Department of Internal Affairs and grants administration

Progress in responding to the Auditor-General's recommendations

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Introduction

1.1 In November 2010, we published a report on our performance audit of how the Department of Internal Affairs (the Department) was managing two grant schemes, the Lottery Grants Scheme and the Community Organisation Grants Scheme (COGS).[1] Our report included three recommendations to improve the Department's processes, including a recommendation to set up a new business system to address the limitations of the current system for managing grant applications.

1.2 We reviewed the Department's progress in implementing the three recommendations in our progress report, *Public entities' progress in implementing the Auditor-General's recommendations 2012*.[2] By early 2012, the Department had addressed two of the recommendations. However, it had experienced delays in replacing the old system for managing grant applications.

1.3 In 2013, we reviewed the Department's progress again. We found that further improvements have resulted in increased accountability and transparency for grants decision-making. After further delays, the Department has progressed work on a new system for managing grants and clients that incorporates and is in keeping with the intent behind the Government's Better Public Services result area 10: "New Zealanders can complete their transactions with the Government easily in a digital environment." The Department expects to start using the new system in a staged process from September 2014.

Background

1.4 The Department manages several schemes that provide grants to community organisations. Many community organisations — such as clubs, charities, cultural bodies, and small incorporated societies — rely heavily on grants for their operational funding or special projects. Through its community advisory service, the Department helps to build leadership and capability in communities.

Our audit scope and findings

1.5 In November 2010, we looked at whether the Department managed grants in keeping with the principles and expectations that we outlined in our 2008 good practice guide, *Public sector purchases, grants, and gifts: Managing funding arrangements with external parties*.

1.6 We looked at the Department's administration of two grant schemes:

- the Lottery Grants Scheme; and
- COGS.

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1   *Department of Internal Affairs: Administration of two grant schemes*, available on our website.

2   Published in April 2012 and available on our website.

1.7 We found that the Department's systems and processes were effectively helping the Department to put into practice principles which were consistent with the principles in our good practice guide. These principles are evident at all four stages of grants administration:

- planning how the grant schemes work;
- selecting recipients;
- monitoring how money is spent; and
- reviewing the effectiveness of the grant schemes.

1.8 However, we found that Grants Online – the Department's system for managing grant applications – was outdated and had significant limitations. At the time of our audit, the Department had recently completed a business case to replace Grants Online. The Department expected to put a replacement system into effect in late 2010, soon after our 2010 report was published. Our 2010 report noted that it was important for the Department to have the new system up and running promptly to address many of the matters that we and the Department had identified.

1.9 We considered that the Department could do more to support decision-making committees for the Lottery Grants Scheme funds and COGS by making decisions more transparently and accountably.

1.10 We made three recommendations and listed some suggestions for improvements. We recommended that the Department:

- implement, in a timely manner, a new business system for grant administration that meets the identified requirements, and then monitor that system to ensure that it improves the effectiveness and efficiency of grant administration as intended;
- improve the recordkeeping about decisions made by the Lottery Grants Scheme and COGS committees by:
  - working with the committees to ensure proper recording of reasons why applications are approved or declined or a lesser amount than requested is granted; and
  - ensuring that members of the COGS committees properly and consistently complete the information required by the Local Distribution Committee Members' Assessment Tool; and
- revise its agreement with the Lottery Outdoor Safety Committee to ensure that accountability requirements for recipients of large grants are adequate and appropriate for the size and nature of those grants.

1.11   In April 2012, we reported on the progress that the Department had made in addressing our recommendations and suggestions.[3] The Department had made some progress but had not completed all of its intended actions.

1.12   In particular, progress on replacing Grants Online had suffered setbacks. The "go live" date for the replacement system was first delayed for more than a year and then the Department's contract with the original vendor was cancelled. The Department tested a prototype based on another public entity's grants management system but found that it was not fit for purpose.

1.13   When we published our 2012 report, the Department was considering other options, including another procurement process. We suggested that the Department could share the lessons it had learned with other public entities that are looking at similar arrangements for large joint projects. We noted that we expected to be kept informed of progress through our regular relationship management and annual audit processes.

1.14   Three years after the original "go live" date for the grants management system, it is timely to review the Department's progress.

The response to our findings and recommendations

1.15   The Department has responded seriously to our recommendations and suggestions. The Department has referred often to our recommendations and suggestions in guidance material, planning documents, and communication with staff and members of distribution committees.[4] Staff told us of improvements that were a direct result of our recommendations and that our 2010 and 2012 reports gave impetus to planning and carrying out other improvements.

