

Navigating today's complex business risks

Europe, Middle East, India and Africa
Fraud Survey 2013



Contents

| | |
|-----------|---|
| 1 | Foreword |
| 2 | Executive summary |
| 4 | Managers feel increased pressure to deliver growth |
| 8 | Unethical business practices – spotlight on fraud |
| 12 | Bribery and corruption – a stubborn stain |
| 16 | Compliance programs – always more to do |
| 20 | Conclusion – navigating the risks |
| 22 | Selected country results |
| 24 | Survey approach |
| 25 | Contact information |

Foreword

None of us can be in any doubt about the level of pressure on today's businesses. All are operating in extremely challenging conditions, with instability across many markets, sluggish or minimal growth in others and an aggressive enforcement environment around the world.

Our survey asked over 3,000 board members, executives, managers and their teams across 36 countries about the nature of this pressure. We wanted to understand how it was being felt and its impact on business conduct.

The results make for uncomfortable reading. We found that executives and their teams are indeed under increased pressure – and it is being felt personally. They are also bleakly realistic about the market challenges they face.

Furthermore, our survey shows that to find growth and improved performance in this environment, an alarming number appear to be comfortable with or aware of unethical conduct. This includes recording revenues early, underreporting costs or encouraging customers to buy unnecessary stock. This is coupled with the perception that bribery and corruption remain widespread in several markets.

Whether this behavior is driven by pressure to deliver unrealistic results in difficult markets, or a desire for increased personal recognition and reward, the fact that it is as widespread as our results suggest will be of real concern to management and boards.

The results also show that many in business are either ignoring, or are blind to, these risks. We continue to see too many executives thinking fraud and corruption are problems faced only by other companies or in other sectors. We continue to see individuals espousing the view that compliance programs are irrelevant to their roles. And we continue to see business leaders failing to ask enough questions – whether about the third parties they are engaging with, or the financial results they are being presented with from other parts of the business. This is particularly the case in rapid-growth markets.

Given these results, we have also provided details of some features that we have observed in businesses that effectively manage fraud, bribery and corruption risks. Successful businesses consistently acknowledge that the risks are real. And then they never stop asking difficult questions and demanding answers.

Our survey shows that if you don't ask those difficult questions, there is a high risk that you are overlooking significant threats to your business.

Sincerely



David L. Stulb

Global Leader
Fraud Investigation & Dispute Services



42%

of board directors and senior managers are aware of some type of irregular financial reporting in their company, page 8



57%

of respondents feel that corrupt practices are widespread in their country, page 13



49%

of sales staff do not consider their company's anti-corruption policy to be relevant to their work, pages 18 and 19

Executive summary

Our survey of over 3,000 board members, managers and their teams delivers three clear messages:

Executives and their teams are under increased personal pressure to produce growth in extremely challenging conditions.

Unethical conduct – including fraud, bribery and corruption – in response to this pressure is not just a hypothetical risk. One in five respondents have seen financial manipulation occurring in their companies. Fifty-seven percent believe that bribery and corruption are widespread in their country.

Compliance programs work, but not well enough. Companies that do not keep asking the right questions – and demanding answers – are exposing themselves to significant risk.

Feeling the pressure

According to our survey, the vast majority of businesses are under increased pressure to meet the targets of their investors and owners, and deliver improved financial performance.

They are also facing pressure to cut costs – and individuals are feeling this personally through pressure on their salaries and bonuses.

There is little optimism among our respondents that market conditions will improve over the next year.

So, if the market is not going to pick up, how does management deliver improved performance? Do they expand into rapid-growth markets, where winning contracts can go hand-in-hand with corruption? Do they look to further reduce costs, putting pressure on suppliers or staff? Or do they take a much bigger risk? Do they distort performance reports?

Strain on ethical behavior

One in five of our respondents have seen financial manipulation of some kind occurring in their own companies. In rapid-growth markets, over a quarter of respondents are witnessing manipulation such as overstated sales and understated costs.

Furthermore, management is clearly aware of this issue. Forty-two percent of board directors and senior managers are aware of some type of irregular financial reporting in their company. Within finance this amounted to almost a quarter of respondents.

Overall, more than a third of respondents believe that companies in their countries often reported their financial performance as being better than it was. While this isn't necessarily consistent with our experience in dealing with senior executives, if these perceptions are reflected in actual conduct, this is deeply troubling. Businesses have good reason to look critically at what is being reported to headquarters and ask the question: do these results add up?

The risk from misreporting is compounded by the risk to the business from corrupt practices. Our survey shows that there remains a significant proportion who see bribery and corruption as acceptable.

- ▶ In rapid-growth markets, 67% think that bribery and corrupt practices are widespread
- ▶ More than a quarter of sales and marketing respondents consider offering personal gifts or services to win or retain business as acceptable – almost double that of all respondents

Yet, as in previous surveys, many respondents appear to be in denial about how close bribery and corruption are to home. They see it happening widely in their country, but when asked about its occurrence in their sector, they hold a different view. The results seem to say: "Everyone else is doing it, but not me or my business."

The reality, however, is more likely to be that if it is happening in your country, it is happening in your sector. And if it is happening in your sector, it may well be happening in your business.

Navigating the risks

Compliance messages are getting through to employees. For example, the majority of respondents are aware that their company has an anti-bribery policy. But these results do not tell the whole story.

First, management appears to think compliance programs are more effective than they actually are. Sixty-seven percent of board directors and senior managers believe their commitment to anti-bribery and anti-corruption policies has been strongly communicated, compared with 44% of other employees.

Second, compared to our 2011 Survey, fewer people consider their company's compliance program to be relevant to their work. Fewer than half thought that their colleagues would say it was fairly or very relevant.

Third – and perhaps of most concern to compliance executives – over one in six respondents feel their compliance program harms their competitiveness. This raises the question: what choices do these individuals perceive when conducting business? Are they stuck in a mind-set of false choice between being compliant and winning the work?

Businesses will always manage these risks differently. One size does not fit all, even in a single business, let alone across sectors and geographies. But we find that businesses that manage the risk of fraud, bribery and corruption most effectively share some common features:

They own the problem. Boards and senior management acknowledge that the risk is real for them and their business.

They deal with the issues. Teams across businesses, functions, geographies and grades understand that the risks are relevant to them and their work.

They communicate the risks and the benefits. The costs of fraud, bribery and corruption are understood at an individual level. Behavior is not only limited by controls, but is driven by a common culture.

They focus effort. Squeezing efficiencies out of shrinking resources is a necessity in today's environment. Identifying specific risks and focusing resources on these is therefore increasingly important.

They ask questions and demand answers. Management is not afraid to ask difficult questions or turn over stones, knowing that what is hidden cannot be ignored.

Not everyone follows this approach. In fact, one-fifth of respondents in rapid-growth markets stated that management is asking fewer questions regarding the reliability of revenue.

The message from our survey is this: businesses face significant threats and must be aware and take action to navigate these risks.

“Management appears to think that compliance programs are more effective than they actually are.”

Managers feel increased pressure to deliver growth

Our survey confirms what executives across sectors and geographies know: they and their employees are personally under increased pressure to produce growth – in extremely challenging conditions.

Markets remain volatile and, in many countries, there is little optimism that conditions will improve in the short term. Even so, the vast majority of businesses are under increased pressure to meet the targets of their investors and owners.

Specifically, our survey shows that managers in these businesses feel under pressure to deliver improved financial performance, while understanding the realities of the market challenges they face. Only 22% of respondents in mature markets believe that market conditions will improve over the next year.

So where, and how, does management find and deliver the expected growth and profitability? Do they achieve it through expansion into rapid-growth markets, where winning contracts can sometimes go hand-in-hand with bribery or corruption? Or do they further reduce costs, putting pressure on suppliers or their own staff, for example by squeezing salaries and bonuses?

As getting more for less becomes more challenging, some managers may see another option: meeting targets by misrepresenting performance.

