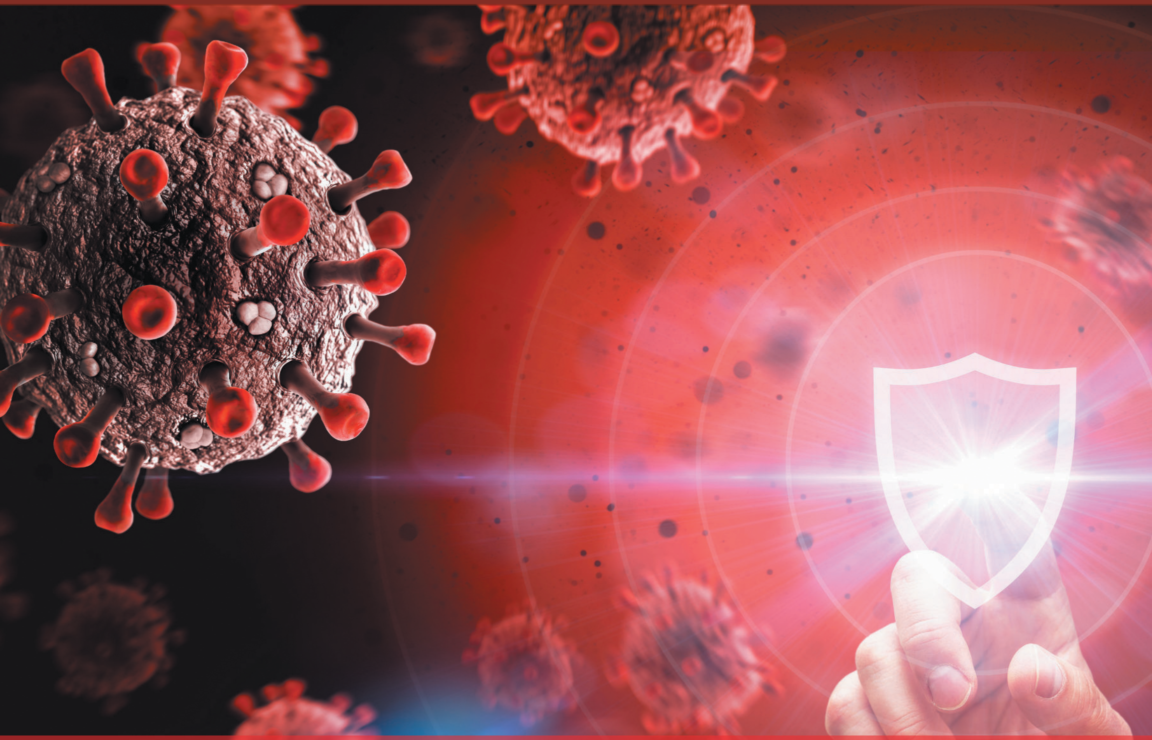
CALLING OUT COVID-19

Business Strategies for Surviving a 'Pompeii Event'



Written by

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Faisal Sheikh, Nigel Krishna Iyer, Brian Leigh, and Geetha A. Rubasundram

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Calling Out COVID-19: Business Strategies for Surviving a 'Pompeii Event'

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This book is dedicated to all the (living and fallen) global frontline heroes, be they clinicians or chaplains or cleaners or carers, who continue to battle COVID-19…THANK YOU!

Also, special thanks to the international teams of researchers who have managed to create a suite of vaccines in such a record-breaking time.

You never know how strong you are until being STRONG is the only choice you have.

—Anonymous

Description

We are currently experiencing the second wave of an unprecedented global pandemic–the COVID-19 crisis, which is destroying established industries such as tourism and attributing to the death of millions of people worldwide. The authors believe that the pandemic is analogous to the ancient Roman tragedy of Pompeii when the citadel was buried under four to six meters (13 to 20 feet) of volcanic ash and pumice in the eruption of Mount Vesuvius in AD 79.

This book is written for business owners, entrepreneurs, leadership, or management teams in public or third sector and professionals who are currently dealing with the COVID-19 epidemic. It offers tools and techniques located in the economics of innovation, other frameworks such as the Fraud Triangle, and the authors extensive experience including rigorous cash management, practical fraud prevention, and detection and advice on implementing and refining corporate governance structures. The book will also be of interest to postgraduate including MBA students and business researchers.

The book concludes by summarizing the key theories that can be used to understand the impact of this Pompeii Event and pragmatic solutions to fight COVID-19. The authors argue that organizations rooted in foresight will survive and emerge as future trail blazers. An extensive appendix is also included which outlines the implications for financial reporting.

Keywords

COVID-19; Pompeii Event; innovation; crisis; uncertainty; decision-making; cash management; fraud prevention and detection; corporate governance; foresight

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Reviews

"A romping, interesting, and well-informed read—not a standard recommendation for many business and accounting texts. The text reiterates the need for trust, good leadership, and the importance of the work force, in the creation of real—living and breathing best in practice, global governance. Behavior and good communication, inside and outside the organization; the move onward from beyond budgeting and agile management, to well informed global management control. A valuable and interesting text for executives, managers, and business students, if they want to survive, be inspired, and respond effectively to a POMPEII EVENT." **—Eileen Roddy, Former Associate Dean Salford Business School, Managing Partner at International Strategy Application, eileen.roddy@outlook.com**

"Written while in the "teeth of the storm," the authors' comparison of the unfolding catastrophe of the 2020 Coronavirus pandemic with the fate of Pompeii in AD 79 is compelling. The socio-economic ramifications of the pandemic are likely to be with us for generations to come. In this book, the connected strategies, activities, and risks posed to the corporate world are carefully examined. That this latest Pompeii Event could be the threshold to a greener world with increased importance assigned to CSR—leaves the reader with some hope of a better future." **—Richard Williams. Staff Partner, Beevers & Struthers, https://beeverstruthers.co.uk/aboutus/richard_williams**

"It's a captivating 125 pages. Despite the fact that multiple authors were involved in the project, its tone and style of presentation flow smoothly, and the appearance of a single voice has been accomplished. The book has potential for a wide and diverse user base. For instance, I can envision it being on a reading list in an accounting seminar, in a business policy and strategy course, a crisis management seminar, or even in a public policy course offered in a sociology department." **—Professor Mark Bettner, Visiting Professor of Accounting at Furman University, mark.bettner@bucknell.edu**

Foreword

A Medical Doctor's and CEO's Perspective

A fantastic and informative read. As a medical practitioner and CEO, Calling out COVID-19 is a quintessential read for everyone, the authors' reference to a *Pompeii Event* is most fitting.

COVID-19 has turned the global economy upside down, forcing medicine and business to take a beating. This book offers a unique insight into business strategy, that is, how to navigate COVID-19 with effective *brain-storming, innovation and a frugal approach.* Lastly, Sheikh's theory of *Smash, Grab and Go* is genius, it is a crucial analysis of how to *revisit an organization's capital investment* structure, most pertinent during such testing economic times.

Chapters 4 and 5 are particularly relevant for persons in positions of authority, with compromised GDPs and soaring unemployment, *disrupted supply chains* have resulted in *fertile ground for fraudulent activity*. The authors identify the burning consequences of the pandemic, educating the reader on the *Fraud Triangle* and, more importantly, the appropriate safeguards to implement, so as "to spot it and stop it before it spreads." The subsequent chapter seamlessly transitions into corporate governance. The acronym of *VICTORY* resonates with my professional person, the logic of such concept is insightful and intelligent, more specifically, *Vision*, a strategic and long-term mindset are crucial to be successful. This coupled with *Yahoo* is truly splendid, that is, celebrating small wins and learning from mistakes.

By far, my professional career and position as a CEO have demanded my consistent attention to the subjects flagged in Chapter 4 and 5. Corporate governance within the Gulf remains relatively new, the Arab Spring has allowed the Middle East and its inhabitants to enjoy much wealth, but with depleting oil reserves, alternative business revenues are being explored within the region. The authors explore the necessity for "fairness, transparency, honesty, responsibility and reputation," concepts that run true within the Gulf. I do, however, implore the authors to traverse the borders of the UK and the United States, while the West maybe considered pioneers of such concepts, the Middle East is attending to corporate governance with a cultural "Je ne sais quoi" which requires additional exploration and focus. I am dedicating considerable efforts to spearhead such efforts in my company, with a belief that such matters will echo throughout the Gulf business world.

I applaud the collective efforts of all the authors, Accountants v COVID-19, is well written, the fine finesse and attention to detail are evident in each chapter, well supported by extensive research and relevant examples. In short, this book is *a must have* for any individual seeking a better understanding of COVID-19, the current economic climate, and how to succeed in the face of adversity.

I am truly humbled and feel most fortunate to be penning a foreword for such an esteemed team of authors, you continue to educate, inspire, and motivate, I remain, forever grateful.

Dr. Yasmin Abdul Ghahfour, CEO
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and Financial Investments
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An FD's / CFO's Perspective

Very often, business-related books focus on the history or research to give advice on the way forward, but the authors here combine history and research to inform the decision-making. In a logical way, the book compares the historical devastation of Pompeii, which happened incredibly quickly, to the impact of COVID-19 and the speed in which the world changed but also that the path to recovery is long and different from what we had before.

As business leaders, the book draws key aspects for us to consider as we start economic recovery, even though the path we take may differ. Not surprisingly, a key focus in the book is the importance of innovation; the book covers what this means, why is it important, the 10 types of innovation, and then how to go about it in a pragmatic way. We cannot afford the time to theorize; speed, as we now know, is essential.

Also, essential, not critical, is cash. Many businesses will have and will continue to experience tight cash flows for some time to come. The book covers the devastating impact of the pandemic but more positively real actions that all businesses could consider utilizing in order to protect and sustain their cash flow.

Sadly, not all people act with honesty and integrity, and we have seen many examples though the pandemic period of fraudulent behavior; it existed before and will undoubtedly continue. The authors demonstrate that as leaders, it is important for us to understand that the drivers will be ever more present, and we all have a role to play throughout our organizations to use the quote "See it, Say it, Sorted."

Whether you run a small business or a global listed company, governance of the business, whether your view is that is it a recent phenomenon or goes back centuries is now an embedded business requirement and, in my view a critical part of the way businesses are run. Many of you will remember some of the examples highlighted but perhaps not the knock-on impact that they had. Again, you will find simple but effective guide to the skills, behaviors, and subjects to aid your thinking and actions. It does not need to be complicated, just appropriate for your business.

As a Finance Director with over 25 years' experience, the last year has been incredibly challenging; so many of the examples within the book resonate with me, but more helpfully, provides actioned-orientated advice that all businesses can consider. I love a list!

Finally, this book is not hard to read. We are all pressed for time, and one of the real attributes of this book is that it is written in a way that is easy to follow, the chapters can be read in isolation if you just want to cover a specific topic, but in all cases, you have a *to-do* list.

COVID-19 is the Pompeii Event of our generation, which inevitably has required businesses to reflect, change, and embrace a different future if they are to survive and thrive.

Julie Charge
Finance Director and Deputy Chief Executive of University of Salford
https://salford.ac.uk/corporate-information/leadership-and-governance

An International Audit Partner's Perspective

The COVID-19 pandemic has created unprecedented socio-economic havoc on a global scale that continues in the shape of national lockdowns, travel restrictions, and social distancing. The authors in the first chapter emphasize the negative impact on the aviation and hospitality industries, which have literally collapsed, leaving a deep wound that may never completely heal. The lead author explored the impact of other historical events such Spanish flu and Ebola but COVID-19 has by far done more damage. Hence, I appreciate the metaphor of the *Pompeii Event* as an attempt to comprehend this seismic event. The future remains deeply uncertain, which is a cause of even greater concern, as businesses operate in a highly inter-connected global economy, including international supply chains.

I am deeply concerned for emerging markets and developing economies that were already under economic pressure and have been deeply affected by this crisis. They are currently suffering from sharp economic downturns coupled with an immense strain on already fragile or fractured health-care systems, loss of trade and tourism, diminishing remittances, poor capital flows, and a constrained financial environment, coupled with insurmountable debt. Exporters of energy and industrial commodities have already been seriously hit, including an unprecedented slump in oil demand and destruction in oil prices. I believe fragmented and experimental fiscal policies, including quantitative easing, will only exacerbate the global economic depression, as the mountains of debt will need to be serviced by future generations. As noted by the authors, the Bank for International Settlements (BIS) (2020) has argued that the pandemic has altered from a *liquidity crisis* in the early stages to a *solvency crisis* that could deepen if the economic recovery is delayed.

Consequently, the tools and theories discussed in four well-argued chapters covering innovation, cash management, fraud prevention and detection, and corporate governance will prove to be *life-saving* initiatives for businesses in the thick of this Pompeii Event. I agree with the authors that new business models are urgently required such as zero-hour contracts rather than mass redundancies that destroy human capital. On the other hand, businesses scramble for the best talent when there is a rebound and need to re-invest heavily in re-training and development, which takes time to transform into superior productivity and profitability, that is, a vicious cycle. I personally believe there should be more support for entrepreneurship and self-employment, which will result in sustainable job and wealth creation. Readers will also derive benefit from the separate appendix that details the financial reporting implications from the fallout from COVID-19.

Overall, I commend the authors for their valiant efforts and foresight to *help solvent but cash-constrained firms across the world that urgently require guidance to navigate and survive this epic crisis.*

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A Financial Reporting Expert's Perspective

At the date of writing this, it is almost 12 months since I left my previous firm and started my current job. I needed fresh challenges and different surroundings, and my impending move seemed the right thing to do.

If somebody said to me this time last year you will only visit your new office twice over the next year, I would have thought they were mad. My new job started just a couple of weeks into lockdown, and it started via Zoom meetings and various calls with IT specialists to get my home laptop compatible with the remote systems of my new workplace. Everything was surreal; there was no need for me to get the train in the morning, I just walk into the front room, press a few buttons, and put on the headphones, and via the magic of the Internet, meet some new colleagues for the very first time.

The world had certainly changed, and many were facing uncertainty, including myself, but I felt very lucky to be able to continue my work in financial reporting, meet new clients, and meet new colleagues. A couple of months after joining my new firm, I get the opportunity to present training materials across the UK and Europe, the Americas, and the Caribbean. What a jet-set style I was leading on paper, where the reality was, I was broadcasting live from the West Midlands. Given the effective ban on traveling unless it was for essential reasons, the world suddenly seemed such a large place; however, like nothing before, I was using technology to the extent that I could be anywhere at any time working live with anybody across the world.

Following the Pompeii Event, it seemed like I was now living in real time in a Hollywood movie, a simulation if you like, where the pandemic had turned everything upside down and inside out. From the economic perspective, it was clear that this Pompeii Event was going to be the largest test of business models, markets, and financial reporting since the Great Depression, but in a modern fully connected world full of surprise, innovation, and great hesitance.

It is now 12 months on, and I am working in the same room, but on reflection, feel as though the last 12 months could have been a dream and I am suddenly in this new normal we often hear about. However, the authors have captured the last 12 months since this Pompeii event and have proven to me that this was not a dream.

This book took me on an amazing journey over the last 12 months, affirming that the last 12 months really did happen. It reminded me of many things I had forgotten about, big events that have since been brushed under the carpet following repeated lockdowns, unprecedented government intervention on a scale I never though possible, breakthroughs in medicine in the form of new types of vaccines, business failures particularly on the High Street, and the travel and hospitality sectors.

In the hope of becoming immune to COVID-19, we seem to have become immune to big news events, have learned to expect the unexpected, nothing seems to shock us anymore. But, on the other hand, the world is full of surprises. The book reminded me of all the great things that the business community has achieved, how the workforce has remained connected while friendships, and extended family life is more distant.

We are only at the start of the fallout from the Pompeii Event and are yet to feel much of the consequences of the lockdown. This book, however, contains everything to prepare finance professionals, business owners, and interested parties for the fallout, and no doubt, the fallout from the fallout.

The COVID-19 pandemic, the Pompeii Event, means going back to the very basics of cash management and budgeting, looking at those things afresh, rebuilding financial controls to cope with new types of working environment, ensuring the board are at the helm steadying the corporate ship through rocky waters, and ensuring stakeholders are served as well as possible, dynamic approaches to governance will be required, and boards will be tested like never before as they move into the survival mode. All sides of the Fraud Triangle are hot—the scope for fraud from misuse or theft of government support to corporate assets, the use of scams and false businesses, has never been greater.

In short, this book covers everything to prepare us for the aftermath of the Pompeii Event and is a stimulating synopsis of how we as individuals, or as a group of individuals, can try and forge a path forward, as the economy fights for survival.

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Acknowledgments

Writing this book, and above all, collaborating with my fellow authors ***Brian Leigh (England), Nigel Iyer (Norway), and Geetha Rubasundram (Malaysia)*** has been an immensely enriching experience. Heartfelt thanks to our families who gave us the time and space to turn around this book in such a short span of time.

This book will remain a bittersweet journey, as on the way, I lost my sister-in-law, Assia, and father-in-law, Shah Ji. I battled COVID-19, and thankfully emerged in awe of this dastardly disease. I believe that this pandemic is merely a *warm-up* and the next *revenge of Mother Earth* or Pompeii Event will be even worse. ***Caveat Emptor!***

As ever, thank you to the BEP team, Scott Isenberg, Charlene Kronstedt, and Sheri Dean, for their ongoing support and good humor. I remain indebted to BEP for helping me find and cultivate my *voice*. Thanks to the folks at Exeter, including Dhinesh, for such a stellar copy-editing job.

Finally, thank you to our gracious reviewers for taking time out of their busy schedules and putting pen to paper. I am glad that my colleague Neil Parsons *survived the book* and wrote in his submission e-mail:

…a superb read. It made my heart beat fast in some parts.

I am to learn…

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CHAPTER 1

"Pompeii Event": The COVID-19 Catastrophe

Introduction

The novel coronavirus (COVID-19), acute respiratory outbreak crisis, probably originated in Wuhan province, in China, in December 2019. COVID-19 rapidly spread to more than 200 countries, in Asia, Europe, the Americas, and Australasia. It has infected millions of human beings and caused approximately one million deaths to date. The global spread of this virus led the World Health Organization (WHO) to characterize this highly infectious disease as a pandemic on March 11, 2020, as it showed increasing human-to-human infection.

COVID-19 continues to exceed infection and death rates compared to other recent coronavirus outbreaks such as MERS-CoV, SARS-CoV, and seasonal influenza. Previous studies argue that movement restriction is viewed as the optimal approach to control the spread of infectious diseases such a COVID-19. This thinking forced governments across the globe to impose unprecedented blanket lockdowns, travel restrictions, and social distancing. This resulted in an unparalleled collapse in consumer demand for goods and services, full or partially stalled production, and the destruction of national and international supply chains. In addition, the emergency or quarantine orders for preventing the spread of COVID-19 has negatively enhanced social problems such as soaring domestic violence, child abuse, alcohol and substance misuse, and severe mental health issues as whole populations were in effect prisoners in their own homes during lockdowns.

COVID-19 and the ensuing global depression has wrecked the entire financial system. In 2020 Quarter 2 (Q2), gross domestic product (GDP) in the UK shrank by a serious 20.4 percent. By contrast, *throughout* the 2008 recession, GDP contracted by no more that 2.1 percent in a single quarter. The last time this happened to UK GDP was due to agricultural depression in the 17th century resulting in falling prices of two staple products, grain and wool, which continued to decline throughout the first half of the 18th century. Currently, 8.1 million workers are furloughed, with unemployment crossing 1.5 million and inflation is close to zero.

The world's largest economy, the United States, suffered its worst period ever in 2020 Q2, with GDP falling to an historic 32.9 percent. Neither the Great Depression nor the Great Recession nor any other crash, according to analysts, three dozen in total over the last 200 years, has ever caused such a harsh impact on the U.S. economy. In stark contrast, the worst quarter during the financial crisis of 2008 was the 8.4 percent GDP drop in the fourth quarter of that year. U.S. unemployment is currently 15 percent and rising, and inflation is falling.

Entire industries such as aviation and hospitality are collapsing, and even billionaires such as Richard Branson have asked for government bail-outs. Investors have started to discount the liquidity risk in stock prices and approximately $23Tn in global market value has been destroyed since the outbreak, although there appears to be a bounce back across global markets. Research suggests that investors respond not to infection or death rates, but rather to the future trajectory of an outbreak such as COVID-19. It is argued that markets decline when there is unpredictably bad news, and rise when there is unexpectedly good news. *However, there remain solvent but cash-constrained firms across the world who require support, and this insight was the reason for writing this book to help them navigate and survive this epic crisis.*

The lead author has termed COVID-19 as a *Pompeii Event*, which will be discussed in further detail together with its impact on global business. The chapter will finish with an in-depth mini-case study on tourism demonstrating the ferocity of this Pompeii Event.

The Pompeii Event—COVID-19 and the Impact on the Global Economy

What constitutes a crisis? Booth (1993) defines crisis as a situation faced by an individual, group, or organization unable to manage using normal protocols. There are three types of crises, namely gradual threat, periodic threat, and sudden threat. Thus, COVID-19 is indeed a sudden threat, which the lead author believes is analogous to the ancient Roman tragedy of *Pompeii* when the citadel was buried under 4 to 6 m (13 to 20 ft) of volcanic ash and pumice in the eruption of Mount Vesuvius in AD 79.

According to ancient sources, the eruption lasted for two days. The initial phase consisted of pumice rain, which lasted for approximately 18 hours, allowing most inhabitants to escape. The second day was full of *pyroclastic flows* that began near the volcano, comprising of fast, thick, and extremely hot ash clouds, destroying everything in its path and suffocating the remaining population and surrounding towns' populations and changing *forever* the landscape, including the coastline. By the evening of the second day, the eruption finished, with only haze in the atmosphere through which the sun shone poorly. The important thing to note is that the explosion took place over several days almost in waves of destruction. Pompeii was acknowledged as an important economic route for goods that arrived by sea and were sent toward Rome or Southern Italy along the nearby Appian Way. Consequently, there must have been severe economic repercussions, which must have taken perhaps years to stabilize.

In the same way, COVID-19 is a *Pompeii Event* because the *initial eruption or rampant spread* of the virus forced the Chinese government to close the entire province of Wuhan, considered the manufacturing hub of China, resulting in the severe reduction if not halting of global supply chains. The *breath-taking spread of the virus or pyroclastic flows* to Iran and Italy resulted in nation lockdowns, coupled with social distancing, which planted the seeds of an unprecedented global depression. Consequently, a nonfinancial or extreme health crisis, namely a pandemic, COVID-19, triggered a global meltdown. The socioeconomic carnage was undoubtedly exacerbated by travel bans that severely affected the aviation and hospitality industries, due to mass cancelations of sports events such as the Champions League and the Olympics, which harshly impacted the sports industry and the ban on mass gatherings causing distress to the events and entertainment industries.

One could argue that the COVID-19 crisis is a *Black Swan* (Taleb 2010) event, which is an unpredictable incident beyond the normal, coupled with severe consequences. Black Swan events are highlighted by their great rarity, extreme impact, and the widespread belief that they were, in hindsight, obvious. Examples include the 2008 financial crunch and the 2001 dot com bubble. Some analysts argue that diversification may offer some protection when a Black Swan event occurs.

However, COVID-19 has transformed into a global public health of post-Biblical proportions and an economic crisis that has affected the $90Tn global economy beyond anything experienced to date. According to Jones (2020), "Some experts warn that half the world's population will be infected by year's end, an incidence that could result in more than 100 million deaths." As of August 2020, the virus has even hit the remote Greater Andamanese tribe, in Brazil, and an isolated tribe in India's Andamans archipelago.

The nearest comparison in the modern era struck more than a century ago, when the so-called *Spanish Flu* devastated the world from 1918 to 1919. According to estimates, approximately 500 million people were taken ill with the disease, which ultimately took the lives of about 50 million people worldwide. Even the H1N1 flu of 2009 was widespread, but not as deadly, with an estimated 60 million cases in the United States, causing less than 13,000 deaths.

Nowadays, companies operate in a highly inter-connected global economy, including international supply chains. Consequently, the economic fallout from COVID-19 is extreme due to the global lockdowns in Q2, coupled with ongoing social distancing. Thus, a ripple effect throughout the global economy was inevitable and continues. In the immediate aftermath of lockdowns, specific industries bore the brunt of the carnage. Retail and hospitality industries came to a grinding halt and as all nonessential travel collapsed, the airline and tourism industries, including oil producers, went into free fall. Williamson (2020) noted, "While some producers reported being busier as a result of stockpiling and anti-virus activities, notably in the food and healthcare sectors, these are very much the minority, and most sectors reported a rapid deterioration in demand and production."

Manufacturing, apart from the medical industry, saw fewer orders as consumer demand severely contracted. In the United States, retail sales fell by 8.7 percent in April 2020, the greatest monthly drop since the government began collecting data. Data from the Federal Reserve highlighted the worst dip in manufacturing output since the 1940s. Manufacturing Purchasing Managers Index (PMI) fell below 50 in all major economies, including the United States, the UK, and Japan, which is considered a contraction of activity. In addition, the precipitous fall in demand had a devastating effect on employment. In March–April 2020, approximately 22 million Americans had filed for unemployment benefits, surpassing all records to date, with another one million signing on in August 2020.

The economic shockwaves are being felt from Beijing to Los Angeles, resulting in a drag on the world economy that has not been witnessed for decades. Every region across the globe is subject to starkly revised growth rates. East Asia and the Pacific will grow by a negligible 0.5 percent. South Asia will shrink by 2.7 percent, Sub-Saharan Africa by 2.8 percent, Middle East and North Africa by 4.2 percent, Europe and Central Asia by 4.7 percent, and Latin America by 7.2 percent. These slumps are expected to overturn years of progress toward United Nations (UN) development millennium goals and potentially send tens of millions of people back into extreme and potentially permanent poverty.

