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2010-715 Audit (consisting of specified forensic audit procedures) of Expenditures under the SNC-Lavalin O&M Contracts

PricewaterhouseCoopers LLP

*Public Works and Government Services Canada
Contract No. EN790-104291/001/ZQ*

January 24, 2011

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Introduction and Background

1. Public Works and Government Services Canada (“PWGSC”), as custodian of approximately 320 federal government buildings (the “Buildings”), was the subject of a media article released on March 10, 2010, in which the reasonability of seven financial transactions was questioned.
2. The media obtained the information with respect to the seven transactions through a request pursuant to the Access to Information Act.
3. We have been advised by PWGSC that on November 22, 2004, PWGSC awarded SNC - Lavalin O&M Inc. (“SNC O&M”) eight (8) contracts for the maintenance and upkeep of the Buildings (the “SNC Contracts”). The transactions outlined in the media article were in relation to payments made by PWGSC to SNC O&M for the seven transactions (the “Transactions”).
4. In response to the Transactions outlined in the media article, the Minister of Public Works and Government Services, Ms. Rona Ambrose, ordered a review of the Transactions as well as a broader examination of the SNC Contracts to determine if costs charged appear to be reasonable and supportable and whether there is any evidence of systemic problems.
5. On April 22, 2010, through a competitive bidding process, PWGSC awarded PricewaterhouseCoopers LLP (“PwC”) contract number EN790-104291/001/ZQ (the “Contract”) to provide forensic audit services to assist PWGSC’s Office of Audit and Evaluation (the “OAE” or the “Project Authority”) in an independent multi-phased audit consisting of specified forensic audit procedures on the expenditure transactions made by SNC O&M on behalf of PWGSC as both custodian and tenant and also on behalf of other government department as tenants. Phase 1 of the Contract, which is the subject of this report (this “Report”), is to conduct specified forensic audit procedures with respect to the Transactions and provide an opinion with respect to the reasonability and supportability of the expenditures examined.
6. All other work requested of us by PWGSC as set out in the Contract (and related contract amendments) will be reported on separately, once completed.
7. The purpose of this Report is as follows:
 - to present the results of our work on the Transactions, including the conclusions reached in relation to the supportability and reasonability of the Transactions (Chapter 1); and

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- to present observations and recommendations as a result of our examination of the Transactions (Chapter 2).
8. Our Restrictions and Qualifications, which must be read in conjunction with this Report, are attached to each Chapter as Appendix 1-A and 2-A.



Chapter 1- Phase 1- Seven Transactions

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Introduction and Background

1.1 As noted in paragraphs 1 through 8 of the Introduction and Background to this Report, PWGSC awarded PwC the Contract to conduct an audit, consisting of specified forensic audit procedures.

1.2 The work for Phase 1 of the Contract required the following:

- i. Conduct specified forensic audit procedures with respect to the Transactions; and
- ii. Provide an opinion with respect to the reasonability and supportability of the expenditures examined.

1.3 The Transactions and their costs, as published in the media article, are summarized below:

<u>Transaction</u>	<u>Description</u>	<u>Amount</u>	<u>Additional Details</u>
1	Purchase of Two Plants and Two Pots	\$1,948.72	<ul style="list-style-type: none">• Purchase of two tropical plants:<ul style="list-style-type: none">▪ Cycas revolute approx. 3' to 3.5' tall; and▪ Yucca elephantipes approx. 6.5' to 7' tall.• Purchase of two pots with sub-irrigation system and liner.• Inspection certificate and delivery.• Maintenance costs for nine months.
2	Installation of Three Blinds	\$1,414.95	<ul style="list-style-type: none">• Supply and install three Altex Sheerweave 4400 3% grade blinds with chain control system.• Blind dimension as follows:<ul style="list-style-type: none">▪ 2 blinds: 24.75" width by 108" height; and▪ 1 blind: 61.25" width by 86" height• Remove the current blinds.

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<u>Transaction</u>	<u>Description</u>	<u>Amount</u>	<u>Additional Details</u>
3	Installation of Door Bell	\$1,000.41	<ul style="list-style-type: none"> • Supply of a doorbell, transformer and chime. • After hours installation of above material and dedicated circuits. • Clean-up of the site.
4	Removal of Exit Sign	\$256.22	<ul style="list-style-type: none"> • Electrical services to disconnect electrical connection to Exit Sign. • Removal of both the cabling and the Exit Sign. • Repair the ceiling. • Clean-up of the site.
5	Installation of Six Pot Lights	\$5,266.80	<ul style="list-style-type: none"> • Purchase of materials including six pot lights, one dimmer switch and cabling. • After hours installation of above material and dedicated circuits. • Clean-up of the site.
6	Removal of Light Switch	\$1,000.41	<ul style="list-style-type: none"> • Removal of light switch from a wall. • Re-connection of lights to electrical junction box located approximately 15 feet away.
7	Extra Cleaning Services of the Minister and Deputy Minister's Offices	\$18,650.87	<p>Additional extra cleaning services, during a six month period, for floors 17A1 and 18A1 of Place du Portage, Phase III at 11 Laurier Street, Gatineau, Quebec:</p> <ul style="list-style-type: none"> • Dust all surfaces (tables, desk, cubicle partitions); • Collect all garbage and recycling; • Clean the bathrooms; and • Vacuum the carpets.

1.4 The media obtained the information with respect to the Transactions through a request pursuant to the Access to Information Act.

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- 1.5 The Transactions outlined in the media article are in relation to payments made by PWGSC to SNC O&M, pursuant to the SNC Contracts, for the Transactions.
- 1.6 In response to the Transactions outlined in the media article, the Minister of Public Works and Government Services, Ms. Rona Ambrose, ordered a review of the Transactions as well as a broader examination of the SNC Contracts to determine if costs charged appear to be reasonable and supportable and whether there is any evidence of systemic problems.
- 1.7 The purpose of this Chapter of this Report (“Chapter 1”) is to present our Phase 1 opinion with respect to the reasonability and supportability of the Transactions.
- 1.8 Our Restrictions and Qualifications, which must be read in conjunction with this Chapter, are attached hereto as Appendix 1 - A.
- 1.9 Our working papers, containing our detailed procedures and analysis, in support of our findings and conclusions outlined in this Chapter (the “Working Papers”) have been provided separately to the Project Authority.
- 1.10 In addition, during the course of the audit, consisting of specified forensic audit procedures, certain matters came to our attention, such as the need for improved documentation and the need to increase the frequency of cost audits, which merited the attention of PWGSC. These observations/findings along with our recommendations are described in Chapter 2 of this Report, entitled Phase 1 - Observations and Recommendations.

Scope of Engagement

- 1.11 Under the terms of Phase 1 of the Contract, PwC was required to perform the following:
- i. Review background documentation provided by PWGSC;
 - ii. Prepare a work plan with timelines to PWGSC for approval;
 - iii. Obtain an understanding of the process used by SNC O&M to award and oversee work;
 - iv. Develop criteria to appropriately measure whether the expenditures with respect to the Transactions are reasonable and supportable;
 - v. Assess the Transactions against the developed criteria to conclude whether or not the expenditures are reasonable and supportable;
 - vi. Provide regular updates to PWGSC, on the progress of the audit, consisting of specified forensic audit procedures, and/or any significant findings; and
 - vii. Report and present the opinion and findings, with respect to the reasonability and supportability of the Transactions, to PWGSC Senior Officials including the Audit and Evaluation Committee.
- 1.12 We received PWGSC's full co-operation and assistance while conducting our procedures throughout Phase 1 of the Contract.
- 1.13 The purpose of this Chapter of this Report is to provide PWGSC with our opinion in relation to the reasonability and supportability of the Transactions.
- 1.14 Our work was executed in accordance with the Canadian Institute of Chartered Accountants standards detailed in the Standard Practices for Investigative and Forensic Accounting Engagements.
- 1.15 The findings presented in this Chapter of this Report are based solely on information provided to us by PWGSC and their representatives, SNC O&M and their representatives, SNC O&M's subcontractors and their representatives, and other service/product suppliers (see Restrictions and Qualifications set out in Appendix 1 - A).

Scope of Examination

1.16 We list below the sources of information we relied upon to conduct our work. Our approach is explained in paragraphs 1.29 and 1.30 of this Chapter.

