National Defence Défense nationale

Chief Review Services Chef - Service d'examen

CRS CS Ex

AUDIT OF NDHQ O&M EXPENDITURES

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SYNOPSIS

This report presents the results of an internal audit of National Defence Headquarters expenditures for operations and maintenance. Headquarter organizations expend approximately $0.9B annually from their locally managed budgets on operations and maintenance. The purpose of this audit was to provide assurance that the ensuing management processes and practices are effective in ensuring diligent, compliant and transparent use of these funds.

The requirement for sound financial control has received renewed emphasis within the Department—as witnessed by widespread mandatory training and increased verification efforts. Despite these efforts, the audit showed that there is a high rate of non-compliance with the Financial Administration Act*, Treasury Board contracting policy and departmental procurement and payment policies.*

Compliance remains heavily dependent on paper-based documentation and manual certifications, despite significant recent investments in technology. Stove-piped, non-integrated systems complicate retrieval of "cradle-to-grave" documentation in support of transactions and frustrate attempts to develop automated control and monitoring systems, in particular for high-volume, low-dollar value transactions.

Another contributing factor to non-compliance is that policies and practices have often been developed in isolation without an overarching view of the total process. Inconsistencies with respect to financial coding and the absence of standard approaches to common business processes make it difficult to compare results among units or over time. In many cases there has been a preoccupation with minor details—e.g., moving small amounts of money among budgets, maintaining duplicate expenditure logs and entering detailed information in multiple systems—resulting in funds that are over-administered yet under-managed. This preoccupation with the details may, in some cases, have diverted attention from more significant financial indicators. At a macro level, the Department has only limited ability to relate outputs to business plans as a mechanism for performance measurement, or to use departmental free-balance information as a mechanism to realign resources to changing priorities.

Consolidation and simplification is warranted. As stated in a recent speech by the Comptroller General of Canada, we need "better rules, not more rules." Ultimately, developing and supporting an overarching strategy for the complete expenditure cycle—from planning through contracting, procurement, payment, reporting and monitoring—will best address these issues. This will be an iterative process, with change occurring at both departmental and governmental levels. We are satisfied that successful implementation of the initiatives documented in the management action plan will result in improvements.

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RESULTS IN BRIEF

Introduction

1. Many recent Chief Review Services (CRS) audits[1] have examined the management control framework as it relates to expenditures for a particular commodity type—contracted information technology (IT), medical services, travel and hospitality, to name a few—or using a particular payment vehicle (acquisition cards, for example). This audit took a 90-degree approach and examined all operations and maintenance (O&M) expenditures made by selected National Defence Headquarters (NDHQ) budget managers, regardless of commodity type or payment method. The audit considered the complete expenditure cycle, from planning and budgeting, through procurement and contracting, to payment, and finally monitoring and review.

2. Because similar populations were examined, albeit from a different angle, it is not surprising that this report repeats many of the observations and findings of the previous CRS audits. The broad-based sample included in this audit lends weight to the conclusion that the issues are systemic, not isolated to a particular group, and that effective solutions will require Department of National Defence (DND)-wide involvement. It also highlights the challenge facing departmental resource managers due to the wide-range of financial policies, processes and practices they encounter and must manage on a daily basis.

Background

3. This audit is similar in nature to the CRS *Audit of Management of Local Funds*, reported in fiscal year (FY) 2003/04. While the earlier report was based on sampled expenditures at Wings and Bases, this audit focused on O&M expenditures made by resource managers located at NDHQ—$0.9B in FY 2004/05. More than 500 financial transactions made by six NDHQ fund centres (FCtrs) were examined.[2] The FCtrs varied considerably in total dollars expended and number of transactions processed. There was also significant variation in the type and method of procurement. Despite this, many common issues were observed.

4. A scorecard[3] was produced documenting results within each of the sampled FCtrs. These results were provided to stakeholders within each of the audited groups. Briefing participants, while receptive to the findings, emphasized that local action would only partially resolve the issues, and that meaningful change required a more global approach.

[1] Reports of previous CRS audits can be viewed at www.forces.gc.ca/CRS.
[2] A profile of the sampled NDHQ FCtrs and details regarding the sampled transactions are included at Annex C.
[3] The Consolidated Departmental Scorecard is included at Annex D of this report.

5. Individual FCtr results were then combined to determine a departmental score. In several areas the departmental score was determined to be lower than the cumulative score for individual FCtrs. This is because the magnitude and impact of the issue only becomes apparent when a Department-wide view is taken. For example, while resource managers are reasonably effective in monitoring the status of their individual budgets and free balance, an absence of common reporting practices and continued reliance on auxiliary spreadsheets make this an onerous, labour-intensive task from a Department-wide perspective.

Overall Assessment

6. The results of this audit ***preclude providing assurance*** that NDHQ financial management processes and practices are effective in ensuring diligent, compliant, transparent use of O&M funds. **Overall, compliance with the *Financial Administration Act* (FAA), Treasury Board (TB) contracting policy, and departmental policies could be improved for 77 percent of the 534 sampled transactions.** Twenty-two percent of sampled invoice transactions and 33 percent of sampled acquisition card transactions were clearly non-compliant with the FAA and/or contracting policy. Many additional sampled transactions were of questionable compliance (e.g., certifications illegible or not dated, weak or insufficient supporting documentation).

7. In part, the high rates of non-compliance are the result of policies and practices that have not been sufficiently modified to reflect current business processes and system capabilities. Despite technological advances, compliance remains heavily dependent on paper-based documentation and manual certifications. Stove-piped approaches to business planning, procurement, and payment have resulted in incompatible policies and have complicated the retrieval of "cradle to grave" documentation in support of transactions. As groups implement various compensating methods, accuracy and consistency of management information and efficiency of processes are negatively impacted.

8. Financial control practices are not sufficiently differentiated by risk. Seventy-three percent of overall NDHQ O&M transactions comprise only 9 percent of the expended dollars, yet receive a disproportionate amount of attention from financial administrators and managers. Processes relating to low dollar value transactions have not yet been sufficiently streamlined or rationalized, resulting in funds that are over-administered yet under-managed.

9. Ultimately, developing and supporting an overarching strategy for the complete expenditure cycle—from planning through contracting, procurement, payment, reporting and monitoring—will best address these issues. Such a strategy should encompass automated controls, and assure consistent, reliable management information in a streamlined, efficient fashion. It should consider centralization and/or standardization of processes such as bill paying, and contracting for common commodities. It is recognized that this will be an iterative process, with change occurring at both departmental and governmental levels. This report makes interim recommendations to assist in ultimately reaching this state.

Principal Observations/Issues

Compliance with *Financial Administration Act* (FAA) and Contracting Policies

10. Rates of non-compliance with the FAA and contracting policies remain high.[4] For example, 22 percent of the 211 sampled invoice transactions and 33 percent of the 89 sampled acquisition card payments were clearly non-compliant, as they lacked proper contracts and/or any FAA Section 34 certification or were for wrong amounts. Overall, 77 percent of the sampled transactions exhibited some non-compliant characteristics. For these transactions, the adequacy of the FAA Section 34 certification, the sufficiency of supporting documentation, the appropriateness of the contracting methodology and contracting terms, and/or the underlying value for money was questionable.

11. Certain improvements have been put in place as a result of recent initiatives to revitalize the comptrollership function, including widespread mandatory training. For example, two of the six audited groups have recently revised their certification process for acquisition card purchases; one other audited group has recently formalized their contracting process for training. However, further improvements in the areas of delegation of authority, contracting for services, and interdepartmental payments are warranted. Enhanced monitoring, including development of risk-based “Smart Controls,” is required, along with timely implementation of an integrated procurement-to-payment (P2P) process.

12. **Delegation of Authorities**. While the new delegations of authority forms have provided some clarity, confusion regarding restrictions, differences between authorities (FAA Section 32 versus contracting, for example), and financial roles (resource centre (RC) manager versus RC administrator, for example) persists. Within the National Capital Region (NCR), the process remains paper-based and therefore cumbersome to track, monitor, and update. Delegated authorities as they relate to acquisition cards and to specific contracting vehicles are recorded separately. In many cases, these authorities are not current, easily accessible, or consistent with other delegations. None of the audited groups had a local record of the authorities delegated to acquisition cardholders and therefore could not ensure that financial limits and restrictions were adhered to. Finally, but perhaps most importantly, the documented authorities have not been used to assign or restrict system profiles or privileges, precluding a Smart Controls approach to ensuring proper authorities.

13. **Contracting Practices**. This was not intended to be an audit of contracting practices. However, when preliminary analysis demonstrated that 40 percent of the NDHQ O&M expenditures (approximately $347M in FY 2004/05) were for contracted services, it became apparent that contracting would be an important focus. Four of the six sampled groups expended a significant portion of their budget on contracted services. One of these four groups had a relatively sound control framework, including documented competition, well-defined statements of work, and payment based on

[4] Detailed sample results have been provided at Annex C.

deliverables. Contractual arrangements within the other three groups exhibited troubling characteristics. Consistent with previous CRS reports,[5] we observed situations of contract splitting, work outside the scope of the contract, work in advance of the contract, and contracts initiated in the absence of proper authority. We also continue to observe situations where contractors are assuming inappropriate roles—including project and financial management—over long periods of time, with little apparent succession planning. FAA Section 34, as it relates to contracts for services, remains problematic. In the absence of clearly defined deliverables, per diem payments remain the norm. These per diem payments are made, in many cases, with insufficient documentation to confirm hours worked. Finally, many low dollar invoices are paid in the absence of a local purchase order (LPO) or call-up against a standing offer (SO). As a result, proper contracting authority cannot be confirmed. Overall, contracting practices were clearly non-compliant, or questionable for 42 percent of the 211 sampled invoice payments.

14. **Interdepartmental Settlements**. Approximately 11 percent of the in-scope expenditures for this audit were payments to other government departments (OGD)—over $100M in FY 2004/05.[6] Department-wide, approximately 20,000 interdepartmental settlement transactions during FY 2004/05 accounted for expenditures approaching $500M.[7] While these transactions are often viewed as lower risk overall because the dollars are staying within the Government of Canada, they are high risk to individual budget managers because of a lack of adequate supporting documentation. As part of the integrated Financial Information Strategy (FIS) environment, the interdepartmental settlement process has been designed to be paperless; however, budget managers receive insufficient electronic information to confirm receipt of goods, or value for money. Thirty-six percent of the sampled transactions did not meet the documented FAA Section 34 certification requirements. The current method of settling these transactions has proven cumbersome, with many transactions held in pending accounts, and individual managers unsure when or if the established commitments will be cleared. Given the materiality of the dollars involved, increased attention to these transactions is warranted.

15. **Enhanced Monitoring Required**. Monitoring to ensure compliance and value for money remains, for the most part, ad hoc. Three of the six sampled NDHQ groups had some form of internal monitoring and compliance cells (as part of their Level One (L1) comptroller group); the others rely entirely on corporate resources within Assistant Deputy Minister (Finance and Corporate Services) (ADM(Fin CS)) and ADM (Materiel) (ADM(Mat)) to fulfill this role. As a result, the extent of monitoring varies considerably. Some groups complained that the same transactions have been reviewed three

[5] Contracting for Professional and Technical Services – 2002/03, Contracting for Advertising and Related Services – 2002/03, Contracting for Healthcare Services – 2003/04, Internal Audit and Assessment Reports related to Contracted IM/IT Maintenance Support – 2004/05, Contracting for Professional Services within Assistant Deputy Minister (Information Management) (ADM(IM)) – 2005/06, all available at www.forces.gc.ca/CRS.
[6] Based on FMAS analysis: 7,152 transactions, $108.6M.
[7] Includes I5 and I9 FMAS transactions during FY 2004/05 – 20,562 transaction lines, $498.7M.

times, while others had rarely or never been reviewed. While at least 26 compliance reviews of acquisition card use have been completed, the FAA Section 34 and FAA Section 33 processes for some multi-million dollar contracts, with high dollar payments, have had limited oversight.

