

**AUDIT OF THE
CONTRIBUTION AGREEMENTS
with the**

*XI FINA World Championships – Montreal 2005
Organizing Committee*

*Prepared for the
Department of Canadian Heritage*

**Audit Conducted by
Samson & Associates**

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1 Introduction

1.1 Background

1.1.1 *Brief description of the program*

Sport Canada supports the achievement of high-performance excellence and the development of the Canadian sport system to strengthen the unique contribution that sport makes to Canadian identity, culture and society. Through its Hosting Program, Sport Canada enables sport organizations to stage international events in Canada, as well as the Canada Games. This program aims to enhance the development of high-performance sport and the international profile of sport organizations. Contributions received from Sport Canada are subject to specific terms and conditions regarding expenses incurred.

1.1.2 *Brief description of the recipient*

The Organizing Committee for the XI FINA World Championships (Montreal 2005) was incorporated as a non-profit organization in 1998 under the *Canadian Corporations Act*. It was established for the purpose of organizing the Championships, which were held in Montreal from July 17 to 31, 2005, after the bid was awarded in July 2001. During the Championships, Montreal hosted approximately 3,200 athletes and officials from one hundred forty-five (145) countries who participated in the four aquatic disciplines sanctioned by FINA (swimming, diving, water polo and synchronized swimming). These Championships are the largest sport event of this kind to be held in Montreal since the 1976 Olympic Games, and this was the first time they were held in North America.

1.1.3 *Contribution of Canadian Heritage*

Canadian Heritage (PCH) signed three contribution agreements with Montreal 2005 (see Table 1 for objectives of the contribution agreements) for a total of \$16,830,000:

- 2002-03 agreement for \$200,000;
- 2003-04 agreement for \$6,393,000; and
- 2004-06 agreement for \$10,237,000.

In addition to these three agreements, PCH provided \$100,000 to *les Internationaux du Sport de Montréal* and \$70,000 to the Aquatic Federation of Canada in 2001-02 for expenses related to the bid. Financial contributions by PCH therefore amounted to \$17 million. PCH also provided services worth \$2 million, bringing its total contribution to \$19 million for the Championships. These services include federal coordination, essential federal services and communications expenses.

Under the 2004-06 contribution agreement, the Department withholds \$1.5 million until all the required reports are received, including this audit report.

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Table 1 Contribution agreements between Canadian Heritage and Montreal 2005

Date of the Agreement	Description / Terms and Conditions	Term of the Agreement	Amount
June 20, 2002	Agreement #1 – To cover costs associated with the completion of the business plan and partial payment of the FINA hosting fees.	01/04/02 to 31/03/03	\$200,000
May 8, 2003	Agreement #2 – To pay for promotion, advertising, printing, travel, meals and accommodations and administrative expenses, salaries, personnel fees, as well as related compulsory deductions.	01/04/03 to 31/03/04	\$500,000
June 9, 2003	First amendment to Agreement #2 - To increase the amount of the contribution.	09/06/03 to 31/03/04	\$3,000,000
November 21, 2003	Second amendment to Agreement #2 – To increase the amount of the contribution.	21/11/03 to 31/03/04	\$2,893,000
May 11, 2004	Agreement #3 – The contribution will be used to fund activities set out in the overall budget of Montreal 2005, except for three activities identified in the budget: bid-related costs, travel expenses of athletes paid to FINA and FINA sponsorship fees. Expenditures for the exchange of goods or services are not eligible. A new template of the contribution agreement introduces new terms and conditions: Montreal 2005 must submit to the Department financial and quarterly activity reports and quarterly cash flow projections.	1/04/04 to 31/03/06	\$9,237,000
April 18, 2005	First amendment to Agreement #3 - Terms and conditions added with regard to governance, legacy, protocol and accreditation, insurance and recognition of federal government's financial support.	-	-
July 31, 2005	Second amendment to Agreement #3 – To increase the amount of the contribution.	1/04/04 to 31/03/06	\$1,000,000
	Total of contribution agreements		\$16,830,000

1.2 Audit Objectives

The objective of the audit is to provide assurance to program officials that:

1. the funding provided to the recipient was used for the purposes set out in the contribution agreements;
2. the funding provided was used in accordance with the report submitted by the recipient, with respect to the use of the Government of Canada contribution;
3. the recipient implemented an internal control framework to operate the activities

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- described in the contribution agreements;
4. there was sound management with respect to contracts; and
 5. the recipient complied with the terms and conditions of the contribution agreements.

1.3 Audit Scope and Timing

This audit covers the \$16,830,000 contribution provided by the Department of Canadian Heritage to the XI FINA World Championships - Montreal 2005 Organizing Committee for the period between April 1, 2002, and March 31, 2006. Since the PCH contribution is included in the overall budget of Montreal 2005, we reviewed all of the expenditures of Montreal 2005, which amounted to \$39,738,456.

The audit was conducted between December 12 and 21, 2005, in the Montreal 2005 offices, located at 1010 de la Gauchetière in Montreal. The audit had to be completed before the offices permanently shut down on December 31, 2005.

1.4 Audit Methodology

The auditors examined the accounts and records of Montreal 2005 that related to the contribution agreements. Audit procedures were performed in accordance with generally accepted auditing standards, including a general review of the accounting procedures, and such tests of accounting records and supporting documentation as were considered necessary. The methodologies and criteria contained in the *Transfer Payment Policy* and *Guide on Grants, Contributions and Other Transfer Payments* were referenced, as necessary, in the conduct of this audit.

