
MINISTRY OF ENVIRONMENT AND ENERGY

Conservation and Prevention Division

Under the *Environmental Protection Act*, the *Ontario Water Resources Act*, the *Environmental Assessment Act*, the *Waste Management Act* and a number of related acts, the Ministry of Environment and Energy is charged with a broad mandate of protecting the quality of the natural environment in order to safeguard the ecosystem and human health.

The Ministry's Conservation and Prevention Division is responsible for promoting the reduction of waste and pollutants and the conservation of energy and water. It is also responsible for programs that facilitate environmentally sensitive decision making in land use and economic development issues through effective planning and environmental assessment. In addition, the Division provides funding to municipalities for water and sewage capital projects.

For the 1996/97 fiscal year, the Division had about 180 staff and total expenditures of \$224 million, of which \$200 million related to grants provided to municipalities for waste reduction and for water and sewage capital projects.

OBJECTIVES AND SCOPE

Our audit objectives were to assess whether satisfactory procedures were in place to:

- measure and report on the performance of the Conservation and Prevention Division in contributing to the effectiveness of the Ministry in protecting the environment and human health; and
- ensure that grants were disbursed with due regard for economy.

Our audit included a review and analysis of all relevant documentation and management reports pertaining to the activities of the Division, as well as discussions with appropriate staff. We also reviewed relevant work on the Division by the Ministry's Management Audit Branch. The work of the Branch on grant payments for water and sewage projects was useful in reducing the extent of our work in that area. Its observations on the monitoring of such grant payments were incorporated in our report.

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OVERALL AUDIT OBSERVATIONS

To be more effective in meeting the provincial waste reduction goal, the Ministry needs to measure and report on the effectiveness of its waste reduction programs and work with the municipalities to reduce the cost of collecting and processing recycled materials in their communities.

To better protect the environment through the environmental assessment process, the Ministry needs to establish indicators to measure and report on the effectiveness of the process and monitor compliance with the terms and conditions of approved projects.

In our 1994 *Annual Report* we indicated that significant savings could be achieved if municipalities were required to review water conservation and system optimization measures and, where applicable, implement such measures before water and sewage expansion projects were approved for provincial funding. While the Ministry agreed with our recommendation, the requirement was still not in place at the time of our current audit. To ensure that due regard for economy is observed, we again recommend that such a requirement be established as a prerequisite for the approval of future expansion projects.

Furthermore, the Ministry needs to verify information that has a direct impact on eligibility and the amount of funding for water and sewage projects, and to monitor actual project expenditures more closely to ensure timely identification and recovery of overpayments.

DETAILED AUDIT OBSERVATIONS

WASTE REDUCTION

Out of concerns for environmental protection and for the lack of landfill capacity in the province, the Ministry in 1989 announced two waste reduction goals: a reduction in solid waste disposal of at least 25% by 1992; and a further reduction to 50% by the year 2000. The reductions were to be achieved by means of the “3Rs” (Reduction at source, Reuse and Recycling).

To support these waste reduction goals, the Division has given its Waste Reduction Branch the key responsibility of developing and delivering programs designed to reduce the waste going to landfill sites. In this regard, branch staff:

- develop and implement regulations, policies and guidelines that support the “3Rs”;
- provide technical and financial assistance to municipalities and industries in processing materials diverted from landfill sites and in identifying markets and uses for such materials; and
- monitor demand and price trends in the marketplace to assist municipalities in developing markets for recycled materials.

GRANTS ADMINISTRATION

The Division provides financial assistance to municipalities and industries in support of waste reduction initiatives such as the Blue Box Program. In 1996/97 the amount of grants disbursed totalled approximately \$10 million. Grants for waste reduction are currently being phased out.

We reviewed the grants in support of waste reduction and were satisfied that adequate procedures were in place to ensure that the disbursement of grants complied with the terms and conditions of agreements with the recipients.

