



# OFFICE OF THE PROCUREMENT OMBUDSMAN



## CHAPTER 2

### PROCUREMENT PRACTICES REVIEW

### *DEPARTMENTAL VERIFICATION OF SUPPLIERS' RECORDS TO VALIDATE CONTRACT PAYMENTS*

OTTAWA  
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STRENGTHENING THE CONFIDENCE OF CANADIANS IN PUBLIC PROCUREMENT

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## Executive Summary

2.1 The Government of Canada buys goods and services from many different suppliers through contracts worth about \$14 billion a year. Like any household, the government incurs bills that must be paid. Before paying bills, Canadian taxpayers look at the invoices they have been sent to make sure they are accurate and fair. The Government of Canada does the same thing, but the government's purchases are large and complex and many departments may be involved.

2.2 While the government is committed to procurement that is fair, open and transparent, there are a number of risks it has to manage. The use of audit, inspection and examination of supplier records upholds the principles by demonstrating the price being paid is fair and reasonable. This is true, especially in cases of high-risk contracts such as large cost-reimbursable contracts where the price is not determined until after the work is done and the amount to be paid under the contract can vary with a number of factors.

2.3 The Financial Administration Act (FAA), legislated by Parliament, sets out the procedures the Government of Canada is expected to follow in managing taxpayers' money. Before a payment is made, the FAA says that the government's program managers must make sure that work specified in contracts has actually been done, that goods or services have been received and that the amount charged agrees with the price written in the contract. If the contract does not state a firm price, program managers are expected to see that the amount invoiced is reasonable before a payment is approved. If an error occurs in the process and a supplier is paid more than the amount that was due, the FAA requires that the overpayment be collected and the money returned to the government.

2.4 The government processes millions of invoices a year, and there is a risk of making an incorrect payment if an invoice was prepared or paid incorrectly. The government recognizes these risks and has developed mitigating strategies. One of the ways it manages the risk of incorrect payment, and the need to later recover overpayments, is to incorporate audit provisions – referred to in this report as the “audit provision” – in contracts. Of the tens of thousands of contracts that the Government of Canada issues every year, most provide for the examination, inspection or audit of the suppliers' books and records. The government can and does include an audit provision in its contracts to the effect that the government has the right to conduct reviews, inspections and audits and recover overpayments or payments made in error. Included in the terms of the contract, suppliers are required to keep detailed documentation, such as time sheets or contracts with subcontractors, for six years.

2.5 These audits provide assurance that the contracts do not contain a material amount of loss to the Crown due to excessive profits or inaccurate or unreasonable costing practices; deter contractors from initiating unacceptable practices by maintaining a sufficient level of audit presence; and provide quality control information on the acquisitions process, including contract management. The risk of excess charges could

be mitigated by the undertaking of cost audits, as appropriate, which is authorized in clear audit provisions of the terms and conditions of contracts.

2.6 This year, the Office of the Procurement Ombudsman (OPO) reviewed whether government procurement managers are effectively using departmental verification of suppliers' records to ensure correct contract payments as a means to maintaining fairness, openness and transparency in the procurement of goods and services. The period of review was from April 1, 2007, to January 5, 2010. This review looked at eight departments and agencies chosen for their size and their contracting activity: Public Works and Government Services Canada (PWGSC), National Defence, Foreign Affairs and International Trade, Agriculture and Agri-Food Canada, Canadian Heritage, the National Research Council of Canada, the Public Service Commission and the Canadian Nuclear Safety Commission. The review looked at whether these eight organizations included the right to audit, inspect or examine suppliers' records in their contracts and whether they actually undertook any of these activities. The review also looked at a type of contract used by the Government of Canada in special circumstances called a "cost-reimbursable contract." Audit provisions are particularly important in "cost-reimbursable" contracts.

2.7 Cost-reimbursable contracts are considered high-risk contracts because the specific price to be paid to the supplier is not known at the time the contract is signed. The amount to be paid must be calculated based on a number of factors such as the actual costs of materials, parts or subcontract work; the number of hours of labour at a fixed rate; or a volume or demand that will vary with time. Typical cost-reimbursable contracts would be for professional services at a per-hour rate or for the repair and overhaul of defence materiel, such as fixed wing aircraft or helicopters. In the latter case, the rate per hour for scheduled maintenance can be determined when the contract is signed, but the actual amount of required maintenance will depend on flying time. Some contracts specify a maximum profit percentage. These contracts may be "sole-sourced," that is, they may not go to competitive bidding. In the example of the maintenance of a specific aircraft such as the F-18 fighter, only the suppliers with proprietary rights and specialized expertise are qualified for the work and the contract may be in force for the many years of the life of the aircraft, with periodic amendments. PWGSC is the contracting authority for the majority of such cost-reimbursable contracts for itself and other government departments such as National Defence. According to PWGSC figures, there are over 4,000 such contracts awarded each year with an estimated annual dollar value of \$5 billion.

2.8 The Office of the Procurement Ombudsman's review focussed on two areas. In the first, the eight departments and agencies were contacted and questioned on their use of the audit provision. Secondly, the Office reviewed how PWGSC exercised the audit provision in cost-reimbursable contracts. The review looked at the use of audit provisions in these cost-reimbursable contracts because they often involve large amounts of money, they are often sole-sourced under one of the allowable exceptions, and the amounts payable are based on suppliers' calculations of cost or profit. Because of the large amounts involved, if overpayments were to occur, these overpayments could involve millions of dollars. In addition, as a number of these contracts are for military procurement, the program is important to the Department of National Defence

(DND) and is of interest to the U.S. military, which shares with Canada many of the same suppliers.

2.9 All eight of the organizations reviewed used a standard audit provision in the contracts where they were the contracting authority. PWGSC included the audit provision in nearly all of its own contracts and in contracts it issued on behalf of other departments. In the eight organizations examined in the first part of the review, the Office found that audit provisions were used like an “insurance” policy. The existence of an audit provision may have a deterrent effect and helps to prevent overcharging the government in the first place, but it will not be effective unless suppliers know that there is a chance of the clause being actually invoked. This clause also authorizes the recovery of overpayments or payments in error.

2.10 The eight organizations said that although all contracts included an audit provision, procurement managers had not performed any formal audits, inspections or examinations of suppliers' records during the period under review. The organizations had not issued specific guidance on how this control should be used. They had not formally considered how conducting a certain number of audits, inspections or examinations would reinforce the preventive value of the control. The organizations said that overpayments were prevented by other controls and procedures. For example, they said that financial officers closely scrutinized invoices and supporting documentation in the file for a given contract. In a limited number of cases, the clause had been used informally to obtain additional documentation from the suppliers.