The PCH program, Corporate Review Branch and Grants and Contributions Centre of Expertise staff were verbally informed of the audit findings during a meeting held on January 27, 2006, at the Department's offices.

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1.5 General Findings

Based on our audit, in our opinion,

1. All the funding provided to Montreal 2005 was used for the purposes set out in the three contribution agreements (**for more details, see section 2.1**).
2. The funding provided was used in accordance with the report submitted by Montreal 2005, with respect to the use of the Government of Canada contribution (**for more details, see section 2.2**).
3. The recipient's internal control framework was adequate for delivering the activities described in the contribution agreements, **except where noted in section 2.3**.
4. Montreal 2005 exercised sound contract management, **except for the examples described in section 2.4**.
5. The recipient complied with all of the terms and conditions of the contribution agreements, **except where noted in section 2.5**.

2 OBSERVATIONS AND CONCLUSIONS

2.1 Review of Financial Activities

The results of the audit of expenses incurred under the contribution agreements by Montreal 2005 can be summarized as follows (**a detailed statement of expenditures is provided in Appendix A**):

PCH contribution justified by the audit:	\$16,830,000
Amount provided by PCH:	<u>\$15,330,000</u>
Amount of holdback:	\$1,500,000
Less: interest earned on PCH funds (note 1):	<u>\$56,238</u>
Amount owed to Montreal 2005:	<u>\$1,443,762</u>

Observations

The 2004-06 contribution agreement states in section 2.1: “*the maximum contribution for the XI FINA World Championships is sixteen million dollars (\$16,000,000), including all the interest generated on the amounts already paid and those generated during the period covered by this Agreement*”.

The recipient did not identify the interest earned on the Department’s contribution. Accordingly, we estimated that \$56,238 in interest was earned on departmental funding. This figure was obtained by applying the interest earned each year to the percentage of annual revenue provided by PCH to the total revenue of Montreal 2005 and taking into account the funding advanced by the City of Montreal in 2005.

Note 1 – Calculation of interest earned on funding provided by PCH

	Interest earned	PCH funding	Interest attributed to PCH
2002	0	n/a	0
2003	8,776	99.70%	8,750
2004	46,356	95.00%	44,039
2005	52,815	6.53%	<u>3,449</u>
Total interest earned on PCH funding			<u>\$56,238</u>

Recommendation

In compliance with the contribution agreement, the \$56,238 in interest earned on funding provided by the Department should be deducted from the \$1.5 million holdback.

2 OBSERVATIONS AND CONCLUSIONS

2.1.1 *Calculation of expenditures eligible for the Canadian Heritage contribution*

Expenditures declared by Montreal 2005, from Appendix A	\$39,738,456
Less: audit adjustments, from Appendix B (note 1)	<u>(6,859,580)</u>
Eligible expenditures, from Appendix A	\$32,878,876
Less expenditures covered by other contributions:	
Contribution of the Government of Quebec	(414,985)
Employment programs	(156,184)
City of Montreal – deficit absorption	<u>(4,774,702)</u>
Expenditures eligible for the PCH contribution	<u>\$27,533,005</u>

Note 1 – The adjustments apply to three categories of expenditures: expenditures not authorized by the Board of Directors, expenditures identified as ineligible in the budget of the 2004-06 contribution agreement and costs for the exchange of goods or services as stipulated in the 2004-06 agreement.

Findings

The \$200,000 contribution by PCH for 2002-03 was used, as required, to pay the US\$100,000 (CAN\$160,507) security deposit to FINA, as well as part of the fees for preparing a business plan.

The next two PCH contribution agreements amounting to \$16,630,000 funded part of the \$27,533,005 of the eligible expenditures of Montreal 2005 to organize the Championships, as required in the agreements.

Adjustments valued at \$6,859,580 do not affect the PCH contribution because the adjusted expenditures eligible for the PCH contribution are greater, \$27,533,005 compared to \$16,830,000.

2.1.2 *Calculation of the maximum contribution of Canadian Heritage*

In accordance with the *Federal Policy for Hosting International Sport Events*, the maximum contribution from the federal government was set at 35% of the total event costs. In addition, the contribution must not exceed 50% of the total amount of public sector funding allocated for the event, taking into account direct, indirect and essential services, as well as any contributions related to legacies.

Total cost of Championships

Expenses incurred by Montreal 2005 according to Appendix A	\$39,738,456
Plus other costs:	
• Costs related to the bid	170,000
• Infrastructure costs	21,200,000
• Public services	<u>6,600,000</u>
Total cost of Championships	<u>\$67,708,456</u>

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Maximum contribution of Canadian Heritage: 35% of the total cost, or \$23,697,959

The total contribution of Canadian Heritage is:

- direct contribution to Montreal 2005	16,830,000
- contributions to ISM and AFC	170,000
- contribution in services	<u>2,000,000</u>

Total contribution of Canadian Heritage \$19,000,000

This condition was met.

Total public sector contribution

• Canadian Heritage	19,000,000
• Government of Quebec	
- direct contribution to Montreal 2005	414,985
- contribution to the City of Montreal for capital assets	14,100,000
• City of Montreal	
- absorption of Montreal 2005 deficit	4,774,702
- infrastructure contribution	7,100,000
- services and security	4,600,000
• Government employment programs	<u>156,184</u>

Total public sector contribution \$50,145,871

Maximum contribution of Canadian Heritage: 50% of the public sector contribution, or \$25,072,935. The total contribution of PCH is \$19 million, which meets the 50% condition.