EFFECTIVENESS OF WASTE REDUCTION

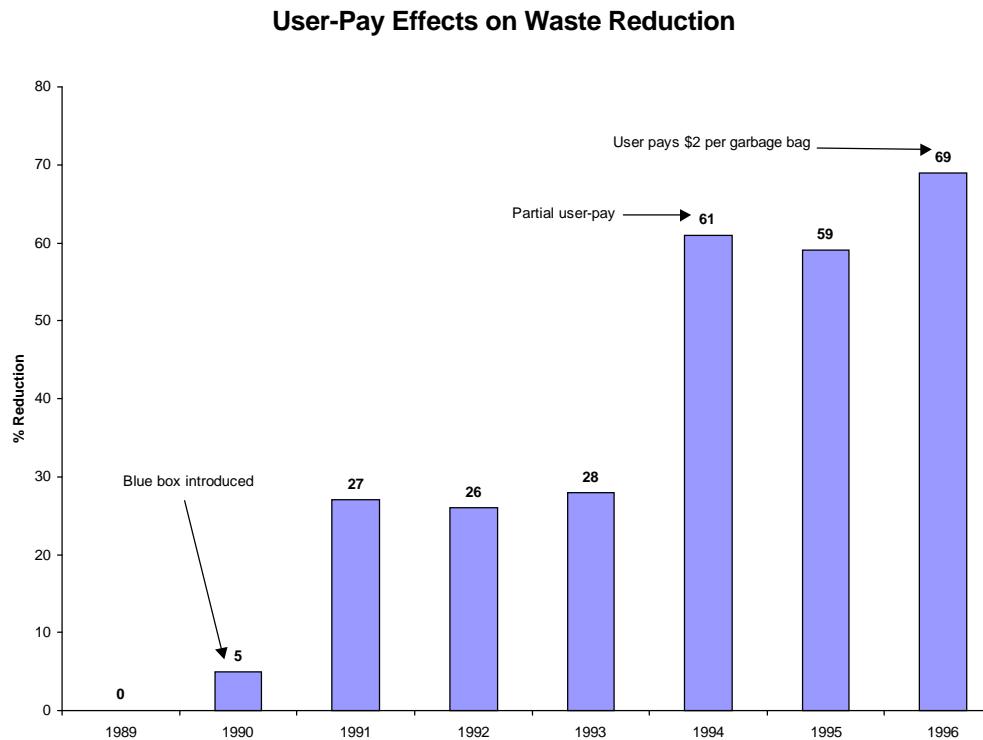
At the time of our audit, the Ministry had collected data on solid waste disposal up to 1994. The data indicated that solid waste going to landfill and export declined from 7.7 million tonnes in 1990 to 7 million tonnes in 1994. For the same period, capital and operating expenditures for municipal garbage collection and disposal declined from \$873 million to \$693 million.

Since the 1989 Ministry announcement of waste reduction goals, the provincial recycling initiative had been widely accepted by the municipalities. By 1994 over 500 municipalities, representing approximately 3,000,000 households or 94% of the Ontario population, had already established recycling (Blue Box) programs.

Ministry officials informed us that the 1989 waste reduction goals were based on total solid waste disposed of in 1987, on a per capita basis. On that basis, the Ministry indicated that the province has achieved its first reduction goal of 25% by 1992. However, as most municipalities have already established their recycling programs, success since then has been more limited. Ministry officials estimated that an additional reduction of 5% had been achieved since 1992 or about 30% of the 1987 base year.

In reviewing the best practices of Ontario municipalities, we noted that a number of smaller municipalities (population under 50,000) were successful in reducing waste beyond the provincial average of 30%. In addition to recycling, the key factor common to their success was the application of some kind of user-pay principle to encourage reduction and reuse. The significant reduction of solid waste attained by applying the user-pay principle is demonstrated by the reduction data from one of these municipalities as illustrated below.

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Source: Ministry of Environment and Energy

The municipality involved initiated the Blue Box recycling program in 1990. This municipality's recycling experience was similar to that of other municipalities in that it was able to reduce its waste by over 25% and levelled off shortly after the recycling program was introduced.

To educate the public and promote reduction, the municipality in 1994 and in 1995 gave out 52 free tags for garbage bags to every household in the community. All garbage bags had to be tagged to be picked up. If households required more than 52 bags for the year they had to purchase additional tags at \$1.50 each. As a result of this initiative, the municipality was able to increase its solid waste reduction from 28% to 61%.

In 1996 free garbage tags were no longer given out and all tags cost \$2 each. All revenues from the sales of tags were to be used to reduce property taxes. By applying the full user-pay principle, solid waste reduction was increased by an estimated 10% beyond the 1995 level.

While the user-pay principle has been a success when it was implemented, its use has not been accepted in a number of larger municipalities. Residents of these municipalities perceived the user-pay principle to be a form of double taxation over and above their property tax and were also concerned about the possibility of illegal dumping.

The Ministry has committed \$390,000 for conducting pilot projects to investigate the applicability of user pay in three larger municipalities. The Ministry has plans to encourage more use of pilot/demonstration projects to generate more ideas/options for waste reduction.

