

Summer internship project report

On

FINANCIAL RATIO ANALYSIS & RISK MANAGEMENT

By

VIKHYAT AGARWAL

2019BBA033



Under the supervision of

MS. TANUSHKA JANGID

(Submitted in partial fulfilment of the requirements of the BBA degree)

Institute of Management

JK LAKSHMIPAT UNIVERSITY

(2020 - 21)

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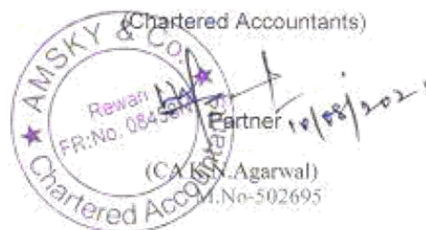
SUMMER INTERNSHIP COMPLETION CERTIFICATE

This is to certify that VIKHYAT AGARWAL, pursuing his B.B.A, has successfully completed summer internship under live project program (Work from Home) in Finance Discipline covering topic of Financial Ratio Analysis & Risk Management from our office situated at Bharawas Gate, Rewari, Distt- Rewari (Haryana) from 16th June 2021 to 31st July 2021.

We found him sincere, hardworking, technically sound and result oriented. He worked well as part of a team during his tenure. We take this opportunity to thank him and wish him all the best for his future.

For M/s AMSKY & Co.

(Chartered Accountants)



DECLARATION BY THE CANDIDATE

I, the undersigned, solemnly declare that the project report is based on my own work carried out during our study under the supervision of **Mr. K. N. Agarwal (Industry mentor) & Ms. Tanushka Jangid (Faculty mentor)**.

I assert the statements made and conclusions drawn are an outcome of my research work. I further certify that

1. The work contained in the report is original and has been done by me under the general supervision of my supervisor.
2. The work has not been submitted to any other Institution for any other degree / diploma / certificate in this university or any other University of India or abroad.
3. I have followed the guidelines provided by the university in writing the report.
4. Whenever I have used materials (data, theoretical analysis, and text) from other sources, we have given due credit to them in the text of the report and given their details in the references.



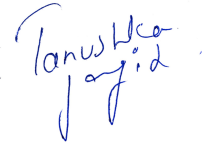
Vikhyat Agarwal

2019BBA033

Institute of Management

CERTIFICATE

It is certified that the Summer Internship Report titled **Financial Ratio Analysis and Risk Management** submitted by **Vikhyat Agarwal** is an original piece of research work carried out by the candidate under my supervision.

A handwritten signature in blue ink, reading "Tanushka Jangid".

Sign. of the Faculty Guide

(Ms.Tanushka Jangid)

ACKNOWLEDGEMENT

The internship opportunity I had with **AMSKY & CO.** was a great chance for learning and professional development. Therefore, I consider myself as a very lucky individual as I was provided with an opportunity to be a part of it. I am also grateful for having a chance to meet so many wonderful people and professionals who led me through this internship period.

I express my deepest thanks to **Mr. K. N. Agarwal (Industry mentor) & Ms. Tanushka Jangid (Faculty mentor)** for taking part in useful decisions & giving necessary advice and guidance and arranged all facilities to make life easier. I choose this moment to acknowledge their contribution gratefully.

I perceive this opportunity as a big milestone in my career development. I will strive to use gained skills and knowledge in the best possible way, and I will continue to work on their improvement, in order to attain desired career objectives.

Sincerely,

Vikhyat Agarwal

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Objectives of the project

The Objective of the study is to understand the process of consolidation of the financial statements of companies. Identification of the basic risks (internal and external) and frauds associated with different departments (accounts payable, cash operations, taxes, services) in the financial sector of the company and suggesting methodology to minimise the risks and frauds occurring in the sector.

Another objective of the study is to understand the workings of the finance and accounts department of a company and its day to day activities.

