



COST RECOVERY FRAMEWORK

July 2010

Internal Audit Branch



TABLE OF CONTENTS

STATEMENT OF ASSURANCE	i
EXECUTIVE SUMMARY	1
1. INTRODUCTION	7
1.1 Background.....	7
1.2 Audit Objectives	8
1.3 Audit Scope.....	9
2. OBSERVATIONS – MANAGEMENT FRAMEWORK	11
2.1 Roles and Responsibilities	11
2.2 Integrated Planning	12
2.3 Human Resources	13
2.4 Policies, Procedures, and Guidelines	15
2.5 Training.....	16
2.6 Monitoring	17
3. OBSERVATIONS –TIMEKEEPING	21
3.1 Compliance with the National Timekeeping Protocol.....	21
4. OBSERVATIONS – COSTING MODEL.....	25
4.1 Single Model to Charge Departments and Agencies	25
4.2 Simplification of Invoice Processing Procedures	26
4.3 Disbursements.....	27
4.4 Monthly Billing.....	30
5. OBSERVATIONS, RECOMMENDATIONS, AND MANAGEMENT RESPONSES .	33
APPENDIX A – METHODOLOGY	39
APPENDIX B - COST RECOVERY FINANCIAL INFORMATION.....	41

STATEMENT OF ASSURANCE

We have completed the internal audit of the Cost Recovery Framework in the Department of Justice. The overall objectives of the audit were to review and assess the adequacy and appropriateness of the established management control framework for cost recovery and the single model for charging departments and agencies. As part of this, the audit examined and assessed the policies and procedures that form part of the cost recovery framework; the existing mechanisms to appropriately link cost recoveries with the budget allocation process; the appropriateness of standardized interdepartmental Memoranda of Understanding (MOUs); and the efficiency and appropriateness of practices related to the recovery of disbursements.

The internal audit was conducted in accordance with the requirements of the Treasury Board Secretariat (TBS) *Policy on Internal Audit* and the Institute of Internal Auditors' *Standards for the Professional Practice of Internal Auditing*. The audit team assessed the management control framework against criteria derived from the TBS *2003 Management Accountability Framework*, as well as TBS audit guides.

In our professional judgment, sufficient and appropriate audit procedures have been conducted and evidence has been gathered to support the accuracy of the conclusions reached and contained in this report. The conclusions were based on a comparison of the situations, as they existed at the time of the audit, against audit criteria. It should be noted that the conclusions are only applicable to the areas examined.

EXECUTIVE SUMMARY

In 2004 the Treasury Board Secretariat (TBS) conducted a Review of Legal Services, which examined, inter alia, the sustainability of funding and the management of legal services in the Government of Canada. Its findings supported reliance on a hybrid model to fund the provision of legal services, which allows the Department to receive A-Base funding with the remaining portion of its costs being recovered from client departments and agencies that use legal services.

In October 2006, the Treasury Board Secretariat (TBS) approved the establishment of a Net Voting Authority, in the amount of \$178 million (i.e. excluding Employee Benefit Plan contributions), to the Department of Justice for the provision of legal services. The Department of Justice developed a single cost recovery model with various cost categories. These costs are used to establish uniform charge-out rates for the counsel and paralegals who provide legal services. The model is based on the full cost of delivering services, and the charge-out rates are to be applied consistently for all types of legal services including advisory, litigation, and legislative/regulatory drafting. Disbursements paid by the Department of Justice on behalf of client departments are recovered through a separate disbursement recovery process. In an effort to streamline this process, as of April 1, 2008, disbursements below \$200 are recovered by incorporating these disbursement costs into the charge-out rates.

Revenues from cost recovery are significant, exceeding \$200 million annually for the first time in 2008-09 and accounting for more than a third of the departmental operating budget. Moreover, the cost recovery process involves most departmental organizations, including management, legal practitioners, and financial and administrative staff. The full impact of the move to a Net Voting Authority regime and standardized legal services rates on the Department and its external stakeholders is still being realized.

This audit focused on reviewing and assessing the adequacy and appropriateness of the existing management control framework for cost recovery and the single cost recovery model for charging client departments. In our opinion, the management framework is insufficiently robust to support cost recovery.

Roles and Responsibilities

Two main departmental offices are involved in managing the cost recovery process: the Finance Branch, which is responsible for implementing the financial aspects of cost recovery; and the Law Practice Management Directorate (LPMD), which is responsible for the business side of law practice. (It should be noted that effective July 2009 the Chief Financial Officer (CFO) Branch was established. Recommendations in this report are therefore addressed to the CFO.)

Both of the above offices are integrally involved in cost recovery management. Continued collaboration is therefore required to identify and implement continuous improvements in the cost recovery process.

Integrated Planning

We found that there is a need for an integrated plan that sets out a strategy for the management of cost recovery. The plan should address gaps and identify enhancements, including measurable objectives; resource requirements; clear accountabilities, roles, and responsibilities; policies, procedures, and documented processes; and timelines for action. At a minimum, the plan would address the issues of resources at all levels of the Department, work instruments, process design, professional development, and communications.

Human Resources

When Net Voting Authority was originally introduced in April 2007, the Department was given little time and no incremental resources to implement it. It was also introduced at a time when the Finance Branch was experiencing high staff turnover and financial expertise was uneven across portfolios.

At the time of the audit, financial management advisors (FMAs), who are professional financial officers reporting under the CFO, could be found in only two portfolios: Public Safety, Defence and Immigration; and Aboriginal Affairs. We were told that, at the time of the audit, the resource situation in Finance was improving and a plan was under way to have FMAs employed in the portfolios and in the three specialized legal areas (i.e. the Litigation Branch, the Legislative Services Branch, and the Public Law Sector). In our opinion, it is essential to proceed with this plan to ensure portfolio and sector management are provided with the requisite financial support to meet their accountabilities.

Policies, Procedures, and Guidelines

At the time of the audit, the Department was preparing to enter its third year of cost recovery under Net Voting Authority. While some formal procedures were in place, portfolios were using numerous distinct methods to obtain client approval for recovering legal service costs. These processes were often complex and varied significantly by client department. Legal sections in the regions were using different approaches for managing and monitoring recoverable costs apart from those related to the processing of interdepartmental settlements (IS). Portfolios have developed and, in some cases, documented their own procedures for billing, which have been distributed to the DLSUs and regions. Furthermore, we found that Finance had not provided any best practices, lessons learned, or benchmarks on cost recovery. More documented financial policies, procedures, and guidelines to direct activities relating to cost recovery are required.

Training

In the early stages of cost recovery, management meetings, conference calls, conferences, and seminars routinely took place and national templates were distributed to the business managers to assist them in planning and tracking their recoverable costs. While Finance continues its consultations with departmental staff, we were told that the national templates were not used by staff for their day-to-day work. Instead, groups developed their own sets of procedures and templates to collect and track information on recoverable costs. More extensive training on the use of the national templates would have been beneficial.

In our view, more extensive training is required for departmental staff involved in day-to-day cost recovery activities.

Monitoring

Both Finance and the portfolios have a role to play in monitoring revenue targets. Portfolios are responsible for ensuring payment from their clients, but lack standardized processes to support their position. This situation should improve with the implementation of the new standardized legal services agreements with client departments set for April 2009.

Finance monitors the financial position of the Department primarily through the Financial Situation Report (FSR). However, the revenue/cost recovery component of the FSR is relatively new and forecasts from the portfolios in the regions have not been accurate. An FSR Working Group has been formed to further develop this reporting tool to allow management to obtain clear and more timely information on expected revenues. In our opinion, an effective monitoring

program would allow Finance to identify problem areas and take early and remedial action to address issues.

It is important for Finance to track those accounts receivable related to hourly-based cost recoveries at an earlier stage than is currently the practice. A methodology is needed to capture and identify receivables at the time the Statement of Account from iCase is issued. This would allow for more effective monitoring and enable early detection of problems requiring remedial action.

