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**Management and Financial Audit
of Selected Programs in the Information Highways
Application Branch (IHAB)**

Prepared for the Audit and Evaluation Branch by

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Canada

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1.0 EXECUTIVE SUMMARY

Background

This audit was undertaken at the request of senior management. Hallux Consulting Inc. was contracted to undertake the work on behalf of the Audit and Evaluation Branch (AEB) with most of the fieldwork conducted between March and May 2000.

The objectives of the audit were to determine:

- if management has reasonable assurance that programs are well managed and are being implemented in a timely manner;
- if proper financial planning controls exist for the management of the programs; and
- if management has the necessary tools to ensure that Programs being delivered by third parties (in particular with Alternative Service Delivery (ASD) arrangements) are implemented effectively.

The audit focused on four programs (Community Access Program, Learnware, NetCorps and VolNet) within the Information Highways Applications Branch (IHAB). These four programs utilize grants and contributions extensively as part of program delivery. They deal with relatively small amounts directed to non-profit, community and education groups that in turn leverage additional funds and provide public services essential to the national and international success of IHAB programs. Consideration was also given to the contracting practices within the Branch during the period 1995-2000.

Key Findings

IHAB's contribution programs demonstrate many of the attributes of a well-managed program as identified by Industry Canada's Practices for Grants and Contributions¹ and the Office of the Auditor General². Staff are enthusiastic about their work and are working actively with program participants to find solutions and to make necessary adjustments to the program.

Nevertheless, comptrollership gaps were identified during the audit that offer opportunities to improve overall program management:

- ***Funds claimed by recipients in advance of need and based on budget***
A total of \$1.3M of \$36M paid during 1998-1999 and 1999-2000 was paid according to the budget rather than actual activity levels.
- ***Funds were not always consistently administered in accordance with terms and conditions set for contribution programs.*** CAP and VolNet programs are currently being administered more in line with a grants program.
- ***Inadequate adherence to requirements stipulated in government policy:***

¹ As set out in *Grants and Contributions at Industry Canada - Management Practices*, March 2000.

² As defined in *A Risk Assessment Framework for Grant and Contribution Programs*, Discussion Draft, March 7, 2000 prepared by the Office of the Auditor general in collaboration with Industry Canada.

While there is no evidence of fraud or personal benefit associated with existing practices, there were several examples of variance from Treasury Board policy noted during the audit. Specifically:

- In terms of the *application of contracting requirements*, contracts examined did not always identify clear deliverables and there were cases identified that could easily infer an employee-employer relationship;
- With respect to the *management of financial requirements*, staff in CAP and VolNet focused more on whether claimed costs were within budget, rather than on whether they met the definition of eligible cost.
- In terms of the *allocation of expenditures to a fiscal year*, auditors found examples of advance payments in one fiscal year which related to program activity in a subsequent fiscal year (VolNet, CAP)
- *When working with Alternative Service Delivery (ASD) partners, payment and monitoring activities were inconsistent with government policy.* Several instances were identified where payments were made for costs not clearly defined as eligible, and where insufficient consideration was given to the extent to which program targets were met.

Several key factors contributed to these practices. Within IHAB there is a strong focus on achieving published targets without giving adequate attention to Treasury Board and departmental financial management requirements. As well, staff do not clearly understand all administrative requirements associated with contribution programs. Finally, insufficient resources were allocated to IHAB's salary envelope, leading to an excessive use of contractors who are not as knowledgeable of government financial management policies and practices.

CONCLUSION

Based on the audit work undertaken, we have concluded that:

- IHAB management was so focused on the attainment of the established performance targets, that they gave inadequate attention to their comptrollership responsibilities;
- While staff worked diligently to implement programs in a timely manner, the evolving nature of the program and the time required to forge the necessary partnerships with other organizations resulted in IHAB being unable to implement the program within the established timeframes and according to departmental standards;
- While proper financial planning controls exist within Industry Canada for the management of programs, these were not adequately followed by IHAB; and
- IHAB did not use the necessary range of tools and mechanisms to adequately ensure that its programs, delivered by third parties, were being implemented effectively.

Industry Canada accepts the findings, conclusions and recommendations of the audit report, and has developed an action plan to reinforce management accountability and practices through control measures, training, monitoring, reporting, and further review and audit scrutiny.

2.0 INTRODUCTION

In 1997, the Canadian government committed itself to making information and knowledge infrastructure accessible to all Canadians by year 2000, thereby making Canada the most connected nation in the world. This commitment has been reiterated on numerous occasions since that time including in the October 1999 Speech from the Throne. Industry Canada, through the Information Highway Applications Branch (IHAB) in particular, has been at the forefront in striving to ensure that the government achieves objectives set out in the government's Connectedness Agenda.

Several programs have been launched by IHAB in this regard:

- **SchoolNet.** Under this program, Industry Canada is working to increase the level of and extent of connectivity within Canadian schools including First Nations schools and libraries.
- **Community Access Program (CAP).** The primary objective of this program is to create universal public access to the Internet by establishing public access points in remote, rural and disadvantaged urban communities.
- **Computers for Schools.** Under this program, used computer equipment is refurbished as required and is then donated to schools, libraries and not-for-profit organizations.
- **Learnware.** Key objectives of this program include stimulating the growth and development of Canada's new media learning and Internet applications industries, populating Canada's Information Highway with high-quality Canadian Learnware and public access applications, and improving access to the Internet for schools, libraries, community access centres and volunteer organizations.
- **VolNet.** This program is targeted specifically at the voluntary, not-for-profit sector. The objective of the program is to provide access to computer equipment, the Internet, new information technologies, network supports and training.
- **NetCorps International.** Under this program, information technology graduates are sent to third world nations to assist them in increasing their connectivity.
- **Francophone Intranet.** This program is to serve Francophone communities throughout Canada, especially those outside Québec.
- **Canada's Digital Collections.** Through this program, Canadians 15 to 30 years of age are provided with entrepreneurial and technology-based job experience by converting collections of significant Canadian material into digital form for display on the Internet.
- **Information Highway Science & Entrepreneurship Camps.** Under this program, funding is provided to organizations which run camps for young people focused on science, engineering and technology-related fields.

