



Agriculture and  
Agri-Food Canada

Agriculture et  
Agroalimentaire Canada



# REPORT: AgrilInsurance Program Audit

Office of Audit and Evaluation

The AAFC Audit Committee recommended this audit report for approval by the Deputy Minister on March 12, 2014.

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## EXECUTIVE SUMMARY

As part of Agriculture and Agri-Food Canada's (AAFC) suite of Business Risk Management (BRM) programming, AgrilInsurance is a federal-provincial-producer cost-shared program established to mitigate the financial impacts of production losses by providing insurance protection.

The federal role in the AgrilInsurance program is primarily comprised of five activity streams:

- Processing provincial claims for federal premiums and administration costs.
- Analyzing provincial proposals for insurance plans.
- Preparing Federal/Provincial Agreements.
- Actuarial Certifications.
- Federal Crop Reinsurance Fund management.

At AAFC, AgrilInsurance is managed within the Programs Branch, Production Insurance and Risk Management Division (PIRMD). The BRM Financial Services and Administrative Unit provides support to PIRMD.

The audit of the AgrilInsurance Program was included in AAFC's 2013-2016 Risk-Based Audit Plan.

The audit indicated that effective controls were generally in place to support the administration and monitoring of AgrilInsurance payments and appropriate monitoring controls were designed related to program self-sustainability.

A recommendation was made related to reviewing the recipient audit criteria to ensure that they meet future program needs.

## 1.0 INTRODUCTION

### 1.1 BACKGROUND

- 1.1.1 Production insurance programming has existed since the 1950s. In 2007-2008, the programs under the federal-provincial-territorial *Growing Forward* multilateral framework agreement were initiated. The agreement defines the policy framework that includes the Business Risk Management (BRM) suite of programs, which are designed to assist farmers to manage the risk of production losses.
- 1.1.2 As part of the BRM suite of programming, AgrilInsurance is a federal-provincial-producer cost-shared program established to mitigate the financial impacts of production losses by providing insurance protection. It minimizes production and asset losses caused by severe but uncontrollable hazards like drought, flood, wind, frost, excessive rain, heat, snow, uncontrolled disease, insect infestations and wildlife. Producers receive indemnity payments when they experience a production loss during the year. The indemnity payments are made from the provincial insurance account and are composed of premium payments shared by the federal and provincial governments and producers. The program is available in all provinces and each province has either a Crown Corporation or a branch of the provincial agricultural department responsible for administering the AgrilInsurance program.
- 1.1.3 The federal role in the AgrilInsurance program is primarily comprised of five activity streams:

#### **1. Processing provincial claims for federal premiums and administration costs.**

The program is cost-shared with provinces that deliver the program to their producers. Provincial claims are received, assessed and processed for payment.

AAFC shares a national production insurance statistical system (PINSS) with the provinces which contains data on provincial plans across Canada. The system makes national program information available and governments use it to provide timely information and payments.

#### **2. Analyzing provincial proposals for insurance plans.**

The provinces submit proposals for new and/or amended insurance plans to the federal government for their assessment against program authorities. These proposals can either enhance existing coverage or provide new coverage to their producers.

### **3. Preparing Federal/Provincial Agreements.**

The Operational Document is an appendix to the Federal/Provincial Agreement and is administrative in nature. It outlines the plans by agricultural products, as well as the coverage, program details and obligations of each party. The document also describes the actuarial certification documents and schedule of the self-sustainability, probable yield methodology, and premium rate methodology. An Operational Document is prepared by each province and reviewed by AAFC. A new Operational Document is prepared and signed when a province makes changes to its insurance plans, but not more frequently than once per year.

### **4. Actuarial Certifications.**

As per the Crop Insurance Regulations, each province is required to obtain independent actuarial certifications every five years on the soundness of the probable yield methodologies, premium rate methodologies, and the self-sustainability of its Crop Insurance Fund. AAFC's actuaries within the Production Insurance and Risk Management Division review the provincial actuarial certifications.

### **5. Federal Crop Reinsurance Fund management.**

AAFC has agreements in place with specific provinces to provide them with loans when crop loss claims for a specific year exceed the balance in the province's crop insurance fund.

