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Audit of Accounts Receivable Phase II – Collections, Write-offs and Remissions

November 2016

Audit of Audit of Accounts Receivable Phase II – Collections, Write-offs and Remissions

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PDF

Cat. No. Em20-55/2017E-PDF

ISBN: 978-0-660-07184-8

ESDC

Cat. No. SP-1134-01-17

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Executive Summary

The Audit of Accounts Receivable – Collections, Write-offs and Remissions was included in the 2015–17 Risk Based Audit Plan. Accounts Receivable (A/R) are governed by several key pieces of legislation and policies. Sections 23, 24 and 25 of the *Financial Administration Act* (FAA), sections 4 to 9 of *Debt Write Off Regulations*, Treasury Board of Canada Secretariat (TBS) Directive on Receivables Management and Guideline on Collection of Receivables set out the main legal and policy requirements to manage the A/R life cycle.

According to section 6.2.1 of the Directive on Receivables Management, the Chief Financial Officer (CFO) is responsible for ensuring that internal controls for the administration of A/R are established, are in place and include, at a minimum:

- The appropriate division of duties related to credit-granting, collections, maintenance of accounting records, handling and reconciling of money, and write-offs;
- The provision of complete audit trails to track all claims from the transaction that gave rise to the receivable through to its final settlement;
- The establishment and monitoring of results-based measurement mechanisms; and
- The preparation and distribution to management of periodic reports on the financial and non-financial activities of the portfolio, including receivable ageing statements.

Employment and Social Development Canada (ESDC) generates A/R from many programs as part of regular operations. Programs generating the highest levels of A/R and recoveries are the Canada Student Loans Program (CSLP), Employment Insurance (EI), Canada Pension Plan (CPP), Old Age Security (OAS), Wage Earner Protection Program (WEPP) and Grant and Contribution (G and C) Programs.

The management of A/R and recoveries of overpayments is a shared responsibility among Program areas, the Chief Financial Officer Branch (CFOB), an external service provider and the Canada Revenue Agency (CRA).

On August 1, 2005, A/R collection activities were transferred from ESDC to the CRA. This arrangement is specified in the Memorandum of Understanding (MOU) signed in November 2015 by the two parties.

Write-off, as defined by the FAA, is the removal of a debt in whole or in part from the A/R records. The writing-off of any debt obligation or claim does not affect any right of Her Majesty to collect or recover the debt, obligation or claim in the future. Remission, as defined by the FAA, is the decision to forgive an otherwise legally enforceable debt. This means that the debt is forgiven and the Crown gives up the right to resume collection at a future date, the debtor is released from the obligation to pay. The debt may be forgiven in whole or in part.

Audit Objective

The objective of this audit was to assess the design and operating effectiveness of key controls surrounding the collections, write-offs and remissions of A/R.

Summary of Key Findings

- Overall, roles and responsibilities are clearly defined, communicated and understood by programs and CFOB staff.
- Segregation of duties for collections, write-offs and remissions of A/R is appropriate within programs and CFOB.
- Adequate oversight is in place for collection activities performed by ESDC and write-offs and remissions of A/R¹.
- Access controls to program and corporate financial systems are designed effectively and audit trails are maintained.
- ESDC A/R information recorded in the Departmental Accounts Receivable System (DARS) allow collection activities to be performed by CRA on CSLP accounts in default for more than 270 days, EI accounts, CPP and OAS fraudulent accounts, WEPP and G and C programs.
- ESDC collection activities are performed and initiated on a timely basis for CSLP; for EI², CPP and OAS accounts where the claimant is currently receiving benefit payments. Most A/R for these programs are on track to be collected within the timelines established by ESDC programs.
- Data integrity issues combined with unavailability of data with respect to CPP and OAS accounts not in receipt of benefits are impacting the ability of CRA to perform collection activities on all CPP and OAS accounts.

Audit Conclusion

The audit concluded that key controls surrounding the collections, write-offs and remissions of A/R were in place and operating as intended. There is a need to improve the accuracy of CPP account data available in DARS and make non fraudulent OAS data available in order to undertake collection activities on accounts where the claimant is currently not receiving benefit payments.

¹ Oversight of collection activities at CRA has not been examined.

² CRA does collect inactive EI debts (e.g. not in receipt of benefits). Collection activities performed by CRA were not examined in the context of this audit.

