Discussion Next-Level Auditing (Monday afternoon)

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We present nine challenges and a case for the auditing profession. We also include feedback received from presenting at conferences, workshops and in classrooms. Based on this we diagnose the status quo and share insights on how to best move forward to improve awareness of smart methodology and technology to address the completeness assertion.

1) You are the franchisor of a Chinese restaurant franchise with 1,000 locations. I run one of them. My franchise only records half of the meals sold. How do you detect my unrecorded sales?

2) Seemingly similar, you are the franchisor of a hotel franchise with 1,000 locations. I run one of them. My hotel regularly rents out rooms without recording. How do you detect my unrecorded rentals?

3) You are in charge of a dealer network of 1,000 stores. By coincidence, a few dozen fake stores are located. Moreover, it appears many more may exist. How do you detect all these unauthorized stores and new arising ones as early as possible?

4) You are on the management team of a western IT device production company that wants to outsource five licensed production units to the East. You know a competitor was plagued by a lot of cloned unlicensed production units. What is your approach to prevent this from happening to you?

5) You are at a tax revenue agency that wants to rely on a royalty receiver's internal control over completeness of revenue. What are your key criteria in screening?

Note: A royalty (sometimes, running royalties, or private sector taxes) is a usage-based payment made by one party (the “licensee”) to another (the "licensor") for the right to ongoing use of an asset, sometimes an intellectual property (IP). Royalties are typically agreed upon as a percentage of gross or net revenues derived from the use of an asset or a fixed price per unit sold of an item of such, but there are also other modes and metrics of compensation. Source: Wikipedia.

6) How to involve owners in smart audit oversight? For example, pension fund depositors and beneficiaries over pension fund management that orders and pays the audit.

7) How does smart auditing provide stakeholders with assurance that management did not understate and dump non-product output, like waste and pollution?

8) How to move assurance of completeness upstream to the point of first recording, in near real-time, while framing materiality for single data items?

9) How to get off-balance sheet derivatives back on the balance sheet? Covering $700 trillion, equalling 10 years worldwide gross domestic product. Which internal control measures can the audit profession articulate and attest for the micro-to-macro reporting channel from each individual financial institution to a governmental systemic risk agency? Connecting indicators on the micro-level (FpML: Financial product Mark-up Language) to

macro-level indicators (Bookstaber).

Case: You are the franchisor of a hair salon franchise with 1,000 locations that has the exclusive right to sell and use hair products of a high-end brand. I run one of them as a franchisee. In order to underreport royalties to the franchisor, my salon doesn't record clients that did not make a reservation and paid cash. Furthermore, my salon often dilutes or replaces the high end hair product with counterfeit, and sells the original product to the customer under the counter. What is your approach to keep me honest and offer the customer 100% assurance that she gets the genuine product in her hair? What is the added value, as return on investment, for franchisor, producer, franchisee, tax agency and internal and external auditor?

The first four challenges illustrate illicit shop-in-shop fraud scenarios. The first two are inside your premises and the latter two outside. Whether or not your management is involved in the latter two can only be decided after investigation. The first two challenges are about detection (negative assurance), while challenge 3 is about detection and prevention, and challenges 4 and 5 are about prevention (positive assurance).

Case Service dynamics (Tuesday morning)

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A service, even if conceived as a whole entity during its lifecycle, is subject to several changes according to its delivery context.

Let’s consider the lifecycle dynamics of the email service at a business firm with more than 5000 employees spread out into more than 100 offices all over the nation.

The service manager at the IT department is in charge of developing and delivering the email service to the whole organization. In this case study the description of the email service will be furtherly specified and enriched with new details along the lifecycle steps.

Let’s suppose the service manager must specify the email service offering according to what has been defined in (Van Sinderen, et al., 2013) in order to satisfy the requirements coming from his/her customer (or stakeholder) community. Meanwhile the service manager is in charge to design the service and look for providers able to deliver the (whole or part of the) services he has offered.

Let’s suppose that the email service is provided via Web browser and email client, on Intranet, on Internet, and on mobile devices. The service manager has chosen to outsource the email service (mailbox management for sending, receiving, archiving, securing and anti-spamming, etc.) to provider A and the network management to provider B. Moreover email service for mobile devices (like Blackberry) is provided by a mobile network operator C.

How to model services? What if the service changes? What about the relationships between the contracts between A and B (or C) and the contract between A and customer?