Introduction to financial Ratio analysis

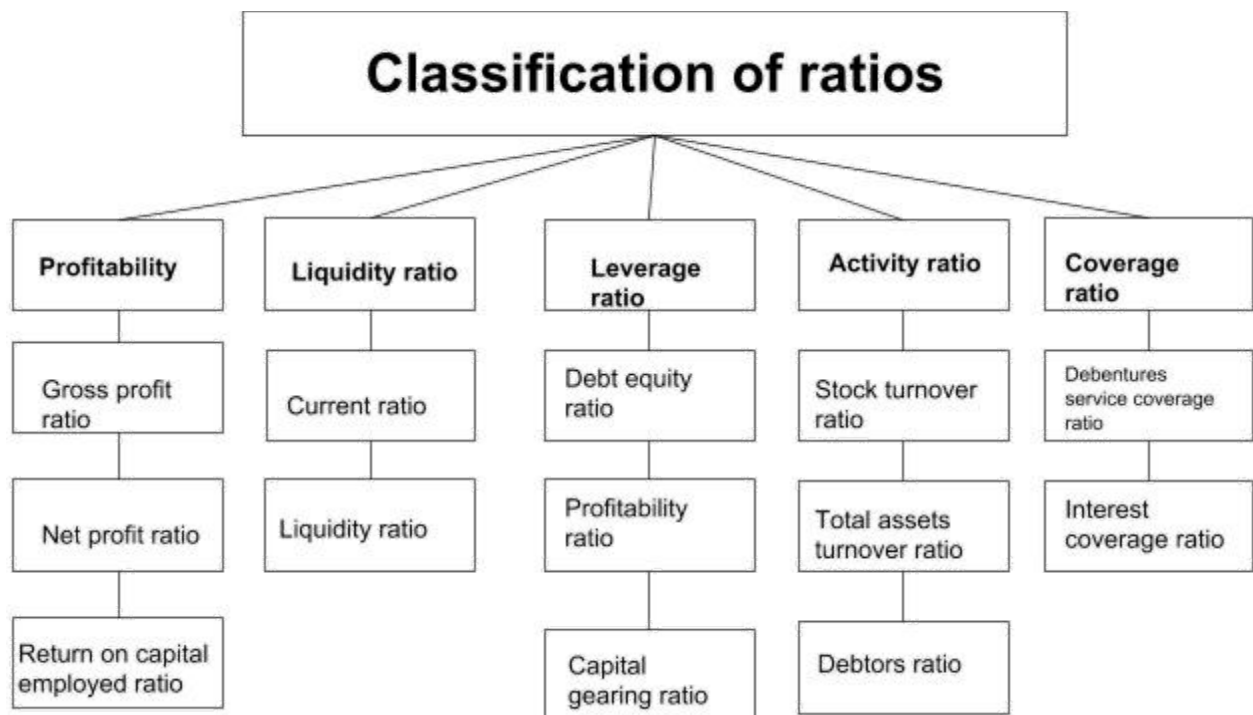
Ratio analysis is used to understand the information contained in financial statements with a view to know the strength or weaknesses of the firm and to make forecasts about the future prospects of the firm and thereby enabling the financial analyst to make different decisions regarding the operations of the firm and also managing different risks associated with the sector.

Fundamental Analysis has a very broad scope. One aspect looks at the general (qualitative) factors of a company. The other side considers tangible and measurable factors (quantitative). This means crunching and analyzing numbers from the financial statements. If used in conjunction with other methods, quantitative analysis can produce excellent results.

Ratio analysis isn't just comparing different numbers from the balance sheet, income statement, and cash flow statement. It's comparing the number against previous years, other companies, the industry, or even the economy in general. Ratios look at the relationships between individual values and relate them to how a company has performed in the past, and might perform in the future.

Ratio analysis is an attempt to derive quantitative measures or guides concerning the financial health and profitability of business enterprises. Ratio analysis can be used both in trend and static analysis. There are several ratios at the disposal of an analyst but their group of ratios he would prefer depends on the purpose and the objective of analysis.

A financial ratio measures a company's performance in a specific area. For example, you could use a ratio of a company's debt to its equity to measure a company's leverage. By comparing the leverage ratios of two companies, you can determine which company uses greater debt in the conduct of its business. A company whose leverage ratio is higher than a competitor's has more debt per equity. We can use this information to make a judgment as to which company is a better investment risk.



Ratio analysis

Liquidity ratios

Current ratio = current asset / current liabilities

Acid-test ratio = (current asset-inventories) / current liabilities

Solvency ratio:

Debt Equity Ratio = Debt/equity

Fixed asset ratio = Fixed assets/long term funds

Debt service coverage ratio = EBIT / Long term borrowings

Activity ratios

Inventory turnover ratio= net sales / average inventory

Accounts receivable turnover ratio = Net credit sales /Average accounts receivable

Working capital turnover ratio = Net sales / Average working capital

Total assets turnover ratio = Net Sales / average fixed assets

Profitability ratios

Net profit ratio = Net profit / sales

Return on Investment= [Net profit + Interest expense {1-t}]/Long term funds

Return on equity =Net profit/ shareholders fund

Earnings per share=Net profit/No. of equity shares

Comparative financial statements

In this, the company compares the financial statements with past years / periods. This process tells the trends in the financial statement of the company. This shows the efficiency of the management or the decisions taken by the management by analysing the trends. This helps in evaluating the new management or a new decision taken by them.

