Following the Cash:

Exploring the Expanding Role of Canada's Auditor General

Roger Gibbins, Ph.D.

Loleen Youngman Berdahl, Ph.D.

Katherine Harmsworth

October 2000

Canada West Foundation

ISBN# 1-895992-75-3.

CANADA WEST FOUNDATION
P.O. BOX 6572, Station D
Calgary, Alberta T2P 2E4
Ph: 403-264-9535
Fax: 403-269-4776
www.cwf.ca

Introduction

Since 1867, Canadian federalism has been defined by continued debates on the appropriate role of the federal and provincial orders of government. While the Constitution Act of 1867 clearly identifies areas of federal and provincial jurisdiction, the 20th century practice of federal transfers for provincial programs gave rise to significant overlaps and a "muddying" of authority.[1] Perhaps the most visible example of this muddying is Canadian health care. Health care falls into the provincial jurisdiction, but the federal government transfers revenues to the provinces to help finance the programs. In exchange for receiving these funds, the provinces agree to meet the conditions outlined in the Canada Health Act. Thus, by using its spending power, the federal government has been able to effectively expand the scope of its activities beyond those outlined in the formal division of powers. In so doing, the federal government strongly influences the direction of provincial policies, but does not assume the responsibility to establish or provide provincial programs, nor does the federal government bear the burden of responsibility for the quality and performance of these provincial programs.

Not surprisingly, these federal ventures into provincial territory create significant public policy debates. Some critics, including provincial governments, question the appropriateness of the federal government's efforts to expand its role through the use of its spending power. This question is being raised again in response to the recent expansion of the role of the federal Auditor General. As this report will demonstrate, changes over the last 25 years have led to the possibility of the Auditor General using accountability arguments to increase the federal government's role in areas of provincial jurisdiction.

Federal ventures into provincial territory create significant public policy debates. Some critics, including provincial governments, question the appropriateness of the federal government's efforts to expand its role through the use of its spending power. This question is being raised again in response to the recent expansion of the role of the federal Auditor General.

Recent positions taken by the Auditor General of Canada, L. Denis Desautels, suggest that it is not only possible, but probable that accountability arguments will be used to expand the federal role. In the November 1999 Report of the Auditor General of Canada, Desautels drew attention to potential "accountability" problems posed by new collaborative arrangements between the federal and provincial governments, and with organizations in the private and voluntary sectors. Examples of these new arrangements included Labour Market Development Agreements between the federal and provincial/territorial governments, the National Child Care Benefit, and the Canadian Millennium Scholarship Foundation. Desautels argued that such arrangements "…can erode the ability of Parliament to scrutinize the use of federal power and the right of citizens to accountable government" (OAG, 1999b: 18). He voices the same concerns with federal support for health care delivery: "Parliament cannot readily determine the extent to which each province and territory has satisfied the criteria and conditions of the *Canada Health Act"* (OAG, 1999b: 50). In short, Desautels believes that Parliament requires better information on how provincial and territorial governments are using federal funds.

In the Auditor General's opinion, a transfer of revenues does not imply a transfer of accountability:

> The creation of the partnering agreement does not reduce the accountability of the federal government to Parliament for the use of federal funds and authorities. Since the accountability relationships are more complex, the federal partner needs to ensure that the arrangement is structured so that there is an appropriate level of reporting back to ministers and Parliament (OAG, 1999a: 5-16).

What happens if the OAG decides to follow federal cash through to provincial program delivery? What are the implications for our broader understanding of contemporary federalism?

Desautels' implication is clear: provincial governments should report in some fashion through federal ministers for their expenditure of federal funds even though, as in the case of health services, the funds are spent within the jurisdictional domain of provincial governments. If the federal government's accountability in partnership relations is to be met, "the federal partner is responsible for organizing and managing the relationships with its partners so that it can *obtain necessary information, monitor results and make (or require) adjustments as needed* (emphasis added)" (OAG, 1999a: 5-16). Clearly, this presents significant opportunity for an expansion of the federal role in provincial jurisdictional areas.

In a narrow sense, Desautels' position can be seen as a logical extension of the 1876 legislation that created the Office of the Auditor General (OAG), legislation designed to ensure that Parliament could hold federal agencies accountable for the expenditure of public funds. At the same time, this line of argument posits a centralizing role for the Auditor General that was not envisioned in the initial legislation, *and one which may be at odds with conventional understandings of federal theory and practice.* What happens, then, if the OAG decides to follow federal cash through to provincial program delivery? What are the implications for our broader understanding of contemporary federalism?

This paper explores how the role of the federal Auditor General has expanded since 1975. Our goal throughout is to understand the emerging centralizing role of the OAG, and to encourage informed public debate about the nature of that role. As will be demonstrated, this expansion has important public policy implications, and goes to the heart of key questions about the nature of Canadian federalism at the start of the 21st century.

Research Questions and Methodology

To assess any changes in the role and practice of the federal Auditor General, the following questions must be answered:

- How have the Auditor General's legislative guidelines changed over time?

- What is the Auditor General's institutional capacity? Are we dealing with a skeletal office with a limited capacity to affect the larger dynamics of Canadian federalism, or are we dealing with an office with sufficient institutional capacity – resources, staff, public credibility, and visibility – to significantly shape those dynamics?

- How have various Auditor Generals defined their roles? How have such definitions changed over time?

- How has the Office of the Auditor General (OAG) addressed its legislative mandate? Of particular interest here will be the manner in which, over the years, the OAG has redefined accountability.

- What are the centralizing aspects of the OAG? How are federal principles reconciled with the principles of financial accountability?

To answer these questions, the Canada West Foundation conducted an extensive review of related legislation, annual reports and related literature.

