

**COMPLIANCE REVIEW REPORT  
for Aboriginal Affairs and Northern Development Canada  
Nutrition North Canada**

**Contribution Agreement  
Signed on March 30, 2011  
with  
Arctic Ventures 2000 Ltd.**

**by Samson & Associates  
March 31, 2012**

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## 1.0 Executive Summary

On April 1, 2011, the Nutrition North Canada replaced the Food Mail Program, which was operated by Canada Post since the late 60's. Much like Food Mail, the purpose of Nutrition North Canada is to make nutritious food more accessible and more affordable to residents of isolated northern communities that lack year-round surface and marine transportation links to southern centres.

Accordingly, Aboriginal Affairs and Northern Development Canada commissioned a compliance review based on specific objectives for the period covering April 1, 2011 to December 31, 2011. The results of the review are as follows:

### i) Passing on the Subsidy

**Review Objective:** Verify that the recipient is passing on the value of the subsidy to customers, i.e. that selling prices are reduced by the amount of the subsidy.

**Finding:** The shift to more premium items within product categories during the review period has resulted in overall product category prices to remain at pre-subsidy levels or be just slightly less than the shelf prices customers paid before the NNC subsidy is applied.

**Finding:** For eligible NNC heavy and bulky items typically sea lifted, the impact of the subsidy is to mitigate air transport costs and has no impact on the shelf price of these items.

**Conclusion:** The review concludes that the recipient is passing on the value of the subsidy to the purchaser of eligible NNC products.

### ii) Program Visibility

**Review Objective:** Verify that program visibility requirements are met (e.g. subsidy rates are written on cash receipts and program material, such as posters, are clearly visible in the store).

**Conclusion:** The review found that the recipient was clearly identifying the NNC subsidy on cash register receipts and signage was on display throughout the store.

### iii) Claims and Reporting

**Review Objective:** Test the recipients' reporting and claiming systems and procedures with regards to gap and control issues, i.e. verify that the process used by the recipient to prepare detailed reports and calculate the amount of subsidy to be claimed is sound and precise, and that mechanisms to detect and correct errors are in place.

**Finding:** Arctic Ventures does not claim the five percent packaging allowance.

**Conclusion:** With the exception of the omission of the five percent packaging costs in the

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subsidy claim, the review of the reporting and claiming systems and procedures revealed that the controls were adequate to ensure the subsidy being claimed is precise and that the mechanisms to detect and correct errors were in place.

**iv) Respect of Program Rules**

**Review Objective:** Verify that recipients respect all program rules, especially in regards to sales to ineligible customers such as mining camps or construction companies.

**Conclusion:** The review revealed that the recipient was respecting the program rules with respect to sales to ineligible customers.

## **2.0 Introduction**

### **2.1 Background**

On April 1, 2011, Nutrition North Canada (NNC) replaced the Food Mail Program, which was operated by Canada Post since the late 60's. Much like Food Mail, the purpose of NNC is to make nutritious food more accessible and more affordable to residents of isolated northern communities that lack year-round surface and marine transportation links to southern centres.

There are currently 103 communities eligible for the program (82 are eligible for a full subsidy and 21 for a partial subsidy), located in Nunavut, the Northwest Territories, Yukon, Labrador, Quebec, Ontario, Manitoba and Saskatchewan. Two levels of subsidy rates per kilogram have been established for each community; Level 1 (higher) for the most nutritious perishable foods and Level 2 (lower) for other eligible items. Communities where operating and transportation costs are higher (e.g. Grise Fiord, Nunavut) tend to have higher subsidy rates.

Northern retailers and southern suppliers registered with the program (the recipients) are responsible to manage their supply chain and claim a subsidy from NNC for eligible food and non-food items that they air ship to eligible communities. On a monthly basis, they must submit a claim form (kg x subsidy rates), a detailed shipment report (kg per item, community, client type, etc.), invoices and waybills to receive the payment (most receive advance payments based on forecasted weights). These documents are submitted to the program's claims processor under contract with Aboriginal Affairs and Northern Development Canada (AANDC) (the Saskatchewan Institute of Information Technology in collaboration with Crawford). The claims processor verifies the claims and provides NNC with a recommendation for payment. Registered northern retailers must also submit, directly to NNC, a monthly pricing report for a pre-determined list of food items. These and other program requirements are identified in contribution agreements between the recipients and AANDC.

