

**Corporate Portfolio Management - Credit Insurance  
Final Audit Report  
Report Nr. 06/10  
March 30, 2010**

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## Introduction

In accordance with our Audit Plan, EDC Internal Audit performed an audit of Corporate Portfolio Management for credit insurance. Corporate Portfolio Management is the planned and continuous, ongoing monitoring activities done to identify changes in credit risk post origination. It includes the mitigation strategies and tools used to manage these exposures and the measurement and reporting of these exposures to management and the Board. The Credit Monitoring and Review Policy establishes the standards for monitoring EDC's portfolio of credit commitments within the Financing Group and Insurance Group programs, and describes the process for assessing changes in credit risk. The policy has the goal of ensuring that EDC's credit commitments are monitored appropriately, and if post-commitment actions may be required, to outline decision making and reporting responsibility for such actions. EDC's corporate portfolio of credit exposure includes credit insurance, loans, bonding and trade finance obligations.

## Audit Objectives & Scope

This report contains the findings for the audit of the credit insurance component of EDC's portfolio. The overall objective of this audit was to review the design effectiveness of the internal controls over the Corporate Portfolio Management process of EDC's portfolio of credit insurance commitments for:

- Changes in credit risk post-origination;
- Credit risk measurement at the portfolio level for credit insurance; and,
- Credit risk mitigation activities (e.g. reinsurance, hedging, etc.).

In examining corporate portfolio management for credit insurance, the audit addressed the following risk elements of EDC's Enterprise Risk Management (ERM) framework: insurance, compliance, change management & alignment, transaction processing, governance, system and portfolio concentration & capital allocation.

Audit fieldwork was performed from October 2009 to March 2010.

## Internal Audit Opinion

In our opinion the design effectiveness of the Corporate Portfolio Management process for the credit insurance portfolio is **Well Controlled**<sup>1</sup>. No major<sup>2</sup> control issues were noted. Two moderate issues were noted and are described in the following section.

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<sup>1</sup> 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.

<sup>2</sup> Our audit findings are ranked 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.

## Audit Findings & Recommendations

### 1. Credit Insurance Exposure Reporting

Each quarter, a risk management report is prepared for the Board which includes an analysis of the credit exposures in aggregate and also by industry sector, country and top obligors and how they compare to policy limits. Credit insurance exposures are included for information purposes but are not included in the reported aggregate, sector, country or top obligor credit exposure amounts and are not considered when reporting against limits. Credit insurance exposures are short-term in nature, and the risks associated with the products differ from the risks associated with medium/long-term products making a meaningful aggregation complex. However, limits should take an aggregate view of credit risk from all sources within the Corporation. Therefore we recommend that the Risk Management Office (RMO) work in collaboration with VP, Credit Insurance Underwriting to develop a timeline for including credit insurance exposures with EDC's other credit exposures under a single credit exposure limit framework.

Rating of Audit Finding - Moderate

Action Owners - VP, Portfolio Management in collaboration with VP, Credit Insurance Underwriting

Due Date - Q4 2010

### 2. Risk Mitigation

An important aspect of the Relationship and Asset Management (RAM) group's role is to provide exposure and portfolio risk management solutions via reinsurance and other means for all of the Insurance Group's contingent liabilities. An operational framework for RAM detailing approved activities, strategies and delegation of authorities to mitigate the risk of significant loss in EDC's Insurance portfolio has not been defined. As a result, risk transfer activities have been limited to some reinsurance. IA is recommending that a mandate be established for RAM that includes a strategy, instruments and budgets based on a clearly defined risk appetite. In addition, key performance indicators should be established for the group in order to assess the impact and efficacy of their activities.

Rating of Audit Finding - Moderate

Action Owner - Manager, Relationship and Asset Management

Due Date: Q1 2011

## Conclusion

The audit findings and recommendations have been communicated to and agreed by management, who has developed action plans that are scheduled for implementation no later than Q1 2011.

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