
AUDIT AND EVALUATION
DIRECTORATE

DIRECTION GÉNÉRALE
DE LA VÉRIFICATION
ET DE L'ÉVALUATION

AUDIT OF THE MANAGEMENT CONTROL
FRAMEWORK FOR GRANTS AND
CONTRIBUTIONS
2004-65154
FINAL ADVISORY REPORT
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1.0 EXECUTIVE SUMMARY

In accordance with the Internal Audit and Evaluation Risk-based Work Plan, an audit of the Management Control Framework for Grants and Contributions was carried out during the 2004-05 fiscal year and included transaction from the 2002-03 and 2003-04 fiscal years.

The objectives of the audit were to assess whether:

- an effective management control framework (systems, policies, procedures and controls) and management practices are in place and are appropriate to ensure compliance, program effectiveness and financial integrity;
- programs are established in compliance with Treasury Board's *Policy on Transfer Payments*; and
- payments are made in accordance to the Terms and Conditions of the applicable program.

This report is being prepared for information and is intended to complement other audits and reviews that have been carried out recently in the Department that raised similar type findings.

Conclusion

There are numerous tools available to assist program managers in fulfilling their program requirements; however, Departmental staff were not always aware of the existence of these tools to assist in administering the grants and contributions programs.

The audit identified weaknesses in the verification and payment processes carried out under Sections 33 and 34 of the *Financial Administration Act* (FAA). There were weaknesses in the level of documentation examined and maintained on file prior to contribution claims being authorized for payment. Evidence could not always be found in files to show the program officers confirmed the terms and conditions contained in the contribution agreement for payment had been fulfilled prior to releasing payments. As well, in many of the files examined there was not always evidence to support the payments that were made. For example, there were not always reports from recipients, cash flow statements or expense reports to ensure that recipients accounted for funds received prior to receiving additional funding.

In addition, it was also noted that in some instances, the Departmental Class Grants and Contribution authority was being used to make payments to recipients whose specific program authorities had terminated.

At the same time that this audit work was being carried out, other audits were being conducted on specific grant and contribution programs in the Department. Audit such as those conducted on the contribution programs for the Pacific Salmon Foundation and the Yukon Salmon Subcommittee identified similar type issues. These issues include: departmental staff not being fully aware of administrative guidelines for a contribution program; weaknesses in the process for authorizing payments under sections 33 and 34 of the FAA, as well as compliance with terms and condition of contribution agreement and the Treasury Board's *Policy on Transfer Payments*. In addition, the Audit and Evaluation Directorate (AED) recently conducted a Value for Money

Audit on the Fisheries Access Program. That audit also identified weaknesses with the section 33 and 34 processes.

Earlier this year, the Audit and Evaluation Directorate undertook a project to develop tools to assist in the audit of the Management Control Framework associated with financial policy areas. In the course of completing this work, AED identified significant, systemic problems with the macro financial policy development and revision process in DFO. Finance and Administration Directorate coordinate a program to improve the departmental financial policy development and revision process.

Given the numerous audits and reviews that have included recommendations to address the issues related to the administration of grants and contributions, no further recommendations are being made in this audit.

Management Response

Issues raised in this audit will be addressed through Management Actions Plans submitted for the specific audits. In addition, mandatory Management Modernization Training sessions are planned for the fall of 2005 for senior managers in the Departments. This will include training related to financial management responsibilities.

Since the time of the audit, there have been a number of initiatives undertaken that will improve the management and control of grants and contributions. New terms and conditions and processes for the Departmental Class Grants and Contributions Program have been put in place. As well, Headquarters Finance has undertaken a number of functional reviews in the regions to identify areas for improvements in the processing of transactions. Finance is continuing to follow-up on the results of these reviews.

2.0. INTRODUCTION

In accordance with the Internal Audit and Evaluation Risk-based Work Plan, an audit of the Management Control Framework for Grants and Contributions was carried out during the 2004-05 fiscal year.

