Innocents abroad

With opportunity comes risk, as multi-national companies that have entered new jurisdictions have often discovered. *ALB* reports

Every western company wants a bit of the Asian apple – and in particular the Chinese cherry at the moment. The rush to get a toehold in Asia means that multinational companies (MNCs) are pouring into new jurisdictions at a fast pace.

It's exactly these companies that are at the most risk of corporate fraud in Asia according to experts. On the one hand, their thirst to operate in a jurisdiction puts them in a position of need, but their disregard for following the rules that prevent fraud doesn't help them either.

"The risks are high for a number of reasons," says Steve Vickers, president and chief executive officer of International Risk. "They're working in non-transparent jurisdictions where it's difficult to get information because of poorly developed legal systems, and these jurisdictions are often undergoing confusing and rapid change."

Cookie-cutter approach

Where MNCs fall down on fraud is a lack of understanding of the culture that they are working in. While a company may come with a high tech anti-fraud package that works well in the US or Europe, local working practices can render them ineffective.

This lack of understanding can start right at the beginning of a project when a MNC chooses a joint venture party in a new country. "There is a reliance on middlemen to make introductions," says Vickers. "The company neglects to do real due diligence."

This error is normally compounded by a series of actions or procedures that result in the company losing control, as well as demonstrating that a cookie-cutter approach to doing business in new countries should be avoided at all costs.

This approach is evident when companies export risk management tools from one context into another. These tools are often technology-based and ignore the human element, ie how people in one culture work together in a very different way from those at headquarters.

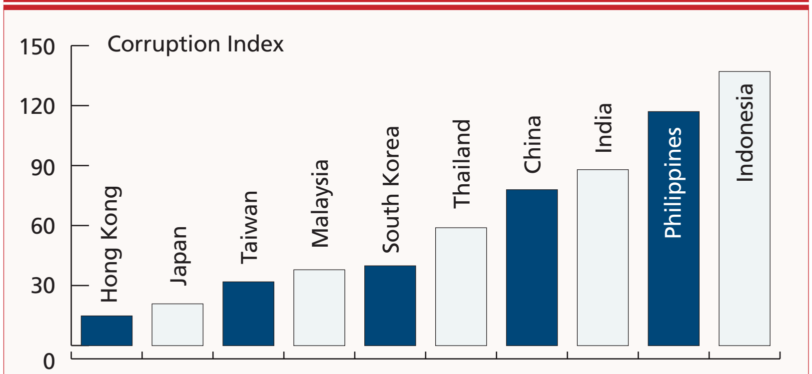
There is also often a lack of serious due diligence and investigation when a MNC hires a team. They ignore the personal element which means that the team have a tribal loyalty to each other, not to their new employer.

The world's least corrupt nations

1	Iceland
2	Finland
	New Zealand
4	Denmark
5	Singapore

Source: Transparency International Corruption Perception Index

Asian countries on the corruption scale



Source: Transparency International Corruption Perception Index

The world's most corrupt nations

151	Angola
152	Cote d'Ivoire,
	Equatorial Guinea
	Nigeria
155	Haiti, Myanmar,
	Turkmenistan
158	Bangladesh, Chad

Source: Transparency International Corruption Perception Index

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Vickers also wants MNCs to grasp that they can't expect the internal auditors to adequately police companies. "For example," he says, "in Japan you have a culture where internal audit will not question senior management."

Finally, in nearly all cases of fraud, when the company makes an investigation it nearly always discovers that there was a prior, less serious fraud that was brushed under the carpet. While it might seem strange that companies would ignore internal fraud, broadcasting it can hurt a company's reputation or, even worse, land it in front of the regulator. What this does, according to Vickers, is to "create a culture where people think that the worst thing that is going to happen to them if they are caught is that they will get fired".

Types of fraud

The main type of risk that companies face is collusion: where someone inside the company works with an external contact (maybe a supplier or vendor) to defraud the MNC. A typical example here is supply chain fraud at either the purchasing or distribution end of the operation.

At its worst, companies can discover that their distribution channel is being used to distribute counterfeit products or, in the case of NEC in Japan, they can lose control of their brand.

In the NEC case, when the company began investigating reports of pirated products bearing their brand appearing in Hong Kong and Beijing, it discovered that counterfeiters had set up a parallel company with fake NEC signs, cards and packaging.

A company can also find itself blackmailed by an entrepreneurial distributor who has the right to sell a fast-moving, high demand product. The distributor, however, is demanding kickbacks from buyers. When the company finds out, the distributor turns round and says 'if you don't like it I'm moving to your competitor across the road and I'm taking the distribution network with me'.

Five years of advertising and brand building can disappear in less than a day.

Finding the fraudsters

While companies rely on auditors – external and internal – to point out any dodgy dealings, the reality is most companies find out there is a problem through an anonymous letter from a disgruntled supplier/vendor or member of staff.

However, while waiting for that letter to drop through the letter box, there are some common signs that companies should look out for. For example, the alteration of accounts for supposed reasons of convenience, key finance staff unwilling to take holidays, customer complaints about the accuracy of IT and database systems or when the IT manager role has a fast turnover.

There are no obvious fraudsters however. Most frauds are perpetrated by nondescript and often well-regarded employees and colleagues. However, one thing that is worth looking out for is a lifestyle that is at odds with an employee's earnings.

It's hard to watch over an entire business like a hawk, so businesses should focus on the areas that are most vulnerable. In general these will be the high volume parts of the business, where a multitude of transactions can hide a fraud, or high value, where the rewards for a minor fraud could be great.

When the company is alert to the fraud they should set up a procedure for investigation. Ideally, this procedure should be in place prior to any fraud coming to light.

While springing into action after the event brings some chance of recovery, there's no doubt that in the case of corporate fraud, prevention is better than cure. **ALB**

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