



# **Internal Audit - Management of the Compensation Reserve (Archived)**

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# ARCHIVED - Internal Audit - Management of the Compensation Reserve

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# **Executive Summary**

## **Background**

The compensation reserve is a provision in the federal fiscal framework, agreed to by TBS and Finance, which establishes an envelope to cover the increased costs for appropriation-dependent federal organizations resulting from wage increases. These increases can result from collective bargaining or other mechanisms and generally take the form of straight economic increases, restructures of pay lines, recruitment and retention allowances and other types of payments or benefits.

The Expenditure and Management Strategies Sector (EAMS) and the Financial Analysis Division of the Comptrollership Branch managed the compensation reserve until it was transferred to the Human Resources Branch (HRB). The transfer to HRB was done with limited documentation of processes or information to support past decisions. This situation complicated the transition process. Due to the lack of documentation associated with the transfer of the compensation reserve, and the increased scope of the function itself, the current management team is slowly building policies, procedures and an infrastructure. This action is required to ensure the decisions impacting the establishment, monitoring and allocation of the compensation reserve will be well supported and documented in the future.

## **Review Objectives**

Our audit was designed to assess whether the compensation reserve processes provide management with accurate and timely information for the planning and establishing, monitoring and allocation of the compensation reserve funds.

## **Summary of Findings**

The administration of the compensation reserve is still in transition. Although the processes for the administration of the compensation reserve still need to be strengthened, the group has made significant progress over the last few months. We have however identified a number of weaknesses that should be addressed. In summary they are:

***Lack of a formal compensation reserve guideline*** - During the audit no evidence was found of formal documentation related to guidelines, principles or procedures available to the Strategic Planning and Analysis Division (SPAD) when the function was transferred to HRB. The absence of this documentation complicated the transfer of the function because SPAD did not have complete information on the process. There is a need to develop a comprehensive compensation reserve guideline to address uncertainties and identify specific policies and procedures.

***Limited resources to manage the compensation reserve process*** - Given the limited resources allocated to the management of the compensation reserve, there is a risk of error to TBS. The compensation reserve deals with a significant amount of money and decisions are made in a very dynamic environment under severe time pressures with little room for error. We recommend that TBS study the possibility of adding additional resources to SPAD to decrease the overall risk to TBS.

***In-house developed database manages the compensation reserve*** - The reliability and flexibility of the in-house database is at risk due to its size and demands on the software. The program is at risk of reaching its maximum capacity if the database becomes much larger. The system performance could also become compromised the larger it becomes.

***Access control over the database*** - Other than limited restricted access, there are currently no formal controls over access to the database or changes made to the information in the database. We recommend stronger controls be implemented to safeguard the accuracy and confidentiality of the database.

***Compensation Reserve reference levels established at the beginning of a negotiating mandate*** - The compensation reserve funding is currently established at the beginning of a negotiating mandate and is not subsequently updated to reflect changes in the Public Service population and the impact of the changes in the economic environment. As a result, the reserve may not reflect current needs of government departments. The level of funding of the compensation reserve should be reviewed annually to ensure it meets the actual costs associated with signed collective agreements. SPAD should also explore the possibility that the wage base used to establish the compensation reserve could be reviewed annually to account for the impact of significant changes in employee population within departments. This would help relieve funding pressures for departments.

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## **Management Response**

The audit findings have been discussed with management and they concur with the audit findings. To better position itself to respond to challenges facing the Branch, the Human Resources Branch (HRB) is currently reorganizing based on three broad themes: Compensation; People Management; and, Leadership. Analysis and Research and Compensation (ARC), which managed the Compensation Reserve as part the Strategic Planning and Analysis Division (SPAD), is now managing the reserve as a separate division (the Compensation Planning Division (CPD)). Reorganization is not complete, and roles and responsibilities have not been finalized. Detailed responses to the recommendations can be found in section 4.

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## **1.0 Background**

The Audit Committee of Treasury Board Secretariat ("TBS") requested that an internal audit be conducted on the management of the compensation reserve during fiscal 2001-02.

The compensation reserve is a provision in the federal fiscal framework, agreed to by TBS and Finance, which establishes an envelope to cover the increased costs for appropriation-dependent federal organizations resulting from wage increases. These increases can result from collective bargaining or other mechanisms and generally take the form of straight economic increases, restructures of pay lines, recruitment and retention allowances and other types of payments or benefits.

The compensation reserve was managed by the Expenditures and Management Strategies group (EAMS) and the Financial Analysis Division of the Comptrollership Branch until it was transferred to the Human Resources Branch (HRB). The transfer to HRB was done with limited documentation of processes or information to support past decisions. This situation complicated the transition process between the two divisions. Due to the lack of information associated with the transfer of the compensation reserve and the increased scope of the function itself, the current management team is slowly building policies, procedures and an infrastructure to ensure the decisions impacting the establishment, monitoring and allocation of the compensation reserve will be well supported and documented in the future. This process requires a significant amount of time and resources from HRB.

The compensation reserve can be broken down into essentially three processes: the establishment of the funding levels in the compensation reserve, the allocation of the funds from the reserve to departmental reference levels, and the monitoring of the overall compensation reserve. HRB has not yet managed a full cycle of the compensation reserve and hence management is still learning and gaining knowledge about the processes.