2.11 Audits may be conducted at any time within a six-year period specified in a contract. Suppliers are required to keep detailed documentation during this period, including time sheets, contracts with their suppliers and subcontractors, and invoices from their supply chain. Suppliers appear to accept this requirement as part of doing business with the Government of Canada and the government's need for accountability to taxpayers. All eight organizations said that the audit provision is useful even if never formally used because both the government and the supplier know that an audit can be conducted. This promotes compliance with the terms of the contract. The effect is similar to the way a potential audit promotes taxpayers' compliance with the Income Tax Act.

2.12 During the period under review, PWGSC procurement officers had not formally invoked the audit provision for any contracts other than cost-reimbursable contracts. They had rarely used the audit provision even for high-value, complex contracts such as those for information technology projects. At the end of our review, PWGSC had prepared a draft internal audit report on Information and Technology Branch task authorization contracts, which deals with some of the topics raised in this review. Another internal audit completed by PWGSC of construction contracts recommended that the Department ensure that construction contracts include a more detailed audit provision in its standard terms and conditions, and that these audits be undertaken. We have been informed by officials at the Department of National Defence that internal audits conducted at National Defence have often recommended to PWGSC that it invoke the clause for specific contracts where there is believed to be a higher risk of overpayment. The Office recommends that PWGSC and other departments and

agencies consider invoking the audit provision in the case of high-risk, complex contracts, as is being done for cost-reimbursable contracts.

2.13 For cost-reimbursable contracts, PWGSC has for many years employed a cost audit program. This program is used to validate that the contract payments for goods and services are appropriate and assist the contracting officer in determining a final price for such contracts. The program employs Audit Services Canada (ASC), a special operating agency within the Department, to conduct the audits. Audit Services Canada produces a report that may suggest adjustments to the price to be paid, based on its interpretation of the contract requirements. The contracting officer, who is responsible for administering the contract and recommending invoices for payment, is also involved in negotiating the final price with the supplier. PWGSC is currently undertaking to clarify the process and accountability for disposing of the cost audits' suggested adjustments.

2.14 We note that PWGSC has undertaken a renewal of this program to make it more relevant and effective. In the interim, the number of audits of cost-reimbursable contracts has decreased, and mandated or required audits for cost-reimbursable contracts have become backlogged. In a number of cases, it has taken considerable time to establish the validity of the audit adjustments, which has had a corresponding effect on recovering the appropriate amounts in a timely manner. PWGSC has recognized this problem and has recently allocated additional resources to clear the backlog.

2.15 PWGSC's Cost Audit Program (CAP) for cost-reimbursable contracts represents a good practice with clear financial benefits through the recovery of overpayments to suppliers. PWGSC is currently carrying out an action plan to renew the program and implement the many needed improvements. Implementing the improvements identified and obtaining sustainable funding are crucial to the effective survival of this important program.

2.16 PWGSC has made good progress in revising its approach to cost-reimbursable contracts. However, there are some important issues that it was continuing to address at the completion of our review. One of them is to clearly identify the roles and responsibilities of all the players in the determination of the final disposition of the "audit adjustments." This is a particularly complex matter given the multitude of players involved: DND (or other department) as the department with the program and the appropriation; PWGSC as contracting authority with the concentration of duties in the hands of the contracting officer; ASC as the cost auditor (PWGSC is the employer of record for ASC employees); and of course the affected suppliers.

2.17 The vision and direction of the renewal resonate with most stakeholders as being an improvement over the current way of operating. Key proposals being considered intend to alleviate the problems of the buildup of audit backlogs due to lack of funding and unclear selection parameters; the slow recoveries due to the timing of audits; and the use of various methods of recovery that may be unauthorized. The renewed program will use a risk model to focus discretionary audit effort, with a new risk assessment methodology that goes beyond simple dollar value. Audits will occur over the whole life of a contract, not as a post-contract activity, which will be of more value to



managers approving payments under section 34 of the FAA. There will be a measure of accountability through program reporting to the Directors General Council (DG Council) under the Assistant Deputy Minister, Acquisitions Branch. To keep up with the requirement for mandatory audits and enable the Cost Audit Group (CAG) to perform discretionary audits on a risk selection basis, the renewal is working toward a multi-faceted approach to stable funding.

2.18 We were impressed with the efforts of PWGSC to strengthen the relevance, efficiency and effectiveness of its Cost Audit Program. We encourage all other government departments to review the new program framework and, where appropriate, to adapt it to their own contracting activities.

2.19 In our view, the confidence of Canadians in public procurement and the government's commitment to transparency would be strengthened by the publication of summary level results of the Cost Audit Program.

2.20 Another issue that merits further study is whether to continue the current practice of having the cost audits done exclusively by government employees or whether the program would benefit by using some of the expertise available in the private sector.

### Recommendations

2.21 As part of their account verification risk mitigation strategies, departments should include a guideline as to how and when to use the audit provision for contracts that do not fall under the auspices of CAG at PWGSC and are of a cost-reimbursable nature, taking into consideration the expectations of suppliers' record keeping and the principle of openness regarding audit suppliers.

2.22 The DG Council in the Acquisitions Branch of PWGSC should monitor the implementation of the updated action plan and report progress to senior management on a frequent basis.

2.23 In order to strengthen transparency and enhance the deterrent effect of cost audits, summary level reporting of the CAP results should be prepared and made available to the public.

All departments and agencies involved in this review were given an opportunity to review this report and their comments were taken into consideration when it was finalized.

## Introduction

### Context

2.24 The procurement or acquisition of a good or service involves a number of steps. These entail the pre-contractual phase, which includes activities related to the identification of a need and the definition of requirements; the contracting phase, which includes the bid solicitation and contract award process; the contract administration phase, which includes contract amendments, monitoring progress, following up on delivery and payment action; and the post-contractual phase, which includes final actions such as proof of delivery and the completion of financial audits. Contracts are let either under the authority of PWGSC or subject to financial limitations under the authority of individual departments.

2.25 Under section 34 of the Financial Administration Act (FAA), program managers are delegated authority to certify that the work has been performed, the goods supplied or the service rendered, as the case may be, and that the price charged is according to the contract or, if not specified in the contract, is reasonable, before a payment can be issued. The FAA also requires that all identified overpayments be collected.

2.26 Under Treasury Board's Policy Directive on Account Verification (in effect until October 2009),

"It is government policy to pay on time, neither early nor late, amounts that represent a legitimate obligation and are correct. Account verification processes are to be designed and operated in a way that will maintain probity while taking into consideration the varying degrees of risk associated with each payment."