Recommendations

1. The Assistant Deputy Minister (ADM) of Benefit Delivery Services (BDS)³ should update its delegation of authorities and the Functional Guidance and Procedures (FGP) in order to comply with relevant program legislations.
2. The ADM of BDS, in collaboration with the CFO, should ensure the accuracy and availability of CPP and OAS data to ensure the proper establishment and commencement of collection activities on these accounts.

³ Throughout the reporting phase of the audit, an organizational change took place within the Department. As a result, we have issued the audit recommendations to the ADM of BDS within the Transformation and Integrated Service Management Branch.

I. Background

I.1 Context

The Audit of Accounts Receivable – Collections, Write-offs and Remissions was included in the 2015–17 Risk Based Audit Plan. A/R is governed by several key pieces of legislation and policies. Sections 23, 24 and 25 of the FAA, sections 4 to 9 of *Debt Write Off Regulations*, TBS Directive on Receivables Management and Guideline on Collection of Receivables set out the main legal and policy requirements to manage the A/R life cycle (establishment, collection, write-off and remission).

According to section 6.2.1 of the Directive on Receivables Management, the CFO is responsible for ensuring that internal controls for the administration of A/R are established, are in place and include, at a minimum:

- The appropriate division of duties related to credit-granting, collections, maintenance of accounting records, handling and reconciling of money, and write-offs;
- The provision of complete audit trails to track all claims from the transaction that gave rise to the receivable through to its final settlement;
- The establishment and monitoring of results-based measurement mechanisms; and
- The preparation and distribution to management of periodic reports on the financial and non-financial activities of the portfolio, including receivable ageing statements.

Programs generating the highest levels of A/R and recoveries of overpayments in ESDC are the CSLP, EI, CPP, OAS, WEPP and G and C Programs.

The management of A/R and recoveries is a shared responsibility among Program areas, the CFOB, an external service provider and the CRA. Program areas manage client accounts and establish overpayments in their respective benefit payment systems. The National Accounts Receivable unit within CFOB, maintains account balances in DARS.

Multiple parties are currently involved in collecting A/R owed under various departmental programs:

- collections of CSLP accounts in good standing are performed by an external service provider;
- collections of programs' accounts that are still in receipt of benefits are performed by ESDC; and
- the responsibility for collecting the other debts, including student loans in default, is performed by CRA since 2005.

I.2 Audit Objective

The objective of this engagement was to assess the design and operating effectiveness of key controls surrounding the collections, write-offs and remissions of A/R.

I.3 Scope

The audit of Accounts Receivable Phase I, which focused on governance, establishment, monitoring and reporting, was completed in fiscal year 2015–16. The scope of the Audit of Accounts Receivable Phase II focused on collections, write-offs and remissions activities of the A/R life cycle. Departmental programs examined during the audit included CSLP, EI, CPP, OAS, WEPP and G and C Programs. Collection activities performed by CRA were not examined in the context of this audit.

I.4 Methodology

This audit used a number of methodologies during the conduct phase completed between May and July 2016 including:

- Documentation review and analysis;
- Sampling and file review testing;
- Process observation and analysis;
- On-site observations and walkthroughs at regional processing centers located in Ontario, Quebec and Prince Edward Island; and
- Data analysis of collections, write-offs and remissions of A/R.

File review results were derived from random samples of:

- 314 accounts for collections; and
- 318 accounts for write-offs and remissions

2. Audit Findings

2.1 An adequate control environment is in place to support collection, write-off and remission activities

Roles and responsibilities

The management of A/R and recoveries is a shared responsibility among Program areas, the CFOB, an external service provider and the CRA. Program areas are responsible for managing program overpayments within their respective areas. They carry out these responsibilities by developing guidelines and processes to establish overpayments, calculating overpayments and penalties when applicable, inputting these into their programs' system, and sending notification letters to clients. The National Accounts Receivable unit within CFOB, maintains account balances in DARS.

Once overpayment accounts are established:

- CSLP has contracted with an external service provider to manage the repayment of Canada Student Loans. The service provider returns to ESDC those loans that have no repayment activities in 270 days despite all the collection efforts, these loans are transferred to CRA for further collection activities;
- Collections of CPP and OAS accounts that are still in receipt of benefits are performed by ESDC; and
- Collections of EI, G and C, WEPP as well as CPP and OAS fraudulent accounts are performed by CRA.

CFOB has been granted the authority to write-off all unrecoverable debts except for certain overpayments specified by the *EI Regulations subsections 56(1)e and 56(2)*. In other cases, Treasury Board approval is required for non-budgetary and employment related debts before they can be written-off.