Senior management requested that the Audit and Evaluation Branch (AEB) conduct an audit of the management of these programs with a particular emphasis on financial management practices. Hallux Consulting Inc. was contracted to conduct this audit on behalf of the AEB.

MANAGEMENT AND FINANCIAL AUDIT OF SELECTED PROGRAMS IN THE IHAB PROGRAM

3.0 OBJECTIVES OF THE AUDIT

The objectives of this audit were to determine:

- if management has reasonable assurance that programs are well managed and are being implemented in a timely manner;
- if proper financial planning controls exist for the management of the programs; and
- if management has the necessary tools to ensure that Programs being delivered by third parties (in particular with ASD arrangements), are implemented effectively.

4.0 SCOPE AND METHODOLOGY

The audit focused on those programs with a significant grants and contributions component to program funding. Programs included:

- Community Access Program;
- Learnware;
- NetCorps; and
- VolNet.

The grants and contributions components of these four programs during the past two fiscal years (1998-1999 and 1999-2000) was almost 90% of the total \$36 million spent by IHAB³. Within these programs thirty-seven contribution agreements were selected for review. Site visits were also made to twenty-five organizations receiving contribution payments either directly or through an Industry Canada service delivery partner.

The practices used for handling initial program enquiries, processing applications, assessing projects, arriving at a recommendation for funding, the establishment of a contribution agreement, the administration of the agreement and the monitoring of projects were evaluated against both internal and external criteria. Internal requirements for administering grants and contributions are contained in the Program Policies Manual and Program Procedures Manual, as supplemented by Programs and Services Board decisions which are circulated to Responsibility Centres. These are also set out in *Grants and Contributions at Industry Canada—Management Practices*, March 2000. The practices employed by IHAB were also compared to those defined by the Office of the Auditor General in collaboration with Industry Canada in *A Risk Assessment Framework for Grant and Contribution Programs*, Discussion Draft, March 7, 2000.

As part of the audit, a sample of contracts over the period 1995-2000 for all programs within IHAB including the four listed above, was examined. During this period, 11,836 contracts were issued by IHAB with a total value of \$157,323,823. Using judgmental sampling techniques, 413 contracts with a value of \$79,459,486 were selected for review. The practices used in awarding and administering these contracts were compared with the requirements as set out in Treasury Board Secretariat's *Contracting Policy*.

The audit also compared the observed management control framework within IHAB and its programs with a framework developed by Robert Anthony, John Dearden and Vijay Govindarajan in *Management Control Systems* (see Annex 1 for a brief description of the elements of this management control framework).

Most of the fieldwork related to this audit was conducted between March and May 2000.

³ See Annex 4 for a breakdown of the contribution expenditures by program for the period 1998-1999 and 1999-2000. While the actual payments made under the Learnware program during this period were relatively low, at the time the audit sample was selected the budget was over \$10 million. Much of this was reprofiled to 2000-2001.

5.0 FINDINGS

IHAB's contribution programs demonstrate many of the attributes of a well managed program as identified by Industry Canada's Practices for Grants and Contributions and the Office of the Auditor General. Comptrollership gaps were identified in the areas of program and financial management.

5.1 Overall Management of Programs

IHAB's practices for managing contribution programs were compared with attributes outlined in the Department's Management Practices for Grants and Contributions, and with those established by the Office of the Auditor General. This comparison (see Annex 2 and 3 respectively) shows that IHAB has adopted many of the practices identified for well-managed organizations. These practices include the following:

- An explanation of how recipients are expected to benefit from funding is prepared for all contribution programs and is included in the summary prepared for Industry Canada's Programs and Services Board. The report that goes to the Board must also provide a linkage of the specific project to overall program objectives.
- Detailed eligibility criteria have been established for all programs. The actual determination of eligibility is generally made by third parties on behalf of Industry Canada.
- A wide range of approaches is used to advise potential applicants of the programs.
- Potential projects are often reviewed in batches so that the most suitable projects receive funding.
- Signed agreements are in place between Industry Canada and recipients. Agreements clearly describe respective responsibilities.
- Programs are readjusted when results are not consistent with initial expectations.
- Management reporting is very focused on the achievement of results (i.e., total money spent to date, number of organizations connected, number of young people signed up, etc.).

There are several areas, however, where performance is not at the level identified for well-managed programs. Areas for improvement are as follows:

- Program officers improving confirmation that all funds claimed by program recipients are used for eligible purposes: Approximately \$1.3 million of the \$36 million paid in contributions during the 1998-99 and 1999-2000 fiscal years, had not been used during the reporting period strictly as originally intended. Payments corresponded with the original budgets rather than actual activity levels as set out in the contribution agreements.
- The extent to which contribution programs are managed more like grants programs: In two of the four programs examined (CAP and VolNet), funds to recipients were administered in a manner more consistent with a grants program, rather than according to the agreed to terms and conditions of the contribution program.

Although staff are working hard to achieve the established program targets, several factors have made the attainment of these targets a challenge.

It is clear from our discussions with program managers that they are very focused on the targets that have been set for their programs and are doing their best to ensure that they will be achieved within the established timeframes. Staff are enthusiastic about their work. Audit team members observed staff actively working with program participants to find solutions to issues that inevitably arise with new programs.

When one approach did not work as quickly as hoped, staff adjusted the program delivery approach so that overall program targets could still be achieved within overall timeframes. For example, many programs are being delivered in conjunction with provincial government departments. In some provinces, however, agreements could not be struck. In these provinces, for programs such as CAP and Computers for Schools, partnerships for program delivery have been struck instead with regional or municipal economic development organizations or other third parties.

