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## Audit of the Recovery Process of Contract Overpayments

September 2011

7053-75 (CRS)



Canada 

## **Caveat**

This audit is not intended to assess the performance of Public Works and Government Services Canada (PWGSC) or contractors; rather, it is an internal assessment of processes and practices within the Department of National Defence (DND).



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## Acronyms and Abbreviations

ADM(Fin CS)	Assistant Deputy Minister (Finance and Corporate Services)
ADM(Mat)	Assistant Deputy Minister (Materiel)
A/R	Accounts Receivable
ASC	Audit Services Canada
CA	Contract Authority
CAG	Cost Audit Group
CAP	Cost Audit Program
CRS	Chief Review Services
DFA	Director Finance and Administration
DFPP	Director Financial Policy and Procedures
DGMSSC	Director General Materiel Systems and Supply Chain
DMPP	Director Military Program Planning
DND	Department of National Defence
DRMIS	Defence Resource Management Information System
FAM	Financial Administration Manual
FSR	Field Service Representative
FY	Fiscal Year
GL	General Ledger
ICS	Interim Contract Support
OPI	Office of Primary Interest
OWSS	Optimized Weapons Support System
PA	Procurement Authority
PAV	Primary Air Vehicle
PWGSC	Public Works and Government Services Canada
WLAV	Wheeled Light Armoured Vehicle



## Results in Brief

In accordance with the Chief Review Services (CRS) internal audit work plan for fiscal year (FY) 2009/10, CRS conducted an audit on the recovery of overpayments from contract management and cost audits.

Between January 2003 and February 2010, CRS received 213 Audit Services Canada (ASC) reports regarding audits on DND contracts. The audit reports identified potential overpayments of \$71.8 million to be further investigated by the Crown. After an ASC audit report is issued, PWGSC takes the lead on confirming the overpayments and negotiating a settlement with the contractor. DND, as the Procurement Authority (PA) for the contract, is responsible to collect, and record the refund from the contractor.

Prior to the 2009 PWGSC renewal of the Cost Audit Program (CAP), PWGSC funded all contractor audit services and determined which contracts were audited. The renewal of the CAP required that client departments pay for the cost of the contractor audits in the future.<sup>1</sup>

### Findings and Recommendations

**Monitoring.** The turnover of DND PAs and the absence of a central point of contact have resulted in limited visibility regarding the status of overpayment recoveries. Of 47 sampled ASC audit reports, DND PAs were able to provide information regarding the recovery of potential overpayments for only three. Of the surveyed PAs who started after an ASC audit of their contracts had been completed, none was made aware of the audit and that possible follow-up was required. Additional information was collected from PWGSC which demonstrated that recoveries totalling \$21.25 million were received for 27 of the sampled 47 ASC audit reports. At the time of the audit, recoveries related to 14 reports were under negotiation. At least two years had elapsed from the date the ASC report was issued for all 14 reports. The longer the negotiations take the more difficult it is to recover overpayments due to the turnover of DND PAs and the increased difficulty of locating and verifying supporting documentation.

It is recommended that the Assistant Deputy Minister (Materiel) (ADM(Mat)) establish a central point of contact to collect contractor audit information and monitor the progress of settlement negotiations for ADM(Mat) contracts.

### Overall Assessment

To take full advantage of the opportunities for savings identified in contractor audits, the Department needs to implement better risk management practices and strengthen the governance and monitoring of the contractor overpayments recovery process.

<sup>1</sup> November 2009 PWGSC Communiqué to all Acquisitions Branch employees regarding the CAP.