- i. PWGSC's Alternative Forms of Delivery Tenant Service Call-Ups (the "AFD Work Order"); SNC O&M invoices; Process for Tenant Direct Projects between PWGSC's Corporate Accommodation ("Corporate Accommodation") and SNC O&M; and, other supporting documentation gathered by PWGSC with respect to the Transactions (see paragraphs 1.17 through 1.28 of this Chapter for scope limitation);
- ii. SNC O&M's subcontractor (the "Subcontractors") invoices, cost quotes, purchase orders, cancelled cheques and other supporting documentation gathered by SNC O&M with respect to the Transactions (see paragraphs 1.17 through 1.28 of this Chapter for scope limitation);
- iii. Other supporting documentation gathered by the Subcontractors with respect to the Transactions (see paragraphs 1.17 through 1.28 of this Chapter for scope limitation);
- iv. Correspondence gathered by PWGSC, SNC O&M and certain of the Subcontractors with respect to the Transactions;
- v. Cost estimates and correspondence from suppliers not involved in the Transactions;
- vi. Gatineau Portfolio Contract for Project Management Services ("PM Services"), Project Delivery Services ("PD Services") and Optional Services, including the Statement of Work (the "SoW"), executed between PWGSC and SNC O&M with an operational start date of April 1, 2005, and authorized change deviations and contract amendments in effect from April 1, 2005 to March 22, 2010 (the "GP Contract"), as provided by PWGSC;
- vii. Statement of Contract Costs as audited by SNC O&M's auditors, Deloitte & Touche LLP (the "Auditors"), with respect to the GP Contract for the fiscal years 2005/06 to 2009/10;
- viii. Audit Service Canada's Auditors Report ("ASC Reports") with respect to the 2005/06 fiscal year-end audits performed for the Pacific Portfolio, Ottawa Perimeter Portfolio and Quebec Portfolio;
- ix. PWGSC's Office of the Chief Risk Officer's report dated July 18, 2007; and

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- x. Interviews and discussions were conducted with the PWGSC employees from within PWGSC's Real Property Branch ("RPB") (custodian and the SNC Contracts' project authority); Acquisitions Branch (contracting authority); and, Corporate Services, Policy and Communications Branch (tenant services). Interviews and discussions were also conducted with SNC O&M employees and the five (5) Subcontractors involved in the Transactions. Pursuant to PWGSC's request, the names of the PWGSC employees, the SNC O&M employees and the five (5) Subcontractors will not be disclosed in this Report. These names are contained within the Working Papers which have been provided separately to the Project Authority.

Scope Limitation

1.17 We note in the paragraphs that follow certain limitations regarding the scope of our work as well as limitations of the information gathered in relation to our scope of work.

1.18 For the purpose of this Chapter, we define the following terms:

- i. Reasonable – the cost component for the Transaction meets all of the reasonability criteria as detailed in paragraph 1.37; and
- ii. Supportable – the cost component for the Transaction meets all of the supportability criteria as detailed in paragraph 1.37.

1.19 We examined the documentation provided to us and attempted to verify where possible the completeness of that documentation.

1.20 PWGSC advised us that on November 22, 2004, PWGSC awarded the SNC Contracts for the maintenance and upkeep of the following eight (8) regional portfolios:

- i. Atlantic Portfolio;
- ii. Quebec Portfolio;
- iii. Ontario Portfolio;
- iv. Gatineau Portfolio;
- v. Downtown Ottawa Portfolio;
- vi. Ottawa Perimeter Portfolio;
- vii. Western Portfolio; and

viii. Pacific Portfolio.

- 1.21 We have been advised by PWGSC and SNC O&M that the terms and conditions of the SNC Contracts with respect to the above noted portfolios are similar in nature. Recognizing that the Transactions all occurred in the Gatineau Portfolio, for the purposes of Phase 1 and this Chapter, we only examined the GP Contract.
- 1.22 We performed site visits relating to six (6) of the Transactions to inspect the area where the goods/services were purported to have been supplied/rendered by the Subcontractors. As the removal work was reported to have been completed, we could not inspect the work done with respect to the removal of the Exit Sign (Transaction #4) and the removal of the light switch (Transaction #6). PWGSC showed us the general location where the sign and wall were respectively located prior to their removal. With respect to certain of the electrical work, we did not request that walls or ceiling tiles be opened to inspect the installation/removal of various materials i.e. transformer, electrical conduit, and electrical workings (Transaction #3, #4, #5 and #6).
- 1.23 The Financial Administration Act (“FAA”) requires that no payment shall be made for any goods or services provided to the government of Canada unless an authorized person provides certification pursuant to Section 34 of the FAA (“S.34 FAA”). We relied on PWGSC’s certification pursuant to S.34 FAA confirming that the work has been performed, the goods were supplied and the price charged is according to the AFD Work Order.
- 1.24 For the purpose of this Chapter, we have examined selected accounting records and data as necessary to support our work in relation to our mandate of assessing the reasonability and supportability of the Transactions.
- 1.25 Our procedures and findings reported on herein relate only to the Transactions we were asked to review. We cannot comment on whether the Transactions are representative of a larger population of transactions.
- 1.26 We have not, as it is not part of our mandate, reviewed PWGSC’s specific internal controls regarding the administration and payments governed by the GP Contract. We understand that the OAE commenced a review of PWGSC’s monitoring controls over SNC O&M’s expenditures. We have not, as it is not part of our mandate, reviewed any of the OAE’s work that may have been carried out.
- 1.27 In keeping with our scope and mandate, the following were not audited, examined, reviewed, analyzed or assessed, in any manner whatsoever. As such, we make no representations related to:

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- i. Necessity or requirement for the goods or services provided in relation to the Transactions;
- ii. Tendering or award process that resulted in the awarding of the GP Contract, and any subsequent extensions, to SNC;
- iii. The Crown's option(s) to extend the GP Contract;
- iv. SNC O&M's performance against the Key Performance Indicators stipulated in the GP Contract with respect to the Transactions;
- v. The efficiency of PWGSC's AFD approach with respect to the GP Contract and the estimated annual savings of the outsourcing of PM and PD Services to SNC;
- vi. SNC O&M discharging all of its responsibilities pursuant to the GP Contract;
- vii. PWGSC's monitoring of SNC O&M to ensure services are delivered in accordance with the terms and conditions of the GP Contract;
- viii. Testimony or documentation related to the hearings before the Parliamentary Standing Committee on Government Operations and Estimates with respect to the Transactions; and
- ix. Legal interpretation of the GP Contract including the SoW.

1.28 We refer to the attached Appendix 1 - A which sets out additional restrictions and qualifications regarding this Chapter.

General Approach

1.29 As noted previously in this Chapter, PwC was engaged by PWGSC under Phase 1 of the Contract to conduct specified forensic audit procedures with respect to the Transactions and provide an opinion with respect to the reasonability and supportability of the expenditures examined. In this regard, our general approach for Phase 1 of the engagement was as follows:

- i. Review background information gathered by PWGSC with respect to the Transactions;
- ii. Attended SNC O&M's offices to obtain and review all available supporting documentation with respect to the Transactions;
- iii. Meet with the Subcontractors to obtain full particulars with respect to the work surrounding the Transactions and obtain all available supporting documentation;
- iv. Conduct interviews with individuals involved in the Transactions and gather additional information with respect to the authorization process, work performed, project management, payments issued and actual costs incurred;
- v. Develop criteria to measure each cost component of the Transactions in order to assess reasonability and supportability;
- vi. Assess each cost component of the Transactions against the developed assessment criteria;
- vii. Provide regular updates to PWGSC with respect to the progress of our Phase 1 work; and
- viii. Prepare and issue this Chapter of this Report to PWGSC with respect to our findings in relation to the reasonability and supportability of the Transactions.

Specific Procedures Performed

1.30 The specific procedures performed in conducting Phase 1 of the audit, consisting of specified forensic audit procedures, are outlined below:

- i. We reviewed the documentation gathered and provided to us by PWGSC (see paragraphs 1.17 through 1.28 of this Chapter for scope limitation).

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- ii. We attended an introductory meeting with representatives from SNC O&M, RPB and PWGSC's Acquisition Branch to identify key contacts and to discuss the various phases of the engagement.
- iii. Physical site visits were scheduled and conducted to inspect the work performed in relation to the Transactions, except for accessing floors 17A1 and 18A1 of Place du Portage Phase III, Gatineau, Quebec ("Phase III") which pertains to the extra cleaning transaction (Transaction #7). Due to the fact that this Transaction pertained to extra daily cleaning services, we determined that obtaining access to the floors would not provide any additional benefit particularly when we were provided copies of the floor plans.
- iv. We reviewed SNC O&M's current prequalified vendor list to ensure that all of the Subcontractors that were involved in the Transactions were listed.
- v. We requested and obtained SNC O&M's supporting documentation with respect to the Transactions. We were provided with a binder of documents which we understand was compiled in anticipation of SNC O&M's attendance before the Parliamentary Standing Committee on Government Operations and Estimates (see paragraphs 1.17 through 1.28 of this Chapter for scope limitation).
- vi. Based on our review of the documentation received, we identified individuals from both SNC O&M and Corporate Accommodation that were involved in each of the Transactions. We requested and conducted interviews with those individuals who were currently employed and whom we deemed relevant along with those SNC O&M individuals that we were advised were involved in the compilation of the supporting documentation.
- vii. Interviews were also conducted with PWGSC's current and former technical authority (the "Technical Authority") responsible for the GP Contract.
- viii. We conducted interviews with the Subcontractors involved in the Transactions to obtain full particulars with respect to the work performed including the: cost quotes issued to SNC; dates work performed; invoicing process; and, cost breakdown. We further requested certain of the Subcontractors to provide us with copies of their invoices with respect to the purchase of materials from their suppliers.
- ix. We met with SNC O&M representatives, [*], to discuss the discrepancies noted between the information that they provided in relation to the information obtained from the Subcontractors.

