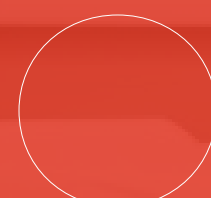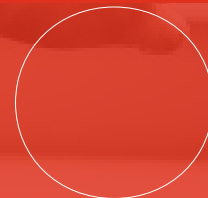October 2016

Internal Audit & E- Commerce Industry Speaker – CA Kartik Radia

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About E- Commerce Industry

E-Commerce – An Introduction

Electronic commerce (ecommerce) is a type of business model, or segment of a larger business model, that enables a firm or individual to conduct business over an electronic network, typically the internet. EC is the buying and selling of goods and services, or the transmitting of funds or data, over an electronic network, primarily the internet.

E-Commerce or Electronics Commerce business models can generally categorized in following categories.

- *B2B (Business to Business) - Example Staples, Quill, Office Max (Office Supplies), Medline, VWR, Gore Medical (Medical Supplies), Grainer, MSC Industrial, Fastenal, Parts Now (Industrial Supplies), Carolina Biological etc..*

- *B2C (Business to Consumer) – Example Amazon, Alibaba, Flipkart, Jabong, Myntra, E-bay, Shopclues, abof , Voonik etc.*

- *C2C (Consumer to Consumer)- Quikr, Sulekha.com, Olx.com*

E-Commerce - Some Facts

- *In 2006 the European e-commerce market was worth £66 billion. By 2011 that's forecast to reach over £200 billion, a massive increase – with Britain the biggest market of online shoppers on the continent.*

- *In 2010, the United Kingdom had the biggest e-commerce market in the world when measured by the amount spent per capita. As of 2013, the Czech Republic was the European country where ecommerce delivers the biggest contribution to the enterprises total revenue. Almost a quarter (24%) of the country's total turnover is generated via the online channel.*

- *With 668 million internet users, China's online shopping sales reached $253 billion in the first half of 2015, accounting for 10% of total Chinese consumer retail sales in the same period.*

- *Economists have theorized that e-commerce ought to lead to intensified price competition, as it increases consumers' ability to gather information about products and prices.*

- *India had an internet user base of about 354 million as of June 2015 and is expected to cross 500 million in 2016. The penetration of e-commerce growing at an unprecedented rate, adding around 6 million new entrants every month.*

- *In 2015, the largest e-commerce companies in India were Flipkart, Snapdeal, Amazon India, and Paytm.*

- *By 2020, India is expected to generate $100 billion **online retail revenue** out of which $35 billion will be through fashion e-commerce. Online apparel sales are set to grow four times in coming years.*

*Source - Wikipedia

Key Drivers For The Advent And Growth Of E-commerce Business

- Shift in the dynamics of consumer preference

- Brand trustworthiness and loyalty

- Buying Convenience – Analysis, comparison and evaluation(quick comparison of different options)

- Varity of choice provided at one click

- Cost, economy and effectiveness (competitive pressure)

- Intelligent business applications and software

- Deep Internet penetration

- Attractive and interesting business models – only responsibility for a customer centric focus, supply chain effectiveness and IT investments.

- Advancement of Payment banking and retail banking infrastructure

*Source - Wikipedia

Emergence of E-Commerce Industry

Amazon .com

- *Amazon was founded by Jeff Bezos in the year 1994.*

- *Amazon.com started as an online bookstore, later diversifying to sell DVDs, Blu-rays, CDs, video downloads/streaming, MP3 downloads/streaming, audiobook downloads/streaming, software, video games, electronics, apparel, furniture, food, toys and jewelry.*

- Now Amazon.com, Inc. which is the is the largest Internet-based retailer in the world by total sales and market capitalization* is an American electronic commerce company with headquarters in Seattle, Washington.

- The company also produces consumer electronics—notably, Amazon Kindle e-readers, Fire tablets, and Fire TV—and is the world's largest provider of cloud infrastructure services (IaaS). Amazon also sells certain low-end products like USB cables under its in-house brand AmazonBasics.

- In 2015, Amazon surpassed Walmart as the most valuable retailer in the United States by market capitalization, and is as of 2016 is the ninth most valuable company[20] overall.

