

IFC Compliance & Reporting under Companies Act 2013

DFA Course Module 1 , Unit 22

18.03.2022

Internal & Forensic Audit - Gamechanger

- Transformation to RBIA
- Catalyst in reviewing Internal Controls, assistance in IFC framework implementation
- GRC / SPA & EPM , Risk Management
- Increasing role in fraud deterrence & detection, **forensic approach** in IA
- Extensive **deployment of BI, Data Analytics** & CAAT, Focus on Standards – **IIA, ISACA, SIA**
- **Companies Act 2013 : IFC** : Sec – 134, 138 , 177 on ERM, Audit Committees & IA, Vigilance
- CARO 2016 & 2020 on Internal Audit activities
- SEBI Clause 49 on Audit Committees
- Value – add & drive growth

Internal Controls & Internal Audit

- Internal controls are a system consisting of **specific policies and procedures** designed to provide **management with *reasonable assurance*** that the goals and objectives it believes important to the entity will be met.
 - Process to ensure:
 - **Reliability of financial reporting.**
 - **Effectiveness & efficiency of operations.**
 - **Safeguarding of assets.**
 - **Compliance with applicable laws & regulations.**
 - Designed, implemented & maintained by TCWG -- **Management & NOT Auditors**
 - Provides only reasonable assurance..

Why IFC

- **Promote operational efficiency** and effectiveness
- Provide **reliable financial information**, no financial misstatements
- Safeguard **assets and records** , **minimizes fraud & losses**
- **Encourage adherence to prescribed policies**
- **Comply with regulatory agencies**
- **Timely financial information**, secures brand image
- **Drive growth, contain costs, improve business process efficiency**

Internal Financial Controls

- **Audit Committee** is required to evaluate Company's "IFCFR" Sec.177 (4)(vii)
- **Directors' Responsibility Statement**, in the case of listed companies, to include a statement that they have laid down IFC to be followed by the company and that such IFC are adequate and were operating effectively – Section 134 (5)(e).
- The **report of the Board** shall also contain the details in respect of adequacy of IFCFR with reference to the Financial Statements - **Rule 8(5) (viii)**
- Auditors required to report on whether the company has **adequate internal financial controls** system in place and the **operating effectiveness of such controls** – Sec.143(3)(i)
- Standards on Auditing (SA) 700 issued by the ICAI, specifically required the auditor to state that the auditor's consideration of the internal controls in the entity are **not** for the purpose of expressing an opinion on the effectiveness of the entity's internal control
- Reporting on IFCFR deferred for one year i.e., upto 31.03.2015. applicable from FY 15-16
- **Management Responsibility – Establish Internal Control over Business Operations.**
- **Auditor Responsibility – Report on Internal Control over Financial Reporting**

Framework & date of IFCFR

- **Framework** – COSO 2013, CoCo – Turnbull Guidance, ICAI GN with SA 315 Appendix
- Reporting on internal financial controls system is **similar to reporting on operations** of the company. Whilst the **testing is carried out** on the transactions recorded **during the year**, the **reporting is as at the balance sheet date**.
- Reporting on **IFCFR will not be applicable with respect to interim financial statements** such as quarterly or half yearly statements **unless such reporting is required under any other law or regulation**
- **IFCFR on CFS** – Auditor of parent company will **consider the report of auditors of Indian components** and issue a report keeping in mind the concepts of materiality and professional judgment
- Previously in CARO, the mention was on the adequacy of the control whereas the focus has now extended **to adequacy plus operating effectiveness**. Extensive coverage to **all business cycles**

ICAI GN on IFC- Key highlights

- **Scope – significantly larger than CARO**
- **IFC (134) vs IFCFR (143)**
- **Document process flows**
- **Perform walkthroughs**
- **GITC , application controls, preventive & detective controls**
- **Segregation of Duties**
- **Controls benchmarking**
- **TODE (Design)**
- **TOCE (Operational)**
- **Sampling technique for TOC**
- **Timing of testing, extending sample size**
- **Remediation plans**
- **Opinion on IFCFR**
- **Document material weakness , if any**
- **Communication to TCGW (report to Board / Audit Committee)**
- **Reporting**

SIA 12, Internal Control Evaluation

(Issued in February 2009)

❖ Deals with the aspects such as:

- ✓ Nature, Purpose and Types of Internal Controls
- ✓ Inherent Limitations of Internal Controls
- ✓ **Role of Internal Auditor in Evaluating Internal Controls**
- ✓ Monitoring Internal Audit findings
- ✓ Communication of Continuing **Internal Control Weaknesses**

Role of Internal Auditor

- ❖ Examine continued effectiveness of internal control system through evaluation and make recommendations, if any, for improving effectiveness.
- ❖ Focus towards improving **internal control structure**
- ❖ Make management aware, as soon as practical and at an appropriate level, of **material weaknesses** in design or operation of internal control systems

Vigilance & Alertness

7 Golden Principles

- ✓ To find *Facts* and not *Faults*
- ✓ To *Guide* and not *Chide*
- ✓ To extend a *helping hand* and not *point fingers*
- ✓ To *Demonstrate* and not *Remonstrate*
- ✓ To be *Corrective* and not *Coercive*
- ✓ To “*Be Aware*” instead of saying “*Beware*”
- ✓ To distinguish *bonafide* from *malafide*