CONSULTING HAUS

INTERNAL CONTROLS OVER FINANCIAL REPORTING

OVERVIEW: QATAR & SAUDI ARABIA

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1. ICoFR and its benefits

The primary objective of ICoFR is to provide reasonable assurance that the financial statements are free from material misstatement

WHAT IS ICOFR?

- A system of policies, procedures, and processes implemented by organizations to ensure the completeness, accuracy, reliability and integrity of financial statements.
- It serves as a critical component of corporate governance, safeguarding against financial misstatements, fraud, and regulatory non-compliance.
- The typical steps involved within an ICoFR assessment include:

  i. Identifying key financial reporting processes and risks.

  ii. Designing and implementing controls to address those risks.

  iii. Testing the operating effectiveness of controls to ensure they function as intended.

  iv. Reporting deficiencies and providing recommendations for remediation.

IMPORTANCE FOR ORGANIZATIONS AND STAKEHOLDERS

1. For organizations, ICoFR aids in risk mitigation, fraud prevention, and enhancing operational efficiency
2. For stakeholders, it instills confidence in FS and minimizes financial mis-management
3. As a whole, ICoFR helps preserve the organization's reputation and trustworthiness in the market

ASSOCIATED BENEFITS

- ESTABLISHING EFFICIENT AND EFFECTIVE GOVERNANCE PRACTICES
- ENSURES SEGREGATION OF DUTIES AND MINIMIZES ERRORS
- RISK MANAGEMENT AND CONTINUOUS IMPROVEMENT
- RELIABILITY OF FINANCIAL REPORTING
- ASSURANCE TO KEY STAKEHOLDERS AND INVESTOR CONFIDENCE
- COMPLIANCE WITH APPLICABLE LAWS AND REGULATIONS

2. Stakeholder Expectations and Roles in ICoFR

Successful implementation and maintenance of ICoFR require active collaboration among both internal and external stakeholders

EXTERNAL STAKEHOLDERS

ICoFR plays a crucial role in fulfilling transparency, accuracy, and reliability in financial reporting to external stakeholders, including regulators, investors, creditors, shareholders and the statutory auditors. Detailed below are some of the responsibilities an entity has to external shareholders.

01 REGULATORS

- A regulated and/or listed entity is expected to adopt globally recognized internal control frameworks. Their financial statements are expected to accurately reflect their state of affairs.

02 INVESTORS AND CREDITORS

- A regulated and/or listed entity is expected to generate reliable financial statements backed by strong internal controls.

03 SHAREHOLDERS

- A regulated and/or listed entity is expected to ensure transparent and accurate financial reporting.

04 STATUTORY AUDITORS

- A regulated and/or listed entity is expected to adopt and implement an effective ICoFR framework.

INTERNAL STAKEHOLDERS

Internal stakeholders play a critical role in ensuring the effectiveness of ICoFR by implementing, monitoring, and maintaining controls that safeguard financial integrity. Their responsibilities vary based on their roles within the organization.

01 BOARD / AUDIT COMMITTEES

- Ensure financial statements are based on an effective ICoFR framework.
- Approve budgets, and grant authority for implementing ICoFR practices.

02 SENIOR MANAGEMENT CEO / CFO

- Provide resources, skills, training, and governance to support ICoFR implementation.

03 PROCESS OWNERS

- Collaborate with the internal control ("**IC**") team to manage financial reporting controls and discuss critical or complex control inputs.

04 INTERNAL CONTROL TEAM

- Provide guidance on financial reporting controls and their effective management.

05 INTERNAL AUDIT

- Assess and validate the effectiveness of ICoFR practices across the organization.