The reinsurance fund is held within the Consolidated Revenue Fund and AAFC sets reinsurance rates in collaboration with the provinces to make sure reinsurance programs are self-sustainable. The final report on reinsurance rates is reviewed by an independent actuarial firm before it is sent to the Department of Finance as the reinsurer.

1.1.4 At AAFC, AgrilInsurance is managed within the Programs Branch, Production Insurance and Risk Management Division (PIRMD). The BRM Financial Services and Administrative Unit provides support to PIRMD.

1.1.5 The Audit of the AgrilInsurance Program was included in AAFC's 2013-2016 Risk-Based Audit Plan.

## **1.2 AUDIT OBJECTIVE**

1.2.1 The objective of the audit was to assess the effectiveness of the administration and monitoring controls for AgrilInsurance Payments to the provincial governments, and the management controls in place to ensure the self-sustainability of the program.

### **1.3 AUDIT SCOPE**

- 1.3.1 The internal audit examined the AgrilInsurance Program and Federal Crop Reinsurance Fund, as defined by the Growing Forward multilateral agreement in 2007-2008 and ending in 2012-2013. The AgrilInsurance Program defined by the Growing Forward 2 (GF2) multilateral agreement was not included in audit testing, but will be considered for inclusion in future Risk-Based Audit Plans.
- 1.3.2 The audit scope included only those areas under federal responsibility. Therefore, the design and delivery of provincial crop insurance programming that receives funding under AgrilInsurance was not included in the audit. Also, the audit scope did not include the Wildlife Compensation programming related to AgrilInsurance. This is a separate auditable entity and will be considered as part of future risk-based audit planning processes.
- 1.3.3 Audit criteria are presented in Annex A of this report.

### **1.4 AUDIT APPROACH**

- 1.4.1 The audit approach and methodology was risk-based and consistent with the *International Standards for the Professional Practice of Internal Auditing* and the *Internal Auditing Standards for the Government of Canada*, as required under the TBS' *Policy on Internal Audit*.
- 1.4.2 Internal Audit performed the following reviews:
- Planning Phase: Internal Audit conducted a risk assessment to determine the audit's objective and scope. The results of OAE's program evaluation of the AgrilInsurance program were considered in the planning of this audit engagement. Based on the risk assessment, the audit criteria and audit program were developed for use in the audit's conduct phase.
  - Document Review: Internal Audit assessed key program documentation to obtain an understanding of the program operations, including the tools/templates used by program staff and examples of reports prepared by program management.
  - File Review: Internal Audit selected a sample of 50 claims and payments, 17 associated holdbacks, 5 Payables-At-Year-End (PAYEs), 5 confirmation letters and 2 recipient audit reports to review. Samples were selected for the time period of November 2011 to March 2013 in order to select files completed after the establishment of the BRM Finance and Administrative Services Unit.

- Interviews: Internal Audit conducted interviews with members of program staff and management, program financial staff (BRM Finance and Administrative Services Unit), and the Service and Program Excellence Directorate (SPED) Recipient Audit Unit (RAU).

1.4.3 The audit fieldwork took place from August to November 2013.

## **1.5 CONCLUSION**

- 1.5.1 The audit indicated that effective controls were generally in place to support the administration and monitoring of AgrilInsurance payments and appropriate monitoring controls were designed related to program self-sustainability.
- 1.5.2 A recommendation was made related to reviewing the recipient audit criteria to ensure that they meet future program needs.

## **1.6 STATEMENT OF CONFORMANCE**

- 1.6.1 In the professional opinion of the Chief Audit Executive, sufficient and appropriate audit procedures have been conducted and evidence gathered to support the accuracy of the conclusion provided and contained in this report. The conclusion is based on a comparison of the conditions, as they existed at the time, against pre-established audit criteria that were agreed on with management. The conclusion is applicable only to the entity examined.
- 1.6.2 This audit conforms with the *Internal Auditing Standards for the Government of Canada*, as supported by the results of the quality assurance and improvement program.