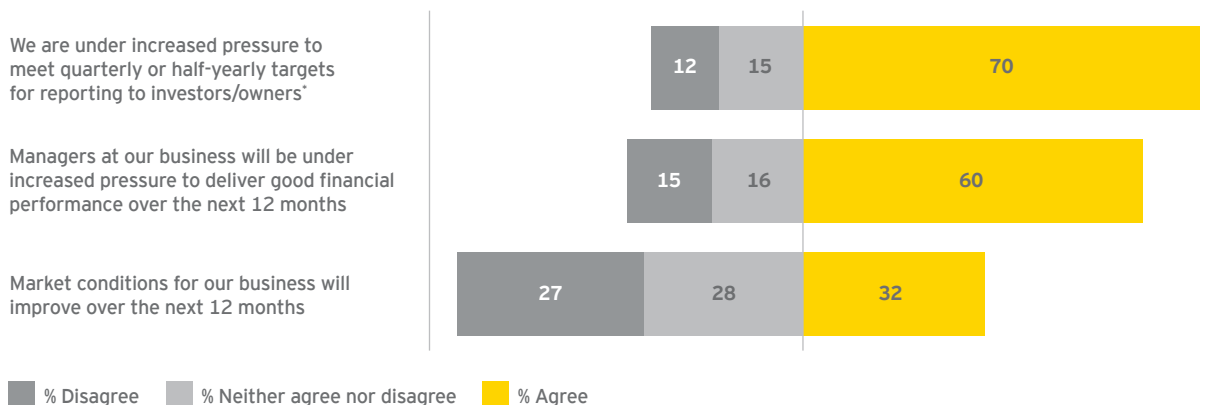
Pressure in rapid-growth markets

The increased expectation of strong financial performance from rapid-growth markets is being felt directly by managers in those regions. Over a third of respondents “strongly agree” that management will be under increased pressure to deliver good financial performance over the next year.

It is possible that the economic conditions in these markets will provide increased opportunities. In contrast to the mature markets, 47% of respondents in rapid-growth economies think market conditions will improve over the next year.

However, our survey also shows that, in rapid-growth markets, there remains a greater perceived risk that bribery or other unethical practices may be used to win business. Businesses in these markets are also seen to be more likely than those in mature markets to misrepresent their actual financial performance.

Figure 1
Increasing financial pressure



Q: To what extent do you agree or disagree with each of the following statements?

Base: All respondents (3,459)

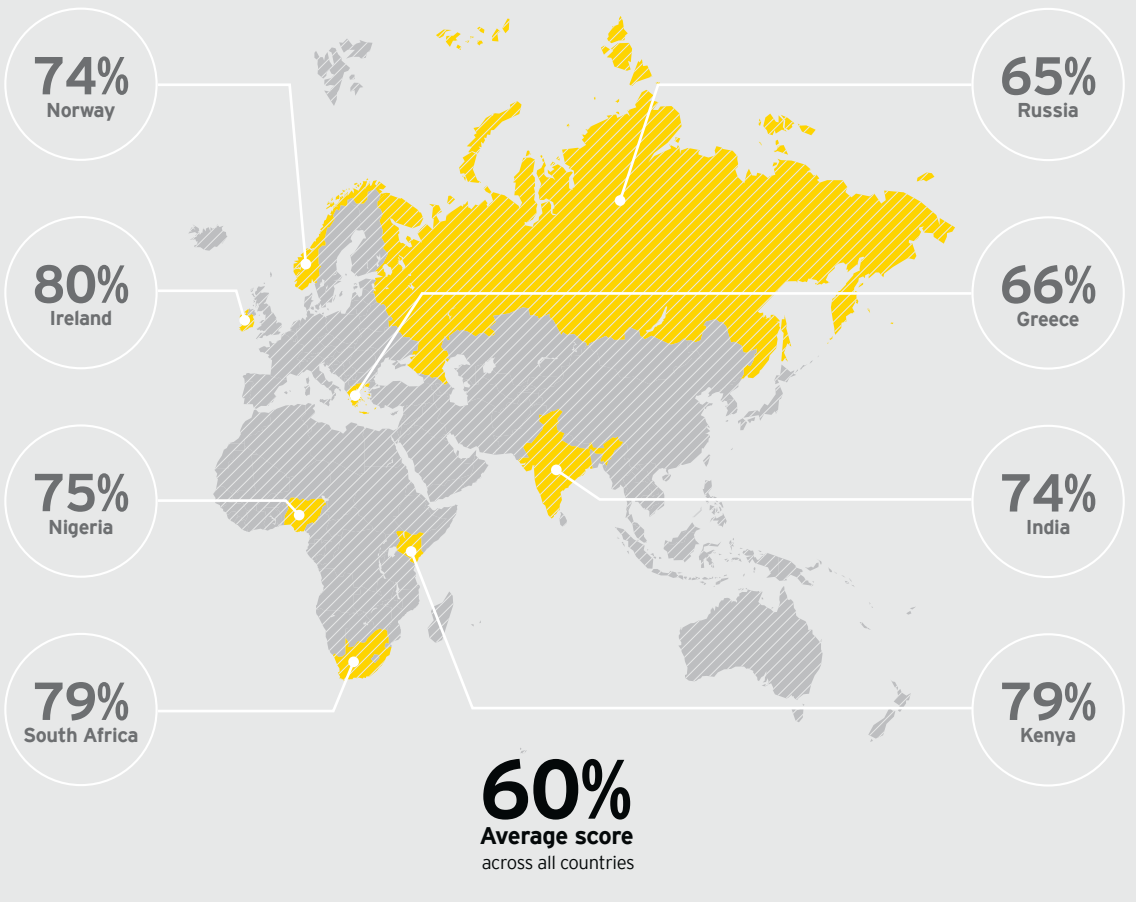
The “Don’t know” percentages have been omitted to allow better comparison between the responses given.

* Statement only asked if company is listed on the stock exchange (821)

Figure 2

Feeling the heat

% Agree: Managers at our business will be under increased pressure to deliver good financial performance over the next 12 months

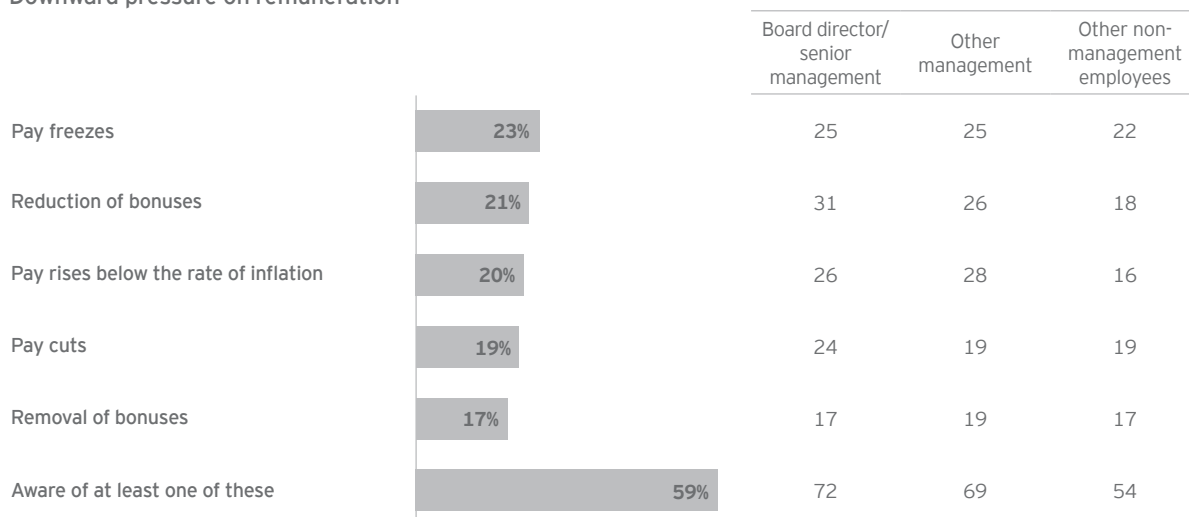


Q: To what extent do you agree or disagree with the following statement? Managers at our business will be under increased pressure to deliver good financial performance over the next 12 months.

Base: Ireland (100); Greece (100); Russia (100); Norway (100); Nigeria (103); South Africa (100); Kenya (100); India (100)

A breakdown for all countries included in the survey is shown in "Selected country results" on p22 (Table 1).

Figure 3
Downward pressure on remuneration



Q: Are you aware of any of the following affecting people at the department or division of the company you work for in the last 12 months?
 Base: All respondents (3,459); Board director/senior management (246); Other management (769); Other non-management employees (2,444)
 The "Don't know" and "Not aware of any of these" percentages have been omitted to allow better comparison between the given responses.

Cutting costs – increasing risk?

