INTERNAL CONTROL SYSTEM IMPLEMENTATION IN FINANCIAL ACCOUNTING AND REPORTING

Vasily Kudrin, CIA, CFE, CCSA. Conference "FINCONF", 5 October 2020



SPEAKER



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- Professional in finance and business with over 20 years of experience in real sector, finance and advisory.
- More than 300 professional projects and educational events in process organization, risk management, internal control, transformation of corporate systems.
- Vasily Kudrin has current professional international diplomas: CIA (internal audit, since 2004), CFE (investigation and risks of fraud, since 2007), CCSA (self-assessment of internal control and risks, since 2004).
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EXPERIENCE

- Experience in internal audit, corporate governance and internal control in accordance with international and generally recognized standards and recommended practices since 2002 (largest oil company, investment company, retail group, international consulting).
- Participated in the boards and working groups of a number of professional public organizations, such as Russian and Global Institute of Internal Auditors (IIA), the Association of Certified Fraud Examiners (ACFE).
- Member of organizations in the field of corporate governance and internal control (Association of Corporate Directors (AND), Russian Institute of Directors, RID) and digital investments (RACIB, Crypto Valley), participates in the coordination board of the "Debate Club" that deals with innovations in corporate governance, risk management and control.

CALL FOR ORGANIZATIONS OF DIFFERENT LEVELS

Approach applicability

LARGE ORGANIZATIONS

Application as an express approach to improving the internal control system in financial accounting and financial statement preparation.

MEDIUM BUSINESS

The main approach for the development and improvement of the internal control system.

SMALL COMPANIES

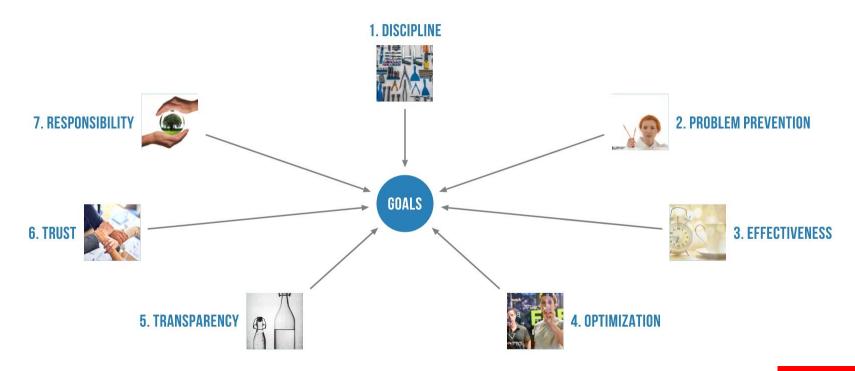
Starting approach (launch), implementation of separate stages and techniques, planning.

MICROBUSINESS

Understanding the objectives, control environment, and the underlying motivation and interest of business participants in financial transparency.

ACCOUNTING AND REPORTING INTERNAL CONTROL IMPROVEMENT GOALS

Planning, organizing, motivation, control



NORMATIVE AND METHODOLOGICAL BASE

Laws, bylaws and legal norms, recommendations and standards, leading practice



REGULATORY FRAMEWORK IN RUSSIA

GENERAL LEGAL REQUIREMENTS

- Federal law dd. 06.12.2011 # 402-FZ "On accounting" (article 19.1)
- Organization of internal control to combat legalization (laundering) of proceeds from crime and financing of terrorism // Federal law # 115-FZ On combating legalization (laundering) of proceeds from crime and financing of terrorism (as amended on 28.12.2013) (articles 3, 7)

INDUSTRY SEGMENT

Example: Law of the RF dd. 27.12.1992 # 4015-1 (as amended in 2013) "On organization of insurance business in the Russian Federation" (article 28.1)

KEY PAPER

Information of the Ministry of Finance of the Russian Federation # PZ-11/2013 on organization and implementation by an business entity of internal control of the facts of economic activity, accounting and preparation of accounting (financial) statements

TAXATION SEGMENT

- Chapter 14.7 of Tax Code of the Russian Federation (part one), information on internal control system within tax monitoring, article 105.26 "General provisions on tax monitoring" (incl. clauses 6, 7), article 105.27 "Procedure for submitting an application for tax monitoring, making a decision to conduct (omission to conduct) tax monitoring."
- Requirements for declaration on internal control system within tax monitoring // Order of Federal Tax Service of the Russian Federation dated 04.21.2017 N MMB-7-15 / 323 @
- Requirements for organization of internal control system // Order of the Federal Tax Service of the Russian Federation dd. 16.06.2017 # MMB-7-15 / 509 @

STANDARDS (REGULATIONS, RULES)

- Financial accounting standards (general, industry) and reporting
- International standards of auditing (ISA)



