MINISTRY OF COMMUNITY AND SOCIAL SERVICES

Transfer Payment Agency Accountability and Governance

The Ministry of Community and Social Services plans and arranges for a wide variety of social services throughout Ontario, including services for children and families, young offenders and persons with developmental or physical disabilities.

In most instances, the Ministry does not deliver services itself. Instead, it provides strategic direction and annual funding for service planning and delivery to approximately 3,400 community-based, mostly non-profit agencies.

Ministry transfers to all of its agencies for the 1996/97 fiscal year are estimated at $2.1 billion. Total transfers by program are as detailed below.

Transfer Payments to Agencies
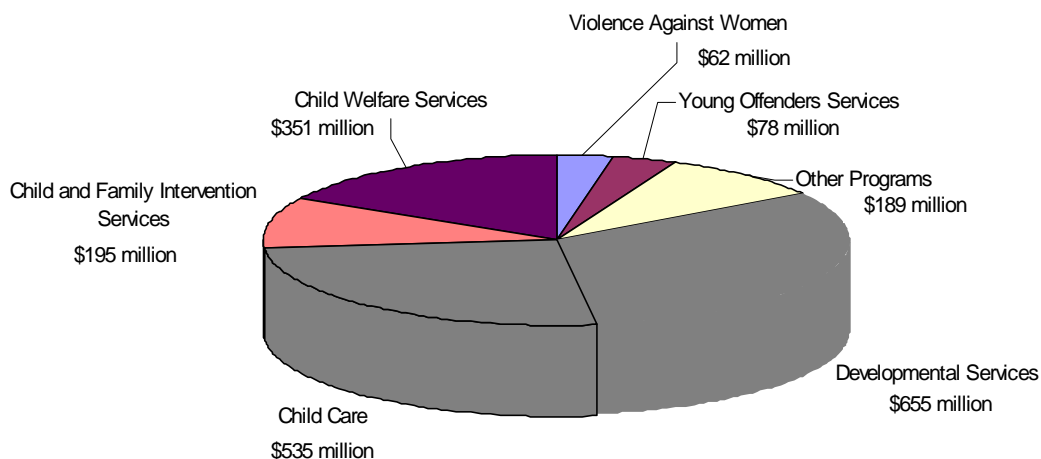
Source: Ministry of Community and Social Services

Many of the Ministry's transfer payment agencies owe their beginnings to dedicated groups of people who provided social services in their communities on a voluntary basis with little or no support from government. These services have expanded over time due to increased need and

a general trend towards community-based care. As a result, many of today's social services continue to be delivered by community-based agencies with volunteer boards of directors that are independent of the Ministry, even though the Ministry now provides a substantial portion of their funding.

OBJECTIVES AND SCOPE

Our audit objectives were to assess whether the Ministry:

*   had established and communicated to its transfer payment recipient agencies reasonable expectations for their accountability to the Ministry as well as for agency governance; and

*   had procedures in place to determine whether transfer payment recipient agencies were meeting the Ministry's expectations.

In preparing for this audit, we reviewed a number of documents and publications specifically concerned with governance and accountability. These included enabling legislation, central agency directives and publications issued by authoritative bodies such as the Canadian Institute of Chartered Accountants and the Canadian Comprehensive Auditing Foundation.

The scope of our audit included a review and analysis of the Ministry's administrative procedures, as well as interviews with appropriate head office, area office and agency staff. We also reviewed a representative sample of transfer payment agency files at selected area offices and visited agency facilities where warranted.

Additionally, we sent questionnaires to a sample of chairs of agency boards of directors and to the senior management personnel of agencies that were not selected for interviews or a more detailed file review.

Our audit also included a review and analysis of the audit plans and relevant reports issued by the Ministry's Comprehensive Audit and Investigations Branch. Although the Branch reported on governance problems at individual agencies it had audited, it had not reported on the accountability and governance framework between the Ministry and its agencies and, consequently, we were unable to reduce the scope of our work.

OVERALL AUDIT OBSERVATIONS

In light of the current government's efforts to restructure and outsource service delivery, agency accountability and governance is an increasingly important issue. However, establishing and communicating requirements for the effective accountability of transfer payment recipient agencies to the Ministry and for their governance is a complex undertaking. While a range of options for accomplishing this is available to the Ministry, there are no definitive criteria for establishing the most appropriate accountability and governance frameworks in particular circumstances.