As of December 31, 2011, seven northern retailers and 26 southern suppliers were registered with NNC. Northern retailers are those entities that operate one or multiple food retail stores in eligible communities. Southern suppliers are food providers operating out of non-NNC eligible communities that supply eligible items directly to small northern retailers, commercial establishments (restaurants, etc.), social institutions (daycares, etc.) and individuals (referred to as direct or personal orders) located in eligible communities.

The selection of recipients for this compliance review was based on perceived risk and geographical location. Risk levels for compliance review purposes were based on the current experience with recipients regarding the claiming and reporting process, i.e. difficulties encountered by the claims processor, on information brought to the program's attention by interested parties, and on materiality. For practicality and cost-effectiveness reasons, at least two recipients have been selected per geographical location.

### **2.2 Objectives**

The objective of the recipient compliance review is to provide assurance that the NNC recipient is in compliance with the terms and conditions of the funding agreements signed with AANDC. Specifically, the compliance review will:

1. Verify that recipients are passing on the value of the subsidy to customers, i.e. that selling prices are reduced by the amount of the subsidy;
2. Verify that program visibility requirements are met (e.g. for northern retailers, that subsidy rates are written on cash receipts and program material, such as posters, are clearly visible in the store, and, for southern suppliers, that the amount of the subsidy reduction is clearly identified on customers' invoices);
3. Test the recipients' reporting and claiming systems and procedures with regards to gap and control issues, i.e. verify that the process used by recipients to prepare detailed reports and calculate the amount of subsidy to be claimed is sound and precise, and that mechanisms to detect and correct errors are in place; and
4. Verify that recipients respect all program rules, especially with respect to sales to ineligible clients such as mining camps or construction companies.

### **2.3 Scope**

The scope included the funding provided by AANDC to Arctic Ventures 2000 Ltd. (Arctic Ventures) for the period April 1, 2011 to December 31, 2011. The review was conducted at the offices of Arctic Ventures in Iqaluit, Nunavut, from March 5 to 9, 2012.

### **2.4 Approach and Methodology**

The compliance review included the examination of the following:

- The pricing/invoicing practices in relation to the subsidy, e.g. profit margins on subsidized products vs. unsubsidized products;
- The weighing and shipping process;
- Accounts receivable to ensure that ineligible customers such as mining and construction companies are not receiving the subsidy;
- The sale and/or purchasing records and supporting documentation to verify compliance with program rules;
- The reporting and claiming systems and procedures, to determine how the recipient:
  - ensures that only eligible items are claimed for and reported;
  - calculates the appropriate weight of items being claimed;
  - makes monthly claims and detailed reports that are valid and accurate; and
  - ensures controls are in place to find errors and fix them on a timely basis.

Furthermore, the review included the conduct of interviews with the recipient. The sampling approach and appropriate coverage were determined during the planning phase of the review.

### **2.5 Conclusion**

The recipient has complied with the objectives of the review.

### **3.0 Compliance with the Objectives**

#### **3.1 Passing on the Subsidy**

**Review Objective:** Verify that the recipient is passing on the value of the subsidy to consumers, i.e. that selling prices are reduced by the amount of the subsidy.

**Finding:** The recipient has instituted procedures to ensure that the value of the subsidy is passed on to customers through lower prices.

**Conclusion:** The recipient is passing on the subsidy to the consumer for NCC eligible items shipped by air freight.

**Observation Note:** The recipient reported that there has been a shift to more premium products which typically have a longer shelf life. This has occurred within the last year and has somewhat lessened the impact of the subsidy on retail prices. For example, Lactantia PurFiltre milk has replaced Nielsen milk which has a much shorter shelf life. Management was of the opinion that one impact of the NNC program has been to make consumers more aware of the products that they purchase and, in the process, more aware of product expiry dates. The shift to Lactantia has meant fewer returns but a slight increase in price for the milk.