Compliance with the National Timekeeping Protocol

Legal practitioners (counsel and paralegals) and computer specialists (CSs) need to adhere to the requirements of the National Timekeeping Protocol in recording their time. Section 3.1 of the NTP states: “to help ensure data integrity, time should be recorded on a daily basis or as soon as practically possible thereafter”. Some practitioners throughout the Department enter their time into iCase at the end of the month or later. The Department must ensure that timekeepers enter their time into iCase regularly, preferably daily.

Single Model to Charge Departments and Agencies

The costing model for legal services is based on a sound and reasonable methodology that is consistent with TB requirements.

Simplification of Invoice Processing Procedures

Justice staff in the regions and DLSUs expend significant time and effort in attempting to identify the area of a client department that has incurred the legal service and is responsible for payment. This issue accounts for some of the difficulties in obtaining the client department approvals for payment.

The introduction of standardized legal services agreements in fiscal year 2009-10 represents a positive move toward improving and standardizing management of interdepartmental arrangements including the invoicing process. Client departments are expected to provide Justice with a single set of financial (FIS) codes or, at most, one set per organizational unit led by an Assistant Deputy Minister or equivalent. During 2008-09, Justice invoiced against 475 different cost centres within the 154 client departments it serves.

In our opinion, a more simplified invoicing process that allows for more timely processing of cost recoverable transactions by client departments is required.

Disbursements

The current process of recovering disbursements is administratively cumbersome. The Cost Recovery Section of Finance estimated that the Department is not recovering for all disbursements to which it is entitled. The Department took steps to simplify the process in 2008-09 by including an hourly charge of \$0.40 in the rates to cover disbursement transactions below \$200. (A recent analysis suggests that the \$0.40 increase is insufficient to fully cover disbursements below \$200.) This initiative notwithstanding, the management of disbursements still poses a problem for Finance. A review of the rates charged for disbursements and an analysis of the various options for recovering disbursements are required.

Monthly Billing

The Department's present quarterly billing process presents serious cash flow issues for management. Approximately 60% of cost-recovered revenues flow into the Department during the last three months of the fiscal year. This can create constraints on spending and reduce flexibility to expend earlier in the year.

More frequent billing would not only have a positive impact on the cash flow of the Department, but it would also enable administrators to identify billing errors more quickly. Year-end invoicing would also be simplified and billing errors would be more readily identified.

The management responses to the recommendations contained in this report were provided by the Chief Financial Officer, Chief Financial Officer Branch and the Assistant Deputy Minister, Management Sector.

1. INTRODUCTION

1.1 Background

In 2004 the Treasury Board Secretariat (TBS) requested a Review of Legal Services to examine, inter alia, the sustainability of funding and the management of legal services in the Government of Canada. The review was jointly undertaken by the Department of Justice and TBS, in consultation with selected government departments and agencies.

This review led to a better understanding of the relevant costs of providing legal services to the Government. Its findings supported the continued reliance on a “hybrid” model to fund the provision of legal services in the Department of Justice. This hybrid model entails a mix of A-Base funding and recoveries from departments and agencies¹, and recoveries from other organizations such as crown corporations, and non-federal and international organizations. Services provided over and above established levels would be charged to client departments, while levels of service provided without charge to these client departments would be reviewed and established annually by the Department of Justice.

The hybrid model is intended to balance the demand, supply, and oversight of legal services to the Government. It provides the Department with A-Base funding to meet a certain level of demand for legal services and allows client departments to fund demands for legal services beyond the resources available to the Department. The model also provides incentives for these client departments to manage their demand for legal services and recognize shared accountabilities with respect to government legal matters.

In October 2006, the TB approved Net Voting Authority² for the Department of \$178 million (i.e. excluding Employee Benefit Plan contributions) for the provision of legal services. On April 1, 2007, Net Voting Authority came into effect and the Department of Justice began cost

¹ For ease of reference in this report, we will refer to these government departments and agencies as “client departments”.

² Net Voting Authority is defined as a special, revenue re-spending authority from Parliament that allows a department to use some of its revenues to finance directly related expenditures. Under this mechanism, there is normally a well-established core level of activity funded through appropriations. The Net Voting Authority is provided to fund fluctuating demands from user groups that, while consistent with program objectives, would otherwise jeopardize the relatively stable “core” budget of a department.

recovery of legal services based on a funding model that includes a mix of appropriation (A-Base) and recovery from client departments.

The Department of Justice has developed a single cost recovery model with various cost categories. These costs are used to establish uniform charge-out rates for the counsel and paralegals who provide legal services and for computer specialists (CSs). The model is based on the full cost of delivering services, and the charge-out rates are applied consistently for all types of legal services, including advisory, litigation, and legislation/regulatory drafting. Rates are reviewed annually, adjusted, and submitted to TB for approval.

Disbursements paid by the Department of Justice on behalf of client departments are recovered through a separate “disbursement recovery” process. In an effort to streamline this process, as of April 1, 2008, disbursements below \$200 are recovered by incorporating these disbursement costs into the charge-out rates, as approved by TB. This was done in an effort to eliminate the cumbersome administration involved for both the Department and its clients.

Budgets are provided to departmental responsibility centres based on an A-Base allocation and revenues from Net Voting Authority. These revenues represent a significant funding source for the Department, with more than a third of its operating budget coming in the form of Net Voting Authority. In 2007–08, the Department of Justice collected \$213.7 million from cost recovery including disbursements. As of December 8, 2008, the Department had collected \$98 million (i.e. 44%) of the anticipated \$225 million in revenue for 2008-09.

The following risk factors were considered in this audit: level of recovery of actual costs; adequacy of documentary support for cost recovery claims against clients; appropriate use or application of financial controls; clarity of accountabilities and expectations; compliance with policies or procedures related to cost recovery; adequacy of monitoring, guidance, and direction; appropriateness of rates; and consistency of reporting.

1.2 Audit Objectives

The main objectives of this audit were to review and assess the adequacy and appropriateness of the existing management control framework for cost recovery and the single cost recovery model for charging client departments.

The audit team reviewed and assessed:

- a) roles, responsibilities, and authorities for approving and initiating cost-recovered services to ensure they are appropriate and consistent with enhancing overall accountability;

- b) the policies and procedures that form part of the cost recovery framework, including:
 - accounting/charging procedures to determine consistency with TB policies;
 - internal reporting procedures aimed at providing the Department of Justice management and clients with timely and accurate information on services to departments/agencies and associated costs;
 - processes for consulting, communicating, and settling disputes with clients;
- c) the existing mechanisms to link cost recoveries appropriately with the budget allocation process;
- d) the appropriateness of generic, interdepartmental Memoranda of Understanding (MOUs);
- e) the efficiency and appropriateness of practices related to the recovery of disbursements.

Finally, the auditors reviewed and assessed whether the costing model and the rates for legal services were appropriate and consistent with applicable TB policies.

1.3 Audit Scope

The audit included activities at headquarters, four regional offices (British Columbia, Prairie, Quebec, and Ontario) and two departmental legal services units (Health Canada and Canada Border Services Agency DLSUs).

The audit focused on the management framework for cost recovery, but excluded extensive testing to ascertain the accuracy of costs recovered and the reliability of reporting this information. This will form the basis for a second audit to be undertaken at a later date.

The recovery of salary costs for Department of Justice counsel who participate in secondment or interchange agreements with other organizations falls outside the scope of the Net Voting Authority regime and was therefore excluded from the audit.

The planning and on-site examination phases for this audit were carried out between November 2008 and February 2009.

Details of the audit methodology employed are outlined in Appendix A.

2. OBSERVATIONS – MANAGEMENT FRAMEWORK

2.1 Roles and Responsibilities

An integrated management approach that responds to business requirements associated with the practice of law and facilitates cost recovery is required.

At the time of the audit, two main departmental offices were involved in managing the cost recovery process. These were the Finance Branch and the Law Practice Management Directorate (LPMD). The Director General (DG), Finance, was the lead executive responsible for implementing the financial aspects of cost recovery. It should be noted that effective July 2009 the Chief Financial Officer (CFO) Branch was established. Recommendations in this report are therefore addressed to the CFO, who reports to the Deputy Minister. The DG, LPMD reports to the ADM, Management Sector and is responsible for providing functional direction and support on business practices related to the practice of law, such as legal information and systems (i.e. iCase timekeeping), standard legal services agreements, and reporting on the delivery of legal services.

Since both offices are integrally involved in cost recovery management, it is important that they collaborate to manage the cost recovery process. The issues of timekeeping and billing are inextricably linked to the cash management of the Department and require a unified and fully coordinated approach to optimize the cost recovery process. Areas that require coordination relate primarily to the timely entry and validation of timekeeping, the simplification of invoice approval with clients, and the creation of a central repository for all legal services agreements.

We were told that financial staff in the Department can request reports from the LPMD, but some financial staff continue to indicate a need for greater access to iCase timekeeping information, an integral component of the cost recovery process. Financial staff who have responsibilities for the whole of the Department and the portfolios indicated that improved access to this information would facilitate the process of identifying trends, isolating processing bottlenecks, planning and assessing workloads, and conducting simulation analyses.

We note that portfolios, departmental legal services units, regional offices, the Public Law Sector, the Litigation Branch, and the Legislative Services Branch each have a role to play in the cost recovery process. Portfolio business managers have experience in overall business planning and performance management as well as the day-to-day operations of the portfolio. Input from all internal stakeholders would be advantageous in the standardization of the invoicing process, the development of work instruments, and the design of a training package for staff involved in the day-to-day cost recovery process.

In our view, an integrated and coordinated management approach is required that responds to the business requirements associated with the practice of law and facilitates cost recovery.

Recommendation and Management Response

- 1. It is recommended that the CFO and the ADM, Management Sector, continue to work together to further develop an integrated and coordinated management approach that responds to business requirements and facilitates cost recovery.**

Agree. Optimizing management practices in regard to the Department's cost recovery processes has been identified as one of the priorities of the CFO and requires close collaboration between CFO Branch (CFOB) and Management Sector. Although management practices may not be formalized, the collaboration among CFOB, Management Sector, portfolios, and regions on specific files related to cost recovery practices is evident, as for example, with the standardized legal services agreement, the re-engineering of billing practices, and the system integration of the cost recovery process. By September 2010, the CFO and the ADM, Management Sector will determine the most appropriate mechanism through which discussions on common themes can be addressed, either through the establishment of a new working committee or through existing forums, as well as the appropriate governance from which management decisions will be attained.

2.2 Integrated Planning

There is a need for an integrated plan that sets out a strategy for the management of the Department's cost recovery.

Successful organizations use planning to identify issues, activities, resource levels, and initiatives that will contribute to the achievement of stated objectives. Planning is also the process by which managers identify priorities, which is an important aspect of managerial responsibilities, especially in situations where resources are scarce. A strategy includes the articulation of

strategic choices, which provides information on how an organization intends to achieve its priorities and associated results.

We found that an integrated plan that sets out a strategy for the management of cost recovery has not been developed. A strategy is needed that sets out a vision for the end-state of cost recovery and the steps required for its effective implementation. The plan should include measurable objectives; resource requirements; clear accountabilities, roles, and responsibilities; policies, procedures, and documented processes; and timelines for action. At a minimum, the plan would address the issues of resources at all levels of the Department, work instruments, process design, professional development, and communications.

Recommendation and Management Response

- 2. It is recommended that the CFO, with the support of the ADM, Management Sector, ensure that an integrated plan is prepared that sets out a strategy for the management of cost recovery.**

Agree. The CFOB strategic plan has identified the need for the establishment of a net vote framework that would articulate the Department's management of its net vote authority, including the re-engineering of cost recovery processes. The framework will be a formal document that provides context, standards, and directions, as well as the supporting structure. This document will consist of a set of ideas, conditions, or assumptions that determine how the management of the net vote authority and cost recovery processes will be approached, perceived, and understood by departmental staff. Articulated roles and responsibilities will ensure all requirements are assigned so that established standards may be adhered to. It is anticipated that the net vote framework project will move forward over the next two years (i.e. 2010-11 and 2011-12), and that the development of an integrated plan for the management of cost recovery formalizing the vision will be part of discussions noted under Recommendation 1. In support of such a framework, the plan will focus on gaps and the development of enhancements, which will direct resources to priorities, set a direction with deliverables, establish a timeframe, and ensure objectives are met.

2.3 Human Resources

More financial management advisor positions are needed for cost recovery in the portfolios and the three specialized legal areas.

When Net Voting Authority was originally introduced in April 2007, the Department of Justice was given little time and no incremental resources for its implementation. The TB submissions

for Net Voting Authority and the 2007–08 legal services rate structure were only approved in October 2006 and March 2007 respectively. Client departments were only advised of the new rates in a letter from the Deputy Minister in April 2007. Moreover, Net Voting Authority was introduced at a time when the Finance Branch was experiencing high staff turnover and financial expertise was uneven across portfolios.

As noted earlier, during the audit, the Department was in the process of implementing the Chief Financial Officer (CFO) model in an effort to comply with the Treasury Board *Policy on Financial Management Governance*. Under this model, financial management advisors (FMAs) would have a line reporting relationship to the Finance Branch and would physically reside within portfolios and sectors to provide independent financial management and oversight to the ADAG and portfolio/sector management. At the time of audit, FMAs, who are qualified professional financial officers, could be found in only two portfolios: Public Safety, Defence and Immigration; and Aboriginal Affairs.

We were told that, at the time of the audit, the resource situation in Finance was improving and a plan was under way to have FMAs employed in all of the portfolios and in the three specialized legal areas (i.e. the Litigation Branch, the Legislative Services Branch, and the Public Law Sector). In our opinion, it is essential to proceed with this plan to ensure portfolio and sector management are provided with the required support to meet their financial accountabilities.

Recommendation and Management Response

3. It is recommended that the CFO ensure that each of the portfolios and the three specialized legal areas at headquarters are appropriately staffed with FMAs.

Agree. The financial management advisor function continues to gain support and be strengthened throughout the Department. The CFO has made presentations to each of the Direct Reports to the Deputy Minister within the National Capital Region to discuss the role of the FMAs, and outline their responsibilities and how they are to operate within the Department. Additional FMAs have been hired including the FMA director, remaining positions are being created, and permanent financial resources are being requested from the Department. As of March 31, 2010 there are 8 FMAs within 10 portfolios/sectors and some areas have hired and/or requested more than one FMA. Departmental support is growing and plans are moving forward; however, some challenges may be encountered in regard to competing demands for limited departmental resources, given the current government fiscal restraints. It is intended that within the next two years the FMA function will be fully integrated within the Department's business.

2.4 Policies, Procedures, and Guidelines

More standardized procedures for cost recovery are required at all organizational levels in the Department.

Documented policies, procedures, and guidelines promote the consistent, effective, efficient, and economical conduct of activities. These instruments also help to provide assurance that organizational resources are suitably safeguarded.

At the time of the audit, the Department was preparing to enter its third year of cost recovery under Net Voting Authority. While some formal procedures were in place, we noted that portfolios were using numerous distinct methods to obtain client approval for recovering costs related to the provision of legal services. These processes were often complex and varied significantly by client department. We also found that portfolios' guidance varied in level of detail and, in some cases, allowed up to thirty days following the close of a quarter for approving expenditures. Several individuals interviewed noted the need for detailed operating procedures for cost recovery at the portfolio/regional level. Finance staff advised that efforts are under way to address this.

The audit revealed that legal sections in the regions use different approaches for managing and monitoring recoverable costs apart from those related to the processing of interdepartmental settlements. We found that portfolios have developed and, in some cases, documented their own procedures for billing, which have been distributed to the DLSUs and regions. However, Finance was not involved in the development of these procedures. Also, we found that Finance had not provided any best practices, lessons learned, or benchmarks on cost recovery.

More documented financial policies, procedures, and guidelines to direct activities relating to cost recovery are required.

