Health Canada and the Public Health Agency of Canada
Santé Canada et l'Agence de la santé publique du Canada

# Audit of Accounts Receivable Management at the Public Health Agency of Canada

## April 2018

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# List of Acronyms

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| ADA | Allowance for doubtful accounts |
| AR | Accounts Receivable |
| CFO | Chief Financial Officer |
| CGC-OCFO | Centre for Grants and Contributions, Office of the Chief Financial Officer |
| DWORC | Debt Write-off Review Committee |
| FOD-SSP | Financial Operations Directorate, Shared Services Partnership |
| G&Cs | Grants and Contributions |
| GCIMS | Grants and Contribution Information Management System |
| HC | Health Canada |
| HC/PHAC | Health Canada/Public Health Agency of Canada |
| OCFO-PHAC | Office of Chief Financial Officer, Public Health Agency of Canada |
| PCA | Private-sector collection agency |
| PHITS | Public Health Information Tracking System |
| TB | Treasury Board |
| TBS | Treasury Board Secretariat |
| TPP | Travelling Public Program |

# Executive Summary

### *What we examined*

We examined the management control framework that was put in place to ensure fair, effective and efficient management of accounts receivable (AR), and minimize the risk of loss.

The audit focused on the policies, processes, and procedures in place for recording, collecting, writing off and monitoring AR from external parties during the 2016-17 and 2017-18 fiscal years.

### *Why it is important*

Receivables are important government assets that require prudent management. This is integral to achieving the objectives of responsible fiscal management. The Financial Operations Dirctorate, under the Shared Services Partnership, provides services to support the management of accounts receivable for the Public Health Agency of Canada.

The Treasury Board Secretariat's Management Accountability Framework for fiscal year 2015-16 highlighted the importance of, and its expectations for, AR management by including it as an indicator of sound financial management. In addition, the updated Treasury Board *Policy on Financial Management* and the *Directive on Public Money and Receivables* requires Deputy Heads to ensure:

- Governance and oversight over financial management are effective;
- Internal controls over financial management are effective;
- Financial information supports decision-making and accountability to Canadians;
- Standardized and efficient financial management practices are in place; and
- The financial management workforce is agile and sustainable.

### *What we found*

We found that a management control framework was in place to support ongoing management of AR. We observed that:

- Policies established for the management of receivables and removal of debt were consistent with Treasury Board policies;
- Internal Control Division monitoring of effectiveness on controls related to AR management provided information to support management of risks related to AR management;
- Recording of receivables from the cost recovery program was done on a timely basis; and,
- A process for write-offs is in place and is consistent with the requirements of the *Debt Write-off Regulations*.

Management has made efforts to improve the management of accounts receivable. However, opportunities to address deficiencies were identified in the areas of:

- Regular reporting to senior management on collection activities or the collectability of accounts;
- Clarifying roles and responsibilities of the various players involved in the accounts receivable management process;
- Enhancing guidance and tools to support the collection of outstanding accounts receivable;
- Timely recording of receivables from G&Cs recipient audits, and proper documentation of justification of change in receivables;
- Timely collection action and monitoring of accounts; and
- Enhancing the process for determining the allowance of doubtful accounts.

Management agrees with the recommendations in this report, and has provided an action plan to address the agreed upon recommendations to further strengthen the management control framework supporting accounts receivable management.

# A-Introduction

## Background

1. Receivables are defined in the Treasury Board (TB) *Directive on Public Money and Receivables* as “financial claims incurred through the tax system or arising from accrued revenues transactions, expenses overpayments and other recoverable payments that will result in a future inflow of cash[1].” They are core assets that involve millions of dollars annually and have a wide range of transactions. Given this complexity, departments and agencies are expected to manage resources effectively to ensure sound and prudent use of public funds. The Treasury Board Secretariat’s (TBS) Management Accountability Framework (MAF) for fiscal year 2015-16 highlighted the importance of, and its expectations for, accounts receivable (AR) management, by including it as an indicator of sound financial management.

2. In addition, the TB *Policy on Financial Management* and the *Directive on Public Money and Receivables* expect Deputy Heads to ensure[2]:

    - Governance and oversight over financial management are effective;
    - Internal controls over financial management are effective;
    - Financial information supports decision-making and accountability to Canadians;
    - Standardized and efficient financial management practices are in place; and
    - The financial management workforce is agile and sustainable.

