global economic crime survey 2005

Indonesia

Introduction

Rodney Hay, Dispute Analysis and Investigations

I am pleased to present the Indonesian results of the third biennial PricewaterhouseCoopers' Global Economic Crime Survey. The 2005 report provides an insight into the growth, impact and future of global economic crime. Our local report compares Indonesian economic crime trends against regional and global results, and provides us with a better understanding of the cause and impact of economic crime in Indonesia.

The 2005 report incorporates two additional areas of focus that were not included in the 2003 global report: the effectiveness of fraud risk management systems and a profile of fraud perpetrators. These additional areas were explored to provide a greater understanding of the effectiveness of preventative measures and expose the backgrounds and motivations of those who commit fraud.

In undertaking this survey, 3,508 interviews were conducted across 34 countries. The local results are based upon responses from 75 companies in Indonesia. Of these organisations, 17% are listed on the stock exchange and 73% have offices outside of Indonesia.

The surveyed companies came from the following industries:
- *Manufacturing (30%)*
- *Technology (7%)*
- *Trade - wholesale & retail (7%)*
- *Services (27%)*
- *Financial services (11%)*
- *Other industry sectors (18%)*

Following is a summary of our findings in the context of the Indonesian business environment.

Indonesian Findings – Executive Summary

1. Fraud, a significant and growing threat worldwide

During the past two years, 47% of companies in Indonesia were victims of an economic crime. Although this is a four percentage point decrease on the results of our 2003 survey, the incidence of economic crime is still higher than the global average of 45%. Global results show that the number of incidents of reported fraud increased by eight percentage points compared with the 2003 survey. This highlights the fact that the incidence of global economic crime is increasing.

2. Types of economic crime

Corruption continues to be of significant concern for companies operating in Indonesia.

- Of companies that suffered an economic crime in the past 2 years, 66% had been subjected to corruption. This is well above the regional average of 33% and the global average of 24%

- The incidence of other types of economic crimes was generally in line with global results. Of the companies that reported incidents of economic crime in the past two years 46% suffered asset misappropriation and 29% were victims of counterfeiting. The incidence of deception based offences such as false pretences was significantly less then global and regional averages.

3. Cost – intangible v. bottom line

- The survey results indicate that the average tangible losses suffered by companies in Indonesia is significantly less then the regional and global averages. The average total loss from fraud reported by companies in Indonesia was USD475,826 which compares favourably with the regional average of USD1,588,042 and the global average of USD1,735,913

- The intangible damage suffered by companies in Indonesia as a result of corruption and insider trading was

Corruption continues to be of significant concern for companies operating in Indonesia

perceived to be higher then the regional and global results

- Respondents in Indonesia concluded that the most significant intangible damage caused by economic crime incidents in their company was a result of a "decline in work morale" and an "impairment of business relations".

4. The perpetrators

- 44% of perpetrators of economic crime in Indonesia were employed internally by the organisation and 51% occupied positions of middle management or above
- The typical perpetrator profile in Indonesia is a male aged 31-40 years whose highest level of education is 1st degree graduate. The global trend indicates that perpetrators are getting younger and their level of education higher.

5. The cause of serious fraud incidents

- Our respondents were asked to evaluate the extent to which thirteen predefined factors had played a role in the two most serious fraud incidents that had occurred within the company. According to responses from companies in Indonesia, the following five factors were the most significant causes of fraud incidents:

  - Collaboration with external parties
  - Internal collaboration
  - Insufficient Internal controls
  - Lack of awareness of wrong doing
  - Difference in foreign business ethics.

6. Reaction and recovery

The percentage of funds recovered after a fraud incident is significantly lower in Indonesia compared with regional and global results.

- Of respondents that had suffered a serious fraud, 70% were unable to recover any of the loss resulting from the incident
- Only 5% of respondents were able to recover more than 61% of the loss
- In Indonesia the main perpetrator was dismissed by 24% of companies, however in 31% of cases no action was taken
- A surprising result is that only 27% of companies in Indonesia were insured for economic crime losses.

7. Prevention and detection

It appears that organisations have a greater awareness of their exposure to economic crime and are more proactive in their efforts to detect it. While the traditional avenues of internal audit, external audit and tip-offs retain their vital roles in detecting economic crime, new alternatives such as whistleblower hotlines and corporate security are also providing positive results.

8. Moving forward – the future

The 2005 global crime survey revealed that organisations are more susceptible to fraud during rapid periods of change. As a developing country, Indonesia will continue to experience exponential change, which in turn will increase the risk of economic crime. Our survey reveals that companies in Indonesia are optimistic about there ability to deal with this risk. Only 16% of respondents indicated that it was either likely or very likely that further incidents would occur. Companies need to ensure that they are not underestimating the threat of economic crime. Fraud risk management, including regular fraud risk assessments, should form a key part of the enterprise wide risk management program.