Recommendation and Management Response

- 4. It is recommended that the CFO, with support from the ADM, Management Sector, as required, ensure that a complete suite of directives, procedures, and guidelines for cost recovery is developed to ensure the implementation of standard procedures across the Department.**

Agree. Senior Management Board (SMB) has approved the creation of a senior management steering committee to oversee a business process re-engineering project being undertaken to develop standardized cost recovery directives, procedures, and guidelines for

implementation across the Department. The timeframe for the project is over the next two years with a projected implementation date of April 1, 2012., integrated with the iCase NG project. This project will also take into consideration the net vote framework as outlined in the response to Recommendation 2.

2.5 Training

More extensive training is required for departmental staff involved in cost recovery activities.

During the early stages of cost recovery, Finance devoted time and resources to evolve the costing and charging function (i.e. develop a costing model and legal services rates). Finance staff met routinely with Portfolio business managers to assess costs, validate revenue forecasts, discuss rates, and answer questions. The Director General, Finance, also led quarterly Finance conferences and bi-weekly conference calls with portfolio business managers and regional finance directors to discuss cost recovery issues. The Cost Recovery Team, which consisted of staff from the Resource Management Division of Finance, met with all DLSU heads and held two seminars with client departments.

While Finance has continued its consultations with departmental staff, we found there is a need for more financial management training for all staff involved in day-to-day cost recovery activities. This includes counsel in the DLSUs, regions, Public Law, Litigation Branch, and Legislative Services, who need to understand the cost recovery process and the role they play in the process. Although national templates were distributed to the business managers to assist them in tracking their recoverable costs, we were told that these templates were not used by some staff for their day-to-day work. Instead, groups developed their own sets of procedures and templates to collect and track information on recoverable costs. Specific training on the use of the national templates would have been beneficial. We are of the view that more training is required for all staff involved in day-to-day cost recovery activities.

Recommendation and Management Response

- 5. It is recommended that the CFO with the support of the ADM, Management Sector, as required, ensure that more extensive training is provided to departmental staff involved in cost recovery activities.**

Agree. See response to Recommendation 4. As part of the business process re-engineering project, appropriate training will be developed and delivered to departmental staff involved in cost recovery activities.

2.6 Monitoring

There is a need to improve the monitoring program for cost recovery and forecasting of revenues.

Monitoring is the ongoing, systematic process of collecting, analyzing, communicating, and using performance information. Monitoring is an essential component of assessing an organization's progress toward meeting expected results. It supports decision making, accountability, and transparency.

Given the significance of cost recovery to the financial and cash management position of the Department of Justice, it is important that appropriate mechanisms be in place to monitor the process closely. We found two key issues with respect to the monitoring of the cost recovery process:

- **Lack of standardized legal services agreements for cost recovery**
Both Finance and the portfolios have a role to play in monitoring revenue targets. Portfolios are responsible for ensuring payment from their clients, but they lack such tools as standardized legal services agreements to support their position. This situation should improve with the implementation of the new standardized legal services agreements with client departments set for April 2009 and the establishment of a central repository within the Finance Branch for all legal services agreements.
- **Financial Situation Report (FSR) effectiveness as a monitoring tool for cost recovery**
Finance monitors the financial position of the Department primarily through the Financial Situation Report (FSR). FSR call letters are sent out nine times during the fiscal year, beginning in June and August, and every month thereafter.

In 2007-08, following the implementation of Net Voting Authority, the revenue/cost recovery component of the FSR was relatively new and still in its early stages. One focus of the FSR was to monitor budgets, and more specifically, section D was designed to forecast revenue. However, as the Department transitioned to a clearer process, submission of section D was deferred. As a result, we found that the information submitted was neither reliable nor meaningful. During this period, the Resource Management Division developed an alternative forecasting approach based on Salary Management System (SMS) FTE data to assist in the validation of portfolio input. During the audit period, this approach was still being used to challenge the submitted

information. Greater access to iCase data would better facilitate the financial challenge function at the departmental and portfolio levels.

A 2004 guide to preparing the FSR exists, but it requires updating. The amounts (based on portfolio and regional inputs) have been inaccurate, partially because of the lack of instructions on how to forecast these revenues. The numbers are reviewed and challenged by Finance's Resource Management Division, which is responsible for departmental estimates, budgeting, and forecasting. The December 2008 FSR reported a possible surplus position of \$17.9 million from cost recovery, but the revised forecasted revenue for January 2009 reduced this figure by \$6.7 million. It is not clear whether the surplus is a result of non-utilized A-Base funding or cost recovery revenue, because internal mechanisms do not align costs with funding sources.

We note that a Financial Situation Report Working Group, which consists of Resource Management Division staff and financial management advisors from two portfolios, has been formed. Its purpose is to develop FSR work instruments, reporting structure, and guidelines to address the needs for budget management, cash management, and revenue reporting.

In our opinion, an improved monitoring program would allow Finance to identify problem areas and take early and remedial action to address issues.

Recommendation and Management Response

6. It is recommended that the CFO improve the monitoring program for the recovery of costs and forecasting of revenues.

Agree. During the 2008-09 fiscal year, the CFOB utilized two different approaches in forecasting revenues to establish a best practice going forward. The first approach was based on a monthly portfolio input, while the second one was based on quarterly costing and revenue simulations. In 2009-10 we were able to better balance the use of these two approaches and this resulted in reducing the revenue forecast fluctuations. For 2010-11 we will work with LPDM to explore options to facilitate access to the iCase timekeeping information and gain a greater visibility on the A-base discounts to further improve the accuracy and reporting of revenue forecasts. We agree that an improved monitoring program needs to be in place and that during the audit period we worked through some transitory issues as we moved through a net vote authority implementation and an appropriate forecasting of revenues; however, we support the use of the Financial Situation Report (FSR) as a reliable monitoring tool. Our view is that the revenue forecast

fluctuations in 2008-09 were not due to the tool itself but rather due to the changes to input and assumptions on FTEs and to the demand requirements from client departments.

The implementation of the financial management advisor function will give an additional focus to financial activities and enhance the Department's ability to monitor cost recovery and revenue forecasts. This function's reporting relationship with the Resource Management Division will also facilitate the development and implementation of standard processes, and assist in common messaging. The FSR working group will continue to discuss best practices, update documents, establish new standards, and communicate its results to appropriate staff.

There is a need to develop a procedure to capture and recognize accounts receivable related to cost recovery for hourly billings.

Finance is not tracking accounts receivable for cost recoveries related to hourly billings and disbursements and is not aware of the actual amount of outstanding billings. The departmental practice in the case of hourly billings is to issue an iCase Statement of Account, or what is known as a "polite invoice," to the client department. Finance only recognizes the transaction as an accounts receivable after the client department has provided the Financial Information Strategy (FIS) code³ and it is actually received at the Cost Recovery Section in the Finance Branch for processing. In the case of Crown corporations and other levels of government, no FIS code is required and the Finance Branch recognizes the accounts receivable when the invoice is received and processed in the Cost Recovery Section. It is our opinion that once a polite invoice for services billed has been issued, an accounts receivable has been created.

We found that there is no standardized process to manage receivables associated with cost recovery related to hourly billings. For example, while regions track each of their respective statements of account, no formalized reporting mechanism is in place to present their status to the portfolios. We found that for the regions and DLSUs contacted, the cost recovery transaction is initiated when the region sends the respective DLSU an iCase Statement of Account, which may or may not include supporting documentation. After an appropriate review, the DLSU provides the FIS codes on behalf of the client department to the regional office, which then forwards the transaction to the Cost Recovery Section at headquarters for processing. Consequently, the portfolios are only aware of the Statement of Account after it has been paid (i.e. Statement of Account with the client FIS code sent to the Cost Recovery Section and recovery has taken place).

³ FIS Codes are needed for the processing of interdepartmental transactions (known as "interdepartmental settlements" or ISs) through the government's Standard Payment System.

It is important for Finance to track accounts receivable at an earlier stage than is currently the practice. A procedure is needed in the case of hourly billings to capture and identify receivables at the time the Statement of Account from iCase is issued. This would allow for more effective monitoring and enable early detection of problems requiring remedial action.