16. Effective monitoring need not be labour-intensive. In a fully integrated P2P process,[8] Smart Controls can be developed based on established business rules. For example, a business rule might preclude payment of any invoice that cannot be electronically matched to a purchase order (PO) and receipt document. Such business rules can be developed, modified, and continuously monitored, with further attention paid only to those transactions flagged as exceptions. Issues such as illegible signatures, or certifications that are not dated become irrelevant in such a system. However, development of such a monitoring system is heavily dependent on standardized processes (so that business rules can be defined) and integrated systems (so that all information relating to a transaction is seamlessly available electronically)—two conditions that continue to elude the Department.

17. **Integrated Procurement to Payment**. The absence of an integrated P2P system not only slows the development of some Smart Controls, it continues to hamper manual monitoring as well. Previous CRS audits have highlighted the requirement for a link between payments and the related contractual vehicles (a linkage provided seamlessly in an integrated P2P system). In response, the Department directed that all invoices must be paid against a pre-established commitment, and that the commitment must provide sufficient information to relate to a contract. While intuitively a reasonable approach, inappropriate implementation of this directive has undermined management information and has had a significant negative impact on the efficiency of the payment process. Two of the six sampled groups have resorted to using bulk commitments, rendering the free balance totally unreliable, contravening the intent of FAA Section 32, and failing to provide the desired contractual information. Because the directive does not differentiate by invoice size and because the vast majority of invoices continue to be of very small dollar value, groups not using the bulk approach have experienced a significant decrease in efficiency. During FY 04/05, approximately 25 percent of commitments were established for amounts less than $500.

18. Many current initiatives related to procurement and payment—including mandatory commitment accounting, increased acquisition card use, mandatory use of SOs, and directed use of the Canadian Forces Supply System (CFSS) for local purchases—appear to be incompatible, and developed in the absence of an overarching P2P strategy. As a result, it is virtually impossible to ensure all current departmental policies and directives with regards to these initiatives are being followed. Consolidation and simplification of these initiatives is warranted.

[8] The P2P process refers to all steps and documents required to acquire and to pay for goods. It includes, for example, the statement of requirements, information on potential sources/vendors, the contract and/or purchase order, any receiving documents, as well as invoices, or acquisition card statements. Accountability for the P2P process within DND is divided primarily between ADM(Mat) and ADM(Fin CS). Source documents are tracked in various systems including MASIS, CFSS, and FMAS.

Adequacy of Management Information

19. Financial comparisons over time or among similar units are hampered by inconsistencies in the financial architecture, frequent restructuring, and ambiguity regarding correct coding. As well, and as previously discussed, current methods of implementing commitment accounting result in unreliable reporting of free Balances. Finally, business plans are not well integrated with information in the Financial and Managerial Accounting System (FMAS), frustrating attempts to measure either performance or the achievement of financial objectives.

20. **Lack of Consistency in the FMAS Architecture**. The financial coding structure is based on Funds, FCtrs, cost centres (CCtrs), and General Ledger (GL) codes. However, there is a lack of common understanding as to what these fields represent, and how they should be properly assigned. Within many groups there is little distinction between FCtrs and CCtrs, with budgets and RC managers being assigned to both. Review of the FMAS FCtr and CCtr descriptions indicates that for the most part the assignment is organizationally based (for example, each section is considered a “cost centre”). However, this is inconsistent. One of the sampled FCtrs encompassed a complete headquarters L1 organization. Their local funding (approximately $130M annually) had not been allocated to any subordinate FCtrs. By comparison, another L1, with much less local funding (approximately $52M annually), had allocated this funding among 14 subordinate FCtrs. Other situations exist where the assignment of FCtrs and CCtrs is activity or even commodity based. An analysis of information based on GLs is equally unreliable. Within this audit, one monthly recurring invoice was observed where charges relating to a single commodity had been allocated to 12 different GL accounts. As well, there have been significant yearly changes to the coding structures. More than 10 percent of FCtrs, CCtrs or GLs were “new” in FY 2004/05.[9] The end result is that comparisons among groups, or between years, lack reliability. This reduces the utility of the information for decision-making purposes.

21. **Business Plans not Integrated with Financial Reporting**. The lack of integration between business plans and the financial reporting system has frequently been documented as a limitation to effective management in the annual attestation process. Among the six observed groups, there is a lack of consistency in the business planning process and, in particular, the method with which resource requirements are documented. While some deviation would be expected, given the varying mandates of L1 groups, the current lack of commonality complicates comparison or consolidation, and increases the difficulty of devising a departmental approach to tracking business planning figures within FMAS. Because the two cannot easily be related, financial performance and achievement of funded objectives cannot be readily measured.

[9] Including 79 of 447 FCtrs, 484 of 4151 CCtrs, and 81 of 1139 GLs. “New” FCtr/CCtr/GL were those with FMAS expenditures in FY 2004/05, but no expenditures in FY 2003/04.

Efficiency of Processes

22. There are currently few standard methods of processing financial transactions. Each of the observed groups used different approaches, some much more efficient than others. Benchmarking studies suggest that streamlining and/or reengineering these processes would result in significant cost savings.

23. **Few Standard Approaches**. A previous audit of travel claims noted that although automated claims processing has been introduced, the majority of groups require additional (as many as six in one group) manual worksheets to complete a claim. In the course of this audit, within one group, five different methods of invoice payment were observed, each with different handoffs, required authorities, and documentation requirements. Approaches to cost recovery, activity tracking, and performance monitoring varied considerably among the observed groups. Efficiency is affected not only directly, as some approaches are more streamlined than others, but also indirectly, as monitoring and review time is increased by the lack of consistency, and training time is increased as personnel must learn new methods when they move among units. The departmental Shared Support Services (SSS) group cited the lack of consistent approaches as a significant challenge to providing trained personnel to complete common services within the Department.

24. **Significant Potential for Savings**. While not new concepts, benchmarking studies continue to state that significant savings are possible through outsourcing, functional consolidation, automation, and/or reengineering. A recent *Deloitte Research*[10] paper suggests that process costs can be reduced by as much as 30 percent by making a zero-based evaluation of how a process should be completed. Current DND process costs have not been documented so it is not possible to extrapolate these saving for the Department. However, in the course of the audit we observed opportunities within all sampled groups to streamline current financial administration processes. Only one observed group was making full use of FMAS for reporting purposes. Within the other five groups, transactions were entered, and re-entered in FMAS, downloaded to spreadsheets for further manipulation, and monitored by several groups—with little added value from a management perspective. This is particularly so given that 73 percent of the transactions comprise only 9 percent of the dollars.[11] Reengineering these processes would free up significant numbers of personnel for more value-added activities.

25. The CRS *Audit of the Management of Local Funds* discussed several strategies to improve the efficiency of financial management, including centralized or consolidated bill payment and movement towards e-commerce and e-business. In addition to increasing efficiency, a more consolidated, automated approach would serve to increase

[10] "Fit for the Future": A Financial Services Industry Study by Deloitte Research.

[11] This analysis is based on transaction type as detailed on page 20/22. A concurrent CRS Audit of Acquisition Card Use determined that in FY 2004/05, expenditures under $5K comprised 92 percent of total invoice and acquisition card transactions but only 8 percent of total dollars paid to vendors.

compliance by restricting certifications to authorized personnel, and providing linkages to all supporting documentation. These strategies, combined with rationalization (or elimination) of low value-added financial practices must be considered if maximum leverage of the Department's finite financial resources is to be achieved.

Principal Recommendations

26. While the audit observations and recommendations have been organized in the areas of compliance, adequacy of information, and efficiency, they are very inter-related and, to some degree, all speak of a need for an overarching strategy for financial management which is seamless and fully integrated. In such a system, plans would be developed, adjusted, funded, and recorded in a fashion that would allow subsequent financial performance to be monitored and measured; delegated authorities would be integrated with system authorities and would be continuously monitored; commitments would be created based on procurement documents; and payments would be clearly linked to all supporting documents. Such a strategy would support compliance, with system controls and continuous monitoring replacing many of the current manual controls. It would also serve to enhance management information and increase efficiency.

27. While increased attention to financial administration is required in the short-term to achieve desired levels of compliance with the FAA and contracting policies, in the longer term, system capabilities must be exploited if labour-intensive manual controls are to be replaced with a more cost-effective, automated control system. It is recognized that current government initiatives in the areas of common support service may impact implementation of such an approach; as a result, the report recommendations are interim steps to facilitate reaching this final state.

Recommendations and Management Action Plan

CRS Recommendation and OPI	Management Response/Action Plan
Improve Compliance by:	
❖ Integrating, streamlining and automating the process for delegation of authorities—OPI: ADM(Fin CS)/DFPP	DND's ultimate goal is to develop and maintain an electronic database of delegated financial authorities, and to relate system access authorities in FMAS, MASIS and other systems to this database. Discussions are under way to develop a database which documents delegated financial authority; proposed completion date is late 2006-07 subject to IM/IT availability. Further work to relate the database to system authorities will commence once Treasury Board Secretariat (TBS) provides clarification on the way ahead for Electronic Authorization and Authentication. Situation will be re-assessed in 2007-08.
❖ Providing improved contracting tools and increased monitoring of contracts for services—OPI: ADM(Mat)/DGMSSC/DMPP; COS ADM(Mat)/DC Pol	Mandating the use of CFSS and MASIS for all procurement and contracting will provide the improved contracting tool required, as it will be based on an end-to-end process that is embedded in one system. Work to improve tools for contracting for services is ongoing. A web-based Service Contracting Requested System implemented in 2005 has increased efficiencies, and created the impetus for more consistent procedures. By providing improved contract tracking and reporting, the system increases managers' ability to analyze contracting patterns and to identify contracting irregularities. In addition, contracting tools and guides, and contracting presentations organized by subject area, have been added to the DC Pol website. Additions and revisions to the DC Pol website will be made on an ongoing basis. DC Pol recently developed the first set of contracting instructions to supplement DAODs. DC Pol will continue to create additional instructions. DC Pol is at the preliminary stage of developing web-based contracting training packages that will consolidate core contracting information. With regards to monitoring, in 2005 DC Pol implemented a web-based Contract Reporting System. Combined with a query tool, this system promotes increased reporting, improves the Department's ability to satisfy contract-reporting requirements, and provides increased monitoring capability. In addition, a Contract Monitoring Framework and a Site Assistance Review Framework have been added to the DC Pol website. These provide standards, based on TB and DND regulations, to apply when reviewing DND/CF contracting activities.

CRS Recommendation and OPI	Management Response/Action Plan
	To date, DC Pol has conducted two site assistance reviews and participated as the contracting subject matter expert on a financial review. The Compliance and Monitoring Cell will take part in future reviews on an as required basis. By April 1, 2006 the current Compliance and Monitoring section in DC Pol will become part of a new Program Integrity Directorate in COS ADM(Mat). Resources will be increased from the past year and the cell will continue to play an oversight and advisory role for contracting compliance and monitoring activities throughout the Department. ***Audit Note*:** *While we applaud efforts to improve contracting standards, training, and information, we believe that increased independent monitoring of contracting activity by subject matter experts is the best means of assuring all TB and departmental requirements are met*.
❖ Completing more consistent, risk-based monitoring, based on business rules—OPI: ADM(Fin CS)/DFPP & DAPPP	As part of the ADM(Fin CS) Performance Measurement Program, DAPPP/AP FAA Compliance Team is developing target levels of compliance based on the level of risk associated with each transaction. They are also reassessing the compliance team resources and will place more emphasis on high-risk compliance. These initiatives will be in place by end FY 2006/07.
❖ Approaching PWGSC to develop a more workable/ accountable approach to interdepartmental settlement transactions—OPI: ADM(Fin CS)/DFPP & DFA	The Government-wide interdepartmental settlement process is established by TBS in consultation with all departments. The present process is not likely to change. Application of the process within DND, however, is an ADM(Fin CS) activity. DFPP and DFA personnel are currently in the process of discussing mandatory FMAS FAA Section 34 and Section 33 certifications as they apply to all interdepartmental settlements. Proposed completion date is 31 March 2007.
❖ Advancing efforts to integrate and fully automate the P2P process—OPI: ADM(Mat)/DGMSSC & ADM(Fin CS)	ADM(Mat) and ADM(Fin CS) recognize the need to implement a standardized P2P process. While work is ongoing to fully integrate MASIS/CFSS/FMAS, timelines will depend on departmental decisions with respect to single enterprise resource planning (ERP) software. The current P2P process developed in MASIS does provide an automated three-way match between the contract, receipt of goods/services, and the invoice. Mandating the use of MASIS and CFSS as the only systems of record for procurement will result in an integrated P2P process.

