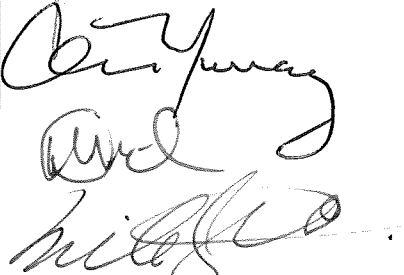




Hamilton

**CITY OF HAMILTON**  
**City Manager's Office**  
**Office of the City Manager**

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| <b>TO:</b>                | Chair and Members<br>Audit, Finance and Administration Committee   |
| <b>COMMITTEE DATE:</b>    | August 16, 2017  |
| <b>SUBJECT/REPORT NO:</b> | Management Action Plans for Use of External Consultant's<br>Audit Report Recommendations<br>(CM17015/FCS17075/PW17063) (City Wide)<br>(Outstanding Business List Item) |
| <b>WARD(S) AFFECTED:</b>  | City Wide  |
| <b>PREPARED BY:</b>       | Brigitte Minard 905-546-2424 x2297<br>Andrea McKinney 905-546-2424 x2261   |
| <b>SUBMITTED BY:</b>      | Chris Murray<br>City Manager<br><br>Dan McKinnon<br>General Manager, Public Works<br><br>Mike Zegarac<br>General Manager, Finance & Corporate Services                 |
| <b>SIGNATURE:</b>         |   |

**RECOMMENDATION**

- (a) That Report CM17015/FCS17075/PW17063, respecting the Management Action Plans for Use of External Consultant's Audit Report Recommendations, be received; and,
- (b) That the item respecting the Management Action Plans for the Use of External Consultant's Audit Report be considered complete and removed from the Audit, Finance and Administration Committee's Outstanding Business List.

## **EXECUTIVE SUMMARY**

Management appreciates the opportunity to respond to the findings of report AUD17008. After careful consideration of the findings, review of current status of process improvements and existing policies and By-laws, Management has developed a response to AUD17008.

Management acknowledges the findings of the report generally; noting Management had previously identified similar areas for improvement and had launched initiatives to proactively address them. Recognizing the audit sample spanned a number of years, current status was not necessarily reflected in the findings. A number of the recommendations are either underway or complete and the findings will be used to enhance these existing initiatives.

In this report Management will provide updates on the initiatives that were in the process of being implemented or may already be complete at the time of the Audit report's issuance. This includes specific process improvements that were implemented in Hamilton Water to address project management practices, that are being expanded in Public Works and then across the City. This report will also provide clarity on areas of procurement, such as the current Council approved definition of Consulting, as well as an update on the automated vendor management tool, which is now being implemented.

Specifically Management acknowledges that coding of accounts is an area that requires improvement from a process perspective.

## **Alternatives for Consideration – Not Applicable**

## **FINANCIAL – STAFFING – LEGAL IMPLICATIONS**

**Financial:** The implementation of these Management Action Plans for the Use of External Consultant's Audit Report will strengthen internal controls for finance, which may lead to savings and better value for money being achieved on expenditures on external consultants. Given a number of recommendations relate to in-flight initiatives and technology investments, there are no additional investments required at this time.

**Staffing:** The Management Action Plans for the Use of External Consultant's Audit Report will be implemented using the existing Council-approved staff complement.

Legal: None.

## **HISTORICAL BACKGROUND**

The Use of External Consultant's Audit Report (AUD17008) was discussed at the April 10, 2017 Audit, Finance and Administration Committee meeting and subsequently approved by Council. The report directed the Senior Leadership Team (SLT) to provide management action plans for the implementation of the recommendations contained in the audit report.

As acknowledged by the Director of Audit Services during the meeting, it is standard process for management to provide a management response at the time of issuance. This includes the opportunity to agree or disagree with an audit recommendation, provide rationale to support that decision, and the expected completion date (for recommendations that Management agreed with).