Recommendation and Management Response

- 7. It is recommended that the CFO develop a procedure to capture and recognize accounts receivable related to hourly-based cost recoveries.**

Agree. See response to Recommendation 4. Part of the business process re-engineering project will include how and when to recognize accounts receivable related to cost recovery transactions.

3. OBSERVATIONS – TIMEKEEPING

3.1 Compliance with the National Timekeeping Protocol

Legal practitioners (counsel and paralegals) and CS staff need to adhere to the requirements of the National Timekeeping Protocol in recording their time.

Accurate and complete timekeeping information supports the effective planning, funding, and management of departmental activities. In the Department all legal practitioners (counsel and paralegals) and computer specialists (CSs) are required to record their time in iCase in accordance with the National Timekeeping Protocol (NTP). Section 3.1 of the NTP states: “to help ensure data integrity, time should be recorded on a daily basis or as soon as practically possible thereafter”.

We found that some legal practitioners do not comply with NTP requirements regarding timely recording of their time into iCase. The practitioners interviewed noted that while they log their time on a daily basis, they often enter their time into iCase at the end of the month or later. LPMD provided sample data for a random three-week period. These data showed that 33% of the total timekeeping hours were entered into iCase more than 10 days following the sample period. This can cause delays in processing billings, which, in turn, affects the cash position of the Department. The 2007 Internal Audit Report of iCase stated that time is often entered retroactively after a lengthy period and the lead counsel is not required to periodically provide an official record of assurance that the time recorded against files is correct. The report also noted the effect this has on data integrity: “There have been some poor timekeeping practices by certain sections or staff, such as bulk time entry against a few files and time recorded infrequently. These practices are likely to introduce inaccuracies.”

While the regimen of private practice timekeeping in six-minute units of account (i.e. timekeeping of every one-tenth of an hour) may be unnecessary at the Department of Justice, not entering time in accordance with the NTP is an unsound business practice. We also noted that guidelines issued to some practitioners provide up to 30 days to enter timekeeping following the end of a month. This practice causes significant delays in presenting invoices to client departments for settlement and is inconsistent with the NTP. Quebec is the only regional office

where management requires legal practitioners to enter timekeeping data into iCase daily. Weekly entry of time is permitted only in exceptional circumstances.

The Department must ensure that timekeepers enter their time into iCase regularly, preferably daily. The Department could consider incorporating this requirement into the performance appraisal process.

Recommendation and Management Response

8. It is recommended that the ADM, Management Sector, remind departmental managers that legal practitioners and CS staff must comply with the requirements of the National Timekeeping Protocol for recording of time into iCase.

Agree. The Management Sector will ensure that appropriate and periodic communications are disseminated to all practitioners on the need to comply with the requirements of the NTP. In addition, the Management Sector will request that the Department's Executive Committee take action to promote and monitor adherence to the NTP

Legal practitioners in the regions contacted are recording time to miscellaneous and general client files contrary to NTP requirements, which delays cost recovery.

Cost details on invoices need to be clearly specified and readily identifiable for the client. Consequently, charges entered by legal practitioners against client accounts should clearly specify the client file that was worked on. Section 3.4.2 of the iCase National Timekeeping Protocol stipulates: "Time should be recorded to a specific client or specific corporate Justice file and the use of miscellaneous files should be avoided whenever possible."

Client administrative staff within the DLSUs reported that legal practitioners in regional offices sometimes enter time in iCase against a client general file or a miscellaneous file instead of a specific client (case) file. They indicated that this should not be permitted because it is administratively difficult to identify to which client file the costs should be assigned. The DLSUs and portfolios noted that billing against a client general file or miscellaneous file can delay the payment of the entire invoice.

Legal practitioners should adhere to the provisions of section 3.4.2 of the National Timekeeping Protocol.

Recommendation and Management Response

- 9. It is recommended that the ADM, Management Sector, remind legal practitioners of the need to comply with the National Timekeeping Protocol with respect to entry of time to miscellaneous and general client files.**

Agree. The importance of recording time to a specific client file or a specific corporate Justice file rather than to a general or miscellaneous file whenever possible will be among the key messages identified in communications regarding the need for compliance with the National Timekeeping Protocol. Efficiency and effectiveness remain guiding principles for establishing standards with respect to the opening of files. See response to Recommendation 8.

4. OBSERVATIONS – COSTING MODEL

4.1 Single Model to Charge Departments and Agencies

The costing model for legal services is based on a sound and reasonable methodology that is consistent with TB requirements.

The costing model used to charge for legal services should provide a relevant, complete, and fair representation of the costs incurred by the Department in the provision of legal services, in accordance with the TB *Policy on Common Services*. Rates are to be applied consistently across the Government and should be used for all types of legal services delivered to client departments (i.e. advisory, litigation, and legislative/regulatory drafting).

Department of Justice legal services are considered a mandatory common service under the TB *Policy on Common Services*. As a guiding principle, mandatory services are funded mainly through appropriation, and optional services are funded mainly by full cost recovery through Net Voting Authority. For those mandatory services not funded by appropriation, rates charged must be set to recover, but not exceed, the full costs of providing each specific service.

We reviewed the costing model (including the rates) for legal services to ensure it is appropriate and consistent with applicable TB policies, to assess its completeness, and to verify that it fairly represents the costs incurred by the Department of Justice. We examined the five different cost categories:

- direct salaries for all counsel and paralegals
- direct overhead (i.e. support salaries and O&M)
- indirect support costs
- Employee Benefit Plan (EBP) costs
- accommodation

We reviewed the costing framework, which outlines the steps used to create the costing model and which was developed by the Costing and Charging Section. We examined the Costing Procedures document, which identifies the steps followed to download financial information

from the Integrated Financial and Materiel System (IFMS) and staffing information from the SMS. We also examined a report prepared by external consultants. This report concluded that the costing model was based on sound costing methodology and reflected all appropriate costs; that the costs per FTE of legal services computed by the costing model were a reasonable estimate of the actual costs; and that the administrative overhead resources, as a percentage of total FTEs, were, if anything, at the low end of comparably sized departments. We found the costing model for legal services to be appropriate.

4.2 Simplification of Invoice Processing Procedures

Invoice processing related to cost recovery transactions from client departments should be simplified.

Invoice processing related to cost recovery needs to be streamlined and efficient. This would be indicated by a billing process based on the financial and administrative requirements of Justice Finance, the client department, and the TB *Directive on Payment Requisitioning and Cheque Control* as well as the Receiver General's *Information Notice 2006-002 Appendix 6*. Cost recovery invoicing processes should not involve Justice Finance performing invoice-related work tailored to meet the specific requirements of the accounting processes of various client departments.

We found that Justice staff in the regions and DLSUs expend significant time and effort in attempting to identify the area of a client department that has incurred the legal service and is responsible for payment. These staff are also having difficulties in obtaining from the client department the approvals for the transaction that are required before the transaction can be forwarded to the Cost Recovery Section of Finance for recovery through the IS process. This is occurring both with regard to legal services recoveries and disbursements. Under the current cost recovery invoicing processes, Justice Canada is performing much of the accounting work that should rightfully be done by the client department itself.

The implementation of the new standardized legal services agreement beginning fiscal year 2009-10 represents a move toward improving and standardizing the management of interdepartmental arrangements including the invoicing process. The new legal services agreement emphasizes the steps required to conform to the federal government's IS process and the need to restrict the level of FIS codes to limit the number of client invoices prepared by Justice Canada. Client departments are expected to provide Justice with a single set of financial (FIS) codes or, at most, one set per organizational unit led by an Assistant Deputy Minister or equivalent. Restricting the level of FIS codes is designed to limit Justice's administrative burden in effecting payment. We found that during 2008-09 Justice invoiced against 475 different cost

centres within the 154 client departments it serves. In Health Canada alone, we identified 78 units in its five branches where invoices are sent for approval.