CRS Recommendation and OPI	Management Response/Action Plan
Enhance Management Information by:	
❖ Revisiting FMAS architecture with a view to standardizing and streamlining—OPI: ADM(Fin CS)/DB, DFPP & DFA	FMAS upgrade 4.7 in September 2006 will align the system with the TBS approved standard Government-wide Integrated Financial/Materiel System Core SAP 4.7. While some aspects were streamlined, FMAS has limited customization to meet some DND specific needs. The next major revisit of the FMAS architecture will occur as part of the DND single ERP currently being lead by VCDS. DFPP established a GL Chart of Accounts Working Group and they are streamlining GLs and providing a consolidated Chart of Accounts document. Proposed completion date for the GL review is 31 March 2007.
❖ Endorsing a more common approach to business planning with integration to FMAS—OPI: VCDS/DDM	Since the Defence Program Activity Architecture (PAA) was approved by TBS June 2005, we have been aligning other processes to it. There is currently a plan in place to more closely align resources and tasks to the PAA. This involves revisions to the Defence Plan, modifications to the business planning process, developing performance indicators to the PAA and attribution of the FMAS CCtrs to the PAA. This cooperative effort should take 2-3 years to reach maturity and primarily involves DDM, DFPPC, ADM(Fin CS) as well as L1 contribution.
❖ Revisiting policy and directives regarding the requirement to link all payments to commitments in FMAS—OPI: ADM(Fin CS)/DFPP	The policy on mandatory commitment accounting was further expanded upon in a DFPP letter dated 23 November 2005, which outlines the differences between funds reservation, pre-commitment, and commitments. This letter provides improved direction to users on how commitments should be used. Additional policy direction to be promulgated during FY 2006-07 and FY 2007-08. ***Audit Note:*** *Policy should focus on ensuring commitments produce accurate, reliable free-balance information. Consideration should be given to whether all payments need to be linked to a prior commitment.*

CRS Recommendation and OPI	Management Response/Action Plan
Develop a Strategy to Improve Efficiency of Business Processes:	
❖ Reengineer to develop and document standard procurement and payment processes—OPI: ADM(Mat)/DGMSSC & ADM(Fin CS)	Under the guidance of the Defence Oversight Committee on Contracting, the following activities will be undertaken: It is agreed that standardized processes and training programs are required. ADM(Fin CS) is currently taking steps to standardize procedures for the use of payment cards across the Department and to standardize the P2P process for all procurement activities. Initial aide memoires and improved training will be available in FY 2006/07. In addition, the ADM(Mat)-developed Procurement Administrative Manual (PAM) is to provide an end-to-end procurement process that includes contracting and payment processes and documents each procurement activity at a very basic level. The PAM also provides training content with the goal to standardize procurement practices across the Department. DGMSSC will mandate and promulgate the PAM as the DND compendium for procurement and contracting. The procurement guidelines in various documents will be replaced with a link directly to the PAM. ***Audit Note:*** *Consolidated ADM(Mat) and ADM(Fin CS) efforts will produce the most efficient results.*
❖ Explore potential for shared services, consolidation, and centralization—OPI: ADM(Mat) & ADM(Fin CS)	The Defence Oversight Committee on Contracting will direct the exploration. More emphasis will be placed on high value, high risk and complex transactions by imbedding contracting resources from ADM(Mat) into other L1 organizations. DFPP is also investigating increased use of Electronic Data Interchange to standardize and centralize large-volume payment processing. Preliminary analysis will begin fall 2006/07. ADM(Mat) will cooperate fully with ADM(Fin CS) in developing a strategy for potential shared services, consolidation and centralization.

INTRODUCTION

Audit Objectives

- To provide assurance that NDHQ financial management processes and practices are effective in ensuring diligent, compliant, transparent use of O&M funds:
  - Consider adequacy of internal controls, performance measurement and management information; and
  - Explore opportunities to increase efficiency in the processing of these transactions.

Scope

- Expenditures for O&M by FCtrs within NDHQ during FY 2003/04 and FY 2004/05, approximately $0.9B annually;
- Examination of the complete expenditure cycle, as shown in Figure 1, including planning and budgeting, delegations and accountability, procurement and contracting, payment and recording, and monitoring and review; and
- A detailed discussion of the audit population is included at Annex A.

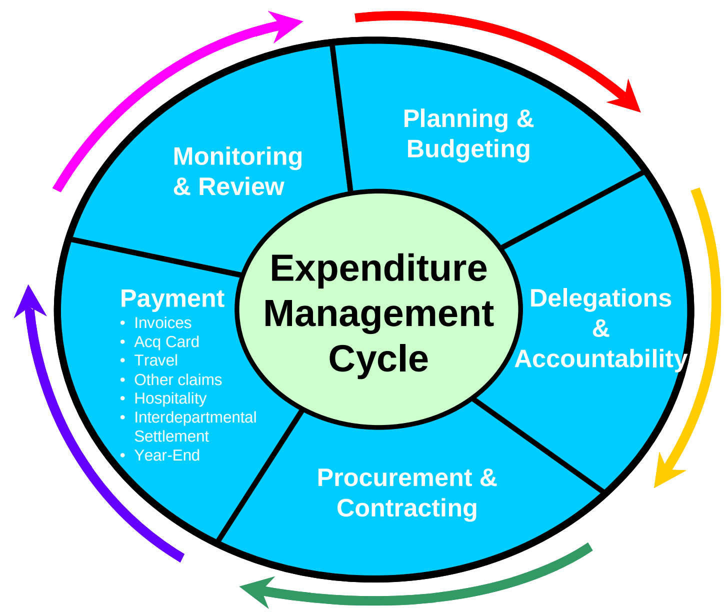

Figure 1—Expenditure Management Cycle.

Methodology

The methodology included:

- Review of relevant policies and directives;
- Population survey based on FMAS data, using computer-assisted audit techniques, see Annex A;
- Development of audit criteria for each phase of the expenditure management cycle, see Annex B;
- Directed sampling, and review of supporting documentation within six NDHQ FCtrs. A profile of the sampled FCtrs is included at Annex C;
- Interviews and discussion with comptrollers, RC managers, RC administrators, finance and supply staff;
- Development of FCtr and departmental "Scorecard" included at Annex D; and
- Benchmarking and literature review.

DETAILED OBSERVATIONS AND RECOMMENDATIONS

Compliance with FAA and Contracting Policies

Higher than desired levels of non-compliance with the FAA and contracting policy persist despite widespread mandatory financial management training. Increased attention to delegations of authority, contracts for services and interdepartmental payments is warranted. In the longer term, a fully integrated, automated P2P process should assist in ensuring cost-effective, efficient compliance.

Higher than desired levels of non-compliance persist.

Transaction Types	Total Examined	Clearly Non Compliant	Some Weaknesses Observed
Acquisition Card	89	33%	65%
Invoices	211	22%	60%
Travel Claim	41	2%	46%
TANS	33	88%	0%
Other Claim	31	10%	52%
Hospitality	30	17%	57%
OGD	47	34%	53%
Year-End (PAYE)	18	0%	28%
Adjusting Entries (SA)	34	0%	47%
Total	**534**	**24%**	**53%**

Table 1—Levels of Non-Compliance.

- As shown in Table 1,[12] 22 percent (46 of 211) of sampled invoice transactions and 33 percent (29 of 89) of sampled acquisition card payments were clearly non-compliant, as they:
  - Were for wrong amounts (including those where PST had been paid);
  - Contained ***no*** FAA Section 34 certification; or
  - Were for over $5K and lacked a properly authorized contract.

- The degree of compliance could be improved for a further 337 of the 534[13] sampled transactions. Weaknesses observed included:
  - FAA Section 34 completed by inappropriate individuals;
  - Lack of FAA Section 34 certification for interdepartmental settlements and Departmental Travel Account/Travel Authorization Number (DTA/TAN) transactions;
  - No evidence of contracting authority for amounts under $5K (e.g., no LPO);
  - Certifications not legible, or not dated;
  - Supporting documentation incomplete or not accessible; and
  - Indications of split contracting, inappropriate sole-sourcing, inappropriate use of SOs and supply arrangements.

[12] Complete sample results have been provided at Annex C.
[13] Overall, 77 percent of sampled transactions exhibited at least one non-compliant characteristic (412 of 534).

- Contrary to some departments, DND has not established target levels of compliance,[14] nor clearly determined critical versus desirable conditions of compliance (e.g., missing certifications versus illegible or non-dated certifications; missing FAA Section 34 on invoice versus missing FAA Section 34 on interdepartmental settlement transaction).
- However, the observed rates of non-compliance, in particular for invoice and acquisition card payments, are much higher than desirable.[15]

Some improvement is occurring…

- ADM(Fin CS) recently developed an on-line training package as part of a Comptrollership Action Plan.
- More than 16,000 individuals have completed this mandatory training as a precursor to retaining delegated authorities.
- This has resulted in increased awareness and, while still too early to measure statistically, appears to be resulting in some improvements. For example:
  - Two of the sampled groups had recently revised their processes for acquisition card purchases and are now maintaining adequate supporting documentation and completing FAA Section 34 certification on these transactions.
  - Another sampled group did not formally document contracts for training during FY 2003/04. This was remedied during FY 2004/05.

…however there is still significant room for improvement.

- We continue to question the quality of many FAA Section 34 certifications.
- In some situations, the individual certifying Section 34 lacks adequate documentation to confirm that goods were received and/or services rendered. Their certification is based on information passed on from others; information which is often not fully documented.
- In addition, invoices were observed which contained insufficient detail to confirm that the rates charged were in agreement with the contract.
- Other invoices contained no link to a PO or a contract, making it impossible to confirm that the quantity and price were as agreed, or that proper contracting authority was exercised.
- In the sample of 211 invoices, 105 instances were observed (50 percent) where FAA Section 34 certification was absent, deemed to be inadequate, or not fully supported.

[14] Benchmarking conducted as part of the Audit of Management of Local Funds determined that one department had established a target compliance rate of 95 percent, while another was targeting 96 percent compliance. In both cases, errors had been clearly defined.
[15] The Audit of Management of Local Funds determined a rate of non-compliance of 7.4 percent; however, results cannot be directly compared due to differences in the sampling methodology.

- In the same invoice sample, there were 89 instances where adherence to proper contracting policy (including proper authority, no split contracting, and adequate competition) was questionable.[16]
- In addition, 88 percent of 33 TAN/DTA transactions sampled were non-compliant primarily because individuals are unaware of the requirement to complete FAA Section 34 certification on these transactions.

Large number of policies—some of which are conflicting—complicate compliance.

- Given the wide range of commodities procured by RC managers, and the multitude of accompanying policies and directives, it is difficult to ensure all relevant rules are followed. The policy regarding provision of hospitality, for example, is well known and, for the most part complied with. However, other specific policies regarding the procurement of items such as ergonomic chairs, picture frames, bottled water, French language training, and most recently, the mandatory use of standing offers, are less well known.
- Conflicting policies and initiatives exist. For example, ADM(Fin CS) is currently encouraging the widespread use of acquisition cards. ADM(Mat) on the other hand, has issued a directive stating all purchases over $1K should be made through a purchasing agent using the CFSS. For many RC managers, these directives appear incompatible.

Managers often have insufficient information to attest to compliance.

- On an annual basis, L1s are asked to attest that all funds have been used in accordance with TB and departmental policy. Typically, L1s' responses are based on input from subordinate RC managers.
- However, many RC managers do not have a "cradle to grave" view of the majority of their financial transactions. The sampled FCtrs processed between 73 percent and 3 percent of transactions against their funding. Four of the six processed less than half the transactions against their funding, as shown in Annex C.
- For the majority of transactions against their funding, these RC managers simply provide financial coding to another group. This group completes the transaction including contracting, receipt of goods and payment. The RC manager often receives no supporting documentation, and subsequently is not in a position to confirm that these funds were used in accordance with policy.

[16] Some transactions contained more than one instance.

- Despite repeated requests, no documentation was provided for 58 sample transactions (11 percent). The majority of these transactions were cases where the funding RC manager had not entered the transaction in FMAS, and did not receive any supporting documentation.

