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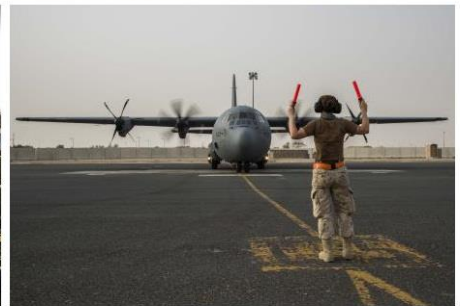
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ASSISTANT DEPUTY MINISTER (REVIEW SERVICES)



Reviewed by ADM(RS) in accordance with the *Access to Information Act*. Information UNCLASSIFIED.

## Non-Public Property Audit of Specialty Interest Activities—Part 1: Financial Sustainability



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Canada

## Caveat

Non Public Property (NPP) is created under the *National Defence Act* (NDA). The purpose of NPP is to provide benefit to serving and former members of the Canadian Armed Forces (CAF) and their families or for any other purpose approved by the Chief of the Defence Staff (CDS). Each unit's NPP is vested in the commanding officer of that unit.

NPP is a unique type of crown property, the governance of which is assigned to the CDS. Pursuant to subsection 41(1) of the NDA, the CDS shall exercise his authority subject to any directions that may be given to him by the Minister.

Subsection 41(3) of the NDA provides that the *Financial Administration Act* does not apply to NPP. Revenues from NPP operations constitute NPP pursuant to section 2 of the NDA.

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## Acronyms and Abbreviations

ADM(RS)	Assistant Deputy Minister (Review Services)
B/W/U	Base/Wing/Unit
CAF	Canadian Armed Forces
CFMWS	Canadian Forces Morale and Welfare Services
CFO	Chief Financial Officer
CNA	Community Needs Assessment
FY	Fiscal Year
MD NPP	Managing Director, NPP
NPP	Non-Public Property
OHS	Occupational Health and Safety
OPI	Office of Primary Interest
PSP	Personnel Support Program
RAM	Regional Accounting Manager
SIA	Specialty Interest Activity
Sr VP PSP	Senior Vice President Personnel Support Program

## Foreword

This audit was included in the NPP Risk-based Audit Plan for Fiscal Years (FY) 2017/18 to 2019/20. The audit objective was to provide assurance on the adequacy and effectiveness of the existing governance framework supporting Specialty Interest Activities (SIA), and to assess compliance with environment, health and safety regulations and policies. The audit's two distinct lines of inquiry are being reported in two separate parts.

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**Note:** Please refer to [Annex A—Management Action Plan](#) for the management response to the ADM(RS) recommendations.

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## 1.0 Introduction

### 1.1 Background

Specialty Interest Activities (SIA) are an important part of military culture providing military personnel, their families and the broader Defence community an opportunity to socialize and engage in group or individual leisure activities within their local communities. At the individual level, SIAs contribute to physical, social and familial wellness while collectively they help foster esprit de corps and develop unit morale, all with the aim of contributing to operational readiness of the CAF.

Specialty Interest Activities on Bases/Wings/Units (B/W/U) can include the following:

- golf clubs
- curling clubs
- marinas and sailing
- horse riding clubs
- rod and gun clubs
- campgrounds and cabins
- food and beverage services

Specialty Interest Activities focus on serving the military, their families and Defence community with excess capacity open to the general public. They are operated as social enterprise businesses, with the goal of being financially profitable and sustainable while re-investing profits in the Defence community. In FY 2018/19, there were 39 SIAs in Canada administered through Personnel Support Programs (PSP) with four entities managed as external concessions. In FY 2017/18, SIAs had a combined asset value of \$17.4 million and generated revenue of \$14.7 million. During the same fiscal period, SIAs in Canada produced \$188,989 in net income.<sup>1</sup>

In cases where an SIA is not financially sustainable, the activity may be discontinued or run as a concession by a third party. All SIAs operate under the umbrella of the B/W/U fund as NPP Morale & Welfare activities and are managed by the Senior Manager PSP on the B/W/U.

