



RISK ADVISORY UPDATE

INTERNAL FINANCIAL CONTROL

INTRODUCTION TO INTERNAL FINANCIAL CONTROL (IFC)

The scale of the Satyam Scandal of 2009 and the inability of the audit process to find the financial fraud committed by the management brought to focus various loopholes in the regulatory and legal framework dealing with the board of directors and auditors of the company.

The Satyam scandal made Indian legislators search for best practices across the world like Sarbanes Oxley regulations in the United States (US), Turnbull Guidance in the United Kingdom (UK) and JSOX in Japan to raise the bar of corporate governance in India. The outcome of that search was the introduction of IFC regulations in The Companies Act -2013.

IFC is defined in the explanation to **Section 134(5)(e) of The Companies Act 2013** as the policies and procedures adopted by the company for ensuring -

- the orderly and efficient conduct of its business, including adherence to company's policies,
- the safeguarding of its assets,
- the prevention and detection of frauds and errors,
- the accuracy and completeness of the accounting records, and
- the timely preparation of reliable financial information."

BENEFITS OF IFC

With adequate and effective internal financial controls, some of the benefits that the companies would experience include:

- Senior Management Accountability.
- Improved controls over financial reporting process.

- Improved investor confidence in entity's operations and financial reporting process.
- Promotes culture of openness and transparency within the entity.
- Trickle down of accountability to operational management.
- Improvements in Board, Audit Committee and senior management engagement in financial reporting and financial controls.
- More accurate, reliable financial statements.
- Making audits more comprehensive.

APPLICABILITY OF IFC

<p>Section 134 of Companies Act</p>	<p>All listed entities</p>	<p>The Directors Responsibility Statement shall state the directors had laid down internal financial controls to be followed by the company and that such internal financial controls are adequate and operating effectively.</p>
<p>Section 143 of Companies Act</p>	<p>All entities (listed/unlisted)</p>	<p>The auditor's report shall state whether the company has adequate internal financial controls with reference to financial statements in place and the operating effectiveness of such IFC.</p>
<p>Section 177 of the Companies Act</p>	<p>All entities having an audit committee</p>	<p>The audit committee shall evaluate internal financial controls and risk management systems. The audit committee may call for comments of auditors about internal</p>

		control systems before their submission to the Board.
Schedule IV	All entities having independent directors	The independent directors should satisfy themselves on the integrity of financial information and ensure that financial controls and systems of risk management are robust and defensible.
Rule 8 (5) of Companies Accounts Rules	All entities (listed /unlisted)	The board report shall state the details in respect of adequacy of internal financial controls with reference to the financial statements.

FRAMEWORK FOR IFC

Management and Auditors need some set of benchmarks to assess the adequacy and effectiveness of IFC. Without these benchmarks assessment will be subjective without any guiding posts. The bench marks are called as framework. Like the Accounting Standards which are used the framework to evaluate the financial statements. The frame work of IFC is given by Standard on Auditing (SA) 315 issued by the Institute of Chartered Accountants of India (ICAI). The frame work explains the following components.

- Control Environment
- Risk Assessment
- Control Activities Information system and communication
- Monitoring.

CONCLUSION

The introduction of IFC regulations has definitely given us the chance to improve the internal control environment in most organizations by drawing the attention of the board of directors and auditors to the neglected concept earlier. It's our responsibility as the management and auditor to look at it from a fresh perspective beyond compliance and use it as an opportunity to promote risk management and governance process within their organization.


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