Mitigating compliance risk with Dynamics 365 Finance

Leveraging Dynamics 365 Finance to reduce compliance risk and improve control efficiency for Internal Controls over Financial Reporting

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1 Executive summary

The US regulatory environment is continually changing, and organizations must maintain awareness of the legal, regulatory and capital impacts of their business decisions. The Sarbanes-Oxley Act was introduced to restore and enhance public confidence in the financial reporting and disclosure process and improve executive responsibility and accountability.

Many organizations face compliance concern related to Section 404 of the Sarbanes-Oxley Act (SOX). This rule requires management to assess the effectiveness of the company's internal control over financial reporting, including the appropriateness of the control documentation, and report on internal controls within an organization's annual report to shareholders. Organizations that maintain a deliberate SOX compliance strategy are more likely to strike the right balance between compliance adoption, organizational agility, and growth.

Technology is a key enabler to address the change and complexity in an organization's compliance environment. It is crucial to understand how your underlying technology environment can help support your business process, compliance and regulatory requirements such as Sarbanes-Oxley.

While the compliance obligations of Sarbanes-Oxley are broad and can be complicated, Microsoft Dynamics 365 Finance includes functionality that helps organizations meet their compliance obligations in a flexible, adaptable, and scalable fashion.

This whitepaper discusses the dimensions of SOX and some relevant aspects of Microsoft Dynamics 365 Finance to help customers address SOX compliance.

This document was prepared by PricewaterhouseCoopers LLP ("PwC") and Microsoft Corporation ("Microsoft"). It provides information to help current and prospective customers to evaluate the reporting and compliance capabilities of Microsoft Dynamics 365 Finance (version 10.0.10 [May 2020]).

Microsoft Dynamics 365 Finance was used as the basis for evaluating how the software supports SOX compliance objectives out-of-the-box. The statements made in this document may also apply to to successor versions of Microsoft Dynamics 365 Finance. Each implementation of Microsoft Dynamics 365 Finance is unique, and the way this software is deployed might affect an organization's ability to meet its U.S. generally accepted accounting practices (GAAP), or Sarbanes-Oxley (SOX) compliance requirements. Customers should evaluate these implications and consult a professional advisor based on their business processes and needs.

2 Overview of Sarbanes-Oxley

The Sarbanes-Oxley (SOX) Act was signed into law on July 30, 2002. This act was designed to restore and enhance public confidence in the financial reporting and disclosure process and the accounting profession. In addition, it was designed to strengthen enforcement of federal securities laws and improve executive responsibility and accountability.

The Sarbanes-Oxley Act Section 404 requires SEC registrants to provide the following with their annual filing:

- A statement of management's responsibility for establishing and maintaining adequate internal control over financial reporting;
- A statement identifying the framework used by management to evaluate the effectiveness of internal control;
- Management's assessment of the effectiveness of internal control as of the end of the company's most recent fiscal year end; and
- A statement that the company's external auditor has issued an attestation report on management's assessment

3 Definition of risks for SOX or Internal Controls over Financial Reporting (ICFR)

Before identifying how to manage risks in the business, organizations must identify the specific risks to be mitigated. When an organization sets out to assess risk, it's helpful to first define a set of goals or requirements. The following illustrates some risk categories to consider:

1. **Compliance** - Risks as defined by a governing body or regulations that the organization is lawfully responsible to demonstrate how they are mitigating the risks within the regulation

2. **Financial Reporting** - Managing the risk of incomplete or inaccurate information being reported on the company's financial statements

3. **Operational** - How to mitigate risks to the company's running of the day-to-day business

By preparing a population of risks before identifying what controls to implement in your processes and technology, an organization can begin to identify what steps they need to take to address the risks and what tools or options are available to help in this effort.

4 Microsoft Dynamics 365 Finance features to capture the value of controls

Microsoft Dynamics 365 Finance provides functionalities that enable organizations design processes and controls to mitigate their organization's unique risks. To take advantage of these functionalities, organizations must be proactive in designing Microsoft Dynamics 365 Finance and the associated business and IT processes to enforce the controls and effectively mitigate the identified risks.

As a Software as a Service solution, Microsoft Dynamics 365 Finance is hosted and supported by Microsoft. Microsoft issues SOC 1 and SOC 2 reports to help provide customers assurance that Microsoft has implemented appropriate controls to address the risks related to both the hosting and development of the Microsoft Dynamics 365 software. Organizations should understand the coverage and limitations of the SOC report and follow suggested Complimentary User Entity Controls (CUECs) to help manage their organizations IT General Control risks, including but not limited to access control, segregation of duties, configuration management, integration development, data management and reporting.

