Katzscan Quarterly

Supply Chain, Governance, Fraud, Turnaround Help

2nd Quarter - 2009

I know that tax season is upon us and filing deadlines are near, so take a little break with this issue.

Thank you for allowing me to communicate with you. I hope you find the content informative.

Happy reading - enjoy - and your comments and suggestions are appreciated.

Sincerely,

Norman

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SUPPLY CHAIN CORNER

Affordable & Achievable Supply Chain Technologies

There are core technologies that supply chains rely on, not just for efficiency, but for basic performance: an Enterprise Resource Planning (ERP) system, automatic identification, and Electronic Data Interchange (EDI). These technologies are plentiful in solution options and have become very affordable to implement, with the return on investment sometimes measured in just a few months.

The ERP system is the core repository of a company's data, containing customers, finished goods, raw materials, suppliers, inventory (count, value, and location), purchase orders, work orders, sales orders, accounting functions, and manufacturing bills (labor, operations, and materials). The process flows are greatly defined by how the ERP system works, i.e. what has to be done prior to something else happening. There are thousands of ERP systems out there, and they range from small (QuickBooks Pro®) to the very large (Oracle® and SAP®).

With the core technology -- the ERP system -- in place, we now look to extend the reach and capabilities by adding on automatic identification and EDI.

Bar coding is a tried-and-true automatic identification ("auto-id") methodology that has proven itself for reliability and efficiency over and over again. Another type of auto-id methodology in the news a lot the past few years is radio frequency identification (RFID). Barcode scanning for inventory, receiving, picking, packing, manufacturing, fixed assets, and other uses is a relatively simple way of extending your ERP system and automating manual processes which increases accuracy and throughput.

EDI is a means of performing business transactions via standardized file formats through secured networks as opposed to the use of paper documents. Business transactions include purchase orders, invoices, bills of lading, payment remittances, and credit & debit adjustments. As opposed to the inefficiency of printing documents and mailing or faxing them, wondering if they were truly received by the recipient party, transactions sent through EDI are always acknowledged; thus a transaction unacknowledged for one business day would be a cause for concern. Imagine the efficiencies in going paperless and being able to manage by exception instead of the need to follow up with all faxed, mailed, and e-mailed business transaction documents, especially to e-mail systems that do not provide read-receipt notification.

With core technologies in place and a company reaping the benefits of greater efficiency and throughput, key performance indicators can be used to spot internal bottlenecks and problem areas.

Next newsletter: Applying External Metrics To Internal Performance

FOCUS ON FRAUD

How Internal Pressures Cause Fraud

Aside from external causes and societal demands, fraud can also be caused due to internal pressures of an organization. The failure of executive management to properly staff for key positions, train employees, enable employees to ask for (and receive!) help when they really do need it, and the creation unattainable benchmarks all contribute to pressures that can force an otherwise honest employee to commit fraud. Powerless to ask for help because it is seen as a sign of weakness and could jeopardize their job, too many people are left to toil and are forced to commit fraud to satisfy outlandish demands and out of fear of reprisal.

Frauds due to internal pressures can take different forms. For example, an employee who is supposed to inspect 10% of all in-bound raw materials might reduce the percentage inspected to 7% even though the expectation or inspection report might be 10%. Rushed quality tests, allowing for greater deviations from the "first quality" benchmark, in order to meet unrealistic goals are another result of the frauds due to internal pressures. Pushing manufacturing equipment to their limit to squeeze out more production -- and then refusing to allow downtime for preventative maintenance -- can be considered a fraudulent activity. Unrealistic sales goals are a fairly common source of forced fraud, especially if "numbers" are needed to meet or exceed financial analysts' expectations or drive bonuses.

Internal pressures include increasing new orders, recurring orders, picks per hour, manufacturing throughput, receipts per hour, and quality inspection throughput. Likewise, demanding decreases in times for manufacturing, picking, quality inspection, receiving, physical inventory, and cycle counting can all lead to fraud, especially in the absence of the necessary staff, training, and tools -- technology or otherwise -- needed for the employee to fairly and properly perform the task assigned to them.

Next newsletter: When Internal Fraud Boils Over

TURNAROUND TIPS

Financial Reports Due Diligence

At my first Turnaround Management Association (Florida chapter) meeting, I surveyed six turnaround professionals and asked the question: "What is it like not knowing if you can trust the numbers on the reports your given upon which you have to make financial decisions in the best interest of the ailing company?"

All respondents told me that it was a considerable problem, and in particular, one person answered back: "You don't know what kind of a nightmare this is for us."

Nobody wants an ailing company to fail, not the creditors, not the employees -- no one. And yet, without performing the necessary due diligence, how can a turnaround professional trust that they are making the right decisions? Is it ethical to alleviate responsibility because decisions were made based on the "available" data in hand, regardless of whether the data was trustworthy or not?

Taking a cue from the Good Governance section of this newsletter, the right thing to do for the customer -- the company in crisis -- is for the turnaround professional to perform the necessary due diligence to provide assurance that the financial reports are accurate or at least within an acceptable level of tolerance.

The additional benefit of an external analysis may also reveal that -- contrary to negative comments -- the company's business software applications are accurate and continue to be capable of supporting operations with integrity. This is a huge money-saver at a time when cash for continuance of daily operations is of primary concern.

Next newsletter: The System May Not Stink.....And Here's Why

GOOD GOVERNANCE

Legal versus Ethical

Just because something is legal to do, does not make it ethical to do.

This may be the greatest reason why so many politicians and businesses get into trouble. The consistent reason (excuse?) given for an action that has led to a disaster is that it was legal to do. There are likely few greater examples than the financial crisis of 2008: in the course of business, there was a lot done legally, but too much was done unethically.

It is relatively easy to know what is legal and what is illegal: laws are written down and, aside from loopholes, there is generally a good understanding of what is permissible by law.

But what about ethics? Not typically written down, and sometimes ambiguous, ethics is much more difficult to define that laws, as there may be more gray than black-and-white in ethics. To determine what is ethical behavior, a person may need to rely on their own judgment which will have been influenced by morals, values, environment, etc., and herein lies the problem for most people in determining what is or is not ethical behavior.

While laws tell us what is legal and not legal, ethics tells us what is right and wrong. For example, an ethical behavior statement in an employee manual might restrict the gifts an employee can receive from a vendor or supplier so as not to influence an employee's decision in which vendor or supplier to use. (And the same statement should be found in the supplier or vendor manual too!)

It is very unfortunate that too many people cannot distinguish between right versus wrong behavior, and what's possibly worse is the example this is setting for the next wave of employees.

In a joint study by Junior Achievement and Deloitte, teens were surveyed and asked if unethical behavior was needed to get ahead in business. In 2005, 22% of teens surveyed responded that unethical behavior was needed to get ahead in business; in 2007, that response jumped to 41% of surveyed teens. As the world suffers from the greatest financial crisis to affect the globe, one wonders if the root cause can be found in the fact that -- for the most part -- government and business continue to create its own problems.

Next newsletter: Relative Distance

Attachments: