



MEMORANDUM

To: Graham Whitmarsh
Deputy Minister
Ministry of Finance

April 27, 2009
File No.: 500160
Cliff No.: 176947

Cheryl Wenezenki-Yolland
Comptroller General
Ministry of Finance

From: Stuart Newton
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Subject: Final Report on Incentive Payments Audit – Phase II

We are pleased to provide you with our report on the audit of incentive payments made by the Ministry of Finance (MoF) to public sector employers distributed between July 1, 2006 and April 30, 2007. This report provides background on the incentive payments; the purpose, objectives and scope of our audit; and our overall conclusions, together with our detailed observations.

Background

In November 2005, at the release of British Columbia's Second Quarterly Report, the Minister of Finance, Honourable Carole Taylor, introduced the concept of a Negotiating Framework. The Minister indicated there was up to \$6 billion allocated to fund compensation increases for over 300,000 public sector employees in British Columbia. The framework covered employees from a range of sectors, including: Social Services, Crown Corporations, Education, Health, Colleges, Universities, Hospitals and the Public Service. Payment was to be provided in three parts with up to:

1. \$1 billion as an incentive for bargaining units to reach timely settlements with the government in contract negotiations;
2. \$4.7 billion over four years for annual compensation increases; and
3. up to \$300 million as a dividend option for those who sign contracts, without labour disruption, that extend beyond March 31, 2010, should the surplus on the audited public accounts for 2009/10 fiscal year exceed \$150 million.

In order to qualify for the incentive payments the following rules applied:

- For contract agreements expiring on or before March 31, 2006: a new agreement had to be reached prior to contract expiry and ratified by May 31, 2006.

- For contract agreements expiring after March 31, 2006 and before March 31, 2007: a new agreement had to be reached prior to contract expiry and ratified by May 31, 2007.
- For contract agreements expiring after March 31, 2007: a new agreement had to be reached prior to the contract expiry date and incentive payment wording within the new contract would then be approved by the MoF.

Although not covered by a contract agreement, management staff were also eligible for incentive payments.

The incentive payments were funded through the MoF. In order to expedite payment of the incentives, the MoF provided funds directly to individual employers and employer associations who were responsible for disbursing these payments to their eligible employees. The employers and employer associations receiving the funds were advised that the Province would be conducting random audits to confirm that the money was paid to employees in accordance with the agreed eligibility criteria.

In July 2007, Internal Audit & Advisory Services (IAAS) issued their audit report for the \$712 million (referred to as Phase I) in incentive payments issued to over 229,000 public sector employees up to June 30, 2006. An additional \$252 million was distributed between July 1, 2006 and April 30, 2007 primarily to school districts (\$205 million), but also to other groups whose contracts expired after March 31, 2006 or who had payments outstanding from the first round (includes payments to the BC Medical Association (BCMA) of \$25 million and \$22 million for certain bargaining units and management staff within colleges, ICBC, UVIC and other organizations). Once the audit of the initial incentive payments (\$712 million) was completed the Secretary to Treasury Board requested that IAAS perform an audit (Phase II) of this second set of incentive payments.

Purpose

The purpose of this audit was to provide assurance that the incentive payments distributed between July 1, 2006 and April 30, 2007 were only made to eligible employees for the approved amounts.

Objectives and Scope

The objectives of this audit were to determine whether:

1. There were appropriate tracking and accountability mechanisms between the MoF (as the provider of funds) and the individual employer entities (being the recipients of such funds) to ensure accuracy of amounts paid to employer organizations.

2. Incentive payments issued by the government were paid:
 - to only eligible employees;
 - for the correct amounts; and
 - on a timely basis.

The scope of this audit included the portion of the early incentive signing bonus, from the 2006 Negotiating Framework, that was paid to employees who were members of the public sector and whose employers were part of the Government Reporting Entity. It also included various “fee-for-service” providers such as physicians and midwives. The scope is limited to those groups and individuals who were given payment for the incentive bonus by the Province between July 1, 2006 and April 30, 2007.

Overall Conclusions

We tested a statistically valid sample drawn from the list of employers funded up to April 30, 2007, and found that, with the exception of the BCMA specialist group, over 98% of the incentive payments issued to their employees, were correct and paid to only eligible recipients. In addition, we found that these payments were made on a timely basis. The BCMA specialist group within our sample was treated separately because of the self-declaration method used by the doctors to calculate their incentive payments. We found a higher error rate within this group which resulted in 80% of these incentive payments being correctly calculated and paid. These results are more fully outlined in Section 2.3 below.