Common size financial Statements

In this, the company's balance sheet is represented as a percentage of the common base figure. This is usually sales in income statement and balance sheet total in case of balance sheet. This helps in analysing the company over time. It also tells the expenses in terms of percentage of the sales which helps to analyse them further and manage them properly.

Limitations of financial analysis

- Dependence on historical costs.
- Intangible assets not recorded
- Based on a specific time period.
- Not always comparable across companies
- No predictive value
- No discussion of non-financial issue
- Subject to fraud

Risk, frauds and risk management

What is risk?

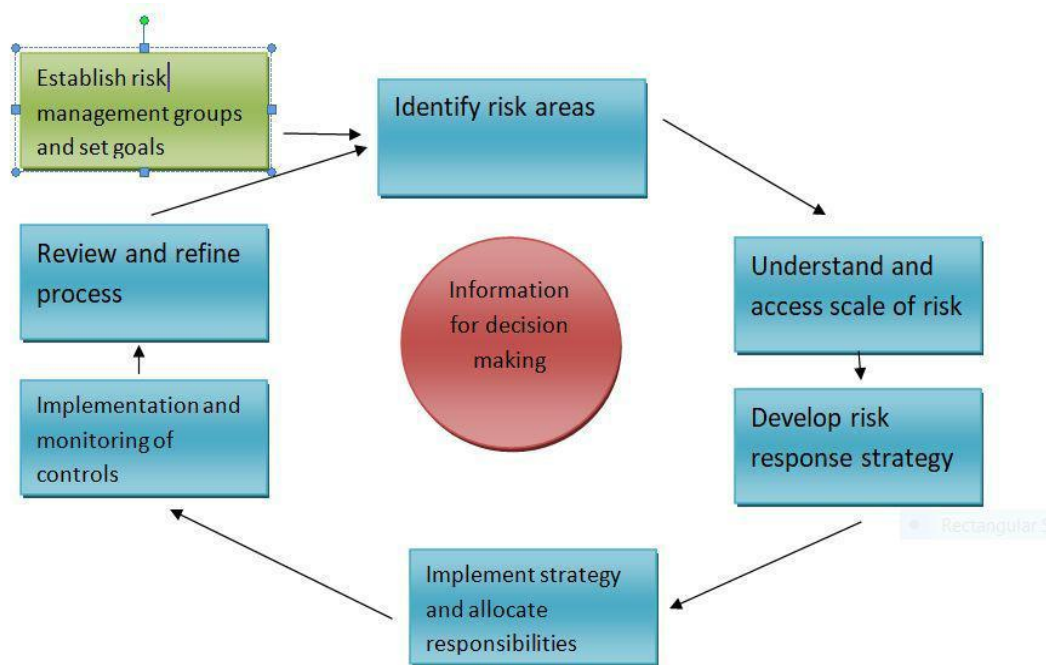
Risk involves the chance an investment's actual return will differ from the expected return or possibility of losing some of all the original investment. Financial risk is any of various types of risk associated with financing, including financial transactions that include company loans in risk of default. To minimize the risks we need risk management.

What is risk management?

Risk management is defined as the process of understanding and managing risks that the entity is inevitably subject to in attempting to achieve its corporate objectives. It is about understanding the nature of potential events that could influence the organisation to achieve its objectives and where they represent threats, making positive plans to mitigate them.

It is a comprehensive approach to managing the risks utilizing the integrated efforts of all risk owners including senior management and business units and risk management agencies such as legal, audit, insurance, safety and environmental and human resources.

Risk management cycle



Requirements for risk management

Under clause 49, The company shall:

- Lay down procedures to inform board members about the risk assessment and minimisation procedures.
- Periodically review to ensure that executive management controls risk through means of a properly defined framework.
- Included in its annual report, a management discussion and analysis report on the risks and concerns within the limits set by the company's competitive position.

Factors of financial risks

Internal risks: Risks that deal with the chance that the strategies and actions the business leaders choose may have negative effects on operations.