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- x. We requested and obtained from PWGSC's Corporate Security Directorate, copies of the security sign-in sheets that the Subcontractors would have signed in accessing the Gatineau Portfolio buildings, in an attempt to confirm the amount of time spent on each of the Transactions except for the extra cleaning services (Transaction #7). Due to the fact that the extra cleaning services are an addition to existing daily services, reviewing the sign-in sheets would not provide any relevant information. As such, this information was obtained from our interviews with the particular cleaning subcontractor.
- xi. Where necessary and appropriate, we contacted various suppliers and subcontractors, not involved in the Transactions, to obtain cost estimates with respect to the services/goods provided for certain of the Transactions for comparison purposes.
- xii. We conducted follow-up telephone conversations and/or correspondence with the Subcontractors to obtain further information.
- xiii. We attended meetings with SNC O&M's senior management including its president, Mr. Charlie Rate, and PWGSC to discuss our developed assessment criteria, our preliminary findings and SNC O&M's additional information with respect to certain of the Transactions.
- xiv. We attended further meetings with SNC O&M's senior management and staff to discuss our additional findings and potential discrepancies identified during Phase 1 of our engagement.

Summary of Findings

1.31 We summarize below our key findings with respect to Phase 1 of our engagement. In order to assess the reasonability and supportability of the Transactions, it was necessary to assess the cost components of SNC O&M's invoices issued to PWGSC. We note that in the delivery of commercial realty management services (which includes PM Services and PD Services), it is industry practice to charge costs in addition to the subcontractor costs. We further note such costs may not be applicable in the context of the maintenance and operation of one's personal residence. We discuss these cost components and our key findings in the following paragraphs.

Cost Components

1.32 We understand from our meetings and discussions with both PWGSC and SNC O&M that the process for the management of tenant department initiated requests ("Tenant Direct Requests") is as follows:

- i. Prior to July 2007, Tenant Direct Requests < \$25,000 could be initiated directly by the tenant to SNC O&M. Subsequent to July 2007, PWGSC increased the threshold to \$40,000 at the request of tenant departments as PWGSC believes it supports a more efficient approach.
- ii. Once SNC O&M received the Tenant Direct Request, they would obtain cost quotes in accordance with the SNC O&M procurement policy (a copy of which we have retained in our records) and prepare a cost quote in the form of an AFD Work Order for the tenant's review and approval.
- iii. Upon receipt of the duly executed AFD Work Order, SNC O&M would issue a Purchase Order ("PO") authorizing the subcontractor to supply/perform the requested goods/services.
- iv. Upon the subcontractor's completion of work described in the AFD Work Order, SNC O&M would issue an invoice to the tenant for payment. The tenant would review the invoice and authorize payment in accordance with S.34 FAA.

1.33 The Transactions in this Chapter are Tenant Direct Requests under the \$40,000 threshold stipulated by PWGSC and were managed by Corporate Accommodation.

1.34 Our analysis of SNC O&M's invoices rendered to Corporate Accommodation for payment, with respect to the Transactions, contained the following four (4) cost components:

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- i. Subcontractors Construction costs (the “Subcontractors Costs”);
- ii. SNC O&M’s Project Management (“PM”) Labour;
- iii. SNC O&M’s Management fee; and
- iv. Federal taxes (Goods and Services Tax (“GST”)).

1.35 Table 1 below, summarizes the Transactions and the details of the cost components which are discussed in further detail in this Chapter.

Table 1 – Transaction Summary

<i>Transaction</i>	<i>Subcontractors Costs</i> \$	<i>SNC O&M’s PM Labour</i> \$	<i>SNC O&M’s Management Fee</i> \$	<i>Federal Taxes (GST)</i> \$	<i>Total Cost</i> \$
1 Purchase of Two Plants and Two Pots	[*]	[*]	[*]	92.80	1,948.72
Installation of Three					
2 Blinds	[*]	[*]	[*]	67.38	1,414.95
3 Installation of Door Bell	[*]	[*]	[*]	47.64	1,000.41
4 Removal of Exit Sign	[*]	[*]	[*]	12.20	256.22
5 Installation of Six Pot Lights	[*]	[*]	[*]	250.80	5,266.80
6 Removal of Light Switch	[*]	[*]	[*]	47.64	1,000.41
7 Extra Cleaning Services of the Minister and Deputy Minister’s Offices	[*]	[*]	[*]	888.14	18,650.87
Total	[*]	[*]	[*]	1,406.60	29,538.38

Note 1: PWGSC and SNC O&M agreed the PM Labour is a minimum [*] for the Gatineau Portfolio. Pursuant to the GP Contract, PM Labour includes the following costs dedicated to a project: (1) Project Managers; (2) Project Officers; (3) Tenant Service Staff; (4) Inspectors; (5) Estimators; (6) Safety Coordinators; (7) Administrative and Accounting; (8) Information Systems; and (9) Data Entry Personnel.

Assessment of Supportability and Reasonability

1.36 As noted previously, the purpose of this Chapter is to provide an opinion with respect to the reasonability and supportability of the Transactions. We note that our findings are only in relation to the Transactions, and, we cannot comment on whether or not the Transactions are representative of a greater population of transactions.

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Cost Component Assessment Criteria

1.37 The cost component assessment criteria (the “Assessment Criteria”) were developed to assess the reasonability and supportability for each of the four separate cost components. The criteria are outlined below.

<i>The Assessment Criteria</i>		
<i>Cost Component</i>	<i>Reasonability Criteria</i>	<i>Supportability Criteria</i>
Federal Taxes (GST)	The rate in effect at the time of the Transactions was 5%. Was the GST charged by SNC O&M in accordance with the applicable rate?	The GST rate is set by legislation and pursuant to the GP Contract.
Management Fee	The calculated amount included in SNC O&M's invoices is in accordance with the contractual Management Fee percentage.	The Management Fee is stipulated in the GP Contract.
PM Labour	PM Labour is an allowable pass-through cost without mark-up for overhead or profit. Confirmation that SNC O&M did not charge more than actual labour costs relating to the Transactions.	SNC O&M is able to provide detailed support of actual time spent on the projects and/or the total annual actual PM Labour costs are reconciled in accordance with terms of the contract.
Subcontractors Costs	The amounts charged by the subcontractor were assessed for reasonability as follows: (1) Determine whether SNC O&M was required to follow a procurement process and, if yes, was it followed and was the lowest bid awarded the contract? In the event that the lowest bid was not awarded the contract, SNC O&M's files adequately document the supporting rationale for not complying. (2) Review the service agreement (if any) and applying the contractual rates stipulated therein; (3) Review the breakdown of costs for both labour and materials cost (if any), and/or obtain comparative	The amounts charged by the subcontractor were assessed for supportability as follows: (1) Determine whether there was an AFD Work Order issued by PWGSC to SNC O&M requesting the goods/services; (2) Determine whether subcontractor invoice(s) were issued to SNC O&M; (3) Determine whether proof of payment was issued by SNC O&M to the subcontractor; (4) Match the subcontractor invoice and proof of payment to the amount on SNC O&M's invoice to PWGSC and PWGSC's AFD Work

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<i>The Assessment Criteria</i>		
<i>Cost Component</i>	<i>Reasonability Criteria</i>	<i>Supportability Criteria</i>
	cost estimates from other suppliers and/or the Subcontractors if considered applicable and necessary; (4) Review the legislative requirements (if any) governing the profession and apply the requirements to the service provided; and (5) Determine the reasonability of costs based upon the following criteria for (3) & (4) above as the lower of: a. \$150; or b. < ± 10%.	Order; (5) Conduct interviews with the Subcontractors to discuss items (1) to (4) and (6) and (7); (6) Attend the premises to observe the service provided; and, (7) Review the security sign-in sheets for supporting documentation that the subcontractors attended the site to complete the work.

1.38 PWGSC was provided with and agreed to the established Assessment Criteria.

1.39 On July 9, 2010, the Assessment Criteria were initially discussed with SNC O&M during a meeting between us, SNC O&M and PWGSC. On September 1, 2010, a copy of the Assessment Criteria was forwarded in writing to SNC O&M for their review and comments. On September 7, 2010, SNC O&M wrote to us outlining their position with respect to the Assessment Criteria. A copy of SNC O&M's response to the Assessment Criteria is attached as Appendix 1 - B.

1.40 The Assessment Criteria were applied to each cost component of the Transactions. A summary of our findings with respect to our supportability and reasonability assessments is outlined in paragraphs 1.41 to 1.91 of this Chapter.

