



Western Economic
Diversification Canada

Diversification de l'économie
de l'Ouest Canada

Audit of First Jobs in Science and Technology

WESTERN ECONOMIC DIVERSIFICATION CANADA

Audit, Evaluation & Ethics Branch

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1.0 Executive Summary

1.1 The audit of First Jobs in Science and Technology (FJST) is an internal audit assurance engagement to report on management controls used to deliver FJST, and to identify any opportunity for improvement that could be applied to future programs. The audit topic is identified in the Western Economic Diversification Canada (WD) 2008 – 2011 Risk Based Audit Plan. The audit examined evidence of the effectiveness of management controls that were in place for the delivery of the FJST program and to provide assurance to WD Senior Management whether or not payments made to recipients were in accordance with the terms and conditions of the program. The audit examined the extent to which management controls for the FJST program met the standards and criteria established by the Treasury Board of Canada Secretariat (TBS) Policy on Transfer Payments.

Findings

1.2 The audit found that overall the FJST program was reasonably managed during the audit period and until its discontinuation in 2005. There were appropriate controls for disbursing payments to recipients in accordance with the terms and conditions of contribution agreements.

1.3 Results of the criteria examined are summarized as follows:

Criteria	Assessed Results
A business risk and management control framework exists	Criteria mostly met
Projects qualified for funding	Criteria met
The company and graduate were eligible and qualified	Criteria mostly met
WD complied with appropriate authorities	Criteria met
Claims and payments were supported with adequate documentation	Criteria mostly met
WD performed sufficient due diligence throughout the project life cycle	Criteria partially met

1.4 The audit work identified opportunities for improvement. Most of the opportunities for improvement have already been implemented based on recommendations from other recent audit engagements on grants and contributions that have occurred since the FJST program was discontinued in 2005. The specific gaps identified through this audit were:

- Risk levels, once assessed at the project approval stage, were not reassessed during the project life cycle;
- Insufficient documentation of risk mitigation strategies was developed and kept on file when unusual circumstances were encountered;

- The monitoring approaches used could have been more rigorous given business and inherent risks associated with most of the small and medium enterprise recipients; and
- There was a general lack of evidence in measuring project results.

Conclusion

- 1.5** In summary, controls established for the FJST program by management were reasonably effective in design and operated satisfactorily. Based on internal audit standards and criteria selected, sufficient audit work has been completed and analyzed to support the conclusion that the management control framework for which WD management is responsible was appropriate for the size and risks of the FJST program.
- 1.6** In accordance with the Government of Canada internal auditing standards, a reasonable assurance is provided that relevant and reliable management controls existed for the delivery of the FJST program from 2002 through to 2005 when the program ceased.
- 1.7** In addition, opportunities for improvement have been identified in this report where those controls can be strengthened in order to mitigate risk and contribute to management excellence for future programs of similar design and delivery.

2.0 Introduction

2.1 The FJST was introduced in March 1997 to assist small and medium enterprises to develop a workforce of science, technology and engineering professionals. The program provided small businesses with the necessary assistance to enhance their competitive positions through technological adaptation and innovation. Assistance was provided to organizations employing recent graduates who assisted firms with the development and adoption of productivity enhancing technologies.

Audit Context

2.2 It is possible that in the future, WD may be tasked to offer business assistance programs similar to the FJST that WD discontinued in 2005. To support WD's commitment to management excellence, it is prudent to undertake an end-of-program internal audit to assess the effectiveness of the controls used to deliver programs like FJST, and to identify any opportunity for improvement that could be applied to future programs of similar design and delivery. The lessons learned from this audit and the audit of International Trade Personnel Program, a similar program that was also recently audited, will be beneficial in future program planning and design.

Audit Scope

2.3 The FJST was announced in March 1997 and discontinued in 2005. To ensure the relevance and currency of the audit findings, the audit period was limited to project payments and approval transactions completed from April 01, 2002 to March 31, 2007. While project approvals ceased in 2005, WD commitments were honoured until 2007. This department-wide audit covered all WD regions and headquarters.

