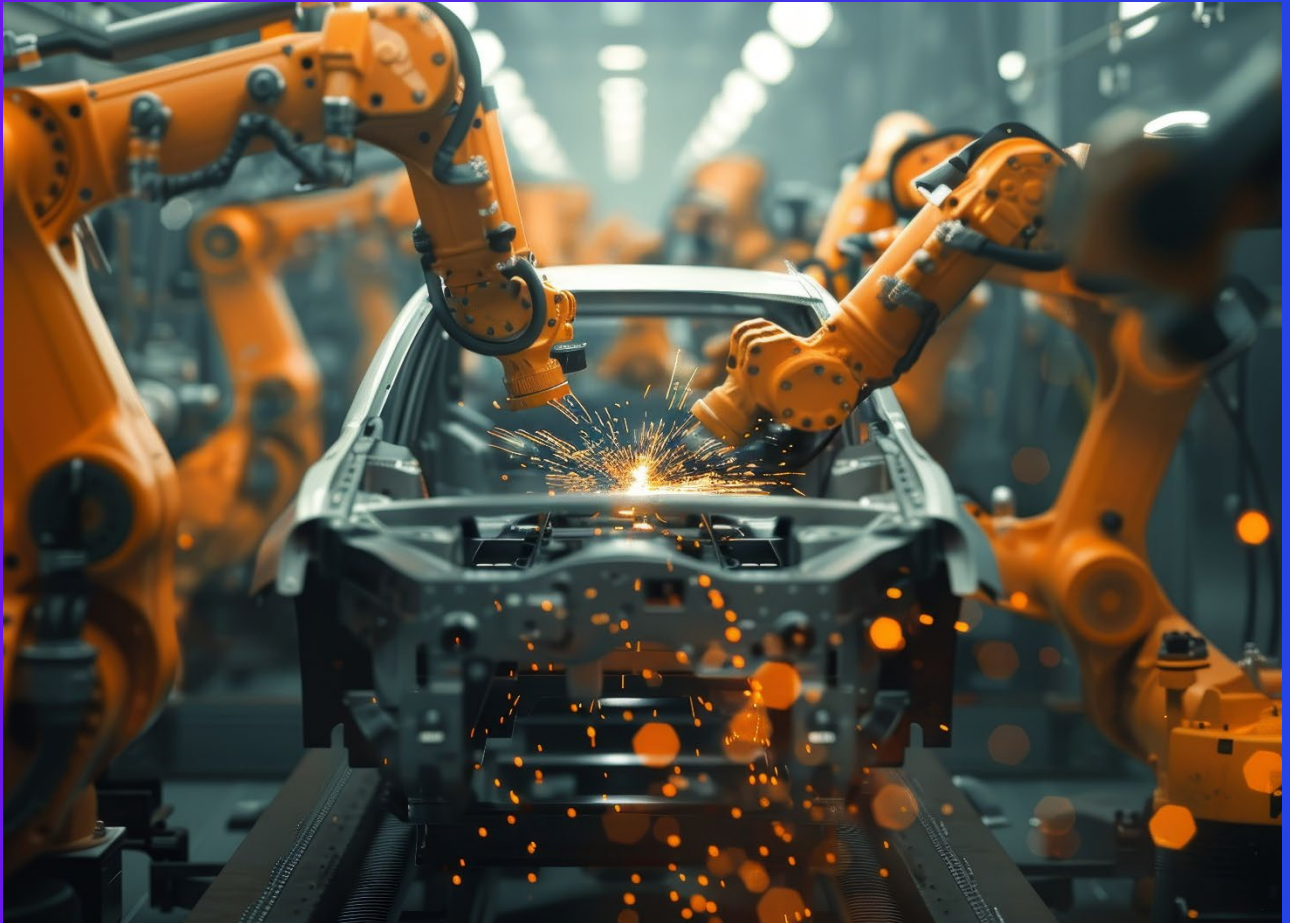




Evolving fraud trends in the Automotive and Industrial Manufacturing sector in India



October 2024

kpmg.com/in

KPMG. Make the Difference.

1 Introduction

India's manufacturing sector, including Automotive and Industrial manufacturing (Auto and IM), has undergone significant transformation driven by technological advancements and changing consumer preferences. The Indian manufacturing sector generates around 17 percent of the country's GDP and is projected to be one of the fastest-growing sectors. India has the capacity to export goods worth USD1 trillion by 2030 and is on the road to becoming a major global manufacturing hub.¹

The Indian manufacturing sector has grown to the extent of 12.1 per cent during the last fiscal year.² Wherein the automotive sector sales have grown to the extent of 12.5 per cent in the last fiscal year.³ However, this growth and transformation have also evolved ways in which frauds are perpetrated by fraudsters. This document provides a broad view of these trends and suggests actionable measures to mitigate fraud risks.