## **2.0 DETAILED OBSERVATIONS, RECOMMENDATIONS AND MANAGEMENT RESPONSES**

2.0.1 This section presents the key observations, based on the evidence and analysis associated with the audit, and provides recommendations for improvement.

2.0.2 Management responses are included and provide:

- An action plan to address each recommendation
- A lead responsible for implementation of the action plan, and,
- A target date for completion of the implementation of the action plan.

### **2.1 ROLES AND RESPONSIBILITIES AND POLICY DISCUSSIONS**

2.1.1 AAFC interfaces with the provinces on several different levels related to AgrilInsurance. The foundation of the working relationship is defined by the production insurance legislation, the *Growing Forward* Multilateral Agreement, and bilateral agreements with the provinces. Operational Documents define the insurance plans for each province on provisions related to areas such as Yield-based Coverage, Non-Yield-based Coverage, and Estimate of Provincial Weighted Average Harvested Yield for each agricultural product, and estimated administrative costs.

2.1.2 AAFC and the provinces discuss policy matters at the AgrilInsurance Working Group and the Business Risk Management Policy Working Group. The documented Terms of Reference for these working groups had clear rules for composition, mandate and processes. The working group minutes showed evidence of discussions related to the program's objectives, parameters and affordability.

### **2.2 PROGRAM DATABASE AND ELECTRONIC PROCESSING SYSTEM**

2.2.1 The Production Insurance National Statistical System (PINSS) application is a web-based interface developed by AAFC and used by provincial crop insurance agencies and corporations and AAFC to submit and process Production Insurance, Wildlife, and Reinsurance claims and related statistical information, and to access reports.

2.2.2 The audit reviewed the design of key controls related to the verification and approval of contribution payments and the tracking of program expenditures. The audit did not include testing the effectiveness of system controls.

2.2.3 Information provided by the database administrators indicated that:

- Audit trails are automatically produced within PINSS and cannot be turned off. Although audit trails do not capture field-level changes or

monitor keystrokes, the audit file review demonstrated that mitigating payment controls and sign-offs were in place for the audit sample.

- No data retention policy is in place for PINSS data; however, as there is no technical need to archive the data and due to the historical nature of insurance programming, all data is considered active and must be retained.
- Automatic incremental data back-ups are performed daily and the entire database is backed-up weekly. Back-ups are moved to an off-site storage facility within a few days.
- Special business procedures and approvals are defined in PINSS to reverse transactions, correct errors and re-process transactions.
- Basic data validation rules are in place to prevent incorrect data entry.

2.2.4 All PINSS users are assigned to profiles that define their roles and the nature of their system access. The audit team validated that generic users do not have edit-access to the system.

2.2.5 The PINSS system electronically interfaces with the departmental financial system (SAP SATURN). Reconciliations of PINSS data and SAP SATURN data are performed on a quarterly basis by the BRM Finance and Administrative Services Unit. The reconciliations are reviewed and approved by the PIRMD Director.

2.2.6 Systems changes are prioritized by the PINSS Steering Committee and are dependent on funding being available in the PINSS budget. Annual budgets are prepared based on project application maintenance costs and any enhancements that are planned. When the PINSS budget is finalized, the PIRMD Director signs a cost recovery agreement with the Information Services Branch (ISB). The cost for all system upgrades performed on PINSS is tracked by ISB and this information is provided to the program monthly. In addition, the cost of application maintenance is reported to the program on a quarterly basis. When a change to PINSS is made, it is requested by program staff and performed by the database administrators. These changes are then tested by program staff, independent of the database administrators who created the changes. Testing is performed in a separate, production-like environment before being approved by program staff and being moved into production.

## 2.3 PRODUCTION INSURANCE CONTRIBUTION PAYMENTS

2.3.1 **Verification and Approval of Contribution Payments:** Claims are submitted by the provinces via PINSS to PIRMD for review and approval. The claims payment process for AgriInsurance is documented and communicated to program staff. Clear roles and responsibilities are described for program support staff, financial analysts, operations staff, actuarial personnel, the Chief of Finance, and the PIRMD Director.