3. Foundational Outcomes and Continuous Improvement

A successful ICoFR framework reflects management's unwavering commitment to continuous improvement, addressing evolving risks and maintaining robust internal control mechanisms to support sustainable growth and operational excellence

FOUNDATIONAL OUTCOMES OF EFFECTIVE AND CONTINUOUS ICoFR

MANAGEMENT'S COMMITMENT TO CONTINUOUS IMPROVEMENT

1. **Regular monitoring and assessment:** Periodic reviews ensure the internal control framework remains adequate and effective, addressing new risks, process changes, and regulatory updates.
2. **Training and awareness:** Management should provide ongoing education to reinforce the importance of internal controls and equip employees with skills for implementation & maintenance.
3. **Adapting to regulatory changes:** Policies and procedures are regularly updated to ensure compliance with evolving laws, regulations, and industry standards.
4. **Enhancing IT systems and automation:** Management should integrate advanced technologies and automated controls to boost accuracy, efficiency, and monitoring in processes.
5. **Encouraging feedback and reporting:** An open-door policy and whistleblower mechanisms allow employees to report control deficiencies, risks, or compliance issues safely, without fear of retaliation.
6. **Establishing clear accountability:** Roles and responsibilities for internal controls are clearly defined, ensuring accountability for maintaining and improving the control environment.
7. **Timely remediation of deficiencies:** A systematic approach is used to address deficiencies, root causes, and implement corrective actions promptly to strengthen controls.
8. **Fostering a culture of continuous improvement:** Management should foster a mindset focused on identifying improvement opportunities and embedding leading practices into daily operations.

4. QFMA's ICoFR requirement

QFMA mandates a robust framework for listed entities, emphasizing the establishment and maintenance of ICoFR. These provisions are designed to enhance financial transparency, ensure regulatory compliance, and safeguard stakeholder confidence

QFMA PROVISIONS MANDATING ICoFR FOR LISTED ENTITIES IN QATAR

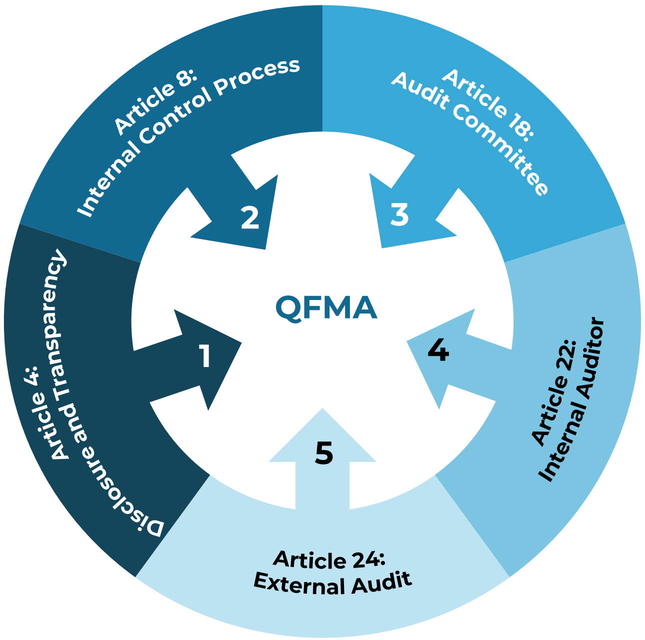
On 15th May 2017, the Qatar Financial Markets Authority ("**QFMA**") issued the Corporate Governance rules, applicable to all companies and legal entities listed on the main market. The QFMA Governance Code outlines several provisions that mandate the establishment and maintenance of ICoFR for listed companies. Key provisions are outlined below.

INTERNAL CONTROL PROCESS

- Listed companies must establish an effective system with independent units for risk assessment, internal control policies and procedures, audit, and compliance oversight. Qualified internal auditors should manage this system with access to all departments for comprehensive oversight.

DISCLOSURE REQUIREMENTS

- Companies must disclose their compliance with the Governance Code provisions in their annual reports, including information on internal control systems and risk management procedures.



AUDIT COMMITTEE

- The Audit Committee is responsible for reviewing and monitoring the effectiveness of the internal control system, including financial reporting controls, and ensuring adequacy and compliance with relevant laws and regulations.

INTERNAL CONTROL REPORTING

- Internal auditors must submit quarterly reports to the Audit Committee on internal control achievements, covering financial affairs, investments, risk management, and compliance. The reports should also assess the company's performance in implementing the internal control system according to the Governance Code.

EXTERNAL AUDIT

- External auditors must assess and report on the effectiveness of the company's internal control systems, informing shareholders about control functions and performance, particularly regarding internal controls over financial reporting.

