

# economic crime survey 2003 united kingdom

## economic crime: a continuing threat

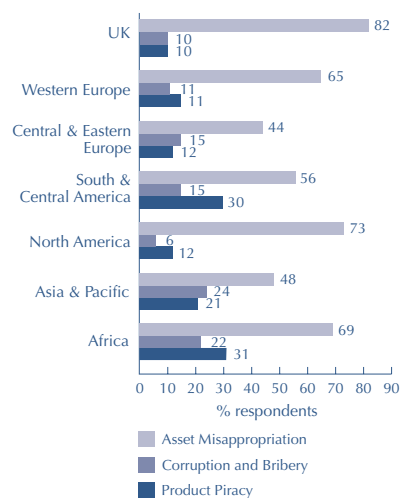
More than half of the organisations surveyed in the UK reported having been the victim of economic crime within the last two years, compared to 41% of firms in our 2001 survey. The UK reported a higher incidence of economic crime than the rest of continental Europe, North and South America and Asia. Overall, 37% of organisations globally indicated that they had been the victim of economic crime.

However, it is not necessarily the case that the UK has a greater problem with economic crime, as the UK may have provided a more self-critical set of responses or have a lower threshold for acknowledging crime. Regardless, it cannot be denied that economic crime continues to be a threat that requires attention.

The nature of the economic crimes committed in the UK was markedly different to some of those committed overseas. The UK respondents reported a higher level of asset misappropriation, such as payment diversion, than any of the six global regions, but relatively little corruption and bribery or product piracy and counterfeiting. Given that the weak

global economy is forcing companies to focus more strongly than ever on their bottom lines, it appears that insufficient attention is being paid in the UK to asset misappropriation, which is generally considered to be a preventable economic crime.

**Economic crimes suffered most frequently by those reporting an incident**



### Ineffective controls?

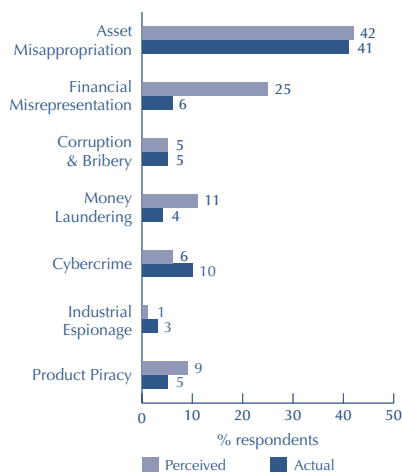
Two findings in particular indicate a gulf between the actual and perceived effectiveness of organisations' controls.

Firstly, 81% of UK respondents are confident that their controls are stronger than a year ago and UK organisations are more confident in their controls than their global colleagues; a similar finding appeared in 2001 and yet the level of economic crime continues to increase. Secondly, 85% of UK organisations are confident that their controls could deal with a potentially major financial loss or damaged reputation.

The first of these findings suggests organisations are misleading themselves as to the strength and effectiveness of their controls. People who wish to commit economic crime generally focus not on controls, but on ways to circumvent them while avoiding detection. Correspondingly, despite the respondents confidence, recent high profile cases have demonstrated that organisations are generally ill-prepared for major economic crime, often with catastrophic consequences. Organisations would be well advised to consider and minimise their exposure to such risks while planning their response to a major incident of economic crime.

A further problem lies in the difficulties UK companies apparently face in identifying the economic crimes which are actually taking place. For example, respondents underestimated the actual incidence of cybercrime. Conversely, respondents considered financial misrepresentation and money laundering to be more prevalent than the actual reported incidence. We believe that a regular process of fraud risk assessment is the most appropriate way to ensure that an organisation's controls are kept commensurate with the risks, and that crimes committed are swiftly discovered.

#### Economic crime in the UK: perceived versus actual incidence



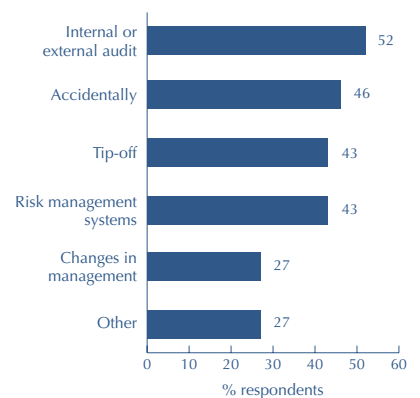
#### Discovery and reporting of economic crime

