
Report on W. J. Stelmaschuk and Associates Ltd.

Ministry of Children and Family Development

Distribution

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**Internal Audit & Advisory Services
Office of the Comptroller General
Ministry of Finance**

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Glossary

BCHMC	British Columbia Housing Management Commission
FTE	Full-Time Equivalent
the ministry	The Ministry for Children and Family Development
PMG	Provincial Monitoring Group
Stelmaschuk or WJS	W.J. Stelmaschuk and Associates Ltd.

Executive Summary

We have completed our audit of W.J. Stelmaschuk and Associates Ltd. (Stelmaschuk or WJS). The Ministry for Children and Family Development (the ministry) contracts with Stelmaschuk to provide services in the areas of family support, training and support, youth justice, children and care, and residential services. The purpose of the audit was to review Stelmaschuk's contracts and its financial and operating records to determine the reliability of its reporting and compliance with the terms of its contracts with the ministry.

As a result of our examination we conclude that:

- The services which are clearly defined in measurable terms in the contracts were provided, in all significant respects, to the ministry. However, the contracts specify a number of service deliverables that are not defined in measurable terms, so we could not conclude on their delivery to the ministry.
- Based on our review of Stelmaschuk's organizational structure and payroll system, staffing levels were consistent with the levels specified in the contracts.
- Stelmaschuk has well functioning financial control and monitoring systems throughout its organization, and the financial reporting was accurate, complete and timely.
- Funding was applied appropriately and for the purpose intended in the contracts. Stelmaschuk has appropriate controls and procedures in place for the recording and allocation of contract revenue and program expenses to the applicable programs.
- Revenue and expenditures were properly and consistently allocated to the programs. Although within the contract reform guidelines of 10%, we found that administrative expenditures were not applied consistently between programs.
- Based on our review of general expenditures and payroll we did not find any material unearned revenue.
- The surplus recorded by Stelmaschuk in 2001 was not material and was reasonable.

Overall, we found that Stelmaschuk had a strong organizational infrastructure to support the delivery of its contracted programs for the ministry. Our primary recommendation is for Stelmaschuk to review its administrative cost allocation procedures to ensure there is a consistent basis for the application of these charges. We also have recommendations for the ministry to improve the clarity of its contract deliverables and requirements.

We would like to thank the management and staff at Stelmaschuk and the ministry for their assistance and co-operation during this audit.

David J. Fairbotham
Executive Director
Internal Audit & Advisory Services

October 7, 2002

Introduction

The Ministry for Children and Family Development (the ministry) contracts with W.J. Stelmaschuk and Associates Ltd. (Stelmaschuk) to provide services in the areas of family support, training and support, youth justice, children-in-care, and residential services.

Stelmaschuk is a diversified Canadian company based in Maple Ridge. The British Columbia government provides approximately \$6 million in annual funding to the company through the Ministry for Children and Family Development and the Ministry of Attorney General.

Internal Audit & Advisory Services routinely performs audits of agencies, which hold contracts with the ministry. Selection for audit is based on the significant level of funding and past concerns with service delivery.

Purpose

The purpose of the audit was to review Stelmaschuk's contracts and its financial and operating records to determine the reliability of its reporting and compliance with the terms of its contracts with the ministry.

Audit Scope and Objectives

The scope of the audit included an examination of Stelmaschuk's financial and program management systems, controls and records to determine whether:

- those services which are clearly defined in measurable terms in the contracts had been fully provided;
- staffing levels were appropriate based on criteria agreed on between Stelmaschuk and the ministry;
- financial reporting was complete, accurate and timely;
- budgeting and monitoring procedures were appropriate;

- ministry funding was applied towards reasonable program expenditures that related to the purposes of the contracts;
- revenue and expenses were appropriately allocated between programs; and
- unearned revenue was defined in the contracts and refunded to the ministry where appropriate.

Audit Approach

The audit primarily involved interviews with Stelmaschuk management and the review of contracts, financial and operating records, reports and related documents. The Vancouver/Richmond and Okanagan regions were selected for review based on the value and variety of contracts held in those regions.

During the course of this audit, it was determined that some contracts did not provide for measurable deliverables or outputs, and that the underlying information did not support straightforward verification of the achievement of measurable deliverables.