2.27 For the purposes of this review, we categorized government contracts into two main bases of payment:

- Those that are considered to be firm price: This type provides for a price, which is not subject to adjustment, for performance of the contract or part of it. It gives maximum profit incentive to the contractor for cost control in that the contractor assumes full responsibility for all costs under or over the firm price. In addition, it places a minimum administrative burden on both contracting parties. A simple example would be a purchase of furniture for an agreed-upon firm price.
- Contracts that are considered to be cost-reimbursable: For these contracts, the final price to be paid to the supplier is not known at the time the contract is signed. These include contracts that are cost-reimbursable with fixed time rate, cost-reimbursable with incentive fee, cost-reimbursable with fixed fee, cost-reimbursable with fee based on actual costs, and cost reimbursable with no fee. For example, a contract for professional services based on a per-hour rate with a limitation on total expenditure would be considered a fixed time rate contract.

2.28 Cost-reimbursable contracts are considered higher-risk, but both types of contracts may be subject to government audit. PWGSC maintains a Cost Audit Group



(CAG), which commissions audits of cost-reimbursable contracts for which it is the contracting authority. PWGSC employs Audit Services Canada (ASC), which is a special operating agency within the Department, to conduct those audits. PWGSC's Supply Manual includes the following guidance for cost-reimbursable contracts (Exhibit1):

#### Exhibit 1

- (a) Cost reimbursable contracts or contracts with cost reimbursable elements require special attention because the price is not specified in the contract, but rather is determined after the completion of the work. All cost reimbursable contracts must include a clause indicating that the cost incurred will be subject to audit by PWGSC.
- (b) For all cost reimbursable contracts valued to \$50,000 or more awarded to Canadian suppliers, the contracting officer must, on completion of the work, place on file a certification that the final amount paid represents a reasonable price.
- (c) This certification may be based on the findings of a formal or an informal audit. This audit provides the basis for certification that the price is reasonable.
- (d) All contracts containing cost reimbursable elements must include an appropriate basis of payment clause.
- (e) All cost reimbursable contracts must also include clause C0300C, which calls upon the contractor to provide a cost submission to the contracting officer upon completion of the contract or annually for multi-year contracts spanning more than one contractor fiscal year.
- (f) The requirement for a cost submission will be listed as a mandatory deliverable item within the contract. However, for repair and overhaul (R&O) service contracts, the contracting officer or audit agency may determine whether a cost submission is needed as a deliverable item. The clause pertaining to R&O service contracts must be used.

Source: PWGSC Supply Manual – version 10-1; 4.70.20.35

2.29 Government contracts typically contain a number of clauses that are referred to for payment of a supplier's invoice, such as Basis of Payment clauses and clauses pertaining to invoicing. Most contracts entered into by the federal government and issued by PWGSC also have in their general conditions an article that provides for the examination, inspection or audit of payments made under the contract, which we refer to in this report as the "audit provision." In general, suppliers are required to keep their supporting documentation, such as time sheets, invoices and agreements with subcontractors, for a period of six years to be available for audit, inspection or

examination, and provide reasonably required facilities for any audit or inspection. According to the various typical contract clauses, the contracting authority has the right to recover overpayments or payments made in error. The following is an example of a typical standard condition article found in highly complex contracts for services (Exhibit 2):

## Exhibit 2

### Services

2035 30 (2008-05-12)

### Accounts and Audit

1. The Contractor must keep proper accounts and records of the cost of performing the Work and of all expenditures or commitments made by the Contractor in connection with the Work, including all invoices, receipts and vouchers. The Contractor must retain records, including bills of lading and other evidence of transportation or delivery, for all deliveries made under the Contract.
2. If the Contract includes payment for time spent by the Contractor, its employees, representatives, agents or subcontractors performing the Work, the Contractor must keep a record of the actual time spent each day by each individual performing any part of the Work.
3. Unless Canada has consented in writing to its disposal, the Contractor must retain all the information described in this section for six (6) years after it receives the final payment under the Contract, or until the settlement of all outstanding claims and disputes, whichever is later. During this time, the Contractor must make this information available for audit, inspection and examination by the representatives of Canada, who may make copies and take extracts. The Contractor must provide all reasonably required facilities for any audit and inspection and must furnish all the information as the representatives of Canada may from time to time be required to perform a complete audit of the Contract.
4. The amount claimed under the contract, calculated in accordance with the Basis of Payment provision in the Articles of Agreement, is subject to government audit both before and after payment is made. If an audit is performed after payment, the Contractor agrees to repay any overpayment immediately on demand by Canada. Canada may hold back, deduct and set off any credits owing and unpaid under this section from any money that Canada owes to the Contractor at any time (including under other contracts). If Canada does not choose to exercise this right at any given time, Canada does not lose this right.

(Source: PWGSC SACC Manual)

2.30 The use of the above provision is an important tool in obtaining the assurance that the price being charged is fair and reasonable. The use of the audit provision in procurement represents a risk mitigation strategy to ensure fairness, openness and transparency in the procurement process.

2.31 The PWGSC Supply Manual makes several references to the audits of contract payments and several specific references to the audit of payments for Defence contracts. This manual is to be used by PWGSC contracting officers and makes reference to the involvement of the Cost Audit Group.

2.32 The Cost Audit Group within the Acquisitions Branch at PWGSC manages the Cost Audit Program (CAP). The CAP fulfills the obligation for audits of Canadian suppliers' records under a memorandum of understanding with the Canadian Commercial Corporation and the Supply Manual requirement for audits of Major Crown Projects (MCPs). CAG also strives to select a number of other cost-reimbursable contracts according to a number of criteria, such as on request from a contracting officer or according to a sampling methodology.

2.33 Similar risk management strategies are found in government contracting around the world. Price certification is important not only to ensure value for money spent, but also to increase the confidence of both taxpayers and suppliers that the administration of contracts is being conducted with probity and fairness. The "audit provision" control is part of the control framework used by the government to ensure that it pays a reasonable and fair price for services rendered or goods received in accordance with the terms and conditions of a contract.

### **Why it Matters**

2.34 This review should be of interest to Parliament, government departments and agencies, suppliers and those involved with military procurement. It should also be of interest to the U.S. military, which shares a number of suppliers with Canada's Department of National Defence (DND).