INTERNAL CONTROL SYSTEM DEVELOPMENT APPROACH

Financial accounting and reporting

PLANNING

Examining reports of past periods

Control environment analysis

Specification of material statements and processes

Detailed plan

RISK ASSESSMENT

Risk assessment criteria

Inherent risk assessment

Fraud and abuse risk assessment

Examining typical control procedures and leading examples

IMPROVEMENT PLANS

Finalization of description of deficiencies in internal control system

Preparation of recommendations

Elaboration of improvement plans (improvements)

RISK IDENTIFICATION

Structuring and studying processes related to groups of material transactions

Preparing for interviews with process owners

Risk identification and description

CONTROL DIAGNOSTICS

Determination of available control procedures

Identification of those responsible for implementation and improvement of control procedures

Control evaluation; deficiencies

DEVELOPMENT OF REGULATIONS

Selection of recommendations and improvement plans for regulation purposes

Preparation of regulations

MANAGEMENT ASSERTIONS (1)

(1) Level of classes of transactions (accounting), (2) Level of reporting items, (3) Level of statements (disclosures)

COMPLETENESS

All assets, liabilities, transactions are recorded in full at the reporting date or for the reporting period.

EXISTENCE

Assets and liabilities do exist at the reporting point in time.

OCCURENCE

The represented income and expenses, in fact, have occurred.

CUT-OFF

Transactions and events have recorded in the correct accounting period.

MANAGEMENT ASSERTIONS (2)

(1) Level of classes of transactions (accounting), (2) Level of reporting items, (3) Level of statements (disclosures)

ACCURACY

Transactions have been accurately recorded at the appropriate (proper) amounts.

VALUATION

Assets, liabilities are included in the financial statements appropriate amounts. Transactions, events, balances and other financial aspects have been disclosed accurately at their appropriate amounts.

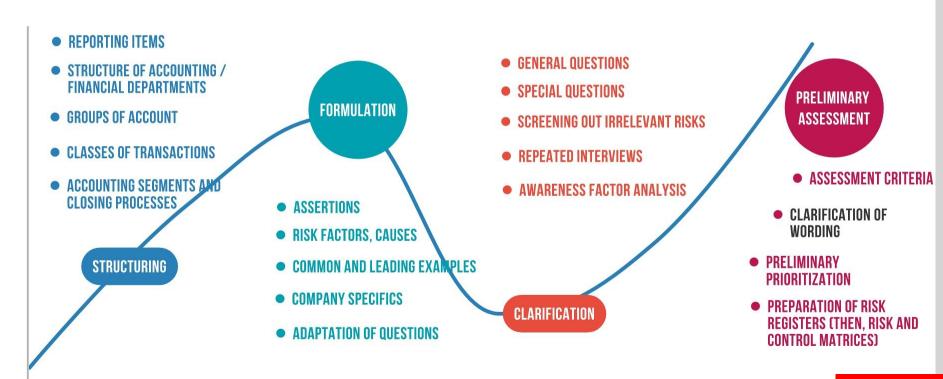
RIGHTS AND OBLIGATIONS

The organization has the rights to own or use the recognized assets, and the liabilities recognized in the financial statements are indeed the company's liabilities.

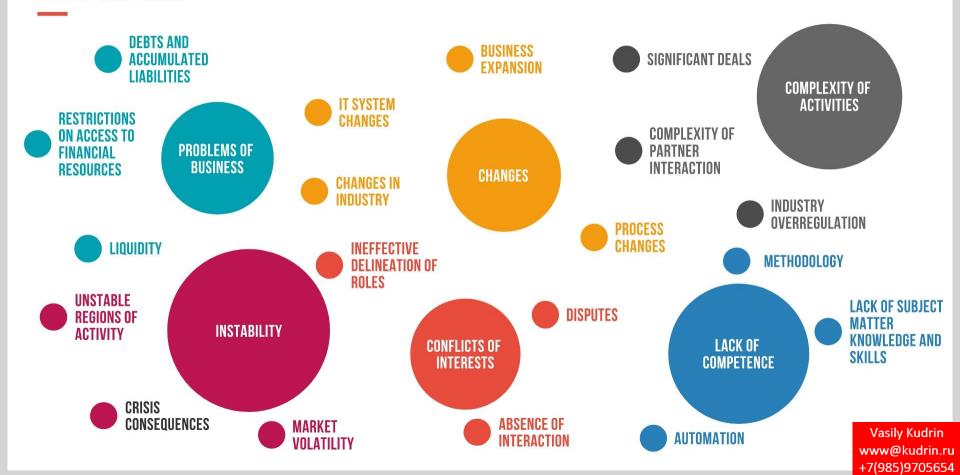
CLASSIFICATION, PRESENTATION

Items are correctly classified, grouped / disaggregated, described and clearly presented in the financial statements.