The Role of the Auditor General

The issue of accountability is important at all levels of government. The revenues spent by governments are *public funds* – that is to say, funds raised from the general public and spent by governments on behalf of the public. Thus, although we may refer to "federal monies" or "provincial revenues," all these funds in fact are public. Governments act as trustees, and are

The revenues spent by governments are public funds – that is to say, funds raised from the general public and spent by governments on behalf of the public. Thus, although we may refer to "federal monies" or "provincial revenues," all these funds in fact are public. Governments act as trustees, and are not owners of the funds.

Generating Public Monies:
Canadian Federalism and Fiscal Imbalance

At the time of Confederation, it was thought that the powers given to the provinces were minor, requiring few fiscal resources. For this reason, the federal government was given the right to use any form of taxation (direct or indirect), whereas the provincial governments were restricted to direct taxation. Direct taxation was understood to primarily include income tax (a highly unpopular form of taxation not used in Canada in 1867), sales taxes and property tax. Overall, a fiscal imbalance was created in the Constitution, with the federal level having access to significantly greater forms of revenue than the provinces.

Much has changed since 1867. First, both the federal and provincial governments have lost their aversion to the use of income taxes. Canadian citizens pay income taxes to both federal and provincial governments; at present, approximately six out of every ten income tax dollars go directly to the federal government, with the remainder going to the provincial governments according to the residency of the taxpayer.[2]

Second, with the advent of the social welfare state, the provincial jurisdiction over health, education and social welfare has become highly important. Indeed, many of Canada's key policy debates concern matters falling within provincial jurisdiction. These program areas are among Canada's most expensive – by no means "minor," as believed in 1867.

The result of these two changes is a large imbalance between revenue needs and spending power. The provinces have jurisdiction over the most expensive policy areas, yet have fewer revenues. The federal government has fewer expensive policy areas, but a large pool of revenues. Not surprisingly, a system of intergovernmental transfers has developed.

It should be noted that both court decisions and modern taxation practices have rendered the concept of "indirect taxation" meaningless. Canada's key tax sources – income tax, sales taxes, and payroll taxes – are accessible to both orders of government. Thus the modern fiscal imbalance reflects historical patterns, rather than constitutionally entrenched realities. While theoretically provinces could raise income and other taxes to cover their jurisdictional expenses, and thus be able to reject federal transfers, the reality is that taxpayers will only tolerate so much. Thus, correcting the fiscal imbalance would require significant reductions in the federal tax "take," with provinces then claiming the available tax room. A second alternative would be the transfer of provincial powers to the federal level.

Clearly, neither option is likely to appeal to both orders of government. For this reason, it is likely that fiscal imbalance and federal transfers will define Canadian federalism in the years ahead.

At the federal and provincial levels, independent and impartial auditor offices have been established to ensure that governments are accountable for the use of public funds. These auditors review how their respective governments spent public funds, and report on whether the money was used as intended.

not owners of the funds. Governments must be responsible to the public and spend funds in a manner that meets public intention and approval. This involves two stages. First, a government must seek the approval of Parliament (if federal) or its legislature (if provincial) before collecting or spending money. Second, a government must allow for an annual independent review of how funds were spent (OAG, n.d.).

At the federal and provincial levels, independent and impartial auditor offices have been established to ensure that governments are accountable for the use of public funds. These auditors review how their respective governments spent public funds, and report on whether the money was used as intended. At the federal level, this office is known as the Office of the Auditor General of Canada. At the provincial level, the chief public auditor is known as either the Auditor General of [province name], or the Provincial Auditor. For clarity, in this paper all references to the "Auditor General" refer to the federal level, unless otherwise noted.

The Evolving Legislative Mandate of the Office of the Auditor General

The legislative history of the OAG from 1855 to present is one of increased responsibilities and powers. In 1855, an act "to secure the more efficient Auditing of Public Accounts" established a Board of Audit with an auditor and two other members. The new Auditor General's duties included auditing all public institutions, financial control, issue and record expenditures, and the keeping of public accounts. To ensure independence, the new Auditor General was ineligible to sit in either house of the Legislature.

What is particularly noteworthy about the debates leading to the 1977 revision is the absence of debate about the centralizing role of the OAG.

Table 1 outlines the major revisions to the Auditor General's role since 1855. A general pattern of expanding audit powers is clear, although a distinction between distributing public monies and reporting on the use of these monies was set in 1931, when the separate government position, the Comptroller of the Treasury, was created to be responsible for issuing cheques (OAG, n.d.). The most recent major revision to the OAG, which occurred in 1977, again expanded the powers of the Auditor General.[3] This expansion did not occur without public debate, however. In the years leading up to the 1977 Auditor General Act, a growing controversy surrounded the appropriate boundaries to the autonomy of the OAG. This controversy also included the OAG's limited capability to audit programs due to staff and budget restrictions, and the usefulness of the role of the Public Accounts Committee (PAC) in the Auditor General's annual reports (Sutherland, 1981: 192).

What is particularly noteworthy about the debates leading to the 1977 revision is the absence of debate about the centralizing role of the OAG. Despite the fact that massive financial transfers from the federal government to the provincial and territorial governments now defined the Canadian welfare state, *there was no suggestion that the scope of the OAG should be expanded to include oversight of provincial program delivery in fields of provincial jurisdiction.*

Legislation passed in 1977 mandated the Auditor General to call attention to anything from his examinations that he considered should be brought to the attention of Parliament.

