



Auditor General

MANITOBA

Report to the Legislative Assembly
Independent Auditor's Report

Forensic Audits

October 2018

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Auditor General
MANITOBA

October 2018

The Honourable Myrna Driedger
Speaker of the House
Room 244, Legislative Building
450 Broadway
Winnipeg, Manitoba R3C 0V8

Honourable Ms. Driedger:

It is an honour to provide you with my report titled, *Forensic Audits*, to be laid before Members of the Legislative Assembly in accordance with the provisions of Section 28 of *The Auditor General Act*.

Respectfully submitted,

Original Signed by:
Norm Ricard

Norm Ricard, CPA, CA
Auditor General

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Introduction

This volume includes the results of 3 forensic audits conducted by my Office.

Two stem from Special Audit requests (Pharmacare and Thompson District Office) and one from our citizen concern line (RM of DeSalaberry).

When we use the term Special Audit we are referring to an audit undertaken pursuant to Section 16 of the *Auditor General Act (the Act)*. Section 16 permits the Lieutenant Governor in Council (Cabinet), the Minister of Finance or the Public Accounts Committee to request a Special Audit of the accounts of a government organization, recipient of public money or other person or entity that in any way receives, pays or accounts for public money. It is important to note that Section 16 further states that I am not obliged to do so if I am of the opinion that the requested audit would interfere with my primary responsibilities.



As far as I am aware, an Auditor General for the Province of Manitoba has never refused a Special Audit request. I would consider an audit request as potentially interfering with my primary

Special Audits

- Pharmacare, October 2018
- Thompson District Office, October 2018
- Northern Airports and Marine Operations, March 2014
- Office of the Fire Commissioner, January 2013
- Society for Manitobans with Disabilities, December 2010
- Image Campaign for the Province of Manitoba, October 2007

responsibilities if the investigative effort required to address the issue would be so great as to require significant reassignments of staff, and consequently cause significant delays in completing other priority audits, or if the request represented one of several concurrent special audit requests such that the combined effort was having the same impact as noted above. Another consideration for refusal of an audit request would be if I believed the subject matter of the requested audit was not suitable for the Office.

Suffice to say, however, that whenever I receive a Special Audit request, no matter the source, it is given serious consideration, and if considered suitable for the Office, every effort is made to undertake the audit.

Some may wonder why, as Auditor General for the Province of Manitoba, I conducted an investigation of a rural municipality. While municipalities are not a “government organization” as defined in the *Auditor General Act* (and as such are not part of the Province’s government reporting entity), they are a “recipient of public money” as defined by the *Act*, typically because they receive one or more government of Manitoba grants. Section 15 of the *Act* permits me to conduct audits of recipients of public money. As a result, over the past 10 years our Office has conducted a number of audits of Rural Municipalities, each stemming from information received through our citizen concern line.

Audits conducted in rural municipalities in the past 10 years

- Rural Municipality of DeSalaberry, October 2018
- Rural Municipality of Lac du Bonnet, August 2013
- Rural Municipality of St. Clements, June 2012
- Rural Municipality of St. Laurent, December 2010
- Rural Municipality of La Broquerie, March 2008

In my comments for each of the forensic audits included in this report I discuss a specific matter showcased by the audit.

I would like to thank my forensic audit team for their diligence in carrying out each of these audits.

**Original Signed by:
Norm Ricard**

Norm Ricard. CPA, CA
Auditor General

Pharmacare: Special Audit of Financial Irregularities and Controls

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Auditor General's comments

This report is the result of a Section 16 Special Audit on the manual Pharmacare claims process and the transactions processed by a specific former employee. We determined that the employee processed many suspicious payments over several years totaling more than \$236,000. We recommended that our findings be forwarded to Civil Legal Services.

How did this happen? We found an internal control environment with many significant gaps which enabled the employee to process, undetected, many transactions with no support. These unsupported transactions resulted in "refund" cheques to several individuals. We found no supervisory controls and no standards or expectations for documentation.

Sadly, issues around the lack of support documentation are not unusual findings for my Office. This audit highlights, yet again, the critical importance of setting appropriate documentation standards for specific transaction types and in ensuring compliance through supervision.

The audit also highlights how the use of modern technology can greatly assist in strengthening the control environment.

My staff and I extend our thanks and appreciation for the cooperation and assistance received from the many dedicated employees of the Department of Health and Healthy Living.

**Original Signed by:
Norm Ricard**

Norm Ricard, CPA, CA
Auditor General

Recent reports that discuss the importance of proper documentation and supervision include:

- Management of Manitoba's Apprenticeship Program, July 2017
- East Side Road Authority, September 2016
- Management of Provincial Bridges, July 2016
- Northern Airports and Marine Operations, March 2014
- Waiving of Competitive Bids, March 2014

Report highlights

Special audit

We looked at manual entries

of prescription drug purchases and adjusting entries

5

recommendations made

What we found

\$236,000 in suspicious payments

between October 2007 and March 2015

Gaps in internal controls that made this possible

No supervisory reviews
of manual transactions

Lack of documented support
no guidance on needed documentation

Few automated controls
DPIN dates back to 1994

Introduction

In November 2014 The Winnipeg Police Service notified Pharmacare of a potential misappropriation of funds. The police had an individual in custody who was in possession of a Pharmacare cheque. When questioned, the individual was unable to provide a reasonable explanation for why they had the cheque so the police notified Pharmacare. Pharmacare conducted a preliminary investigation and found that an employee was entering unsupported transactions into the Pharmacare system which resulted in illegitimate payments being issued to several individuals. The employee was terminated as at March 17, 2015.

On August 25, 2015, the Minister of Finance requested a special audit under Section 16 of *The Auditor General Act* of the Pharmacare claims process and the transactions made by a specific employee.

On August 28, 2015, I agreed to conduct the special audit.

Background

Pharmacare is a drug benefit program (Program) administered by the Department of Manitoba Health, Seniors and Active Living (Manitoba Health). The Program is provided to all eligible Manitobans as defined in *The Prescription Drug Cost Assistance Act*. The Program assists those who cannot afford high prescription drug costs. To be eligible, an individual must:

- Be eligible for Manitoba Health, Seniors and Active Living coverage.
- Not be covered by other provincial or federal prescription drug programs.

Eligible individuals must apply to receive benefits. Coverage is based on total family income and the amount you pay for prescription drugs. During each Pharmacare year (April to March), individuals are required to pay a part of the cost of their eligible prescription drugs; this portion is known as the deductible. Deductibles are calculated by the Drug Programs Information Network (DPIN) system for each Pharmacare applicant based on his/her family income. Per legislative requirements, the income figures are based on income earned 2 years prior to the applicable Pharmacare year. All drug costs in excess of the deductible are then covered by the program.

Pharmacare uses the DPIN system to administer the program. DPIN is an electronic, online, point-of-sale prescription drug database that connects Manitoba Health and pharmacies in Manitoba. DPIN generates complete drug profiles for each client including all prescription drug purchases made at pharmacies. Information is captured in real time for all Manitoba residents (including Registered First Nations), regardless of insurance coverage or final payer. DPIN has been used by Manitoba Health since July 1994.

There are 2 ways in which prescription drug purchases are entered into DPIN:

Automated entries: The first way is done automatically through pharmacies. A client provides his/her Provincial Health Identification Number (PHIN) to the pharmacy. The pharmacy enters the client's prescription drug purchase into the system. Once the client has purchased enough prescription drugs to reach their deductible, the system will recognize that the deductible has been reached and the client's prescription drug purchases for the remainder of the Pharmacare year will be paid by Pharmacare. Under this method, no disbursement is made by Pharmacare directly to the client.

Manual entries: The second way that prescription drug purchases are entered into DPIN is through manual entries made by Pharmacare employees. This occurs when receipts for prescription drug purchases are submitted by Pharmacare clients for reimbursement. This can happen when:

- Drugs have been purchased outside of Manitoba.
- Payments could not be processed by the pharmacies for some reason (e.g. a system malfunction).
- Eligible medical supplies and equipment are purchased (such as blood glucose monitoring strips).

Receipts for prescription drug purchases are received in the mail and batched by Pharmacare staff. They are scanned to microfilm and manually assigned a microfilm reference number. Pharmacare staff then input the receipts into DPIN with the microfilm reference number. This reference number is used to locate the documentation when needed. The original receipts are retained in accordance with Manitoba's record retention policy.

Because microfilm is an outdated technology, in September 2016, Pharmacare started digitally scanning receipts and documents on a go forward basis.

When a payment needs to be issued, staff calculate the payment amount and manually enter the information needed by the system to print a cheque. Cheques are printed by the Department of Finance and sent to Pharmacare for mailing.

In addition to prescription drug purchases, as described above, manual adjusting entries can be made in DPIN by Pharmacare staff.

Manual adjusting entries (carrier 10 and 12): Sometimes manual entries must be made to a client's account to adjust their accumulated expenses. The most common reason for this is a marital breakdown. Spouses share a Pharmacare account. When the marriage ends, one spouse

is removed from the joint Pharmacare account and given their own Pharmacare account. Often the spouse that is removed from the joint account has made prescription drug purchases during the year. These expenses are removed from the joint account and added to the new account. The manual addition to the new account is referred to as a "carrier 10 add", and the manual deduction of expenses from the joint account is known as a "carrier 12 minus".

A new deductible is calculated for each account. If prescription drug purchases exceed the deductible an interim payment will be made.