Action Points

- Determine where your fraud risks are. Fraud risks vary for different sized organisations, different types of organisations and different industries. Consider conducting a fraud risk assessment.
- Be proactive around fraud prevention and detection. Consider introducing specific measures such as:

  - Pre employment screening
  - Transaction analysis incorporating fraud profiling
  - Whistleblower systems
  - Awareness / education programs and staff surveys

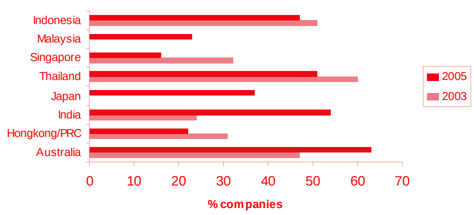
- Be aware of the value of evidence. Ensure you have a fraud incident response plan and consider appointing professional external investigators when incidents arise.
- Review fidelity insurance arrangements. Ensure policy limits and deductibles are appropriate in the context of your risk appetite. Be aware of policy exclusions, conditions and claim preparation requirements
- Systematically review the internal control environment. Assess procedural weak points and take regular corrective action.

Indonesia and Economic Crime

1. Fraud, a significant growing threat

The 2005 Global Economic Crime Survey highlights the growing risk of economic crime throughout the world. Our 2005 Survey reveals that 47% of the 75 companies surveyed in Indonesia suffered an economic crime during the previous two years. This represents a four percentage point decrease on the 2003 survey results. The number of economic crime incidents in the Asia Pacific region has decreased in every country except for Australia and India. The Asia Pacific region was the only region that did not experience an overall increase in the number of reported economic crimes.

Organisations subject to economic crime in past 2 years



The following factors can cause fluctuation in the rate of reported economic crimes:

- A tightening of market regulations resulting in increased efforts to demonstrate transparency and good governance
- Companies taking active steps to detect incidences of fraud
- Changes in culture relating to the stigma attached in reporting fraud
- An increase in the actual level of economic crime.

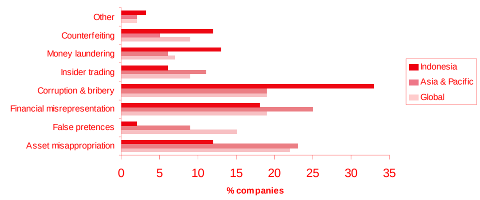
Whilst Indonesia has experienced a decrease in the level of economic crime, the level is still high. Companies operating

in Indonesia need to continually assess the risks of fraud. Our results show that Indonesian companies are optimistic about their ability to reduce the level of economic crime. When asked whether their organisation was at risk of economic crime over the next 5 years, only 16% of respondents indicated that it was either likely or very likely that further incidents would occur. Whilst the optimistic outlook is encouraging, companies need to ensure that they are not underestimating the threat of economic crime. The global economic crime survey indicates that economic crime is an increasing risk face by companies regardless of the industry for country that they operate in.

2. Types of Economic Crime

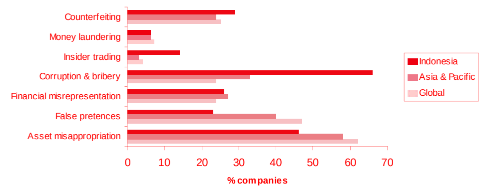
Our 2005 survey results show that corruption continues to be of significant concern for companies operating in Indonesia. The perception that corruption is part of doing business is a difficult stigma for the government, the community and private sector to overcome. During the past four years, positive steps in the fight against corruption have been under taken including the enactment of strong anti – corruption laws and the establishment of the Corruption Eradication Commission ("Komisi Pemberantasan Korupsi"). Despite these positive steps, our survey results show that corruption is still perceived to be the most prevalent economic crime in Indonesia.

Which type of economic crime would you consider to be the most prevalent in your country?



- 33% of companies believe that corruption is the most prevalent economic crime in Indonesia.
- According to the global survey the most prevalent economic crime throughout the world is asset misappropriation
- The high incidence of corruption experienced by companies in Indonesia during the past two years validates the perception that corruption is a significant problem. 47% of companies in Indonesia that stated they had been the victim of an economic crime in the past two years. 66% of those companies stated that they had been subjected to corruption. This is significantly above the global and regional results.

What type of crime has your organisation been subject to?



