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# List of Acronyms and Abbreviations

AAP	Automated Accounts Payable
CFOB	Chief Financial Officer Branch
EBP	Employee Benefits Plan
Gs&Cs	Grants and Contributions
ICFM	Internal Controls over Financial Management
OCAE	Office of the Chief Audit Executive
O&M	Operations and Maintenance
OGD	Other Government Department
PAYE	Payable at Year End
PCH	Department of Canadian Heritage
RMD	Resource Management Division
TBS	Treasury Board of Canada Secretariat

# 1.0 About the Review

## 1.1 Background

The Department of Canadian Heritage (PCH or the Department) plays a vital role in the cultural, civic, and economic life of Canadians. Arts, culture, and heritage represent more than \$57 billion in the Canadian economy and close to 673,000 jobs in sectors such as film and video, broadcasting, music, publishing, archives, performing arts, heritage institutions, festivals, and celebrations.

As part of the Department's Risk-based Audit Plan, the Office of the Chief Audit Executive (OCAE) engaged the services of an external firm to conduct a targeted Review of Accounting Estimates and Methodology.

## 1.2 Objective and Scope

The overall objective of the review is to assess PCH's accounting estimates and methodology and determine if they are designed and operating effectively.

The scope of this review was limited to the year-end accounting estimates and methodologies related to the following types of estimates:

- Vacation and Compensatory Time, Severance Benefits and Doubtful Accounts; and
- Payables at Year-end (PAYE) for Salaries, Transfer Payments and OGD related costs.

The scope period will be fiscal year 2022-2023 whereby a sample of estimates was selected for further analysis and testing.

## 1.3 Approach and Methodology

To support the assessment of the processes, controls, and methodologies in place to support accounting estimates, the review team developed and reviewed activities for each relevant lines of inquiry of the review and ensured comprehensive coverage by the engagement. The review included, but was not necessarily limited to, gathering, and examining documentation, guidelines, procedures, and policies; obtaining data and information through interviews and data requests; and conducting walkthroughs and analysis of key processes and controls. They included, but were not limited to:

- Complete a qualitative and quantitative current state analysis and assessment of the accounting estimates and methodology to identify the potential impacts of any gaps found;
- Sample selection and testing of accounting estimates to verify that the procedures and policies are consistently followed. (i.e., Payables at Year-End (PAYE), Year-end Vacation Liability, and Employee Future Benefits);
- Review the accounting estimates methodology at PCH; and
- Provide recommendations on how to improve the design and operating effectiveness of the accounting estimates methodology.

## 2.0 Key Findings & Recommendations

The key findings and recommendations for the accounting estimates review are thematically grouped in the report to provide clear categorization. The thematic categorization provides an overarching framework for grouping and linking findings with their corresponding recommendations.

The review established the following four (4) thematic categories of findings, two (2) of which have corresponding recommendations indicated by: Procedures & Training; Information Management & Performance Monitoring; Verification Strategy; and Testing.

### 2.1 Procedures & Training

Key Findings & Observations	Recommendations
<ul style="list-style-type: none"> <li>● Procedures for the year-end vacation and compensatory time, employee benefits and doubtful accounts estimates are detailed, well documented and align with TBS guidelines.</li> <li>● Procedures for year-end pension and severance estimates are defined by the TBS and effectively followed.</li> <li>● Procedures for creating non-Gs&amp;Cs PAYEs estimates provide clear guidance, instruction, and templates.</li> <li>● Procedures for creating Gs&amp;Cs PAYEs estimates provide the key dates and templates, however there is a lack of concrete procedures and guidance for these accounting estimates.</li> <li>● Annual training is made available to Resource Management Directorates (RMDs) through CFOB. RMD feedback is positive. However, training requirements are not mandatory for RMD staff.</li> <li>● Procedures and training primarily focus on the creation of accounting estimates (i.e., RMD and client focused), however, generally do not describe verification, validation and/or monitoring activities (i.e., CFOB responsibilities)</li> <li>● RMD generally takes the lead on the development of year-end accounting estimates. Program Managers review and validate RMD generated estimates.</li> <li>● Knowledge relating to what expenditures qualify as a PAYE and when the year-end accounting estimate procedures should be applied was found to be inconsistent.</li> <li>● Guidance on year-end procedures for transfer payment recipients was not present.</li> <li>● Generally, the year-end accounting estimates follow a standard of procedures that align with TBS guidelines, best practice standards, and demonstrate a high degree of reasonableness.</li> <li>● Training for year-end accounting estimates is detailed and provides RMD with satisfactory guidance on the preparation of year-end accounting estimates, however, guidance with respect to supporting evidence for PAYEs for Gs&amp;Cs could be improved.</li> </ul>	<p>The Chief Financial Officer should review existing training materials and processes developed and delivered by CFOB with the goal of identifying/validating gaps in knowledge delivery and implement the requisite improvements.</p>