Accordingly, in addition to reviewing the financial reports and financial information, we modified our approach to review the agency's infrastructure to determine whether it supported the achievement of the services outlined in the contracts. In addition to interviews with ministry staff, the review included an assessment of Stelmaschuk's:

- management systems and procedures;
- service delivery and quality standards;
- internal and external reporting and monitoring procedures;
- training and recruitment procedures; and
- staff management and control procedures.

Comments and Recommendations

1.0 Provision of Contracted Services

Objective

To determine whether those services which are clearly defined in measurable terms in the contracts had been fully provided.

Conclusion

We found those services which are clearly defined in measurable terms in the contracts were provided, in all significant respects, to the ministry. However, the contracts specify a number of service deliverables, which are not defined in measurable terms so we could not conclude on their delivery. In addition, our assessment is that Stelmaschuk currently has the infrastructure and capacity for effective service delivery.

1.1 Contract Criteria

We reviewed the contract service deliverables for the Okanagan and Vancouver/Richmond regions to evaluate the clarity of the deliverables, and whether they could be evaluated in this audit.

We found that:

1. The Okanagan region contracts were clearer in terms of contract service deliverables and required resources. For example, most of the Okanagan contracts are specific about the hours of operation for a program or the number of FTE's or service hours the contractor is required to deliver.
2. The Vancouver/Richmond region has listed service deliverables, however they are less clearly defined. For example, while the number of beds, bed days and clients are defined, the staffing requirements to deliver the related services are either described as "sufficient" or not defined.

Stelmaschuk has worked with the Okanagan and South Fraser regions to standardize output criteria in order to provide consistency in service delivery. We suggest that the Vancouver/Richmond region review these criteria to evaluate their applicability. In particular, we have found that incorporation of "service hours" provides a more easily understood performance measure than FTE. FTE is subject to different interpretations particularly when both full and part time services are required by the contract. Where feasible, measurable and clearly defined service deliverables should be incorporated in the Vancouver/Richmond contracts to ensure greater consistency and clarity for communications, reporting, staffing and service delivery expectations.

Recommendations

(1) We recommend that the Vancouver/Richmond Region:

- **adopt a contract structure similar to that used in the Okanagan or the South Fraser Regions; and**
 - **consider adopting a service hour model for its contracts, similar to the Okanagan Region.**
-

Vancouver/Richmond Region's Response:

The Vancouver/Richmond region will incorporate these recommendations and adopt a service hour model upon renewal of contracts.

1.2 Organizational Infrastructure

The following is a summary of our observations on the key elements of organizational infrastructure at Stelmaschuk, which provide assurance that contracted services and deliverables are being met.

Standards

As is the case with other ministry-funded agencies, Stelmaschuk delivers its services to meet a number of external service delivery standards. Examples include standards for Staffed Children's Residential Services, and for the *Community Care Facilities Licensing Act*.

Currently, Stelmaschuk is reviewing its program management and service delivery in order to meet the standards required for accreditation, with the objective of all its programs becoming accredited in 2002.

Control systems and procedures

Stelmaschuk has a documented management control system and has integrated policies and procedures. These control systems and procedures include:

- Policy and procedures manuals at three levels in the organization: the Policies and Guidelines-Personnel and Administration at a corporate level; Community Based Program Manager's Handbook for programs and program managers; and the New Employee Orientation Manual for employees. These manuals provide the comprehensive procedures and guidelines required for management and staff. These policies and procedures are being reviewed and updated to meet the needs of accreditation.
- Stelmaschuk management and administrative staff regularly review practices for compliance with these policies and procedures and external program standards. The reviews provide recommendations for improvement and require responses from the program managers for follow-up.

Reporting and monitoring

A number of external agencies also provide monitoring and compliance reports with regard to Stelmaschuk's programs and facilities and include:

- the Provincial Monitoring Group (PMG) who assess quality of service delivery for residential care and self-help for adults with development disabilities.
- Ministry of Health and Ministry Responsible for Seniors (Community Care Facility Act) for granting Interim or Final "Licensed Care Facility Permits"; and
- Vancouver Regional Health Board Facilities Licensing Inspection section.

For the most part, the recommendations in these reports were minor, and Stelmaschuk implemented them as quickly as was feasible and reasonable.

Staff in the programs provide a variety of internal reports to monitor their service delivery. These were reviewed to determine compliance with contract and regulatory requirements as well as internal procedural requirements. Copies of these reports are provided to the Ministry as a condition of the contract or on an "as requested" basis.