The Phase I and Phase II audits combined covered all the \$964 million in incentive payments issued up to April 30, 2007. There are some organizations that have agreements with their employers which expire after April 30, 2007. When their agreements are settled, they will receive approximately \$22.7 million in incentive funding.

Through our Phase I and II audits, we identified a net surplus of \$28.1 million being incentive funding issued to employers that exceeded what was paid by them to their employees. The MoF has been informed of this and has established a policy and processes to request repayment from organizations which received excess funding of \$30,000 or greater and to provide additional funding to organizations with funding shortfalls of \$30,000 or greater.

Observations

1.0 Reconciliation of Funding to Employers

Staff from both Treasury Board (TBS) and the Ministry of Health (MoH) recorded the issuance of incentive payment funds to 87 employers throughout the province who received funding between July 1, 2006 and April 30, 2007. To measure the accountability of the employers that received this funding, it was necessary to determine how much of the funds were actually paid to the employees.

At the Comptroller General's request Financial Reporting and Advisory Services (FRAS) gathered information to determine how much of the funding provided by the MoF had actually been paid by the 87 receiving organizations to their employees. The employers were asked to submit a reconciliation between the funds they received and the amounts they paid to their employees. FRAS is continuing to collect the approximately 20% of outstanding reconciliations that had not been received at the time of our audit. From the reconciliations received, we found that there were:

- \$6.4 million in payments to employers that were in excess of the amounts they disbursed to their eligible employees;
- other employers' funding fell short by \$0.9 million of the amounts that they disbursed to their eligible employees; and
- potential net recoveries from employers of \$5.5 million.

We have communicated the above information to FRAS, who have initiated a process to recover any excess funds owed to the government and reimburse those employers with identified shortfalls.

2.0 Testing of Payments to Employees

2.1 Statistical Sampling

For Incentive Payments Phase II, similarly to Phase I, BC STATS used a statistical sampling methodology to select an audit sample. This sample was used to assess whether the employees who received incentive payments were eligible for these payments and to determine if eligible employees were paid the correct amounts. Our initial audit sample consisted of 17 employers, selected from the 87 that received incentive funding in this phase. The sample was chosen from all areas of the public sector including Community Services, Crown Agencies, Schools, Universities, Colleges, Health and the Provincial Government (Appendix A).

During our testing, we noted that one of the employers, BCMA, issued incentive payments to their members on a basis different from the rest of the groups. Instead of the employer determining the amount of incentive payment that the individual would receive based on agreed criteria, the amount of incentive payment was determined based upon a self-declaration of annual earnings by the members.

Through discussions with BC STATS, it was determined that BCMA (counted as two employer groups – one for specialists and one for general practitioners) would be removed from our statistical sample as their incentive payments were determined on an entirely different basis and, therefore, any errors should not be extrapolated over the entire population. Our review of the results of BCMA claims is described in further detail in Section 2.3 of this report.

For the remainder of our sample, our audit testing involved extracting the incentive eligibility rules from each employer group's contract agreement. These rules were then applied to the employees in the group to determine whether they were eligible and paid correctly. We also noted whether the incentive payments were processed within a reasonable length of time.

From our audit testing, we identified 78 errors which were a combination of 59 overpayments of \$28,918 and 19 underpayments of \$10,115. Individual errors ranged between \$20 and \$3,700. Forty-seven percent of the errors were categorized as calculation errors which included payments that were not prorated correctly and incorrect payments for employees on maternity leave. The two remaining error types noted included cases where employees received an incentive payment when they did not meet the qualifying criteria and other cases where employees were qualified to receive a payment but were not paid.

2.2 Extrapolation of the Errors

We provided a summary of the errors that we found in our audit sample to BC STATS to allow them to estimate the number of errors that would occur within the total population (excluding BCMA). As the rate of errors varied significantly between sectors, they used a "sector weighting" methodology which resulted in a combined error rate for Phase I and II of 1.71%. Based on their extrapolation of errors over the Phase II population of 81,000 employees (\$227 million), they estimated that there would be 1,390 errors¹ consisting of:

- 1,010 estimated overpayments totalling \$565,600; and
- 380 estimated underpayments totalling \$437,000.

This would result in a net estimated overpayment of \$128,600, which represents 0.06% of the total \$227 million disbursed to employers as of April 30, 2007.