## 2.2 Risk Management & Performance Monitoring

Key Findings & Observations	Recommendations
<ul style="list-style-type: none"> <li>• Documented procedures include annual data analytics for all Automated Accounts Payable transactions and PAYEs. High level variance analysis (i.e., Year-over-year) is performed.</li> <li>• Transactional level analyses for PAYEs (i.e., estimate to actual) are performed and/or tracked.</li> <li>• Internal critical errors are being tracked and reported with varying degrees of consistency (i.e., Good for Operations and Maintenance (O&amp;M) and Salaries, inconsistent for Gs&amp;Cs)</li> <li>• Inconsistent tracking of payments and settlements for PAYEs.</li> <li>• Internal Controls over Financial Management (ICFM) monitoring framework and plans are designed to support departmental level reporting and does not speak to controls at the year-end accounting estimates level. However, the design of financial management controls and a sample of transactions related to PAYES can be tested during ICFM assessments of pay administration, grants and contributions, or financial close business processes. The level of risk influences the scope of work of such ICFM assessments.</li> <li>• Ultimate accountability for financial reporting rests with the CFOB, however, it has limited access to source documentation supporting PAYE requests.</li> </ul>	<p>The Chief Financial Officer should assess the extent to which additional risk mitigation strategies specific to year-end accounting estimates would be effective in meaningfully decreasing residual risks.</p> <p>The Chief Financial Officer should conduct an annual variance analysis of PAYE estimates to actuals and develop processes/procedures to effectively monitor and reconcile “long-term” PAYEs.</p>

## 2.4 Verification Strategy

Key Findings & Observations	Recommendations
<ul style="list-style-type: none"> <li>• At a high-level, the Account Verification Strategy focuses on assessing accuracy of payments and settlements and ensuring that transactions are approved following the appropriate policies and guidelines.</li> <li>• Effectively aligns with Treasury Board guidelines/directives.</li> <li>• Includes a risk-based approach and effectively supports risk management practices.</li> <li>• Account verification and sampling strategy is detailed and documented.</li> <li>• Account verification strategy is updated annually and is aligned with the annual risk assessment.</li> <li>• PAYE signoff authority is validated via internal check system.</li> <li>• Transactional level analyses for PAYEs (i.e., estimate to actual) are performed as per the strategy in place for high risk and low risk non-salary and transfer payment transactions.</li> <li>• Not intended to measure accuracy of accounting estimates (i.e., budget to actual).</li> </ul>	<p>None</p>

## 2.3 Substantive PAYE Testing

### Key Findings & Observations

#### 1. PAYE Submission Forms

- Overall, 76.4% of PAYE samples had corresponding submission forms that met all assessment criteria.
- 17.6% of PAYE samples had submissions were signed after the due date. (These were viewed as acceptable because they were not received after the CFOB “internal” deadline.
- 6% of PAYE samples had submissions which did not use the expected template.
- CFOB uses an internal verification system to confirm that the signing individual has proper Section 33/34 signoff authorization.