Emerging market and developing economies will be battered by economic tsunamis, including pressure on already fragile or fractured health care systems, loss of trade and tourism, diminishing remittances, poor capital flows, and a constrained financial environment, coupled with insurmountable debt. Exporters of energy and industrial commodities have already been badly hit, including an unprecedented slump in oil demand and destruction in oil prices. CNN Business (2020) cited in Poynter (2020) reported “US oil prices plunged falling below $0 Monday to $-37.63 a barrel. That’s the lowest level since NYMEX opened oil futures trading in 1983” in Q2**.** Demand for metals and commodities used in the transport industry such as rubber has also plunged. Although global agriculture markets are well stocked and supplied, trade restrictions and severe supply chain disruptions will create food security challenges, especially in sub-Saharan Africa.

The International Monetary Fund (IMF) recently forecast a 3 percent drop in global output in 2020, which would be the worst deterioration in recent memory. The organization envisions a subdued recovery in 2021, with GDP growth of a modest 5.8 percent worldwide.

It is argued that the, albeit brief, snapshot from the ongoing socioeconomic fallout from the COVID-19 pandemic demonstrates the momentous *speed, scale, and scope* of the unfolding crisis—*the key constituents of a Pompeii Event* (see Figure 1.1)—that has *buried* the global economy and caused immeasurable socioeconomic carnage.

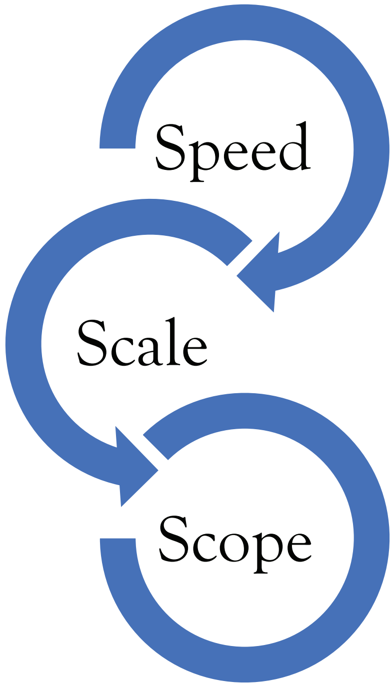

Figure 1.1 Key constituents of a Pompeii Event

Consequently, it is argued by the authors that it will not be business as usual, which occurred after the 2008 financial crunch, but a wholesale transformation in global socioeconomics. The authors argue that this Pompeii Event will continue to create *disruption*—on a truly global scale, and the strategy should be to stay ahead of the curve in one's industry or field and will potentially lead to greater self-reliance on a national and international level, *aggravation*—of pre-existing tensions such as the current polarization of politics or mass migration or Brexit, *redefinition*—of the global order especially Sino-U.S. relations, which continue to worsen and *return*—of the next Pompeii Event, which is anticipated to be something related to climate change, see Figure 1.2.

The Bank for International Settlements (BIS) (2020) has stated that future writers may describe the pandemic as, "the defining moment of the 21st century" or as the lead author has argued a "'Pompeii Event' not a Black Swan event with further waves expected."

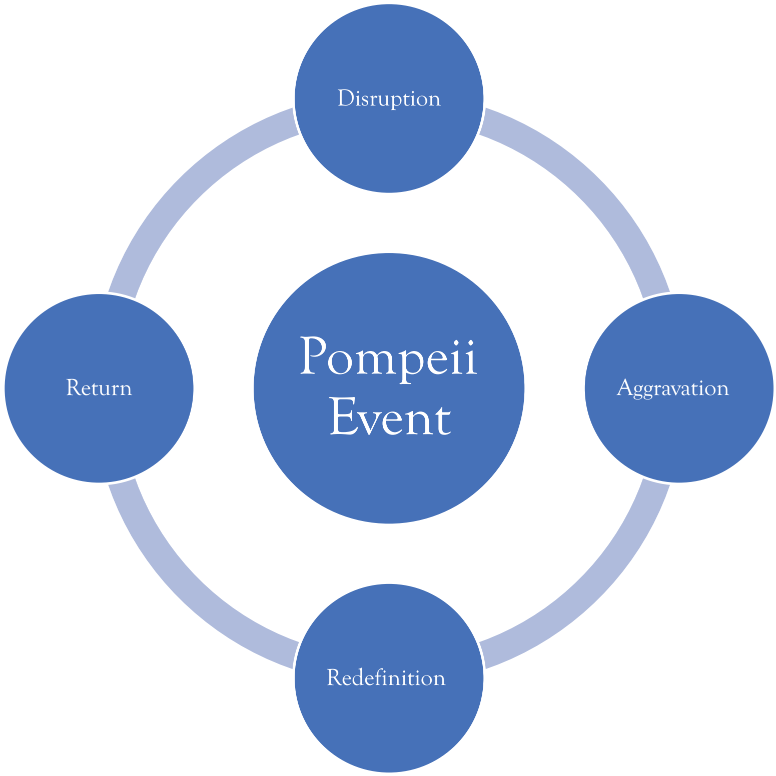

Figure 1.2 Continued fallout from the Pompeii Event

There was hope that there would be a recovery in Q3 of 2020 as governments across the globe started easing social distancing requirements and reopening their economies which did not happen. However, this is unlikely, as there continue to be regional and national waves of COVID-19 infections, resulting in regional or local lockdowns, and until a vaccine is found, the 2020 northern hemisphere winter appears to be ominous.

The U.S. Federal Open Market Committee (FOMC) suggested that the rise in COVID-19 cases in the United States since mid-June was damaging economic growth and that, "The path of the economy will depend significantly on the course of the virus. The ongoing public health crisis will weigh heavily on economic activity, employment and inflation in the near term, and poses considerable risks to the economic outlook over the medium term" (cited in Congressional Research Service 2020).

The Global Fightback Against This Pompeii Event—COVID-19 and the Immediate Future

After a tardy response, in part due to inconsistent and potentially flawed data from China, central banks and monetary authorities across the globe have set in motion an array of monumental interventions in financial markets coupled with a raft of fiscal policy initiatives to stimulate their faltering economies (gathered and created from various online sources), Table 1.1.

Although global central banking spending including by the United States and UK authorities has topped more than $4.5Tn, there remains a tradeoff for governments, which is to *save the people or save the economy*. The BIS (2020) has argued that the pandemic altered from a *liquidity crisis* in the early stages to a *solvency crisis* that could deepen if the economic recovery is delayed. This was further emphasized by IMF managing director Kristalina Georgiev who stated in late March 2020 that the global economy had entered a recession and called for *very massive* spending and

Table 1.1 Fiscal policy spending and policies to fight COVID-19

Country	Total direct spending	% of GDP	Loans and loan guarantees	% of GDP
United States	USD 484Bn	2.4	USD 2.3Tn	9.3
UK	GBP 350Bn	11.8	GBP 350Bn	10.7
Canada	CD 107Bn	6.2	–	–
Czech	Czk 100Bn	1.8	CZK 900Bn	15.9
Egypt	EGP 50Bn	0.8	EGP 50Bn	0.8
Israel	Ils 2.8Bn	0.4	–	–
India	IR 1.7Tn	967	USD 1Bn	0.04
Poland	ZL 212Bn	9	ZL 700M	0.1
Nigeria	NGN 3.5Tn	2.3	USD 6.9Bn	7.5
Romania	RON 9Bn	0.9	EUR 400M	0.2
Russia	RUB 1.4Tn	0.3	–	–
Saudi Arabia	SR 120Bn	3.9	–	–
Turkey	LR 100Bn	185	–	–

that, "A key concern about a long-lasting impact of the sudden stop of the world economy is the risk of a wave of bankruptcies and layoffs that not only can undermine the recovery but can erode the fabric of our societies" (IMF 2020). She also argued that emerging markets will need $2.5Tn in outside financing.

Why does the economic fallout continue unabated? Initially, during the height of the pandemic when governments were enforcing blanket lockdowns of people, economic activity practically ceased. The health of people was put before their economic welfare, which continues to have far-reaching consequences.

COVID-19 outbreaks are expected, and a major second wave was expected in the winter months, as was witnessed in the UK. Inevitably, restrictions on movement will be reintroduced or there will be extensions that will damage economic activity, thus prolonging the global depression. Businesses and individuals will probably struggle to service company and personal debt, making the cost of borrowing more expensive, and ultimately leading to mass company liquidations and bankruptcies, which will exacerbate or deepen the global depression. According to this negative scenario, global growth could contract by approximately 8 percent in 2020 (World Bank 2020).

Some analysts argue that many lesser developed countries or emerging economies were already suffering from poor growth before this Pompeii Event. Consequently, efforts to contain COVID-19 where there was already limited health care capacity could potentially hasten deeper and longer depressions that may damage long-term growth prospects and damage productivity. It is further argued that economies with informal sectors accounting for one-third of the GDP and 70 percent of total employment, such as in South America and South Asia, are particularly vulnerable. Policymakers in these nations will need to implement wide reaching income support and credit support programs.

This Pompeii Event, namely COVID-19, has affected every sphere of global socioeconomic life and businesses need concrete solutions. A mini-case study will explore the impact of COVID-19 on the travel and tourism industries and offer some tangible solutions.

Impact of Pompeii Event on Global Travel and Tourism—A Mini Case Study

It is acknowledged that health is vital for an industrious and growing society. On the one hand, anxiety and disease can wreck production, consumption, recreation, travel and tourism, and general well-being. An infection normally attacks weaker groups in society, such as the poor and elderly, causing food and health care insecurity. On the other hand, COVID-19 initially attacked international travelers, and the pandemic was spread through travel and struck the affluent classes across the globe.

As already discussed, health calamities such as the Ebola virus in West Africa, the Middle East Respiratory Syndrome (MERS) outbreak in the Republic of Korea, and the COVID-19 pandemic negatively impacted health and caused huge socioeconomic upheaval. During the Ebola virus in West Africa from 2013 to 2014, government receipts, including both direct and indirect taxes, dramatically fell and foreign investment decreased by U.S. $600M over the two years. It was estimated that the total global economic loss due to SARS was $40Bn. In a similar but stark contrast, *COVID-19 has severely disrupted global trade and supply chains, weakened asset prices, and forced businesses to make difficult decisions with limited information wiping 0.5 percent off global GDP, which equates to approximately $300Bn.*

Tourist arrivals in Hong Kong shrunk by 68 percent in two months during the 2003 SARS outbreak and in South Korea international tourists severely contracted by 41 percent in the summer season. On the other hand, analysts argue that COVID-19 has permanently changed the global landscape and has severely damaged the international travel, tourism, and hospitality industries, which are highly vulnerable to shocks like COVID-19. These shocks are not new to the travel and tourism industry, which has coped with natural disasters such as earthquakes, human threats like terrorist attacks and the global 2008 financial crisis. Hence, the global travel and tourism has managed to create risk mitigation strategies and emerge stronger. However, the authors argue that the COVID-19 pandemic is global, and the risk is not just about the travel and tourism industry hemorrhaging cash or losing profitability but losing lives on a momentous scale. Thus, COVID-19 is a *supershock* or a Pompeii Event to the travel and tourism industry, a Pompeii Event of such epic proportions that it has the power to trigger a seismic shift to parts, if not the entire, global travel and tourism industry.

Ongoing international travel bans and mandatory quarantine for returning tourists, affecting international air travel, resulted in tourism mainly grinding to a halt in March 2020 and even the growth of travel and tourism has been questioned. Chang et al (2020) suggest that the effect on air travel, cruises, and accommodation has been *disastrous*. Tourism is highly sensitive to official guidelines to counteract pandemics because of limited mobility. Consequently, within a few months of COVID-19 initially being recognized in China's Wuhan province, in December 2019, global tourism demand collapsed. *In fact, the entire tourism value chain has been influenced, and it has been reported that bookings are down from China to Canada by approximately 70 percent, between October 2019 and March 2020*. The situation worsened when the WHO declared a pandemic. The UN World Tourism Organization (UNWTO) (2020) declared the tourism sector to be "one of the hardest-hit by the outbreak of the coronavirus disease, with impacts on both travel supply and demand, particularly in China, the world's leading outbound market in spending." It was forecast that Spain would have no tourists within weeks of the outbreak period, and in Australia, there were potentially one million jobs are under threat.

According to Ranasighe et al (2020), the March 2020 data published by the global hospitality data firm STR suggests occupancy rates approximately 96 percent down across the entire global hospitality industry due to the ongoing COVID-19 crisis. EY (2020) undertook an extensive survey of the Cypriot tourism sector, and most of the participants expected to make losses, only 25 percent expected to reopen in July 2020, and it was believed that foreign tourists would choose to vacation at home, also known as *staycation*.

In response to the breakneck spread of the virus, governments across the globe have embraced health-centric policies based on WHO (2020) guidance, with the aim to control the human-to-human transmission of the virus, and corresponding care for those infected. As already discussed, the latter has resulted in unprecedented monetary and fiscal interventions to contain the expected economic downturn.

The travel and tourism sector is a vital pillar in any economy and has an important role to play in the national and global economic recovery. As noted earlier, the sector has proven to be resilient to global shocks and helps other areas of the economy through *ripple effects* (EY 2020). However, COVID-19 is a Pompeii Event that will fundamentally change the sector and a member of the EU Parliament's Transport and Tourism Committee, Karima Delli, astutely noted (EU Parliament May 13, 2020):

"It is crucial to reassure citizens that tourism and travelling will be possible and safe this year. We should use this ***crisis to redesign tourism across the EU" (Emphasis by authors).***

The preceding comment, especially the final comment, is hinting toward *innovation*, which will be discussed in much greater detail in Chapter 2.

No one can precisely forecast the final financial damage from COVID-19 to the travel and tourism industry. The authors believe that the travel and tourism sector will probably witness mass redundancies, mergers and acquisitions or rationalization, home or native tourism will boom with a contraction of luxury travel and tourism as the market for international tourism declines. Hence, the authors offer the following financial policy prescriptions to protect international travel and tourism, rather than just the typical heavy discounting in a crisis:

- Once government-backed job security programs, such as the UK furlough scheme, are curtailed, companies should offer zero-hour contracts rather than making staff redundant who are the bedrock of the travel and tourism business.
- Offer *freebies* such gratis meals or drinks or faster check-ins or check-outs or guided tours.
- Variable rates for all services by crafting *no-frills*, budget plus and luxury products.
- Carriers should offer an adaptable travel waiver policy to their customers and complimentary modifications to tickets to maintain customer loyalty.
- Suspend noncancelable fees and credit card charges.
- Strategic marketing of the hashtag *#Travel Tomorrow* under the patronage of the UNTWO.

- Investing in innovative social media marketing campaigns, across all platforms, especially those favored by millennials such as Snapchat and Tik Tok, celebrating ethnic culture such as the highly successful *Incredible India.*
- Airlines should offer an adaptable travel waiver policy to their customers and complimentary modifications to tickets to maintain customer loyalty.

How Should Businesses Across the Globe Respond to This Pompeii Event—COVID-19?

In the current COVID-19 climate, an appropriate framework to help navigate and respond is VUCA *(volatile, uncertain, complex, and ambiguous*). Introduced by the U.S. Army War College, VUCA described the increasingly, if not *permanently* volatile, uncertain, complex, and ambiguous world, following the end of the Cold War. The authors would argue that the Pompeii Event—COVID-19—has dramatically intensified the elements of VUCA. A summary of each section is as follows:

Volatile: On December 31, 2019, Chinese government officials confirmed multiple cases of pneumonia from an unknown cause, and then a week later, on January 07, 2020, the outbreak was identified as a new coronavirus. Since then, there have been millions of reported cases and more than a million fatalities worldwide, and COVID-19 continues to present health experts with an extremely fast-moving situation. As the pandemic grows, the advice continues to change creating further confusion, unnecessary uncertainty, and anxiety.

Uncertain: The next phases of the Pompeii Event remain unclear, and the only certainty is that a vaccine(s) may help. The lack of clear information continues to feed the global hysteria and trauma, which was evidenced by panic buying of items such as toilet roll, pasta, and hand sanitizer in the early stages. Then, British tourists, during the summer of 2020, rushed home to avoid fortnight quarantines from blacklisted destinations such as Spain and France.

Complex: Due to the *speed, scale, and scope* of COVID-19's global spread, and the fact that people live and operate in an inter-connected world, it becomes increasingly difficult to fully comprehend the outbreak, let alone the trajectory of the virus. It is abundantly clear that variables to understand and counter this Pompeii Event cannot be understood or analyzed from merely one perspective such as economics and the occasion demands an interdisciplinary approach. *Thus, later chapters grounded in innovation, financial management, counter-fraud, and corporate governance will be introduced to offer a multifork response to this unprecedented moment in history.*

Ambiguous: As already noted, COVID-19 is unique, unprecedented, and the lead author developed an analogy, namely the Pompeii Event, *to capture the speed, scale, and scope of the crisis, which has not only buried the global order, but continued waves of the virus will yield further disruption, aggravation, redefinition, and return*.

In a VUCA world, businesses across the world are scrambling to salvage what they can and move forward in the face of unparalleled uncertainty. Contemporary scholarship about entrepreneurial uncertainty is dominated by two main ideas: *effectuation* and *causation* (Read, Song and Smit 2009). The effectuation research argues that entrepreneurs acknowledge uncertainties and adapt to them by controlling their means. By contrast, research with a causal orientation asserts that entrepreneurs make efforts to reduce uncertainties through information acquisition or planning techniques. Although entrepreneurs are thought to use both types of logic in their efforts to transcend uncertainty, this book will focus on the latter approach, namely *reducing information asymmetries through planning techniques*.

Hence, the central claim of the book is that the critical success factors of survival and uncertainty are a continued drive for *innovation (Chapter 2), sound cash management (Chapter 3), fraud prevention and detection (Chapter 4), and robust corporate governance (Chapter 5). A separate appendix has been added, which details the financial reporting implications of the fallout from COVID-19.* ***(NB: All statistics regarding COVID-19 such as death rates or from the fallout of the pandemic for example government spending were correct as at December 2020.)***

CHAPTER 2

Innovation 101

As discussed in Chapter 1, businesses across the world face an economic upheaval, referred to as a Pompeii Event (PE), unique in our history and which continues to cause mass structural changes. Consequently, consumers are wary of spending their hard-earned cash, particularly on non-necessities and luxuries, especially those people who have lost their jobs. These are indeed challenging times for businesses, but also an opportunity to explore new business models.

As the global economy continues to reopen, business leaders will need to examine and change their business models accordingly to accommodate social distancing until vaccines have been fully rolled out and rapid-result COVID-19 testing is universally available. This will adversely affect a large constituent of the economy, especially where people are in close vicinity—such as in schools, universities, restaurants, and airlines.

Manufacturing businesses that are actively engaged in the fight against COVID-19 by producing personal protective equipment (PPE) such as face masks have seen demand for their products dramatically increase, while other enterprising entrepreneurs recognized an opportunity to convert their manufacturing facilities into the production of these products. Even in the hospitality industry, which has been severely affected by the pandemic, some restaurants that have been ordered to close their dining room services, have pivoted to kerb-side take-outs and delivery services. Many other businesses may need to change to survive. These are examples of innovation, which is even more crucial if not a critical success or survival factor during a Pompeii Event and will be explored in greater depth.

What Is Innovation?

According to the Merriam Webster dictionary, the meaning of innovation is:

"a new idea, method, or device; the introduction of something new."

Thus, innovation is usually associated with the application of superior solutions that can satisfy new, or existing, or unknown requirements. Innovation occurs through the supply of newer, if not more effective, products, services, processes, and technologies that are made accessible by innovators to stakeholders, including markets, governments, and society at large. Innovation is not the same as invention because innovation is the practical application of the invention. The legendary management guru Peter Drucker maintained that without innovation, organizations would age and decline.

Most of the research on creativity and innovation emphasizes the requirement for time and effort for creative thought, the cycle of failure and triumphs, and the implementation of innovation. *On the other hand, in the current crisis, time is a luxury as people are losing their lives and businesses are teetering close to the edge or are already finished*. As already documented, the pandemic continues to pose great challenges to the global economy as well as people's daily lives and will have severe consequences beyond the spread of the disease. However, a crisis is a strong driver of creativity and innovation, as witnessed in the Second World War when manufacturing plants were converted successfully to meet the needs of the war effort. It is already apparent that creativity and innovation are emerging at the national, institutional, organizational, and individual levels within the countries affected by COVID-19; for example, Journeyman Distillery in Three Oaks, Michigan, has pivoted from making whiskey to producing hand sanitizer during the current crisis.

Innovation Economics

Innovation economics (IE) is a recent branch of economics that clearly emphasizes innovation, including the investigation of technology, knowledge, and entrepreneurship. IE attempts to understand where new ideas come from and how policies can be constructed that will actively facilitate the expansion of intellectual capital or new ways of thinking.

Consequently, as countries across the world transition from an industrial model of production toward a knowledge-based economy, IE becomes not only increasingly relevant but extremely important.

In this section, a description of the key theory in the field of innovation, namely *Schumpeter's 1953 innovation theory of trade cycle*, will be made and will conclude with some modern theories. It is important to note that reality is highly complex; thus, any theory is a simplification of reality, as it is built on assumptions, which attempts to better understand this reality. Consequently, theories are always incomplete and subject to criticism and revision.

Joseph Schumpeter believed trade cycles to be the product of innovation activity undertaken by entrepreneurs in a competitive or capitalist economy. He argued that trade cycles are an intrinsic part of the process of economic growth of a capitalist system. Schumpeter developed his model or theory of the trade cycle as comprising of two distinct stages.

The first stage discusses the initial influence of the innovation that entrepreneurs introduce into their production processes. *The second stage* accrues because of the reactions of competitors because of the early effect of the innovation.

In Schumpeter's world it is assumed that the economy is at equilibrium where all the factors of production (land, labor, capital) are fully employed. Every firm is producing efficiently with average costs equal to price, product prices are equal to both average and marginal costs; hence, profits are zero or breakeven. There is no net saving and no net investment. Schumpeter refers to this equilibrium state of the economy as a *circular flow* of economic activity that merely repeats over and over, analogous to the circulation of blood in an animal organism.

However, the circular flow of economic activity becomes agitated when an entrepreneur successfully executes an innovation. Schumpeter argued that the major function of an entrepreneur is the pursuit of innovation activity that results in real *profit*, not changes to margins. He also stated that innovation is comprised of:

(a) Introducing a new product
(b) Embracing a new technique of production
(c) Unlocking a new market

(d) Securing a new source of raw materials or semimanufactured goods
(e) Altering production processes within a firm

Innovations are commercially viable applications of inventions by entrepreneurs.

Schumpeter argued that an entrepreneur is an extraordinary (wo)man possessing exceptional skills that allow him or her to introduce something *new* to the existing economic system. It is important to note that he or she is not a capitalist, rather a strategic coordinator who can marshal the required hard cash for presenting his or her leading innovation.

Introducing an innovation marks a start of the business cycle, as the entrepreneur manages to attract resources away from other established industries; both prices and investment increase. As the innovation leads to greater production, the circular flow in the economy rises, supply exceeds demand, and there is disequilibrium in the economic system.

The economic system experiences a wave of expansion referred to as the *primary wave*. This primary wave leads to a *secondary wave* of growth caused by the impact of the original innovation on the firm's competitors. As the original innovation is demonstrated to be profitable, other entrepreneurs follow suit in *swarm-like clusters*. The original innovation creates further innovation in related products, resulting in an upsurge in prices and profitability. The economic system experiences a multiplier effect or cumulative expansion of economic activity. As the purchasing power of consumers increases, even the demand for the products of the noninnovative industries increases, and their prices and profits also rise, that is, there is a wave of expansion across the entire economy.

On the other hand, the cycle of prosperity wanes as *new* products resulting from previous waves of innovations supplant older versions whose production begins to contract as their prices and profitability are reduced. There will be a period of reflation, uncertainty, and disinvestment, as risk increases and depression sets in, causing widespread bankruptcies, company liquidations, and the collapse of markets. Crucially, innovation stops, but the economy cannot continue in depression, as innovation-oriented entrepreneurs continue their quest for profitable innovations and the natural forces of recovery ensure a revival. Falling aggregate consumption has a restorative impact, as the depletion of inventories will need to be replenished. This sparks fresh investment, and audacious entrepreneurs will start innovation again, and so, another trade cycle begins.

The major criticisms of Schumpeter's (1953) innovation theory of trade cycle are:

- It is argued that the Schumpeter's business cycles are rooted more in sociological factors than in economic factors.
- Schumpeter's theory is like *overinvestment theory*; it differs only with respect to the cause of variation in investment when the economy is in a stable equilibrium.
- It is maintained that like other theories of the business cycle, Schumpeter's theory also ignores other factors that cause fluctuations in the economic activities such as the rate of interest. Innovation is not the primary factor, rather is one of many factors that cause fluctuations in the economy.

Despite these flaws, Schumpeter's innovation theory of trade cycle is widely respected and is used to determine the economic fluctuations and underscores the importance of innovation in modern economies. Three cutting-edge models of innovation, which may be useful in the current Pompeii Event, will now be outlined.

1. *Jobs to Be Done*

This innovation model was created by Tony Ulwick, which gravitates around the concept that rather than considering what characteristics or advantages a customer would want to purchase, an innovation should instead try to discover what job or activity or outcome a customer is trying to complete, and then, produce a solution accordingly.

It is regarded as a powerful tool as it allows companies to develop an offering that a customer can *hire* to undertake their function. For example, accountants could *hire* Excel worksheets to perform a specific activity such as the preparation of a set of financial statements.

The jobs to be done framework enables organizations to gain valuable insights from people regarding the issues that they are encountering. By investigating the workflow and communicating with workers, it may be possible to find an innovative solution, resulting in a product that could do the whole *job,* and therefore make it much more attractive to a customer.