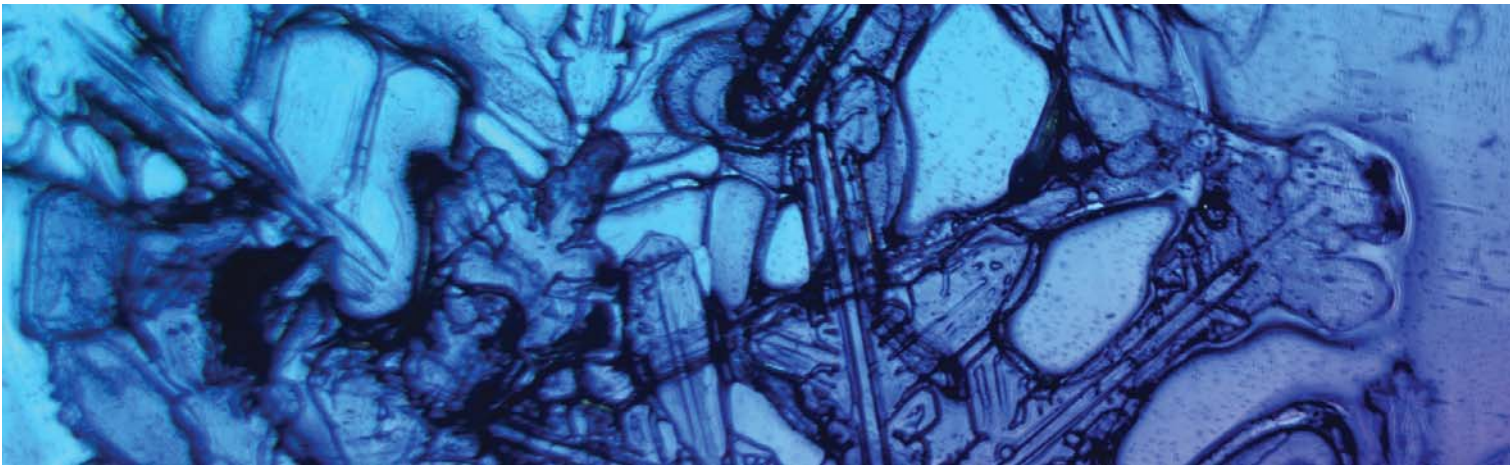
In view of the difficulty organisations face in the identification of risks and the implementation of effective controls, it is perhaps not surprising that traditional pro-active controls fared poorly in the discovery of economic crime compared to the more reactive controls. Of those UK organisations who had suffered economic crime in the last two years, risk management systems were only cited by 43% of respondents as having played a role in their discovery. The tip-off was reported as having been equally effective, and accident even more so (46%). Internal and external audit were the most effective detection mechanisms but were still cited by only just over half of respondents.

Of the UK organisations surveyed, only one third stated that they had a policy regarding the reporting of economic crime to the authorities. One third had no such policy, with a further third of organisations not answering this question, suggesting

that they did not have, or were unsure of their company policy. This implies that many UK companies need to pay urgent attention to the Proceeds of Crime Act 2002. This legislation widens the scope of crimes in respect of which it is necessary to report suspicions concerning their proceeds, and the range of individuals and entities on whom this responsibility is imposed. It also demonstrates a trend towards increased transparency, which we believe is set to continue.

#### Factors in the detection of economic crime





## Recovery of losses

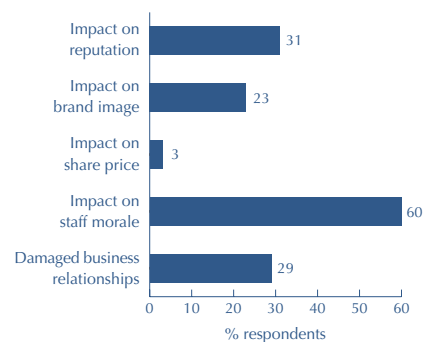
According to our survey, the UK is more proactive than the rest of the world in implementing corrective measures to reduce exposure to the risk of economic crime. However, UK organisations are doing significantly less than their Western European counterparts with regard to two very important forms of corrective action, namely improving standards of staff awareness and training, and tightening up all reporting structures. These are “carrot and stick” measures in which the creation of an ethical culture is combined with a powerful deterrent. We consider them to be vital elements of any system of internal control.

The UK is leading the way in insuring against economic crime. Approximately 50% more organisations take out insurance in the UK than in either Western Europe or the rest of the world. In terms of the type of insurance taken out, more UK organisations insure against theft by employees (86%), third parties (71%) and malicious attacks (40%) than their Western European counterparts.