Delegation of Authorities

Delegation of Authority forms have clarified some authorities…

- Financial authorities that are clearly documented and fully understood are fundamental to the management control framework.
- New forms created by Director Financial Policy and Procedures (DFPP) have clarified some authorities, and provide more complete information than the previous specimen signature cards—however, ambiguity continues to exist.
  - Five of the six sampled groups had documented their authorities using the most recent forms, and had completed the required annual review at the time of the audit.
  - In two of the groups, there were instances where the wrong form had been used—i.e., "Other RC manager" rather than "RC administrator"—thereby giving some individuals inappropriate authorities.
  - One of the sampled groups had created confusion by restricting individuals to invoices and claims, while elsewhere on the form granting them authority to raise LPOs or call-ups against SOs.
  - Most forms specified particular CCtrs for which an individual had signing authority. Documentation was incomplete and often unavailable in instances where individuals had been given specific authority to sign for other CCtrs—ADM(Mat) personnel completing FAA Section 34 for invoices charged to other L1 funding for example.

…however, ambiguity continues to exist.

- Delegated authority as it applies to acquisition card purchasing has been recorded separately from other authorities, and has not been subject to annual review. Many issues were observed in the recording of these authorities:[17]
  - None of the six sampled groups had a complete local record of the authorities delegated to acquisition cardholders, and therefore could not ensure purchasing limits and restrictions were adhered to.
  - There was ambiguity regarding the contracting authority of cardholders within all sampled groups.

[17] A concurrent CRS Audit of Acquisition Card Use further documents issues regarding delegation of authority to acquisition cardholders.

- Two cardholders within one sampled group had changed directorates. While the default coding related to their acquisition card had been changed to ensure the proper budget was affected, there was no record that the new RC manager had authorized these individuals to purchase against this funding.
- The authority granted by Director Contracting Policy (DC Pol) to enter into specific contracts is often documented in an e-mail or memorandum. Many groups had less than complete records of these authorities.

The process remains paper-based and cumbersome to track, monitor, update.

- The delegation process remains paper-based and therefore cumbersome and time-consuming to track, monitor and update. Director Accounts Processing, Pay and Pensions (DAPPP) compiles a spreadsheet of authorities within the NCR; however, it contains only key fields and therefore is insufficient for many monitoring purposes. In addition, it is not widely available.
- Delegated financial authorities do not restrict system access or system role(s). For example, the ability to electronically approve claims within Claims-X has not been restricted to individuals with delegated Section 34 authority. A similar situation exists within FMAS. This currently reduces the potential to use automated Smart Controls to ensure valid authorization based on a user's system profile.
- Ultimately, integrating delegated financial authorities with system access authorities will streamline processes, and greatly assist in ensuring compliance.
- Such approaches will eliminate situations of illegible or undated certifications, and wrong payment dates. Combined with robust log-in controls, automated certification processes will reduce the risk of unauthorized transactions being processed.

Problems persist in the area of Contracting for Services.

Contracting for Services

- As shown in Annex A—Figure 3, 40 percent of NDHQ O&M expenditures (approximately $347M in FY 2004/05) are for contracted services. As such, it is not surprising that four of the six sampled groups spent significant amounts on this commodity.
- One of these four groups had recently revisited its contracting practices and currently has a relatively sound control framework. The contracts are primarily for the provision of training courses. Competition is documented, the course content is well defined, and payment is by course serial. Student critiques are used as a quality control tool.

Situations of:

- ***work outside scope,***
- ***contract splitting,***
- ***work in advance of contract, and***
- ***vague statements of work***

continue to occur.

- Contracts for Information Management/Information Technology (IM/IT) services and consulting predominated in the other three groups. Contracts within these groups demonstrated many of the non-prudent characteristics documented in several recent CRS reports.[18]
- We observed: statements of work outside the scope of the contracting vehicle; requirements that appeared to be split in order to stay within call-up limits; extensions and follow-on contracts with little or no documented justification; and individuals entering into agreements without the requisite authority.
- One group had made extensive use of a supply arrangement for IT services related to Government On-Line (GOL). Over a four-year period, it had entered into 161 agreements under this arrangement[19]—58 percent of the arrangements were for approximately $78,875, the call-up limit. Forty percent of all completed call-ups were subsequently amended by 50 percent, again the limit of their authority. The rationale for the amendment was as simple as "work not completed." Further, at least 26 percent of the contractors returned on subsequent contracts within the same area, for periods of up to three years.
- Competition was questionable. While the requisite number of bids was sought, in a high percentage of cases only the company providing the current incumbent completed the bid process.
- One software application which in total cost over $800K was completed using a series of $78K call-ups and subsequent extensions. The total project cost had not been documented nor approved in the group's business plan.
- While RC managers were aware that these practices might not be viewed as "transparent" and "fair", they cited in-year funding limitations as the rational for not engaging in a proper but more time-consuming contracting process. Adequacy of training and clarity of policy did not appear to be the problem, but rather a pervasive culture where following the rules was perceived as secondary to achieving the operational objective.

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[18] Contracting for Professional and Technical Services – 2002/03, Contracting for Advertising and Related Services – 2002/03, Contracting for Healthcare Services – 2003/04, Internal Audit and Assessment Reports related to Contracted IM/IT Maintenance Support – 2004/05, Contracting for Professional Services with ADM(IM) – 2005/06, all available at www.forces.gc.ca/CRS.

[19] Not all of these were within the audit directed sample. However, summary information on these contracts was reviewed as part of the audit conduct.

- Another sampled group contracted for the development of a Managed Readiness Information System using the same GOL vehicle—raising questions as to whether it was within the intended scope as it will not result in an on-line system to provide services to the public. Individual call-ups exceeded the call-up limit by as much as $100K, the requisite competitive bids were not sought, and the individual signing the agreement did so without authority. Further, the invoices contained insufficient detail to confirm correct rates had been charged, and the individual signing FAA Section 34 was not in a position to confirm that the hours had indeed been worked.
- In another sampled situation, a SO providing services related to benefits-driven procurement was used. While the SO stated that individuals contracted under the agreement should have Master in Business Administration, Certified Management Consultant or Project Management Professional qualifications and relevant experience in "e-business solutions," the DND prerequisites were that the individual have a background in science or engineering, as well as 10 years' experience as a military officer. The rate paid, while in agreement with the signed call-up, was not as listed in the standing offer, and while the original agreement was within the call-up limit, it was subsequently amended because the work was not finished.

Payments based on per diem rates, rather than deliverables, remain the norm.

- With the exception of the one sampled group, where payment was by course serial, payments based on per diem rates were the norm.
- Often statements of work were vague, with no clearly defined deliverables. Contractors were engaged "to assist", "to participate in" and to "contribute to."
- While contracts normally state the per diem rate is for a 7.5-hour day, it is not unusual for contractors to bill (at straight time) for 10 to 12 hour days. In addition, many invoices included weekend work. With no documented pre-authorization of extra hours, and no apparent subsidiary time-keeping systems, we question managers' ability to confidently validate these hours at the end of the month.

In some situations contractors are assuming inappropriate roles over lengthy periods of time with questionable value for money.

- We observed situations where contractors had been in place for several years and/or were assuming inappropriate roles. In particular, one individual—who stated he had been a contractor in the organization for ten years—was serving as CCtr coordinator, and was named as our audit point of contact for financial information regarding the group.

- In another sampled organization, a long-serving contractor was in a project management role, and determined which other contractors would be sent specific requisitions.
- In a third sampled organization, we noted a contractor who had been in place at least six years, at a cost approximately four times higher than comparable staff.
- As other audits have reported, we question the validity of a competitive process that continually returns the same incumbent. Succession planning is also suspect if these individuals are the only ones who can fulfill these roles.

- Another group was given a "Corrective Action Suggested" rating in this area on the scorecard (Annex D). While contracted services were not a major area of expenditure for this group, we noted several instances where bulk hotels and meals were paid in the absence of a properly authorized contract. As documented in the CRS Audit of Travel, Hospitality and Conferences, the requirement for contracts, and contracting authority when purchasing these commodities remains not well known.

- Interviewees stated that the urgency of the requirement, in-year funding limitations, insufficient pre-facilitated contracting tools, and shortages of specialist resources resulted in the bypassing of some contracting rules.
- The apparent lack of consequence when inappropriate contracting practices are followed may lead some managers to believe that these practices are condoned or even endorsed.

- Despite the stand-up of the Defence Oversight Committee on Contracting, and DC Pol's Compliance and Monitoring Cell, there is a heavy reliance on individuals certifying FAA Section 34 and FAA Section 33 to ensure proper contracts are in place. This monitoring is late in the process. In addition, many of the issues become apparent only when a more comprehensive view is taken, rather than on an individual transaction basis.

Lack of supporting documentation for inter-departmental settlements makes it difficult for many managers to attest to value for money.

Interdepartmental Settlements

- As shown in Table 2, interdepartmental settlements comprised approximately 11 percent of our target population—over $100M in FY 2004/05.
- Departmentally, approximately 20,000 interdepartmental settlement transactions accounted for expenditures of $499M in FY 2004/05.

- The payments were for a wide range of goods and services, including translation, training courses and furniture. Approximately 20 percent of the dollars within our target population were expended for building rental.
- Several sampled groups expressed concern over the lack of information regarding services provided.
- In accordance with a Public Works and Government Services Canada (PWGSC) imposed FIS process, the DND group establishes a commitment for the estimated value of the service, and the department providing the good/service accesses this funding on completion, often with no further notification to DND.
- Problems arise when the actual cost varies from the committed value, when wrong commitment numbers are used, or when the commitment sits open either because the other department is slow or unable to deliver the service, or is slow to bill.
- While the documented business process states that the funding group must complete FAA Section 34 certification on the accompanying invoice notification, few groups receive such documentation. Further, interdepartmental settlement transactions are currently not included in the Department's FAA Section 33 certification process.
- 34 percent of the interdepartmental settlement transactions in our sample lacked FAA Section 34 certification, while a further 53 percent had an inadequate FAA Section 34 process[20].
- In the absence of a paper trail, and with insufficient electronic information, RC managers cannot fully discharge their responsibilities, and therefore are not in a position to subsequently attest or account for these transactions.
- The current method of interdepartmental settlement has proven very labour-intensive. In FY 2004/05, for period 12 alone, Director Financial Accounting (DFA) force-cleared 1,841 transactions out of the Interdepartmental Settlement Suspense Account at year-end. These transactions totalled over $55M. Three individuals were dedicated to this task at year-end.
- Because interdepartmental settlement payments result in dollars moving among departments, rather than leaving government, some would argue that they are lower risk. However, for individual RC managers, the lack of full supporting documentation makes it difficult to confidently attest to probity and value for money with regards to these transactions. As demonstrated in Annex C, for some RC managers these expenditures are their primary payment type.

[20] Including cases where no documentation was provided to confirm the certification.

- It is difficult for individual RC managers to take corrective action in this regard—departmental or inter-departmental action is required. For this reason, scorecard ratings (see Annex D) for individual groups suggest "Some attention required," while at the departmental level, "Corrective action is suggested."
- Given the materiality of the total dollars involved, the Department should liaise with PWGSC to develop a more workable/accountable approach to settling inter-departmental transactions.

P2P Processes and Systems

Non-integrated P2P processes and systems hamper monitoring and slow the movement to "Smart Controls."

- Providing assurance on compliance with all governmental and departmental policies is complicated by the absence of an integrated P2P process.
- Previous audits have spoken of the difficulty in obtaining all relevant contracts and other procurement documents, as these are not clearly linked to payment transactions.
- We noted similar difficulty in ensuring accountable items were properly recorded on Supply Customer Accounts (SCA), as payment transactions often provide little information on serial numbers, or other traceable characteristics.
- Three sampled transactions involved the purchase of high value musical instruments. These had not been placed on SCA accounts at the time of the audit, increasing the risk of loss or theft.
- For many low-dollar value invoice transactions (up to $5K), purchasing documents do not exist—i.e., LPOs, call-ups, evidence of competitive bids—so proper contracting and purchasing authority cannot be confirmed. For 14 percent (29 of 211) of the sampled invoices, proper contracting could not be confirmed as purchasing documents were incomplete or unavailable.
- Literature reviews indicate that successful development of Smart Controls for the P2P process is dependent on an integrated system, with clear links between all documents related to an individual transaction—i.e., delegated authorities, PO, contracts, receipt documents and invoices.
- Efforts to move to a more comprehensive suite of Smart Controls are hampered by stove-piped, non-integrated systems.
- While more widespread implementation of the Materiel Acquisition and Support Information System (MASIS) may serve to alleviate this issue, implementation has not progressed smoothly or as rapidly as desired.