#### 2. PAYE Amount

- PAYE amounts in the accounting system reconciled with the amounts approved on the PAYE Submission Forms for 100% of the Gs&Cs, O&M, OGD Salary, and PCH Salary samples.
- Submission of amounts for the G&Cs are verified against the remaining contract amount, but recipient-based validation is limited.
- Employee Benefit Plan (EBP) expenditures are reflected in the year end accounting estimates (i.e., Statement of Operations) which aligns with TBS guidelines about EBP inclusions.
- EBP is included in PAYE amounts (i.e., OGD salaries) demonstrating alignment with TBS guidelines.

#### 3. Supporting Documentation

- Supporting documentation for PAYE estimates was received for 100% of the samples selected.
- 97.1% of the supporting documents received reconciled with the PAYE submission form.
- Supporting documentation for all non-Gs&Cs PAYEs met expectations. However, Gs&Cs supporting documentation was noted to lack recipient details outlining the satisfactory completion of their obligations.
- Supporting documents are not kept in centralized database (i.e., CFOB does not have direct access. Generally, kept with RMD).

#### 4. Reconciliation

- Corresponding invoices/supporting documentation were present for 67% of all samples categories excluding Gs&Cs.
- 100% of invoices/supporting documentation which was received reconciled with the corresponding PAYE amounts.
- Variance analysis performed compares the year-over-year estimates, however, no variance analysis is performed to examine the accuracy of accounting estimates to actuals.
- Inconsistent tracking of payments and settlements.



## 3.0 Maturity Model Assessment

To assess the maturity of the end of year accounting estimates process, the **Business Process Maturity Model (BPMM)** was applied. It provides a structured approach to assess, optimize, and continually improve business processes. This model outlines evolutionary stages of process maturity, guiding organizations from ad-hoc activities to fully optimized processes.

With the application of this model, the review team concluded that based upon the key attributes of the five (5) levels of process maturity, the Accounting Estimates and Methodology Process is most appropriately classified at a maturity of: **Level 3 – Standardized**.

### 3.1 Key Maturity Assessment Highlights

The accounting estimates process largely performs to a degree of excellence which merits a classification as a Standardized process. However, the assessment noted that criteria is not always met, which in turn contributes to the current limitations the process experiences that prevent it from being classified in a higher-level category.

The below are key findings contributing to the level 3 rating:

- Consistent training is provided of employees in the form of annual training.
- Usually, consistent execution of the process – inconsistent respect for PAYE due dates.
- Standardized tools and methodologies for most aspects of the process.
- Largely manual process (minimal automation).
- Defined roles and responsibilities.
- Absence of quantitative performance monitoring of the process.
- There is only a high-level understanding of reasons driving variations in the process.
- Procedures are well documented – Gs&Cs lacks concrete procedures and guidance.
- Procedures align with best practices – guidance for transfer recipients was not present.

## 4.0 Conclusion

Based on the review conducted on PCH’s accounting estimates and applicable methodologies, the team concluded that the accounting estimates process was functioning as designed and met the expectations established by the review criteria. The process was generally effectively utilizing standardized tools such as document templates and had well defined roles and responsibilities within the process. Additionally, the processes in place and methodologies applied performed at a mostly consistent level of execution with some inconsistencies with respect to PAYEs. There are some areas improvement opportunities identified to address minor gaps in training and establish a foundation for which PCH may develop tools and practices that encourage continuous process improvement and optimization.

## Statement of Conformance

In my professional judgment as Chief Audit Executive, this review was conducted in conformance with the Institute of Internal Auditors' International Standards for the Professional Practice of Internal Auditing and with the Policy and Directive on Internal Audit of the Government of Canada, as supported by the results of the quality assurance and improvement program. Sufficient and appropriate review procedures were conducted, and evidence gathered, to support the accuracy of the findings and conclusion in this report. The findings and conclusion are based on a comparison of the conditions, as they existed at the time, against pre-established review criteria that were agreed with management and are only applicable to the entity examined and for the scope and time period covered by the review.

Original signed by

**Bimal Sandhu**

Chief Audit Executive

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With the assistance of resource from Raymond Chabot Grant Thornton.