Table 1:
Major Changes in the Legislative Mandate of the Office of the Auditor General

Year	Legislatively Mandated Responsibilities and Powers
1855	Auditing all public institutions Financial control Issue and record expenditures Keeping of public accounts
1878	***Additional duties:*** Authorization of payments of every public officer who received public monies Examination of all accounts forming the Consolidated Revenue Fund (CRF) Examination of any other public accounts of the Treasury Board related to the Dominion of Canada Audit activities of Minister of Finance Countersign all annual public accounts Ensure effective parliamentary control
1886	***Additional duties:*** Auditing every appropriation account within the public service Examine, direct and certify appropriation accounts ***Revoked duties:*** Countersign all annual public accounts
1931	***Additional duties:*** Call attention to any case where money was expended outside conditions of a grant Call attention to any case where an objection of the Auditor General was overruled by the Governor in Council or Treasury Board (Dominion Law Reports, 1986: 229).
1967	***Revoked duties:*** Inquire into and report on matters related to the financial affairs of Canada Note: reporting of improper retention of funds redirected to Treasury Board rather than Minister of Finance
1977	***Additional duties:*** Call attention to anything from examinations that he considered should be brought to attention of Parliament Report cases where money has been expended without due regard to economy or efficiency

On July 14, 1977, "An Act respecting the office of the Auditor General of Canada and matters related or incidental thereto" was passed by the House of Commons. This Act mandated the Auditor General to call attention *to anything* from his examinations that he considered should be brought to the attention of Parliament (ss. 5, 6, and 7 s-s 7(1)). The Auditor General's previous duties were carried forward as well. The Act specifies the types of cases that should be included in the Auditor General's report, the most significant being cases where money has been expended without due regard to economy or efficiency. The Auditor General was also charged with examining financial statements within the Financial Administration Act, and any other statement that the President of the Treasury Board or the Minister of Finance may present for audit. The Auditor General is entitled to access documents by s. 13 of the Act. This gives him the power to require such information, reports and explanations from the public service of Canada as he deems necessary for the fulfillment of his responsibilities. In order to carry out the duties of the OAG, the Auditor General has control over personnel management and is entitled to place his employees in any department he deems necessary.

Overall, it is clear that the legislatively mandated role of the OAG has expanded greatly since 1855. However, the expansion of powers has related only to the Auditor General's role in auditing public monies spent by the federal government, and has *not* been formally expanded to include provincial spending. Thus, the expansion of the Auditor General's centralizing role has not occurred in response to legislative change.

Overall, it is clear that the legislatively mandated role of the OAG has expanded greatly since 1855. However, the expansion of powers has not been formally expanded to include provincial spending.

Institutional Capacity of the OAG

The Auditor General is more than an individual; "he" is also an office – the Office of the Auditor General – and a public institution. It is important to ask, therefore, about institutional capacity. Simply put, does the Auditor General have the institutional capacity to make waves within the federal system, should he choose to do so, or is he a player at the margins with the capacity to create only the occasional ripple? The answer to this question is of considerable importance in assessing the Auditor General's *potential* centralizing role.

There are many aspects to institutional capacity, only some of which can be discussed here. We have already observed that the legislative mandate of the Auditor General facilitates but does not dictate an expansive role. A second aspect of institutional capacity relates to budget and staff. Here, Table 2 provides some useful information. Total expenditures grew rapidly from the mid-1970s to the mid-1980s, and then grew more slowly before hitting a peak of

Table 2: Office of the Auditor General Budgetary Capacity				
Years	Personnel Average[4] ($ 000)	Change in Five Year Average (%)	Total Net Expenditures Averages ($ 000)	Change in Five Year Average (%)
1970-74	4,256	--	4,772	--
1975-79	11,159	162	18,631	290
1980-84	24,107	116	35,540	91
1985-89	32,704	36	46,668	31
1990-94	41,682	28	57,000	22
1995-99	30,804	-26	41,089	-28

Source: Public Accounts of Canada, Summary Tables

If there has been a recent expansion in the centralizing role of the Auditor General, this has not been reflected in net institutional capacity.

$58.4 million in 1993-94. By contrast, total expenditures had fallen to $49.3 million by 1996-97, and then rebounded to only $53.7 million by 1998-99.

It is clear that the OAG is not a small institutional player in absolute terms, although it may appear so relative to total federal expenditures and the scope of the OAG's mandate. There is a capacity "to make centralizing waves" should there be an inclination to do so. It is also clear, however, that the OAG's institutional capacity has not increased dramatically over recent years. The percentage increase in personal costs and total expenditures over the last ten years, calculated in absolute terms without accounting for inflation, has been only 9.8% and 2.1% respectively. This is well short of explosive growth. If there has been a recent expansion in the *centralizing* role of the Auditor General, this has not been reflected in net institutional capacity. At the same time, it is important to remember that the Auditor General has considerable discretion with respect to where resources will be deployed. Thus, an increased OAG interest in provincial matters need not require a net increase in institutional resources.

Another aspect of institutional capacity is the combination of public visibility and political credibility. There is little question that Auditor Generals have staked out a position capable of moral suasion and leadership. Given an inherent public wariness of government expenditures, Auditor Generals command an attentive public audience and an exceptionally attentive audience among opposition MPs as well as the general public. As a consequence, their influence is not entirely dependent on more mundane organizational resources such as staff and money. With respect to the centralizing aspects of the Auditor General's role, the non-partisan reputation of the Auditor General and the high public esteem in which he is held means that it would not be easy for provincial governments to shrug off any public criticisms emerging from the OAG. Thus, for example, criticisms of provincial health care delivery leveled by the Auditor General might carry more weight than similar criticisms by the federal Minister of Health; the latter are easier to dismiss as "political" or "partisan" than are the former.