3. In working to fulfil its mandate, the Public Health Agency of Canada (PHAC) is engaged in activities that may result in the establishment of an AR. These activities are primarily related to the recovery of overpayments from contribution agreements, revenues from inspection fees, charges to other government departments, and other recoveries, such as those related to salary overpayments.

4. PHAC’s gross AR balance at the end of fiscal year 2016-17 was $11.6M. As shown in Table 1, this amount is made up of receivables from external parties, other government departments and agencies, and employee advances. Receivables from other government departments account for the majority of the AR for PHAC. These receivables relate to the provision of various finance and administrative services to other organizations within the Government of Canada. A significant amount of receivables were classified as employee advances. This was mainly due to the challenges resulting from the new pay system. The introduction in 2016 of the Pay Transformation Initiative and the new pay system (Phoenix) has resulted in pay challenges, including issues of over-payments and under-payments of employees salaries across all government departments and agencies. Receivables from external parties were mainly comprised of recoveries of overpayments from contribution agreements ($1.2M – 75%) and revenues ($317K - 19%). The audit focused solely on

[1] Appendix A: Definitions of the TB Directive on Public Money and Receivables
[2] Section 4 of the TB Policy on Financial Management

accounts receivables from external parties. Receivables from other government departments and agencies were excluded due to the low level of risk associated with the collection of inter-departmental transactions.

**Table 1 – Breakdown of the Public Health Agency of Canada's Gross Accounts Receivable as at March 31, 2017**

| | **Amount ($'000)** | **Percentage (%)** |
|---|---|---|
| External Parties | $1,632 | 14% |
| Other Government Departments | $6,197 | 53% |
| Employee Advances | $3,821 | 33% |
| Total | $11,650 | 100% |

5. The Health Canada (HC) and PHAC Standard on the Management of Receivables was developed by the Financial Operations Directorate, under the Shared Services Partnership (FOD-SSP). The Standard defined the responsibilities and requirements for the management of AR within PHAC. Responsibility for the management of accounts receivable is shared between FOD-SSP, the Centre for Grants and Contributions (CGC), and the Travelling Public Program (TPP) within the Health Security Infrastructure Branch. In general, this process involves activities related to recording or invoicing, collection, and write-off. The monitoring of AR occurs within each of these steps.

6. The FOD-SSP has responsibility for the collection and monitoring of most accounts receivable. Recoveries of overpayments on contribution agreements are managed through the Centre for Grants and Contributions within the Office of the Chief Financial Officer (CGC-OCFO).

# B-Findings, Recommendations and Management Responses

## Governance

## Governance Structure and Oversight

7. We expected that a governance structure was in place to monitor all activities of the AR lifecycle, from recording to collection, and to eventual write-off of outstanding debts.

8. Oversight is important for ensuring effective financial management processes are in place, and it supports the stewardship responsibilities of senior management. This requires an appropriate structure and regular reporting on all phases of the AR lifecycle.

9. At PHAC, we found that the Debt Write-Off and Review Committee (DWORC) had been in place to provide oversight for the removal of debt. However, we found limited documented evidence to demonstrate oversight of the collection of outstanding non-G&C debts. The DWORC reported to the Chief Financial Officer (CFO), and met twice a year to review debt write-off requests, waivers of interest, and administrative charges requests, and made recommendations to the CFO.

10. While its primary responsibility was for formally revieweing debt write-off requests, the DWORC also received other information relating to receivables and write-offs by region, and aged receivables by program and region. We did not find regular reporting to either the DWORC or to senior management on collection activities or the collectability of accounts. We observed that the write-off of uncollectible accounts at PHAC had increased significantly from $4,236 in FY2014-15 to over $442K in FY2016-17, and at the time of the audit, nearly 20 percent of outstanding items were over three years old, which exceeded the time limit for legal action imposed in most provinces.

11. Enhanced reporting on AR management would provide better information to support decision-making, and would further enhance oversight within the governance framework.

#### Recommendation 1

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| The Chief Financial Officer (CFO) enhances reporting on accounts receivable to help in the management of risks for the collection and collectability of outstanding accounts receivable. |

#### Management response

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| Management agrees with recommendation. |

The Financial Operations Directorate (FOD) will implement regular reporting to the CFO and Deputy Chief Financial Officers (DCFO) showing the status of outstanding accounts receivable by type and by age.

## Guidance and Tools

12. We expected that internal policies and guidance tools were available to employees to discharge their responsibilities, as they relate to receivables.

