

Slovakia

Economic Crime in a Downturn

The Global Economic Crime Survey
November 2009

Introduction

We are pleased to present to you the results of our Global Economic Crime Survey for 2009 – the largest study of its kind in the world, prepared by PricewaterhouseCoopers. In this survey, the fifth in the row, we contacted thousands of enterprises, as we did in previous years. Top managers of 3,037 companies from 55 countries of the world, including Slovakia, have shared their experience with real economic crimes they experienced recently.

In contrast to economic crime surveys which we conducted in the past and which covered two-year periods, this time we had to take into consideration the major turnabout in the economic situation which came in the second half of 2008. Therefore, our current survey was focused on the period from August 2008 to August 2009. The economic downturn has raised the following fundamental questions: How will the economic downturn manifest itself in economic crime? Are companies more exposed to economic crime? If so, why? What changes have occurred in this area, and what is the trend we can expect?

Slovakia has been included in the global economic crime survey for the second time in the survey's history of more than ten years. In the following sections, we have also tried to find an answer to the issue of whether Slovak companies are exposed to a different economic crime-related risk profile than companies in other parts of the world. We are also interested in the shift that was made in Slovakia as of the day the results of our previous survey conducted in 2007 were published.

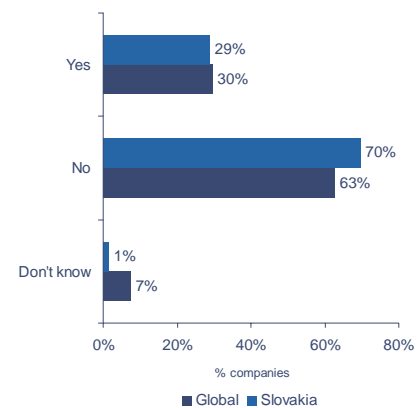
This year's economic crime survey is focused mainly on changes that happened in the last 12 months. We believe that our findings presented in this publication will provide you with interesting information, and help you protect both your corporate and personal interests.

Economic crime incidence

About every third respondent to our survey said that his company experienced some form of economic crime in the last 12 months. Slovakia is no different in this – the difference between the global average and Slovak respondents is within one per cent.

Thus, the current survey gives a very clear answer to the question we asked in the conclusions of our 2007 survey: "What direction will economic crime in Slovakia be taking?" Total incidents of economic crime correspond to the size and type of the Slovak economy.

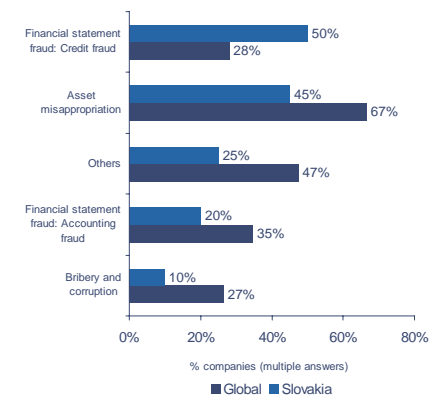
Was your company a victim of economic crime in the last 12 months?



The percentage is no different from the global average. Therefore, the Slovak economy is not exposed to higher economic crime than the economies of other EU countries or other neighbouring countries.

However, a closer look at the incidence of individual types of economic crime shows interesting differences. Slovak firms reported a higher rate of credit fraud – whether in relation to financial institutions, or to common creditors. Globally, this type of fraud has been reported by about 28% of affected firms, while in Slovakia it is 50%.

The most frequent types of economic crime



Very interesting is the low number of corruption incidents reported. In contrast to the global average of companies that have experienced corruption (27%), only 10% of Slovak respondents reported this type of fraud. Paradoxically, 28% of all Slovak respondents expect that their companies will probably experience corruption next year, and another 22% were not able to give an answer to this question.

This number of responses is almost twice as high as the global average, indicating that companies operating on the Slovak market do not trust the economic environment, whether at the public or the private sector level.

This disparity between real corruption incidents and expectations may have two explanations. However, these explanations are contradictory – the perception of corruption in the company is either worse than the actual incidence, or companies are not willing to admit actual corruption incidents. In addition, the situation is made more complicated by the frequent opinion that positive corruption, which is corruption bringing benefits to the bribing company, is part of business tactics, and thus is not perceived as a fraudulent activity.



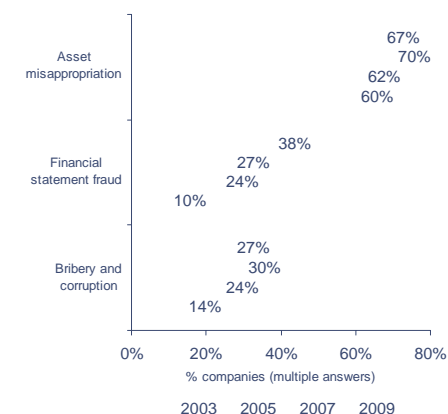
In the last 12 months, 30% of all companies surveyed were victims of economic crime. Slovakia is no exception.

Financial statements fraud – a rising star among fraud

Economic crime may have many different forms. Some of these are more common than others, but any of them may cause significant damage to its victim. Historically, asset misappropriation has always been the most frequent type of economic crime. However, the economic downturn has brought a dramatic increase in incidents related to manipulating financial statements.

The diagram on the right shows the dramatic increase in this type of economic crime. Compared to the previous survey conducted in 2007, 38% of affected companies report having experienced this type of fraud within the last 12 months. These incidents are linked to two factors – on the one hand, they relate to manipulating the financial statements to show better results for shareholders or the company's management, and on the other hand, they are committed in order to obtain new, or keep existing, credit facilities or credit financing. Both factors are clearly connected with one another: The pressure on companies and their management is increasing, and the effort to survive leads to such types of fraud being attempted.