Management of the compensation reserve is complex for the following reasons:

- The dollar value of the compensation reserve is significant as it is designed to fund increases in salary and benefits resulting from collective bargaining negotiations of approximately 380,000 federal

government employees, employees of government agencies and some Crown Corporations. The overall administration of such a reserve is in itself complicated and cumbersome.

- Although the compensation reserve is managed by HRB, it also involves many other groups such as: EAMS, program sector analysts, the Department of Finance and other Government departments.
- The compensation reserve provides for many different groups such as: collectively bargained groups, separate employers, RCMP, DND and others. Each of these entities have different compensation systems and pay structures, rules and processes that the Strategic Planning and Analysis Division (SPAD) must take into account to ensure that unique situations are dealt with while ensuring each is treated consistently. In addition, certain of the benefits collectively bargained may also apply to separate employers and hence SPAD must consider the ripple effect of their funding decisions on the government as a whole. Moreover, because of the tendency of public sector unions to pattern bargain, one of the key concerns is the identification of long-term cost implications of precedent setting agreements.
- There is also complexity due to the fact that contracts do not always coincide with a fiscal year end or a calendar year end; this makes the allocation of the funds to the departments and the tracking of spending more difficult.
- The most recent mandate for the compensation reserve provided funding for three years for the government as a whole but the timeframes covered by labour negotiations for individual groups can vary and may not match the timeframes set up for the reserve. Therefore, when new negotiations begin, it may be difficult to determine if a group should be funded from the current mandate or if it should be included in the upcoming cycle for the compensation reserve.
- The costing and allocation processes are detailed and cumbersome and have many variables to consider which adds to the overall complexity. Labour agreements are becoming more complex and settlements include items that may not have been included in previous labour agreements. Determining how to cost and allocate these items so that departments are treated equitably presents a challenge.
- The establishment of the compensation reserve requires the use of a number of assumptions on future economic conditions and market trends to allow the forecast of the negotiation mandate. Since a negotiation mandate can last for several years, assumptions used must be as accurate and realistic as possible.

The compensation reserve, administered by HRB, is continuously being reviewed and reengineered where deemed appropriate. As SPAD manages through the three phases of the cycle, the processes and procedures are being formally documented.

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## 2.0 Review Objectives and Scope

Our audit was designed to assess whether the compensation reserve processes provide management with accurate and timely information for the planning and establishing, monitoring and allocation of the compensation reserve funds.

The internal audit included the following:

- Review of the overall objectives and purpose of the compensation reserve.
- Mapping and description of the processes used by the HRB for the:
  - Establishment of the compensation reserve;
  - Allocation of the compensation reserve funds; and
  - Monitoring of the compensation reserve.
- Identification of inherent risks within the compensation reserve processes.
- Identification of internal controls.
- Identification of weaknesses within the process and its implication.
- Development of recommendations to strengthen the compensation reserve processes.

## Approach

The approach taken included the following:

- Interviews with personnel from Strategic Planning and Analysis Division ("SPAD") responsible for managing and allocating the compensation reserve funds within HRB;
- Interviews with personnel from other functional areas within TBS involved with SPAD in the establishment, allocation and monitoring of the compensation reserve (such as Expenditure and Management Strategies [EAMS] and the Collective Bargaining Group);

- Review of documents supporting the current process;

Our internal audit focused on providing observations and recommendations over the management of the compensation reserve process.

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## 3.0 Overview of the Processes

Management of the compensation reserve is divided into three main processes. A written description of these processes follows and a flowchart is included in Appendix A. The description and flowchart illustrate the process followed for collective bargaining. It should be noted that the compensation reserve also manages the funding requirements for other non-bargained groups; as a result, the compensation reserve processes are modified to address the specific requirements of the different groups. The process description and flowcharts in Appendix A only address the general process used for collective bargaining and do not address changes required when non-bargained groups are involved, therefore there may be slight variations in the process followed for non-bargained groups which are not reflected in the process flowcharts.

### Establishment of the compensation reserve

The funding levels in the compensation reserve are established at the beginning of each collective bargaining cycle. The length of the cycle is generally established based on economic conditions. The current negotiation mandate established the reference levels in the reserve for approximately three years starting March 2000. The level of the reserve is established based on a business case developed by HRB's various stakeholders, including SPAD, Labour Relations Division and the Human Resources Management Division. The business case represents an estimate of the future costs to be incurred as a result of labour negotiations to be undertaken by TBS during the cycle of the global compensation framework (including PSSRA 1-1, separate employers-PSSRA 1-2, some Crown Corporations, Canadian Forces and RCMP). The business case established includes a number of assumptions such as future economic increases, labour market trends and inflation rates. The compensation reserve has three main components:

- Economic - to address basic wage increases;
- Group specific - to address specific compensation issues; and
- Labour market differential - to address recruitment and retention issues.

When the business case is prepared by HRB, each of these components is addressed individually to determine the amount of funds to be made available for the duration of the mandate. Each component is managed and monitored separately. However, funds from the first two components, economic and group specific, can be transferred from one category to the other when required without additional approval from Finance. Although there is no specific control over these inter-group transfers, it allows management to address varying needs between these components and more adequately risk manage the compensation reserve as a whole. The funds for the labour market differential are to be used only for specific circumstances and need a justification to support their use within the terms of an agreement. Funds in this category cannot therefore be transferred to the other two categories.

Once HRB has completed the business case, it is presented and discussed with EAMS. EAMS provides a support role to HRB by challenging the assumptions used by HRB in the business case to help ensure all assumptions and market factors are appropriately addressed in the business case.