At a strategic level, a business plan for the Waste Reduction Branch was completed in May 1997. The business plan outlined the directions of the Branch, including its missions, goals and strategies, that would guide all activities undertaken by the Branch. However, we noted that

the provincial goal of a 50% reduction in solid waste disposal by the year 2000 was not mentioned in the business plan.

While the provincial reduction goal was to be achieved in less than three years, our review indicated that the Ministry had not measured or reported on the effectiveness of its waste reduction programs since 1994. Without a timely assessment of the effectiveness of its various waste reduction programs, the Ministry cannot adjust strategies or develop appropriate action plans on a timely basis.

Recommendation

To be more effective in meeting the provincial waste reduction goal, the Ministry should:

- incorporate the provincial goal in the Waste Reduction Branch business plan to guide all waste reduction activities; and
- measure and report on the effectiveness of its waste reduction programs to permit the timely adjustment of strategies and the development of action plans.

Ministry Response

The Waste Reduction Branch used the provincial waste reduction goal to develop its business plan and develop priority projects. The provincial goal will be formally noted in the branch business plan.

The Ministry will monitor and report on the effectiveness of its waste reduction programs and use those measures to adjust the strategies and action plans as the province works toward the reduction target.

The Waste Reduction Branch has recently requested diversion data for 1995 and 1996. The information collection was coordinated with the Association of Municipal Recycling Coordinators, the Corporations Supporting Recycling, and the Recycling Council of Ontario. This data will be collated and released in 1997.

RECYCLING (BLUE BOX) PROGRAM

Marketable materials collected by the municipal recycling program (commonly known as the Blue Box Program) can be grouped into six major categories, namely: glass, paper fibre, corrugated cardboard, steel cans, aluminum cans and plastic bottles. These materials are usually reported to the Ministry by weight. The latest data gathered by the Ministry for 1994 indicated that the municipalities had collected 470,000 tonnes of these materials.

SUSTAINABILITY OF BLUE BOX PROGRAM

The Blue Box Program was designed to be financially self-sustaining or at least affordable to the municipalities after five years of provincial assistance. Initially, the municipalities received start-up capital funding from the province and \$20 million from a private industry group formed

to support recycling. The province also provides grants to assist municipalities with their operating costs for the first five years of the Blue Box Program. Since the Program's inception in 1986, the province has provided over \$200 million in capital and operating grants to the municipalities. Currently, capital and operating grants (1996/97 — \$8 million) are being phased out as most municipalities have already operated their Blue Box Program for more than five years.

At the time of our audit, the Ministry had not compiled cost and revenue data from municipalities relating to the Blue Box Program for 1995 and 1996. In reviewing the Blue Box Program's 1994 revenue and cost data for over 500 municipalities provided by the Ministry, we noted that 12 municipalities or less than 3% were able to break even financially. About 170 of these municipalities reported costs in excess of revenues of over \$250 per tonne. For about 50 high-cost municipalities, costs in excess of revenues ranged from \$400 to over \$1,000 per tonne.

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However, Ministry officials indicated that the financial costs involved should not be the only consideration in determining whether to use the Blue Box Program for protecting the environment. More importantly, the Program would alleviate environmental concerns regarding potential air pollution, ground water contamination, conservation of energy, and the lack of landfill sites and incinerators.

Because of various local differences, it would be difficult to compare the economy or efficiency of municipal Blue Box operations without an in-depth analysis of each of the municipalities. For example, without including the savings in landfill and garbage disposal costs (see discussion in the following section), the costs and benefits of recycling cannot be fully determined. However, our review of the 1994 revenue and cost figures provided by the Ministry indicated that the original objective of having municipalities operate the Blue Box Program on a self-sustaining basis is probably unrealistic without substantial cost reduction for many of the municipalities.

Recommendation

To ensure that the Blue Box Program is sustainable, the Ministry should work with municipalities to reduce the costs of collecting and processing recycled materials.