Conclusions

The funding provided to Montreal 2005 was used for the purposes set out in the contribution agreements.

The contribution limits of 35% of the total cost and 50% of the public sector contribution were adhered to.

The \$27,533,005 in eligible expenditures incurred by Montreal 2005 under the contribution agreements is more than adequate to cover the \$16,830,000 contribution paid directly to Montreal 2005 by Canadian Heritage.

2 OBSERVATIONS AND CONCLUSIONS

2.2 Review of Compliance with Funding Provided with the Report Submitted by Montreal 2005

Observation

We reconciled the expenditures presented in the financial report of Montreal 2005 with the audited financial statements of Montreal 2005 since the beginning of its operations in April 2002 until December 31, 2005. Our review of supporting documents showed that transactions were accurately reported in the financial reports.

Conclusion

The audit demonstrated that the funding provided to Montreal 2005 was used in compliance with the report submitted to Canadian Heritage by Montreal 2005 for the period ending December 31, 2005.

2.3 Assessment of Internal Control Framework

2.3.1 *Governance and Management Framework*

Montreal 2005 experienced three distinct periods in its organization. The governance frameworks have varied in the three periods.

First management team 2001-02 – Start-up

After obtaining the Championships in July 2001, a Board of Directors was formed. The Board approved the general by-laws, a code of ethics for members of the organizing committee and the committee's political and organizational structure. A code of conduct was studied for the Board, but its adoption was postponed a number of times and was never adopted by the Board during this time. A Vice-president/CEO (Vice-President/CEO) was hired in November 2001. One of his mandates was to prepare a business plan and a budget estimate to stage the Championships. The Board authorized cheque-signing authorities: the secretary-treasurer signed all the cheques with a second signature from a designated Board member or the Vice-President/CEO. After presenting a budget that was considered to be too high by the Board, the Vice-President/CEO was fired in July 2002. The Board of Directors Chair resigned in October 2002.

Observations

There were few financial activities during this period due to a lack of revenue.

In April 2002, a firm was hired to help develop a business plan and prepare a sponsorship program.

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Second management team 2002-04 – Preparing for the Championships

A new chair of the Board of Directors was appointed in October 2002 and a new Vice-President/CEO was hired that same month. The employment contract for the Vice-President/CEO is confidential. The contract with the new Vice-President/CEO is signed by one of his corporations. Although some Board members opposed this approach, a majority decided to accept the proposed candidate. Two Board members were tasked to finalize and sign the agreement with the new CEO.

The business plan and budget were finalized in October 2002. Three new members joined the Board of Directors in December 2002: a federal government representative, a provincial government representative and a City of Montreal representative.

This Vice-President/CEO held the position until February 2005.

Observations

In 2003 and 2004, Montreal 2005 experienced financial problems that resulted in FINA's decision to withdraw the Championships from Montreal in January 2005. In our opinion, the management framework in place did not allow for comprehensive monitoring of cash flow and did not ensure transparency in all financial decisions and transactions. The projected revenues did not come in at the expected times, and major commitments were made. The Board of Directors did not exercise greater control, which would have enabled Montreal 2005 to ensure that only key commitments were made and that financial obligations under various contracts could be met.

All of the cheques made out to the Vice-President/CEO during this time were signed by the Vice-President/CEO and by a member of the Board of Directors, in accordance with the policy established by the Board. It would have been better if the Board's policy had not allowed an individual to sign cheques made out to himself.

Third management team – 2005 – Championships

Montreal 2005 was successful in recovering the Championships in February 2005 after the City of Montreal guaranteed that it would assume responsibility for any deficit.

A new Board of Directors was formed in February 2005, co-chaired by the mayor of Montreal and an experienced manager with expertise in organizing major events. A new Vice-President/CEO was hired in February 2005. The organizational chart was changed, and new vice-president positions were created to complete the priority tasks in order to stage the Championships. Staff changes were also made at the senior management level.

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After a governance clause was added to the 2004-06 contribution agreement, the organizing committee took the following measures:

- an official code of conduct for members of the Board of Directors and organizing committee officials was approved by the Board in April 2005;
- all contracts were submitted for the Board's approval;
- cheques were signed by the VP Finance, and the Vice-President/CEO or the co-chair/treasurer; a signatory may not sign a cheque made out to himself.

In addition, a code of ethics and a conflict of interest policy were developed and distributed to each employee.

Observations

The new team had to quickly deal with the urgency of the situation, which required effective operations and the identification of funding sources.

The Board of Directors, except for one agreement that was cancelled in March 2005, approved all contractual agreements with various hotels and other service suppliers.

The new administration also hired an internal team for securing corporate sponsorships to replace the marketing firm hired for this purpose in April 2002. The new internal team obtained sponsorships with a total value of close to \$9 million in a period of only four months.

The following weaknesses were corrected: the lack of a formal cash flow management process and an inadequate distribution of cheque signing authorities.

2.3.2 Revenue and cash flow management

Table 2 presents the projected and actual revenues for two periods: the start of Montreal 2005 operations in April 2002 until December 31, 2004, just before the withdrawal of the Championships by FINA; and 2005, the year the Championships were held.