Regular reports are provided to senior management within IHAB on the status of program achievements in comparison to original targets. Targets have typically been established in terms of the number of connections, number of young people placed, etc.

Notwithstanding these efforts, program implementation for programs examined in the course of this audit has not proceeded as quickly as initially anticipated. The first projects within Learnware were just starting in the last quarter of the 1999-2000 fiscal year, a year after the program was first announced. This necessitated re-profiling most of the funding for the program to the 2000-2001 fiscal year and beyond. A significant amount of funding for CAP lapsed and/or was re-profiled over the past two fiscal years due to difficulties in reaching agreements with several provinces. The number of connections in place and computers shipped under the VolNet program is running at approximately 70% of initial targets. The level of activity in NetCorps is running slightly behind schedule. The first half of the 1999-2000 fiscal year was spent putting the necessary infrastructure in place within IHAB and its delivery partner, thus delaying efforts to identify young people to act as interns in other countries.

IHAB management has not adopted several elements of the department's management control framework because these were seen to be impeding achievement of targeted results within the originally established timeframes. In comparison to the general model outlined in Annex 1, the following elements were identified:

- **External Environment:** In large measure, all of IHAB's contribution programs are delivered through partnerships with other organizations, many of which are not-for-profit organizations or other levels of government. This is consistent with the government's stated objective of program delivery through partnerships, as well as with the general recognition within the public sector that various levels of government must work together to address the complex issues facing Canadians.

IHAB's ability to control these parties, however, is limited. All partners to the agreement are committing resources and thus want the ability to influence the overall direction. For some programs, Industry Canada's contribution is as low as 20% of the total necessary resources. In such an environment, all parties must be convinced of the likelihood of overall objectives being achieved. A considerable amount of time is often required before consensus can be achieved amongst all the partners. Planning cycles and timelines can also be quite different for each of the partners in a particular program. All of these factors can have a significant impact on the timelines necessary to implement a program.

- **Organizational Structure:** Over 200 individuals currently work within IHAB⁴. The salary budget for the 1999-2000 fiscal year, including that for students, was approximately \$6.7 million. For the 1998-99 fiscal year, it was almost \$8 million. Base funding for the Branch covers the salary for only 39 full-time indeterminate positions.

Developing partnerships and administering a range of contribution programs can be extremely labour intensive. The funding envelope provided for salaries is insufficient for the number of resources required. The relatively short duration of the funded programs (typically 3-4 years maximum at a time), has also led to the use of a large number of secondments and term employees. These employees tend to move on to other opportunities where the funding is more stable. The high degree of turnover due to the level of secondments, term employees and contract resources results in a greater potential for corporate memory loss and difficulties ensuring continuity with potential partners.

- **Rules, Factors and Influences:** IHAB is delivering its services within a very dynamic environment. One key policy objective is to ensure that all Canadians become connected. It has specifically targeted its programs to the disadvantaged who potentially could be irreparably left behind. Computers and web-based technology have had the fastest penetration rate of any technology ever developed. Forty-seven days for an Internet-based company is deemed to be equivalent to a year for an "old-economy" company.

In such an environment, an organization requires considerable flexibility to adjust quickly, and to bring on board the resources it requires in a timely manner. As noted in the Auditor General of Canada's April 2000 report to Parliament⁵, the public service staffing system is rule-bound and inefficient. Staffing for a new position that needs to be classified, which is the norm for an organization such as IHAB, takes (on average) 230 calendar days. Such delays in getting positions classified and filled can seriously impede IHAB's ability to get a program up and running in a timely manner.

⁴This figure is based on the Industry Canada Telephone Directory available on the World Wide Web as of May 1st, 2000.

⁵2000 Report of the Auditor General of Canada-Chapter 9, *Streamlining the Human Resource Management Regime: A Study of Changing Roles and Responsibilities*.

5.2 Financial Planning Controls

At the individual transaction level, results achievement were considered most important.

In most programs examined, at the individual transaction level, the audit team found variations from government policy. There was no evidence of fraud or personal benefit associated with these practices. Rather, staff appeared to be motivated by a desire to achieve program objectives within the required timeframes, leading to the observed shortcuts.

Specific examples of variance from Treasury Board policy were found in the following areas:

- ***Application of Contracting Requirements:*** Government contracting is to “be conducted in a manner that will stand the test of public scrutiny in matters of prudence and probity, facilitate access, encourage competition, and reflect fairness in the spending of public funds.”⁶ A review of contracting indicated an extensive use of sole-source contracts and Advance Contract Award Notices (ACAN). Rarely were contracts under \$25,000 subject to a competitive process, notwithstanding Treasury Board policy direction to use such a process whenever it is cost effective to do so. Several of these contracts were subsequently amended to up to \$100,000. In one case, the ACAN listed skills that were not included in the résumé of the individual awarded the contract.

Contracts were not always structured to identify clear deliverables against which to report progress and make payments. In one case, consultants were engaged on a verbal go-ahead and when the invoice for the work was submitted, no written contract was found to be in place.

Furthermore, the *Contracting Policy* requires that contracting authorities ensure that an employer-employee relationship will not result when contracting for the services of individuals. As well, the use of temporary help services is to be confined to those situations not exceeding 20 weeks, and for which it is not feasible to assign public services. In our review of contracts over the period 1995 to 2000, more than ten instances were identified where individuals had one contract after another, the longest of which covers almost five years. The nature of the duties and the time commitment to IHAB was such that one could easily infer an employer-employee relationship.

- ***Management of the Financial Requirements of Contribution Programs:*** All of the contribution agreements that Industry Canada has entered into in the course of delivering the programs IHAB is responsible for have very clearly defined terms and conditions. IHAB's partners are expected to commit certain resources to the endeavour and the targets to be

⁶ Treasury Board Secretariat, *Contracting Policy*

⁷ Paragraph 10.2.3 of the *Contracting Policy* states: “Exception (b) sets specific dollar limits [\$25,000] below which a contracting authority may set aside the competitive process. However, contracting authorities are expected to call for bids whenever it is cost effective to do so. When the proposed contract is estimated to exceed the dollar limits, the contracting authority is to call for bids.”

achieved are set out. All of the agreements describe the allowable costs for which recipients may be reimbursed.

