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Internal Audit : Effect on Financial Reporting

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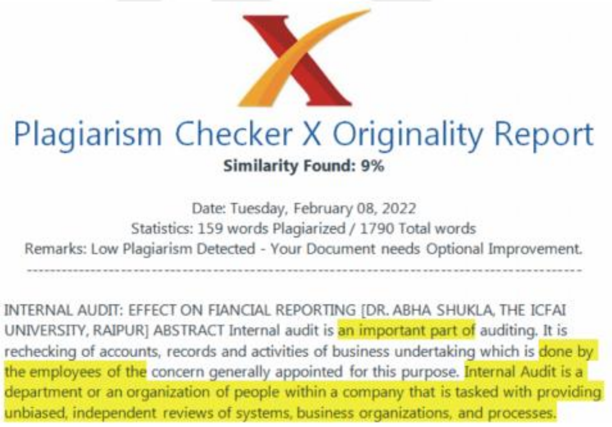

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INTERNAL AUDIT: EFFECT ON FIANCIAL REPORTING [DR. ABHA SHUKLA, THE ICFAI UNIVERSITY, RAIPUR] ABSTRACT Internal audit is an important part of auditing. It is rechecking of accounts, records and activities of business undertaking which is done by the employees of the concern generally appointed for this purpose. Internal Audit is a department or an organization of people within a company that is tasked with providing unbiased, independent reviews of systems, business organizations, and processes.

ABSTRACT

Internal audit is an important part of auditing. It is rechecking of accounts, records and activities of business undertaking which is done by the employees of the concern generally appointed for this purpose. Internal Audit is a department or an organization of people within a company that is tasked with providing unbiased, independent reviews of systems, business organizations, and processes. The role of Internal Audit is to provide senior leaders and governing bodies of an organization an objective source of information regarding the organization's risks, control environment, operational effectiveness, and compliance with applicable laws and regulations. The reviews performed by internal check are often called internal audits. An internal audit may be used to assess an organization's performance or the execution of a process against a number of standards, policies, metrics, or regulations. Accurate accounting records kept in line with globally recognized accounting procedures and standards should always be backed up by financial statements.

KEY WORDS

Audit, Errors and frauds, companies, independence, public assets.

INTRODUCTION

Internal Audit is a department or an organization of people within a company that is tasked with providing unbiased, independent reviews of systems, business organizations, and processes. The role of Internal Audit is to provide senior leaders and governing bodies of an organization an objective source of information regarding the organization's risks, control environment, operational effectiveness, and compliance with applicable laws and regulations. The reviews performed by Internal Audit are often called internal audits. An internal audit may be used to assess an organization's performance or the execution of a process against a number of standards, policies, metrics, or regulations. These audits may include examining a business's internal controls around corporate governance, accounting, financial reporting, and IT general controls. Internal audits may also entail evaluating the effectiveness/efficiency of critical business operations such as supply chain management. Those individuals working in Internal Audit are called internal auditors. Internal auditors may cover all areas of an organization or specialize based on their skill-sets.

Objective of The Study

The aim of internal audits is to identify weaknesses within the organization's processes and control environment internally so that they can be fixed as quickly as possible to prevent harm to the organization or its stakeholders. Accordingly, the internal audit plan for an organization should be driven by risk basis or, in other words, be designed to examine those areas that present the greatest risk to the company. The internal audit plan should also include a component of the strategic needs of an organization.

Internal Audit & Financial Statement

Financial statements should be provided with prior year's comparable numbers. Borrowers should make sure that all financial transactions are consistently recorded and categorized when submitting comparative statements. Any changes in accounting methods (e.g., categorization of balance sheet or income statement items) or financial policies from the previous year should be identified and explained in the financial statements' additional notes.

(Source : Depositphotos)

Specific Requirements

The majority of revenue-generating or commercially oriented initiatives are undertaken or operated by autonomous or semi-autonomous organizations. A thorough set of financial accounts indicating the project's operational performance should be made available to the Bank when the project or agency responsible for executing or administering the project is a financially autonomous or semi-autonomous entity. Consolidated financial accounts, which contain financial transactions relating to the project(s) being executed, are a standard practice for executing agencies. Consolidated financial statements, which include the executing agency's and the project's activities, should contain enough data to allow the project's and executing agency's accounts to be reviewed individually. Bank employees will determine and advise the borrower of the extent to which the project's accounts are to be divided and disclosed throughout the project evaluation and loan negotiations. This will be stated in the loan agreement as well.

The following should typically be included in financial accounts presented to Companies or by autonomous and semi-autonomous agencies:

i. An income statement or a revenue and expense statement;

ii. a balance sheets;

iii. a cash flow statement; and,

iv. notes or comments with further information and disclosure to clarify the entries in (i) and (ii) above. Each statement's function and important elements are discussed below.The income statement summarizes the financial outcomes of operations throughout the reporting period. The statement should generally incorporate financial information from the following areas when demonstrating the results for the reporting period:

Revenues (divided by source) *Sales* (sales may be needed to be represented individually for each main category or operational activity in some situations). For example, a tele communications project could be asked to prove sales of telephones, telex, and telegraphs, among other things.

