



**AUDIT OF
THE CONTRIBUTIONS FOR
THE NORTHERN DIMENSION PROGRAM**

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**Foreign Affairs Canada
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Audit Division (ZIV)**

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EXECUTIVE SUMMARY

The Internal Audit Division (ZIV) undertook an audit of the management of the contributions for the Northern Dimension Program as part of its review of Departmental Grants and Contributions. The objective of the audit was to determine the extent to which the contribution program was managed with sound comptrollership practices and complied with legislative and regulatory requirements.

We observed that some good management and administrative practices are in place. Overall, three of the five audit objectives were achieved. The contribution agreements were found to be in agreement with the majority of the requirements of the TB and Departmental Transfer Payment Policies. However, we noted opportunities for improvements to ensure that program funds are managed with due diligence and that payments are made in accordance with the policies. Specifically, these opportunities relate to:

- compliance with all the Program's Terms and Conditions;
- justification and timeliness of expenditures;
- implementation of a formal mechanism for contribution agreement amendments; and,
- the management of the process involved with recipient audits.

A total of five audit recommendations are raised in the report and all are addressed to the Northern Dimension Program. Management has responded to each recommendation indicating action already taken or decision made, as well as future action. Management has stated that all five recommendations have been implemented.

OVERVIEW

1.1.1 The Northern Dimension of Canada's Foreign Policy (NDFP) was announced by the Minister of Foreign Affairs on June 8, 2000. The announcement also included a commitment of \$10 million over five years, from a reallocation of existing departmental resources. Details of the policy were ratified by Cabinet in September 2000.

1.1.2 Treasury Board approved the terms and conditions for the creation of a new Class of Contributions in support of the FAC Northern Dimension of Canada's Foreign Policy.

1.1.3 NDFP is framed by three principles - meeting our commitments and taking a leadership role; establishing partnerships within and beyond government; and engaging in ongoing dialogue with Canadians, especially northerners. In keeping with this framework, the NDFP has four overarching objectives:

1. To enhance the security and prosperity of Canadians, especially northerners and Aboriginal peoples;
2. To assert and ensure the preservation of Canada's sovereignty in the North;
3. To establish the Circumpolar region as a vibrant geopolitical entity integrated into a rules-based international system; and,
4. To promote the human security of northerners and the sustainable development of the Arctic.

1.1.4 These objectives have been pursued through a focus on five priority areas for action over several years: (1) strengthening the Arctic Council; (2) helping to establish the University of the Arctic and enhancing a Canadian and Circumpolar research network; (3) strengthening co-operation with northern Russia; (4) promoting sustainable development through economic and trade opportunities; and (5) implementing the Canada-EU Joint Statement on Northern Cooperation.

1.1.5 While the Northern Dimension Program is managed by the Aboriginal and Circumpolar Affairs Division (AGA), its benefits affect a large number of divisions and missions, as well as FAC's relationships with a number of key domestic departments, from which it serves to leverage matching funds.

1.1.6 As it is focussed on the circumpolar region, the NDFP has become a key component of Canada's bilateral relations with the other seven Arctic key partner countries: Russia, the United States (Alaska), Norway, Iceland, as well as the European Union and the three countries that are members of both the EU and the Arctic Council (i.e., Finland, Sweden and Denmark - including Greenland). The Northern Dimension of Canada's Foreign Policy provides resources to support cooperative activities

undertaken by Missions and by geographic divisions to advance Canada's bilateral relations. It is also the instrument to implement high-level political commitments such as the 1999 Canada-EU Joint Declaration on Northern Cooperation, or December 2000's Joint Statement between Canada and the Russian Federation of Cooperation in the Arctic and the North.

1.1.7 The NDFP also represents one of the major sources of funding for Canada's participation in the Arctic Council, the principal international forum where circumpolar issues are addressed.

1.1.8 Approximately half of the funding for the NDFP is provided in the form of contribution funds (Vote 10). This allows the Department to enter into joint projects with other levels of government, Indigenous organizations, non-government organizations, academic institutions and others throughout Canada that have interests in the North.

1.1.9 ZIV supported the program in developing its Risk-Based Audit Framework (RBAF) in February 2001 and overall, the level of risk associated with funding the NDFP is considered to be medium. The overall risk is assessed as medium because of such factors as *** the diversified number of partners and target groups seeking financial support; the total program value; recipients that are both inside and outside Canada; the many and varied recipients; the almost unlimited scope for action; the variable interest; willingness of potential partners to cooperate ; the requirement to reallocating FAC resources from competing programs to fund the NDFP; and finally, the need for a close partnership with many partners and target groups.

SCOPE, OBJECTIVES AND METHODOLOGY

2.1 Scope

2.1.1 This audit focussed on the administrative practices, processes (systems) and controls related to the management of the contributions for the Northern Dimension Program. The contribution agreement is in effect for the fiscal years 2000/01 to 2004/05. The Audit Team audited the contribution program in accordance with Treasury Board and Departmental Transfer Payment Policies.

2.2 Objectives

2.2.1 The overall objective was to determine the extent to which the contribution program was managed with sound comptrollership practices and complied with legislative and regulatory requirements. In particular, the audit focussed on determining whether:

- the contribution agreement was justified under appropriate authorities;
- the contribution agreement was prepared in accordance with FAC's Policy on Transfer Payments;
- the terms and method of payments were in compliance with Treasury Board approved terms and conditions;
- the Program Officers conducted project monitoring; and,
- there is an adequate management process concerning contribution recipient audits.

2.3 Methodology

2.3.1 The audit examined the major business processes and key controls associated with the management of the contribution agreements at FAC. The contribution files examined were dated from the onset of the program, i.e. 2000/01, with a focus on the years 2002/03 and 2003/04.