2. Ten Types of Innovation

The ten types of innovation is a framework for appraising the spectrum of innovations a company is currently utilizing. It is based on robust research of more than 2,000 innovation projects by renowned innovation consultancy Doblin, which discovered that there are ten distinct methods that a company can use to innovate:

1. *Profit model*: How you produce money
2. *Network:* How you link with others to generate value
3. *Structure:* How to coordinate and align your human capital and assets
4. *Process:* How you use established or better methods to do your work
5. *Product performance:* How you develop unique features and practicality
6. *Product system:* How you craft matching products and services
7. *Service:* How you sustain and augment the value of your offerings
8. *Channel:* How you supply your offerings to customers and users
9. *Brand:* How you symbolize your offerings and business
10. *Customer experience:* How you nurture convincing interactions

The research clearly highlighted the influence of companies trying more than one type of innovation. Although most companies innovate by enhancing the performance of their product (no. 5), those companies that attempted to add value by innovating in multiple ways were regularly more successful, and it was found to be more probable that their innovations would make a positive return on investment and crucially stock market returns.

The ten types of innovation framework gives an excellent foundation for evaluating whether there are further ways that a company could try to add value or considering other methods to tackle a challenge such as using the different approaches mentioned in the list. Undoubtedly, it is a very powerful tool or lens for a company to use to assess its current portfolio of innovation projects because it will highlight potential gaps internally and externally, which may be exploited.

3. *Effective Brainstorming*

Brainstorming or *a group discussion to produce ideas or resolve problems or challenges* is known the world over and used in most organizations. However, it is highly ineffectual in generating solutions. The technique was introduced by Alex Osborn, a real-life *Mad Man* in the 1950s. Brainstorming is based on four premises: (a) spawn as many ideas as possible, (b) rank imaginative or original ideas, (c) merge and distil the ideas created, and (d) refrain from disapproval during the activity. This process must be relaxed and amorphous and supported on two questionable psychological premises, namely that the presence of co-workers can enhance performance and quantity leads to quality.

Osborn notoriously claimed that brainstorming should improve creative performance by 50%, rather than when people are working independently of each other. On the other hand, decades of scientific research suggests there is immaterial evidence for the idea that brainstorming generates greater or superior ideas than the same number of individuals would produce when working independently of each other. A vast body of evidence suggests that brainstorming may damage creative performance, resulting in a collective performance regression, which is the antithesis of synergy.

However, there have been recent and significant breakthroughs in understanding how teams collectively create ideas, which has led to the generation of far more suitable brainstorming techniques such as *brain-netting*, which are highly relevant in the current Pompeii Event characterized by social distancing and remote working.

Virtual teams were all the rage before the pandemic, but now they are the norm across all industries. The evolution of e-mail and collaboration tools such as Zoom make remote working almost seamless, but what happens when a team needs to mutually brainstorm in real time?

Ideas could be pitched through e-mail, but then it becomes challenging to archive those ideas for future reference. It is important to create a central location online where team members can cooperate, for example, using a cloud-based document storage or an online collaboration tool such as google.docs. There are also off-the-shelf brainstorming tools that can facilitate a greater visual and collaborative experience. Another brain-netting exercise for groups utilizes an online mind-mapping tool to answer highly structured questions or divergent ideas from the main problem.

Developed in 1992, the *stepladder technique* is another highly effective brainstorming technique that encourages every member in the team to contribute individually before being influenced by everyone else and can be conducted virtually.

The session starts with the facilitator or chair sharing the topic or question or issue with the entire team. Once the topic is shared, everyone leaves the room, except two members of the team. These two members will then deliberate the topic at hand and share their ideas. Then, one further member is added to the group who will contribute his or her ideas *before* the other two discuss theirs. This cycle is repeated until everyone from the original group is in the room. The power of this technique is that it thwarts groupthink in teams where one or two members may be highly influential over the rest of the group. This technique enables shy participants to express their ideas without feeling intimidated.

The stepladder technique is useful for medium-sized groups ranging from 5 to 15 people. Once the group gets larger, however, it takes much longer and may become unwieldy.

The Importance of Innovation

In one short year, the COVID-19 pandemic has thrown the world into chaos and unchartered waters. At the start of the crisis, to protect human life on a grand scale, nations completely shut down, with most instituting quarantine, travel restrictions, and requiring nonessential workers to stay at home. This obligated organizations and workers in the public and private sector, almost overnight, to pivot their presence, productivity, and partnerships, as this Pompeii Event unfolded. Thankfully, technology has allowed hundreds of millions of people, across the globe, to remain linked, and above all, healthy.

It is important to note that spectacular digital innovation in the last 20 years, including cloud computing, artificial intelligence (AI), and the growth of machine learning, has successfully allowed major stakeholders in the world such as businesses, governments, health care, students, and workers to adjust to the turmoil of the disorder caused by the pandemic.

The technologies that have allowed the world to remain connected are the result of many years (decades in the case of the Internet) of creative imagination, leadership, world-class knowhow, determination, colossal risk, major investment in research and development (R&D), robust intellectual property protections, and affordable licensing. Since 2000, the American giant Verizon Wireless has invested approximately $116Bn into building its U.S.-wide network and pledged to invest a further $17Bn in network improvements for the foreseeable future. A notable case is Wi-Fi, and its latest innovation version 6.0, which is set to deliver almost triple download speeds, facilitate the greater spread of connected devices in the home and at work and related data consumption. This will be important in the unfolding pandemic or Pompeii Event, including the expected spikes and waves of the virus, as it will allow locked-up families and workers to stay better connected, continue functioning, and stay calm because of superior user experience underpinned by Wi-Fi 6.0's greater bandwidth. As already witnessed, the load on Wi-Fi during lockdowns or localized lockdowns substantially increased; hence, the ability to connect to a wireless network rather than a home-based Wi-Fi network is extremely beneficial.

Team-working software such as Microsoft Teams and Zoom have proved to be highly useful and have saved businesses as they scrambled to reconnect in the aftermath of this Pompeii Event. These technological innovations, including video conferencing, have enabled remote teams to function normally to ensure a steady workflow and viable projects, such as audit assignments. Organizations that were more technologically savvy and ahead of the curve have transitioned into the *new normal* more smoothly and less stressfully. However, even slow adopters, who will have endured many shock waves, have been sustained through much online goodwill and support with even software vendors offering free support.

Specific innovations that will allow, help, counter, and ultimately quell, the current pandemic are drones and robots underpinned by AI, and they are being utilized to deliver supplies, particularly to remote areas, with increasing scale and scope. The Internet of Things, supported by a vast network of CCTV cameras and smart connected sensors, has come of age in this Pompeii Event, as it can help maintain social distancing rules. In addition, data science, cloud computing, machine learning, and AI are all contributing to track, trace, crucially predict, and ultimately terminate the ongoing spread of COVID-19.

Without the discussed technologies, it would have been very challenging, if not impossible, to adapt so quickly and relatively smoothly (in the developed world) with potentially much higher mortality rates. Past investments coupled with strong Intellectual Property (IP) in consistent networks, the cloud and superior microchips have not only borne fruit but ensured seamless working and educational opportunities, which will also yield a much-needed vaccine sooner rather later.

All this underscores just how vital it is to preserve and reward continued investment in innovation. However, the question is *how to innovate* in a crisis or Pompeii Event.

Innovating During a Pompeii Event

Contingency planning (CP) is the most common approach for preparing an organization to manage a crisis. A CP is a reasonable preparation tool for situations in which enough of the future can be foreseen to facilitate a plan. However, this approach fails during a Pompeii Event, such as the current COVID-19 pandemic, as it is impractical, if not impossible, to execute. For example, what CP could businesses and government agencies have undertaken after the recent, August 4, 2020, 1.1 kiloton bomb blast in Beirut (considered to be one-tenth of a nuclear explosion), resulting in 190 deaths, 6,500 injuries, $15Bn in property damage, and leaving an estimated 300,000 people homeless?

It is apparent that a generic or off-the-shelf approach cannot be adopted in a Pompeii Event. By contrast, with events with a sufficiently high likelihood of occurrence such as a cyber-attack, it is possible to build-in proactive protection such as holding inventory or building in redundancies. However, this protection becomes useless during a Pompeii Event, as the latter become unfeasible and uneconomical as businesses scramble to survive.

The only alternative to CP during a Pompeii Event is *crisis management* to ensure a superior innovation trajectory that is underpinned by speed, adaptability, open channels of communication, and encouraging informal networks. As a Pompeii Event requires crisis management and rapid innovation, this could be viewed as a special case of innovation management. Hence, standard economic theory that purports to understand innovation, including agency theory and theory of contracts, becomes redundant.

It is argued that innovation under these exceptional circumstances or a Pompeii Event can be enhanced by exploiting *communities of practice* (CoP) where individual and social expertise is leveraged to produce useful products and services. This is established practice across the international tech sector; for example, Apple uses CoP to respond to customer needs and produces innovative products such as the iPhone. CoP should be adopted by all organizations, regardless of sector, size, and type; even start-ups that can get extensive support from local colleges and universities. *Why*?

Problem-solving in a crisis or a Pompeii Event setting is often collaborative and immensely stressful. An example is the well-documented (and Hollywood dramatization) case of the Apollo 13 engineers who brainstormed and crafted a safe passage back to earth for their astronaut colleagues.

A ground-breaking empirical study of the Broadway industry, which is comprised of many apparently disparate elements such as directors, producers, and performers, which operate in networks to produce innovative musicals. The major finding was that the likelihood of success strongly correlates with the degree of clustering. In addition, it is contended that diverse or cross-functional teams are more likely to find optimal solutions.

For example, Mercedes in 1997 had to manage the recall crisis of its A-Class car, and the team was made up of safety engineers, logistics, marketing, and public relations (PR) experts. Therefore, it is possible to find innovative solutions during a crisis that are supported by diverse cross-sectional teams. This approach improves communication, cooperation, capacity, culture, and reduces information asymmetries, which could prove to be lethal. In fact, research on knowledge networks suggests that organizations that have fewer than average cross-unit relationships are unlikely to effectively respond to an unexpected crisis or a Pompeii Event. Even those organizations that cannot afford the luxury of cross-sectional teams during a crisis or a Pompeii Event can adopt a very simple heuristic, namely "do what most of your neighborhood is doing" to ensure an accurate, fast, error-tolerant, and scalable innovation.

A detailed consideration of what may be considered the optimal approach to innovation during a Pompeii Event, namely the *frugal framework,* will be made, with proven examples of best practice, which should serve as a guide and inspiration for many organizations.

The "Frugal Approach" for Successful Innovation During a Pompeii Event

This Pompeii Event has necessitated exceptional responses from across the world; such has been the swiftness and brutality of the virus. Most countries have had to circumvent the luxury of following the traditional innovation processes of testing and trialing new technologies, processes, and medicines. Lack of time and resources available to respond to the crisis, including rapid scaling, has led to an explosion of responses. For example, China constructed a 1,000-bed hospital in merely 10 days, and distilleries across the world have pivoted to supply millions of liters of hand sanitizer.

All major stakeholders, including multinational companies, leading universities, G20 nations, and influential nonprofit-making organizations, have risen to the challenge of this Pompeii Event. Consequently, early research emanating from universities and health agencies in China helped the rest of the world to understand the impact of COVID-19, and scientific endeavors deepen to find a vaccine. Rapid testing kits to detect the virus were produced in a matter of weeks, including Alibaba's machine learning image detection model, which purportedly detects COVID-19 in only 15 seconds.

Company supply chains have rapidly adjusted in a way reminiscent of the Second World War, when factories were re-engineered to build war supplies. Thus, for example, the luxury goods company LVMH has successfully converted its perfume factory to produce hand sanitizer for France's health care sector, and Taiwanese electronics giant Foxconn is producing face masks. Major designer labels have temporarily switched from chic evening gowns to medical gowns, and carmakers are producing ventilators on a mass scale to satisfy global demand.

Engineers are skillfully using three-dimensional (3D) printers to create PPE, such as plastic shields for health care workers, relatively cheaply, and en-masse. This is making supply chains resilient, as suppliers can source locally and quickly. To capitalize on this sudden change, HP has accelerated its *3D as a service* business model innovation; thus, customers only need to pay for what they print. The moral of the story is that digital transformation of industries has not suffered a hiatus during this crisis.

To keep the global economy functioning as smoothly as possible, supermarkets and logistics services have created safety protocols to protect their employees and customers. Educators across all levels have created effective online classrooms and implemented fresh pedagogical techniques. It appears that data science has come of age as a global information resource in order to educate the public and track the spread of the pandemic. Big Data, including brilliant visualizations, has mushroomed, apparently overnight, notably Johns Hopkins Coronavirus Resource Center—https://coronavirus.jhu.edu/map.html—which shows the somewhat frightening global extent of the pandemic.

It is commonly acknowledged that globalization has helped spread the virus, but cocreation with others across the world is helping solve this crisis, bolstered by the Internet that is facilitating collaboration initiatives. For example, experts across the world are proactively providing open access to research findings on the virus. The Irish Open Source Ventilator community has been collaborating with engineers, designers, and medical practitioners globally, to develop low-cost, open-source ventilator designs.

All this highlights, *frugal innovation (FI)*—more for less, maximum and high impact, being innovative, and being creative in the face of tight constraints and the abyss. FI has long been the mainstay of lesser developed countries, enabling developments such as the African mobile money transfer innovation MPESA and the Bangladeshi ground-breaking microcredit Grameen initiative. This approach to innovation does not mean poor quality, rather the best solution given the status quo. As already illustrated, FI will only work if it is underpinned by any of the four *Rs: research, re-engineering, recycling, and rapidity*, see Figure 2.1.

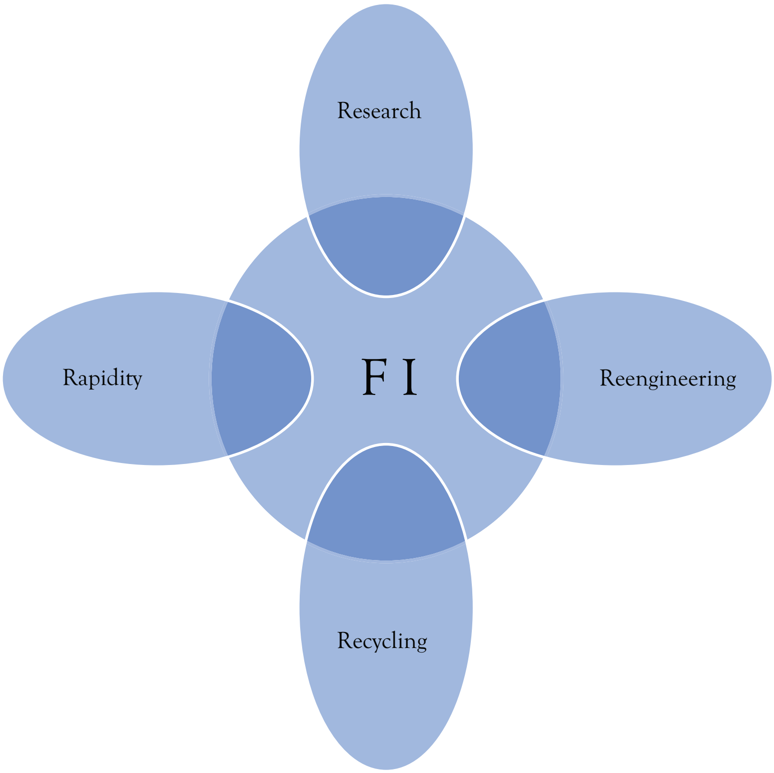

Figure 2.1 4 Rs of successful frugal innovation

The following are practical innovations that strongly highlight 4R features, Table 2.1.

Necessity is the mother of innovation, and human beings can be resourceful, especially in a crisis and by conjuring up frugal solutions. However, it is vital to suspend, albeit temporarily, high regulatory standards, in order to quickly address new demands at minimal cost. This Pompeii Event has deeply shaken leadership teams into action while hastening trends already underway such as home working. This is undoubtedly creating new opportunities that visionary leaders, regardless of sector and size, can capture and exploit. By operating differently, empowering workers across all pay grades with the scope to innovate rapidly and grab opportunities ahead of competitors, these leaders will further extend their lead or become market leaders.

Table 2.1 4R features

Innovation	Characteristics	FI—*R*	Scaling Trajectory
Virtual ecosystem: https://coronavirus.startupblink.com/	StartupBlink has developed a coronavirus innovation map to highlight enterprises created in response to the COVID-19 crisis.	Research	Open source thus scaling not an issue and will lead to collaborations and even more scaling.
Open source and portably designed ventilators	OxVent has re-engineered ventilators to utilize and repurpose 90% off-the-shelf parts.	Reengineering	Open source allows distributed and bespoke manufacturing. Portability ensures simplicity, value-for-money, and ramping up of production and distribution.
PPE: Masks and visors	A4 acetate that is normally used for overhead projector presentations can be transformed into a simple face mask that covers the face and the neck.	Recycling	Simple, cheap, and mass production is no problem, especially in the developing world where PPE remains problematic.
Workflow in health care systems	Lean management techniques can be used, including in ICUs, to ensure fast, wider care is provided to a maximum number of patients, particularly in this pandemic or Pompeii Event. These techniques have been successfully used in the Indian health care system so that surgeons have become more productive than their Western counterparts.	Rapidity	This has been successfully adopted across China and in temporary *nightingale hospitals* in the UK that can hold up to 4,000 patients.

Looking beyond this Pompeii Event, innovation may become permanently disrupted because the physical barrier to cooperation posed by social distancing has been mitigated via online digital tools. In fact, it is argued that the pandemic is causing the most effective innovation sharing and collaborative creation of new knowledge. This is all possible through social media, coupled with data science, that is allowing the instantaneous sharing of local, regional, and national experiences agilely, promptly, and without borders. This will ultimately better equip humanity for the next Pompeii Event and improve the lot of humanity in general.

In short, the biggest lesson for innovators from this Pompeii Event is that they can potentially *learn from everyone, innovate for everyone, and the only standard is their imagination.* The next chapter will discuss how to ensure stable cash flow, which will underpin any drive for *innovation*.

CHAPTER 3

Cash Flow Management 101

Introduction

This Pompeii Event is teaching us many new lessons. The pandemic has brought us to our knees, crippling economies, destroying families, and robbing individuals of their health and life. Although a spark of hope has been reignited with news of a vaccine, the reality of life remains somber, with borders remaining shut or with limited access, travelers subjected to quarantine and other restrictions, struggling businesses (although some have enjoyed growth and innovation), immobile humans stuck at home with limited area of travel, suffocated by the constant wearing of masks, and other restrictions to fight the curve. As already argued, the full impact of this pandemic on businesses and supply chains will continue to be disastrous as this Pompeii Event continues to unfold.

The aviation industry has been particularly badly hit, even with the plethora of government bailouts and other credit arrangements. This is hardly surprising because countries around the world have closed their borders with limited air travel. Hong Kong's Cathay Pacific will reportedly be cutting 8,500 jobs. Malaysia Airlines and Air Asia have also faced severe liquidity issues and are reverting to their shareholders and exploring alternative financing to remain afloat. Even billionaires such as Sir Richard Branson are asking for government bailouts.

Thus, the authors will attempt to understand the cash flow challenges resulting from this Pompeii Event, initially from a theoretical perspective and then offer concrete advice to mitigate this unprecedented crisis. Thus, regardless of size, sector, or specialism, the bottom line is that *Cash is King*.

Analysis of the Pompeii Event From a Cash Perspective

Pre the pandemic and Pompeii Event, the hallmark of the 2019 globalized economy, especially for manufacturing companies, was long supply chains. The logic for this phenomenon was that some countries have cheaper production costs, and so it was more profitable to purchase the parts or materials in a cheaper geographic location. This resulted in goods produced in cheaper locations, based on a number of assumptions that have been ripped to shreds by COVID-19; costs are lower in the other location, logistics are inexpensive, and the cash wrapped up in the long supply chain is cheap and available.

However, the pandemic has severely disrupted these assumptions due to hard lockdowns coupled with social distancing across the world. The theory of financial contagion provides a framework to assess the implications of both the spread of the pandemic and its impact on the global financial system. It is important to acknowledge that financial and biological contagions are interrelated, which mirrors the interconnected global environment, thus allowing a proper risk assessment and response to the COVID-19 pandemic (Peckham 2013). Consequently, the *New Normal* is here to stay, with further changes expected. Hitt et al. (2020) argue that the New Normal is unlikely to be a static equilibrium because the pandemic shock or Pompeii Event has triggered other unforeseen dynamics, which will be widespread even after the pandemic eases such as continued remote working. Furthermore, long-term strategic changes will be required to navigate the new competitive landscape marked by technological, socio-political, and institutional changes emerging from the new environment.

Although the sudden eruption of the pandemic was unexpected, it is remarkable to observe that most of the global corporate world was not prepared to face the socioeconomic fallout from COVID-19. It could be argued that there should have been corporate governance, risk management, and crisis management practices already in place to start dealing with this Pompeii Event. The question is why these mitigation strategies failed at the outset of coronavirus, given that many companies quickly adopted digital platforms such as Zoom and Microsoft Teams in order to communicate and keep the *show on the road*.

One possible explanation that could explain the poor response to the Pompeii Event is the typical corporate tick-box mindset that merely focuses on regulatory compliance and bottom line profits. The Pompeii Event has exposed weaknesses in the normal business environment such as a lack of agility and violated the usual governance expectations in accordance with legitimacy and resource-based theories. Consequently, the companies, regardless of size or sector, were not ready to deal with the sudden evaporation of hard cash due to hard lockdowns and social distancing. The horror of this Pompeii Event can be summed up in the adage "show me the money—the battle of the healthiest cash flow." This has only strengthened the belief of the authors that for too long, cash has been taken for granted.

Unfortunately, the predominate focus has always been on the profit motive, regardless of the status quo of liquidity or cash, and this situation is only exacerbated in cases of accounting fraud. This phenomenon is explored in greater detail in the next chapter where a consideration will be made as to whether companies ever learn their lessons.

As the current Pompeii Event continues to send wave upon wave of challenges, it is advisable for the preservation of hard cash for at least one year, or even longer, to ensure survival, let alone growth. The situation is so uncertain such that nobody can accurately anticipate consumer demand for the foreseeable future, which is heavily dependent on social distancing and further lockdowns; although, the breakthroughs in finding vaccines will help. The business liquidity situation is so dire that as on November 5 the UK Office for National Statistics (2020) reported that 42 percent of businesses surveyed had less than six months cash reserve, 21 percent were unsure, and 3 percent stated they had none, with only 34 percent noting that they had more than six months of cash in reserve.

On the other hand, it is not all bad news for everyone. For example, one of the author's local grocery vendors had reported an immediate increase in business and crucially cash. Movement restrictions had made his cash business a vital source of supplies, and even when the restrictions were lifted, the owner-manager had made enough money to invest in further property. Thus, the big lesson is that the local business traders will have an edge over the large out-of-town shopping centers in the short term or at least until the national populations have been significantly inoculated from the virus. Similarly, there have been many other businesses that have also reported an increase in demand, especially those with online platforms such as Amazon, and companies focused on providing basic necessities or enterprises, with sufficient diversification and innovation (as extensively discussed in Chapter 2).

As news of a vaccine for the deadly virus spread, there was a rebound in many international markets and economies, with a potential for a much discussed *bounce back recovery*. For example, the Australian Bureau of Statistics stated that in November 2020, 24 percent of companies had reported an increase in revenue compared with 16 percent in October 2020, and 22 percent of businesses had reported capital expenditure plans for the next three months. The U.S. Bureau of Economic Analysis also reported an increase in the annual rate of the real gross domestic product by 33.1 percent in the third quarter of 2020. Hence, businesses across the globe are becoming increasingly bullish, expecting a global recovery. However, this should be predicated on sound planning and contingency plans, as there is already confirmation of mutations of COVID-19.

This Pompeii Event has made the authors very philosophical, as they have been forced, along with millions of other citizens across the world, to use personal protective equipment (PPE), including the use of face masks, and this has become a metaphor for human and business survival. However, air and cash are taken for granted, and both are imperative for human and business survival.

Capital Structuring in a Pompeii Event

The authors believe that as the pandemic continues, even as the vaccine is being administered across the globe, there will be a lag effect, which will impact the financial structure of companies. Although bank credit is relatively cheap and plentiful, there will be competition for funds.

According to the pecking order theory, firms prefer internal financing compared to external funding, and if they embark on external funding, the firm would prefer debt rather than equity. It is argued that firms fall into certain financing patterns or habits that have no material effect on firm value. Thus, the current pandemic environment could potentially have significant, if not momentous, repercussions for company structure. Investors remain edgy about prospects postpandemic, which explains wild swings across global capital markets, and they may not want to invest unless a higher return can be promised, which automatically increases the cost of capital.

Consequently, alternate sources of finance such as crowdfunding become attractive. However, owner-managers, managers, and boards must acknowledge that consumer perceptions and trends play an important function in the way the firm continues to progress, including the availability and accessibility of the sources of funds that it will rely upon. This mirrors the legitimacy theory and resource-based theory. The former helps to understand the organization's behavior in implementing, developing, and communicating its social responsibility policies. The major assumption of the *legitimacy theory* is satisfying the organization's social contract, which allows the recognition of its objectives. The *resource-based theory* posits that firms own *resources*, a subset of which allow them to achieve competitive advantage, and a further subset that leads to enhanced long-term performance. It is argued that *resources* that are valuable and exceptional can lead to the creation of competitive advantage, thus highlighting the importance of planning, budgeting, and strategy even during a Pompeii Event.

Cash Flow and the Environmental Future: Key Questions

COVID-19 has revealed the utmost vulnerabilities of human beings. It is surprising to note how an invisible virus essentially brought global trade and supply chains to a grinding halt. Some argued that this pandemic is the *revenge of mother earth* and a tipping point has been passed where climate change is irreversible. Most airlines are forecasting that passenger levels may return to prepandemic levels in 2024. Consequently, the domino effect on other industries will be substantial, extremely costly, and will ultimately affect global purchasing power.

What does this have to do with cash flow, especially when survival is the primary objective and corporate social responsibility appears to be a distant memory?