Given that Audit Services submitted the report prior to Management having the opportunity to provide action plans, Management, after careful consideration, is now requesting an amendment (for one recommendation) to Audit, Finance and Administration Report 17-005.

Report AUD17008 included a recommendation that the SLT provide the Audit, Finance and Administration Committee by the 2017 calendar year end the management action plans for addressing the implementation of the audit report recommendations. This report meets that requirement, provides additional information and is submitted to this Committee four months earlier than required by Council.

Management recognizes this audit spanned a number of years, including pauses in the work by the Audit Services Division. While Management agrees in principal with some of the findings, there are other components that either have been addressed or were being implemented when the report was released.

After consulting with the Director of Audit Services, Management understands that the reference to lack of a clear definition of consulting relates to awareness and understanding generally, versus a definition itself.

The definition of consulting is contained in the Council approved Procurement By-law and is regularly reviewed. The definition is:

“Consulting and Professional Services” means services rendered by members of a recognized profession or possessing a special skill. Such

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services are generally acquired to obtain information, advice, training or direct assistance.

## **POLICY IMPLICATIONS AND LEGISLATED REQUIREMENTS**

Procurement Policy By-law (17-064)

Procurement Policy By-law (16-070), since superseded by By-law 17-064

## **RELEVANT CONSULTATION**

- City Manager
- General Manager, Finance and Corporate Services
- General Manager, Public Works
- Director of Financial Planning, Administration & Policy
- Director of Financial Services
- Manager, Procurement

## **ANALYSIS AND RATIONALE FOR RECOMMENDATIONS**

Generally Management agrees with the findings, but notes that the Audit report captured a previous period in time and Management has been focused on improving processes and practices in the organization for a number of years, including upgrading through automation and standardization and development of a new governance model.

The audit completed was a Value for Money audit. The first and lead finding in the report related to “cost allocations”; while cost allocations are an accounting issue that needs addressing, it does not entirely align with the definition of a Value for Money Audit. Per the original report outlining the Value for Money Auditing Pilot (CM11006), “Value for Money (VFM) auditing (performance, efficiency and control) examines activities for efficiency and effectiveness.” Value for money can be more broadly defined in the following manner:

### **Definition of Value for Money**

There are three criteria to assess the value for money of government spending (i.e. the optimal use of resources to achieve the intended outcomes):

Economy: minimizing the cost of resources used or required (inputs) – spending less;

Efficiency: the relationship between the output from goods or services and the resources to produce them – spending well; and

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Effectiveness: the relationship between the intended and actual results of public spending (outcomes) – spending wisely.

*Source: National Audit Office, UK*

Management would like to provide context to the \$40 million Biogas/Digester project that was addressed in Report AUD17008. This is the project that was identified as having \$30.9M of costs incorrectly coded to consulting expenses in Report AUD17008 (Appendix “A” to Report AUD17008, page 4).

This project was partially eligible for an Infrastructure Stimulus Funding (ISF) from the federal and provincial governments. In order to access stimulus funding within the timeframes stipulated, Public Works leveraged a new procurement model, while working with Corporate Services, in a transparent process. The outcome was \$10 million in federal funding and \$10 million of Provincial funding (total of \$20 million in funding received) that was a direct offset to costs to the City.

The project approach was fully approved by Council (Reports FCS09052, FCS09052(a), FCS09052(b), FCS09052(c), FCS09052(d), FCS09052(e), FCS09052(g), FCS09052(i), FCS09052(j) and FCS09052(k)) and, as a result of the model used, staff was able to be complete the project within the tight completion timelines required by the Federal government to access the funding.

Management believes that leveraging federal funding to help complete a project that met its objectives and alleviates the City’s large infrastructure deficit meets the spirit and definition of “value for money”, particularly economy.

#### **Audit Management Action Plan Responses:**

Management appreciates the work of the Audit team, and believes that a number of the recommendation and observations in report AUD17008 are already being actioned, and in some cases are complete. Details are provided below.

