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Report of the Auditor General of Canada

CHAPTER 1

Follow-up Audit on Internal Controls Over Financial Reporting



Office of the Auditor General of Canada

OAG

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CHAPTER 1

Follow-up Audit on Internal Controls Over Financial Reporting

Performance audit reports

This report presents the results of a performance audit conducted by the Office of the Auditor General of Canada under the authority of the *Auditor General Act*.

A performance audit is an independent, objective, and systematic assessment of how well government is managing its activities, responsibilities, and resources. Audit topics are selected based on their significance. While the Office may comment on policy implementation in a performance audit, it does not comment on the merits of a policy.

Performance audits are planned, performed, and reported in accordance with professional auditing standards and Office policies. They are conducted by qualified auditors who

- establish audit objectives and criteria for the assessment of performance,
- gather the evidence necessary to assess performance against the criteria,
- report both positive and negative findings,
- conclude against the established audit objectives, and
- make recommendations for improvement when there are significant differences between criteria and assessed performance.

Performance audits contribute to a public service that is ethical and effective and a government that is accountable to Parliament and Canadians.

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Follow-up Audit on Internal Controls Over Financial Reporting

Main Points

What we examined

Internal controls over financial reporting are measures that departments put in place to ensure that the financial information they use to make decisions, and to report internally and externally, is reliable.

In large departments, work to ensure that effective internal controls over financial reporting are in place began in 2005, under the audited departmental financial statements initiative. In 2009, the departments' focus shifted from audited financial statements to implementing the requirements of the Treasury Board Policy on Internal Control. The Policy's objective is to ensure that effective internal controls over financial reporting are in place to adequately manage risks relating to the stewardship of public resources. The Policy requires departments to publicly disclose each year the results of their risk-based assessments of their internal controls over financial reporting and of the improvements they plan to put in place.

In 2011, we followed up on our 2006 audit of internal controls over financial reporting and found that progress in addressing our past recommendations had been unsatisfactory. At that time, none of the seven large departments we audited—Agriculture and Agri-Food Canada; Department of Finance Canada; Foreign Affairs, Trade and Development Canada; Human Resources and Skills Development Canada; Aboriginal Affairs and Northern Development Canada; Transport Canada; and Veterans Affairs Canada—had fully assessed their internal controls over financial reporting.

In this follow-up audit, we examined whether the same seven departments were on track to meet their planned dates to complete this work, including whether they had identified and addressed gaps and weaknesses and whether they had implemented a program of ongoing monitoring. We also examined the steps the Treasury Board of Canada Secretariat, including the Office of the Comptroller General, had taken to review the departments' implementation of the requirements of the Policy on Internal Control, including monitoring departments' established timelines for completing their risk-based assessments.

Audit work for this chapter was completed on 23 August 2013. More details on the conduct of the audit are in **About the Audit** at the end of this chapter.

Why it's important

The 2009 Policy on Internal Control is intended in part to ensure that effective systems of internal control over financial reporting are implemented across government. Such controls serve to safeguard public resources against loss due to waste, abuse, mismanagement, errors, fraud, omissions, or other irregularities and to provide reliable and transparent reporting of how government spends public funds to achieve results for Canadians. Effective internal controls over financial reporting serve to ensure, for example, that government expenditures are appropriately made and that government revenues are fully collected and protected. Therefore, it is important that departments complete the work related to effectiveness of internal controls over financial reporting on a timely basis.

What we found

- Five of the seven audited departments and the Treasury Board of Canada Secretariat have made unsatisfactory progress in response to our 2011 recommendations. Though all seven departments have made progress in completing the first assessment of their internal controls over financial reporting, including addressing gaps and weaknesses, only Agriculture and Agri-Food Canada and Finance Canada have fully addressed our recommendation.
- In 2011, most audited departments had expected that they would complete their first assessments by 31 March 2013, but this was not fully accomplished. For the most part, all seven departments have documented their business processes and tested whether internal controls within these processes are effectively designed. Only Agriculture and Agri-Food Canada, Finance Canada, and Veterans Affairs Canada have fully tested how effectively their internal controls are operating, and have identified and addressed gaps and weaknesses. In addition, only Agriculture and Agri-Food Canada and Finance Canada have fully put in place a program of continuous monitoring.

- Aboriginal Affairs and Northern Development Canada; Foreign Affairs, Trade and Development Canada; Human Resources and Skills Development Canada; and Transport Canada are forecasting that they will need several more years to fully implement the requirements of the Policy on Internal Control, including an additional one to three years to complete the first full assessments of their internal controls. We believe that these timelines are too long, given that the departments have been working to assess the effectiveness of internal control over financial reporting for many years.
- The Treasury Board of Canada Secretariat, including the Office of the Comptroller General (OCG), has provided guidance and support to departments to assist them in completing their work on internal controls. However, while the OCG has monitored departmental progress in implementing the requirements of the Policy on Internal Control, it does not view responding to delays in departmental timelines as part of its role. The OCG has noted that the Policy on Internal Control does not provide timelines for departments to complete the work on internal controls and that the related responsibility rests with departments. Therefore, while it was aware of delays and of departments' revised timelines, it did not act to help ensure that departments completed the required work within planned timelines. The OCG understands the amount of work left to be done and realizes that it will take years for many of the departments to complete the full implementation of the Policy requirements. However, we believe that the OCG should work with the departments to see that this work is completed without delay.

