

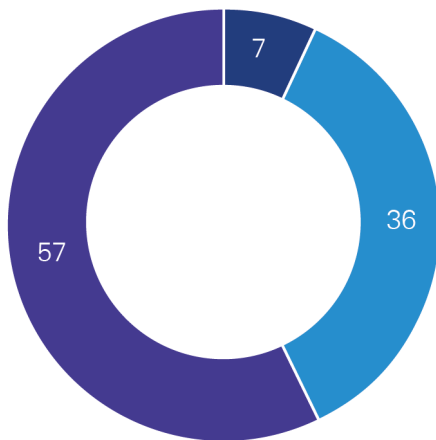
Financial misstatement

Generally accepted accounting principles (GAAP)^v, as well as the US FCPA^{vi}, require companies to make and maintain accurate books and records.

In our experience, the most common financial misstatement risks in the Life Sciences industry are accelerating revenue to meet business targets or delaying revenue if targets have already been met for a specific reporting period.

While more than a third (42%) of industry leaders stated that financial misstatement is likely, our survey finds that the majority of respondents (71%) average fewer than five internal investigations a year.

How likely is the risk of financial misstatement within your company?

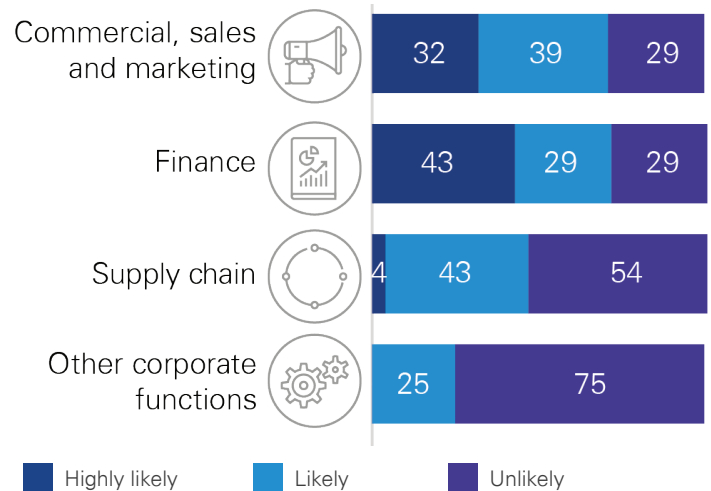


Highly likely Likely Unlikely

Source: KPMG Middle East Life Sciences 2020 Industry compliance survey

When looking at various aspects of the business functions, those most likely to be exposed to the risk of financial misstatement of books and records are finance and commercial, sales and marketing.

For each department, how likely is there to be exposure to risk of financial misstatements?



Source: KPMG Middle East Life Sciences 2020 Industry compliance survey

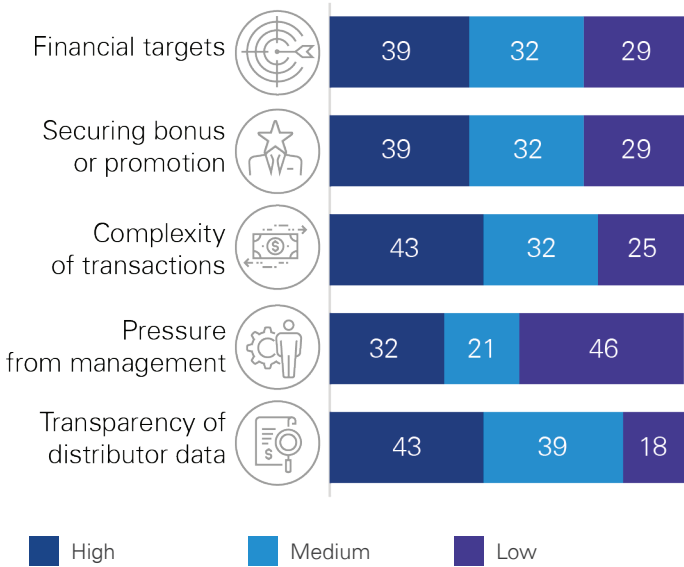


Factors leading to financial statement fraud

In the Middle East, the Life Sciences industry is heavily reliant on public health care spending.^{vii} With recent government budget cuts and the move towards generic and locally manufactured medication, regional business leaders are experiencing significant pressure to meet targets.

As per 43% of respondents, complexity of transactions and reduced transparency due to reliance on distributor data are the factors with a high likelihood of contributing to financial misstatements. These were followed by financial targets and securing performance bonuses and promotions (39%).