2.3 British Columbia Medical Association (BCMA)

The BCMA includes two distinct groups, general practitioners and specialists. BC Stats as part of their selection process chose the specialist group for our audit sample. The incentive payments for the specialists were handled differently from all the rest of those individuals who received their payments between July 1, 2006 and April 30, 2007. As noted in the previous section, each BCMA member was asked to make a claim based on their calculated eligible earnings from fiscal 2005/06. There were three levels of incentive funding available depending on the member's level of earnings and the following claims were made:

¹ See Appendix B for BC STAT's methodology. As explained in that appendix, the actual number of errors would fall somewhere within a range surrounding the estimate of 1,390 errors. In this case, the actual number of errors is estimated to be between 1,290 and 1,500. Overpayments and underpayments are also calculated based on a range.

Eligible Earnings	Number of Claims	Incentive Level Claimed	Total Claimed
Over \$100,000	3,297	\$2,700	\$8,901,900
\$50,000 - \$100,000	194	\$1,350	\$261,900
Less than \$50,000	189	\$675	\$127,575
Members with no claims	586	N/A	N/A
Total	4,266	N/A	\$9,291,375

Our audit identified the following information with regards to the claims submitted by BCMA members:

- 220 were over claims (totalling \$317,250); and
- 56 were under claims (totalling \$74,250).

We also noted that there were no claims received from 586 specialists who would have been eligible to receive incentive payments. By including those that did not claim, the error rate for the BCMA sample is 20%. However, if only the over and under claims are considered, the error rate drops to 7.5% which is still significantly greater than the 1.2% found in the rest of the Phase II sample (non-BCMA groups).

We have shared our findings in this area with the Director, Analysis, MoH who has indicated that an assessment will be made to determine whether any recoveries or adjustments will be made. Because of the high error rate noted above, we are encouraging the Director to continue with this planned assessment.

In conclusion, we want to acknowledge and thank Treasury Board Staff and staff from Financial Reporting and Advisory Services, Ministry of Health, Public Sector Employers' Council Secretariat, BC STATS and various employer organizations who assisted us in conducting our review.

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Enclosure

Appendix A – Population and Sample Size

The following table is a breakdown of the total population of employers:

Sector	Number of Organizations	Number of Employees	Avg. # of Employees per Org.
Community	5	514	103
Crown Agencies	4	1,090	273
Health	5	7,174	1,435
Provincial Government	4	622	156
School Districts	60	70,644	1,177
Universities & Colleges	9	7,680	853
Total	87	87,724	

The following table is a breakdown of the sample employers we tested:

Sector	Number of Organizations	Number of Employees	Avg. # of Employees per Org.
Community	1	13	13
Crown Agencies	3	950	317
Health – BCMA specialists	1	4,266	4,266
Health - other	1	17	17
School Districts	9	3,852	428
Universities & Colleges	2	1,613	806
Total	17	10,711	
% subjected to detailed audit testing	19.5%	12.2%	

**Appendix B – Sampling Strategy Methodology
and Extrapolation of Results *Draft Report***

OFFICE OF THE COMPTROLLER GENERAL
MINISTRY OF FINANCE

**Incentive Pay Audit Phase II:
Sampling Strategy Methodology
and Extrapolation of Results
*Draft Report***

October 2007



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1.0 Introduction

In the early months of 2006, the Province of British Columbia, through the MoF, made available additional funds to those public sector unions that were negotiating labour contracts. These additional funds were to be distributed to the individuals in each labour union if their contract was renewed prior to the expiry of their existing collective agreement.

In addition to workers employed directly by the Province of British Columbia, these funds were also made available to all public sector organizations that receive funding either directly or indirectly from the Province, including crown corporations, the provincial health authorities, universities and colleges, schools districts, and social services organizations. Further, these funds were also made available to the management staff of those same organizations.

The amount paid to any one individual varied, based on a number of criteria that differed from one organization to the next. These included which union or management group the individual belonged to, and the amount of work they had completed in the previous two years (which reduced the amounts paid to part-time workers, and those hired within the two years).

By June 30, 2006, approximately \$712 million was paid out to roughly 229,000 workers in 635 public sector organizations. An additional \$252 million was paid to just under 88,000 workers in 87 organizations after June 30, 2006, to workers whose contracts expired after March 31, 2006. Readers should note that some public sector organizations have more than one union, and based on the expiry dates of the existing collective agreements, made payments both prior to and after June 30, 2006.