The entities have responded. The departments and the Secretariat agree with all of the recommendations. Their detailed responses follow the recommendations throughout the report.

Introduction

1.1 In total, federal government departments, agencies, and other entities spend nearly \$300 billion each year to deliver programs and services to Canadians. The Government of Canada's objective in having the requirements of the Treasury Board 2009 Policy on Internal Control (the Policy) implemented appropriately and on a timely basis is to ensure that the risks related to the stewardship of public resources are adequately managed through effective internal controls, including controls over financial reporting.

1.2 Internal controls over financial reporting are the procedures and activities put in place by departments to provide reasonable assurance that

- all financial transactions are recorded;
- internal and external financial information is reliable;
- revenues received and expenditures made are properly authorized; and
- financial resources are protected against material loss due to waste, abuse, mismanagement, errors, fraud, omissions, and other irregularities.

1.3 Some examples of these controls include

- procedures to verify that departments pay for only those goods and services that have been authorized and that were received in the quantity and quality requested and at the agreed price;
- procedures to protect money received by the government from being lost or stolen; and
- procedures to review records regularly for accuracy and completeness, so that managers have reliable financial information for decision making and for reporting to parliamentarians and to Canadians on their department's performance.

1.4 In recent years, the government has gone through several significant changes, including moving toward the centralization of systems and services, the restructuring of programs and services, a reduction in spending, and the sharing of services. Given the impact of these changes, it is important that they be based on reliable financial information. The financial pressures facing the government, along with

its stated intent to return to balanced or surplus budgets, also underscore the importance of ensuring the integrity of financial information.

1.5 The 2005 audited departmental financial statements initiative required departments to work toward having controls that would also be strong enough to support an audit based on these controls. In 2008, when all the readiness assessments were completed, none of the selected departments could demonstrate that they had sufficient controls in place to support such an audit. Subsequent to these findings, the departments' focus shifted from audited financial statements to the requirement for mandatory annual public disclosure of their risk-based assessments of controls over financial reporting and of their planned improvements. This requirement is set out in the Policy on Internal Control.

1.6 As shown in Exhibit 1.1, deputy heads are responsible for ensuring that their departments have effective risk-based systems of internal control and that these systems are properly maintained, monitored and reviewed, and corrected. Under the *Financial Administration Act*, deputy heads are designated as the accounting officers for their organizations and, as such, they have a legal obligation to appear before parliamentary committees on behalf of their ministers and answer questions about the measures taken to maintain effective systems of internal control. The Comptroller General of Canada, within the Treasury Board of Canada Secretariat, provides guidance to departments and oversees the effectiveness of the system of internal control over financial reporting across the federal government.

What we found in our 2011 audit

1.7 In our 2011 Status Report of the Auditor General of Canada, Chapter 1—Financial Management and Control and Risk Management, we stated that overall progress in addressing our previous recommendations on internal controls over financial reporting had been unsatisfactory. While the departments had made some progress toward completing their annual risk-based assessments, none of the departments had fully assessed their internal controls for financial reporting. Accordingly, in the 2011 report, we made two recommendations aimed at getting this work completed.

1.8 First, we recommended that Agriculture and Agri-Food Canada; Department of Finance Canada (Finance Canada); Foreign Affairs, Trade and Development Canada; Human Resources and Skills Development Canada; Aboriginal Affairs and Northern Development Canada; Transport Canada; and Veterans Affairs Canada,

in consultation with the Office of the Comptroller General, should review the timelines set for completing their full risk-based assessments of the effectiveness of their financial reporting controls and for addressing the identified gaps and weaknesses, to ensure that they are timely. In addition, our recommendation included that the departments put in place a program for continuous monitoring. The departments agreed with this recommendation. Second, we recommended that the Treasury Board of Canada Secretariat (the Secretariat) should continue to review the implementation of the requirements of the Policy and that this should include monitoring of the departments' established timelines for completing their risk-based assessments of these controls. The Secretariat agreed with this recommendation.

1.9 The House of Commons Standing Committee on Public Accounts recommended in 2012 that departments complete this work according to the timelines laid out in our 2011 report.