The answer is that this Pompeii Event is throwing out all manner of opportunities that will potentially impact cash and long-term sustainable models of business or value creation. The prestigious IBM Research Insights titled *Meet the 2020 Consumers Driving Change* report suggests that 60 percent of consumers surveyed were willing to change their shopping habits to reduce negative environmental influence, with 70 percent willing to pay a premium of 35 percent for brands that are sustainable and environmentally friendly. This is undoubtedly a great opportunity, if not a matter of survival, and firms need to consider diversifying products and markets and urgently consider the following questions:

- *How long can we sustain ourselves financially before considering an option to close?*
- *What can we do differently? And, how would this change our business model, cost, and most importantly, our cash flow without compromising our value for money? Can this also be linked to sustainable development?*
- *How do we manage stakeholders' expectations—internally and externally?*
- *Where can we obtain reliable market intelligence? How do we leverage this information to become more agile and lean, with faster decision making?*
- *What current financing options are no longer suitable for the New normal? What are the alternate financing methods available that can help the company tap into the green economy?*
- *And, what are our competitors doing?*

Apple may be used as a *green* benchmark. On July 30, 2020, Apple announced its third quarter results for the fiscal year 2020. It posted an 11 percent increase in revenue compared to the previous year, 18 percent increase in quarterly earnings per diluted shares, declaring a cash dividend of $0.82 per share of the company's common stock, approved a four-for-one stock split while generating an *operating cash flow of $16.3Bn* during the quarter and is crucially still on track in terms of their new $100M Racial Equity and Justice Initiative and their commitment to being carbon neutral by 2030.

It is argued that information and digitalization will be the key drivers or assets that will enable businesses to effectively plan. Indeed, keeping track of changes and statistics will potentially be a daily occurrence, as this Pompeii Event plays out. The next section identifies options, strategies, and the way forward.

Cash Flow in the Pompeii Event

Many businesses have acknowledged that their cash flow management needs an overhaul and been left wanting in the face of the pandemic. Theoretically, it can be argued "How hard can it be to put together the cash coming in, the cash going out, and balancing the rest?"

Fundamentally, cash flow management is simply about cash inflows and outflows and managing the surplus and deficits accordingly. However, in a cash-strapped scenario, the traditional debt and equity funding can be difficult to access and is usually expensive.

Across the globe, governments have put in place a raft of bailouts or stimulus packages; however, there is no bottomless pit of cash, and this is financed through higher direct or indirect taxes. Consequently, these measures are not feasible in the long run and merely *economic band-aids* that are designed for short-term respite. In fact, government bailouts and programs may not be the best solution. A survey of over 500 businesses by the British Chamber of Commerce and TSB Bank found that most companies that took advantage of government backed debt such as the Bounce Back loan program and Coronavirus Business Interruption Loan Scheme during the Pompeii Event, feared it would damage their future prospects. The banking industry estimates that £35Bn of COVID-19 debt was potentially unsustainable, with 250,000 companies at risk of collapsing, putting three million jobs at risk.

Initially, short-term solutions can be considered. The authors argue that this Pompeii Event may, in fact, be an opportunity to explore alternative sources of finance and rebuilding more sustainable and resilient companies and by extension economies. This can be achieved by redirecting finance into new forms of investments with the help of regulators, governments, and multilateral institutions, working in partnership with innovative private firms.

Short-Term Solution: Smash Grab Go

At the time of writing, operational budgets are being ripped up as companies across the globe attempt to adapt to the *New Normal*. The adage *Cash is King* has never felt truer, and even at the best of times, managing liquidity is an art, not a science. So, what are businesses supposed to do?

The formula for survival is simple—simultaneously *smash, grab, and go* (Sheikh 2020), see Figure 3.1.

Smash fixed costs, especially rent as homeworking is becoming the norm; vendor solutions, such as Microsoft Teams, are successfully allowing collaborative working and above all protecting the key asset; the company's employees. Deloitte, which employs 19,000 people in the UK, has decided not to renew leases on 4 of its 50 UK offices, to reduce its need for expensive property leases while instituting a remote working environment for about 500 employees and in the process converting fixed costs into variable costs (or completely removing them). This approach will make business more agile and allow it to operate, albeit in the short term (may be medium term), around the breakeven point.

Similarly, revisit the organization's capital investment plans and assess those that are crucial and those that can be delayed, but which will probably require renegotiation. It is important to remember, every cent or penny saved is going to be useful somewhere, so negotiate! Defer any nonessential spending as soon as possible, especially if the country

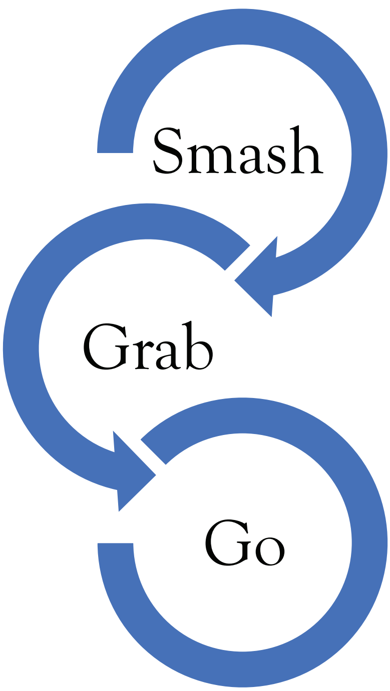

Figure 3.1 Smash, grab, go

in which the business operates does not have a strong recovery plan or pattern and the cases of COVID-19 are high or rising. Avoid embarking on a cost-cutting frenzy such as wages at the risk of compromising future value creation or reputation. However, some businesses in this Pompeii Event will be forced to make redundancies such as Danone who, in November 2020, reported that it would be cutting up to 2,000 jobs aiming for $1.2Bn in savings.

It is important to acknowledge that businesses operate in different environments because of the given industry, and the approach will vary accordingly. Thus, a multinational or trading business will need to consider the different phases of recovery, government policies, and volatile foreign exchange differences among many other factors that could influence the supply chain. However, everything can be contained if a proper plan and strategy are in place. Consideration can be made of the following (translated) Latin phrase:

"To win a war quickly takes long preparation"

Grab receivables by the scruff of the neck; now is the time to send legal notices to those nasty and loss-making *90 day-ers*. Even if they are big high-street brands, *name and shame* them and post a list of them on social media so that they stop taking advantage. If the situation is dire, then consider factoring, but ensure that the customers are creditworthy. *Grab* that slow-moving or problematic inventory, take a deep breath, and sell it. The company's working capital position will improve and will be in a better position to secure further lines of credit or renegotiate terms.

Go after the customers, forget the financial backers such as the lenders, because they stuck with you through thick and thin and religiously bought the company's products and/or services and importantly bought into the company's vision. Talk to the company's most valued customers rather than knee-jerk price slashing or deep discounting. The American Saks Fifth Avenue faced this challenge during the 2001 recession and undertook deep price cuts that temporarily enhanced revenues, but ultimately dented its luxury status for many long-time customers.

Singapore Airlines has been hit hard because it only flies international routes. The airline has converted two Airbus A380 serving fine-dining meals across the different cabin classes with prices varying from $37 to

$441. It was interesting to note that the seats were snapped up within half an hour of bookings opening, with more on the waiting list.

If the "customer is right, then the market must be right" (Sheikh 2020); thus, create a range of offerings such as deluxe, standard, and budget or recalibrate product offerings without jeopardizing quality or consistency and crucially hard-won customer loyalty. The American car insurer Progressive Corp discovered how sensitive policyholders were to reimbursement delays relating to written-off vehicles. They cut the payment cycle by 35 percent and witnessed customer loyalty shoot up by 50 percent. The hotel industry has been severely affected, but they have recalibrated. Some chains have rolled out their w*ork-from-hotel* packages catering to individual needs by providing not just workspaces but access to their meeting spaces, mail and courier services, printing facilities, free flow of beverages, and some, with even childcare and entertainment.

Another point is the possibility for firms to reach out on their Business Interruption Insurance, which may cover the damages from COVID-19 fallout. However, there has been a mixed acceptance of whether the Business Interruption Insurance provides coverage due to COVID-19, and it may be worthwhile investing in a specialist insurance lawyer to make your insurer accountable.

Nuts and Bolts Maintenance: Working Capital Position and Dashboards

The traditional way of managing cash flow revolves around managing the firm's working capital—the big three "accounts receivable, accounts payable and inventory." Managing these three components seamlessly and even ruthlessly can immeasurably enhance a business and can save a business during the current Pompeii Event. Taking a disciplined approach to invoices and payment receipts will ensure liquidity and where to focus as the pandemic continues to unfold. Although it is tempting to empathize with an established receivable account that is under pressure, this may not be advisable if the company is also experiencing a financial quagmire. Consequently, keep costs under control and prudent credit management underpinned by manageable discounts, rather than credit extensions, and this should ensure timely receipts and be a warning signal if the situation begins to deteriorate. If things are desperate, companies can seek immediate, but expensive, relief by factoring receivables, which the authors believe will become an important finance option for many businesses over the next 18 months until the vaccine and boosters have been fully rolled out.

Similarly, inventory management is essential in the current climate supported by considering any discounts offered that could benefit the company in the short to medium term. However, this will need to be balanced with demand and the present state of cash flow. This may be the right time to consider the just-in-time business philosophy where zero inventory is held on site, thus saving associated costs such as storage. However, this is a complex business approach that requires careful planning, as it relies heavily on trusted relationships between a satellite of suppliers and Kaizen or continuous improvement. Hence, a new corporate culture may be required that could exacerbate the already volatile situation.

Monitoring vital ratios, such as days payable outstanding, days receivable outstanding, inventory turnover, and the simple, yet powerful, cash conversion cycle, may ensure liquidity and ultimately survival in the present Pompeii Event.

Undoubtedly, cash will become less plentiful; therefore, decisions will have to be reviewed, and the balance of profit and cash compared with the risks being continually evaluated. The cash conversion cycle measures the performance of a business from investing in raw materials, through the change due to manufacturing or service, through to the final product, through to finally being delivered to the customer, and payment from the customer being received. Consequently, how quickly a business can convert its investment in materials or time to collecting the cash from its customer will be crucial as the crisis continues.

These ratios will indicate how much the cash budget can be flexed. The authors argue that it may be worthwhile if the business invests in or upgrades its current accounting information system so that it generates a daily *cash dashboard.* Using a cash dashboard helps an organization to focus on what it needs to achieve as a business and is the foundation for creating a detailed action plan that will have the highest impact in the shortest possible time.

Dashboards can significantly enhance the whole business and not just the cash performance. They can also highlight where decisions must be made between balancing cash, profit, and business risk.

All over the world, banks and financial institutions are pivoting to help businesses survive and potentially prosper in this unprecedented Pompeii Event. For example, in September 2020, HSBC Singapore launched the first Receivables Finance Program for SMEs through the Singapore's Networked Trade Platform (NTP). This will expedite access to funding from between 15 minutes to one day. This convenient platform will be extremely beneficial to SMEs in terms of speed and reduced administrative costs, with the immediate benefit of another source of much needed finance.

Rather than squeezing payables or vendors, it would be better to be upfront and honest and negotiate. In the current pandemic, they too will be under pressure with cash flow constraints and attempting to balance their books. The worst-case scenario would be a breakdown of trust, and a *cash on demand* situation is not good for anyone as it will damage longer-term working relationships. It will be advantageous to attempt to work out something that is mutually beneficial across the supply chain,

There continue to be regulatory and health and safety costs that need to be factored into all cash decisions and management decision making. Most governments have imposed restrictions such as social distancing, registering of customers, and temperature checks, which will negatively impact store footfall. Otherwise, organizations will face fines and penalties that will damage cash flow. For example, Chicago's Department of Business Affairs and Consumer Protection planned to proactively investigate retail stores during the festive season to ensure compliance with capacity limits and other COVID-19 regulatory requirements, noncompliance carries a penalty up to $10,000 for violations.

The airline industry has been badly hit even with government bailouts and other credit arrangements. This is hardly surprising because countries around the world have closed their borders with limited air travel. In October 2020, there were many reports of job cuts to reduce losses. Many of the airlines have also retired certain fleets and have carried out several rounds of reducing the employee counts and salaries. Malaysia Airlines and Air Asia have also faced liquidity issues and are reverting to their shareholders and other financing means to remain afloat. Air Asia is also shutting down its Japan operations and is also rumored to be considering an exit from Australasia. However, some of the airlines are working hard to sustain themselves in innovative ways. As already noted, Singapore Airlines has a creative and alternate use of its fleets. Air Asia Berhad has also jumped onto the digital wallet bandwagon with *The BIG* initiative, and Air Asia Health offers end-to-end medical services via a digital platform.

Hence, disruption is all around the world. It is crucial to identify the way forward, incorporate change management to become lean and agile, and to achieve this, accessibility to various sources of funds and stringent cash flow management has become more important than ever.

Cash Flow Management—Beyond the Pompeii Event

Going forward, in the face of the pandemic, cash flow must be considered a companywide issue, rather than merely the responsibility of the finance function. Consequently, this will require management buy in and should become a key performance indicator (KPI) across the organization not just linked to the chief finance officer's (CFO's) performance-based compensation. This will require a change of culture and clear communication, such as a weekly situation report, outlining what superfluous expenditure has been cut or changes in procurement policy have been made. This will require a proactive synchronization of the financial and business strategy.

Just like any other strategies, cash flow management strategies should be embedded in budgetary and forecasting practices, with a clear focus to establish, communicate, and implement these practices across the enterprise. Given the current pandemic situation, a short-term rolling budget will be the best technique, incorporating a *beyond budgeting (BB) mindset*. BB is based on *four factors:* governance and transparency, creating accountable teams, goals and rewards, and planning and control. BB can be summed up in the following, Table 3.1 Beyond budgeting.

As will be noted from the table, the critical success factors in this approach are decentralization and empowerment of all staff in the organization, which is vital in the face of the pandemic and crucially postpandemic. Thus, using relative targets through benchmarking will encourage employees to enhance their own performance. Continuously readdressing plans empowers employees to think about value creation or cost savings (i.e., improved cash flow), rather than achieving set numbers within the budget. Using on-demand allocation of resources, for example, on-demand printing in the publishing industry, rather than allocating for the year ahead, reduces costs and ultimately improves cash flow.

Another excellent and highly recommended technique for this Pompeii Event is *zero-based budgeting*, which is a simple yet powerful reassessment tool for each budget line item and helps justify its value. This forces businesses to make timely and informed decisions, especially with redundant projects or products and loss-making divisions. In contrast to this, incremental budgeting is based on the past and on out-of-date practices, with little, if any, justification.

Table 3.1 Beyond budgeting

Governance and transparency	
1. Values	Commit people to a shared cause; not a central plan—for example, improve cash flow
2. Governance	Govern via shared principles and robust judgment; not detailed rules and regulations
3. Transparency	Make information accessible and transparent; do not limit and control
Accountable teams	
4. Teams	Organize around a smooth network of accountable teams; not centralized roles
5. Trust	Trust teams to control their performance; avoid micro-management
6. Accountability	Based on universal criteria and peer reviews; not on hierarchical relationships that breed favoritism
Goals and rewards	
7. Goals	Encourage teams to set challenging goals; do not transform goals into fixed contracts or milestones
8. Rewards	Base rewards on performance; not on fixed KPIs
Planning and control	
9. Planning	Planning must be a continuous and inclusive process; not dictated from the top, down the organization
10. Coordination	Coordinate connections or relationships enthusiastically; not via annual budgets
11. Resources	Make resources available just in time; not just in case, as this saves costs
12. Controls	These should be frequent with feedback loops; avoid budget variances, as they breed mistrust

Source: Adapted by authors

Going back to basics as an approach is a solid technique and is based on the worst-case scenario, which is not having any revenue at all. This concentrates thinking and what would to be done in the next crisis or Pompeii Event. This plan should be documented and periodically revised to ensure validity and current accuracy.

It is important that companies consider their breakeven point (the point at which there is no profit or loss) in both unit and currency amounts and consider the *range of desperation* when there is no other option but to call it quits (hopefully, this will not be an option if proper strategies and plans are executed).

Buy Now Pay Later. A Digital Disruption and Cash Flow Savior?

COVID-19 has disrupted markets and customer preferences, creating a greater need for to embed technology and digital innovation into businesses. IBM's U.S. Retail Index reports that the pandemic has accelerated the shift from physical to digital shopping by an estimated five years. Department stores are expected to see a decrease of 60 percent at least over the entire year, with e-commerce expected to grow by 20 percent in 2020. This digital disruption is not just limited to the retail sector but will encompass every sector of national economies and the global economy.

The pandemic has forced customers online, due to lockdowns and social distancing, and coupled with growing unemployment there has been a fall in purchasing power and growing personal debt. However, the growing fintech business model known as *Buy Now Pay Later (BNPL)* has become a cash flow savior for some companies.

BNPL allows customers the option of taking home goods today and paying for them by a specific date in the future, without suffering any interest. If the repayments are made in full by the final day of the deal, the customer only pays the receipt price, but can crucially either spread the payments or make a one-off payment at a later date. These schemes are run by retailers themselves, while others use secondary payment platforms that charge between 2 and 8 percent of the sale.

According to the Office for National Statistics, more than half of UK young adults aged between 22 and 29 do not have any savings. A UK survey from *Compare the Market* found that BNPL schemes had been used by approximately 10 million UK adults within the past year. Consequently, BNPL should be explored by all businesses in the current pandemic, as the market for allowing customers to take home essential purchases in the here and now, without having the necessary monies to pay for them immediately. It is considered that this payment method will grow over time.

In the United States, more than a third of all adult consumers have successfully utilized a BNPL scheme, with the 35 to 44 age group being the most likely to use such services. Microsoft has also set their sights on BNPL, and in September 2020, announced that customers would be able to finance the new Xbox, with a recommended retail price of $499, in monthly, with interest-free payments through a partnership with payment service provider Klarna and Citizen's Bank.

The major attraction of BNPL schemes is that they are interest-free. However, customers should be aware that late payments will incur fees, lump-sum interest, or other charges, depending on the terms and conditions of the provider. The duration and conditions of the payment scheme will differ depending on the retailer or provider. Some allow for payments as and when the customer has the funds and the balance is settled by the end of the contract. Others ask for periodic repayment amounts, such as weekly, until the balance is fully honored. BNPL schemes can run for any timeframe from 30 days to a year or even longer.

Another significant feature of BNPL schemes is they often only require a soft credit check. Thus, a provider will only search for bankruptcy or debt agreements and confirm the customer details, but crucially the search will not count toward a credit score. This trend is set to increase as people lose their jobs during this Pompeii Event. Hence, customers with a poor credit rating may not qualify, but the search will not negatively affect their credit rating. A benefit of using BNPL schemes regularly and paying the full balance within the stated timeframe is that it can help boost a customer credit score, allowing them to borrow more. This will also benefit by helping the economic recovery.

This fintech innovation needs to be actively pursued by all businesses in the current climate, as it will significantly improve company cash flow as BNPL vendors forward monies immediately, and nonpayment or bad debts become nonexistent. This all positively impacts liquidity, including payables and inventory management. In addition, it is also recommended that businesses consider omni-channel fulfillment capabilities, including, but not limited to, *buy online and pickup in store* or to have an expanded shipment from store service.

A major concern for some organizations would include issues pertaining to logistics and supply chain impacting their businesses, especially if there are lockdowns or different phases of COVID-19 recovery. Fortunately, there are many logistics and transport companies that also provide services to ensure e-commerce, such as Geodis My Parcel. However, it is imperative to check if there are any movement restrictions in delivery to geographical locations experiencing local lockdowns or perhaps the business may want to consider having mini fulfillment centers if there is a consistent demand in those locations.

Walmart is one such company that has incorporated many of the aforementioned in the face of this Pompeii Event. In the early stages of the COVID-19 pandemic, Walmart was credited with its ability to thrive during the initial months of the crisis. Walmart's robust e-commerce platform coupled with an agile business model ensured its operating costs remained under control. Walmart is a model omni-channel retailer with a delivery service to fulfill online customer orders within two hours and with mini fulfillment centers. Walmart has also been positive and confident about its end-of-year projection and growth, especially with respect to the Christmas season. (It was interesting to note that Walmart's reported cash and cash equivalents had increased from $8,606,000 as on October 31, 2019 to $16,906,000 as on July 31, 2020).

Another example is Home Choice International PLC (HCL), an investment holding company with interests in retail and financial services. HCL was incorporated in Malta, listed on the Johannesburg Stock Exchange, and based primarily in South Africa with expanding operations in Mauritius, with a vision "to offer innovative retail and financial services products to the growing African middle class through digital platforms." HCL has stood out for its consistent focus on the female mass market for more than 30 years, an omni-channel retailer and has rapidly growing digital channels for both its retail and financial arms.

HCL is known to utilize their customer data combined with data science and analytics to better understand their customer preferences.

Apart from empowering women with its digital inclusivity strategy, HCL is also using that same data to understand the financial and credit requirements for these women to provide more accessible and a quicker response to their needs. In its interim presentation, in June 2020, the approach to data and leveraging that information resulted in an increase from 19 to 39 percent for their *Homechoice—Retail* and from 85 to 90 percent for their *Finchoice—Financial*. Capital expenditure dropped from R71M to R56M, and the net debt to equity ratio for June 2020 was 10.5 percent as compared to 18.1 percent in June 2019. The lockdown strategies integrated with their sustainable value creation targeted at empowering women resulted in a cash balance of R379M as of June 2020 in comparison to a balance of R121M in June 2019.

Sustainable Finance and Cash Flow Opportunities in the COVID-19 or Pompeii Event

Early in the pandemic, COVID-19 was viewed as the *great leveler*, affecting rich and poor equally. On the other hand, it has become evident that COVID-19 is the *great divider*, exasperating the multitude of structural inequities between wealthier and poorer nations and ultimately people, leading to calls for social justice. The authors believe that the opportunities to construct competitive advantage and to marshal private capital to help assist in the recovery and aid growth, from this horrendous Pompeii Event, make it essential to keep up the impetus in this area.

Unquestionably, decisions made under the current circumstances, as the pandemic continues to rage with the recent announcement of further mutations (December 2020), could influence the real economy and financial ecosystem for many years down the road. Thus, there is a sense of urgency to *get it right* by a variety of stakeholders, beginning with business that can ultimately improve their bottom line and become cash-resilient.

Initially, it is important to define what sustainable development is, as it underpins the notion of sustainable finance. The renowned 1987 Brundtland Commission defined sustainable development as a development that meets the needs of the present without compromising the ability of future generations to meet their own needs. This has been grouped into three elements: *environment, social, and economic***.** The global multilateral institutions have pushed the sustainable agenda further with 17 interlinked Sustainable Development Goals designed to achieve a more sustainable future for all by 2030. This has been complemented by a push to link this to sustainable finance, which has been taken up by financial and nonfinancial institutions internationally.

Sustainable finance has been defined as any form of financial service that integrates *environmental, social, and governance (ESG)* considerations into investment and lending decisions. Differentiating between sustainable debt and equities, each portfolio has its own advantages and disadvantages. The sustainable debt market includes green, social, and sustainability bonds and loans that finances projects with positive environmental and/or social benefits, as well as debt securities that react to the sustainability performance of the borrower.

The sustainable equity portfolio includes ESG or socially responsible investment equity and/or bonds for which ESG factors have been integrated into the investment process. Although it may seem that these financing innovations are inclined toward climate footprints and de-carbonization (Paris Agreement), it could also motivate active stewardship among shareholders.

Several sources have reported that the onset of the COVID-19 pandemic has accelerated an increase of interest in sustainable finance, especially because ESG funds have outperformed their non-ESG equivalents, suggesting that companies that address sustainability are more resilient during periods of market turmoil, and that ESG performance had a high or moderate impact on the cost of capital depending on firm type. There are many other avenues for ESG funds, grants, and financing options that can be accessed by businesses around the world. Hence, it is important for businesses to pick up on these opportunities to move ahead. A growing body of research highlights a positive correlation between ESG and performance, although there is a need to identify KPIs from overall trends. This helps in gaining an appreciation for emergent socioeconomic features that drive investment performance, and ultimately inform risk and volatility evaluations.

It may appear that the SDGs and possibly sustainable finance are complex and more aligned toward big multinationals; however, it does not need to be overwhelming and could be appropriate for other types of organizations, regardless of size. It is more important to ensure a collective and integrated business model that could contribute positively to any of the said goals and unleashing financial opportunities at the same time.

Earlier in 2020, HSBC launched Singapore's first Green Loan for SMEs to further encourage the involvement of SMEs in sustainability projects. In 2019, the European Union established a €10Bn Innovation Fund to focus on highly innovative technologies that can bring about significant reductions in carbon emissions. However, only projects that are mature in their planning and business model could apply for up to 60 percent of additional costs in the form of flexible grants.

Although green bond issuance has diminished since the outbreak of COVID-19, offerings of sustainability and social bonds have risen. For example, in 2019/2020, the Institute of International Finance reported recent monthly volumes in excess of $7Bn in social bond issuances, in comparison with a monthly average of $1.2Bn in 2018/2019, and with the potential for further sustained growth.

Philips and Pfizer are among the big corporate players that have issued sustainability bonds, both in excess of $1Bn that will channel some of the monies to COVID-19 responses, while governments and development banks across the globe have been issuing specific COVID-19 bonds to help confront the fallout due to the pandemic.

It is interesting to note that the Bank of America, MSCI, Morningstar, and HSBC, as ESG leaders, have recently highlighted key benchmarks and have performed better than those companies with worse ESG profiles. Consequently, those with superior ESG ratings were much less volatile and are crucially less risky.

There is a pressure on organizations to consider social factors in relation to how corporations are addressing the needs of workers, customers, and suppliers. The 2020 Black Lives Matter movement has bolstered the need for companies to re-evaluate their behavior toward British Black, Asian, and Minority Ethnic (BAME) stakeholder groups. How they are reacting to these social issues will have consequences for ensuring trust and the bolstering of their brands, which could alter the ESG risk profile faced by the financial services industry.

This all indicates that COVID-19 has led to a shift from green finance by itself, to an approach that strongly favors the *S* or Social. This is supported by the 2020 UN Environmental Program report entitled: *Implications of the COVID-19 Pandemic for Global Sustainable Finance: An Initial Framework for Response Strategies* and discusses the *drive for ESG alpha*, given the *surge of focus on social issues*. Furthermore, while it is too early to tell what the long-term impacts of this increased focus may be, there is potential for a major *repricing* of social issues in ESG ratings, and going forward, this may motivate efforts to strengthen the coherence of ESG ratings information.