Ministry Response

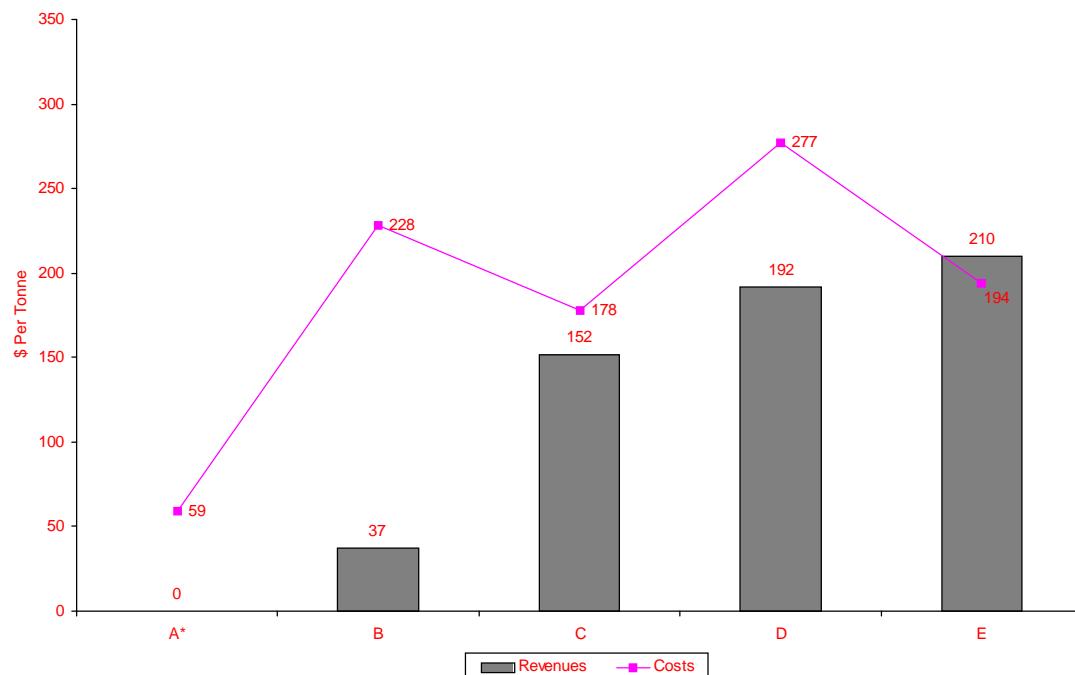
The Ministry is working with the municipalities to promote cost-efficient collection and processing procedures to promote effective facility operation and to increase material capture rates. For example, the Ministry has funded pilot projects on variable rate waste collection systems in large municipalities which will increase diversion rates. The Ministry also encourages the municipalities to consider avoided disposal costs when calculating the costs of diversion.

COSTS AND BENEFITS OF RECYCLING

As the Ministry had data only to 1994, we extended our review to include 1995 revenue and cost data from five larger municipalities (A to E in the following chart) in five different regions. Although prices in 1995 were at a record high for most recycled materials and economies of

scale were possible, most of these large municipalities were still not able to break even, as illustrated in the following chart.

Recycling Costs and Revenues in Selected Large Municipalities



* Contractor was paid for collection and retained proceeds of recycling.

Source: Various municipalities

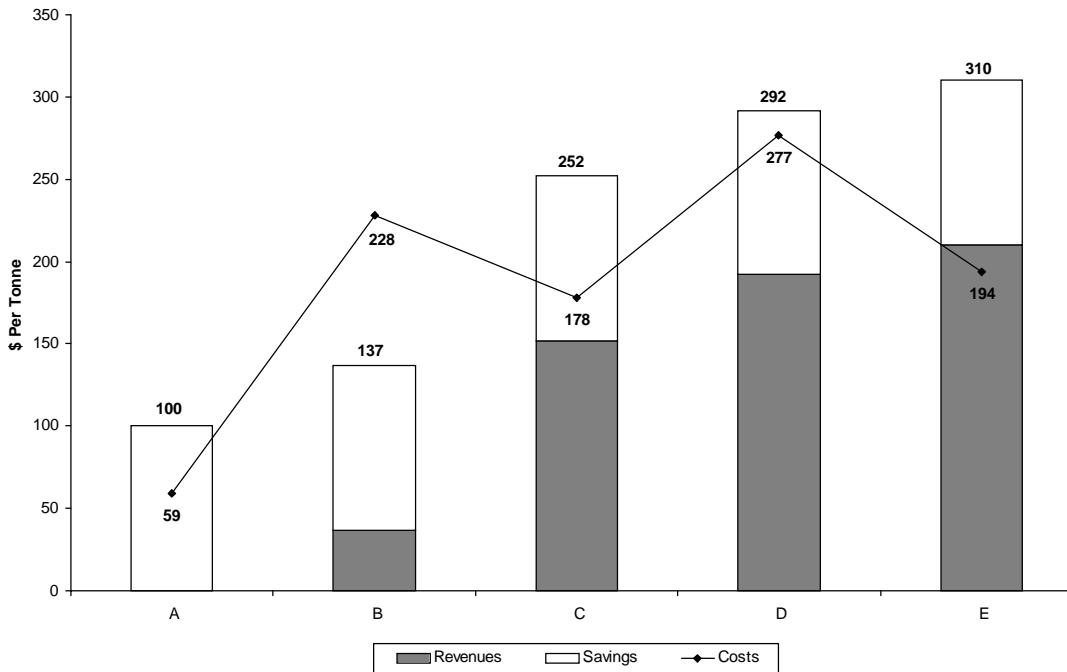
According to the chart, the Blue Box Program appears to be quite costly. However, our analysis indicated that it would have been even more costly for most of these municipalities if they did not have the Program because they would have:

- still incurred the costs of disposing of the recyclable materials through landfill, which in 1994 averaged about \$100 per tonne; and
- received no revenue to offset the disposal costs of the recyclable materials.

