

MicroSave Briefing Note # 92

Internal Audit and IT-Based MIS System

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Scope of the IT-based MIS for Internal Audit

An IT-based MIS system plays a crucial role in maintaining records/data accurately. It provides a level of reliability to the stored information, while supporting analysis and strategic decision-making. It also saves time in analysing and consolidating information input across geographies, and provides greater efficiency by supporting operational processes.¹ With the maturation of the sector, IT-based MIS systems for Internal Audit have an important role to play in a variety of circumstances including:

1. **Multiple products:** In the case of multiple products offered by a microfinance institution (MFI), the internal auditor can easily verify whether the client has taken more than one type of loan at a time. This makes it easy for the internal auditor to assess whether it was a mistake or has been done intentionally by a loan officer.
2. **Urban microfinance:** In urban areas the population is very dense and branches are located in close proximity. There may be cases where clients have taken loans from two different branches. It can be really challenging to identify such cases if the system of loan tracking is manual. With an IT-based MIS system, the internal auditor can make such checks across the branches and can identify such cases.
3. **Credit-worthiness of the client:** An internal auditor can easily make a credit check of clients who are in their second or more loan cycles using most IT-based MIS systems. This can help in ascertaining that previously delinquent clients have not been provided with loans.
4. **Increased competition and multiple borrowing:** An increased number of MFIs in competitive markets pose a unique challenge for the auditor, because the clients can borrow from several simultaneously. Where this exists, access to a credit bureau can help internal auditor in identifying cases having multiple loans.
5. **Individual lending:** Internal audit teams generally check to ascertain whether the guarantor has given guarantees to more than one client. This can be easily verified if data is managed using IT-based MIS system.

Currently, most MFIs have manual information systems. This makes the task of internal audit challenging and cumbersome. While conducting an audit, the auditor has to depend on hard-copy documents. It is very difficult to track changes if they have been made in ledgers, files or registers. Much time is wasted as the internal auditor moves back and forth between the electronic and paper documents while conducting audits. This problem is solved with an IT-based MIS system because there is real time tracking of any changes made in data² as in Equitas, the fastest growing microfinance institution in India.

Internal Audit Perspective of an MIS3

To accomplish an internal audit, the auditor must complete several vital tasks:

- **Audit Plan:** Internal audit departments require detailed audit plans and schedules, which must be available to all department staff. An IT-based MIS with a fully integrated internal audit module supports a detailed audit plan and operational details.
- **Audit Management:** For smaller MFIs, audit management is not difficult. A typical small MFI with 4-5 branches can easily audit its branches within 2 months. But for larger MFIs (for example with more than 100 branches) managing Internal Audit is a cumbersome task. To conduct quarterly audits for all branches requires the management of an enormous amount of information. Compounding this problem is the need to track and follow up the audit findings with branches.
- **Integrated Audit Trend:** An audit results in key findings and recommendations for a branch on specific issues. It is very important for MFIs to monitor audit trends across branches for the following reasons:

¹ Management Information Systems (MIS) for Microfinance, Ali Ahmad, The First Microfinance Bank Ltd., August 16, 2010