In fact, it can be argued that the report believes the future will be an amalgam of economic, social, and environmental health issues, not just a reaction to and revival from the pandemic "strengthen resilience not only of the financial system, but of the economy, society, and environment."

In short, it should be clear that the adage Cash is King will remain the guiding principle in the coming months and the medium term until the global roll out of the COVID-19 vaccine achieves a tipping point. The authors used various theoretical frameworks to understand the implications for cash flow in the face of this Pompeii Event. Consequently, immediate, *nuts and bolts* and long-term solutions predicated on agility, fin-tech, and the ESG future were offered as ways of surviving and creating long-term value for all stakeholders. It is apparent that the nexus of finance and the environment is here to stay, and this may be the resetting of capitalism in general or alternative futures such as the progressive utilization theory (Prout). This is an integrated socioeconomic system that purports to enable both people and the planet to flourish.

The authors now move onto explore the phenomenon of fraud in the next chapter, which is a direct threat to cash flow and will severely undermine any recovery from this vicious Pompeii Event, COVID-19, and the resulting economic depression that has become a fertile ground for the factors that encourage fraud and which will persist for months, and if left unchecked, for years to come.

CHAPTER 4

Fraud 101

In the wake of this Pompeii Event, governments across the world are borrowing tens of billions of dollars in order to satisfy spending needs, as tax receipts have plummeted. National gross domestic products (GDPs) are deteriorating, and unemployment rates are sky rocketing. Millions of workers are working from home due to hard and soft lockdowns and are social distancing, which has also disrupted local and global supply chains. The result is a fertile ground for fraudulent activity. For example, in December 2020, in America, two owners of New York pharmacies were charged in a $30M COVID-19 health care fraud and money laundering case, due to exploiting Medicare rules that were intended to help patients obtain access to essential COVID-19 medications.

Although imperfect, the most appropriate theory to understand why fraud occurs is Cressey's (1953) *The Fraud Triangle,* which argues three conditions are necessary, namely *pressure*, *opportunity,* and *rationalization*, see Figure 4.1 for the perpetration of any type of fraud. The analogy of starting a fire is a good way to visualize why a fraud occurs. Pressure is the *source of heat for the fire*, opportunity as the *fuel that keeps the fire going*, and rationalization as *oxygen that keeps the fire burning*.

The principal factor contributing to an increase is pressure from the economic fallout due to the unfolding pandemic. As workers lose their jobs or are overworked, they will be tempted to look for internal control weaknesses and rationalize any fraudulent activity such as embezzlement due to mounting bills such as mortgage payments. Consequently, the Fraud Triangle is amplified in a downturn and even more so in a Pompeii Event. An exploration of how to deal with the menace of fraud will now be made.

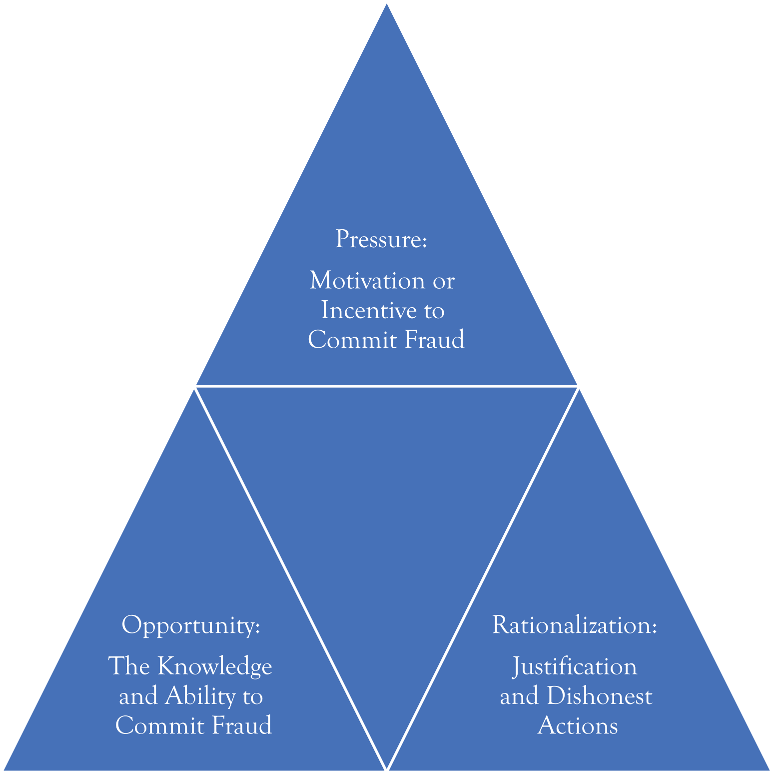

Figure 4.1 The Fraud Triangle by Donald R. Cressey (1953)

Source: Adapted by authors

The Menace of Fraud and What to Do

Everyday life in general needs money, and everyone who handles money needs basic numeracy skills. For example, when buying or selling something, the money is followed; when dinner is made and a recipe may be followed, which means that the chef is in touch with weights and measures, and employed people need to be aware of what they earn and what taxes they pay. Unfortunately, life is full of some people trying to take advantage of others. Individuals are reasonably good at spotting fraud because no one likes to be cheated. So rather than saying "everyone is an accountant," which sounds a bit dull, the authors argue that "everyone is a Fraud Detective."

The latest research shows that the true cost of fraud on society, on organizations, and on lives is continuously rising. Measured as a percentage of turnover, some researchers put the figure as high as 10 percent. Experiences since the appearance of COVID-19 suggest that the figure is not going down.

Similarly, international organizations, such as the UN and the OECD, typically put the global cost of corruption (and fraud) at around 5 percent of GDP. According to professional bodies, institutes of auditors, fraud examiners, and other research bodies, if the same consideration is given to companies, the figure is between 3 to 7 percent of sales (e.g. in sectors such as the construction industry). The Chartered Institute of Management Accountants put the cost of financial crime at over 6 percent of GDP. It is not purely money but also the costs of damage to reputation, the organizational culture, and all those *problems down the line*, which can, in fact, be measured.

The cost of fraud and cost of stopping it spiraling out of control in this Pompeii Event will inevitably lead to a stark COVID-19 credit crunch. Consequently, it is argued by the authors that this may be an ideal time to rethink if not shake-up how fraud is dealt with and undertake something that really works: *to spot it and stop it before it spreads.*

The cruel irony of the year 2020 is that it has resulted in so-called *20-20 vision* or a moment to stop and reflect upon the behavior and actions of individuals, and as a collective, the human race. It is apparent that some of the things that were done in the past were unnecessary and wrong such as "jumping on planes all the time for meetings which would last an hour" and "crowding together allowing the spread of diseases." On the other hand, COVID-19 is an opportunity that can stimulate new insights and fresh ideas on how to eradicate all that unnecessary waste.

The authors suggest that whether one is a board member, manager, or an employee working in an organization, everyone can play a valuable role in defending the organization against the threat of fraud.

Consequently, every organization can:

- Raise its efforts to identify early warning signs where the organization is losing money to fraudsters as well as greedy suppliers, middlemen, and customers.

- Motivate and educate *everybody* around the organization to help guard against and spot attempted fraud before it spreads, thus saving money, which is already a precious commodity in this Pompeii Event (see Chapter 3).
- Revolutionize the way fraud is investigated by taking charge internally; look for effective and fast resolutions and avoid investigations becoming dramatic and spinning out of control and deal with fraud with both *passion and compassion***.**

The authors contend that each reader is a fraud detective, and at the end of this chapter, the reader will have an opportunity to take an online test to discover what type of fraud detective they are. Fraud detective DNA may lead toward the transactional, intuitive, technocratic or holistic quadrants.

It is worthwhile posing the rather provocative question: "Are accountants and auditors actually boring?" Monty Python and its famous *vocational guidance counselor* sketch seems to think so. In this sketch, a chartered accountant who wants to become a lion tamer instead is told by the counselor that the results of his personality tests describe him as dull, unimaginative, timid, spineless, easily dominated and humorless, exactly the right qualities to be a chartered accountant. *It is an iconic sketch, but is that really the sort of people accountants are, or has a society made them that way? Are these people the fraud detectives who could be the saviors of society?*

The authors have in their almost 100 years of combined professional experience, seen many frauds and can be summarized as follows:

- Fraud is one of the oldest habits in the world going back thousands of years, and even with the advent of computers, to many aspects of business in the 1980s, not much has changed. The Fraud Triangle holds true, and bending the rules for a benefit and rationalizing why that is acceptable is part of human nature.
- Fraudsters are so desperate to make money and not get caught that they engage in a type of *corporate bullying*, which is destructive not only for all those who try to stand up to them, but also all those around them who do not want to take part.

- The consequences of fraud, deception, and fraudulent behavior are deep. This includes false reporting, use of stolen goods, slave labor, black market sales for cash, major tax evasion, and even environmental damage.
- There are a plethora of new rules and regulations thus it is fair to ask why are auditors and fraud specialists so inept at identifying fraud. The question provides a clue to the answer, and the authors argue that people are drowning in so many rules that the spirit of these rules has been lost. Consequently, people may have abdicated their responsibility for fraud detection and deterrence to the experts.

The authors believe it is time to simplify the way that fraud is discussed, so that every stakeholder is educated with fraud awareness and empowered to play a part in seeing it and stopping it. This will also contribute to a much needed financial and emotional resilience in the months and years to come.

No one likes to be cheated, fooled, or deceived. Arguably one of the most popular film and drama genres is crime, the hero being the detective, be it Sherlock Holmes, Miss Marple, or a modern-day version. It can be observed that the detective is the defender of those who were deceived and wronged, and perhaps many would like to transform into a Sherlock Holmes.

The authors reiterate that as most people handle money and are accounting for it, they are accountants to some extent, and as they do not like to be cheated, they are also *fraud detectives***.** Here are some examples:

Example 1

> Someone is having dinner with a friend and they are presented with the bill. Upon inspection, it is apparent that an unordered dessert and a 25 percent service charge, which was not made clear at the start of the meal, have been added to the bill.

More than likely, most customers would question the bill and request a quiet word with the manager, but there would be no ruckus.

Example 2

> Someone is having some repair and renovation work undertaken by their regular builder who is an ardent follower of the *reduce—reuse—recycle mantra*. However, the bill itemized costs include:
>
> | | |
> |---|---|
> | Cement and plaster | $1,000 |
> | Admin charge for plumbing (20 percent) | $ 200 |
> | Tools | $ 524 |

Most people would challenge the 20 percent admin mark up as it appears that they are being taken advantage of and query the tools bill, as it would be assumed that the builder should already possess them for the job in hand.

Example 3

> In the current COVID-19 crisis, a struggling student finds much needed work through a job agency. Upon receipt of the first paycheck, it becomes clear that they have been overpaid as the correct tax and insurance deductions have not been undertaken. They believe that they are honest citizens and call up the agency who categorically state that the deductions have been correctly processed, and it is up to them to make a further declaration if they believe that they have been overpaid. What should the struggling student do as they are potentially becoming involved in fraud?

The everyday examples highlight that most people do not want to be cheated or deceived, especially when it is their own money. If the analogy is extended, most people would not like their loved ones to be defrauded. Should people be not concerned if their workplace, regardless of size and sector, is being potentially defrauded?

Defining Fraud

Over the years, the word *fraud* has been overcomplicated. In the 1980s, it meant "someone who obtained a benefit by deception," and since then, many academics and specialists have considered the phenomenon of fraud, if the reader looks for a fraud definition on the Internet, they will find many pages. For example, a professional anti-fraud body has renamed *theft* (which is a part of fraud) as *asset misappropriation*. Even calling *fraud*, *white-collar crime* adds to the ambiguity.

The following is a useful current definition used by the authors:

"Anything deliberate and dishonest (or unethical), done by anyone, external or internal which removes value, destroys reputation and culture of an organization or person."

Most people who undertake fraud know what they are doing, although there is a well-supported theory that states it is hard for the perpetrator to realize when they have crossed the line. When it comes to what is dishonest or unethical, one is immediately into a subjective or gray zone. Eventually, everyone needs to make up their own mind as to what constitutes dishonest or unethical.

The authors make a distinction between external and internal fraud because they argue that for many years, the most common and rather narrow perception of fraud has been that insiders are stealing from an organization, usually taking high personal risks for relatively low rewards. On the other hand, a much larger group of potential external fraudsters such as greedy suppliers, unethical customers, middlemen, agents, consultants, hackers and organized criminals are taking relatively lower risks for rather higher rewards.

For example, one of the authors vividly remembers during an audit assignment that he was summoned to an emergency meeting with the client. The client rather bemusedly asked why he had been billed for $500 for *consulting work* when all he had was a short telephone conversation with the engagement partner.

There are always exceptions to the rule as some people get involved with fraud due to uncontrollable factors, and others are pathological criminals, and include:

- The person who committed fraud because they were already conditioned and were *part of a fraudulent culture.*
- The "I deserve it" or *license to bill* people. The employee or consultant who has *an overdeveloped sense of entitlement*.

- And, *the corporate psychopath*, a rather nasty person who gets pleasure out of hurting people and glorifying themselves in the process.

Using the preceding definition, an attempt has been made to list seven basic types of fraud, which will be prevalent in the current Pompeii Event:

1. *Greedy suppliers:* This ranges from small-scale fraud such as shops and builders that try to overcharge, major suppliers and contractors who factor in large overcharges, and all other sorts of fraud where suppliers pay bribes, use illegal labor, deliver poor quality, and put lives at risk.
2. *Customers who take unfair advantage:* This includes everything from customers who do not pay or deliberately go bankrupt before paying, to customers who want bribes.
3. *Unnecessary middlemen:* Agents, consultants, and advisors who are providing an unnecessary service that may be illegal.
4. *Dirty money:* This could be transactions with complex *front* companies located in tax havens who usually have obscure or offshore bank accounts. In the commercial world, this is common and ranges from tax evasion, to companies that want to conceal their identity and owners behind shell companies.
5. *False figures:* This is usually in the domain of *accounting or creative accounting* where costs may be underreported, and revenues overstated.
6. *Insiders:* Where employees (including senior management) engage in deceptive, unethical or illegal activities. At its most simple, this could be straightforward theft where someone is acting alone, but it could also be much bigger and involve suppliers, customers, dirty money, and middlemen.
7. *Outsiders:* Attempts by information technology (IT) hackers and cyber fraudsters who are attempting phishing, man-in-the-middle attacks, fake websites, and ransomware. Attempts can also be made by other opportunists, organized criminals, and even competitors; in short, any outsider who is trying to unfairly take advantage. Although cybercrime is constantly in the media, one interesting

observation, when considering incidents over the past year, is that the attacks appear to be more seem *robotic* in nature, suggesting the nexus of artificial intelligence (AI) and machine learning algorithms.

The preceding *seven basic types of fraud* are not meant to be exhaustive, and organizations in the current pandemic should be vigilant for a variation or multipronged attack consisting of any combination of the seven. Apart from cyber fraud, the rest of the frauds have been undertaken for centuries.

Why does fraud persist? The authors believe, the major reasons, garnered through their collective experience and research are, in descending order:

10. *People overcomplicate matters:* For example, the Association of Certified Fraud Examiners (one of the many professional fraud bodies) has a subcategory for fraud called "Asset Misappropriation." Why not just call it *theft*?
9. Fraud is considered a *developing country's phenomenon:* The authors argue that Westerners have allowed themselves to falsely believe that corruption and fraud happen mostly in poorer nations, such as in parts of Africa, Asia, and South America, or pariah states such as North Korea. Observers are dazzled by the *corruption perception index*, which portrays many affluent rich countries as low-corruption zones. That might be correct, but the problem is that in a country where the perceived costs of corruption are approximately 25 percent of GDP compared to one where the perceived costs of GDP are approximately 3 percent, it must be considered that 3 percent of GDP per capita in an affluent country, is much more than 25 percent of GDP per capita in a poor country.
8. *Dependency on computers:* People have become lazy and believe that robots with AI using *big data* will find fraud. Robots and AI have their place, especially when humans are still in control, but fraud is still so human that it needs humans to find it because humans are quirky and unpredictable. One of the authors was recently contacted by someone who had been told by his bank that they

no longer wanted him as a customer because their AI robot had detected his voice, making calls to the bank's voice activated system to remove money from other accounts. However hard he tried to protest that this was *not him*, the bank's fraud officer insisted that the *robot never makes mistakes*. In attempting to clear up the mistake, he informed his employer who promptly suspended him, and for several months felt that his life had become, as he described it, a "Kafkaesque universe." In the end, with some help from CIFAS, the UK fraud prevention authority, enough pressure was put on the bank to re-examine its *robot fraud detector*, and when they finally investigated, they found that it had *made a mistake*.

7. *Zero tolerance*: Having a *zero tolerance* policy toward fraud, in principle, is proper; however, all human beings are imperfect. Everyone has probably crossed the unethical line, albeit as small as accepting extra change from a cashier, but that does not mean that all people are fraudsters. Consequently, if zero tolerance was applied to the latter, then almost every person would have to be locked up. The biggest error of judgment is that the more someone is boxed in and the harsher the punishment, the more they are likely to fight their corner. Many fraudsters have more than enough financial resources at their disposal in order to fight back. The authors argue that that every religion and faith preaches tolerance and, in a sense, *restorative justice* of some form. An excellent modern-day example is the late Nelson Mandela and Desmond Tutu's Truth and Reconciliation Commission, which probably saved South Africa and ultimately forced affirmed foes to reconcile and move on. Perhaps, *restorative justice* is just what fraudsters are pining for and want to actively make amends if only the thresholds to do so were lower.

6. *Dirty money that we choose to ignore:* The world is awash with dirty money, but the perpetrators are rarely brought to justice. Occasionally, there is a major breakthrough (such as the Panama Papers in 2016), but the lawyers, accountants, administrators, and sometimes governments, who are behind the shell companies, individual regulations, which keep them alive, move swiftly to make them

even more watertight. *One senior police officer, known to the authors and specializing in dirty money, stated that if regulators managed to open all the centers of dirty money and shell companies on the same day, probably every government would fall.*

5. *Obsessive compliance disorder:* Unfortunately, auditors and other *verifiers* operate in a *tick-box* or *bureaucratic* or *management by exception* world. In the literature, this is referred to as *compliance*, a profession that has mushroomed in recent years. There is compliance for everything, but in the end, authentic compliance does not exist in the world of finance and accounting. The authors argue that even an external report, where the auditors say they have been professionally skeptical, has very little value today.
4. *Someone else's problem:* While most people, even senior management, believe that fraud costs are substantial, they are reluctant to believe that it occurs in *their* organization. As a defense, some will refer to their reams of procedures and controls; whilst others tend to highlight the last audit where typically zero or very few minor frauds are reported to management. Thus, while there is plenty of fraud and corruption in the world, it is not happening on senior management's watch. Surely, when everybody thinks like this, something could be fundamentally wrong.
3. *Panicking at the last minute:* Management oscillates widely between doing nothing about fraud, leaving it to the box tickers, and mad panic when they feel that matters are out of control. The situation is usually exacerbated by sensationalist journalists and headlines. On the other hand, it has already been acknowledged that 5 percent of the GDP or sales is the approximate cost of fraud. Thus, this panic is like the way people become shocked when they notice homeless people on the streets. There is hunger and disease in certain parts of the world, but may be some people are just conditioned not to see it. The same is true of fraud, may be people have conditioned themselves to believe that fraud is not there and is *someone else's problem*.
2. *Waiting for the whistleblower:* It has become the norm, and the stark reality is that most people do not want to become a whistleblower. Based on the authors' experiences, becoming a whistleblower only

unleashes the full might of the institution, which usually exonerates the perpetrator or "sweep the mess under carpet" in order to avoid *reputational damage* and either the whistleblower is *hung out to dry* or unceremoniously leaves the organization. For example, in 2011, Michael Woodford was suddenly removed as the CEO of Olympus Corporation after exposing a major accounting fraud.

1. *A false sense of security and reliance on (for want of a better acronym)* *C^3.R.A.P^2:* Mountains of rules and regulations will not help the pandemic of fraud. Thus, *C^3 is for c*odes of *c*onduct and ***c***ompliance with these codes, in the full knowledge that hardly anyone is reading anything these days. *R is for r*isk analysis, which seems to rather ignore the risk of fraud. *A* is for external *a*udits, which, judging by how few frauds are discovered by external auditors, are completely misunderstood, and *P^2* is for 20 years of a tsunami of *p*olicies and *p*rocedures, which have become a necessary evil, but which no one ever has the time to read, *leading to many big words but little action.*

The Opportunity for Reset in This Pompeii Event

As fraud and corruption continue to spread, a revolutionary reset is needed without too much blame and shame. For example, the authors know an established investment bank, which has genuinely made the effort to turn the corner from the dark days and is following the mantra to *"rethink everything."*

If something radical is undertaken, this generation can succeed in eradicating fraud. The following are eight proposed pathways to cut out fraud and learn from years of failure.

Eight Pathways to Eradicate Fraud

Based on their professional and academic experience, the authors have crafted eight pathways, which in some way, people can utilize to make a positive contribution to the eradication of fraud. However, a stop must be made to the blame game, a halt to the nefarious gossiping, people must stop being passive bystanders and blaming others (such as auditors and accountants) for not doing enough. In fact, it is high time to stop shaming people who are involved but instead encouraging them to come out into the open.

(The authors have added several short-anonymized examples they have experienced as the pandemic continues to unfold.)

A. *All Hands on Deck*

Management should be empowering and trusting every single employee to play their role in the defense against fraud and corruption.

Depending on where a person is in their organization and the role they currently undertake the first step that is, putting ones toe in the water, to take a genuine and reflective interest. The following simple yet powerful questions can be posed: *"How would someone, external or internal, decide to defraud my organization, what would they do, and how would they get past all the checks and balances?"* This method is called *thinking like a thief*. Consider how the opposition thinks and remember that there really is an opposition out there. Then the employee will not only begin identifying fraud, but start their journey into becoming a bona-fide fraud detective.

Post-COVID-19 Example

> In March 2020, just before the lockdown, a European charity got a bad feeling about operations in one of its African field offices. No red flags had been raised in the past by external auditors, but the outgoing financial controller sent a strong warning to the chief financial officer that she should investigate. However, as travel was impossible, rather than waiting, the chief executive took charge, and in the space of a few weeks, had secured the bank account, communicated with the local staff, and made it crystal clear that head office had tightened control and were there to help. The situation calmed down and then improved dramatically. Pre-COVID, there would have been a drawn-out investigation and much

> frustration. In this case, early intervention by the chief executive demonstrated his care and matters improved.

Post-Pompeii Event, this type of agile and lean action will become commonplace and nip fraud in the bud before it blooms. As the British Transport Police slogan goes "See it, Say it, Sorted."

B. *Situational Awareness is Key*

*By thinking like a thief: It i*s a useful exercise to list out all the frauds that could be hitting an organization. This simple action will yield many avenues of investigation, which should be shared with all internal stakeholders as a genuine exercise in transparency and accountability.

Post-COVID-19 Example

> An energy company, as part of its business, was buying and selling carbon credit certificates. Knowing that there are many false certificates floating around the market, a smart financial controller had a closer look at the sales and purchase transactions to reveal a zero-sum gain, plus the fact that the trading company they were dealing with was a front company in Jersey, most probably run by organized criminals. Spotting it early enough enabled the energy company to quickly back out of the deals.

Situational awareness of fraud empowers everyone and removes the need for a whistleblower, which may be too late in the current climate. This is potentially true with detecting cyber fraud or attacks, which can be thwarted by normal people spotting unusual anomalies or patterns.

C. *Embracing Curiosity*

Curiosity usually starts with a hunch, which can become a nagging doubt, and this should be fostered by the fraud detective. This human trait can stem a potentially well-oiled fraud, and organizations ignore it at their peril. *It is proven: if someone takes an interest in what is going on, they will see or notice things.*

Post-COVID-19 Example

> The curiosity of an accountant who spotted that one customer was receiving sales invoices, which were then reversed the next year, helped put a stop to a scheme where salespeople regularly moved sales from the next year into the current year, in order to achieve their targets.

Human beings are naturally curious, and it is that curiosity that can be harnessed in the defense against fraud and corruption.

D. Being Passionate and Compassionate in Dealing With Fraud

Fraudulent behavior usually occurs because people merely slide into bad habits, for example, they get too greedy. They rationalize what they do or become part of a fraudulent culture. It is never easy to pull back, especially if the penalties for being caught are severe, and it is potentially easier to cover up the fraud. When anyone is investigating fraud, they should be mindful of the following:

- *Clearing innocent people of suspicion is one of the most important objectives.*
- *It is easy to start rumors and hard to reverse them. Avoid creating a culture or climate of blame and fear.*
- *Negative emotions such as anger and revenge are a distraction, and it is the experience of the authors that investigations, predicated by retribution rarely end well.*
- *Most people who have done bad things would like to undo them and would prefer a graceful, and if possible, honorable way back or a quiet exit.*
- *The best informants and witnesses are the perpetrators themselves. It is surprising how much people want to talk and befriend fraud detectives.*

As already noted, showing tolerance and forgiveness when looking into fraud will result in a better chance or resolving it, rather than a long drawn-out and painfully expensive investigation. It is worth mentioning that the words *truth* and *reconciliation* are also accounting terms.

E. Never Panic

Even when a fraud is uncovered, there is no need to be shocked or panic. Fraud is just a regular aspect of life, and if any of the official statistics are to be believed, it is as normal as bad weather, or the common cold. Consequently, when something that possibly looks like fraud, it probably is some form of fraud. There is an old phrase that comes to mind: "If it looks like a duck, swims like a duck, and quacks like a duck, then it probably is a duck."

