

Indigenous Relations—Follow-up Audit on Systems to Assess First Nations Development Fund Grants

INTRODUCTION

The First Nations Development Fund is a lottery grant program available exclusively to First Nations in Alberta. It is supported by a portion of revenues from government-owned slot machines in Alberta First Nation casinos. From 2006 to 2016, the Department of Indigenous Relations allocated over \$980 million in FNDF grants to support hundreds of social, economic and community development projects in Alberta's First Nation communities. A detailed breakdown is provided in Appendix A.

In 2013, we found inadequacies in three aspects of the FNDF program: communication of eligibility requirements, assessment of applications, and monitoring of recipients' compliance with grant agreements.¹ We recommended that the department improve its:

- communication of eligible uses of FNDF grant funds
- processes to review and approve grant applications by:
 - formalizing its processes to review complex² grant applications
 - obtaining sufficient information to support its assessment of grant applications
- processes for monitoring compliance with reporting requirements and its actions to correct non-compliance with grant agreements

The department has acknowledged that there are areas of misalignment between the requirements of the grant agreement and its current processes to assess FNDF grant applications and monitor compliance with the agreement. Over the 10 years since the agreements between First Nations and the department were signed, both the program and the department's relationships with First Nations participating in the program have evolved. The department has indicated it has attempted to respond to this evolution by providing greater autonomy to First Nations in managing FNDF funding allocations.

In our follow-up audit we assessed FNDF's processes against the requirements of the current grant agreement.

AUDIT OBJECTIVE AND SCOPE

Our objective was to determine whether the Department of Indigenous Relations has made the necessary improvements to fully implement our recommendations.

We examined grant applications made for projects at the River Cree Resort and Casino because the original audit dealt primarily with one large complex application for River Cree, and we wanted to provide continuity in our testing. However, we also tested other complex grant applications to provide a thorough assessment of the state of the department's processes for assessing all complex applications.

¹ *Report of the Auditor General of Alberta—July 2013*, pages 17–28.

² The department defines a complex grant application as one that proposes projects having the potential to include gaming-related activity, such as developments near existing casinos, or having principal and/or interest payments over \$1 million.

We conducted our field work from October 2015 to October 2016. We substantially completed our audit on December 5, 2016.

WHY THIS IS IMPORTANT TO ALBERTANS

The FNDF is an opportunity to support good social, economic and community-based projects. It's important for Albertans to know that the program is operating as intended and funded projects provide value to First Nation communities.

WHAT WE EXAMINED

To perform the follow-up audit, we:

- interviewed management and staff to learn what actions they took to make the needed improvements to implement our recommendations
- examined the department's policies, processes and systems for its FNDF grant program
- tested the department's processes to communicate eligible uses of FNDF funds; to review and approve complex grant applications; and to monitor compliance with the grant agreement and actions taken to correct instances of non-compliance

CONCLUSION

We conclude that management has implemented one of our three recommendations: the department has improved its systems to communicate its interpretations of eligible uses of FNDF grant funds.

We have repeated two recommendations because the department is still unable to:

- demonstrate it has made sufficient improvements to its processes to assess and approve complex grant applications
- monitor for and correct non-compliance with the grant agreement

FINDINGS AND RECOMMENDATIONS

Improve review processes—recommendation repeated

CONTEXT

In 2013,³ we found that the department had added processes to assess one complex application that had been submitted by Enoch Cree Nation in support of the River Cree Resort and Casino. We recommended that the department formalize those processes so that future complex grant applications would be subject to similarly rigorous review processes.

We also found that the department had approved some grant applications without doing sufficient analysis. For example, the department approved \$18 million for capital improvements as part of the River Cree application, without information regarding the estimated costs or timing of the planned improvements. Without this information it would be difficult to assess if the capital improvements were properly described, reasonable and eligible for FNDF funding. We recommended that the department consistently obtain sufficient information to support its assessment of grant applications.

CRITERIA: THE STANDARDS OF PERFORMANCE AND CONTROL

The department should have systems and processes to review and approve grant applications.

³ Report of the Auditor General of Alberta—July 2013, no. 2, page 24.

OUR AUDIT FINDINGS

KEY FINDINGS

- The department formalized its processes to assess complex applications, but those processes do not give sufficient guidance on the use of professional advice for complex applications, and the department has not consistently sought this advice.
- The department approved some projects without having sufficient information to support its assessment against required criteria such as the reasonableness of project costs.

Use of professional advice to assess complex applications

The department formalized its processes to assess complex grant applications in its procedure manual by defining criteria to differentiate complex from regular applications. The department defines complex applications as those that propose projects having:

- the potential to include gaming-related activity, such as developments near existing casinos
- principal and/or interest payments over \$1 million

Further, the formalized processes now require the department to obtain professional advice for complex applications. The professional advice obtained may be internal or external legal, accounting, financial or other professional advice depending on the nature and complexity of the application.