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Table 2 Revenue for Montreal 2005

Source of Revenue	2002-04 Revenue	2005 Revenue	Total Revenue
Government support			
✓ Government of Canada	\$13,193,000	\$3,637,000	\$16,830,000
✓ Government of Quebec	315,000	99,985	414,985
✓ City of Montreal (Services)	-	-	-
✓ Salary subsidies	11,002	145,182	156,184
Sponsorships (Corporate Support)	175,000	9,012,083	9,187,083
Ticket Sales	160,484	6,960,136	7,120,620
Other Sources	53,776	1,201,106	1,254,882
TOTAL	\$13,908,262	\$21,055,492	\$34,963,754

We found that most income sources other than those from governments did not materialize as forecasted. As of December 31, 2004, only \$389,261 was generated as revenue from sources other than government (sponsorship revenue, ticket sales and other sources) out of total revenues of \$13,908,263, or under 3%.

Observations

Our review of the cash flow management process and controls for the period up until January 2005 revealed a number of deficiencies:

- There was inadequate discipline and planning for sound cash flow and commitment management given the inadequate funding sources.
- The many service contracts concluded by Montreal 2005 had created a financial obligation that generated substantial periodic payments leading up to the Championships. For example, a partial system for managing hotel payments was set up, but it did not consider other operations disbursements, such as administrative and operating expenditures, which constantly fluctuated in value.
- Remuneration for the firm responsible for the position of Vice-President of Marketing increased from \$80,000 to \$180,000 in September 2003 after seven months in the position. This contract amendment was made retroactive to the date of hiring. It generated unexpected additional expenditures of \$75,000 for this retroactive increase and \$100,000 per year

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afterward. This contract amendment was authorized by the Vice-President/CEO. It was not approved by the Board of Directors and was not mentioned in the Board minutes. An audit adjustment was made for this increase in fees in Appendix B.

2.3.3 Significant financial commitments

FINA (Fédération internationale de natation amateur)

The agreement for hosting the Montreal Championships, signed with FINA on June 21, 2001, involved significant financial commitments. The various commitments toward FINA totalled \$7,293,367 US in periodic payments spread out over the period of 2001 to 2005. Payment of the initial \$100,000 US deposit, due on December 31, 2001, was paid late, on April 2, 2002. As for the costs of the host broadcaster, only the first payment of \$449,000 US was made to FINA. The following two payments, which were higher and due on January 1, 2004 and 2005, were not met. Payments to FINA for the other commitments were made around the dates required.

Once FINA reawarded the organization of the Championships to Montreal 2005, it was decided that Montreal 2005 would pay the Canadian broadcaster directly in Canadian funds, resulting in substantial savings in exchange rates.

Accommodation costs

Starting in early 2003, Montreal 2005 signed a number of agreements with hotels and residences in the Montreal area to guarantee the number of rooms, meals and other services required by FINA policies and by-laws. This required Montreal 2005 to guarantee the reservation of a minimum number of rooms and meals for athletes and their delegations. A total of 16 contracts were signed with Montreal hotels and residences. All the agreements contained an advance payment schedule that provided for the total payment of accommodation and meal costs before the hosting of the Championships.

In most cases, only the first three or four payments were made, due to inadequate financial resources. This forced Montreal 2005 to stop making the required periodic payments, thereby breaching its financial commitments.

In spring 2005, Montreal 2005 asked all expected delegations to confirm the number of nights required in writing. It became apparent that the number of nights confirmed by the delegations was fewer than the number of nights reserved and guaranteed by Montreal 2005. It was then decided to invoke the attrition clause included in each accommodation contract to minimize Montreal 2005's financial obligation. The income received from the various sources finally permitted Montreal 2005 to pay out most of the late amounts before the opening of the Championships.

FINA also required Montreal 2005 to guarantee that it would not bill the delegations for rooms that were reserved but not used, forcing Montreal 2005 to absorb the cost of the unused rooms.

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By the end of the Championships, this totalled roughly \$2.3 million. Montreal 2005 then negotiated with each hotel establishment and was able to bring this amount down to \$1.2 million.

2.3.4 Conclusions

Most of the internal control weaknesses that were identified occurred from October 2002 to January 2005, the date FINA withdrew the Championships.

The main weaknesses identified during this period include:

- decision-making centralized by the Vice-President/CEO;
- lack of a formal comprehensive cash flow management process;
- financial commitments made with no regard to the timing of funding; and
- inadequate distribution of signing authorities to the Vice-President/CEO.

It is also our opinion that the financial information presented at Board meetings could have been more exhaustive and detailed to ensure greater transparency, given the cash flow management problems Montreal 2005 had to deal with.

2.4 Assessment of contract management

The audit revealed that, on the whole, Montreal 2005 set up an acceptable contract management framework. Procurement policies were also developed and generally followed. However, as described in sections 2.4.1 to 2.4.6, we identified some situations where the rules of sound contract management had not been adhered.

2.4.1 *Service contracts – Verbal agreements*

The audit revealed that out of the 17 contracts reviewed in the period from April to July 2005, six contracts were reached verbally without then being ratified in writing. These contracts were however approved by the Board of Directors. The VP Finance explained that, in these cases, management issued calls for tender and the successful bids met all the requirements regarding the kinds of services, the cost and the delivery schedule. Before these invoices were paid, financial services ensured that the goods and services had been received according to the established procedure and that the amounts invoiced matched those contained in the supplier's bid.

2.4.2 *Opening ceremonies*

In its 2001 bid to FINA, the bid committee planned on having the opening ceremonies organized by Cirque du Soleil. Due to budgetary constraints, Cirque du Soleil was not chosen in the planning, and another firm was hired. The contract with this firm was cancelled in January 2005 once FINA withdrew the Championships. The Cirque du Soleil was once again considered an asset to help Montreal 2005 recover the Championships. Once the Championships were given

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back to Montreal 2005, a verbal agreement was reached with Cirque du Soleil for the opening ceremonies. The final contract with Cirque du Soleil was not signed until October 17, 2005, three months after the Championships.