The business case is then presented by HRB and EAMS to the Department of Finance for final approval. After Finance approves the business case, the funding level for the compensation reserve is established and will remain for the duration of the planning period and becomes the basis for all future negotiations. There are very few individuals who know the total amount of the compensation reserve.

Subsequent adjustments to the established compensation reserve are requested only in instances of significant changes to the mandate parameters; for example, the current compensation reserve was initially approved for a one-year mandate, then revised to a two-year mandate and subsequently revised again to a three-year mandate. At the same time the mandated level of economic increases was also revised a number of times as bargaining conditions changed. In such cases, a new business case must be prepared and a process consistent with that of establishing the full compensation reserve must be followed to obtain additional funds. If certain occupational negotiations cannot be settled within the terms and conditions established in the initial mandate, but the costs can be absorbed by the overall reserve, there is usually no need to go back to Finance for additional funds. These types of changes are risk managed and are absorbed within the established reserve.

However, there are cases where the amount of funding required to reach a settlement exceeds the ability of the compensation reserve to risk manage. In these instances, approval for increased funding is sought from Finance in advance of approving the higher mandate.

The key risks and controls associated with the establishment of the compensation reserve are as follows:

<b>Key Risk</b>	<b>Control</b>	<b>Deficiency</b>
<p>The compensation reserve was not established for the appropriate length of time.</p>	<p>Collective bargaining and other divisions of HRB are consulted at the beginning of the process to ensure appropriate assumptions are used.</p> <p>EAMS reviews the business case prepared by SPAD and challenges the assumptions used.</p> <p>TBS can approach Finance to seek agreement to lengthen the mandate and get the required funding.</p>	<p>None</p>
<p>The economic assumptions used in the business case are incorrect or not realistic based on current market conditions.</p>	<p>A survey is conducted prior to the development of the business case to analyze the market conditions. The market survey will be specific to the group undergoing negotiations (e.g., correctional officers, economists, etc.)</p> <p>The Labour Relations Division in conjunction with the Analysis, Research and Compensation group from within HRB reviews the external labour market, current and forecasted economic conditions and the expectations of unions.</p> <p>EAMS challenges the reasonableness of the assumptions based on their knowledge of the economic conditions to ensure they are realistic.</p> <p>The Department of Finance will ultimately challenge all assumptions used.</p>	<p>None</p>
<p>The compensation reserve is established using the incorrect wage base.</p>	<p>The wage base used is derived using pay records from the PWGSC regional pay system and directly from organizations that do not use the PWGSC pay system. It is based on the current employee population at the time the reserve is set.</p>	<p>If the wage base provided by an organization is incorrect they may not receive an appropriate amount of funding. This is more specific to organizations such as DND, the RCMP and certain Crown Corporations.</p>
<p>The compensation reserve base does not include a complete list of departments, agencies, Crown Corporations, etc. covered by the reserve.</p>	<p>None</p>	<p>SPAD inherited the compensation reserve from EAMS without complete documentation on included and excluded organizations.</p>



## Monitoring the compensation reserve

SPAD monitors the compensation reserve balance on a regular basis when new agreements are signed or when allocations are made from the reserve. The team monitoring the level of the compensation reserve is mainly composed of three members of SPAD. A large database developed in house enables the team to monitor and track the level of compensation reserve funds available or used at any point in time.

SPAD monitors the level of the three main components of the reserve individually. The ongoing monitoring presents a challenge to SPAD since there are not sufficient resources available to develop and maintain the database.

SPAD meets on a regular basis with stakeholders involved in labour negotiations to stay apprised of negotiation status, developments, potential pressures and impact on the compensation reserve. This allows SPAD to provide management with current information to assess the adequacy of the compensation reserve, potential pressures and possible ripple effects.

When a tentative agreement is reached with a union, SPAD reviews the costing of the agreement to ensure the terms and conditions are within the compensation reserve framework. SPAD is required to provide a sign-off before management of TBS approves the agreement.

This process also applies to areas other than collective bargaining groups. In these cases the groups/organizations also have approved mandates and SPAD monitors to ensure they stay within their mandates.

The key risks and controls associated with the monitoring of the compensation reserve are as follows:

Key Risk	Control	Deficiency
Not all signed agreements are entered into the database to monitor the level of the compensation reserve.	There are cross checks performed between the allocation made to the departments during the various supply periods and the tracking spreadsheet that records the provisioning and expenditures of the reserve and the database used to monitor the level of the compensation reserve.	None
There are not sufficient funds within the compensation reserve for current negotiations.	The database keeps a running total of the balance remaining in the compensation reserve. When negotiations are under way, SPAD enters the information in the schedule based on the approved mandate.	None
SPAD is not aware whether funds in the compensation reserve will be sufficient for all remaining groups within the mandate (groups for which negotiations have not been started).	The database keeps a running total of the liabilities for unsigned agreements and with this SPAD can ensure that funds are set aside for the remaining agreements.  In addition, for agreements which have not been formally signed or approved but for which SPAD has given an informal approval, any additional monies over the mandate are tracked	Until the processes are fully documented and HRB has had experience with a full compensation reserve cycle, this risk is not completely mitigated.