**Governance.** While some departmental guidance exists in the Financial Administration Manual (FAM), accountabilities need to be further defined and procedures need to be better communicated. Evidence from project files indicated that recoveries of \$22.2 million had been credited to current or future contractual liabilities instead of being recorded as “Refunds Previous Year’s Expenditures.” Crediting the refunds against current year expenses results in the refund being re-spendable by the Department. This is contrary to departmental guidance, as refunds of previous years’ expenditures are considered “governmental” rather than “departmental” revenue.<sup>2</sup> Although also considered governmental revenue, statutory authority is currently provided to DND to spend an amount equal to the proceeds from the disposal of surplus assets. Similar authority does not exist for refunds from previous years’ expenditures. As an incentive for DND to engage additional contractor audit services in the future, it is suggested that ADM(Mat), in conjunction with the Assistant Deputy Minister (Finance and Corporate Services) (ADM(Fin CS)), investigate the possibility of requesting statutory authority to spend an amount equal to the refund of previous years’ expenditures relating to contract overpayments. In addition, transactions should be better identified in the Defence Resource Management Information System (DRMIS), as currently aggregate recovery information is not readily available.

It is recommended that ADM(Fin CS) update the FAM to clearly stipulate accountabilities for the contract overpayments recovery process, provide better guidance on the procedures for recording recoveries of contract overpayments and enhance the identification of recovery transactions in DRMIS.

**Risk Management.** Observations made in the ASC audit reports have not been developed into lessons learned that are shared across the Department. Based on CRS analysis of the overpayments identified in the sample of 47 ASC audit reports, four of the ten common types of overpayments may require additional contractor audits to effectively mitigate, as these types of overpayments cannot be identified through current FAA Section 34 verification. However, contractor audit coverage on DND contracts has declined over the years and, at the time of this audit, no new contractor audits had been confirmed for 2011. One of the main reasons is that contractor audit services, previously funded by PWGSC, must now be funded by client departments and currently guidance on funding options has not been made clear. Contractor audits early in the life of a long-term contract can be a deterrent for future overcharges, thereby providing the Department with a direct financial benefit.

It is recommended that ADM(Mat), in conjunction with PWGSC, develop a risk-based model to assess contract risks of overpayment and utilize additional contractor audit services.

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<sup>2</sup> FAM Chapter 1018-1 Managing Public Revenue.

**Request for ASC Audits.** DND has taken action on six of the seven previous audit recommendations which suggested that PWGSC be requested to investigate potential overpayments of \$42.62 million. Prior to the PWGSC renewal of the CAP, DND could recommend, but did not determine whether or when an audit or further investigation would occur. At the time of this CRS audit (April 2011), an ASC audit had been initiated on five of the seven recommended contracts and a sixth contract had been investigated by the PWGSC Contract Authority (CA). Negotiations were complete for two of these six contracts. At the time of the CRS audit, DND had recovered \$1.17 million.

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**Note:** For a more detailed list of CRS recommendations and management response, please refer to [Annex A](#)—Management Action Plan.

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## Introduction

### Background

Between January 2003 and February 2010, CRS received 213 ASC audit reports identifying \$71.8 million of potentially recoverable excess profits and overpayments<sup>3</sup> related to defence contracts. Once an audit reports is issued by ASC, the responsible PWGSC CA is to validate the observations with the contractor and negotiate a settlement. While PWGSC takes the lead in initiating ASC audits and in negotiating a settlement, DND as the PA is responsible to collect and record the contractors' refunds.<sup>4</sup>

CRS does not have the authority to conduct external audits on defence contractors, but rather has audited DND's management of some higher-risk defence contracts. Potential overpayments of \$42.62 million were identified in seven previous CRS contract management audits. All seven audits recommended that DND request PWGSC assistance in initiating ASC audits to validate these potential overpayments.

### Objectives

The objective of this audit was to assess DND control, governance and risk management practices related to the contract overpayments recovery process.

### Scope

The audit scope included:

- DND policies, business processes and practices regarding collecting and recording contractor refunds pertaining to the 213 ASC audit reports issued between January 2003 and February 2010; and
- DND actions on the recommendations in seven previous CRS contract management audits relating to overpayment recoveries.

This is not an audit of PWGSC or the contractors' business processes. Due to the absence of information within DND for 44 of the 47 sampled audit reports, information was obtained from the PWGSC Cost Audit Group (CAG) electronic database and paper files. However, the CRS audit team did not audit the CAG recovery tracking system.

