



Veterans Affairs
Canada

Anciens Combattants
Canada

February 2014

AUDIT OF OVERPAYMENTS

Audit and Evaluation
Division

Canada

Acknowledgements

The audit team would like to gratefully acknowledge the staff in VAC Finance Division and Service Delivery Branch. Their contributions were essential to this audit.

TABLE OF CONTENTS

1.0 EXECUTIVE SUMMARY	i
2.0 BACKGROUND.....	1
3.0 ABOUT THE AUDIT	1
3.1 OBJECTIVES.....	1
3.2 SCOPE.....	2
3.3 METHODOLOGY	2
4.0 AUDIT RESULTS	3
4.1 HANDLING OF OVERPAYMENTS.....	3
4.2 BUSINESS PROCESSES	5
4.3 OVERSIGHT AND REPORTING	6
4.4 AUDIT OPINION.....	9
5.0 DISTRIBUTION.....	10
APPENDIX A - AUDIT CRITERIA	
APPENDIX B - RISK RANKING OF RECOMMENDATIONS AND AUDIT OPINION	

1.0 EXECUTIVE SUMMARY

The purpose of this audit is to provide assurance that departmental activities with respect to the processing of overpayments are in compliance with policies, procedures, and regulations. The audit reviewed the overpayments of four programs: Disability Award, Disability Pension, War Veterans Allowance, and Earnings Loss.

An overpayment is any amount paid to a beneficiary to which there is no entitlement, or which exceeds entitlement and are “debts to the Crown”. Veterans Affairs Canada is required¹ to pursue and collect any outstanding amounts of overpayments.

The total annual gross receivables (overpayments and other receivables), as of March 31, 2013, reported by VAC in the 2013 Public Accounts of Canada was \$25.5 million. Of that amount, there is \$20.9 million in program overpayments, of which \$20.6 million is for overpayments related to the four programs in this audit’s scope.

Within the four programs, the auditors reviewed a sample of 155, out of a total of 8,007, overpayment transactions generated during 2012-2013 and found that 75% of the overpayment amounts that formed the audit sample were recovered. However, there are a number of aged² overpayments (\$9.8 million), outstanding for up to 15 years, where no funds have been collected.

Overall results

The audit team determined that departmental activities related to the processing of overpayments were “Generally Acceptable”. Overpayments in aged receivables require attention and business processes need to reflect the operating environment. Oversight, monitoring, and reporting of overpayments should also be improved to ensure effective management of receivables and to determine and address systemic issues.

Recommendations

- R1 It is recommended that the Director General, Finance Division, actions outstanding overpayments in aged receivables. (Critical)**
- R2 It is recommended that the Director General, Service Delivery and Program Management Division, in collaboration with the Director General, Finance Division, and the Director General, Centralized Operations Division, ensures documented, updated and integrated business processes exist for the actioning of overpayments. (Essential)**

¹ Treasury Board "Directive on Receivables Management". (2009)

² * An “aged” receivable is an amount due, categorized by the length of time that it is outstanding (e.g., 1-30 days past due, 31-60 days past due, 61-90 days past due, and 90+ days past due).

R3 It is recommended that the Director General, Finance Division, in collaboration with the Director General, Service Delivery and Program Management Division, and the Director General, Centralized Operations Division, improves the reporting, monitoring, and oversight of overpayments. (Critical)

Chief Audit Executive's Signature

Kim Andrews
Acting Chief Audit Executive

Date

The Audit Team consisted of:

Jonathan Adams, Audit and Evaluation Director
Karen Walsh, A/Audit and Evaluation Director
Vaughn Horton, Audit and Evaluation Manager
Lana Wright, A/Audit and Evaluation Manager
Sivajan Nagulesapillai, Audit and Evaluation Officer
Jean-Pierre Goudreau, Audit and Evaluation Officer

2.0 BACKGROUND

An overpayment is any amount paid to a beneficiary to which there is no entitlement, or which exceeds entitlement³. Overpayments are established as receivables by Veterans Affairs Canada (VAC) and are “debts to the Crown”. Under its requirement⁴ for prudent management of receivables, the Department is responsible for identifying, managing, and resolving overpayments. An overpayment may be recovered, remitted, or written-off. Recovery is normally the first course of action. A remission is the cancellation or forgiveness of an overpayment. Overpayments may be written-off when all reasonable collection action has been taken and there is no possibility of foreseeable collection⁵.