As the following chart illustrates, by including the \$100 per tonne disposal cost savings with revenues received from the recycled materials, these municipalities would see their Blue Box Program become cost effective, even without considering the benefits to the environment.

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Recycling Costs, Revenues and Potential Savings in Selected Large Municipalities



Source: Various municipalities

More importantly, Ministry and municipal officials informed us that most municipalities did not take the costs of landfill and garbage disposal into consideration when expressing their concerns about the high cost of recycling. Even if they did, they were mainly using only the current operating costs of landfill in their decision making rather than the full costs of using landfill sites, as discussed in the next paragraph.

In order to determine the costs and benefits of having the Blue Box Program, the municipalities should consider the full costing of alternatives such as landfill or incineration (which usually costs more because of more stringent environmental requirements). In the case of landfill, current operating costs while important are only a small part of the total costs. Future costs such as closure costs, post-closure costs, potential environmental costs from gas pollution and ground water contamination, contingent liabilities for legal costs, as well as costs for locating and establishing replacement landfill sites, are also very significant and relevant for their decision.

Recommendation

The Ministry should work with municipalities to adopt the use of full costing for assessing the most cost-effective method for the disposal of waste in their communities.

Ministry Response

The Ministry agrees with the importance of the full costing of waste activities. The Ministry has encouraged municipalities, and will continue to work with them, to adopt the use of full cost accounting for assessing the costs of disposal of waste.

COMPLIANCE WITH LEGISLATION

To encourage reuse, Regulation 340 of the *Environmental Protection Act* requires a minimum of 30% of soft drinks to be sold in refillable containers. Our audit revealed that the Ministry had not enforced this legislative requirement. Currently, less than 2% of soft drinks are sold in refillable containers.

BACKGROUND

During the 1980s, out of concerns for the protection of the environment, most industrialized nations adopted legislative measures to curb the increasing use of non-refillable bottles by:

- banning their use;
- levying environmental taxes; or
- requiring a mandatory deposit system for refillable bottles.

A mandatory deposit system became the law for most major American states and Canadian provinces. In step with the environmental legislative measures taken by these other jurisdictions, Ontario was considering the introduction of similar legislation. In response to the anticipated legislation, the soft drink industry maintained that a deposit system would be too expensive for consumers.

As the province was initiating its Blue Box Program, the industry offered to share part of the capital start-up costs by contributing \$20 million. The province accepted the industry offer and passed legislation in 1985, requiring 40% of soft drink sales to be in refillable containers. The 40% quota is to be reduced to 30% when prescribed recycling targets are met. In addition, the industry committed itself to maintaining the refillable glass bottle as a viable option for the consumer by:

- pricing refillables at 30% lower than non-refillables to provide an incentive to consumers;
- giving equal advertising prominence to both refillables and non-refillables;
- making refillables available at 98% of retail outlets; and
- promoting the environmental benefits of refillables through advertising.

EFFECTS OF THE LEGISLATION

Since the legislation was enacted, sales in refillable bottles have dropped to less than 2% of soft drinks sold. Consequently, municipalities were receiving more and more plastic soft drink bottles and were concerned about high costs of up to \$1,800 per tonne for recycling. While revenue from these plastic bottles over the last five years averaged about \$240 per tonne, it

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was never enough to cover their recycling costs. At the time of our audit, the revenue for recycled plastic bottle material had declined to about \$66 per tonne.

While plastic containers account for less than 2% of recycled materials by weight, they represent about 20% of municipal recycling costs because of the volume they occupy. Currently, about half of the plastic containers are used for soft drink bottles. Municipalities were concerned that the soft drink industry has been able to reduce the amount of materials used through better technology. As the recycled materials are being sold by weight, the municipalities estimated that material reduction by the industry has reduced their revenue correspondingly.

Municipalities have maintained that the costs of disposing of non-refillable soft drink bottles are being unfairly shifted from the direct users, that is, the soft drink industry and consumers, to the municipalities and taxpayers. According to the municipalities, this is a violation of the fundamental user-pay principle of environmental conservation.