### Methodology

- Distributed questionnaires to DND PAs responsible for 24 of the contracts audited by ASC to determine the amount recovered and DND PAs' understanding of the cost recovery process. The 24 contracts were managed by 18 DND PAs.

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<sup>3</sup> ASC, a group within PWGSC, conducts audits to assess any excess profit or overpayments in contractors' claims to the Crown by validating the accuracy of actual costs and labour recording systems. Excess profits are only recoverable if the series of all contracts by the same contractor are audited. On a voluntary basis, ASC sent 213 reports to CRS between January 2003 and February 2010. However, there could be more ASC contract audit reports completed for DND during this period that were not forwarded to CRS.

<sup>4</sup> PWGSC Supply Manual, Chapter 8 Annex 8.5, January 2010.





- Interviewed staff at ADM(Fin CS), ADM(Mat), PWGSC internal audit, PWGSC CA, and PWGSC CAG.
- Reviewed DND, PWGSC and Treasury Board policies and procedures.
- Collected and analyzed data in Contracting Database Management System, DRMIS, PWGSC contracting database and PWGSC CAG record keeping system.
- Selected a sample of 47 contracts audited by ASC with potential recoveries of \$57.5 million in order to determine the actual dollar amount recovered. This sample provided 80 percent coverage of the total potential recoveries of \$71.8 million identified in all 213 ASC audit reports between January 2003 and February 2010.



## Findings and Recommendations

### Monitoring

Additional funds may be recovered more rapidly if the Department establishes a monitoring process for recoveries of contract overpayments.

### Procurement Authority Turnover

The turnover of PAs and the absence of departmental central monitoring of recoveries of contract overpayments result in limited visibility of the status of recovery actions within DND. Resolution information<sup>5</sup> was available for only three of 47 sampled ASC audit reports managed by 18 DND PAs.

- Six of the 18 PAs were aware that an ASC audit took place but three of the six either did not know the resolution of the audit findings or could not provide evidence.
- The six PAs who were aware of an ASC audit were in their current position at the time of the ASC audit. PAs who were not in place at the time of the audit had not been made aware of the audit and that follow-up action might be required.

The CRS audit team consulted PWGSC for information regarding the resolution of the remaining 44 samples. Table 1 summarizes the gathered information.

Sample Status	Source of Information	No. of Files	Potential Recoveries Identified in ASC Audit Reports	Settlement Amount	\$ Recovered
ASC Audit with Known Resolution	DND	3	\$12.60M	\$8.45M	\$8.71M
ASC Audit with Known Resolution	PWGSC	24	\$23.03M	\$12.54M	\$12.54M
<b>Total with Known Resolution</b>	N/A	<b>27</b>	<b>\$35.63M</b>	<b>\$20.99M</b>	<b>\$21.25M</b>
ASC Audits with Unknown Resolution – in Progress	N/A	14	\$14.15M	N/A	N/A
ASC Audits with Unknown Resolution – No Information	N/A	6	\$7.70M	N/A	N/A
<b>Total with Unknown Resolution</b>	N/A	<b>20</b>	<b>\$21.85M</b>	<b>Unknown</b>	<b>Unknown</b>
Complete CRS Sample	N/A	47	\$57.48M	N/A	N/A

**Table 1. Resolution of the 47 Sampled ASC Audits.** This table shows that the Crown obtained recoveries of \$21.25 million related to 27 ASC audit reports. The majority of the information was obtained from PWGSC as limited information was available within DND. Where recoveries exceed the settlement amount, the settlement includes an amount which the Crown owes the contractor.

<sup>5</sup> The decisions made during negotiations between the Crown and the contractors, and the final amount received by the Crown to resolve the overpayments suggested in the ASC audit report.