VAC is responsible for disbursing funding, based on legislative/regulatory entitlement, to Veterans and related beneficiaries. In 2012-13, VAC provided \$3.2 billion in program funding to Veterans and their families. In this same period, total annual gross receivables (overpayments and other receivables) were \$25.5 million, of which \$20.9 million were outstanding program overpayments (a decrease from \$22.3 million in 2011-2012).

This audit looked at the overpayments related to four programs: Disability Award, Disability Pension, War Veterans Allowance, and Earnings Loss. At March 31, 2013, there was \$20.6 million in overpayments related to the four programs included in the scope of the audit. The \$20.6 million accounted for 81% of the Department’s total annual gross receivables of \$25.5 million.

3.0 ABOUT THE AUDIT

3.1 Objectives

The objectives of the audit were to:

1. Determine if VAC is in compliance with policies, regulations and procedures for actioning overpayments;
2. Identify systemic issues that cause overpayments; and
3. Determine if overpayments are properly reported.

The audit criteria relevant to each objective are outlined in Appendix A.

³ *Canadian Forces Members and Veterans Re-establishment and Compensation Act*, Section 88. , *Pension Act* Section 83. , *War Veterans Allowance Act* Section 18.

⁴ Treasury Board "Guidelines on Collection of Receivables". (2009)

⁵ *Debt Write-Off Regulations*, 1994

3.2 Scope

The scope included overpayments created in the 2012-2013 fiscal year for the Disability Award, Disability Pension, War Veterans Allowance, and Earnings Loss programs.

Program overpayments not in scope for this audit include:

- Health Care Benefits, Veterans Independence Program, Long Term Care, and Vocational Rehabilitation Programs;
- Transactions that should have been recorded as overpayments but were not; and
- Overpayments incurred at Ste. Anne's Hospital.

The audit team also analyzed the status of, and systemic issues causing, overpayments within the Department's aged receivables. Aged receivables reflect the length of time receivables have been outstanding as of March 31, 2013.

3.3 Methodology

This audit was conducted in conformance with the *Institute for Internal Auditors (IIA) Standards* and the Internal Auditing Standards for the Government of Canada, as supported by the results of the quality assurance and improvement program.

Interviews and Direct Observation

Interviews were conducted in person, or by telephone, with VAC staff responsible for the identification, processing, and reporting of overpayments. Through the interviews, the audit team obtained an understanding of the roles and responsibilities, key activities and adequacy of internal controls; and, gathered documentation to support findings.

On-site visits were conducted with the Service Delivery Branch and VAC Finance Division allowing the audit team to interview staff responsible for processing overpayments and observe the systems used to process overpayments.

Documentation Review

Government of Canada, Treasury Board (TB), and departmental documentation related to the management of receivables was reviewed to determine compliance with the applicable policies, procedures and regulations. Some key documents reviewed include:

- *Financial Administration Act*,
- *Debt Write-off Regulations, 1994*,
- *Treasury Board Directive on Receivables Management*,
- *Pension Act*,
- *Canadian Forces Members and Veterans Re-establishment and Compensation Act*,
- VAC Financial Policy and Procedures Manual, and
- VAC Accounting Policy and Procedures Manual.

File Review

The audit team conducted a file review to determine whether VAC is complying with policies, regulations and procedures, and identify systemic issues that cause overpayments. During 2012-2013, 8,007 transactions totaling \$20.6 million were established as overpayments for four programs (see Table 1 below). Total 2012-13 expenditures for these programs were \$2.6 billion, with 2,000,000 payment transactions. A statistically valid sample of 155 overpayments created in 2012-2013 for these programs was selected based on volume of transactions, materiality of the overpayment, and associated risk.

Table 1 – Overpayments created in Client Service Delivery Network in 2012-2013 (for year ending March 31, 2013)		
Program	Overpayments	Total Amount
Disability Award	135	\$4,896,307
Disability Pension	6,456	\$12,112,189
War Veterans Allowance	238	\$98,859
Earnings Loss	1,178	\$3,459,732
Total	8,007	\$20,567,087

Source: VAC Statistics Directorate

Also, the status of overpayments in aged receivables was analyzed in the audit. Aged receivables are a financial management tool used to reflect the length of time receivables have been outstanding. VAC is required⁶ to pursue and collect any outstanding amounts.