Our discussions with representatives of the soft drink industry indicated that the industry was aware of the concerns of the municipalities. However, the industry maintained that alternatives, such as a deposit system, would lead to a high-cost inefficient system parallelling the Blue Box Program. The industry was willing to work with the province and the municipalities again to determine how to pay its fair share and not have taxpayers subsidizing the industry.

Ministry officials indicated that the legislation was difficult to enforce as it involved consumer preference in the marketplace. Since 1995 the Ministry has been reviewing the legislation with the intention of proposing legislative changes regarding refillable soft drink containers.

To date, the review of the legislation has not been completed and there has been little progress in dealing with the industry on this issue.

Recommendation

The Ministry should expedite its review of the legislation regarding refillable soft drink containers and at the same time work with the industry to develop a practical solution to address the concerns of the municipalities.

Ministry Response

The Ministry has undertaken a review of the waste regulations and will continue to work with the municipalities and industry on solutions to this issue.

ENVIRONMENTAL ASSESSMENT

The Conservation and Prevention Division administers the *Environmental Assessment Act*, the purpose of which is to provide for the protection, conservation and prudent management of the environment. To achieve this, the Act requires environmental problems or opportunities to be considered and their effects planned for before development or building takes place.

The Act requires the consideration of a broad range of environmental effects (including biophysical, social, cultural, technical and economic) in the planning and development of public projects, such as roads, sewage treatment plants, hydro corridors and landfill sites. The envi-

ronmental assessment process also considers community values, stakeholder knowledge and public opinion before projects are approved.

REVIEW AND DECISION PROCESS

Ministry staff review each environmental assessment submission and notify the public of the submission. After receiving comments from the public, the Minister decides whether a hearing by the Environmental Assessment Board (the Board) is required. The process has been criticized by the proponents of projects as being untimely, ineffective and too costly.

Our examination of the last 30 submissions approved indicated that on average the Division reviewed approximately ten per year. On average the process took 30 months from the submission of the project to approval by the Minister. In one case, the approval took over eight years.

Our sample of approvals included both those which required Board hearings and those which did not. When submissions did not require Board hearings, the average time for approval was about 26 months. However, the Ministry's Practices and Procedures Manual suggested 12 months for processing and approving such submissions.

Ministry officials indicated that an amendment to the Act, effective January 1, 1997, was meant to address the concerns relating to the environmental assessment process as follows.

- The amendment requires proponents of projects to indicate specific terms of reference at the beginning of the environmental assessment process.
- Once the terms of reference are approved by the Minister they become binding on the proponents, the Ministry and the Board, and no additional issues can be introduced. A mediation process and strict timeframes are to be imposed for all key steps throughout the environmental assessment process, thus ensuring that issues are identified and resolved on a timely basis.

However, the amendment was criticized by environmental groups. These critics indicated that the amendment requires proponents to consult such persons as may be interested when they are preparing proposed terms of reference for an environmental assessment. However, what constitutes "consultation" and "interested person" is not clearly defined. Thus, there is no assurance that all interested persons will be consulted. The proponents of a major project have considerable time and resources to prepare the terms of reference. Conversely, outside stakeholders may not have sufficient time to come forward with their concerns. Consequently, significant issues of a complex nature may never be addressed.

According to the Ministry, the amended legislation empowers the Ministry to issue a deficiency statement when an environmental assessment submission is incomplete or inadequately prepared. If the deficiency is not addressed within seven days, the Minister may reject the submission.

As the legislation has just been amended, it is too early for us to assess its impact on the environmental assessment process.

MEASURING AND REPORTING ON THE EFFECTIVENESS OF ENVIRONMENTAL ASSESSMENT

As previously indicated, the stated objective of the *Environmental Assessment Act* is to provide for the protection, conservation and prudent management of the environment. However, there are no indicators in place for measuring and reporting on the effectiveness of the Ministry in achieving this objective.

The environmental assessment process often imposed terms and conditions on proposed projects. Essentially, the process is a prediction of environmental impacts, and terms and conditions are designed to minimize damage to the environment. Terms and conditions sometimes include requiring proponents to report to other ministries or outside agencies that certain approval conditions have been met. However, there was a concern that the Ministry had no consistent process in place to regularly monitor compliance with all the terms and conditions, including the reporting requirement.

Establishing a mechanism for monitoring compliance with the terms and conditions and the effectiveness of the process would assist the Ministry in achieving a more effective assessment process.