Is management cutting costs and putting pressure on teams in ways that could increase the risk of unethical practices or misrepresented performance?

Our survey asked about the downward pressure on salaries and bonuses. Board and senior management level respondents were understandably most aware of pay cuts, pay freezes or below-inflation rises, as well as reductions in or removal of bonuses. The vast majority were seeing these cost-cutting strategies in their business; only 25% were not aware of any.

Below board and director level, however, we still found the majority of respondents observing downward pressure on pay and remuneration. In rapid-growth markets, where the battle for talent remains fierce, individuals are seeing more reductions in their remuneration than in developed markets. In particular, reductions or removal of bonuses appear to be hitting businesses in rapid-growth markets more than mature markets. In India, 43% of respondents were witnessing this.

Greater pressure to deliver growth and downward pressure on reward can be a risky combination. Both pressures can, in some cases, drive actions that could damage the business, such as fraud, bribery and corruption. The incentives for unethical conduct can be strong when personal remuneration is at stake and pressure to deliver growth is being felt directly. At the same time, a focus on growth and cutting costs can weaken the systems and teams in place to prevent and detect these actions.

Any sense that unethical conduct is acceptable will increase the risks significantly. Our survey findings in later sections of the report indicate that a significant minority of respondents across markets and sectors continue to see unethical conduct in their organization.

A photograph of a rocky coastline with blue water and a white text box. The rocks are dark brown and layered, with some water splashing against them. The text box is white with a black border and contains the following text:

The incentive for unethical conduct can be strong when personal remuneration is at stake and pressure to deliver growth is being felt directly.

Unethical business practices – spotlight on fraud

The pressure to deliver growth and strong financial performance in difficult conditions is evident. But are executives, managers and their teams willing to cut corners or even act illegally to meet increasingly aggressive targets?

Our results show that fraud or other unethical conduct is not just a hypothetical risk. There is pressure on executives and businesses to deliver results in extremely challenging conditions. There is also a perception that unethical conduct is widespread in some countries. A significant minority of respondents say that unethical conduct is occurring in their own businesses in an effort to meet short-term financial targets.

Do key stakeholders have a complete and accurate picture?

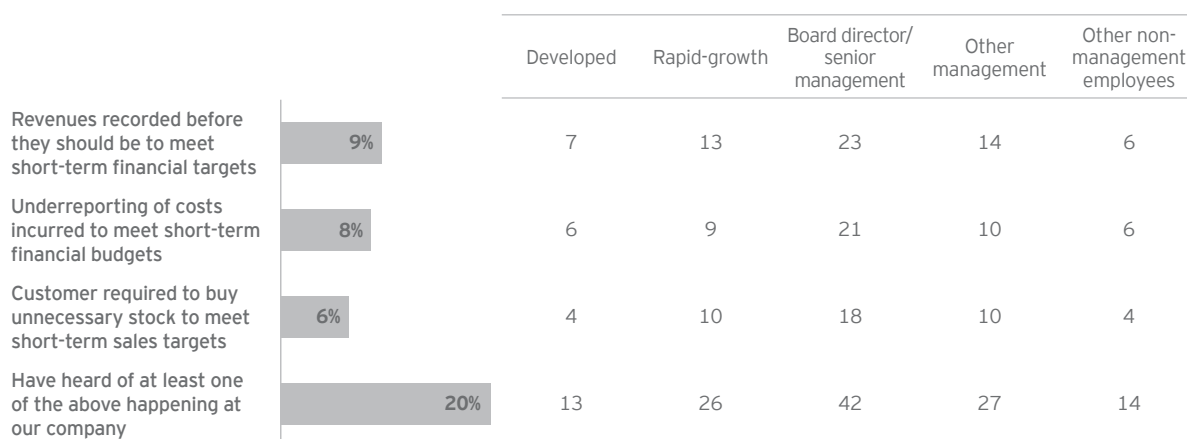
Our survey results show that financial performance within companies may be distorted:

- ▶ One in five respondents have seen financial manipulation of some kind occurring in their own companies (see figure 4).

- ▶ It is more pronounced in rapid-growth markets, where over a quarter of respondents are witnessing this behavior.
- ▶ The most common examples reported relate to overstated sales and understated costs.
- ▶ In the financial services sector – where regulatory action has been intense – 9% of respondents had seen revenues recorded before they should have been; 7% were aware of underreporting of costs; and 9% knew of customers being sold unnecessary products to meet short-term sales targets. Historically, this particular issue has hit financial services companies hard, with a number of institutions paying compensation to customers for mis-selling products and services, as well as incurring hefty regulatory fines.

In such circumstances boards and audit committees should ask tough questions of management and others about their company's results.

Figure 4
Unethical conduct by organizations including directors and senior managers

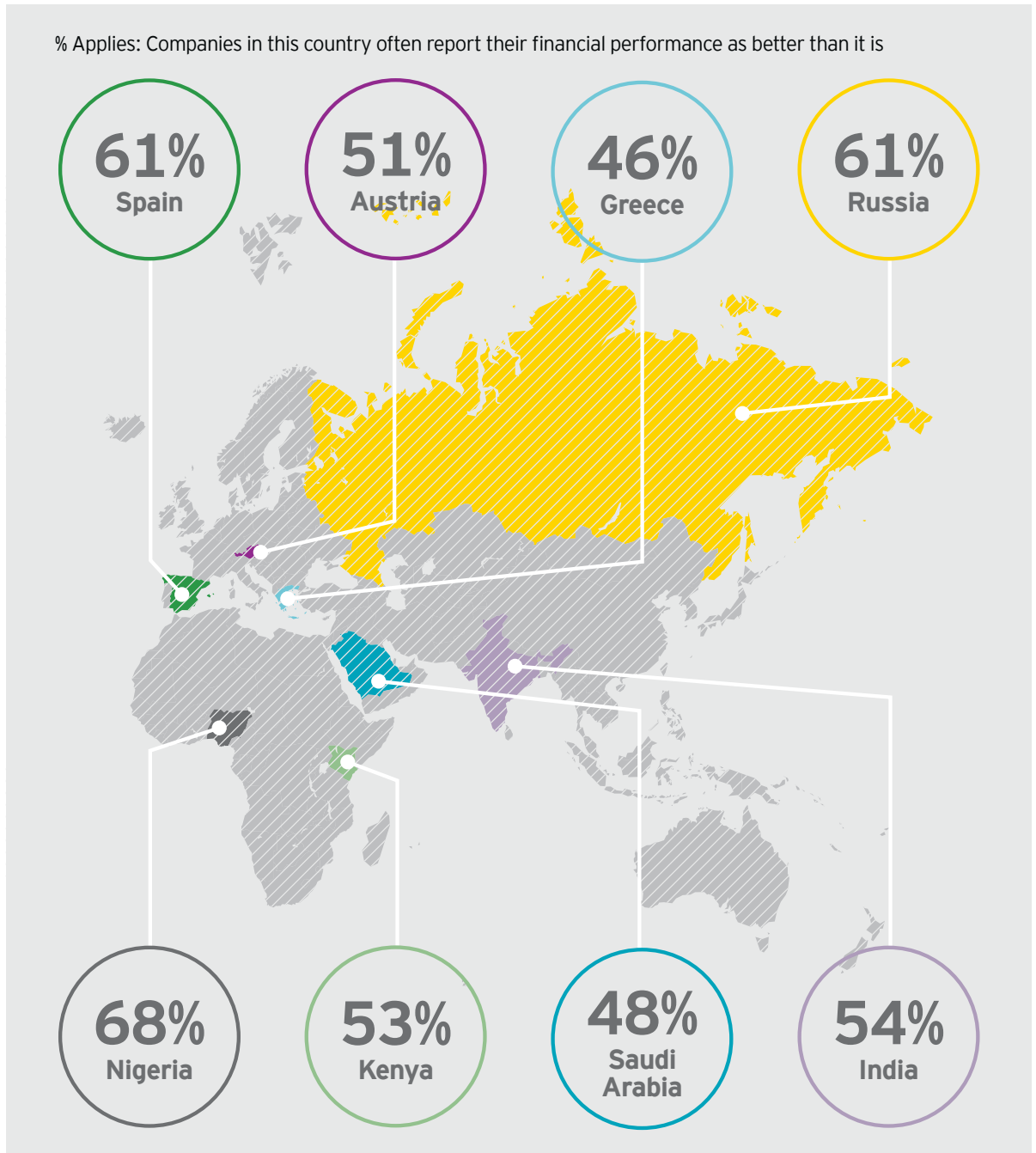
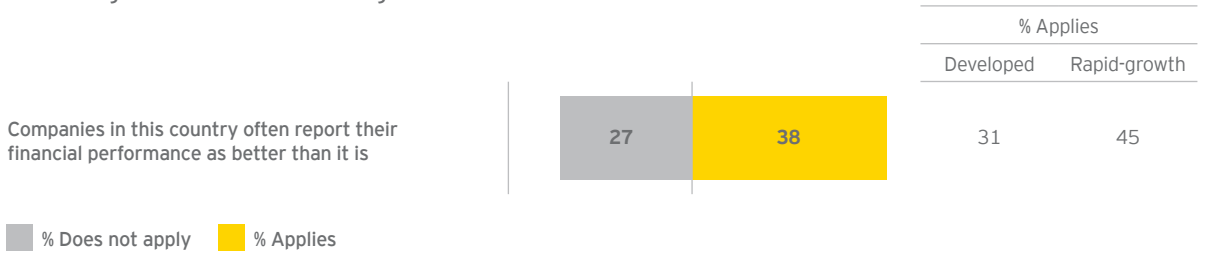