	to ensure the funding envelope is not over committed.	
Funds will be disbursed or committed when they are not available.	<p>The database tracks the amount of money spent from the compensation reserve as well as current negotiations. Mandates will not be approved if funds are not available.</p> <p>When a tentative agreement has been reached, SPAD must review the costing of the agreement to ensure terms and conditions are within the compensation reserve reference levels and must provide approval.</p>	None
Risk that an agreement is signed without considering the overall impact of the settlement on other negotiations (ripple effect).	SPAD staff is becoming familiar with the potential costs on other groups and provide advice/warnings to senior management when appropriate.	<p>Although SPAD tries to consider the ripple effects of all negotiated settlements, there is no formal mechanism in place to ensure consistency and accuracy.</p> <p>SPAD, in conjunction with LRD and HRM is currently working on a document outlining the potential ripple effects that each group may have on others. The next step will be to identify and, where possible, quantify the nature and magnitude of the ripple effects.</p>

## Costing and allocation of the compensation reserve to departments

### Approval of negotiating mandates for occupational groups

The negotiator working for the Labour Relations Division discusses the mandate for the group with SPAD to ensure it falls within the funding parameters of the compensation reserve. In addition, SPAD is also given the business cases that support the request for terminable allowances. SPAD would then make a recommendation to the CHRO for the overall costs to the compensation reserve including ripple effects as well as the strengths and weaknesses of the business case for terminable allowances. The negotiator cannot exceed this mandate without prior approval.

### Costing

Once a tentative labour agreement is reached with a union, SPAD reviews the costs estimates of the various components of the agreement produced during the negotiations. SPAD produces these estimates in conjunction with members of Collective Bargaining team and they are also shared with the union. These estimates are then used to produce the government-wide cost of the agreement to ensure it falls within the terms and conditions of the overall compensation reserve framework. The costing of the agreement is performed by SPAD using an in-house developed spreadsheet. This spreadsheet incorporates the wage base for each department and group, the contract dates, the economic increases for each fiscal year and all other terms and conditions negotiated in the new collective agreement. Once the costing is complete, SPAD will compare its costing to the estimated costing prepared by the Labour Relation Division of HRB for accuracy. The manager of SPAD will verify the analysis to ensure the numbers derived in the spreadsheet are reasonable and there is no risk of a significant error.

## Allocation Calculation

Once the costing has been approved and the agreement has been ratified, SPAD prepares the allocation of the funds to the various departments on the same spreadsheet used to perform the costing. Once the detailed allocation is completed, a verification step is performed by SPAD to ensure overall accuracy of the allocations. SPAD is responsible for establishing the overall allocation to each department and agency.

The allocation made by SPAD to departments and agencies represents the best estimate of funding requirements as the allocation is based on the wage base in effect when the compensation reserve was last established. The allocation does not take into account changes to compositions of groups within departments, growth of personnel and new program implementation. Departments must internally fund wage and benefit increases resulting from new collective agreements for employees not included in the departmental wage base at the time the last mandate was set. This has been the cause of many complaints from departments and agencies and a significant amount of time is spent justifying this position.

## Distribution of allocation information

Once SPAD is satisfied with the costing and the allocation, the wage base allocation information is provided by e-mail to EAMS and to TBS program analysts. The TBS program analysts constitute a link between departments and SPAD, the program analysts are responsible for forwarding the information to the departments. Analysts answer some basic questions from departments on allocations and forward the more technical questions to SPAD.

Until March 2001, SPAD was providing a significant amount of information to departments regarding the allocation. The information was included in a large number of spreadsheets, some of it was fairly technical and difficult to understand by analysts and resulted in numerous questions for SPAD. In March 2001, the information provided to departments was streamlined and condensed into two spreadsheets that highlight key information to users and made it simple for the program analysts to use. There are a number of different opinions in terms of the level of information that should be provided to the program analysts for their departments by SPAD.

The key risks and controls associated with the costing and allocation of the compensation reserve are as follows:

Key Risk	Control	Deficiency
<p>The costing prepared by SPAD does not reflect the terms of the tentative agreement with the union.</p> <p>There is an error in a formula in the spreadsheet used to perform the costing and the allocation.</p>	<p>The costing prepared by SPAD is compared to the costing information provided by other employees from SPAD working in conjunction with Labour Relation Division.</p> <p>Two individuals within SPAD perform the overall costing verification using two separate costing programs and results of the calculations are cross-checked.</p>	None
<p>The costing is not properly allocated by year.</p>	<p>The costing by year is reviewed by two individuals in SPAD using the method described above.</p> <p>Government departments review allocations in detail and would identify significant errors in annual allocations as it impacts their budget.</p>	None

Allocation of the funds to some departments is not properly done.	Government departments would comment if insufficient funding were received for a new collective agreement as it would impact their budget.  Two individuals within SPAD independently review the allocation to the departments for accuracy.	A risk exists if a government department received excess funding as the department may not remit the excess. The risk is mitigated since the overall allocation must reconcile to the approved wage base. If one organization received an excessive allocation, this would be offset by a shortfall with another entity that would be reported prompting a review.
Allocations are not sufficient to fund negotiated compensation increases at the departmental level.	Allocation is performed based on the approved wage base established in the initial mandate and does not take into account changes in employee population resulting from staff movement, new programs, downsizing, etc. This is consistent with the current basis for the compensation reserve.	Government departments must fund the costs associated with population changes through amounts approved by TB for new programs or within their own budgets. Fundamental changes to the basis and purpose of establishing the compensation reserve would be required to fully address this weakness.