Audit Report 2016-03 identified that the use of a business case or project charter is not consistently prepared to support the need to hire a consultant and/or to outline information such as roles or responsibilities of both internal and external project participants.

Management agrees that the use of project management tools such as business cases and project charters should be implemented consistently throughout the organization.  
Status:

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- Recognizing a large portion of the audit sample focused on projects in Hamilton Water, Management can advise that in 2014 a Project Management Office was launched in Hamilton Water to standardize project management processes and practices.
- This centralized function is designed to ensure consistency and compliance with respect to project management, accounting and compliance with corporate policy.
- Public Works (PW) is looking into options designed to ensure consistency and compliance in regards to project management across PW.
- A Project Management Community of Practice (COP) is also being established across the City.
- This COP will mirror the Continuous Improvement COP that was established by the Performance Excellence Office and is co-chaired by PW. The first session of the Project Management COP is expected to occur in Q4 2017.
- The Community of Practice for Project Management will guide staff and ensure project management processes and methodologies are enabled consistently across the City.

Business case templates that outline the rationale of projects and the use of external consultants:

- This is a component of the implementation of Multi-Year Budgeting Framework and Business Planning, which is currently underway.

Procurement is currently modernizing their processes, including implementing new software that automates the vendor management process (detail provided below in the response to audit recommendations).

Enhancing financial controls and monitoring:

Many of the actions identified in the Action Plans are related to financial controls such as standardizing and monitoring contingencies, gapping, budget variances and vendor performance.

Additionally, in 2016, a new corporate governance structure was developed that has now been implemented. Its primary focus for 2017 includes consolidating Business and IT Governance across the City, identifying areas where the City can improve and streamline corporate processes, supporting the implementation of Multi-year Budgeting, oversight of major strategy/project status reporting, and the creation of internal dashboards to increase monitoring of performance. This includes enhancing and updating processes related to business planning, business cases and reporting with appropriate documentation.

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Management Action Plans For Audit Report Recommendations:

**Recommendation 1. That the Senior Leadership Team (SLT) identifies roles and responsibility to set policy and oversee the use of consultants. This should include:**

The development of policies and procedures relating to the hiring of outside consultants, in conjunction with the procurement Policy. These policies should include the following:

- A clear definition of consulting;
- Guidelines on the preparation of business case justification and financial thresholds;
- Approval processes with specified dollar thresholds;
- Documentation and transfer of project knowledge;
- Documentation and approval for changes (e.g. scope, cost, timeline or deliverables);
- Performance measurement / vendor evaluation requirements;
- Action plans as a result of recommendations; and
- Reporting requirements (i.e. annual reporting to Council).

The development of a standard business case template for completion prior to engaging a consultant as part of the procedures. The business case should promote improved planning to minimize change orders for consulting engagements.

Policies, procedures and business case template requirements should recognize program versus project requirements and indicate at which point in the project lifecycle steps are captured.

Improved corporate tracking of the use of consultants for annual reporting to Council. This should detail the actual costs, type of spending and benefits received by the City.

Generally Management agrees with the themes that are identified for improvement as it relates to financial controls and processes. A significant amount of work has been underway, some of which is currently in the implementation phase.

1. A clear definition of consulting.
  - The definition of consulting is contained in the Council approved Procurement By-law and can be re-reviewed.

“Consulting and Professional Services” means services rendered by members of a recognized profession or possessing a special skill. Such services are generally acquired to obtain information, advice, training or direct assistance.

2. Guidelines on the preparation of business case justification and financial thresholds.

Approval processes with specified dollar thresholds are already governed by the Procurement Policy By-law, which is a publicly available document. The approval levels are disclosed in a transparent manner. Any items greater than \$250,000 (including procurement of the use of external consultants) are approved by Council either through the budget process or a Council report. Positions have specified levels of delegated signing authority that are enforced by Finance and Administration as an existing financial control for the organization.

