Cash Disbursements - Direct Lending
Audit Report
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Distribution:

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Vice President & Corporate Controller
Assistant Corporate Controller
Director, Loans Services and Corporate Accounts Receivable

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Introduction

As per our 2015 Audit Plan, Internal Audit performed an audit of the Cash Disbursements - Direct Lending process. Loan agreements are developed and negotiated by EDC Business Teams. Loans Services has the responsibility for the post-signing management and general administration of the loans, and Corporate Banking is responsible for the wire transfer of funding to clients. EDC processes over 860 direct lending disbursements a year amounting to approximately $8B of cash outflows.

Audit Objectives & Scope

The overall objective of our audit was to review controls over disbursements for Direct Lending including:

- Policies and procedure framework including the Resolution Respecting Signing Authorities, Loans Services Delegation of Authority (DOA) and procedures within Corporate Banking;
- Segregation of duties including whether the preparation, reviews, and approvals over disbursements are appropriately segregated;
- Authorization and recording of payments; and
- Daily cash reconciliations.

The scope of this audit was to review the design and operating effectiveness of controls over the Cash Disbursements - Direct Lending process. This includes all disbursements related to such loans from the point of setting up the facility in the Loan administration system. While our scope included all key controls unique to direct lending disbursements, many of these controls are common to all disbursements.

Consideration was given to the effectiveness of controls to mitigate fraud risk. The testing period for our audit was from July 2014 to July 2015.

Internal Audit Opinion

In our opinion, the Cash Disbursements - Direct Lending process is ***"Well Controlled"***.[1] We found that key controls pertaining to the Direct Lending disbursements process are effectively designed and operating as intended. One moderate issue related to reconciliations was noted and is described in the following section. Management has agreed to implement the corrective actions no later than Q4 2015.

[1] Our standard audit opinions are as follows:

- **Strong Controls**: Key controls are effectively designed and operating as intended. Best in class internal controls exist. Objectives of the audited process are most likely to be achieved.
- **Well Controlled**: Key controls are effectively designed and operating as intended. Objectives of the audited process are likely to be achieved.
- **Opportunities Exist to Improve Controls**: One or more key controls do not exist, are not designed properly or are not operating as intended. Objectives of the process may not be achieved. The financial and/or reputation impact to the audited process is more than inconsequential. Timely action is required.
- **Not Controlled**: Multiple key controls do not exist, are not designed properly or are not operating as intended. Objectives of the process are unlikely to be achieved. The financial and/or reputation impact to the audited process is material. Action must follow immediately.

Audit Findings & Action Plans

1. Reconciliation Controls

Cash reconciliations help to detect fraud and/or errors relating to cash flows and are an important monitoring control for management. Accordingly, two cash reconciliation controls have been designed and implemented. The Morning Cash Reconciliation (MCR) examines the anticipated closing cash balance of the previous day to the actual opening cash balance that morning. This is a daily control and the purpose of the reconciliation is to confirm that the actual cash balance is consistent with expectations based on disbursements released the previous day. Any discrepancies are investigated and resolved. The End of Day (EOD) Cash Reconciliation control compares the number of transactions per the Cash Management System to the number of transactions processed in the wire transfer system. This is a daily control and the purpose is to confirm that all disbursements expected to have been processed matches the total released disbursements and would identify if any additional disbursements were released or if any were missed.

The MCR completed by Corporate Banking does not have defined thresholds for items requiring investigation and resolution. Through discussions with management it was noted the threshold was $3M however, during testing we noted this threshold was not always adhered to and variances greater than the threshold were left unexplained. Based on substantive testing performed, we were able to obtain satisfactory explanations for these variances from the Corporate Banking team. Nevertheless, a lack of documentation regarding the investigation and resolution of variances increases the risk that an issue and/or error is not identified and resolved in a timely manner.

Additionally, we noted several instances where both the MCR and EOD reconciliations were not signed off by a reviewer as evidence it was reviewed and approved by the appropriate Corporate Banking officer. A lack of documented review and approval increases the risk that unauthorized cash transactions are processed and not detected.

Management has agreed to develop and implement procedural documentation detailing the MCR process which will define the threshold of variances that must be investigated and the assumptions for determining reasonability of the threshold. Additionally, Management will ensure reconciliations are reviewed and approved by an independent Corporate Banking Officer.

Rating of Audit Finding – Moderate[2]
Action Owner – Assistant Corporate Controller
Due Dates – Q4 2015

[2] The ratings of our audit findings are as follows:

- **Major**: a key control does not exist, is poorly designed or is not operating as intended and the financial and/or reputation risk is more than inconsequential. The process objective to which the control relates is unlikely to be achieved. Corrective action is needed to ensure controls are cost effective and/or process objectives are achieved.
- **Moderate**: a key control does not exist, is poorly designed or is not operating as intended and the financial and/or reputation risk to the process is more than inconsequential. However, a compensating control exists. Corrective action is needed to avoid sole reliance on compensating controls and/or ensure controls are cost-effective.
- **Minor**: a weakness in the design and/or operation of a non-key process control. Ability to achieve process objectives is unlikely to be impacted. Corrective action is suggested to ensure controls are cost-effective.

Conclusion

The audit findings have been communicated to and agreed by management, who has developed action plans that are scheduled for implementation no later than Q4 2015.

We would like to thank management for their support throughout the audit.