Training and recruitment

Stelmaschuk's policies, procedures and personnel files were reviewed with regard to recruitment, selection, orientation and training:

- recruitment is based on defined core competencies;
- new employees are put through an orientation process;
- ongoing training is provided; and
- performance is reviewed on an ongoing basis.

Surveys

The Division Manager undertakes satisfaction surveys with individual recipients and with families. These surveys are used to ensure that:

- Clients understand the extent of services that can be provided by Stelmaschuk; and
- Issues raised by the client or their family are addressed in a responsive manner.

The survey results were found to be positive regarding the services that had been provided.

2.0 Staffing Levels

Objective

To determine whether staffing levels were appropriate based on criteria agreed on between Stelmaschuk and the ministry.

Conclusion

Based on our review of Stelmaschuk's organizational structure and payroll system, we conclude that staffing levels are consistent with the levels specified in the contracts.

Organizational structure and backfill procedures

We reviewed Stelmaschuk's corporate and program organization structures, management policies and procedures and interviewed staff at the Head Office, BC Programs Office and Program sites. We found that:

- Temporary vacancies, whether a result of a resignation or short-term requirement, are managed by moving existing staff up into the vacant position, and filling-in through relief staff in order to provide sufficient staff coverage at all times.
- If these vacancies are a result of a resignation, Stelmaschuk will fill the permanent position with qualified internal staff, or if required, through an external competition process.

Bi-weekly staff schedules, timesheets and reports

Timesheets, leave records, payroll system and reports, general ledger, and master scheduling of staff were reviewed at the Head Office and at the program site. We found that staff scheduling, timesheet/leave management and payroll procedures are well documented and followed.

- Bi-weekly time sheets and leave forms are completed and approved in accordance with the staff schedule by the Program Manager before transmittal to the Stelmaschuk Head Office payroll section.
- The Payroll Supervisor at Stelmaschuk Head Office has control procedures in place to pre-audit timesheets prior to entry into the payroll system.
- Reconciliation and approval procedures are in place to ensure that pay and benefits are accurately attributed to the programs, and are accurately recorded in the general ledger.

3.0 Financial Management and Reporting

Objective
To determine whether financial reporting was complete, accurate and timely; and budgeting and monitoring procedures were appropriate.

Conclusion

We found that Stelmaschuk has well functioning financial control and monitoring systems throughout its organization, and that the financial reporting was accurate, complete and timely.

We found that both Stelmaschuk and the regions have misinterpreted the financial reporting requirements contained in Client Service Agreements and government policy. As a result, Financial Reporting requirements for an annual financial statement audit have not been met.

Financial
organizational
structure

Stelmaschuk's control system is documented and defines key responsibilities, duties and authorities of its managers, administrative and operational staff. In our review of operating procedures and through interviews with staff, we determined that there is a clear segregation of duties and approvals between the accountant, accounts payable and receivable staff, contract administrator, payroll, and the program staff.

Budget
development and
expenditure
monitoring

We reviewed the manner in which budget information is collected and updated. We found that the organization has a reliable process in place for the preparation, approval and monitoring of annual program budgets. These processes include:

- Monthly Statement of Income and Expenditure reports produced for each program. This report includes: transactions for the current month, budget comparisons for the month, actual year-to-date to budget, and variances of monthly actual to budget.
- Monthly review and monitoring of budgets by Program Managers, Division Managers and Head Office staff.

Modifications to the budget and approvals for extra one-to-one care are discussed with the ministry and approved by way of a modification agreement.

Appropriateness
of financial
systems and
controls

Interviews were carried out with the Accounting staff and various financial records were sampled. We found that the financial management and control procedures were followed and well documented.

Disclosure of
related party
transactions

We reviewed the externally prepared financial statements for each program and a financial statement note is prepared for related party transactions regarding the programs' premises rents or leases. As discussed further below, transactions between related companies were at fair market value. However, we found that related party transactions with DM Leasing, for office equipment, computers and vehicles, are not disclosed in the notes to the financial statements.

External
reporting

Government policy and a sample of Client Service Agreements were reviewed for financial reporting requirements. General Management Operating Procedures 6.4.12 and Section 9.01(d) of the Client Service Agreements set criteria for financial reporting and the need for financial review or audit. If a contractor's total revenue received from the province within a fiscal year is \$100,000 through \$499,999 the contractor is required to submit an annual review of its financial statements. If the contractor's total revenue received is \$500,000 or above, the Contractor is required to submit an annual financial statement audit.