*Source - Wikipedia

Emergence of E-Commerce Industry

Alibaba.com

- *Alibaba.com was founded in the year 1999 by Jack Ma to provide business-to-business portal to connect Chinese manufacturers with overseas buyers.*

- *Alibaba.com provides consumer-to-consumer, business-to-consumer and business-to-business sales services via web portals. It also provides electronic payment services, a shopping search engine and data-centric cloud computing services.*

- *In December 2001, Alibaba.com crossed break-even and achieved profitability.*

- *In September 2013, the company sought an IPO in the United States. The pricing of the IPO raised to US$25 billion, making it the largest IPO in history.*

- *It is the world's largest retailer as of April 2016. Alibaba entered India's e-commerce space with 25% stake in Paytm owner One97*

*Source - Wikipedia

Future Outlook of E-Commerce Industry

1 *Deeper and Deeper understanding of the customer and his/her profiling- buying patterns, income group, employment/occupation, age group and other demographics*

2 *Customized choice - customized screen-view (the player has all the information such as buying pattern, behavior to the specific customer which can enable to provide single screen view of suggested customized choices.)*

3 *Artificial intelligence – example Siri (Personal Shopping Assistant)*

4 *Innovation - Social Innovations, Technology Innovation, Market Research Innovation, Supply chain innovation*

Key Risks in E- Commerce Industry

Key Risks Areas in E- Commerce Industry

Supply Chain Management
(Inefficient supply chain management / inadequate supply chain support)

Sales & Marketing Strategy
(Inefficient Sales & Marketing Strategy not aligned with market, weakness in implementation of Sales & Marketing Strategy)

Vendor Management
(Inefficient vendor sourcing, contacting and monitoring management)

Information Technology
(Ineffective technology selection, upkeep, and security, business application not aligned to business requirement)

Claim, Refund and Return
(Lack of defined customer care procedures, ineffective customer care and support practices)

Key Risks & Controls – Revenue Assurance

Sr. No	Risk	Control
1	Unauthorized creation of or Changes to Sales Prices Master Data	Ensure all changes in prices are approved. Conduct periodic review of sales price master.
2	Unauthorized creation of or Changes to Product Master Data	Implement system settings to ensure that Product Master Data are complete and consistent.
3	Selling to customers with fraudulent intention or low solvency may lead to financial loss and incorrect quantitative figures in the financial statements.	Automated standard rating procedures are implemented to verify customer's identity, solvency and integrity
4	Acceptance of orders for non-available products leads to unjustified billing, incorrect quantitative figures in the financial statements and customer dissatisfaction.	System settings ensure that only available products can be ordered. (e.g. (1) products on stock; (2) products available due to drop ship agreements (3) products available due to cross-docking agreements)
5	The recording of duplicate sales leads to incorrect quantitative figures in the financial statements, customer is billed twice and receives the same product twice.	System settings are implemented to ensure that a customer order number is automatically created and do not allow double customer order numbers.
6	Missing Return Policy leads to erroneous returns and financial losses.	Ensure that Return Policy guidelines and other relevant policies (e.g. signature policy) are documented, up-to-date, approved and communicated to employees involved in the CRR process.

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Key Risks & Controls – Revenue Assurance

Sr. No	Risk	Control
7	Duplicate claims lead to financial loss and incorrect quantitative figures in the financial statements.	Ensure that fictitious and duplicate claims are prevented.
8	Fictitious, unauthorized or/and erroneous customer returns result in financial losses and incorrect quantitative figures in the financial statements.	Ensure that customer returns comply with company's return policy.
9	Acceptance of unauthorized and noncompliant returns with the Return Policy lead to customer dissatisfaction, financial loss.	Ensure that returned goods are within Return Policy and are matched to a closed customer order.
10	Items with poor quality are recorded as sellable stock without quality checks and could be delivered to customers and thus may lead to customer dissatisfaction,	Ensure that damaged goods are not recorded as sellable stock.
11	Incomplete bookings of returned goods into stock lead to incorrect financial statements. Delays in claims processing lead to customer dissatisfaction, penalty payments.	Ensure that customer claims are timely processed and booked completely and in the correct accounting period.