Exhibit 1.1 Summary of key roles and responsibilities for implementing the Policy on Internal Control

Position	Roles and responsibilities
Deputy head	<ul style="list-style-type: none"> • Ensure the establishment, maintenance, monitoring, and review of the departmental system of internal control to mitigate risks. • Sign an annual departmental statement called the Statement of Management Responsibility Including Internal Control Over Financial Reporting, acknowledging, among other things, the conduct of an annual risk-based assessment of internal controls over financial reporting to ensure their ongoing effectiveness. • Engage the departmental audit committee on risk-based assessment plans related to the effectiveness of internal controls. • Monitor compliance with the Policy on Internal Control through audits and reviews. • Ensure that appropriate and timely action is taken to address significant weaknesses. • Provide reports to the Comptroller General as requested. • Investigate and act when significant issues related to Policy requirements arise.
The Comptroller General of Canada	<ul style="list-style-type: none"> • Oversee the effectiveness of the system of internal controls across the federal government, including monitoring compliance with this Policy. • Monitor whether appropriate and timely action is being taken to address significant issues that departments identify in their annual departmental Statement of Management Responsibility Including Internal Control Over Financial Reporting. • Monitor government-wide compliance and report periodically to Treasury Board. • Where there is indication of non-compliance with the Policy, request that a deputy head conduct an audit or review. • When a department has not complied with Policy requirements, recommend corrective measures.

Source: Treasury Board Policy on Internal Control

Focus of the audit

1.10 For this chapter, we reviewed the progress that the Secretariat and the seven selected departments had made in response to the recommendations from our 2011 audit. At that time, five of the seven selected departments—Agriculture and Agri-Food Canada; Finance Canada; Foreign Affairs, Trade and Development Canada; Transport Canada; and Veterans Affairs Canada—stated that they were in the process of carrying out risk-based action plans to complete their assessments of financial reporting controls by 31 March 2013. The other two selected departments—Human Resources and Skills Development Canada, and Aboriginal Affairs and Northern Development Canada—stated that they would complete this work by 31 March 2014 and 31 March 2015 respectively.

1.11 In 2011, the Auditor General informed the Standing Committee on Public Accounts of plans to do more performance audit work on internal controls. Given this, and the fact that many departments had indicated in our 2011 audit that they would have completed their work by 31 March 2013, we undertook this follow-up audit.

1.12 In this audit, we assessed whether the seven departments were on track to meet their planned dates to complete this work, including whether they had identified and addressed gaps and weaknesses and had implemented programs of ongoing monitoring. This effort included assessing whether the amount of time planned for completing this work is too long.

1.13 We also looked at the steps the Secretariat had taken to review the departments' implementation of the requirements of the Policy on Internal Control, including monitoring departments' established timelines for completing their risk-based assessments.

1.14 We did not assess internal controls within the audited departments and therefore offer no assurance on the effectiveness of the controls over financial reporting. More details on the audit objective, scope, approach, and criteria are in **About the Audit** at the end of this chapter.

Observations and Recommendations

Internal controls over financial reporting

Departments have made progress, but completing the work will take several years

1.15 In response to our 2011 recommendation, the audited departments agreed to complete the first full risk-based assessment of internal controls, including

- **Step 1a.** Documenting business processes and internal controls—this requires carrying out a risk-based assessment of a department’s most important business processes and documenting the process, including the controls it expects are in place;
- **Step 1b.** Testing the design effectiveness of internal controls—this relates to assessing the risks associated with a specific business process and ensuring that controls are designed to address the risks; and
- **Step 1c.** Testing the operating effectiveness of internal controls—this involves testing the controls identified under the design-effectiveness phase to ensure that they are working as intended throughout the year.

The audited departments also agreed to complete the following work:

- **Step 2.** Identify and address gaps and weaknesses in internal controls, and
- **Step 3.** Put in place a program of continuous monitoring of internal controls, which means conducting ongoing testing to ensure that the controls continue to operate effectively.

Exhibit 1.2 shows the steps and status of the departments’ actions.

1.16 Our audit work included interviews with staff within the selected departments, a review of supporting documentation, and an examination of a sample of the work completed by the departments between 1 October 2010 and 31 March 2013 to test the design and operating effectiveness of their internal controls. We examined whether the departments had

- done the work necessary for completing their first full risk-based assessments according to planned timelines reported in our 2011 chapter,
- addressed gaps and weaknesses identified during the assessments, and
- put in place programs for continuous monitoring of their controls.

Exhibit 1.2 Departments' status in implementing the requirements of the Policy on Internal Control over financial reporting

Department	Complete the first full risk-based assessment of internal controls					Complete the work required to		
	Step 1a Document business processes and internal controls	Step 1b Test the design effectiveness of internal controls	Step 1c Test the operating effectiveness of internal controls	Planned date (fiscal year) to complete first full assessment as of June 2011	Current planned date (fiscal year) to complete first full assessment	Step 2 Identify and address gaps and weaknesses in internal controls	Step 3 Put in place continuous monitoring of internal controls	
Satisfactory progress								
Agriculture and Agri-Food Canada	●	●	●	2012-13	Complete	●	●	
Finance Canada	●	●	●	2010-11	Complete	●	●	
Unsatisfactory progress								
Veterans Affairs Canada	●	●	●	2010-11	Complete	●	○	
Transport Canada	●	●	◐	2011-12	2013-14	◐	⊗	
Aboriginal Affairs and Northern Development Canada	●	●	○	2014-15	2014-15	○	⊗	
Human Resources and Skills Development Canada	●	●	○	2013-14	2015-16	○	⊗	
Foreign Affairs, Trade and Development Canada	●	◐	○	2012-13	2014-15	○	⊗	

● **Substantially complete**—Most required actions are completed.