2.1. BACKGROUND

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. Transfer payments may be used by departments to meet strategic objectives. The major types of transfer payments are grants, contributions. All transfer payments are subject to the Treasury Board Secretariat's Policy on Transfer Payments dated June 2000. This Policy is currently being revised and is expected to be released by April 1, 2006

Fisheries and Oceans Canada (DFO) makes use of grant and contribution programs to assist in meeting its strategic objectives. For the fiscal year 2002/03, grants and contributions totalled \$12,219,810 or 8.0% of annual expenditures. This amount was comprised of eight grant and sixty-four contribution programs. For the fiscal year 2003/04, grant and contribution payments totalled \$7,968,060 or 5.6% of annual expenditures. The majority of the grants and contributions are for comparatively small amounts with two grants (Supplement to the Natural Sciences, Engineering and Research Council of Canada (NSERC) Scholarships and Small Craft Harbours (SCH) Divestitures) making up approximately 90% of the total grant payments and contribution payments from two initiatives (Longer Term *Marshall* Response Initiative and Aboriginal Fisheries Strategy) making up approximately 85% of the total contribution amounts.

The Department has also established a Class Grant and Contribution Program to address limited grants and contributions, typically for amounts less than \$50,000 with a total expenditure of approximately \$2,000,000 annually. The Class Grant and Contribution Program is utilized by most sectors in the Department to fund external organizations in support of such activities as collaborative studies, research projects, conference fees, promotion of DFO's mandate, participation in consultations, etc. This program encourages partnering with the private sector as well as other levels of government both nationally and internationally. The Deputy Minister is responsible for the overall approval of the contribution agreements while the Minister has the authority for approving the grant programs.

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.

2.2. OBJECTIVES AND SCOPE

The objectives of the audit were to assess whether:

- an effective management control framework (systems, policies, procedures and controls) and management practices are in place and are appropriate to ensure compliance, program effectiveness and financial integrity;
- programs are established in compliance with Treasury Board's Policy on Transfer Payments; and
- payments are made in accordance to the Terms and Conditions of the applicable program.

SCOPE

The scope of the audit included:

- an examination of the framework in place for managing grant and contribution programs in DFO;
- a selection and analysis of a sample of grant and contribution programs; and
- a selection and analysis of a sample of Class Grant and Contribution Programs.

The scope encompassed the examination of grants and contributions in Headquarters and the Pacific Region as these two locations represented the most significant concentration of grant and contribution activities. The audit examined a sample of grant and contributions transactions for fiscal years 2002-03 and 2003-04.

The Audit and Evaluation Directorate has completed audits and evaluations for a number of grant and contribution programs and there are also a number of audits included in AED's work plan that are in progress or are scheduled to be conducted. As such, these programs were excluded from the audit. These included the *Marshall* Response Initiative, the Aboriginal Fisheries Strategy, the Canadian Coast Guard Auxiliary and the Divestiture Grants Program for Small Craft Harbours.

Audits of the Contributions to Pacific Salmon Foundation and the Yukon Salmon Sub-Committee were undertaken concurrently as the MCF audit and the results reported on in separate reports. Findings from those reports are used to demonstrate areas for improvement in the overall management control framework for grants and contributions.

2.3. METHODOLOGY

The following methodology was followed in conducting the audit:

- audit programs, questionnaires and audit criteria were developed;

- interviews were conducted with officials from Headquarters and Pacific Regional finance staff, as well as selected program managers;
- a review of internal documentation and reports relating to the delivery of the programs;
- a review of relevant Treasury Board and departmental documentation (e.g. policies and agreements); and
- an examination of selected transactions made under the various grant and contribution programs.

The Treasury Board is in the process of developing a guide for the audit of grants and contributions in departments. The criteria identified in the draft audit guide were used in this audit.