2.35 The inclusion and use of the audit provision, which allows the government to review, inspect and audit, reinforce the principles of fairness, openness and transparency. Especially in cases of high-risk contracts such as large cost-reimbursable contracts where the price is not determined until after the work is done and the amount to be paid under the contract can vary with a number of factors, the use of this provision upholds the principles of transparency by demonstrating the price being paid is fair and reasonable. This would strengthen the confidence of stakeholders in the fairness and openness of the procurement process.

2.36 These audits also provide assurance that the contracts do not contain a material amount of loss to the Crown due to excessive profits or inaccurate or unreasonable costing practices; deter contractors from initiating unacceptable practices by maintaining a sufficient level of audit presence; and provide quality control information on the acquisitions process, including contract management.

2.37 PWGSC has been conducting audits of cost-reimbursable contracts for many years. According to the latest departmental data available, there are over 4,000 cost-reimbursable contracts let each year with a value of over \$5 billion. A key aim of this review was to identify potential improvements in their systems and practices for this procurement control. The review also sought to identify potential improvements in how the control is applied in other government departments and agencies.

2.38 When properly used, the audit provision provides a deterrent to improper billing. However, it does place considerable requirements on suppliers in terms of document retention and record keeping, with related costs that suppliers have to take into consideration when bidding or negotiating their price.

## Focus of the Review

### Review Objectives

#### Overall Objective

2.39 Our overall objective for this review was as follows:

To assess whether the risk mitigation strategy of auditing contract payments is working effectively and contributing to maintaining the fairness, openness and transparency of government procurement.

#### Sub-Objectives

- I. To determine the extent to which the systems and practices for auditing contract payments in a number of organizations have been implemented as a control and applied.
- II. To review the improvements to strengthen the contract audit program for cost-reimbursable contracts currently under way at PWGSC compared with the systems and practices previously in use for audits of those contracts and to report on the degree of progress made and any good practices implemented.

### Scope and Period of Review

2.40 This review followed two lines of inquiry. First, we selected a number of typical departments and agencies in addition to PWGSC and questioned them on their use of the audit provision as one account verification control and its perceived value to the procurement function. The eight organizations that we included were Public Works and Government Services Canada, National Defence, Foreign Affairs and International Trade, Agriculture and Agri-Food Canada, Canadian Heritage, the National Research Council, the Public Service Commission and the Nuclear Safety Commission.

2.41 Secondly, we reviewed the program at PWGSC that audits cost-reimbursable contracts. These contracts are considered higher-risk, as they are often of a non-competitive nature and are high-value, and the amounts to be paid are undefined because the contracts are negotiated on either a profit ratio or cost-recoverable basis.

We focussed our review procedures on the proposed improvements to the program being considered by the Department.

2.42 Our review covered the period from April 1, 2007, to January 5, 2010.

### **Review Methodology**

2.43 In order to review the utilization of the audit provision, we selected eight departments and agencies of varying size and contracting activity and sent them a general questionnaire on how they relied on the audit provision for payment verification and in what situations they invoked the clause. We asked for supporting documentation and discussed the responses received with some of their officials. We also questioned them on their openness to audit suppliers.

2.44 In order to review PWGSC's renewal of its Cost Audit Program, we used questionnaires, interviews and document review. We inquired about the CAP issues identified by the department, and how they planned to go about addressing them. We discussed some of the issues with a client department to gain their perspective. We also referred to a review of certain aspects of the CAP done by PWGSC Internal Audit.

2.45 We relied on relevant sections of the Financial Administration Act (FAA) and related Treasury Board (TB) policies and directives to develop our approach and help frame our review questions. In particular, we relied on the TB Directive on Losses of Money or Property, the TB Policy on Account Verification, the TB Contracting Policy and referenced material. We also relied on pertinent sections of the Public Works and Government Services Canada (PWGSC) Supply Manual and the PWGSC Standard Acquisition Clauses and Conditions (SACC) Manual.

### **Review Observations**

#### **Audit Provisions are an Important Tool to Protect the Integrity of the Procurement Process**

2.46 Audit provisions in some form are a feature in the terms and conditions of most government contracts. They form the contractual basis for any inspection, review or audit of records that the suppliers must retain as outlined in exhibit 2. The PWGSC Supply Manual makes the distinction between complex and non-complex contracts, and for the complex contracts, it requires more elaborate contract audit provisions along with more detailed additional clauses concerning matters such as for cost submission and basis of payment as a consequence. It also provides direction on audit provisions to be included in cost-reimbursable contracts.

2.47 The use of this provision may be relied on to conduct a formal or informal audit of a supplier's records or to demand further documentation or information from a supplier to support price certification, which sends a signal to the supplier community that the government is operating in a fair and transparent manner by ensuring suppliers comply with the terms and conditions of contracts.

2.48 In this line of inquiry, we set out to determine how organizations use the audit provisions in contracts (other than cost-reimbursable contracts managed by PWGSC), both where they are the contracting authority and where PWGSC is the contracting authority. In cases where the audit provision is included in contracts, we sought to determine when the audit provision is invoked and how the results of the audits are used.

2.49 PWGSC is often the contracting authority for the larger departmental contracts. For those, we sought information as to the department's dealings with PWGSC for audit selection as well as for resolving any issues raised by the audits.

2.50 In order to determine how the audit provision is used, we sent questionnaires to eight departments (and agencies) chosen for their size and contracting activity, and we held discussions with their officials. We sought to determine whether those departments and agencies include the audit provisions in their contracts and how they apply those clauses as a payment verification control.

2.51 We found that all the departments and agencies use the standard audit provisions in most of the contracts where they are the contracting authority. (The wording for these clauses is usually taken from PWGSC's Standard Acquisition Clauses and Conditions Manual.) With few exceptions, PWGSC includes the audit provision in all contracts for which it is the contracting authority for both its own acquisitions and acquisitions in its role as a common service provider for client departments.

2.52 PWGSC is the recognized leader in government contracting, and its manuals are referred to for guidance by procurement officers throughout government. Generally, the audit provision and additional payment-related clauses follow the templates provided in the PWGSC Standard Acquisition Clauses and Conditions (SACC) Manual and require that suppliers keep detailed records to support their invoices for payment; the clause also requires the supplier to keep these records for six years to be available for audit, examination or inspection by the Crown upon request.

2.53 All the departments and agencies questioned informed us that they find the audit provisions useful to support ad hoc requests for additional documentation, but that for contracts under their authority, they had not invoked the audit provision to conduct audits of supplier records for the period under review. The organizations were of the view that other controls over payments sufficiently reduced the risk of erroneous payments to make such audits unnecessary.