◐ **Moderately complete**—Additional action is still required.

○ **Partially complete**—Considerable action is still required.

⊗ **Not started.**

1.17 Completing the first risk-based assessment of internal controls over financial reporting. As detailed in Exhibit 1.2, we found that, while most of the seven departments had completed the documentation and design-effectiveness testing of their assessments of internal controls, four departments—Transport Canada; Aboriginal Affairs and Northern Development Canada; Human Resources and Skills Development Canada; and Foreign Affairs, Trade and Development Canada—had yet to finish testing the operating effectiveness of these controls. Three of the departments—Transport Canada; Human Resources and Skills Development Canada; and Foreign Affairs, Trade and Development Canada—indicated that, to finish this work, they would need an additional two years beyond the planned completion dates set in 2011. The delays for these three departments and the length of the timelines for the four departments are significant, considering that departments have been focusing on this work since the audited departmental financial statements initiative in 2005.

1.18 Identifying and addressing gaps and weaknesses in internal controls over financial reporting. The risk-based assessment of internal controls in departments' business processes can identify both gaps in the design of controls and weaknesses in the way they operate. Departments must then address these gaps and weaknesses to optimize the effectiveness of their internal controls. As shown in Exhibit 1.2, we found that Transport Canada; Aboriginal Affairs and Northern Development Canada; Human Resources and Skills Development Canada; and Foreign Affairs, Trade and Development Canada had yet to complete the work that might lead to the identification and remediation of gaps and weaknesses in their systems of internal control.

1.19 Continuous monitoring of internal controls over financial reporting. As detailed in Exhibit 1.2, we also found that, of the seven departments we audited, only two—Agriculture and Agri-Food Canada, and Finance Canada—had fully implemented an ongoing monitoring program. Veterans Affairs Canada has made progress in implementing an ongoing monitoring program, but has not yet fully put it in place. We note that work required to ensure that internal controls remain effective is not a one-time exercise that is complete once the departments have finished their initial risk-based assessments of internal controls.

1.20 Overall progress. From our follow-up work, we concluded that three departments—Foreign Affairs, Trade and Development Canada; Human Resources and Skills Development Canada; and Transport Canada—were experiencing delays in completing work related to

internal controls over financial reporting. These delays have already added a further two years to the dates planned in 2011 for completion of this work in these departments. While Aboriginal Affairs and Northern Development Canada is keeping with the timeline it planned in 2011, the Department has much work left to do. We also noted that Veterans Affairs Canada has yet to fully implement a program for ongoing monitoring of controls. While the departments indicated that they had experienced significant changes, including workforce adjustment and strategic reviews, we believe that the amount of time they are taking to complete this work is too long. We therefore assessed the progress of these five departments against our 2011 recommendations as unsatisfactory (Exhibit 1.5).

1.21 Importance of completing this work. It is important to complete these risk-based assessments, as the work that the departments have done in implementing the requirements of the Policy has uncovered issues that needed improvements. These issues could result in added costs if left unaddressed. On the basis of this work, the departments have said that they made changes to their internal controls to address these issues. It is also possible for the departments to identify, through this work, opportunities to make business processes more efficient, potentially saving money. Exhibit 1.3 presents three examples that departments provided of actions resulting from work performed on their assessments of internal controls.

Exhibit 1.3 Departments have noted actions resulting from departmental assessments

Initial state	Action
<p>Poor controls over access to IT systems left data exposed to potential inappropriate activity, such as the processing of unauthorized transactions. For example, one department detected four cases where terminated employees still had access to their systems.</p>	<p>Controls were strengthened to ensure that only current authorized employees have access to the departments' information systems. This helped reduce the risk that terminated or unauthorized employees could initiate transactions using outdated user identification and passwords.</p>
<p>The collection of large amounts of cash from clients for payment of fees for services left the department exposed to the potential for theft or loss of money.</p>	<p>Processes were standardized and included implementing an online payment system to help mitigate the risk of theft or loss that could result when goods and services are paid for with cash.</p>
<p>Processes that apply to millions of dollars of annual grants and contributions were found to be inefficient and overly burdensome on applicants due to the number and complexity of forms used.</p>	<p>Effective controls were used to support streamlining and standardization to make the process more efficient for both external clients and departmental staff. For example, the number and complexity of forms has been reduced to make it easier for the client to complete a request for funding and for the department to process the request.</p>

1.22 Exhibit 1.4 presents three examples of processes we noted during this audit where internal controls had not yet been fully assessed. While this may not mean that other departmental oversight mechanisms to help address issues within these processes are lacking, or that controls do not exist, the departments cannot be fully satisfied that internal controls over financial reporting are effective until they have completed these assessments.

