

# The enemy within

Executives are not taking fraud and corruption seriously enough, leaving their companies vulnerable to serious financial losses. In an extract from their book, *Fraud and Corruption: Prevention and Detection*, **Nigel Iyer** and **Martin Samociuk** explain how to tackle unmanaged commercial risk.

**M**any executives would argue that they take fraud and corruption very seriously, having spent the last 20 years implementing extensive corporate governance and control frameworks.

However, in spite of tougher legislation and vociferous corporate rhetoric in recent years, not that much has changed in the world of fraud and corruption. Reports of major fraud scams and bribery scandals are just as prevalent now as they were 20 years ago.

## Overkill in bureaucracy and legislation

Although there have been improvements in reporting requirements and awareness has increased, there is a lot still to be done to prevent the recurrence of fraud and corruption. In particular, too many executives still rely on the belief that people are basically honest.

Sadly, however, the recent spate of corporate collapses and the fact that investigators around the world continue to prosper show that there are plenty of dishonest people around.



**Martin Samociuk**

Martin Samociuk worked in a copper smelting business in Africa before joining UK-based firm Network Security Management in 1981, which has grown to become one of Europe's leading fraud investigation and prevention companies. He became managing director and then chairman and CEO before deciding, in 1999, that managing investigators was becoming too stressful, as he was constantly trying to recover money from increasingly sophisticated fraudsters. In 2000, he founded Hibis Consulting in Australia.



So much time and effort has gone into creating corporate responsibility agendas, defining corporate governance and internal controls frameworks, and implementing risk management strategies that little time has been left to get to grips with the actual risks of fraud and corruption; that is, the way criminals think and the methods they use.

Fraud and corruption differ from many other risks in that they are perpetrated by intelligent people who are secretly looking for loopholes. That is why it comes as such a shock to management and employees when a fraudster is uncovered; honest staff find it very difficult to believe that dishonest people have been working alongside them.

There has been considerable effort made around the world to improve laws and definitions to ensure that legal processes are capable of adequately punishing fraudsters, corrupt employees and corporate psychopaths. However, organisations have not been making the same effort to detect criminal activity and prevent it from succeeding in the first place.

### The true cost

There is a wealth of research demonstrating the extent and effects of corporate fraud and corruption. However, this is of little value if board executives and senior managers are reluctant to take fraud and corruption seriously.

Many senior executives believe that their organisation is unlikely to be a victim of fraud and corruption, or that since they have not experienced any problems in the past, they must be safe. Once executives have experienced the effects of a major fraud or corruption scandal there is very little need to convince them to invest in preventing a reoccurrence.

They also realise that their past inaction has led to significant losses. Because these losses eventually come off the bottom line, every dollar lost reduces net income by the same amount. If an organisation's profit margin is 10%, recovering the loss means ten times that revenue has to be generated. To recover \$10 million, \$100 million must be made.

In most cases, hidden indirect costs, such as constraints on expansion and development, damage to reputation and employee morale, greatly outweigh the direct costs.

## COULD THIS BE YOUR ORGANISATION?

An email arrives at head office alleging that certain directors have been buying personal items on the company's account and that some of the marketing expenses are not genuine. Furthermore, people who speak up are being ignored.

It is not the first email of this kind, and rumours have been circulating for a while. However, financial results in the region are strong and local management resents interference. The tone of the emails is becoming increasingly angry and some of the claims about fraud and corruption are hard to believe.

You are one of seven recipients of this email. You are not directly responsible for the division concerned and it is easier to close your eyes to unsubstantiated claims by assuming that they cannot be true. However, if enough resources were dedicated to uncovering the truth, you would find that many of the allegations are true, and in fact just the tip of the iceberg.

In reality, profits are declining, losses are being systematically hidden in the books, some managers have covert ownership in business partners via offshore companies, property frauds are taking place and bribes are being paid out.



Nigel Iyer

Nigel Iyer is a director and founder member of Hibis Scandinavia and a director of Hibis Europe Ltd. Since graduating from university and qualifying as a chartered accountant, he has focused on the prevention and investigation of fraud and corruption, initially working for large corporations and then for UK-based Network Security Management. In 1999, he co-founded the Hibis Group ([www.hibis.com](http://www.hibis.com)), which specialising in the prevention of fraud and corruption.

In addition, the costs of investigation are not to be taken lightly. If a case is complicated and involves the international movement of funds, the investigation costs can be very complex. It is not unusual to spend \$1 million investigating a \$10 million fraud. If it involves international money movement and offshore tax havens, this can cost from 30% to 100% of the amount lost.

Probably the single largest and most overlooked expense is the cost of all the ongoing cases that have not yet been discovered.

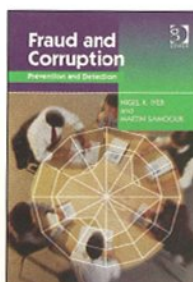
### Make money by not losing it

Once the need to stop losing huge sums of money is recognised at board level, there are effective measures that can be put in place to prevent fraud and corruption.

Even for multinational organisations, the solution has to come from within because there is little help from governments or regulators. Tackling fraud and corruption on an international level is always difficult. There is not even an internationally agreed definition of fraud and corruption.

Rather than waiting for precise international definitions to materialise, organisations should start tackling the problems by gaining a better understanding of the fraud and corruption risks that they face and developing a much greater level of resistance to them.

As a senior manager or executive director, it makes sense to pay more attention to the behaviour of fraudsters, corrupt employees or corporate psychopaths, rather than being blinded by accounting, legal or procedural issues. ■



*Fraud and Corruption: Prevention and Detection* is available from Gower Publishing.

Website: [www.gowerpub.com](http://www.gowerpub.com)