The Practice of the Auditor General's Office

It is important to note the discretionary nature of the Auditor General, who is not simply a creature of his legislative mandate. Auditor Generals have approached the definition of their roles and the construction of public profiles in quite different ways. There has been ample scope for self-promotion (of an institutional character), for building (or not building) a public profile, and for articulating (or not articulating) a centralizing role for the OAG beyond what one might find in the relatively sparse language of the legislative mandate. In addition, the mandate gives the Auditor General significant latitude in the scope and nature of his inquiries. The Auditor General cannot annually ride herd on all aspects of the federal government; he must of necessity pick and choose. Therefore, the adoption of a *centralizing* role is, to a degree, a matter of individual choice rather than a matter of legislative mandate. We should stress, however, the qualification "to a degree," for it may also be that the accounting principles adopted by the Auditor General may in themselves promote a centralizing role.

The non-partisan reputation of the Auditor General and the high public esteem in which he is held means that it would not be easy for provincial governments to shrug off any public criticisms emerging from the OAG.

It is clear from a survey of twenty-five annual reports that the Auditor General, as an individual, plays a large part in shaping both the role of the Auditor General and the Office of the Auditor General. James J. Macdonell, Auditor General during the 1970s, is a notable illustration. One only needs to look at the Auditor General Act of 1977 to see Macdonell's own vision of the OAG. As his predecessor wrote, "The vision, innovative thinking and driving energy of James J. Macdonell fuelled the initial development of comprehensive auditing in Canada." As we shall discuss shortly, it is the principles of comprehensive auditing, combined with the manner in which individual Auditor Generals have defined their roles, that have led to the emergence of a more centralizing OAG role.

Ken Dye not only continued the development of comprehensive auditing during his tenure as

Auditor General, but also left an indelible mark. Although Macdonell conceived the concept of comprehensive auditing, the implementation and application of this auditing technique fell to Dye. He implemented comprehensive auditing as a working reality throughout government and strove to make value for money auditing (VFM) effective to meet the needs of Parliament. Furthermore, Dye struggled to ensure that the OAG had unlimited access to information. As Denis Desautels wrote in his 1991 inaugural annual report:

> James J. Macdonell translated his vision of comprehensive auditing into a new Auditor General's Act. He reaffirmed the role of the Office as an independent legislative auditor and established the basis for the development of new audit methodologies. Kenneth M. Dye continued with the development of comprehensive auditing. Under his tenure the Office's credibility and recognition by the Canadian taxpayers became well established. His term was characterized by many accomplishments in the international sphere, in the accounting profession, in the government, and within the Office (OAG, 1991: 15).

Attest auditing (also known as financial auditing) involves an audit of the federal government's annual financial reports. (These include all federal agencies, departments and Crown corporations.) The OAG selects a random sample of reported amounts and disclosures from each department and agency, and then collects the evidence necessary to confirm the reliability of the statements. In this way, the OAG is able to comment on the overall reliability of the government's financial statements. Attest auditing focuses on reliability, consistency and fairness of presentation.

In 1991 Desautels outlined two main issues for his own term of office. The first issue centred on the effective management of programs in areas where different orders of government are involved. The second issue concerned accountability and the accounting of results. As is apparent in his 1999 Annual Report, the management of collaborative programs between the federal and provincial governments, and the related issue of accountability, continue as predominant themes in Desautels' definition of the OAG. The point to stress in the present context is that the federal-provincial focus was a matter of choice; a different Auditor General might well have pursued quite different targets, and perhaps targets with less serious implications for federal governance.

Traditional Versus Comprehensive Auditing

The increased centralizing role of the OAG is in part promoted by the accounting principles adopted by recent Auditor Generals. Prior to the 1977 Auditor General Act, the OAG used two forms of audit: attest auditing and compliance auditing (see sidebars).[5] Both attest and compliance auditing are based on hierarchical accountability: the subordinate party answers to the higher authority. Since the 1977 Auditor General Act, the OAG has used three forms of audit: attest auditing, compliance auditing and value for money (VFM) auditing. When value for money auditing is combined with attest and compliance auditing, the entire audit system is referred to as comprehensive auditing (see Figure 1.)

Value for money auditing (also known as performance auditing) involves an examination of systems and results. The Auditor General examines programs and departments to ensure that due attention has been paid to the "three Es" – effectiveness, efficiency and economy. Effectiveness refers to the extent to which a program meets its objectives, and is measured through program evaluation. Efficiency refers to productivity levels and management techniques, and is measured through performance measure systems. Economy refers to the program costs. Because the concepts of effectiveness, efficiency and economy are broadly defined, VFM audits involve matters not traditionally seen as "financial." These include auditing leadership techniques, values, ethics, the appropriate and relevance of decisions, and management direction. These "non-financial" dimensions mean that the VFM audits require broader methodologies, and therefore may require greater access to information. With VFM auditing, accountability is based on agreements: partners answer for performance and accomplishments in relation to agreed upon objectives.

Taken together, comprehensive auditing principles invite OAG commentary on government policy and policymaking.