Rate the below factors for risk of financial misstatement:



Source: KPMG Middle East Life Sciences 2020 Industry compliance survey

Common schemes of financial statement fraud for Life Sciences

Based on our experience, channel stuffing is the most common accelerated revenue risk for Life Sciences companies globally. Our survey finds this is also the case in the Middle East, with 54% rating it 'high risk'. Middle East regulations do not allow a direct market authorization for Life Sciences companies and mandates the use of local distributors.

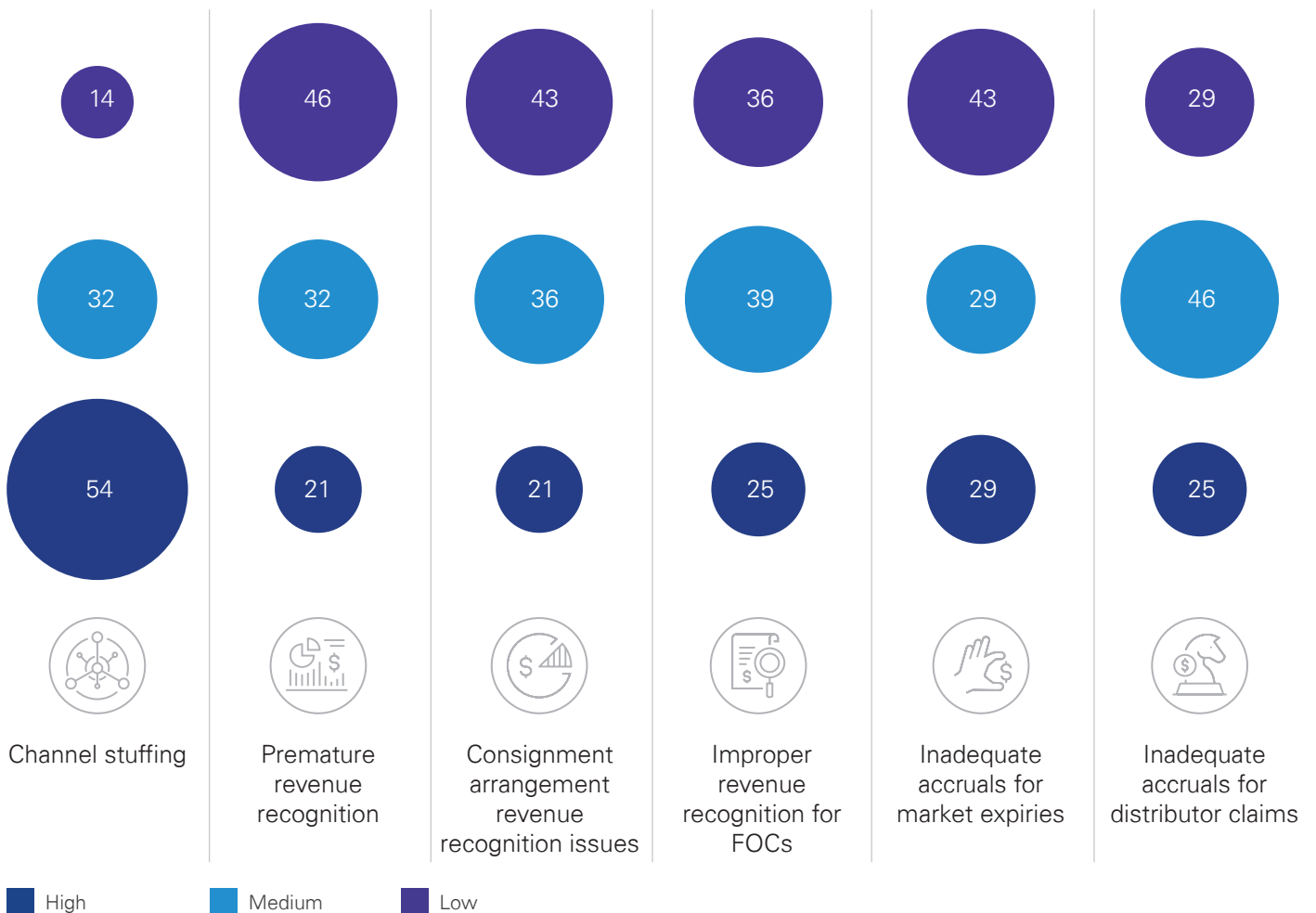
The recent trend of subsequent alteration of tender quantities by the government has further heightened the risk of excess quantities with distributors.

Product expiry is another area of concern. Life Sciences companies are frequently unable to make accurate accruals on the books for product expiries due to delayed

and disputed claims from distributors. Sales teams work closely with distributors and customers in the field and are usually aware of product expiries in the market. However, this information is not always passed on to finance and regional management teams in time to make accruals for expiries and take corrective actions.