2.54 Although PWGSC recognizes complex contracts and contracts containing a cost-reimbursable element (such as contracts for professional services where the final price is based on a fixed time rate with a limitation on expenditure) to be higher-risk, the use of the audit provision is not explicitly part of the organizations' risk management frameworks. Among the important controls that minimize the risk of erroneous payments mentioned by the departments and agencies are the following:

- Internal audits of large contracts. In these instances, they do not audit supplier records, but confine their scope to documentation and information held within their organizations.



- Control systems in place for verifying payments, such as standard documentation and procedures to verify proof of receipt of goods or services in order to sign under section 34 of the Financial Administration Act that goods have been received and services rendered.
- To satisfy section 33 of the FAA before issuing the cheque, on a sampling basis according to a transaction-type risk assessment, conducting a thorough check for the existence on file of appropriate documentation to support a payment.
- Post-payment verification of all documentation on file supporting a payment, with transactions selected on the basis of risk.

2.55 The organizations routinely consider the effectiveness of their account verification controls. They believe that since most contracts are not regarded as high-risk and since their current account verification procedures to mitigate risk can result in the discovery of most overpayments, the risk of their undetected occurrence is reduced to an acceptable level.

2.56 None of the organizations had formally reviewed their use of the audit provision or the nature and extent of record keeping being required on the part of suppliers. Suppliers appear to accept this requirement as part of doing business with the Government of Canada and the government's need for accountability to taxpayers. None had developed specific written guidance on the use of the provision as a risk mitigation strategy for those contracts for which they are the contract authority, in particular for contracts containing a cost-reimbursable element. The organizations questioned also indicated that they would each follow distinctive procedures should they find it necessary to invoke the audit provision. For example, some indicated that they would give the responsibility for conducting the audit to their internal audit division, while others would leave it to the discretion of the procurement officer administering the contract.

2.57 All the organizations deemed the audit provision to be a useful preventive control, even if never formally used as a detective control to find overpayments that may have occurred. Officials told us that there are occasions where the manager responsible for signing off under section 34 of the FAA on an invoice for payment may request from the supplier additional information to support the invoice. While this would not be considered to be formally invoking the audit provision, the existence of the audit provision in a contract can provide the organization with the authority to request additional information within the terms and conditions of the contract. This may also act as a deterrent to improper invoicing by suppliers.

2.58 All eight departments and agencies said that the audit provision is useful even if never formally invoked because both the government and the supplier know that an audit can be conducted if necessary. This promotes compliance with the terms of the contract. The effect is similar to the way a potential audit promotes taxpayers' compliance with the Tax Act.

2.59 The inclusion of the audit provision in their contracts provides the organizations with a sense of comfort that they can verify supplier records in cases where they may

judge that specific information is required to confirm that a payment was justified. However, its usefulness as a preventive control depends on the possibility of it being invoked formally, or informally, such as through requests for additional information. The organizations had not considered potentially conducting a certain number of audits, inspections or examinations on the suppliers' premises for the purpose of reinforcing the value of the audit provision as a preventive control.

2.60 The organizations often call on PWGSC to administer their larger, more complex contracts. None of them were aware of any audits having been conducted for their contracts administered by PWGSC, other than those conducted under PWGSC's Cost Audit Program. As to the potential impact on suppliers in terms of cost and effort to comply with the audit provisions, PWGSC pointed out to us that although it has not specifically considered this issue, it has put in place an Office of Small and Medium Enterprises to deal with any issues that this category of suppliers may find to be impediments to participating in PWGSC contract competitions.

### **There is Potential for Further Application of the Audit Provision in Departments and Agencies**

2.61 We inquired further into the potential for auditing complex information technology (IT) contracts. We found that PWGSC's Acquisitions Branch (AB) includes information technology professional services contracts that are paid on a fixed time rate basis in its CAP. These contracts are typically per-diem rate contracts where the level of professional effort is not determinable before the work begins, and the final price is not known until after the work is done. For example, such a contract may require IT specialists to bring modifications to off-the-shelf software, or implement an IT application in a particular context. However, we were told that few cost audits have been done on these contracts administered by PWGSC in recent years, reducing the effectiveness of the audit provision as a risk mitigation measure. At the end of our review, Internal Audit at PWGSC had prepared a draft audit report on Information and Technology Branch task authorization contracts, which deals with some of the topics raised in this review.

2.62 Where organizations do not refer to PWGSC common services for the procurement of these IT services and are themselves the contract authority, none of them had formally considered invoking the audit provision to support the account verification for these contracts. Given that PWGSC contracting officers consider the audits of these types of cost-reimbursable contracts to be a valuable procurement control in establishing a fair price to be paid under fixed time rate IT professional services contracts, other organizations could possibly benefit from implementing this good practice where they are the contract authority.

2.63 We noted two specific good practices related to the use of the audit provision. DND internal audits often recommended that cost audits be done in some cases where PWGSC is the contracting authority.

2.64 In another example, PWGSC Internal Audit recommended using the audit provision for construction contracts (see Exhibit 3). These types of contracts do not

appear to fall within the audit universe defined by CAG. In this case, the internal audit of the PWGSC construction contracting process recommended that the Department ensure that construction contracts include a more detailed audit provision in the standard terms and conditions, and that these audits be undertaken. We concur with those findings (Exhibit 3):

### Exhibit 3

#### **Extract from Audit of PWGSC Construction Contracting Process**

##### Strengthening of Audit Clause

43. To reduce the risk of excessive project cost and to demonstrate value-for-money to the Crown, it is important that a clearly worded, specific provision for the Crown's right to undertake an audit is included within the standard construction contract terms and conditions and that audits are subsequently carried out.

44. The standard template for construction contracts contains a General Conditions clause #51 for records to be kept by a Contractor. This clause incorporated most of the criteria for an audit to be undertaken. Such criteria included a requirement for records to be retained for a period of at least 2 years; access to records of associated sub-contractors; and the right of an audit if the Crown determined a requirement. However, consistent with other audit clauses used in contracting, these clauses could be strengthened to include reference to: the Crown's right to validate the accuracy of the Contractor's time recording system, and the amounts claimed including the number of hours charged and costs incurred for materials, supplies, other direct costs and travel and living expenses; the results and findings of the audit as being conclusive; and prompt refund to Canada if there has been any overpayment.