Delegation of authorities to write-off OAS and CPP debts

Remission is applicable only to CPP and OAS debts pursuant to the *CPP Act/OAS Act* and authority for remissions is delegated to CPP and OAS programs. The departmental CFOB Debt Write-off Policy states that the *CPP Act/OAS Act* do not provide authority to Processing and Payment Services Branch (PPSB) to write-off a debt. However, PPSB's delegation of authorities gives program staff the authority to write-off debts and its FGP provide instructions on writing off CPP and OAS debts. The write-off authority resides with CFOB, not with PPSB. Although the risk of writing off accounts without the proper authority is low (all reviewed transactions were adequately approved), delegation of authorities has to be clearly documented and communicated to PPSB staff.

Overall, other than the exception noted above, roles and responsibilities are clearly defined, communicated and understood by CFOB, and programs' staff. Various departmental policies, delegated authorities manual and an online reference tool are available on the ESDC Intranet for reference and guidance.

Segregation of duties

Authorization of benefit entitlement and establishment of program overpayments are performed at the program level. Collection of A/R is completed either by the CRA or by program staff who has no access to cash and cheque handling. Write-off of accounts is recommended by CRA to ESDC when accounts are identified as uncollectible, these proposed write-offs are subject to CFOB sampling. Once CFOB is satisfied that all accounts meet the write-off criteria, they obtain the proper authorization to write off the accounts. Remission (applicable to CPP and OAS) is recommended by the program officer and is reviewed and approved by the required level of authority according to the delegation of authority instrument. The audit team concludes that there is appropriate segregation, between incompatible functions, within programs and CFOB, for collection, write-off and remission activities.

Oversight

CRA recommends to ESDC accounts for write-off. Before presenting the recommended write-offs to ESDC National Write Off and Remissions Review Committee (NWORRC), CFOB reviews a random sample of these accounts. The sample is comprised of 281 CSLP write-offs greater than \$25,000 and all write-offs greater than \$25,000 for all other programs. The sample also includes 281 program write-offs for less than \$25,000. This activity is performed to ensure proper documentation as outlined by the CFOB sampling checklist by bad debt type is on file.

Overpayments specific to the *EI Regulations subsections 56(1)e and 56(2)* are approved by the EI program but are not included in the CFOB samples. A total of \$4 million EI overpayments have been written off in fiscal year 2015-16 under *EI Regulations subsections 56(1)e and 56(2)*. Our file review identified errors in writing off accounts under *EI Regulations subsection 56(2)*, i.e. accounts were written off even though they did not meet the outside of 12 month criterion. Management should consider having these write-offs reviewed by CFOB, the Integrity Services Branch (ISB) or NWORRC.

CPP and OAS remissions are identified by program officers. All remission transactions less than \$25,000 are reviewed by the level of required authority based on threshold. All remissions greater than \$25,000 are reviewed by NWORRC.

NWORRC's mandate is to review the debts proposed for write-off or remission requiring Treasury Board approval as well as all other write-off and remission of debts valued over \$25,000. Following review, NWORRC recommends for approval to the appropriate delegated authority (i.e. CFOB, Treasury Board or Senior ADM of PPSB), the proposed write-off or remission over \$25,000.

ISB is responsible for sampling transactions to ensure that departmental procedures were followed and proper authorisation was obtained.

The audit team concludes that appropriate oversight is in place for the write-off and remission of A/R at the departmental level⁴.

Systems access

All access requests must be initiated by the responsible managers or authorized requesters; access right is based on job profile. Access control is managed through a centralised approach where access requests are sent to the Management of Identity, Control and Access (MICA) at Shared Services Canada. Once MICA has validated the requester, MICA will create, modify or cancel the access in accordance with the request. User activities are tracked by program and corporate systems which have an audit trail log available for user activity enquiries. The audit team reviewed access controls to program and corporate financial systems and found that access is controlled and audit trails are maintained.

Recommendation

1. The ADM of BDS should update its delegation of authorities and the FGP in order to comply with relevant program legislations.

Management Response

Management agrees with the recommendation. Transformation and Integrated Service Management Branch (TISMB) will collaborate with the CFOB to ensure that the processes used for collections, write-offs and remissions are compliant with the FAA, the CPP and the OAS Act. Actions are expected to be completed by September 30, 2017.

2.2 Collection activities of CSLP are adequate and performed in a timely manner at the service provider

ESDC has contracted with an external service provider to manage the repayment of Canada Student Loans. The service provider returns to ESDC those loans that have no repayment activities in 270 days despite collection efforts. A CSLP loan becomes delinquent the day after a scheduled payment is missed. The service provider works with the borrower to bring the loan back into good standing before sending it back to ESDC for CRA collection.