## 4.0 Audit Findings

The processes described in section 3.0 identify key risks and associated controls for each component of the compensation reserve cycle. In instances where control weaknesses have been identified, they have been brought forward as recommendations. Section 4.0 of the report deals with some of the most significant deficiencies identified in Section 3.0 as well as observations and recommendations related to the overall framework of the compensation reserve.

### (i) Absence of compensation reserve guidelines

TBS does not have a formal compensation reserve guideline addressing the establishment, management and allocation of the compensation reserve. The lack of a guideline makes it difficult to ensure fairness and consistency, as there are no principles and procedures to follow.

### Recommendation

We recommend TBS continue the work it has begun on developing a compensation reserve guideline that would outline clear principles and expectations relating to the establishment of the compensation reserve, as well as the costing, allocation and monitoring of the funds. The compensation reserve guideline should include:

- basic principles related to the administration of the compensation reserve;
- roles and responsibilities of individuals involved with the compensation reserve;
- a definition of the intended use of the compensation reserve funds;
- a clear outline of what the compensation reserve covers and what it does not cover;
- the identification of parties and organizations covered by the compensation reserve;
- definition of the wage base to be used to allocate funding;
- principles behind the allocation of the funds;
- procedures to be followed for the establishment of reference levels for the compensation reserve;
- identification of monitoring activities; and
- process for the costing and allocation of funds.

### Management response

HRB is formalizing and elaborating on the compensation philosophy and policies for the federal public service. Included in this project is a requirement to document the funding relationships and rationales for the organizations that have access to funding from the compensation reserve. This is especially true for separate employers, appropriation dependent crowns, uniformed members of the RCMP and the military. The

Compensation Planning Division, in conjunction with program analysts and other employees in the Human Resources Branch, have begun work on this aspect and a draft is expected to be completed by December 2002.

## **(ii) Documentation of the compensation reserve processes**

During our audit we observed that the processes and procedures of the compensation reserve were not or were only partially documented. Many of the TBS employees involved in establishing the last compensation reserve have left the organization or moved to other positions. As a result, a significant amount of corporate knowledge has been lost. The compensation reserve process administered by HRB is still in transition since the transfer from EAMS and the Financial Analysis Division of the Comptrollership Branch. As HRB becomes more familiar with all cycles of the process, documentation is becoming more rigorous.

### **Recommendations**

We recommend HRB, together with other parties involved with the compensation reserve processes, complete the documentation of the processes and procedures used for the management of the compensation reserve, more specifically the processes relating to the establishment, monitoring and allocation of the reserve. It is crucial that all the relevant parties be involved in the documentation process to ensure processes and procedures are accurately documented. The documentation will help ensure standardization of procedures from one situation to another, facilitate the training of new employees and maintain an appropriate level of corporate memory within the division in case key employees leave the organization or the division.

We also recommend documentation be reviewed regularly and updated as required to ensure new information is captured and processes are kept up to date.

### **Management response**

CPD is continuing to work on documenting the compensation reserve guidelines and processes, with a first draft to be completed by the end of fiscal year 2002/2003. Included will be a more systematic approach to collecting required information concerning separate employers and appropriation dependant crown corporations.

## **(iii) Wage base and employee population used to establish the compensation reserve is not revised annually**

The wage base in effect at the beginning of a negotiating mandate is used throughout the compensation reserve mandate, which can vary in length ranging anywhere from one year to several years. Currently, the negotiated settlements are based on the wage base that was established in March 2000. When a collective agreement is settled with a union, the costing and allocation of funds to departments is based on the population and wage base established at the beginning of the mandate and does not take into account employee movement, growth of departments and new program development. For any growth in the department's population that is the result of a TBS submission, program analysts were advised to take into account wage inflation when developing the costs of the additional personnel. For growth for any other reason (e.g. creating new or filling vacant positions) departments must internally fund increases in wages or changes in their employment levels since the establishment of the compensation reserve reference levels. This can create significant funding pressures on the departments in the short run and can also create inconsistencies in the methods used in departmental TB submissions when addressing expected workforce movement, growth or program development. The fact that the wage base is not updated to reflect actual employee levels creates concern from departments relating to the funding and allocation process and the ensuing financial pressures associated with it.

### **Recommendations**

We recommend that SPAD explore the possibility that the wage base be adjusted annually to reflect the actual employee population. Changes in department size or significant employee movements might possibly be taken into consideration when the allocation of funds from the compensation reserve is provided. Such an annual adjustment would decrease funding pressures on departments and would more appropriately reflect the actual salary costs.

We also recommend TBS review on an annual basis, the adequacy of the compensation reserve for changes in economic conditions, inflation, market place fluctuations, and other factors that may impact labour negotiations and settlements.

## **Management response**

There is currently a project underway in the Compensation Planning Division (which manages the reserve) to formalize and elaborate on the annual compensation plan for the Public Service. This would provide a more systematic process with respect to the determination of funding requirements. During this project, CPD will explore with the department of Finance, the possibility an annual review of both the economic conditions and the size of the federal wage base on which the funding for the compensation reserve is based, with an aim of adjusting them if conditions warrant. A first draft of the plan is expected to be complete by mid-December 2002.