Paradoxically, the UK is less successful in recovering money lost as a result of economic crime than either Western Europe or the world as a whole. This may simply reflect organisations’ reluctance to pursue claims through the civil or criminal justice systems. Alternatively, this may be a result of companies insuring against the wrong risks, failing to adhere to the policy conditions, or agreeing an excess which is too high in relation to the likely losses. Organisations should therefore regularly review their insurance cover to ensure it adequately addresses the ever-changing risks to which they are exposed.

However, the statistics above relate only to the recovery of direct financial losses associated with economic crime. These are often insignificant compared to the indirect losses such as reputational damage which can result from economic crime. Our survey identified a much greater awareness of the collateral damage caused by economic crime with, for example, 60% reporting such incidents having had an adverse effect on staff morale.

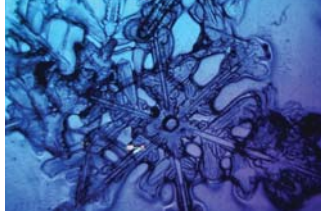
## Collateral damage



## Corruption & Bribery

Only 5% of the UK organisations surveyed reported having suffered as a consequence of corruption and bribery in the past two years. This reflects similar findings to the ‘Transparency International’ ranking of countries by perceived corruption rate, where the UK was well placed.

Elsewhere in the world, bribery and corruption is much more prevalent, particularly in Central and Eastern Europe and in Africa. While UK respondents may be tempted to adopt



local practices in their overseas operations, such an attitude can have very serious consequences. Under the Anti-Terrorism, Crime and Security Act 2001, UK companies, their directors and other UK nationals can now be prosecuted for the bribery of foreign officials carried out by their overseas staff. Even though the actual bribery may take place entirely in a foreign jurisdiction, a UK based director can be subject to an unlimited fine or seven years imprisonment. The Corruption Bill currently being debated in parliament would tighten the rules further and make life even harder for companies and individuals who continue to believe that bribery and corruption are acceptable in some parts of the world.

## Financial Misrepresentation

25% of organisations perceive financial misrepresentation to be prevalent in the UK, with just 6% having been involved with such incidents in the last two years. The difference between these two figures may reflect the increased

publicity that such incidents generate, making many respondents believe the problem is more widespread than it actually is.

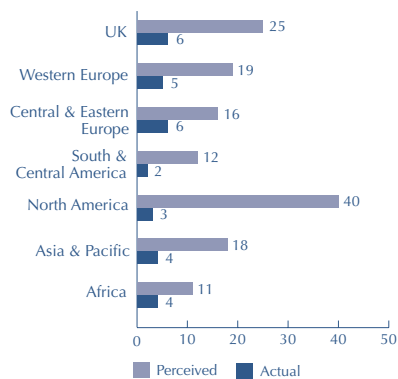
However, this should not underplay the effects should an incident be detected. Where an organisation trades on its reputation, the discovery of an accounting irregularity can have a devastating impact. Globally, 84% of organisations who had experienced financial misrepresentation in the

last two years indicated that they had suffered some impact as a consequence. In many cases, this impact was judged by organisations to be "serious". Regulators and governing bodies in the UK and abroad are introducing new legislation in this area, coupled with stiffer penalties for the companies and the individuals running them. Firms should therefore be seeking to comply with the new rules at all costs.

