

BI – Accounts Receivable - A Dialogue

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(In this article I am continuing the dialogue of the MD of a large company with Mr. Basu who is the head of one of the large Business Units of the company. Mr. Basu tries to outwit his MD this time, but he is in for a very big surprise.)

The audit of the previous financial year (which was a recession year) has been taking place. Generally everything has been going smoothly in the audit. No major problems identified to date. Then the bomb falls. The auditors of the company had recently changed. The new auditor has asked the company to provide a big amount for Account Receivable defaults. The new audit company is very meticulous in their work and very renowned for its professionalism.

Both the MD and Basu have been taken by surprise. MD has asked for an urgent meeting and Basu has rushed to the HO.

MD's Secretary : Good Morning Mr. Basu, MD is waiting for you. (In a hushed voice of warning she adds ...) ... and his mood is not good.

Basu breaks into a cold sweat as he enters into MD's cabin. He has noticed that the temperature in MD's cabin is always inverse of the MD's mood... and today the temperature is really low.

Basu : Good M..morning Sir.

MD : Huh.

Basu : Anything wrong Sir ?

MD : I had a preliminary meeting with the Auditors yesterday evening. They want us to provide for Rs. 10 crores on Accounts Receivables. This can considerably hit our bottom line.

Basu : What is the reason ? Our AR balances are well under control !

MD : Basu that is what I don't understand. I have seen your AR reports for the last one year. It shows a fairly low balance in the old outstanding. And yet the Auditors are asking for a write-off.

Basu : Sir I have brought with me a presentation on the AR balances for the last 6 months. Can we review the same ?

MD : Huh. Ok.

The presentation shows the columns as age buckets of : 0-30 days, 30-60 days, 60-90 days, 90-180 days, 180-365 days, and > 365 days. The last 6 months are shown in rows, and the amounts of each age bucket are shown. Most of the months are showing consistent results.

The amounts which are >365 days are showing just about 2 crores in each of the month. Not bad, thinks the MD, considering that the turnover of the division is almost 1200 crores.

MD : The numbers > 365 days are just about 2 crores, and yet the Auditors are suggesting a Rs. 10 crores write off ? You have any explanation for this Mr. Basu.

Basu : Nothing I can readily think of Sir. But we have a very good team of accountants in our AR department, and they have been there for more than 7 years. The previous auditors have not raised any such comments. How can these new auditors raise such serious comments.

MD : Basu, our new auditors are very tech savvy. They had taken a full list of all open documents in Accounts Receivables from our ERP a few days back. They are working with our BI developers and have made a report on AR balances.

Basu : Oh, I did not know that BI technology can also be used for auditing.

MD : Yes, they have done it very well. In fact they are sharing the reports with us today. They shall be coming in any moment now to discuss that report.

MD's Secretary ushers in the new Auditor, Mr. Waghmare. Both MD and Basu are quite surprised to see the new auditor coming in with a sleek looking laptop, rather than a bulky old file. He also looks too young to be an auditor. The previous auditor was bald, had a big paunch and wore droopy clothes. He really looked like a grouchy auditor. This young man looks smart and more like a model.

MD : Are you alone or is your senior is likely to join ?

Auditor : Good morning Gentlemen. I am alone and I am the senior. Shall we start ?

He connects his laptop to the projector, and after a brief hiccup the screen lights up with a PowerPoint presentation. The subject of the presentation is Accounts Receivable Analysis.

MD : Mr. Waghmare, you have indicated a Rs. 10 crores provision for AR. This is going to hit our bottom line badly. What is the support for such a huge provision.

Auditor : Sir, a couple of day's back we took your AR data from your IT team and then discussed our requirements with your BI developer. Since your BI developers are also Chartered Accountants, they were able to grasp our requirements very quickly. We got the report late night yesterday, and so this morning I had called you regarding the possible provision number.

MD : (Looking at the screen) Your report shows the column of current dues, overdue and unapplied credits. What is that column of unapplied credits ?