13. Through the FOD-SSP, multiple governing documents were developed to provide direction relating to the management of receivables. We examined these documents and determined that relevant roles and responsibilities, denoted in the Health Canada/Public Health Agency of Canada (HC/PHAC) Standard on Management of Receivables and the Standard on Removal of Debt, were consistent with Treasury Board expectations, and were available to employees via the intranet.

14. We identified opportunities for improvement in regard to the Standards. First, the HC/PHAC Standard on Management of Receivables included requirements for the following:

    - an assessment of the creditworthiness of customers, where necessary;
    - use of collection activities that were appropriate and cost-effective, including the use of private-sector collection agencies (PCA) or provincial small claims court; and
    - suspension of debtor accounts when it appeared debt recovery was unlikely to occur in a timely manner.

    However, program and accounting operations staff indicated that assessing creditworthiness of a client was not performed prior to conducting business with a client, nor had any debtor accounts been suspended as a result of debtor non-payment. We also noted that there was insufficient guidance on what constitutes appropriate and cost-effective collection activities and there was a lack of guidance documents to assist accounting operations staff in performing these collection activities in an effective and efficient manner.

15. Second, the Standard on Removal of Debt allowed for the write-off of debt when the costs of collection were not justifiable in relation to the amount of the debt or the probability of collection. It also allowed for the reinstatement of debt previously written-off when it was known that the debtor's financial position had improved, and that the debtor was capable of paying the debt. However, no guidance was provided on how to determine when the costs of collection were unjustifiable, nor was responsibility for determining the change in the debtor's financial position established.

16. Third, we also noted improvements were required to clarify the roles and responsibilities of the various players involved in the AR management process. As per the HC/PHAC Standard on Management of Receivables, collection activities were the responsibility of the Accounting Hubs. However, we observed that this was not the case for recoveries related to

contribution agreement overpayments. In these instances, it was the responsibility of the program staff to monitor and follow up on outstanding AR balances. This inconsistency between the Standard and the actual practice could have resulted in gaps in the collection process and redundant activities, resulting in inefficiency in the collection process.

17. Overall, we found that internal policies were in place and available to employees, however, improvements are required to enhance oversight and guidance.

### Recommendation 2

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| The Chief Financial Officer amends guidance documents and procedures to enhance accounts receivable management including:<br><br>▪ clarifying roles and responsibilities for the re-instatement of debts, and the monitoring and collection of debts related to recoveries of contribution agreement overpayments;<br>▪ developing guidance documents to facilitate collection activities such as locating the debtor, and determining whether the debtor is capable of repaying the debt; and<br>▪ establishing a method for determining when the cost of collection is not justifiable in relation to the amount of the debt or the probability of collection. |

### Management response

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| Management agrees with recommendation.<br><br>FOD will refine the Standard on Receivable Management to further clarify roles and responsibilities for items such as the on-going monitoring and collection of debts related to recoveries of contribution agreement overpayments.<br><br>FOD will prepare a guidance document to support accounting hub staff in determining which advanced collection activities to pursue based on the nature of the debt. The document will include direction on considering the cost of the collection when determining the appropriate recovery activity. |

## Risk Management

18. We expected to find that mechanisms, including reporting on factors that impact risk of collection or collectability of account, were in place to identify, address, and report on risks related to recording, collection, write-off, and remission[3] of receivables.

[3] As per the *Financial Administration Act* (section 23 (2),and 23(8), remission of debt occurs when the Governor in Council considers that the collection of the other debt is unreasonable or unjust or that it is otherwise in the public interest to remit the other debt. A remission has the effect of a pardon for the offence for which the penalty was incurred, and thereafter the offence has no legal effect prejudicial to the person to whom the remission was granted.

19. These reports were an important management tool for providing the information required to ensure effectiveness of risk mitigating measures, and to support continuous improvement of the AR management process.

20. We noted that the Internal Control Division (ICD), within the Shared Services Partnership, conducted tests of operating effectiveness on controls related to AR management. These tests by ICD served as a mechanism to inform senior management on some of the risks related to AR management, such as segregation of duties, and adequacy of supporting documentation. Furthermore, the HC/PHAC Standard on Management of Receivables referenced mechanisms to address risks related to AR, such as the assessment of the creditworthiness of customers, or suspension of debtor accounts. However, through interviews, we found that these mechanisms were not utilized.

21. As indicated previously in the section related to Governance, there was limited reporting to inform management on the AR management process. We did not observe the reporting of factors that impact collectability of accounts that would inform management of risks related to the AR collection.