The Health Canada DLSU has now addressed this issue by using a unique approach. The DLSU will use only one financial code for Health Canada when the new legal services agreement is implemented in April 2009 and will pay Justice under this one financial code for all legal services. To ensure that each transaction is sent to the appropriate Health Canada unit, the DLSU will assign the iCase Client Cost Centre code to each of the active Health Canada legal files. The iCase Client Cost Centre code enables the DLSU to quickly identify which organizational unit within Health Canada is responsible for approving the costs to be recovered. This approach facilitates the routine review of file status. During the DLSU's implementation of the iCase Client Cost Centre, a file review was conducted and 4,521 of the 10,751 files were closed. Of the remaining 6,230 open files, 3,772 were deemed to be "active" (i.e. time has been recorded against them during the fiscal year). As files become active or new files are opened, the iCase Client Cost Centre Code is appended.

In our opinion, a more simplified invoicing process that allows for timely approval of cost recoverable transactions by client departments is needed. This will require a collaborative approach on the part of both Justice and client departments to explore the different opportunities available to simplify invoicing processes.

Recommendation and Management Response

- 10. It is recommended that the CFO, in consultation with the ADM, Management Sector, assess opportunities to simplify invoicing related to cost recovery transactions in client departments.**

Agree. See response to Recommendation 4. One of the anticipated outcomes of the business process re-engineering project will be to simplify invoicing related to cost recovery.

4.3 Disbursements

A review of rates charged for some disbursements and an analysis of the various options for recovering disbursements are required.

The recovery of legal disbursements from client departments should be managed fairly, efficiently, and effectively to minimize the risk of loss and ensure clients pay for bona fide disbursements related to litigation cases for which they are accountable.

Disbursements are generally non-FTE-related costs paid by the Department in the conduct of a particular file or initiative. These costs include court fees, witness fees, and the costs of transcripts, interpretation, photocopying, printing, travel, and online research. These disbursements generally occur when litigation cases take place. They do not significantly affect the DLSUs, because few litigation cases are managed there and client departments generally provide the office, equipment, and supplies.

Disbursements currently represent approximately six percent of the total recoveries in the Department of Justice. In fiscal year 2008-09, disbursements totalled \$6,336,048 as of December 8, 2008, of which \$2.1 million had yet to be recovered.

The recovery of disbursements poses a problem for the Department of Justice, both at headquarters and in the regions. Disbursements are paid by the regional offices on behalf of client departments and are recorded in Fund 29 against a specific FIS code in the departmental financial system (IFMS). FIS codes are IFMS accounts provided by the clients that enable interdepartmental settlements (IS). The Cost Recovery Section of Finance does the actual recovery through IFMS, which produces a Cost Recovery Report.

Delays occur in the collection process for two reasons. First, there are data input errors and coding issues within the Department of Justice itself and the litigation case to which the disbursement applies is not always properly identified. Secondly, clients experience difficulty sorting out billings, because of the complexity and volume of transactions, and often require additional information before they will provide the Department with a FIS code.

The Cost Recovery Section currently employs 1.5 FTEs to recover disbursements. We were told that there are plans to increase this number by an additional FTE. Due to coding errors related to disbursement charges such as insufficient or improper billing information, the Section often returns items for correction, sometimes months after the fact. In the interim, the same error may be repeated several times before it is corrected. Year-end rejections often come too late for staff to re-process them. As a result, the portfolio or regional office must incur the charge against its own budget. The B.C. and Prairie regions each estimated an annual loss of about \$100,000 because of this. The A/Chief of the Cost Recovery Section estimated the Department is losing about \$500,000 annually to non-recovered disbursements from client departments. He maintained that managing disbursements continues to be a significant challenge.

The volume of transactions, the nature of the work, and the continual need to settle accounts with clients make it difficult for the Cost Recovery Section to keep staff. Staff turnover has been significant and we found that the section has seen three different people in the Cost Recovery

Officer position in the last two years. Significant time and costs are incurred throughout the Department of Justice and in client departments to settle these accounts and the process affects the harmony of Department-client relationships.

The Department took a big step to try to ease the problems it was having before the 2008-09 legal services rates were released. An analysis of the disbursements showed that in 2006-07, 41,194 (i.e. 78.9%) of the 52,210 disbursement transactions were for amounts under \$200, which represented \$900,000 of the \$13 million being recovered. With TB approval, management incorporated disbursements under \$200 into the legal services rates. An additional \$0.40 per hour was added to the rates for lawyers and paralegals for fiscal year 2008-09. Disbursements under \$200 are currently recorded in Fund 26. However, a recent analysis of Fund 26 by the Resource Management Division found that these disbursements exceed original forecasts and will total \$2.2 million in 2008-09. The \$0.40 per hour built into the rates was based on annual disbursements of \$900,000. This analysis suggests that the increase was insufficient to recover these disbursements fully and this component of the rates must be revisited.

The change to streamline the management of disbursements was supported by client departments. Notwithstanding, the Department continues to have problems managing disbursements and needs to further explore this issue. The implementation of the new legal services agreement with client departments set for April 2009, which calls for the provision of a single set of financial codes, or at most, one set per ADM or equivalent, should assist in this regard. Factoring disbursements above the current \$200 threshold into the legal services rates could also assist with managing disbursements. Data shows that in 2007-08, 53,989 of the 57,907 transactions were under \$500. Those over \$500 (i.e. 3,918) accounted for \$9,042,965 or 81.4% of the \$11,104,380 in disbursements. Other options that the Department might consider include showing both disbursements and timekeeping on the same Department of Justice invoice (i.e. similar to private practice) or decentralizing the recovery of disbursements to the regional offices.

Recommendations and Management Responses

- 11. It is recommended that the CFO conduct an annual review of Fund 26 to ascertain the adequacy of the rate being charged to cover costs associated with disbursements under \$200.**

Agree. Fund 26 is reviewed annually and the analysis of small value, high volume disbursements is part of the annual process of establishing legal services rates. It is to note that, due to the high volatility of these costs, we use historical data to determine the amount to be included in the rates. In our analysis, the risk of under/over estimating in this

particular element is embedded in the global Risk Factor wherein all parameters with high volatility or high fluctuation are covered in a global risk mitigation approach. Various thresholds (e.g. \$200 or \$500) are analyzed in terms of total cost for the Department and fairness for clients. The analytical process is followed by a formal departmental approval process where options are challenged and best “value for money” threshold is approved by the Department’s senior management.

12. It is recommended that the CFO explore various options for recovering disbursements to improve efficiency and address the issues noted in this report.

Agree. See response to Recommendation 4. The recovery of disbursements will be included in the scope of the business process re-engineering project.

4.4 Monthly Billing

There is a need for the Department to move to a monthly billing process.

Generally accepted accounting practices call for billing of services to be initiated, recorded in an accounts receivable system, and generated within an established time period after initial service delivery. This time period is often no longer than a month unless there is agreement with the client to some other billing frequency.

The current system followed in the Department is to bill clients on a quarterly basis and this is presenting serious cash flow issues for management. Currently, approximately 60% of cost-recovered revenues flow into the Department during the last three months of the fiscal year. This can create constraints on spending (e.g. for training and purchase of assets) and reduce flexibility to expend earlier in the year. As of December 8, 2008, the Department had collected \$98 million (i.e. 44%) of the anticipated \$225 million in revenue for 2008–09, with seven organizations having collected less than 40% of forecasted revenues. One DLSU indicated in an interview that, as of January 13, 2009, the billing for the first quarter of 2008-09 had yet to be completed. We also found that one client is only paying its Department of Justice account at the end of the fiscal year.

In our view, there are several benefits for the Department in increasing the frequency of its billing to client departments to be more in line with normal business practice, which is monthly or less. Not only would more frequent billing have a positive impact on the cash flow of the Department, but it would also enable administrators to identify billing errors more quickly. Instead of attempting to resolve errors that have built up over a three-month period of time, administrators would only have to deal with issues that occurred during the previous month.

Year-end invoicing would also be greatly simplified and any billing errors would only pertain to one month of transactions.