45. We validated that construction projects are rarely audited. It is important that audits be carried out on a regular basis. Such audits could be carried out by the Acquisitions Branch, Cost Audit Group or auditors hired by RPB Project Managers. The Cost Audit Group administers a Cost Audit Program, which serves to protect the financial interests of the Crown through systematic audits of contracts that PWGSC has issued. These audits provide assurance that the contracts do not contain a material amount of loss to the Crown due to excessive profits or inaccurate or unreasonable costing practices; deter contractors from initiating unacceptable practices by maintaining a sufficient level of audit presence; and provide quality control information on the acquisitions process, including contract management.

63 (...) we concluded that:

The risk of excess charges could be mitigated by the undertaking of cost-audits, as appropriate, which is authorized in clear audit provisions of the terms and conditions of construction contracts.

2.65 In summary, for both firm-price and the higher-risk cost-reimbursable contracts, the organizations find the audit provision to be a valuable instrument of control, but use it only occasionally and have not formally considered whether making less restricted use of its potential could provide further benefits. Nor have they considered the potential impact on suppliers in terms of the cost and effort to comply with the audit provisions. We believe that as part of their account verification risk mitigation, organizations should look into formalizing when and how the audit provision could best be used. As PWGSC is looking into updating its methodology for its own CAP, when assessing how the audit provision should be used, other organizations may want to obtain information as to the improvements being made by PWGSC.

## Recommendation

2.66 As part of their account verification risk mitigation strategies, departments and agencies should include a guideline as to how and when to use the audit provision for contracts that do not fall under the auspices of CAG at PWGSC and are of a cost-reimbursable nature, taking into consideration the expectations of suppliers' record keeping and the principle of openness regarding audit suppliers.

### PWGSC Maintains a Cost Audit Program

2.67 For many years, as a risk management strategy, PWGSC has managed a program to audit supplier records for cost-reimbursable contracts. There are at least 4,000 cost-reimbursable contracts signed annually by the Crown with an estimated value of over \$5 billion, including Major Crown Projects (MCPs). This program mitigates certain risks identified in the Departmental Integrated Risk Management Policy, such as the risk to departmental reputation and risks to the efficiency of procurement processes.

2.68 Cost-reimbursable contracts are used where the specific amount to be paid to the supplier is not known at the time the contract is signed. The amount to be paid must be calculated based on a number of factors such as the actual costs of materials, parts or subcontract work; the number of hours of labour at a fixed rate; or a volume or demand that will vary with time. For example, one type would be service contracts that are based on an hourly rate with a limitation on total expenditure. Another typical cost-reimbursable contract would be one for the repair and overhaul of defence materiel, such as fixed wing aircraft or helicopters. The rate per hour for scheduled maintenance can be determined when the contract is signed, but the actual amount of required maintenance will depend on flying time. Some contracts specify a maximum profit percentage. Cost-reimbursable contracts may be "sole-sourced," that is they may not go to competitive bidding. In the example of the maintenance of a specific aircraft such as the F-18 fighter, only the suppliers with proprietary rights and specialized expertise are qualified for the work, and the contract may be in force for the many years of the life of the aircraft, with periodic amendments. PWGSC is the contract authority for the majority of such cost-reimbursable contracts on behalf of other government departments such as National Defence (DND).

2.69 Government cost-reimbursable contracts are often complex and frequently involve projects of significant value. Contracts are typically carried out by a prime contractor and many subcontractors, each of which may participate in numerous government contracts, as well as private sector work. In such an environment, it is essential that only allowable costs be identified and charged to the appropriate government contract. Cost-reimbursable contracts have been the major focus for government audits of suppliers' records.

2.70 Many of the audits of cost-reimbursable contracts have been of directed (sole-source) contracts. To the extent there is transparency of the audit selection criteria, the implementation of the overall audit plan, and the methods and effectiveness of recoveries, supplier confidence that a competitor is allowed to charge a fair and reasonable price only and is not receiving an unfair advantage is enhanced.

2.71 In some cases, such as for Major Crown Projects or when an audit of a Canadian defence contractor is requested by the U.S. military or by NATO, the audits are mandatory. The selection of other audits can be based on a sampling technique or be the result of a request based on a risk assessment. Contracts under \$50,000 are not included in the CAP population for selection.

2.72 PWGSC maintains a distinct group called the Cost Audit Group (CAG) within the Policy, Risk, Integrity and Strategic Management (PRISM) sector of PWGSC's Acquisition Branch (AB) to manage these cost audits. In consultation with the client department and the contracting officer, CAG manages the selection and scheduling of the audits, and employs Audit Services Canada (ASC) to perform the work. For the period under review, the CAP has focussed on the audit of defence contracts.

2.73 ASC is a special operating agency within PWGSC that provides audit services to all government departments. It also performs overhead studies at CAG's request that support subsequent audits. A memorandum of understanding (MOU) between ASC and AB exists for these services. ASC employs professional audit staff in the National Capital Region, staff at regional offices and subcontractors in the regions when necessary. An issue that merits further study is whether to continue the current practice of having the cost audits done exclusively by government employees or whether the program would benefit by using some of the expertise available in the private sector.

2.74 The results of the audit are forwarded to the PWGSC contracting officer (CO) who is responsible for administering the contract for a client department such as DND. The Cost Audit Program is one of the principal tools available to COs to discharge their responsibility to ensure that prices paid pertaining to cost-reimbursable contracts are in accordance with contract terms and conditions, and are fair and reasonable.

2.75 A cost audit may identify suggested adjustments based on the audit findings and the auditor's interpretation of the contract terms, such as an adjustment for what in the auditor's opinion was an overpayment. According to the PWGSC Supply Manual, which provides direction to COs, "the contracting officer will establish a final price with the contractor based on the audit findings. Every effort will be made to do this within 90 days of the audit report being received. The contracting officer will notify CAG of the terms of the settlement and resolution of all audit issues raised in the contract audit."

2.76 "On occasion, differences of opinion or interpretation may arise between the CO and the auditor regarding the legitimacy of audit findings. The relevant director should resolve these differences of opinion in concurrence with the Director, Acquisition Program Integrity Secretariat, before CAG takes close-out action. "

2.77 The Supply Manual states that CAG's role is to advise the CO on dealing with the audit findings and resolving any audit adjustments. The CO informs CAG and the Director of Procurement of any disagreements with the audit. The CO is also primarily responsible for recovering any overpayments when identified.

2.78 Audit adjustments do not constitute a receivable until such time as the CO has made a final price determination. The practice has been for the client department to



account for any recovery of overpayments at the time that an amount has been settled by the supplier.