- Recoveries of \$21.25 million<sup>6</sup> have been obtained relating to 27 ASC audit reports. The ASC audit reports originally identified \$35.63 million as potential overpayments. After further validation of contractor supplied information, settlements of \$20.99 million were negotiated. All agreed-upon amounts owed by the contractors have been recovered.
- Resolution of the findings in 20 of the 47 audit reports has not yet occurred. Negotiations are still in progress for 14 of the 20, while no information can be located on the other six. The potential overpayments identified in these 20 audits total \$21.85 million.

If central monitoring of the recovery process existed within DND, the Department could benefit from quicker recoveries.

**Timeliness of Recoveries of Contract Overpayments**

There are risks to the Department if recoveries are delayed for a prolonged period. Information needed to substantiate charges during PWGSC negotiations with the contractor could be lost or misplaced if delays occur. DND has not set any targets regarding the turn-around time for recovery of contract overpayments.

For the 27 audits where settlement had occurred, the length of time between the date of the ASC audit report and the date of overpayment recovery

- was unknown for 21 of the 27, as this information had not been recorded; and
- varied between 3 and 67 months for the remaining 6 audits.

During interviews, PWGSC officers indicated that delays to the cost recovery process are common due to the involvement of multiple stakeholders and the fact that audits are sometimes performed years after contract completion, making it difficult to confirm some details. There was evidence that, in three instances, DND caused a delay of up to one year by not forwarding follow-up information or identifying a point of contact in a timely fashion. From the sample, all 14 reports that are still in negotiations, with total potential recoveries of \$14.15 million, have been in this state for more than two years. While the Statute of Limitations stipulates that the Crown has up to six years upon the date of discovery to recover overpayments from contractors<sup>7</sup>, several provincial statutes have two- or three-year limitations.

**Recommendation**

1. ADM(Mat) establish a central point of contact to collect contractor audit information and monitor the progress of negotiations on ADM(Mat) contracts.  
**OPI:** ADM(Mat)

<sup>6</sup> \$12.54 million of the \$21.25 million is based on information provided by PWGSC CAG based on records in their electronic database as well as in paper files. CRS audit team did not audit the CAG record-keeping system.

<sup>7</sup> The Defence Production Act.

## Governance

More clearly defined accountabilities and improved training could result in more consistent accounting treatment of recoveries related to contract overpayments.

### Departmental Guidance and Procurement Authority Understanding

Although the FAM does provide some guidance with respect to the recovery process for contract overpayments, clear accountabilities are not defined. Roles and responsibilities are neither well communicated nor clearly understood by DND PAs. Additional guidance on specific procedures with respect to contractor recoveries has not been provided, nor is there a common understanding of the appropriate accounting treatment by the PAs within the Department.

FAM Chapter 1018-1 Managing Public Revenue specifies that refunds of expenditures should be credited back to the original expenditure if received in the same fiscal year as the original expenditure.<sup>8</sup> Otherwise, they must be recorded as a refund of previous years' expenditures and DND does not have authority to re-spend these amounts. The General Ledger (GL) account "Refunds Previous Year's Expenditures" exists for this purpose.<sup>9</sup>

Based on our audit results, currently the method used to account for recoveries does not comply with this FAM chapter. The accounting treatment for \$22.2 million of recoveries related to 12 sampled audit reports was examined. Other than \$69,898 that was recovered through a cheque, the remainder was recovered by reducing DND's current liability to the contractor; none appeared to have been recorded in the GL account "Refunds Previous Year's Expenditures" in DRMIS.<sup>10</sup> Currently, there are cases where DND is given special spending authority to re-spend funds pertaining to a prior year's expenditure,<sup>11</sup> such as proceeds from a sale of real properties, a disposal of an asset, and a sale of intellectual properties. As an incentive for DND to engage additional audit services in the future, it is suggested that ADM(Mat), in conjunction with ADM(Fin CS), investigate the possibility of requesting statutory authority to spend an amount equal to the refund of previous years' expenditures relating to contract overpayments.