## **(iv) Resources allocated to monitor and allocate the compensation reserve**

Until recently there were only two individuals working on this file. This has considerably slowed the development of the monitoring system and documentation. There are now three full-time individuals within SPAD who have the overall responsibility for the complex task of monitoring and allocating the compensation reserve and assisting in preparing the business cases for labour negotiations. They are accountable for the maintenance of the database that monitors the level of the compensation reserve, the costing of agreements, the allocation of funds to departments resulting from the settlements of collective agreements, liaison with other divisions within HRB to discuss status and possible impacts of negotiations on the compensation reserve and liaison with departments and program analysts. They must also analyze and account for the possible ripple effects one settlement could have on other agreements or negotiations in process as well as in the future. Collective agreements have become more and more complex adding to the complexity of the costing of the agreements and the allocation of funds from the compensation reserve. The limited resource base delays the development work and increases the risk of errors.

The limited number of individuals involved with the compensation reserve also raises a succession planning issue within SPAD. The Manager is currently heavily involved in all aspects of the compensation reserve processes and a prolonged absence or departure from the organization could significantly impact the compensation reserve processes since a complete understanding of the compensation reserve process is limited to that individual. Other members of SPAD have only a general or a partial knowledge of the processes.

## **Recommendations**

Given the complexities associated with the compensation reserve process as well as the increasing workload, we recommend that TBS perform a review of the human resources allocated to the compensation reserve processes. Additional resources for such an important function would allow SPAD to develop and implement improved processes to help reduce the risk of errors and to increase the level, quality and timeliness of advice and assistance to the other stakeholders in the compensation reserve. This will also help mitigate the increasing risks associated with the complex collective agreements signed by TBS and ensure implications of settlement are identified and quantified prior to finalization of agreements. There may be instances where decisions are not documented as they should be and crossover controls are not consistently applied given the current level of work required by the group.

We also recommend that TBS develop a succession plan to mitigate the risks of departures or prolonged absence of SPAD key employees. Such a succession plan will allow TBS to review the resources allocated to SPAD and ensure they are appropriate and aligned with the level of responsibility of SPAD key employees.

Given the limited number of individuals involved in the compensation reserve process, there is a greater risk of losing knowledge in the event of a departure. We recommend TBS implement a formal information sharing process to ensure no knowledge is lost in the event of staff changes. Sharing of information concerning the different processes associated with collectively bargained groups, separate employers, Crown Corporations, etc. would help mitigate the overall risk associated with the compensation reserve process.

## **Management response**

The Compensation Planning Division (CPD) is hiring an additional person to work on this file, and the successful candidate is expected to be on strength in September 2002. With the addition of another employee, existing work will also be re-allocated amongst individuals in the group, with an aim of creating knowledge transfer and backup for each of the main tasks associated with managing the reserve. This will allow for better succession planning and reduce any of the negative consequences surrounding the unplanned departure of members of the team.

CPD is also looking at opportunities to reduce resource requirements through the greater use of automated tools and interfaces with other Treasury Board systems.

In addition, the creation of a "Compensation Cluster" within HRB has allowed CPD to draw on the resources and expertise of the other organizations in the Cluster.

Once HRB reorganization is complete, and the roles and responsibilities of each of the organizations within the Compensation Cluster have been determined, resource requirements may be revisited.

## **(v) In-house database**

SPAD has created an in-house database containing information on compensation reserve funds disbursed, fund balances and the status of current negotiations. This database was created on an Excel spreadsheet and is very large in size. The ability of the Excel spreadsheet to support a database of this size may be at risk and could result in the loss of a significant amount of information. The database is also not very flexible or user friendly and requires a significant amount of time to update.

In addition, controls over the database are limited. While there are informal tracking mechanisms there is a need for more formal control mechanisms, such as the identification of the last user or changes made to the database. Access to the drive on which the database resides is restricted to the three individuals working on the reserve and the Director, however access to the database itself is not restricted by a password. Such easy access to the database makes it vulnerable to manipulation and unauthorized change.

## **Recommendation**

We recommend TBS assess the need for the implementation of a new database that will facilitate SPAD's monitoring of the compensation reserve. We have been informed TBS is currently analyzing the need for a more functional and reliable expenditure management information system, which could facilitate the monitoring of the compensation reserve. We support the initiative of pursuing the feasibility of including compensation reserve functionality in this new expenditure tracking system. Failing that, TBS should investigate acquiring a more robust database to be used to handle the information needs associated with the effective running of the Compensation Reserve.

We recommend stronger controls be implemented to safeguard the accuracy and confidentiality of the database. Additional security features over the database, specifically monitoring and access controls, should be implemented and monitored to more adequately safeguard the integrity of the information maintained in the database.

## **Management response**

Redundancy within the database has been built-in by saving copies on each occasion where changes are made. This reduces the risk of losing data or creating a corrupt file. However, these are short-term measures while consultants are engaged to assess the possibilities of using either commercial software (accounting packages) or specifically developed software. A consultant will be hired by October 2002, with recommendations expected by January 2003.

The proposed Compensation Reserve Management System will be capable of, but not limited to, tracking sources of funds as well as organizational payrolls, costing of collective agreements, calculating departmental allocations, validation of data, tracking of changes to database, tracking of transactions and originators, automatic generation of reports on expenditure, balance sheets, liabilities, and, where possible link with other TBS systems such as the Expenditure Management Information System.

Access control over the database: In addition to the control already in place, i.e., restricted access to the drive on which the database is stored, the database itself has now also been password protected. Only individuals working on the database are provided with the password.