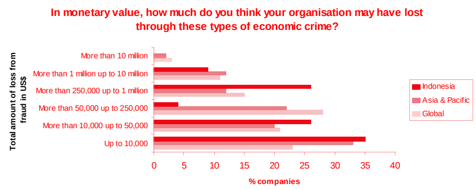
The confronting reality for 44% of companies surveyed is that the perpetrator of economic crime was employed by the organisation.

Key points relating to corruption

- Corruption is often perceived as a victimless economic crime, however the reality is that systemic corruption can cause significant economic damage, which in turn negatively impacts upon business prosperity and the community
- Corruption is not just a government problem. In most instances it requires a person offering the bribe in addition to the person receiving the bribe. The business community must maintain an ethical stance on this issue and resist the pressure to use bribery and corruption as means of doing business
- Governments can assist the business community fight corruption, by simplifying processes, having transparent fees and charges by providing methods to report instances of bribery and corruption
- Under article 5 of Indonesian Law 20 of 2002 it is an offence for any person to give or promise something to a civil servant with the aim of persuading him to perform an action or not perform an action in violation of his obligation
- Indonesian Anti Corruption Laws includes penalties of up to 20 years imprisonment

3. Cost – intangible v. bottom lineline

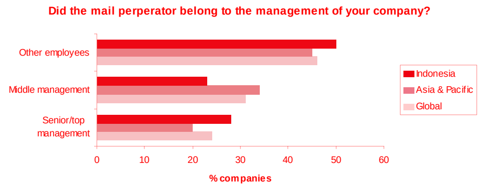
- The 2005 survey results provide an in-depth insight into the impact of economic crime. The impact is measured in terms of the monetary value for tangible economic crimes. As explained in the Global Report, respondents were asked to provide an estimated value of the loss from tangible items namely asset misappropriation, false pretences and counterfeiting. The average total loss from fraud reported by Indonesian organisations was USD475,826 which compare favourably to the regional average of USD1,588,042 and the Global average of USD1,735,913.



Frequently, the intangible effects of economic crime are often overlooked by organisations because they are hard to measure, quantify and substantiate to management. However, the intangible effects of economic crime are progressively becoming more visible to organisations. For instance, 83% of respondents believe that incidents of economic crime resulted in a decline in staff morale and motivation. According to 50 % of respondents, economic crime impaired their business relations, whilst 21% reported a loss of reputation to the company and or brand.

4. The perpetrators

The confronting reality for 44% of companies surveyed is that the perpetrator of economic crime was employed by the organisation. Of these, 51% occupied a position of middle management or above. In Indonesia the typical perpetrator is a male (90%) between the ages of 31-40 whose highest level of education is 1st degree. This result reinforces the need for organisations to carry out effective pre-employment screening and increase monitoring of high risk employees and positions. Furthermore organisations should ensure that a code of conduct is in place and that management, and employees in high risk positions have signed an acknowledgement that they agree with the content. In the event that a fraud incident occurs, evidence that the person understood the organisations code of conduct may be an important factor in determining what course of action can be undertaken.



5. The cause of serious fraud incidents

Our respondents were asked to evaluate the extent to which thirteen predefined factors had played a role in the two most serious fraud incidents occurring within the company. The respondents rated each of the factors with a value between one and five. A rating of five indicates that the factor applies completely and a rating of one indicates that the factor does not apply at all. The following graph shows the average rating for each of the factors.

According to responses from companies in Indonesia, the following five factors were the most significant causes of serious fraud incidents:

- Collaboration with external parties
- Internal collaboration
- Insufficient internal controls
- Lack of awareness of wrong doing
- Difference in foreign business ethics.

Companies should consider incorporating fraud risk management principals into the broader risk management framework. By considering factors such as the opportunity to commit fraud and profiles of fraud offenders, companies can tailor their controls, procedures and responses to mitigate risks without inhibiting the efficiency of the organisation. A single approach may not be effective for all companies, therefore a fraud risk management framework needs to be tailored to the objectives, culture, industry & size of the company.

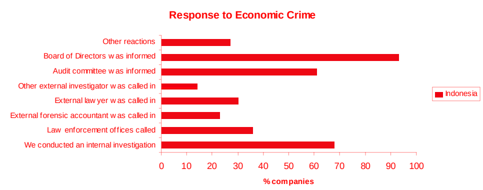
6. Reaction and recovery

The Indonesian results clearly show that once a fraud incident occurs, it is unlikely that the funds will be recovered. Companies are generally reluctant to embark on a long and expensive recovery process with no certainty of success. This factor emphasises the need for organisations to have a robust fraud risk management framework combined with a fraud incident response plan.