The audit team found that with two programs (CAP and VolNet), program staff focused more on whether the claimed costs were within the identified budget, rather than whether they meet the definition of specific costs. A heavy reliance was placed on the recipients to identify eligible costs without follow-up or spot checks by program staff. Several VolNet recipients claimed exactly what was budgeted, even though actual costs were more or less than costs outlined in budgets. As a result of preliminary findings from this audit, NetCorps program staff have already taken steps to institute spot checks of the financial records of program recipients. Some program participants had excellent financial records and were able to easily identify their allowable costs. Others need to enhance their own processes to meet Industry Canada's requirements.

- ***Allocation of Expenditures to a Fiscal Year:*** Government policy¹ requires that only under exceptional circumstances should advance payments for expenditures eligible for reimbursement under a contribution agreement likely to be incurred in the next fiscal year, be charged to a previous fiscal year. When this is done, it is not to exceed the expenditures expected to be incurred by the recipient during April of the following year. In the administration of contracts for goods and services, costs are to be allocated to the year in which the goods or services are received. Progress payments are to be made upon the completion of defined milestones. Examples in variance with these policies were found both in the administration of the contribution agreements and in the administration of contracts for goods and services:
 - Under the VolNet program, a payment was made in late March 1999, in order to have 2,400 computers set aside and reserved for delivery early in the next fiscal year. The first of these 2,400 machines was shipped in July 1999, and the last in March 2000. Additional payments during the 1999-2000 fiscal year were sufficient to cover demand, based on previous experience, for five months into the next fiscal year.
 - During the fourth quarter of the 1999-2000 fiscal year a commitment was established with another federal department in anticipation of signing an agreement for work to be carried out during the 2000-2001 fiscal year. The funds were to go into a suspense account to be drawn down upon as required. Any funds not expended by March 31, 2001 were to be returned to IHAB in April 2001. The commitment was cancelled when the other government department declined to sign the proposed agreement.
 - A large number of contracts associated with the CAP program were issued at the end of the 1999-2000 fiscal year showing that 80% of the associated work would be completed within a few days. The balance was to be completed before the end of the following fiscal year. Concerns with these contracts in the Comptrollers Branch resulted in few payments being issued.

¹Treasury Board Secretariat Policy on Comptrollership, Chapter 2-12, *Policy on Transfer Payments*, issued October 15, 1996. The new *Policy on Transfer Payments* issued June 1, 2000 has a similar requirement.

Several factors have contributed to practices being inconsistent with Treasury Board and departmental requirements for financial and program management. These factors include the following:

- **Organizational Structure:** As noted earlier, there are a large number of contract resources in IHAB. Contractors are much less likely to be aware of the government policy requirements associated with contracting and the delivery of government programs, in particular contribution programs thus contributing to the practices observed by the audit team. On the other hand, such individuals, because of their lack of familiarity with government norms in delivering these types of programs, may be better able to identify alternative methods to achieving the desired program objectives when initial approaches prove insufficient.
- **Rules, Factors and Influences:** The environment within which IHAB is delivering programs is constantly changing. In addition, all programs are new and results are difficult to predict, especially in the short term.

In such an environment, detailed long term planning (more than a few months in advance) can be problematic. Events are unlikely to unfold in a predictable manner. Any number of events such as potential partners taking longer than anticipated to arrive at a decision, or delays in the approval process at all levels with respect to program design, can have a significant impact on planned program timelines.

Federal government planning processes generally have a relatively long lead-time. The resource allocation process typically starts in the September prior to the next fiscal year. Other than to reduce overall requirements, it is difficult to make substantive changes once initial projections have been provided.

For most program delivery, these types of processes are adequate. For IHAB they have proven to be constraints. Staff have taken actions to ensure that program objectives continued to be advanced while, at the same time, minimizing the amount of funds that would lapse and would therefore be unavailable to them over the life of the program.

- **Culture and Climate:** The staff and management within IHAB are very enthusiastic about their work and the results of these programs. Throughout this audit, audit team members observed a "can do" attitude on the part of managers and staff. Many commented, however, about the volume of work and the lack of time to verify certain things. Time is considered to be at a premium. They feel they do not have the time to stop and confirm the requirements of the government policy framework as it applies to contracting and administering contribution agreements. The high number of contractors acting as program officers, as noted earlier, with the resulting high level of turnover, exacerbates this problem.

5.3 Program Implementation by Alternate Service Delivery Parties

Management is focused on how well ASD partners are assisting in the overall achievement of program objectives. Insufficient attention is being given to whether implementation activities are conducted in a manner consistent with the government's management framework, and the terms and conditions of agreements.

IHAB management appears to be primarily interested in seeing marked progress towards established targets with partners, rather than with ensuring that each partner fulfills specific contractual obligations. Monitoring of partners is very limited. Insufficient information is currently required by the CAP and VolNet programs to adequately support claims under the contribution agreements. As a result, program officers are unable to make an informed judgment as to whether ASD partners have carried out their responsibilities in a manner consistent with the terms and conditions of the agreements.

Several instances were identified where payments were made for costs not clearly defined as eligible by the contribution agreement:

- Payments to one CAP partner were \$646,000 more than Industry Canada's share of the eligible costs in 1998/99, and \$35,200 more than Industry Canada's share in 1999/00. Payments in 1998/99 matched the annual maximum set out in the contribution agreement. Based on direction from IHAB, a second invoice in 1999/00 that would have matched payments with the maximum set out in the agreement was not submitted by the CAP partner as originally planned.

In each year, the number of sites eligible for financial support was less than the target for the period. It is understood that verbal agreements at the working level that were never formalized and approved by both parties, permitted more flexibility in how the funds could be used and what was deemed acceptable as matching funds.