Audit Objectives

2.4 The objectives of the audit were:

- To assess the controls that were in place for the FJST and their effectiveness;
- To provide WD Senior Management with assurance whether or not payments made to recipients were in accordance with the terms and conditions of the programs; and
- To make recommendations for control and due diligence improvements for future programs of a similar design and delivery.

Audit Criteria

2.5 The audit criteria were drawn from contribution agreement terms and conditions, other government wide post-graduate initiatives, WD's due diligence – program assessment review procedures, and the TBS Policy on Transfer Payments. The selected audit criteria to guide conduct of the audit were:

- A business risk and management control framework exists;
- Projects qualified for funding;
- The company and graduate were eligible and qualified;
- WD complied with appropriate authorities;
- Claims and payments were supported with adequate documentation; and
- WD performed sufficient due diligence throughout the project life cycle.

2.6 The results of examining these criteria have been summarized based on four ratings:

- (4) Criteria met;
- (3) Criteria mostly met;
- (2) Criteria partially met; and
- (1) Criteria not met.

Risks Assessed

2.7 The FJST audit assessed the following program-specific risks to ensure that the management control framework was sufficient to mitigate the following:

- WD program objectives were not met;
- Federal values and ethics were not respected;
- Non-qualifying projects were approved;
- Recipients were not eligible companies;
- Individual beneficiaries were not recent graduates;
- WD did not apply appropriate due diligence in monitoring the program's success; and
- Disbursements were not made in accordance with terms and conditions of contribution agreements.

3.0 Observations and Recommendations

(i) Management Controls

Audit expectations were:

- That management had an appropriate framework in place to set program direction, precedents, procedures, program objectives and priorities;
- That a contribution agreement setting out the terms and conditions of the project existed;
- That a sound project assessment review framework with decision sign-off stages was in place and well understood by project officers;
- That eligibility of projects, graduates and documentation was communicated and appropriately applied throughout the project cycle
- That authorities and limitations were structured, clarified and communicated;
- That management compared results achieved against expectations on a periodic basis; and
- That program evaluation activities were used to identify program strengths, weaknesses and impacts as well as alternative ways of program delivery.

Management Framework

- 3.1** The FJST program was reasonably managed. There were appropriate controls for screening and approving projects. While procedural memos, precedents and instructions existed in various forms in the regions and headquarters between 1997 and 2002, key uniform strategic directives were initiated March 2002 onwards by the Deputy Minister and the program-operations directorate to guide the renewal and administration of the FJST program until its elimination in 2005. Implementation, administration, eligibility, cut-off dates, promotion and procedural rules were streamlined and clarified in ensuing memos. Such documentation provided the authoritative design and reference sources for staff to effectively and consistently deliver the program.
- 3.2** Projects examined were appropriately approved within the time limitations and within the dollar limits set. Projects and graduates were found to be eligible and met the program criteria. Corporate registry searches were done where warranted. Clarifications were sought where needed. In some cases, the facts were noted on file, while other times there was only a diary that client was spoken to without further details.
- 3.3** A formative evaluation of FJST was done in 2004. The evaluation concluded that the program was relevant, making impacts and contributing to success for small and medium enterprises. There were differing views on whether the program should be delivered by WD or by a third party.

- 3.4** Documentation for more than twenty audit program points that were tested was generally strong. However, 12 of the 64 sample project files had at least one issue associated with the examination against the various audit program points reviewed for each file. Of particular note, at the initial stage of hiring it was sometimes hard to verify the under-employment of the graduate and there was no evidence on file to confirm this fact. In speaking with program officers, many felt that if the employee was willing to accept this job at that salary, then they must be under-employed. Management considered this program, overall, to be a low risk program. As such, WD did not require any further evidence on file to verify the under-employment status of graduates.
- 3.5** Table 1 summarizes the main points from the audit verification results of the sample files examined:

Table 1: Sample Analysis

Description	Total	Percentage
Number of active projects in audit period	402	
Number of sample projects examined	64	
Percentage of sample size to population files		16%
Project Files examined by audit	64	100%
Project Assessment Review Risk Ranking of sample		
Low	56	88%
Medium	6	9%
High	0	0%
No assessment found on file – outside audit period	2	3%
Audit Exception Summary:		
Files with exceptions to the file review criteria established	5	8%
Files with an unusual matter without clear documentation to support resolution of the matter on file	12	19%

- 3.6** The challenge was that over 88% of the projects examined were rated as low risk. It was apparent from files reviewed that the risk assessment completed was weighted heavily on the fact that the maximum contribution of \$20,000 was deemed as being of low significance compared to the higher contribution amounts regularly funded under other WD programs. None of the projects were assessed as high risk, and only 9% were rated as medium risk.
- 3.7** For independent audit analysis purposes, the majority of the clientele served by the program were small and medium enterprises, which often have limited resources to apply to the administration of government programs. That factor in itself becomes an inherent

risk of high concern for any direct government assistance program. There have been examples in the past where other government departments have not adequately mitigated these risks.

- 3.8** Internal Audit considered that the 88% rate of low risk ranking across the population was likely far too low considering all the available risk indicators. The low dollar value may have weighed too heavily in the risk assessment.
- 3.9** Overall, the opportunities for improvement were assessed as low risk given consideration to significance, the program's elimination in 2005, and potential impact given that WD currently does not deliver any similar programs. Continuous improvement efforts have already taken place based on recommendations from recent audits around the overall management and administration of grants and contribution programs. Therefore, the recommendations listed will only apply to future programs of similar design and delivery.

Recommendation #1: If and when WD establishes similar programs in the future, project specific risk should be reassessed periodically. Risk is not static and needs to be revisited throughout the life cycle of the project.

(ii) Monitoring and Results

Audit expectations were:

- That external and internal environments were monitored to obtain information that may signal a need to re-evaluate risks and WD's objectives;
- That appropriate and timely progress reports and claim documentation was communicated;
- That financial and non-financial reporting was reviewed and approved;
- That the rigour and evidence of monitoring was commensurate with risk level;
- That processes were in place to monitor financial and operational performance on an ongoing basis; and
- That adequate and appropriate documentation supported claims.

3.10 There were appropriate controls for disbursing payments to recipients. Pay stubs, T4s and payroll registers were used to validate salaries as appropriate. Progress reports were requested from recipients and were received. Prior to payments progress reports were requested and were received. Payments made were within the limits indicated in the project approval records. Where funds were not entirely spent, they were de-committed. Companies met their obligations under the WD terms and conditions.

3.11 There were notes on file about consultations with supervisors and reasons for decisions made. In a few instances though, rationale for disposal of unusual situations could have been better documented and these conditions are discussed in more details below.

- 3.12** In more than 35% of the samples tested, claims were not filed quarterly, but rather at the end of the project where the entire qualifying amount was then being claimed. A number of the graduate employees had already left the company before the claims were submitted. This would have hindered any opportunity for WD to contact the graduates to confirm that program objectives were still being met.
- 3.13** There was no evidence of site visits by WD officers to validate progress reports. There was little documentation on file to confirm that alternate procedures, such as site visits or interviews, had been done to minimize the risk of misrepresentations in the progress reports. There was heavy reliance on the companies receiving the money to accurately state the duties of the person being hired. There was little verification done by WD to confirm that the employer's claims represented what the employee was actually doing and was still eligible for funding.
- 3.14** For those projects ranked as medium risk in the sample selected, there was no documentation on the file to suggest that their claims processes adopted were any different from those applied to the low risk files. The same standardized claims review method applied whether the recipient had been rated low or medium risk. Despite the fact that some applicants were first-timers and others were repeat applicants, there was nothing on the files to indicate any more or less rigour of monitoring.
- 3.15** Quality and completeness of the documentation on file could have been improved. 19% of sample files tested were missing one thing or another. These included:
- Three instances where limitation on project amounts had changed but this was not realised until the last claims;
 - Nine instances where situations of under-employed and its relation to starting salary or salary rate at last employment seemed questionably subjective without insufficient documentation on file;
 - Four instances files were not updated with completed amendments and schedules but just preceding emails correspondence;
 - Four instances where graduates moved from one company to another separate company and thus effectively they were under FJST for over 12 months; and
 - Four instances where graduates were hired before degrees were actually obtained.
- 3.16** WD could have tightened up its due diligence and monitoring processes to ensure that unusual circumstances encountered during the life of the project were fully documented to provide an adequate audit trail.
- 3.17** Internal Audit found that there was no requirement for final project reports to analyze and demonstrate accomplishments to ensure linkages to program objectives and results.