Demo Company - Account Receivables				Show USD				
as_on_date	28/09/2007			TERMS_NAME	(All)		Neg_Pos	(All)
potential_due	(All)			curr_code	(All)		due_cat3	(All)
SBU.	(All)			Due_Date	(All)		SO	(All)
BU.	(All)			proj_mgr	(All)		Project_Number	(All)
ProvisionClass	(All)			credit_prd	(All)		PROJECT_NAME	(All)
Region.	(All)			PO_No	(All)		Retention_Reason	(Multiple Iter)
OS Amt				Due-Cat-2-2	Due-Cat-1-2			
				a: CurrentDue	b: PastDue	z:UnApp	Grand Total	
External / Group	Cust_Name	Inv_No						
External				1,207,407,279	1,224,123,344	464,945	2,431,065,678	
Group Receivables				219,278,647	167,874,190	7,820	387,145,017	
Grand Total				1,426,685,926	1,391,997,534	472,765	2,818,210,695	

Figure 1

Auditor : Sir, that column is the root cause of the problem. You see the reports given by the SBU accountant did not contain this column. When we studied his process, we found that there is very little discipline to adjust receipts against outstanding invoices. Many receipts remain unadjusted in the customer's account. As the volume is very large, the accountant applies the receipt on a FIFO basis to the outstanding. In that manner, the entire balance of unapplied credits disappears and the outstanding in the relevant age buckets stand reduced.

Basu : Yes Sir. That's true. The work load is very high, and it is not possible to link all invoices.

MD : Mr. Waghmare, what's wrong with this way of working ? It saves a huge amount of time at the operating level, and yet gives fairly correct view of the outstanding. It has been done consistently by us over the last so many years, and we never had any objections.

Auditor : Sir, in the manual way of working, what you say is entirely true. To generate an aging report of outstanding is very difficult considering the huge volumes. So it is natural that the accountant has applied the receipts to the oldest invoices.

MD's Secretary rolls in a trolley of tea.

MD : Please have some tea Mr. Waghmare.

Auditor : Thanks. (continuing) But there are two fundamental problems in this way of working. One..due to the very large volume of receipts, the SBU accountant has not segregated advances received and the receipt against invoices. Due to this, the advances have also got adjusted against the old dues. Secondly and more importantly, there are several cases of disputes due to which the customers have not paid money . However the when the unadjusted credits are applied, those invoices are shown as settled for reporting purposes.

MD : Oh, now I am getting the picture. Basu, this is very serious. But Mr. Waghmare, how did you find out about the disputed invoices ?

Auditor : I identified your top 5% of customers having the highest AR balances. I found out your customer account manager and discussed with him. Invoices which had payment terms of only 30 days were outstanding for over 90 days. You see, because the accounts team is not linking each receipt to the invoice, practically all the customer account managers are maintaining their own record of receivables in their dairy. Those records are very accurate. I check all the top customers with the diary and found that there were several invoices circled. When I asked the account manager, he said that those invoices were under dispute due to incorrect delivery, performance issues, etc. So I tagged all such invoices in the system with the reason codes and you can see the reason code wise analysis of dues.

I also tagged all advances separately. So now I have the receipts against dues separately from the advances and I also have the disputed invoices separately. As most of the disputed advances are more than 365 days old, I have recommended you to provide for them.