More frequent billing should be easy to apply where departmental cost recovery is on the basis of full-time equivalents (FTEs) rather than on billable hours. Portfolios that have a single client department with a stable, constant demand for legal services are generally utilizing the FTE basis as a method for recovering costs. Close to 80% of recoveries is done through the FTE method. In this case, the SMS is the financial system used to track employee movements and assignments to specific cost centres.

In the case of clients whose legal services are charged on the basis of billable hours and for whom iCase is used as the management system to track information on specific cases and practitioners' time, it would be important for practitioners to comply with the requirements of the National Timekeeping Protocol. This method currently accounts for about 16% of the recoveries. (The remainder of recoveries in the Department relate to disbursements.)

It is our view that it is important for the Department to increase the frequency of its billing practices by invoicing client departments on a monthly basis.

Recommendation and Management Response

13. It is recommended that the CFO and the ADM, Management Sector, move to invoicing client departments on a monthly basis.

Agree. For FTE-related billing, the implementation of monthly billing has been proposed to commence on October 1, 2010. For timekeeping and disbursements billing, see response to Recommendation 4, as these will be included in the scope of the business process re-engineering project.

5. OBSERVATIONS, RECOMMENDATIONS, AND MANAGEMENT RESPONSES

An integrated management approach that responds to business requirements associated with the practice of law and facilitates cost recovery is required.

- 1. It is recommended that the CFO and the ADM, Management Sector, continue to work together to further develop an integrated and coordinated management approach that responds to business requirements and facilitates cost recovery.12**

Agree. Optimizing management practices in regard to the Department’s cost recovery processes has been identified as one of the priorities of the CFO and requires close collaboration between CFO Branch (CFOB) and Management Sector. Although management practices may not be formalized, the collaboration among CFOB, Management Sector, portfolios, and regions on specific files related to cost recovery practices is evident, as for example, with the standardized legal services agreement, the re-engineering of billing practices, and the system integration of the cost recovery process. By September 2010, the CFO and the ADM, Management Sector will determine the most appropriate mechanism through which discussions on common themes can be addressed, either through the establishment of a new working committee or through existing forums, as well as the appropriate governance from which management decisions will be attained.

There is a need for an integrated plan that sets out a strategy for the management of the Department’s cost recovery.

- 2. It is recommended that the CFO, with the support of the ADM, Management Sector, ensure that an integrated plan is prepared that sets out a strategy for the management of cost recovery.....13**

Agree. The CFOB strategic plan has identified the need for the establishment of a net vote framework that would articulate the Department’s management of its net vote authority, including the re-engineering of cost recovery processes. The framework will be a formal document that provides context, standards, and directions, as well as the supporting

structure. This document will consist of a set of ideas, conditions, or assumptions that determine how the management of the net vote authority and cost recovery processes will be approached, perceived, and understood by departmental staff. Articulated roles and responsibilities will ensure all requirements are assigned so that established standards may be adhered to. It is anticipated that the net vote framework project will move forward over the next two years (i.e. 2010-11 and 2011-12), and that the development of an integrated plan for the management of cost recovery formalizing the vision will be part of discussions noted under Recommendation 1. In support of such a framework, the plan will focus on gaps and the development of enhancements, which will direct resources to priorities, set a direction with deliverables, establish a timeframe, and ensure objectives are met.

More financial management advisor positions are needed for cost recovery in the portfolios and the three specialized legal areas.

3. It is recommended that the CFO ensure that each of the portfolios and the three specialized legal areas at headquarters are appropriately staffed with FMAs.....14

Agree. The financial management advisor function continues to gain support and be strengthened throughout the Department. The CFO has made presentations to each of the Direct Reports to the Deputy Minister within the National Capital Region to discuss the role of the FMAs, and outline their responsibilities and how they are to operate within the Department. Additional FMAs have been hired including the FMA director, remaining positions are being created, and permanent financial resources are being requested from the Department. As of March 31, 2010 there are 8 FMAs within 10 portfolios/sectors and some areas have hired and/or requested more than one FMA. Departmental support is growing and plans are moving forward; however, some challenges may be encountered in regard to competing demands for limited departmental resources, given the current government fiscal restraints. It is intended that within the next two years the FMA function will be fully integrated within the Department's business.

More standardized procedures for cost recovery are required at all organizational levels in the Department.

4. It is recommended that the CFO, with support from the ADM, Management Sector, as required, ensure that a complete suite of directives, procedures, and guidelines for cost recovery is developed to ensure the implementation of standard procedures across the Department.....15

Agree. Senior Management Board (SMB) has approved the creation of a senior management steering committee to oversee a business process re-engineering project being undertaken to develop standardized cost recovery directives, procedures, and guidelines for implementation across the Department. The timeframe for the project is over the next two years with a projected implementation date of April 1, 2012., integrated with the iCase NG project. This project will also take into consideration the net vote framework as outlined in the response to Recommendation 2.

More extensive training is required for departmental staff involved in cost recovery activities.

- 5. It is recommended that the CFO with the support of the ADM, Management Sector, as required, ensure that more extensive training is provided to departmental staff involved in cost recovery activities.16**

Agree. See response to Recommendation 4. As part of the business process re-engineering project, appropriate training will be developed and delivered to departmental staff involved in cost recovery activities.

There is a need to improve the monitoring program for cost recovery and forecasting of revenues.

- 6. It is recommended that the CFO improve the monitoring program for the recovery of costs and forecasting of revenues.....18**

Agree. During the 2008-09 fiscal year, the CFOB utilized two different approaches in forecasting revenues to establish a best practice going forward. The first approach was based on a monthly portfolio input, while the second one was based on quarterly costing and revenue simulations. In 2009-10 we were able to better balance the use of these two approaches and this resulted in reducing the revenue forecast fluctuations. For 2010-11 we will work with LPDM to explore options to facilitate access to the iCase timekeeping information and gain a greater visibility on the A-base discounts to further improve the accuracy and reporting of revenue forecasts. We agree that an improved monitoring program needs to be in place and that during the audit period we worked through some transitory issues as we moved through a net vote authority implementation and an appropriate forecasting of revenues; however, we support the use of the Financial Situation Report (FSR) as a reliable monitoring tool. Our view is that the revenue forecast

fluctuations in 2008-09 were not due to the tool itself but rather due to the changes to input and assumptions on FTEs and to the demand requirements from client departments.

The implementation of the financial management advisor function will give an additional focus to financial activities and enhance the Department's ability to monitor cost recovery and revenue forecasts. This function's reporting relationship with the Resource Management Division will also facilitate the development and implementation of standard processes, and assist in common messaging. The FSR working group will continue to discuss best practices, update documents, establish new standards, and communicate its results to appropriate staff.

There is a need to develop a procedure to capture and recognize accounts receivable related to cost recovery for hourly billings.

- 7. It is recommended that the CFO develop a procedure to capture and recognize accounts receivable related to hourly-based cost recoveries.....20**

Agree. See response to Recommendation 4. Part of the business process re-engineering project will include how and when to recognize accounts receivable related to cost recovery transactions.

Legal practitioners (counsel and paralegals) and CS staff need to adhere to the requirements of the National Timekeeping Protocol in recording their time.

- 8. It is recommended that the ADM, Management Sector, remind departmental managers that legal practitioners and CS staff must comply with the requirements of the National Timekeeping Protocol for recording of time into iCase.22**

Agree. The Management Sector will ensure that appropriate and periodic communications are disseminated to all practitioners on the need to comply with the requirements of the NTP. In addition, the Management Sector will request that the Department's Executive Committee take action to promote and monitor adherence to the NTP

Legal practitioners in the regions contacted are recording time to miscellaneous and general client files contrary to NTP requirements, which delays cost recovery.

- 9. It is recommended that the ADM, Management Sector, remind legal practitioners of the need to comply with the National Timekeeping Protocol with respect to entry of time to miscellaneous and general client files.....23**

Agree. The importance of recording time to a specific client file or a specific corporate Justice file rather than to a general or miscellaneous file whenever possible will be among the key messages identified in communications regarding the need for compliance with the National Timekeeping Protocol. Efficiency and effectiveness remain guiding principles for establishing standards with respect to the opening of files. See response to Recommendation 8.