4.0 AUDIT RESULTS

4.1 Process for Actioning Overpayments

Overpayments can be identified by various VAC units, be system-generated, or be reported to the Department by the recipient. Once an overpayment is identified, it is recorded in the Client Service Delivery Network, the primary system used for processing overpayments. Recovery is the first course of action in the overpayment process. There may be instances where a recovery is not desirable (e.g., recovery may create undue financial hardship). Overpayments can otherwise be remitted or written-off.

⁶ Treasury Board "Directive on Receivables Management". (2009)

Aged overpayments must be recovered, remitted, or written-off.

A detailed review of the 155 overpayment transactions from 2012-2013 was conducted to investigate the timeliness of processing. At the time of the file review in July 2013, 75% of the overpayment amounts that formed the audit sample had been recovered. Furthermore, outstanding program overpayments for all programs, declined from \$22.3 million in 2011-2012 to \$20.9 million in 2012-2013.

Although most of the overpayments created in 2012-2013 were collected, there are uncollected overpayments in aged receivables. Treasury Board policy requires that receivables are promptly recognized and vigorously pursued for collection⁷. Table 2 below shows, by relative age and program, the overpayments reported where no monies have been recovered. The analysis of overpayments in aged receivables did not include investigations into the reasons for the delay in actioning these aged receivables.

Table 2 – Overpayments with no recoveries in aged receivables (as of March 31, 2013)					
	Disability Award	Disability Pension	War Veterans Allowance	Earnings Loss	Total
Up to 1 year	\$440,895	\$698,597	\$21,770	\$643,619	\$1,804,881
1 to 2 years	\$252,201	\$1,090,124	\$12,282	\$254,468	\$1,609,075
2 to 3 years	\$946,649	\$810,088	\$10,644	\$165,101	\$1,932,483
3 to 4 years	\$2,141	\$142,096	\$38,584	\$3,860	\$186,681
4 to 5 years	\$2,002	\$86,871	\$54,054	\$45,418	\$188,345
6 - 10 years	\$25,000	\$496,937	\$38,405	\$33,816	\$594,158
11 - 15 years	-	\$206,350	\$3,268,589	-	\$3,474,939
+15 years	-	-	-	-	-
Total	\$1,668,888	\$3,531,062	\$3,444,329	\$1,146,282	\$9,790,561

Source: VAC Statistics Directorate

Recommendation 1

It is recommended that the Director General, Finance Division, actions outstanding overpayments in aged receivables. (Critical)

Management Response

⁷ Treasury Board "Directive on Receivables Management, Section 5.2 Expected results". (2009)

Management agrees to review aged accounts receivable with the aim of clearing long outstanding receivables as either - recoveries, remissions and/or write-offs.

4.2 Business Processes

Business processes support the achievement of departmental objectives. Processes may be communicated informally or documented formally. In some cases, documentation may not be required as the processes are well understood, relatively simple, or involve only a few people. In other cases, documentation is necessary to ensure consistency within the organization. Documented processes also provide a method/tool to transfer corporate knowledge.

Documented, updated and integrated business processes should exist.

There are multiple units within VAC that are involved in the processing of overpayments. The audit team noted that there is good communication between the teams processing overpayments, and that there is sufficient segregation of duties between processing, collecting, maintaining, reconciling and reporting accounts. However, there is limited documentation outlining the complete overpayment process, and there are inconsistencies in the existing documentation. For example, key financial controls identified specific dollar limits for which each work unit was authorized to process, whereas the program policies did not. Also, there is no evidence of integration among the units.

A pilot project was initiated in 2009, and is still ongoing, for the Disability Pension and Disability Award Programs. The objective of the pilot is to investigate overpayments to determine if they are based on administrative errors, and recommend a course of action before a letter is sent to the program recipient, to prevent any undue stress or anxiety for the recipient. Currently, the pilot is implemented only for the two Disability Programs. The audit team noted that an evaluation of the pilot project should be completed and that consideration should be given to implementing the process for the other two Programs in this audit to further prevent undue stress or anxiety on program recipients.

Recommendation 2

It is recommended that the Director General, Service Delivery and Program Management Division, in collaboration with the Director General, Finance Division, and the Director General, Centralized Operations Division, ensures documented, updated and integrated business processes exist for the actioning of overpayments. (Essential)

Management Response

Management agrees with this recommendation. The development of integrated business processes reflecting the current organizational environment and processing steps conducted across work units supports the consistent and efficient resolution of overpayments.