22. Appropriate reporting is necessary to help management identify and assess risks of non-collection, as well as develop mitigating measures to reduce the risk of loss (see Recommendation 1).

## Internal Controls

## Recording

23. An AR can be the result of revenue-generating activities, or recovery of overpayments to suppliers, employees, or G&Cs recipients. Timely recording of receivables helps to ensure collection action is taken when customer invoices become overdue. The audit examined the recording of receivables from the Travelling Public Program (TPP), and recoveries of overpayments from contribution agreement payments.

<u>Travelling Public Program (TPP)</u>

24. The TPP is a cost recovery program that is partially dependent on revenues to fund its inspection activities. We found that TTP invoicing was initiated by the programs, and recorded in the Public Health Information Tracking System (PHITS). On a monthly basis, reconciliation between the database and the departmental financial system (SAP) was performed to ensure accuracy of the information in SAP. This reconciliation is important for ensuring that all TPP revenues are recorded on a timely basis and are accurate. We examined the reconciliation of TPP revenues recorded in the PHITS and SAP and found it to be effective.

<u>Grants & Contributions (G&Cs) Overpayment Recoveries</u>

25. Recovery of overpayments from contribution agreements is important for ensuring public funds are used only for their intended purpose. This can be accomplished through regular

monitoring of recipient expenditures, or PHAC-commissioned audits of recipient expenditures. For both types of recoveries, the Centre for Grants and Contributions (CGC) and the program areas were responsible for identifying the recovery amounts.

26. We assessed the timeliness of identification and recording of G&Cs recoveries, and the adequacy of the supporting documentation in substantiating the recovery amount. Through our review of 30 AR transactions, we noted that the recording of recoveries from regular monitoring of recipient agreements was done on a timely basis. However, we found one instance where a credit memo, or reduction of an identified receivable, was not approved by an individual with the appropriate delegated authority. In two instances, recipient reports were overdue by more than 500 days. Since the review of the reports provided by recipients is required in order to determine whether an overpayment had occurred, it is important that recipient reports be submitted on a timely basis.

27. We found the CGC also conducted audits on select recipients. When an overpayment was identified, the program director was responsible for validating the recovery amount, and establishing a repayment plan with the recipient. Once the amount was validated, the CGC recorded the receivable in the Grants and Contribution Information Management System (GCIMS). We found, however, that nearly a year was required to validate the final recovery amount. Furthermore, the amount of the recovery was often reduced with minimal documentation of the justification for the change. Of the 14 recipient audits completed in fiscal 2016-17, 10 either took more than a year to finalize, or the amount of the recovery was significantly reduced. Overall, the amount of the recovery proposed by the program was half of the amount identified through the recipient audit. We also noted that, in one instance, a recovery was offset against a payment to the recipient without an established AR. In another instance, a recovery was overridden without any evidence that it had been approved by an individual with the appropriate delegated authority.

28. A PHAC internal *Audit of the Management of Grants and Contributions* that examined agreement management practices also identified areas of improvement with respect to recoverable amounts identified through recipients.

29. Overall, it was found that the recording of receivables was timely. However, improvements are required to ensure timely recording of contribution agreement recoveries identified through recipient audits.

### Recommendation 3

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| The Chief Financial Officer establishes a process to review and approve recipient audit results to ensure timely recording of accounts receivable. |

### Management response

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| Management agrees with recommendation. |

The Centre for Grants and Contributions (CGC), within the Office of the Chief Financial Officer, will consult with its stakeholders to establish a process to review and approve recipient audits, and ensure timely recording of accounts receivable (AR). This process will be included in the Standard Operating Procedures (SOP) database and training materials, in order to enable ready access and communications for those employees responsible for grants and contributions program delivery.

## Collections

30. Timeliness of collection actions is critical to maximize the recovery of receivables in the shortest period of time possible, thereby properly discharging departmental stewardship responsibilities. The Treasury Board (TB) *Directive on Public Money and Receivables* also requires departments to take timely and cost-effective collection actions to pursue receivables. Departments are also expected to have in place standardized and efficient financial management practices.

31. At PHAC, the process for collection of receivables involved an array of activities that were designed to recover debts to the Crown at a minimal cost and minimize the risk of loss. These activities include direct contact with the debtor, monitoring of outstanding balances, and review of accounts to ensure accuracy of recorded information. Collection activities were decentralized and vary depending on the type of client, that is, a receivable arising from operating authorities as opposed to recoveries of overpayments from contribution agreements.