Q: Which, if any, of the following have you heard of happening at your company in the last 12 months?

Base: All respondents (3,459); Developed (1,500); Rapid-growth (1,103); Board director/senior management (246); Other management (769); Other non-management employees (2,444)

The "Don't know" and "Not heard of any of the above" percentages have been omitted to allow better comparison between the given responses.

Figure 5
Promoting the business or “cooking the books”



Q: Can you indicate whether you think the following applies, or does not apply, to your country or industry? Companies in this country often report their financial performance as better than it is.
 Base: All respondents 2013 (3,459); Developed (1,500); Rapid-growth (1,103); Austria (100); Greece (100); India (100); Kenya (100); Nigeria (103); Russia (100); Saudi Arabia (100); Spain (100)
 The “Don’t know” percentages have been omitted to allow better comparison between the responses given.
 A breakdown for all countries included in the survey is shown in “Selected country results” on p22 (Table 2).

Is management aware and taking necessary action?

These results are concerning enough on their own, but our survey also shows that management is clearly aware of this issue.

Forty-two percent of directors and senior management are aware of some type of irregular financial reporting in their company. Within the finance area, nearly a quarter of respondents are aware.

To understand whether these misstatements – identified by directors and senior management – were manifesting themselves in financial reporting, we asked whether financial performance was being consistently overstated by companies in their countries.

Thirty-eight percent of all respondents – and 45% of those in rapid-growth markets – believe companies in their countries often report financial performance as better than it is (see figure 5). Sixty-one percent of respondents in Spain believed companies often exaggerated their results – showing that the practice is not limited to rapid-growth markets.

The results also serve as a warning for multinational companies with subsidiaries in, for example, India (where 54% think financial performance is often exaggerated), Russia (61%) or Nigeria (68%). These businesses have good reason to look critically at what is being reported back to the center from other jurisdictions.

Too good to be true? Asking difficult questions

Accurate financial reporting is essential in order for businesses to understand performance. However, if management does not conduct a sufficiently rigorous review or fully understand local operations, there is a risk that poor performance can be hidden and management intervention delayed.

From our observations during fraud investigations, inflating revenue through fictitious or early recognition or hiding costs can be the result of a variety of practices. These include raising invoices early and using provisions to manage the release of profit. Yet these strategies can be identified if management looks closely and asks the right questions:

- ▶ Are reported results consistent with the cash requirement and cash performance of the business?
- ▶ Are balance sheet metrics, such as inventory and accounts receivable, keeping pace with changes in sales?
- ▶ How does performance compare to other business units? Are relative changes in line with your expectations? Is one business performing exceptionally?
- ▶ Is the business unit responsive to more detailed questions about reported results?
- ▶ What visibility do you have over aspects of performance that can be verified independently such as cash and inventory?
- ▶ How do reported results compare to other information such as recruitment patterns or recent new customer wins?
- ▶ Does the business regularly report results in line with budget?



Bribery and corruption – a stubborn stain

Compliance programs developed to counter bribery and corruption have been in the spotlight for several years. Our survey results show that, even though compliance messages are getting through, a significant proportion of respondents still see unethical behavior as acceptable.

When asked if certain unethical practices would be acceptable to help a company win or retain business, 52% of respondents did not feel any of them to be justified. This is a similar percentage to our *Global Fraud Survey* published in 2012 and our 2011 *European Fraud Survey* and significantly up from 41% when we first asked this question in 2009.

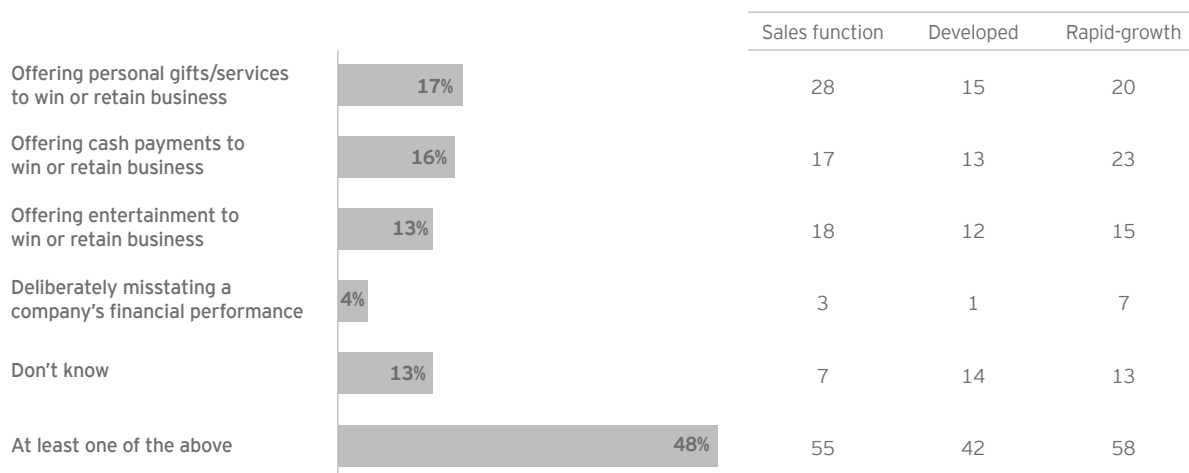
It is clear that the compliance messages are getting through to employees. A majority of respondents are aware that their business has an anti-bribery policy and many are aware of its content.

However, when asked about the prevalence of unethical practices in their country, respondents give a very different picture of the risk. In rapid-growth markets, 67% think that bribery and corrupt practices are widespread. In mature markets, more than a third think the same.

Our results show that, despite the existence of compliance programs and awareness of them, a significant and influential group still regards unethical business practices as acceptable. They are willing, for example, to make cash payments or offer personal gifts or entertainment to win or retain business. Compliance teams should therefore be under no illusion; there is still some way to go:

- ▶ More than a quarter of sales and marketing respondents consider offering personal gifts or services to win or retain business as acceptable – almost double that of all respondents.
- ▶ In rapid-growth markets, over half of respondents may condone one or more of the unethical practices described in our survey.
- ▶ In India, over a third of respondents feel offering cash payments to win or retain business can be justified – triple that of Western Europe.

Figure 6
Unethical practices seen in organizations



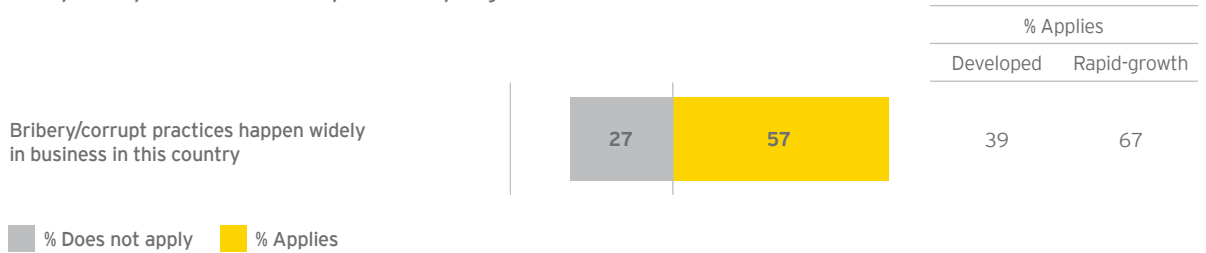
Q: Which, if any, of the following do you feel can be justified if they help a business survive an economic downturn?
Base: All respondents 2013 (3,459); Sales (238); Developed (1,500); Rapid-growth (1,103)

Figure 7
Compliance message getting through



Q: For each of the following, please can you tell me whether it applies, or does not apply, to your organization or whether you don't know?
 Base: All respondents (3,459); Developed (1,500); Rapid-growth (1,103)
 The "Don't know" percentages have been omitted to allow better comparison between the responses given.