Monitoring remains inconsistent, and non risk-based.

Monitoring

- As might be expected within a sample of this size, a few transactions were observed which displayed questionable prudence in the use of public funds.
- In one instance, a group paid a civilian elite athlete's costs, including airfare, entry fees, and salary for ten days, to participate in an extreme sporting event. It is questionable whether the objectives of promoting military ideals and values, benefiting recruiting, and retaining high-calibre soldiers were met by sponsoring a civilian.
- In another instance, the cost of post-graduate training for a reservist was reimbursed to an extent far exceeding departmental policy and in the absence of an approved learning plan.
- These instances raise questions regarding an RC manager's authority to spend funds in the absence of clear policy. Neither expenditure had previously been challenged, to some extent because monitoring remains ad-hoc and, with the exception of materiality, non risk-based.
- Three of the six sampled FCtrs had internal review groups while others rely entirely on centralized departmental resources to complete this function. As a result, some interviewees stated they are constantly being questioned while others have never had transactions reviewed.
- In addition, our ability to electronically highlight anomalies, or unusual transactions, (as would be the case with a robust P2P system) remains limited.

Recommendations

Improve compliance by:

- Integrating and streamlining the process for delegation of authorities through automation;
- Providing better contracting tools and increased monitoring of contracts for services;
- Completing more consistent, risk-based monitoring, based on Business Rules;
- Approaching PWGSC to develop a more workable/accountable approach to interdepartmental settlement transactions; and
- Advancing efforts to integrate and fully automate the P2P process.

Adequacy of Management Information

Financial comparisons over time or among similar units are hampered by inconsistency in the financial architecture, frequent restructuring and ambiguity regarding correct coding. Current methods of implementing commitment accounting are very labour-intensive and have decreased the accuracy of free balance information. Additionally, business plans are not well integrated with the financial information reporting systems, frustrating attempts to measure either performance or the achievement of financial objectives.

Financial Architecture

Group/unit financial comparisons are complicated by lack of consistency in the FMAS architecture.

- The Department's FMAS has a coding structure based on fund, FCtr, CCtr, GL and (optional) Internal Order (IO) fields. However, inconsistencies in the assignment of these fields complicate comparisons, and/or performance measurement.
- Determining the audit population was complicated by lack of consistency in "fund" definitions.
- Several organizations, including the Canadian Defence Academy (CDA), the Canadian Forces Medical Group (CFMG) and the Cadets have been designated Corporate, or "C," funds (see Annex A, page 1/3). All expenditures by these groups are recorded to the applicable Corporate fund. As a result, they have no recorded "O&M" or local "L" expenditures. Any measure of departmental operating expenditures, which is based on an analysis of local funds, excludes the day-to-day operating costs of these groups.
- For groups with access to both local and corporate funds, there is often no clear definition as to when each funding source should be used. This results in some large groups (ADM(Mat) for example) reporting lower operating and maintenance costs than some much smaller groups.
- Further confusion exists within the "L" funds. For example, should O&M expenditures related to research and development (R&D) be coded to Fund L101 – Operations and Maintenance expenditures or to L105 – Research and Development? Similarly, should Salary Wage Envelope (SWE) expenses related to Construction be coded to the fund for SWE or the one for Construction? While either approach may have merit, consistency among groups is required if financial performance is to be compared.

There is ambiguity in the assignment and use of:

- *Funds*
- *Fund Centres*
- *Cost Centres*
- *General Ledger codes*

- To highlight the confusion, FY 2004/05 expenditures for paper, pens, and supplies (PP&S) exceeded $40M; $34M was coded to O&M expenses, and the remaining $6M was coded to 23 other funds.

- The budget which funds a particular expenditure is intended to be documented by the "Fund Centre," while the "Cost Centre" records the point of consumption. However, this distinction does not exist in practice. In many cases, CCtrs have become an additional budgetary or planning division. So, for example, furniture, which is paid for by Ottawa, but delivered to Gagetown, cannot normally be distinguished using the financial coding from furniture paid for by Ottawa but delivered to Edmonton. These expenditures are not reflected as a cost of operations for the unit consuming the goods.
- FCtrs (with no further subordinate FCtrs) have been assigned to organizational units ranging from L1s and Directors General, down to Sections and even Units. This complicates comparisons of expenditures for similar units.
- While the delegation document states that an RC manager "*is the incumbent of a position that is allocated a budget…"* and the RC managers guide indicates, "*cost centres have no actual budget*" many groups have assigned RC managers at the CCtr level, complicating accountability, and further reducing comparability among units.

- Selection of the proper GL code is also complex. Many previous audits have discussed the overabundance of GL codes with insufficient direction to distinguish among them.
- In addition, many units select GLs to meet local needs, rather than to ensure accurate departmental recording. They code to unused or unusual accounts as a means of tracking particular expenditures for local purposes. For example, one FCtr codes all costs associated with providing an in-house national freight run (i.e., the "Green Fleet") to a GL for "Rental of Ships and Boats." This provides local visibility to these charges—because no other costs are charged to this GL—and facilitates subsequent cost-recovery. While perhaps meeting local requirements, such approaches provide misleading departmental information and undermine the accuracy of the departmental financial statements.
- A further example of inaccurate and inefficient financial coding is the centralization of procurement and payment for personal data assistant (PDA) rentals for units within the NCR to facilitate contracting and to ensure technological compatibility. A consolidated invoice is received monthly; however, rather than paying the invoice from one budget, the invoice cost is split among all users. A proportion of the invoiced amount is charged to

financial coding provided by each user at the time the service is ordered. No restrictions are placed on the GL used, nor is the appropriateness of the coding challenged. In fact, the billing group is often unaware of the coding used as they simply charge to the provided “commitment.” For one observed month, a $37K consolidated invoice resulted in 132 separate lines of financial coding, many of which were under $100. The charges were recorded to nine funds, 65 FCtrs, and 111 CCtrs. Twelve GL accounts were used including those for telegrams, voice services, professional services, purchase of computers, and purchase of other office equipment.

- Rental of one of the PDAs was coded to a travel GL, with the rationale that travel funding had been used to pay for the expense.

Data inconsistencies complicate comparison, performance measurement, and the development of Smart Controls.

- This lack of discipline in both the assignment and use of the FMAS coding structure complicates comparisons among units. Frequent changes to the structure make it difficult to compare over time. For example, in FY 2003/04 the number of “L” funds was expanded from 6 to 14. There have been similar changes in the number and assignment of FCtrs, CCtrs, and GLs. In FY 2004/05, there were 79 new FCtrs, 484 new CCtrs and 81 new GLs. As a result, it becomes nearly impossible to track and identify some expenditure trends.
- Unreliable coding complicates the development and implementation of Smart Controls, which would highlight exceptions and anomalies. Current attempts result in a very high number of false positives; i.e., situations that appear to be incorrect or unauthorized, which upon further investigation are coding irregularities.
- As well, the lack of discipline in financial coding will undermine departmental efforts to achieve a clean audit opinion on financial statements.
- Until more consistent approaches to coding are mandated and monitored, any comparisons or management decisions based on this information are suspect.
- While the initiative to provide widespread financial training is commendable, it is questionable whether consistency can be achieved if 16,000 individuals are indeed involved in financial management within the Department.

Many commitments are simply bulk planning figures…these provide unreliable free balance information and no improved contracting information.

Commitment Accounting Approaches

- FMAS is intended to provide information not only on expenditures, but also on dollars that have been committed to a particular use by entering into a firm agreement or contract. Reducing budgeted dollars by the amount expended and the amount committed gives a picture of the free balance.
- In a fully integrated P2P process, commitments would be automatically created at the time of purchase initiation, i.e., when a PO is created, a call-up issued, a travel claim initiated, or training authorized.
- In the absence of a fully integrated system, direction was provided that invoices could not be paid without first creating a commitment. In theory, this would not only improve free balance information, but would provide a long-sought link between payments and the contracting vehicle. However, implementation of this policy has not, in all instances, resulted in improved management information.

- Two of the six observed groups had recorded all planning figures as commitments, far in advance of firm contractual obligations to spend, and contrary to the intent of FAA Section 32. One of these groups was using system adjustments (SA) to clear acquisition card transactions, travel expenditures, and even taxi charges against these commitments—a significant investment of labour that provides no additional management information.
- Bulk commitments were observed which provided no subsequent link between payment and contract. An observed $1M commitment was cleared with payments to 27 vendors (therefore involving a minimum of 27 contracts). Payments to these vendors, using this commitment, ranged from $18 to $155K.
- Department-wide, in FY 2004/05, more than 8,000 commitments, with a total value exceeding $1B included payments to more than one vendor, and therefore related to more than one contract.
- In contrast, some contracts relate to multiple commitments.
- In the previous PDA example, for budget monitoring purposes, each of the 132 users had established a unique commitment, implying a separate contract, when in fact, the same contractual agreement was used.
- In FY 2004/05, 11,215 invoices, with a total value exceeding $300M, were coded to multiple commitments.

- In both these cases, i.e., bulk commitment used for multiple contracts, or multiple commitments used for same contract, the desired link between payments and contracts is not being achieved.

Current approach to commitment accounting leads to inefficiencies.

- One RC manager received direction from his L1 comptroller to commit additional funds or risk them being reallocated—despite the fact that the business plan clearly documented the intended use of these funds.
- Another administrator estimated that, to meet departmental requirements, 75 percent of his commitments are entered immediately prior to paying an invoice (providing no additional free-balance information), using arbitrary, locally generated contract numbers.
- Within one of the sampled groups, 55 percent of commitments were for less than $5K (the threshold above which contracting authority is significantly limited); 20 percent of the commitments were established for amounts less than $500.
- Approximately 25 percent of commitments established Department-wide in FY 2004/05 were for amounts less than $500.

- It can be argued that the resulting inaccurate, misleading information is more detrimental than the previous absence of information, in particular in light of the significant impact on efficiency.

Links between Business Plan and Financial Reporting

Difficult to relate financial data to planned activities and outputs.

- Annual attestation letters have frequently cited the difficulty that RC managers have in relating financial data to planned activities and outputs as documented in the business plan.
- The issue initiates with the business plan itself. While each of the observed groups had completed a comprehensive business plan, which documented funding requirements, priorities, risks, and shortfalls, a standard approach does not exist. Each of the six observed business plans, while comprehensive and complete in itself, used a unique approach. As well, each group's requirement for business plans from subordinate FCtrs (or CCtrs) varied. This lack of standardization complicates comparisons, and makes consolidation of the information difficult.
- In addition, lack of a standardized business planning approach makes integration with FMAS more difficult.

Ad-hoc approaches to producing this information are labour-intensive, and do not provide Department-wide results.

- Some groups have attempted to remedy this by assigning IOs (or as mentioned commitments) for tracking purposes. One of the sample groups had assigned over 750 IOs, of which over 400 are active.
- These approaches are very labour-intensive, and not consistently applied.

- As shown in Annex C, SAs comprised 55 percent of one group's transactions—i.e., half the original entries were entered a second time, primarily in an attempt to track against planned activities.

- While groups have good monitoring systems in place to ensure total funding is not overspent, most have little means of ensuring the funds were spent in accordance with the business planning allocation. This limits the Department's ability to apply performance measures to this critical area.

Recommendations

Enhance management Information by:

- Revisiting FMAS architecture with a view to standardizing and streamlining;
- Endorsing a more common approach to business planning with integration to FMAS; and
- Revisiting policy and directives regarding the requirement to link all payments to commitments in FMAS.

Efficiency of Processes

There are currently few standard approaches to processing financial transactions. Each group or unit takes a slightly different approach, requiring different documentation and authorities, and applying different restrictions to essentially the same transaction. Processes are not sufficiently differentiated by dollar value, with the result that small dollar value transactions receive disproportionate attention. Benchmarking studies suggest significant cost savings by streamlining and/or reengineering these processes.

Standard Approaches

Multiple methods of completing common business processes reduce efficiency.