However, the procedure manual does not give sufficient guidance on the use of professional advice. It does not clarify how department staff should determine what type of advice to use, the extent of advice required or the extent to which the department may rely on the professional advice applicants have provided in support of their applications.

Because the guidance is insufficient, the department has not consistently sought professional advice when assessing complex applications. Of the complex applications we tested, the department sought professional advice on only two, and in one of those cases the advice came from the department's internal auditor. Reliance on the internal auditor's advice to assess applications may pose a risk to the auditor's independence, as the audit process includes assessing project applications for appropriate approval and the use of grant funds to complete the projects.

The department has recently developed further guidance for assessing complex applications. It has documented this guidance in its Complex Application Assessment Process, which it intends to incorporate into its procedure manual. The new process gives greater flexibility in identifying an application as "complex" and outlines a six-step process that will be followed and documented in application files. However, we were unable to test this new process, as the department had not approved any new complex applications since developing it.

Information to support project approvals

The department received and assessed a range of complex grant applications from First Nations, including capital expenditures for large construction projects, additional funding for previously approved capital projects, and projects to finance prior operating deficits. The department has processes to assess each application, and in the applications we tested we found that the department had obtained information to ensure the application was complete and the project properly described.

However, the department has not consistently obtained sufficient information to support its assessment of grant applications. Specifically:

- The grant agreement indicates that the department's review and approval processes include ensuring that rationale is provided for costs in excess of costs of a similar project. But the department's assessment does not consider the reasonability of project costs. Projects were approved with widely varying finance costs and construction costs with no indication of whether those costs were reasonable within the circumstances of each project.
- In the case of one significant application made to support a financing project, the department did not take project revenues into consideration when assessing the funding request, even though the project was a for-profit business. There was no documentation to explain the department's rationale for not including these revenues.
- Since our original audit, the department has received additional grant applications connected with the River Cree Resort. In each case, the department's assessment and approval did not consider the entity's ability to support the increasing financing costs.

RECOMMENDATION 6: IMPROVE REVIEW PROCESSES—REPEATED

We again recommend that the Department of Indigenous Relations improve its processes to review and approve grant applications by:

- formalizing the additional review processes it developed for complex grant applications
- consistently obtaining sufficient information to support its assessment of complex grant applications

CONSEQUENCES OF NOT TAKING ACTION

Without sufficient analysis to support its granting decisions, the department cannot demonstrate how it approves applications according to the requirements of the FNDF program. As a result, it may award grants for funding uses that are inconsistent with the objective of the grant program.

Monitor for and correct non-compliance—recommendation repeated

CONTEXT

In 2013⁴ we recommended that the department improve its processes to monitor First Nations for compliance with the reporting requirements of the grant agreement. The grant agreement requires all funding recipients to submit an approved financial report annually on June 30. Further, final reporting on a project is due within 90 days of completion.⁵ Each recipient must report:

- revenues from all sources, including interest income
- costs and any donated labour, services, material and equipment received
- explanations of significant variance or delays

We found the department did not consistently monitor First Nations to ensure they complied with reporting requirements. First Nations had not submitted project reports in a timely manner, yet the department had not taken corrective action on late reporting. First Nations continued to receive funding despite being non-compliant.

The grant agreement requires the department to review the eligibility of expenses and compare actual expenses to the approved application. For submitted reports, we found that the department had not documented its analyses to compare actual to budget project costs or obtain explanations for variances.

⁴ *Report of the Auditor General of Alberta—July 2013*, no. 3, page 26.

⁵ Grant agreement, Section 5.2 Reporting.

CRITERIA: THE STANDARDS OF PERFORMANCE AND CONTROL

The department should monitor and audit approved grant applications to ensure recipients comply with agreements.

OUR AUDIT FINDINGS

KEY FINDING

The department does not consistently follow its processes to:

- advise First Nations of overdue reporting
- enforce compliance with reporting requirements by withholding payments
- follow up on audit findings of non-compliance
- regularly visit each First Nation to discuss matters concerning FNDF and to observe the status of projects

Reporting

We examined a sample of open and closed projects to determine whether annual reporting was received on time. We found that First Nations continue to submit project reports late. Of the reports we examined, most were submitted late—on average approximately five months after the due date. Our findings are summarized below.