Figure 8
Acceptable practices in developed and rapid-growth markets



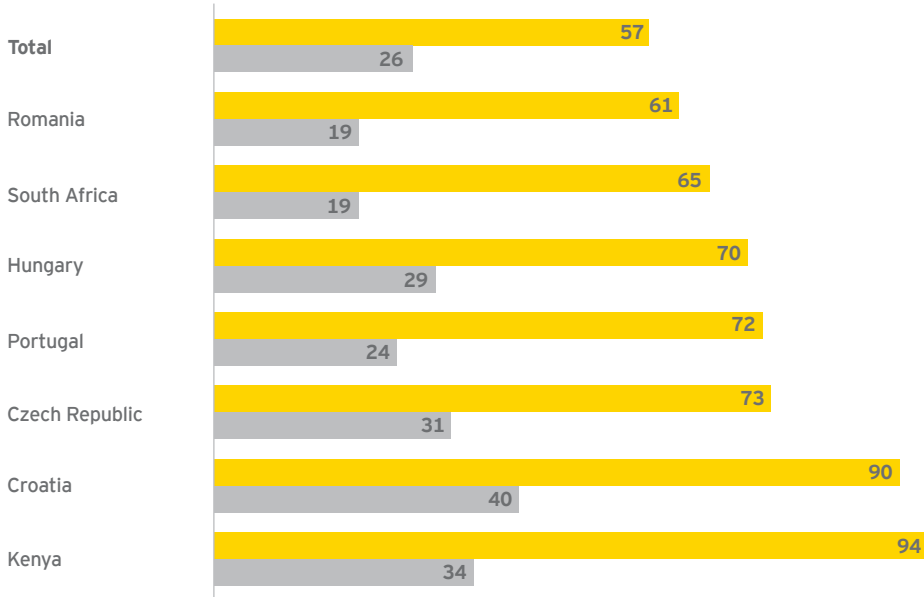
Q: Can you indicate whether you think the following applies, or does not apply, to your country or industry?
 Base: All respondents (3,459); Developed (1,500); Rapid-growth (1,103)
 The "Don't know" percentages have been omitted to allow better comparison between the responses given.

It couldn't happen here

As in previous surveys, many of our respondents appear to be in denial about how close bribery and corruption are to home. They see it happening widely in their country, but when asked about its occurrence in their sector, they hold a different view. The results seem to say: "Everyone else is doing it, but not me or my business."

For example, 57% of all respondents feel that corrupt practices are commonplace in their country. But only 26% feel it is common to use bribery to win contracts in their sector (see figure 9).

Figure 9
The corruption perception gap



■ % Applies: Bribery/corrupt practices happen widely in business in this country
 ■ % Applies: In our sector, it is common practice to use bribery to win contracts

Q: For each of the following, can you indicate whether you think it applies, or does not apply, to your country or industry?
 Base: All respondents (3,459); Romania (100); South Africa (100), Hungary (100); Portugal (100) Czech Republic (100); Croatia (100); Kenya (100)
 The "Don't know" percentages have been omitted to allow better comparison between the responses given.
 A breakdown for all countries included in the survey is shown in "Selected country results" on p23 (Table 3).

Our own experience of investigations across these regions, as well as the evidence from publicly reported regulatory investigations, settlements and prosecutions, indicates that most sectors are prone to unethical business practices.

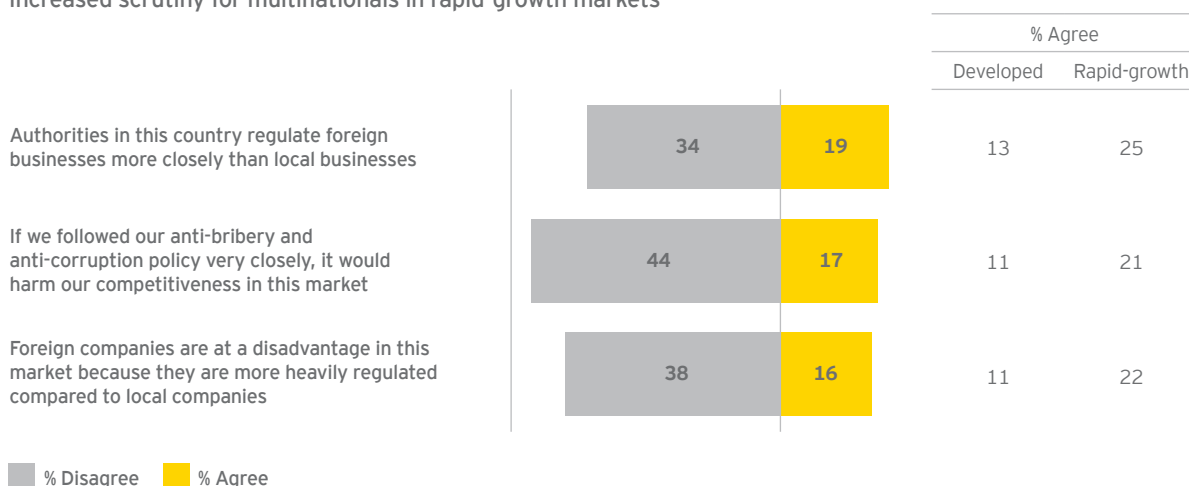
Favoring the home team?

It cannot be assumed that a large multinational will be given an easier time by local regulators just because of its importance to the local economy. Our survey results suggest the opposite: multinationals may be *specifically* targeted by regulators in rapid-growth markets.

We asked respondents about regulators in their own countries and the extent to which they focused on foreign companies. The results indicate that businesses headquartered in mature markets face increased scrutiny from regulators in rapid-growth markets. A quarter of respondents in rapid-growth markets agree that their domestic authorities regulate foreign businesses more closely than local ones.

It is therefore essential that multinationals understand the rapid-growth markets in which they operate as well as, if not better than, more developed markets. However, the survey results raise questions about whether this is happening in practice. Responses from those in rapid-growth markets with local headquarters suggest a much higher awareness of fraud and corruption risk than those based, for example, in Western Europe. Forty-six percent agree that companies in their countries often misrepresent financial performance, compared with only 29% of those with headquarters in Western Europe. Nearly three-quarters agree that corrupt practices are widespread in business in their country, compared with 58%.

Figure 10
Increased scrutiny for multinationals in rapid-growth markets



Q: To what extent do you agree or disagree with each of the following statements?

Base: All respondents (3,459); Developed (1,500); Rapid-growth (1,103)

The "Don't know" and "Neither agree nor disagree" percentages have been omitted to allow better comparison between the responses given.

A breakdown for all countries included in the survey is shown in "Selected country results" on p23 (Table 4).

Involved in acquisitions? Skepticism is crucial

Given the perception that bribery and corruption can be prevalent in rapid-growth markets, it is important for businesses to be vigilant when considering expansion through acquisition in these markets. The phrase "buyer beware" has never been more appropriate.

Businesses need to:

- ▶ Understand who the business partners and agents of the acquired business are through risk-focused due diligence
- ▶ Understand how key operating licenses, contracts or resources were won by the company
- ▶ Understand how key leaders in the business are remunerated and how this might affect behavior
- ▶ Look for evidence of robust action where any incidents of impropriety have occurred previously. Has the tone in the acquired business been appropriately set from the top?
- ▶ If financial due diligence allows, review the types of costs being capitalized in license or rights costs and being incurred in marketing expenses

Compliance programs – always more to do

Our survey results suggest an environment of pressure to deliver results, with respondents perceiving misstatement, bribery and corruption as widespread. It therefore remains essential that compliance programs are continuously strengthened and improved to reduce the risk of, and increase the detection of, fraud and corruption. This is challenging in an environment of significant cost cutting, where compliance departments are under increasing pressure to deliver more effective programs.