Further, certain stakeholders stated that whilst distribution agreements have clear clauses for expiry claims, informal agreements between commercial teams and distributors exist. These may further increase the risk of companies recording and paying for such claims—often in the subsequent reporting period without the required accruals.

Rate the likelihood of encountering the financial misstatement risks below:



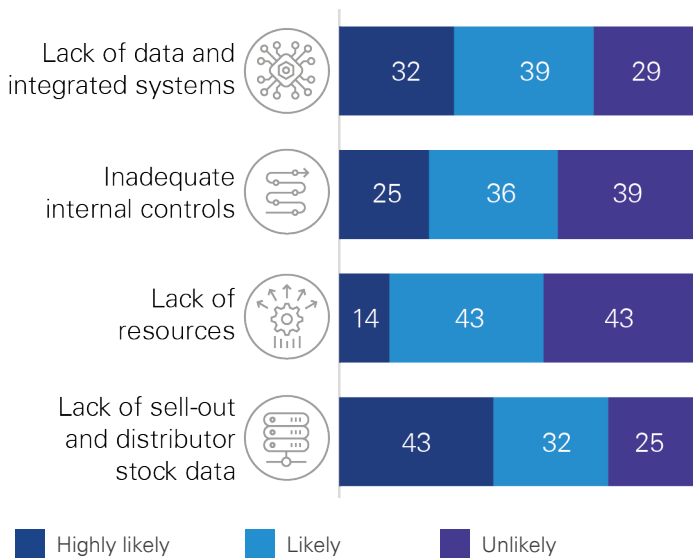
Source: KPMG Middle East Life Sciences 2020 Industry compliance survey



Challenges in identifying financial misstatement risks in the Middle East

Our survey identifies the lack of integrated systems and distributor data as two main challenges when seeking to identify financial misstatement risks. Life Sciences companies are dependent on distributors for timely and accurate reporting of financial data and supporting documentation for sales, marketing and promotional activities. This is coupled with the challenge of integrating non-standardized distributor reported financial data in their systems for monitoring.

Rate the likelihood of encountering the following when identifying financial misstatement risks:



Source: KPMG Middle East Life Sciences 2020 Industry compliance survey

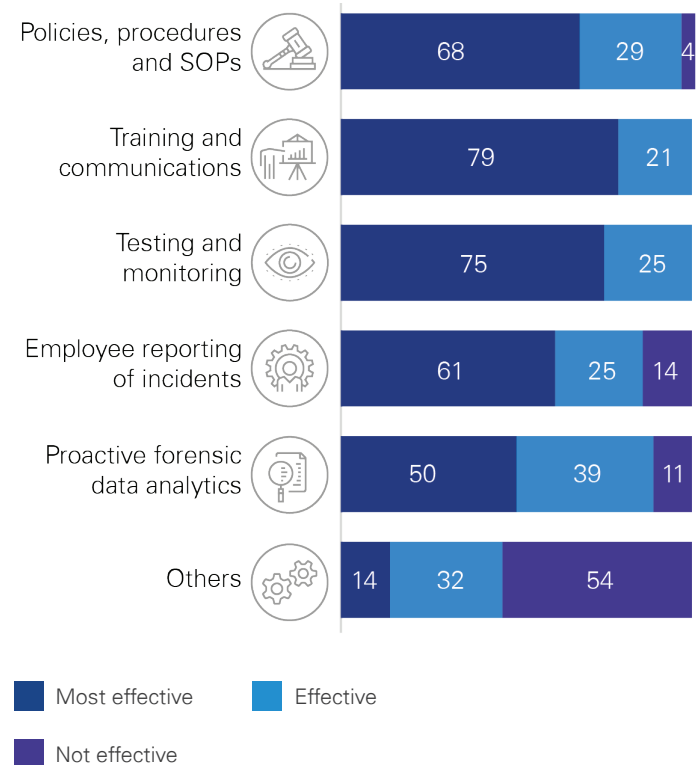
How to mitigate financial statement risks

From our experience, Life Sciences companies have global accounting policies and procedures to mitigate financial statement risks such as channel stuffing, accelerated revenue recognition and delaying accruals for distributor claims. Our survey finds that regional SOPs and guidance, trainings and transaction monitoring are most effective to mitigate financial misstatement risks.

Regional business leaders have been focusing on early detection measures to mitigate financial statement fraud. Proactive data analytics is one such approach, recently implemented in the Middle East. Companies are also

increasingly demanding that distributors upscale their systems and provide direct, automated reporting on a daily basis to monitor and review distributor sell-out and stock positions.

Rate the below elements effectiveness for mitigating financial misstatement risks:



Source: KPMG Middle East Life Sciences 2020 Industry compliance survey



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