1.23 Completing the remaining work without delay will require the commitment of senior departmental officials, the allocation of sufficient resources, and the development and ongoing monitoring of action plans.

Exhibit 1.4 Examples of processes where internal controls have yet to be fully assessed

Department	Process
Aboriginal Affairs and Northern Development Canada	Environmental liabilities—amounts for contaminated sites across Canada, related to such things as abandoned mining sites and soil remediation of hydrocarbon contamination from old fuel tanks
Foreign Affairs, Trade and Development Canada	Capital assets—amounts for the purchase, maintenance, and disposal of land, buildings, machinery, and equipment at various locations around the world
Human Resources and Skills Development Canada	Accounts receivable—overpayments, penalties, and accrued interest from Employment Insurance, Old Age Security, and other programs

Exhibit 1.5 For most departments, the progress in addressing our 2011 recommendation is unsatisfactory

2011 Recommendation	Progress
<p>The seven audited departments, in consultation with the Office of the Comptroller General, should review the timelines set for completing their full risk-based assessment of the effectiveness of their financial reporting controls and for addressing identified gaps and weaknesses, to ensure that they are timely. The departments should also implement programs for continuous monitoring of these controls to confirm their ongoing effectiveness.</p> <p>(Recommendation 1.25 of the June 2011 Status Report of the Auditor General of Canada, Chapter 1—Financial Management and Control and Risk Management)</p>	<p>Satisfactory for</p> <ul style="list-style-type: none"> • Agriculture and Agri-Food Canada • Finance Canada <p>Unsatisfactory for</p> <ul style="list-style-type: none"> • Aboriginal Affairs and Northern Development Canada • Foreign Affairs, Trade and Development Canada • Human Resources and Skills Development Canada • Transport Canada • Veterans Affairs Canada

Satisfactory—Progress is satisfactory, given the significance and complexity of the issue, and the time that has elapsed since the recommendation was made.

Unsatisfactory—Progress is unsatisfactory, given the significance and complexity of the issue, and the time that has elapsed since the recommendation was made.

1.24 Recommendation. Foreign Affairs, Trade and Development Canada; Human Resources and Skills Development Canada; Aboriginal Affairs and Northern Development Canada; and Transport Canada should complete their assessments of internal controls within the planned timelines, including addressing gaps and weaknesses. In addition, these four departments and Veterans Affairs Canada should fully implement a program of ongoing monitoring without delay.

Aboriginal Affairs and Northern Development Canada, Human Resources and Skills Development Canada, and Transport Canada's response. Agreed. Aboriginal Affairs and Northern Development Canada, Human Resources and Skills Development Canada, and Transport Canada recognize the importance of completing the testing of internal controls over financial reporting, addressing gaps and weaknesses, and implementing a program for ongoing monitoring of these controls, while working on other equally important priorities.

Each department has put in place systems for internal controls over financial reporting, including requirements for internal reconciliations and analysis, and post-verification reviews. Work is under way to ensure that these and other internal controls are operating effectively to mitigate risk.

Building on concrete steps taken to date, the departments will undertake to complete their first full risk-based assessments of internal controls over financial reporting, including identifying and addressing gaps and weaknesses in internal controls by 31 March 2015, 31 March 2016, and 31 March 2014 respectively. As the initial assessment for each key process is completed, Aboriginal Affairs and Northern Development Canada, Human Resources and Skills Development Canada, and Transport Canada will implement a program for continuous monitoring of their internal controls over financial reporting.

Foreign Affairs, Trade and Development Canada's response. Agreed. Foreign Affairs, Trade and Development Canada agrees that it is important to complete the testing of internal controls over financial reporting, address gaps and weaknesses, and implement a program for ongoing monitoring of these controls. However, due to recent changes enacted by legislation, the Department must reconsider its current implementation plans, including timelines. *Economic Action Plan 2013 Act, No. 1*, the Act that implemented the merger of the Department of Foreign Affairs and International Trade and the Canadian International Development Agency, received Royal Assent on 26 June 2013, creating the new Department of Foreign Affairs,

Trade and Development (DFATD). As a result, the existing implementation plans for both former entities will be merged, and a new planned completion date for DFATD will be determined. DFATD is committed to ensuring that the requirements of the Policy on Internal Control are fully implemented by the new completion date.

Veterans Affairs Canada's response. Agreed. Veterans Affairs Canada is actively implementing its program for the continuous monitoring of internal controls. Full implementation will be completed by 31 March 2014.