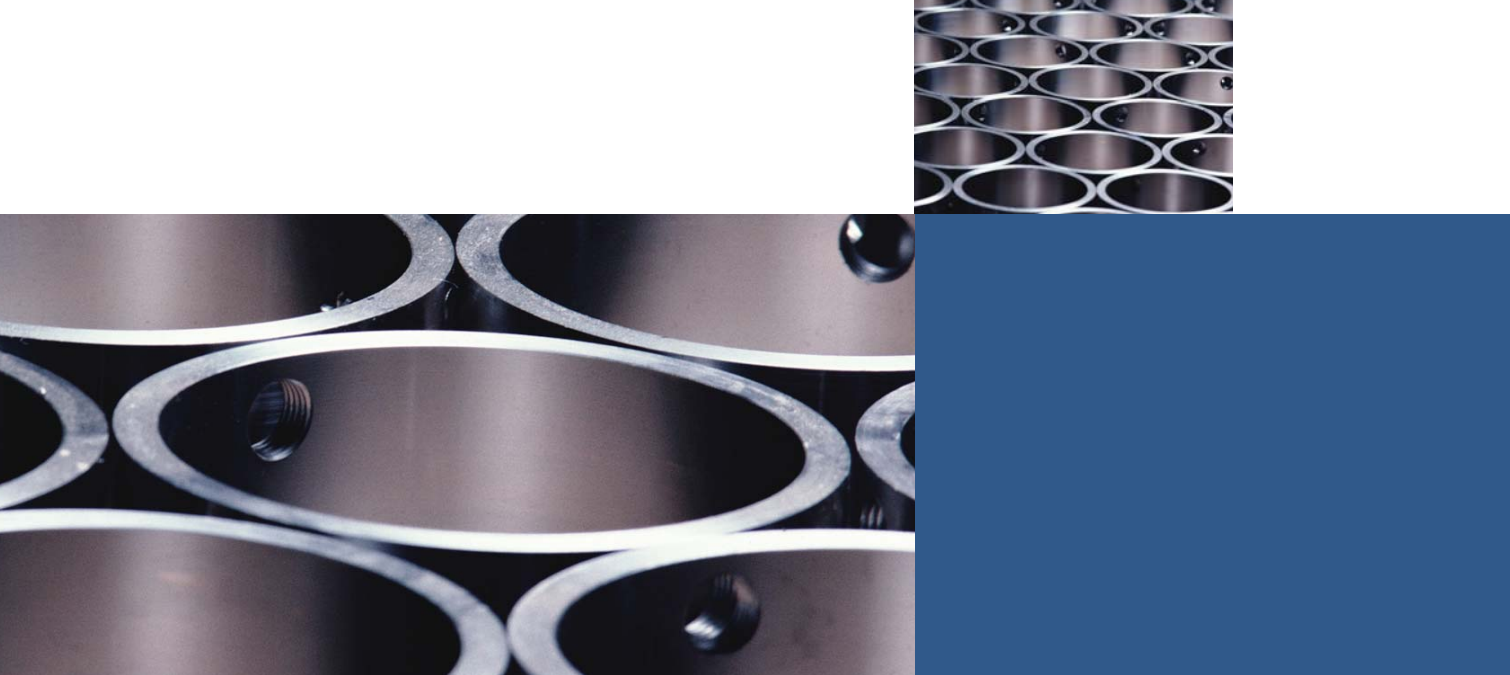
## The Board's role

Looking ahead over the next five years, only 8% of UK respondents believed that the risk of their organisation suffering economic crime would decline. This was significantly more pessimistic, or perhaps more realistic, than the other Western European and global respondents. The UK respondents considered financial misrepresentation, cybercrime and money laundering to be most significant growth areas of the future.

**Financial misrepresentation in the UK and globally: perceived versus actual incidence**



*only 8% of uk respondents believed that the risk of their organisation suffering economic crime would decline*



Set against this background, we believe it is imperative that Boards of directors take a proactive role in preventing economic crime in their organisations. This should include the following key elements:

- Determining a stance on economic crime issues. Essentially, senior management must strike the right balance between a long-term ethical policy on economic crime and short-term commercial considerations.
- Identifying what policies are appropriate to their organisations. Good practice would include a code of conduct (currently only used by 68% of UK respondents), pre-employment screening (59%), a whistle-blowing system (52%), and specific fraud training for management (26%).
- Ensuring that an ethical culture is disseminated throughout the organisation, supported by policies

which are rigorously adhered to. An example would be annual compliance returns being completed by employees.

Since our last survey in 2001, the world has experienced unparalleled increases in transparency and corporate ethical standards. Companies which fail to keep pace with these developments risk not just the straightforward financial loss caused by economic crime but also the more serious reputational damage from which it is sometimes impossible to recover.

#### Prevention measures taken by organisations



Clearly, not every incident of economic crime results in financial meltdown for the company involved. However, in the current climate, organisations are well advised to remember that prevention is always better than cure. Any proposal to reduce an organisation's exposure to economic crime must be promoted by the highest level of management and co-ordinated by appropriately senior employees. Any strategy that is not consistently applied across the company or group will inevitably be flawed.

## PricewaterhouseCoopers Investigations & Forensic Services

Territory	City	Contact	Telephone	Email
United Kingdom	London	Andrew Clark	020 7804 5761	andrew.p.clark@uk.pwc.com
	London	Will Kenyon	020 7212 2623	will.kenyon@uk.pwc.com
	London	Edwin Harland	020 7804 5843	edwin.harland@uk.pwc.com
	Birmingham	John Tracey	0121 265 5783	john.f.tracey@uk.pwc.com
	Manchester	Mark Stansfield	0161 247 4082	mark.stansfield@uk.pwc.com
	Leeds	Fran Marwood	0113 288 2479	fran.marwood@uk.pwc.com
	Edinburgh	Martin Dougall	0131 260 4314	martin.w.dougall@uk.pwc.com

[www.pwc.com/crimesurvey](http://www.pwc.com/crimesurvey)

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