Post-COVID-19 Example

> It was discovered by the chairman of a company based in country X that the management and minority owners of the subsidiary in country Y had, behind the backs of everyone, sabotaged the business, stolen assets, and were in the process of setting up a parallel business. The main perpetrator was even heard to say "I will destroy them" when talking about the mother company. But rather than panic and cause, an all-out war in a landscape which might have been hard to control, the Chairman instead put in place a strategy to save the business, staff and revenues in the short term, neutralize the threat, and ensure the long term survival and success of the subsidiary, all very calmly and without panicking.

F. Become Part of the Fraud A Team

Teamwork is essential when uncovering fraud, more so in the current pandemic when people are increasingly working remotely. Silo-mentality, protectionism, elitism, and internal rivalries need to be confined, albeit for the short term, to the dustbin, if not only for successfully rooting out fraud but also for job preservation. This attitude should also improve work culture and help people to focus on bouncing back from this Pompeii Event.

Some of the most successful football teams work together to *out-think the opposition*. Similarly, there should be an onus to "out-think the fraudsters, whoever they are."

Post-COVID-19 Example

> One of the oldest banks in Europe, where fraud previously was only talked about in hush-hush tones, transformed its culture and empowered its employees to become its eyes and ears.

G. Take Charge of Technology

Most organizations are already leveraging technology in their systems, but it is important not to let technology take control. The travel restrictions caused by COVID-19 have forced organizations to rethink how they control and monitor their operations. What has been seen is that expensive and often complicated solutions are reliant on big data and require highly trained and expensive specialists to operate them, but may not, after all, be the best way forward.

For example, universities and other bodies that administer examinations are doing so remotely, and students have undertaken them in their private rooms, where there is scope to cheat. On the other hand, smart device technology devices already owned by the students, such as mobile phones, can be successfully administered on a relatively inexpensive basis, rather than the need to install advance surveillance equipment in every student's room.

H. Stay Ahead of the Problem

This last action is extremely simple, but may be the hardest to implement because it requires major a paradigm shift in the world with considerably less reliance on whistleblowers, a reactive approach, and less drama. This mindset, coined by one of the authors, is *precrime* and is a method of keeping ahead of the fraud before it takes root.

The authors *define precrime fraud* as: "The capability to detect, contain and remove fraud before it grows and spreads." This should *not* be confused with punishing innocent persons for crimes that have not yet been committed. This approach consists of triangulating the following key variables based into a *precrime Fraud Triangle*, see Figure 4.2:

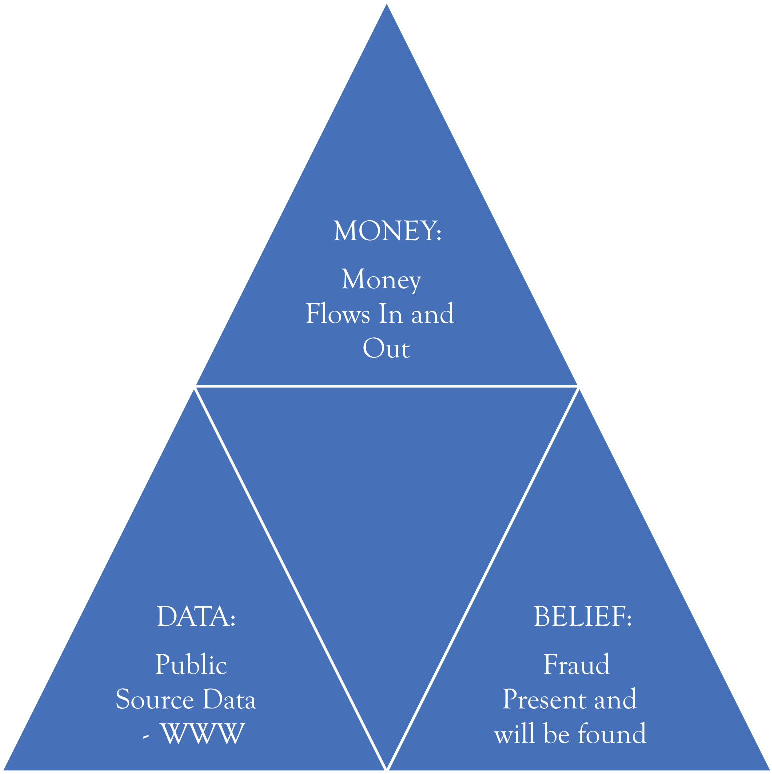

Figure 4.2 Precrime Fraud Triangle

1. *MONEY*: Identifying the key money flows in and out of any organization
2. *DATA*: Public source data (such as on places, companies, people)
3. *BELIEF*: Inherent belief that fraud is always *there to be found and removed*

In the earlier restaurant bill and builder examples, the *precrime Fraud Triangle* can be applied as the brain rapidly assimilates:

1. *MONEY*: The fact that some restaurants and builders will try to cheat customers (although people hope that will not be the case)
2. *DATA*: Customers could easily use their smartphones to check the Internet for restaurant service charges or cost of materials or surcharges that may be applicable in that location or job

3. *BELIEF*: The customer is reading their bill or invoice and its *data-stream*

Using the *precrime Fraud Triangle* will allow practitioners to quickly identify the tell-tale signs of fraud at an early stage and taking action to prevent future fraud and will lead to:

- Significantly less direct and indirect losses
- Fewer and more streamlined investigations
- Much less drama, guilt, blame, and shame for all stakeholders, including victims, management, perpetrators, as well as bystanders, and crucially a better chance of achieving *win—win* resolutions

The cost of fraud is substantial and will probably increase greatly in what are going to probably be lean financial years, as the world recovers from this Pompeii Event. Therefore, the authors believe that each one of us has an incentive to be proactive, contribute to the fight against fraud, and all become *fraud detectives*. It is time to stop thinking of fraud as frightening, shocking, or exceptional, and instead treat it as a relatively normal occurrence, even though human nature tends to block out such thoughts.

The authors firmly believe that the *precrime Fraud Triangle* is the way forward. This precrime insight is a self-belief, and courage is required to look behind the numbers for strange patterns, trusting in colleagues and gut instinct, which all dampen fraud. At a time when people need to find every way to be more effective and resilient, let there be a transformation of bad news into good news.

A question which remains to be asked, is what kind of fraud detective are you? The answer to this question will depend on who you are and how you interact with your organisation. Thus, for example if your organisation encourages empowerment of people, this will strengthen your personal fraud detective traits, encouraging you to be more holistic and crucially raise concerns. On the other hand, if the governance-culture is all about box ticking or compliance you may not be inclined to investigate further or highlight any problematic issues. Governance of organizations is the topic of the next chapter.

Fraud Test

Based on extensive research and professional experience the authors believe there are typically four key fraud detective traits, and people tend to be stronger in one, or some, of these traits. To find out more and take the Fraud Detective Challenge click on:

www.b4fraud.com

After taking the test you will receive a report describing your current: ***Transactional, Technocratic, Intuitive and Holistic Fraud Detective DNA.***

CHAPTER 5

Corporate Governance 101

What Is Corporate Governance?

For those readers who are interested in English literature and know one of the poet Philip Larkin's most famous quotes, it could be reworked for corporate governance as "Corporate Governance began in nineteen ninety-one."

Of course, it did not start in 1991, and in the second section of the chapter, it will be shown how corporate governance developed over the centuries. However, from a UK perspective, 1991 was a critical year in the development of corporate governance. In May 1991, the Financial Reporting Council, the Stock Exchange, and the accountancy profession joined together and tasked Sir Adrian Cadbury to form a committee to consider corporate governance.

It was set up to address the financial aspects of corporate governance due to concerns about financial reporting, accountability, and controversies over directors' pay. However, from such narrow beginnings, many reports have been produced, and the subject has expanded greatly. In December 1992, The Report of the Committee on the Financial Aspects of Corporate Governance and The Code of Best Practice were published, now universally known as *The Cadbury Report*. It is worth noting that while all companies and businesses need to be well run and managed, in the context of this chapter, all the discussion relates to listed companies.

Today, it is unlikely that the words corporate governance would immediately lead the knowledgeable person to think instantly about accounting or financial reporting and fraud, as will be seen in the second section of the chapter, but these were the drivers that eventually caused great concern over corporate governance. It is even possible to relate this back to the early 18th century.

The Cadbury Report came up with what has consistently remained the definitive definition and explanation of corporate governance, and this has not changed over 30 years since the report. It states:

> Corporate governance is the system by which companies are directed and controlled. Boards of directors are responsible for the governance of their companies. The shareholders' role in governance is to appoint the auditors and to satisfy themselves that an appropriate governance structure is in place (Introduction 2.5).

This quote is stated, word for word, in the introduction to the Financial Reporting Council's The UK Corporate Governance Code July 2018, the UK's latest version.

Cadbury further explained that the board's responsibilities include setting company strategy, providing leadership, supervision of management, and reporting to the shareholders on their stewardship of the company. The concept of a stewardship company, as compared to a proprietary company, is where the ownership (shareholders) is separate from the control (directors). It is worth remembering that while directors normally hold shares in the company, it is mainly not relevant under these circumstances.

While the concept of shareholders is most important in both corporate governance and in company law, the narrow view of directors only being responsible to the shareholders and only there for the benefit of the shareholders is now not the accepted position. The concept of shareholders has expanded into that of stakeholders; and directors need to consider all stakeholders. This idea has become much more prevalent over the years, and the language and categories of stakeholders has both changed and expanded.

As already noted, the growth of corporate governance is connected to financial reporting and information available to stakeholders, with financial reporting problems being one of the main drivers of the original reports. In 1975, The Accounting Standards Steering Committee, which was made up of the major professional UK accountancy bodies, produced a discussion paper entitled *The Corporate Report.* In it, they discussed users and their information needs, which is effectively a forerunner of stakeholders; they regarded users as: the equity investor group, the loan creditor group, the employee group, the analyst-adviser group, the business contact group, the government, and the public.

There are various definitions of a stakeholder, but commonly accepted is that a stakeholder is an organization or person who can affect or be affected by the policies or activities of the entity. The preceding list has been expanded over the years, and external auditors, customers, and suppliers (named individually rather than part of the more general business contact group), regulators and stock exchanges, local communities, and environmental groups can be added to the list. However, the reader may consider any listed company and decide who that company affects or is affected by, and that person or organization is then a stakeholder. In effect, there is an ever-expanding accountability of listed companies for their behavior, and that behavior is the responsibility of the directors.

In a perfect financial world, the directors of listed companies would always act such that they maximize the benefit to the stakeholders. This does not happen, and minor issues through to fully blown scandals do occur with listed companies. It is worth remembering that directors are not philanthropists, but no doubt want to benefit from being a director of a listed company. The word *pay* as used by Cadbury has now been superseded by *remuneration,* and it includes salary, bonuses, benefits, pension contributions, and shares or share options. In the perfect world, the interests of the directors would align with the interests of shareholders, managers, and the organization. This is usually known as *alignment of interests* or *goal congruence*.

As noted, much is expected of the directors, and some of the skills that they need will be discussed as the chapter progresses, but as a generality, the following practical skills are required:

- *Supervision or overseeing*
- *Control*
- *Internal regulation ensuring a sound (good quality) system of control*
- *Successful operation of the organization*
- *Interaction with shareholders*

This list was arrived at after the views of institutional shareholders were sought, and they also believe that directors must be accountable.

There are also several generally accepted concepts about the behavior of directors:

- *Fairness—To all who have an interest in the organization, effectively stakeholders*
- *Openness and transparency—There should be discussion and disclosure such that clear and reliable information is available to stakeholders such that they can judge the directors and make well informed decisions*
- *Independence—This can be achieved by the use of nonexecutive directors*
- *Honesty*
- *Responsibility—Responsible behavior with sanctions available if required*
- *Accountability—Being accountable to all stakeholders, but particularly the possibility of removal from the board if appropriate*
- *Reputation—The need to uphold the organization's reputation*
- *Judgment—Many judgments will need to be made; thus, the correct mix of experience is required*
- *Integrity—Straightforward behavior is required*

As noted, directors need to be accountable, but this is not quite as clear cut in practice, as it is in theory and as might be hoped. In the UK, both the Companies Act 2006 and The UK Corporate Governance Code July 2018 have provisions to protect stakeholders and particularly shareholders, from the excessive behavior of directors and from directors being overly remunerated. The Code states: "All directors should be subject to annual re-election." Company law provisions offer annual general meetings and voting for members (shareholders).

While there is a necessity to take care when discussing directors' remuneration, especially when considering absolute amounts of remuneration as compared to relative amounts of remuneration, it is generally accepted that compared to the average national wage, listed company directors are very well remunerated. Some directors receive eye-watering remuneration; for example, Elon Musk of Tesla earns virtually nothing by way of salary but has a 12-level agreement that could eventually end in a $55Bn payday. And Persimmon plc's CEO, Jeff Fairburn, received £38.97M in the financial year ending 2018, but the surrounding furor caused him to step down on December 31, 2018.

It is also worth considering who invests in the shares of listed companies and why. It is generally accepted that the two main reasons for investment in shares are capital appreciation and dividends. However, in recent years, corporate social responsibility (CSR) has become much more of an issue and investors also buy shares for this reason, in order to influence the behavior of major corporations.

(CSR means that a company has a responsibility to society and is a moral stance that considers ethics, respect for the individual, respect for the environment, and compliance with law.)

The investors in listed company shares run from individuals to smaller limited companies to public limited companies (PLCs) and other listed companies and institutional investors. As on March 28, 2020, Marks and Spencer Group plc (M&S) had 148,135 shareholders, of which 144,033 were described as private (97.23 percent of total shareholders, holding 8.56 percent of the issued share capital) and 4,102 were described as institutional and corporate (2.77 percent of total shareholders, holding 91.44 percent of the issued share capital). If the reader was to imagine holding 100 shares in M&S and receiving the annual general meeting (AGM) information, would the reader go to the AGM, bother to send in the voting form or vote online and even if the reader were to vote, it would be 0.000005 percent of the total votes? (Institutional investors include pension funds, insurance companies, investment banks, unit trusts, investment trusts, hedge funds, endowment funds, and venture capitalists.)

The individual or private shareholder cannot realistically hold the directors to account. Over the years, it became more apparent as to the importance of institutional investors to hold the directors to account. As can be seen in the M&S shareholdings, the institutional shareholders effectively hold all the power, and with that, must go responsibility.

In his 1992 report, Cadbury included a section on institutional shareholders (sections 6.9–6.12). He noted that in the 30 years up to 1992, there had been a reversal and institutions, not individuals, now held the majority of shares of quoted companies, but that they were holding them on behalf of individuals, such as insurance policy holders and members of pension funds.

Thus, effectively there is common interest between the individual shareholder and the institutional shareholder in the standards of financial reporting and governance. Cadbury was looking for responsibility from the institutional shareholders to bring about change in companies where necessary and not just to sell their shares. Cadbury welcomed a statement by the Institutional Shareholders' Committee on the Responsibilities of Institutional Shareholders in the UK, which required institutional investor contact with senior executives in order to exchange views on various issues, to positively use their voting rights, and to take a positive interest in the composition of the board.

In September 2012, the Financial Reporting Council issued The UK Stewardship Code, which was the first time that they had issued such a code. It consisted of principles and guidance and effectively codified what had become deemed to be best practice over the 20 years since The Cadbury Report. In 2020, the Financial Reporting Council issued a new and expanded version of the code. The code has further defined the meaning of stewardship as "the responsible allocation, management and oversight of capital to create long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society." For example, the economy benefits from employment and the various elements of taxation generated by the company, this in turn can lead to improved standards of living and can help with political stability.

The 2020 code also effectively considers CSR as it states "Environmental, particularly climate change, and social factors, in addition to governance, have become material issues for investors to consider when making investment decisions and undertaking stewardship." As already noted, this is becoming increasingly more important to investors and to society as a whole.

The 2020 code requires asset owners and asset managers to consider and report on the following issues:

- *The effective application of the UK Corporate Governance Code and other governance codes*
- *Directors' duties, particularly those matters to which they should have regard under Section 172 of the Companies Act 2006 (relates to the central obligation of directors to act in good faith)*
- *Capital structure, risk, strategy, and performance.*
- *Diversity, remuneration, and workforce interests*
- *Audit quality*
- *Environmental and social issues, including climate change*
- *Compliance with covenants and contracts*

The chapter will now consider the development of corporate governance.

The Development of Corporate Governance

As already noted, corporate governance did not begin in 1991. If a wider view of corporate governance is accepted, and that being the way business is controlled and directed, then corporate governance could be traced back to biblical days. Genesis (47:13–27) describes Joseph's dealings with Pharaoh with respect to bread, sheep, cattle, and horses. In modern terminology, Joseph was effectively acting on behalf of the *people* who could be compared to shareholders.

Moving forward to the time of Ancient Rome and the Roman Empire, a film and a TV program both highlighted, albeit in a funny way, those times. The 1966 film, *A Funny Thing Happened on the Way to the Forum*, starring Zero Mostel and the 1969/1970 BBC series *Up Pompeii*, starring Frankie Howerd, set in the Ancient Roman town of Pompeii, both highlighted how life was and how business was performed in those times.

Relatively more recently, the East India Trading Company traded from 1600 to 1874, when it was dissolved. It was a merchant trading company, which at one stage was involved in half the world's trade.

However, considering the current importance of CSR, it is interesting to note that in 1684, the company became involved in the slave trade. The governance of the company consisted of one governor, a court of directors or committees, which was actually 24 directors, and they reported to the Court of Proprietors, which was effectively the shareholders, thus an element of similarity when compared to today's structures.

A further example of the same era is that of the South Sea Bubble Scandal. The South Sea Company was formed in 1711 in London and survived until 1720 when its share price collapsed, and the company went out of existence causing substantial damage to the entire economy. As with the East India Trading Company, it was similarly involved in the slave trade. After its collapse, it transpired that its prospectus had been dubious, many people had profited unlawfully, directors were arrested, and estates were forfeited and assets confiscated.

A consideration the last 100 years offers many examples of problems that highlight corporate governance issues. It is worth reminding the reader that poor corporate governance is not simply directors who cannot or do not manage and/or direct and control a company's business competently, but they are managing everything relating to the business. The problems that will be explained, as developments move through to the current day, will highlight some general incompetence of directors. This will include behavior that can be considered dubious or unethical, through to serious criminal actions.

The U.S. 1929 Wall Street Crash was caused by an unsustainable rise in share prices over the preceding years. Reasons include overproduction of consumer goods, decline in traditional industries, and excess consumer debt that could not be paid. Commentators vary as to whether or not they believe that fraud and other illegal and immoral acts had a material impact on the crash.

As will be seen as the chapter develops, the UK currently expects that: "The board and its committees should have a combination of skills, experience and knowledge," as well as the appointment of directors to be on merit and objective criteria, promoting diversity of gender, social and ethnic backgrounds, cognitive and personal strengths.

It is worth comparing the board of directors of the major UK bank, Barclays Bank, in 1965 and currently.

The 1965 Board consisted of the following:

- *9 knights (Sir)*
- *3 Commanders of the British Empire*
- *1 Order of the British Empire*
- *3 Members of the British Empire*
- *3 right honorable*
- *1 honorable*
- *1 field marshal*
- *3 military cross-holders*
- *8 untitled individuals*
- *Mr. Theodore David Barclay, a member of the founding family*

While it may be unfair to state that this was entirely status-biased, it was generally accepted that a titled person or similar improved the look of the board in this period. Notably, the board has no gender or ethnic diversity and on the face of it, no diversity at all.

Today's board consists of 13 people with both gender and ethnic diversity, as expected.

As the late 1960s approached, there were a number of problems that arose, but some of those were not entirely management issues but accounting problems. The current relative tightness and lack of choice in accounting due to local and international standards can be traced back to some of the problems of this period. The fact that accounting or financial reporting standards have been developed is a response to some of the following issues. While accounting was relatively flexible, profit manipulation was much easier than it is today, and a knock-on effect was the share price.

The 1967 takeover of AEI by GEC was surrounded by accounting scandal. Half way through the year, AEI had forecast a full-year profit figure of £10M, but when the end of year figures were produced, the losses were £4.5M, a turnaround of approximately £14M, which may seem relatively small by today's standards, but which was a materially substantial sum in 1967. The turnaround was due to differences in the valuation of contracts and inventory, and this seems to have been a turning point in the public's understanding of the malleability of profit figures. It is generally accepted that this scandal and problems with Pergamon Press (following) led ultimately to the introduction of UK accounting standards.

In 1969, Robert Maxwell lost control of Pergamon Press and subsequently an inquiry by the UK's Department of Trade and Industry found that the share price of this listed company had been maximized through transactions between the company and Maxwell's private companies. The benefit would have been a higher value of the shares in the proposed takeover of Pergamon Press by the American Leasco Data Processing Equipment Corporation of New York. Judgment, misapplication of and changes in the application of accounting principles were clearly recognized during the investigation into the scandal.

The 1990s saw a number of company problems, three of which will be considered, two of which relate to criminal behavior and one of which may be considered as the culmination of poor or mismanagement. The Bank of Credit and Commerce International was set up in 1972 in Karachi, Pakistan, but registered in Luxembourg. In the 1980s, the financial regulators of several countries started to investigate the company. A 1986 U.S. Customs undercover operation was the beginning of the company's eventual demise. The company and several directors were charged with money laundering, fraud, larceny, facilitating drug traffickers, avoiding regulation, and illegally taking control of an American bank. In July 1991, a Luxembourg court ordered the company's liquidation, and the company was subsequently wound up.

During the 1980s, Polly Peck, a company controlled by Asil Nadir, went through a major expansion program to become a global conglomerate, and by 1989, it was a member of the FTSE 100. However, it had an unsustainable amount of debt, the books were being falsified, cash was being moved around, and the sales and thus the profits were being overstated. This was helping to prop up the share price, and seemingly £378M was stolen by Asil Nadir. In 1991, the company effectively collapsed with £1.3Bn of debt. As everything unraveled and court cases approached, in 1993, Asil Nadir fled to Turkish-controlled Northern Cyprus. It was not until 17 years later, in 2010, that he returned to the UK to face justice and was found guilty of seven cases of theft, with a 10-year prison sentence imposed. This company collapse was one of the catalysts for the first UK Corporate Governance Code.

In 1884, a newly arrived Russian immigrant set up his first penny market stall in Leeds. Ten years later, Michael Marks was joined by Tom Spencer, and from those small beginnings, the British, but ultimately worldwide retail business, M&S grew. From then onward, the company went on seemingly never-ending growth and an ever-improving profile, becoming the darling of the high street. Marks family members were involved in running the business until the 1980s, but eventually nonfamily members took over as directors. The business went from strength to strength opening stores in Paris and Hong Kong, and in 1984, they set up their financial services section. By 1997, profits exceeded £1Bn for the first time, and the business looked to expand and to be on the up and up.

In 1998, everything started to go awry; half year profits fell by 23 percent as did the share price the following year. The board saw attempted coups, resignations, and the entire business started to drift into a decline from which it has never properly recovered. Unlike the previous two examples, nothing untoward caused the problems, except the commentators of the day put this down to incompetence and a sudden change from a company that had been unable to do anything wrong, not being able to do anything right. The system, by which the company was directed and controlled, had clearly gone downhill.

By the early 2000s, things had got worse generally, and American companies were clearly becoming a major problem. Tyco and WorldCom were two well-known companies where much went wrong, but the most well-known scandal was that involving Enron.

Enron was formed in 1985 with Kenneth Lay becoming both Chairman and Chief Executive Officer. The company became an energy trader and supplier, and at the time, the newly deregulated American market effectively allowed betting on future energy prices (effectively a form of gambling). In 1990, Jeffrey Skilling was appointed as the head of the newly formed Enron Finance Corporation as the dot-com era was about to take off and the Nasdaq (second only to the New York Stock Exchange (NYSE) by market capitalization of shares traded) was continually showing increasing share prices. Skilling decided to transition Enron's method of accounting from historical cost accounting based on actual cost, to mark-to-market accounting, which is based on fair value that can be manipulated and that gave Enron the possibilities to account for estimated future profits as actual current profits.

This was used when Enron entered a partnership with Blockbuster (known as a video rental chain) to enter the expanding video on demand (VOD) market, and then, as the dot-com bubble was about to burst, Enron decided to build high-speed broadband telecom networks. These projects were not successful, but the accounting system allowed Enron to show profits because of expected future growth (as decided by Enron) that never actually materialized. Enron also used off balance sheet finance via special purpose vehicles to ensure that its mountain of debt did not come to the notice of investors and readers of the financial statements, an accounting ploy that the regulators have tried to stop in the intervening years, as by doing this, companies are ensuring that they do not show a true and fair view.

By the end of the 1990s, Kenneth Lay was a good friend of the presidential Bush family, which generated him some benefits, and the company was America's seventh largest with $70Bn turnover. Generous share options and bonuses were given to directors at the time when the business was making vast losses, and eventually, it was found that $2Bn had disappeared. On August 14, 2001, Jeffrey Skilling resigned for *family reasons* as major losses were announced, and the share price started to drop. On December 2, 2001, the company filed for a Chapter 11 bankruptcy, and the share price had plummeted to $0.26.

That effectively was the end of Enron, and the fallout was extensive. It was eventually decided that long-term fraud had taken place, and this had a personal effect on the major players. Employee Cliff Baxter committed suicide on January 30, 2002. Andy Fastow, the Chief Financial Officer, cut a deal with the authorities and served five years in prison. Kenneth Lay was convicted on six charges of fraud and conspiracy and four charges of bank fraud but died of a heart attack before being sentenced. And, in 2006, Jeffrey Skilling was convicted of conspiracy, fraud, and insider trading, eventually being released from prison in February 2019, rather than February 2028 after agreeing to give $42M to the victims of the fraud.

There were further ramifications of the scandal. Arthur Andersen was the world's foremost and most prestigious firm of auditors at the time and was the company's auditors. In June 2002, the firm was found guilty of obstructing justice due to shredding documentation and effectively that was the end of Arthur Andersen, at the time a seismic event in the world of international auditing.