- People
- Model
- Fraud

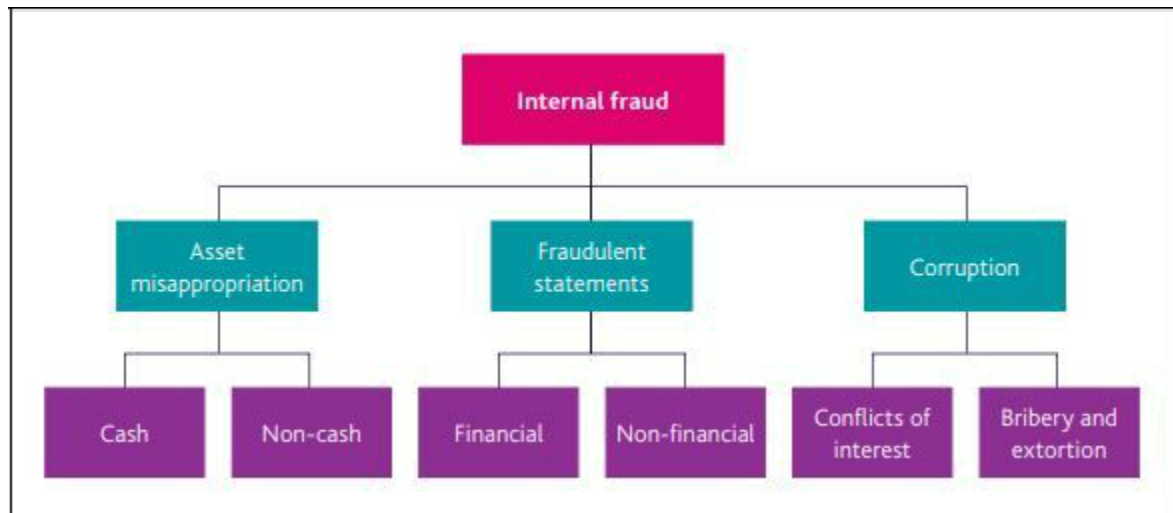
External risks: Risks depending on outside factors and decisions made by other organisations and consumers.

- Legal
- Economic

What is a fraud?

Corporate fraud commonly consists of activities that are done in a dishonest or illegal manner, such as theft, conspiracy, money laundering, bribery and extortion. It is done to make a personal gain for oneself and/or create a loss for another. It has an economic impact on the business, other employees and other parties.

Types of frauds



Asset misappropriation

It involves the theft or misuse of an organisation's assets. Any employee can steal from an organisation by making off with assets, such as cash or fixed assets. Weak controls can encourage employees to engage in these activities.

Fraudulent statement

This is usually in the form of falsification of financial statements to reveal excellent financial results. Examples of such falsification includes:

- Extending the depreciation period to delay depreciation recognition.
- Capitalize expenses
- Counting the non-existent inventory, which reduces the cost of goods sold.