Interim payments: Interim payments are a type of payment made part-way through the Pharmacare year. The Pharmacare year is April 1 to March 31. When a client applies for Pharmacare, the deductible is set at that time. When prescription drug expenses incurred by the client between April 1 and the time of the application exceed the set deductible, a cheque for the excess is issued to the client. This payment is known as an interim payment.

Scope and audit approach

Pharmacare expenses totaled \$266 million for the 2016 fiscal year. Our audit focused on payments resulting from the manual entries made by the suspected employee (employee) during the entire period of employment (October 29, 2007 to March 17, 2015). These transactions totaled \$1.1 million.

Our objectives were as follows:

1. To determine the extent of illegitimate disbursements processed by the employee.

For the employee's entire term of employment we examined the following transactions processed by the employee for supporting documentation:

- Manual entries of prescription drug purchases.
- Interim payments, including the calculation of the related deductible.

We also examined all manual adjusting entries (carrier 10 and 12) over \$1,000 for all employees for the entire term of employment. We examined entries for all employees because the system is unable to track these entries by employee.

2. To determine whether there were adequate controls in place to ensure that only properly supported disbursements were made to individuals.

Our audit was performed in accordance with Investigative and Forensic Accounting (IFA) standards as established by the Chartered Professional Accountants of Canada (formerly the Canadian Institute of Chartered Accountants). IFA standards are designed for engagements that "involve disputes or anticipated disputes, or where there are risks, concerns or allegations of fraud or other illegal or unethical conduct."

We interviewed management and staff at Pharmacare to gain an understanding of the systems and related controls.

During our testing, some required records were unavailable. Due to system storage limitations, Pharmacare will archive certain client data (removing it from the active database). Client IDs and data for individuals who have left the province, or are inactive for a certain period of time, are archived. For some of the archived records that we needed to access, the information had been purged. As a result we were unable to audit these amounts.

Findings and recommendations

1 Suspicious payments of over \$236,000

After examining the manual entries of prescription drug purchases, as well as interim payment entries, we found that the suspected employee processed over \$236,000 in unsupported payments during the period of employment. As discussed in greater detail below, this is made up of \$180,915 in payments from manual entries of prescription drug purchases and approximately \$55,886 in interim payments from manual adjusting entries.

MANUAL ENTRIES OF PRESCRIPTION DRUG PURCHASES

We examined \$274,529 in payments that were generated because the employee manually entered receipts into the system. We found that \$180,915 in payments were not supported by receipts and were suspicious in nature because the entries were higher dollar amounts, and were processed repeatedly to the same group of individuals. As a result, it is highly unlikely that these transactions were calculation or administrative errors. We found that \$90,128 in payments were properly supported, and we were unable to conclude on \$3,485 in payments.

INTERIM PAYMENTS

As shown in **Figure 1**, interim payments totaling \$836,484 were processed by the employee during the period of employment. We were able to recalculate the deductible for \$635,713 in payments as well as confirm the backup, however, for \$51,606 in payments, we were not able to calculate the deductible because the income information to support it was not available. We did check the backup for these payments and no issues were noted.

We found that \$55,886 of these interim payments resulted from suspicious manual adjusting entries (carrier 10) to increase the client's expenditures. These entries were suspicious for the reasons noted above, and because no supporting documentation was available. In addition we found that \$67,885 of the payments had purged DPIN data, microfilm numbers that didn't exist, and/or drug purchases in DPIN that did not add up to the payment amount. We were unable to determine whether these situations were due to administrative errors or were intentional.

The remaining \$25,394 in payments had administrative errors where the cheque amounts didn't equal the interim payment calculation.

Figure 1: Interim payments

	Total
Total legitimate & supported	\$ 635,713
Irregularities Found:	
Suspicious disbursements	55,886
Unsupported disbursements	67,885
Income information to calculate deductible unavailable	51,606
Administrative errors resulting in incorrect cheque amounts*	25,394
Total irregularities	\$ 200,771
Total interim payments	\$ 836,484

* Note: this is not \$25,394 in errors, it's the total value of cheques where we found errors.

Recommendation 1: We recommend that Manitoba Health forward our detailed audit findings to Civil Legal Services.

RESPONSE OF OFFICIALS:

The department scheduled a meeting with counsel from Civil Legal Services for July 2018.

2 Manual adjusting entries insufficiently supported

There were a total of \$1.2 million in manual adjusting entries made by all staff during the period of the employee's employment. Because manual adjusting entries can result in interim payments or increase a client's accumulated expenses to the deductible level, we considered these entries to be at a high risk of inappropriate use. As a result we examined all entries over \$1,000.

Figure 2 summarizes all the manual adjusting entries made by all employees during the period under examination.

Figure 2: Manual adjusting entries (Carrier 10 and 12)

	Total
Total legitimate & supported	\$ 788,011
Irregularities found:	
Insufficient support*	425,675
Information purged	1,778
Total irregularities	\$ 427,453
Total manual adjustments over \$1,000	\$ 1,215,464

* Note: because there was insufficient support, we were unable to conclude on the appropriateness of the entries.

\$788,011 of the manual adjusting entries were properly supported, but for \$427,453 we could not locate backup documentation such as an application to join a couple's individual accounts. As a result we were unable to conclude on the appropriateness of the entries. Of this total, at least \$55,886 is suspicious as referred to in **section 1**.

Given the lack of guidance on documentation needed to support entries as discussed in **section 3**, the lack of available supporting documentation may be more the result of weak administrative processes than an effort to process inappropriate transactions.

3 Significant internal control gaps

We reviewed the processes and controls used by Pharmacare to issue payments to Pharmacare clients and found the following gaps in controls that made it possible for unsupported payments to be made. This increases the risk that illegitimate disbursements can occur.

3.1 No supervisory reviews of manual transactions

We found that there was no supervisory review to ensure that manual entries of prescription drug purchases, interim payments, and manual adjusting entries were properly supported and calculated.

We noted that the DPIN system, which dates back to 1994, has very few automated controls or calculations, elevating the importance of proper supervisory review in preventing or detecting errors and inappropriate entries.

Also, DPIN does not have the ability to track which staff member recorded a manual entry. Therefore, even if an error was discovered, there would be no way of knowing who made the error.

PRESCRIPTION DRUG PURCHASES

As noted in **section 1**, entries were recorded in client accounts by the employee to increase the clients' accumulated expenses. These entries were not reviewed by a supervisor. By entering these amounts, a client reached their deductible much faster. Once the deductible was reached, any legitimate or fictitious expenses would be paid by Pharmacare.

INTERIM PAYMENT AMOUNTS

When expenses exceed the deductible and an interim payment is required, the interim amount is manually calculated by an employee; it is not an automated function within DPIN. We noted that there was no supervisory check to ensure the interim payment calculation was correct. The manually calculated amount was entered into DPIN by a Pharmacare clerk and processed for payment. There was also no supervisory review to ensure the cheque amount equalled the manually calculated amount.

When an interim payment is issued, another manual entry must be made to reduce the client's total expenses by the amount of the interim payment. This brings the total expenses down to the deductible amount so no further interim payments are issued. However, we found there was no supervisory check to ensure this occurred. We found instances where the manual entry was not made after a payment was issued. This results in the possibility that a duplicate interim payment could be made.

MANUAL ADJUSTING ENTRIES

As noted in the Background section, sometimes manual adjusting entries must be made to a client's Pharmacare account which can result in interim payments. We noted that these entries are not reviewed and could lead to inappropriate cheques being issued. In **section 2** we reported that many manual adjusting entries were not sufficiently supported.

INCOME CAN BE CHANGED BY ANY EMPLOYEE

In most cases, income amounts are received directly from the Canada Revenue Agency (CRA) and automatically downloaded into DPIN. This information is used by DPIN to calculate the deductibles. We noted however, that an employee can access a screen that would allow him/her to manually change an individual's income amount. A reduction to the reported income would result in the system calculating a reduced deductible which may trigger an interim payment. Manual adjustments such as these were not reviewed by a supervisor.

Recommendation 2: We recommend that the Department conduct a benefit/cost analysis for making enhancements to the DPIN system to build automated internal controls over the processing of manual Pharmacare transactions, and to implement enhancements where it makes business sense to do so.

RESPONSE OF OFFICIALS:

Many enhancements to DPIN system are currently underway, such as assignment of a user ID and timestamp to each and every manual entry into DPIN.

Other enhancements to DPIN might not be possible given some technical limitations of the DPIN infrastructure. Many of these have already been identified by an internal finance audit of DPIN processes and procedures. These limitations will only be overcome with a complete replacement of the DPIN system which will be assessed in Wave three of the Health System Transformation.

Recommendation 3: We recommend that Pharmacare ensure there is supervisory review of all manual transactions and, if applicable, that the review occur before a cheque is generated.

RESPONSE OF OFFICIALS:

Shortly after the issue and potential fraud was identified, the department initiated a supervisory review of all cheques issued prior to the cheque being generated. This review is conducted by the Manager of Pharmacare Operations and entails a review of all information that was entered as well as confirmation that there is legitimate documentation supporting the issuance of a cheque directly to a client. However, this process was unsustainable for the volume of cheques we issue so we have since reduced the number of cheques that undergo this comprehensive review and now approximately 5% of cheques undergo this review.

3.2 No guidance on needed documentation

There was no documented guidance for staff on what would be appropriate backup for DPIN entries and payments. We found that different employees had varying amounts of detail on their supporting documentation. Specifically, we found the following weaknesses:

- Microfilm backup did not always have Client IDs and PHINs documented.
- Interim payment calculations were not always documented. Depending on the employee preparing the backup, some documents showed a detailed calculation, some just showed the final payment amount, while others had nothing written for support at all.
- Some income amounts used to calculate deductibles were not supported.