Existing policies permit portions of an SIA operation to be publicly supported based on the premise that CAF personnel and their families should have access to a reasonable level of goods and services similar to a progressive Canadian community. The local public/non-public resources provided may vary over time and between locations depending on resources available and the Commanding Officer's assessment of the SIA's needs against other priorities. The decision to provide additional resources is at the discretion of the Commanding Officer. B/W/U Commanders are ultimately accountable for the SIAs on their B/W/U.

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<sup>1</sup> Excludes concessions and new SIAs that were created during the financial audit review period of FY 15/16-17/18.

## 1.2 Objective

The objectives of this audit were as follows:

- To assess the adequacy and effectiveness of the existing governance framework of SIAs in ensuring that SIAs remain financially sustainable (Part 1); and
- To provide assurance that the existing management control framework ensures compliance with applicable health and safety laws, regulations and policies including the *Canada Labour Code Part II* and Canada Occupational Health and Safety (OHS) Regulations (Part 2).

## 1.3 Scope

The scope of Part 1 of the audit included a review of both long and short-term financial plans and results for FYs 2015/16 to 2017/18.

The scope of Part 2 of the audit included the governance framework, OHS Committees and Health and Safety Representatives, training and awareness, and incident reporting. The audit also included control activities in support of key OHS legal requirements for the period extending from April 2016 to March 2018 at both the corporate and local levels.

## 1.4 Methodology

The following methodology was used to conduct the audit:

- Reviews of policies, directives, guidance documents, hazardous occurrence reports and meeting minutes (B/W/U Fund meetings and OHS meetings);
- Site visits to:
  - Kingston: Garrison Golf and Curling Club
  - Borden: Circled Pine Golf and Curling Club, Base Borden Rod and Gun Club
  - Edmonton: Edmonton Garrison Memorial Golf and Curling Club, Edmonton Saddle Club
  - Halifax: Hartlen Point Golf Club, Shearwater Yacht Club, CFB Halifax Curling Club, Falls Lake Cottages and Campgrounds
  - Greenwood: Greenwood Golf Club, Lake Pleasant Cottages and Campgrounds;
- Walkthroughs of SIA facilities at each site visited;
- Examination of SIA financial statements from FY 2015/16 to FY 2017/18; and
- Interviews.

## 1.5 Audit Criteria

The audit criteria can be found at [Annex B](#).

## **1.6 Statement of Conformance**

The audit findings and conclusions contained in this report are based on sufficient and appropriate audit evidence gathered in accordance with procedures that meet the Institute of Internal Auditors' *International Standards for the Professional Practice of Internal Auditing*. The audit thus conforms to the Institute of Internal Auditors' *International Standards for the Professional Practice of Internal Auditing* as supported by the results of the quality assurance and improvement program. The opinions expressed in this report are based on conditions as they existed at the time of the audit and apply only to the entity examined.



## 2.0 Findings and Recommendations

### 2.1 Planning and Risk Management

Planning and risk management activities are occurring formally and informally at both the local and Canadian Forces Morale and Welfare Services (CFMWS) division head level. At the local level, SIA business plans are completed by SIA managers and approved by Senior Managers PSP, with approval from B/W/U Commanders. CFMWS has developed an SIA entity plan template to support local managers in the development of business plans. In addition, budgeting and financial expectations are included in the business plan to complement risk management and planning activities. Proposed budgets are reviewed by local accounting staff, the Regional Accounting Managers (RAM) and the Senior Managers PSP to ensure programming, financial and delivery objectives are addressed.

Notwithstanding these stated practices, planning and risk management activities can be further complemented by gathering community feedback with respect to SIAs. The Community Needs Assessment (CNA) Survey is an existing market research tool used to advise, inform and justify programming decisions and funding for NPP activities on B/W/Us. Specialty Interest Activities policies and directives promote using the CNA as a primary tool for advising SIA decisions; however, CNAs are not being used in this capacity at the moment. An opportunity exists to leverage the CNA process to further inform decisions with respect to the creation and continuity of SIAs.

The CNA should include an environmental scan to determine whether the existence of an SIA is warranted. For example, if the activity is already offered by the local business community, there is a risk that an SIA may inadvertently compete with local privately run businesses. In FY 2017/18, sampled golf courses had, on average, eight or more private sector competitors in their local area. Although the CNA can show demand for a particular SIA, if the local business community can offer the service, CFMWS may wish to consider leveraging the existing services to fill a defined SIA need for B/W/U communities.