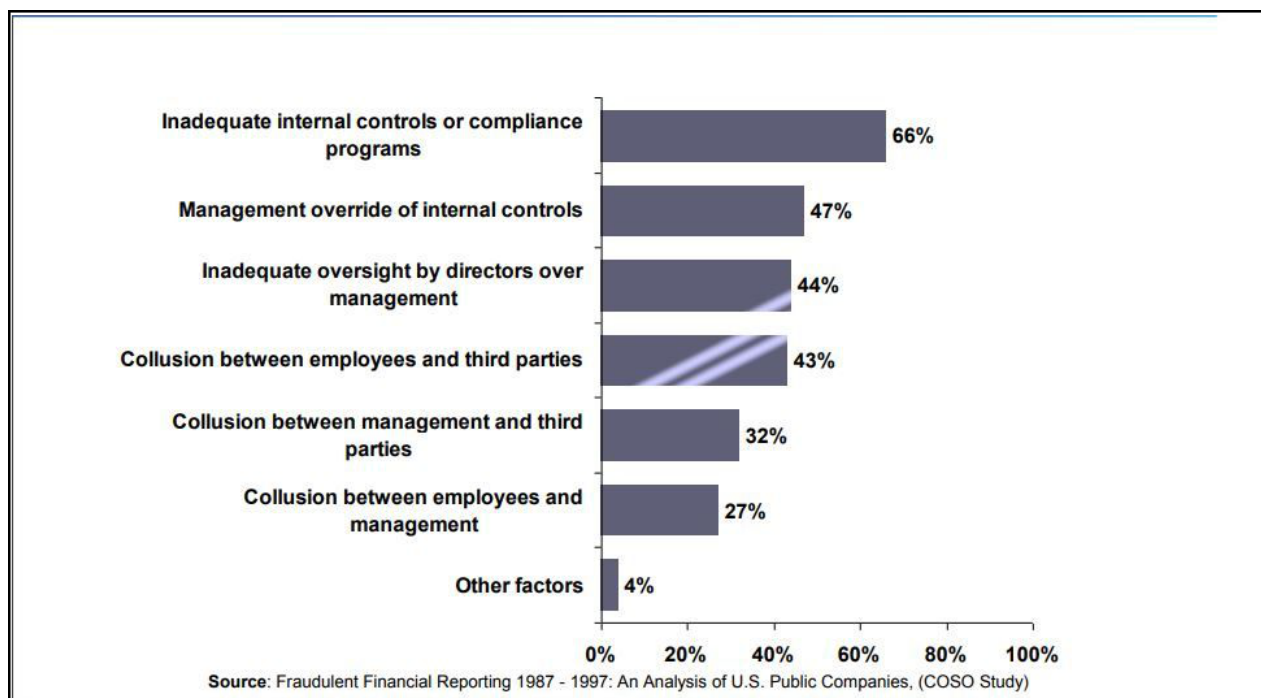
Corruption

It consists of activities such as use of bribes, improper use of confidential information, conflicts of interest or collusive tendering.

Supply chain fraud

A supply chain is a network between the company and its suppliers to produce and distribute a specific product, and the supply chain represents the steps that it takes to get that product to the customer. Supply chain fraud has become a widespread and increasing global risks for organisations. Modern supply chain has become more vulnerable to fraud due to its global reach, the depth of supplier networks, the sheer number of transaction, volume of financial activity, the increasing need of resources to combat fraud, and the complexity of information technology systems. However, most of the companies do not take supply chain fraud prevention seriously. According to ACFE(Association of Certified fraud examiner) 44.7 percent of fraud cases were discovered through a accident while 39.2 percent of the cases were discovered by internal audit, management review, account reconciliation or document examination.

Enablers of fraud and misconduct in supply chain



How are supply chains targeted?

Supply chain operations provide abundant opportunities for fraud or misconduct, both by employees and external parties. Common supply chain fraud scheme includes :-

Asset Misappropriation	Financial Misrepresentation	Bribery/Corruption
■ Forgery ■ Cash Theft ■ Merchandise Theft ■ Unpaid Services ■ Billing Schemes ■ Payroll Schemes	■ Revenue Recognition ■ Expense Recognition ■ Asset Inflation ■ Channel Stuffing ■ Earnings Manipulation ■ Cookie-Jar Accounting ■ Insider Trading	■ Bribery of Government Officials ■ Commercial Bribery ■ Insider Trading ■ Kickbacks ■ Contract Manipulation ■ Poor Decision-making

The impact of supply chain frauds

The discovery of an organisations failure to comply with regulations can have catastrophic effect on the supply chain :-

- Manufacturing slowdown or breakdown
- Quality or capacity reduction
- Loss of market share
- Increased insurance cost
- Damage to the brand and increased media/advertising cost
- Inability to supply customers