- Manual adjusting entries often did not show the calculation leading up to the amount, and often lacked an explanation for why the entry was made.
- Receipts were not always provided for the manual entry of prescription drug purchases.

Recommendation 4: We recommend that Pharmacare develop documentation requirements for each type of entry made into DPIN. This guidance should include checklists of all information required to support a particular entry.

RESPONSE OF OFFICIALS:

This recommendation was also identified in a review by internal finance and has been actioned. The process will be finalized once any possible technical enhancements to DPIN are completed so that both the documentation requirements and auditing activities can be simultaneously implemented and communicated to staff.

3.3 No process to confirm previously self-reported income

Typically, Pharmacare sets deductibles (using information electronically received from CRA) based on income of the tax year that is 2 years before the current Pharmacare year. However, there are situations when Pharmacare clients self-report their income, in some cases, with no support. This can happen when there has been a change in the client's financial situation, or if the person has never filed a tax return. In these situations, the deductible is set based on income information provided by the client. For example, if an individual was applying for Pharmacare in 2016, typically income reported to CRA for 2014 would be used to set the deductible. However, if the client changed jobs in 2016 and made less money, he/she would self-report the 2016 income and it would be used to set the deductible. Two years later in 2018, when Pharmacare is setting the client's new deductible for 2018, they would obtain the 2016 income information from CRA. However, there is no process to check whether the self-reported income that was provided back in 2016 agrees with the income information provided by CRA in 2018.

It should be noted that Pharmacare has the ability to pursue recoveries from a client under certain circumstances, for example, if errors are discovered on the account.

Recommendation 5: We recommend that Pharmacare establish a process to compare self-reported income figures with income information from the CRA once it becomes available. Recovery processes should be established for situations where self-reported incomes were significantly below actual income reported to the CRA and resulted in Pharmacare paying for prescription drugs that the client should have paid for.

RESPONSE OF OFFICIALS:

Self-reported figures are not automatically validated when CRA information is received. A process is underway to develop a procedure to achieve this and ensure these reported values are reviewed and reconciled automatically each year.

3.4 No automated microfilm numbering system, and DPIN cannot recognize if a false or incomplete microfilm number is entered

At the time of our audit, documents were scanned onto microfilm and a staff member manually assigned a number to each scan. The numbering sequence was manually tracked on a piece of paper. This reference number was entered into the DPIN system to link the microfilm support with the DPIN entry and is used to locate the document. We found instances where the numbers assigned to the microfilm were out of sequence, had transposition errors, or jumped in sequence. The misnumbering of microfilm backup creates delays and/or the inability to find the backup for DPIN entries.

Another microfilm number issue is that DPIN cannot differentiate between authentic microfilm numbers and those that are made up, reused or entered incorrectly. We found instances of microfilm numbers entered into DPIN that had missing digits, transposition errors, or were completely made up. This weakness allows for the potential for fraud to occur as the microfilm number could be completely made up and the entry would still go through.

Digital scanning is now being used by Pharmacare and this has eliminated the microfilm numbering problem on a go forward basis.

**Thompson District Office:
Special Audit of Missing Licences
and Cash Management Practices**

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Auditor General's comments

This report is on our Section 16 Special Audit of the Department of Sustainable Development's Thompson District Office. We were asked to conduct a forensic audit of the cash deposits and cash management processes. We found a number of irregularities that suggest funds were being misappropriated, but we could not estimate the amount because of weaknesses in the documentation maintained by the Branch.

The issuance and sale of licences and permits is currently a manually intensive process. Our audit revealed many gaps in how inventory and funds were being managed, which increased the risk of irregularities occurring. Greater use of computerized systems would provide opportunities to re-engineer the process, gain efficiencies in transaction processing and allow for a stronger control environment.

As we reported in our March 2014 report on Manitoba's Framework for an Ethical Environment, Manitoba has a fraud prevention and reporting policy that is not well understood. The policy requires that an internal fraud exposure evaluation be completed by each department, but these were not being conducted. Fraud exposure evaluations help identify those areas within a department that warrant additional internal controls, including significant management oversight. The findings in this report highlight what can occur in weak control environments and why fraud exposure evaluations are so very important.

My staff and I would like to thank the dedicated staff at the Department for their cooperation and assistance throughout the audit.

Original Signed by:
Norm Ricard

Norm Ricard, CPA, CA
Auditor General

Report highlights

Special audit

To determine extent of missing licences and funds, and to assess internal control framework

5 recommendations made

What we found

Value of missing licenses totalled about **\$33,000** (between 2005-2014)

Extent of missing funds could not be determined due to weak documentation

Gaps in internal controls that increased the risk of funds being misappropriated

- No risk assessments
- Inadequate segregation of duties
- No periodic inventory counts
- Money remittance orders not properly completed
- Outdated paper-based system

Web Version

Introduction

On May 27, 2014, the Minister of Finance requested a special audit under Section 16 of the *Auditor General Act* of cash management processes in the Thompson District Office of the Department of Sustainable Development. This request was made after Sustainable Development discovered a missing deposit and missing licences at the Thompson District Office. After Sustainable Development officials performed some preliminary work on the missing deposit and licences they terminated the employee (District Clerk) they suspected was responsible for the missing items.

On May 29, 2014, the Auditor General agreed to conduct a special audit.

Background

Licences and permits

Sustainable Development's Licensing Branch administers 65 different licences and permits using multiple information systems. The Licensing Branch handles the largest volume of licences and permits sold by Sustainable Development. Other licences and permits are administered by the Parks, Fisheries, and Forestry branches of Sustainable Development.

Sustainable Development has 6 regional offices throughout Manitoba and 50 district offices. At district offices, the public can purchase:

- Hunting licences
- Angling licences
- Commercial fishing licences
- Timber permits
- Provincial park passes
- Special event permits

There are over 200 permit/licence categories that are issued and sold to the public. For example, there are 7 different types of angling licences. Overall, there are about 752,000 licences sold annually. Sustainable Development reported licence and permit revenue of \$29,292,000 in its 2014-15 Annual Report.

Over 800 vendors sell Sustainable Development's licences and permits. Most of the vendors are commissioned private businesses such as convenience stores, gas stations, and department stores. Government operated vendors include 50 district offices and 64 campgrounds and park gates. The value of licences/permits issued by government operated vendors in 2014/15 amounted to \$23,311,000.

Licences are printed by an external printing company, and are pre-numbered. Each licence is a 4 carbon copy form. A document is produced weekly by Sustainable Development for each vendor which details the sequence of licences provided to the vendor, the quantity sold, and the licence numbers that should still be in inventory. At the end of the season the Licensing Branch requests that vendors return unsold licences. Individual vendor activity is manually tracked with each vendor's inventory kept in separate file boxes. Manual entry of information is required in various databases in Winnipeg for purposes of updating inventory, vendors, and revenue.



Photo of Licensing Branch vendor boxes

How licence and permit sales are processed by district offices and recorded by the Department

When a customer purchases a licence/permit, the clerk fills out the licence/permit (a 4 carbon copy form for the majority of licences/permits) and provides the top copy to the customer.

The sold licence number is recorded by the clerk on the Licence Remittance form and removed from the Licence Reconciliation form (which is a control listing of the licences available for sale at the district office).

On a daily/weekly basis, depending on volume, a Money Remittance Order (MRO) is prepared by the clerk for each type of licence/permit (a 4 carbon copy form). The MRO records the name of the payors, the method of payment and the amounts received for that period. The originating district office files the top copy of the MRO. Deposit slips are then prepared for the cash and cheques totaled on each MRO.

At the Thompson District Office cash and cheques are deposited to the bank in Thompson. The MRO package is then compiled and contains the following:

- The 3 remaining copies of the MRO.
- The Licence Remittance form. The completed form includes the quantity and the specific licence numbers sold. It does not contain information about the purchaser or to whom the licence was issued.
- The remaining carbon copies of the sold licences/permits.
- The deposit slip.

The MRO is the key document for data entry into the accounting systems, for licence/permit inventory control, and providing management information to Sustainable Development's various operating divisions. It also forms the basis for bank deposits.

The MRO package is forwarded by the district office to the branch for which the transaction type relates. For example, hunting licences are sent to the Wildlife Branch, timber permits are sent to the Forestry Branch and angling licences are sent to the Fisheries Branch.

Upon receipt of the MRO package, the various branches update their licence/permit inventory records. The licence/permit copies are removed from the MRO package and kept by the branch.

The branch then forwards the remaining MRO package documents to the Financial Services Branch in Winnipeg. Financial Services manually enters the MRO information into Sustainable Development's accounting system and stamps the MRO to indicate it has been posted. Summary sales totals from Sustainable Development's accounting system are posted to the Province's financial accounting system.

Financial Services then sends one copy of the MRO back to the appropriate program area and one copy back to the originating sales office. The originating office must sign to confirm that their copy was received. The district office matches the copy received from the Financial Services Branch to their original copy and reviews for any changes.

On a regular basis the Financial Services Branch in Winnipeg transfers funds from the bank account in Thompson to the bank account in Winnipeg. Bank reconciliations are prepared by Financial Services Branch.

Audit approach

The objectives of our audit were to:

- Determine the extent of the missing licences and funds in the Thompson District Office.
- Assess the adequacy of Sustainable Development's control framework over licence inventory, revenues, receivables, and receipts.