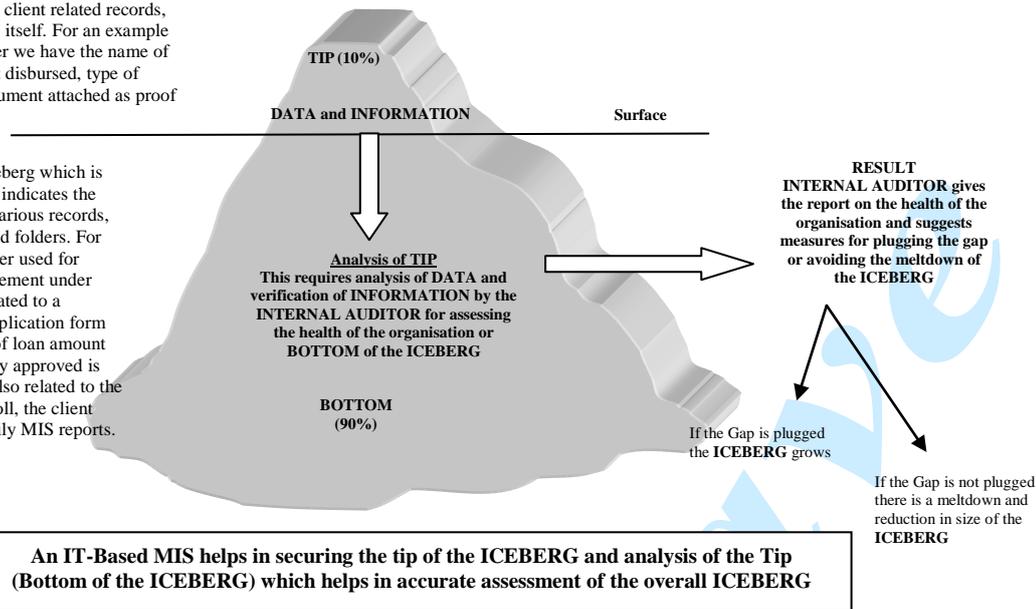
² Innovation in India: Microfinance and Information System by Greg Chen, March 31, 2009, downloaded on August 16, 2010

³ Continuous Monitoring and Continuous Auditing: From Idea to Implementation published by Deloitte, August 16, 2010

Model representing the functioning of Internal Auditor and the role of IT based MIS

Tip is represented by the records, file, and folders like filled loan application form; daily, weekly, and monthly reports, vouchers, client related records, and IT based MIS itself. For an example on a given voucher we have the name of the client, amount disbursed, type of entry, related document attached as proof

Bottom of the iceberg which is under the surface indicates the inter relation of various records, registers, files, and folders. For example, a voucher used for recording disbursement under observation is related to a particular loan application form where the detail of loan amount applied and finally approved is mentioned. It is also related to the disbursement scroll, the client passbook, and daily MIS reports.



- to find the key areas of risk and check the effectiveness of control mechanisms;
 - to organise trainings on specific issues like accounts, MIS, and customer relationships in response to the findings;
 - to identify types of fraud and flag early warning indicators;
 - to check compliance; and
 - to follow up on recommendations for the branches.
- **Documentation:** In a manual system internal audit reports are kept in a hard copy and distribution/sharing is quite difficult. Moreover, to prepare a report requires lot of time. If the internal audit system is integrated with the MIS, the documentation is done as soon as the audit is completed. Once verified, it can then be widely circulated within the organisation for comments.

Role of Internal Audit in IT based MIS

As the microfinance sector diversifies and brings in new innovations, the risk profile of the sector is changing. Increased competition is aggravating the complexity of the internal audit functions. IT-based MIS provides enough capability to handle all these changes.

The challenges of competition, multiple lending, tracking clients, analysing repayment capacity will make the task of internal audit more complex. To

check for compliance, and to verify if there is any fraud, the internal auditor has to conduct IT Audit of the system⁴, because most of the information is stored there. This is one of the most credible risks for the internal auditors posed by an IT-enabled MIS. This facilitates the task of the auditor by allowing him/her to examine the log file generated by the system, and thus to identify who has entered and what information they sought from the system. The internal auditor should also look into the reports and their accuracy, and validate them in the field.

The above 'iceberg' model shows the precise role of IT-based MIS. By providing accuracy and speed, an IT-based MIS system helps the internal auditor identify and plug risks more effectively. This prevents the MFI from experiencing a 'melt-down' from eroding system that trigger very high risk.

Microfinance is all about managing operations and risk, and therefore requires an efficient monitoring system. Audit plays this function. An IT-based MIS system helps the auditors in analysing large numbers of branches quickly and efficiently, thus reducing cost and saving time with more accurate and reliable results. IT-based MIS is can therefore significantly enhance the capability of internal auditors.

⁴ Management Information Systems: Comptroller's Handbook by Comptroller of the Currency Administrator of National Banks, Page 17 to 23, May 1995