Updates to business processes and the delivery of financial services were identified during the refresh of corporate governance in 2016. An overview of the corporate governance refresh was presented to the Audit, Finance and Administration committee on April 10, 2017 (presentation accompanying Report AUD17008, “Governance Update”). As part of the multi-year budget framework, a corporate-wide business case template for the budget process for enhancements/reductions was developed in 2016 and is currently being implemented. A process for more detailed business cases during the process is currently under development and is expected to begin implementation in fall 2017.

The Performance Excellence Office is working with Corporate Services to modify business processes and procedures. This will include the rollout of a business case template for the hiring of external consultants in a manner that includes both identification of risks and value for the organization. A corresponding business procedure will be developed and implemented to accompany this new business case template.

- Documentation and transfer of project knowledge.

Staff will develop and implement a documentation and knowledge transfer process.

- Documentation and approval for changes (e.g. scope, cost, timeline or deliverables).

Consistent project management practices address components of this recommendation. Additionally the City's new Governance model has created a body (the Business



Improvement Team) that is accountable for overseeing major project reporting with score carding. This will be further enabled by the consolidation of corporate services and the standardization of processes that is underway. Bringing together the resources that deliver traditional corporate functions, such as finance and procurement, into the same department maximizes the City's ability to enforce standard processes and procedures, as well as increases operational capacity for oversight.

To add context to findings on scope changes, one example of a project that experienced unique challenges was that of the Woodward Upgrade project which was identified as exceeding the original consultant's proposed cost. These additional costs were attributed to a unique situation related to the economic recession of 2008/2009. While this scope change was not documented in a single comprehensive memo, there was considerable reporting to Council about the issue through annual budget presentations and historical capital detail sheets showing the evolution of the project, and a report to Council (PW12060/FCS12064) outlining the revised plan. This ultimately endorsed securing a \$200M grant, which is entirely consistent with the value for money principal of "economy (spending less)".

The development of the community of practice for project management will help provide training to project managers to ensure that scope changes are properly documented with appropriate rationale. Expected completion: June 2018

- Reporting requirements.

Per the Capital Projects' Monitoring Policy (most recently approved with Report FCS14031), a Capital Projects Status Report is to be submitted by departments to their respective Committee of Council three times a year as of June 30<sup>th</sup>, September 30<sup>th</sup> and December 31<sup>st</sup>.

Reports to Council on the use of consultants will be considered by Corporate Services. This action requires further research and discussion with other municipalities to determine best practices. Finance will present the findings to Council for consideration before creating a new process. Expected Completion: June 2018

**Recommendation 2. That Procurement ensure that policies and procedures relating to contingencies be developed and investigate methods of automating contingency limits.**

Agreed. The guiding policy for Procurement is the Procurement Policy By-law. Procurement is currently conducting an investigation and attempting to benchmark the use of contingencies and the appropriate percentages with other public sector

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agencies. Recommendations will be brought through the Procurement Advisory Committee for consideration in the next Procurement Policy review at the end of 2017.

A related business procedure will be created to provide guidance for the development of contingencies and the responsibility of monitoring the contingencies included in procurements and approving exceptions that meet the criteria of the business procedure. Expected Completion: March 2018, or when the next Procurement Policy By-law is approved by Council.

**Recommendation 3. That Procurement investigates methods tracking vendor performance and incorporating past performance into the awarding of future contracts.**

Agreed. This item has partially been completed. It was previously identified internally as an area for improvement by Management. Procurement Policy #8 outlines the process to be followed for Vendor Performance Evaluation. Departments have used this policy to deal with issues of poor vendor performance and is a current practice, which has resulted in Council imposed bans on bidding. As of June 2017, there are eighteen active bans, four expired bans where the vendor is allowed to bid but the performance is being closely monitored, fifteen vendors who are on a "watch for" listing and eleven vendors who are not to be solicited for quotations.

