OBM | Office of Internal Audit

Development Services Agency

Loan Processing Audit

Audit Period: July 2013 through March 2014

Results Summary:

Objective	Conclusion *
Loan Application Intake and Review	Improvement Needed
Loan Disbursement	Well-Controlled
Loan Collection	Well-Controlled with Improvement Needed

* Refer to Appendix A for classification of audit objective conclusions.

Report number: 2014-DSA-01 **Issuance date: June 25, 2014**

Executive Summary

Background

The Ohio Development Services Agency (DSA) Business Division has a variety of loans to assist Ohio companies to grow and create and retain jobs in Ohio, while the Minority Services Development Division offers loans to help small, minority and disadvantaged businesses contribute to job creation and growth in Ohio. The Community Division has a variety of loans to assist communities to improve economic development. DSA had outstanding loans for the following programs, as of March 2014:

- 166 Direct Loan Program - 174 active loans with an outstanding balance of $264.9 million
- Innovation Ohio Loan Fund - 85 active loans with an outstanding balance of $68.1 million
- Ohio Enterprise Bond Fund - 51 active loans with an outstanding balance of $251.2 million
- Minority Business Direct Loan - 9 active loans with an outstanding balance of $3.0 million
- Energy Loan Fund - 9 active loans with an outstanding balance of $20.1 million

During the audit, OIA identified opportunities for DSA to strengthen internal controls and improve business operations. OIA conforms to the *International Standards for the Professional Practice of Internal Auditing.* OIA would like to thank DSA staff and management for their cooperation and time in support of this audit.

This report is solely intended for the information and use of agency management and the State Audit Committee. It is not intended for anyone other than these specified parties.

Scope and Objectives

OIA staff was engaged to perform assurance work related to DSA's Loan Processing procedures. This work was completed between February and June 2014. The scope of this review included the key processes related to application intake, application review, disbursements, and collections for selected loan programs. The selected loan programs include: 166 Direct Loans, Innovation Ohio Loan Fund, Ohio Enterprise Bond Fund, Minority Business Direct Loans, and Energy Loan Fund. The scope of the review did not include loan monitoring processes. The audit period is July 2013 through March 2014.

The objectives of the review included the following:

1. Evaluate the design and effectiveness of controls within the application intake/review processes.

2. Evaluate the design and effectiveness of controls within the loan funds disbursement process.
3. Evaluate the design and effectiveness of controls within the loan collection process.

Detailed Observations and Recommendations

The Observations and Recommendations include only those risks which were deemed high or moderate. Low risk observations were discussed with individual agency management and are not part of this report. However, the low risk observations were considered as part of the audit objective conclusions.

Observation 1 – Office of Energy's Paper Loan Files are not Secured

Ohio Revised Code provides that each agency adopt rules regulating access to the confidential personal information (CPI) the agency keeps, whether electronically or on paper. Agencies should develop controls to address the protection of information deemed as personally identifiable from intentional or unintentional disclosure or misuse. Records including CPI and other confidential information should be maintained electronically, or in lockable filing cabinets or locked rooms when not in use.

The DSA Office of Energy receives Energy Loan Fund (ELF) applications and supporting documents from potential borrowers through a secured web portal, and maintains the documents electronically. However, the Office also prints loan documents and creates paper loan files. The paper loan files include sensitive information such as bank account numbers, tax documents, financial statements, and social security numbers. The Office does not maintain the paper loan files in lockable filing cabinets or in locked file rooms.

Paper loan files that are not properly secured increases the risk that borrowers' sensitive information is inappropriately accessed or compromised.

Recommendation

Evaluate the need of maintaining paper loan files with sensitive information when the information is also received and maintained electronically. Discontinue creating and maintaining the paper loan files if there is no longer a business need. Otherwise, maintain paper loan files containing sensitive information in locked cabinets or in locked rooms when not in use. Develop and implement agency policy and procedures surrounding documentation containing sensitive documentation to address, at minimum, securing all sensitive records and providing instances when secured documentation is to be maintained in electronic and paper formats.

Management Response

The Energy Loan Fund is currently being integrated into the SalesForce enterprise CRM platform. All loan documentation will be maintained in this electronic platform moving forward. A plan will be put in place to upload and then either secure or destroy all paper loan files.

