



## AUDIT OF THE INDIGENOUS TAX ADMINISTRATION AGREEMENTS' GOVERNANCE FRAMEWORK

Audit Report

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Internal Audit Directorate

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## EXECUTIVE SUMMARY

### WHAT WE EXAMINED

The objective of this audit was to provide reasonable assurance that the Department of Finance Canada's governance framework for Indigenous Tax Administration Agreements is effective. The focus of this audit was on the agreements and remittances to Indigenous groups.

To assess the adequacy of the framework, we reviewed the governance processes and structures in place that are most relevant to the subject matter (integrity and transparency, accountability and compliance with laws and regulations, and risk and priorities).

### WHY IT IS IMPORTANT

Strengthening Canada's relationship with Indigenous peoples is a government priority as stated in the Minister's mandate letter and in the 2018–19 Departmental Plan. The systems and processes used in the administration of the Indigenous Tax Administration Agreements in general, are modeled on the systems and processes used in the administration of tax agreements with the provinces and territories, which involve much larger dollar amounts. Findings from this audit may, to some extent, be relevant to federal-provincial-territorial tax agreements.

### WHAT WE FOUND

The Department of Finance has a well-established governance framework in place for Indigenous Tax Administration Agreements (TAAs), which ensures that the agreements and remittances are managed with integrity, transparency, accountability and in compliance with laws and regulations. The governance framework is also risk-sensitive and designed to efficiently address government priorities.

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**Acting Chief Audit Executive**

## BACKGROUND

1. In July 2018, the Deputy Minister of the Department of Finance Canada (the Department) requested that an internal audit be conducted on the effectiveness of the Department's governance framework for Indigenous Tax Administration Agreements (TAAs).
2. Multiple stakeholders within the Department have a role to play in this governance framework. The Tax Policy Branch (TPB) is responsible for the development and evaluation of federal taxation policies and legislation in the areas of personal income tax, business income tax, and sales and excise tax. The TPB is also responsible for the negotiation of, and aspects of the administration related to, arrangements with provinces, territories and Indigenous groups<sup>i</sup> in respect of a number of tax administration and coordination agreements, such as TAAs. Responsibility for the Indigenous TAAs rests with the Intergovernmental Tax Policy, Evaluation and Research Division within the TPB.
3. The Financial Management Directorate (FMD) of the Corporate Services Branch (CSB) is responsible for remitting the taxes to Indigenous groups based on the estimates and reconciliation adjustments prepared by the TPB in accordance with the TAAs. The Law Branch also plays a key role in the preparation and review of documents at the negotiation phase of TAAs and providing advice on the TAAs on an as needed basis.
4. There are currently 54 Indigenous TAAs<sup>ii</sup> in effect; 8 First Nations Sales Tax Agreements (FNST), 15 First Nations Personal Income Tax Agreements (FNPIT), and 31 First Nations Goods and Services Tax Agreements (FNGST).
  - FNST arrangements relate to the taxing of three products by Indigenous groups (tobacco, alcohol and fuel) and are considered legacy agreements. There are no new agreements being negotiated at this time given that over the last 10 years the focus has been on negotiating FNGST arrangements.
  - FNGST arrangements relate to the taxing of the full GST base in respect of consumption on a taxing Indigenous group's lands. It is available for both *Indian Act* bands and Indigenous self-governments.

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<sup>i</sup> Indigenous groups include *Indian Act* bands as well as Indigenous self-governments.

<sup>ii</sup> For more information, see the Department's [website](#).

- FNPIT arrangements relate to levying income tax on all individuals resident on a taxing Indigenous group's lands. It is currently only available for Indigenous self-governments.
5. Under Indigenous TAAs, the Canada Revenue Agency (CRA) collects, administers and enforces Indigenous taxes on behalf of the Indigenous groups. The Department of Finance is responsible for calculating, remitting and accounting for remittances to Indigenous groups in respect of these taxes.
  6. On an annual basis, the Office of the Auditor General (OAG) performs specified auditing procedures on all of the calculations and documentation related to TAA remittances to Indigenous groups. This work is performed in order to ensure that the calculations, remittances and overall administration frameworks comply with the laws and the terms of the relevant Indigenous TAAs.