The Shift to Comprehensive Auditing

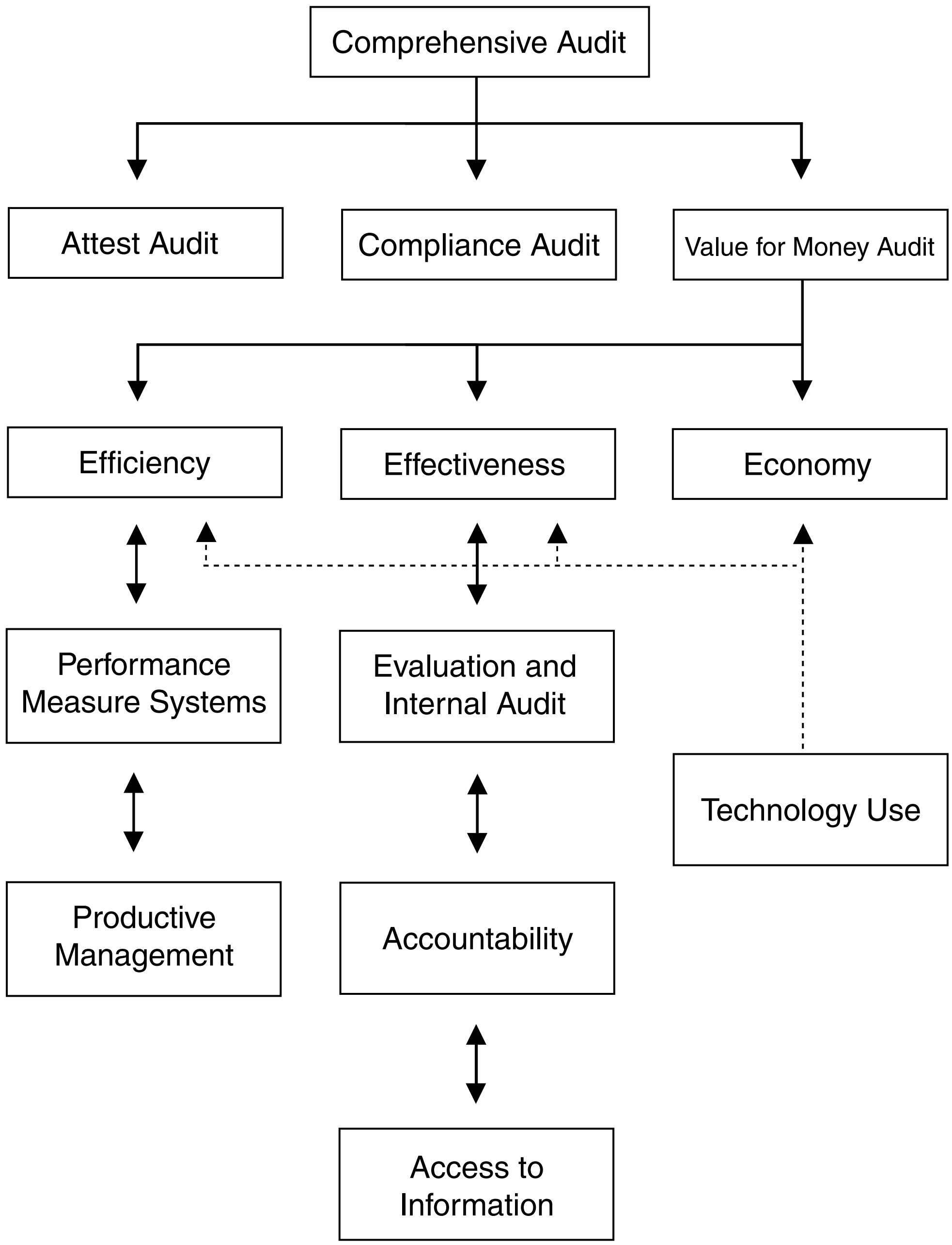
At first blush, there may appear to be little connection between the auditing principles and practices adopted by the OAG and the operation of the Canadian federal state. However, it is difficult to make sense of the changing character of the OAG, and to make sense of its potential centralizing role, without first paying close attention to auditing principles. Although many might assume that a huge gap exists between the world of accountants and the political world of federal politics, the OAG has closed this gap dramatically.

As noted earlier, the responsibilities and power of Auditor General were expanded by the 1977 Auditor General Act. The Auditor General is now responsible for reporting annually to the House of Commons on the work of his office. He is to report on "anything that he considers to be of significance and of a nature which should be brought to its attention." Moreover, the

***Compliance auditing* involves an audit of an individual department's or agency's compliance with its governing laws and regulations. This involves checking the spending authority contained in the annual budget and relevant legislation.**

***Value for money auditing* (also known as performance auditing) involves an examination of systems and results. Because the concepts of effectiveness, efficiency and economy are broadly defined, VFM audits involve matters not traditionally seen as "financial." These "non-financial" dimensions mean that the VFM audits require broader methodologies, and therefore may require greater access to information.**

Figure 1:
Comprehensive Auditing Overview



Auditor General is to report "cases which he has observed that money has been expended without due regard to economy or efficiency" (Dominion Law Reports, 1986: 230). This is the statutory expression of the emergence of *value for money auditing.*

This new legislation opened the way for an increased reliance on the audit of systems, and a redirection of the audit interest and concern towards economy, efficiency, and effectiveness (Balls, 1978: 616). As Auditor General Ken Dye stated in 1984:

> It has become evident that to know "how much" is being spent does not necessarily answer the question of whether it is being spent for the purposes intended and whether value is being received. Public concern for greater accountability and value for money demands more than traditional attest and financial authority auditing… (OAG: 1984: 12).

This departure from traditional auditing practices to comprehensive auditing has shaped both the role of the OAG and the role of the Auditor General himself. The VFM auditing framework concepts of *efficiency, effectiveness*, and *economy* act as overarching themes which flow into concerns about evaluation, accountability, internal audits, access to information, accounting practices, and technology, especially performance measure systems. They also shape discussions on public policy issues and productive management issues such as leadership techniques, values, and ethics. Clearly, the emergence of comprehensive auditing expands the scope of the OAG's activities in a dramatic way.

It is difficult to make sense of the changing character of the OAG, and to make sense of its potential centralizing role, without first paying close attention to auditing principles.

How and why did Canada move from a more traditional and limited auditing approach to the expanded principles of comprehensive auditing? The chronological history of comprehensive auditing in Canada proves the point that the role of the OAG in many ways reflects the vision of the persons holding the position of Auditor General (see Table 3).

