, in addition to the annual audit of financial statements, most Crown corporations are subject to value-for-money audits known as “special examinations,” which are to be carried out at least once every five years by the Auditor General. These include an audit opinion on the fulfilment of management responsibilities.

RECENT REVIEWS OF THE GOVERNANCE FRAMEWORK

The legislative framework for the governance of Crown corporations has not undergone any significant amendments since 1984. At that time, changes to the FAA were introduced in order to strengthen the control and accountability framework. The 1984 amendments created the model for Crown corporation governance that is in place today, outlining roles and authorities of the board of directors, management, the responsible minister, the Minister of Finance, the Treasury Board, the Governor in Council, Parliament, and external and internal auditors.

Since that time, the Auditor General and various parliamentary committees have conducted several important reviews of Crown corporation governance. While the government has generally agreed with the findings of key reports, until very recently it has not proposed implementing substantial changes to the legislative framework under which federal Crown corporations operate. It has, however, issued new and expanded policy guidelines in response both to those reviews and to evolving governance practices in the private sector. Some of the key reviews and recommendations are discussed below, as well as recent legislative and policy changes affecting Crown corporations.

In 2000, the Auditor General carried out an examination of the corporate governance processes of a group of Crown corporations to determine whether key governance features are functioning in Crown corporations. The governance features examined included: the appointment process of directors, CEOs and chairs; the capacity of the government to review and challenge corporate plans and ensure mandate relevance; and the composition, roles and

responsibilities, and performance of audit committees. The examination revealed weaknesses in key areas and the need for further improvement to ensure the effective implementation of the FAA and the quality of Crown corporation governance. A follow-up report by the Auditor General in 2002 examined executive compensation at Crown corporations and found inconsistencies in how such corporations manage the overall compensation for their executives. It recommended that compensation disclosure be improved.

In November 2003, the Auditor General released a report on sponsorship and advertising in government. The report, entitled *Government-Wide Audit of Sponsorship, Advertising, and Public Opinion Research*, identified three main issues concerning financial management in six Crown corporations: the improper transfer of funds between federal organizations; the lack of evidence of value-for-money in the allocation of contracts; and the failure to detect, through internal audit, the inappropriate movements of public funds.

In February 2004, the government launched a commission of inquiry (the Gomery Commission) into the issues identified in the Auditor General's 2003 report. The commission was mandated to investigate and report on questions raised by the Auditor General and to make recommendations to the government, based upon its findings, in order to prevent mismanagement of activities in all federal entities in the future. At the same time, the government announced an internal review of the governance framework of Crown corporations.

On 15 February 2005, the Auditor General tabled the third Status Report to Parliament in the House of Commons. Chapter 7 of the report assesses the progress made by the government and Crown corporations in implementing recommendations from the 2000 audit report (and 2002 observations), as well as the related 2002 report of the House of Commons Standing Committee on Public Accounts. It also discusses recent developments in corporate governance and their possible implications for the governance and accountability framework of Crown corporations. In the report, the Auditor General found that on the whole, progress in addressing previous recommendations had been unsatisfactory although individual Crown corporations had made improvements to their own governance structures and practices.

The government in turn had made some progress in implementing best practices. For example, in October 2003, it issued *Guidelines for Audit Committees in Crown Corporations and Other Public Enterprises*. The intent of the guidelines was to ensure that such audit committees include members with the requisite knowledge and experience in financial management and accounting.

The government's own review, entitled *Meeting the Expectations of Canadians – Review of the Governance Framework for Canada's Crown Corporations*, was tabled in the House of Commons on 17 February 2005, two days after Auditor General's 2005 Status Report. Among the six main findings of the review is the need to reassert the role of Crown corporations as instruments of public policy. Further, the review found that the accountability regimes for Crown corporations require clarification and strengthening, as do the stewardship roles of the boards of directors. Notably, the review of Crown corporation governance found that there were questions as to who precisely is accountable to the government for the corporation: the board and its chair, or the CEO. Furthermore, the phrasing "through a Minister to Parliament" that defines ministerial accountability in the FAA has caused confusion about precisely to whom in government the corporation is accountable.

The review contains more than 30 measures, intended to address these findings by:

- clarifying the relationship between ministers and Crown corporations;
- strengthening the corporations' accountability regimes;
- making the appointment process more transparent;
- strengthening their audit regimes; and
- making their activities and operations more transparent.