File reviews completed by the audit team indicated that the collection was initiated immediately by the service provider and 84% of sampled accounts were brought back to good standing following collection efforts.

⁴ Oversight of collection activities at CRA has not been examined.

2.3 Not all collection activities are carried out because of data integrity and availability issues

Collection of accounts by CRA

CRA is responsible for collecting all A/R accounts. File reviews confirmed that CRA collection activities are performed on all EI accounts, CPP fraudulent accounts, OAS fraudulent accounts, G and C, WEPP and student loans in default. However, this audit was not designed to express an opinion on the adequacy of the collection services performed by CRA. An Audit of Accounts Receivable – Delivery of ESDC's Commitments as per the MOU with CRA is included in the approved 2016–18 Risk Based Audit Plan. This planned audit will examine to what extent ESDC responsibilities vis-à-vis CRA collection activities are adequate.

CRA is currently not collecting all CPP and OAS A/R since it does not have all the information required to perform collections on these specific accounts. CRA is only able to collect fraudulent accounts since this information is available in DARS. Due to system conversion challenges between the Information Technology Renewal Delivery System (ITRDS) and DARS, not all CPP data in DARS is accurate. Furthermore, OAS accounts of the OAS on-line system have not been converted to DARS and CRA collection officers do not have direct access to this system.

Without a systematic collection on all CPP and OAS A/R, the Department is not optimizing the use of its resources and may be giving up potential recoveries. Having accurate information on CPP accounts and available information on OAS accounts would increase the collection rate for these programs and allow CRA to fully perform collection activities included in the MOU.

Collection on accounts still in receipt of benefits

For beneficiaries who are currently receiving CPP or OAS benefits, ESDC initiates collection by deducting a monthly recovery rate on payments based on income. The default deduction rate is 25% of the payment for CPP and OAS. For low income seniors, the CPP and OAS deduction rate is 10% of the payment.

The EI automatic deduction process allows CRA to perform collection activities on all EI accounts with active ESDC participation. The default deduction rate is 50% of the EI benefit payment and starts automatically following a 21-day grace period. Clients call CRA to discuss a reduced deduction rate if they disagree with the default 50% rate.

Our file reviews indicated that collection on the EI accounts, CPP and OAS accounts that are still in receipt of benefits is operating appropriately. Overall, collection activities are being undertaken following the waiting period which is 21 days for EI and 30 days for CPP and OAS. 78% of sampled accounts were on track to recover the A/R within the program established timelines; which is five years for A/R less than \$10,000 and ten years for A/R greater than \$10,000.

Recommendation

2. The ADM of BDS, in collaboration with the CFO, should ensure the accuracy and availability of CPP and OAS data to ensure the proper establishment and commencement of collection activities on these accounts.

Management Response

Management agrees with the recommendation. TISMB will continue to work with the CFOB to implement the Overpayment Data Clean-up Strategy which will identify and address the number of accounts where there is low to no probability of recovery and ensure that the data being transferred to the new system is accurate and up to date. Actions are expected to be completed by September 30, 2017.

2.4 Opportunities exist to evaluate if strengthened A/R monitoring may improve overall management of the A/R life cycle

The audit team expected that the Department would have key performance indicators (KPIs) to monitor collection, write-off and remission activities. Section 6.2.1 of the Directive on Receivables Management requires the establishment and monitoring of results-based measurement mechanisms. We found that no KPIs have been developed for the programs included in the audit scope except for CSLP. CSLP has a Service Level Agreement with the external service provider. KPIs relevant to collections are default reduction by loan ageing, delinquency rate and borrower satisfaction which includes overall satisfaction, service access, service quality, Repayment Assistance Awareness, etc. WEPP has set up an A/R dashboard to monitor its recovery rates and write-off amounts by year and by type of entitlement. For other programs scoped in this audit, we did not find any KPIs to monitor how the Department is performing with regards to collection, write-off and remission activities.

The analysis of write-off data for fiscal year 2015–16 demonstrated that the most significant root cause for write-offs was time limitation, i.e. statute barred for further legal action. Results from data analysis indicated that accounts were written off due to time limitation reached for collection across CSLP (86%), EI (74%) and G and C (71%) programs. For WEPP, 65% of the subrogated debt write-off was due to bankruptcy discharge. Given the nature of WEPP, it is understandable that most write-offs would be triggered by the bankruptcy discharge. Write-offs under CPP were typically triggered by death of the beneficiary.