Recommendation

For the environmental assessment process to be more effective, the Ministry should establish indicators to measure and report on the effectiveness of the process and monitor compliance with the terms and conditions of approved projects.

Ministry Response

On January 1, 1997, Bill 76 was implemented to increase the effectiveness of the Environmental Assessment program. In addition, the Environmental Assessment Branch was reorganized to include a Continuous Improvement Section whose primary function is to establish performance measurement systems that will monitor and evaluate the effectiveness and efficiency of the Environmental Assessment program and monitor Bill 76 improvements.

The approach includes allocating resources to develop a comprehensive and systematic project management and auditing system. Indicators will be established to measure success in addressing time, cost and certainty, and in providing environmental protection.

Reporting requirements to the respective ministries and agencies are regularly included in a project's terms and conditions of approval. These have included the requirement to submit annual progress reports, or report on the results of a monitoring program for review by the government agency to ensure compliance. These requirements will be built into the Branch's new performance measurement system.

FUNDING FOR WATER AND SEWAGE PROJECTS

Under the *Ontario Water Resources Act* and the *Environmental Protection Act*, the Ministry of the Environment and Energy is responsible for ensuring that drinking water and sewage effluent processed by treatment plants meet established health and environmental guidelines. Municipalities have received varying amounts of provincial funding for their water and sewage capital projects.

Since April 1, 1994 water and sewage projects have been funded under a new grant program called the Municipal Assistance Program (MAP). By March 31, 1997 MAP had committed \$400 million to assist municipalities with 229 construction projects with total costs of over \$800 million. At the time of our audit in early 1997, about \$300 million of MAP funding had been disbursed to the municipalities.

Grants are based on a number of weighted factors including a community's population, with funding up to 70% of gross costs for communities with less than 1,000 people. All municipalities are eligible for additional assistance of up to 15% of gross costs depending on the number of provincial priorities being met. With additional assistance from the Ministry of Northern Development and Mines, some northern communities can obtain provincial funding up to a maximum of 92.5% of total capital costs.

PROJECT APPROVAL

To be considered for MAP funding, a proposed project has to address one or more of the following provincial priorities: Environment / Health; Economic Renewal / Regional Development; Growth Management/ Intensification; and Water Efficiency / System Optimization. Ministry staff score and rank project applications based on how well the municipalities address the various elements of the provincial priorities. Depending on funding availability, a cutoff score is established. Projects with scores above the cutoff are approved for funding.

DUE REGARD FOR ECONOMY

Predecessor grant programs aimed to alleviate significant health, environmental or growth problems related to water or sewage services. MAP introduced an additional objective of promoting water conservation as well as regular maintenance and the efficient use of existing water and sewage facilities.

In our 1993/94 audit of the previous grant program, we reviewed a sample of water and sewage projects which had received funding for expanding the existing capacity. Our review indicated that if water conservation measures had been taken, the need for many of the projects could have been eliminated or deferred for an extended period of time. For example, by repairing damaged water mains, installing water meters and charging customers for water based on volume used, two municipalities were able to lower their peak water demand by approximately 50%. In addition, the need for \$50 million in expansion capital projects for the two municipalities was deferred for up to 20 years.

In 1993/94 ministry officials indicated that there was little incentive for some of the other municipalities to implement water conservation measures as they were eligible for larger grants for expansion than for rehabilitation projects. They also mentioned that many municipalities

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should have undertaken water conservation and system optimization measures instead of applying for expansion grants when their plants were at capacity. Approval would most likely be given for the expansion, as holding up an expansion project where a plant was close to capacity would mean taking on significant health/environmental risks.

At the time of our audit in 1993/94, the Ministry was in the process of evaluating new project applications under MAP. In light of the significant cost savings potential, we recommended that the Ministry tighten the funding guidelines to ensure that municipalities not only review water conservation and system optimization measures, but also implement any applicable cost-effective measures before expansion projects can be approved for provincial funding.

The Ministry responded by stating that it “has undertaken a pilot project to review the merits of undertaking water conservation programs before expanding an existing sewage treatment plant. It is expected that the pilot results can be used to improve funding formula criteria to promote water conservation over the next two years of program funding.” On April 18, 1995 the Ministry forwarded a progress report to the Legislative Assembly’s Public Accounts Committee indicating that the “pilot activities have now shown that demand management measures, like those listed by the auditor, are often cost effective” and that “system optimization and water conservation are now important criteria for grant eligibility.”

However, at the time of our current audit there was still no requirement for applicable water conservation and system optimization measures to be implemented before expansion projects could be approved for provincial funding. In almost half of the expansion project files that we examined, water conservation / system optimization studies were either not completed or recommendations for such measures were not implemented.