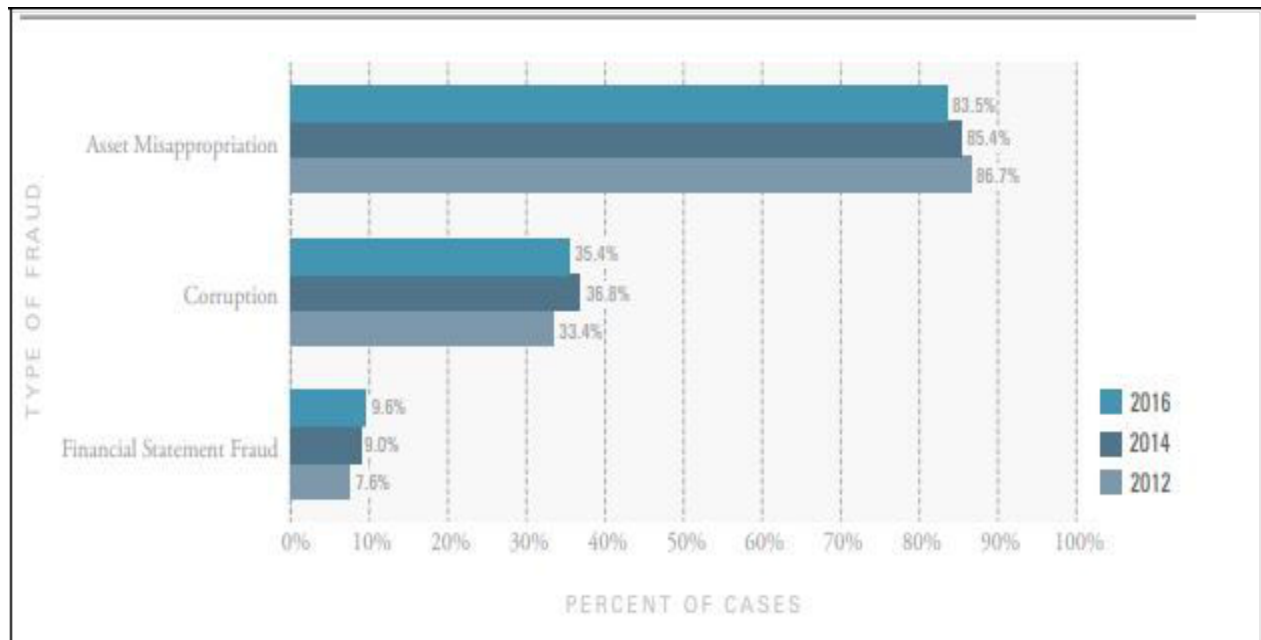
The scale of the problem

As one of the key aspects of fraud is deception, it can be difficult to identify.

Although survey results and results do not give a complete picture, the various statistics do offer a useful indication as to the extent of the problem.

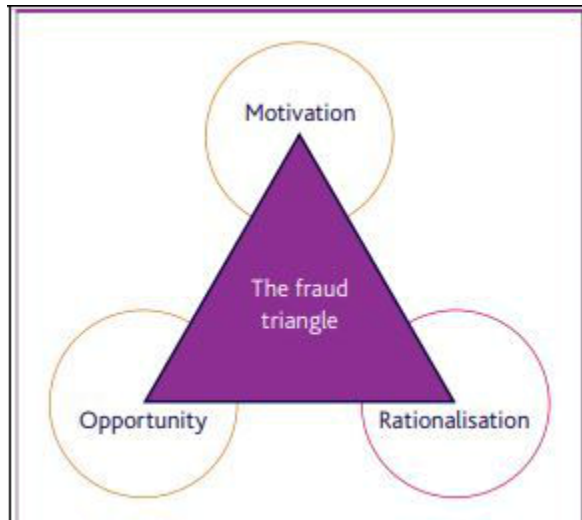
It is estimated that asset misappropriation is by far the most common of the three primary categories.

On the opposite end is the financial statement fraud, which was involved in less than 10 percent of the cases.



Why do people commit fraud?

We can not define any single reason for fraud and explanation of it takes a lot of factors into account. A fraud triangle is based on the premise that fraud is likely to result from a combination of three factors:- motivation, opportunity and rationalization.



Motivation:- It is based on greed or need. Other reasons include problems with debts and gambling. Personality and temperament, including how frightened the person is about the consequences of taking risks, play a role.

Opportunity:- Fraud is most likely in a company where there is a weak internal control, poor security, unclear policies or little fear of exposure.

Rationalization:- Some people rationalize fraudulent actions as:-

Necessary - when done for the business

Harmless - because the victim is large enough to absorb the impact

Justified - because 'the victim deserved it' or 'because I was mistreated.

Miscellaneous Activities

Cash operations

As a business owner you are likely to accept cash payments from customers. Although convenient for customers, this comes with a slew of problems for you. And there are a number of ways in which an individual can commit fraud by stealing cash from a business.

Earlier, the cash payment was done extensively. Then slowly the company shifted to paying the expenses by bank and now almost all the payments are done through bank. Some of the payments done by cash include :-

- Traveling expenses to employees who travel short distances.
- Traveling expenses to employees who have to travel in urgency.
- Small legal expenses.
- Refreshment expenses.
- Any other expenses as directed by the head.