Access control and segregation of duties

A key component of compliance is the introduction of controls to secure access to features and data. To enforce effective controls, companies should create appropriate checks and balances to confirm that their systems are not only secured but also maintain strong segregation of duties between conflicting functions in the organization that may reduce the potential risk of unintended, malicious or fraudulent activity.

Microsoft Dynamics 365 Finance supports role-based security, which, when configured appropriately, helps manage growing complexities in organizations security by utilizing reusable permissions, default and sample security definitions. In a role-based security environment, users are assigned to roles based on their responsibilities in the organization and their participation in business processes. Microsoft Dynamics 365 Finance supports segregation of duties giving the ability to setup rules indicating when two duties must be performed by separate roles or users for better security or better compliance with policies and regulations. Microsoft Dynamics 365 Finance supports access only to authorized users through single sign-on and multi-factor authentication capabilities.

In Microsoft Dynamics 365 Finance, the extensible data security framework can be used to help organizations protect their data. By using this framework, organizations can create data security policies that, for example, grant 'view' access to one subset of sales orders and 'edit' access to another subset of sales orders. Microsoft Dynamics 365 Finance supports electronic signatures to help enable compliance and accountability as required by regulations, law or company policy for critical business processes.

Documenting processes and controls

Microsoft Dynamics 365 Finance provides a central location for users to view, manage, and control the internal controls, business process content and reporting for the organization's compliance program. The Compliance Center provides access to required documentation, internal controls, and status tracking. From the Compliance Center, users can view graphs representing the efficiency and effectiveness of the internal controls, examine key performance indicators, manage action items from alerts or workflow, and add links to important external compliance sites.

The Business Process Modeler in Microsoft Dynamics Lifecycle Services is pre-populated with a standard process map based on the APQC's (American Productivity & Quality Center) cross industry framework. Power Automate with Microsoft Dynamics 365 Finance delivers capabilities to automatically document business processes, by recording tasks performed in Microsoft Dynamics 365 Finance as process flow diagrams and step by step documentation.

Business rules and automation via workflow

Microsoft Dynamics 365 Finance workflow editor allows an organization to help define business rules and automate processes, enabling users to follow a specified set of processes that give companies greater and stronger internal automated controls.

Workflow in Microsoft Dynamics 365 Finance enables the setup of an approval process for selected transactional functions, for example accounting journals. The approval process allows a user to help define the conditions under which approvals are required and link this to the organizational hierarchy to provide appropriate levels of review and approval. The posting of the transaction is therefore placed in a pending status until the appropriate approvals are received providing internal control over workflow-enabled processes. Lastly, in addition to capturing levels of approach, workflow capabilities in Microsoft Dynamics 365 Finance provide a mechanism to track the status of a document workflow (e.g., from initiation, to pending approval, approved, or rejected) to help provide a timely completion of an open item.

Configurable business process controls

Another example to enable company policies through automation in Microsoft Dynamics 365 Finance, is leveraging business process capability to help prevent and/or detect risk through configuration or configurable business process controls. Module specific policies can be configured to provide internal control for a specific business process. For example, within accounts payable, configuration can be applied at an organization, vendor, or product level to enable automated control areas such as a three-way or two-way match. Matching policies may be defined for any level based on invoice totals and tolerances to provide control, yet flexibility per your organization's requirements. If a matching discrepancy exceeds the tolerance it may need to be resolved or accepted should the differences be based on approval by an authorized user.

Further, you can create controls to validate data input (e.g., within your customer or vendor master records) for additional control across the organizations critical master data.

Tracking and tracing changes

Many compliance requirements focus on recording exactly what was done, when, and by whom. Microsoft Dynamics 365 Finance supports audit trails to identify the origin of an entry, the user who created it, and the date and time when it was created. Database logging in Microsoft Dynamics 365 Finance provides the capability to track, trace and report changes to data fields and tables that are relevant to your compliance strategy. Alert rules can also be configured to deliver automatic notification about sensitive data.