4.3 Oversight and Reporting

Oversight is important to ensure that departmental direction, plans, and actions are appropriate. Management should be provided with timely and accurate financial and operational information in order to fulfill the oversight function.

Oversight, monitoring, and reporting require improvements.

VAC is required to establish and monitor results-based measurement mechanisms, and prepare and distribute periodic reports to management⁸.

The VAC Financial Policies and Procedures Manual (FPPM) is a departmental manual that outlines responsibilities for oversight and reporting, including the requirement to distribute receivables reports to management on a quarterly basis. The review of the FPPM and interviews with staff indicate that the FPPM no longer reflects the operating environment and, as a result, there are gaps in the assignment of responsibility for oversight and monitoring of the processing of overpayments. According to the Treasury Board Directive on Receivables Management, the departmental Chief Financial Officer (CFO) is responsible for overseeing the monitoring of receivables and identifying any significant difficulties, gaps, or compliance issues. The audit team determined that the *Portfolio Aged Analysis of Accounts Receivable Report* was last provided to the CFO in September 2011. Resuming regular distribution of this report to the CFO is required to maintain policy compliance.

There are systemic issues causing overpayments.

Systemic issues are common, inherent, and recurring situations that give rise to overpayments. This is in contrast to overpayments that are generated by case-specific or isolated factors. The systemic issues identified in the file review are presented in Table 3 below.

⁸ Treasury Board "Directive on Receivables Management, 6.2 Internal control". (2009)

Table 3 – Systemic issues			
VAC Program	Number of Overpayments Reviewed	Systemic Issue	Overpayments Reviewed with Systemic Issue
Disability Award	48	Incorrect legislation used in adjudication	40%
		Untimely disclosure of other benefits	33%
Disability Pension	67	Delay in receipt of death notification	91%
War Veterans Allowance (WVA)	10	Delay in receipt of death notification	70%
Earnings Loss	30	Untimely disclosure of earning	90%

Source: Audit and Evaluation Division

The first systemic issue, overpayments resulting from VAC staff using incorrect legislation when adjudicating, is preventable as the decision making is within VAC's control. This type of systemic issue accounted for 40% (19/48) of the sampled Disability Award overpayments. Some incorrect decisions originated from inexperience with the program when it began in 2006; whereas, others were recent errors indicating a need for training in the legislation and/or changes to the quality control process.

The remaining systemic issues are more difficult to prevent as the Department relies on the timeliness of disclosure of information from the recipient or family. For example, the recipient's untimely disclosure of other benefits such as workers' compensation benefits accounted for 33% (16/48) of the systemic issues for the Disability Award program. Another example is with regard to the Earnings Loss Program which requires the recipient to report earnings to the Department. The majority (90%) (27/30) of the sampled Earnings Loss overpayments were caused by untimely disclosure of earnings⁹. Finally, overpayments occur when the Department receives notification of a Veteran's death long after the date of death. Delays in death notification were prevalent in 70% (7/10) of the War Veterans Allowance overpayments and 91% (61/67) of the Disability Pension Program overpayments.

Monitoring and reporting systemic causes of overpayments would allow management to determine the most appropriate corrective action and reduce the number of overpayments in the future.

⁹ A June 2013 'Audit of Earnings Loss' recommended obtaining annual recipient income information. Implementation of the management response is currently in progress.

Exception reporting¹⁰ is required.

Risk is mitigated when people have relevant information to make decisions. Information should flow to managers in various areas of the Department to enable them to identify and highlight pervasive issues. Exception reporting is a control element that ensures transactions are correctly identified, handled, and reported allowing managers to identify and manage risk. Assuring reliable data can be difficult without exception reporting of issues and errors.

Although the audit trail for processed overpayments was sufficient, there is limited reporting of the causes of overpayments (systemic or otherwise). Generic reasons for overpayments such as “administration error” are captured in the Client Service Delivery Network but adequate detail (i.e., cause of overpayment) is not captured and the underlying causes are not investigated. Exception reporting would ensure that the causes are identified and addressed.