2.4.3 Documentation of payments and services obtained

The firm chosen in April 2002 to prepare a sponsorship recruitment plan received \$65,000 in fee advances before the contract was signed in early 2003 for \$250,000 plus a 10% commission for each sponsorship sold. The supplier's file did not contain adequate documentation and information to justify the total amounts paid for services obtained. However, all disbursements were supported by adequate source documentation.

2.4.4 The Vice-President/CEO from October 2002 to January 2005

Payments to the Vice-President/CEO during this period were consistent with the terms of his contract, with one exception. These payments involved fees, sponsorship commissions and travel costs. His claims for meals and kilometrage complied with Treasury Board directives. Sometimes his expense accounts lacked explanations justifying the travel, and source documentation was not always adequate (credit card receipts instead of original invoices) or sometimes missing. The Vice-President/CEO and a Board member signed all these cheques.

A March 2004 audit conducted by Consulting and Audit Canada revealed that a total of \$216,852 was advanced to Montreal 2005 by one of the two companies owned by the Vice-President/CEO so that Montreal 2005 could temporarily meet its financial obligations. Repayments by Montreal 2005 included interest at an average rate of 19% and management fees for a total of \$36,089. No lending contract or other document was signed to formalize the transaction or establish the terms. An audit adjustment for this expenditure is included in Appendix B.

2.4.5 Payments of commission advances to the Vice-President Marketing

The firm occupying the position of Vice-President Marketing received advances on sponsorship commissions totalling \$25,000, or \$5,000 per month between October 2003 and February 2004, even though no such type of remuneration was mentioned in the contract. Consulting and Audit Canada revealed this anomaly in its March 2004 audit and had recommended that the firm's contract be amended to include the payment of commissions. Montreal 2005 then stopped these commission payments but did not amend the contract. Montreal 2005 ended the agreement with this firm in December 2004. As part of the final settlement, \$25,000 in commission advances that had been paid were recovered, which effectively cancelled this expenditure.

2.4.6 Payment of a performance bonus not provided for in the contract

2 OBSERVATIONS AND CONCLUSIONS

A performance bonus of \$11,438 was paid to a senior staff member in October 2004 although there was no provision for this in his contract. Payment of this bonus was authorized by the Vice-President/CEO, but was not submitted to the Board of Directors for approval. An audit adjustment for this expenditure appears in Appendix B.

2.5 Review of compliance with the terms and conditions of the contribution agreements

According to our audit, Montreal 2005 was in overall compliance with the terms of the contribution agreements except in certain cases, particularly with regard to the requirement to report periodically on the use of funds paid and the progress of preparations for the Championships. Specifically:

- ✓ In an amendment to a contribution agreement signed on November 21, 2003, Montreal 2005 agreed to negotiate in good faith to sign, by March 31, 2004, a multiparty agreement with the Government of Canada, the Government of Quebec, the City of Montreal, the Aquatic Federation of Canada and *les Internationaux du Sport de Montréal*. This agreement was not signed. However, the obligations for Montreal 2005 provided for in this agreement were included in the 2004-06 agreement signed with the Canadian Heritage.
- ✓ Schedule D of the contribution agreement signed on May 11, 2004, included terms and conditions that were not all met. For example, Montreal 2005 did not formally submit the following documents as required in the agreement with Canadian Heritage:
 - October 2002 updated business plan;
 - A revised budget within 30 days following Board approval;
 - Projected cash flows required within 60 days following the end of each quarter; and
 - A quarterly financial statement showing the budgeted and actual revenues and expenses for the period. Montreal 2005 did not submit any of these quarterly financial statements directly to Canadian Heritage.

According to the Montreal 2005 executive, having a departmental representative on the Board of Directors, who attended all Board meetings where strategic issues were discussed, compensated for this. During these meetings the departmental representative was provided with financial statements including revenue and expense statements, budget amendments and cash flow projections. The departmental representative gave the reports provided to the Board to the PCH program officer. These reports met the department's requirements as per Schedule D of the 2004-06 contribution agreement. Furthermore, Montreal 2005 provided the Department with a copy of quarterly progress reports to FINA; for the Department, these reports presented the update of the Business Plan and activity information as required.

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In our opinion, having a departmental representative attend Board meetings does not discharge the obligation to comply with the terms of Treasury Board policies on accountability and transparency of operations. The financial information required by Canadian Heritage was one of the terms of the contribution agreement Montreal 2005 had to follow. This information was meant to allow the Department to closely monitor the use of the funds provided and ensure that funds were paid when required and that the funds were used as they were intended.

Conclusion

Montreal 2005 was in compliance with the terms of the contribution agreements, except that it did not formally provide all the reports required by Schedule D of the 2004-06 contribution agreement.