Compliance programs therefore need to be highly focused. This can be achieved through a tailored approach to key risk areas and increasing efficiency through the use of, for example, forensic data analytics to highlight business risk. However, compliance programs aimed at deterring unethical business conduct are still not working as effectively as they should.

Our survey raises four issues that those responsible for compliance programs need to address:

- ▶ Senior management thinks programs are more effective than they actually are
- ▶ Programs are too narrow or not seen as relevant
- ▶ Programs are perceived as constraining competitiveness in the market
- ▶ The increased risk due to current market conditions has not been matched by increased compliance efforts

There is clearly a risk that the pressure to deliver results, coupled with the perceived irrelevance and performance-hindering nature of compliance programs, could lead to a tacit acceptance of unethical behavior. Programs may be ignored or circumvented because they make it more difficult to achieve financial targets.

Senior management unaware of the issues

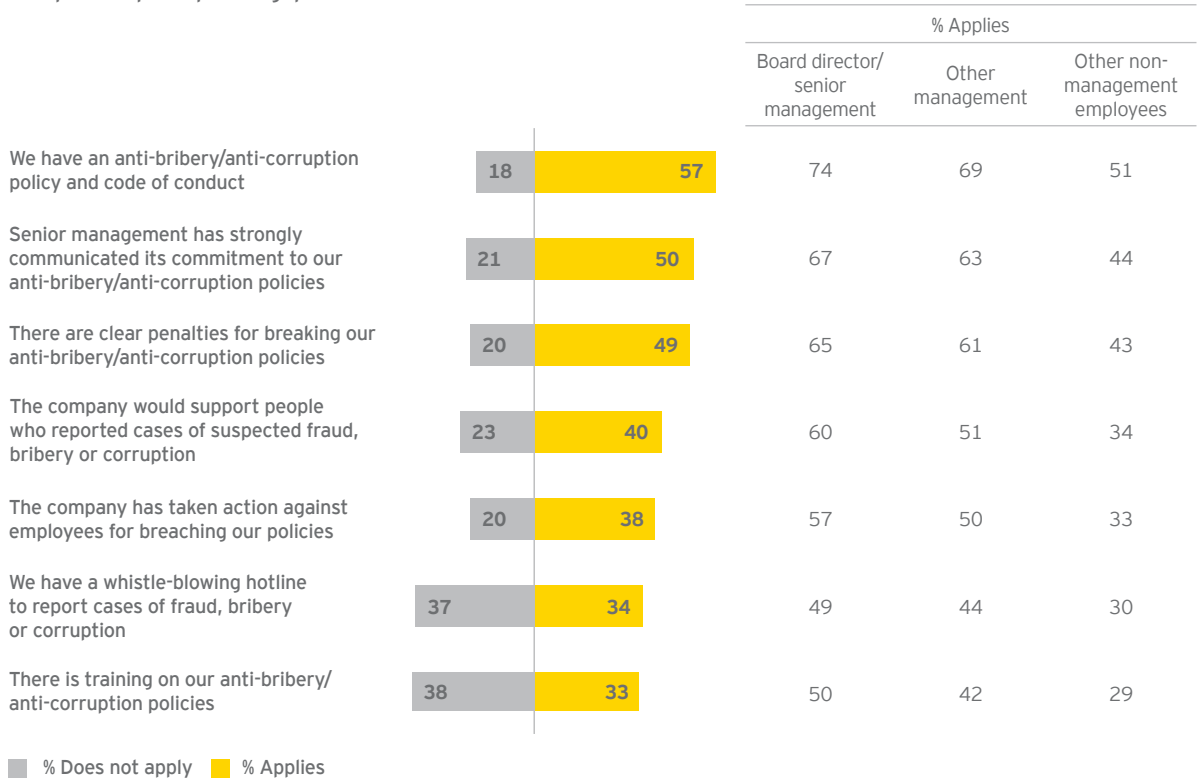
The majority of respondents are aware that their company has an anti-bribery policy. Other responses suggest that compliance programs are reasonably embedded. But these results do not tell the whole story.

Our results suggest a significant perception gap between senior management and employees when it comes to the effectiveness of compliance programs. Sixty-seven percent of directors and senior managers believe that their commitment to anti-bribery and anti-corruption policies has been communicated strongly, compared with 44% of other employees. Sixty percent of directors and senior managers believe that their company would support people who reported cases of suspected fraud, bribery or corruption, whereas only 34% of other employees agree.

This indicates that employees may lack trust in their organization when reporting such activities, a concern that is made more dangerous if senior management turn a blind eye to it. Senior management responses suggest that they are not receiving the right kind of feedback on the implementation of their compliance programs.

Compliance programs aimed at deterring and preventing unethical business conduct are still not working as effectively as they should.

Figure 11
Compliance perceptions gap



Q: For each of the following, please can you tell me whether it applies, or does not apply, to your organization or whether you don't know?
Base: All respondents (3,459); Board director/senior management (246); Other management (769); Other non-management employees (2,444)
The "Don't know" percentages have been omitted to allow better comparison between the responses given.

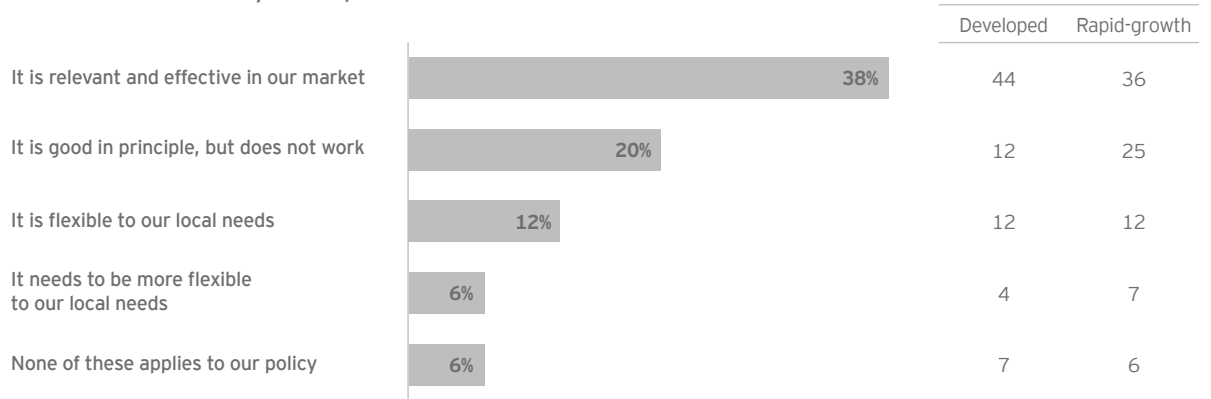
Focus is too narrow

The results also raise questions over the breadth of the compliance programs that are in place. Fewer than half of respondents knew that their company's policy contains guidance on gifts or hospitality, and less than a quarter knew of policies on political contributions. More than half of respondents do not know whether their company has specific procedures to guide dealings with government officials. It appears that even where compliance programs are in place, there are still fundamental gaps in the areas covered by these policies.

We asked respondents whether they thought that their company's compliance program was effective in their specific market. Only 38% of respondents agreed it was relevant and effective in their markets.

Companies are struggling to apply global compliance programs to local offices. Challenges include tailoring programs to the specific issues faced in local markets, while managing the risks that arise from allowing programs to be flexible to local needs. Twelve percent of respondents agree that their company's compliance program is flexible to their local needs. Where bribery and corruption are prevalent in local markets, compliance programs that reflect local needs must also address corruption risks robustly.