There are several ways in which cash frauds can be committed :-

No accountability :- You could lack proper accountability, when your cash handling procedures aren't as tightly controlled as they could be. And there is no chain of custody when cash is removed. Employees are in and out without record. When this happens, it's really difficult to track down where and what errors happened. You won't be alerted to suspicious behavior as soon as possible and it becomes almost impossible to fix them.

Risks of theft :- This includes both internal theft and robbery. There's a risk of employee theft at any point in the cash cycle : during transaction, while cash is in transit, while it's being counted, while it's been deposited or any other time.

Robbery is another possibility, when you keep too much cash on hand or your money is exposed to customers at any point, you risk getting robbed.

Counterfeit fraud :- This fraud is real and is increasing rapidly. Criminals have almost perfected the task of printing fraudulent bills, and if you accept this cash, you'll be the one suffering the loss at the end of the day.

Transactional errors :- This error is inevitable in nature. If your employees don't have the right documents and have no proper training, then they would not be comfortable processing any type of transaction, from making voids and processing refund to handling out discounts

Accounting errors :- This includes lose counts, record number incorrectly, skip numbers, mix up denomination when handling large volume of cash. This risks increases when your employees are counting and sorting money at the end of the day.

Payment of expenses through banks

The voucher which is passed for payment is paid mostly through the bank. In the month end, a report is made in which outstanding payment is recorded and the reasons for why it is outstanding for a period of more than 1 month is given.

Risk management process

Risk management is defined as the process of identifying, monitoring and managing potential risks in order to minimize the negative impact they may have on an organization. An effective risk management process will help identify which risks pose the biggest threat to an organization and provide guidelines for handling them.

The report on high risk is communicated to the board of directors in a periodic manner. Here are the steps :-

1. Identify hazards :- Here are some ways to identify hazards :-

- Incident report forms
- Self - inspection checklists
- Observation and consultation
- Regular maintenance checks
- Knowledge sharing

2. Assess the risks :- Now, the risks is rated high, medium or low as per the guidelines issued by the corporate office(Mumbai). It is based on the probability of the event to occur and the consequence of that event. Probability is given as per the possibility of the event occurring in next 12 months. The consequence can be qualitative or quantitative. The qualitative consequences are rated on the basis of the impact it has on Profit before interest depreciation and tax. Qualitative consequences include loss of life, destruction of

property, loss of reputation etc. The ratings of probability and consequence are multiplied and then the resultant number is the deciding factor of the rating of the risk.

3. Control the risks :- Often a series of controls should be implemented to reduce the risk posed by a hazard. The hierarchy of risk control is useful in determining appropriate and interim risk control measures.



4. Monitor/ review control measures :- How are controls monitored?

- Ensure audits and workplace inspection are conducted.
- Ensure listed control measures are in use and maintained.
- Risk register reviewed on a regular basis.

Income taxes

The Income tax procedures are vast and have to be complied with. The income tax includes

- **Tax Deducted at Source/ Tax Collected at Source**: The tax is deducted at source on expenses such as rent, salary, professional services, contract and payment to foreign residents. The tax is deducted at source when the expenses are booked in the books. At month end, the summary of the taxes deducted is taken out using SAP and is paid by the company.

- **Advance Tax:** The advance tax is paid by the company on the basis of the estimated income of whole year. The due dates for paying advance tax are 15th June, 15th September, 15th December, 15th March.
- **Tax audit:** The Company is subject to tax audit as per section 44AB of the Income Tax Act. The tax audit is generally started in the month of June. The last day to submit the audit report is 30th November as transfer pricing provisions are applied.
- **Transfer pricing:** The companies try to evade tax by transferring profits to associate entities which are in a lower tax bracket or that country has a lower tax rate or no tax is levied on it. To stop this, transfer pricing provisions were introduced. The arm's length price is calculated and transactions are then adjusted for the same.
- **Assessment procedures:** Income tax authorities carry out assessment under various sections of the Act to ascertain if the tax paid is correct or not.

Risks and fraud activities

Income tax fraud is the willful attempt to evade tax law or defraud the IRS.

Tax fraud occurs when a person or a company does any of the following:

- Intentionally fails to file a income tax return
- Willfully fails to pay taxes due
- Intentionally fails to report all income received
- Makes fraudulent or false claims
- Prepares and files a false return

Is it Negligence or Income Tax Fraud?