Work on monitoring progress

The Secretariat has monitored departmental progress on internal controls over financial reporting, but has not acted on delays

1.25 In 2011, we recommended that the Treasury Board of Canada Secretariat (the Secretariat), including the Office of the Comptroller General (OCG), continue to review the implementation of the requirements of the Policy on Internal Control and that this should include monitoring the departments' established timelines for completing their risk-based assessments. We noted that the Secretariat was satisfactorily providing ongoing support and guidance to assist departments in implementing the requirements of the Policy. The Secretariat agreed with the recommendation.

1.26 Our audit work related to OCG's monitoring of progress included interviews with Secretariat staff, a review of documentation, and an examination of a sample of the results of the Secretariat's key process for monitoring departmental progress in assessing their internal controls to determine if the Secretariat had satisfactorily addressed our recommendation.

1.27 Responsibilities of the Comptroller General. The Policy on Internal Control states that the Comptroller General is responsible for, among other things, overseeing the effectiveness of the system of internal controls over financial reporting across the government; monitoring that appropriate and timely action is being taken to address significant issues identified in the departments' annual public reporting in the Statement of Management Responsibility Including Internal Control Over Financial Reporting (the Statement); and recommending corrective action when a department has not complied with the requirements of the Policy.

1.28 The Policy also provides that, if the Comptroller General of Canada determines that there are significant issues in complying with the Policy, he or she may request that the deputy head of a department conduct an audit or review to assess whether the requirements of the Policy have been met, take corrective action if necessary, and report back on the results achieved. If there is a failure to remedy any non-compliance, the Comptroller General may make a recommendation to Treasury Board to address the issue.

1.29 Monitoring by the Comptroller General. Monitoring by the Office of the Comptroller General (OCG) mainly included reviewing what the departments had reported in the annex accompanying each statement as part of the Comptroller General's annual Management Accountability Framework assessment. We found that, overall, for the departments we audited, this document provided a good picture of their progress in completing this work. We also noted that the OCG engaged departments—for example, through meetings with deputy chief financial officers and through various workshops. In addition, monitoring and guidance by the OCG included providing advice on related topics, creating a dedicated website to assist departments, and facilitating the sharing of information.

1.30 The OCG told us during this audit that, since the Policy does not prescribe timelines for completing the first full risk-based assessment of internal controls over financial reporting, the OCG does not consider changes to timelines to be non-compliant with the Policy, and therefore the OCG did not act on the changes.

1.31 Overall progress. In 2011, the Secretariat, including the OCG, agreed with our recommendation to monitor established timelines for completing this work. However, as noted above, the OCG told us that it does not believe it is responsible for acting on departments' timelines, including any delays, as there are no timelines in the Policy. As noted in this report, we concluded that for most departments, progress has been unsatisfactory. The recommendation in our 2011 report stated that the OCG should monitor whether departmental actions are appropriate and timely, and therefore we expected that the OCG would have taken action on these delays. While recognizing the responsibility of departments to do this work, the OCG has an important oversight role related to the completion of this work by departments. Therefore, as noted in Exhibit 1.6, our assessment is that the progress of the Secretariat, including the OCG, against our 2011 recommendation has been unsatisfactory.

1.32 Importance of acting on the departments’ status in completing this work. In our view, given that many of the departments have timelines for completing their assessments of internal controls over financial reporting that are years away, the Comptroller General should work with the departments to address getting this work done. This is important because the departments cannot be fully satisfied that internal controls over financial reporting are effective until they have completed this work.

Exhibit 1.6 Treasury Board of Canada Secretariat’s progress in addressing our recommendation is unsatisfactory

2011 Recommendation	Progress
<p>The Treasury Board of Canada Secretariat should continue to review the departments’ implementation of the Treasury Board Policy on Internal Control to support the effectiveness of internal controls for financial reporting across government. This should include monitoring the departments’ established timelines for completing their risk-based assessments of these controls. The Secretariat should also monitor the departments’ actions to address significant issues identified as a result of their assessments, including monitoring that the actions are appropriate and timely.</p> <p>(Recommendation 1.26 of the June 2011 Status Report of the Auditor General of Canada, Chapter 1—Financial Management and Control and Risk Management)</p>	<p>Unsatisfactory</p>

Satisfactory—Progress is satisfactory, given the significance and complexity of the issue, and the time that has elapsed since the recommendation was made.

Unsatisfactory—Progress is unsatisfactory, given the significance and complexity of the issue, and the time that has elapsed since the recommendation was made.

1.33 Recommendation. The Office of the Comptroller General of Canada should work with Aboriginal Affairs and Northern Development Canada; Foreign Affairs, Trade and Development Canada; Human Resources and Skills Development Canada; Transport Canada; and Veterans Affairs Canada to see that the first full risk-based assessments of internal controls over financial reporting, the identification and the addressing of gaps and weaknesses, and the implementation of a program of ongoing monitoring, as applicable, are completed without delay.