FAM Chapter 1020-2<sup>12</sup> states that refunds of expenditures, owing to DND, are to be included in accounts receivable (A/R). The FAM also lists four criteria for determining when an A/R transaction should be created. Audit evidence indicated that PAs have not created an A/R transaction to record the contractor's liability to the Crown. Instead, no entry was made in DRMIS until receipt of the overpayment. An A/R should be created after PWGSC completes the negotiations and DND becomes aware of the settlement

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<sup>8</sup> FAM Chapter 1018-1 Managing Public Revenue.

<sup>9</sup> Refunds of prior years belong to the Central Revenue Fund via a cheque to the Receiver General.

<sup>10</sup> The recoveries were through credits to current activities or incorporated into negotiations with the respective contractor leading to a reduction of future obligations.

<sup>11</sup> FAM Chapter 1018-1 Managing Public Revenues, paragraph 18 to 24.

<sup>12</sup> FAM Chapter 1020-2 Accrual Accounting Principles for Accounts Receivables states an A/R shall be recognized when a) the revenue generating activity has taken place; b) the activity gives rise to a future benefit; c) the Department has a legal basis on which to assert a right to receive the benefit; and d) the amount is known.

amount. When A/Rs are not established to record recoveries, periodic reports to highlight overdue refunds cannot be produced and outstanding payments cannot be escalated to ADM(Fin CS).

Thirteen of the 18 surveyed DND PAs were either unaware of or misidentified policies relating to the recovery process for contract overpayments. Instead of referring to policies, the majority of the PAs relied on colleagues, supervisors and their PWGSC CA for cost recovery guidance.

### **Identification of Cost Recovery Transactions**

Aggregate cost recovery information is not available within DND. A business process in DRMIS has not been set up to allow transactions pertaining to recoveries of contractor overpayments to be identified. Current practice leaves it up to users to enter descriptions in the notes of the transactions as opposed to assigning an identifier. As a result, no report can be generated to provide total recoveries received for the fiscal year.

### **Recommendation**

2. ADM(Fin CS) update the FAM to clearly stipulate accountabilities for the contract overpayments recovery process, provide better guidance on the procedures for recording recoveries of contract overpayments and enhance the identification of recovery transactions in DRMIS.

**OPI:** ADM(Fin CS)

## Risk Management

Improvement in managing contract-related risks would help mitigate the Department's risk of being overcharged.

## Risk Assessment

Information in the ASC audit reports was not collected and analyzed in the Department; thus, no formal lessons learned have been developed or communicated to DND PAs. Analysis of the types of overpayments occurring and their frequency could assist DND PAs in managing contractual risks.

Ten common types of overpayments were indentified in the 47 audit reports sampled.

- A more robust FAA Section 34 process by the contract management team could be an effective means of reducing or eliminating six of the ten types. They included excess mark-up on materiel, insufficient supporting documentation for claimed expenses, unsupported labour hours, out-of-scope work charges, invalid embodiment fee mark-up and double-billing errors. In these cases, additional supporting documentation should be obtained prior to FAA Section 34 certification of invoices. The ASC audit reports identified \$22.09 million of potential overpayments in these categories.
- The remaining four types of overpayments would not be addressed through a more robust Section 34 process. These types of overpayments include excess overhead and general administration costs, understated contractor revenue leading to a lower reported profit, inadequate subcontractor transfer cost and excess firm management fees. Invoices do not contain detail with respect to these charges, and in some cases the overpayment can only be determined upon completion of the contract and/or through an audit of the contractor's accounting records. The largest single type of potential overpayment was excess overhead. Approximately \$12.67 million of potential overcharges of this type were identified.