3.0 OBSERVATIONS AND RECOMMENDATIONS

3.1 MANAGEMENT CONTROL FRAMEWORK

A well structured management control framework for grants and contributions addresses the following attributes:

- 1.0 Appropriate Program
- 2.0 Appropriate Funding Instrument
- 3.0 Capacity to Deliver the Program
- 4.0 Risk Management Strategies
- 5.0 Program Objectives
- 6.0 Terms and Conditions
- 7.0 Program Implementation and Reach
- 8.0 Eligibility, Selection and Approval
- 9.0 Agreements
- 10.0 Handling of Public Money
- 11.0 Monitoring and Payments
- 12.0 Information for Management Decision Making

Each of these attributes was examined during the audit.

3.1.1 *Appropriate Program*

Criteria: Appropriate practices and procedures should be in place to ensure that transfer payment programs are consistent with government and departmental rules and priorities and that the program addresses a need.

Findings

Transfer payment programs are initiated to respond to program requirements. There are numerous tools available to assist program managers in fulfilling their program requirements through the use of grants and contributions. Treasury Board policies and guidelines, such as the *Transfer Payment Policy*, which identifies conditions for a transfer payment program and *A Guide to Preparing Treasury Board Submissions* sets out parameters that Departments must follow in requesting authorities for programs. In addition, the Departmental Finance and Administration web site provides information on the administration of transfer payment programs. Interviews also found that Human Resources and Corporate Service staff provide advice and guidance to program staff in the development of transfer payment program approval documentation.

Despite the availability of these tools, the audit team observed that there was a lack of awareness on the part of some Departmental staff of the existence of these tools and noted that training would be beneficial.

3.1.2 *Appropriate Funding Instrument*

Criteria: Options for the most appropriate funding instrument [grant, contribution or other] should be examined so that the most appropriate funding instrument is being used.

Findings

There are guidelines in place to assist program managers in determining the appropriate funding instrument. The Departmental Finance and Administration web site provides a link to the Treasury Board Secretariat (TBS) *Guide on Financial Arrangements and Funding Options*. This document provides guidance on selecting the appropriate funding instrument. There was not always evidence, however, that alternate funding instruments were considered. It was noted the Departmental Class Grant and Contribution Authority was used when another funding alternative may have been more appropriate. For example, the Pacific Region used the Departmental Class Authority to make payments that had previously been expended against a separate authority (Pacific Stream Keepers). There were also examples such as the Contribution to the Canadian Bluefin Research Fund and the Contribution for the Ottawa University and Institute of Oceans Science where a contract could have been used as opposed to the Departmental Class Authority.

3.1.3 *Capacity to Deliver the Program*

Criteria: The Department should have the capacity to effectively deliver and administer the transfer payment program, including monitoring, learning and training.

Findings

With the exception of some large contribution programs such as, the *Marshall* Response Initiative and the Aboriginal Fisheries Strategy, DFO is not a major user of transfer payment programs and as such does not have a Centre of Expertise for Grant and Contribution programs. Human Resources and Corporate Services staff is relied upon to provide guidance to program staff during the development of programs. Some sectors have expressed an interest in receiving training in the administration of grants and contributions to enable them to play a more active role in these programs. In addition, for programs that are delivered primarily in the regions, such as contribution programs with the Pacific Salmon Foundation and the Yukon Salmon Sub-Committee, it is not always clear who the point of contact is at a national level.

3.1.4 *Risk Management Strategy*

Criteria: An adequate and appropriate risk management framework should be developed, implemented and utilized.

Findings

With the issuance of Treasury Board's *Policy on Transfer Payments* in 2000, all new transfer payment programs and programs whose Terms and Conditions are being renewed must include a Risk Based Audit Framework (RBAF) as part of the submission. The development of RBAFs is the responsibility of the program manager and used to identify risks in the programs as well as determining appropriate strategies to manage and mitigate the risks.