- One VolNet partner, whose records were examined as part of the audit, had been reimbursed for some inadmissible costs. Discussions have been initiated between the VolNet partner and IHAB to recover these costs.
- Within NetCorps, one coalition member had inadequate documentation to substantiate expenditures claimed.

Other instances were noted of payments being made to ASD partners where insufficient consideration appears to have been given to the extent to which the program targets were reached:

- Payments to one partner under the CAP Youth Program exceeded costs incurred by more than \$100,000 in 1998/99. Payments were approximately \$40,000 more than actually expended in 1999/00. Furthermore, the required hours provided were only about 75% of the target and the average time per youth was significantly less than it was supposed to be. The payments matched rather the annual maximums set out in the agreement.

- One CAP partner received over \$16,000 to establish two sites in different municipalities. Only one machine was subsequently installed at each location. In both cases availability to the public was not advertised as required. No documentation detailing the agreement could be found in IHAB's files.
- In the first round of the VolNet program (which was completed in March 2000) the number of connections achieved was approximately 70% of the original targets. While some payments to voluntary organizations were adjusted to reflect lower expectations, the reductions were not proportionate to the actual number of connections in comparison to the original target.

Not all of the agreements entered into for the programs examined as part of this audit had provisions for adjusting payments if planned targets were not achieved. Generally, each partner was to be reimbursed for all of the eligible costs incurred up to a ceiling amount without direct reference to attaining specific targets.

In both the CAP and VolNet programs, examples were found where expected results had been overestimated in internal IHAB management reports although no instances of this were found in external reporting. CAP figures included sites for which payment had been made to the partner but sites had not yet been established. Several different errors were found in the reported VolNet connection figures. Instances were found where the reported number of connections as a result of the VolNet program included: connections that were expected to happen several months after the contribution agreement ended; organizations that already had an Internet connection at the outset but participated in the training; and projected figures rather than actuals.

The key elements of the management control framework that contributed to these findings were as follows:

- **Rules, factors and influences:** As noted earlier, staff took whatever action they felt they could to ensure that program objectives continued to be advanced while, at the same time, optimizing the utilization of approved resources.
- **Culture and climate.** Managers and staff within IHAB have a "can do" attitude. There is an understanding that one must be flexible when dealing with partners if one wishes to have a long-term relationship. Partners, especially those in the not-for-profit sector, need to believe that they will not be out-of-pocket as a result of participating in the delivery of a federal government program.

There is also considerable pressure on staff to demonstrate that they are making progress towards the targets. With limited time and resources, they focused on actions that would help them achieve targets, and spent minimal time confirming that all delivery partners carried out obligations to the fullest.

6.0 CONCLUSIONS

IHAB's contribution programs demonstrate many of the attributes of a well-managed program as defined by Industry Canada management practices and the Office of the Auditor General. While delays have occurred in program implementation, they are due in large measure to challenges inherent in working extensively with third parties and the growing pains associated with any new and evolving program.

There are, however, opportunities for improvement in IHAB's financial and program management practices both in terms of contribution programs and contracting practices. Specific opportunities for change include:

- ***Ensuring a better alignment between the applicable management framework and the environment within which IHAB is trying to deliver its program.*** IHAB is trying to deliver a new and evolving program within tight timeframes. IHAB has broken new ground within Industry Canada in terms of the manner in which successful partnerships have been forged with a range of not-for-profit and voluntary organizations.

The government recognizes that it needs to modernize the structures of government so that it will have an administration ready to meet the challenges of the twenty-first century⁹. As noted by the Auditor General in his April 2000 report, however, this is not easily achieved. Legislation, jurisprudence and years of parliamentary practice have all shaped the management framework within which programs are currently delivered.

- ***Ensuring improved recognition of the human resource requirements associated with delivering the range of programs IHAB utilized to achieve its targets:*** When the Program was designed, insufficient resources were allocated to the salary envelope. In direct response to this, management has used available operating funds and has hired a significant number of contract resources. To ensure continuity in program delivery, and to benefit from the knowledge that these individuals have developed, several contractors have had a series of contracts within the Branch and have carried out roles similar to that of government employees.

The program could not have been delivered without relying on a significant level of contract resources. However, there are a number of risks associated with using contract resources in this manner. Such resources are less likely to be aware of government policy requirements for contracting and for delivering contribution programs. Training needs to be provided to overcome this lack of knowledge. This was precluded from happening due to intense time pressures and the overall shortage of human resources. Turnover amongst these resources is also likely to be significantly higher than amongst indeterminate employees.

⁹ *Getting Government Right. Governing for Canadians*, February 20, 1997.

It should be noted that the recently strengthened Treasury Board *Policy on Transfer Payments*¹⁰ requires that departments ensure that a "capacity exists to effectively deliver and administer the transfer payment programs including monitoring, learning and training". The implementation of this new policy by Industry Canada will serve to address several of the issues identified by this audit.

- ***Ensuring a better understanding of the strengths and limitations of grants versus contributions programs, and the program structures required to successfully implement each of them:*** Grants and contributions are valuable tools used by the government to further approved federal government policy and program objectives. Both are considered to be transfer payments and, when provided to non-commercial enterprises, are not expected to be repaid. However, there are significant differences in how each type of program is administered. Grants are not subject to audit to verify that the funds were spent exactly as stipulated in the agreement but eligibility and entitlement may be verified. Contributions are provided to individuals and organizations for specific purposes pursuant to a written agreement and are subject to audit.

A grant program requires less infrastructure to administer but does not provide the same degree of accountability. On the other hand, a contribution program is much more expensive to administer. Before each payment is authorized, program staff must be satisfied that amounts being requested are consistent with the terms and conditions of the contribution agreement.

Industry Canada chose to employ contribution programs for the transfer payments administered by IHAB, but the human resources allocated to support the program were not commensurate with what was required. Government policy "to manage transfer payments in a manner sensitive to risks, complexity, accountability for results and economical use of resources"¹¹ needs to be kept in mind at the outset when designing any program involving grants and/or contributions and deciding which of the two funding mechanisms will prove optimal.