- The IRS can usually distinguish when an error is the result of negligence or the willful evasion of the tax law.
- Tax auditors look for common types of suspicious and fraudulent activity, such as:

- Overstatement of deductions and exemptions
- Falsification of documents
- Concealment or transfer of income
- Keeping two sets of financial ledgers
- Falsifying personal expenses as business expenses
- Using a false Social Security number
- Claiming an exemption for a nonexistent dependent, such as a child
- Willfully underreporting income

GST

The Goods and Service Tax was implemented in India from 1st July 2017. Since then, major reform in software SAP is undertaken by the company to accommodate the reforms of GST. TCS was the company who was hired to take this mammoth task.

When GST was implemented, many problems were faced by the company as many provisions needed clarification. These problem are now smoothened and GST is paid and returns are filed in timely manner.

The GST now paid by the company is almost double the amount earlier paid by the company in indirect taxes. This blocks the working capital of the company.

Basic features of GST:

- Broad-based consumption tax – Levied on all goods and services
- Certain goods and services to be exempted
- Imposed on money spent, not money earned
- Transaction-based, multi-stage tax applying at each stage of the production and distribution process

Common GST Fraud Practices:

- Under-reporting of total sales, resulting in lower GST output tax
- Fictitious supplier invoices created to facilitate higher ITC claim
- Collusion between related parties – undervaluing supplies where the recipient cannot claim full ITCs
- Claiming of ITCs on expenses disallowed under the law
- Underpayment of GST on “imported services” (e.g. FS companies)
- Suppliers not registering for GST where required
- Suppliers charging GST where not registered
- Identification of direct expenses and common expenses for ITC claim

Protecting against Frauds and Errors:

- Ensure a robust internal system for recording, processing and reporting GST
- Consider the potential for manipulation (e.g. manual v automated actions)
- Separation of duties for GST (approving, processing, reporting, payment)
- Develop comprehensive reconciliation procedures for GST reporting
- Conduct periodic reviews
- Vendor verification – Confirm GST registration status and details
- Education – Personnel to know consequences of GST fraud and errors
- Training – Ensure personnel are GST-knowledgeable and aware of risks

Insurance

Insurance fraud comes in a few different shapes and sizes. Some types of fraud are done on purpose, some types involve small lies that may seem like they won't matter, and some are committed without the person committing them even realising. The cost of insurance fraud each year is big — it's in the billions — and while it may seem easy to ignore these costs because they only affect insurance companies, the reality is that insurance fraud ends up costing you and others, be it in the form of higher premiums, higher excesses or policies with more things an insurer won't cover — all of which are aimed at cutting down the increasing costs of fraud.

Types of Insurance Frauds

1. Non-disclosure fraud

Non-disclosure can be both deliberate and inadvertent. Fraudulent non-disclosure basically means that you haven't revealed information to an insurer that might affect their decision to insure you or to pay out a claim. For example, when applying for car insurance, you may neglect to mention a conviction for drink-driving or you may tell your insurer that your car is always parked in a secure garage overnight when, in fact, it's typically parked on the street. It's important to note that even unintentional non-disclosure is still fraudulent.

2. Deliberate fraud

Deliberate fraud is premeditated and calculated in an effort to defraud an insurance company. That is, someone planned to commit fraud to make money. Common types of deliberate fraud include setting fire to property or faking a theft in order to receive an insurance payout.

3. Exaggeration fraud

Exaggeration is pretty straightforward and is mainly limited to when a person makes a claim — it involves exaggerating the amount of damage or the cost of the loss in order to increase the payout of a claim.

As we can see from the various types, insurance fraud isn't limited to criminals. Even well-behaved people can often be tempted to leave out important information or inflate the value of a claim for their own personal gain, and it can also be the case that a person doesn't realise they are committing a crime by exaggerating the facts or failing to disclose important information.

Fraud Detection & Protection

- Insurance companies are putting a lot of resources and money into combating insurance fraud, and new technology and software is being used to identify it, along with specialist claims training and engaging with specialist investigators.
- Additionally, the Insurance Fraud Bureau of Australia (IFBA) works with insurance companies to notify them of information relating to possible insurance fraud so that those companies can then investigate and act on these suspicions of fraud. The IFBA also works to help develop strategies that can be used across the industry to help stamp out insurance fraud and, as a result, protect honest consumers from having to bear some of the costs of insurance fraud.
- The Insurance Council of New Zealand (ICNZ) have an online form along with a toll free number (0505 372 835) where the public are encouraged to call and report information about potential Insurance fraud cases. ICNZ use the information submitted to make investigations with Insurers who may take further action if necessary.

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