The costing model for legal services is based on a sound and reasonable methodology that is consistent with TB requirements.

Invoice processing related to cost recovery transactions from client departments should be simplified.

- 10. It is recommended that the CFO, in consultation with the ADM, Management Sector, assess opportunities to simplify invoicing related to cost recovery transactions in client departments.....27**

Agree. See response to Recommendation 4. One of the anticipated outcomes of the business process re-engineering project will be to simplify invoicing related to cost recovery.

A review of rates charged for some disbursements and an analysis of the various options for recovering disbursements are required.

- 11. It is recommended that the CFO conduct an annual review of Fund 26 to ascertain the adequacy of the rate being charged to cover costs associated with disbursements under \$200.29**

Agree. Fund 26 is reviewed annually and the analysis of small value, high volume disbursements is part of the annual process of establishing legal services rates. It is to note that, due to the high volatility of these costs, we use historical data to determine the amount to be included in the rates. In our analysis, the risk of under/over estimating in this particular element is embedded in the global Risk Factor wherein all parameters with high volatility or high fluctuation are covered in a global risk mitigation approach. Various

thresholds (e.g. \$200 or \$500) are analyzed in terms of total cost for the Department and fairness for clients. The analytical process is followed by a formal departmental approval process where options are challenged and best “value for money” threshold is approved by the Department’s senior management.

12. It is recommended that the CFO explore various options for recovering disbursements to improve efficiency and address the issues noted in this report.30

Agree. See response to Recommendation 4. The recovery of disbursements will be included in the scope of the business process re-engineering project.

There is a need for the Department to move to a monthly billing process.

13. It is recommended that the CFO and the ADM, Management Sector, move to invoicing client departments on a monthly basis.31

Agree. For FTE-related billing, the implementation of monthly billing has been proposed to commence on October 1, 2010. For timekeeping and disbursements billing, see response to Recommendation 4, as these will be included in the scope of the business process re-engineering project.

APPENDIX A – METHODOLOGY

The criteria for the audit were based on the *Guidance on Assessing Control* issued by the Criteria of Control Board (CoCo) of the Canadian Institute of Chartered Accountants, the TBS *Management Accountability Framework* (MAF) and other TBS guidance on auditing management frameworks.

The audit methodology consisted of:

- an analysis of the management control framework in place using a risk-based approach related to key elements of the framework;
- a review of relevant policies at the departmental and central agency level;
- a review, analysis, and discussion with stakeholders of cost recovery processes in the Department;
- interviews with key personnel in:
 - the Finance Branch and Law Practice Management Directorate;
 - the portfolios of Public Safety, Defence and Immigration; Tax Law Services; Business and Regulatory Law; and Aboriginal Affairs;
 - the Public Law Sector and Legislative Services Branch;
 - four regional offices (British Columbia, the Prairie Region, Quebec, and Ontario) by telephone;
 - the Health Canada and Canada Border Services Agency DLSUs.
- review of documentation and an analysis of financial data.

The audit was undertaken in a manner consistent with the Treasury Board *Policy on Internal Audit* and related guidelines and procedures, and with generally accepted auditing standards.

APPENDIX B - COST RECOVERY FINANCIAL INFORMATION

TABLE 1

**Cost Recovery - Summary Report
April 1, 2007 to March 31, 2008**

Portfolios	Regions and Sectors										Total
	Atlantic	Ontario	British Columbia	Prairie	Northern	Quebec	Head Quarters	Legislative Services	Civil Litigation	Public Law	
Aboriginal Affairs	\$1,347,518	\$4,962,980	\$11,500,222	\$20,547,579	\$2,194,753	\$1,856,125	\$15,997,694	\$811,809	\$945,722	\$573,908	\$60,738,310
Business & Regulatory Law	\$3,146,282	\$7,485,993	\$6,693,152	\$5,281,509	\$230,143	\$8,021,380	\$51,008,736	\$9,040,524	\$3,656,224	\$2,872,852	\$97,436,795
Central Agencies	\$3,534	\$375,585	\$58,948	\$113,044	\$0	\$33,708	\$7,090,869	\$749,277	\$1,010,279	\$242,823	\$9,678,067
Public Safety, Defence and Immigration	\$686,634	\$6,089,483	\$2,893,350	\$2,273,554	\$32,983	\$3,339,211	\$8,609,640	\$277,116	\$1,038,755	\$505,352	\$25,746,077
Justice ¹	\$0	\$162,062	\$12,840	\$455	\$0	\$83,400	\$1,356,750	\$332,912	\$31,581	\$363,612	\$2,343,614
Tax Law	\$149,856	\$428,279	\$596,501	\$446,964	\$2,956	\$565,224	\$25,071,703	\$0	\$12,044	\$0	\$27,273,525
Other	\$0	\$54,945	\$0	\$62,100	\$31,678	\$0	\$191,491	\$76,880	\$0	\$16,099	\$433,193
TOTAL	\$5,333,824	\$19,559,328	\$21,755,013	\$28,725,205	\$2,492,513	\$13,899,046	\$109,326,883	\$11,288,518	\$6,694,605	\$4,574,646	\$223,649,582
Secondments	\$110,324	\$95,525	\$204,263	\$442,796	\$60,686	\$410,158	\$6,746,660	\$635,543	\$62,103	\$1,197,451	\$9,965,510
Total Legal	\$5,223,500	\$19,463,803	\$21,550,749	\$28,282,410	\$2,431,827	\$13,488,888	\$102,580,223	\$10,652,975	\$6,632,502	\$3,377,195	\$213,684,072

1. The Justice Portfolio fulfils a central agency function by coordinating legal services on issues that cut across multiple areas of government and includes advisory and legislative services. The portfolio also acts as a core resource for government as a whole by providing advice on highly specialized areas of law such as human rights law, constitutional and administrative law, and international private law.

TABLE 2

**Cost Recovery - Summary Report
April 1, 2008 to January 30, 2009**

Portfolios	Regions and Sectors										Total
	Atlantic	Ontario	British Columbia	Prairie	Northern	Quebec	Headquarters	Legislative Services	Civil Litigation	Public Law	
Aboriginal Affairs	1,143,412.07	4,428,665.66	9,754,479.04	17,453,302.37	2,420,173.80	2,088,949.63	15,860,893.83	615,239.17	937,827.42	389,599.82	55,092,542.81
Business & Regulatory Law	1,585,548.65	4,197,768.73	3,189,744.25	2,394,637.21	130,243.50	3,110,490.83	33,134,544.42	7,138,014.42	3,026,231.52	811,740.96	58,718,964.49
Central Agencies	6,496.54	350,203.31	26,594.41	73,497.04	-	33,066.65	4,000,654.00	37,233.71	740,451.70	197,085.52	5,465,282.88
Public Safety, Defence and Immigration	343,143.11	2,315,546.52	1,466,333.40	1,103,874.09	68,187.61	864,064.83	6,171,285.62	92,714.00	508,112.53	223,817.20	13,157,078.91
Justice ¹	-	81,538.00	5,625.75	-	-	2,218.80	-	133,479.35	58,048.67	105,714.00	386,624.57
Tax Law	68,015.06	171,599.73	225,456.68	163,541.53	-	197,361.13	15,622,690.21	379.79	11,986.23	-	16,461,030.36
Other	-	4,311.22	-	23,786.26	-	-	19,352.09	51,171.05	743.34	545.90	99,909.86
TOTAL	3,146,615.43	11,549,633.17	14,668,233.53	21,212,638.50	2,618,604.91	6,296,151.87	74,809,420.17	8,068,231.49	5,283,401.41	1,728,503.40	149,381,433.88

1. The Justice Portfolio fulfils a central agency function by coordinating legal services on issues that cut across multiple areas of government and includes advisory and legislative services. The portfolio also acts as a core resource for government as a whole by providing advice on highly specialized areas of law such as human rights law, constitutional and administrative law, and international private law.