Back to Basics - Blind Spot in Internal Audit of Revenue Cycle

While driving, there is an area termed as a blind spot, a blind spot is the area of the road that can't be seen by looking forward through your windscreen, or by using your rear-view and side-view mirrors. Blind spots can be large enough in size to easily block another car, motorbike, cyclist, or pedestrian from your view.

Similarly in an internal audit, does the auditor come across blind spot areas and how to make them more visible, and try to understand risk and exposure for that areas? A blind spot in auditing can be in any of the areas where the management is hiding something material facts deliberately from the auditor or the auditor missed something important, but as an auditor how these areas can be more visible and identify whether any fraud risk exists in that area or material facts are hidden?

Take an example auditing the revenue cycle, from order to cash, the auditor will perform the normal routine steps to verify the transaction from order to cash and do the sampling test to ensure the revenue recognition principles are met, the cutoff is ensured, discounts/rebates are recognized, provision is made for aged debtors, disputed/legal cases are added to notes to account and so on. But the blind spot could exist and can be reduced with the help of the below review;

- Revenue to cash reconciliation (Blind Spot – Fictitious sales and debtors);
- Number of systems/applications used in revenue process (Blind Spot – Customer data mismatch);
- Number of genuine customer base (Startup fraud, JPMorgan Chase is suing the 30-year-old founder of Frank) (Blind Spot – Fictitious customers, sales and debtors);
- Reconciliation of data and reports from the multiple systems and apps used;(Blind Spot – financial assertion, uniform financial figure across the company);
- Source of account confirmation and matching the balances with customer books of account; (Blind Spot – Balance mismatch)
- Customer customers and customer buyers' financial position; (Blind Spot – Recoverability and provision)
- The pricing and costing of products for each customer; (Blind Spot – Transfer pricing and related party sales)
- Margin analysis of each customers product range vis-à-vis cost of sales; (Blind Spot – Manipulated COS)
- Actual sale or accommodation transactions; (Blind Spot – Inflated revenue)
- Contracts and amendments with customers not accounted; (Blind Spot – Inflated profit)
- Leads generated from social media vis-à-vis actual customer base; (Blind Spot – Ghost customers)
- Customer retention ratio year on year basis; (Blind Spot – Ghost customers)
- Geographical consolidation of balances and reconciliation; (Blind Spot – Financial misstatement and concealment)
- Foreign debts, currency forecast including fluctuation; (Blind Spot – Provision misstatement)
- In the case of the FS industry, the customer base, and actual NPA classification. (Blind Spot – Provision misstatement).

The above is just an example that could be blind spot areas during the audit of the revenue cycle (order to cash). Each audit cycle will have an area of the blind spot and will be different from one industry to another industry. How the auditor uses his/her expertise to ensure that the risk of blind spots during the audit work is not overlooked, and area of blind spot is minimized to ensure that results of operations are not misstated.