- ***Greater recognition by staff at all levels within IHAB of their comptrollership responsibilities.*** In recent years, the government has placed increasing emphasis on managing for results rather than on the resource inputs, activities and the outputs. At the same time it has made it clear that all managers have comptrollership responsibilities so that the necessary levels of control and accountability for the management of public funds can be achieved.¹¹

IHAB has focused very heavily on the attainment of the targets set for the program at the expense of comptrollership responsibilities. A better balance between achieving results and respecting comptrollership responsibilities is required before IHAB will have a management framework consistent with that which has been set out by the government in *Results for Canadians: A Management Framework for the Government of Canada*.

¹⁰ Treasury Board of Canada Secretariat, *Policy on Transfer Payments*, June 1, 2000.

¹¹ See the *Report of the Independent Review Panel on Modernization of Comptrollership in the Government of Canada*, October 1997.

In light of the above, we have concluded that:

- IHAB management was so focused on the attainment of the established performance targets, that they gave inadequate attention to their comptrollership responsibilities;
- While staff worked diligently to implement programs in a timely manner, the evolving nature of the program and the time required to forge the necessary partnerships with other organizations resulted in IHAB being unable to implement the program within the established timeframes and according to departmental standards;
- While proper financial planning controls exist within Industry Canada for the management of programs, these were not adequately followed by IHAB; and
- IHAB did not use the necessary range of tools and mechanisms to adequately ensure that its programs, delivered by third parties, were being implemented effectively.

7.0 RECOMMENDATIONS

Based on the opportunities for improvement identified for IHAB's financial and program management practices, the following recommendations are put forward for consideration:

- The ADM, SITT and the Director General, IHAB should ensure that an accountability structure, in the context of modern comptrollership, is put in place to ensure that all staff comply with the government's financial management policies and practices.
- The Director General, IHAB, should submit a proposal to the Programs and Services Board, who would in turn provide advice to the Minister, on whether IHAB programs be delivered utilizing grants or contributions, recognizing fully the risks and limitations of both, and should seek to obtain the human resources commensurate with the option chosen.
- The Director General, IHAB should ensure that all staff and contract resources administering contracts and/or contribution agreements, are familiar with and follow the applicable government policy.
- The Director General, IHAB should ensure that an adequate monitoring system is in place for all IHAB programs.
- The Director General, IHAB should ensure that partners delivering a program on behalf of Industry Canada are well informed of the financial management framework required for managing the program.

8.0 ACTION PLAN

Management Response - General Comments

Industry Canada accepts the findings, conclusions and recommendations of the audit report, and has developed an action plan to reinforce management accountability and practices through control measures, training, monitoring, reporting, and further review and audit scrutiny.

Notwithstanding the positive program outcomes of IHAB, the audit results indicate instances where the department's standards for financial and program management have not been met. The audit found that IHAB's contribution programs demonstrate many of the attributes of a well-managed program as identified by Industry Canada's Practices for Grants and Contributions and the Office of the Auditor General; nevertheless, comptrollership gaps were identified that offer opportunities to improve overall program management. These comptrollership gaps will be addressed in the following action plan as an omnibus response to the recommendations made in the audit report.

Industry Canada values highly the essential role that the internal audit function plays in ensuring that the highest levels of modern comptrollership are met in the department's financial and program management practices.

Action Plan

immediate actions:

1. All managers and staff will be reminded of their responsibility and accountability under the Financial Administration Act and the Treasury Board policy on transfer payments.

Financial, contracting and program authority will be temporarily removed from all managers and administrators in the Community Access Program (CAP) and the VolNet Program. Signing authority will be reinstated upon completion of the Contracting and Financial Signing Authorities courses provided by the Comptroller's Branch as well as the Program Delivery course provided by the Program Services Branch. The department will deliver this training to the appropriate staff in CAP and VolNet before the end of October 2000. All other IHAB managers, program officers, and administrators will also participate in this training within a reasonable time frame.

In the interim, the Assistant Deputy Minister, Spectrum, Information Technologies and Telecommunications (SITT) will exercise the required authorities with respect to CAP and VolNet.

In recognition of the progress made in improving their financial and program management practices over the past year, signing authority will be retained for the NetCorps and Learnware programs, as the most serious comptrollership gaps found in the audit did not occur in these programs.

2. The Department will initiate a measured review from a legal perspective of IHAB projects, agreements and contracts. A status report will be presented to the Departmental Audit and Evaluation Committee (DAEC) by January 2001.
3. IHAB will review all payments against claims, identify any overpayments or reimbursements of ineligible costs, and provide the results of the review and an action plan to the Program and Services Board (PSB) by December 2000.
4. IHAB will seek the sign-off of Industry Canada Legal Services on all IHAB agreements and contracts over \$5,000 before they are signed by program managers. This arrangement will be reviewed in July 2001.
5. All IHAB directors will engage in early consultation with Industry Canada Legal Services and the Comptroller's Branch on proposed projects and contracts before any verbal or written commitments are made to third parties, and to ensure full compliance with policies, guidelines and legal requirements as these agreement and contract projects are developed.
6. The Director General, Audit and Evaluation Branch will initiate an internal audit of a sample of IHAB pilot projects, not covered by the scope of this audit, to be completed within 60 days.
7. The hold-back percentage for all IHAB programs will be 10%, as a minimum, in accordance with conventional departmental practice. This offers the Department some protection if any overpayments are made.
8. IHAB will complete as soon as possible, the staffing of a financial officer (F1-3) and a contracting officer (PG-3) in order to provide expert, objective advice and support to IHAB managers in exercising their responsibilities. These officers will, as an interim measure, report to the Comptroller's Branch. This reporting arrangement will be reviewed in July 2001.

medium-term actions:

9. IHAB will review their organizational design and present a report to the PSB by November 2000. The report will deal with issues such as whether an appropriate level of resources have been allocated to the salary budget, and whether the staff complement model ensures the necessary competencies are present. The PSB will review the report and make recommendations to the DAEC.
10. IHAB will prepare an assessment of whether it is using the appropriate instrument (grant, contribution, or contract) to deliver its programs, and present their findings to the PSB by December 2000. The PSB will review the report and provide advice to the Deputy Minister on this issue.