The expanded role of the OAG, as mandated in the 1977 Auditor General Act, reflected the vision of then-Auditor General James J. Macdonell. Macdonell wished to improve financial information, conduct systems-level investigations, improve internal audits and reliable instruments of financial control, and create a role for central leadership in order to achieve higher standards of financial management. In his tenure, Macdonell established the

Table 3: The Evolution of Comprehensive Auditing in Canada	
Period	**Evolution of Comprehensive Auditing**
1978-1981: Establishing the Comprehensive Auditing Framework Auditor General James J. Macdonell	Framework for comprehensive auditing established ("FRAME"). This framework guided comprehensive auditing for years ahead. Three pillars for improved resource management outlined to "help managers manage" economically, efficiently and effectively. These pillars guided VFM auditing specifically.
1981-1991: Developing and Expanding Comprehensive Auditing Auditor General Ken Dye	Expanded methodologies of VFM auditing, which led to increased need for OAG access to information. Resolution of legal dispute over access to information solidified expanded OAG role. Improved quality of data collection. Enhanced technologies allowed for more detailed accounting and faster access to information.
1991-Present: Increasing the Public Role of the OAG Auditor General Denis Desautels	Emphasis on use of VFM auditing. VFM auditing necessitating OAG commentary on public policy and policymaking.

framework that would guide comprehensive auditing for years ahead.

Ken Dye, who became Auditor General in 1981, devoted his ten-year leadership to developing comprehensive auditing. In his 1984 report, Dye expanded on the concept of value for money auditing:

> In essence, it involves establishing reasonable criteria for the efficient and economic operation of a particular entity by evaluating the actual performance of the organization in terms of those criteria, then providing an opinion as to whether due regard for value for money has been demonstrated (OAG, 1984: 6).

The expanded methodologies of VFM auditing by definition create a need for greater access to information. According to Dye, access to information, both financial statements and departmental evaluations, was important not only to the OAG but also to Members of

Parliament. To ensure this access, Dye worked on improving the quality of data. In the mid-1980s, Dye focused on the integrity of evaluations and financial statements. In 1985, he recognized the necessity to change accounting practices in order to improve financial information and to have relevant and timely financial information (OAG: 1985: 7). This led the way to the implementation of accrual accounting in the early 1990s.

The access to information issue also led to a legal dispute concerning the expanded role of the OAG. During an audit of Petro-Canada, a Crown corporation, and its acquisition of Petrofina Inc., the Auditor General was denied access to documents he deemed necessary for conducting a proper audit. Although the declaratory judgement was in favour of the right of the Auditor General to access any and all information he deems necessary to conduct his audit, it was later overturned by the Federal Court of Appeal. The Supreme Court of Canada affirmed the Federal Court's decision. In other words, the Supreme Court agreed that the Auditor General Act should be narrowly construed. If the judgement had been upheld, it would have placed the importance of the roles of the Auditor General and value for money auditing above the importance of Cabinet secrecy (Dominion Law Reports, 1986: 234), and would have clarified that every act of Parliament is subject to the scrutiny of the OAG.

The present Auditor General, Denis Desautels, has emphasized VFM auditing for much of his tenure.

During his tenure, Dye firmly established comprehensive auditing within the federal government. It became clear in the 1980s that VFM auditing created a significantly larger scope for the OAG. At the same time, measurement systems improved as the supportive technologies evolved in the 1980s. The rapid development of technology has important ramifications for the OAG for it allows for more detailed accounting and faster access to information.

The present Auditor General, Denis Desautels, has emphasized VFM auditing for much of his tenure. In his 1991 annual report, Desautels voiced his concern over the deficit, and identified a need to focus on results in the administration of public affairs. These two priority areas fall within the VFM auditing framework. "Measuring outputs (efficiency) and the outcomes (effectiveness) of program activities would appear to be a precondition for moving from a regime of central control," wrote Desautels (OAG, 1991: 16). Concerns over information for Parliament, developments in information technology, the importance of internal auditing practices, and program evaluation continue to mark annual reports of the Auditor General throughout the 1990s.

So, where does value for money auditing stand in the year 2000? The VFM auditing practice annually yields four reports with about 35 individual chapters each. The audits range across studies of entities, sectoral programs and government wide issues (OAG, 1997). A recent value-for-money audit manual, released by the OAG in January 2000, has refined some of the concepts inherent in VFM auditing. To begin, the official definition of VFM auditing is:

> A systematic, purposeful, organized and objective examination of government activities. It provides Parliament with an assessment on the performance of these activities; with information, observations and recommendations designed to promote answerable, honest and productive government; and encourages accountability and best practices. Its scope includes the examination of economy, efficiency, cost-effectiveness and environmental effects of government activities; procedures to measure effectiveness; accountability relationships; protection of public assets; and compliance with authorities. The subject of the audit can be a government entity or activity (business line), a sectoral activity, or a government-wide functional area (OAG/CESD, 2000: 4).

It is currently recognized by the OAG that VFM auditing requires commentary on government policy and policy making.

It is currently recognized by the OAG that VFM auditing requires commentary on government policy and policy making. It is noted that audits should examine the implementation rather than the formulation of policy and should not question the merits of government programs. But it is also apparent that the OAG does wield significant public policy power. The Audit Manual states:

> The AG's mandate and role as servant of Parliament requires him to bring to the attention of Parliament, and thus the public any matter that he deems relevant to the exercise of his responsibilities. To this extent at least, the AG can legitimately play a role in shaping the public policy debate (OAG/CESD, 2000: 6).

And, of course, most contemporary public policy issues have a significant federalism or intergovernmental dimension.

To summarize, the Auditor General Act of 1977 is a loosely worded document that gives the Auditor General the power to decide what, how and when to audit. The technical interpretation and application of the law is left solely to the Auditor General (OAG/CESD, 2000: 7). When the broad interpretation of the AG Act is combined with the latitude of VFM auditing, including the OAG's ability to comment on public policy and access to information, there is no question that the Auditor General's role has expanded significantly over the past 25 years.