2.79 The CAP is important in providing assurance that suppliers are invoicing according to the contract terms, in assisting the CO in making a final price determination and in recovering any overpayments that may have been made. Some audits have determined potential adjustments of up to millions of dollars, either owed to the supplier or to be recovered. To date, recoveries have been made in cash or through offsetting claimed overpayments with future supplier invoices. Under the audit provision, the Crown has the right to recover an amount identified against any other amounts owing to the supplier.

2.80 Currently, under government accounting rules, all recoveries of money that was expended in prior fiscal years are deposited to the Consolidated Revenue Fund (CRF).

2.81 In some cases, it can take considerable time for the CO to resolve audit adjustments on a contract. For example, one audit covered the period from January 2002 to March 2004. The audit was dated March 31, 2006, and was referred to the CO in the 2007-2008, fiscal year, but the audit adjustments still had not been resolved at the time of our review in 2010.

### **PWGSC Undertook a Review to Strengthen the Efficiency and Effectiveness of its Cost Audit Program**

2.82 In 2008, PWGSC Acquisitions Branch tasked CAG to undertake a review of the CAP to explore a number of long-standing issues. The areas to be examined included mandate, organizational capacity and structure as the first priorities, and subsequently issues relating to procedures and governance. The review led to a CAP renewal project, which noted a number of areas for improvement. After the period of our review, in March 2010, the Department approved a detailed update to its action plan, which deals with many of the issues brought forward in this review.

2.83 One key area identified for improvement is the usefulness of the current audit methods. The review of the CAP noted that audits commissioned to support final price determination resulted in the identification of audit adjustments pertaining to potential billing errors that occurred many years previously. The review found that this made it difficult to establish the validity of the audit adjustments and recover the appropriate amounts.

2.84 Good data and timely informative reporting are a fundamental requirement for good program management. The renewal noted that departmental data on amounts under audit needs to be updated, the existing data available does not include Major Crown Projects, and reporting methods need to be improved.

2.85 While CAG currently does not produce operational reports on its performance and risk exposure, it expects this to change with the renewal of the program. Quarterly status reports will be provided to the proposed DG Council. In future years, CAG expects to provide information on risk exposure by contract type and by sector. This is



expected to include information on the population of cost-reimbursable contracts. Some of the items of information to be reported to the DG Council would include the following:

- The number and value of all active contracts of a cost-reimbursable nature
- The number and value of cost-reimbursable contracts awarded in a fiscal year
- The number and value of cost-reimbursable contracts under audit and audited by fiscal year
- The value of audit adjustments by contract award year and by fiscal year
- The amounts recovered by contract award year and by fiscal year
- An ageing of the amounts of audit adjustments to be recovered, with collection status

2.86 During the review activity, CAG significantly decreased the number of audits. For example, the number of audits started in the past three years was 114 in 2006/2007, 64 in 2007/2008, and 22 in 2008/2009. The CAP fell behind in performing mandatory audits and performed fewer discretionary audits. During that time, its budget allocation also decreased. In the past, the budget was around \$5 million, but this has decreased to about \$2.5 million for the past few years. This led to a backlog of both mandatory audits and audits that had been otherwise selected.

2.87 In 2009-2010, the Department provided CAG with approval for additional funding of \$2.5 million to address the backlog. As a priority, CAG plans to complete the backlogged audits through 2009-2010 and in 2010-2011. The changes proposed by its renewal will not be applied to the backlog audits.

2.88 CAG is also working on resolving the key issue of the instability of the current funding formula to provide the desired capacity for audits. The renewal is still ongoing, and staff are following the updated action plan for stabilizing the funding of the CAP and implementing the needed improvements identified to date.

### **An Internal Audit Review of Current CAP Practices Found Some Flaws**

2.89 During our review, PWGSC Internal Audit also performed a certain number of specified review procedures relating to the recovery from suppliers of audit adjustment amounts identified by the CAP audits. Their review selected a risk-based sample of closed files to ascertain whether the recovery decisions taken were consistent with the cost audit findings, properly documented and justified.

2.90 Their review confirmed some of the issues identified by the CAG renewal study, such as cost audits not always being followed up and recovery procedures not always being effective. It also raised the important issue of the need to clarify the authorities required for a decision not to pursue amounts identified by a cost audit as recoverable. The review made no recommendations. Nevertheless, as part of its renewal project, AB is addressing concerns raised by that review in its updated action plan.

2.91 During our review, PWGSC Internal Audit also began to perform specified review procedures on a sample of files where CAG is still in the process of attempting to recover amounts identified by the CAP. CAG will be expected to produce an action plan to deal with any concerns raised by that review.

### **PWGSC is Developing a new Approach**

2.92 The focus of our review procedures was on the CAP renewal process and substance, in order to identify improvements being considered, as well as potential improvements that could be incorporated in the renewal. We looked to see to what extent the renewal proposals address identified issues, in accordance with relevant sections of the FAA, TB policies and directives, and the PWGSC Supply Manual.

2.93 The renewal has developed a vision and direction as to how the Cost Audit Program should function that resonate with most stakeholders as being an improvement over the current way of operating.

2.94 The following key proposals being considered intend to alleviate the problems of the build-up of audit backlogs due to lack of funding and unclear selection parameters, the slow recoveries due to the timing of audits, the often large amounts identified and the use of various methods of recovery that may be unauthorized:

- a. A risk model will be developed for where to focus discretionary audit effort.
- b. The audits will normally be done over the whole life of a contract, and not only as a post-contract activity. The audits will initially focus on the supplier financial information systems. This will be of more value to those signing under section 34 before payment. Subsequent audits of the same supplier will need only to update the reliance on controls, with less transactional auditing. This approach should prevent errors in invoicing from occurring, rather than detecting them long after the fact.
- c. Parameters to measure program performance and its effectiveness will involve cost audit ratios, and the DG Council will be consulted on the measures and their use. The CAP will regularly monitor and report on recovery rates relative to the investment in cost audits.
- d. The recovery activities would include the following improvements:
  - i. By virtue of initiating audit activity at the start of a cost-reimbursable contract, factors contributing to pricing errors should be detected early, reducing the potential for their occurrence and potentially allowing departments and agencies to obtain refunds.
  - ii. Recovery activities will be supervised by a Directors General Council, and a report prepared. The renewal is proposing that the DG Council include representatives of key client departments, as well as of its own finance and legal branches. Terms of reference (TORs) may be modelled on the TORs for the departmental External Audit Committee and recommend reporting

of sector-by-sector risk assessments, operational statistics and lessons learned.