32. Through efforts to streamline and standardize financial operating processes, FOD-SSP consolidated activities related to the processing of accounts receivable and accounts payable transactions and centralized 13 accounting offices to two Accounting Hubs in 2012. This transition led to challenges with respect to some receivables as supporting documentation was lost or destroyed.

<u>Receivables from Operating Authorities</u>

33. The Accounting Hubs, within the Shared Services Partnership, were responsible for collection of AR related to operating authorities such as program revenues for both HC and PHAC.

34. Collection actions by the Accounting Hubs typically entailed sending a series of reminder letters (a process referred to as dunning), and attempting to reach debtors via phone or email. Advanced collection procedures, such as the use of private-sector collection agencies (PCAs), were utilized if an account was outstanding for more than 120 days and initial attempts to reach the debtor were unsuccessful.

35. Through analysis of the data in SAP and a customer aging report, it was observed that improvements are required to ensure timely follow up of outstanding customer accounts. Specifically, the analysis showed that dunning letters were not initiated within the timelines established in the HC/PHAC Standard on Management of Receivables (30, 60 and 90

days); and five percent of customer accounts over 120 days overdue were sent to a PCA. The delay in sending accounts to PCA may decrease the probability of fully recovering outstanding accounts receivable, thereby increasing the risk of loss.

36. In addition, the Accounting Hubs internal collection procedures stated that accounts sent to a PCA were to be returned after 180 days (six months) if collection efforts by the PCA were not successful. We found through a review of customer accounts with the PCA that, at the time of this audit, only one account for PHAC was with the PCA. In this instance, the account had been outstanding for more than two years before it was sent to the PCA. It stayed with the PCA for two years before it was finally returned to PHAC in May 2017.

37. As previously noted, the Accounting Hubs were responsible for collection activities for both HC and PHAC. Therefore, we further analyzed all accounts for both organizations that had been sent to the PCA. We found that approximately 90 percent had been there for more than 180 days, with some accounts being there for as long as ten years. Interviews indicated that once receivables were sent to PCA, there was minimal ongoing communication on the status of the receivables and customer accounts were not actively monitored. The longer that customer accounts remain with the PCA, the less likely the Agency could take timely action in managing accounts, such as suspending debtor's accounts to no longer authorize further credit to the debtor, or provide goods or services, use of facilities, or rights or privileges to the debtor.

38. It was observed that the Accounting Hubs has started to take measures to reduce the number of accounts with the PCA. As of August 2017, we noted that the number of customer accounts remaining with the PCA for more than 180 days had been reduced to approximately 60 percent, and the average number of days reduced to 400.

39. Overall, progress has been made to reduce receivables over one year old; however, improvements are required to ensure timely collection action to further help minimize the risk of loss.

Recoveries of Overpayments from Contribution Agreements

40. Recovery of overpayments from contribution agreements was the responsibility of program staff and the CGC. Once notified of an overpayment, recipients were provided the option to repay the funds in full or a recovery plan could be established to set-off against future agreements. Where no recovery plan had been established, follow-up of outstanding amounts were performed as part of the regular G&Cs recipient monitoring process. In cases where a recovery plan was negotiated, details of the plan were entered into GCIMS and recovery was facilitated through automatic deduction from outgoing payments to the recipient, and no further collection effort was required.

41. We analyzed the information recorded in GCIMS and noted that, at PHAC, a majority of the receivables had been recovered or a recovery plan had been established.

Interest Calculation and Account Monitoring

42. According to the TBS *Guideline on Interest and Administrative Charges*, when an account is overdue or a payment is late, departmental officials will charge interest compounded monthly at the average bank rate, plus three percent (3%). The audit team conducted testing on a sample of transactions to determine whether interest was appropriately charged. We found that no interest was charged for nearly 50 percent of the overdue accounts. Amounts of uncharged interest was relatively small as they mostly related to the TPP program, where the AR balance in 2017 was only $317K. Nevertheless, improvements to the process of charging interest should be made as they are receivables due to PHAC and should be collected. With respect to recoveries of G&Cs overpayments, we found that interest was calculated on overdue accounts in SAP. However, this information was not reflected in GCIMS. Therefore, this information was not available to the program staff responsible for following up on outstanding amounts. As a consequence, recipients are often unaware that there may be unpaid interest charges on their account. Management has indicated that efforts are being made to rectify the situation.