Treasury Board of Canada Secretariat’s response. Agreed. Consistent with its responsibilities as set out in the Policy on Internal Control (the Policy), the Office of the Comptroller General (OCG) will continue to work with Aboriginal Affairs and Northern Development Canada;

Foreign Affairs, Trade and Development Canada; Human Resources and Skills Development Canada; Transport Canada; and Veterans Affairs Canada on the completion of risk-based assessments of internal controls. It will do so in a manner that fully respects the responsibilities of deputy heads for implementing the Policy and setting appropriate timelines for the assessments. Specific attention will be paid to determining whether any significant changes in the implementation plans are warranted and to supporting departments to address any issues that are identified. The engagement of these five departments on these issues by the OCG will be completed by 31 March 2014.

Conclusion

1.34 We concluded that overall progress in addressing our 2011 recommendations has been unsatisfactory. Though the departments have been working to implement the requirements of the Policy on Internal Control over financial reporting, only Agriculture and Agri-Food Canada and Finance Canada had completed the work. The other five departments should ensure they complete this work without delay.

1.35 The Treasury Board of Canada Secretariat, including the Office of the Comptroller General (OCG), has provided guidance and support to departments to assist them in completing their work on internal controls. However, in terms of the monitoring role of the Treasury Board of Canada Secretariat, while the OCG is aware of departments' progress in completing this work, it does not view responding to departmental timelines and delays as part of its role. As a result, although it was aware of the delays and of the departments' revised timelines, it did not act on that information to help ensure the timely completion of this work.

1.36 We believe the OCG should work with departments to see that the remaining work is completed without delay.

About the Audit

All of the audit work in this chapter was conducted in accordance with the standards for assurance engagements set out in *The Canadian Institute of Chartered Accountants Handbook—Assurance*. While the Office adopts these standards as the minimum requirement for our audits, we also draw upon the standards and practices of other disciplines.

As part of our regular audit process, we obtained management's confirmation that the findings reported in this chapter are factually based.

Objective

The audit objective was to determine whether the Treasury Board of Canada Secretariat (the Secretariat) and the seven selected departments had made satisfactory progress toward addressing the two recommendations on internal controls over financial reporting in our 2011 Status Report of the Auditor General of Canada, Chapter 1—Financial Management and Control and Risk Management, and whether these departments had since implemented the Policy on Internal Control.

Scope and approach

The audit covered the Secretariat, which includes the Office of the Comptroller General (OCG), as well as the following seven large departments, which together represent about 60 percent of government expenditures:

- Agriculture and Agri-Food Canada;
- Department of Finance Canada;
- Foreign Affairs, Trade and Development Canada;
- Human Resources and Skills Development Canada;
- Aboriginal Affairs and Northern Development Canada;
- Transport Canada; and
- Veterans Affairs Canada.

On 26 June 2013, the *Economic Action Plan 2013 Act, No. 1* received Royal Assent. That Act effectively merged the Canadian International Development Agency (CIDA) and Foreign Affairs and International Trade Canada into a new department: Foreign Affairs, Trade and Development Canada. The audit work conducted was done in Foreign Affairs and International Trade Canada before it was replaced by Foreign Affairs, Trade and Development Canada. The audit work did not include CIDA, as it was not part of the Department when we conducted our audit work.

At the end of our examination phase, the name Human Resources and Skills Development Canada (HRSDC) changed to Employment and Social Development Canada (ESDC). There was no impact to our audit work and findings.

The audit approach included

- interviews with staff in the selected departments and the Secretariat;
- review and analysis of documentation in support of actions taken on the two recommendations;
- examination of a sample of the departments’ own assessments of key internal controls (21 to 45 controls were selected for each department, depending on the total number of key controls tested by each); and
- examination of a sample of 19 reviews performed by the OCG of departments’ progress in assessing internal controls as reported annually by each department in its Annex to the Statement of Management Responsibility Including Internal Control Over Financial Reporting.

We did not assess internal controls within the selected departments and therefore offer no assurance on the effectiveness of these controls over financial reporting.

Criteria

Criteria	Sources
<p>To determine whether Treasury Board of Canada Secretariat and the seven selected departments have made satisfactory progress toward addressing the two recommendations on financial controls in the 2011 June Status Report of the Auditor General of Canada, Chapter 1, and whether they have now implemented the Policy on Internal Control, we used the following criteria:</p>	
<p>The Treasury Board of Canada Secretariat monitors departmental compliance with the Policy on Internal Control, and with related directives and standards and the overall state of financial control government-wide.</p>	<ul style="list-style-type: none"> • Policy on Internal Control, Treasury Board, 2009 • Framework for the Management of Compliance, Treasury Board, 2009 • 2011 June Status Report of the Auditor General of Canada, Chapter 1—Financial Management and Control and Risk Management, Recommendation 1.26 and related response of the Secretariat
<p>The selected departments assess the effectiveness of their systems of internal controls for financial reporting and ensure that it is maintained, monitored, and reviewed, with timely corrective measures taken when issues are identified.</p>	<ul style="list-style-type: none"> • Policy on Internal Control, Treasury Board, 2009 • Policy on Financial Management Governance, Treasury Board, 2009 • 2011 June Status Report of the Auditor General of Canada, Chapter 1—Financial Management and Control and Risk Management, Recommendation 1.25 and related response of the departments

Management reviewed and accepted the suitability of the criteria used in the audit.