We examined relevant accounting records from the Thompson District Office for the years 2008-2014. This is the period of time that the District Clerk was working there. We also obtained copies of the cancelled cheques from the bank for 2013. We reviewed Sustainable Development's procedures and policies that relate to the issuance of licences and receipt of cash at the Thompson District Office. We also visited the Portage la Prairie and Falcon Lake District Offices to compare procedures in place over licence inventory and sales. We met with Sustainable Development staff, reviewed notes from interviews Human Resources staff did with the District Clerk, and reviewed files from the termination process.

Our audit was performed in accordance with Investigative and Forensic Accounting (IFA) standards as established by the Chartered Professional Accountants of Canada (formerly the Canadian Institute of Chartered Accountants). IFA standards are designed for engagements that *"involve disputes or anticipated disputes, or where there are risks, concerns or allegations of fraud or other illegal or unethical conduct."*

Findings and recommendations

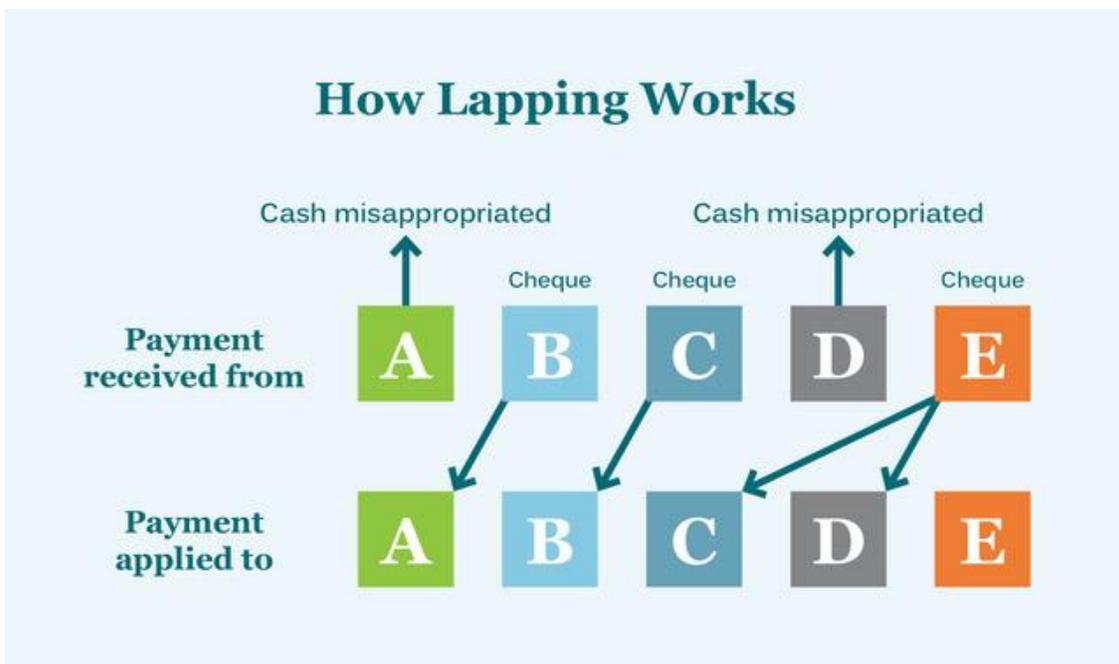
1 Value of missing licences was \$33,341, extent of missing funds could not be determined

Sustainable Development officials provided us with a list of licences that went missing from the Thompson District Office between 2005 and 2014. The total value of the missing licences on the list was \$33,341. We were able to determine that the Department's list of missing licences was accurate. Given the significant control weaknesses, as discussed in **section 2**, there was a heightened risk that for certain cash sales, licence copies were destroyed and the cash was misappropriated.

In an effort to determine whether funds from sales were misappropriated we attempted to reconcile bank deposits to Money Remittance Orders (MROs - see Background for description) and licence/permit records. We found a number of irregularities that suggest funds were misappropriated. However, we could not estimate the amount of misappropriated funds because of weaknesses in the documentation maintained by the Branch as explained below.

A commonly used technique to misappropriate cash is to record certain cash sales in an organization's sale summaries with a cheque(s) subsequently received. This is generally referred to as a lapping (see **Figure 1**). We looked for evidence that this might be occurring. We obtained the fiscal 2013 bank deposit records and copies of the cheques included in each bank deposit.

FIGURE 1



We noted the following:

- There were instances where the names of purchasers on MROs did not match the names on the submitted cheques.
- Many MROs did not list the purchasers, rather they only showed totals, and the supporting listings only noted licence numbers but not names of purchasers. As such, linking to the cheque that was used to purchase a specific licence was not possible.
- There were instances where the District Clerk prepared an MRO indicating an individual paid with cash even though the individual actually paid by cheque. We found that these cheques were recorded by the District Clerk on an MRO at a later date but attributed to other individuals.

In **Exhibit 1** we summarize the events regarding missing Caribou licences and sale proceeds.

An additional documentation issue that impeded our efforts occurred when a licence was purchased for an individual by another individual. As a result the name on the cheque was not the name on the licence. There was no process to connect the sold licences to the cheque used to pay for them.

From April 2013 to March 2014 the Thompson District Office received 84 cheques. The average time to deposit these cheques was 38 days. For 36 of these cheques the time to deposit ranged from 37 to 87 days, for an average of 73 days. Cheques should be deposited daily, but at least weekly when volumes are low. Long delays like the ones that occurred at the district office may indicate cheques were withheld for future use to cover for misappropriated cash.

The above findings show a pattern of irregularities which are not just recording errors. The effort required by our Office to document all suspicious occurrences over the 9-year period, and to determine the likely amount of misappropriated cash, exceeded what we were prepared to apply to this audit. In addition, the documentation weaknesses that we noted further limited the likelihood of successfully identifying all occurrences. As a result we focused our attention on identifying internal control weaknesses. In **section 2** we discuss the internal control weaknesses at the Thompson District Office that make the misappropriation of cash possible.

The Thompson District Office has 2 other sources of revenue that cannot be reconciled to pre-numbered inventory and where no other reconciliations or analyses are done on these revenues to assess completeness.

These sources are:

- Shower sales at camp sites (cash received not reconciled to coin machines logs).
- Crown land revenues.

As a result, Sustainable Development has no assurance on the completeness of such revenues and we are not able to conclude on the extent to which these types of funds may have been misappropriated.

EXHIBIT 1

Missing Caribou licences and sales proceeds

Sustainable Development officials compiled an information package about missing caribou licences and cash which included relevant documentation and their interview notes with the District Clerk and other staff. After our examination of the information package and meetings with Sustainable Development officials we prepared the following summary of events. This is an illustration of a pattern of irregularities, lack of timely oversight, and what can occur when multiple duties are performed by one individual.

Every year, in mid-summer, caribou licences go on sale to the public. In 2013, that sale started on June 6 for the Thompson District Office. There is a high demand for caribou licences and we were told that all available licences are sold each year over the 2 day sales period.

Caribou licences are a 3-part form—the original part is provided to the hunter and the 2 copies are sent to the Licensing Branch in Winnipeg. The Licensing Branch retains one copy and the other copy is sent to the caribou biologist. The caribou biologist prepares a spreadsheet that documents information about the caribou licences sold, including the hunter's name, date of birth, licence number and hunting area chosen.

The District Clerk was responsible for the inventory and sales of wildlife licences, including caribou. The District Clerk transferred some licences and a cash float to other clerks in the District Office who were assisting with the caribou licence sales. At the completion of the sale, the sold licences along with the monies collected and the cash float were transferred back to the District Clerk.

After the first 2 days the District Clerk prepared a MRO and a Licence Remittance Form which detailed the licences sold. MRO #52027 and a licence remittance form were completed at the end of the day on June 7, 2013 which covered the caribou licences sold. There were 214 caribou licences sold for a total of \$14,594. According to the District Clerk, she also prepared a corresponding bank deposit for \$14,594. The District Clerk said she did not have time to make the bank deposit or mail the MRO and licence copies to Winnipeg before she left work on June 7. The District Clerk said she left a note for the summer student to make the deposit and mail the documents to Winnipeg. The District Clerk was in and out of the office from June to August helping with forest fire fighting and was also on vacation.

During the first week of September 2013, the caribou biologist was preparing the hunter spreadsheet when she realized that she had not received the caribou licence information from the Thompson District Office, and subsequently followed up with the District Clerk. At that time the District Clerk provided the caribou biologist with copies of the caribou licences sold on June 6 and 7. According to the District Clerk, she then asked the summer student if she had mailed MRO #52027, the licence

remittance form and the licence stubs, and made the corresponding bank deposit. The summer student said that she never received the note from the District Clerk asking her to make the deposit and mail the documents.

It was not until December that Finance Services staff in Winnipeg noticed that the deposit for caribou licence sales was missing along with MRO #52027 and the licence remittance form. This started the formal investigation and involvement of Human Resources to perform inquiries of the District Clerk.

The District Clerk told Sustainable Development officials that in early September, when she learned that the caribou deposit may not have been taken to the bank, she searched the safe and found all the documentation and the cash/cheques from the caribou sales in the back of the safe. The District Clerk said that all the forms, licences and money were there, and it balanced to \$14,594. She told officials that she asked another staff member to mail the documentation and make the deposit on September 3rd or 4th. According to bank records this deposit was not made. We reviewed human resources interview notes with other Thompson staff. The staff denied being asked to make the bank deposit.