Scope of Work - Revenue Assurance

Coverage	Sub Processes
Price Control & Order processing	• Review of process of price change circulars • Customer Order Verification Process • Collection recording and work order process • Review of discount structure and its application • Approvals for discount and special benefits, etc. • Production including initial design, hosting and quality process • Invoice generation and approval process • Control over service start & end
Control over Deals	• Deal initiation, approval and tracking • Controls over Deal incentives – provisions and pay outs • Controls over adherence to deal terms and action in case of default (levy of applicable penalty)
Revenue Recognition	· Review of revenue masters for annuity and monthly billing • WIP review process • Accruals and revenue reversals
Collections Management	• Collection recording process • Refund process • Balance confirmation and reconciliation

Key Risks & Controls – Customer Operations & Catalogue Management

Sr. No	Risk	Control
1	Customer Master Database is not updated and does not capture mandatory information for execution of order	Standard procedures are implemented to verify customer mandatory information such as Name, email Id, Contact Number and address.
2	Incorrect customer code creation	Customer code is created by system and is unique to each customer.
3	Customer complaint not resolved within the specified turnaround time can cause customer dissatisfaction and bad reputation	Procedures are in place to ensure the complaints are resolved within TAT. Review of open complaints is carried out weekly.
4	Lack of Escalation mechanism in place or ineffective Escalation mechanism may lead to customer being disinterested in raising concern which will impact company's reputation adversely.	Escalation mechanism is in place to ensure timely and satisfactory closure of the customer's complaints.
5	Delayed order processing leads to missed revenue or penalty payments.	Open order status is regularly reviewed by management to identify incomplete, cancelled, partially filled, and open overdue orders. Issues are followed up and timely resolved.
6	An incorrect picklist leads to incorrect deliveries, customer dissatisfaction and incorrect quantitative figures in the financial statements.	Picklist is automatically created based on the order and cannot be changed by picker.

Key Risks & Controls – Customer Operations & Catalogue Management

Sr. No	Risk	Control
7	Incorrect or ineffective catalogue management can reflect on sales adversely. Delay in updation of product and services catalogue may lead to revenue loss	Review effectiveness of catalogue management practices, is conducted such as filters, search from the keywords, service description etc.. Also the catalogue are updated on a timely basis.
8	Shipment of damaged goods leads to customer dissatisfaction, financial losses and incorrect quantitative figures in the financial statements.	Goods prepared for shipping are checked for damage and physically reconciled with the picklist.
9	Incomplete and/or incorrect deliveries lead to customer dissatisfaction, financial losses and incorrect quantitative figures in the financial statements.	System only allows to scan out items associated to picklists and orders cannot be completed if picklist is not fully scanned out.
10	Incorrect or unauthorized removal of items from the picklist leads to incomplete deliveries, customer dissatisfaction, financial losses and incorrect quantitative figures in the financial statements.	The removal of correct items from a picklist is verified and subject to proper authorization.

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Scope of Work - Customer Operations & Catalogue Management

Coverage	Sub Processes
Customer On- boarding	• Customer Registration • Customer Verification & Activation • Code creation – Approvals & Documentation
Service Category & Catalogue Management	• Mapping of customer and Service Description • Service catalogue update – Timeliness, Approval & Accuracy • Deactivation of Service Description and Catalogue
Customer Management	• Customer management process (Service delivery, Rating, Helpdesk, etc.) • Sending of renewal reminders to the customers due for renewal • Calling process – scheduled and unscheduled calls and follow-up process for renewal • Process of renewing the customer contract • Customer Upsell • Re-hosting process • Deactivation of Customer

Customer Complaint Handling and Resolution	• Adherence to Complaint management process
	    ➢ Tracking of Complaints and its status
	    ➢ Flagging to respective departments for action
	    ➢ Review of TATs for resolving complaints
	    ➢ Escalation mechanism in place
	• Reason analysis and creation of action plan
	• Analysis of Open aged complaint tickets

Notes:

Existence of policies & procedures including authority matrix for critical transaction & its adherence shall be reviewed for each processes.

Key Risk & Controls – Admin & Vendor Management

Sr. No	Risk	Control
1	Unauthorized vendor selection or selection without following vendor selection guidelines	Vendor selection guidelines are followed and vendor selection is finalized as per the approval matrix
2	Unauthorized / incorrect change / creation of vendor master data leads to false Financial Statement	'System settings prevent incomplete or inconsistent entry of vendor master data.
3	Unauthorized purchases are made that are not in agreement with the company strategy and the established budget. Non-sellable inventory lead to a loss of revenues and liquidity risk	Half yearly Business Plans are prepared and approved in line with the authority matrix
4	Buying above market value and / or unfavourable payment terms.	Purchasing Team performs and documents competitive bidding for all contracts according to the Purchasing Guideline
5	No valid agreement in place. Agreed rebates are not monitored and requested.	Contracts are regularly monitored: Applicable discounts and expiring contracts are duly identified and appropriate actions are initiated
6	Unfavorable commitments are made without authorization / unauthorized purchase orders are sent to supplier which may lead to financial disadvantages.	POs are created in the ERP and released after review with the Business Plan