To this end, the government proposed to: introduce legislation to ensure a split in the positions of a Crown corporation's CEO and the chair of the board; review the appointment of public servants to the boards of Crown corporations, so as to restrict their participation; and take steps to require that the CEO be the sole representative of management to the board of directors. The report also announced the government's intention to amend the relevant legislation to allow the appointment of the Auditor General of Canada as auditor for all Crown corporations.

Greater transparency would be achieved by, first, ensuring that the Main Estimates clearly outline the funds allocated to each Crown corporation receiving parliamentary appropriations, and second, extending the *Access to Information Act* to 10 of 18 Crown corporations that are currently excluded from the application of that Act. The Act would not be extended to the 7 remaining federal Crown corporations until the government introduced mechanisms to protect commercially sensitive information.⁽⁸⁾

(8) An eighth excluded Crown corporation, the Canada Pension Plan Investment Board, is a federal-provincial entity, and its inclusion under the Act would require provincial consent.

The government stated that the intent of the reforms is to bring the governance of Crown corporations more in line with reforms in the private sector. The report indicated that implementation of the measures would flow from legislative, policy, and guidelines changes, which would be pursued in consultation and collaboration with Crown corporations. Seven of the 31 measures are now completed and implemented.⁽⁹⁾

Several legislative changes affecting Crown corporations took place in 2005. *An Act to implement certain provisions of the budget tabled in Parliament on February 23, 2005* came into force on 29 June 2005.⁽¹⁰⁾ Among other measures, this Act includes amendments to the *Financial Administration Act* and other statutes in order to implement components of the *Review of the Governance Framework for Canada's Crown Corporations*, including naming the Auditor General as either joint or sole external auditor for all Crown corporations except the Bank of Canada.⁽¹¹⁾ It also amends the *Financial Administration Act* to extend the application of financial management and control provisions in that Act to wholly-owned subsidiaries of parent Crown corporations and to certain parent Crown corporations.

In addition, since the tabling of the Governance Review in 2005, some action has been taken to implement several of the measures requiring a change in guidelines or policy. Notably, the government introduced reforms to the Treasury Board policy on the appointment process. The modified appointment process provides for greater involvement by the board of directors in the selection of CEOs of Crown corporations. However, the government continues to make the final determination for the positions of chair and directors.⁽¹²⁾ The reforms gave a

(9) See the Treasury Board Secretariat's 2005 *Annual Report to Parliament: Crown Corporations and Other Corporate Interests of Canada*, tabled on 4 April 2006.

(10) Certain sections will come into force on a day to be fixed by order of the Governor in Council.

(11) Previously, the Canada Pension Plan Investment Board, Public Sector Pension Investment Board, Canadian Race Relations Foundation, and Canada Post Corporation were audited by private sector firms. Canada Development Investment Corporation, Canada Mortgage and Housing Corporation, Business Development Bank of Canada, Canada Lands Company Limited, Atomic Energy of Canada Limited and VIA Rail Canada Inc. were previously jointly audited by the Office of the Auditor General and private sector firms.

(12) A revised process for appointing Crown corporation boards of directors, chairs, and CEOs was first announced by the federal government in March 2004, but was not fully defined and implemented at the time. The 2005 Treasury Board review provided further clarification. With respect to the appointment of CEOs, the appointment process varies among Crown corporations. Depending on the statutory provisions, CEOs may be appointed by the Governor in Council, by the board of directors with the approval of the Governor in Council, by the Governor in Council on the recommendation of the board of directors, or by the board of directors itself.

greater role to Parliament by providing an opportunity for Members of Parliament to vet nominations. However, Members of Parliament participating in a review of a Crown corporation appointment under the new process expressed frustration with the way in which candidates were identified, and confusion as to their role in the process given that the government would continue to make the final determination.⁽¹³⁾

On 31 August 2005, by Order in Council, the following 10 Crown corporations (previously falling outside the provisions of the *Access to Information Act*) were brought under the Act:

- Canada Development Investment Corporation;
- Canadian Race Relations Foundation;
- Cape Breton Development Corporation;
- Cape Breton Growth Fund Corporation;
- Enterprise Cape Breton Corporation;
- Marine Atlantic Inc.;
- Old Port of Montreal Corporation Inc.;
- Parc Downsview Park Inc.;
- Queens Quay West Land Corporation; and
- Ridley Terminals Inc.

Finally, the government reported in the 2005 *Annual Report to Parliament: Crown Corporations and Other Corporate Interests of Canada* that Crown corporations are, wherever possible, already voluntarily implementing the Governance Review measures, without waiting for legislation that will force them to comply.