Sustainable Development officials also noted that some individuals who had purchased caribou licences on June 6 and 7 were employees of Sustainable Development. The employee cheques and other cheques that were used to buy caribou licences in June were deposited in August and were coded with a different MRO number than noted above. If done properly, these cheques would have been included in the deposit that the District Clerk said she found in the back of the safe.

2 Inadequate control framework

2.1 Risk assessments not done

While Sustainable Development had numerous internal control documents relating to revenue and inventory, they did not conduct a risk assessment to fully understand the risks associated with each vendor type (camping offices, district offices, private vendors) or dollar values involved, to ensure appropriate controls were in place to mitigate the risks.

Examples of risks that should be assessed include:

- Only one clerk to sell licences, maintain inventory and record the transaction in Branch records.
- Cash transactions.
- Highly portable inventory.
- Deposits not made daily/weekly.
- History of unsold licences not returned.

Our March 2014 report on *Manitoba's Framework for an Ethical Environment* noted the following on page 322:

“The Fraud Prevention and Reporting Policy requires an internal fraud exposure evaluation be completed by each department. Fraud exposure evaluations would help identify those areas within a department that warrant a particularly strong internal control, and significant management oversight. Our discussions with senior department officials indicated that no departments have complied with this policy requirement. The department's Comptrollership Plans were noted as an aspect of fulfilling this requirement, however an internal fraud exposure evaluation is a more detailed and focused risk management exercise...”

Given the Department's reliance on physical inventory and cash based sales, conducting a fraud exposure evaluation should be a Department priority.

Recommendation 1: We recommend that Sustainable Development prepare a documented risk assessment, including fraud exposure evaluations, for each vendor type and location to ensure appropriate controls are in place to mitigate significant risks. We further recommend that the assessments be periodically reviewed.

RESPONSE OF OFFICIALS:

The Department agrees with the recommendation to document risk assessments and fraud evaluations.

The Department has been taking steps in this direction with the establishment of annual spot audits/site reviews at various Regional Offices, District Offices, Provincial Park Campgrounds Offices, and Provincial Park Gates on a rotating, randomized, annual basis. This has been in place for the past 4 years. In 2017/18, there were reviews at 25 locations throughout the province. The Department Audit Committee, chaired by the Deputy Minister, meets a minimum of 3 times per year, and receives a report of this activity upon completion. Staff in Financial Services Branch (Headquarters) provide the review team with recommendations of sites to visit based on concerns they may have seen through the course of the past year. It is also noted that the Financial Services staff from Winnipeg who are not involved with performing sales or inventory transactions and are therefore independent of sales/cash and inventory processes perform the on-site “spot audits/site reviews.”

However, it is noted that a detailed risk assessment to better manage this process and better evaluate potential fraud is not yet being done. The Department agrees the current annual spot audits/site reviews could be scaled up, and formalized through better risk assessment frameworks. The Executive Financial Officer will work with staff both in and out of the Department to expand and enhance the current approach to spot audits / site reviews, with the recommendation of designing and documenting risk assessment, including fraud evaluations, in future annual processes.

The Department also acknowledges better follow-ups are required with results of the spot audits / site reviews, and the Department commits to developing better post-audit processes. This ensures following up on recommendations and ensuring any change requirements are taken.

2.2 Internal control weaknesses at the Thompson District Office

As noted in **section 1**, we identified a pattern of irregularities at the Thompson District Office involving the management of cash and inventory. We believe the following internal control weaknesses increased the risk of such irregularities occurring.

INADEQUATE SEGREGATION OF DUTIES AND NO COMPENSATING CONTROLS

Three kinds of functional responsibilities should be performed by different individuals:

1. Recording of transactions. This duty refers to the accounting and recordkeeping functions.
2. Control of inventory and sales.
3. Periodic reconciliation of existing assets to recorded amounts.

In an ideal situation an individual should not be responsible for more than one of the above tasks. Incompatible responsibilities make it possible for a person to create and conceal errors, irregularities and misstatements. Segregating such functions has 2 major benefits: irregularities are made more difficult to accomplish because collusion between 2 or more persons would be required (most people hesitate to seek the help of others to conduct wrongful acts), and innocent errors are more likely to be found and corrected.

At the Thompson District Office, one individual performed all of the following tasks:

- Controlled licence and permit inventory.
- Sold licences and permits.
- Collected cash/cheques from the sale of licences and permits.
- Prepared the MROs.
- Prepared and made the bank deposit.
- Maintained physical custody of the cash float.

In order to minimize the risk of misappropriation of funds and inventory, some of these tasks should not be performed by the same individual, specifically:

- A clerk that collects cash/cheques from the sale of licences/permits should not also prepare the bank deposit.
- The individual that sells the licences should not also control the inventory of licences.
- The individual that sells licences/permits should not also be prepare the MRO.
- The individual that reconciles inventory on hand should not also be in charge of the inventory.

We understand that staffing limitations in small district offices may at times make it difficult to segregate all incompatible functions. In these situations a mitigating control would be effective supervision. We found, however, that there was no supervisory review of bank deposits at the Thompson District Office to ensure deposits agreed to the detail recorded on the MRO (or to more detailed documents attached to the MRO) and, as discussed below, that supervisors were not conducting licence inventory counts for reconciliation to sales.

Having one individual perform multiple functions increased the risk of asset misappropriation at the Thompson District Office. Sustainable Development officials acknowledged that greater segregation of duties might be possible in a location like Thompson where there are 2 offices (regional and district), but would be more difficult in rural district offices that only have limited staff. We noted that at the Falcon Lake District Office bank deposits were reviewed by a separate individual and that the preparer and reviewer both initialed the bank deposits.

Recommendation 2: We recommend that Sustainable Development segregate incompatible duties at its various locations whenever possible and practical. When not possible or practical, we recommend that Sustainable Development conduct additional or extended procedures (for example, supervisory reviews), based on the specific risks associated with each location.

RESPONSE OF OFFICIALS

The Department agrees with the recommendation to segregate duties whenever possible and practical and/or to conduct extended procedures as required.

District Offices have limited staff and it is sometimes difficult to separate incompatible duties. To mitigate this, the Department has improved annual training that occurs on cash and revenue handling in regions. Regional Management is included in the annual spring training sessions that are undertaken by Financial Services Branch (Winnipeg HQ) out in the Regions to improve on-site supervision, enforce deposit and reporting rules and oversee the documented procedures. (Note: This training consists of Winnipeg staff such as the Revenue Manager going out to various Regional Offices in Manitoba, and providing training sessions for new and existing staff, with handouts and manuals of procedures. The sessions now have supervisors invited and attending.) The supervisors are also responsible for on-site security and safety of assets and staff. There was an emphasis placed on the responsibilities for this role in recent years to improve local monitoring. In spring 2018, additional emphasis was provided on revenue collection procedures and the fact that spot audits / site reviews will be conducted across the province in summer 2018. Staff were encouraged to contact Winnipeg staff or their supervisors if they have questions about revenue collection procedures.

The department has referenced the importance of segregation of duties in the Comptrollership Plan, and in larger centres like Winnipeg and Regional Offices this works well, with multiple clerks in the same offices that have assigned different duties / components of work to ensure segregation of duties. For example, staff who prepare sales documents should be different from staff member who prepares the deposit documents.

However, the Department acknowledges that in remote areas there is opportunity to review this further. The Department, through Financial Services Branch, will work with management in Regions to review the extent of segregation of duties in remote areas, look for opportunities to ensure segregation of duties is maximized, and that supervisors are involved with more frequent reviews in remote locations based on specific risks in those locations. This will require the Financial Services Branch to review and create Department policy on this, with specific location-specific procedures based on any specific risks and realities in remote areas.

Policy is in place that staff who reconcile the point of sale systems and the bank accounts are separate from the person preparing and making the deposits.

The Department, through Financial Services Branch and management in the Regions, will work with the Human Resources to clarify the roles and responsibilities in the position descriptions of administrative staff, supervisory staff, regional management and financial services staff as it relates to cash handling and inventory duties, and ensure these documents align with policy goals of segregation of duties.

NO PERIODIC INVENTORY COUNTS CONDUCTED

Sustainable Development's Remittance Procedures (for licences/permits etc.) require the following:

"Each office with an inventory of outstanding documents must confirm the amount outstanding on the tracking log to a physical count of the documents on a frequent basis. This count must be documented and signed off by the individual completing the count and filed for future reference."

We note that the Remittance Procedures do not:

- Specify how often the inventory counts should be done.
- Include a requirement to submit the inventory count results to the Licensing (or responsible) Branch. By not requiring the submission of count results Sustainable Development will not know if districts offices are conducting counts. Further, if there are missing licences, Sustainable Development will not know until unsold licences are sent back to the responsible branch.
- Provide guidance on who should be conducting the inventory counts.

Inventory counts should not be done by individuals who are also responsible for the custody, selling and recording of licence/permit transactions.

We found that the District Office did not maintain tracking logs and that it was not performing inventory counts.

Recommendation 3: We recommend that Sustainable Development strengthen its inventory Remittance Procedures to include:

- How often the inventory counts should be done.
- A requirement that the inventory count results be submitted to the Licensing (or responsible) Branch. If inventory counts are not conducted there should be a follow up process in place.
- Guidance on who should be conducting the inventory counts. The individual who conducts the count should not be responsible for the custody, selling and recording of licence/permit transactions.

RESPONSE OF OFFICIALS

The Department agrees that the inventory remittance procedures required strengthening.