5. CMA's ICoFR requirement

CMA mandates a robust framework for listed entities, emphasizing the establishment and maintenance of ICoFR. These provisions are designed to enhance financial transparency, ensure regulatory compliance, and safeguard stakeholder confidence

CMA PROVISIONS MANDATING ICoFR FOR LISTED ENTITIES IN KSA

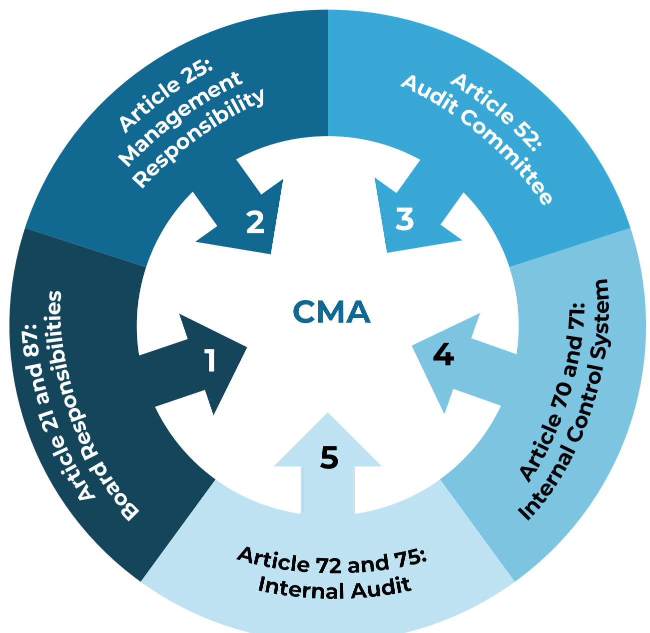
On 16th August 2017, the Capital Market Authority ("**CMA**") issued the Corporate Governance rules, applicable to all companies and legal entities listed on the main market. The CMA Governance Code outlines several provisions that mandate the establishment and maintenance of ICoFR for listed companies. Key provisions are outlined below.

EXECUTIVE MANAGEMENT RESPONSIBILITY

- The executive management of listed companies should implement effective internal control and risk management systems and ensure compliance with the board-approved risk levels.

BOARD RESPONSIBILITIES

- The board of listed companies is responsible for establishing and overseeing internal control rules and procedures.
- The board's annual report must include the results of the review of the internal control system's effectiveness and the audit committee's opinion on its adequacy.



AUDIT COMMITTEE AND INTERNAL AUDIT

- The Audit Committee should monitor the company's activities and ensure the integrity and effectiveness of internal control systems.
- The internal audit department should review the company's internal and financial control systems, as well as its risk management system.

INTERNAL CONTROL SYSTEM

- The board must approve an internal control system to assess risk management policies, governance implementation, and compliance with laws and regulations.
- The listed company must establish units or departments for risk assessment and internal control management.

INTERNAL AUDIT UNIT

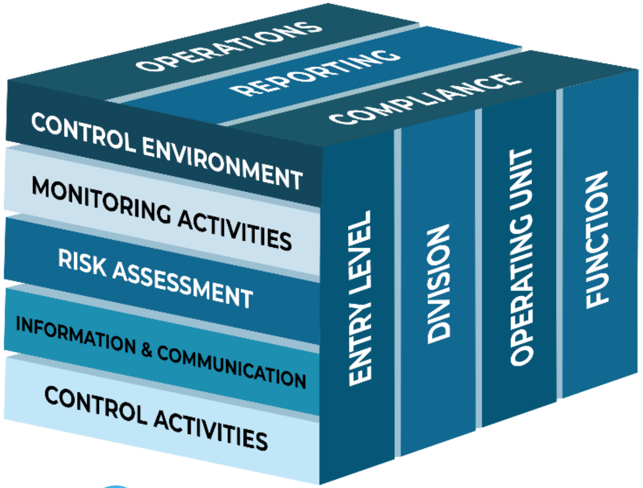
- The internal audit unit should assess and monitor the internal control system and ensure compliance with applicable laws, regulations, and company policies.
- It must submit a quarterly written report to the Board and Audit Committee, including an assessment of the internal control system and final opinions and recommendations.

