Office of the Superintendent of Financial Institutions

Internal Audit Report

on

Human Resources
Performance Management

November 2010

OSFI
BSIF

Canada

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1. Background

**HR –
Performance
Management
Process**

The Audit Committee and the Superintendent approved an audit of OSFI's Human Resources – Performance Management for inclusion in Audit and Consulting Services audit plan.

The HR division, who is the key guardian of the Performance Management (PM) process, is responsible to provide guidance/support to OSFI management in managing and overseeing the process to ensure its quality, fairness, transparency, and consistency.

As stated in the PM Guide, the Performance Management (PM) process is a continuous cycle that helps managers and employees work together to establish work and performance goals as well as monitor their progress towards achieving them, recognizing the need to identify corrective action, where necessary. It is an opportunity for an employee to receive and provide feedback regarding his/her actual performance and contributions relative to OSFI's performance expectations as set out in the employee's Goal Commitment Document (GCD). At the same time, it should offer the employee and his/her manager an opportunity to discuss and plan for the employee's career development.

There are four key steps in OSFI's Performance Management cycle:
- o Setting performance expectations.
- o Monitoring performance throughout the year.
- o Reviewing performance (including the mid-year review and the year-end appraisal).
- o Rewarding performance.

The PM process is a very significant contributor to OSFI's mandate due to the importance, complexity, and difficulty to acquire, develop, and maintain the skills, experience, and knowledge required to conduct OSFI's activities, resulting in people risk being rated high on an inherent basis in many areas of OSFI. It supports OSFI's mandate by requiring management and staff to work in partnership to deliver solutions related to performance and career development.

2. Audit Objectives, Scope, Approach, and Criteria

**Audit
Objectives**

The purpose of this audit was to provide assurance on the adequacy of design and operation of the management framework, practices and controls in place to manage and oversee OSFI's Performance Management process to ensure its quality, fairness, transparency, and consistency.

2. 2. Audit Objectives, Scope, Approach, and Criteria, Continued

Audit Objectives (Cont)

The objectives were to determine:

o Whether policies and procedures addressing activities of the PM process were developed and formally documented.
o Whether policies and procedures were adequate and were properly communicated to all OSFI managers and employees.
o Whether policies and procedures were applied as designed and consistently across the office.
o Potential areas for improvement, as appropriate.

Audit Approach

The scope of the audit included OSFI's Performance Management process, including performance planning, monitoring, and reviewing as well as management oversight controls around the performance process.

Excluded from the scope of this audit:
o "Rewarding Performance"

In order to review a completed performance cycle, our audit work focused primarily on the performance management activities carried out during the fiscal year 2008-2009. However, recognizing that the process is evolving, A&CS found it necessary to review and understand information relating to events before and after the chosen performance cycle, as appropriate.

Audit Criteria

The Audit Criteria listed in *Appendix A* was derived from the *COSO Framework*. The criteria was used to help us ascertain the extent to which existing management controls ensure that Performance Management key inherent risks in the areas of "*Governance*, *Process, and People*" are properly mitigated and monitored.

The audit was conducted in accordance with *The Institute of Internal Auditors' International Standards for the Professional Practice of Internal Auditing*, consistent with the Treasury Board Policy on Internal Audit.

3. Audit Conclusion

The internal control framework over the performance management process needs to be improved to ensure its quality, fairness, transparency, and consistency across the office.

The main document governing Performance Management (PM) at OSFI is the Performance Management Guide ('Guide'). We noted that there is lack of clarity with regard to the force of this document (i.e. is it mandatory or not) and with regard to its true nature (i.e. is it a policy or just a guide). The degree of complexity in the process and ambiguity in this Guide, outdated related documentation, as well as a lack of awareness of the Guide's content, all have led to variation in staff interpretation and inconsistencies in its application. Consequently, employee morale and the staff retention could be significantly impacted if PM-specific risks are not effectively managed. The recent employee survey indicated that while performance management scored the second lowest on percent favourable (out of 6 survey categories), the overall survey results were positive with 92% of respondents agreeing they would "recommend OSFI to others as a good place to work. The PM process is a significant contributor to OSFI's mandate due to the importance, complexity, and difficulty to acquire, develop, and maintain the skills, experience, and knowledge required to conduct OSFI's activities.