This also caused a major rethink in the United States. The Financial Accounting Standards Board whose responsibility it is to establish and improve *Generally Accepted Accounting Principles* substantially raised its level of ethical conduct, and in July 2002, President George W. Bush signed the Sarbanes—Oxley Act into law (see next section) perhaps an ironic act considering the friendship between Kenneth Lay and the Bush family and as Deakin and Konzlemann noted in 2003 "The Sarbanes—Oxley Act is a mirror image of Enron: the company's perceived corporate governance failings are matched virtually point for point in the principal provisions of the Act."

In an ideal world, Enron would have been the nadir with respect to corporate governance, and the hope would have been that both illegal acts and poor management would have been eliminated; however, that has not happened and over the last 20 years, since Enron, there have been many problem companies where corporate governance issues have been the culprit. A few examples follow, all being slightly different from each other, but showing that there are many different ways in which corporate governance goes wrong, and that it is not only an American or British problem.

Parmalat was an Italian food and dairy company, which had grown rapidly throughout the 1970s. Its financial performance started to go wrong in the 1990s, as it expanded quickly and took on further debt. By the end of 2002, Merrill Lynch analysts were beginning to be concerned about the business's ability to repay its debt, despite having sufficient cash showing on its balance sheet. Over €3Bn of cash held in the Cayman Islands was *verified* with a forged Bank of America letter.

Among the problems subsequently ascertained were forged letters, inflated revenues, fake assets, off balance sheet finance, and low-quality audit procedures. The family who sets up a business often dominates, as in this case, and the minority shareholders are not protected, and this is prevalent in certain areas of Europe.

April 20, 2010, was the most inauspicious of days for BP (formerly known as British Petroleum), which by 2010 was operating in many parts of the world. At around 10 p.m., the first mate on the charter ship, Damon B. Bankston, noticed what he thought was a problem with the Deepwater Horizon rig, which was preparing to drill for oil in the Gulf of Mexico. The back of the ship was covered in drilling mud, which was falling from the sky like black rain. Explosions occurred, and eventually, after two days of fires, the rig sank 5,000 feet to the bottom of the Gulf of Mexico and America's worst-ever oil spill ensued.

BP had had problems over the previous five years with oil spills in Alaska and an explosion in Texas where 15 people died. Eleven people died in the Gulf of Mexico disaster. One question that could be asked: did BP's directors not learn from their previous errors?

While much has been written about the disaster, one of the expert analysts, Tom Bergin, believes that BP at the time was a compulsive cost-cutting company, but that the disaster ultimately hinged on the two top executives who had run the company over the previous 20 years, John Browne and then Tony Hayward. Bergin believes that: "The story of the oil spill is a 20-year tale of Browne's determination to create the largest corporation in the world and Hayward's battle to succeed, and then outdo, his mentor."

Ultimately, the spill has cost BP upwards of $65Bn and caused huge damage to the coast and animals of the area after spilling approaching 200 million gallons of oil in the Gulf of Mexico. It also soured relations between the UK and the United States and their respective leaders at the time, David Cameron and Barack Obama, due to the political storm that it caused in the United States. It also caused the American administration to revert to using the old name of BP 'British Petroleum', even though the company had not been known by this name since 1998, which in itself generated diplomatic tensions.

In order to highlight the worldwide importance of corporate governance and the fact that problems arise all over the world, the penultimate example is that of the Japanese company Toshiba. In July 2015, the then CEO of Toshiba resigned in the face of an accounting scandal centered on accounting improprieties that had taken place over the previous seven years and $1.2Bn overstatement of profits, ultimately considered to be fraudulent. Despite Toshiba's seeming efforts to implement good corporate governance, the company's culture seemed to work against this happening.

The final example is the UK-based fashion company Boohoo Group plc, which hit the headlines in July 2020. It seemed that much of its clothing was being manufactured in factories in Leicester, which is a city in the Midlands in the UK. Investigation found that up to 18 factories were paying employees below the hourly, statutory minimum wage, and audits were undertaken to establish the facts and to consider the working conditions of the employees.

Over two days in July, £1.5Bn was wiped off the share price, but this has now started to drift up again and analysts believe that at the maximum, 5 percent will be lost from its sales, leaving a question mark over good and ethical corporate governance.

Types of Corporate Governance

Corporate governance has become a global issue, but this section will mainly concentrate on the UK and American systems. These differ from each other, but it would be hoped that the end product, that is, a well-run business for the benefit of stakeholders, was the same. Whether it is exactly the same is very much a matter of opinion.

As noted in the first section, *The Cadbury Report*, published in December 1992, in the UK, was the game changer when considering corporate governance. This has been updated over the years, extra reports looking into more specific areas have been produced and from a UK perspective, the current code to be followed is the Financial Reporting Council's The UK Corporate Governance Code July 2018.

(As an aside, for American readers, it is worth expanding slightly using Cadbury as an example, to show how trade is multinational, one of the drivers of improved corporate governance. Sir Adrian Cadbury was a member of the Cadbury family and was the Chairman of Cadbury and Cadbury Schweppes for 24 years, as well as a director of the Bank of England.

In March 2010, Kraft acquired Cadbury, eventually becoming the Kraft Foods Group Inc, which eventually split into Kraft Heinz and

Mondelez with the Cadbury brand staying in Mondelez. And, to complete the circle of the British company returning to a major position in the UK, on September 7, 2020, it was announced that Cadbury had become the Official Global Chocolate Partner Of Liverpool Football Club, one of the world's premier football (soccer) clubs who had won the 2019/2020 English Premier League, arguably the world's top league. And, Liverpool Football club is owned by the American Fenway Sports Group.)

As stated, the UK has generated a number of reports on the road to the current code. The 1995 Greenbury Report was set up under the terms of reference: "To identify good practice in determining directors' remuneration and preparing a code of such practice for UK PLCs." Directors' remuneration is a key area of the current code, as will be seen.

The Hampel Report of 1998 was set up to consider the implementation of the Cadbury and Greenbury reports and to update as appropriate, which it did. This was quickly followed by the *Turnbull Report,* which highlighted the importance of directors in ensuring high-quality internal controls, financial reporting, and systems to discourage and catch fraud and professional audits, in the business, all of which are in the current code.

The 2001 *Myners Report* was a report to the British Government on institutional investors, as at the time, it was felt that they were not proactive enough with respect to the companies in which they invested. This led to The UK Stewardship Code of September 2012, subsequently updated in 2020 (see What is Corporate Governance? section).

The January 2003 Higgs review was set up partly due to the concerns over the American scandals, particularly Enron. Its remit was to consider particularly the role and effectiveness of nonexecutive directors and the audit committee. Again, these are major areas in the current code. Allied to this was the *Smith report* of the same year; the key issue that was considered was the independence of the external auditors because of their importance to the shareholders and their position to undertake their key, legal role on behalf of the shareholders. This was deemed to be crucially important to consider but problematic at the time, due to the behavior of Arthur Andersen in the Enron scandal.

Due to the reviews, changes in government, and changes in perceptions, there have been updates of the UK code over the years, and the current code is the Financial Reporting Council's The UK Corporate Governance Code July 2018 (the Code), which will be considered in some detail.

Before considering the details, an understanding is required as to how the Code operates on almost a philosophical, through to a practical basis, especially when compared to America. The critical point is that the Code is not legislation (c.f. The Public Company Accounting and Reform Investor Protection Act 2002, commonly known as The Sarbanes—Oxley Act [Sarbox]). May be this highlights a major difference between the UK and U.S. attitudes and thinking and the deemed perception of the United States being a litigious society.

The Code sets out principles, which are intended to: "emphasise the value of good corporate governance to long-term sustainable success." These principles are to be applied, and there are provisions that offer guidance as to the implementation of the principles, but flexibility is allowed. Thus, the Code is looking for companies to follow the spirit of the Code rather than the letter, but noting that there is no real letter. This also helps to avoid a box-ticking exercise, as the Code notes that there is no rigid set of rules to be applied nor a *right way* to apply it.

The application of the principles needs to be followed by high-quality reporting as to how they and the provisions have been applied, avoiding boilerplate reporting, and this will be in the annual report. However, it is not necessary or mandatory to comply with a provision, and the circumstances of the company must be considered, particularly size, complexity, and its history and ownership structure. The voluntary nature of following principles and provisions must be taken very seriously by directors, and it is not expected that there will be any deviation from the principles, but deviation from provisions, as noted, must be justified and this is known as *comply or explain*.

Explanations should set out the background as to why this has occurred, a clear rationale and the impact of the action. The Code believes that this is a positive opportunity for the company to communicate to its stakeholders and not an onerous obligation. It is then down to the shareholders and stakeholders to make what they will of the deviations; effectively allowing *the market* to decide, but with the ultimate sanction of annual re-election.

Before a consideration of some of the key areas in the Code, it is worth noting a number of matters that have become much more important since Cadbury. Cadbury used the word shareholders, but the Code notes that the directors and the company need to build and maintain successful relationships with a wide range of stakeholders (see definition in first section).

Since Cadbury, CSR has become ever more important and has crept into life on an almost daily basis, for example, motor vehicle emissions and recycling. The Code uses expressions such as “long-term sustainable success of the company,” “company contributing to wider society,” and “the company’s purposes, values and strategy and its culture are aligned.”

The Code also states: “There should be a means for the workforce to raise concerns in confidence and—if they wish—anonymously.” This effectively relates to whistleblowing and is covered by the Public Interest Disclosure Act 1998 in the UK. Due to such problems as the Zeebrugge ferry disaster, the Clapham train crash, the Piper Alpha oil platform explosion, and Enron, it became clear that employees knew of malpractice and wrongdoing but took no action due to a fear of reprisal from the company with potential dismissal. The Act allows workers to report concerns subject to specific rules to be followed.

It must be taken as read that the current edition of a corporate governance code contains the current thinking on corporate governance. Countries update their code or law or stock exchange rules as the business world changes, politics change, and people’s views change. Thus, it can be accepted that the current July 2018 UK version is up to date, although a new, updated version may have been delayed due to the current pandemic. The operation of the 2016 and 2018 versions were reviewed by the Financial Reporting Council in their January 2020 annual review, and they concluded that there is room for improvement in the quality of the reporting.

The Code has five sets of principles, each of which will be briefly outlined. However, it is worth noting that overriding all of this is Section 172 of the (UK) Companies Act 2006, which states:

> A director of a company must act in a way he considers, in good faith, would be the most likely to promote the success of the company for the benefit of the members as a whole, and in doing so have regard to....

Thus, there is a fiduciary duty and a requirement to act in a bona-fide manner and consider such matters as the long-term consequences of decisions, the interests of company employees, fostering good relationships with stakeholders, including the community and the environment, to maintain a reputation for high standards of business conduct, and to act fairly as between members (shareholders) of the company.

There are five sets of principles and the key issues from each set will be highlighted as follows.

1. **Board Leadership and Company Purpose**
   If the company is to be successful, it must be led by an entrepreneurial board (see final section).

   The board is to ensure that necessary resources are in place, usually considered to be financial resources and human resources.

   The board is to establish a framework of prudent and effective controls in order to assess and manage risk. It is worth noting that this is not defined any further; thus, it concurs with the idea of a set of principles, leaving the board to decide on the specifics of the systems to be put in place.

   Effective engagement with and participation from shareholders and stakeholders is required. The UK Stewardship Code (see first section) dovetails with this requirement.

   Workforce policies and practices are to be consistent with the company's values and long-term sustainable success, with the workforce being able to raise any matters of concern. This is consistent with current CSR thinking and whistleblowing, as noted previously.
2. **Division of Responsibilities**
   The chair leads the board and is responsible for directing the company. The chair should ensure the smooth operation of the board, being objective and promoting a culture of openness and debate, and that accurate, timely, and clear information is received by all directors. The chair needs to facilitate an effective contribution from the nonexecutive directors.

No one individual or group of individuals should be allowed to dominate the decision making of the board. To help ensure this happens, the role of chair and that of the chief executive should not be exercised by the same individual. The chief executive, often known as the CEO, is tasked to lead the company's business.

This does happen occasionally, and the shareholders and financial press are usually critical of such behavior. Stuart Rose was CEO of M&S from May 2004 until May 2010 and Chairman from May 2008 until January 2011, thus an overlap of two years from May 2008 until May 2010 when he held both positions. This was heavily frowned upon at the time. The United States is not as tight with this concept.

There should be several nonexecutive directors, with half the board being independent. The Code defines independent. One of the nonexecutive directors should be appointed as the senior nonexecutive director and must act as a sounding board for the chair. There are a number of further issues relating to nonexecutive directors.

3. **Composition, Succession, and Evaluation**

A formal, rigorous, and transparent procedure is required for appointments to the board, being based on merit and objective criteria. A combination of skills, experience, and knowledge is required by the board in totality, and diversity of gender, social background, ethnic background, cognitive strengths, and personal strengths need to be considered.

The analysis of the board of Barclays Bank (Development of Corporate Governance) shows how appointments to the board have changed over the years. A February 2011 report entitled *Women on boards* was commissioned by the UK's coalition government and led by Lord Davies of Abersoch. There were updates until 2015, and the intention was to encourage UK-listed companies to increase the number of women on boards. This has been reasonably successful. Thus, politics, CSR, and corporate governance principles have coincided to improve the representation of women on boards of listed companies.

A formal and rigorous annual evaluation of the board is required.

A nomination committee, mainly consisting of independent nonexecutive directors is to be established to consider appointments and an orderly succession on to the board and to senior management positions.

The annual report should describe the work of the nomination committee.

4. **Audit, Risk, and Internal Control**

There need to be formal and transparent procedures to ensure the independence and effectiveness of internal and external audit functions.

Procedures should be established to manage risk and to oversee the related internal control systems. The board needs to decide the nature and extent of the principal risks that it is willing to take in order to achieve its long-term strategic objectives.

To do this, an audit committee must be established. It will have at least three independent nonexecutive directors (deemed smaller companies need only have two), with one member having recent and relevant financial experience. The main roles and responsibilities of the committee include:

- *Monitoring the integrity of the financial statements and formal announcements*
- *Considering and advising the annual reports being fair, balanced, and understandable*
- *Reviewing internal financial controls and internal controls and risk management systems*
- *Monitoring and reviewing the internal audit function (if there is not one, then an annual consideration as to whether one is needed)*
- *Matters relating to the appointment and removal of external auditors and their supply of nonaudit services*
- *Reviewing the external auditor's independence and objectivity (consider Enron and Arthur Andersen)*

The annual report should describe the work of the audit committee.

5. **Remuneration**

Remuneration policies and practices should promote long-term sustainable success, with executive remuneration being aligned to the company's purpose, values, and the successful delivery of the long-term strategy.

A formal and transparent procedure is required for the development of executive directors' and senior management's remuneration policy, with no director being involved in their own remuneration decisions.

A remuneration committee needs to be established consisting of three independent nonexecutive directors, and this committee should be responsible for determining the policy, together with reviewing workforce remuneration.

When determining executive director remuneration policy, the following should be considered: clarity, simplicity, risk, predictability, proportionality, and alignment to the company's culture.

The annual report should describe the work of the remuneration committee.

Before considering the American provisions, it is worth noting that while many countries have their own rules, The Organization for Economic Cooperation and Development has developed six general corporate principles. To a great extent, they reflect the basic principles of UK corporate governance as previously outlined.

1. *Ensuring the basis for an effective corporate governance framework: Promotion of transparent and efficient markets, consistency with the rule of law and clear responsibilities of supervisory, regulatory, and enforcement authorities.*
2. *The rights of shareholders and key ownership functions: The protection of and exercise of shareholders' rights.*
3. *The equitable treatment of shareholders: This highlights minority and foreign shareholders who should have the opportunity to obtain effective redress for violation of their rights.*
4. *The role of stakeholders in corporate governance: Their rights to be recognized through law or agreement.*

5. *Disclosure and transparency: Timely and accurate disclosure of various information is to be made.*
6. *The responsibilities of the board: The board offers strategic guidance; the board is to monitor management, and the board is accountable to the company and its shareholders.*

Arguably, the biggest change in the American attitude to corporate governance occurred due to the collapse of Enron, as previously discussed. Enron had weak or even no proper corporate governance, there was unethical behavior at the highest levels in the company, and the quality of the audit provision was extremely poor.

Due to Enron, Sarbox (see previously) came into federal law in 2002. As this is law, it does not allow the concept of comply or explain, it is rules based, those rules being law. Analysts believed that Sarbox contained some tough provisions, which caused disquiet and it applied to non-U.S. companies but who had a U.S. listing, thus a number delisted from the NYSE. There was a subsequent relaxation to help accommodate foreign companies. Sarbox has 11 subdivisions or key areas that include the introduction of a Public Company Accounting Oversight Board and related auditor independence provisions.

Financial improvements include internal control reports and certifying of financial reports by the CEO and chief financial officer or finance director. The Corporate and Criminal Fraud Accountability subdivision is there to attempt to ensure that there is no manipulation, alteration, or destruction of any records, and those found guilty will be under criminal law and will be dealt with accordingly. There are further subdivisions relating to white-collar crime and corporate fraud, and criminal sanctions apply.

In 2010, Barack Obama's America enacted the Dodd—Frank Wall Street Reform and Consumer Protection Act (Dodd—Frank) in response to the 2008 financial crisis; however, in May 2018, some of the provisions of the Act were rolled back due to laws enacted by the Trump administration. The idea of the reforms was to oversee the financial system, especially the elements that were believed to have caused the 2008 crash. Key areas of the Dodd—Frank Act were, for example, to monitor the financial stability of major financial firms, to break up banks when deemed appropriate, and to introduce investing restrictions on banks (the Trump law eased the restrictions particularly on small and regional banks) and to expand and strengthen whistleblowing, which had been introduced in Sarbox.

As well as federal law, America has state law, and Delaware is the state where many American companies are incorporated; thus, its relevant laws relate to many companies. Commentators believe that several of its practices are anti-shareholder and less demanding on directors (as noted by Simon Graham of the UK law firm Wragge and Co.), presumably to entice major corporations to incorporate in Delaware.

The American Securities and Exchange Commission (SEC) is an independent agency of the American government and is responsible for enforcing federal laws such as Sarbox. It is tasked with regulating the American stock markets and to protect investors. The stock exchanges themselves have their own rules, and probably, the best-known American exchanges are the NYSE and the National Association of Securities Dealers Automated Quotations exchange, better known as Nasdaq.

Finally, it is worth noting that as well as American federal and state law and financial institution law, interested parties are producing their ideas as to best corporate governance practice. In July 2016, *Commonsense Principles of Corporate Governance* was published by several senior executives from major companies and institutional investors such as General Motors, Berkshire Hathaway, and BlackRock. It recommended best practice in areas such as a director's loyalty to the company and its shareholders, independent directors, industry experience, board diversity, refreshment of the board, and evaluation of directors. Eagle-eyed readers will note clear similarities with the UK code.

- In January 2017, another new American code was launched by several similar asset managers and owners entitled Corporate Governance Principles for U.S. Listed Companies. Its six principles encapsulate much that has been discussed so far and suggest that British and American practices should go together, and that it is probably not unreasonable to state that the best practice discussed is good from a worldwide perspective. The six principles are:

- *Principle 1:* Boards are accountable to shareholders.
- *Principle 2:* Shareholders should be entitled to voting rights in proportion to their economic interest.
- *Principle 3:* Boards should be responsive to shareholders and be proactive in order to understand their perspectives.
- *Principle 4:* Boards should have a strong, independent leadership structure.
- *Principle 5:* Boards should adopt structures and practices that enhance their effectiveness.
- *Principle 6:* Boards should develop management incentive structures that are aligned with the long-term strategy of the company.

As noted, corporate governance is not only a British and American concept but relates to companies and thus investment throughout the world. Since the 1960s, there has been a nonstop increase in world trade, multinational enterprises (MNEs), and access to global stock markets, thus the importance of corporate governance globally.

India may be used as an example. The year 2009 was crucial in the development of India's corporate governance. Although there had been various legislations and regulations up to then, in that year, the Corporate Governance Voluntary Guidelines was issued. However, in the same year, India had its own corporate scandal due to the Satyam Computer Services Company being involved in a manipulation of financial statements scandal. This then led to a new Companies Act in 2013, which contained many of the ideas already seen in this chapter. Currently, the Indian system follows the 2013 Act together with the 2019 National Guidelines on Responsible Business Conduct, which is CSR based and which has superseded the 2009 Voluntary Guidelines. This is all overseen by the Securities and Exchange Board of India.

While this section has only covered the UK, America, and India as examples, most countries in the world have some sort of corporate governance rules, and these can be researched if required. It is worth noting that the structure of business, often related to the number and type of shareholders, will influence the rules of a given country.

Good Corporate Governance During a Pompeii Event

As has already been noted, the Code states that a successful company is led by an entrepreneurial board. The Oxford English Dictionary defines an entrepreneur as one who undertakes a commercial venture; however, the Collins Dictionary expands noting that risks are involved in order to make a profit. This is much closer to the current understanding of entrepreneurial. Effectively, boards need to take financial risks in order to keep generating profits by creating new opportunities and moving the business forward constantly. A business that sits on its laurels will soon be overtaken by its competitors.

The current environment has seen major changes in the way certain businesses can operate; thus, those businesses must be imaginative and entrepreneurial in order to succeed in the future. There are new opportunities as old ones die away. This has been how business has operated over many centuries.

The Industrial Revolution, which occurred in the UK, Europe, and America from approximately 1760 to 1830, meant that there was a transitioning from hand production to machine production, with new industrial tools and mechanization taking over. Wages improved, economies grew, and society changed out of all recognition; this effectively became the beginning of capitalism as it is currently understood.

Unfortunately, both the First and Second World War changed economies and how businesses had to operate. The First World War saw major changes in the American economy, with increased exports to Europe and an improvement in wages and the aircraft industry, which was in its infancy, saw a major increase in demand. In the UK, it allowed many more women to go to work, as they replaced the male factory workers who were drafted into the military.

As the year 2000 approached, the Nasdaq index reached an all-time high as dot-com companies came to the fore. In October 2002, the index had lost 78 percent of its peak value. At the time, many of the start-up dot-com companies did not last, as there were too few users being chased by too many companies, but life under lockdown would have been greatly more intolerable for many millions of people without the technology that spun out from those early days.

Some companies became famous overnight but did not survive. Perhaps, the most famous British company of the era was boo.com, which was founded in 1998 by three Swedish entrepreneurs and sold fashion over the Internet. Some $135M of venture capital was invested in the company, but by May 2000, the company had been placed in receivership, and it was eventually liquidated. However, it may be worth considering that without such innovation and imagination, would many of today's online fashion and other retailers be in the position that they are currently and would they have been of benefit to so many people unable to have visited physical premises during lockdown? However, there are two examples of companies that were set up around this time that have had a major economic impact over the years.

In 1995, Amazon sold its first books online. It had been set up by Jeff Bezos who it is fair to state is the perfect example of an entrepreneur. Also founded in 1995 by Pierre Omidyar was eBay, and it is reasonable to state that these two businesses have greatly changed the way businesses operate in many parts of the world.

One British company is worth noting for its innovation and development over nearly 200 years, as an example of moving forward and being entrepreneurial and not hoping for something to happen. In 1833, John Menzies opened a bookshop in Edinburgh, and throughout that century, the business expanded across Scotland. After the Second World War, the business expanded , and by 1965, had 90 wholesale warehouses, 350 stalls at railway stations, and 161 shops.

Toward the end of the 20th century and into the 21st century, the business started to move newspapers and heavy freight, and by the early part of this century, had disposed of the retail outlets and focused on cargo handling and passenger services. In 2018, the distribution business was disposed of, and it is fully involved in the aviation business and can be seen on runways at many of the world's airports. At the end of September 2020, the executive chairman of the company, Philipp Joeinig, noted that revenue had dropped by almost 34 percent and pretax losses had been made. He stated that the company may well finish up “having a smaller business,” and that the workforce may reduce from 32,000 to 25,000.

As the months since March 2020 have shown the world, nothing can be taken for granted. It is possible that the next few years will see major shifts in the way economies operate, and the knock-on effect will be in the way that business must operate. As with all changes, there will be winners and losers, but it does seem that entrepreneurship of the highest order will be necessary.

Already there have been some big losers and big winners. Big losers include the airline industry and related tourism businesses, but domestic tourism has had the opportunity to benefit from the lack of overseas travel. In the UK, high streets in major cities (downtown in American terminology) have suffered greatly, but local shops have benefitted to some extent.

In the UK, many of the major supermarkets have seen their click and collect (order online, they pack it for you, and you simply collect the goods) and delivery greatly expand, and job opportunities are now available for people who have been made unemployed in other sectors. Restaurants that have been locked down at times and that have been avoided by some people, now deliver, and this has seen an increase in business for delivery firms and the use of more drivers by those firms. And, in general, home deliveries have increased greatly due to people not being willing or able or allowed to venture out.

This then offers opportunity to the new entrepreneurs to follow in the footsteps of British entrepreneurs, such as Richard Branson (Virgin), Terence Conran (habitat and restaurant chains), and James Dyson (Dyson products), and American entrepreneurs such as Sergey Brin and Larry Page (Google), Bill Gates (Microsoft), Elon Musk (Tesla), and Mark Zuckerberg (Facebook). Hopefully, the entrepreneurs who became the most famous and appreciated will be the people who are finding the vaccines that defeats the COVID-19 pandemic.

As businesses attempt to survive through, for example, frugal innovation (see Chapter 2) and hope to enjoy a phoenix-like resurgence, there will be a temptation to cut corners, sacrifice internal controls, and undertake management override. However, as this chapter has demonstrated, poor corporate governance tends to breed short-termism, institutional destruction, and a loss of trust in the professions and the markets.

It could be argued that scandals such as Enron potentially wreak more socioeconomic destruction than street crime, and it could even be argued that corporate crime is a form of violent crime. Many social problems, such as the tyranny against native communities and indigenous populations, contamination of food, medical negligence, and unsafe working conditions, are as a result of concerted corporate power.