2.95 The renewal is developing a new risk assessment methodology that goes beyond simple dollar value, similar to the one used by the Defense Contract Audit Agency (DCAA) in the U.S., and that will take into account the following factors:

- Previous audit experience, by vendor
- Experience of the contracting officer(s)
- Client department risk mitigation measures
- Types of contracts
- Dollar value of contract
- Dollar value of all contracts with the same supplier

2.96 To keep up with the requirement for mandatory audits and enable CAG to perform some discretionary audits on a risk selection basis, the renewal is also suggesting a multi-faceted approach to funding which may involve the following:

- Appropriation funding of core procurement (i.e. CAG) activities, which could take the form of an umbrella TB submission;
- Fee-for-service / MOUs for account verification activities; this would rely on client departments paying a share of the costs; and
- Financial incentives to encourage compliance by contractors.

2.97 The methods of funding is a key question to resolve, since establishing a sustainable method of funding is a top priority for the renewal, and decisions on these questions will need to be taken as soon as possible.

2.98 In January 2010, the PWGSC Supply Manual was updated. One of the sections relating to contract audits was deleted and marked for further review. The intention is to incorporate some of the changes as a result of the renewal. As the Supply Manual serves as the primary guidance tool for government procurement operations, this will be a crucial step in the renewal. No timetable has been set for incorporating these changes in the regular revisions to the Manual.

2.99 We are encouraged that PWGSC has undertaken a rigorous review of the program. It has completed the first steps of identifying program shortcomings and developing a new framework designed to make the program more efficient and effective. It has now to take the next essential steps detailed in its updated action plan, particularly in relation to obtaining sustainable funding and assigning appropriate resources for its implementation.

## The Renewal Plans to Address a Number of Process Issues

2.100 The current focus of the Cost Audit Group is on clearing the backlog of overdue audits and defining the start-up costs for the new approach being developed. This has left considerable work to be done to complete the renewal. In addition to the proposals previously mentioned that need to be approved and put into operation, there are a number of governance and process improvements that the renewal of the program will need to address over the coming months.

2.101 One key issue relates to the roles and responsibilities with respect to resolving the audit adjustment amounts identified as potential overpayments by the audits. Our review of the Supply Manual and renewal proposals, our discussions with PWGSC staff and the internal audit review finding that the Acquisitions Branch is working to clarify the authorities and the process for ensuring that decisions not to pursue amounts potentially owing are approved in accordance with those authorities, indicate to us that the authorities, roles and responsibilities with respect to resolving the audit adjustments and making recoveries from suppliers need to be clarified.

2.102 As the decisions relating to amounts to be recovered can have important financial implications, the concentration of duties in the hands of the CO varies from the fundamental principles of internal control. Within the process of dealing with the audit adjustments, there needs to be a clear division of duties and clear accountability for decisions taken.

2.103 Currently, the CO is responsible for negotiating the contract, administering the contract, recommending invoices for payment to the client department, selecting contracts for audit, playing a major role in disposing of the audit adjustments, negotiating the final price with the supplier and playing a major role in the collection of any amounts deemed recoverable as the result of audit. The updated action plan includes an item to address the question of roles and responsibilities in relation to disposing of the audit adjustments.

2.104 While we are encouraged by the actions of the Department to date, it is imperative that the process for final price determination be finalized as soon as possible, so that recovery of any overpayment is maximized and losses minimized. The renewal's proposal to have audits start at the beginning of the contract term should further help to minimize the amounts to be recovered and to enhance the possibility of maximizing the recovery of amounts identified as owing by suppliers. The proposed monitoring of the CAP by the DG Council will also be important to this effort.

2.105 Some important areas included in the updated action plan for further consideration are the following:

- a. The audit methodology in terms of scope, approach, materiality or format of audit report and nature of audit opinion needs to be further defined.
- b. As noted above, the renewal is proposing several improvements to CAP information and reporting. The current methods of data collection, analysis and reporting will need considerable improvement to support the proposed risk model

and performance measurement, and to support future budgeting forecasts. Some form of summary level reporting is being considered and would improve the transparency of the program. The updated action plan has set ambitious timelines for improvements in this area.

2.106 In our view, the confidence of Canadians in public procurement and the government's commitment to transparency would be strengthened by the publication of summary level results of the Cost Audit Program.

### **The Renewal will Require Important Consultation with Several Stakeholders**

2.107 While considerable background policy work is being done to renew the contract audit function at PWGSC, the Department has also recognized that several important stakeholders need to be consulted to implement an effective program of cost audit for cost-reimbursable contracts. Those being consulted include the following:

- a. The cost analysts within the Acquisitions Branch at PWGSC, who negotiate the rates for cost-reimbursable contracts.
- b. The PWGSC contracting officers, who have had the bulk of recovery responsibility in the past, deal with suppliers on a regular basis and thus should have valuable input to provide to the risk model for audit selection and to the eventual audit methodology.
- c. The Acquisitions Branch DG Council that will supervise the CAP.
- d. The client departments concerning funding mechanisms, audit selection, audit methodology and recovery procedures.
- e. The Treasury Board Secretariat (TBS) if changes to the method of funding are required to finance the renewal of the cost audit function.
- f. Audit Services Canada on the required capacity in terms of expertise to implement the renewed approach, and possibly on how in the immediate future the Department could meet the principle of openness in contracting through joint audits with other suppliers or subcontracting of audits by ASC.

Cooperation from interested stakeholders will be crucial to the successful implementation of any action plan. The renewal has considerable work ahead to keep a sustained focus on its consultation activities.

### **Recommendations for the CAP renewal**

2.108 We are encouraged by the PWGSC Acquisition Branch's approval of an updated action plan for the renewal of the CAP. The DG Council in the Acquisitions Branch of PWGSC should monitor implementation of the updated action plan and report progress to senior management on a frequent basis.

2.109 In order to strengthen transparency and enhance the deterrent effect of cost audits, summary level reporting of the CAP results should be prepared and made available to the public.

## Conclusion

2.110 The risk mitigation strategy of including audit provisions in government contracts is proving useful to departments and agencies and supports the principles of fairness, openness and transparency. Departments and agencies could benefit from integrating into their account verification risk mitigation strategies clearer direction on their use, especially relating to higher-complexity contracts.

2.111 PWGSC's Cost Audit Program for cost-reimbursable contracts represents a good procurement practice with clear benefits in terms of fairness, openness and transparency, as well as financial benefits through the recovery of overpayments to suppliers. A renewal of this program is under way, and improvements identified in the March 2010 updated action plan are urgently needed. Implementing the improvements identified and obtaining sustainable funding are crucial to the effective survival of this important program.

All departments and agencies involved in this review were given an opportunity to review this report and their comments were taken into consideration when it was finalized.