Figure 12
Relevance and flexibility of compliance frameworks

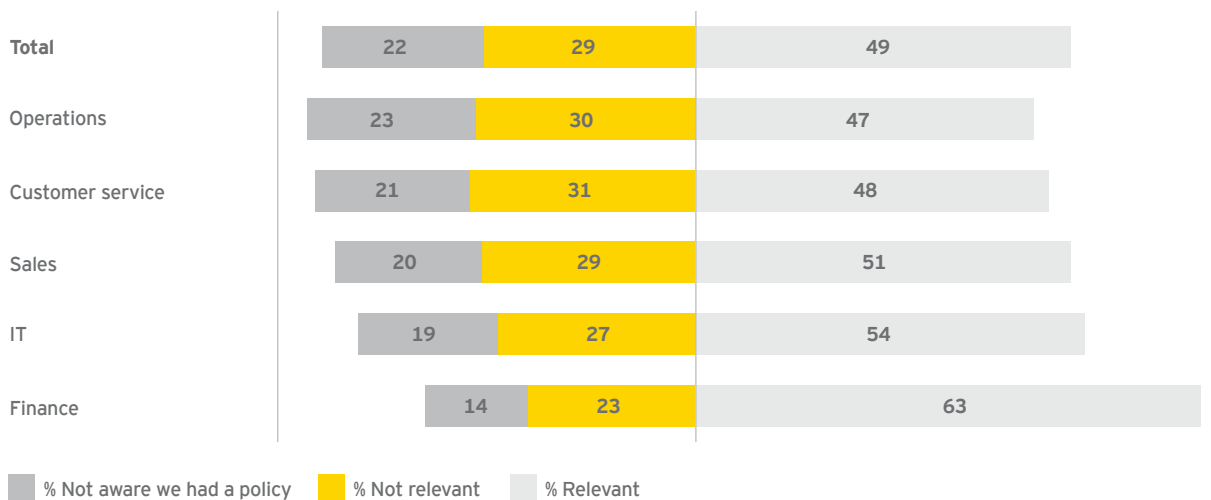


Q: Which, if any, of the following apply to your company's anti-bribery/anti-corruption policy?

Base: All respondents working for a company with an anti-bribery policy in place: 2013 (1,955); Developed (829); Rapid-growth (639)

The "Don't know" and "Not applicable" percentages have been omitted to allow better comparison between the responses given.

Figure 13
Awareness of compliance programs by function



Q: Thinking about your company's policy on anti-bribery/anti-corruption, how relevant do you think most of your colleagues would say it is in relation to their own work?

Base: All respondents (3,459); Operations (536); Customer service (516); IT (299); Finance (289); Sales (238)

Compliance? Not my responsibility

We have seen a widespread reduction, for those countries we surveyed in our 2011 *European Fraud Survey*, in the percentage of respondents who consider their company's anti-bribery and anti-corruption program to be relevant to their work. Fewer than half of respondents think their colleagues would say it was relevant.

Arguably, the sales function should recognize the importance and relevance of a company's anti-bribery policy more than any other. Just under half of respondents from this function do not consider the policy particularly relevant to their role and in many cases are not even aware of its existence.

Compliant business equals less competitive business?

Probably of most concern to compliance executives is the view among over one in six respondents that following their compliance policy very closely harms their competitiveness in the market.

So employees falsely perceive there to be a choice: implement compliance policies to the letter and risk losing opportunities, or take the risk of non-compliance and keep a competitive edge. Typical remuneration mechanisms are likely to encourage the unethical choice; employees rarely get a pay rise or promotion simply for complying with policy. In the context of widespread pay cuts, the temptation to achieve results through bribery and corruption is even greater.

Businesses need to consider how they incentivize employees to act ethically. As they focus more closely on driving ethical growth for shareholder value, the absence of mechanisms to recognize ethical behavior seems a missed opportunity.

Increased effort not keeping pace with the challenge

Given the enforcement environment, it is unsurprising that a third of respondents feel their company's efforts to combat fraud, bribery and corruption have increased over the last few years.

However, our survey also finds that some key control areas are not getting the focus that they should, including checks on third parties and questions relating to the reliability of revenue recording. For example, only 12% of respondents indicate that they had been asked for information on the identity of third parties, customers or suppliers.

Given there may be some level of misreporting being observed in businesses especially in rapid-growth markets, it is surprising that one fifth of respondents in these markets feel that management is asking fewer questions regarding the reliability of revenue.

Equally surprising is the 22% of respondents in rapid-growth markets who feel that their business is less thorough about checking on third parties, given the high profile third parties have had in many recent enforcement actions.

Certain findings support our conclusion that the delivery of effective compliance programs is under strain. For example, in several countries a high percentage of respondents state that their company has an anti-bribery policy, senior management has communicated its commitment and there are clear penalties for breaching the policy. Yet in these same countries, there is also a high percentage that think bribery and corruption are widespread, or think it is common practice to use bribery to win contracts.

The damage to shareholder value that can arise as a result of misreporting or corruption can be far greater than any resulting regulatory fines.

Conclusion – navigating the risks

Six steps to help protect your business

Market conditions continue to be extremely difficult for multinational companies, particularly those looking to expand into rapid-growth markets. Bribery and corruption issues around the globe continue to challenge even the most robust compliance organizations. At the same time, regulators across the globe continue to increase their focus on corporate and individual misconduct. Our experience in conducting fraud, bribery and corruption investigations and assisting clients remediating identified issues is consistent with the findings in this survey. One in five respondents has seen financial manipulation occurring in their companies. Fifty-seven percent believe bribery and corruption are widespread in their country.

Across jurisdictions, sectors and functions, individuals are feeling increased and direct pressure. Some individuals respond to this pressure by taking short cuts, acting unethically or even illegally. Businesses manage this risk in many ways, but we have observed common features among those who manage it most effectively.

Our survey findings indicate a level of risk that unethical conduct could be greater for multinationals headquartered in mature markets. Not only is the enforcement environment becoming increasingly aggressive but regulators in rapid-growth markets are perceived by a quarter of respondents as being more focused on the behavior of foreign businesses.

1

Own the problem

The survey results show that compliance programs are not working as effectively as they should. Significantly, employees are not convinced that management is serious about the issue. In businesses where the risks of fraud, bribery and corruption are properly acknowledged, compliance is not seen as a “tick-box” exercise. In these businesses, management owns the problem, and boards challenge management to ensure that they are prioritizing risk and dealing with issues effectively.

6

Ask questions, demand answers

Forty-two percent of directors and senior managers are aware of some kind of irregular financial reporting in their company. All senior managers should be asking tough questions about the reporting they are receiving.

However, our survey shows that one-fifth of respondents in rapid-growth markets feel management is actually asking fewer questions regarding the reliability of revenue. This does not fit well with the finding that suggests businesses in rapid-growth markets are more likely to misrepresent their financial performance.

Companies with robust approaches to fraud, bribery and corruption exercise their audit rights on third parties and insist that their suppliers regularly respond to requests for information.

2

Deal with the issues – make compliance relevant

Fewer than half of our respondents thought that their colleagues would say compliance was fairly or very relevant to their role. They – including sales professionals – think compliance is someone else’s problem.

With only 38% of respondents considering their compliance program to be relevant and effective, there is clearly a long way to go for many businesses. Making compliance relevant to local teams does not mean diluting the program or bending the rules. It means engaging with local teams to manage specific requirements while retaining a robust and consistent approach.

3

Communicate the risks

Losing that deal, missing that target, not delivering that growth does not often look like the best option to an executive. Our survey shows that these outcomes may be perceived as the consequence of ethical conduct.

Businesses that have a strong code of ethics are not just good at controlling behavior. They excel at communicating the risks of unethical conduct. Punishing unethical conduct sends a strong message to employees, and these companies are not afraid to share information on the number of people sanctioned for ethical breaches.



Protect your business

5

Focus resources

The need to squeeze efficiencies out of compliance and internal audit functions is an inevitable consequence of today’s difficult economic environment. A sharp focus on key risks is critical, and begins with understanding where the risks are.

Having identified the risks, however, businesses need to act. More than a fifth of respondents in rapid-growth markets, for example, thought their business was becoming less thorough in conducting checks on third parties. We often find compliance functions unable to cope with the volume of third parties they need to evaluate. Often, this is a result of an ineffective risk-based approach, or a failure to appropriately leverage available technology solutions.

Whatever the sector, technology has a key role to play in helping focus resources. The use of forensic data analytics can identify incidences of anomalous activity and guide more detailed assessments.

4

Communicate the benefits

Over one in six respondents think that their compliance policy harms their competitiveness.

However, managing the risk of fraud, bribery and corruption also helps businesses to succeed in challenging markets. Managing the risks of third-party relationships effectively, for example, is critical to conducting business across a wide range of markets. Forensic pre-acquisition due diligence – covering, for example, the risk of fraud, corruption and money laundering – can be the difference between a successful transaction and the loss of investor confidence.