Reporting/Analytics

As organizations increase their use of configurable controls, certain risks may still require the use of manual review controls. For risks that require periodic reporting and reviews, Microsoft Dynamics 365 Finance has capabilities to enable customers to extract required information out of the environment and prepare it for appropriate review:

- **Preconfigured Reports** - For general report requirements commonly used by businesses, Microsoft Dynamics 365 Finance has preconfigured reporting options that can be used by organizations to review general business process information.
- **Customized Reports** - For report requirements that are not filled through the preconfiguring reporting options, Microsoft Dynamics 365 Finance has opportunities to build customized reports either through updating the preconfigured reports or designing new reports from scratch through the selection of information from Dynamics data tables.
- **Power BI** - Through Microsoft's Power BI, companies can perform complex analytics and data visualizations that can aide in the review and decision making of report data. Power BI can be connected to Dynamics and built up based on a business's needs.

Audit trails

When high risk activities can't be controlled through other configurations or reporting. A company may need to enable specific review of user activity and compare back to business process requirements to confirm appropriateness of the activity.

Audit trails can be enabled to see changes to information stored in the Microsoft Dynamics 365 Finance data tables. By enabling audit trails on these tables, management can keep a record of old and changed values within configurations, master data, and transactional data. Best practice is generally to limit the enablement of audit trails on master data and configurations, due to potential impact on system performance through tracking high volumes of transactional activity.

5 Bringing it all together – A Governance approach to security and controls

Organizations need to actively identify, mitigate and monitor risks within their business operations to establish an effective internal control environment. A common pain point is finding the right balance of risk mitigation and operational efficiency to help achieve the appropriate level of internal control for the organization. By investing in strategic enterprise-wide business transformation enabled by Microsoft Dynamics 365 Finance, opportunities exist to implement security and control procedures that could likely enhance risk management and deliver standardized, sustainable business processes.

PwC's security and controls integration methodology focuses on delivering the right mix of automated, manual and security-related controls to help manage identified risks across business processes enabled by the Microsoft Dynamics 365 Finance solution. Collaborating with an organization, PwC prioritizes leveraging standard Microsoft Dynamics 365 Finance functionality and designing security controls that could likely help increase automation and simplify compliance efforts. PwC's security and controls methodology places emphasis on:

- Designing preventive, automated configurable controls leveraging standard out-of-the-box Microsoft Dynamics 365 Finance capabilities
- Establishing effective and efficient user security and segregation of duties
- Maintaining fit-for-purpose audit insights, business process monitoring and exception-based reporting
- Driving scalability and sustainability of an organization's compliance environment
- Establishing effective audit trails, logging and monitoring practices
- Post integration support to validate compliance and control effectiveness and adoption

6 Summary of Microsoft Dynamics 365 Finance considerations to help mitigate risk

While the compliance obligations of Sarbanes-Oxley are broad and can be complicated, Microsoft Dynamics 365 Finance has been designed with the capabilities to help organizations meet their compliance obligations in a flexible, adaptable and scalable fashion.

By integrating security and controls considerations into your overall Microsoft Dynamics 365 Finance implementation, an organization can build the right foundation to achieve its internal control objectives and benefits including:

- Automate control activities, eliminate redundant/inefficient controls, and improve the overall quality of your internal control framework by reducing manual touchpoints
- Decrease the level of effort required to help sustain controls and perform audits
- Increase your internal control coverage and comfort by maturing the use of out-of-the-box Microsoft Dynamics 365 Finance functionality
- Established governance model that focuses on awareness of the control environment and monitoring of compliance within the Microsoft Dynamics 365 Finance solution

By deploying Microsoft Dynamics 365 Finance with a proactive focus on internal control design, your business management solution will likely remain relevant to the needs of your people, the needs of regulation and compliance and to the demands of your industry and business.

7 Contacts page

PricewaterhouseCoopers LLP (PwC) and Microsoft Corporation have formed a strategic alliance to help companies engage in enterprise transformation projects that use Microsoft Business Applications technology. With this alliance, PwC is the first major alliance recognized by Microsoft's Dynamics Group as a Global Business Transformation Partner, which allows it to build business transformation services around the Dynamics 365 suite of applications.

Under the agreement, PwC consultants help provide advice and implementation assistance to clients who select Dynamics 365 together with other Microsoft technologies, including Microsoft Dynamics 365 Finance (enterprise resource planning (ERP), customer relationship management (CRM) and business intelligence (BI) solutions, as part of a business transformation project.

PwC contacts

Jamie Draper, Principal
james.draper@pwc.com

Abhijit Patankar, Principal
abhijit.patankar@pwc.com

Rajesh Balaraman, Principal
rajesh.balaraman@pwc.com

Matthew Korros, Director
matthew.d.korros@pwc.com

Michael Gallagher, Sr Manager
michael.gallagher@pwc.com

Microsoft contacts

Dynamics 365 for Operations IFRS Discussion
daxifrs@microsoft.com

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