6. COSO framework for internal control

CH adopts the globally recognized COSO framework for the ICoFR assessment to strengthen governance and enhance oversight of financial reporting controls

COSO FOR INTERNAL CONTROLS

- The Committee of Sponsoring Organizations of the Treadway Commission (**"COSO"**) prescribes the integrated framework for internal controls, that facilitates to strengthen and enhance their overall governance and internal control structures.
- This framework enables a flexible and reliable approach to the design and evaluation of internal control systems for operational, compliance, and reporting objectives.
- *We conduct the design and operating effectiveness testing of the financial reporting controls based on the COSO framework, which focusses on five integrated components of internal controls and their respective sub-components as below:*



CONTROL ENVIRONMENT

1. Demonstrates commitment to integrity and ethical values
2. Exercises oversight responsibility
3. Establishes structure, authority, and responsibility
4. Demonstrates commitment to competence
5. Enforces accountability

RISK ASSESSMENT

1. Specifies suitable objectives
2. Identifies and analyzes risk
3. Assesses fraud risk
4. Identifies and analyzes significant change

CONTROL ACTIVITIES

1. Selects and develops control activities
2. Selects and develops general controls over technology
3. Deploys control activities through policies and procedures

INFORMATION & COMMUNICATION

1. Uses relevant information
2. Communicates internally
3. Communicates externally

MONITORING ACTIVITIES

1. Conducts ongoing and/or separate evaluations
2. Evaluates and communicates deficiencies

7. Design effectiveness testing methodology

By conducting design effectiveness testing, organizations can proactively address weaknesses in their internal control framework, reducing the risk of financial misstatements and ensuring compliance with regulatory requirements

DESIGN EFFECTIVENESS ("DE") TESTING METHODOLOGY

Design effectiveness testing of ICoFR ensures that controls within Entity Level Controls ("**ELCs**"), Information Technology Level Controls ("**ITGC**") and Process Level Controls ("**PLCs**") are properly designed to prevent or detect material misstatements. The process typically involves the following steps:

Step 1

Scoping

Identify the significant accounts and key controls relevant to the scoped-in processes to initiate the ICoFR assessment.

Step 2

Walkthroughs

Perform walkthroughs with process owners by tracing sample transactions from initiation to financial statement impact.

Step 3

RCMs

Prepare a Risk and Control matrix ("**RCM**") encompassing ELCs, ITGCs and PLCs, and map relevant risks, including all applicable financial reporting risks, to internal controls.

Step 4

DE testing

Evaluate whether controls are appropriately designed to address the identified risks. If not, identify gaps / improvement opportunities to enhance the internal controls.

Step 5

Report

Summarize key observations, control gaps, and recommendations for improving design of controls within ELCs, ITGCs and PLCs.

Step 6

Follow up

Perform monitoring and testing of remediated controls and ensure that management has implemented the appropriate improvements.

Step 7

Update

Update the relevant documentation to reflect changes to the controls and circulate to the stakeholders.

By completing these steps, organizations can ensure their ICoFR controls are well-designed to mitigate financial reporting risks before proceeding to operating effectiveness testing.

8. Operating effectiveness testing methodology

By performing operating effectiveness testing, organization can assess whether the controls are consistently executed and reliable in practice

OPERATING EFFECTIVENESS ("OE") TESTING METHODOLOGY

Operating effectiveness testing phase evaluates whether key controls within ELCs, ITGCs and PLCs are functioning as designed over a specified period. The process typically involves the following steps:

SCOPING

Identify and scope-in, by applying quantitative and qualitative criteria, key controls with ELCs, ITGCs and PLCs that require testing.

TESTING PLAN

Establish testing procedures, determine sample size based on control frequency and risk level, and define the testing period to ensure continuous coverage.

PERFORM TESTING

Perform testing procedures to Identify any control failures, exceptions, or deviations and determine the impact on financial reporting.

REPORTING OF FINDINGS

Identify control failures, exceptions, or deviations, assess their impact on financial reporting, and communicate findings to management, process owners, and the audit committee.

REMEDIATION AND RETESTING

Collaborate with management to develop action plans addressing deficiencies, implement process improvements, and retest remediated controls to verify their effectiveness before final reporting.

MANAGEMENT REPORT

Summarize the control testing results, deficiencies, and remediation efforts, including conclusions on the reliability of controls over financial reporting.

A well-executed operating effectiveness assessment ensures compliance with financial reporting regulations and strengthens the organization's internal control framework.