We found that the Ministry deliberately does not involve itself in the day-to-day operations of its transfer payment recipient agencies (hereinafter called "transfer payment agencies"). Its

current approach to agency accountability and governance has evolved over time and attempts to balance the need for agencies to be accountable to the Ministry with the need of agencies to be reasonably autonomous and flexible in carrying out their day-to-day responsibilities. The Ministry has characterized this approach as "overall service system management" of agency service delivery.

Successful overall service system management by the Ministry requires an effective account-ability framework to provide assurance of prudent expenditure of public funds and compliance in carrying out program requirements. However, our review of ministry practices indicated that they are generally ineffective in ensuring transfer payment agency accountability for financial performance and service delivery. Based on our review of agency files and subsequent discus-sions with ministry staff, it was evident that there was considerable confusion and little consen-sus as to the roles and responsibilities inherent in the Ministry's stated intention of overall service system management of agency service delivery. For the transfer payment agencies we reviewed, the Ministry lacked sufficiently detailed financial and performance information on which to base informed service planning and funding decisions and, therefore, could not hold the agencies accountable for services provided or funds expended.

With the exception of the annual financial budgeting and settlement process, most of the Ministry's analysis and understanding of agencies' operations was not systematic but rather reactive to unusual circumstances which generally came to light as a result of specific com-plaints. In addition, the results of such analyses and subsequent directions to agencies were often not documented but rather communicated informally through personal contact with individual program supervisors.

The weak accountability relationship between the Ministry and its transfer payment agencies increases the importance of sound agency governance for ensuring agency compliance with ministry expectations. However, we found that the Ministry had not communicated to agencies clear expectations for board roles and responsibilities and their accountability to the Ministry and, therefore, could not readily assess whether agencies were being adequately governed.

In our view, the Ministry needs to significantly improve transfer payment agency accountability and encourage effective agency governance by adopting the principles identified in our detailed audit observations. For example, the Ministry ought to strengthen both the accountability framework between itself and its agencies and the governance of agencies by ensuring that it systematically:

• establishes measurable and meaningful expectations for service outcomes for each pro-gram that it funds. In those instances, where establishing measurable and meaningful service outcomes is not practical, the Ministry should define and communicate minimum or acceptable levels of care necessary to meet desired outcomes;

• periodically evaluates service outcomes or the quality of services provided;

• identifies the type of operating and financial information it requires to effectively monitor agency service delivery and financial performance. In particular, the Ministry needs to assess the reasonableness of funding in light of the outcomes or services actually received by clients to ensure that it obtains value for money spent;

- critically assesses agency service delivery costs to ensure funding is reasonable and equitable, preferably at the time of the funding decision or subsequently through its annual financial settlement process; and

- defines and communicates expectations for agency governance and requirements for acceptable operating policies and procedures to be followed by individual agencies.

DETAILED AUDIT OBSERVATIONS

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Many of the Ministry's transfer payment agencies owe their beginnings to dedicated groups of people who provided social services in their communities on a voluntary basis with little or no support from government. These services have expanded over time due to increased need and a general trend toward community-based care. As a result, many of today's social services continue to be delivered by community-based agencies with volunteer boards of directors that are independent of the Ministry, even though the Ministry now provides a substantial portion of their funding.

Given these service delivery and funding arrangements, the Ministry needs an effective means of holding agencies accountable for their expenditures of public funds. It also needs to ensure that the governing boards of agencies are appropriately constituted and adequately informed about both ministry expectations and the performance of their agencies.

In our *1995 Annual Report,* we described a seven-step accountability framework for holding governing bodies of transfer payment recipients accountable for the use of public funds, as described in the table below.

Accountability Framework for Transfer Payment Recipients

• The Legislature or the ministry sets objectives and assigns the responsibility for meeting them to a board of directors.
• Both parties agree on the specific results to be achieved, as well as how these results will be measured. This step requires a performance contract or memorandum of understanding.
• The Legislature or ministry gives the board of directors the authority necessary to carry out its responsibilities and to achieve the specific results; in other words, it empowers the board to do its job.
• The board of directors then decides on the most appropriate strategies for achieving the agreed upon objectives, as well as on the specific results and performance to be achieved by the organization. The chief executive officer (CEO) is informed of these aims and is empowered by the board to achieve them.
• The CEO reports periodically on results achieved and demonstrates that responsibilities have been carried out appropriately. This process is termed "accounting for results."
• After receiving assurance through an objective and independent evaluation, the board of directors reacts to and acts upon the results that the CEO has reported.
• Finally, coming full circle, the Legislature or ministry receives, in keeping with the reporting regime it has established, reports from the board of directors about the organization's performance.