3.18 From the files reviewed, it appears that delegation of the project assessment and monitoring to less experienced staff was the norm. However, there was no evidence on file that senior staff had reviewed and agreed with the assessment and the level of monitoring action taken even though claims and project assessment review forms were signed by the appropriate level of authority.

Recommendation # 2: WD should tailor its due diligence and monitoring processes to be commensurate with the level of risk assessed.

Recommendation # 3: WD should ensure that files contain adequate documentation when unusual circumstances are encountered. At a minimum, there should be documentation on file to both support and explain any key decisions rendered on the project by an appropriate level of management.

Conclusion

3.19 In summary, the controls established for the FJST program by management were reasonably effective in design and operated satisfactorily. Based on internal audit standards and criteria selected, sufficient audit work has been completed and analyzed to support the conclusion that the management control framework for which WD management is responsible was appropriate for the size and risks of the FJST program.

3.20 In accordance with the Government of Canada internal auditing standards, a reasonable assurance is provided that relevant and reliable management controls existed for the delivery of the FJST program from 2002 through to 2005 when the program ceased.

3.21 In addition, opportunities for improvement have been identified in this report where those controls can be strengthened for future programs of similar design and delivery.

4.0 Audit Strategy and Approach

Planning

- 4.1** The audit planning work started January 2008 and audit examination ended in April 2008. Sources of reference reviewed included: TBS Policy on Transfer Payments, Government of Canada Post-Secondary and Youth job programs, WD Corporate Risk Profile, and previous WD audit reports of relevance in assessing risk. Other background materials about FJST were reviewed in order to acquire deeper knowledge of the program and to identify risks. Materials from sample contribution agreements, the Treasury Board Secretariat, the Office of the Auditor General reports, and the Institute of Internal Auditors were utilized in selecting audit criteria and developing audit program. Based on knowledge gained of the program and its challenges, Internal Audit examined the selected management controls and assessed the identified risk.

Standards and Methodology

- 4.2** Government of Canada internal auditing standards were used in conducting and reporting on the audit. Emphasis was placed on factual evidence, analyzing evidence, and associated documentation. The audit objectively analyzed conditions with objectivity and against risk exposure, significance, cause and probable effect. Recommendations were selected based on risk exposure, significance, and actionable added-value points that will contribute to management excellence.
- 4.3** The option of interviewing recipient staff and/or former graduate employees where necessary was left open to be assessed after analyzing internal WD documentation files, resources, risk and current management control frameworks.
- 4.4** Consideration was given to the results of the follow-up of previous related audits and the extent that management action plans have been implemented to date. Some of the recommendations arising from previous audits from 2005 to 2007, and a formative evaluation of the program done in 2004, apply to the issues observed in this audit.
- 4.5** Through a follow-up of the previous audits, Internal Audit was able to conclude that since 2005 management controls have improved significantly in terms of project review assessment processes and monitoring and payment processes.

Sampling

- 4.6** Judgemental random sampling, based on stratified dollar amount ranges within the population, was used to select project files for testing. Table 2 summarizes the population of the program between 2002 and 2007 and details of the sample projects selected for testing:

Table 2: Audit Period FJST Population

Description	Total	Percentage
Program claims for 2002 – 2005 audit period projects	\$8,851,000	100%
Dollar value of sample projects examined	\$1,631,967	18%
Number of active projects in audit period	402	100%
Number of sample projects examined	64	16%

Audit team

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Acronyms - Glossary

FJST	First Jobs in Science and Technology
WD	Western Economic Diversification Canada
TBS	Treasury Board of Canada Secretariat

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