As a final observation, Veterans’ accounts are adjusted for a variety of reasons (to correct errors, issue urgent payments, etc.). Some are actual adjustments, some are overpayments. The method used in the Client Service Delivery Network to process overpayments is also used to process recipients’ account adjustments. Both are reported as overpayments, making differentiating between overpayments and account adjustments difficult. Developing an exception report of the account adjustments would distinguish between the overpayment and account adjustments.

Recommendation 3

It is recommended that the Director General, Finance Division, in collaboration with the Director General, Service Delivery and Program Management Division, and the Director General, Centralized Operations Division, improves the reporting, monitoring, and oversight of overpayments. (Critical)

Management Response

Management agrees to implement a risk-based approach to ensuring corporate oversight, reporting and management of aged accounts receivable in compliance with the TB Directive on Receivables Management. This will improve the timeliness and accuracy of the financial reporting for accounts receivable.

A consultative approach will be used to engage key departmental staff in the review of the reporting, monitoring and oversight of overpayments.

¹⁰ Exception reporting is a method to report data abnormalities which management uses to monitor and/or address.

4.4 Audit Opinion

In the opinion of the audit team, departmental activities related to the processing of overpayments were “Generally Acceptable”.

5.0 DISTRIBUTION

Assistant Deputy Minister, Service Delivery

Assistant Deputy Minister, Human Resources and Corporate Services

Assistant Deputy Minister, Policy, Communications and Commemoration

Director General, Service Delivery and Program Management

Director General, Centralized Operations Division

Director General, Finance Division

Executive Director and General Counsel, Legal Services Unit

Senior Director, Strategic Financial Planning and Resource Management

Director, Statistics

Director, Access to Information and Privacy

Appendix A - Audit Criteria

While the majority of the Audit Criteria are “Partially Met”, when taken together, the weaknesses were mitigated by other factors and therefore the audit opinion is “Generally Acceptable”.

Objective 1: To determine if VAC is in compliance with policies, regulations and procedures for actioning overpayments.	
Audit Criteria	Results
1. There is appropriate segregation of duties.	Met
2. Authority, responsibility and accountability are clear and communicated.	Partially Met
3. Management identifies and assesses the existing controls that are in place to manage risks associated with overpayments.	Partially Met
4. Financial and program management policies and authorities are established and communicated.	Partially Met
5. Compliance with financial and program management laws, policies, and authorities is monitored regularly.	Partially Met
6. Transactions are coded and recorded accurately and in a timely manner to support accurate and timely information processing.	Partially Met
7. The organization provides employees with the necessary training, tools, resources and information to support the discharge of their responsibilities.	Partially Met

Objective 2: To identify systemic issues that cause overpayments.	
Audit Criteria	Results
1. The organization has in place a process to identify change opportunities/ requirements.	Partially Met
2. Exception reporting is available to identify systemic errors.	Partially Met

Objective 3: To determine if overpayments are properly reported.	
Audit Criteria	Results
1. The oversight body/bodies request and receive sufficient, complete, timely and accurate information.	Partially Met
2. Reviews are conducted to analyze, compare and explain overpayment trends.	Partially Met
3. Appropriate and timely financial and non-financial reporting is communicated internally and externally.	Partially Met

Sources: The *Audit Criteria related to the Management Accountability Framework: A Tool for Internal Auditors* (March 2011) published by the Treasury Board Secretariat’s Internal Audit Sector, Office of the Comptroller General, and The Committee of Sponsoring Organizations of the Treadway Commission Framework.

Appendix B - Risk Ranking of Recommendations and Audit Opinion

The following definitions are used to classify the ranking of recommendations and the audit opinion presented in this report.

Audit Recommendations

- Critical** Relates to one or more significant weaknesses for which no adequate compensating controls exist. The weakness results in a high level of risk.
- Essential** Relates to one or more significant weaknesses for which no adequate compensating controls exist. The weakness results in a moderate level of risk.

Audit Opinion

- Well Controlled** Only insignificant weaknesses relating to the control objectives or sound management of the audited activity are identified.
- Generally Acceptable** Identified weaknesses, when taken individually or together, are not significant or are compensated by mechanisms in place. The control objectives or sound management of the audited activity are not compromised.
- Requires Improvement** Identified weaknesses, when taken individually or together, are significant and may compromise the control objectives or sound management of the audited activity.
- Unsatisfactory** The resources allocated to the audited activity are managed without due regard to most of the criteria for efficiency, effectiveness and economy.