CFO SERIES 1 of 3

ASA
Going The Extra Mile

TOP 10 WARNING SIGNS NO CFO SHOULD IGNORE

SUMMARY | 1ST SEPTEMBER, 2021

Amongst the many red signals that must be watched by CFOs, there are a few that must not be ignored. In this webinar by ASA, Parveen Kumar, National Head, Assurance, ASA and Amarjit Chopra, Ex-President, ICAI and Ex-Chairman, NACAS discussed 10 key signals that CFOs must pay careful attention to. Discussion was also around what actions should be taken as preventive measures.

With the Revised Code of Ethics by ICAI, role of the preparer of financial statements which is, key management personnel, including CFO, has come into radar of another regulator. To top it up, recent and significant amendments in Schedule III of The Companies Act (applicable from 1st April 2021) have substantially increased the disclosure and reporting requirements in financial statements. CFO needs to be in complete control of what is being presented to the stakeholders.

The pandemic has exacerbated the Fraud triangle viz., opportunities, pressure and rationalization, thereby increasing the risk of fraud. While deviations from normal checks and controls might provide an opportunity; Pressures like financial uncertainty and reduced job security remains high concern areas. Attitude is critical and fraudsters will always rationalize deviant behaviour.

With all of this, CFOs need to exercise more caution and be more aware of the indicators of trouble, both financial and operational. One of the important red flag that must not be ignored is when promotors are paying extra ordinary attention to ring-fencing their personal assets. Frequent changes in bill of materials or vendors is another signal. Over-reliance on technology and system-generated reports should not be blindly relied upon without applying professional scepticism. Another warning sign is a sudden increase in the number of complaints. CFOs need to read the signal, where whether whistle blowers are scared. Undue delays can also be an indicator of inaccurate budgeting or fraudulent motives of personnel involved. A thorough analysis of the causes of these delays needs to be carried out.

Financials Red Flags that must not be ignored include slipping financial ratios. If for example, the Current ratio has moved from 1:1 to 1.5:1, this could be due to old inventory lying in stock or mounting trade receivables. CFOs need to carefully monitor reasons behind the changes in ratios. An increase in working capital or an overdependence on external sources for working capital requirement is certainly a sign of trouble like a downwards changes in the net worth of investments. Increasing inventory, ageing, inventory turnover ratio and key indicators needs to be closely watched on a regular basis. Finally, proper disclosures are expected by all the stakeholders.

In conclusion, in addition to keeping a close eye on the company's finances, the CFO must ensure the following to mitigate her personal risk

- **Existence of controls over key risk areas;**
- **Effective Whistle blower mechanism;**
- **Proper disclosures in financial statements and Management Reports.**
- **Zero Tolerance for non-compliance with regulations and statutory requirements,**
- **Have the right consultant, who is available when required with the proper technical knowledge; and finally**
- **Continuous training of team members.**