In addition, for non-competitive contracts where the contractors' profit level is negotiated instead of being determined by a competitive procurement process, additional contractor audits could help determine if the contractor has earned profit in excess of the negotiated level. Thirty-six percent of the average annual \$2.83 billion value of DND contracts tendered through PWGSC over the last three years was non-competitive contracts.<sup>13</sup>

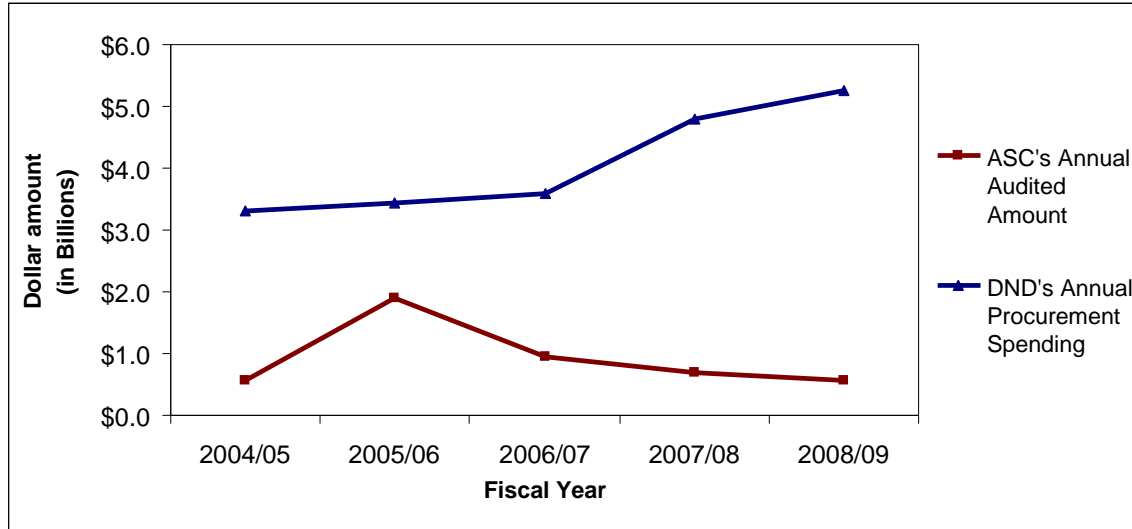
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<sup>13</sup> PWGSC Contracting Database; \$2.83 billion represents contracts and amendments between FY 2007/08 and FY 2009/10 (inclusive), where "non-competitive" was indicated under the contract award process.



**Utilization of Additional Contractor Audit Services**

As shown in Figure 1, between FY 2005/06 and FY 2008/09, ASC annual audited amount of DND contracts declined by 71 percent while DND procurement spending<sup>14</sup> increased by 53 percent.



**Figure 1. DND’s Annual Procurement Spending versus ASC’s Annual Audited Amount on DND Contracts.** DND’s procurement spending has increased while ASC’s annual audited amount on DND contracts decreased from FY 2005/06 to FY 2009/10. The data is summarized in Table 2.

Fiscal Year	ASC’s Annual Audited Amount (in \$Ms)	DND’s Annual Procurement Spending (in \$Ms)
2004/05	\$ 562.45	3,306.80
2005/06	\$1,910.08	3,436.10
2006/07	\$ 936.83	3,600.80
2007/08	\$ 696.79	4,785.70
2008/09	\$ 552.61	5,257.30

**Table 2. DND’s Annual Procurement Spending versus ASC’s Annual Audit Coverage on DND Contracts.**

There have not been any new ASC audits confirmed for DND in 2011 due to a new PWGSC funding approach introduced in 2009 that requires client departments to pay for future contractor audits. However, many projects did not budget for this cost when seeking approvals. Other factors that affect the utilization of additional audit services by DND include the following:

<sup>14</sup> Total DND spending on National Procurement, Capital Equipment and Investment Cash, based on DND Financial Status Reports between FY 2005/06 and FY 2008/09 published by Director Budget.

- Low probability of DND being able to re-spend the recovered funds as it usually takes longer than a year from the start of an audit to the completion of the recovery process of contract overpayments.<sup>15</sup>
- A centrally managed risk-based model of contracts does not exist to prioritize contractors' audits within the Department. Currently, the decision to engage contractor audits is at the discretion of individual DND contract office.
- Different funding approaches have not been analyzed in the Department to provide guidance. Consideration could be given to establishing a central source of funding and/or having future projects incorporate audit costs as part of early project cost estimates.