Recommendation 1: Implementing a new business system in a timely manner

1.16   The Department has experienced delays in addressing this recommendation. The Department pursued several options that proved unworkable, particularly given the Government's growing focus on all-of-government capability. The Department used the drivers of, and knowledge from, the previous business case to prepare a new business case with more realistic timelines and to ensure that prospective vendors understood the Department's requirements.

1.17   The Department signed a contract with a new vendor in September 2013 and estimates that the Grants Client and Management System (the new system) will start to go live in a staged process from September 2014. The Department

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3   *Public entities' progress in implementing the Auditor-General's recommendations 2012*, available on our website.

4   Distribution committees decide which applicants will receive a grant and allocate funding to grant recipients.

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is working with the vendor to finalise detailed requirements and confirm time frames in April 2014.

1.18　In our view, the Department has prepared the new business case carefully and thoroughly. The expected outcome of a better and more flexible solution is a reasonable result for the work that has been done, although replacing Grants Online has taken much longer than was anticipated at the time of our 2010 report. Work included getting the application and customer compliance aspect of the new system into line with *Better Public Services* result area 10 and the Department's objective of empowering communities and people to participate in society and the economy. We spoke with Department staff who told us that, although delays had been frustrating, the current solution should suit the Department's business and customer needs much better.

1.19　The Department set aside about $2.5 million to fund work in 2012/13 and 2013/14 on the new business case and the request for proposal process for the new system. The Department has allocated $4.71 million over five years (from 2012/13 – counted as "year 0" – to 2017/18) to implementing the project. The new system is to be hosted overseas by a specialist in grants administration systems using "cloud" hosting. This option is in keeping with the Government's approach to digital services, and was cheaper.

1.20　The project team for the new system has worked with the Department's "Cloud Programme" to trial the proposed cloud risk framework, which has been approved by Cabinet. The Chief Executive of the Department approved the cloud hosting of the new system, as recommended in the cloud risk framework.

1.21　In our view, considering the project's size, the development costs have been reasonable. We recognise that it is common for projects of this kind to be delayed when an organisation has explored avenues that prove unsuitable. Also, a changing policy environment meant that the Department had to align its business needs with the Government's focus on all-of-government capability. The new system is designed to be flexible and scalable enough for other business units and agencies that manage grants to use.

1.22　The Department plans to introduce the new system in stages and will confirm the detailed time frame for this when it has finished verifying what it needs the system to do. Staging means implementing the new system with one grants fund first, then gradually adding others. To avoid further delays, the Department is setting clear milestones with the vendor, with penalties for late delivery. The Department will retain Grants Online until it is satisfied that the new system is working.

1.23 The Department has worked to ensure that the new system is in line with its new financial management system, the Financial Applications and Transformation (FAST) project, a shared services arrangement with the Department of Inland Revenue. FAST is intended to improve efficiency and effectiveness.

1.24 The Department has considered how it can better manage grants and grant applications in the interim. It has decided not to invest further in Grants Online, although has made some "workaround" improvements to business practices. This means that the new system will incorporate some better practices already in place.

Recommendations 2 and 3: Improving accountability and recordkeeping

1.25 The Department has made progress with our other two recommendations since our 2012 progress report. In 2012, the revised contract and accountability agreements for the Lottery Outdoor Safety Committee came into effect. The committee's assessment and recording processes have been improved and monitored.

1.26 A new accountability agreement for large grants (some more than $1 million) is now used for the Lottery Outdoor Safety fund. Grant recipients must provide detailed information at two or more milestone points before the Department releases the next instalment of funding. A new grants agreement with milestones is in place for grants of more than $100,000. The Department's advisor for Outdoor Safety reported that the new grants agreements are working well and have required some organisations to upgrade their accounting and financial management skill sets. This improvement should provide the Department with much greater risk control and assurance that the grants are used for the intended purpose.

1.27 The Department has responded well to our recommendation to improve how it records decisions made by the Lottery Community Grants committees and COGS Local Distribution Committees.[5] The Department has revised the training material for COGS and Lottery Grants Scheme national and regional community distribution committees. The training material now clearly sets out the obligations for transparent and accountable decision-making. For COGS, the obligation to properly complete the grants assessment tool is emphasised in the guidance handbook for Local Distribution Committee members and in material for training facilitators. Training for both COGS and Lottery Grants Scheme committee members includes guidance and practical exercises to provide thorough understanding of how to identify and deal with conflicts of interest.

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5 Lottery Community, part of the Department of Internal Affairs, distributes grants through a national committee and 11 regional committees.