Source: Office of the Provincial Auditor

In addition, the issue of what constitutes appropriate accountability and governance relationships has been the topic of a Management Board Directive as well as a number of studies and publications in recent years. Three of these in particular have significantly influenced our views in this area and, consequently, our assessment of the Ministry's existing accountability and governance framework for transfer payment agencies. They are listed below.

- *Management Board Directive 1-11 for Transfer Payment Accountability,* issued in January 1989.

  This Directive prescribes a four-step accountability framework with the following key requirements:

  - setting expectations with respect to the objectives and results that the transfer payment recipient is to achieve;

  - entering into an agreement which ensures that there is an understanding about the objectives and results to be achieved and the responsibilities for reporting performance;

  - timely reporting of objectives and results achieved; and

  - taking necessary corrective action on a timely basis.

  We understand that this Directive is currently being reviewed with a view to strengthening its requirements.

- *Effectiveness Reporting and Auditing in the Public Sector,* published by the Canadian Comprehensive Auditing Foundation in 1987 and followed up in 1994 by a video-documentation package entitled *In Search of Effective Governance.*

  These studies conclude that there are 12 attributes of effectiveness that, taken together, provide a comprehensive view of an organization's effectiveness or performance. They propose that management be responsible for providing information on these attributes to their governing bodies and that auditors lend credibility to these representations by attesting to their fairness.

- *Guidance on Control,* published by the Canadian Institute of Chartered Accountants in 1995.

  This publication sets out 20 criteria of control that, when in place, support people in the achievement of an organization's objective.

These documents generally concur in their recommendations for effective accountability and governance. Requirements include: establishing measurable performance targets and indicators; effectively monitoring results achieved against targets; and monitoring the relationship between results achieved and costs incurred.

We believe that the direction and guidance provided in the publications cited above need to be considered when implementing our recommendations, which we present under the headings of "agency accountability" and "agency governance."

AGENCY ACCOUNTABILITY

SERVICE OUTCOMES

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Service outcomes are the only reason for providing social services. Service outcomes are a direct result of the quantity and quality of services provided by individual transfer payment agencies. Consequently, establishing measurable and meaningful expectations for service outcomes is essential if the Ministry is to evaluate service effectiveness and appropriateness and to assess the reasonableness of costs incurred.

However, our review of the service schedules which form part of an agency's annual budget request and agreement with the Ministry indicated that they generally included only high level descriptions of service activities and provided basic statistical information such as the number of clients expected to be served. They did not provide measurable and meaningful service outcomes where these could have been established. Consequently, the Ministry often lacked the basis for assessing service effectiveness and the appropriateness of costs incurred.

The Ministry has recognized the need to develop a transfer payment agency accountability framework that identifies desired results and monitors and reports progress toward the achievement of those results. For example, in August 1991 the Ministry's Management Committee approved an accountability framework for all transfer payment agencies which was to:

- evaluate service results based on an expected client outcome approach;

- use the elements of the Management Board's Directive for Transfer Payment Accountability;

- ensure that service standards are linked to desired outcomes; and

- support the move to a service system management approach rather than bilateral agency/ ministry management.

Although we were advised at the time of our audit that the provisions of this framework had not been implemented, the Ministry plans to implement a similar accountability initiative for all social services over the next two years.

While measurable service outcomes are desirable, we are aware that there are some services for which it is not practical to establish measurable service outcomes which are readily apparent. For example, some service outcomes may be difficult to define, may not be determinable for some time or may be significantly influenced by factors beyond an agency's control. In such instances, there should be clear agreement between the Ministry and the agency involved as to what constitutes appropriate services and criteria for performance evaluation.

Our review of program files and discussions with appropriate staff revealed the absence of such agreements. Therefore, services provided could not be monitored or assessed, and the Ministry had no assurance that they were appropriate in the circumstances or that value for money had been received.