In August 2006, staff of the Office of the Comptroller General, MoF approached BC STATS to aid in the development of an audit of the payments made. The objectives of the audit were to determine whether:

1. there were appropriate tracking and accountability mechanisms between the MoF (as the provider of funds) and the individual employer entities (being the recipients of such funds), and
2. incentive payments issued by the government to individual employer entities were paid:
 - to only eligible employees;
 - for the correct amounts; and
 - on a timely basis.

Given the large number of organizations and individuals within the public sector, it was logistically inefficient to audit each and every payment made. BC STATS provided expert advice on drawing an optimal sample that would maximize statistical confidence and make most efficient use of MoF's audit resources.

An initial audit examined the payments made prior to June 30, 2006. The sampling plan devised for that audit, and the extrapolation of the results to the population, are reported in a separate report².

The current report deals only with the Phase II audit, conducted of payments made between July 1, 2006 and April 30, 2007. The report summarizes the methodology employed to draw the sample, and presents an extrapolation of the audit results across the payments made after June 30, 2006, and the range of accuracy based on the confidence levels associated with the sample.

2.0 Methodology

This section summarizes the stratified cluster sampling approach.

Assumptions

Four factors were considered when devising a sampling methodology for the Phase II audit.

1. The error rates to be found in each sector in the secondary audit would be similar to those found in the primary group of payments made prior to June 30, 2006.
2. Sector groups: the sample needed to ensure that each sector had adequate representation, in light of the findings of the primary audit. That is to say, for those sectors where a higher error rate was identified in the primary audit, a larger sample was drawn for the secondary audit.
3. Bargaining units and management groups in each organization: it was determined that for the purpose of sample, these were irrelevant (although were important considerations for the audit, in that the appropriate incentive payment varied between organizations and bargaining units within organizations.)
4. The BC Medical Association (BCMA) payouts were dealt with in a manner inconsistent with the rest of the public sector organizations. The assessment of the number and magnitude of errors in incentive payments made through the BCMA was therefore made on a different basis from the rest of the public sector.

Only payments made to Specialist doctors through the BCMA were audited. Due to significant differences between the payment criteria of Specialist incentive payments and General Practitioner payments, it was deemed inappropriate to extrapolate the results of the Specialist audit to the General Practitioner doctors.

² BC Stats; prepared for Ministry of Finance. *Incentive Pay Audit: Sampling Strategy Methodology and Extrapolation of Results, Final Report* (March 2007).

Sample of non-BCMA organizations

The sample of non-BCMA public sector employers was based on the following confidence assumptions:

- Based on the results of the primary audit, it was assumed that 98.7% of payments were made correctly, and 1.3% were in error.
- Assumed margin of error in the sample: +/- 0.2 percentage points at the 95% confidence level (i.e. 19 times out of 20). In other words, if the sample were to be repeated 20 times, 19 of those times would yield an error rate between 1.1% and 1.5%.

This sample yielded a total of 16 organizations.

3.0 Findings & Confidence Interval

This chapter describes what was found in the audit conducted by the Office of the Comptroller General, extrapolates the results across all of the payments made between July 1, 2006 and April 30, 2007 in the entire BC public sector, and the statistical interpretation of that extrapolation.

3.1 Audit project

As described above, the sampling methodology for non-BCMA employees selected 16 employers from the 85 non-BCMA organizations that received incentive funding to pay out between July 1, 2006 and April 30, 2007.

In addition, a total of 4,266 payments to Specialist doctors were audited.

3.2 Findings

As shown in Table 1 the audit conducted by the Office of the Comptroller General of non-BCMA public sector employers found 78 errors in the 6,445 individuals employed by the 16 organizations audited. This yields an average error rate of 1.2% across the 16 organizations.

The dollar value of the 78 errors was found to be \$28,918 in overpayments (59 individuals who received more than they were entitled as per the terms of the incentive payout), and \$10,115 in underpayments to 19 individuals.

Table 1. Audit results, non-BCMA (payments made after June 30, 2006)

	Number of organizations	Number of individuals	Amount paid (dollars)
Total population*	85	81,375	\$226,887,644
Total audited	16	6,445	\$17,506,529
Number of errors found		78	
Error rate (unweighted)		1.2%	
<hr/>			
Dollar value of errors			
Overpayment		59	\$28,918
Underpayment		19	\$10,115
Net of payment error			\$18,803

**Approximate figures for the total population; excludes BCMA*

As shown in Table 2 the audit of payments made to Specialists through the BCMA found 862 errors in the 4,266 individuals. This yields an average error rate of 20.32%.