The global recovery should not be at the cost of poor corporate governance, as global markets cannot afford another Pompeii Event or Enron-style scandal. However, acknowledgment must be made of the difficulties that boards are currently encountering. Some of this is due to the pandemic, and some issues have been exacerbated over 2020, while other matters are due to ongoing progress and changes in the world. These include the rise of populism, the environmental crisis, diversity, dynamic shareholder expectations, and technological innovations such as artificial intelligence (AI) or blockchain, which will change the operation of many functions, including that of the board.

Corporate Governance Response to This Pompeii Event

It should be noted that as well as best practice codes, the actual behavior of directors is of key importance. The directors need to be looking constantly at their conduct and remember how they are being judged. They need to remember the multitude of key performance indicators (KPIs) by which they will be eventually judged. These include innovation, sound cash management, minimization of waste, and careful consideration of fraud prevention.

In order to ensure, at the minimum, company survival, it is considered that even more advice should be sought from the nonexecutive directors. They are the company's critical friends, and if they have been chosen wisely, they have the experience and knowledge to greatly aid strategic decision making. They should help the board become even more collaborative, a team and a consensus should be built to ensure that the correct decisions are taken and enacted. A suggestion as to the areas to be considered comes via the acronym *VICTORY*.

Vision: Although the short term is critical, boards must never lose sight of the bigger picture and the long term. Impartial, inquisitive thinking and a strategic mindset are particularly important if the board is to be strategically capable.

Inquisitive: The short-term firefighting and longer-term vision should be underpinned by inquisitive foresight and a continuous strategic mindset. Every decision will have unforeseen (at the time) negative or positive consequences.

Contribution: Active contributions and supportive engagement in board meetings should occur, such that constructive guidance and positive action follows. A board's function involves an interplay of shared knowledge, experience, and skills, which should be based on genuine empathy, situational awareness, and emotional intelligence.

Timely: Given the magnitude of the unfolding crisis, action-orientated boards are necessary, and if necessary, decisions should be executed in real time.

Organized: Poor organization of meetings or communications should not be tolerated, even though remote working is currently the norm. In fact, remote meetings are proving to be more robust than their face-to-face versions, as participants are more relaxed in their home setting and casual dress makes for a less stressful but still a professional environment. The solution to voluminous e-mails is to agree an organization protocol such as no e-mails during key holidays and a 24-hour response period. Technology such as Microsoft Teams allows seamless face-to-face connectivity.

Relax: This is an unprecedented crisis, and the organization will be besieged by internal and external pressure, which must be managed; otherwise, there will be ill-health and absence, which will only worsen the status quo. Consequently, the board will need to balance and renew organizational resources, energy, and health, to ensure a healthy workspace albeit remotely.

Yahoo: Celebrate even small wins and dispassionately learn from mistakes, as ultimately all boards and companies are comprised of imperfect human beings.

If the collective eye of the board is on the survival of the company and value creation for all, they will experience VICTORY. This Pompeii Event and the application of VICTORY has *the potential for the renaissance of the classic understanding of the shareholder—board—management interface, where the board is a genuine proxy for shareholders, and corporate governance where the functioning of the board is the method through which companies are directed and controlled.*

CHAPTER 6

Conclusion

On December 31, 2019, Wuhan City health officials reported a strange collection of 27 pneumonia cases, the origin of which was unknown, but with an initial source connected to the infamous but currently closed Wuhan Wet Market. This was later established to be a novel coronavirus (2019-nCoV) or COVID-19. The novel COVID-19 pandemic completely caught the world off guard, wholly unprepared and seemingly helpless in the face of the unprecedented socioeconomic fallout.

The pandemic has created a *new normal* that is leading to an unthinkable paradigm shift that is affecting everything, including how people live, work, and shop. Across the globe, governments have spent approximately $12Tn to combat the socioeconomic side-effects resulting from COVID-19, such as unparalleled state intervention to support the unemployed and small businesses.

In February 2020, the *lead author (Faisal Sheikh, England),* like millions across the globe, thought that a short, sharp, hard lockdown would solve the crisis. However, weeks became months, and the continued social distancing and restrictions disorientated the lead author, who was desperately attempting to find meaning during the global havoc and rising international death toll (the United States has suffered 500,000 deaths and counting), resulting from an invisible virus that appeared to be disrupting every facet of life. Emerging nations were particularly hard hit; for example, according to some commentators, during the inception of the pandemic more than 50 percent of Malaysia's small and medium sized enterprise (SME) sector closed.

During one late 2020 summer night as the lead author contemplated the crisis and crises in general, he began thinking about historical precedents such as the 1918 Spanish flu. Then, he had a sudden thought that the COVID-19 pandemic was analogous to the ancient Roman tragedy of *Pompeii* when the citadel was buried under 4 to 6 meters (13–20 feet) of volcanic ash and pumice after the eruption of Mount Vesuvius in AD 79. Within a matter of days, he managed to assemble a team of experts, notably all qualified accountants and practicing academics, residing in *England (Brian Leigh), Malaysia (Geetha Rubusundram)* and *Norway (Nigel Iyer*), and they began thinking how they could help businesses navigate this *Pompeii Event, that is, Accountants versus COVID-19.*

It became apparent that businesses regardless of size, sector, specialty, or geography were confronting a set of challenges for which there was no conventional wisdom or *playbook*. Most businesses appeared to maintain existing systems with information technology (IT)-based extensions such as Zoom to ensure management teams and workers could continue servicing customers from their homes. The authors decided that, based on their professional experience and environmental analysis, *agile innovation (Chapter 2), rigorous cash management (Chapter 3), all-encompassing fraud prevention and detection (Chapter 4), and dynamic corporate governance (Chapter 5) were critical success factors to survive this Pompeii Event.*

The following is a summary, Table 6.1, of the salient theories or metaphors and tools or techniques offered by the authors to help businesses to successfully thrive under the pressure of the pandemic, including an extensive appendix, which covers the financial reporting implications due to COVID-19.

Many organizations with a remote workforce will be experiencing the phenomenon of what the lead author calls *Green Productivity*. Communications and meetings are taking place virtually and located in people's homes, where the boundaries between management and subordinates are becoming blurred. Everyone has unwittingly introduced their families and partners and may even have jointly celebrated or acknowledged personal moments such as birthdays. The *professional (BLUE)* and *private (YELLOW)* have merged to create in most cases superior *productivity (GREEN)*, which can be leveraged for the benefit of the organization and the individual. Consequently, the authors believe it is important to realize that the successful implementation of any of the aforementioned techniques is based on the key assumption of empowered employees and management teams rooted in foresight.

As this conclusion is being written, the world is in the thick of the second wave of COVID-19 or the second *pyroclastic* flow from the eruption

Table 6.1 Summary of salient theories or metaphors and tools or techniques

Chapter	Theoretical lens	Toolbox
Chapter 1: Pompeii Event: The COVID-19 Catastrophe	– Pompeii Event – VUCA	– Critical success factors
Chapter 2: Innovation 101	– Schumpeter's 1953 innovation theory of trade cycle	– Jobs to be done – Ten types of innovation – Effective brainstorming – Frugal innovation
Chapter 3: Cash Flow Management 101	– Legitimacy theory – Resource-based theory – Pecking order theory – Progressive utilization theory	– Smash, grab, go – Working capital – Dashboards – Beyond budgeting – Zero-based budgeting – Going back to basics – Buy Now Pay Later – Sustainable finance
Chapter 4: Fraud 101	– Fraud Triangle – Pre-crime Fraud Triangle	– Fraud detective – Seven basic types of fraud – Ten reasons why fraud persists – Eight pathways to eradicate fraud – Online fraud detective type test
Chapter 5: Corporate Governance 101	– Emergence of corporate governance	– Types of corporate governance – Six principles of corporate governance – VICTORY model

of Mount Vesuvius, that is, *Pompeii Event*. However, teams of scientists have been working hard in the preceding months, and the rollout of the Pfizer BioNTech, The University of Oxford, AstraZeneca, and Moderna vaccines has not only raised morale but led to a rallying of the financial markets. However, humanity is still in trouble and far from out of the woods. The great 12th century poet Rumi wrote:

"The cure for the pain is in the pain"

"These pains you feel are messengers. Listen to them"

This extreme crisis can become a source of deep learning, if not renewal, once the lava from the eruptions cools and this Pompeii Event subsides. For example, it is argued that the aftermath of the European-wide, 14th century Black Death, which caused 200 million deaths, ushered in an era of positive economic growth and laid the foundations for the coming European Renaissance and Industrial Age.

The lead author believes that to survive and succeed during this uncertain and evolving pandemic, it is not enough to implement the outlined critical success factors. In fact, it is critical to embed foresight across all levels in the organization because it is a matter of when, not if, the next Pompeii Event suddenly erupts possibly in the shape of global warming. The great futurist Inayatullah (2007) states:

> Deconstructing the normalcy of the past, scenario planning directs our thinking towards foreseeable alternative futures that remind us that while we cannot predict a particular future always accurately, by focussing on a range of alternatives, we can better prepare for uncertainty, indeed, to some extent embrace uncertainty.

The breathtaking speed, scale and scope of COVID-19 has challenged all organizations to intentionally incorporate change, together with the capacity to pivot to the dynamic terrain of the future. The *new normal*, characterized by physical distancing, increasingly digital services, and remote working underpinned by digitally focused communications, is here to stay.

Finally, according to another noted futurologist Ziauddin Sardar, *postnormal times* is a stage of deep change highlighted by *complexity, chaos, and contradiction.* This will essentially make *decision making* for the foreseeable future highly challenging, due to a fast-moving external environment, coupled with constantly changing information, all in a flawed yet beautiful world**.** In short, what will ultimately separate the present and future winners from the losers will be those individuals or boards or companies or organizations who are mindful of the following:

> *We are drowning in information, while starving for wisdom. The world henceforth will be run by synthesizers, people able to put together the right information at the right time, think critically about it, and make important choices wisely.*
>
> —E.O. Wilson (1929) American Biologist

Appendix

COVID-19 Implications for Financial Reporting

Many entities that are trading in the unfolding COVID-19 pandemic will suffer loss of revenue, greater expenses, write-off of inventory, and will need to re-evaluate accounting policies, such as estimates, to ensure that they are consistently applied.

Most major accounting firms including the Big 4 firms have created superb online resources that lucidly explain the potential impact from the ongoing pandemic and summarize the key points of accounting standards covering the entire gambit from revenue recognition to onerous contracts. These guides will undoubtedly be vital for any company wondering how to apply the specifics of International Financial Reporting Standards (IFRS) due to the ongoing impact of COVID-19.

Consequently, the following are considered to be the major implications for financial reporting, as applicable to most types of entities covering IFRS where applicable or country-specific Generally Accepted Accounting Principles (GAAP).

Earnings Before Interest, Taxes, Depreciation, and Amortization (EBITDA)

Earnings before interest, taxes, depreciation, and amortization (EBITDA) and adjusted EBITDA are used by many businesses as a gauge of operating profitability and usually as a proxy or substitute for cash flow. The accounting metric is regularly used as a starting point to value businesses, and an analyst would normally apply a multiple to a company's EBITDA to help determine its enterprise value.

The exceptional economic impact of the COVID-19 pandemic has amplified the importance of these financial measurements, as borrowers attempt to maintain financial covenants in their credit agreements, and potential buyers and sellers struggle to ascertain whether EBITDA, if established without an adjustment for the financial impact of COVID-19, will supply a precise representation of a company's value. An example is in merger and acquisition (M&A) transactions, where a multiple of EBITDA is a familiar valuation technique for deciding the purchase price in an M&A transaction. However, as the crisis continues to unfold, some businesses are booming because of higher revenues (e.g., health care, pharmaceuticals, and technology). Thus, buyers may request a downward EBITDA adjustment to eradicate the impact due to the COVID-19-related revenue increase, consequently lowering the purchase price.

Outline of EBITDA and Adjusted EBITDA

EBITDA is one of the most utilized non-GAAP measurements of earnings. Although the inputs are normally based on GAAP principles, the terminology is not defined explicitly in GAAP.

Adjusted EBITDA is calculated by adding or deleting specific expenses to and from EBITDA, see Figure. A.1. This provides a better picture of

	Gross Operating Revenue
–	Operating Costs and Expenses
=	**Consolidated Net Income**
+	Interest Expense
+	Income Taxes
+	Depreciation and Amortization
=	**EBITDA**
+ /-	Permitted Adjustments and Add-backs
=	**Adjusted EBITDA**

Figure A.1 EBITDA and Adjusted EBITDA

a company's profitability and ensures sound comparison of a business both from year-to-year and crucially with its industry competitors.

Adjusted EBITDA

A company's EBITDA may not give the entire picture, as businesses will have nonrecurring or one-off items of revenue or expense or other revenues or expenses that would need to be standardized in order to achieve a more realistic profitability. Examples of common EBITDA adjustments include:

- One-off legal settlements or disbursements
- One-off revenue such as special projects
- Nonvalid business entertaining expenses
- Above- or below-market executive remuneration or benefits
- Above- or below-market rent expenses

EBITDA and Adjusted EBITDA in Credit Transactions

EBITDA is a critical metric in credit transactions, as it is often used by lenders to appraise whether or not the borrower has enough cash flow to service the loan. The definition of adjusted EBITDA is an extremely negotiated term in a loan agreement. Most loan agreements normally allow for add-backs to EBITDA for *extraordinary, nonrecurring, and unusual costs, expenses, and losses***.** It is important to note that these terms are not defined in loan agreements but are interpreted based on GAAP principles, for example U.S. GAAP, and universally accepted definitions of these terms;

1. *Extraordinary* is no longer defined in U.S. GAAP; but in the past, a cost arising from an event or transaction was considered *extraordinary* if the event or transaction was (a) unusual and (b) infrequent.
2. *Unusual* is defined by U.S. GAAP as an underlying event or transaction that is a nonrecurring or one-time gain or loss that is not believed to be part of normal business operations.

3. *Nonrecurring* is not defined in U.S. GAAP but is present in the Securities and Exchange Commission's (SEC's) rules and regulations concerning the use of non-GAAP financial metrics in public filings. Thus, an expense is *nonrecurring* if the expense is instigated by an event or transaction that has not occurred within the last two years and is not expected to repeat within the following two years.

The Impact of COVID-19 on EBITDA and EBITDAC

As COVID-19 continues to spread, the profitability of many organizations is being directly or indirectly hit. During government-sanctioned global lockdowns in March or April 2020, including recent *circuit breaker* (October 2020) lockdowns, most businesses were forced to close. This negatively impacted global supply chains as entities found it difficult to source materials, resulting in unfulfilled customer orders. Companies that were unable to pivot to a remote workforce such as aviation suffered a decline in revenues. Thus, the addition of the *C* to the EBITDAC metric is intended to quantify a company's losses attributed to the ongoing COVID-19 pandemic.

The following is a list of potential COVID-19-related expenses that could be negotiated as add-backs in determining adjusted EBITDA.

- Cessation fees and related expenses due to cancelation of contracts and events
- Higher pay for employees and contractors' pay in high-risk jobs such as the disposal of COVID-19-infected bodies
- Information technology (IT) expenses involving the facilitation of remote or tele-working, including software and license fees
- Marginal training and IT expenses resulting from converting employees to home working and then back to office working
- Higher than normal printing, shipping, and delivery expenses suffered in order to assist working from home
- Costs associated with deep cleaning and disinfecting facilities, more than usual, as per government regulations

- PPE costs, including the purchase of face masks for employees and customers and hand sanitizer
- COVID-19 testing kits for in-office employees

Illegitimate Add-Backs

Most businesses will probably find that their biggest COVID-19 loss is associated with lost revenue. In fact, this has become highly contested, because a German technology company Schenck Process LLC reportedly added back €5.4M to its earnings. The company argued that this is the amount it would have made had there not been the pandemic and was due to a state-enforced lockdown. Schenck Process LLC's operating profit for the period—*adjusted EBITDAC* of €18.3M—was 20 percent higher than the same period a year earlier, instead of 16 percent lower.

The authors believe that lost revenue will not be an allowable add-back in many accounting jurisdictions. As an example, the notion of *lost revenue* does not exist in U.S. GAAP, and other GAAP dominions also clearly state that lost revenue is not an allowable add-back. In fact, in March 2020 SEC published guidance, openly reiterating that lost revenue should not be presented in financial disclosures. Furthermore, the SEC provided guidance regarding expenses, which stated that only irregular expenses that resulted due to abnormal business could be added back.

In short, adding back lost revenue is dishonest, misleading, and tantamount to creative accounting, because it will never be regained.

Going Concern

Companies negatively affected by COVID-19, for example, small businesses or those in the areas of leisure and hospitality, travel, and aviation, will need to consider going concern issues. They should consider running different sensitivity analyses or scenarios to establish whether there is any material uncertainty as to their ability to continue as a going concern. This may result in further disclosures, particularly if there is a material uncertainty.

It may even be necessary, in some cases, to prepare the accounts on a going concern basis, which will be underpinned by the impact on future trading. Concerning the timeframe, the affected company will need to consider, as a minimum, the initial 12 months after the balance sheet date, or the date when the financial statements are signed off. However, the authors believe that it would be prudent to consider a longer timeframe, as the pandemic will probably end by 2022, but there will most probably also be a global recession occurring.

Events After the Reporting Period

The COVID-19 situation continues to be a fluid situation; thus, entities must consider applying the requirements of IAS 10, Events After the Reporting Period. IAS 10 covers two important categories:

Adjusting events: These are events that provide further information regarding conditions existing at the end of the reporting period. These events may result in alterations to the figures contained in the financial statements, if deemed necessary.

Nonadjusting events: These are conditions that only occurred after the end of the reporting period. Consequently, these will result in disclosures in the financial statements (where material) but will crucially not affect the amounts recognized in the financial statements.

The application of the impact of COVID-19 is probably dependent on an entity's year-end. Chinese authorities warned the World Health Organization as to several cases of an unusual strand of pneumonia, in Wuhan, by December 31, 2019. However, the important information about the virus and its magnitude only became apparent in early 2020. *Therefore, entities with reporting periods ending on or before December 31, 2019, will probably apply the developments as a nonadjusting event*. Thus, the figures in the financial statements will remain unaffected, but the disclosures should be detailed. The disclosures must explain the nature of the event and an estimate of its financial effect. Although it is challenging to quantify the financial implications, it is better to supply a range of estimated effects compared to not at all.

If the probable impact is that the entity is no longer a going concern, then it must alter its financial statements, which should be prepared on a break-up basis rather than a going concern basis. Consequently, all items as per the financial statements will be held as current rather than noncurrent, at their sale values, and specific items, for example, provisions relating to their closure, will need to be included.

It can be assumed that for any reporting event ending after January 31, 2020, COVID-19 will be an adjusting event. Thus, entities will need to review all the areas that are subject to judgment and estimation such as carrying values. The impact of the pandemic on these financial statements is probably going to be material and extensive. Entities will have to spend a considerable amount of time checking assumptions and estimations, and the detailed guides (online resources, mentioned earlier) are going to be extremely useful.

Although it is not possible to cover all the possible impacts, the following are the most widespread and urgent issues affecting almost every entity. They are revenue recognition, impairments, inventory, property, plant and equipment, and provisions. The authors will also briefly discuss debt instruments, which is a highly complex area of accounting and should be treated with care, and ultimately, professional guidance should be sought for all applications of accounting standards.

Revenue Recognition

Most entities' sales and revenue will decline due to the lower economic activity and consumer demand, following the steps taken to control the pandemic, such as lockdowns and social distancing. Entities will need to consider returns that are higher than normally expected, further price reductions, lost volume discounts, and penalties for late delivery. IFRS 15 Revenue Recognition, when considering contracts with customers, highlights that variable consideration is recognized only when it is highly likely that amounts recognized will not be altered when the uncertainty subsides. Consequently, senior management should reassess both its estimate of variable consideration and whether the recognition level is met.

IFRS 15 is applicable only to those contracts where senior management expects a customer to honor its obligations as they arise. Given the current pandemic, senior management might decide to continue supplying a customer even when they are fully aware that the customer might not be able to pay for some or all the goods being provided. This is problematic, if not blatant accounting fraud, as revenue is recognized only when it is probable that the customer will pay the transaction price when it is due, net of any price discount.

IFRS 15 posits that an entity is required to reveal information that allows users to understand the nature, amount, timing, and uncertainty of cash flows arising from revenue. Thus, any uncertainty arising due to the COVID-19 pandemic that impacts revenue must be disclosed such as whether a customer is able to pay and the material estimates made, for example, in connection with variable consideration.

Impairments

The possibility for impairments in the ensuing pandemic climate is considerable. There is a high risk of impairment to goodwill, as the acquisition price of an entity will have more than likely been calculated based on estimated cash flows. When the annual goodwill impairment test is performed by entities applying IFRS standards, they must compare the carrying amount of the goodwill with its recoverable amount. A major constituent for assessing recoverable amount is to estimate the present value of future cash flows, which are probably going to be lower. It is important to acknowledge that currently goodwill impairment cannot be reversed, meaning that the current pandemic could have a long-term effect on this asset value.

Inventory

The COVID-19 pandemic has caused major disruptions to global supply chains, and coupled with lower consumer demand, may cause decreases to the net realizable value of inventories. Therefore, entities will need to assess whether the carrying value of their inventory needs to be written down. These write-downs could be due to slow movement in inventory, cheaper commodity prices, or inventory obsolescence due to lower-than-expected sales.

IAS 2 Inventories, states that fixed production overheads are included in the cost of inventory based on normal production capacity. Reduced production may affect the extent to which overheads can be included in the cost of inventory. Entities will need to assess the materiality of any write-downs and if they require disclosure in accordance with IAS 2.

Property, Plant, and Equipment

The COVID-19 pandemic has caused global lockdowns, which will probably mean that property, plant, and equipment is underutilized or will remain idle for a period of time, or that capital projects are suspended.

According to IAS 16 Property, Plant, and Equipment, there is a requirement that depreciation continues to be charged in the income statement, even if an asset is provisionally idle.

IAS 23 Borrowing Costs states that the capitalization of interest is suspended when development of an asset is postponed.

Provisions

IAS 37 Provisions, Contingent Liabilities and Contingent Assets, states that in order to recognize a provision where an entity has a present obligation; it is likely that an outflow of funds is required to clear the obligation, and a consistent estimate can be quantified.

Regarding senior management's actions in connection with COVID-19, this should only be accounted for as a provision if there is a present obligation for which the outflow of economic benefits is probable and can be reliably estimated. For example, a provision for restructuring, due to home-working, should only be recognized when there is a comprehensive and official plan for the restructuring, and senior management have created a binding expectation in those affected that the plan will be executed.

IAS 37 does not allow provisions for future operating costs or future business recovery costs.

IAS 37 expects that an entity clearly reveals the nature of the obligation and the forecasted scheduling of the outflow of economic benefits or monies.

Leases

A lessor and a lessee may potentially renegotiate the terms of a lease due to COVID-19. Thus, a lessor might allow a lessee a dispensation in relation to the lease payments. In other cases, a lessor may enjoy government-backed compensation as an inducement to offer such dispensations. Consequently, both lessors and lessees should consider the requirements of IFRS 16 Leases and whether the dispensation should be accounted for as a lease adjustment and extended over the remaining period of the lease.

Lessors and lessees should also consider whether inducements received from a government body are government grants and apply the relevant standard, namely, IAS 20 Accounting for Government Grants and Disclosure of Government Assistance.

Financial Instruments

An entity may have financial instruments on its financial statements, and this may include loans, trade, and other receivables, debt instruments not measured at fair value through profit or loss, contract assets, lease receivables, financial guarantees, and loan commitments. It will then need to consider the implications of IFRS 9 Financial Instruments' Expected Credit Loss model (ECL) due to the COVID-19 pandemic. Senior management will need to ascertain if the ECL is measured as a 12-month or lifetime ECL. If the credit risk (risk of nonpayment) has increased dramatically, then so will the estimate of ECL. For example, if a borrower's repayments become delayed due to the impact of COVID-19, there will still be a credit loss if the lender is not compensated for the lost time value of money.

In addition, IFRS 9 Financial Instruments expects entities to consider progressive information, including macro-economic data, when ascertaining whether there has been a material increase in credit risk and when measuring ECLs. Consequently, progressive information should include impact of the spread or the downside of the COVID-19 pandemic on ECLs.

Lenders may voluntarily, or under government advice, offer payment holidays on current loans or lower fees and interest rates on new loans. This action may impact ECLs, because payment deferrals imply a higher credit risk or default, and lower fees or interest rates on new lines of credit suggest that the loans are not made at market rate.

Senior management should consider the requirement to highlight the impact of the virus on the impairment of financial assets and disclosures as required by IFRS 9. Disclosures due to the pandemic, disclosures may include how the impact of progressive information has been incorporated into the ECL estimate, information regarding major changes in assumptions made in the reporting period and thus changes in the ECL.

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Calling Out COVID-19

Business Strategies for Surviving a 'Pompeii Event'

Faisal Sheikh • Nigel Krishna Iyer • Brian Leigh • Geetha A. Rubasundram

We are currently experiencing the latest wave of an unprecedented global pandemic—the COVID-19 crisis which is decimating established industries such as tourism and hospitality and causing the deaths of millions of people worldwide. The authors believe that the pandemic is comparable to the Ancient Roman tragedy of Pompeii when the citadel was buried under four to six metres (13–20 feet) of volcanic ash and pumice following the eruption of Mount Vesuvius in AD79.

This book is written for business owners, entrepreneurs, leadership and management teams in the public and third sector and professionals who are currently dealing with the COVID-19 pandemic. It offers tools and techniques within the economics of innovation, other frameworks such as the Fraud Triangle and the authors' extensive experience including rigorous cash management, practical fraud prevention and detection and advice on implementing and refining corporate governance structures. The book will also be of interest to postgraduates, including MBA students and business researchers.

The book concludes by summarizing the key theories that can be used to understand the impact of this Pompeii event and offers pragmatic solutions to fight the economic impact of COVID-19. The authors argue that the organisations rooted in foresight will survive and emerge as future trailblazers. An extensive appendix is also included which outlines the implications for financial reporting.

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