After nearly fifteen years of development, the methodology of the comprehensive audit "uses techniques from the fields of social sciences, management consulting, management sciences and engineering, and merges them into the discipline of auditing" (OAG/CESD, 2000: 37). The evolution of comprehensive auditing included a shift from system-based auditing to results-based audit practice and a review of individual programs that cross departmental lines, with shared responsibilities. The pursuit of efficiency, effectiveness and economy is vigorous and has developed into an audit that examines more than financial statements and compliance with legislative authorities. Comprehensive auditing had grown to include discussions on almost every aspect of government. It was inevitable that the scope of comprehensive auditing would expand to include federal-provincial partnerships and the provincial delivery of programs funded in part (and perhaps in small part) by Parliament.

When the broad interpretation of the AG Act is combined with the latitude of VFM auditing, including the OAG's ability to comment on public policy and access to information, there is no question that the Auditor General's role has expanded significantly over the past 25 years.

Implications of Comprehensive Auditing on Accountability

As noted earlier, all revenues collected and spent by governments are public monies. Governments are entrusted to use these monies on behalf of the public, and are accountable to elected representatives (the House of Commons at the federal level). The Auditor General reports to the House of Commons whether public monies have been spent appropriately, and the House, acting on behalf of the public, holds the Government to account.

In a unitary system, or in a federal system without intergovernmental transfers, value for money auditing poses no conceptual challenges. Governments each collect their own revenues, and then are accountable for their use of these same monies. However, in the current Canadian federal system, accountability as measured by VFM audit standards becomes confused. A single taxpayer pays taxes to both the federal and provincial governments. The federal government then transfers some of its collected revenues to the provincial level. Which government, federal or provincial, should be held accountable for the transferred monies? Can accountability for funds be transferred along with the funds themselves?

The VFM auditing raises this question because its emphasis on effectiveness, efficiency and economy has created a situation in which the Auditor General must comment on public policy.

If federal funds are being spent on provincial programs, or on federal-provincial programs, then VFM auditing almost impels the Auditor General to "follow the cash." This places the Auditor General in the position of commenting on provincial public policies – a clear negation of federalism principles.

A central component of accountability and an essential tool for VFM auditing is proper access to information, including accounting practices and the integrity of financial statements as instruments of information for Parliament. If the federal government is accountable for the transferred monies, and therefore has access to provincial information, this too runs contrary to federalism principles.

If federal funds are being spent on provincial programs, or on federal-provincial programs, then VFM auditing almost impels the Auditor General to "follow the cash." This places the Auditor General in the position of commenting on provincial public policies - a clear negation of federalism principles.

Currently, the OAG's definition of accountability is being reworked. Traditionally, accountability has been defined in hierarchical terms with a subordinate party answering to a higher authority. With the emergence of alternative service delivery and partnership arrangements between federal and provincial governments, accountability is now defined as:

> A relationship based on the obligation to demonstrate and take responsibility for performance in light of agreed upon expectations. In this view, accountability is about the requirement to answer for what you have accomplished (or not) that is of significance and of value (OAG/CESD, 2000: 8).

Taken together, VFM auditing combined with an expanded definition of accountability raises serious questions about the shifting nature of Canadian federalism.

The Auditor General and Federalism

The analysis of the Auditor General's centralizing role is one that brings into play laudable but potentially conflicting principles: financial accountability and federalism. Comprehensive auditing assumes that the federal government will be responsible for all public monies it spends. Federalism assumes provincial and territorial governments will be accountable through their own procedures to their own electorates for the expenditure of public funds on provincial programs and responsibilities. From this perspective, the source of such funds is irrelevant; it all flows ultimately from the same taxpayer. Thus the fact of financial transfers from the federal government need not and should not imply any centralizing role for the OAG.

It should be noted that the principles of financial accountability and federalism do not necessarily have to conflict. For example, it could be possible for federal and provincial Auditors General to work together to establish consistent accounting criteria, with provincial Auditors General required to adhere to federal VFM accounting principles when auditing programs that receive federal transfer revenues.

Recent trends suggest that the Auditor General is pursuing financial accountability principles without attempting to protect the federalism principles. As mentioned earlier, the OAG is redefining accountability to be based upon a partnership rather than hierarchical model. However, at the same time the Auditor General tends to use a language that equates provincial and territorial governments with other agencies that might be involved in the delivery of federal programs. Note, for example, the following passage from the Auditor General's April 1999 Report:

> Collaborative arrangements are an alternative way – a potentially more innovative, cost-effective and efficient way – to deliver programs and services that traditionally have been provided by federal government departments and Crown corporations. In collaborative arrangements, the federal government, other levels of government *and organizations in the private and voluntary sectors* agree to share power and authority in decisions on program and service delivery (emphasis added)" (OAG/CESD, 2000: 13).

Recent trends suggest that the Auditor General is pursuing financial accountability principles without attempting to protect the federalism principles.

One could argue that a rhetoric that equates provincial governments with organizations in the private and voluntary sectors is insufficiently sensitive to the federal spirit. The province of Quebec, for example, is not simply the Victorian Order of Nurses writ large.

Because the provincial governments (as recipients of transfers) must report to meet the unilaterally-imposed standards of the federal government (provider of transfers), the VFM auditing approach reinforces a federal model build on the hierarchical relationship between levels of government rather than a partnership model based on constitutionally equal orders of government. Within the auditing framework, provincial governments ultimately report upwards to Parliament through the Auditor General; there is no suggestion that federal departments and agencies might report to provincial audit authorities.

Taken to its extreme, this understanding of accountability could have profound implications for Canadian federalism. These include:

- Reduced provincial autonomy and an increased centralization of powers. Given that provinces are dependent upon federal transfers to meet their jurisdictional responsibilities, provincial governments may become further compelled to match their programming and policy with federal standards and policy goals.