- 2.3.2 The audit team assessed a sample of 50 production insurance premium claims and found that appropriate review and authorization were documented within the PINSS system. Section 34 Financial Administration Act (FAA) approval was clearly indicated and performed by authorized individuals. The audit team also confirmed that the amounts recorded in PINSS reconciled with the amounts recorded in SATURN.
- 2.3.3 AgrilInsurance is a cost-shared program, with premium costs allocated between the federal government, provincial governments and producers. The prescribed cost-sharing ratio is applied on a claim-by-claim basis and is calculated in the PINSS system. The cost-sharing ratio is also monitored via PINSS reports on a provincial level.
- 2.3.4 The program is permitted to apply several types of holdbacks on premium payments. These amounts are calculated automatically by the PINSS system and are reviewed and approved as part of the documented step-approval process for claims payments. The PINSS system has reporting capabilities to track federal holdbacks, releases and ineligible amounts by claim. The audit team reviewed the approval process for the 17 claims with holdbacks in the sample of Production Insurance claims and found that the claims showed evidence of appropriate review and authorization by program management.
- 2.3.5 Annually, provinces submit an administrative cost budget. The BRM Finance and Administrative Services Unit assesses the budget against historical actual costs to determine if the budget is reasonable. Quarterly updates and reviews are also completed to monitor administrative expenses throughout the year. Based on the program's history, the BRM Finance and Administrative Services Unit has established variance tolerances in order to assess fluctuations in costs. However, there are no limitations on administrative costs set out by the *Growing Forward* Multilateral Agreement. Administrative expenses are categorized within PINSS and the system requires a variance explanation when amounts exceed budget by more than 10 percent. For capital expenditures, provinces are required to submit a business case to justify these expenses. Within the sample reviewed, five administrative expense claims from three provinces were assessed and it was observed that the review and approval steps are similar to program expense claims, with the exception of not requiring an actuarial review.
- 2.3.6 **Payables- At-Year-End:** The BRM Finance and Administrative Services Unit provides each province with a customized template to complete on an annual basis with information related forecasts for premiums and administrative expenses, as well as Payables-At-Year-End (PAYE) from prior periods. The BRM Finance and Administrative Services Unit then transfers the data onto spreadsheets and it is analyzed and approved by

PIRMD. PAYE amounts are calculated based on claims data stored in the PINSS system. Once approved, PAYEs are set up in PINSS and SATURN.

- 2.3.7 The audit team reviewed the processes followed to assess the reasonableness of provincially submitted data and confirmed that processes were in place to request and receive provincial confirmations. Variances were calculated to assess the reasonableness of financial information (e.g. actual expenditures compared to budgeted amounts or statistic amounts). There was evidence of PAYE calculations being performed, as well as review and approval by program management, including Section 34 FAA certification.

## 2.4 FINANCIAL MONITORING, RECIPIENT AUDIT, AND ACTUARIAL CERTIFICATION

- 2.4.1 **Audited Financial Statements:** As per the *Growing Forward* agreements, the provinces are required to submit audited financial statements annually. The BRM Finance and Administrative Services Unit reconciles these statements with SATURN and PINSS information. Audited financial statements were submitted by nine of 10 provinces for fiscal year 2011-2012. For the nine financial statements received, there was evidence of review and reconciliation of figures by the BRM Finance and Administrative Services Unit. For the one province that did not yet submit financial statements, holdbacks were applied.
- 2.4.2 **Recipient Audit:** Under *Growing Forward*, section 17.3 imposed a requirement to perform a compliance audit at least every five years.<sup>1</sup> All provinces were audited between 2009-2010 and 2012-2013.<sup>2</sup> Audit interviews indicated that these recipient audits were performed using a standard statement of work and that risk assessments and actuarial reviews, together with the standard statement of work, were used to establish the scope of the audits.
- 2.4.3 The audit team reviewed the two recipient audits completed since November 2011. The audit team validated that the auditors contracted to perform the recipient audits were not the same auditors who performed the financial statements audits of the recipient organizations. In both audits, criteria were clearly stated and specific to the AgrilInsurance Program. Internal Audit noted that the criteria did not include an assessment of the investment strategies used by provinces to invest insurance program account funds. PIRMD had also identified a need to expand the scope of recipient audits to include verification that the provinces are properly applying actuarial certification guidelines. Because this is a specialized type of work not readily available

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<sup>1</sup> Note that under *Growing Forward* 2, recipient compliance audits are to be performed periodically.