IDENTIFICATION, FORMULATION, DESCRIPTION OF RISKS



RISK FACTORS



RISKS



EARNINGS, PROCEEDS

- Incomplete reporting on revenues, proceeds
- Conversely, overestimation by reporting in a past period proceeds (revenues) of a new period
- Incorrect classification by groups



DEBTS

- Incomplete reporting on debt due to incomplete contractual process
- Debt reported in non-existent transactions
- Incorrect estimates of debt



PAYROLL

- Distortion or loss of data during transfer in systems
- Inflated calculations
- Errors in calculating salary taxes



REPORTING

- Violations of completeness of information when closing books
- Distortion when shifting or transforming
- Presentation errors
- Distorted estimates

EFFECTIVE CONTROL AND CONTROL DEFICIENCY



EFFECTIVE CONTROL

 Effective control over the preparation of financial statements provides reasonable assurance about the reliability of financial reporting and the process of preparation of financial statements for external purposes. If there is one or more material "weaknesses", the organization's internal control over the preparation of the financial statements cannot be considered effective.



MATERIAL WEAKNESS

 A material weakness is a deficiency, or combination of deficiencies, in internal control over the preparation of financial statements where there is a reasonable possibility that material misstatement of annual or interim financial statements will not be prevented or timely discovered.

CONTROL EVALUATION



DESIGN

How control is conceived (designed), description of control, its model



IMPLEMENTATION

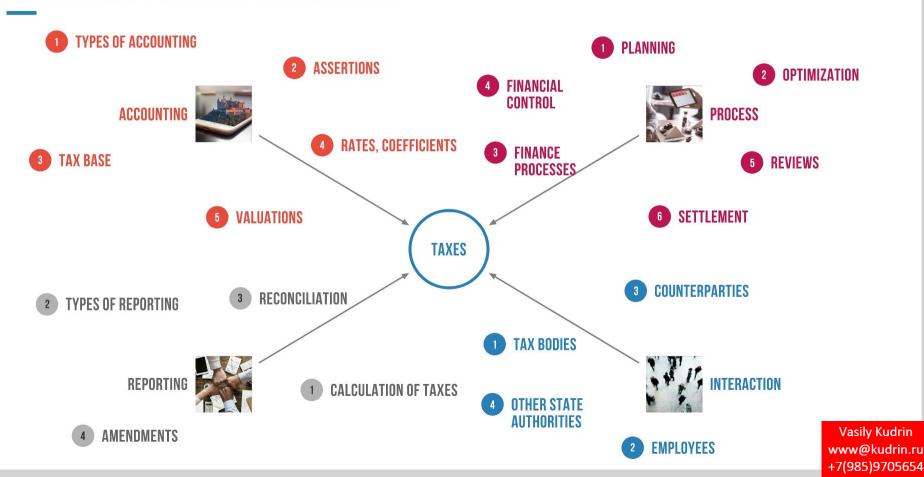
How information is communicated to the employees, how control is imputed in systems and processes



OPERATIONAL EFFECTIVENESS

How effective the control is when it is performed according to design

CONTROL AND TAX RISK MANAGEMENT



Audit and improving internal control system (ICS) over accounting and financial reporting (FR)

Project detailed planning

- Planning of work scope, deadlines for their completion and a detailed work program
- Identifying interviews and preparing an interview schedule
- Preliminary discussion of corporate-level risks affecting reporting, materiality assessment taking into account potential future events
- Preliminary (top-level) description of accounting and reporting processes based on classes (groups) of material accounts and transactions
- Identification of key (sub)processes
- Specification of work program and schedule of interviews
- Development of a preliminary methodology for determining materiality

Assessment of risks and CLC/GCC

- Description, selection and assessment of corporate level controls (CLC) and general computer controls (GCC), preliminary recommendations, formation of a typical risk map and selection of processes
- Completing description of accounting and reporting processes ("as is"), identification of possible negative consequences (WCGW, "what could go wrong") connected to objectives (prerequisites) of preparing financial statements based on relevant management assertions, specification of (sub) lower-level processes
- Preliminary identification and assessment of risks of distortion of reporting, assessment of consciousness factors
- Support in preliminary description of control procedures

Assessment of ICS in accounting and FR processes

- Conduct walkthrough for evaluation of control design
- Risk assessment and description controls of the financial statement closing process
- Assessing control in the process of closing financial statements
- Completion of preparation of documentation for assessment of ICOFR (for general and process - manual and machine-dependent - control procedures)
- Recommendations for control improvements
- Recommendations for ensuring effective segregation of duties and fraud prevention
- Preparation of standard control forms (templates, checklists)

Project close

- Preparation of recommendations on self-assessment of controls, information exchange and knowledge management, testing methodology
- Preparation of a general methodology for periodic monitoring performed by management
- Development of recommendations for automation
- Checking completeness of controls based on assessing the coverage of financial statements reliability statements
- Completion of general methodology papers
- Finalization of final recommendations of the whole project
- Preparation of a presentation on project's results

Time:

1-3 months

4-7 months

8-10 months

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