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Headline: Need to formalise processes to fight fraud

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Companies venturing abroad will have to step up procedures to assess risks in foreign markets, reports MELVIN YONG

COMPANIES expanding into regional markets will need to develop formal processes to identify and assess potential fraud risks in their target markets, say industry watchers.

These include having to carry out due diligence to better understand the foreign business partners and parties that will conduct business on their behalf.

"As long as people have material needs and wants, there will be fraud. The challenge for companies is mitigating the risks fraud presents to an acceptable level but they can never banish it altogether," said Owen Hawkes, partner at KPMG in Singapore.

"What is needed is a concerted effort to understand the risks a given organisation faces, to put in place a holistic suite of measures to mitigate those risks, and education and training to ensure that the board, management and staff are all actively guarding the organisation against fraud," he added.

The recently released Singapore Fraud Survey 2014 by KPMG and Singapore Management University (SMU) found that the quantum of losses suffered by companies due to fraud has jumped more than three-fold to about $22 million now compared with just three years ago. The average cost of employee fraud is $457,000.

The survey also found that internal parties are involved in 75 per cent of the reported fraud, which is harder to detect and therefore very significant.

"Internal fraud is committed by what we call 'knowledgeable insider' who know the internal controls procedures and how to circumvent them," said Associate Professor Themin Suwardy of the Singapore Management University. "The range of things they can commit is also much wider than the external fraudster," added Prof Suwardy, who is also Singapore divisional president at CPA Australia.

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– Owen Hawkes, partner at KPMG in Singapore

Specific to companies venturing abroad, two thirds of respondents felt that the risk of bribery and corruption was a key concern for Singapore companies conducting business in the region. Half of them were concerned about the need to provide payments or gifts in order to win or retain business compared with just 20 per cent in 2011 when a similar survey was conducted.

More than a third of respondents were also concerned about foreign government officials and overseas-based third parties, with more than four in 10 saying they were very concerned about interacting with foreign governments, while 36 per cent were very concerned about using third parties.

Experts say companies will need to better manage this by assessing the risks inherent in the environment in which they are intending to operate by conducting due diligence and understanding the practices in the relevant country. "Otherwise, they risk being blind-sided by practices they may never have known existed," said Mr Hawkes. Companies should also ensure that their employees, management, and even business partners understand the expectations of the organisation, he added.

The KPMG-SMU Fraud Survey also found that various approaches are being used by organisations to mitigate risks in cross-border activities. Three quarters said employees were issued guidelines for mitigating cross-border risks, two thirds have compliance programmes, while six in 10 had conducted training for their staff.

Although these are good starting points, much more will have to be done to check on fraud when operating in foreign markets. "With cross border activities, especially for the first time, the risks will be higher because you are dealing with more uncertainty. You have new people – staff, suppliers, customers and other parties – new regulations, perhaps different business practices and so forth, so it takes a while to set the culture and tone right," said Prof Suwardy.

Boards, management and employees have a vital role in combating fraud. "The board has to ensure that a framework is in place to prevent, detect and respond to fraud and exercise oversight to ensure that it is being operated effectively," said Mr Hawkes of KPMG. "Management must dedicate sufficient time and resources to addressing fraud risks and engage with fraud issues at a sufficiently granular level when they arise."

Employees have a huge advantage in assisting their company in preventing and detecting fraud.

"Because they are on the ground, they can see how business activities are undertaken, what risks arise, and how controls are operated in reality. Employees can feed back information on threats, control failures, and unusual or anomalous activities providing they are trained and empowered to do so," added Mr Hawkes.

Observers say fraud often occurs because of the lack of effective working controls.

"It is not enough to have control procedures in place but it is important to make sure they cover your risk areas and are carried out effectively," said Prof Suwardy. "All company directors and managers need to have a healthy dose of professional scepticism. Of course, you need to trust your employees but please verify."

When doing business abroad, companies need to undertake risk assessment procedures to understand and prepare for potential risks. They should carry out due diligence to understand who they are working with and who will be conducting business on their behalf.

One approach is to develop formal processes for identifying and assessing potential risks in new territories that a company intends to enter. These assessments typically include reviewing relevant business factors such as:

- the risks inherent to the new jurisdictions;
- the nature of contractual relationships;
- government relationships;
- cultural norms and differences in those jurisdictions, as well as any relevant laws and regulations; and
- reliance on agents.

These processes should be refreshed periodically or during major changes to business operations. In addition, in-country personnel should be educated on such risks and on how to manage them.

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