Recommendations

In order to help determine whether services provided by transfer payment agencies are effective, appropriate and represent value for money spent, the Ministry should, where practical, establish measurable and meaningful service outcomes. In cases where it is not practical to establish such service outcomes, the Ministry should establish appropriate service expectations and criteria for performance evaluation.

The Ministry should then periodically assess service outcomes or alternatively service quality and take corrective action where necessary.

Ministry Response

The Ministry agrees that it needs to establish measurable performance targets and indicators; effectively monitor the results achieved against the targets established; and monitor the relationship between the results achieved and the costs incurred.

The Ministry agrees that establishing service outcomes and developing the means to measure and monitor those outcomes is a complex undertaking. Because of this, the Ministry will be moving in stages.

The government has set clear expectations that all ministries will develop comprehensive performance measurement systems for their programs and activities, to support business planning and to enhance public accountability. As part of its 1997/98 business plan, the Ministry has developed performance measures for its accountability to the government and to the public. The Ministry will develop additional performance measures for all of its programs and activities.

AGENCY FUNDING REQUESTS AND APPROVALS

As part of the Ministry's annual financial planning and budgeting process, most agencies are required to submit a standardized budget request package to the Ministry by August 31 of the fiscal year to which it relates. The budget packages generally include a service schedule for each service for which funding is requested and other information such as the amount of funding requested, the number of employees associated with the service and salary levels by position.

The budget request is to be reviewed prior to funding approval, taking into consideration factors such as the previous year's expenditure review and other information available to the Ministry, including government directives.

Our review of the Ministry's funding review and approval process revealed a number of concerns which are illustrated by the following points.

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- In order to implement government-directed program constraints, the Ministry has since 1991/92 imposed across-the-board percentage changes to most agency base budgets without regard to prior years' surpluses or deficits or changes in demand for services. For example, for 1995/96 and 1996/97, the Ministry imposed across-the-board funding decreases averaging 3.5% and 2.5%, respectively, for most programs.

- In some cases the Ministry also approved additional contingency or other one-time funding requests. However, there was insufficient evidence in the files we reviewed to indicate that the need for and reasonableness of the amounts requested and approved had been assessed.

- There was also insufficient evidence in the files we reviewed that the Ministry related the amount of an agency's total funding approval to an assessment of the value of the underlying services to be provided. For example, the Ministry did not determine the cost-per-unit of service to permit the comparison of the costs for similar services or the identification of higher-cost services that could benefit from a more detailed review.

- Most budgets were not reviewed and approved until October or November, approximately seven months into the fiscal year.

The Ministry had recognized the need to relate funding requests and approvals to the underlying value of the services to be provided. For example, in the "1995 Child Welfare Contingency Funding Review Guidelines," the Ministry indicated that the impact of volume increases and other unusual circumstances on staffing, travel, client-related professional services and financial assistance costs should be analyzed to determine funding eligibility. For example, where changes in the mix of children result in higher care costs, documentation should clearly explain the reasons for the increase, such as that the children in care are on average older than previously and have increased levels of need resulting in higher placement costs or more hours of service per child.

In our view, the Ministry's overall agency funding review and approval process would be significantly improved if such detailed analyses were required to be performed periodically on each agency's total service costs.

Recommendation

In order to help ensure that service funding is equitable and appropriate for each agency, the Ministry should:

- **critically assess requests for funding and ensure that the amounts approved are commensurate with the demand for and value of the underlying services to be provided; and**
- **review and approve budget requests on a more timely basis.**

Ministry Response

The Ministry agrees that funding amounts approved should be commensurate with the demand for and value of the underlying services to be provided, and the Ministry will document any changes in demand for services when making annual funding decisions.

> *The Ministry is aware that there is a range of funding for individuals with similar needs and that there is a need to rationalize service costs. As part of its strategy to ensure an efficient use of resources, the Ministry will establish provincial benchmarks for residential care programs in the form of levels of support with corresponding funding ranges. Once provincial levels are established, the Ministry will put into effect funding levels for residential services. These limits will be phased in over a three-year period and will reflect the different needs of individuals and the different kinds of services that they receive.*
>
> *The Ministry agrees that budget requests should be reviewed and approved on a timely basis and is taking steps to speed up this process.*

ANNUAL PROGRAM EXPENDITURE RECONCILIATIONS

In most cases, agencies are required to submit an Annual Program Expenditure Reconciliation (APER) for each program funded, together with an audited agency financial statement no later than four months after the end of the fiscal year. The primary purpose of the APER is to reconcile a program's eligible expenditures with its approved budget in order to identify any surpluses.