Based on total ministry revenues of over \$5 million per year, audited financial statements are required for Stelmaschuk's operations in British Columbia. Stelmaschuk and the ministry regions have applied the financial reporting criteria to the individual component schedules rather than the Client Service Agreements. As a result, audited financial statements have not been prepared, and the Client Service Financial Reporting requirements have not been met.

Recommendations

(2) **We recommend that:**

- **Stelmaschuk review whether the Financial Statement note should be expanded to include those transactions with DM Leasing for the program office equipment, computer systems and vehicles; and**
- **for fiscal 2003, Stelmaschuk submit consolidated audited financial statements for its BC operations that contain supplementary regional schedules at the program level.**

Agency Response:

Our external accountant prepared the notes to the Financial Statements. We are unclear as to the context of the first recommendation, as the external accountant's Review Engagement Report states that the Financial Statements were prepared and presented in accordance with generally accepted accounting principles. We will, however, discuss your recommendation with them.

We support your recommendation for providing consolidated audited financial statements. We would, however, prefer to internally prepare the supplementary regional schedules based on the audited financial information to minimize our audit costs, and the indirect cost to the ministry. Our controller will certify that the internally prepared statements are derived from the audited financial information.

4.0 Application and Allocation of Ministry Funding

Objective

To determine whether ministry funding was applied towards reasonable program expenditures that related to the purposes of the contracts; and revenue and expenses were appropriately allocated between programs.

Conclusion

We found that funding was applied appropriately and for the purpose intended in the contracts, and that Stelmaschuk has appropriate controls and procedures in place for the recording and allocation of contract revenue and program expenses to the applicable programs.

Except for administrative fees noted below, we found that revenue and expenditures were properly and consistently allocated to the programs.

Balance Sheets
and Operating
Statements

We reviewed expenditures for relevance to the programs and compared budget to actual as well as the method of allocation of expenditures. We did not find any non-ministry related expenditures or other unusual items. Internal operating statements agreed to external statements, and explanations were obtained from Stelmaschuk for all significant or unusual balances and/or transactions. Our review indicates that funding was applied appropriately and for the purpose intended in the contracts.

Administration
Fees

The general ledger and its supporting documents were examined and staff were interviewed with regard to administrative fees attributed to each program.

For the fiscal year April 1, 2000 – March 31, 2001 administrative fees were not consistently applied between programs. A number of procedures were used to allocate administration fees, including:

- using the rate specified in a contract;
- recording a set amount to accounts such as Head Office for photocopying, travel, rent or utilities. These amounts are grouped as a line item in the external financial statement as "administration fees/costs"; or
- recording a set amount of "admin fee", depending on whether the program is running a deficit.

We found that the administration fees ranged from a low of 0.9% to nearly 10%. Administrative fees are a relatively small portion of total costs. Therefore, these variances did not have a significant impact on the overall surplus. Stelmaschuk is aware of this issue and is currently reviewing its administration fee allocation procedures so they are more consistent and accurate.

In addition, we found that the salaries of the senior managers were allocated to direct program expenses. Senior managers are closely involved in the day-to-day operations of the programs and, based on discussions with the senior managers, the majority of their time was related directly to programs. However, some of their activities are not program specific (for example, accreditation meetings or management meetings) and normally would be considered general administration. Stelmaschuk should ensure there are appropriate guidelines and support for charging senior manager time directly to the programs.

Recommendations

(3) We recommend that W.J. Stelmaschuk:

- **review the administration charges and ensure that there is a consistent and supported basis for the application of these charges; and**
 - **ensure there are appropriate guidelines and support for the allocation of senior manager salaries as a direct program charge.**
-

Agency Response:

Measures have been put in place to have administrative charges applied to all contracts on a consistent and supported basis.

The contract reform report describes administrative expenditures to include "board of directors' meetings, and other administrative related meetings". WJS, however, considers accreditation and management meetings to be program related as they pertain to the day to day operations of the program. At these meetings the senior managers' role is to represent the programs in his/her sector or region. We do not classify these meetings as administrative.

WJS believes the allocation of their salaries is adequately represented as a direct program expense.

Okanagan Region's Response:

The Okanagan region has negotiated operating budgets for all the components it contracts with Stelmaschuk using GMOP 6.4 policy and the similar Contract Reform Project sub-committee report.