Investors and regulators are looking for global companies to show their ability to prevent and detect fraud or other unethical behavior. This can often be demonstrated through an audit of the effectiveness of the compliance function. This has been adopted by a number of leading companies in Germany, as a result of the country’s recently adopted compliance management system audit standard.

Selected country results

Table 1 – Increasing financial pressure

| Managers at our business will be under increased pressure to deliver good financial performance over the next 12 months | % Agree |
|---|-----------|
| Ireland | 80 |
| South Africa | 79 |
| Kenya | 79 |
| UK | 75 |
| Nigeria | 75 |
| Egypt | 74 |
| India | 74 |
| Norway | 74 |
| Slovenia | 67 |
| Greece | 66 |
| Italy | 65 |
| Russia | 65 |
| UAE | 65 |
| Croatia | 64 |
| Sweden | 63 |
| Hungary | 62 |
| Netherlands | 62 |
| All respondents | 60 |
| Switzerland | 60 |
| Finland | 60 |
| Saudi Arabia | 58 |
| Belgium | 57 |
| Poland | 57 |
| France | 54 |
| Portugal | 54 |
| Spain | 54 |
| Slovakia | 53 |
| Austria | 52 |
| Germany | 52 |
| Czech Republic | 49 |
| Ukraine | 44 |
| Romania | 43 |
| Serbia | 40 |
| Baltic States | 39 |
| Turkey | 32 |

Q: To what extent do you agree or disagree with the following statement.

Table 2 – Promoting the business or “cooking the books”

| Companies often report their financial performance as better than it is | % Applies |
|---|-----------|
| Nigeria | 68 |
| Slovenia | 66 |
| Russia | 61 |
| Spain | 61 |
| Croatia | 58 |
| India | 54 |
| Serbia | 54 |
| Kenya | 53 |
| Austria | 51 |
| Ukraine | 49 |
| Saudi Arabia | 48 |
| Greece | 46 |
| Turkey | 45 |
| Portugal | 43 |
| Poland | 42 |
| Egypt | 40 |
| Italy | 40 |
| Ireland | 38 |
| All respondents | 38 |
| South Africa | 35 |
| Belgium | 34 |
| Germany | 34 |
| Slovakia | 33 |
| Baltic States | 28 |
| UK | 27 |
| UAE | 26 |
| Czech Republic | 25 |
| Netherlands | 23 |
| Hungary | 19 |
| Sweden | 18 |
| Romania | 17 |
| France | 16 |
| Switzerland | 16 |
| Norway | 10 |
| Finland | 7 |

Q: Can you indicate whether you think the following applies, or does not apply, to your country or industry?

Table 3 – The corruption perception gap

| | Bribery/corrupt practices happen widely in business in this country | In our sector, it is common practice to use bribery to win contracts |
|------------------------|---|--|
| | % Applies | |
| Kenya | 94 | 34 |
| Greece | 84 | 29 |
| Croatia | 90 | 40 |
| Slovenia | 96 | 46 |
| Portugal | 72 | 24 |
| South Africa | 65 | 19 |
| Slovakia | 84 | 41 |
| Czech Republic | 73 | 31 |
| Romania | 61 | 19 |
| Hungary | 70 | 29 |
| Nigeria | 89 | 50 |
| Serbia | 83 | 44 |
| Poland | 59 | 22 |
| Spain | 65 | 29 |
| Egypt | 71 | 37 |
| Italy | 60 | 27 |
| Belgium | 51 | 19 |
| Austria | 46 | 15 |
| All respondents | 57 | 26 |
| UK | 37 | 6 |
| Ukraine | 85 | 54 |
| Baltic States | 47 | 21 |
| Ireland | 43 | 17 |
| Russia | 82 | 56 |
| India | 69 | 44 |
| Germany | 30 | 9 |
| France | 27 | 7 |
| Saudi Arabia | 66 | 46 |
| Netherlands | 23 | 4 |
| Turkey | 55 | 39 |
| Norway | 17 | 2 |
| Sweden | 12 | 4 |
| Finland | 12 | 8 |
| UAE | 24 | 20 |
| Switzerland | 10 | 7 |

Q: Can you indicate whether you think the following applies, or does not apply, to your country or industry?

Table 4 – Increased scrutiny for multinationals in rapid-growth markets

| Authorities in this country regulate foreign businesses more closely than local businesses | % Agree |
|--|-----------|
| India | 54 |
| Serbia | 37 |
| Saudi Arabia | 36 |
| Kenya | 36 |
| South Africa | 29 |
| Russia | 28 |
| Nigeria | 26 |
| Croatia | 25 |
| Slovakia | 23 |
| Baltic States | 23 |
| Ireland | 21 |
| UAE | 21 |
| All respondents | 19 |
| Poland | 19 |
| Ukraine | 18 |
| Egypt | 18 |
| Norway | 17 |
| Romania | 16 |
| Greece | 16 |
| Netherlands | 16 |
| France | 15 |
| Turkey | 15 |
| Switzerland | 15 |
| Austria | 13 |
| Hungary | 12 |
| Portugal | 12 |
| Sweden | 12 |
| Slovenia | 12 |
| Finland | 12 |
| Spain | 11 |
| Germany | 11 |
| Czech Republic | 11 |
| Italy | 11 |
| Belgium | 9 |
| UK | 8 |

Q: To what extent do you agree or disagree with the following statement?

Survey approach

Between November and December 2012, our researchers – the global market research agency Ipsos – conducted 3,459 interviews with employees of large companies* in 36 countries by telephone, online or in person. Interviews were conducted on an anonymous basis using local language in all countries.

Participant profile – region and country, company size, role and sector

| Number of interviews | |
|----------------------|-------|
| Eastern Europe | 1,256 |
| Baltic States* | 100 |
| Croatia | 100 |
| Czech Republic | 100 |
| Hungary | 100 |
| Poland | 100 |
| Romania | 100 |
| Russia | 100 |
| Serbia | 156 |
| Slovakia | 100 |
| Slovenia | 100 |
| Turkey | 100 |
| Ukraine | 100 |

| Middle East, India and Africa | |
|-------------------------------|-----|
| Egypt | 100 |
| India | 100 |
| Kenya | 100 |
| Nigeria | 103 |
| Saudi Arabia | 100 |
| South Africa | 100 |
| UAE | 100 |

| Western Europe | |
|----------------|-----|
| Austria | 100 |
| Belgium | 100 |
| Finland | 100 |
| France | 100 |
| Germany | 100 |
| Greece | 100 |
| Ireland | 100 |
| Italy | 100 |
| Netherlands | 100 |
| Norway | 100 |
| Portugal | 100 |
| Spain | 100 |
| Sweden | 100 |
| Switzerland | 100 |
| UK | 100 |

| Number of employees globally | | % |
|------------------------------|--|----|
| Above 5,000 | | 43 |
| 1,500 - 4,999 | | 20 |
| 1,000 - 1,499 | | 11 |
| 500 - 999 | | 10 |
| Less than 500 | | 7 |
| Don't know | | 9 |

| Role within organization | | % |
|--------------------------|--|----|
| Board director | | 1 |
| Senior management | | 6 |
| Other management | | 22 |
| Other employee | | 65 |
| Other | | 6 |

| Sector | | % |
|--|--|----|
| Government and public sector | | 19 |
| Financial services | | 13 |
| Technology, communications and entertainment | | 10 |
| Transportation | | 10 |
| Consumer products/retail/wholesale | | 9 |
| Manufacturing/chemicals | | 6 |
| Power, utilities and extractive industries | | 6 |
| Healthcare and life sciences | | 5 |
| Real estate | | 4 |
| Professional firms and services | | 3 |
| Other sectors | | 15 |

* Estonia, Latvia and Lithuania

For the purpose of this report, "developed" countries include Austria, Belgium, Finland, France, Germany, Greece, Ireland, Italy, Netherlands, Norway, Portugal, Spain, Sweden, Switzerland and UK. The "rapid-growth" countries, taken from our *Rapid-Growth Markets Forecast: Winter 2013*, include Czech Republic, Egypt, India, Nigeria, Poland, Russia, Saudi Arabia, South Africa, Turkey, UAE and Ukraine.

* Large companies are defined as those with more than 150/250/500/1,000/1,500 employees depending on the country, or as quoted on a stock exchange or is a multinational.

Results for Serbia and Nigeria were downweighted to 100 interviews per country in aggregated results.

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