An effective and timely APER process could compensate in part for some of the Ministry's deficiencies in reviewing and approving agency funding requests identified in the previous section of this report. However, we found that the APER process was not timely or effective in meeting its intended purpose for the reasons cited below.

- APERs compare an agency's total program expenditure to the approved budgeted amount and therefore cannot detect inappropriate or ineligible expenditure items. Reconciling actual to budgeted expenditures by individually detailed cost categories would, in our view, make this process more useful.

- The audited financial statements submitted by agencies with their APERs are usually prepared on a consolidated basis for all of an agency's programs and activities. APERs are to be prepared on a modified cash basis of accounting, but the financial statements are based on a full accrual accounting basis and, unlike APERs, often have a calendar rather than a fiscal year-end.

  As a result, in most cases the submitted financial statements cannot be reconciled with an individual program's reported expenditures or budget and consequently add no credibility to the reported total program expenditure amount.

- In a number of instances, APERs had not been reviewed or approved for prolonged periods of time. For example, we noted one case where an agency's APER had not been completed for the last five years.

We also found that when APER reviews indicated funding surpluses, area offices often did not recover them, but permitted some or all of these surpluses to be retained by the agency for other purposes or reallocated them to other agencies.

However, in our view, prudent financial practice would require all prior years' expenditure surpluses to be recovered and used to reduce the deficit.

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> **Recommendation**
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> **In order to improve the effectiveness of the Ministry's Annual Program Expenditure Reconciliation process and obtain useful information for the subsequent year's funding decisions, the Ministry should:**
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> - **ensure that both the Annual Program Expenditure Reconciliations and audited agency financial statements contain sufficiently detailed and comparable information to allow detection of ineligible or inappropriate expenditure items; and**
> - **review and appropriately act on all Annual Program Expenditure Reconciliation results on a more timely basis.**
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> *Ministry Response*
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> *The Ministry agrees that Annual Program Expenditure Reconciliations should show enough information to allow for detection of ineligible expenditure items.*
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> *The Ministry has taken steps to inform agencies and their auditors of the Ministry's financial policies. Specifically, the instruction package for Annual Program Expenditure Reconciliations, distributed annually to all agencies, contains all relevant policies, including an extensive list of eligible and ineligible expenditures. In the service contract signed by the agencies, it states that they "will comply with Ontario's policies on the treatment of revenues and expenditures." This requires agencies to properly reflect expenditures and surpluses in their financial statements. In order to assist in informing agency auditors of the implications of these particular policies, the Ministry wrote an article for publication by the Institute of Chartered Accountants of Ontario. The article was distributed to all its members.*
>
> *In addition, the Ministry continues to take steps to review and appropriately act on all Annual Program Expenditure Reconciliation results. The Ministry has introduced mechanisms to help ensure adherence to its Annual Program Expenditure Reconciliation policies. The Ministry will continue to promote and facilitate increased awareness of these policies for use by agencies and their auditors.*

OTHER ACCOUNTABILITY REQUIREMENTS

A recent joint publication by the Canadian Institute of Chartered Accountants and the Canadian Comprehensive Auditing Foundation stated that governing bodies are in effective control when they know what information they need, ensure that they receive it and then take appropriate action based on that information. Accordingly, as a starting point for an effective accountability framework, the Ministry must have a clear understanding of its role in the accountability process and must identify, in specific terms, what information it needs to make informed judgments.

Our review of agency files and subsequent discussions with ministry staff showed that some staff saw their roles as little more than providing funding to agencies, while others indicated that they assumed a much more pro-active and involved service planning and monitoring function. As a result, we found little agreement as to what information ministry staff would need or what analyses and decisions they would have to make to be effective service managers.

Our review of both the financial and service-related information in the Ministry's files indicated that it was inadequate to support the Ministry in assuming an effective service management role, as the points below indicate.