43. The HC/PHAC Standard on Management of Receivables identified the Accounting Hubs as being responsible for performing periodic reviews of debts to ensure that the information in SAP was accurate and up-to-date, and that money received is posted to the correct customer or vendor account. This review also ensures timely clearing of customer payments against customer invoices so that interest is only charged on past due invoices. Through analysis of aging transactions, we found that almost 20 percent of PHAC's transactions took longer than ten days to match a payment to an invoice in a customer's account. Therefore, additional work may be required to cancel interest transactions.

44. Further, a review of client account balances in SAP revealed that 17 percent of the outstanding accounts have outstanding balances made up of only interest charges. In addition, we noted that there were ten customer accounts that have credit balances greater than one year old. Although some of these debts were relatively small as it related to unpaid interest charges, they were receivables due to the Crown and should have been collected, failing which they should have been written off. The credit balances represent invoicing errors or overpayments by the customer, and therefore, should have been returned to the customer.

45. As noted in the HC/PHAC Standard on Management of Receivables, when it appeared unlikely that recovery of a debt would occur in a timely manner, or the likelihood of recovering the debt was low, the debtor's account should have been suspended. When a debtor's account was suspended, the department would no longer authorize further credit to the debtor, or provide goods or services, use of facilities, or rights or privileges to the debtor. The Accounting Hubs were responsible for suspending a debtor's account(s) in SAP. The audit team observed five instances at PHAC where an invoice was posted in the customer's account, even though there had been an invoice outstanding for at least one year. We found that no communication exchange was held with the programs to suspend accounts, and when accounts were returned from the collection agency, they were not suspended. As a result, programs continued to conduct business with a client, despite past collection issues.

46. Analysis of the information provided to the Debt Write-Off and Review Committee (DWORC) provided valuable insight into the effectiveness of past collection activities. In analyzing the rationale provided for write-offs, it was found that in the majority of the cases, evidence of an account sent to a collection agency was not kept on file. In one instance, it was found that monies were given to a customer in error, but collection action was not initiated in a timely manner, at which point the customer could not be located, and legal proceedings were statute-barred. Overall, almost all of the write-offs in fiscal 2016-17 were related to evidence of debt lost or destroyed, and the majority related to debts dating from over 10 years ago being written-off in fiscal year 2016-17. Management indicated that a concentrated effort was made to write-off debts that were no longer collectible.

47. As receivables are largely considered to be a short-term asset, they are normally expected to be settled within one year. The results of the audit indicate that improvements are required to ensure timely collection of receivables.

### Recommendation 4

The Chief Financial Officer pursues accounts receivable greater than one year in order to take timely actions to recover or write-off debts and enhance the process for determining an allowance for doubtful accounts.

### Management response

Management agrees with recommendation.

The quarterly reporting to the CFO and Deputy CFO will clearly reflect accounts receivable that are greater than one year old for ease of reference, and will be used to target collection efforts. The results of collection actions will also be shared with Corporate Accounting on a quarterly basis for consideration in the determination of the allowance for doubtful accounts.

## Write-off and Remission

48. We expected to find that a process was in place, and followed for the timely write-off, remission, and forgiveness of debts, as well as waivers of interest or administrative charges of departmental accounts receivable that are uncollectible.

49. In the government context, write-off of debt allows the departments and agencies to accurately reflect the net realizable value of receivables by removing accounts determined to be uncollectible. It does not release the debtor from the obligation to pay, nor does it affect PHAC's right to enforce collection in the future. On the contrary, the remission and forgiveness of debt extinguishes the debt and waives the right of Her Majesty to reinstate the debt. During the scope of the audit, no remission or forgiveness of debts were submitted by PHAC on any of their uncollectible accounts.

50. The *Debt Write-off Regulations*, 1994, require departments to establish a formal process for the writing-off of debt, and prescribes the criteria for debt write-off. Namely, that all reasonable collection actions have been taken and all possible means of collection have been exhausted; and there is no possibility now or in the foreseeable future, to collect through set-off prior to writing off accounts receivable that have not been settled in full. The Regulations also allow departments to write-off debts when the cost of collection and other administrative costs of collection are not justified in relation to the amount of the debt and the probability of collection.