	A	B	C	D	E	F	G	H	I	J	
1	Demo Company - Account Receivables				Show USD						
2											
3	as_on_date	28/09/2007		External / Group	(All)		PO_No	(All)			
4	potential_due	(All)		ProvisionClass	(All)		Neg_Pos	(All)			
5	SBU.	(All)		curr_code	(All)		due_cat3	(All)			
6	BU.	(All)		Due_Date	(All)		SO	(All)			
7	Region.	(All)		proj_mgr	(All)		Project_Number	(All)			
8	Retention_Reason.	(Multiple Items)		credit_prd	(All)		PROJECT_NAME	(All)			
9											
10	OS Amt			Due-Cat-2-2	Due-Cat-1-2						
11				a: CurrentDue	b: PastDue						
12	TERMS_NAME	Cust_Name	Inv_No		b: <= 30	c: 31-60	d: 61-90	e: 91-120	f: 121-150	g: 151-180	h:
13	30 NET	Customer-498		15,933,021	7,565,751	4,586,052	2,121,017	519,929	1,218	18,365	
14		Customer-748		15,717,953	1,155,508	6,027,745	3,660,287			132,003	
15		Customer-1069		4,391,350	3,993,562	4,600,523	4,607,257	1,303,860	1,850,956		
16		Customer-471		13,080,783	1,792,812	613,490	523,563	565,562		969,650	
17		Customer-512		12,851,355	809,378	761,903	532,832	105,681	417,138		
18		Customer-481		1,149,528	1,251,535	1,620,330	1,426,758	1,316,920	2,177,446	5,839,497	
19		Customer-467		8,718,079	1,330,514	31,463	268,416			1,031,723	
20		Customer-1134		1,164,898	822,688	1,683,394	2,493,540	1,439,191	1,633,553	2,005,534	
21		Customer-487		3,732,331	3,934,622	1,591,000	1,174,026		362,351		
22		Customer-503		7,062,125	742,465	1,817,218	365,143	267,589			
23		Customer-462		4,777,384	2,827,111	1,472,506	188,512				
24		Customer-485		5,808,963	1,481,942	156,950			15,980	558,102	
25		Customer-468		3,553,928	1,931,026	1,301,267	180,060	745,099			
26		Customer-508		3,490,878	877,525	1,112,103		128,036			
27		Customer-482		864,589	761,537	643,063	922,751	993,580	717,011	521,130	
28		Customer-486		2,987,244		694,302	949,828				
29		Customer-492		2,862,948	641,782	288,778			818,314		

Figure 2

Basu : (wiping sweat off his forehead) Oh, ok. I have also understood. I think discipline is lacking in the accounting department, which has led to this problem.

Auditor : Mr. Basu, you should first ensure that there is only one version of reporting, and your entire division should act only on that. And this version should be the one coming from your ERP. All corrections should be made in that. Applying receipts on a FIFO basis to old dues is unacceptable. This hides the rotten apples .

MD : Very well said Mr. Waghmare. I appreciate this feedback. Basu, I think you shall have to accept this provision, even though it will hit your bonuses pretty badly.

Basu : B..but sir, the staff is awaiting the bonuses, and this will affect them badly.

MD : I leave that problem for you to handle Mr. Basu.

Observations :

In my practice in BI, I have seen the above scenario is a number of companies. Sheer laziness is the cause of not linking receipts to invoices. Of course this laziness is well supported by extremely innovative reasons, but the overall cause is laziness. This can eventually have disastrous consequences. The modern BI tools have the capability of number crunching huge volumes of data, and so the excuse of 'huge data' is now no longer valid.

Design Principles :

- 1 BI technology should not be used only when the data is 'perfect'. It should be used even to 'perfect' the data. It is a very rare scenario that all your data will be perfect. But the ability provided by BI technologies to see the overview of the data and then drill down to the problem areas enables the users to quickly identify such problem areas and make quick corrections, rather than attempting corrections all over the ERP system. This way quick business results can be obtained.
- 2 Always provide a mechanism by which certain additional attributes can be added to the base data without in anyway changing the integrity of the base data. In the above example the Auditor has tagged the reason for non-collections and brought this as a dimension in the report. At the current state, this dimension may or may not be available in the ERP. But the ability to add such a dimension considerably improved the usability of the report. Eventually the ERP must be customized to add such attributes since the ERP is the best place for such data storage. But since ERP customization can take considerable time, always provide for such a quick workbench. I know I am going to antagonize the ERP and BI purists, but then we are talking practical stuff.
- 3 BI report can be used not only for decision making by also for auditing. In fact getting an auditor to review and comment on BI reports is very important. They are very well trained in understanding numbers and the facts behind those numbers. Getting their opinion and making the required changes is, in my opinion, a very important step in the BI lifecycle.

When you design BI reports don't work on the basis of the current limitations. Think about an ideal state, and then work towards that ideal state. The BI technologies will help you rapidly achieve the ideal state. Don't think of BI as just another 'reporting' tool, but think about it as an enabler of business benefits and actionable information.

About the Author:



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