Contractor audits could provide benefits beyond the Department. Within DND, contractor audits together with FAA Section 34 verification will help mitigate the risk of overpayments. An audit early in the life of a long-term contract could be a deterrent to subsequent overpayments. Based on information provided by PWGSC CAG,<sup>16</sup> the direct monetary benefit for the Crown is an average return of \$2.20 for every dollar spent on contractor audits. Within the CRS audit sample, 27 ASC audits resulted in recoveries of \$21.25 million,<sup>17</sup> an average of \$0.79 million per audit.

### Recommendation

3. ADM(Mat), in conjunction with PWGSC, develop a risk-based model to assess contract risks of overpayment and utilize additional contractor audit services.

**OPI:** ADM(Mat)

<sup>15</sup> Departments do not have the authority to re-spend refunds of prior year expenditures.

<sup>16</sup> Payback ratio provided by PWGSC CAG based on a 5-year average between FY 2004/05 and FY2008/09 (inclusive). CRS audit team did not verify the accuracy of this information.

<sup>17</sup> \$12.54 of the \$21.25 million is based on information provided by PWGSC CAG based on records in their electronic database as well as paper files. CRS audit team did not audit the record-keeping system.





**Status Update on Prior DND Requests for ASC Audits**

DND has taken action on six of the seven audit recommendations to initiate further investigations by PWGSC or ASC as depicted in Table 3. The remaining audit recommendation regarding ||| contract has been partially addressed. Although \$0.99 million related to the follow-on ||| contract was recovered, DND did not follow up on \$0.27 million of potential overpayments relating to the expired contract, even though the CRS audit recommendation covered both the expired and follow-on contracts. Under the approach where PWGSC funded all contractor audits, once a suggestion to audit a contract had been escalated to PWGSC, DND could only attempt to influence whether or when an audit or further investigation occurred. Therefore, while DND had taken some action to initiate further investigation in all cases, at the time of this CRS audit (April 2011), ASC had audited five contracts and a sixth had been investigated by the PWGSC CA. Negotiations were complete for two of the six. As of March 2011, DND had recovered \$1.17 million.

Contract (Audit Completion of CRS)	Contract Period Audited by CRS	Potential Overpayments Identified by CRS Audit	DND Action on CRS Audit Recommendation	PWGSC/ ASC Actions	\$ Recovered
			<b>Partial.</b> Potential overpayments regarding     contract not followed up on.	<b>Audit Not Requested.</b> No ASC audit requested on the     contract but \$0.99M in overpayments regarding     recovered.	\$0.99M
			<b>Complete.</b> Requested PWGSC to Contract ASC Audit.	<b>Complete.</b> ASC audit completed and DND determined no further recovery actions.	\$0.04M
			<b>Complete.</b> Requested PWGSC CA to investigate.	<b>Complete.</b> PWGSC CA investigated all potential overpayments and determined no further recovery actions.	\$0.15M
			<b>Complete.</b> Requested PWGSC to Contract ASC Audit.	<b>Audit Not Actioned.</b> ASC did not conduct this requested audit.	N/A

Contract (Audit Completion of CRS)	Contract Period Audited by CRS	Potential Overpayments Identified by CRS Audit	DND Action on CRS Audit Recommendation	PWGSC/ASC Actions	\$ Recovered
			<b>Complete.</b> Requested PWGSC to Contract ASC Audit.	<b>In Progress.</b>	N/A
			<b>Complete.</b> Requested PWGSC to Contract ASC Profit Audit on Sole Source Amendments.	<b>Audit Not Started.</b> ASC profit audit can only start once the     contract is completed when all     are delivered.	N/A
			<b>Complete.</b> Contracted ASC Audit Directly.	<b>In Progress.</b> Audit will be completed in September 2012.	N/A
Total		<b>\$42.62M</b>			<b>\$1.17M</b>

**Table 3. DND and PWGSC Actions Resulting from the Cost Recovery Recommendations in Seven CRS Contract Management Audits.** This table outlines the seven CRS contract management audits which recommended possible ASC audits, the actions of DND managers in requesting the audits, and the status of the ASC audits. DND acted on most of the CRS recommendations as indicated by “Complete” under the column “DND Action on CRS Audit Recommendation.”