In recognition of the need to improve the HR- Performance Management process and enhance its contribution to the organization, change initiatives were recently introduced at HR. These initiatives have positive aspects, notably enhancements to the performance management form, including the addition of learning plans to the form and the process. While these changes are positive and directionally appropriate, there are several other areas that need to be addressed to ensure that HR – PM meets its mandate more effectively. These include the following:
   o Formally establishing a Policy to be complied with,
   o Revisiting the "Guide" to ensure procedures and/or guidance including expectations, roles and responsibilities are appropriate, clear and formally established,
   o Effectively communicating to all employees and line managers how the process works,
   o Requiring mandatory training on performance management for all managers,
   o Ensuring job descriptions are available for all positions, and
   o Incorporating employee learning and development plans into the performance management process.

Human Resources, as guardian of the performance management process, should regularly assess the effectiveness of the process in meeting OSFI's objectives and managing people risk, by measuring results against predetermined standards and compliance with the Policy. Results from these periodic assessments should be reported to Executive and learnings should be incorporated into training programs to support continuous improvement in outcomes.

Our observations and recommendations are detailed in Section 5 of this report.

Audit & Consulting Services would like to thank all participants for their cooperation and contribution in the conducting of this engagement.

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Chief Audit Executive, A&CS   Date

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4. Management Response

We thank the audit team for both their collaborative approach and depth of review. While we are in agreement with the findings of the performance management audit, it is important to note that results of prior employee surveys and an increased focus on training and development prompted us to review the performance management process last year, ultimately concluding with a revision of the performance management form and the addition of learning plans to the form and process. We also heard from employee focus groups that more information and training needed to be provided on the performance management process itself, and its link to pay. We will be conducting this training in the latter part of this fiscal year.

We agree with the need for an improved internal control framework as identified in the audit report, such as the need to revise our performance management guideline and create a formal policy. We also recognize the need for a quality control and monitoring process, although we will need to find the right balance between monitoring and reporting, and the operational burden associated with this.

We are committed to addressing the recommendations outlined in the audit. As noted, a number of initiatives have already been undertaken to address some of the findings, and others will be addressed over the next 6-8 months.

5. Observations and Recommendations

5.1

Formal Performance Management (PM) Policy Framework

Observation: The main document governing Performance Management (PM) at OSFI is the Performance Management Guide ('Guide'). We noted that there is lack of clarity with regard to the force of this document (i.e. is it mandatory or not) and with regard to its true nature (i.e. is it a policy or just a guide).

We found several PM related documents available on OSFI net, for which we noted the majority is not dated and some are obsolete, as the contents do not properly reflect current practices. Without a formal comprehensive Performance Management Policy framework, there may be inconsistencies in the process followed to evaluate employees' performance, the handling of poor performers, as well as insufficient documentation to support performance rating decisions. As a result, employee morale and staff retention may become areas of concern that need to be addressed.

We noted the following;
o The roles and responsibilities of the various stakeholders, as listed in the PM Guide, are not well known, followed, or consistently interpreted or implemented.
o There is no defined process to ensure HR conducts reviews, at regular intervals, of the existing guide and procedures to assess their quality and relevance. We recognize however that HR is in the process of conducting a review of the performance evaluation form.
o There is no formally defined policy and/or procedure to deal with employee performance issues from beginning to end, including clear roles and responsibilities of stakeholders regarding steps to follow in a corrective action, and the drafting, retention and monitoring of required documentation.
o There is no clearly defined process or procedure for receiving and addressing non-unionized employee performance-related complaints, nor for escalating them.
o The Guide does not require reviews of employees' performance files or tracking and monitoring of related PM documentation to monitor adherence to the Guide requirements and to evaluate the PM process effectiveness.
o Access to employees' performance information is broadened to all HR staff, as this information is stored in a central area. Inappropriate access to employee's personal information could result in non-compliance with privacy rules.

5. 5. Observations and Recommendations, Continued

5.1

Formal Performance Management (PM) Policy Framework
(Cont)

Recommendation: The PM process should be governed by a Policy and supporting procedural documents that clearly indicate the mandatory requirements. The PM Policy needs to be developed with emphasis on the key activities of the PM process, as well as to promote fairness, transparency and consistency across the office. Attention should be paid to wording, so that any flexibility is explicitly identified in the Policy.