#### **ADM(RS) Recommendation**

1. It is recommended that CFMWS develop and communicate an SIA-focused section of the CNA that can be used to determine the ongoing and/or future need for an SIA. If it is deemed that adjusting the CNA to include the SIAs is not feasible, an equally effective alternative should be explored.

**OPI:** Sr VP PSP

## 2.2 Policies, Procedures and Guidelines

CFMWS has developed SIA policies, directives and manuals to govern the operation and implementation of SIA programming on B/W/Us. The governance framework provides guidance on the operation and delivery of SIA activities. The framework allows some flexibility to deviate from the policy when deemed necessary, with the approval from CFMWS division heads, based on an appropriate rationale. An example of a deviation is that policy dictates that the combined non-military membership at an SIA shall not exceed 50 percent of the total membership. Several SIAs have requested exceptions to this, citing financial sustainability as a rationale. Another example of deviation from the policy is the requirement for an SIA to have a membership committee, a constitution and by-laws. Some SIAs do not operate with a committee, which may expose risks such as:

- The control activities performed by the committee may be omitted.
- Projects, changes and management decisions might be made without consulting the membership base, which can cause conflict and/or dissatisfaction with SIA operations.

### 2.2.1 Financial Sustainability of Specialty Interest Activities

Policies require SIAs to operate as businesses with the goal of being financially sustainable. Differing interpretations across B/W/Us demonstrate a need to ensure the expectations with respect to the financial sustainability of SIAs are clearly defined. For example, some SIAs interpret sustainability as a positive net income where others interpret a net loss as acceptable as long as it is manageable by the B/W/U Fund. In addition, the acceptable amount of Public/Non-Public support that an SIA can accept in support of operations is not clearly defined within the policy.

From FY 2015/16 to FY 2017/18, 33 percent of year-end SIA income statements reported a negative net income.<sup>2</sup> This demonstrates the need for clarity with respect to expectations of sustainability to help ensure that B/W/U Fund health is not at risk due to SIA operations.

The varied interpretations and levels of Public/Non-Public support, create difficulties in assessing and evaluating the financial performance of SIAs in a consistent manner.

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<sup>2</sup> Excludes depreciation.

### ADM(RS) Recommendation

2. It is recommended that Managing Director NPP issue guidance or clarify what is considered ‘financially sustainable’ for SIAs. The guidance should recognize that SIAs operate within a number of different geographical and operational realities.

OPI: Sr VP PSP

## 2.3 Accountabilities, Roles and Responsibilities

Roles and responsibilities are well defined within the policies, which is essential in a decentralized environment:

- At the local level, SIA managers are responsible for planning, coordinating and managing the businesses.
- The SIA managers report to the Senior/Deputy PSP Managers, who direct and control SIA operations to ensure financial and operational objectives are met.
- Accountability for SIA sustainability rests with the SIA managers, the Senior/Deputy PSP Managers and B/W/U Commanders.
- As custodian of NPP, the B/W/U Commander is responsible and accountable for financial performance and ensuring that morale and welfare activities are delivered on base.
- The B/W/U Commanders are also responsible for ensuring that Public/Non-Public spending on SIAs are in accordance with applicable policies.
  - The B/W/U Commander has the discretion to commit additional non-public financial support to an SIA in the interest of ensuring the SIA remains sustainable and available for the base.
- National oversight is provided by CFMWS, Sr VP PSP and the Director of PSP Operations.

## 2.4 Monitoring and Reporting

Per SIA policy, Sr VP PSP is to conduct an annual financial review of SIAs with recommendations for the improvement of operations. More frequent SIA monitoring and reporting activities are occurring at the B/W/U level by SIA Managers, Senior Managers PSP and Regional/Local NPP Accounting Managers. They include:

- Real-time financial reporting: provides managers and staff the ability to track actual numbers versus the planned budget, to inform decisions to increase the likelihood of remaining on budget.
- B/W/U fund meetings: provide SIA oversight, communication and collaboration between the Public and non-Public SIA stakeholders. In B/W/U Fund minutes, records of decision for financial and operational goals are recorded and available. The B/W/U committees and B/W/U Commanders are given a performance report at the B/W/U Fund meetings, where they may also comment on performance and offer their input.