## Annex A—Management Action Plan

### Monitoring

#### CRS Recommendation

1. ADM(Mat) establish a central point of contact to collect contractor audit information and monitor the progress of negotiations on ADM(Mat) contracts.

#### Management Action

DGMSSC/DMPP is leading a departmental engagement with PWGSC to support the development of improvements to the contract cost audit program, including a new funding model and improved management. This is expected to include an appropriately integrated interdepartmental information sharing framework, the precise nature of which has yet to be defined. It may or may not require establishment and resourcing of a central DND office. Given the nature of interdepartmental discussions, and the likely requirement for PWGSC to obtain Treasury Board approval for some elements of the renewal, DND cannot predict timelines for full resolution of the matter; however, both departments are committed to minimizing delays.

**OPI:** DGMSSC/DMPP

**Target Date:** Ongoing

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### Governance

#### CRS Recommendation

2. ADM(Fin CS) update the FAM to clearly stipulate accountabilities for the contract overpayments recovery process, provide better guidance on the procedures for recording recoveries of contract overpayments and enhance the identification of recovery transactions in DRMIS.

#### Management Action

FAM Chapter will add the collection of overpayments on contracts as an example of an account receivable and make Level Ones responsible to monitor and proactively seek collection of overpayments.

**OPI:** ADM(Fin CS)/DFPP

**Target Date:** March 2013

#### Management Action

DRMIS will be modified to enhance the identification of recovery transactions.

**OPI:** ADM(Fin CS)/DFA

**Target Date:** March 2013

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## Risk Management

### CRS Recommendation

3. ADM(Mat), in conjunction with PWGSC, develop a risk-based model to assess contract risks of overpayment and utilize additional contractor audit services.

### Management Action

DGMSSC/DMPP is leading a departmental engagement with PWGSC to support the development of improvements to the contract cost audit program, including a new funding model and improved management. It should be noted that under the *Defence Production Act*, PWGSC is the Government of Canada authority for cost audits. DND, as the client, will collaborate with PWGSC in developing appropriate tools for supporting the program, including assessment of risk.

**OPI:** DGMSSC/DMPP

**Target Date:** Ongoing



## Annex B—Audit Criteria

### Objective

1. An adequate monitoring system of the recoveries of contract overpayments is in place that includes performance targets and utilizes accurate, timely and complete information.

### Criteria

- Department oversight exists to govern the recovery process of contract overpayments.
  - Performance targets are set and evaluated against for the recovery process of contract overpayments.
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### Objective

2. Effective and sufficient communication exists that is facilitated by necessary information systems.

### Criteria

- Communication regarding recovery actions is effective and timely.
  - DND information system supports reporting of recoveries of contract overpayments.
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### Objective

3. Roles and responsibilities clearly defined and necessary training, staff resource & tools are available to achieve recovery objective.

### Criteria

- Roles and responsibilities of parties involved in the recovery process in DND clearly documented.
  - The current governance structure is adequate within DND to facilitate the achievement of recovery objective.
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**Objective**

4. Policies on recovery process of contract overpayments are clear and consistent with objectives & practices are in accordance with policy.

**Criteria**

- Policies regarding recovery process of contract overpayments are clear, consistent and communicated.
  - Policies regarding recovery process of contract overpayments are kept current and facilitate the achievement of cost recovery objective.
  - Past PWGSC cost audits have been reviewed by DND and refunds were received.
  - Practices on processing refund cheques have been consistent across the department and in accordance with policies.
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**Objective**

5. A risk assessment plan exists and is regularly reassessed. Significant risk factors are identified and acted upon.

**Criteria**

- Past CRS audit recommendations to audit high risk vendors have been acted upon.
- Risk assessment of the 213 ASC audits has been performed through data analysis as to provide further added value.