- Few standard approaches to processing financial transactions exist. Even individuals within the same work unit often used differing approaches.
- For example, within one sampled group, one acquisition cardholder had designed a form to document each acquisition card transaction. The form essentially duplicated all information that would have existed on a LPO, negating many of the efficiencies of using an acquisition card. Other cardholders had designed their own log sheets, while still others were not maintaining any supplemental record of acquisition card purchases.
- In another sampled group, we noted five processes for initiating contracts and making payment against them, depending on the source of funding, the contracting authority, and the recording approach.
- Many groups have been reluctant to give up manual processes as automated systems have been introduced. As documented in a recent CRS audit of travel claims, one group was completing six manual forms in addition to entering information into the automated Claims-X system.
- As well, while the reporting capabilities of FMAS have improved with each subsequent release, many groups are hesitant to give up their parallel spreadsheet and other subsidiary systems, creating another source of duplicate effort. Only one of the sampled groups was making full use of FMAS for reporting purposes.

- This lack of consistency makes it difficult to provide training, complicates ensuring compliance, and frustrates the development of business rules useful in developing automated controls.

- Individuals within the Department's SSS Group find it difficult to move from unit to unit without additional training because each group has their own method of executing these common business processes.

Transaction Type	% of Dollars	% of Transactions
Invoices, including interest & adjustments	65%	25%
Acq Cards including adjustments	1%	14%
AMEX airfares	2%	10%
Claims (ACS)	5%	18%
TAXI	< 1%	13%
Payments to OGD's	11%	2%
Adjusting Entries	1%	18%
Year-End	11%	<1%
OTHER	3%	1%
	100%	100%

Table 2—NDHQ In-Scope Expenditures by Transaction Type.

- As shown in Table 2,[21] 73 percent of the overall NDHQ O&M transactions (including acquisition card, airfare, claims, taxi and adjusting transactions) comprise only 9 percent of the net expenditures.
- Efficient processing of these transactions is critical if financial resources are to be fully leveraged, allowing attention to be focused on high-value and/or high-risk transactions.

Current high volume of adjusting entries (SAs) may not be warranted.

- A high percentage of transactions are adjusting entries (SAs). Within the six audited groups, the volume of adjusting entries varied from 6 percent to 55 percent in FY 2004/05 (See Annex C).
- Many of the adjustments are occurring to record transactions against IOs or commitments as previously discussed—a practice of questionable added value. Many other SA's are occurring for the purpose of internal cost recovery.
- We noted one example where a PWGSC contract administration fee charged to one central DND group through seven invoices totalling $164K, resulted in 740 SAs to the groups who initiated the individual contractual requests. Fifty-seven percent of these SAs were for less than $100, which raises questions regarding the administrative cost of this practice versus the alleged improved accuracy of costing information.
- The central group charged the expenditure against coding provided by the client group. In this case, the contract administration charges were recorded against numerous GLs, such as: forms and document printing, public affairs, specialized professional services, management consulting and others.

[21] Columns total more than 100 percent due to rounding.

- Within the total NDHQ O&M population for FY 2004/05, 18 percent of transactions are adjusting entries (SAs)—approaching a million entries. Some 30 percent of these are for amounts less than $100, while more than 60 percent are for amounts less than $500.
- Rationalizing these entries would have a significant impact on efficiency, with only minor (if any) implication on the overall accuracy of data.
- Accounting literature often cites adjusting entries as higher risk transactions because they are manually entered, and often not well supported with backup documentation.

Significant Potential for Savings through Streamlined Financial Processes

- While not new concepts, a 2002 study by Deloitte Research indicates that within most companies there remains significant savings potential through outsourcing, functional consolidation, automation, and reengineering as shown in Table 3.

Category	Potential Cost Reduction
Outsourcing	Up to 10%
Functional Consolidation	10-20%
Automation	15-20%
Reengineering	25-30%

Table 3—Benchmarking – Opportunity for Savings.

- The study[22] points out that the greatest savings are through reengineering—a zero-based evaluation that examines how a process would be designed today if starting from scratch.
- A second study[23] indicates that between 50 and 80 percent of invoice processing costs can be eliminated by reengineering the P2P process.
- In the course of the audit, many transactions were examined where the number of individuals involved and the volume of transactions could be significantly reduced through reengineering—payments for photocopy maintenance, building rentals, commissionaire services and courier services being just a few examples.

- Previous audits have also made recommendations to streamline processes and increase efficiency—targeting opportunities to increase the use of acquisition cards, to more fully automate and integrate the process for travel claims, and to centralize conference planning—to name a few.

[22] "Fit for the Future": A Financial Services Industry Study by Deloitte Research.
[23] « Le monde informatique » – 23 September 2005.

- The benefit of a centralized bill payment approach, currently used by the United Kingdom Ministry of Defence, was discussed in the CRS *Audit of Management of Local Funds.*
- Such an approach could: improve consistency, as far fewer individuals would be involved in entering data in the financial system; improve controls, as expert resources could be applied to validating receipt of goods; and provide processing efficiencies.
- It is difficult to accurately predict the potential savings to the Department through implementation of any of these initiatives, in part as current process costs have not been determined.
- A recent United States of America Department of Defense (DoD) study[24] acknowledges that decades-old financial management problems and various contracting and supply chain challenges, compounded by a multitude of non-integrated information systems, continue to reduce efficiency and effectiveness.
- They estimate that improved efficiency could save 5 percent of their annual budget. However, they point out that this must be accomplished without weakening current control processes.

Recommendations

Develop a strategy to improve efficiency of business processes:

- Re-engineer to develop and document standard procurement and payment processes; and
- Explore potential for shared services, consolidation, and centralization.

[24] "Key Elements Needed to Successfully Transform DoD Business Operations" GAO-05-629T, April 2005.

ANNEX A—POPULATION ANALYSIS

(Based on FY 2004/05 FMAS Information)

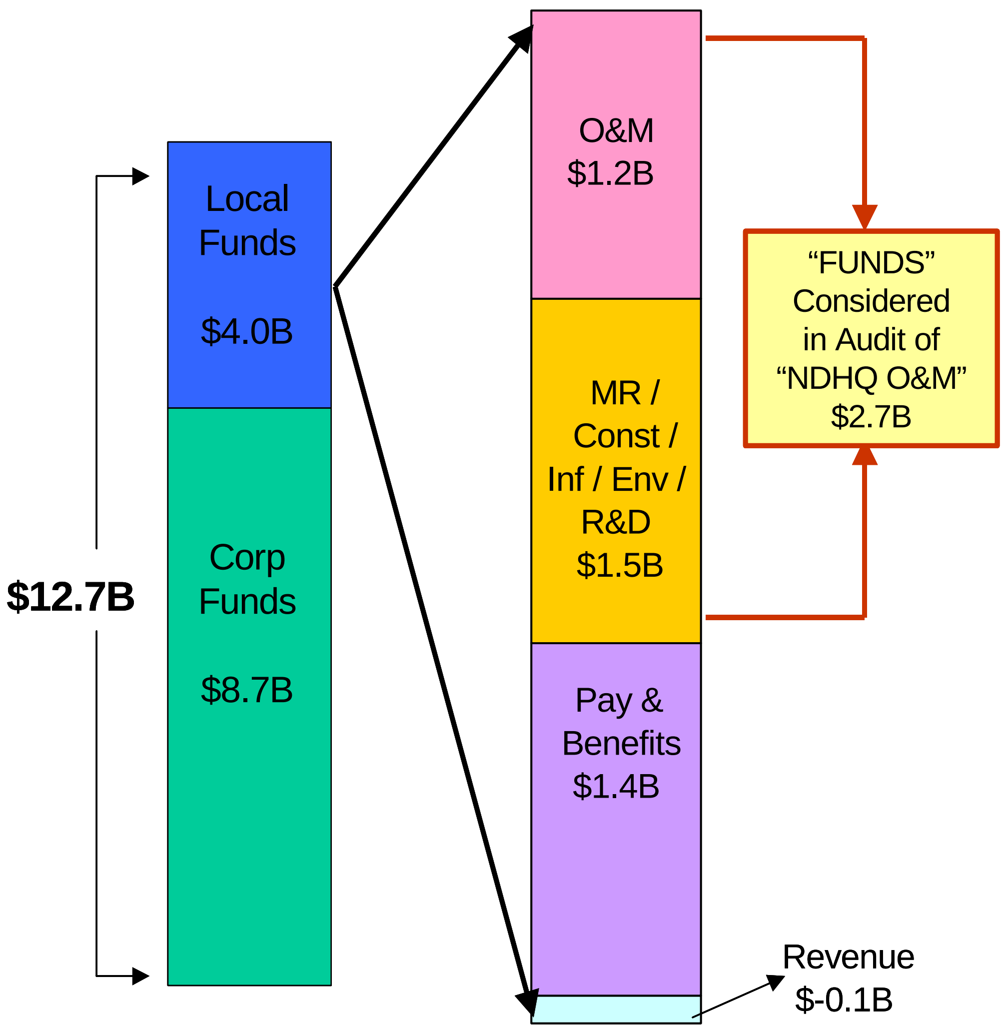

Figure 1—Expenditures by Fund – FY 2004/05.

- FMAS coding structure distinguishes between "Local" Funds (i.e., those funds used by a manager for the functioning of his/her own unit or group), and "Corporate" Funds (i.e., those funds managed by a manager for the benefit of the entire Department, e.g., Military Pay, Capital Acquisition, and Nationally Procured items). This audit considered expenditures of Local Funds.
- Some NDHQ organizations, like CFMG, Canadian Forces Housing Agency, Cadets and CDA only have "Corporate" Funds. Their "Local" or "O&M" expenditures cannot be readily determined based on FMAS information. Audit population is incomplete in this regard.
- Number of "Local" Funds expanded from 6 to 14 in FY 2003/04. Previous to this, Environment, R&D expenditures were included in O&M. The additional funds have created some confusion, for example should PP&S for Environmental or R&D purposes be coded to O&M or to Environment or R&D? Similarly, where should SWE for these purposes be coded?
- Fund analysis highlighted many anomolies. For example, PP&S coded to 26 different local and corporate funds.
- To be consistent with *Management of Local Funds* audit, all "L" funds with exception of Pay and Benefits and Revenue were included in our audit scope.
- Total FY 2004/05 expenditures within the included Funds totalled $2.7B (this was subsequently further reduced by considering only NDHQ FCtrs).

ANNEX A

- Within these "L" funds, audit focus was on NDHQ expenditures.
- No method exists to readily determine if the resources were consumed by an NDHQ or field unit.
- Focused on those expenditures funded by an NDHQ unit, i.e., where the FMAS FCtr was within NDHQ.
- For example, expenditures for trucks delivered to Gagetown, but paid using NDHQ money, would be included in the audit scope.
- $0.9B of the $2.7B of "Local" in-scope expenditures in FY 2004/05 was by NDHQ FCtrs.

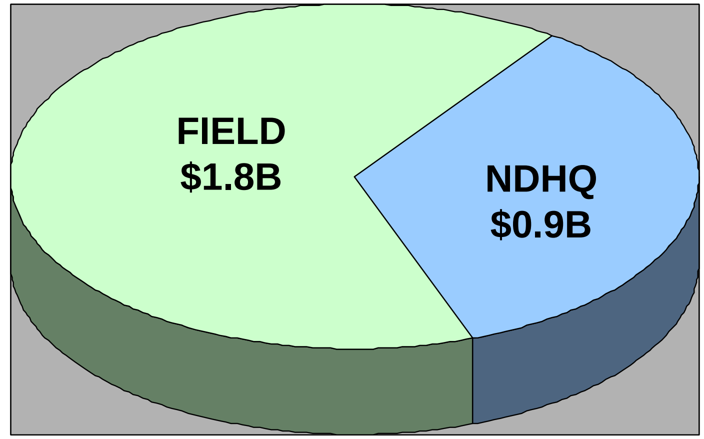

Figure 2—Audit of "NDHQ O&M" In-Scope Local Funds.