## AUDIT OBJECTIVE AND SCOPE

### OBJECTIVE

7. The objective of this audit was to provide reasonable assurance that the Department of Finance Canada's (the Department) governance framework for Indigenous Tax Administration Agreements (TAAs) is effective.

### SCOPE

8. The audit covered the period from January 2014 to December 2018 and included the following key areas of the governance processes and structures in place with respect to the management of the TAAs:
  - Integrity and Transparency;
  - Accountability and Compliance with Laws and Regulations;
  - Risk-Sensitivity; and,
  - Government Priorities.
9. The scope of the audit focused on the roles and responsibilities of the TPB's Intergovernmental Tax Policy, Evaluation and Research Division and the CSB's FMD with respect to the TAAs and remittances to Indigenous groups. Limited work was performed to understand the roles and responsibilities of the Law Branch with respect to the TAAs.

10. The audit did not assess the IT general controls (ITGCs) as this area is assessed on an annual basis by the OAG.

## APPROACH

11. This audit was conducted by the Department's Internal Audit Directorate (IAD).

12. The publications that we used as guidance in determining our audit approach included:

- The Committee of Sponsoring Organizations of the Treadway Commission's (COSO) Internal Control – Integrated Framework (2013);
- The Institute of Internal Auditors (IIA) – The International Professional Practices Framework's (IPPF) Practice Guide – Assessing Organizational Governance in the Public Sector (2014);
- COSO's Enterprise Risk Management – Integrating with Strategy and Performance (2017); and
- IIA – IPPF's Practice Guide – Assessing the Adequacy of Risk Management Using ISO 31000 (2010).

13. During the conduct of the audit, we:

- Interviewed key departmental stakeholders from the TPB, CSB and Law Branch;
- Reviewed relevant documents including TAAs, the 2011 Indigenous Tax Narrative<sup>iii</sup>, applicable legislation, delegations of authorities, and the 2016 to 2018 results of the OAG's specified auditing procedures;
- Performed process control mapping to better understand the system for administering the TAAs and related remittances, the controls in place and to identify the roles and responsibilities of key stakeholders;

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<sup>iii</sup> The Indigenous Tax Narrative is a document describing the processes related to Indigenous TAAs, including roles and responsibilities.

- Conducted walkthroughs of Indigenous TAAs using the process control maps and supporting documentation to test the functioning of processes and controls in the administration of these agreements. Three sample agreements were assessed:
  - FNST: The Little Shuswap Lake Indian Band Sales Tax Administration Agreement (2006);
  - FNGST: The Buffalo Point First Nation Goods and Services Tax Administration Agreement (2011); and,
  - FNPIT: The Carcross/Tagish First Nation Personal Income Tax Administration Agreement (2012).
- Conducted analyses of key departmental documents including calculations of taxes remitted and payment process reports; and
- Reviewed the results of fraud questionnaires and assessed adequacy of controls to prevent/detect fraud.

14. Fieldwork for this audit was substantially completed by March 21, 2019.

## OVERALL OPINION

15. Sufficient and appropriate procedures were performed, and evidence gathered, to support the accuracy of the audit conclusion. The audit findings and conclusion were based on a comparison of the conditions that existed as of the date of the audit against established criteria that were agreed upon with management.
16. The findings and conclusion are only applicable to the entities examined and for the scope and time period covered by the audit.

## STATEMENT OF CONFORMANCE

17. The audit was conducted in conformance with the International Standards for the Professional Practice of Internal Auditing, as supported by the results of the quality assurance and improvement program.