Key Risk & Controls –Admin & Vendor Management

Sr. No	Risk	Control
7	Mismatch between delivery note and delivered items. Mismatch between goods received and goods entered into the system.	'Multiple stages of inventory count on receipt are in place - Gate entry - Warehouse entry - Unpacking and physical counting - Creation of GRN Each stage is performed by different employees
8	Items with poor quality are recorded as sellable stock and could be delivered to customers.	All products need to be booked post quality checks have been performed.
9	Processing fictitious or duplicate invoices may lead to duplicate payments and / or financial disadvantages.	Controls provide reasonable assurance that invoices can only be recorded once if a valid order exists.
10	Inefficient vendor evaluation process impacting the delivery timelines or quality of products	Vendors are evaluated on various parameters on a periodic basis.

Major Spend Review – Admin & Vendor Management

Coverage	Sub Processes
Purchase Requisition	• User requisition – Documentation, Approvals, etc. • Process of tracking of Open requisitions

Vendor Selection & Contracting	• Process of obtaining quotes, Bidding, etc.
	• Price Comparatives – Exceptional approval for selection of high cost vendor
	• Controls over Vendor master– Creation, edits, etc.
	• Controls over Contract and PO
	  ➢ Existence of contract / PO & its validity
	  ➢ Process of validation by legal, exceptional approval for deviation from set terms, etc.
	  ➢ Approval as per authority matrix
	  ➢ Existence of detailed terms,
	  ➢ Tracking of validity & contractual term, etc.
	• Monitoring of Open PO's

Controls over Service Delivery	• Controls over service delivery – user acceptance, proof of delivery, etc. • Controls over Leads – Generation, tracking & distribution • Validation of rates & other contract terms
Invoice Verification & Payment Payouts	· Accounting of Invoices – Accuracy, timelines, etc. · Vendor Payments (including advances) · Accounting of accruals
Vendor Evaluation	• Process and criteria used for periodic evaluation of vendor performance • Share of business allocation – tracking, rationale, etc. • Action on vendor with poor / adverse feedback (including black listing)

Notes:

Existence of policies & procedures including authority matrix for critical transaction & its adherence shall be reviewed for each processes.

Key Risks & Controls – Business Application Effectiveness and Security Review

Sr. No	Risk	Control
1.	Inadequate Business Application Controls leading to business monetary losses	· Periodic review of business applications is conducted to review its effectiveness. · Business Application Controls are determined for each significant application · Business Application walkthrough is effectively carried out to identify the existing application controls and additional application controls required
2	Inadequate delegation of authority mapped in business application	· Application controls are effectively tested to ensure processing integrity · Input / Output controls are checked for significant data / information input and Input Data completeness enhances application controls effectiveness · Critical Application controls are adequately documented
3	Client dissatisfaction and brand reputation Loss of business, revenue, market share	• Application controls asserted to clients are adequately tested by an audit program
4	Existence of manual controls with inherent weaknesses	• Application controls are tested for design and operating effectiveness and adequate documentation of the test of application controls is retained

Business Application Effectiveness and Security Review

Sub Processes	Illustrative Coverage
Logical Access Controls	• User Access Management for key applications & Active Directory • Controls over sensitive access & review of special/ privileged access to key applications • Controls over Password Management
Change Management Controls	• Controls pertaining to managing changes for in-scope systems • Review of special/ privileged access to key applications & segregation of incompatible duties • Third party vendor role in providing support for key applications • Review of patch deployment on servers
Back up & recovery of data	• Compliance to backup policy & defined backup schedule. • Process around restoration of backup. • Backup Retention and Storage (on-site and off-site) • Safety of backup tapes while transfer and retention
Anti Virus Management	• License management system for tracking licenses and users • Update of anti-virus and & for review of logs
Interface Controls	• Controls over interface (Eg. Access appropriateness over interim folder/file generated, etc.) • Review error logs generated during interface processing and their monitoring procedures
Application Security	• Web administration access management • Web server & application security • App security and performance assessment • Website performance

Thank You