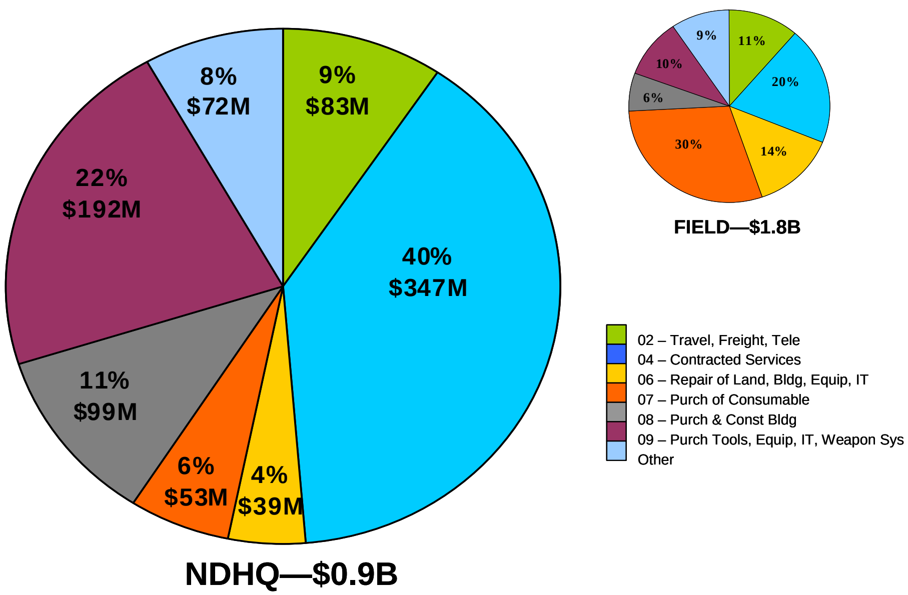

Figure 3—Expenditures by Commodity (SO) NDHQ – $0.9B.

- Examined the commodities (FMAS standard object) purchased by NDHQ FCtrs, and compared to field units.
- Main NDHQ commodity (40 percent) is Contracted Services. Further analysis by GL indicated the services were primarily consulting, IM/IT & professional services.
- This is in contrast to the field where contracted services were primarily for food and cleaning services, and commissionaires.
- Purchase of tools, equipment, IT & weapons is another principal area of NDHQ spending. This emphasizes that the purchases, while funded by headquarters, to a large degree, are not consumed by these groups.

ANNEX A

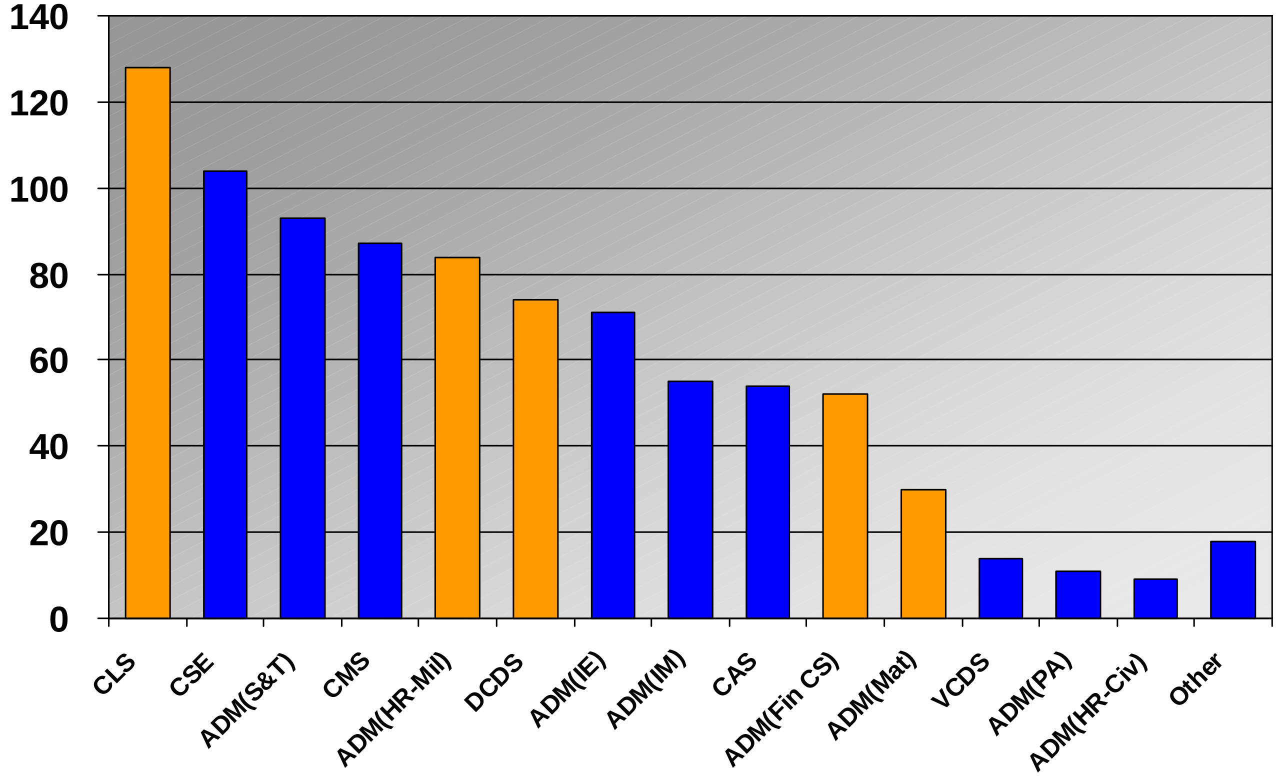

Figure 4—NDHQ In-Scope Expenditures by L1 – $0.9B.

- Further analysis was completed to determine the distribution of "Local" or "O&M" expenditures by L1.
- Analysis suggests that not all O&M expenditures are being captured within these funds. For example, ADM(Mat) has recorded far lower O&M expenditures than ADM(Fin CS), yet is a much larger group. Suggests that a portion of ADM(Mat) O&M type expenditures are recorded within Corporate funds.
- Relative expenditures between the three Environmental Chiefs of Staff suggests that Chief of the Air Staff (CAS) uses a more devolved approach to funding than either Chief of the Land Staff (CLS) or Chief of the Maritime Staff (CMS).
- Sampling approach included transactions from six FCtrs within the five L1s shown in orange in Figure 4.

ANNEX B—KEY CRITERIA

Key criteria were developed to assess each of the review areas. The criteria examined the control framework in place, the creation and reporting of management information, and the processes implemented to manage risk.

Audit Area	Criteria	Control Framework	Management Information	Risk Management
Planning/Budgeting	• Business plan documents resources required by FCtr. • Funding risks have been documented. • Plans and commitments recorded and monitored in FMAS.		✓	✓
Delegations/ Accountability	• Authorities appropriately & consistently assigned, documented, and reviewed. • Annual attestations completed.	✓		✓
Procurement/ Contracting	• Purchasing/contracting is in compliance with delegated authorities. • Purchasing is competitive, quotes maintained. • Contracts have clearly defined deliverables/milestones.	✓		✓
Invoice Payments	• Sufficient information on file to complete Section 34, i.e., LPO, contract, packing slips, timesheets. • Section 34 is properly completed by authorized individual. • Payments are properly recorded in FMAS.	✓	✓	
Acquisition Card Payments	• Use of acquisition cards is in compliance with delegated authorities, and policies. • Sufficient information available to complete Section 34, i.e., receipts, other supporting documents. • Section 34 is completed on a timely basis by authorized individual. • Expenditures properly recorded in FMAS.	✓	✓	
Travel Expenses	• Travel, including airfares is properly authorized, controlled, monitored. • Travel expenses claimed are within policy, properly documented, and appropriately authorized. • Expenses properly recorded in FMAS.	✓	✓	

ANNEX B

Audit Area	Criteria	Control Framework	Management Information	Risk Management
Other Claims	• Claimed items are reasonable and within policy. • An authorized individual completes Section 34, based on sufficient information.	✓	✓	
Hospitality Expenditures	• Hospitality is properly authorized, documented and in compliance with policy.	✓	✓	✓
Interdepartmental Payments	• A process is in place for authorizing services from OGDs. • Section 34 is completed by an authorized individual, based on sufficient information.	✓	✓	
Adjusting Entries	• Adjusting entries which impact a unit's free balance are adequately documented and reviewed.		✓	✓
Year-End Transactions	• A process is in place to ensure Payables at Year-End (PAYE) are properly established and cleared.		✓	
Monitoring/Review	• Fund and Cost Centre managers regularly review transactions against their funding, anomalies are investigated. • Process is in place to monitor and clear unused commitments (including those established as PAYEs) and duplicate payments. • Budget status is reported/discussed periodically with L1 comptroller, Performance Variance Reports (PVR) are used to monitor budget status. • Financial managers are made aware of results of any reviews, corrective action occurs as required. • All source documentation is properly maintained for review purposes.		✓	✓

ANNEX C—SAMPLE PROFILE AND RESULTS

Sample transactions were chosen from six NDHQ FCtrs, representative of five L1 groups. A comparison of the FCtrs based on FY 2004/05 FMAS information is shown in Table 1. As would be expected by their diverse mandates, the FCtrs varied considerably in dollars expended, commodities purchased, and primary payment types.

The volume of adjusting entries (SAs), which varied from 6 percent to 55 percent, speaks to the FCtr's method of recording management information. Two of the FCtrs track business plans using commitments, a third used IOs for this purpose. In each of these FCtrs, a large percentage of transactions are entered twice to record all desired information. This has a significant impact on processing efficiency.

The percentage of dollars processed for payment (settled) by the sampled FCtrs varied from 3 percent to 73 percent. This indicates the degree to which a FCtr has "cradle to grave" control over the transaction, as opposed to simply providing their coding (and funding) to another group, with little subsequent control over procurement and/or payment. This impacts accountability, and the confidence with which the FCtr manager can attest that all funds were used prudently and in accordance with FAA and contracting regulations.

	Fund Centres					
	1	2	3	4	5	6
FY 2004/05 Expenditures within Sample Scope	$2.3M	$9.3M	$4.8M	$3.0M	$128.9M	$5.3M
Principal Commodities	Hospitality, Travel	Building Rental, Furniture, Telecom Installations	Contracted Software Development, Prof Serv, Temp Help, IT Equip	Training, Travel for Training	Wide range including Construction of Buildings, Purchase of Vehicles, IT Equip, Travel, Prof Serv, Temp Help	Consulting Services, Building Rental, Temp Help
Primary Payment Type by $s	Claims	Interdepartmental Settlements	Invoices	Invoices	Invoices	Invoices
Volume of Adjusting Entries	8%	38%	7%	55%	21%	6%
% Settled by FCtr	73%	3%	41%	51%	13%	35%

Table 1—Comparison of Fund Centres.

ANNEX C

Table 2 gives a breakdown of the number and type of transactions sampled by FCtr.

Directed rather than statistical sampling was used to ensure a wide variety of transactions types were examined within each FCtr, causing some transaction types to be over-sampled relative to dollars expended. As a result, error rates cannot be extrapolated to determine the dollar value of errors.

In addition, error rates cannot be directly compared to results in OGDs, or to results in other CRS audits such as the Audit of Management of Local Funds. Such comparisons would imply a consistency in sampling approach and error definition that currently does not exist.

Sampled Transactions	Fund Centres						
	1	2	3	4	5	6	TOTAL
Acquistion Card	13	7	18	25	12	14	**89**
Invoices	23	25	35	36	66	26	**211**
Travel Claims	11	4	4	8	11	3	**41**
TANS	19	4	0	3	5	2	**33**
General Allowance Claims	3	1	4	4	13	6	**31**
Hospitality	8	7	0	6	8	1	**30**
Payments to OGDs (ISs)	7	17	2	5	8	8	**47**
Year-End PAYES	3	3	5	5	0	2	**18**
Adjusting Entries (SAs)	14	4	6	3	3	4	**34**
TOTAL	**101**	**72**	**74**	**95**	**126**	**66**	**534**

Table 2—Sampled Transactions.

ANNEX C

SAMPLE RESULTS

- (Green) Column showing number of transactions examined for each transaction type.
- (Orange) Columns showing number of occurrences of a particular error within the sampled transaction type. A single transaction may contain several errors. The blue headings within this area, (i.e., “No FAA Section 34”) highlight those errors considered “Clearly Non-Compliant,” while the errors with purple headings were considered “Compliance Weaknesses.”
- (Blue) Columns indicating number and percentage of “Clearly Non-Compliant” transactions, including those with no FAA Section 34, wrong payment amount and/or which are non-complaint with contracting policy. Each transaction is counted only once.
- (Purple) Columns indicating number and percentage of transactions that contain any of the other listed compliance weaknesses. Each transaction is counted only once.