The new PM Policy should:
o Ensure roles and responsibilities of the various stakeholders in the PM process, including the PM Champion, are clear and formally established.
o Outline required measures for quality assurance of the PM process, to ensure policy is regularly reviewed for quality and relevance as well as to assess whether its requirements are clearly understood and implemented.
o Contain a distinct section outlining the steps to follow for dealing with poor performers and for improving performance.
o Contain a distinct section outlining the procedures to follow for addressing and for escalating employee complaints regarding their appraisals.
o Define the mechanisms to evaluate compliance with the PM process.
o Define the expectations for the objectives, scope and frequency of HR reviews to evaluate the effectiveness of the PM process.
o Restrict access to employee PM files and information to authorized individuals only.

5.2

Application of the Performance Management (PM) Policy Framework

Observation: The lack of clarity of the wording and the level of ambiguity in the Guide and related documentation has led to variation in staff interpretation and inconsistencies in its application.

We noted the following;
o There are no criteria for managers to follow to determine how much Key Responsibilities (KRs) should weigh vs. goals. Based on our file review, the weighting attributed to KRs and goals tends to be completely random and varies from one manager to the next.
o The Guide's intent is that Key Responsibilities are taken from the job description and should not change from year to year. However, staff and HR members confirmed that written, current job descriptions do not exist for all positions. As a result, Goal Commitment Documents often take the place of non-existent job descriptions.
o Each year, four behavioural competencies are selected from the competency model to include in the PM process. However, the Guide does not provide sufficient clarity/detail to explain the option of selecting between Behavioural and Technical competencies, so that both types are considered. Based on our file review we noted inconsistencies in the selection of competencies.

5. Observations and Recommendations, Continued

5.2

Application of the Performance Management (PM) Policy Framework (Cont)

o There are three rating scales, with different sets of definitions for each, and different weightings to attribute for key responsibilities, goals and competencies in the Goal Commitment Document. Because of the complexity of, and focus on, rating calculations at the year-end review, the application of "*numerics*" has become ineffective and is not achieving HR management's intended outcome.

o Performance assessment and performance pay are not clearly linked in the files reviewed.

o Based on discussion, HR's role is limited in situations where an employee files a complaint about his/her appraisal. HR usually advises employees to document their argument supporting why they do not agree with some or parts of their appraisal form. This document is then filed in the employee's file. However, we found no evidence of the eventual resolution on file.

o Although there were performance improvement plans in the relevant files reviewed, there was no evidence on file of progressive discussions and/or indication of any follow-up taking place before the year-end performance review. We noted that no specific training is provided to managers for dealing with poor performance. Although HR staff is available to assist managers upon request, these cases seem to be handled on an informal basis.

o There was no evidence that mid-year reviews were done on a consistent and timely manner. Based on discussions with HR and staff, the purpose of the mid-year review was not always clear with regard to its *force* (mandatory or not), *objectives* (to solely identify performance issues and/or to note changes in the employee's work plan due to circumstances or resources); and *scope* (to provide feedback to all OSFI's employees or only those who have performance issues).

5. Observations and Recommendations, Continued

5.2 **Application of the Performance Management (PM) Policy Framework** (Cont)	**Recommendation:** In order to effectively implement the PM framework, we recommend: o Performance Management requires a course of its own, which will allow for deeper learning, including specific training for the various steps in the process (i.e. setting expectations for KR, goals and competencies; mid-year and year-end reviews) and for managing poor performers. This training should be mandatory for newly-appointed and existing managers. o All jobs should have job descriptions since they serve as a key foundation for many different HR processes, including compensation system design, job classification group/level, recruitment, and performance management. o The purpose of the mid-year review with regard to its force, objectives and scope should be clarified. HR should monitor that mid-year reviews are held when they should be, and that the results (i.e. positive or negative feedback and/or corrective action to be taken and/or training needs) of the mid-year reviews are documented in the appropriate format and signed-off by manager and employee. o Develop formal criteria to support management in the evaluation of employee performance achievements that clearly link to performance pay.
5.3 **Management Oversight**	**Observation:** Management oversight controls related to information, communication, and monitoring are not adequately built into the performance management process. We noted the following; o Setting individual performance expectations begins with the establishment of OSFI's business plans and related priorities for the organization. These are translated into sector and divisional goals that will contribute to the business plan and the achievement of OSFI's objectives. After the divisional goals have been communicated, employees and managers meet to identify and agree on individual goals for the year. The management call letter requires GCDs to be completed by the first month of the fiscal year, however staff experience delays in receiving the formal communication of corporate goals and priorities, which have significantly impacted the timely issuance of the Goal Commitment Documents (GCD). As a result, employees may be working without having clarity on objectives and priorities.