11. IHAB will establish a monitoring plan which complies with the requirements of the Treasury Board Policy on Transfer Payments. The monitoring plan will be presented for approval by PSB in December 2000.

longer-term action:

12. A follow-up compliance audit of IHAB programs will be undertaken, with a final report due by September 2001. In the interim, IHAB will provide written assurance, on a quarterly basis, to the Assistant Deputy Minister JTT, that its programs are being appropriately managed and that funds are being disbursed prudently and in accordance with the programs' terms and conditions and all applicable legal and policy requirements.

ANNEX 1: KEY ELEMENTS OF A GENERAL MANAGEMENT CONTROL FRAMEWORK

Seven key elements of a general Management Control Framework¹² (MCF) are:

- **External factors.** This first element of the MCF asks overall how does the organization sense and react to its environment and what has been done to manage this environment.
- **Organizational structure.** This element of the MCF considers how authority and responsibilities are aligned and how decisions are made.
- **Rules, factors and influences.** This element asks what is the overriding policy framework and does it support the intended results.
- **Culture and climate.** This element of the MCF looks at the values and norms of the organization and asks if it is consistent and supports intended results.
- **Planning.** This element looks for gaps and appropriate linkages between strategic planning, annual planning and the revision process.
- **Execution.** This element reviews the mechanisms used to ensure the effective implementation of operational activities.
- **Evaluation.** This final element considers how performance is evaluated, as well as the quality of this information and what is done with it.

¹² Adapted from Anthony, Robert, John Dearden and Vijay Govindarajan, 1965. *Management Control Systems*, Boston, Irwin Press

ANNEX 2: IHAB'S ADMINISTRATION OF CONTRIBUTION PROGRAMS IN COMPARISON TO MANAGEMENT PRACTICES FOR GRANTS AND CONTRIBUTIONS AT INDUSTRY CANADA¹³

Attribute	IHAB's Administration of its Contribution Programs
<ul style="list-style-type: none"> • Initial Enquiry (Optional) <ul style="list-style-type: none"> ○ Call, visit, letter, e-mail ○ Essential program information provided ○ Application form 	<ul style="list-style-type: none"> • Information provided to potential program participants in a variety of formats. A key mechanism is the contacts of the third party delivery agents with potential target audiences. Other mechanisms utilized include brochures, direct contacts, and information on the SchoolNet web site.
<ul style="list-style-type: none"> • Formal Application <ul style="list-style-type: none"> ○ Application duly signed (could be a letter) ○ Supporting information provided (as per program requirements) ○ File number assigned ○ Basic information entered into corporate information system ○ Letter sent to applicant listing missing information 	<ul style="list-style-type: none"> • Application process for each program that required the submitting of supporting information • All successful applicants receiving funding directly from Industry Canada were assigned a project number which could be tracked through the Industry Canada financial system. Individual project databases were used to track performance indicators.
<ul style="list-style-type: none"> • Project Assessment <ul style="list-style-type: none"> ○ Eligibility of applicant/project ○ Viability ○ Incrementality ○ Benefits to Canada ○ Environmental assessment ○ Consultations with other government departments 	<ul style="list-style-type: none"> • Extensive use made of advisory groups made up of knowledgeable individuals to evaluate individual projects against established criteria that set out who was eligible under what conditions, for what purposes, and for what amounts.
<ul style="list-style-type: none"> • Recommendation/Approval <ul style="list-style-type: none"> ○ Project Summary Form (PSF) completed and signed by recommending officer ○ PSF must provide full justification for the contribution ○ PSF reviewed by delegated authority ○ Commitment of funds authorized under section 32 of the FAA by signature of delegated authority ○ If contribution is greater than \$500,000, PSF submitted to Program and Services Board ○ Integrity review performed by Programs and Services Board ○ If Programs and Services Board supports recommendation, project submitted to delegated authority for approval ○ Corporate information system updated to reflect pending transaction 	<ul style="list-style-type: none"> • PSF completed and signed at required levels for all approved projects • Corporate information systems updated as required. • Changes made verbally at the working level that were not reflected in the approved agreement.

¹³ Project life steps as set out in *Grants and Contributors at Industry Canada - Management Practices*, March 2000.

MANAGEMENT AND FINANCIAL AUDIT OF SELECTED PROGRAMS IN THE IHAB PROGRAM

Attribute	IHAB's Administration of its Contribution Programs
<ul style="list-style-type: none"> • Letter of Offer/Contracting <ul style="list-style-type: none"> ○ Standard letter of offer used, special conditions added as appropriate ○ Terms of the offers must be consistent with PSF ○ Letter of offer signed by delegated authority ○ When accepted by applicant, monitoring schedule established 	<ul style="list-style-type: none"> • Contribution agreements in place for all projects which are consistent with the information on the PSF • All agreements call for certain targets to be achieved and regular reports to be provided to Industry Canada
<ul style="list-style-type: none"> • Payment of the Contribution (Interim and Final) <ul style="list-style-type: none"> ○ Claim documents received from applicant ○ Claim reviewed by project officer for completeness and accuracy ○ Compliance with contribution agreement verified ○ Site visit performed when appropriate to ensure commitments are met ○ Project officer recommends payment to delegated authority ○ Delegated authority reviews and signs for contract performance under section 34 of the FAA ○ Financial officer proceeds with cheque requisition ○ Corporate information system updated to reflect transaction ○ Repayment schedule established (if applicable) 	<ul style="list-style-type: none"> • Minimal verification undertaken of information provided by claimants or ensuring compliance with the contribution agreement • No formal plan for site visits. Some Regions have implemented site visits on their own. • Appropriate officials have signed off on payments and cheque requisition. • Corporate information system updated to reflect transaction.
<ul style="list-style-type: none"> • Project Monitoring <ul style="list-style-type: none"> ○ Compliance with conditions verified (site visit as required) ○ Benefits reported ○ Financial officer informed (repayable) ○ Repayment made ○ File closed 	<ul style="list-style-type: none"> • Minimal efforts made to verify compliance with conditions. In some instances the information requested from participants was inadequate for an informed decision to be made on compliance.