The sectors work in close collaboration with DFO's Audit and Evaluation Directorate and HQ Finance who provide advice and assistance in developing RBAFs for a program. It was not clearly understood, however, what role each party must play in developing the RBAF, who owns the RBAF and the use that can be made of the document. Sectors often believe that the document is prepared only to meet Treasury Board requirements and is not seen as a management tool.

3.1.5 Program Objectives

Criteria: Program staff and management at all levels should understand the program objectives, how they relate to government and departmental objectives, and how recipients contribute to the achievement of these objectives. Program objectives should state in measurable terms the expected results (outputs, immediate outcomes, intermediate outcomes and final outcomes).

Findings

With the issuance of Treasury Board's *Policy on Transfer Payments* in 2000, all new transfer payment programs and programs whose Terms and Conditions are being renewed must include a Results-Based Management and Accountability Framework (RMAF) as part of the submission. An RMAF is a blueprint for managers to plan, measure, evaluate and report on results throughout the lifecycle of a program.

Program managers are responsible for developing the RMAF. The Audit and Evaluation Directorate and Headquarters Finance provide advice and assistance. As is the case for RBAFs, the roles and responsibilities of all parties are not clearly understood.

3.1.6 Terms and Conditions

Criteria: Departments must obtain Treasury Board approval of the terms and conditions for a class of grant recipients and the terms and conditions for all contribution programs either to a specific recipient or a class of recipients.

Findings

A management control framework contains elements to ensure that a program is well designed and complies with legislation or policies. The terms and conditions, in a Treasury Board Submission establishing a grant or contribution program, are key elements of a management control framework. The contribution agreement defines the terms and conditions for the program management, the funding arrangements and the performance and reporting requirements for the recipient.

It is essential that the contribution agreement accurately reflects to the recipient the terms and conditions set out in the program authority document. The audit found instances in which the terms and conditions in the contribution agreement differed from the program approval documents. The Contribution Agreement for the Contribution to the Pacific Salmon Foundation is an example of this issue. The Management Action Plan prepared in response to the Audit and Evaluation of the Contribution to the Pacific Salmon Foundation included measures to address this issue.

Program managers have the responsibility for ensuring that the terms and conditions are respected and deliverables obtained. Program managers have been delegated Section 34 signing authority of the FAA. Section 34 must be signed prior to a payment being issued (Section 33 – Payment Authority, is a Finance responsibility). When managers attest that the requirements of Section 34 have been met, they are certifying that the requirements for payment as outlined in the terms and conditions of the contribution agreement have been completed. Program managers must have processes in place to ensure that the deliverables or performance objectives specified in the contribution agreement to be met prior to payments being made are in fact being completed. Program officers may attest that these requirements have been met through a variety of methods including: site visits, certifications by experts, or copies of minutes or other publications.

Finance is responsible for processing the payments; however when relying on the verification and certification of accounts by officials with delegated Section 34 FAA authority, Finance Officers must ensure that the system of account verification and related financial controls are adequate and are being consistently followed by those carrying out section 34 authority. The audit found there are generally no processes in place in Finance to monitor the implementation of programs to ensure that terms and conditions and deliverables as outlined in the contribution agreement are complied to prior to payments being requested and made. The examination of finance files indicated that minimal information is kept on file and that Finance does not follow-up nor request evidence to ensure that the terms and conditions have been met, deliverables have been received or that payment is made in accordance with the *Financial Administration Act* or the Transfer Payment Policy.

3.1.7 Program Implementation and Reach

Criteria: Encouraging as many potentially eligible applicants as possible to apply should help ensure fairness of the program and target available funds towards the most promising projects. This means using appropriate and effective communication and promotion to increase awareness in target groups.

Findings

A key ingredient of a successful program is a high level of interest among potential recipients of grants or contributions. An appropriate and effective communication and promotion plan increases awareness in target groups. In the Department, program implementation and reach is generally achieved by diffusion and direct liaison with potential recipients. For some sectors, recipients have historically requested funding through the grants and contributions to help them fund research, development, management and promotion of fisheries and oceans initiatives, thereby contributing to program objectives and the overall departmental mandate.