Period covered by the audit

The audit covered the period between 1 November 2012 and 31 March 2013. To properly understand the current context and the progress made by departments and the Secretariat in response to the recommendations, the audit team also reviewed and considered documentation, information, and decisions made before this period. Audit work for this chapter was completed on 23 August 2013.

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Appendix List of recommendations

The following is a list of recommendations found in Chapter 1. The number in front of the recommendation indicates the paragraph where it appears in the chapter. The numbers in parentheses indicate the paragraphs where the topic is discussed.

Recommendation	Response
<p>Internal controls over financial reporting</p> <p>1.24 Foreign Affairs, Trade and Development Canada; Human Resources and Skills Development Canada; Aboriginal Affairs and Northern Development Canada; and Transport Canada should complete their assessments of internal controls within the planned timelines, including addressing gaps and weaknesses. In addition, these four departments and Veterans Affairs Canada should fully implement a program of ongoing monitoring without delay. (1.15–1.23)</p>	<p>Aboriginal Affairs and Northern Development Canada, Human Resources and Skills Development Canada, and Transport Canada’s response. Agreed. Aboriginal Affairs and Northern Development Canada, Human Resources and Skills Development Canada, and Transport Canada recognize the importance of completing the testing of internal controls over financial reporting, addressing gaps and weaknesses, and implementing a program for ongoing monitoring of these controls, while working on other equally important priorities.</p> <p>Each department has put in place systems for internal controls over financial reporting, including requirements for internal reconciliations and analysis, and post-verification reviews. Work is under way to ensure that these and other internal controls are operating effectively to mitigate risk.</p> <p>Building on concrete steps taken to date, the departments will undertake to complete their first full risk-based assessments of internal controls over financial reporting, including identifying and addressing gaps and weaknesses in internal controls by 31 March 2015, 31 March 2016, and 31 March 2014 respectively. As the initial assessment for each key process is completed, Aboriginal Affairs and Northern Development Canada, Human Resources and Skills Development Canada, and Transport Canada will implement a program for continuous monitoring of their internal controls over financial reporting.</p>

Recommendation	Response
	<p>Foreign Affairs, Trade and Development Canada’s response. Agreed. Foreign Affairs, Trade and Development Canada agrees that it is important to complete the testing of internal controls over financial reporting, address gaps and weaknesses, and implement a program for ongoing monitoring of these controls. However, due to recent changes enacted by legislation, the Department must reconsider its current implementation plans, including timelines. <i>Economic Action Plan 2013 Act, No. 1</i>, the Act that implemented the merger of the Department of Foreign Affairs and International Trade and the Canadian International Development Agency, received Royal Assent on 26 June 2013, creating the new Department of Foreign Affairs, Trade and Development (DFATD). As a result, the existing implementation plans for both former entities will be merged, and a new planned completion date for DFATD will be determined. DFATD is committed to ensuring that the requirements of the Policy on Internal Control are fully implemented by the new completion date.</p> <p>Veterans Affairs Canada’s response. Agreed. Veterans Affairs Canada is actively implementing its program for the continuous monitoring of internal controls. Full implementation will be completed by 31 March 2014.</p>
<p>Work on monitoring progress</p> <p>1.33 The Office of the Comptroller General of Canada should work with Aboriginal Affairs and Northern Development Canada; Foreign Affairs, Trade and Development Canada; Human Resources and Skills Development Canada; Transport Canada; and Veterans Affairs Canada to see that the first full risk-based assessments of internal controls over financial reporting, the identification and the addressing of gaps and weaknesses, and the implementation of a program of ongoing monitoring, as applicable, are completed without delay. (1.25–1.32)</p>	<p>Treasury Board of Canada Secretariat’s response. Agreed. Consistent with its responsibilities as set out in the Policy on Internal Control (the Policy), the Office of the Comptroller General (OCG) will continue to work with Aboriginal Affairs and Northern Development Canada; Foreign Affairs, Trade and Development Canada; Human Resources and Skills Development Canada; Transport Canada; and Veterans Affairs Canada on the completion of risk-based assessments of internal controls. It will do so in a manner that fully respects the responsibilities of deputy heads for implementing the Policy and setting appropriate timelines for the assessments. Specific attention will be paid to determining whether any significant changes in the implementation plans are warranted and to supporting departments to address any issues that are identified. The engagement of these five departments on these issues by the OCG will be completed by 31 March 2014.</p>