51. The TB *Directive on Public Money and Receivables* further requires departments to take timely action for write-off, remission or forgiveness of debts, or waiver of interests or administrative charges, when a receivable is not settled in full. It defines debt write-off as an accounting action that reduces the amount of accounts receivable of a department or agency regarding a debt, or a part of a debt, that has been determined to be uncollectible. It does not release the debtor from the obligation to pay, nor does it affect the right of the department to enforce collection in the future. In addition, departments and agencies are expected to record allowances for doubtful accounts promptly and accurately.

52. Debt-write off is coordinated through the Departmental Accounts Receivable Coordinator within the Financial Operations Directorate, under the Shared Services Partnership.

53. We examined the process for write-offs and found it to be consistent with the requirements of the *Debt Write-off Regulations*.

54. We also reviewed a sample of write-offs approved in fiscal 2016-17, and found that in all cases, they were properly approved. However, we found that write-offs were not performed on a timely basis. As noted previously, the *Debt Write-off Regulations* permit departments to write-off debt owed to the Crown under certain circumstances, including when it is statute barred. In Canada, the limit is between two and six years (with two years being the most prevalent). From the sample of write-offs examined, there were numerous instances where the transaction approved for write-off occurred more than four years after the provincial limit on legal proceedings. In many cases we noted a lack of rigor in the management of, and follow-up on, outstanding debts (as indicated in the section for Collections).

55. Management indicated that prior to the consolidation of various accounting offices there were different accounts receivable management practices among the different offices. As a result, the Accounting Hubs assumed responsibility for many old outstanding receivables, and efforts were made to write-off the older debts.

56. Allowance for doubtful accounts (ADA) is management's best estimate of the amount of accounts receivable that will not be collected. This allows management to anticipate potential problem accounts, develop appropriate corrective actions, and also provides a more accurate picture of the collectability of the accounts receivable. We found that an ADA was recorded at year-end for financial statement purposes. Corporate Accounting and Reporting reviews historical data of receivable transactions and applies percentages

to the aging of outstanding items to adjust the allowance for doubtful accounts at the departmental or agency level, which helps to mitigate risks to financial reporting.

57. Knowledge of specific customer accounts gained through the collection and monitoring process performed by the Accounting Hubs would be valuable for informing the determination of an ADA that is more reflective of the collectability of accounts. However, we observed that the current methodology does not fully utilize the information gained through the collection process.

58. Overall, debt write-offs were consistent with the requirements of the *Debt Write-off Regulations*. However, improvements are required in assessing the probability of collection, in order to better determine an allowance for doubtful accounts (see Recommendation 4).

## C-Conclusion

We conclude that there was an adequate management control framework in place to support ongoing management of accounts receivable. We observed that:

- Policies established for the management of receivables and the removal of debt were consistent with Treasury Board policies;
- Internal Control Division monitoring of effectiveness on controls related to accounts receivable management provides information to support related risk management ;
- Recording of receivables from the cost recovery program was done on a timely basis; and,
- A process for write-offs is in place and is consistent with the requirements of the *Debt Write-off Regulations*.

Management has made efforts to improve the management of accounts receivable. However, opportunities to address deficiencies were identified in the areas of:

- Regular reporting on collection activities, or the collectability of accounts;
- Clarifying roles and responsibilities of the various players involved in the AR management process, and enhancing guidance to support the collection of outstanding accounts receivable;
- Timely recording of receivables from grants and contributions recipient audits, and proper documentation of justification of change in receivables;
- Timely collection action and monitoring of accounts; and
- Enhancing the process for determining the allowance of doubtful accounts.

The areas for improvement noted in this audit report will collectively strengthen the effectiveness of accounts receivable management.

# Appendix A – Scorecard

| Audit of Accounts Receivable Management at PHAC | | | |
|---|---|---|---|
| **Criterion** | **Rating** | **Conclusion** | **Rec #** |
| **Governance** | | | |
| 1.1 Governance structure and oversight | Minor deficiencies | Defining and formalizing reporting requirements related to the collection activities and collectability of accounts receivable (AR) would further enhance oversight within the governance framework. | 1 |
| 1.2 Guidance and tools | Minor deficiencies | Internal policies were in place and available to employees; however, improvements are required to enhance guidance. | 2 |
| **Risk Management** | | | |
| 2.1 Management of risk | Minor deficiencies | Enhanced reporting would help management identify and assess risks of non-collection, as well as develop mitigating measures to reduce the risk of loss. | 1 |
| **Internal Controls** | | | |
| 3.1 Recording | One major deficiency | Timely recording of recovery amounts resulting from recipient audits is required. | 3 |
| 3.2 Collections | Minor deficiencies | As receivables are largely considered to be a short-term asset, they are normally expected to be settled within one year. The results of the audit indicate that improvements are required to ensure timely collection of receivables. | 4 |
| 3.3 Write-off and remission | Minor deficiencies | Write-offs of accounts receivable were appropriately authorized; however, improvements could be made to enhance the estimation of uncollectible accounts. | 4 |

| | | | | | |
|---|---|---|---|---|---|
| No deficiencies | Minor deficiencies | One major deficiency | More than one major deficiency | Failure to accomplish objective of the activity | Unknown; Cannot Be Measured |