## DETAILED FINDINGS

### GOVERNANCE FRAMEWORK – INTEGRITY, TRANSPARENCY AND ACCOUNTABILITY

18. Governance is defined as the combination of processes and structures implemented by an organization to inform, direct, manage and monitor the activities of the organization toward the achievement of its objectives. The internal audit team expected the Department of Finance Canada (the Department) to have an established governance framework in place to ensure that the Indigenous Tax Administration Agreements (TAAs) and remittances are managed effectively. This would include managing the TAAs with integrity and transparency, and accountability.

#### Integrity and Transparency

19. Integrity and transparency are two important attributes of a strong ethical culture. The Cambridge dictionary defines integrity as “the quality of being honest and having strong moral principles that you refuse to change” and defines transparency as “a situation in which business and financial activities are done in an open way without secrets, so that people can trust that they are fair and honest”. These attributes are important in managing the TAAs so that the Indigenous groups trust that they are receiving a fair and appropriate amount of taxes.
20. We found that the Department has processes in place to ensure that all employees adhere to the Values and Ethics Code of the Public Sector and the Department of Finance Code of Conduct. The Department has an established Values and Ethics Program that supports and guides employees in complying with the highest ethics and standards of conduct, including integrity and transparency, in their daily activities.

#### Accountability and Compliance

21. Accountability is necessary to make management and staff answerable for their behaviour and responsive to the organization’s key stakeholders. Compliance refers to conforming with legislation and regulations.
22. While mapping out the TAA related processes and in reviewing the 2011 Indigenous Tax Narrative, we noted that all implicated branches (TPB, CSB and Law Branch) have a good understanding of their roles and responsibilities as they pertain to the administration of Indigenous TAAs. The mapping exercise, with references to the Indigenous Tax Narrative, together with discussions with

the Tax Policy Branch (TPB), the Corporate Services Branch (CSB) and the Law Branch personnel served to produce documentation that depicts current roles and responsibilities.

23. Further, we confirmed that all personnel with *Financial Administration Act* section 33 and 34 signing authorities understand the responsibilities associated with these delegations of authorities and other personnel in Financial Management Directorate (FMD) within CSB verify that these approvals have been given before proceeding with the payment process.
24. In addition, no deficiencies were found in the financial administration of the Indigenous TAAs; none of the three sampled TAAs contravened relevant federal and other legislation. Some minor exceptions were noted in the Office of the Auditor General's (OAG) reports but the issues identified were out of the Department's control.
25. We can conclude that the Department has a governance framework in place for the Indigenous TAAs, which ensures that the agreements and remittances are managed with integrity, transparency, accountability and compliance.

## GOVERNANCE FRAMEWORK – RISK AND PRIORITIES

26. Governance, risk management, and control are interrelated. "Effective governance activities consider risk when setting strategy. Equally, risk management relies on effective governance (e.g. tone at the top, risk appetite, tolerance, and culture; and the oversight of risk management). Likewise, effective governance relies on internal controls and communications (to senior management) about the effectiveness of those controls."<sup>iv</sup> The internal audit team expected that the Department had a governance framework in place for Indigenous TAAs that is both risk-sensitive and designed to efficiently address government priorities.

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<sup>iv</sup> IIA – IPPF's Implementation Guide on Governance – Standard 2110

## Risk-sensitive

27. "Risk is defined as the possibility that an event will occur and adversely affect the achievement of objectives. Risk assessment involves a dynamic and iterative process for identifying and assessing risks to the achievement of (an organization's) objectives."<sup>v</sup>
28. The most recently approved departmental Corporate Risk Profile contains a list of corporate risks (those that affect two or more branches), which is a filtering of all of the branch risk registers. The list of corporate risks, approved by the Executive Committee included only one risk that included the Indigenous TAA processes. The risk statement is as follows "Given the significant financial implications for the affected jurisdiction(s) and counterparties...there is a risk that a failure in supporting systems and processes will impact the timely and accurate delivery of tax and transfer payments to provinces, territories and Indigenous governments, as well as public debt related transactions."
29. The Corporate Risk Management process adequately considers the Indigenous TAA processes and includes mitigating strategies for this risk.
30. Another important element to consider in the field of risk management is the identification of fraud risk. Hence, during our audit, we enquired on both preventative and detective controls<sup>vi</sup> to mitigate such risk.
31. The results from consultations with key personnel and from the Fraud Risk Questionnaire confirmed that the risk of fraud in respect to TAAs is very low and multiple mitigating controls are in place.
32. We are satisfied that the mitigating controls in place to prevent/detect fraud are adequate. Evidence of (preventative) mitigating controls indicated that:
- Both key divisions (Intergovernmental Tax Policy, Research and Evaluation Division and the Financial Management Directorate) rely heavily on the segregation of (incompatible functions) duties for fraud prevention;