APPENDIX A
STATEMENT OF EXPENDITURES
For the period from April 1, 2002, to December 31, 2005

	Reported Amounts	Audit Adjustments <u>Appendix B</u>	Eligible Amounts	Budget Forecasted in 2004-06 Agreement
<i>Executive</i>				
Salaries	\$3,157,397	(\$11,438)	\$3,145,959	\$3,731,500
Contracts (Professional Fees)	\$1,123,985	(\$213,942)	\$910,043	\$569,002
Meetings, Tours, Inspections, FINA (Executive)	\$1,157,987	(\$36,089)	\$1,121,898	\$250,000
Bid (Ineligible Expenses)	\$277,341	(\$277,341)	0	\$280,000
FINA – Athletes Travel (Ineligible Expenses: US\$1 million)	\$1,289,232	(\$1,289,232)	0	\$1,500,000
FINA - Eligible Expenses	\$225,755		\$225,755	
FINA – Licencing Fees to the Aquatic Federation of Canada	\$500,000		\$500,000	\$1,000,000
<i>Production (Operations)</i>				
Ceremonies	\$1,730,824		\$1,730,824	\$400,000
Protocol	\$785,970		\$785,970	\$446,000
Competitions	\$1,048,031	(\$82,000)	\$966,031	\$2,724,325
Volunteers	\$87,685		\$87,685	\$515,500
Meals and Accommodation (Athletes)	\$3,077,163		\$3,077,163	\$3,800,000
Meals and Accommodation (FINA)	\$1,703,550		\$1,703,550	\$1,373,110
Logistics (Operations)	\$1,891,545	(\$112,000)	\$1,779,545	\$1,189,347
Technology (Telecommunications)	\$1,229,400	(\$960,000)	\$269,400	\$1,947,500
<i>Site management</i>				
Sites – Main and Secondary	\$7,347,916		\$7,347,916	\$3,724,200
Related Services	\$1,531,529	(\$325,000)	\$1,206,529	\$1,401,200

APPENDIX A
STATEMENT OF EXPENDITURES
For the period from April 1, 2002, to December 31, 2005

	Reported Amounts	Audit Adjustments <u>Appendix B</u>	Eligible Amounts	Budget Forecasted in 2004-06 Agreement
<i>Marketing</i>				
Public Relations / Communications	\$1,690,643	(\$150,000)	\$1,540,643	\$1,977,500
Member Services (Media)	\$109,797	(\$60,000)	\$49,797	\$140,500
Sponsorships - FINA (Ineligible Expenses: US\$2.5 million)	\$3,252,538	(\$3,252,538)	0	\$3,750,000
Corporate support	\$35,638		\$35,638	
Financing, Merchandising, Concessions	\$90,000	(\$90,000)	0	\$330,000
Host Broadcaster	\$5,572,380		\$5,572,380	\$4,204,050
<i>Administration</i>				
Finance, Administration, Ticket Sales	\$822,150		\$822,150	\$1,293,390
TOTAL EXPENSES	\$39,738,456	(\$6,859,580)	\$32,878,876	\$36,547,124

**APPENDIX B
EXPLANATION OF AUDIT ADJUSTMENTS**

Adjustments for expenditures not authorized by the Board of Directors

Salaries (see 2.4.6)	
Performance bonus paid but not provided for in the employee contract	\$(11,438)
Professional Fees (see 2.3.2, Observations)	(213,942)
Increase in fees paid to firm occupying position of Vice-President Marketing	
Executive (see 2.4.4)	
Management fees and interest not provided for in the Vice-President/CEO's contract	(36,089)

Adjustments for expenditures not eligible under the 2004-06 contribution agreement
(see Table 1, Section 1.1.3)

Bid Expenses	(277,341)
FINA – Athletes Travel	
US\$1,000,000	(1,289,232)
FINA Sponsorships	
US\$2,500,000	(3,252,538)

Adjustments for contributions of goods and services
not eligible under the 2004-06 agreement (see Table 1, Section 1.1.3)

Competitions	(82,000)
Operations	(112,000)
Telecommunications	(960,000)
Related services	(325,000)
Public Relations/Communications	(150,000)
Media services	(60,000)
Financing, Merchandising, Concessions	<u>(90,000)</u>
TOTAL AUDIT ADJUSTMENTS	<u>(\$6,859,580)</u>

APPENDIX C
XI FINA WORLD CHAMPIONSHIPS – MONTREAL 2005 ORGANIZING
COMMITTEE’S COMMENTS

The 2005 FINA World Championships Organizing Committee has not submitted any comments on the report.

**AUDIT OF THE
CONTRIBUTION AGREEMENTS**

with the

*XI FINA World Championships – Montreal 2005
Organizing Committee*

Management Letter

*Prepared for the
Department of Canadian Heritage*

**By
Samson et Associés**

March 7, 2006

A- Mandate

This audit covers the \$16,830,000 contribution made by the Department of Canadian Heritage to the XI FINA World Championships Organizing Committee (Montreal 2005) for the period from April 1, 2002, to March 31, 2006.

B- Observations and Recommendations Regarding the Management of the Project

The following observations were noted during the audit. While this was a secondary objective of our mandate, we believe that these observations and recommendations may assist the Department to improve the management of contribution agreements and control over transfer payments for events of a similar scope.

Terms and Conditions of the Contribution Agreements

Observation

The first two contribution agreements contained few requirements for Montreal 2005 to allow Canadian Heritage to oversee activities and the use of funds. In contrast with the first two agreements, the third agreement (2004-06) was more detailed and contained all the clauses required for this.

Implication

A contribution agreement that does not contain all the standard conditions required by Treasury Board diminishes the ability to control activities and expenses related to the transferred funds.

Recommendation 1

It is recommended that PCH ensure that all contribution agreements contain the standard terms and conditions that will enable the Department to control activities and expenses related to the transferred funds.

Terms and Conditions for Payment of the Holdback

Observation

Section 6.6 in Appendix A of the 2004-06 contribution agreement stipulated that the final payment of the holdback would be made upon reception and approval of a final activity report and the final audited financial statements signed and approved by the recipient's Board of Directors for the full duration of the agreement. In fact, Canadian Heritage requires another document: the audit report of the contribution agreements.