FNDF Project Reporting

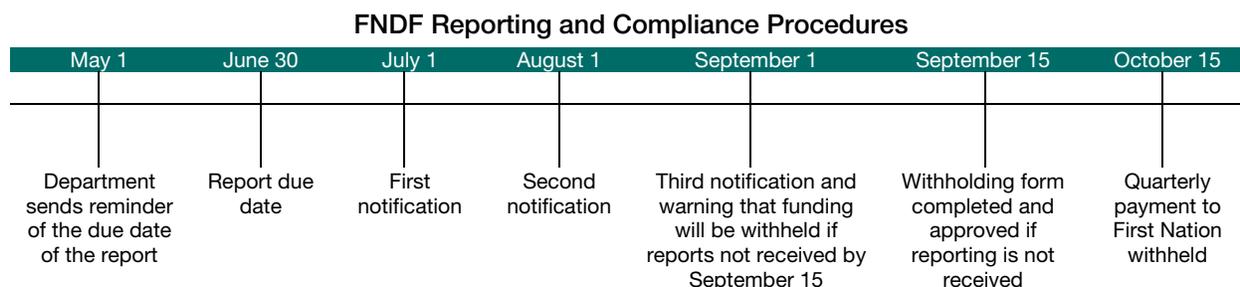


We found that, when reports were submitted, the department’s liaison officers asked for explanations and documented their analysis when reporting indicated variances between actual and budget project costs. This process was improved from our original audit.

Enforcing compliance with reporting requirements

The department formalized a process to withhold payments from First Nations who do not comply with reporting requirements. It developed an Overdue Reporting Notification Procedure, which is included in its procedure manual. The procedure requires the department to provide several notifications to First Nations regarding reporting requirements, and to initiate a process to withhold payments if reporting is not received after three notifications.

These processes are summarized below:



The department has not consistently followed this process to enforce compliance. Notifications were not consistently sent on the schedule noted above. Some liaison officers advised us that they discuss late reporting with First Nations verbally, while others communicated by email. Of the written notifications we observed, fewer than half communicated the consequences for late reporting.

The department put three of 32 projects on payment hold because of late reporting. Although no payments were made to these projects during the duration of the hold, payments continued to be made to other projects for the recipients. The department’s procedures indicate that all projects for the recipient should be placed on a payment hold, but liaison officers explained that they do not place all projects on hold because they consider this consequence too severe.

The department has recently increased its efforts to follow up on non-compliant reporting and has reduced the number of overdue reports. In June 2016 the department sent a letter to 12 First Nations to highlight their reporting obligations under the grant agreement. The letter provided a 60-day notice of suspension of further FNDF funds if reporting was not brought up to date.

The department is also considering changing its deadline for First Nations’ annual reporting from June 30 to August 31. The current deadline is a month earlier than the federal government’s deadline (July 29) for First Nations’ audited consolidated financial statements.⁶ The department feels it can better meet the needs of First Nations by moving its deadline, which is arbitrary, after the federal government’s set deadline.

Follow-up on audit findings

The department’s internal audit group audits each First Nation to ensure compliance with grant agreements and to confirm that grant funds were used for approved purposes. Two common findings arising from audits are a lack of compliance with the requirement to use a dedicated bank account to receive and expend FNDF funding, and a lack of compliance with reporting requirements.

Over the years there has been a lack of clarity between the liaison officers and the internal audit group around responsibility for following up on non-compliance. Recent efforts have been made to improve communication between the two groups to clarify the roles and responsibilities of each.

Site visits to First Nations

⁶ The *First Nations Financial Transparency Act*, s.C. 2013, c.7, assented to 2013-03-27, is federal legislation that requires First Nations to present their audited consolidated financial statements within 120 days of their financial year-end (March 31), which is July 29 annually.

The department has identified site visits as an important means to maintain good relations with funding recipients, observe project status and follow up on outstanding project reporting or other matters. In addition to site visits, liaison officers provide ongoing support and may meet with First Nations off-site as well. Each liaison officer is allocated a portfolio of First Nations and is expected to visit each community at least twice each fiscal year.

We analyzed data on site visits made by liaison officers over the last three fiscal years. Some First Nations had no site visit during a year, while others had only one visit. Two First Nations communities were not visited at all during the three years. One of these First Nations has not provided its project reporting for the past five fiscal years. The department has subsequently visited both of these communities.

The table below summarizes our analysis.

Fiscal year	No visits	One visit	Two or more visits
2013–2014	9	12	25
2014–2015	20	15	11
2015–2016	11	16	19

Source: Information obtained from the department as at April 20, 2016

RECOMMENDATION 7: IMPROVE MONITORING PROCESSES—REPEATED

We again recommend that the Department of Indigenous Relations improve its monitoring processes by consistently ensuring First Nations comply with reporting requirements and acting to correct non-compliance with a grant agreement.

CONSEQUENCES OF NOT TAKING ACTION

Without ongoing monitoring to ensure grant recipients comply with grant agreements, the department may not be able to determine whether funds are used for the intended purposes and projects are managed effectively.