Transaction Types	Total examined	Inadequate FAA Section 32 *	No FAA - Section 34	Inadequate FAA Section 34 **	Insufficient supporting documentation for FAA Section 34	Wrong Payment Amount	Inaccurate GL used	Non-compliant with contracting policy	No proper evidence of contracting authority ***	Appearance of contract splitting	Questionable competitiveness within contracting	Other types of Non-compliance ****	Documentation Not Found	Clearly Non-Compliant (#)	Clearly Non-Compliant (%)	Compliance Weaknesses Observed (#)	Compliance Weaknesses Observed (%)
Acquisition Card	89	6	23	32	29	9	23	1	1	0	0	22	14	29	33%	58	65%
Invoices	211	2	13	57	35	3	14	39	29	9	12	44	21	46	22%	127	60%
Travel Claim	41	7	1	1	2	0	6	0	0	0	0	11	4	1	2%	19	46%
TANS	33	0	29	0	0	1	0	0	0	0	0	1	0	29	88%	0	0%
Other Claim	31	1	0	1	2	2	6	1	3	0	0	5	7	3	10%	16	52%
Hospitality	30	0	3	5	0	0	8	1	2	0	0	15	3	5	17%	17	57%
OGD	47	0	16	24	28	0	1	1	0	0	0	0	9	16	34%	25	53%
Year-End (PAYE)	18	0	0	0	0	0	0	0	0	0	0	1	0	0	0%	5	28%
Adjusting Entries (SA)	34	0	0	0	0	0	0	0	0	0	0	0	0	0	0%	16	47%
Total	534	16	85	120	96	15	58	43	35	9	12	99	58	129	24%	283	53%

*** Inadequate Section 32 includes:**

Pre-approval for travel and training not clearly documented

Claim not approved by supervisor

**** Inadequate Section 34 includes:**

Not dated

Section 34'd after payment made

Illegible name

Signed by inappropriate individual (ie: no Authority for CCtr, Doc Type or Commodity)

***** No Evidence of Contracting Authority includes:**

No Local Purchase Order

No Call-up against Standing Offer

****** Other types of Non-Compliance includes:**

Hospitality approval incomplete / inadequate

Hours worked not within contract, or no apparent record to verify hours

Old year purchases paid out of new year funds

Wrong payment method for commodity (ie: Travel, Fuel on Acq Card, non-travel on AMEX)

Inappropriate Contracting Tool, weak Statement of Work, Poor/No justification for contract extension

ANNEX D—SCORECARD

A scorecard was produced to document results for each of the sampled FCtrs. Numbers 1 through 6 represent the sampled FCtrs, ✓'s indicate positive observations, while ×'s are undesirable observations. Individual results were considered in determining the departmental score. In some cases, the departmental score is lower than individual FCtrs because the magnitude and impact of the issue only becomes apparent when a Department-wide view is taken. An "orange" rating has been used rather than "red" to highlight that current processes need improvement, but need not nor cannot be "stopped."

Review Area	1	2	3	4	5	6	Dept	Remarks
Planning/ Budgeting								✓ Business plans (BP) for six sampled FCtrs all document resource requirements, priorities, gaps and funding shortfalls. × Lack of standard approach to BP complicates comparison, roll-up, and increases resources devoted to preparation. × Only one sampled FCtr could easily compare FMAS resource consumption to BP figures; others cannot use FMAS to readily measure financial performance. × FMAS PVR cannot be used to monitor free balance for five sampled FCtrs—4 FCtrs had not entered planning figures, 4 FCtrs were not properly recording all commitments (i.e., using bulk commitments, or relating to activities vice contracts).
Delegations/ Accountability								✓ 5 of 6 sampled FCtrs had up-to-date delegated authorities documented using current forms. ✓ Mandatory financial management training completed in all six groups. × Instances in two sampled groups where individuals given inappropriate authorities, wrong forms used. × Restrictions not clearly stated. One group entered restriction of "Invoices and Claims" for most individuals while elsewhere delegating them authority to raise LPOs and call-ups against SOs. × Department-wide, acquisition cardholder authorities not subject to annual review, not integrated with other delegated authorities. × None of sampled FCtrs had complete local record of delegated authorities of acquisition cardholders. × All groups had ambiguous delegated contracting authority for some acquisition cardholders. × Current paper-based method of recording authorities is cumbersome, does not facilitate updating, monitoring. × 4 of 6 sampled FCtrs process less than 50 percent of transactions against their funding; difficult for RC manager to attest to probity, compliance.

	No corrective action required at this time
	Some attention required or corrective action has only recently occurred
	Corrective action suggested

ANNEX D

Review Area	1	2	3	4	5	6	Dept	Remarks

Procurement/ Contracting								✓ Large contracts for goods processed through appropriate authorities.
								✓ One group had significantly improved contracting processes in FY 2004/05 over FY 2003/04.
								× LPO and Standing Offer Agreement (SOA) documentation often not completed—proper authorities often not evident.
								× 68 sample transactions were clearly non-compliant with contracting policy, or there was no evidence of contracting authority.
								× Competitive quotes often not maintained, rationale for sole sourcing not documented for small to mid-sized contracts.
								× Contracting for services remains problematic:
								  × Majority had vague statement of work, few concrete deliverables;
								  × Several call-ups where work outside of scope of contract;
								  × Much appearance of contract splitting within one observed group;
								  × Some work in advance of contract;
								  × SOA and SA requirements re. limits, competition, signing authorities not always adhered to;
								  × Many amendments with insufficient justification; and
								  × Two observed instances where contractors play inappropriate role in contract management.
								× Overall, 89 instances of non-compliant or questionable contracting practices (some transactions contained more than one).

Invoice Payments								× 13 of 211 sampled invoices contained ***no*** FAA Section 34 certification. × 35 had insufficient supporting documentation to confirm FAA Section 34, including no LPO or SOA and/or no evidence of contracting authority. × 57 invoices had inadequate FAA Section 34 including illegible signatures, or signatures not dated. Correct payment on due date could not be confirmed for 31 of the invoices. × 3 payments did not agree with contracted amount. × Some invoices for services contained insufficient breakdown of hours to properly confirm. × 3 of 6 groups had no clear process to certify contractor hours worked, in particular weekend and hours after normal business day. × Some financial coding could be more accurate; 14 invoices were inappropriately coded. × RC manager could not/did not provide documentation for 21 transactions.

	No corrective action required at this time
	Some attention required or corrective action has only recently occurred
	Corrective action suggested

ANNEX D

Review Area	1	2	3	4	5	6	Dept	Remarks
Acquisition Card Payments								✓ Primarily low-dollar value, low-risk purchases. ✓ No inappropriate purchases observed. ✓ 2 groups had recently revised process for authorization, certification. ✗ 9 of 89 sampled acquisition card payments were wrong amount (8 included payment of PST, one where also paid invoice for same amount). ✗ Documentation could not be found for 14 transactions. ✗ 23 acquisition card transactions had ***no*** FAA Section 34; 32 had inappropriate FAA Section 34 (primarily because not RC manager). ✗ For 3 groups, process in place is very cumbersome; efficiency gains may not be realized.
Travel Expenses								✓ Most supporting documents well maintained. ✗ Audit trail for Section 32 (prior approval of travel) could be improved. Proper FAA Section 32 not evident for 7 of 41 sampled travel claims. ✗ 29 of 33 sampled DTA/TAN expenditures had no FAA Section 34 certification. (88 percent) ✗ 1 travel claim involved a $1,200 payment error; subsequently recovered.
Other Claims								✓ Most supporting documentation well maintained. ✗ Prudent, equitable use of funds questioned in 2 cases.
Hospitality Expenditures								✓ Transactions recorded as hospitality for most part thoroughly documented, appropriately recommended and properly authorized. ✗ 13 instances observed where proper hospitality authority not obtained; majority not recorded as hospitality. ✗ 3 had no FAA Section 34; 5 had inadequate FAA Section 34.
Inter-gov't payments								✓ Payment against commitment helps to ensure charges are authorized, supported. ✗ Most groups have little in the way of supporting documents for these payments. ✗ 40 of 47 sampled transactions had either ***no*** FAA Section 34 certification, or inadequate certification.
Adjusting Entries								✓ Most groups maintain supporting documentation for large SAs. ✗ Extent of SAs may not be warranted, significant workload with little improved information overall. SAs comprised 55 percent of transactions for one group. ✗ Used to some degree to balance budgets, to code expenditures to match plans.
Year-End Transactions								✓ Most groups have method of ensuring all PAYEs are valid old year expenditures. ✗ In one group, PAYEs accounted for 10 percent of total expenditure, approximately 50 percent cleared without consumption in following year.

	No corrective action required at this time
	Some attention required or corrective action has only recently occurred
	Corrective action suggested

ANNEX D

Review Area	1	2	3	4	5	6	Dept	Remarks
Monitoring/ Review								✓ All groups complete regular budget status monitoring. ✓ All groups have method of monitoring and clearing unused commitments and PAYEs. ✗ 3 of 6 groups had internal monitoring capability (through L1 comptroller staff); extent of compliance monitoring, financial staff-assisted visits varies among groups. ✗ Monitoring does not appear to be risk based. ✗ Method of monitoring/review does not facilitate performance measurement. ✗ Focus is on staying within budget; value for money, prudent use of funds not thoroughly assessed.

	No corrective action required at this time
	Some attention required or corrective action has only recently occurred
	Corrective action suggested

ANNEX E—LIST OF ACRONYMS

ADM(Fin CS)	Assistant Deputy Minister (Finance and Corporate Services)
ADM(IM)	Assistant Deputy Minister (Information Management)
ADM(Mat)	Assistant Deputy Minister (Materiel)
BP	Business plan
CAS	Chief of the Air Staff
CCtr	FMAS Cost Centre
CDA	Canadian Defence Academy
CFMG	Canadian Forces Medical Group
CFSS	Canadian Forces Supply System
CLS	Chief of the Land Staff
CMS	Chief of the Maritime Staff
COS ADM(Mat)	Chief of Staff ADM(Mat)
CRS	Chief Review Services
DAPPP	Director Accounts Processing, Pay and Pensions
DB	Director Budget
DC Pol	Director Contracting Policy
DDM	Director Defence Management
DFA	Director Financial Accounting
DFPP	Director Financial Policy and Procedures
DFPPC	Director Force Planning and Program Coordination
DGMSSC	Director General Materiel Systems and Supply Chain
DMPP	Director Materiel Policy and Procedures
DND	Department of National Defence
DoD	Department of Defense (United States of America)
DTA/TAN	Departmental Travel Account/Travel Authorization Number
ERP	Enterprise resource planning
FAA	*Financial Administration Act*
FCtr	FMAS Fund Centre
FIS	Financial Information Strategy
FMAS	Financial and Managerial Accounting System
FY	Fiscal year (April 1 to March 31)
GL	FMAS General Ledger
GOL	Government On-Line
IO	FMAS Internal Order
IM/IT	Information Management/Information Technology
L1	Level One (reports directly to either DM or CDS)
LPO	Local purchase order
MASIS	Materiel Acquisition and Support Information System
MoD	United Kingdom Ministry of Defence
NCR	National Capital Region
NDHQ	National Defence Headquarters
O&M	Operations and Maintenance
OGD	Other government department
P2P	Procurement to payment
PAA	Program Activity Architecture
PAM	Procurement Administrative Manual
PAYE	Payable at Year-End
PDA	Personal data assistant
PO	Purchase order
PP&S	Paper, pens and supplies
PVR	Performance Variance Report
PWGSC	Public Works and Government Services Canada
R&D	Research and development
RC	Resource centre
SA	FMAS system adjustment (adjusting entry)
SCA	Supply Customer Accounts (formerly DA)
SO	Standing offer
SOA	Standing Offer Agreement
SSS	Shared Support Services
SWE	Salary Wage Envelope
TB	Treasury Board
TBS	Treasury Board Secretariat
VCDS	Vice Chief of the Defence Staff