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Supportability

1.41 We summarize, our assessment of Supportability regarding the Transactions in Table 2 below:

Table 2 – Supportability Assessment

Transaction	Subcontractor's Costs	SNC O&M's PM Labour	SNC O&M's Management Fee	Federal Taxes (GST)
1 Purchase of Two Plants and Two Pots	Yes	In Process ¹	Yes	Yes
2 Installation of Three Blinds	Yes	In Process ¹	Yes	Yes
3 Installation of Door Bell	Yes	In Process ¹	Yes	Yes
4 Removal of Exit Sign	Yes	In Process ¹	Yes	Yes
5 Installation of Six Pot Lights	Yes	In Process ¹	Yes	Yes
6 Removal of Light Switch	Yes	In Process ¹	Yes	Yes
7 Extra Cleaning Services of the Minister and Deputy Minister's Offices	Yes	In Process ¹	No ²	Yes

Note 1: This matter has been discussed with PWGSC and at the request of PWGSC we are in the process of conducting forensic auditing procedures of SNC O&M's actual PM Labour costs. Once these procedures have been completed, we will provide PWGSC with our opinion on the supportability and reasonability of SNC O&M's PM Labour costs.

Note 2: PWGSC advised us that the past practice of PWGSC, as required under the previous AFD contract with the former service provider, and as agreed to with SNC O&M was to treat Extra Cleaning Services as PD Services. We note that this practice is not in accordance with the GP Contract. According to the GP Contract, these services should be classified as PM Services which are subject to a different management fee rate. Accordingly, the management fee charged is not supportable.

1.42 Subject to the limitations noted throughout this Chapter including those listed below and the Assessment Criteria set out above, our conclusions with respect to the supportability of each of the cost components is as follows:

Subcontractors Costs

1.43 Based on the supportability assessment criteria defined in paragraph 1.37, subject to the limitations noted throughout this Chapter, we conclude that based on the documentation that we reviewed all of the Subcontractors Costs were supportable. Our findings/comments with respect to the supportability of the Subcontractors Costs are summarized below:

- i. We could not confirm the exact date(s) that the Subcontractors performed the work in relation to any of the Transactions, as this information is not maintained in either PWGSC or SNC O&M files. SNC O&M stated that the SNC Contracts do not

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stipulate that they are required to maintain records of when Subcontractors attend to perform the work for particular projects.

- ii. For one (1) of the Transactions, (the Extra Cleaning - Transaction #7), the Subcontractor provided services prior to PWGSC's approval of an AFD Work Order and prior to the issuance of a PO by SNC O&M to the Subcontractor. We discussed this Transaction with SNC O&M and they advised us as follows:

“The services have been demonstrated as provided and the ultimate approval has also been demonstrated. As well, there is no financial risk to PWGSC in such an event. Services sometimes require immediate action. In the event that PWGSC was dissatisfied for any reason and had we not attained their approval, it would be our risk and ultimately our cost to bear.”

- iii. SNC O&M did obtain a cost quote from all of the Subcontractors with respect to the Transactions; however; the cost quotes with respect to Extra Cleaning (Transaction #7), Pot Lights (Transaction #5); and, Door Bell (Transaction #3), did not contain any detailed cost breakdown in relation to the work to be performed. PWGSC approved the work to be performed based on the limited information on the AFD Work Order. SNC O&M believes that such detailed information is neither required nor relevant under the SNC Contracts.
- iv. SNC O&M contacted certain of the Subcontractors to obtain further supporting documentation for their files with respect to both the work performed and a cost breakdown which SNC O&M received on March 10, 2010 for Transactions #1, #3 and #5. Subsequent to July 9, 2010, SNC O&M requested and received a cost breakdown for Transaction #6. We cannot confirm what information was obtained after the transaction was completed however; we reviewed all of the information provided to us as at September 24, 2010.
- v. SNC O&M invoices issued to PWGSC were calculated correctly and in accordance with the AFD Work Order.
- vi. All of SNC O&M's invoices in relation to the Transactions were signed off by PWGSC employees pursuant to S.34 FAA.
- vii. The amount of the Subcontractors Costs outlined in both the cost quote and the AFD Work Order reflected the amount paid by SNC O&M to the Subcontractors.

PM Labour

- 1.44 SNC O&M does not maintain timesheets with respect to the time spent by its employees on any specific projects. As a result, we were unable to review and assess the actual

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total time spent by SNC O&M's employees, on a per project basis, in relation to the Transactions.

- 1.45 This matter has been discussed with PWGSC and at the request of PWGSC we are in the process of conducting forensic auditing procedures of SNC O&M's actual PM Labour costs. Once these procedures have been completed, we will provide PWGSC with our opinion on the supportability and reasonability of SNC O&M's PM Labour costs.

SNC O&M's Management Fee

- 1.46 Based on the supportability assessment criteria defined in paragraph 1.37, subject to the limitations noted throughout this Chapter, we believe that SNC O&M's Management Fees for six (6) of the seven (7) Transactions (Transaction #1, #2, #3, #4, #5 and #6) appear to be supportable based upon information provided to us to date.
- 1.47 With respect to Transaction #7 – Extra Cleaning, on October 21, 2010, PWGSC brought to our attention that the categorization of this service should be PM Services rather than PD Services. As a result, it is PWGSC's position that SNC O&M is contractually obligated to charge a different management fee on PM Services transactions. The contractual management fee for PM Services is a lower rate than for PD Services.
- 1.48 Subsequent to corresponding with PWGSC with respect to their position on the classification of the Extra Cleaning as PM Services, we advised SNC O&M with respect to same.
- 1.49 On October 25, 2010, SNC O&M provided us with the general context for their position, as follows:

“The principal distinction involved here is work that is performed within the base services contracted by PWGSC as custodian of all Crown assets versus work that is performed at the request of tenants (in this case the tenant happens to be PWGSC as a department, but it could be any other department or agency within the AFD portfolio). [Tenant requests] also includes additional services that are directly engaged by tenant departments. This includes everything from extra services to raise the service level to hard projects like office reconfiguration. The principal is one of separation of funding. That is to say, PWGSC as custodian does not fund extras requested by individual departments. Each such department is accountable for their own funds. Hence the separate treatment and designation as projects. Oversight on this work is provided by a separate governance process within the AFD contracts and includes ongoing communications between PWGSC account managers (dedicated to specific client departments and accountable to negotiate Occupancy Instruments) as well as the AFD oversight team.”

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- 1.50 On October 29, 2010, SNC O&M provided us with their position that “the charging and payment methodology of tenant requests is clearly defined and has been in operations for five years. Every single transaction receives the approval and authorization of a tenant and / or PWGSC official, including the application of fees, and the mechanism itself for delivery and billing of all tenant services requests, through which a Project Management Fee is applied, was created by PWGSC”.
- 1.51 SNC O&M’s response has been forwarded to PWGSC for their review and follow-up. PWGSC advised us that the past practice of PWGSC, as required under the previous AFD contract with the former service provider, and as agreed to with SNC O&M was to treat Extra Cleaning Services as PD Services. PWGSC further advised us that a review is underway to harmonize contractual requirements and established business practices to provide customer service within operational expectations and industry standards.
- 1.52 Based on the supportability assessment criteria defined in paragraph 1.37, subject to the limitations noted throughout this Chapter, we believe that the Management Fee charged by SNC O&M with respect to Transaction # 7 – Extra Cleaning, is not in compliance with the GP Contract and therefore is not supportable.

Federal Taxes

- 1.53 The cost components with respect to Federal Taxes were calculated correctly and are supportable.

Reasonability

- 1.54 Our assessment with respect to the reasonability of the costs incurred in each of the Transactions was conducted with respect to each of the following financial components which were included in SNC O&M’s invoices rendered to PWGSC: (1) Subcontractors Costs; (2) SNC O&M’s PM Labour; (3) SNC O&M’s Management Fee; and (4) Federal taxes (GST).
- 1.55 Subject to the limitations noted throughout this Chapter including those listed below and the assessment criteria set out above, we conclude that certain of the cost components for four (4) of the seven (7) Transactions appear to be reasonable based upon information provided to us as at September 24, 2010. We were unable to assess the reasonableness of SNC O&M’s PM Labour at this time (see note 1 of Table 3 below). The amounts with respect to SNC O&M’s Management Fees with the exception of Transaction #7 and Federal Taxes appear to be reasonable. The summary of our findings are outlined below in Table 3.

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Table 3 – Reasonability Assessment

<i>Transaction</i>	<i>Subcontractors Costs</i>	<i>SNC O&M's PM Labour</i>	<i>SNC O&M's Management Fee</i>	<i>Federal Taxes (GST)</i>
1 Purchase of Two Plants and Two Pots	Yes	In Process ¹	Yes	Yes
2 Installation of Three Blinds	Unable to Conclude	In Process ¹	Yes	Yes
3 Installation of Door Bell	Yes	In Process ¹	Yes	Yes
4 Removal of Exit Sign	Yes	In Process ¹	Yes	Yes
5 Installation of Six Pot Lights	Yes	In Process ¹	Yes	Yes
6 Removal of Light Switch	Unable to Conclude	In Process ¹	Yes	Yes
7 Extra Cleaning Services of the Minister and Deputy Minister's Offices	No	In Process ¹	No ²	Yes

Note 1: This matter has been discussed with PWGSC and at the request of PWGSC we are in the process of conducting forensic auditing procedures of SNC O&M's actual PM Labour costs. Once these procedures have been completed, we will provide PWGSC with our opinion on the supportability and reasonability of SNC O&M's PM Labour costs.