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<sup>v</sup> COSO's Internal Control – Integrated Framework 2013 – Executive Summary, page 4

<sup>vi</sup> Preventative controls (such as segregation of duties) help to prevent the occurrence of fraud, while detective controls (such as management review) assist in identifying fraud if it does occur.

- Both the Director General, Intergovernmental Tax Policy, Evaluation and Research Division within the TPB, and the CFO have a mechanism to communicate with the Deputy Minister on urgent matters; and
- The Department has a strong commitment to Values and Ethics, which strengthens its governance framework.

33. Other (detective) mitigating controls found during our audit include:

- Manual matching by the Transaction Advisor, FMD of amounts and number of payments entered via the Department's IT SAP financial system with those of the Receiver General's IT SPS system.
- Supervisory review at the end of each payment processed by the Manager, Public Debt, FMD to ensure the completeness and accuracy of payments to the Indigenous groups.
- Indigenous groups receive estimation booklets prior to receipt of remittances and know the amounts to be remitted.

### Government Priorities

34. The government's priorities, as stated in the Minister's mandate letter November 2015, are also the Department's priorities, and include "Work(ing) with the Minister of Indigenous and Northern Affairs to establish a new fiscal relationship that lifts the 2% cap on annual funding increases and move towards sufficient, predictable and sustained funding for First Nations communities." Other references to the Department's priorities/objectives, found in its Departmental Plans 2014–2015 through 2018–2019, include "Work(ing) with other government departments to support reconciliation with Indigenous peoples including establishment of a new fiscal relationship with Indigenous governments."<sup>vii</sup>

35. We did not find any deficiencies or concerns regarding the relationship with Indigenous governments nor the timeliness of the tax remittances to the Indigenous groups.

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<sup>vii</sup> Departmental Plan 2018–19, page 6 – Planned Results: what we want to achieve this year and beyond – Core Responsibilities – Economic and Fiscal Policy

36. Throughout our consultations with different departmental stakeholders, it was confirmed that no complaints were received from Indigenous groups in respect to the administration of Indigenous TAAs.
37. Furthermore, we compared the timeliness of the payments to the Indigenous groups with the timing if CRA had paid the groups directly. The timing was virtually the same as the Department of Finance pays the groups and CRA reimburses the Department the following month. Therefore, the effect is the same as if CRA had paid the groups directly.
38. Overall, the governance framework in place for Indigenous TAAs is risk-sensitive and designed to efficiently address government priorities.

## CONCLUSION

39. The governance framework for Indigenous Tax Administration Agreements (TAAs) is well established and effective.

## **ANNEX A: AUDIT CRITERIA**

The following audit criteria were used in the conduct of this audit:

- Criterion 1: whether the governance framework in place for Indigenous Tax Administration Agreements (TAAs) ensures that the agreements and remittances are managed with integrity, transparency, accountability and compliance with laws and regulations; and,
- Criterion 2: whether the governance framework in place for Indigenous TAAs is risk-sensitive and designed to efficiently address government priorities.

## ANNEX B: ACRONYMS

Acronym	Name in Full
CFO	Chief Financial Officer
CRA	Canada Revenue Agency
CSB	Corporate Services Branch
FMD	Financial Management Directorate
GST	Goods and Services Tax
IT	Information Technology
OAG	Office of the Auditor General
TAA	Tax Administration Agreement
TPB	Tax Policy Branch