The region is confident that Stelmachuk's classifications are consistent with the operating budgets of other contractors in the Okanagan.

Occupancy and
real estate

We examined facility records to determine whether premise lease agreements for Stelmaschuk programs were with related parties and whether monthly payments were reasonable and appropriate. We found:

- Only two of the programs reviewed had residential costs from properties owned by Stelmaschuk. The two programs were not located in the Vancouver/Richmond and Okanagan Regions. However, information on the properties was reviewed, and we found that their rent when compared to fair market value was reasonable.
- For all other programs, the rent was charged by the British Columbia Housing Management Commission (BCHMC) or other non-related parties, and was at fair market value and reasonable.

Related parties

We reviewed related parties and examined selected contracts, agreements and transactions between Stelmaschuk and the related company, DM Leasing Ltd. Vehicles, computers, other office equipment and offices supplies are leased or purchased from DM Leasing Ltd. From all the lease agreements and office supplies

purchase invoices reviewed, the transactions between Stelmaschuk and DM Leasing Ltd. were found to be reasonable and at fair market value. We found transactions were accurately reflected in the general ledger and the financial statements.

5.0 Unearned Revenue and Surplus

Objective

To determine whether unearned revenue was defined in the contracts and refunded to the ministry where appropriate.

Conclusion

Based on our review of general expenditures and payroll (as discussed in section 2.0), we did not find any material unearned revenue.

The surplus and retained earnings recorded by Stelmaschuk in 2001 were reasonable.

Unearned Revenue

Most of the contracts with Stelmaschuk include an unearned revenue clause, which typically states if the "Contractor does not apply those funds to those purposes within the time and manner required under this Component Schedule, the amount of the funds which is not so applied is repayable to the Province". The Province has the discretion to recover the unearned revenue or apply it against future funding. The primary area where unearned revenue can be accrued is through staffing costs. Based on our review of general expenditures and payroll (as discussed in section 2.0), we did not find any material unearned revenue.

However, a general issue with unearned revenue clauses in most ministry contracts, is that there still remains considerable latitude in the definition of unearned revenue and the circumstances in which it is calculated. We understand that in some Okanagan Region contracts with agencies other than Stelmaschuk, clauses have been developed that include the specific conditions for its return to the ministry and a formula for its calculation. We encourage the Okanagan and Vancouver/Richmond Regions to review their contracts with Stelmaschuk and modify the unearned revenue clauses to include appropriate formulas for the calculation of unearned revenue and the specific conditions for its return to the ministry. Inclusion of these clauses can reduce the uncertainty over the conditions and amount of unearned revenue, and reduce the risk of a contractor inadvertently retaining unearned funds.

Recommendation

- (4) We recommend that the Okanagan Region and Vancouver/Richmond Region incorporate clauses in their contracts with Stelmaschuk, which include the appropriate formulas for the calculation of unearned revenue and the specific conditions for its return to the ministry.**
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Okanagan Region's Response:

It is the Okanagan region's intent to have budget schedules that list, in detail, the full cost and number of FTE's attached to the component. It is the region's intent to describe that less than full delivery of this schedule will result in corresponding unearned revenue. Reporting of FTE utilization will be documented in the reporting section of the components.

Vancouver/Richmond Region's Response:

The Vancouver/Richmond region will follow the Okanagan region's approach and try to make this process more formalized as part of the review of each contract.

Surplus and Retained Earnings

We reviewed the fund transfers throughout fiscal 2000/01 and general ledger listing for "Retained Earnings" and compared the surplus/deficit one-month prior to year-end to the final surplus to determine if any major changes had taken place. We obtained a retained earnings continuity schedule for the last two years.

Contract reform provides guidelines for the accumulation of reserves for not-for-profit agencies. However, contract reform does not provide specific guidelines of "profit" and the accumulation of retained earnings in for-profit agencies. Typically, we define a reasonable surplus and retained earnings based on comparative information from other for-profit agencies that we have audited. With the exception of one program, the range for the programs reviewed in this audit was from a surplus of 0.2% to a deficit of 0.4%. The exception was the Venture Challenge program, which had a deficit of 6.0%. As a result, we concluded that the surpluses and accumulated retained earnings of Stelmaschuk for the Vancouver/Richmond and Okanagan Regions in 2001 were reasonable.