**ANNEX 3: IHAB'S ADMINISTRATION OF CONTRIBUTION PROGRAMS IN
COMPARISON TO THE ATTRIBUTES OF A WELL-MANAGED PROGRAM¹⁴**

Attribute	IHAB's Administration of its Contribution Programs
1. Choosing the appropriate funding instrument grant or contribution respects and achieves a balance among principles of accountability to Parliament, favourable cost/benefit, risk management, and reasonable treatment of program recipients.	<ul style="list-style-type: none"> • Chose contributions over grants because of general preference for contributions. No evidence of a detailed analysis of the merits of the two. • There is a requirement for repayment where the contribution has been given to a business to develop a product (Learnware). Most of the contributions (CAP, VolNet, NetCorps) are ultimately going to individuals or not-for-profit organizations to carry out an activity consistent with IHAB's program objectives or to administer the program on behalf of IHAB.
2. Program management at all levels can explain how recipients are expected to benefit from funding and to what end.	<ul style="list-style-type: none"> • Program management can explain, and has done so in the project summaries for Industry Canada's Programs and Services Board, how the ultimate recipients will benefit from the funding. • In all of the programs examined (CAP, VolNet, Learnware, and NetCorps), IHAB is using third party delivery agents that are the direct recipients of the contribution who then in turn enter into an agreement with the ultimate recipient.
3. Program officers understand who is eligible for funding, under what conditions, for what purposes, and in what amounts.	<ul style="list-style-type: none"> • Detailed criteria have been defined for most of the programs examined that define who is eligible for funding, under what conditions, for what purposes, and for what amounts. • The actual determination of eligibility is made by third party delivery agents on behalf of IHAB. In some instances (Learnware), Industry Canada will receive a recommendation on who should receive the contribution and the Minister will make the final determination.
4. Potential applicants are aware of the program.	<ul style="list-style-type: none"> • A range of approaches are used to advise potential applicants of the program. A key mechanism is the contacts of the third party delivery agents with the potential target audience. Other mechanisms include brochures, direct contacts, and information on the SchoolNet web site.

¹⁴ As defined in *A Risk Assessment Framework for Grant and Contribution Programs*, Discussion Draft, March 7, 2000 prepared by the Office of the Auditor General in collaboration with Industry Canada.

MANAGEMENT AND FINANCIAL AUDIT OF SELECTED PROGRAMS IN THE IHAB PROGRAM

Attribute	IHAB's Administration of its Contribution Programs
5. Eligible projects make sense for the applicants to carry out (business case) and for the program to fund (program case).	<ul style="list-style-type: none"> •The design of all programs involving contributions has been subject to review by the Industry Canada Programs and Services Board •All programs reviewed have been implemented in a manner consistent with the broad direction provided by the Programs and Services Board. •Identified projects have all been approved by the Programs and Services Board. Justification including, if appropriate, a business case was required in each case.
6. More deserving projects are funded at an appropriate level.	<ul style="list-style-type: none"> •Projects are typically reviewed in batches, i.e. Learnware, so that the more deserving projects will receive the funding •External committees that include subject matter experts have been used to review and make recommendations on specific projects. Where potential conflicts might exist (e.g., with Learnware), the external expert did not typically review applications from their province
7. Funding is used for the purposes agreed.	<ul style="list-style-type: none"> •A signed agreement is in place between Industry Canada and the recipient of the contribution that clearly lays out the respective responsibilities and the right of the Crown to audit. Similar provisions have been made between the delivery agents and the ultimate recipients. •Program officers have not consistently confirmed that all funds claimed were expended strictly as intended. Several instances were identified in the course of the audit where this had not occurred. •Verbal changes were made to terms and conditions of contribution agreements at the working level. These changes were not documented or subjected to the approval process.
8. Problems with project and program performance are resolved quickly.	<ul style="list-style-type: none"> •Programs are being readjusted when results were not consistent with initial expectations, e.g. CAP, VolNet
9. Management reporting demonstrates a good knowledge of program performance.	<ul style="list-style-type: none"> •Management reporting is focused on total money spent to date, number of organizations connected, number of young people signed up, etc.
10. Money owed to the government is collected (in the case of repayable contributions only).	<ul style="list-style-type: none"> •Not yet applicable. The only program where there will be repayable contributions is Learnware. It is not yet at the point where there would be a potential for repayments.

ANNEX 4: CONTRIBUTION PAYMENTS BY PROGRAM FOR 1998-99 AND 1999-00¹⁵

Program	1998-99		1999-2000	
	Number of Agreements	Payments made	Number of Agreements	Payments made
Community Access Program	15	\$11,092,456	19	7,544,436
Computers for School	7	\$949,012	9	\$2,614,566
Francophone Intranet	1	\$48,777	4	\$903,527
Information Highway Science & Entrepreneurship Camps	1	\$690,000	1	\$345,000
Learnware	2	\$128,343	4	\$218,020
NetCorps	-	-	1	\$4,354,598
SchoolNet	4	\$299,550	7	\$706,450
VolNet	1	\$1,200,000	33	\$4,941,396
Total	31	\$14,408,138	78	\$21,627,993

¹⁵ Taken from the Project Expenditure and Forecast Cash Flow Report produced by the Program Information Reporting System (PIRS) using data as of May 16, 2000