The Department produces several manuals and guidance documents that are updated each year and posted on the intranet with instructions to staff to print manual copies when required.

As discussed in our response to Recommendation 2, the Department conducts annual training sessions in the regions in cooperation with regional staff to provide guidance on policies and procedures.

In addition, over the past couple of years, the Department has also developed new policy and procedure guidelines for counting and safeguarding inventory. However, it is acknowledged that the Department can review and enhance these policies and procedures further, in keeping with the OAG recommendation. For example, how often counts should be done, and how they can be efficiently provided to the central Financial Services Branch, and how a coordinated analysis can be undertaken.

The Licensing Unit (a Unit within Financial Services Branch) is now involved with inventory reconciliations throughout the year rather than just annually when the parks close. The Unit also has improved inventory transfer and receipt procedures to better document the audit trail of inventory movements.

As general policy, the one conducting inventory counts is not the one responsible for custody, selling, and recording of transactions. However, the Department acknowledges this needs to be reviewed and explored further as per the OAG recommendation, particularly in remote locations within the province.

The Department also acknowledges there is opportunity to get Regional managers involved in this process, and the Financial Services Branch will work with Regional managers to develop methods for them to support this process, providing independent oversight and counts on a regular basis, over the clerks conducting the sales.

MROS NOT PROPERLY COMPLETED

All cash and cheques received by a district office are recorded on an MRO. MROs can be prepared daily or weekly depending on the volume. It is a key document supporting the completeness of each bank deposit. However we found that MROs for hunting and fishing licences were not properly completed because only totals were recorded on the form and not the licence numbers, purchasers' names and dates of sale. This makes linking specific cheques to the MRO impossible. Deposit slips list cheque amounts but there can be many cheques for the same amount making it impossible to connect a specific person's cheque to the sale of a licence and conversely, making it possible to conceal the misappropriation of cash as discussed above.

Recommendation 4: We recommend that Sustainable Development include in their quality assurance processes the periodic review of MROs prepared by each district office, campground and park gate to ensure all required information is accurately recorded and properly supported. We further recommend that they provide clerks and supervisors with needed training or directives to ensure expectations are completely understood.

RESPONSE OF OFFICIALS

The Department agrees that quality assurance processes, periodic reviews and training are required.

The Department has conducted rotational site-specific, spot audits and reviews throughout the province since 2013. As per our response to Recommendation 1, it is acknowledged these could be improved with a risk-based assessment framework.

The Department conducts annual training and provides guidance manuals online for clerical and supervisory staff, as described in our response to Recommendation 2. However, it is acknowledged this can be enhanced to ensure roles and responsibilities are understood, and that they are documented in such things as position descriptions. Financial Services Branch will work with Human Resources and Regional management to ensure position descriptions reflect the roles and responsibilities. Financial Services Branch will review training to ensure it is comprehensive in all areas required.

The Department has begun to explore "smart forms" for the Money Remittance Orders (MRO). The smart forms would have automatic calculations (self-balancing) and contain built-in rules that would force critical information in the required fields. The Department will continue its review of this option, with the goal of instituting it in the near future.

The Department will ensure sample documents are included in the annual training materials to ensure relevant examples are available to staff.

The Department currently pre-prints tracking numbers on all MRO documents that are distributed to the Regions, Districts and Campground Offices. All MRO documents must be accounted for, even if voided. Missing MRO documents will be investigated. It is acknowledged that when sending out these MROs across the Province, it is

difficult to track sequential MRO numbers of manual MROs. Until smart forms can be instituted, the Department will analyze how better to monitor MROs across the Province.

2.3 Bank reconciliations not timely

On a monthly basis, bank statements should be reconciled to accounting records.

We found that the Financial Services Branch was several months behind in preparing bank reconciliations. Not conducting bank reconciliations in a timely manner increases the risk to Sustainable Development that errors, omissions, or misappropriations will not be detected or go undetected for extended periods of time.

Recommendation 5: We recommend that Sustainable Development Financial Services staff prepare the monthly bank reconciliations and that they be reviewed and approved by management.

RESPONSE OF OFFICIALS:

The Department agrees that monthly bank reconciliations must be prepared, and subsequently reviewed and approved by management.

The Department has a weekly benchmark for deposits, and monitors for outstanding deposits. The Department is committed to maintaining and completing monthly bank reconciliations by Financial Services staff who are separate from the custody, selling and depositing functions.

The Department acknowledges that the bank reconciliations have not been prepared and reviewed in a timely fashion in the Department in the past. The Department will change the function of the Financial Services staff to focus on reconciling the bank statements, monitor the cash handling process and provide training and support to the Regions and Districts. These staff will be restricted from posting sales transactions to SAP and the point of sale system as these duties deferred their attention from these duties.

The Department commits, based on the above, to review bank reconciliation timeframes, set internal timelines, and work to achieve those timelines for bank reconciliations.

Monthly reports for Management review and approval are now being developed by the Financial Services Branch for Executive Financial Officer and Deputy Minister review and approval:

- Monthly Sales of licences, permits and passes,
- Accounts Receivable*,
- Account Receivable Collections*,
- Inventory Variances, shortages and write-offs* and,
- Bank Reconciliations (to be added in future)

**in place now*

3 Paper-based licences and permits outdated, inefficient

Computerized systems would provide an opportunity to re-engineer the manually intensive process currently in place, gain efficiencies in transaction processing, and allow for a stronger control environment. As discussed below, computerized systems would provide stronger internal controls in the areas this audit identified as being weak (**section 2**).

ELECTRONIC MRO SYSTEM BEING PILOTED BUT WITH LIMITED FUNCTIONALITY

During our visit to the Portage la Prairie District Office we saw that some new systems were being put in place but with limited functionality. We were told that Sustainable Development was moving to a process of electronic MROs (the form on which district offices record each sale) and that it was being piloted in the Portage la Prairie office as part of their point of sale system. This point of sale system allows the clerk to enter the sold licence number directly into the system. The system produces an electronic MRO which automatically lists totals for the different types of transactions. It eliminates the need for the clerk to prepare multiple MROs. We noted that the system was not yet being used to record the names of those who purchased licences. Licences were still being completed manually and the licence holder continued to be provided with a carbon copy of each licence/permit purchased. The plan was for the MRO to be matched to the bank deposit and then immediately be posted to the general ledger.

“SUSTAINABLE DEVELOPMENT” CARDS WOULD ELIMINATE PAPER LICENCES

Some provinces (British Columbia, Alberta, Saskatchewan and Ontario) use computerized systems for selling licences. In these systems individuals are issued “Sustainable Development” cards that record on a magnetic strip the details of the licences or permits they purchased. When an individual purchases a licence or permit, the purchased item is added to their existing Sustainable Development card.

Some provinces allow for purchases over the Internet, via a kiosk, or sold by an individual using a point of sale system. This provides for electronic controls over sales transactions. Another benefit of this technology is that typically there is no paper inventory of pre-numbered licences or permits because a licence is created when it is purchased by the user. As such, the possibility of inventory being misappropriated would be minimized.

In Manitoba most licences are carbon copies. An individual may have multiple licences or permits and therefore multiple carbon copies. An advantage of a modern card system is that Resource Officers can scan an individual's card and see all the current licences they possess.

COMPUTERIZED SYSTEMS WOULD FACILITATE INCREASED EFFICIENCIES

Sustainable Development officials noted that computerized systems would bring numerous advantages including reduced risk of manual entry errors, more controls over the sale of each

unique licence, significant efficiencies and tracking abilities, and easier monitoring by enforcement staff.

At the time of our audit there were 3 different systems to track inventory and revenue for licences and permit sales. All 3 were not directly linked and required separate manual entry. Manual entry increases the risk for errors, requires more human resources, and requires reconciliations between the systems.

There is a significant time lag (i.e. weeks) between when a sale occurs in the field and the recording of the sale transaction in the Department's accounting system. This time lag occurs because the MROs (the form on which district offices record each sale) and the supporting documentation must be couriered to the Financial Services Branch in Winnipeg for inputting of the sales information into the Department's accounting system.

CONSULTANT'S 2010 REPORT ON TECHNOLOGY SOLUTIONS NOT ACTED ON

Management has been investigating technology solutions for several years. A full report was produced by an external consulting firm on August 12, 2010. The report focused on the objective of developing and implementing an effective, efficient and sustainable Licensing Management System. The report considered technical feasibility, economic viability and ensuring legislated requirements were met. At the time of our audit the Department had not yet acted on the consultants recommendations.

Given the inefficient processes noted above, and the overarching control environment concerns, we encourage Sustainable Development to assess the costs and benefits of pursuing more automated system solutions.

Rural Municipality of De Salaberry: Audit of Financial Irregularities



Assistant Auditor General

Brian Wirth

Principal

Jacqueline Ngai

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Auditor General's comments

We receive numerous concerns through our citizen concerns line citizens.concerns@oag.mb.ca. The allegations against the RM of De Salaberry came to us through this process.

While we audited the 5 financial allegations received, we also expanded our audit to include assessing internal controls over council member expense claims. We concluded that 2 of the allegations were substantiated, but could not conclude on one. We also found opportunities to strengthen the claims processing system. Our report includes 8 recommendations to strengthen the RM's processes.

While our citizen concerns line is open to all residents of Manitoba, we would especially like to hear from public servants. If you are an employee of one of the many institutions controlled by the Province of Manitoba and suspect fraud is occurring in your workplace, or if you are aware of the mismanagement of a program or asset, we are interested in what you have to say. All allegations or concerns received will be given serious consideration for further audit or investigatory work.