Also, more recent individual costing models have been password protected to limit access, and write protected, to reduce the possibility of files being inadvertently changed. CPD is also looking at the feasibility of write protecting all fields, except those which are required to change in the costing model template. This will reduce the possibility of formulas being inadvertently changed.

One of the expected requirements of the Compensation Reserve Management System is an audit trail capable of tracking changes made to the database. The System will be developed with different levels of access depending on the responsibility and accountability of the employees working on the database.

## **(vi) Costing models relating to National Defence (DND) department and Royal Canadian Mounted Police (RCMP)**

For DND and RCMP, as with other federal departments, when collective agreements are signed between TB and the unions, the compensation reserve funds the changes resulting from these agreements. However, in the case of RCMP and DND for uniformed members and members of the military these two departments calculate the cost of the agreements on their own and SPAD has little involvement. SPAD is responsible for monitoring the compensation reserve level, a task that is made more difficult when they are not in control of the costing and therefore, ultimately the spending. Although SPAD has been given the wage base of these two entities by the organizations themselves, it required a number of iterations before SPAD was satisfied with the information they were given. In these circumstances it is difficult to validate the information provided to ensure the wage base is accurate and reflects the actual level of employment. Limited control exists due to the difficulty of independently monitoring the accuracy and appropriateness of the departments' calculations. SPAD has made progress and is solidifying the required wage base information and is now in the process of simplifying the costing functions with respect to these two organizations.

### **Recommendation**

We recommend TBS continue to review the costing processes in place relating to DND and RCMP compensation for uniformed members to ensure consistency with the approach taken with other departments. This will help ensure completeness and accuracy of the calculations. SPAD should continue to work towards making the costing process of collective agreements involving these organizations a joint initiative where SPAD would play a more proactive role in the process to better monitor costing of the agreements.

### **Management response**

CPD has also taken a more proactive role by costing the agreements at the aggregate level for the Military and Uniformed Members of the RCMP. CPD will continue to examine the costing models used by these organizations to better understand how they work in ensuring accuracy, completeness and consistency.

## **(vii) Availability of information and documentation relating to Separate Employers and Crown Corporations**

### Separate Employers

Until recently there was not good information sharing between SPAD and the unit in HRB responsible for Separate Employers. Discussions during the audit with both parties indicated that there were steps being taken to improve the information sharing between these two groups, which should improve the quality of the business cases, as well as the costing and fund allocation for agreements signed by these organizations during the next mandate.

### Crown Corporations

HRB has no direct contact with the Crown Corporations themselves. It is with the assistance of the program analysts that this information is collected. However, as it stands now, much of the information required for the preparation of the business case relating to Crown Corporations is not readily available to SPAD. Under the current process, SPAD does not have absolute assurance over the accuracy or completeness of the wage base,



employee population or other information used for the business case provided to them. They do however use other sources of information (e.g. main estimates, payroll reports, information on agency web sites etc.) to evaluate the reasonableness of the wage base.

There is a lack of formal documentation relating to the process on the funding of some appropriation dependent Crown Corporations by the compensation reserve. There is also a lack of formal documentation supporting which crown corporations should be funded by the compensation reserve and which should not.

## **Recommendations**

We recommend TBS review the level of information available to SPAD for separate employers and identify other required data. HRB should ensure their database is accurate and contains the most updated information.

We recommend that SPAD coordinate its efforts with the program analysts to ensure information obtained from Crown Corporations with respect to the wage base is also timely and accurate. We recommend the process used to allocate funds to Crown Corporations be formally documented and address the following issues:

- responsibilities of Crown Corporations and TBS when agreement terms exceed the current negotiation mandate;
- procedures relating to the costing of the agreements, and
- the establishment of a full list of Crown Corporations eligible for funding by the compensation reserve.

We were informed that HRB is in the planning stages of a review of the process and documentation relating to compensation reserve funding of appropriation dependent Crown Corporations. We strongly support such a review.

## **Management response**

Employees in CPD meet regularly with the members of the unit in HRB who are responsible for separate employers to share information and discuss collective bargaining issues and the resulting funding concerns. Employees from CPD are also now usually in attendance when separate employer representatives come to TBS to discuss their collective bargaining issues.

As part of a project to ensure fairness and consistent treatment among the various organizations who have access to the Compensation Reserve, CPD has begun a series of meeting with the TBS program analysts responsible for the various appropriation dependent crown corporations. As a result of these meetings, a draft paper will be prepared, by the end of 2002, that will not only identify the appropriation dependent crown corporations that have access to the reserve, but will also explain the rationale that was used for granting access. In addition, this paper will outline the extent of the access that has been granted and confirm the relevant wage base for each corporation.

## **(viii) Allocation information provided to TBS program analysts and departments**

Once SPAD has completed the costing and the allocation of a specific agreement, the funding allocation information is provided to TBS program analysts to be distributed to the various departments. The level and quantity of information provided to analysts and departments by SPAD has been contentious for some time and results in a number of questions from departments and analysts to SPAD. In March 2001, SPAD streamlined significantly the information provided to users but the issue remains open for discussion.

## **Recommendation**

We recommend the various stakeholders involved in the process communicate clearly to each other their information needs and arrive at an acceptable and appropriate level of information considering the level of effort and resources required by SPAD to prepare the information. Such a process will clarify the needs and constraints faced by each stakeholder and will contribute to reducing the number of questions to SPAD with respect to the fund allocation.