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1.28   Since July 2012, all Lottery Community Grants distribution committees (and several other Lottery committees) must explain in more detail why grant applications are approved, declined, or approved in part. For their recommendation report to decision-making committees, advisors draw on the Better Funding Practices Business Process Manual (the Business Process Manual), which includes examples of reasons for approving or declining an application. Recording reasons for a decision gives applicants more clarity about why their application was declined or only partially funded and helps to guide future committees' decision-making.

Other improvements

1.29   Other improvements that the Department has made in response to our reports include updating the Business Process Manual. In our 2010 report, we noted that the online Business Process Manual was useful and comprehensive and provided a logical and coherent framework for grants administration guidance and procedures. However, the Department could further improve procedural support for – and the quality of information provided to – decision-making committees.

1.30   The Business Process Manual has been updated, is now available online, and includes new policies and criteria. We were shown the online guidance in the Business Process Manual onscreen and noted that the Department has tightened some procedures and improved some forms. This includes a financial assessment checklist for many of the grants funds, with more in-depth analysis of applicants' financial status and history.

1.31   From our observation and downloaded samples, the Business Process Manual appears to be accessible. However, staff told us that it remained difficult to follow. Some staff, especially new staff, used the Business Process Manual more than others. More experienced staff referred to it only when alerted to changes. Staff told us that they expect that the Business Process Manual will be easier to use when it is integrated with the new system. The Department's advisory staff still rely on Grants Online for assessing broad risks, although some have tried out a new Risk Assessment Tool, which is being developed.

1.32   We saw improved financial analysis (recorded in the advisor reports to committees). Some staff told us that the financial skills training required for all advisory staff has helped to improve the capability of new staff and those in regional centres. The increase in capability should enhance the advice and information that staff provide to decision-making committees, encouraging better decision-making.

1.33   The Department informed us about two workstreams that support our suggestion that committee structures and targeted funding could be brought more into line with community priorities.

1.34   The Department has carried out work to bring the Lottery Grants Scheme committee structure more into line with its intent of helping build strong sustainable communities, hapū, and iwi. The Department, in its secretariat role for the Lottery Grants Board, has consulted communities as part of a review of the distribution committees. This review is complete and will be put into effect in 2014. Most committees are likely to remain unchanged, except for some minor adjustments to boundaries of areas covered around Auckland and to allow committees to give multi-year grants.

1.35   The Department is using some Crown funds to carry out a four-year initiative (from 2011/12 to 2014/15) of community-led development in selected communities. The outcome-focused initiative aims to build capability in those communities, approaches funding more cohesively and strategically, and makes the most of the Crown funds that the Department manages for this purpose.

1.36   The initiative supports the Department's aim of "development of strong sustainable communities, hapū, and iwi Māori". An early evaluation by the Department of how the initiative is working shows that more attention to communication, project management, and staff training will be required to ensure that the approach works effectively.

1.37   The initiative has potential to increase the time spent on advisory work in the community. This will require the Department to be responsive to communities' changing needs, which means being more flexible than before. Staff will have a wider outreach in the communities they work with.

1.38   The Department has reviewed its Risk Assessment Tool (which was being prepared during our audit in 2010) to bring it into line with the new system. The tool is intended to work out the risk to compliance, rather than the risk of a funded project not achieving outcomes. The Department has tried out the tool to gather information to help work out indicators of risk. However, the tool has to be refined and tested further before it is fit for purpose and can become part of the process for assessing grants. The Department intends to implement the tool to fit in with the new business system.

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1.39   The Department has made further improvements in line with our suggestions, including:

- training COGS distribution committee members in how to set funding priorities to ensure that priorities are more consistent and more in line with local and national priorities; and

- ensuring that the new system will allow the Department's national and regional advisors to share information about clients, through a "single client view".

1.40   We suggested that the Department could provide better information and more guidance to committees about regional communities for targeted funding and (for COGS distribution committees) for setting local funding priorities.

1.41   The Department provides committees with community profiles that include demographic information. It has introduced training for COGS committees to set priorities using this information and information that comes from members of their communities. However, we note that the information in the community profiles is based largely on the 2006 census and other data that is four or five years old. This means that a profile might not accurately reflect a community when, for example, there has been a significant population change because of industry closures or a change in population because of natural disasters. The Department told us that this information had been updated regularly. We would expect a process to be in place to ensure that the profiles are updated with information from the latest census and other, more recent, publicly available data.

1.42   In our view, the Department's progress addressing our recommendations and suggestions shows how it is committed to working better. The new system will include other improvements that have been considered, but not yet put into effect.

1.43   Through our normal relationship arrangements, we will continue to monitor how well the Department puts the new system into effect. We thank the Department's staff who helped us to prepare this report.