- By not assessing an agency's budget or expenditures in relation to the level and quality of services actually provided, the Ministry can neither measure the agency's performance against its own standards for service delivery nor meaningfully compare the cost of one agency's services against those of other agencies providing the same or similar services.

  This concern is compounded by the fact that expenditure reports received from agencies, including APERs, lack the detail necessary to assess the reasonableness of underlying costs or their appropriateness or eligibility for the services to which they are charged. For example, the Ministry often cannot distinguish between expenditures incurred for direct service delivery from those incurred for administrative purposes.

- In many instances, reported expenditures included allocations for shared or other agency overhead costs, even though there was no evidence that the reasonableness of these allocations had been assessed.

- Service-related information on file normally consisted of general service descriptions which lacked sufficient detail to allow assessment of the reasonableness of services actually delivered, results achieved or costs incurred.

  We noted that for some types of services, the Ministry did receive more detailed statistical data, such as the number of service recipients for each type of service provided. However, where this information was found on file, there was no evidence that it had been reviewed or what actions, if any, had been taken as a result.

- The files we reviewed contained insufficient evidence that the Ministry had assessed the efficiency with which agencies delivered services. For example, the Ministry did not obtain or review operating statistics such as the percentage of time spent by caseworkers in direct service delivery.

- The Ministry generally did not verify any of the financial or service-related information submitted by agencies, even in cases where significant year-to-year fluctuations occurred.

Recommendation

In order to help ensure that it effectively establishes and manages services delivered by transfer payment agencies, the Ministry should:

- **define its service management roles and responsibilities in a way that allows it to effectively establish and monitor service delivery; and**

- **obtain and analyze the information necessary for effective service management.**

> **Ministry Response**
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> **The Ministry agrees that it has an obligation to ensure that the parties with whom it contracts for services have a clear understanding of and agree to the roles and responsibilities of all the parties in the accountability relationship.**
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> **As well, the Ministry believes that timely information should be reported to demonstrate the performance achieved and what has been learned. Steps have been taken to ensure that the Ministry's reporting requirements and information systems are meeting its management needs.**
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> **In addition, as the Ministry's performance measures are defined they will be built into the service-contracting process.**

3.04

AGENCY GOVERNANCE

The Ministry relies on boards of directors to ensure that their administration and the agencies' service delivery are in compliance with the Ministry's requirements. Consequently, the Ministry's role is to ensure that boards of directors develop policies and procedures to meet the Ministry's requirements. The requirements for significant improvements in the Ministry's accountability relationship with transfer payment agencies identified earlier in this section increase the Ministry's reliance on boards of directors to carry out these responsibilities.

However, for such reliance to be warranted, the Ministry needs to define and promulgate the roles and responsibilities of agency boards of directors in the overall service system management process and their accountability to the Ministry to ensure service delivery is in compliance with the Ministry's requirements.

We found that the conditions under which such reliance would be warranted have yet to be established. For example, there is a requirement for the Ministry to define and ensure its expectations are met for:

*   agencies' governance and reporting structures; and
*   board-developed operating policies and procedures designed to ensure that program service delivery is achieved economically, efficiently and effectively.

In our view, establishing such expectations is particularly important at this time given the increasing complexity of operating social service agencies and the voluntary nature of their boards.

We also noted that provincial associations for some types of agencies have developed accreditation processes to assess, among other things, an agency's governance framework and operating policies and procedures. Although many of these accreditation processes are in their early stages, they are beginning to be performed for some agencies. If the Ministry wants to rely on these accreditations, it needs to satisfy itself as to the adequacy of the accreditations and the manner in which they are carried out.

Recommendation

In order to enhance the reliance the Ministry is able to place on transfer payment agencies' governance and service delivery, the Ministry should:

- **establish its expectations for the roles and responsibilities of boards of directors in the overall service systems management process and their accountability to the Ministry; and**
- **provide guidance on operating policies and procedures necessary for meeting the Ministry's program objectives economically, efficiently and effectively.**

Ministry Response

The Ministry agrees that its obligation is to define and contract for the expected results (outcomes) with the boards of directors, monitor and measure the attainment of the results, and evaluate the performance in relation to the contract.

The Ministry, together with the boards, will better define their respective roles and responsibilities so that both parties clearly understand their obligations and carry out their responsibilities accordingly.