The City of Hamilton's Procurement Section was the lead on a cooperative bid solicitation with participation from multiple municipalities and school boards for an electronic bidding solution. One of the requirements included in this procurement was a vendor performance module (technology solution) to capture and track vendor evaluation forms, and vendor performance incident forms.

The completed vendor performance evaluations will be used by Procurement to evaluate vendors per the current Procurement Policy (By-law 17-064). This work was well underway when the Audit Report was presented to Council, but was not included by the Audit Services Division.

This tool will automatically generate both a notice to complete vendor performance evaluations, as well as areas of non-compliance with a particular procurement that need to be addressed. The information was shared with the Audit team prior to the release of the Audit Report by Procurement.

The contract to acquire the software solution has been executed and new vendor performance module it expected to be launched in the third quarter of 2017. Procurement, with the assistance of the Procurement Advisory Committee, will then review and draft revisions for amendments to the Procurement Policy and procedures on the development of a Vendor Performance Program which will utilize the forms and

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possibly incorporate them in the award of contracts for Council consideration in the first quarter of 2018. The revised Procurement Policy and related procedures will be rolled out in 2018. Expected Completion: December 2018.

**Recommendation 4. That SLT assign responsibility to investigate a method of electronically tracking change orders for improved reporting and monitoring capabilities.**

Tracking change orders is a financial control where there is joint responsibility between Corporate Services staff that process payments and staff that are responsible for managing consulting contracts as part of their job duties. Corporate Services will investigate the electronic tracking of change orders. This will be part of a broader review of project portfolio management in the organization. Expected Completion: December 2018

**Recommendation 5. That Procurement provides guidance to staff on procurement issues identified on page 14 and incorporate oversight into random checks performed throughout the year.**

Already a current practice. Procurement currently performs random checks for compliance of Roster Proposals and invoices against the Roster Form of Submittals. Although the random checks are not an exhaustive review of all purchase orders issued under the Roster, it is conducted throughout the calendar year. Procurement is aware of the fourth instance of non-compliance indicated on Page 14 (fourth bullet) of the original Audit Report and it was reported to the Roster Committee as a non-compliance. If Council and the Procurement Advisory Committee would like to increase the frequency of this program, Procurement would require additional resources. Expected Completion: Not Applicable

**Recommendation 6. That Finance develops policies and procedures relating to the use of gapping. These documents should include a definition of gapping, approval requirements and how the use of gapping will be reported to the Senior Leadership Team and Council.**

Agreed. There are components of this that are underway that need to be enhanced. The "Budgeted Complement Control Policy" and the "Budget Control Policy" are the current policies that guide these processes. Any changes to expenditure types (e.g. from transferring funds from employee related cost to consulting costs or vice versa) are already addressed within these two existing policies. Practices already exist for reporting of gapping in the Operating Budget Variance Reports.

Corporate Services is currently investigating the processes for reporting and utilization of gapping across the organization for budget monitoring, variance analysis and

reporting. As part of the new Corporate Governance model and consolidation of resources, Corporate Services will be enhancing their variance reporting and forecasting methodology. A related procedure and/or policy will be developed as necessary once this review has been completed. Expected Completion: September 2017.

**Recommendation 7. That SLT ensure that a skills inventory is developed as part of the City's planned Talent Management System to support the People and Performance Plan. Guidance should be provided on business case analysis to identify potential opportunities to access services in more cost effective ways.**

Agreed. As communicated during the presentation at the Audit, Finance and Administration Committee on, April 10, 2017 the process to scope and implement a computer application for a skills inventory is underway. Consideration for linkage with business case analysis and accessing services in more cost effective ways will be considered as part of the application implementation process. This work is occurring in 2017, with Human Resources likely coming back to Council to request additional funding for capital investment.