2 Critical insights from KPMG in India's survey

KPMG in India conducted a comprehensive survey involving subject experts and received insights from various organisations within Auto IM. The survey results include 70 per cent representation from internal audits, 10 per cent from compliance, 10 per cent from the ethics committee and general counsel, and 10 per cent from finance and other functional leaders.

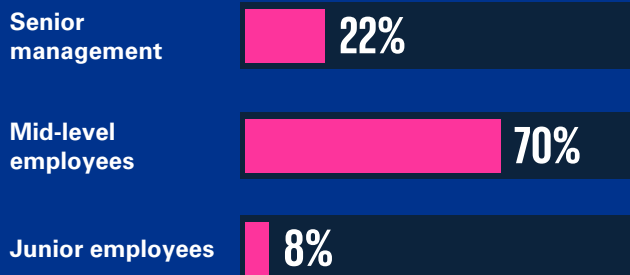
The survey covered key questions pertaining to fraud and leakages faced by these organisations, and the results of the survey are as follows:

1 Survey findings

The survey highlighted key areas prone to fraudulent activities, and the same is given here under:



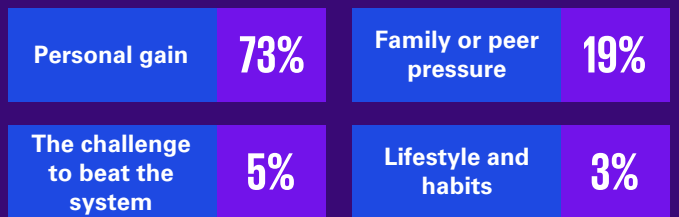
The seniority level of fraudsters



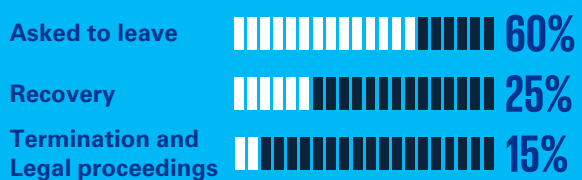
Types of fraud



The overriding motivation of fraudsters



Measures taken by management



1. Manufacturing Industries in India and its Growth, IBEF, July 2024
2. Ministry of Statistics & Programme Implementation, Press Release: Press Information Bureau (pib.gov.in), 31 May 2024.
3. Domestic Sales Trends, Society of Indian Automobile Manufacturers (siam.in)

2 Key areas of fraud

KPMG in India's forensic team has collaborated extensively with clients in various sectors, identifying innovative frauds, key fraud risks and emerging trends.

1. Procurement

- **Employee-vendor collusion:** This is common across all survey results. It involves employees and vendors conspiring to inflate invoices, create fictitious vendor accounts, and authorise unnecessary procurement. Such collusion often includes bribery in cash or kind (gold or silver coins, etc.)
- **Deep-rooted corruption:** Particularly prevalent in organisations with significant procurement spending, corruption extends across various designations, affecting procurement processes and organisational integrity.
- **Influence of suppliers:** External influence from suppliers is a driving force in most procurement frauds. Suppliers with a Significant Share of Business ('SoB') often take a proactive approach to lure employees into continued business and preferential treatment, avoid red flags during reviews, and seek business-sensitive information to win bids/contracts, etc.

2. Sales

- **Manipulation of sales data:** Includes falsifying sales data to meet targets, resulting in financial misstatements and undue bonuses.
- **Scrap sales:** Inadequate controls regarding scrap generation and warehousing, scrap sales to vendors without proper authorisation, and selling of good inventory as scrap in lieu of kickbacks from scrap dealers.
- **Sales return:** No process/timelines defined for addressing sales return, weak controls regarding credit limit checks of customers, leading to sales return, periodic sales returns to manipulate sales reporting data.

3. Dealership and marketing

- **Dealership fraud:** Unauthorised discounts, misappropriation of dealership funds, leakage of business sensitive information to favour dealers, and kickbacks from channel partners are common fraudulent activities.
- **Misuse of power and authority:** Employees misuse their position to allocate a higher share of goods to preferred dealers, weakening other competing dealers by squeezing their business and facilitating hostile takeovers by the preferred dealer group over other dealers.
- **Marketing:** Excess spend on limited areas, campaign not covering the target audience, kickbacks, and other integrity issues due to collusion of marketing team and third-party vendors.