Table 2. Audit results, BCMA

	Number of individuals	Amount paid (dollars)
Total population*	7,124	\$25,064,375
Total audited (Specialists only)	4,266	\$9,296,239
Number of errors found	862	
Error rate (unweighted)	20.2%	
Dollar value of errors		
Overpayment	220	\$317,250
Underpayment	56	\$74,250
Eligible but did not apply	586	\$996,300
Net of payment error (Overpayment, minus underpayment and eligible but did not apply)		-\$753,300

**Total population of Specialists and General Practitioners who were eligible for the payment, based on information from the audit and the Ministry of Health.*

3.3 Extrapolation of Results and Confidence Interval (non-BCMA employers)

3.3.1 Extrapolation of Results (non-BCMA employers)

The sample of 16 organizations and just under 6,500 individuals can be extrapolated across the whole of the 81,375 individuals in the BC public sector who received their payment between July 1, 2006 and April 30, 2007.

For the purpose of the extrapolation, the results of the Phase II audit were combined with those of the primary audit to establish a revised error rate for each sector, based on the larger sample. This approach is consistent with the assumption made in the sampling phase that error rates in the second phase of the audit were the same as the group of payments prior to June 30, 2006. The net result is that the overall error rate, weighted by sector, was slightly lower in the secondary audit, and thus reduces the combined error rate of both sets of incentive payments to 1.71%. Table 3 shows the extrapolation.

Table 3. Extrapolation of results: Phase II audit

	Number of individuals	Amount paid (dollars)
Number of errors found	78	
Error rate (preliminary and secondary audit, weighted by sector) ³	1.71%	
Estimate of errors in the whole population ⁴	1,390	
Subtotals		
Estimated Overpayment	1,010	Average*: \$560 Total**: \$565,600
Estimated Underpayment	380	Average*: \$1,150 Total**: \$437,000

* rounded to nearest 10

** rounded to nearest 100

³ Note that this figure differs from that show in Table 1, as it is weighted to account for the different error rates in the different sectors. In the Phase II audit, the larger sectors had smaller error rates, thus reducing the weighted rate.

⁴ The 81,375 individuals paid between July 1, 2006 and April 30, 2007.

3.3.2 Confidence Interval (non-BCMA employers)

Because the result shown in Table 3 is based on a sample, it is necessary to refer to this as an estimate. The confidence interval for the estimated error rate for the secondary audit is calculated to be +/- 0.12 percentage points, at the 95% confidence level. This means that if the random sample was repeatedly administered, in 19 out of 20 audits the percentage of pay records exhibiting an error would fall between 1.59% and 1.84%.

This confidence range for the secondary audit has, in turn, an impact on the estimates shown in Table 3. Below in Table 4 the range of estimated values is shown for both overpayments and underpayments.

Table 4. Confidence range: non-BCMA employers

	Error rate	Number of errors*	Amount paid (dollars)**
Error rate	1.71%	1,390	
95% confidence range – lower	1.59%	1,300	
95% confidence range – upper	1.84%	1,490	
Subtotals			
Overpayment	1.24%	1,010	\$565,600
<i>Low range</i>	<i>1.16%</i>	<i>950</i>	<i>\$532,000</i>
<i>High range</i>	<i>1.32%</i>	<i>1,070</i>	<i>\$599,200</i>
Underpayment	0.47%	380	\$437,000
<i>Low range</i>	<i>0.43%</i>	<i>350</i>	<i>\$402,500</i>
<i>High range</i>	<i>0.52%</i>	<i>420</i>	<i>\$483,000</i>

* rounded to nearest 10

** rounded to nearest 100

3.4 Extrapolation of Results and Confidence Interval (BCMA)

As noted earlier, only payments made to Specialist doctors through the BCMA were audited. Due to significant differences between the payment criteria of Specialist incentive payments and General Practitioner payments, it was deemed inappropriate to extrapolate the results of the Specialist audit to the General Practitioner doctors.

The barriers that discourage extrapolating the results of the Specialists across the General Practitioners include:

- Different amounts of maximum incentive payments
- Different eligibility criteria
- Without further auditing, it poses a risk to assume that the high “eligible but did not apply” proportion in the Specialist population would be consistent with the General Practitioners