## Appendix A - Risk Assessment

Conclusion	Definition
Well Controlled	Well managed and effective. No material weaknesses noted.
Controlled	Managed and effective. Minor improvements are needed.
Moderate Issues	Requires management focus (at least one of the following criteria are met): <ul style="list-style-type: none"> <li>Control weaknesses, but exposure is limited because likelihood of risk occurring is not high.</li> <li>Control weaknesses, but exposure is limited because impact of the risk is not high.</li> </ul>
Significant Improvements Required	Requires immediate management focus: At least one of the following three criteria are met: <ul style="list-style-type: none"> <li>Financial adjustments material to line item or area, or to the Department.</li> <li>Control deficiencies represent serious exposure.</li> <li>Major deficiencies in overall control structure.</li> </ul>

Review Criteria	Rating
<b>1. PAYE Supporting Documentation</b> The PAYE supporting documentation presents opportunities for improvement for the validation and proper reconciliation of PAYEs.	2
<b>2. Variance analysis performed (i.e., validation of the estimates)</b> Currently there is a high-level year-over-year analysis of the estimates, however, no variance analysis is performed comparing actuals to estimates. The absence of such an analysis limits the ability for PCH to develop a strong understanding of the accuracy of the accounting estimates.	3
<b>3. PAYE Submission Form: the creation of PAYEs correctly follows PAYE policies and procedures</b> Numerous instances of PAYE submissions being signed after the designated deadline; however, it is understood that there is a late allowance incorporated into the written due date.	2
<b>4. PAYE Reconciliation: invoiced amounts match recorded PAYE amounts</b> When invoices are present the invoiced amount always matches the recorded PAYE amount. However, there are instances of the total invoiced amounts exceeding the PAYE amounts. Because a number of invoices contain multiple items not relevant to the PAYE, which increase the difficulty of accurately tracking invoice documents that correspond to a PAYE.	1
<b>5. Reasonableness of the year end accounting estimates</b> Policies and procedures for the year end accounting estimates are reasonable, adhere to both TBS guidelines and industry standards, and are well documented. However, documents are not store centralized which inhibits ease of access.	1
<b>6. PAYE Amounts submitted match the recorded amount in the accounting system</b> PAYE amounts recorded in the accounting system consistently match the amounts recorded in the PAYE submission form, the controls in place effectively mitigate risk.	1
<b>7. Errors are detected, reported, and tracked</b> Critical errors are detected, reported, and tracked.	1

## Appendix B - Management Action Plan

Recommendation	Management Assessment and Actions	Responsibility	Target Date
<p>The Chief Financial Officer should review existing training materials and processes developed and delivered by CFOB with the goal of identifying/validating gaps in knowledge delivery and implement the requisite improvements.</p>	<p>The CFOB will review its current training curriculum and standards for gaps and improvements identified in this review.</p> <p>The CFOB will better explain the definition of a PAYE in the future training session and training material to better educate the different stakeholders.</p> <p>The CFOB will highlight its PAYEs validation process in the year-end training material, including the retention of supporting document as part of the mandatory training for RMDs.</p>	<p>Director, Accounting Operations and Financial Policies</p>	<p>March 2024</p>
<p>The Chief Financial Officer should assess the extent to which additional risk mitigation strategies specific to year-end accounting estimates would be effective in meaningfully decreasing residual risks.</p>	<p>CFOB will review its internal controls over year-end accounting estimates within the Financial Close process to assess the effectiveness of its risk-based approach and the need for modification.</p>	<p>Director, Accounting Operations and Financial Policies</p>	<p>July 2024</p>
<p>The Chief Financial Officer should conduct an annual variance analysis of PAYE estimates to actuals and develop processes/procedures to effectively monitor and reconcile “long-term” PAYEs.</p>	<p>CFOB has a monitoring/reconciliation process that is undertaken in December (Period 9) with respect to the materialization of PAYEs. CFOB will document the process and leverage it to develop a risk-based monitoring approach that will reconcile transactional-level PAYEs.</p>	<p>Director, Accounting Operations and Financial Policies</p>	<p>November 2024</p>