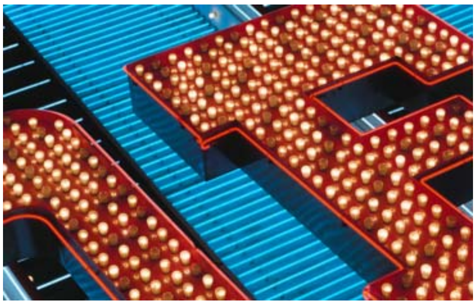
- Of the respondents that were victims of a serious fraud, 70% were unable to recovery any of the loss resulting from the incident.
- Only 5% of respondents were able to recover more than 61% of the loss
- 86% of companies were unable to recover funds from the perpetrator
- Another significant issue for Indonesian companies is that only 27% of companies in Indonesia were insured for economic crime losses.

The low success rate in recovering funds from perpetrators heightens the need for companies to be insured for losses relating to economic crime. Companies should review their fidelity insurance arrangements and ensure policy limits and deductibles are appropriate in the context of potential risks.

Respondents were asked how their company reacted to two serious fraud incidents which had occurred within the past five years. The results show that for most incidents the companies conducted internal investigations rather then use law enforcement, external investigators, forensic accountants or lawyers. If investigations are conducted internally, companies need to ensure that they use staff who are experienced investigators and understand evidence collection procedures. Issues such as confidentiality and independence should also be considered.

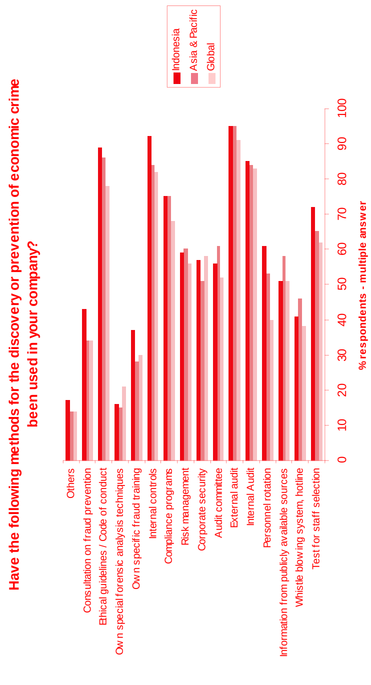


In Indonesia the main perpetrator was dismissed 24% of the time, whilst in 31% of cases no action was taken. In order to initiate criminal or civil action against the perpetrators, companies need to ensure that the evidence is collected in a legal manner and that all relevant facts are considered. Companies should be fully aware of dismissal criteria contained in the Indonesian Manpower Legislation to ensure the correct process is followed.



7. Prevention and detection

Companies are primarily using traditional methods of prevention such as external and internal audit, and implementing codes of conduct and internal controls. As perpetrators become more sophisticated, companies will need to adapt by implementing advanced fraud detection methods such as pattern analysis on transaction data, relationship analysis on suppliers, employees and business partners, and forensic analysis of computer systems. Pro-active strategies such as these will increase the chance of detecting fraud and offer a higher level of protection from the ever improving technologies and methodologies used by perpetrators.



8. Moving forward – the future

The 2005 global crime survey revealed that organisations are more susceptible to fraud during rapid periods of change. As a developing country, Indonesia will continue to experience exponential change, which in turn will increase the risk of economic crime. Fraud risk management, including regular fraud risk assessments, should form a key part of the enterprise wide risk management programs.

An important part of an organisation's fraud risk management strategy is the creation of mechanisms for employees and others to detect and report suspicions of fraud. These mechanisms can be in the form of whistleblower protection policies, 'hot-lines' and pro-active fraud detection programs.

Regular fraud detection strategies, including data analysis, data matching, computer forensic and forensic accounting, should be used to support every fraud risk management programme. Of course, in the event that an organisation does discover they have been the victim of an economic crime, they need to be able to respond effectively and efficiently. Time is often of the essence when a fraud is detected, and organisations need an investigation plan in place to assist staff in responding to such incidents.

A carefully designed plan incorporating advanced investigative techniques can provide a company with the opportunity to identify all perpetrators, estimate the potential losses and ensure that business operations are only minimally affected. Detecting crimes also provides an important opportunity for companies to identify weaknesses in their control and improve security measures. No organisation is immune to the effects of economic crime, so approaching this business threat with an informed approach, and using tried and tested preventative measures will provide the basis for a company to minimise its exposure to the risk of economic crime.

PricewaterhouseCoopers Investigations & Forensics Services

Jakarta	Rodney Hay	+62 21 52890956	rodney.hay@id.pwc.com
	Widiana Winawati	+62 21 52891041	widiana.winawati@id.pwc.com
	Benjamin Noyen	+62 21 52890653	benjamin.noyen@id.pwc.com

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