9. Sampling methodology

A well-structured sampling methodology ensures that operating effectiveness testing provides reliable conclusions on the effectiveness of internal controls, optimizing testing efforts while ensuring regulatory compliance

SAMPLING METHODOLOGY

Below is a structured methodology for selecting samples during operating effectiveness testing assignments:

1. **Define Sampling objective**
   Define sample sizes and coverage, that provides evidence to draw a conclusion on the control effectiveness.
2. **Identify Population**
   Population consists of all instances where the control was performed during the testing period.
3. **Determine sampling approach**
   Perform statistical or non-statistical sampling based on severity of the risk.
4. **Determine sample size**
   Determine the sample size depending on the control frequency and risk level of each key control.
5. **Execute tests**
   Verify supporting evidence and identify exceptions or deviations from control execution.
6. **Report**
   Document findings, remediation actions, and deficiencies, and if no exceptions are found, conclude that the control is operating effectively.

The sample size depends on control frequency, risk level, and reliance on automation. The table below provides **illustrative** sample sizes based on control frequency:

Control Frequency	Risk Level	Sample size (illustrative)
Annual (1x per year)	High	1
	Low	1
Quarterly (4x per year)	High	2-3
	Low	1-2
Monthly (12x per year)	High	3-5
	Low	2-3
Weekly (52x per year)	High	10-20
	Low	5-10
Daily / Continuous	High	25 +
	Low	10-20

Automated Controls: If system-enforced, a single test plus system configuration validation may suffice.

High-Risk Controls: Larger sample sizes should be selected for manual controls prone to error.

Prior Year Deficiencies: If a control had prior weaknesses, an increased sample size may be necessary.

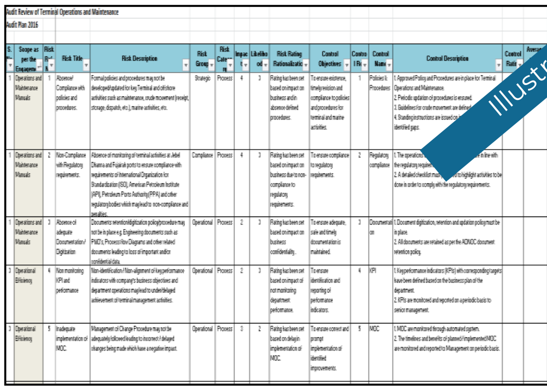
Sampling is key in ICoFR testing to ensure controls operate effectively. Design effectiveness testing typically uses one sample per control to validate the design of the control.

10. Illustrative Documents involved

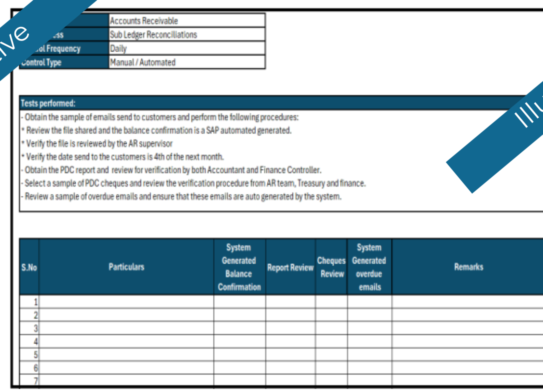
Below we have added few illustrative documents typically employed for ICoFR assessments

ILLUSTRATIVE DELIVERABLES

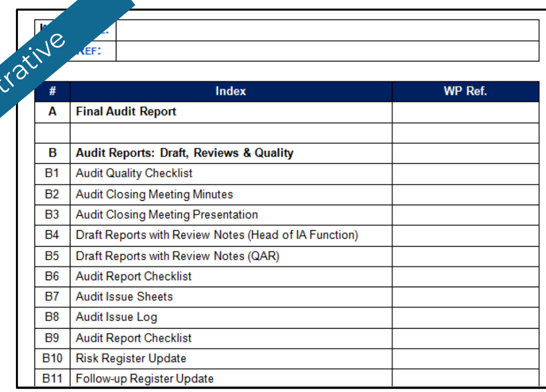
RISK & CONTROL MATRIX (RCM)



TEST SHEETS



WORKING PAPER FILE



MANAGEMENT REPORT – DETAILED OBSERVATIONS

SUMMARY OF OBSERVATIONS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