I would like to thank the staff of the RM of De Salaberry for their cooperation and assistance during our audit.

Original Signed by:
Norm Ricard

Norm Ricard, CPA, CA
Auditor General

Report highlights

Audit of financial allegations

We looked at 5 allegations,
as well as **internal controls**
over expense claims and
credit card transactions

8
recommendations
made

What we found

2 allegations were substantiated,
we could not conclude on
one allegation

\$33,000
in unsupported
credit card transactions
between January 2010 and
May 2014

Project management
services not tendered
as required by policy

Gaps in internal
controls

CAO did not
review council
expense claims
for compliance with policy

Finance committee
stopped reviewing
and approving council
expense claims

Background

In February 2014 we received allegations about financial irregularities at the Rural Municipality of De Salaberry (RM). On July 29, 2014 we scheduled an audit to assess the validity of the financial allegations, and to identify potential opportunities to strengthen related systems and procedures.

The RM is roughly 60 km south of Winnipeg. In 2015 the RM's population was 3,349. The municipality is governed by a 7-member Council, comprised of 6 Councillors and a Reeve. During the period covered by our audit there were 3 different Chief Administrative Officers.

Audit approach

Our audit objectives were to assess:

1. The validity of the financial allegations:
 - Some credit card transactions lacked support.
 - Personal items were charged to RM credit cards.
 - Not all donations at a fundraising event were deposited.
 - There were excessive promotional expenses.
 - Project management services were not tendered.
2. The adequacy of the RM's internal control procedures for processing expense claims.

Our audit covered the period from January 1, 2010 to May 31, 2014.

Our audit was performed in accordance with Investigative and Forensic Accounting (IFA) standards as established by the Chartered Professional Accountants of Canada (formerly the Canadian Institute of Chartered Accountants). IFA standards are designed for engagements that *"involve disputes or anticipated disputes, or where there are risks, concerns or allegations of fraud or other illegal or unethical conduct."*

Findings and recommendations

1 Two allegations substantiated, could not conclude on one

The financial allegations we investigated and our conclusions are summarized in **Figure 1**. Our conclusions are based on transactions that occurred between January 1, 2010 and May 31, 2014. Detailed discussions for each of the allegations follows.

Figure 1: Allegations & conclusions	
Allegation	Our conclusion
a. That some credit card transactions lacked support.	A significant number of transactions were not properly supported.
b. That personal items were charged to RM credit cards.	Charging certain personal amounts to RM credit cards is allowed by RM policy but the policy also requires that the recipient reimburse the RM. All personal amounts were reimbursed.
c. That not all donations at a fundraising event were deposited.	We could not conclude on the completeness of the deposits.
d. That there were excessive promotional expenses.	Between 2010 and 2014 approximately \$16,000 was recorded as promotional expenses. Some promotional items (valued at \$3,978 in total) were given to staff members as a staff appreciation gesture.
e. That project management services were not tendered.	Project management services were not tendered.

Web Version

Allegation 1a: That some credit card transactions lacked support

The Reeve, the Chief Administrative Officer (CAO), and the Public Works Foreman had RM credit cards in the period we examined.

As detailed in **Figure 2**, we found that 28% of credit card transactions processed between January 1, 2010 and May 31, 2014 were not properly supported. We noted that all credit card transactions were approved by the CAO and Council's Finance Committee before the monthly credit card statements were paid.

Figure 2: Detailed audit findings – RM credit cards		
Properly supported	\$86,368	72%
Unsupported	32,951	28%
Total	\$119,319	

We used the following criteria to assess if an amount was properly supported:

- Original receipts or invoices (not copies) were attached to the monthly credit card statement.
- A full description of the expense was provided (detailed restaurant receipts and supplier receipts or invoices showing what was bought – credit card slips or statements alone were inadequate).
- The purpose of business meals and the people attending were documented.

The unsupported transactions included:

- Hotel, restaurant and other charges not supported by a receipt or invoice.
- Restaurant charges with or without a receipt but with no detail about the purpose of the meal or who attended. Of note is that if a restaurant charge was incurred on the date of a Council meeting or conference, and there was a detailed receipt attached, we classed it as supported.

We also found that the RM did not have a policy on when it would be appropriate for Council members and RM staff to incur local meal and entertainment expenses and under what circumstances alcohol would be allowed, if ever. Of the \$119,319 in credit card charges, \$1,604 related to alcohol purchased with meals, or for an event such as a Christmas party.

Recommendation 1: We recommend that the RM develop a policy on local meal and entertainment expenses that:

- Defines the circumstances where such expenses are allowed.
- Requires transactions be supported by original receipts with details of what was purchased.
- Requires documentation on the purpose of restaurant meals and who attended, and documentation on the nature and purpose of entertainment events.
- Defines if and when alcohol charges are allowed.

Allegation 1b: That personal items were charged to RM credit cards

There are 2 instances where the RM will pay the up-front cost for personal charges for RM staff, but will require the staff to re-pay the amounts.

First, the RM has a personal computer purchase plan for Council members and staff, where the RM will pay the upfront cost. The recipient then repays the RM with regular payments deducted from their earnings for up to 2 years, interest free.

Second, the RM has a policy for staff members who attend an out-of-province conference with their spouse. The RM will pay the spouse's conference fees and airfare, and similar to the computer purchase plan, the RM will recover these amounts through regular payroll deductions.

We found \$5,967 in transactions from 2010 to 2014 that were to be repaid to the RM. The amounts were fully recovered from the Councillors or staff members. We did not find any other personal items charged to the RM credit cards.

Allegation 1c: That not all donations at a fundraiser were deposited

It was alleged that not all the donations at a fundraising golf tournament were deposited to the Fond Laval Cloutier Fund (Fund). We examined available documents for the Fund relating to its process, donations, and expenses.

The Fund, held in trust by the RM, is overseen and coordinated by a Board appointed from the Knights of Columbus of St. Pierre, St. Malo and Otterburne, as well as municipal officials from the RM and the Village of St. Pierre (one member each, 5 in total). The Fund, available to residents of the RM and the Village of St. Pierre, helps with the costs of emergency medical care that would otherwise cause undue financial hardship to a family. Applications approved by the Board are forwarded to the RM so that a resolution of Council can be passed to make disbursements from the Fund to approved applicants.

The Fund balance at December 31, 2009 was \$18,687, and at December 31, 2013 it was \$29,563. For the calendar years 2010 to 2013, the main source of revenue for the Fund was from the Fond Laval Cloutier Fund Charity Golf Tournament. During this time period no disbursements were made.

RM officials said that local volunteers run the Fond Laval Cloutier Fund Charity Golf Tournament from start to finish. One volunteer collects the donations and submits the cash and cheques to the RM after the event, with a list of donors and amounts donated by each person. The RM then issues a cheque to the volunteer for the full amount of the donations so the volunteer can pay tournament expenses. Later, the volunteer forwards the remaining money to the RM for deposit to the Fund, and gives the RM a list of the tournament revenues and expenses.

We reviewed the documents prepared by the tournament volunteers for the tournaments held in 2010 to 2012 (there was no tournament in 2013). As shown in **Figure 3**, we found that supporting documents for expenses were not provided in 2010 and 2012, and no expense information was provided in 2011. In addition, no reconciliation of the net profit from the fundraiser to the amount deposited by the RM were provided for 2010 to 2012.

Figure 3: Tournament information prepared by RM volunteers

Information	Tournament year		
	2010	2011	2012
List of donors	34	31	28
Donations (cheques)	\$ 4,100	\$ 4,050	\$ 3,640
Donations (cash)	\$ 1,450	\$ 0	\$ 1,450
Detailed list of expenses	List of expenses only ¹	No info provided	List of expense only ¹
Reconciliation of net profit to deposit	No info provided ²	No info provided	No info provided ²

¹ No supporting documents provided

² Net profit did not equal the amount deposited to the Fund (the differences were under \$200)

The allegation focused on the possibility that some donations were not being deposited to the Fund, but there is no way to assess if this was the case. We could only verify that the cheque provided to the volunteer agreed to the total donations recorded by the volunteer on the listing prepared at the golf tournament. We could not assess the completeness of this listing.

Unrecorded cash donations is a significant risk for most cash based fund raising events. The tournament's process for collecting cash donations, as described above, is highly susceptible to this risk. The RM official noted that in the days following the event, the RM issues charitable donation receipts based on the list of donors prepared by the volunteer. To better ensure all cash donations are recorded, it would be more effective to have a municipal official issue receipts to donors immediately at the event.

Recommendation 2: We recommend that a municipal official issue receipts at the charity golf tournament immediately upon receipt of the donation.

Recommendation 3: We recommend that the RM require a detailed listing of expenses for the charity golf tournament, and that this listing be supported by invoices/receipts.

Allegation 1d: That there were excessive promotional expenses

Between 2010 and 2014 the RM recorded approximately \$16,000 as promotional expenses. Of note was the purchase of 25 jackets with RM logos, for \$3,978 (roughly \$159 each). Eight of these jackets were sold by the RM to Council members, and RM officials said the rest were gifted to RM staff as a staff appreciation gesture. In our view, it is not clear how the distribution of these items to RM staff and officials constitutes a promotional expense.

The RM also bought 100 golf shirts with logos, for \$3,976 (roughly \$40 each). RM officials said these were distributed to organizations in the RM for fundraising events, such as the St. Malo Fire Department silent auction.