Implication

With regards to the contribution agreements for the hosting of major events, the audit team is of the opinion that this additional requirement serves to reduce the risk associated with the control of the transferred funds.

Recommendation 2

Where relevant, it is recommended that a clause be added to the contribution agreement stipulating that PCH may require an audit report before making the final payment.

Interest Earned on the Canadian Heritage Contribution

Observation

Section 2 of the 2004-06 contribution agreement states that the maximum contribution includes all interest generated on amounts paid during the period covered by the agreement. The quarterly financial statements required from the recipient and described in section 7 of Appendix A do not state that the interest earned on funds provided by PCH must be presented.

Implication

Throughout the project, Montreal 2005 did not calculate the interest earned on the PCH contributions, nor did it include it in its financial statements. The audit raised this issue and it should have estimated the interest to be deducted from PCH's final payment. The delayed implementation of this clause may lead to a challenge and dissatisfaction on the part of the recipient.

Recommendation 3

When interest earned on funding provided by the Department is included in the contribution, it is recommended that the agreement stipulate the recipient's obligation to declare the interest earned in its quarterly financial statements.

Required Financial Statements

Observation

The audit revealed that the recipient did not provide the quarterly financial statements as required by the terms of the 2004-06 contribution agreement, including revenue and expenditure statements and forecasted cash flow requirements.

Implication

This situation demonstrates that PCH did not apply the rules for the management of transfer payments, thereby increasing the risk that these funds would not be spent in accordance with the terms of the agreement.

Recommendation 4

It is recommended that the Department ensure that financial statements have been received according to the terms and conditions before advancing funds.

Representation on the Board of Directors

Observation

A departmental official was a voting member of the Montreal 2005 Board of Directors. This placed the Department in the role of funding provider and of manager of a recipient's activities.

Implication

This dual role places the Department in a real or perceived conflict of interest.

Recommendation 5

It is recommended that the Department not designate one of its officials to sit on the recipient's Board of Directors.

Financial Audit

The Department conducted a spot check in March 2004 to assess the internal and financial controls in place. This review allowed the auditors and the Department to set out the terms of the contribution agreement with the recipient and to ensure that the internal control systems were adequate. As for the financial audit of the three contribution agreements, these were not conducted until the end of the three agreements, just before the Montreal 2005 permanently closed its offices.

Implication

It was more difficult to conduct the audit, as a number of employees had already left the organization, office equipment was not all available, and records had begun to be refiled for the archives.

Recommendation 6

It is recommended that the audit not be conducted so long after the event and that, where relevant, an audit be carried out after each agreement.

Recommendation 7

For all major projects, PCH should consider a preliminary meeting with the recipient to ensure that the terms and conditions of the contribution agreement have been well understood and that an internal control system is in place.

ACTION PLAN AND RESPONSE TO THE AUDIT REPORT

Audit report of the contribution agreements with the XI FINA World Championships – Montreal 2005 Organizing Committee

ACTION PLAN AND RESPONSE TO THE AUDIT REPORT

March 22, 2006

General Findings

Sport Canada is satisfied with the audit report, in particular with the finding that all funds provided to Montreal 2005 were used in accordance with the three contribution agreements and that the terms concerning equitable financing in the *Policy for Hosting International Sport Events* were respected (limit of 35% of total event costs and 50% of total public sector contribution).

In 2006-2007, Sport Canada intends to strengthen its contribution agreement for all events receiving more than \$250,000 by factoring in the auditors' conclusions. The contribution agreement for events receiving less than \$250,000 will be modified where relevant.

	General Findings	Status	Comments	Implementation schedule
1	All the funding provided to Montreal 2005 was used for the purposes set out in the three contribution agreements (for more details, see section 2.1).	Accepted	Sport Canada accepts the finding.	N/A
2	The funding provided was used in accordance with the report submitted by Montreal 2005, with respect to the use of the Government of Canada contribution (for more details, see section 2.2).	Accepted	Sport Canada accepts the finding and the fact that the \$6,859,580 adjustments have no impact on the contribution since the \$27,533,005 in eligible expenditures incurred by Montreal 2005 as per the contribution agreement is more than sufficient to cover the \$16,830,000 contribution provided by Canadian Heritage. In addition to the adjustments for ineligible expenses (FINA sponsorships, athletes' travel, exchange of goods and services), Sport Canada agrees with the proposal that unapproved expenses be considered as ineligible expenses. Furthermore, the	N/A

ACTION PLAN AND RESPONSE TO THE AUDIT REPORT

			Department is satisfied with the finding that the terms on equitable financing in the <i>Policy for Hosting International Sport Events</i> were respected (limit of 35% of total event costs and 50% of total public sector contribution).	
3	The recipient's internal control framework was adequate for delivering the activities described in the contribution agreements, except where noted in section 2.3.	Accepted	<p>Sport Canada accepts the finding and intends to strengthen its contribution agreement template:</p> <ul style="list-style-type: none"> ➤ In order for recipients to implement an adequate management framework and ensure comprehensive monitoring of cash flow; ➤ To ensure transparency in all financial decisions and transactions including the delegation of cheque signing authorities; ➤ To create a code of ethics. 	The contribution agreement template will be strengthened.
4	Montreal 2005 exercised sound contract management, except for the examples described in section 2.4.	Accepted	<p>Sport Canada accepts the finding and intends to strengthen its contribution agreement template:</p> <ul style="list-style-type: none"> ➤ In order for recipients to create a framework for contract management and to guarantee transparency in all financial decisions and transactions. ➤ In order for inadequately justified expenses and the payment of unapproved contracts to be considered as ineligible expenses. ➤ In order for commissions paid for sponsorship or corporate support revenues in cash or goods and services to also be considered as ineligible expenses. 	The contribution agreement template will immediately be improved strengthened.