4. Other operational areas

- **Production related:** Quality rejections and inadequate quality checks to seek kickbacks from vendors, weak controls over scrap generation and disposal mechanism, lack of controls on physical stock, leading to manipulation in inventory, etc.
- **Human resources:** Ghost employees deployed through third-party vendor payrolls, illegitimate reimbursements, etc.
- **Administration:** Conflict of interest with various third-party vendors associated across multiple departments and geographical locations; weak internal controls regarding approval documentation for expenses incurred; incorrect budgeting leading to cost overrun for the organisation.



3 Trends in fraud detection

Whistleblowing:

About 80 per cent of fraud detections occur through whistleblowing hotlines and direct complaints to senior management, emphasising the importance of maintaining an effective whistleblower mechanism and effective channels of communication between employees and senior management.

Proactive fraud risk assessments:

Regular fraud risk assessments have proven effective in identifying red flags, especially in procurement processes.

Early warning mechanism:

The use of automated solutions is crucial for the early detection of potential frauds, analysing large volumes of data to identify patterns indicative of fraudulent behaviour.

4 Challenges in fraud detection

- Corrupt employees, preferred vendors, and dealers engaging in fraudulent and corrupt practices are increasingly using messaging applications for communication, making it difficult to track fraudulent activities through traditional e-mail, process, and document reviews. The prevalence of accepting bribes and/or kickbacks in cash to avoid a money trail has also seen an uptick.
- Involvement of related entities: The active involvement of related entities, including family members, through using their bank accounts, floating shell companies, registering companies in their name for transaction purposes, and procuring assets in their name has also been noted.
- Fraudsters are increasingly accepting bribes and/or kickbacks in cash or kind, gifts, entertainment, leisure, or personal travel to avoid a money trail.
- Fraudsters have heightened awareness of fraud detection techniques, including review of electronic data and interview techniques; hence, they use highly improvised techniques for committing fraud. Their responses during post-detection interactions and/or interviews with the management are also well thought out.
- Circumstantial evidence: With the shift in fraud communication methods, reliance on circumstantial evidence to substantiate fraud claims has increased.



5 Recommendations

To effectively prevent and facilitate early detection of fraud in the automotive and industrial manufacturing sectors, we recommend the following:

Effective whistleblower mechanism

- Ensure constant communication about the whistleblower hotline and the company's code of conduct.
- Encourage employees to report suspicious activities without fear of retaliation, fostering a culture of transparency.

Robust fraud-risk assessment framework and periodic fraud risk assessments

- Develop and maintain a comprehensive fraud risk management framework tailored to the sector.
- Conduct regular fraud risk assessments focusing on high-risk areas, such as procurement and sales.

Use of forensic technology tools

- Develop benchmarks for effective use of data analytics in fraud detection.
- Adapt customised offerings such as KPMG Fraud Intelligence Platform, Sales and Distribution Leakage Detector, KPMG Forensic Casebook tool, and KPMG Anti-Corruption Compliance Tool. These can integrate well with various Enterprise Resource Planning ('ERP') systems.

Continuous training and awareness

- Conduct regular training sessions for employees to recognise and report fraud.
- Promote a culture of integrity and ethical behaviour throughout the organisation.

6 Conclusion

The evolving nature of fraud in the automotive and industrial manufacturing sector requires a proactive and comprehensive approach to mitigate fraud and leakages. Leveraging forensic technology, maintaining robust

fraud frameworks, and fostering a culture of transparency and accountability will not only help reduce losses due to fraud and leakages but will also protect the organisation's reputation.



KPMG in India contacts:

Akhilesh Tuteja

Head – Clients & Markets

E: atuteja@kpmg.com

Rajosik Banerjee

Deputy Head,

Risk Advisory and Head,
Financial Risk Management

E: rajosik@kpmg.com

Manoj Kumar Vijai

Partner and Head - Risk

Advisory

Office Managing Partner

E: mkumar@kpmg.com

Suveer Khanna

Partner and Head –

Forensic Services

E: skhanna@kpmg.com

Sidhartha Gautam

Partner and Lead - Auto &

Industrial Manufacturing

Sector, Risk Advisory

E: sidhartha@kpmg.com

kpmg.com/in



Access our latest insights
on KPMG Insights Edge

Follow us on:

kpmg.com/in/socialmedia



The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

KPMG Assurance and Consulting Services LLP, Lodha Excelus, Apollo Mills Compound, NM Joshi Marg, Mahalaxmi, Mumbai - 400 011 Phone: +91 22 3989 6000, Fax: +91 22 3983 6000.

© 2024 KPMG Assurance and Consulting Services LLP, an Indian Limited Liability Partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organization.

This document is for e-communication only. (018_FFLY0924_AB)