(13) House of Commons, Standing Committee on Government Operations and Estimates, *Minutes of Proceedings and Evidence*, 1st Session, 38th Parliament, 24 October 2005, 17:10.

NEW RECOMMENDATIONS

A. Gomery Commission – Phase 2 Report

The Gomery Commission's Phase 2 report, *Restoring Accountability: Recommendations*, was released on 1 February 2006. The report concludes that the recently announced reform package of 2005 addresses many of the concerns that relate to Crown corporations. It identifies two issues that the Commissioner believes merit further reflection: the appointment of members of a Crown corporation's board of directors and the appointment of its CEO. It recommends that appointments to management posts should be free of political influence. In this model, the CEO would be appointed not by the minister, but by the board of directors. Initial appointments to the board of directors would be made by the government on the basis of merit. Thereafter, the directors themselves would be responsible for filling any vacancies on the board.

B. Accountability Act Proposals

The prospective Federal Accountability Act as outlined in the Conservative Party of Canada's 2006 election platform proposes a number of changes to the current governance regime of Crown corporations. While many of these proposals are consistent with the government's 2005 review, there are significant departures, notably in the appointment process. The proposals in the prospective Accountability Act address many of the issues identified in previous reviews by: making the appointment process more transparent; strengthening the audit regime; and making the activities and operations of Crown corporations more transparent. There are two important omissions: the prospective Act as outlined does not contain measures directed towards strengthening ministerial accountability, nor does it contain measures aimed at clarifying the role of Crown corporations as instruments of public policy.

The proposed Accountability Act would introduce a new process to ensure that public appointments are filled on the basis of merit. It would establish a separate appointments agency, the Public Appointments Commission, to set merit-based requirements for appointments to government boards, commissions and agencies, and to ensure that competitions for posts are widely publicized and fairly conducted. Other reforms would be introduced in order to prevent ministerial aides and other political appointees from receiving favoured treatment when applying for public service positions, including (presumably) those at Crown corporations.

A series of proposals in the proposed Accountability Act relate to the powers of the Auditor General. The measures would expand both the mandate and resources of the Office of the Auditor General of Canada, giving it the power to examine and propose changes to the entire range of government grants, contributions and contracting policies in all government departments, Crown corporations and agencies. Other amendments would allow the Auditor General to “follow the money” to its end recipients by providing him or her with the statutory authority to conduct audits of the records, documents and accounts of any individual, institution or company that receives grants, contributions or transfers under an agreement with the Government of Canada. It would ensure that all granting programs are reviewed every five years, strengthen enforcement of government financial guidelines, and introduce new *Criminal Code* penalties for fraud involving the misuse of taxpayers’ money. Funding for the Office would be increased in order to ensure that it has the necessary resources to pursue an expanded mandate.

The prospective Accountability Act would also expand the coverage of the *Access to Information Act* to all Crown corporations, Officers of Parliament, foundations and other organizations that receive government funding or perform public functions. It would remove the government’s ability to exempt Crown corporations and other bodies from the *Public Servants Disclosure Protection Act*, the federal government’s recently adopted legislation facilitating the disclosure of wrongdoing and the protection of whistleblowers in the public sector. The legislation currently covers all federal public sector employees, including those in Crown corporations and the RCMP, but excludes, among others, Crown corporations’ boards of directors.

REFERENCES

- Auditor General of Canada. *2000 Report of the Auditor General of Canada*. Chapter 18, “Governance of Crown Corporations.”
- . *2003 Report of the Auditor General of Canada*. Chapters 3, 4 and 5, “Government-Wide Audit of Sponsorship,” “Advertising,” and “Public Opinion Research.”
- . *2005 Status Report of the Auditor General of Canada*. Chapter 7, “Governance of Crown Corporations.”
- Commission of Inquiry into the Sponsorship Program and Advertising Activities. *Restoring Accountability: Recommendations*. Phase 2 Report. Ottawa, 2006.
- Conservative Party of Canada. *The Federal Accountability Act: Stephen Harper’s Commitment to Canadians to Clean up Government*. Ottawa, 4 November 2005.
- Treasury Board Secretariat. *Annual Report to Parliament: Crown Corporations and Other Corporate Interests of Canada* (for 2004). Treasury Board Secretariat, Ottawa, 2004.
- . *Annual Report to Parliament: Crown Corporations and Other Corporate Interests of Canada* (for 2005). Treasury Board Secretariat, Ottawa, 4 April 2006.
- . *Meeting the Expectations of Canadians – Review of the Governance Framework for Canada’s Crown Corporations*. Treasury Board Secretariat, Ottawa, 2005.