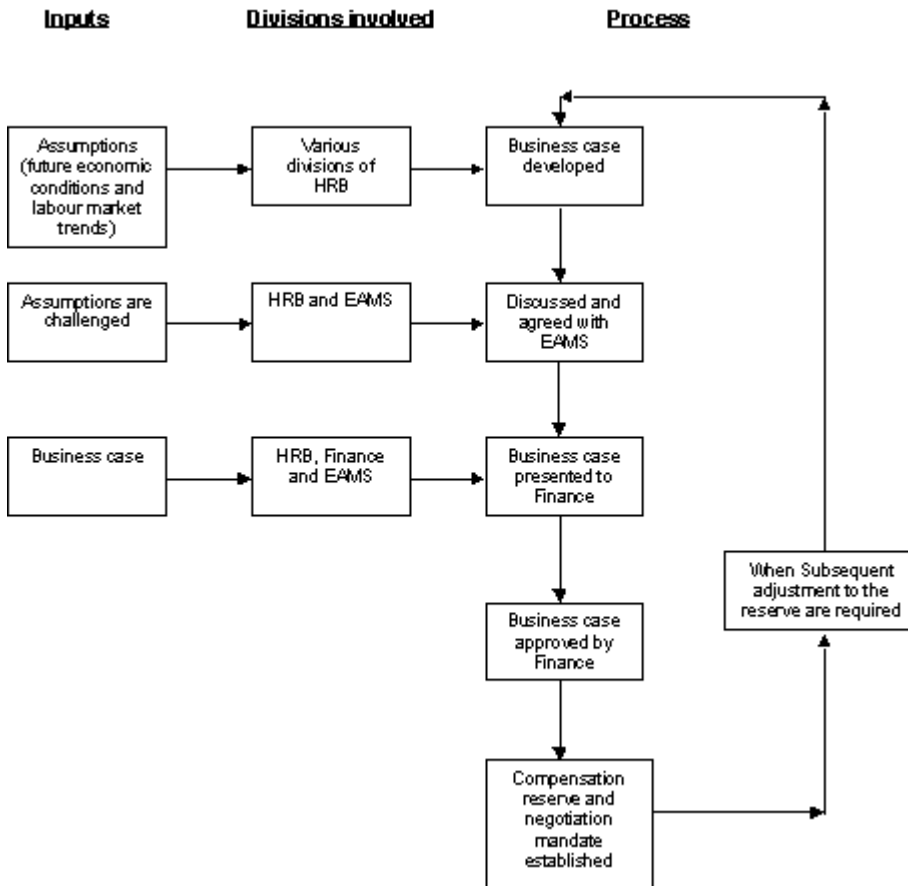
## Management response

CPD has consolidated the funding allocation information going to TBS program analysts into two documents that are easy to understand, use, and transmit to departments. CPD will continue to monitor and respond to the information needs of its clients.

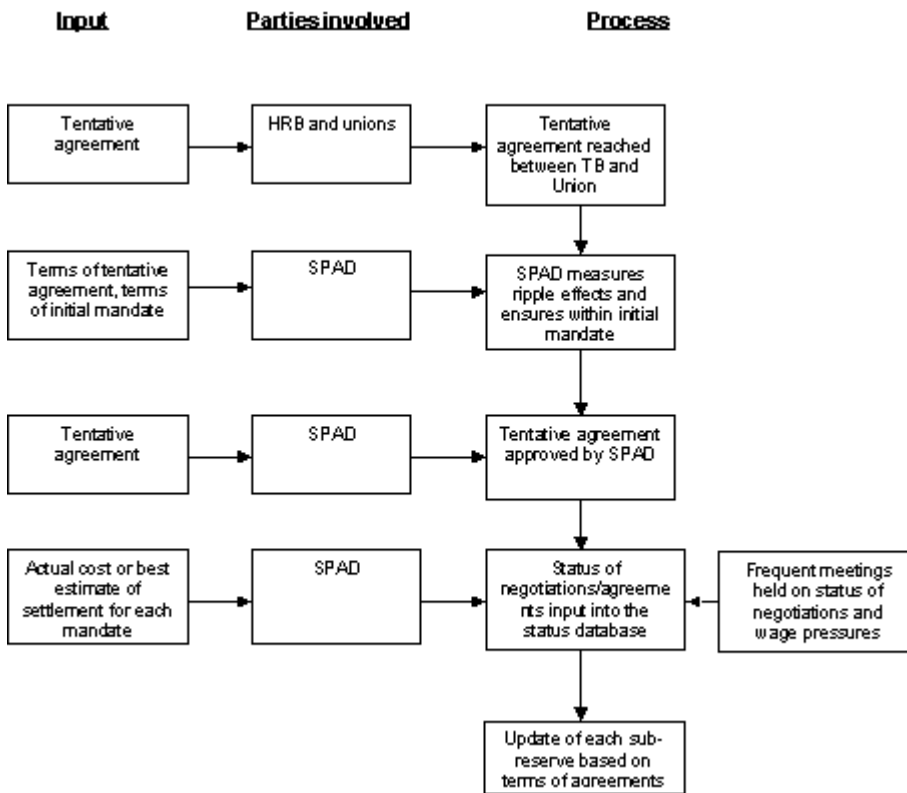
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## Appendix A - Mapping of processes

### (1) Establishment of the compensation reserve



## (2) Monitoring of the compensation reserve



## (3) Allocation of the compensation reserve