Note 2: PWGSC advised us that the past practice of PWGSC, as required under the previous AFD contract with the former service provider, and as agreed to with SNC O&M was to treat Extra Cleaning Services as PD Services. We note that this practice is not in accordance with the GP Contract. According to the GP Contract, these services should be classified as PM Services which are subject to a different management fee rate. Accordingly, the management fee charged is not reasonable.

Subcontractors Costs

1.56 In assessing the reasonability of the Subcontractors Costs, in relation to the Transactions, we relied on the following: (1) Information/documentation obtained from meetings/correspondence with PWGSC, SNC O&M and the Subcontractors with respect to services rendered and/or products supplied; (2) Observations from attending the work site; (3) If possible, obtain supporting documentation from the Subcontractors with respect to similar transactions performed for other customers; and/or, (4) Obtain market comparables for similar transactions from other vendors if considered applicable and necessary; and, (5) assess if procurement processes were followed.

1.57 Paragraph 2.6.4.5 of the SoW states “[SNC] shall demonstrate to the Technical Authority that it has a competitive subcontracting process and a prequalification process,

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reflecting best industry practices, which include: ...development and utilization of a list of prequalified bidders on an equalized rotational basis”.

1.58 SNC O&M’s subcontracting process, which was reviewed by PWGSC’s Technical Authority, and in effect at the time surrounding the Transactions, is as follows:

- i. Expected services < \$5,000 – obtain one quote from a vendor on SNC O&M’s prequalified bidder list;
- ii. Expected services > \$5,000 and < \$25,000 – invite quotes from three (3) vendors on SNC O&M’s prequalified bidder list;
- iii. Expected services between > \$25,000 and < \$200,000 – invite quotes from five (5) vendors on SNC O&M’s prequalified bidder list; and
- iv. Expected services > \$200,000 – the contract will be tendered on MERX.

1.59 During a meeting held on June 30, 2010, with an SNC O&M employee who was a tenant service coordinator at the time surrounding the Transactions, he advised us of the following:

- i. SNC O&M did not have a systematic formal rotation process in place at the time of the seven Transactions outlined in the March 10, 2010 media article;
- ii. He would randomly select the subcontractor to use from the prequalified list of suppliers;
- iii. The selection of subcontractors was at his discretion as a tenant services coordinator;
- iv. For small electrical jobs, he normally selected a certain subcontractor due to their: (1) great reputation; and, (2) knowledge of Place du Portage Phase III; and
- v. He does not know if the rotation process has been formalized; however, he is aware that a lower threshold for the procurement policy from \$5,000 to [*]¹ with respect to single source bids has been implemented.

1.60 SNC O&M senior management has advised that the selection of subcontractors is “most certainly not random. Our professionals determine the most suitable choice for these small jobs based on history, quality, responsiveness and value for money”.

¹ Based on our interview with an SNC O&M facility manager, they advised that the lower threshold of [*]

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1.61 We enquired with the GP Contract's current and former Technical Authorities with respect to their satisfaction of SNC O&M meeting the contractual requirements outlined in paragraph 1.57 above. The Technical Authorities advised us that PWGSC does not verify SNC O&M's rotation of their subcontractors as they rely on SNC O&M to ensure this process is followed in accordance with the GP Contract.

Transaction #1, #3, #4 and #5

1.62 Based on the reasonability assessment criteria defined in paragraph 1.37 subject to the limitations noted throughout this Chapter, we believe that the Subcontractors' Costs for four (4) of the seven (7) Transactions (Transaction #1, #3, #4, and #5) appear to be reasonable based upon information provided to us to date.

1.63 A summary with respect to our reasonability assessment in relation to the assessment criteria defined in paragraph 1.37 is provided below under each of the respective transaction headings.

Transaction #1 – Purchase of Two Plants and Two Pots

1.64 Pursuant to PWGSC's request, SNC O&M retained the services of a subcontractor (the "Plant Subcontractor") to supply and deliver two (2) plants and two (2) pots to Place du Portage, Phase III at 11 Laurier Street in Gatineau, Quebec (the "Phase III").

1.65 As noted in Table 1 above, the Plant Subcontractor's cost totalled [*]. We have been advised that the goods and services provided by the Plant Subcontractor included the following:

- i. Supply two (2) large-sized tropical plants;
- ii. Inspection certificate, delivery, insurance and other costs;
- iii. Supply two (2) pots, sub-irrigation system and liner; and
- iv. Plant maintenance costs for nine (9) months.

1.66 Based on the limitations noted throughout this Chapter and the following reasonability assessment criteria defined in paragraph 1.37: (2) review of the plant service agreement and applying the contractual rates stipulated therein; and, (3) comparative cost estimates obtained from other suppliers, we conclude that the Plant Subcontractor's cost of [*] with respect to the services/goods summarized above appears to be reasonable. The details with respect to our analysis are contained within the Working Papers provided to PWGSC.

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Transaction #3 – Installation of Door Bell

- 1.67 Pursuant to PWGSC's request, SNC O&M retained the services of an electrical subcontractor (the "Electrical Subcontractor") to supply and install one doorbell and chime (the "Doorbell") for the secured room 116A located on floor 10A1 of the Phase III.
- 1.68 As noted in Table 1 above, the Electrical Subcontractor cost was [*], the Electrical Subcontractor provided us with the following cost breakdown:
- i. [*] Material (doorbell, transformer, chime and cabling); and
 - ii. [*] Labour [*] to conduct after hours installation of above material and dedicated circuits.
- 1.69 Based on the limitations noted throughout this Chapter and the following reasonability assessment criteria defined in paragraph 1.37: (3) review the breakdown of costs for both labour and materials cost and obtain comparative cost estimates obtained from other suppliers; and, (4) review the legislative requirements governing the profession and apply the requirements to the service provided, we conclude that the Electrical Subcontractor's cost of [*] with respect to the services/goods summarized above appears to be reasonable. The details with respect to our analysis are contained within the Working Papers provided to PWGSC.

Transaction #4 – Removal of Exit Sign

- 1.70 Pursuant to PWGSC's request, SNC O&M retained the services of the Electrical Subcontractor to remove one (1) Exit sign (the "Exit Sign") located on floor 1B3 of Phase III.
- 1.71 As noted in Table 1 above, the Electrical Subcontractor cost was [*], the Electrical Subcontractor provided us with the following details:
- i. [*] Labour to disconnect electrical connection to the Exit Sign; removal of both the cabling and the Exit Sign; and, repair the ceiling.
- 1.72 Based on the limitations noted throughout this Chapter and the following reasonability assessment criteria defined in paragraph 1.37: (3) review the breakdown of costs for labour; and, (4) review the legislative requirements governing the profession and apply the requirements to the service provided, we conclude that the Electrical Subcontractor's cost of [*] with respect to the services/goods summarized above appears to be reasonable. The details with respect to our analysis are contained within the Working Papers provided to PWGSC.

Transaction #5 – Installation of Six Pot Lights

- 1.73 Pursuant to PWGSC's request, SNC O&M retained the services of the Electrical Subcontractor to supply and install six (6) pot lights, one (1) dimmer switch; and, one (1) electrical outlet in room 101 on floor 3A1 of Phase III.
- 1.74 As noted in Table 1 above, the Electrical Subcontractor cost was [*], the Electrical Subcontractor provided us with the following details:
- i. Supply of materials including six (6) pot lights, one (1) dimmer switch and cabling; and
 - ii. After hour installation of above material and dedicated circuits.
- 1.75 Based on the limitations noted throughout this Chapter and the following reasonability assessment criteria defined in paragraph 1.37: (3) Review the breakdown of costs for both labour and materials cost and the comparative cost estimates obtained from other suppliers, we conclude that the Electrical Subcontractor's cost of [*] with respect to the services/goods summarized above appears to be reasonable. The details with respect to our analysis are contained within the Working Papers provided to PWGSC.

Transaction #2 and #6

- 1.76 On July 9, 2010, we presented preliminary findings to SNC O&M with respect to certain of the Transactions (Transaction #2, #6, #7). Both during and subsequent to the meeting, SNC O&M provided us with additional information. We conducted further forensic audit procedures with respect to the additional information provided by SNC O&M including scheduling several meetings with SNC O&M to discuss our findings and any discrepancies that arose with respect to the information that they have provided and/or obtained from our interviews with the Subcontractors.
- 1.77 On September 27, 2010, SNC O&M provided us with a final revised summary of information with respect to Transactions #2 and #6.
- 1.78 We are unable to conclude on the Subcontractors Costs for two of the Transactions (Transaction #2 and #6). Factors considered in assessing these Transactions are outlined below:

Transaction #2 – Installation of Three Blinds

- i. In accordance with SNC O&M's procurement process, as noted above, SNC O&M is required to obtain one quote from a vendor on SNC O&M's prequalified bidder list. In

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addition, the SoW requires SNC O&M to develop and utilize a list of prequalified bidders on an equalized rotational basis. SNC O&M advised us that they do not retain historical copies of their prequalified supplier lists as the list is a living document open to change on any given day with the addition of newly prequalified subcontractors or removal of any firm that does not meet their quality standards. As a result, we were unable to confirm who and how many suppliers were prequalified to perform the required services at the time of Transaction #2. SNC O&M also advised us that they did not have a systematic formal rotation for their prequalified suppliers at the time of Transaction #2. PWGSC also did not verify whether SNC O&M was rotating suppliers as they advised us that they rely on SNC O&M to ensure this process is followed. Therefore, we are unable to confirm: (1) whether the Subcontractor that SNC O&M retained to perform Transaction #2 was on the prequalified list; and, (2) the names of other suppliers that may have been on the prequalified list thereby preventing us from assessing whether an equalized rotational selection from a list of pre-qualified suppliers occurred in 2008. Therefore, we are unable to conclude as to whether or not SNC O&M followed the procurement process in order to satisfy certain of the reasonability assessment criteria set out in paragraph 1.37 of this Chapter.