Expenditures Include

Supplies, Salary & Wages, Utilities and Rent, Depreciation Interest or financial expenses, Taxes Miscellaneous Others.

Net Income

When utilizing the categorization "others" for income or spending items, any amount regarded substantially significant should be fully explained in the supplemental notes. Table I of the Annex shows an example format for a typical income statement.

Balance-Sheet

The balance sheet is used to indicate the borrower's/executing agency's or project's financial status at the conclusion of the reporting period. Fixed assets (plant, building, machinery), current assets (inventory, account receivable, short term investments, cash), and other assets should all be shown on the statement. Current and long-term obligations should be stated alongside assets. All commitments due within one year, including taxes and other accrued expenditures, as well as the share of long-term obligations maturing in one year, should be included in current liabilities.

Cash Flow Statement

A cash flow statement shows how the entity's net assets and financial structure have changed over the reporting period, as well as its liquidity and solvency. The cash flows for the time should be broken down into three categories: operating, investment, and financing. The cash flows created by operational operations are largely sourced from the entity's revenue-producing activities and include those aspects that are used to calculate net income. The acquisition and disposal of long-term assets generate cash flows from investment activities.

Reporting Requirements for Development Finance Institutions and Agencies

The Bank's financial reporting requirements for development finance institutions (DFIs) and agencies, which include national and sub-regional development banks in member countries, are largely the same as those for financially autonomous borrowers described in Sections 4.2.1 - 4.2.4. In addition to monitoring these institutions' financial soundness, the Bank wants to ensure that their principal assets (i.e. loans to borrowers) are protected, Sub-borrowers are protected, as well as the development goals for which the loan facilities were created. Each sub-project supported with the Bank's credit facility should receive quarterly operational reports.

Operational reports should include a concise summary of each sub-overall project's performance, noting key problem areas and steps taken by the OFT's management to address these issues. The status or progress of the project's implementation should be reported in the write-up for sub-projects that are still being implemented (i.e. construction work-in- progress, schedule of completion, etc.). The write-up for on-going sub-projects that have been fully operational should focus on the project's operational activities and performance, such as profitability and debt servicing to the OFT.

The Company may ask borrowers to generate and submit supplemental information in addition to the financial accounts and reports previously described in the preceding section. The Bank uses this supplemental breadth and depth of an audit review are dictated by the project or entity being auditor's legal and technical requirements. It may also be augmented with particular borrower instructions to increase the audit's detail and scope. Borrowers may not, on the other hand, limit the scope of an audit review in order to prevent the auditor from giving an opinion. The Bank's main concern is that each examination's breadth and depth be sufficient for the auditor to offer an opinion, qualification, or disclaimer on the borrower's financial statements. Formation to conduct a through examination and evaluation of the borrower's financial performance.

Audit Procedures

Audit processes entail a systematic examination of the entity's accounting records and control systems. The processes used are determined by the type of project being audited as well as the effectiveness of the entity's accounting and internal control systems. Audit processes should be extensive and well-planned to allow enough time to gather and compile data on each of the issues specified in the auditor's scope of work. Apart from functional areas such as financial performance, operational processes and financial controls, the Bank mandates that all audits include the fundamental procedures directly connected to the verification of financial transactions.

Depending on the sort of project being audited, the scope of various procedures will vary. Agriculture, health, and education initiatives, for example, typically entail the construction of buildings, warehouses and equipment, as well as the stockpiling of materials and supplies.

Auditor's Report

Following the completion of an audit, the auditor is obligated to submit the results of his examination to the project managers (executing agency) or authorized authorities employing the auditor's services by offering an opinion on the financial statements. As soon as the borrower receives the auditor's report, a copy should be provided to the Bank.

A short form report or a long form report can be used to deliver an auditor's report. The auditor's opinion on the financial statements is usually all that is included in the Short Form Report. Long Form Report goes even further, offering specific comments on the entity's accounting and financial controls, as well as its operational practices, as well as relevant suggestions to the borrower. During the loan talks, the Bank will decide and agree on the format of the audit report with the borrower. The auditor's terms of reference will also include this.

However, constitutional or legislative constraints may prevent a government auditor from submitting his report on an audit of a government agency or institution before it is submitted to the legislature. Bank employees will determine this practice during the project evaluation and work out alternate arrangements with the borrower.

On a project-by-project basis, the submission of different financial reports to the Bank, including interim financial reports and yearly financial statements, is determined. Each loan agreement specifies a deadline for providing financial statements and reports. None the less, the Bank will make every effort throughout loan talks to ensure that the time frame proposed and later agreed upon is reasonable and consistently represents the borrower's capacity to comply.

CONCULSION

It may be inferred as follows based on the framing of the problem, the formation of hypotheses, and the study findings: Internal audit has an impact on the quality of financial reporting, even though it is not yet performing its function properly to improve the quality of financial reporting in terms of audit implementation mechanisms, support staff with expertise in technology information systems/ electronic data processing, and operational experience bank.

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