The audit team completed interviews, walkthroughs and file reviews of remissions in both National Headquarters and regional offices. We noted that 26% of CPP and 31% of OAS remissions greater than \$25,000 were triggered by administrative errors. For remissions less than \$25,000, 64% of CPP and 35% of OAS files reviewed were caused by administrative errors. The majority of administrative errors were caused by not keeping client information (marriage, death, departure from country, etc.) up-to-date.

The auditors believe that establishing some measures, such as the ones identified below may strengthen departmental collection, write-off and remission activities:

- Timeline required to transfer A/R to the CRA so that collection activities can start well in advance of the statute-barred date;
- Timeline to complete write-off/remission from identification of potential write-off/remission to DARS input;
- Administrative error rate as a % of the overall write-off/remission in a given fiscal year; and
- A/R ageing by year as a % of the overall A/R portfolio.

The audit team recognizes the unique nature of ESDC's mandate which focuses on the delivery of social programs and services but believes that strengthened A/R monitoring may improve overall management of the A/R life cycle.

3. Conclusion

The audit concluded that key controls surrounding the collections, write-offs and remissions of A/R were in place and operating as intended. There is a need to improve the accuracy of CPP account data available in DARS and make non fraudulent OAS data available in order to undertake collection activities on accounts where the claimant is currently not receiving benefit payments.

4. Statement of Assurance

In our professional judgement, sufficient and appropriate audit procedures were performed and evidence gathered to support the accuracy of the conclusions reached and contained in this report. The conclusions were based on observations and analyses at the time of our audit. The conclusions are applicable only for the assessment of key controls pertaining to the collections, write-offs and remissions of A/R for CSLP, EI, CPP, OAS, WEPP and G and C Programs. The evidence was gathered in accordance with the *Internal Auditing Standards for the Government of Canada* and the *International Standards for the Professional Practice of Internal Auditing*.

Appendix A: Audit Criteria Assessment

AUDIT CRITERIA	RATING
It was expected that the Department has established appropriate system access controls to ensure only authorized personnel have access to modify A/R, process write-offs and remissions.	●
It was expected that the Department has maintained an audit trail on monitoring of collection, write-off and remission activities.	●
It was expected that the Department has established proper segregation of duties to ensure the control environment is sound for protection of assets.	●
It was expected that the Department has roles and responsibilities related to debt collection, write-off and remission clearly defined, documented and understood.	◐
It was expected that the Department has established key performance indicators, at program and departmental level, on collection activities.	◐
It was expected that the Department has key performance indicators and reports the results to management.	◐
It was expected that the Department has undertaken collection activities on departmental A/R in DARS and on overpayments in program systems.	◐
It was expected that the Department has a process in place to ensure invoices and statements are sent to customers in a timely manner.	●
It was expected that the Department has a process in place to ensure clients are charged the appropriate amount to avoid disputes and potential delays in collection.	●
It was expected that the Department has policies and guidelines in place to ensure compliance with write-off legislation.	●
It was expected that the Department has a process in place to ensure appropriate review and approval of write-offs and remissions.	◐
It was expected that the Department has a process in place to ensure that all write-offs and remissions are completely and accurately recorded while the balance for allowance for doubtful accounts is updated in a timely manner.	◐
☆ Best practice ● Sufficiently controlled, low risk exposure ◐ Controlled, but should be strengthened, medium risk exposure ○ Missing key controls, high risk exposure	

Appendix B: Glossary

ADM	Assistant Deputy Minister
A/R	Accounts Receivable
BDS	Benefit Delivery Services
CFO	Chief Financial Officer
CFOB	Chief Financial Officer Branch
CPP	Canada Pension Plan
CRA	Canada Revenue Agency
CSLP	Canada Student Loans Program
DARS	Departmental Accounts Receivable System
EI	Employment Insurance
ESDC	Employment and Social Development Canada
FAA	<i>Financial Administration Act</i>
FGP	Functional Guidance and Procedures
G and C	Grant and Contribution
ISB	Integrity Services Branch
ITRDS	Information Technology Renewal Delivery System
KPI	Key Performance Indicators
MICA	Management of Identity, Control and Access
MOU	Memorandum of Understanding
NWORRC	National Write-off and Remissions Review Committee
OAS	Old Age Security
PPSB	Processing and Payment Services Branch
TISMB	Transformation and Integrated Service Management Branch
TBS	Treasury Board of Canada Secretariat
WEPP	Wage Earner Protection Program