ACTION PLAN AND RESPONSE TO THE AUDIT REPORT

5	The recipient complied with all of the terms and conditions of the contribution agreements, except where noted in section 2.5.	Accepted	Sport Canada accepts the finding. However, it should be noted that the contribution agreement template created by the Department for all its programs and adapted to the Hosting Program, was used for the first time with this recipient. We will be strengthening certain clauses of the contribution agreement, such as those regarding the type and frequency of financial reporting by the recipient.	The contribution agreement template will immediately be modified.
6	<p>Review of Financial Activities</p> <p>In compliance with the contribution agreement, the \$56,238 in interest earned on funding provided by the Department should be deducted from the \$1.5 million holdback</p>	Accepted	Since the Government of Canada does not want to increase the Organizing Committee's deficit, Sport Canada will modify the 2004-06 contribution agreement such that the maximum contribution for the XI FINA World Championships will be increased from \$17M to \$17,056,238, therefore taking into account the interest earned. The Government of Canada has contributed \$15.5M towards the Championships to date. As a result, the final payment (holdback) to be paid will remain at \$1.5M, which is equivalent to the remaining amended contribution payment of \$1,556,238 less the \$56,238 interest earned.	Sport Canada intends to pay the \$1.5M holdback, which is equivalent to \$1,556,238, the amount remaining in the amended contribution less the \$56,238 interest earned, as soon as the audit report, management letter and responses to these documents are approved by the Department's Audit and Evaluation Committee.

ACTION PLAN AND RESPONSE TO THE MANAGEMENT LETTER

Management letter regarding the audit of the contribution agreements with the XI FINA World Championships – Montreal 2005 Organizing Committee

ACTION PLAN AND RESPONSE TO THE MANAGEMENT LETTER

March 17, 2006

General Findings

Sport Canada accepts six of the seven recommendations and disagrees with the implication of the fourth.

The new contribution agreement template created in May 2004 enabled Sport Canada to introduce terms and conditions, which strengthened the recipient accountability. In light of the audit, certain clauses will now require that organizing committees that receive more than \$250,000 from the Hosting Program state in their financial reports how much interest they have earned on funding provided by the Department. The agreement for events receiving less than \$250,000 will be modified where relevant.

	Recommendation	Status	Comments	Implementation Schedule
1	It is recommended that PCH ensure that all contribution agreements contain the standard terms and conditions that will enable the Department to control activities and expenses related to the transferred funds.	Accepted	Sport Canada accepts the recommendation and will ensure that the contribution agreement used for the FINA World Championships will be used for future events that receive more than \$250,000. The template will also be strengthened to take into consideration recommendations 3, 4 and 6 regarding interest earned on funding provided by the Department, Government of Canada representation on Boards of Directors and recipient audits.	Implementation in 2006-2007

ACTION PLAN AND RESPONSE TO THE MANAGEMENT LETTER

2	Where relevant, it is recommended that a clause be added to the contribution agreement stipulating that PCH may require an audit report before making the final payment.	Accepted	Sport Canada accepts the recommendation. For events receiving more than \$250,000, the branch will ensure that an audit report must be provided before making the final payment.	Implementation in 2006-2007.
3	When interest earned on funding provided by the Department is included in the contribution, it is recommended that the agreement stipulate the recipient's obligation to declare the interest earned in its quarterly financial statements.	Accepted	Sport Canada accepts the recommendation and will strengthen the contribution agreement template for events that receive more than \$250,000 by including a clause that stipulates the recipient's obligation to declare interest earned on funding provided by the Department in its quarterly financial statements.	Implementation in 2006-2007.
4	It is recommended that the Department ensure that financial statements have been received according to the terms and conditions before advancing funds.	Accepted	Sport Canada accepts the recommendation. However, it should be noted that although the recipient did not submit quarterly financial statements, the recipient did provide internal financial reports that included the information required to manage the project.	Implementation in 2006-2007.
5	It is recommended that the Department not designate one of its officials to sit on the recipient's Board of Directors.		Sport Canada has carefully noted the recommendation. However, it raises a governance issue that requires an in-depth analysis. Before accepting or refusing it, Sport Canada will reflect on the role the federal government should play with respect to recipient Boards of Directors for sport events.	
6	It is recommended that the audit not be conducted so long after the event and that, where	Accepted with modifications	Sport Canada agrees that the audit must be carried out as soon as possible. For events receiving more than \$250,000, the contribution agreement template will	Implementation in 2006-2007.

ACTION PLAN AND RESPONSE TO THE MANAGEMENT LETTER

	relevant, an audit be carried out after each agreement.		stipulate that an audit must be carried out in either the planning or early operational phase. Depending on the findings of the initial audit, another one may be conducted before or after the event. For events receiving less than \$250,000, Sport Canada will continue to carry out spot audits.	
7	For all major projects, PCH should consider a preliminary meeting with the recipient to ensure that the terms and conditions of the contribution agreement have been well understood and that an internal control system is in place.	Accepted	Sport Canada accepts the recommendation. In fact, it is a standard practise for Sport Canada to meet with its recipients to ensure that the terms and conditions have been well understood. A written follow-up is also carried out.	Implementation in 2006-2007.