Recommendation

To ensure due regard for economy, the Ministry should require municipalities to not only review water conservation and system optimization measures, but also implement any applicable cost-effective measures before expansion projects are eligible for provincial funding.

Ministry Response

The Ministry agrees with this recommendation. The recently announced Environmental Infrastructure Program provides assistance to municipalities for water and sewage projects. In accordance with this program, the municipalities will be required to identify cost-effective strategies to meet their needs.

VERIFICATION OF KEY INFORMATION

We reviewed MAP application files and noted that Ministry staff had not verified information provided by municipalities that could have a major impact on eligibility and the amount of funding for water and sewage projects.

Our review indicated that many applications lacked supporting documentation. This was of particular significance in cases where the municipalities were eligible to receive an increased grant rate if certain requirements were met. For example, the section of the application that dealt with economic renewal explicitly requested supporting documentation for the information provided. However, for 37% of the projects that received the additional 5% assistance for economic renewal, there was no supporting documentation on file. In some cases the overall scores, excluding the scores for the economic section, would not have been sufficient for the municipalities to receive provincial funding.

Recommendation

The Ministry should ensure that appropriate documentation is received to substantiate critical information on the application that may have a direct impact in determining eligibility and the amount of provincial funding for water and sewage projects.

Ministry Response

The Ministry will provide the municipalities with instructions regarding the appropriate documentation which is required for the Ministry to determine funding eligibility and funding levels.

MONITORING GRANT PAYMENTS

The Ministry provides funding advances to municipalities based on the previous quarterly expenditures claimed and forecasted expenditures for the current quarter. A 10% holdback is imposed on projects until a final audit on the completed project is performed by an evaluation engineer of the Ministry to determine the eligibility of expenditures claimed.

Our review of relevant work performed by the Ministry's Management Audit Branch indicated that the Ministry did not monitor grant payments on a timely basis to ensure that funds were spent only for intended purposes. Specifically, management audit staff of the Ministry observed the following.

- Projected cash flow requirements submitted by municipalities were often overstated, resulting in overpayments in excess of the 10% holdback.
- Advances totalling \$14 million for about 140 projects had been outstanding for two or more years without any claims for actual expenditures being submitted. At the completion of our audit, the Ministry had not determined the status of the projects or of the advances outstanding.
- Final audits by the evaluation engineers indicated that over 84% of the projects audited had some ineligible costs. In 1994 and 1995 final audits identified ineligible actual expenditures claimed totalling over \$58 million in gross costs, representing almost \$19 million in provincial grants. Even when 10% holdbacks were taken into consideration, there were still net overpayments of approximately \$3.6 million relating to 70 projects. At the completion of our audit, the Ministry had recovered about \$2.3 million by offsetting the overpayments

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against other grants due to the municipalities and had invoiced the municipalities for the remainder.

Ministry staff indicated that many projects did not file final claims on completion of their projects. Even where final claims were filed, it often took over six months before the evaluation engineers had time to determine whether the actual expenditures claimed were eligible. The significant delay in identifying ineligible costs resulted in disputes and the inability of some municipalities to repay the grant overpayments.

Recommendation

To ensure the timely recovery of grant overpayments, the Ministry should:

- better assess municipalities' cash flow requirements;
- more closely monitor when the claims for actual expenditures are being submitted;
- actively follow up long-outstanding advances; and
- expeditiously determine the eligibility of claimed expenditures.

Ministry Response

The Ministry agrees with this recommendation, noting that the recommendation should improve program delivery.

The Ministry currently assesses the municipalities' cash flow requirements by using a system which updates actual and estimated project expenditures that are tied to requests for grant advances submitted by the municipalities. Future funding programs will require that the municipalities submit specific cash flow projections in writing on a quarterly basis, and legal agreements will stipulate this requirement.

The payment procedure includes the provision for withholding 10% of the approved grant until the final cost audit has been performed. The purpose of this holdback is to address the issue of overpayment.

In 1996 the Ministry contacted municipal clients regarding outstanding advances. The municipalities submitted final claims and provided the documentation necessary for the Ministry to perform final audits and determine recoveries. The Ministry will continue this practice on a regular basis. In addition, the Ministry will place a "payable by" date on the recovery letters to the municipalities.

The Ministry has taken steps to address the existing volume of final cost audits through various measures, including: the reassignment of staff, the development of approved workplans and monitoring performance on a monthly basis.

The Ministry will assess the impact of these changes and review the program to determine if further improvements can be made to ensure a more timely recovery of grant overpayments.