While the target recipients for some programs are easily identified, there is no formal communication process to inform interested parties of the availability of funding sources. A search of the departmental web site did not provide any information on existing grant and contribution programs. Communication and promotion strategies would foster awareness among potential eligible recipients over and above the present practice of assessing funding requests from the regular stream of applicants.

3.1.8 Eligibility, Selection and Approval

Criteria: Eligibility criteria, conditions of support, and scale of assistance should be documented in the program literature, and should be well understood and applied consistently by program staff.

Findings

The terms and conditions for grants and contributions define eligibility criteria for recipients and activities that can be undertaken under the program. The proposals are evaluated against these criteria. The region/sector assesses the proposal from a program perspective and determines whether it meets the eligibility criteria.

The audit found that a number of Grant and Contribution recipients, who had been recipients under contribution programs with their own authority that had been terminated, continued to receive payments under the Departmental Class Grant and Contribution Authority. In addition, payments have been made for a number of years using the Departmental Class Grant and Contribution Authority instead of having them made under a specific program with its own program authority.

The Departmental Class Grants and Contributions authority is intended for limited payments and not for continuous use, nor to make payments for which previous specific program authorities had terminated

3.1.9 Agreements

Criteria: Departments should establish policies and procedures to ensure that agreements are based on Treasury Board approved terms and conditions for the program.

Findings

The audit could find no evidence of a process in place in which the contribution agreements were verified to ensure that the terms and conditions accurately reflected those in the terms and conditions of the Treasury Board Submission. In a number of cases the program officers who were responsible for writing the contribution agreement did not have access to the terms and conditions of the Treasury Board Submission. The audit also found that finance units did not have copies of the contribution agreements on file.

3.1.10 Handling of Public Money

Criteria: Senior financial officer in conjunction with senior program managers should develop efficient and effective accounting and other procedures to ensure that payment requests meet the requirements of the policy on account verification relating to sections 33 and 34 of the FAA and the requirements of the Payment Requisitioning Regulations.

Findings

The Treasury Board *Policy on Transfer Payments* provides guidance on the payment of grants and contributions. The sections of the policy relating to: Approval, Payment and Accounting; Cash Management; and Accountability of the Recipient have a direct impact on the Handling of Public Money.

Section 34 authority under the FAA, is typically performed by program managers in sectors. The audit found the account verification was performed to varying degrees of rigour in the Department. For larger programs, such as the Pacific Salmon Resource Rebuilding Program, detailed verification requirements were established and followed before payments were made. However, for other programs evidence could not always be found in files to show the program officers confirmed the recipients had fulfilled the terms and conditions in the contribution agreement for payment prior to releasing payments. As well, in many of the files examined there was not always evidence to support the payments that were made. For example, there were not always reports from recipients, cash flow statements or expenditure reports to ensure that recipients accounted for funds received prior to receiving additional funding.

3.1.11 Monitoring and Payments

Criteria: Section 34 of the FAA stipulates that no payment shall be made unless a person with the proper delegated authority certifies that the payee is eligible or entitled to the payment.

Findings

For the majority of the transfer payment programs, program staff is signing under Section 34 of the FAA. This is the appropriate place for this function to occur as the program staff is in the best position to determine if the recipients have met the requirements as defined in the terms and conditions of the contribution agreements. However, there were many examples in which payments were authorized without the recipient having submitted the required documentation. For example cash flow statements were not submitted prior to the first payment being issued; subsequent payments were then released without an accounting of the first payment, these are requirements as stated in the *Transfer Payment Policy*. Finally, there was not always evidence that Finance units ensured that the verification process being performed was adequate.