Transaction #6 – Removal of Light Switch

- i. We were unable to determine the timing of when the light switch removal was performed (in particular it is not clear whether or not the Subcontractor was already on site carrying out other work). This has a direct impact on our conclusion of reasonability as it impairs our ability to assess the incremental cost charged by the Subcontractor for the light switch removal. In addition, it is a contractual interpretation matter as to whether or not the Subcontractor should have been responsible for the incremental cost of the light switch removal. As such, we are unable to assess whether SNC O&M followed the procurement process. Therefore, based on the foregoing, we are unable to conclude whether the reasonability assessment criteria set out in paragraph 1.37 of this Chapter have been satisfied.

1.79 Notwithstanding PWGSC's assistance with respect to the audit, consisting of specified forensic audit procedures, into Transactions #2 and #6; as a result of the above noted factors we are unable to conclude with respect to the Subcontractors Costs for these two Transactions.

Transaction #7 – Extra Cleaning

1.80 We have concluded that the Subcontractors Costs for Transaction #7 appear to be unreasonable. Based on our cost calculation, which is in accordance with the contractual agreement between SNC O&M and the Subcontractor along with information obtained

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from the Subcontractor regarding the incremental hourly labour required, the difference between the calculated cost and the invoiced amount, since the commencement of the contract October 15, 2006 to March 31, 2010, totalled \$50,416.88.

- 1.81 On September 4, 2010, SNC O&M provided us with a copy of their own calculation of the difference between the calculation pursuant to the contract and the invoiced amount, which they define as an “imputed variance”, which totalled \$23,269.32. We have not conducted a detailed review of their calculation.
- 1.82 On September 16, 2010, SNC O&M provided us with their comments with respect to our preliminary observations. Their comments with respect to Transaction #7 are summarized below:
- i. “...in retrospect, using a time and materials approach to extra cleaning could have resulted in a lower cost. We do not agree with a finding of “unreasonable cost”. As we have repeatedly stated, our approach to this service was on a fixed price basis. Such an approach provides cost certainty to the client and reduces administration. Our subcontracts explicitly allow such an approach and the fact we did not choose to use hourly rates does not make the actual result unreasonable.”
 - ii. “We will give up the price certainty and reduced administration for cost savings and assuming that PWGSC wishes to follow this direction, we will reimburse them for the savings.”
- 1.83 PWGSC advised us that they conducted a further investigation into this Transaction including a thorough review of SNC O&M’s cost calculation, in the context of our calculation, and an examination of additional documentation from the Subcontractor which was not provided to PwC. PWGSC further advised us that based on the additional information provided by the Subcontractor and their analysis of SNC O&M’s cost calculation and our own cost calculation, they accepted SNC O&M’s revised calculation of \$31,898.20 (plus GST) in the settlement of this matter.

SNC O&M’s PM Labour

- 1.84 SNC O&M does not maintain timesheets with respect to the time spent by its employees on any specific projects. As a result, we were unable to review and assess the actual total time spent by SNC O&M’s employees, on a per project basis, in relation to the Transactions.
- 1.85 This matter has been discussed with PWGSC and at the request of PWGSC we are in the process of conducting forensic auditing procedures of SNC O&M’s actual PM Labour costs. Once these procedures have been completed, we will provide PWGSC with our opinion on the supportability and reasonability of SNC O&M’s PM Labour costs.

SNC O&M's Management Fee

- 1.86 The Transactions were treated as Tenant Direct Requests. Pursuant to the GP Contract, Tenant Direct Requests are classified in the PD Services category. SNC O&M is contractually allowed to apply/charge a certain management fee against the total construction and design costs for all PD Services projects.
- 1.87 Based on our review of SNC O&M's invoices, the Management Fee charged is adequately supported in accordance with the terms of the GP Contract and calculated correctly for six (6) of the seven (7) Transactions. SNC O&M's Management Fee charged for Transactions #1, #2, #3, #4, #5 and #6 appears to be reasonable as it is in accordance with the terms of the GP Contract.
- 1.88 As outlined earlier in paragraphs 1.47 through 1.52 of this Chapter, PWGSC has now determined that extra cleaning services should be classified as a PM Service in accordance with the GP Contract and that the lower PM Service management fee should have been charged. At the time of the Transaction PWGSC and SNC O&M established that extra cleaning was a PD Service and as such, believed that the appropriate management fee had been applied by SNC O&M.
- 1.89 Notwithstanding that PWGSC and SNC O&M agreed to treat the extra cleaning as a PD Service, this treatment is not in accordance with the GP Contract and therefore, we have concluded that the management fee charged by SNC O&M for Transaction #7 is unreasonable.

Federal taxes (GST)

- 1.90 The Federal Government is required to pay GST on its taxable purchases. The GST rate is set by the government and the rate in effect at the time of the Transactions was 5%.
- 1.91 Based on our review of SNC O&M's invoices, the 5% GST charged is in accordance with the GP Contract and calculated correctly. The GST charged on each of the Transactions appears to be reasonable.

Appendix 1 – A

Appendix 1 - A

Restrictions and Qualifications

1. This Report is not intended to be used for any purpose other than as stated in our Report without our prior consent. We do not assume any responsibility for losses occasioned to readers of this Report or other parties as a result of the circulation, publication, reproduction, or use of this Report or its contents contrary to the provisions of this paragraph. We will not assume any responsibility to any third party to which this Report is disclosed or otherwise made available.
2. In the event that further documents or information become available that could impact our findings, we reserve the right, but are under no obligation, to review such records and reconsider and amend the findings set out in this Report.
3. We have not, as it is not part of our engagement, secured or reviewed electronic communications or electronic documents.
4. Although we attempted, where possible, to verify the completeness of documentation there may be other relevant documentation.
5. Interviews were not conducted with those individuals no longer employed by PWGSC or SNC O&M in relation to the Transactions.
6. This Report is based on our review of the documents and information available to date. Our review does not constitute an audit, as defined by Generally Accepted Auditing Standards prescribed by the Canadian Institute of Chartered Accountants, and we do not provide an audit or review opinion. We have not attempted to audit or otherwise verify the information presented to us beyond the expressed scope stated in this Report.
7. This Report makes references to payments made to SNC O&M by PWGSC. We have obtained the information relating to these payments from PWGSC's internal reporting system; however, we have not specifically reviewed these payments.
8. Our Report, including any schedules and appendices, must be considered in its entirety by the reader. Selecting and relying on specific portions of the analyses, or factors considered by us, in isolation may be misleading.
9. We make no representation regarding matters of legal interpretation.

Appendix 1 – B

7 September 2010

Mr. Steve Malette
Vice-President
Price Waterhouse Coopers

RE: Response to Draft Terms of Reference on Audit of Tenant Service Projects Delivered under AFD Contracts with PWGSC

Dear Mr. Malette

On 1 September 2010 you provided us with your draft “cost component and assessment criteria for the seven transactions”. Given your mandate to submit a draft findings report to PWGSC on 7 September, we provide this response for consideration in preparing your draft

Below you will find comments around the various criterion.

Category 1: Federal Tax

PWC Reasonableness Criteria	SNC-Lavalin Comment	PWC Supportability Criteria	SNC-Lavalin Comment
<i>“The rate in effect at the time of the Transactions was 5%. Was the GST charged by SNC in accordance with the applicable rate?”</i>	We find this test to be appropriate	<i>“The GST rate is set by legislation and pursuant to the GP Contract.”</i>	We find this test to be appropriate

Category 2: Management Fee

PWC Reasonableness Criteria	SNC-Lavalin Comment	PWC Supportability Criteria	SNC-Lavalin Comment
<i>“The calculated amount included in SNC’s invoices is in accordance with the contractual Management Fee percentage”</i>	We find this test to be appropriate	<i>“The Management Fee is stipulated the GP Contract”</i>	We find this test to be appropriate

Category 3: Project Management Labour

We find that both the reasonableness and supportability tests are flawed. For ease of reference, we have split our comments below to address the specific issues with the criteria.

