

**Delegation of Authority
Final Audit Report
Report #22/16
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Introduction

As per our FY2015 Audit Plan, Internal Audit performed an audit of EDC's Delegation of Authority process. This process is operationalized through GEN 002 which is the policy on Delegations of Authority (DOA). GEN 002 contains 26 appendices which includes notes and tables outlining the DOA levels by transaction type. The appendices are an integral part of the DOA Policy. The President & CEO of EDC has the authority to act in the conduct of the business of the Corporation in all matters that are not specifically reserved to the Board. The President in turn delegates authority through various DOA appendices, or via individual letters.

Audit Objectives & Scope

The overall objective was to evaluate the controls surrounding the review and update of GEN 002 and related appendices. This included whether the appendices of GEN 002 were comprehensive and address relevant aspects of EDC's business activities. The scope of the audit included a review of the design of controls over the DOA process for Insurance and Financing appendices. Audit fieldwork was performed during Q4 2015.

Internal Audit Opinion

In our opinion, "*Opportunities Exist to Improve Controls*"¹ within the Delegation of Authority process. A number of individual changes have been made to the Appendices of GEN 002 over the years to address changes in EDC's business activities. Through these cumulative changes, the DOA tables have become complex. In addition, some gaps and inconsistencies in the tables have emerged. While these matters are important, there is no indication that they have resulted in a lack of oversight on business transactions. Management will initiate a comprehensive review of the DOA policy as part of the ERM build out and will include consideration of the detailed findings from this audit.

Audit Findings & Action Plans

1. Periodic Review of GEN002 and Appendices

The DOA Policy (GEN 002) outlines the roles and responsibilities of key aspects of the DOA process. Specifically, Gen 002 states that the SVP Legal Services & Corporate Secretary is responsible for the overall policy. In addition, each SVP is the DOA sponsor of their applicable DOA Appendices but may delegate a member of their team to be the sponsor. As per GEN 002, the DOA sponsor is required to

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.

review the DOA applicable to their business activities not less than once every three years to determine if amendments are needed and if so, effect such amendments. During the audit, we found that responsibility for maintaining the overall DOA policy is not clear as the position of SVP Legal Services & Corporate Secretary no longer exists. As well, DOA sponsors are not always performing regular reviews of the Appendices. Instead, changes to the Appendices have been done on an ad-hoc basis. As a result:

- The DOA tables and notes have become complex and difficult to interpret. For example, the definition of a Tier 1 Authority is not consistent across each appendix. The Tier 1 authority for approving Credit Insurance policy liabilities is the SVP or President whereas a VP is considered Tier 1 authority in other Appendices;
- Inconsistencies have emerged across and within DOA tables. For example, similar risks have different DOA requirements across programs. We also noted that within Financing the DOA for a new transaction is based on the dollar value of the individual transaction whereas any subsequent WAC (waiver, amendment or consent) to that transaction is based on the aggregate exposure to the obligor; and
- DOA has not been defined for some business activities. For example, a Board approved policy exists outlining the methodology for approving obligor risk limits. However, the limit established for an obligor is not subject to DOA. Changes to standard insured risks, EDC's rights and, policyholder obligations are subject to procedural approvals but do not require formal DOA approval. Decision support models (DSM) are used within some product lines to approve exposures. We found that the applicable DOA table does not always address DSM approvals and who can change a DSM.

A DOA workstream is being incorporated into the ERM Transformation Program. Once this workstream is defined, management has agreed to develop action plans to ensure that roles and responsibilities are better defined and performed. Action plans will also address how to identify and correct non-conformance.

Rating of Audit Finding - Major²

Action Owner – To be confirmed by the SVP, CRO

Due Dates – Action Plans will be developed by Q1 2017

2. Inconsistencies between GEN 002 and the Risk & Capital Management Policy (RCMP)

The Risk and Capital Management Policy (RCMP) contains policies that describe EDC's perspective on the prudent origination and management of its risks and capital structure. The RCMP is approved annually by the Board of Directors. During the audit, we noted that DOA topics are sometimes addressed

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.

in the RCMP and the content is not always consistent with the requirements of GEN 002. For example, the Credit Granting Policy within the RCMP states that all decisions must be “recommended and approved”. However, the Appendices to GEN 002 only require one approver and no recommender for some smaller exposures. In addition, the RCMP states that credit commitments in excess of certain thresholds also require an independent endorsement. However, the C1 PRI Appendix allows one SVP to be both the approver and endorser. Some additional inconsistencies were noted between the RCMP and GEN-002 and have been reviewed with management. Management will be developing an action plan to ensure inconsistencies between the RCMP and GEN-002 are identified and eliminated.

Rating of Audit Finding - Major

Action Owner – To be confirmed by the SVP, CRO in Q1 2017

Due Dates – Action Plans will be developed by Q1 2017

3. Segregation of Duties

Delegation of authority enables both empowerment and better oversight by moving decision-making to individuals closer to the transactions. However, a critical challenge in delegating authority is to ensure segregation of duties (SOD) is maintained. During the audit, we noted some instances in the DOA tables where segregation of duties could be strengthened. For example, one Tier 1 authority has been assigned the ability to approve policy liabilities, risk ratings, credit exposures, and claim payments. The ERM Transformation Program will include significant changes to the existing DOA structure/levels. Management has developed action plans to resolve SOD conflicts within the existing DOA tables and will develop an action plan to ensure SOD is addressed as part of the DOA Workstream within the ERM Transformation Program.

Rating of Audit Finding - Moderate

Action Owner – To be confirmed by SVP, CRO in Q1 2017

Due Dates - Action Plans will be developed by Q1 2017.

4. Escalation of Important Policy Matters

The DOA Appendices include text requiring DOA authorities to refer any credit commitment that involves other important policy issue to an SVP to determine if the credit commitment should be approved or referred to the President for approval. Although some examples are included, a definition of an “important policy issue” is not provided in the Appendices. One of the examples is if a credit commitment were to include an important environmental or CSR issues. This could be confusing as the current CSR and environmental policies contain specific requirements on escalating of issues. Management has agreed to develop an action plan to address the escalation of exceptions once the DOA Workstream has been defined under the ERM Transformation Program.

Rating of Audit Finding - Moderate

Action Owner – To be confirmed by SVP, CRO in Q1 2017

Due Dates - Action Plans will be developed by Q1 2017.

Conclusion

The audit findings have been communicated to and agreed by management, who will develop action plans no later than Q1 2017. We would like to thank management for their support throughout the audit.