# Appendix B – About the Audit

## Audit Authority

This audit engagement was identified in the Office of Audit and Evaluation Risk-Based Audit Plan 2017-2020 (3 Years). The audit plan was endorsed by the Department's and Agency's Departmental Audit Committee and approved by the Associate Deputy Minister at Health Canada, and the President of PHAC. The project will be executed under the authority of the Office of Audit and Evaluation.

## Audit Objective

The objective of the audit was to assess the management control framework to ensure accounts receivable are managed fairly, efficiently, and effectively, in order to recover such receivables and minimize the risk of loss.

The lines of enquiry for this audit are presented below.

## Audit Scope

The audit focused on the framework and processes in place for recording, collecting, writing-off, and monitoring accounts receivable during the 2016-17 and 2017-18 fiscal years.

The audit focused solely on accounts receivable from external parties. Receivables from other government departments and agencies are excluded, due to the low level of risk associated with the collection of inter-departmental transactions.

The scope also did not include a review of pay-related receivables, including employee advances, as a result of the Phoenix Pay Transformation Initiative (PTI). The Treasury Board Secretariat is working with departments and agencies to monitor the PTI situation.

This audit was not designed to express an opinion on the accuracy of the financial accounts receivable information reported in the departmental financial statements.

## Audit Approach

The audit was conducted in accordance with the Government of Canada's *Policy on Internal Audit*, in order to examine sufficient and relevant evidence, and obtain sufficient information and explanations to provide a reasonable level of assurance in support of the audit conclusion.

The audit methodology included the examination and review of documentation, policies, standards, guidelines, processes, procedures and frameworks, as well as interviews and detailed testing and analysis. All work was conducted in the National Capital Region.

## Statement of Conformance

In the professional judgment of the Chief Audit Executive, sufficient and appropriate procedures were performed and evidence gathered to support the accuracy of the audit conclusion. The audit findings and conclusion are based on a comparison of the conditions that existed as of the date of the audit, against established criteria that were agreed upon with management. Furthermore, the evidence was gathered in accordance with the Internal Auditing Standards for the Government of Canada and the International Standards for the Professional Practice of Internal Auditing. The audit conforms to the Internal Auditing Standards for the Government of Canada, as supported by the results of the quality assurance and improvement program.

## Lines of Enquiry and Criteria

| Audit of Accounts Receivable Management at PHAC | |
|---|---|
| **Criteria Title** | **Audit Criteria** |
| **Line of Enquiry 1: Governance** | |
| 1.1 Governance structure and oversight | Effective governance structure processes are in place for adequately monitoring of the life cycle of accounts receivable, in order to support oversight and decision-making.[1] |
| 1.2 Guidance and tools | Internal policies, standards, and guidance tools are available to employees to discharge their responsibilities, as they relate to receivables, as well as to foster compliance with relevant policies and regulations.[2] |
| **Line of Enquiry 2: Risk management** | |
| 2.1 Management of risk | Mechanisms, including management reporting, are in place to identify, address and report on risks related to recording, collection, write-off, and remission of receivables. [4] |
| **Line of Enquiry 3: Internal controls** | |
| 3.1 Recording | A defined process is in place to ensure that all receivable transactions, and related allowances for doubtful accounts, are promptly and accurately recorded in the accounts of the department. [2] |
| 3.2 Collections | A process is in place to ensure timely and cost-effective collection actions for receivables and overpayments.[2,3] |
| 3.3 Write-off and remission | A process is in place for taking timely action for write-off, remission or forgiveness of debts, or waiver of interests or administrative charges, when a receivable is not settled in full.[2] |

***Information Sources:***

*1* TBS Policy on Financial Management (April 2017).
2 TBS Directive on Public Money and Receivables (April 2017).
3 TBS Guideline on Collection of Receivables (October 2009).
4 TBS Audit Criteria related to the MAF: A Tool for Internal Auditors (March 2011).