Failure to complete a proper account verification process puts the Department at risk for making payments when the recipient has not met the performance expectations of the agreement and that payments are made for expenditures that are not eligible. It is appropriate for Section 34 of the FAA to occur in the sectors by the program managers as they are the individuals most familiar with the program and are in the best position to determine if the recipient has met the terms and conditions for the program. However, program managers require training on the proper

application of Section 34 of the FAA and their responsibilities therein. Finance units should ensure this function is adequately performed and proper policies and procedures are in place

3.1.12 Information for Management Decision Making

Criteria: *Relevant quantitative and qualitative performance measures should be in place to monitor program performance.*

Findings

As part of the Treasury Board approval process for grant and contribution programs, Departments must include an RMAF and an RBAF as part of the program submission documents. The RMAF includes a performance measuring strategy that provides a means to measure and assess the expected results and allows for reporting on program performance. The RMAF identifies the information that will be required to measure the program and its sources.

Despite having the process in place to develop RMAFs and the appropriate performance measurement strategies, there has not always been a requirement in contribution agreements for recipients to provide the necessary information to allow the program managers to assess the performance of their program.

3.2 CONCLUSION

The audit identified weaknesses in the verification and payment processes carried out under Sections 33 and 34 of the Financial Administration Act (FAA). There were weaknesses in the level of documentation examined and maintained on file prior to contribution claims being authorized for payment. Evidence could not always be found in files to show the program officers confirmed the recipients had fulfilled the terms and conditions related to payment contained in the contribution agreement prior to releasing payments. As well, in many of the files examined there was not always evidence to support the payments that were made. For example, there were not always reports from recipients, cash flow statements or expenditure reports to ensure that recipients accounted for funds received prior to receiving additional funding.

At the same time that this audit work was being carried out, other audits were being conducted on specific grant and contribution programs in the Department. Audit such as those conducted on the contribution programs for the Pacific Salmon Foundation and the Yukon Salmon Sub-Committee identified similar type issues. These issues include a lack of awareness for the administration of a contribution program; weaknesses in the process for authorizing payments under sections 33 and 34 of the FAA, as well as compliance with terms and condition of contribution agreement and the Treasury Board's *Policy on Transfer Payments*. In addition, the Audit and Evaluation Directorate (AED) recently conducted a Value for Money Audit on the Fisheries Access Program. That audit also identified weaknesses with the section 33 and 34 processes.

In addition, it was also noted that in some instances, the Departmental Class Grants and Contribution authority was being used to make payments to recipients whose specific program authorities had terminated.

Earlier this year, the AED undertook a project to develop tools to assist in the audit of the Management Control Framework associated with financial policy areas. In the course of completing this work, AED identified significant, systemic problems with the macro financial policy development and revision process in DFO. These issues have been formally documented in a Management Letter to the Departmental Audit and Evaluation Committee in May 2005. The Management Letter concluded that the problems associated with the financial policy development process in DFO should be addressed prior to undertaking audits of the Management Control Framework of financial policy areas.

It was recommended that the Finance and Administration Directorate coordinate a program to improve the departmental financial policy development and revision process. This recommendation was supported by the ADM, Human Resources and Corporate Services (HRCS) and AED will follow-up on this initiative in one year.

Given the numerous audits and reviews that have included recommendations to address the issues related to the administration of grants and contributions, no further recommendations are made resulting from this audit.

Management Response

Issues raised in this audit will be addressed through Management Actions Plans submitted for the specific audits. In addition, mandatory Management Modernization Training sessions are planned for the fall of 2005 for senior managers in the Departments. This will include training related to financial management responsibilities.

Since the time of the audit, there have been a number of initiatives undertaken that will improve the management and control of grants and contributions. New terms and conditions and processes for the Departmental Class Grants and Contributions Program have been put in place. As well, Headquarters Finance has undertaken a number of functional reviews in the regions to identify areas for improvements in the processing of transactions. Finance is continuing to follow-up on the results of these reviews.