5. Observations and Recommendations, Continued

5.3

Management Oversight
(Cont)

o At the end of each PM cycle, the Sector Management teams review all preliminary employee performance ratings for consistency reasons. However, open communication about this process, which is critical to instill confidence in the performance process, is lacking.

o HR does not conduct reviews of the PM process to evaluate its quality and effectiveness. The last review on record was done in 2003/04 performance cycle. Based on discussion with HR representatives and review of documentation, the transfer of knowledge and accountability for the past review of the PM process, or any previous or subsequent one, were lacking.

o HR's tracking and monitoring of the submission of PM related documentation and timelines by managers as required by HR in the Call Letter is minimal. As a result, HR would not be able to identify and follow-up on outstanding PM related documentation for any given PM cycle.

o Although risk assessment in Corporate Services Sector is conducted at a high level, we are unclear as to whether there is a formal risk management process in place to identify, assess, monitor, and report PM specific risks.

Recommendation: In order to ensure that the PM policy framework is effectively implemented, management oversight controls need to be strengthened, including:

o The process for "cascading down" the corporate goals and priorities should be revisited to ensure managers are provided with the necessary information to comply with the call letter timelines.

o Line managers should be held accountable for their people-management responsibilities. These responsibilities should be outlined in their own performance appraisals, so that managers can be evaluated on their people management skills in their related responsibilities, goals, and competencies.

o Communication from Senior Management to all OSFI managers and employees about how the PM process works needs to be clear and open in order to promote fairness, consistency, transparency and instill confidence in the PM process.

o The HR Division, as the key guardian of the PM system, should conduct periodic reviews to evaluate its effectiveness by measuring outputs and results against pre-determined standards and in monitoring performance trends. These reviews will enable HR to identify specific PM areas that are cause for concern and need to be addressed or where managers, newly-appointed and/or existing, require training.

5. Observations and Recommendations, Continued

5.3 **Management Oversight** (Cont)	o Similarly, HR representatives should be held accountable for the quality of their monitoring, review and reporting on the PM process, including knowledge transfer practices. Their performance on these responsibilities should be evaluated in their own performance appraisal. o HR - Performance Management specific risks should be periodically reviewed and that mechanisms be put in place to help management periodically assess whether controls appropriately mitigate risks identified.
5.4 **Skills Development and Career Planning**	**Observation:** The identification of development and learning requirements is not a formalized process and is not part of the performance management process as recommended by the Guide. We noted the following; o While the main output of the PM process is a performance appraisal review between a manager and his/her direct report, the process does not appear to identify employee skill, competency, and behaviour gaps, if any, between what is expected and what the employee brings to his/her job. Without this picture in hand, employees will not be able to improve their performance in their current role, or build career development plans that better prepare them for a future role of interest, or both. o HR does not conduct periodic follow-up reviews of completed appraisal forms so that trends in employees' performance can be analyzed and learnings, if any, can be incorporated into training programs. Consequently, HR may not be able to identify specific areas where OSFI employees may need training or support. **Recommendation:** Employee training and development should be integral parts of the performance management process to ensure a systematic and disciplined approach is consistently applied throughout the organization. There should be a plan for developing employees so that they can naturally grow through the organization and that jobs can continue whenever someone leaves. The organization's succession plan may provide input for employee development plans. As a result, management needs to ensure the following: o Identification of learning requirements for the current role, as well as future career development planning needs should be completed during the performance management process. It should identify current skills gaps and personal career goals over the short and long term so that required educational qualifications, skills, and competencies can be attained and the appropriate personal career opportunities can be identified.