- Local NPP Accounting staff: monitors entity financial statements to ensure reporting compliance and alerts Senior Managers PSP of any irregularities that may present themselves.

In spite of the oversight noted previously, situations arise where the financial situation of SIAs are not positive, which can put base fund sustainability at risk. An opportunity exists to further supplement monitoring activities by CFMWS division heads. This would increase awareness of any operational challenges and permit the development of timely risk response strategies prior to an entity needing to be placed on probation.<sup>3</sup>

#### **ADM(RS) Recommendation**

3. It is recommended that CFMWS develop a formal and comprehensive business health evaluation and risk-based process to assist, advise and support SIAs on their planning, organizing, implementation and financial monitoring activities. The process should include documented oversight and communication at both the CFMWS division head and local levels.

**OPI:** Sr VP PSP/CFO

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<sup>3</sup> SIA policy refers to a probation status, "when a B/W/U fund subsidiary...has been deemed to be in a serious financial situation by the [CFMWS] CFO it may be placed on probation by the MD NPP... In determining the financial situation of the [SIA] the overall financial situation of the B/W/U will be taken into consideration as well as the results of the latest CNA. In certain circumstances, a detailed [operations] review... may be mandated by [CFMWS] to determine the cause and/or corrective actions required... Failure to meet the direction may result in cessation of the SIA."

### **3.0 General Conclusion**

The CFMWS has developed SIA policies, directives and manuals to govern the operation and implementation of SIA activities, operations or programs on B/W/Us. The governance framework provides guidance on the operation and delivery of SIA activities. However, it also allows managers/supervisors some flexibility to deviate from the policy when deemed necessary, with appropriate NPP approvals. In addition, B/W/U fund financial support to SIAs varied significantly.

The CNA is an existing market research tool used to advise, inform and justify programming decisions and funding for NPP on B/W/Us. SIA policies and directives promote using the CNA as a primary tool for advising SIA decisions. However, CNAs are not being used in this capacity at the moment.

## **Annex A—Management Action Plan**

### **Planning and Risk Management**

#### **ADM(RS) Recommendation**

1. It is recommended that CFMWS develop and communicate an SIA-focused section of the CNA that can be used to determine the ongoing and/or future need for an SIA. If it is deemed that adjusting the CNA to include the SIAs is not feasible, an equally effective alternative should be explored.

#### **Management Action**

CFMWS will continue to include SIAs within the CFMWS CNA. This includes exploring options to use sections of the tool differently (redesign/restyle). The CNAs ensure CFMWS & B/W/U Commanders have the relevant data to make informed decisions on the CAF community needs to develop/redesign local and national programs and where applicable objectives/priorities.

**OPI:** Sr VP PSP

**Target Date:** December 2021

### **Financial Sustainability of Specialty Interest Activities**

#### **ADM(RS) Recommendation**

2. It is recommended that Managing Director NPP issue guidance or clarify what is considered ‘financially sustainable’ for SIAs. The guidance should recognize that SIAs operate within a number of different geographical and operational realities.

#### **Management Action**

CFMWS will revise and amend the SIA policy to include the definition of “financially sustainable.”

**OPI:** Sr VP PSP

**Target Date:** March 2021

## Monitoring and Reporting

### ADM(RS) Recommendation

3. It is recommended that CFMWS develop a formal and comprehensive business health evaluation and risk-based process to assist, advise and support SIAs on their planning, organizing, implementation and financial monitoring activities. The process should include documented oversight and communication at both the CFMWS division head and local levels.

### Management Action

CFMWS will modify the annual consolidated base fund evaluation process to assist and support B/W/U Commanders (normally through local PSP/Chief Financial Officer (CFO) management) in their responsibility to deliver sustainable Morale and Welfare programs/services by end of FY 2020/21.

**OPI:** Sr VP PSP/CFO

**Target Date:** March 2021

## **Annex B—Audit Criteria**

A robust governance framework is in place to ensure the effective operation of specialty interest activities.

1. Policies, procedures and guidelines are in place and are complete, current and communicated.
2. Accountability, roles and responsibilities are clearly defined, formally approved and communicated.
3. Planning and risk management are undertaken on a regular basis and action is taken to address / control identified risks.
4. An effective monitoring and reporting mechanism is in place.