<sup>2</sup> Additional audits were scheduled to be completed on four provinces in 2013-2014.

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through contracting, AAFC's actuarial team will conduct this portion of recipient audits in the future.

- 2.4.4 It would be timely to review the recipient audit criteria to ensure that the compliance audits provide the information needed for effective monitoring under GF2.

**2.4.5 Recommendation 1: The ADM Programs Branch should review the recipient audit criteria in order to meet future AgrilInsurance program needs.**

*Management Response and Action Plan:* Agreed. The DG of BRM Program Development will review the compliance audit standard audit criteria to ensure that they meet the requirements of the new GF2 Multilateral Framework Agreement (MFA). Province specific audit criteria will continue to be included to address specific observations in provinces.

Audit criteria will be developed to ensure provincial management of the Fund (i.e. investments) is compliant, and actuarial staff will develop audit criteria to determine whether actuarial guidelines/methodologies are being properly used by provinces.

*Lead(s) Responsible:* DG, BRM Program Directorate

*Target Date for Completion:* June 2014

## **2.5 FEDERAL REINSURANCE FUND MANAGEMENT**

- 2.5.1 **Reinsurance Fund Monitoring:** Program management provides an update on the status of the federal reinsurance fund to Finance Canada twice annually. In addition, AAFC provides new reinsurance rates to Finance Canada prior to their implementation.

- 2.5.2 As part of monitoring, the program reviews the provincial actuarial certifications. In addition, program management instituted a process of third-party actuarial review to perform:

- Peer review (including an actuarial opinion) of the methodology and the models developed by PIRMD to determine Federal and Provincial reinsurance rates for AB, SK, MB, NB and NS and recommend modifications as needed.
- Peer review (including an actuarial opinion) of the self-sustainability assessment of the Federal Crop Reinsurance Fund prepared by PIRMD and recommends modifications as needed.
- Comments on the recommendations made by PIRMD on reinsurance rates and structure.

- 2.5.3 As noted earlier, the BRM Finance and Administrative Services Unit requests an annual update from the provinces regarding whether or not they intend to forward additional Reinsurance Premiums to the Reinsurance Fund of Canada, over and above the Reinsurance deducted from previously submitted AgriInsurance claims. This confirmation is intended to identify potential Receivables-At-Year-End (RAYEs) that need to be recorded in SATURN.
- 2.5.4 The audit team reviewed the accounts receivable confirmation letters to the provinces for 2012-2013. All provinces with reinsurance agreements indicated that no additional Reinsurance Premiums were going to be submitted so no RAYEs were necessary.
- 2.5.5 **Processing Reinsurance Claims:** Reinsurance claims are processed in the PINSS systems with the same type of claims processing as production insurance claims. The audit team reviewed the PINSS data for the two reinsurance claims paid between 2010-11 and 2012-13 and noted that the required review and approval steps were conducted, including no holdbacks applied since audited financial statements were received.
- 2.5.6 No provinces entered into a reinsurance agreement with the federal government during the auditable period, therefore internal audit did not assess the implementation of this process.

## **ANNEX A: AUDIT CRITERIA**

- 1.0 An effective monitoring regime is in place for the verification and approval of AgrilInsurance program payments to provincial delivery organizations.
- 2.0 The various risks impacting the operation of the AgrilInsurance program have been identified and mitigated through appropriate controls, including risks related to payments to producers and the self-sustainability of the program.
- 3.0 PINSS supports complete and accurate information for use in the administration and monitoring of AgrilInsurance payments.
- 4.0 The federal governance structure and communications strategy for interfacing with the provinces is adequate.
- 5.0 An adequate system of controls is in place to administer the Federal Crop Reinsurance Fund.