2.3.2 We conducted a comprehensive review of relevant program documentation and interviewed key personnel in the Northern Dimension Program, Area Management Office (IAM), and Corporate Finance, Planning and Systems.

OBSERVATIONS AND RECOMMENDATIONS

3.1 Practices and Processes

3.1.1 NDFP's Terms and Conditions state the following points:

- a) Under Stacking, #2.3: The Program will require all potential recipients to disclose all sources of funding for a proposed project at the start and end of a project.

The Program does not currently ensure that all recipients provide this information.

- b) Under Application Documentation, # 2.4: For contribution requests, potential recipients must submit a proposal describing the project, its objectives, implementation plan and time frame, potential risks, total estimated budget, total government assistance being sought from other sources and total being sought from the NDFP. A standardized application process will be developed for all potential recipients who submit a proposal.

The application process does not ensure that potential recipients provide all the above-stated information.

- c) Under Payments, #3.4: ...advances shall be based on prudent cash management principles reflecting the immediate cash requirements of the recipient...

Where advances are issued in several installments, cash flow information is not always provided/requested.

- d) Under Management Framework, #4: The NDFP will use an electronic project tracking and management system which, for each proposal, will track applicant information.

The Audit Team observed that applicant information is either captured in the spreadsheet "NDFP Implementation", or is held in the application file itself. No electronic tracking and management system exists.

Recommendation for AGA

- 3.1.2 **AGA should ensure compliance with all the Program's Terms and Conditions regarding the sections on "Stacking", "Application Documentation" and " Payments", as stated above.**

Regarding the section “MANAGEMENT FRAMEWORK”, AGA should amend the Terms and Conditions to reflect the current project tracking and management system.

AGA Action and Time Frame

3.1.2 AGA has a standardised system in place that requires all recipients to provide information on stacking, relevant application documentation and cash flow information. Furthermore, an enhanced electronic tracking system has been implemented.

3.2 Monitoring, Contribution Payments and Program File Management

3.2.1 AGA monitors, for quality and relevance, the project reports received from the recipients and where needed will consult with the proper authorities before proceeding with the payment process. When the reports or other outputs have been accepted, the documents submitted with the request for payment are reviewed by the Officer for payment approval. The acceptability of all submitted expenditures is determined by the responsible officers. However, there is no evidence on file indicating a follow-up of expenditures that are questionable by their nature and timing. For example:

- expenditures reported in financial statements that have occurred after the end of the contribution agreement; and,
- administrative expenditures for an entire year submitted for reimbursement the day after the contribution agreement was signed.

In addition, results of recipient audits reflect the need to increase scrutiny.

Recommendation for AGA

3.2.2 AGA should ensure that all expenditures are clearly justified, timely and relevant.

Action Plan and Time Frame

3.2.2 As part of the standardised system implemented, one officer manages the record keeping which ensures consistent document management and effective scrutiny of all expenditures. Requests to include already incurred expenses are provided by the recipient when Contribution Agreements are signed by both parties after verbal agreement, and after some expenses have already been incurred. AGA is in regular contact with recipients and guidelines on financial reporting requirements are sent to all recipients. Follow-up with recipients is done at the beginning of the fourth quarter to ensure that they will have all their documentation in on time.

3.2.3 Contribution files were found to be incomplete and disorganized. Not all the information pertaining to an application is on file. For example, application requests; e-mails that stand as proof that the contribution agreement has been approved by SMFH before being finalized; and final reports are not always placed on file. This situation was brought to the attention of AGA's management who, during the course of the audit, took corrective action to complete and organize all current and open files.

Recommendation for AGA

3.2.4 AGA should ensure that all contribution files are complete and organized.

AGA Action and Time Frame

3.2.4 All contribution files are now complete and organized.

3.2.5 Accounting records and other relevant documents are maintained and disclose the amounts paid to recipients.

3.2.6 The contribution agreement was found to be in agreement with the majority of the requirements of the TB and Departmental Transfer Payment Policies. The contribution agreement respects the template as set out by SMD.

3.2.7 Amendments to the contribution agreement are communicated informally through a letter to the recipient. There were no amendments to the contribution agreement reflecting the changes.

Recommendation for AGA

3.2.8 AGA should ensure that all amendments are reflected in a new agreement and approved by SMFH.

Action Plan and Time Frame

3.2.8 All amendments which are requested to contribution agreements are sent to SMFH for approval. The email documentation of correspondence with SMFH is kept on file under the respective contribution agreement. Amendments are sent to the recipient for their signature and kept on file as well as sent to IAM.

3.3 Management of Contribution Recipient Audits

3.3.1 With respect to finalizing the recipient audit report, there is a lack of coordination between the Department and the recipient. Program management is responsible to conclude the process to the satisfaction of all involved. This includes

resolution of any disagreement between the Department and the recipient, as well as determining if recovery of audit adjustments will be initiated by SMD through an invoice or from subsequent recipient payments. In the latter case, this recovery process needs to be controlled by program management.

Recommendation for AGA

- 3.3.2 AGA should ensure proper management of the process involved with recipient audits, at all stages, including the conclusion stage.**

AGA Action and Time Frame

- 3.3.2 AGA works in close collaboration with ZIV on all recipient audits. AGA determines which recipients should be audited and then informs ZIV. AGA contacts the recipients (by email and telephone) to let them know that an audit is planned and also introduces ZIV to the recipient. Once the audit is completed, ZIV provides a copy of the draft audit to both the recipient and AGA. If necessary, AGA provides comments to the draft audit report. If follow-up is required, AGA discusses options with ZIV.**