Risk*	Remediation Owner	Estimated Completion Date
Moderate	Energy Incentives Section Supervisor Fiscal and Educational Programs Support Section Supervisor	December 2014

Observation 2 – Loan Application and Commitment Fees

Loan application fees are charged to cover a portion of the costs involved in processing a loan application. Commitment fees are charged to recover costs of outside legal counsel fees and any consultant fees for independent reviews conducted during loan application review processes. In order to ensure fees are received, DSA tracks receipt of fees and will not assign legal counsel to close loans if borrowers do not submit commitment fees.

Testing revealed DSA did not collect the following application or commitment fees prior to loan closing:

- $50,000 commitment fee for one of five (20%) closed ELF loans tested. The Office of Energy allowed the borrower to finance the commitment fee into the total loan amount rather than collecting the fee from the borrower to offset costs of outside legal counsel and financial consultant fees;
- $30,000 commitment fee for one of six (17%) tested financial incentive loans closed through the Office of Strategic Business Investments (OSBI). The OSBI received the commitment fee 26 days after the loan was closed; and
- $250 application fee for one of five (20%) closed ELF loans tested. The Office of Energy never collected this fee.

Additionally, the Minority Business Division does not centrally track receipt of commitment fees. This may increase the likelihood that outside legal counsel is assigned to close Minority Business Direct loans prior to receipt of commitment fees.

Failure to collect appropriate application fees and commitment fees results in fewer costs that DSA is able to recover for processing loans. Commitment fees that are not collected prior to the assignment of outside legal counsel increases the risk that DSA incurs fees for legal counsel.

Recommendation

Develop and implement procedures and controls to ensure loan application fees are received timely with loan applications and that outside legal counsel is not assigned to close loans until borrowers fully submit commitment fees. Centrally record and track the receipt of all fees so that every individual involved in processing loan applications are notified of the receipt of commitment fees prior to assigning outside legal counsel to close loans. Develop and implement an agency-wide policy over receiving and recording fees during loan application processes to ensure consistency across loan programs and to ensure controls are in place to prevent loan application processes from progressing in instances in which fees are not received.

Management Response

As every division and office charged with administering loan programs integrates the use of

SalesForce into loan program operations, DSA management will develop and implement an agency-wide policy over recording receipt of loan application and commitment fees in SalesForce. The policy will outline procedures and responsibility for verifying receipt of commitment fees prior to assigning outside legal counsel to close loans.

Regarding the ELF loan in which the commitment fee was financed into the total loan amount, this was one of the first loans issued through the ELF and the Office of Energy made a special exception. The Office of Energy has not since allowed financing of commitment fees into total loan amounts and will not do so with future ELF loans.

Risk*	Remediation Owner	Estimated Completion Date
Moderate	Chief Financial Officer	December 2014

Due to the limited nature of our audit, we have not fully assessed the cost-benefit relationship of implementing the observations and recommendations suggested above. However, these observations reflect our continuing desire to assist your department in achieving improvements in internal controls, compliance, and operational efficiencies.

* Refer to Appendix A for classification of audit observations.

Appendix A – Classification of Conclusions and Observations

Classification of Audit Objective Conclusions

Conclusion	Description of Factors
Well-Controlled	The processes are appropriately designed and/or are operating effectively to manage risks. Control issues may exist, but are minor.
Well-Controlled with Improvement Needed	The processes have design or operating effectiveness deficiencies but do not compromise achievement of important control objectives.
Improvement Needed	Weaknesses are present that compromise achievement of one or more control objectives but do not prevent the process from achieving its overall purpose. While important weaknesses exist, their impact is not widespread.
Major Improvement Needed	Weaknesses are present that could potentially compromise achievement of its overall purpose. The impact of weaknesses on management of risks is widespread due to the number or nature of the weaknesses.

Classification of Audit Observations

Rating	Description of Factors	Reporting Level
Low	Observation poses relatively minor exposure to an agency under review. Represents a process improvement opportunity.	Agency Management; State Audit Committee (Not reported)
Moderate	Observation has moderate impact to the agency. Exposure may be significant to unit within an agency, but not to the agency as a whole. Compensating controls may exist but are not operating as designed. Requires near-term agency attention.	Agency Management and State Audit Committee
High	Observation has broad (state or agency wide) impact and possible or existing material exposure requiring immediate agency attention and remediation.	Agency Management and State Audit Committee