Reasonableness:

PWC Criteria	SNC-Lavalin Response
<p><i>“PM Cost is an allowable pass-through cost without mark-up for overhead or profit. Confirmation that SNC did not charge more than actual labour costs relating to the Transactions”</i></p>	<ul style="list-style-type: none"> ○ Over the five year life of this contract, we have consistently applied the contractual requirement such that, at the Class “A” quote stage of a given project, the labour component becomes a fixed price. We have provided PWC with the applicable contractual references as well as the formal contract interpretation and independent legal opinion supporting this approach. In addition, it is our understanding that PWGSC officials responsible for our contract have also confirmed to PWC that this approach has been taken with their endorsement and approval. ○ This approach was taken to avoid unnecessary costs for PWGSC and to simplify administration. It also results in accelerated project delivery, provides cost certainty to PWGSC and leaves all fixed price risk with SNC-Lavalin. ○ Thus far in the audit process, PWC has consistently rejected the use of relevant and readily available benchmarks to determine commercial reasonableness. As we have repeatedly advised PWC, the most relevant and applicable benchmarks for this service (all in the unique PWGSC environment) are the labour charges applied by PWGSC internally for self-performed project delivery and the charges paid by PWGSC to landlords under lease agreements for third party project delivery. Should these benchmarks be evaluated, the findings will show that our costs are reasonable.

The appropriate test of reasonability in this area is simply that SNC-Lavalin charges only what PWGSC has approved.

Supportability:

PWC Criteria	SNC-Lavalin Response
<p><i>“SNC is able to provide detailed support of actual time spent on the projects and / or the total annual actual PM labour costs are reconciled in accordance with the terms of the contract.”</i></p>	<p>The contractual requirement, as agreed and implemented by both PWGSC and SNC-Lavalin is supported by the fixed price work order for each project. These supporting documents are prepared by SNC-Lavalin and approved / signed-off by PWGSC.</p>

Given all of these facts, we are of the strong opinion that Project Management labour charging practices are both reasonable and supportable.

Category 4: Subcontractor Costs

With respect to supportability we find the tests to be appropriate and presume, given that PWC have not advised to the contrary, that all 7 tests have been satisfactorily met for all 7 projects. Below you will find our comments identifying flaws around the reasonableness criteria.

Reasonableness:

PWC Criteria	SNC-Lavalin Response
<p><i>(1) "Was SNC-Lavalin required to follow a procurement bidding process and, if yes, was it followed and was the lowest bid awarded the contract."</i></p>	<p>Our procurement process, as approved by PWGSC, for projects under \$5,000 requires a quote from a prequalified subcontractor. Hence, the concept of always awarding to the lowest bid is flawed. That is to say, sole-sourcing is acceptable for small projects and the criterion requirement to award to the lowest of multiple bidders is simply not applicable</p>
<p><i>(2) "Reviewing the service agreement (if any) and applying the contractual rates stipulated therein."</i></p>	<p>We find this test to be appropriate</p>
<p><i>(3) "Reviewing the breakdown of costs for both labour and materials cost (if any), and / or obtaining comparative cost estimates from other suppliers and / or the Subcontractors."</i></p>	<p>Attaining comparative pricing for these projects is not consistent with the process utilized for vendor selection on small jobs. It is unreasonable to assess costs with such arbitrary thresholds and in isolation from the overall work requirements. That is to say, the only certain way to ensure low bid is to solicit multiple bids for every single project. In a portfolio that requires many thousand such projects each year, all under our sole-sourcing threshold of \$5,000, such an approach is impractical and counter to Government policy.</p> <p>On small projects (those with a value of less than \$5,000), our processes do not require that we obtain multiple bids. Accordingly, comparatives obtained after the fact are neither relevant nor appropriate. The use of sole-sourcing for work of low value is a practice used by SNC-Lavalin with the full approval of PWGSC. This is a universal industry standard, also used by Government departments, and is undertaken with the specific purpose of providing value for money on small projects by avoiding onerous administration and unnecessary cost. In fact, the Treasury Board policy states that from the perspective of value for money, the high cost of awarding a Crown procurement contract far outweighs any economic advantage associated with competing goods and services contracts under \$25,000. Our threshold for sole sourcing is set even lower at \$5,000, but the principle is the same and formed part of the basis for PWGSC's decision to approve our procurement policy.</p> <p>Moreover, the impracticality of seeking tenders on projects under \$5,000 would have a significant impact on both costs and project delivery time. Such a practice, requiring the development of RFPs, together with site visits, a reasonable time for vendors to bid and the bid opening process, would require increased resources and longer delivery timelines. There would also be impacts on the small and medium enterprise market where vendors would have to account for the resources required with multiple job showings in their price structure, resulting in increased tender prices and hence in increased costs to the Crown. This would also have an effect on our vendor base and increased costs over time from vendors not wanting to waste time bidding small jobs because of the time and costs involved, given the limited possible success rate on winning jobs of low value. In summary, we believe that the introduction of competitive tendering for work below \$5,000 would result in higher costs and fewer contractors interested in bidding this work and we doubt that there would be any greater value for money received by the Crown.</p> <p>Requesting competitive bids as a comparative factor in a case where sole sourcing was used is inappropriate since it looks at a project without consideration of the larger context of thousands of small projects being delivered every year. Accordingly, the approach contained in these terms of reference provide an unbalanced view of the recognized fact that sole</p>

	<p>sourcing provides overall benefit and value for money.</p> <p>Rather than trying to test for reasonableness in isolation of the larger context of administering a program of thousands of small projects, the criteria here should be whether or not SNC-Lavalin has an appropriate procurement policy, has received approval from PWGSC to apply it and can demonstrate having supported that policy</p>
<p><i>(4) "Reviewing the legislative requirements (if any) governing the profession and applying the requirements to the service provided."</i></p>	<p>We find this test to be appropriate</p>
<p><i>(5) "For the purpose of this Report, we have determined reasonable costs for criteria (3) & (4) to be determined as the lower of: a) \$150; or, b) $\pm 10\%$"</i></p>	<p>In a contract with annual volumes in excess of \$550,000,000, we do not agree that a tolerance of \$150 or $\pm 10\%$ on isolated, individual small projects is appropriate to determine value for money. As articulated in our response to criteria 3 above, sole-sourcing, by its nature, is not conducive to meaningful comparative analysis for individual projects. This criterion ought to be eliminated altogether. Correct application of criteria one through four will demonstrate reasonableness with respect to subcontractor costs.</p>

Given these facts, we are of the strong opinion that any finding of subcontractor cost "unreasonableness" on these projects by PWC is based on erroneous criterion. Such a finding ignores the core principles of efficiency and responsiveness behind not only the AFD contracts but PWGSC and Treasury Board Policy.

Furthermore, if this criteria were to be utilised, it effectively means that sole sourcing would be discontinued, which, in turn would have a material deleterious effect on costs to the Crown and responsiveness to tenants in the future, whether on work delivered by SNC-Lavalin, PWGSC itself or any other third party.

As always, we remain committed to supporting this audit process and satisfying PWGSC that the objectives of AFD are being met. Should any questions or the need for additional information arise, we are at your disposal. We trust that this, our response to your draft criteria, will accompany the draft report you submit to PWGSC.

Regards,

Original signed by

Charlie Rate
President
SNC-Lavalin O&M



Chapter 2 – Phase 1 - Observations and Recommendations

*Public Works and Government Services Canada
Contract No. EN790-104291/001/ZQ*

January 24, 2011

Introduction and Background

- 2.1 As noted in paragraphs 1 through 8 of the Introduction and Background section of this Report, PWGSC awarded PwC the Contract to conduct an audit, consisting of specified forensic audit procedures on the Transactions.
- 2.2 During the course of Phase 1 of the audit, consisting of specified forensic audit procedures, certain matters came to our attention, such as the need for improved documentation and the need to increase the frequency of cost audits, which merited the attention of PWGSC.
- 2.3 The purpose of this Chapter is to present to PWGSC our observations and recommendations on other matters that came to our attention in carrying out our audit consisting of specified forensic audit procedures.
- 2.4 This Chapter must be read in conjunction with Chapter 1 of this Report including and without limitation to the Scope Limitations and General Approach, which are detailed therein.
- 2.5 Our Restrictions and Qualifications, which must be read in conjunction with this Chapter, are attached hereto as Appendix 2 - A.

Observations

Office of the Chief Risk Officer (“OCRO”)

- 2.6 As part of the audit, consisting of specified forensic audit procedures, we reviewed the July 18, 2007, PWGSC OCRO report (the "OCRO Report") which assessed whether RPB had sufficient controls and frameworks in place to fulfill RPB's responsibilities under S.34 FAA.
- 2.7 The OCRO Report included a number of concerns and recommendations. One of the concerns was with respect to the administration of SNC O&M's Project Management (“PM”) Labour. In particular, the following was noted:
- i. There is a lack of clarity on whether the PM Labour is fixed cost or an estimate, as per the SNC Contracts.
 - ii. The annual audited statement (the “Statement”) with respect to SNC O&M's actual costs has never been provided as the Statement is based on SNC O&M's billed statements of costs and not actual costs incurred.
 - iii. [*]
- 2.8 We have been advised by PWGSC that an action plan was developed to address the concerns and recommendations noted in the OCRO Report and the majority of these were implemented. The concerns with respect to the administration of SNC O&M's PM Labour were recently resolved and PWGSC advised us of the following:
- “For the future, the labour rates will continue to be set as a percentage of the construction and design allowable pass-through costs; however, this practice will be formalized in a written procedure. The procedure will reinforce that reconciliation and an adjustment based on actuals will take place at year end.
- Strict adherence to the contracts implies that business practices may no longer align with the contract and as such, changes to the systems and business practices may be required to bring clarity. A small working group has been formed to discuss in more details what steps will be required to move forward as well as to develop an implementation plan”.
- 2.9 PWGSC has advised us that the majority of the actions in the management action plan have now been implemented and implementation of the remaining actions in response to the OCRO Report is a top priority.