- Provinces acting as service delivery agencies rather than "policy laboratories." One of the chief virtues of federalism is that it allows provinces to experiment with alternative policies and programs. Policies that are successful are often adopted in other areas. In addition, the ability to experiment allows a province to find the policy mix that meets its unique needs. If provinces are confined to federally designed standards, this flexibility is lost, and the very purpose of federalism is brought into question. Provinces become nothing more than providers of federally designed programs.

The ability to experiment allows a province to find the policy mix that meets its unique needs. If provinces are confined to federally designed standards, this flexibility is lost, and the very purpose of federalism is brought into question.

The point to stress is that federalism is based on a high valuation of difference and variation. The reduction of provincial autonomy inherent in a "service deliverer" approach to provinces is contrary to federal values.

There are other risks to the expanded role of the OAG. First, the comprehensive auditing model and the accompanying definition of accountability reinforces the fiscal imbalance in Canadian federalism. In some respects, the emerging auditing model of federalism makes a bad situation even worse. Second, and perhaps most problematic, is the fact that financial accountability blends easily into political accountability; the former becomes the means by which one order of government might impose a particular policy vision on another. If, for example, a provincial government were to disagree with the federal government on the interpretation of the Canada Health Act, the OAG could see its mission as ensuring that the provincial expenditure of funds matched the federal vision. If, as is envisioned by some in the evolution of the Social Union Framework Agreement, there were to be a neutral dispute resolution mechanism through which differences of opinion could be reconciled, this would not pose a problem. However, in the absence of such mechanisms, the OAG cannot be seen as a neutral body *in a federal sense.*

Issues for Public Debate

Our analysis demonstrates that the federal role of the Auditor General is expanding. It suggests, moreover, that this expansion is driven more by a change of accounting principles than by personal whim. However, a continued expansion of this federal role is not inevitable. The Canadian public has both the opportunity and the obligation to ask a number of questions:

Fiscal imbalance. At the root of the questions about the centralizing role of the Auditor General is the issue of intergovernmental transfers. If fiscal imbalance did not exist – if the federal government collected fewer monies and the provinces collected greater monies – there would be no need for transfers to fund provincial programs, and little potential for the OAG to undermine federal principles. (The federal government may still wish to continue transfers for equalization purposes.) The key questions for public debate are "should steps be taken to address Canada's fiscal imbalance?" and "If yes, what steps?"

A continued expansion of this federal role is not inevitable. The Canadian public has both the opportunity and the obligation to ask a number of questions.

Accountability. Assuming the continuation of fiscal imbalance, how should the issue of accountability be resolved? Is the source of public funds irrelevant when it comes to financial accountability? Should provincial governments be accountable only to their own internal audits and their electorates even if their programs are funded in part by money raised through Parliament?

Federalism and Provincial Autonomy. There are many questions for public debate concerning the role of OAG and federalism.

- Do the audit principles adopted by the Auditor General necessitate some consistency across provinces in the measurement of program effectiveness and value for money? If so, how should guidelines be set and by whom?

- Does the audit function of the Auditor General open the door for greater federal regulation of provincial governments? For example, might the Auditor General provide a more effective tool for regulating the provincial delivery of health services than does the principled application of the Canada Health Act?

- Does the expanded role of the Auditor General threaten the principle of unconditional transfers to provincial governments? Are we seeing the emergence of a new form of conditionality?

Our analysis does not provide definitive answers to such questions. However, it suggests that the centralizing role of the Auditor General should be the subject of serious debate. The OAG's role provides excellent terrain for exploring the potentially conflicting interests of financial accountability and respect for federal principles. This exploration is essential for the larger interest in good public policy. ■

The centralizing role of the Auditor General should be the subject of serious debate.

Endnotes

1. Whatever its other merits might be, the Social Union Framework Agreement increases this entanglement even more.

2. While provinces have their own income tax systems, and there are rate and other variations between provinces, the collection of federal and provincial income tax is married. Thus taxpayers pay a single income tax sum. Quebec is the exception to this rule.

3. The only significant addition to the Act since 1977 is the creation of a Commissioner of the Environment and Sustainable Development, who reports directly to the Auditor General and assists him in performing his duties relating to the environment and sustainable development (s.21 through s.25).

4. Excludes professional and special services; includes "other personnel costs" along with salaries and wages.

5. Descriptions of the different forms of auditing are in part drawn from OAG (no date).

Bibliography

Balls, Herbert R. (1978). "The Watchdog of Parliament," *Canadian Public Administration.* Volume 21 (Winter): 584 – 617.

Dominion Law Reports (1986). *Auditor General V. Min of Energy, Mines and Resources.* 23 DLR (4th).

OAG (no date). *Auditing for Parliament.* http://www.oag-bvg.gc.ca/domino/other.nsf /html/bodye.html

OAG (1984a). *Annual Report.*

OAG (1984b). *Auditing for Parliament.*

OAG (1985). *Annual Report.*

OAG (1991). *Annual Report.*

OAG (1997). *Auditor General of the Republic of Argentina – Auditor General of Canada's Address: Challenges Facing Canadian Auditors. November 1997.* http://www.oag-bvg.gc.ca/domino/other.nsf/html/ba_e.html

OAG. (1999a). *Report of the Auditor General,* April 1999.

OAG. (1999b). *Report of the Auditor General,* November 1999.

OAG/CESD (2000). *VFM Audit Manual.* January 2000.

Sutherland, Sharon. (1981). "The Office of the Auditor General of Canada: Watching the Watchdog." In Bruce Doern, ed. *How Ottawa Spends Your Tax Dollars.* Toronto: Lorimer: 616 – 644.