Appendix A – Performance Management Control Criteria

Elements	Components
Governance: • PM Policy Framework	▪ PM related policies and procedures exist and are appropriate, are regularly reviewed, assessed for quality, and are updated. ▪ Role, responsibility, and accountability of the various stakeholders in the overall PM process are clearly documented in the framework and are consistently followed. ▪ PM related policies clearly outline required measures for quality assurance of the PM process. ▪ Criteria used to evaluate performance achievements and merit are clearly established and communicated to OSFI's managers and employees. ▪ Links between performance assessment and performance pay and merit are formally established, transparent and clearly communicated to OSFI staff. ▪ Framework includes a written policy / procedure for progressive discipline / corrective action to deal with employee performance issues. ▪ Framework includes a clearly defined process and procedures for receiving and addressing employee performance complaints to ensure disputes are promptly and properly resolved, incl. mechanism to escalate performance issues. ▪ Framework includes a clearly PM defined calendar, deliverables and control points. ▪ Mechanisms are in place to identify, enforce and monitor adherence to the framework and collective agreements, where applicable, on a regular basis and take timely and appropriate action, as required.
Governance: • Management Oversight	▪ Management oversight activities are built into the process and performed in the ordinary course of running the business, such as formally setting the overall business strategy and the annual corporate goals and ensuring that the latter cascades down to the work units and subsequently to managers and employees in a clear and timely manner. ▪ There is a clear process of annual review at the corporate, work unit, and individual level to evaluate achievements in relation to the priorities/ goals set, identify areas for improvement, and develop plans. ▪ There is an updated organizational chart for each part of the organization. ▪ There is a master list of each job in the organization indicating its status. ▪ There are job descriptions available for each position in the organization. ▪ Managers are held accountable for completing all required steps of the PM process for their direct reports. Further, HR tracks and monitors PM process deliverables due dates and notifies managers, as required. ▪ HR periodically reviews performance ratings and supporting documentation for inconsistencies, as well as trends in performance across the office, and formally reports results to Senior Management. ▪ The PM process (particularly the Sector Peer Review) is open and transparent, and the flow of information is complete, adequate, reliable and timely. ▪ Employee surveys are periodically conducted (at an appropriate frequency) to help management identify and address areas that may require improvement.

Elements	Components
Governance: • Skills Development & Training	• The organization provides employees with the necessary tools, training, resources and information to support the discharge of their responsibilities. • Adequacy of the knowledge, skills and experience of management and HR staff needed to perform assigned tasks related to their HR responsibilities and accountabilities. • Key PM-related roles and responsibilities within HR have been identified, knowledge transfer practices are adequate, and sufficient back up exists amongst HR representatives to ensure a smooth, continuous management of HR's PM related responsibilities. • Key core management / leadership competencies for organizational success have been identified and described, and adequate training is available for managers (new and existing) to develop their people management skills. • Performance reviews emphasize action plans for positive improvement for both, those who meet or exceed their goals and/or competencies and those who do not. Consequently, a personal learning plan that links job skills to training opportunities is part of the annual performance review of each employee. • Results of HR's periodic reviews of completed performance management documentation, and the results of trend analyses in performance management across the office, feed into training programs as appropriate.
Control Processes: • Application of the Policy Framework	• PM related policies and related tools and templates to assist managers in their HR responsibilities are accessible, are applied as intended and consistently. • Employees are provided with ongoing performance feedback and coaching. • HR procedure in place to deal with employee performance-related complaints ensures that: employee disputes are promptly and properly resolved and "expert" resources to investigate and resolve these complaints are accessible to all OSFI employees. • There is a regular senior management review of the nature and resolution of complaints to ensure that PM-related policies are followed consistently. • HR procedure in place to deal with employee performance issues ensures that: sample templates for progressive discipline/ corrective action are compliant with applicable employment legislation; managers timely and properly document steps taken to improve employee's performance and employee acknowledgment is properly documented; employees are informed of their rights and responsibilities when subject to disciplinary / corrective action; employees are regularly coached on how to improve performance and progress discussions are properly documented; and HR, working alongside line managers, tracks all employees on formal performance improvement plans and monitors deadlines. • HR conducts periodic reviews of completed PM documents to assess the quality of content (i.e. key responsibilities are relevant to the job, goals are realistic and measurable, competencies are related to business objectives, etc) and documentation of performance in order to ensure process is transparent, fair and consistently applied across OSFI. • Access to employee PM files and information is limited to authorized individuals and provided on a "need-to-know" basis to ensure confidentiality of personal information is maintained.
Risk Management	Management identifies HR-PM specific risks and periodically assesses whether current controls appropriately mitigate those risks.