The purchases of all other promotional items were small in value and distributed to organizations in the RM for fundraising events. These items included bags, coolers, and umbrellas.

Allegation 1e: That project management services were not tendered

In the period we examined (2010 to 2014), the RM paid about \$45,000 to a consultant for project management services. To buy goods or services valued between \$2,000 to \$10,000, the RM's purchasing policy requires that it solicit a minimum of 3 written quotes and include the purchase in its annual budget. Several payments to the consultant exceeded \$2,000, we noted the RM approved the acquisition of the consultant's services by resolution, however, we could not find evidence that the RM sought written quotations for the related services.

RM officials said the RM does not employ engineering staff, so it needs project management expertise on certain projects. They noted that this consultant is familiar with the RM and provides ongoing services to it. While municipalities develop working relationships with professional service providers, they should periodically tender for services to ensure they obtain value for money.

Recommendation 4: We recommend that the RM tender for project management services every 4 to 5 years and that the RM include this requirement in its purchasing policy.

2 Some gaps in internal controls over expense claims

2.1 Majority of claims properly supported

We examined expense claims for all Council members and the CAOs for the period January 1, 2010 to May 31, 2014. The RM's Council remuneration bylaw has rates and allowances for Council members travelling on RM business or attending conferences. While there is no specific expense and allowance policy for RM staff, we were told rates and allowances for Council members were also used for RM staff.

As detailed in **Figure 4** we found that the majority of expense claims were properly supported.

Figure 4: Detailed audit findings – Expense claims		
Properly supported	\$231,594	98%
Unsupported	2,273	1%
Claims could not be located	3,006	1%
Total	\$236,873	

We used the following criteria to assess if an amount was properly supported:

- Original receipts or invoices (not copies) were attached to the expense claim.
- A full description of the expense was provided, with detailed restaurant receipts and supplier receipts or invoices showing what was bought. Any transaction slips without itemized receipts were inadequate.
- The purpose of business meals and people attending were documented.

Web Version

The unsupported transactions included:

- Restaurant charges without proof of payment, details of what was bought, or people who attended.
- Charges with no receipt.
- Daily compensation and meal allowance charges for attending conferences with no details on which conference it was.
- Charges with no dates.

2.2 Controls over Council expense claims not always followed

All Council members must submit their expense claims on the Friday before the last Council meeting of each month, using the RM's standard expense claim form. Council's expense policy says office staff will code the claims before the Council meeting and make them available for review and approval by the Finance Committee. We noted the following issues:

- **Expense claim approvals stopped:** Starting in 2012, the Finance Committee stopped reviewing and approving Council member expense claims. We were told the Committee did this because it was receiving too much information. The Finance Committee continued approving the CAO expense claims and all other payables.
- **Expense claims not reviewed by CAO:** We noted that the expense policy does not require this.
- **Expenses not submitted on standard claim form:** Rather than using the standard claim form, some Council members submitted their claims using handwritten notes, or an RM "job order" form, or simply submitted the receipts.
- **Expense claims not always submitted on time:** Some Council members would submit shortly after month-end; others would wait a few months. In one case, a Council member waited until the year was over and then submitted all expense claims in a bundle the following year.

We also found that expense claim forms do not require a signature by the claimant to certify that amounts claimed were accurate and for municipal business. As a result CAOs and Council members did not consistently sign their expense claims.

Recommendation 5: We recommend that the CAO review all Council member expense claims for compliance with Council's expense policy, and that the Finance Committee review and approve all Council expense claims before they are paid.

Recommendation 6: We recommend that the RM amend their standard expense claim form for Council and staff to require a signature certifying that all amounts claimed are accurate and incurred on municipal business.

2.3 Bylaw silent on certain meal expenses and rates, and wrong rates claimed

Specific meal per diem rates not listed in bylaws: The Council remuneration bylaw provides a \$45/day meal allowance for attending conventions or seminars outside of the RM but there is no breakdown of rates for specific meals. Nonetheless, some expense claims included specific meal rate per diems (presumably for breakfast, lunch, or dinner).

Wrong rates claimed: Council members can claim a full-day per diem for attending conventions and seminars outside of the RM. But in some cases they claimed the full-day amount for purposes other than attending conventions or seminars.

Some claimants were paid using updated rates that were not in effect at the time the expense was incurred.

Bylaw is silent on whether meal expenses can be claimed when working within the RM: On occasion meal expenses were claimed for work performed in the RM, however, the Council remuneration bylaw does not specifically allow for meals when work is performed in the RM.

Recommendation 7: We recommend that the RM revise the Council remuneration bylaw to include specific meal per diem rates, and to define the circumstances when meals can be claimed for work within the RM.

2.4 Other internal control weakness noted

Bank reconciliations were not prepared promptly: Most bank reconciliations were completed 4 – 8 months after month end. In addition, bank reconciliations were not reviewed or approved by the CAO after they were completed.

Recommendation 8: We recommend that bank reconciliations be completed promptly, ideally within 30 days after month end, and that the CAO review and approve them after they are completed.

Comments of officials

The Rural Municipality of De Salaberry council thanks the Auditor General for a preview of the draft audit report *Rural Municipality of De Salaberry (RM): Audit of Financial Irregularities* and appreciates the opportunity to provide comments ahead of its presentation to Manitoba Ministers and the Legislative Assembly.

Of greatest importance to members of the current council, is to note that the period the audit covered was from January 1, 2010 to May 31, 2014. The majority of existing councillors (6 of the 7) were not part of the council where decisions were made under the period reviewed until October 2010 (2 newly elected) and October 2014 (4 newly elected). Significant changes have occurred since that time. Internal controls have been strengthened to better protect assets of the municipality including those of a financial nature.

The RM's comments to each of our Recommendations are as follows:

Recommendation 1: We recommend that the RM develop a policy on local meal and entertainment expenses that:

- Defines the circumstances where such expenses are allowed.
- Requires transactions be supported by original receipts with details of what was purchased.
- Requires documentation on the purpose of restaurant meals and who attended, and documentation on the nature and purpose of entertainment events.
- Defines if and when alcohol charges are allowed.

While a written policy has not been drafted, the current administration reviews expenses first by the Chief Administrative Officer or designate, then the Finance Committee and finally council. Original detailed receipts are required (in instances where a receipt cannot be located, a statutory declaration is required), attendance at restaurant meals is noted, with the expense accounted for accordingly. Developing a written policy in this regard will be researched and inquiries will be made into how other municipalities address local meal and entertainment expenses.

Recommendation 2: We recommend that a municipal official issue receipts at the charity golf tournament immediately upon receipt of the donation.

Recommendation 3: We recommend that the RM require a detailed listing of expenses for the charity golf tournament, and that this listing be supported by invoices/receipts.

Council agrees with the recommendation from your office that if future events of this nature commence, a municipal official will attend the charity event to issue receipts immediately upon receipt of the donation. As well, a detailed listing of expenses, with supporting documentation will be prepared and kept on file for review.

Recommendation 4: We recommend that the RM tender for project management services every 4 to 5 years and that the RM include this requirement in its purchasing policy.

Current council and administration has followed the municipality's purchasing policy except in cases deemed urgent or where specialized product and services are required. There is a greater understanding that purchases from a single provider need to be considered cumulatively (over at least a one year period) as well as on a per order basis. Staff members are reminded regularly to solicit and document verbal and written quotes for purchases and include these notes with the final invoice.

Council has committed to reviewing the purchasing and tendering policy in due course to ensure it continues to meet the legislative requirements, the needs of the municipality and includes relevant clauses for sole source purchases.

Recommendation 5: We recommend that the CAO review all Council member expense claims for compliance with Council's expense policy, and that the Finance Committee review and approve all Council expense claims before they are paid.

The Chief Administrative Officer reviews all council member expense claims, following review for completeness by the finance clerk. The claims are then included with all other accounts payable batches for review by the Finance Committee prior to each regular meeting of council.

Recommendation 6: We recommend that the RM amend their standard expense claim form for Council and staff to require a signature certifying that all amounts claimed are accurate and incurred on municipal business.

Approximately 2½ years ago, the expense claims for members of council and staff were amended to require a signature. Approximately one and a half years ago the following clause was added to council expense claim forms "I declare that this account consists of authorized time devoted to municipal business and authorized expenses incurred by me on behalf of the Rural Municipality of De Salaberry." More recently, this same clause was added to staff expense claim forms as well.

Recommendation 7: We recommend that the RM revise the Council remuneration bylaw to include specific meal per diem rates, and to define the circumstances when meals can be claimed for work within the RM.

With a general municipal election taking place in October 2018, the indemnity bylaw as well as the recommendation from your office to include specific meal per diem rates, and to define circumstances when meals can be claimed for work within the RM, will be reviewed by the new council in the first few months following their inaugural meeting.

Recommendation 8: We recommend that bank reconciliations be completed promptly, ideally within 30 days after month end, and that the CAO review and approve them after they are completed.

Bank reconciliations had been caught up and were completed in the first few days following month end, but they were delayed again when the Finance Officer position became vacant. The Finance Officer position will be filled on August 27, 2018 with a person holding an accounting designation. We expect that shortly thereafter, all financial matters will be caught up and completed within a reasonable time frame.

Council assures your office and the residents and ratepayers of this municipality that it takes very seriously its legislated obligations to consider the well-being and the interests of the Rural Municipality as a whole. This includes developing and reviewing policies to ensure they continue to meet legal requirements as well as the needs of the municipality and ensuring controls are in place to protect assets belonging to the people in this municipality.