Ultimately, it is staff's intention to have a skills inventory that the City can draw upon so there is a comprehensive understanding of the skills and expertise contained in the organization. This will enable the City to draw upon our own expertise when capacity and workload can be realigned in certain circumstances. This will also require understanding the feasibility of shifting workload, capacity demands and impacts to service delivery before execution. Expected Completion date: December 2018

**Recommendation 8. That SLT identify opportunities for insourcing and cost savings.**

Agreed. This work is already occurring in the organization. SLT considers this as a regular part of both their individual portfolios and collectively. For example, in-sourcing has already been completed in Legal Services, which realizes annual savings of \$1.3 million dollars (when comparing 2016 costs to 2012 costs) through the reduction of external legal costs. There are a number of additional areas that leadership has been exploring. Expected Completion: Ongoing

**Recommendation 9. That Roster Captains with support from Procurement, work to identify opportunities to obtain better value for money for consultants hired with similar skills and / or to perform the same work year over year.**

Agreed. This recommendation will be brought to the Roster Committee for discussion and to determine if a process can be developed to identify opportunities to obtain better

value for money. Procurement will lead this process, utilize the input from the Roster Committee and implement a solution that is consistent with modern public sector procurement standard practices. Expected Completion: December 2017.

**Recommendation 10. That Finance creates a standard dictionary for all project and account codes to ensure consistent classification of charges across the organization and that Finance staff ensure that invoices are allocated accordingly. This should outline when to allocate costs to an operating versus capital account.**

The overall recommendation is reasonable; however, management respectfully disagrees with content contained in the original report for the Biogas/Digester (Energy Recovery) project regarding coding. The purchase order was issued to a consulting engineering firm, it was coded to a consulting account. Per the current, Council-approved definition of consulting, these expenses meet the criteria of consulting as the work issued on the purchase order to a recognized profession (engineering) in the form of an engineering consulting firm. Going forward, the approach to coding of that type of model will be reviewed.

Corporate Services will also investigate the development of a standard dictionary of account codes and will review definitions of capital and operating expenses. Given that Corporate Services is currently in the midst of rolling out new operating budget software and a new Multi-Year Budgeting and Business Planning process, this standard dictionary development will occur when more capacity is available in Corporate Services so that this work can be in-sourced. Procurement can also consider if the definition of a "consultant" is sufficient as part of the next Procurement Policy review that will be occurring at the end of 2017. Expected Completion: September 2018.

**Recommendation 11. That Finance work with operating groups to appropriately plan for consulting expenses through the budgeting process.**

Agreed. Operating and capital budgets are developed, monitored and managed at the Division level within each Department. The Corporate Services Department's Finance and Administration staff work with all areas in the organization throughout the year to plan, develop, and monitor budgets. There will be an increased emphasis on consulting expenses during the 2017 budget monitoring and variance reporting processes. Any budget changes related to this work will be highlighted in budget presentations during the 2018 Budget Process. Expected Completion: March 2018.

**Recommendation 12. Budgets assign consulting budgets at the department level. With the exception of consulting costs to cover staffing resource limitations, General Manager approval should be obtained for use of the consulting budget.**

Disagreed. The process should remain aligned to the approved levels of delegated authority, which is a standard business best practice. General Manager approval is and should continue to be obtained when this level of signing authority is required. It would be inefficient and overly bureaucratic for a General Manager to be required to approve small dollar consulting costs when other members of the organization have had this authority delegated to them. Assigning consulting budgets solely at the department level removes accountability from Divisions and Directors, disempowers the management team broadly, and could expose the organization to unnecessary risk.

Consideration will be given to outlining the importance of value for money in consulting dollars for all individuals with signing authority in the organization. This will include re-training during the business case implementation process.

#### **ALTERNATIVES FOR CONSIDERATION**

Not applicable

#### **ALIGNMENT TO THE 2016 – 2025 STRATEGIC PLAN**

##### **Our People and Performance**

Hamiltonians have a high level of trust and confidence in their City government.

#### **APPENDICES AND SCHEDULES ATTACHED**

None.