Formalize and communicate interpretation of eligible uses—recommendation implemented

CONTEXT

In 2013⁷ we recommended that the department formalize and communicate its interpretation of eligible uses of funding. The FNDF grant agreement defines three categories of eligible uses: economic, social, and community development projects.⁸ We found that the department had to exercise discretion to interpret whether project applications were eligible under these purposes, because the categories were too broad. Insufficient guidance was provided to applicants to clarify project eligibility.

OUR AUDIT FINDINGS

The department has formalized and communicated its interpretation of eligible uses of funds internally to its staff and externally to FNDF applicants by improving its internal and external processes.

Internal processes

In 2013 the department developed the FNDF Grant Program Procedure Manual to communicate to its staff its interpretation of eligible uses of FNDF grant funds. The manual describes project eligibility and reporting guidelines and describes acceptable projects that fall under the three broad categories.

For example:

- projects that fall under economic development include capital investments in buildings, infrastructure, heavy equipment and vehicles
- operations of a profitable business are normally not eligible under economic use; however, certain costs—business feasibility studies and research, business start-up costs, business expansions, and initial and short-term seed funding for operations—would be considered eligible, as they are consistent with community development and growth
- eligible uses under the social development category include child and youth services such as daycare operating costs, as well as recreation, education, addictions, health and justice programs
- community development includes First Nations' administration and operating costs and community events

The department also developed a presentation it uses when training new staff and as a tool for its staff to communicate the requirements to potential grant applicants.

External processes

Liaison officers regularly communicate with First Nations to assist with any questions the First Nations may have in developing project applications. This communication takes place before a First Nation submits its project application to the department. First Nations are therefore made aware of the department's interpretation of eligible uses.

The department holds an annual workshop with First Nations to provide guidance on the technical, administrative and delivery aspects of the FNDF program. The workshops provide the department and First Nations with an opportunity to discuss eligibility of funds and other program-related concerns. We reviewed material from the 2014 and 2015 annual workshops and confirmed that the interpretation of eligible uses was discussed.

⁷ *Report of the Auditor General of Alberta—July 2013*, no. 1, page 23.

⁸ Grant agreement, Section 2.1 Eligible Uses.

APPENDIX A: FIRST NATIONS DEVELOPMENT FUND PAID AMOUNTS

First Nations Development Fund Paid Amounts (in millions)

Treaty*	Fiscal 2006- 2007	Fiscal 2007- 2008	Fiscal 2008- 2009	Fiscal 2009- 2010	Fiscal 2010- 2011	Fiscal 2011- 2012	Fiscal 2012- 2013	Fiscal 2013- 2014	Fiscal 2014- 2015	Fiscal 2015- 2016	Total **
Treaty 6	\$11.8	\$38.8	\$54.5	\$56.0	\$55.7	\$63.0	\$66.7	\$68.7	\$69.9	\$68.5	\$553.7
Treaty 7	\$0.5	\$10.9	\$35.2	\$36.4	\$34.8	\$36.3	\$38.1	\$37.6	\$41.6	\$40.4	\$311.9
Treaty 8	\$1.3	\$6.7	\$11.8	\$12.4	\$12.3	\$13.5	\$14.2	\$14.9	\$15.8	\$15.4	\$118.3
Total **	\$13.6	\$56.4	\$101.5	\$104.8	\$102.8	\$112.8	\$119.0	\$121.2	\$127.3	\$124.3	\$983.8

* Appendix B lists the participating First Nations in Treaties 6, 7 and 8

** Differences are due to rounding

APPENDIX B: FIRST NATIONS COMMUNITIES IN ALBERTA

Participating First Nations Communities in Alberta

Treaty ⁹	Member First Nations
Treaty 6	Alexander, Alexis, Beaver Lake, Cold Lake, Enoch Cree, Ermineskin, Frog Lake, Heart Lake, Kehewin, Louis Bull, Montana, O’Chiese, Paul, Saddle Lake, Samson Cree, Sunchild, Whitefish (Goodfish)
Treaty 7	Blood, Stoney (Chiniki, Wesley, Bearspaw), Piikani, Siksika, Tsuut’ina
Treaty 8	Athabasca Chipewyan, Beaver, Bigstone Cree, Chipewyan Prairie, Dene Tha’, Driftpile, Duncan’s, Fort MacKay, Fort McMurray #468, Horse Lake, Kapawen’o, Little Red River, Loon River, Lubicon Lake, Mikisew Cree, Peerless Trout, Sawridge, Smith’s Landing, Sturgeon Lake, Sucker Creek, Swan River, Tallcree, Whitefish Lake, Woodland Cree

⁹ Alberta First Nations are members of three treaty organizations: Confederacy of Treaty 6 First Nations, Treaty 7 Management Corporation, and Treaty 8 First Nations of Alberta.