Financial Cost Audits

2.10 As part of Phase 1 of the audit, consisting of specified forensic audit procedures, we reviewed the three 2007 PWGSC commissioned Financial Cost Audits executed by Audit Services Canada ("ASC") on three regional portfolios, pertaining to the SNC Contracts, for the fiscal year 2005/06. The ASC cost audits commented on the following issues:

- i. “[They] were not able to obtain from SNC O&M sufficient audit evidence to support actual project management labour costs because SNC O&M claims the approved budget amount on the [Alternative Forms of Delivery Tenant Service Call-Ups (the “AFD Work Order”)] for projects as a fixed price amount and does not track actual costs...”;
- ii. “They could not summarize the total actual or budgeted labour management costs for the year under review”;
- iii. “...the contract does not clearly state that percentages are to be applied as the basis of payment”;
- iv. They “were unable to assess the accuracy or eligibility of the project management labour cost”; and,
- v. SNC O&M was unable to “provide a breakdown of costs specific to the categories Disbursements and Commissioning”.

2.11 The above noted concerns appear to be similar in nature to the issues/concerns raised in the OCRO Report with respect to SNC O&M’s PM Labour.

2.12 The ASC’s audit reports were submitted to PWGSC for their review of audit findings and to determine next steps on March 13, March 30 and June 25, 2009. The audit reports identified a total cost audit adjustment amount of [*] out of \$122,459,162 costs which were subject to audit for the three audited regional portfolios. SNC O&M advised us that after a review of the ASC audit reports that their position with respect to the error in amounts charged should be \$128,218.

2.13 We understand that SNC O&M has submitted payment in the amount of \$128,218 with respect to the audit adjustments. We also understand that PWGSC has cashed the cheque from SNC O&M in the amount of \$128,218. The remaining amount of [*] requires further investigation by PWGSC. It is PWGSC’s position that the acceptance of this reimbursement from the current audit findings will not

prejudice PWGSC's rights for any further reimbursements to be identified as a result of their further investigation or any subsequent audit results.

2.14 We have not verified, as it is outside of the scope of our mandate, the determination of the audit adjustment amounts noted above.

Supporting Documentation

2.15 In Phase 1, the audit, consisting of specified forensic audit procedures, required us to complete an analysis of all supporting documentation in relation to the Transactions. Our observations with respect to this matter are as follows:

- i. The AFD Work Orders prepared by SNC O&M and submitted to PWGSC for their approval contain the total Subcontractor Costs, the PM Labour, Management Fee and taxes. The AFD Work Orders did not contain any details with respect to the breakdown of the subcontractor's costs i.e. time and material.
- ii. SNC O&M's invoices issued to PWGSC for payment also did not contain any detail with respect to subcontractors' costs.
- iii. The files maintained by both PWGSC and SNC O&M were not sufficiently complete to provide support for the amounts charged by SNC O&M to PWGSC. PWGSC advised us that they have committed in their management action plan to conduct a review to determine what level of detail is required on AFD Work Orders and invoices and what supporting documentation is required on file by both PWGSC and SNC O&M.

2.16 The above noted findings have been brought to SNC O&M's attention and they are of the belief that such information is not required under the current terms of the SNC Contracts. SNC O&M further advised that should PWGSC wish to review the level of detail required on AFD Work Orders, they would be pleased to be part of this review.

2.17 In light of the foregoing, SNC O&M, PWGSC and ourselves had to contact the Subcontractors to obtain further details.

Administration of Contracts

2.18 During the course of Phase 1 of the audit, consisting of specified forensic audit procedures, we conducted interviews with several PWGSC employees. Based on

the information obtained during these interviews there appears to have been concerns raised within PWGSC with respect to SNC's accountability to report on their actual pass-through costs incurred to ensure there was no mark-up for overhead or profit. PWGSC has engaged us to further investigate this issue.

Recommendations

2.19 Based on our observations summarized in the above section, and our work in support of Chapter 1 of this Report, we provide our recommendations in the following paragraphs.

OCRO Report

2.20 We recommend that PWGSC continue to address the concerns and recommendations that remain outstanding from the OCRO Report.

Financial Cost Audits

2.21 PWGSC proactively follow-up on any audit adjustments identified in the Financial Cost Audits conducted by ASC. We understand that PWGSC has incorporated the recovery of any audit adjustments in their management action plans.

2.22 We understand that since the commencement of the SNC Contracts, PWGSC has commissioned Financial Costs Audits on three (3) regional portfolios. We also understand that PWGSC recently launched cost audits covering the eight (8) regional portfolios. We recommended and PWGSC concurred to prepare a cost audit strategy to provide more frequent and regular coverage of the administration of the SNC Contracts.

Supporting Documentation

2.23 Both SNC O&M and PWGSC's files lacked sufficient supporting documentation with respect to the details of subcontractors' cost quotes. SNC O&M's files contained quotes from the subcontractors; however, SNC O&M requested further supporting documentation and a cost breakdown from the Subcontractors which was obtained on March 10, 2010, for Transactions #1, #3 and #5.

2.24 It is SNC O&M's belief that such detailed information is neither required nor relevant under the SNC Contracts. We recommend that PWGSC reviews the standards for both the required documents to be maintained in the project files and the level of detail required to ensure that all cost quotes submitted by SNC O&M for approval contain sufficient supporting information. This will result in SNC O&M obtaining the necessary detail required for its files and also provide PWGSC with sufficient detail for assessment/authorization purposes.

Other Recommendations

2.25 As noted in Chapter 1 of this Report, we concluded that the Subcontractor's Costs for Transaction #7 appear to be unreasonable. PWGSC advised us that a financial settlement has been reached with SNC O&M with respect to these extra cleaning services. We recommended that PWGSC:

- i. Conduct a review of all of their files for any other additional cleaning services that SNC O&M may have provided under any of the SNC Contracts;
- ii. Determine whether or not the associated costs were calculated in accordance with the contractual agreement between SNC O&M and the cleaning subcontractor; and
- iii. Determine next steps, if required, including any request for recovery.

2.26 As noted in Chapter 1 of this Report, we could not confirm the exact date(s) that the Subcontractors performed the work in relation to any of the Transactions. SNC O&M stated that the SNC Contracts do not stipulate that they are required to maintain records of when Subcontractors attend to perform the work for particular projects. We recommend that PWGSC review this matter and determine what documentation/procedures are required to track the exact date and location that subcontractors are attending and what documentation/process SNC O&M should maintain/implement.

2.27 As outlined in Chapter 1 of this Report, PWGSC clarified that extra cleaning should be a PM Service and therefore subject to a lower management fee rate than that charged pursuant to PD Services. We recommend that PWGSC:

- a) Review their records to assess the extent to which such extra cleaning services have been rendered since the commencement of the SNC Contracts with respect to assessing the extent of any management fee discrepancy;
- b) Consider any other services that may be provided as PD Services which should be considered PM Services; and
- c) Determine next steps including resolution of any discrepancies.

Appendix 2 – A

Appendix 2 - A

Restrictions and Qualifications

1. This Report is not intended to be used for any purpose other than as stated in our Report without our prior consent. We do not assume any responsibility for losses occasioned to readers of this Report or other parties as a result of the circulation, publication, reproduction, or use of this Report or its contents contrary to the provisions of this paragraph. We will not assume any responsibility to any third party to which this Report is disclosed or otherwise made available.
2. In the event that further documents or information become available that could impact our findings, we reserve the right, but are under no obligation, to review such records and reconsider and amend the findings set out in this Report.
3. We have not, as it is not part of our engagement, secured or reviewed electronic communications or electronic documents.
4. Although we attempted, where possible, to verify the completeness of documentation there may be other relevant documentation.
5. Interviews were not conducted with those individuals no longer employed by PWGSC or SNC O&M in relation to the Transactions.
6. This Report is based on our review of the documents and information available to date. Our review does not constitute an audit, as defined by Generally Accepted Auditing Standards prescribed by the Canadian Institute of Chartered Accountants, and we do not provide an audit or review opinion. We have not attempted to audit or otherwise verify the information presented to us beyond the expressed scope stated in this Report.
7. This Report makes references to payments made to SNC O&M by PWGSC). We have obtained the information relating to these payments from PWGSC's internal reporting system; however, we have not specifically reviewed these payments.
8. Our Report, including any schedules and appendices, must be considered in its entirety by the reader. Selecting and relying on specific portions of the analyses, or factors considered by us, in isolation may be misleading.
9. We make no representation regarding matters of legal interpretation.