Product categories such as produce have also seen a shift to more premium items, particularly those which are organically grown. The store manager noted that since the launch of NNC there has been the virtual disappearance of the long weekend line-ups at the airport for individuals and firms receiving merchandise shipments. Under the Food Mail Program, it was not unusual to have 100 people at the airport on a Saturday morning to receive goods purchased from the South. Today, all merchandise formerly being purchased in the south is now being bought in the north. This shift has resulted in a 100% increase in produce sales during the review period. Arctic Ventures is now able to provide produce of better quality, look and freshness by shipping directly out of Ottawa, a supply chain option that was not permitted under Food Mail.

Sea lift of non-perishable foods and non-food items to the recipient's store are made twice per year, in July and October. Stock items which weigh a lot such as flour, sugar or jam or items which are bulky, such as napkins and diapers, are typically shipped by sea. The freight rate for sea lift varies each year and is significantly lower than that for air freight. Consequently, determining the correct amount to order for an item for sea lift is critical for the store. If shortages of an item that has been sea lifted occur, resupplying has to be by air freight. The recipient noted that customers will be lost if certain products such as diapers or jam are out of stock at the store. An examination of supplier invoices for Arctic Ventures found very few cases of non-perishables and non-food items being brought in by plane between July to October. For example, no flour was ordered during this period as the July sea lift order was sufficient to carry the store to the October sea lift. The grocery manager provided a tour of the main sea lift inventory during the review. Substantial quantities of heavy and/or bulky items were observed as part of the sea lift component of inventory.

When an NNC eligible item that is normally shipped by sea lift is ordered by air freight, the store manager explained that even taking into account the NNC subsidy, the landed air freight costs are still higher than the landed freight costs associated with sea lift. Shipment by air is so significantly higher than sea lift that the subsidy does not compensate for the difference. Consequently, in these cases, the NNC subsidy has no impact on the shelf price of the item but only serves to mitigate sea lift order quantity forecasting errors in demand for the item.

### **3.2 Program Visibility**

**Review Objective:** Verify that program visibility requirements are met (e.g. that subsidy rates are written on cash receipts and program material, such as posters, are clearly visible in the store).

**Finding:** The review found that the recipient was clearly identifying the NNC subsidy rates on cash receipts and that program material, such as posters, are clearly visible in the store.

**Observation Note:** During the walkthrough of the sales floor, it was noted that posters advertising the NNC program are placed strategically throughout the store in six different locations. The NNC subsidy rates are written in marker below the photos on the posters.

The NNC program signage has been a bit of a problem according to the store manager. At the time of this review, the posters are looking tattered and need to be replaced. Arctic Ventures received two shipments of signs but the poster remains the same. In the retail business, stores are not putting up pictures but signs which need to be changed frequently so as to attract the attention of customers.

### **3.3 Claims and Reporting**

**Review Objective:** Test the recipients' reporting and claiming systems and procedures with regards to gap and control issues, i.e. verify that the process used by recipients to prepare detailed reports and calculate the amount of subsidy to be claimed is sound and precise, and that mechanisms to detect and correct errors are in place.

We tested the recipient's reporting and claiming procedure by selecting a random number of transactions from the total claims produced from April 1, 2011 to December 31, 2011 by using statistical sampling techniques.

**Conclusion:** The review of the reporting and claiming systems and procedures revealed that the controls were adequate to ensure the subsidy being claimed is precise and that mechanisms to detect and correct errors were in place.

### **3.4 Respect of Program Rules**

**Review Objective:** Verify that recipients respect all program rules, especially in regards to sales to ineligible customers such as mining camps or construction companies.

***Finding:*** Arctic Ventures has established effective controls to ensure that ineligible customers are not accessing the NNC subsidy on eligible items.

A review of the current accounts receivable was undertaken with the office manager. A sample of three customers was selected comprising a mining, an electrical as well as construction company, and the purchase orders of the companies were examined. For each company selected none of the purchase orders contained eligible items. While there is no restriction on what may be purchased by these companies, the office manager noted that these accounts are typically established to acquire electronic and hardware items as well as special order items.

***Conclusion:*** The review revealed that the recipient was respecting the program rules with respect to sales to ineligible customers.

**APPENDIX A - Recipient's Comments to the Draft Report and the Auditor's Response**

**Recipient's Comments:**

I have read the Draft report and do agree with the findings.

John Bens  
Arctic Ventures 2000 Ltd.

**Auditor's Response:**

No response required.