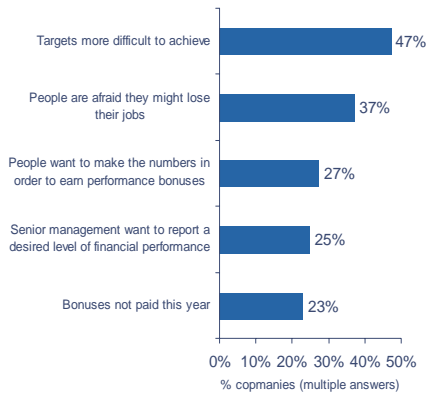
Incidence of the most common types of economic crime



The worsened economic situation has significantly influenced the attitude of employees and members of management to reporting financial results. Our respondents report a rapidly increasing number of incidents where fraud was committed for internal reasons, mainly to manipulate financial indicators for group reporting. Almost one-half of respondents reported that manipulating financial indicators was connected with unrealistic expectations regarding economic results, more than one-third reported, as another reason, fear of losing a job, and about one-fourth stated the effort to get personal bonuses or pressure from top management.

Incidents of manipulating financial statements related to the effort to obtain new credit facilities or credit financing, or keep existing ones, are also rapidly increasing. More than ever, companies must consider their business transactions carefully, and must examine the sound financial position of their business partners. But are companies prepared to do this?

Motives for committing economic crime



A total of 42% of Slovak companies have adopted stricter procedures for examining their business partners

One of the most significant methods of protection against credit fraud is a thorough examination of business partners. These procedures are especially important for companies with a large number of clients belonging to small or medium-sized businesses. The financial position of these companies and, along with this, their willingness to manipulate financial information to hide bad economic performance, may change rapidly. Although the percentage of Slovak companies which have realized this risk slightly exceeds the global average, there is still a majority of companies that have not recently implemented or reviewed this protective mechanism.

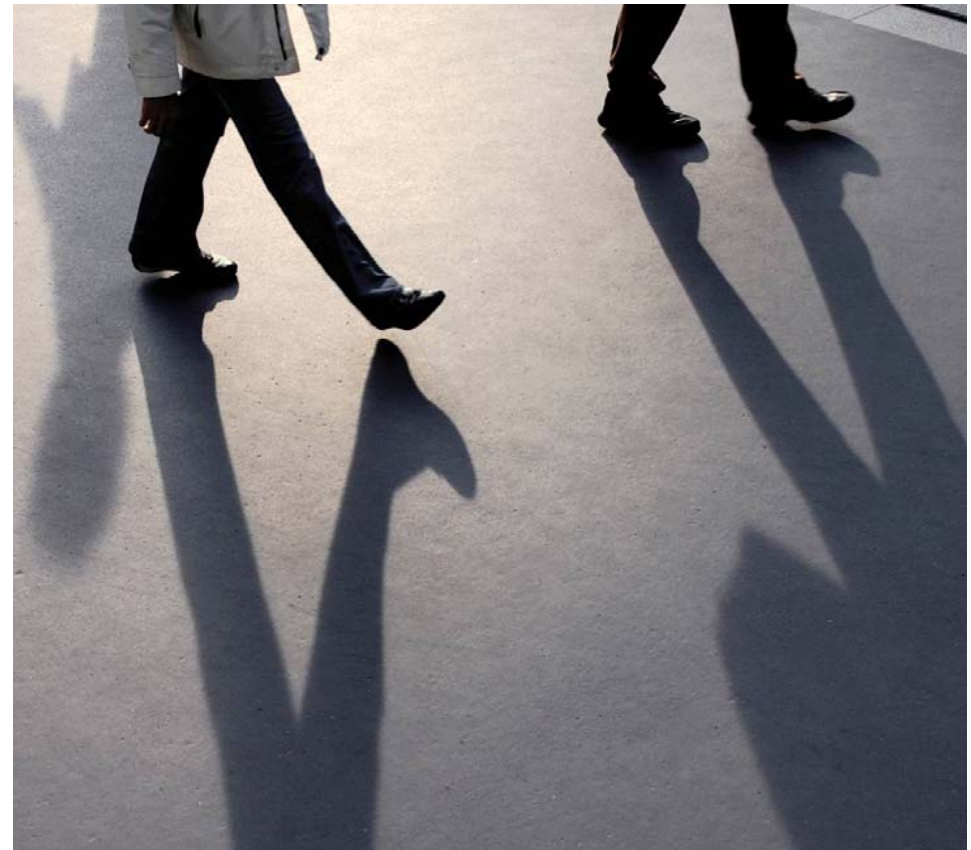
Losses suffered due to economic crime are growing in Slovakia as well

One of the surprising findings of our 2007 survey was that respondents reported relatively low losses caused by economic crime. At that time, we explained this by citing the fact that companies focused on investigating less expensive types of economic crime, mainly on asset misappropriation.

This year's survey has confirmed the increasing trend in damages reported – over 70% of respondents report damage exceeding a value of USD 100,000. This figure exceeds the global average by more than 10%. Globally, it is an increase of more than 10%, if compared to the data from 2007. One-fourth of all incidents reported in Slovakia have exceeded a value of USD 500,000, which is almost identical with the global average.

The increase in losses was also confirmed by respondents to the survey. More than one-half of respondents in Slovakia have reported increase in their losses related to economic crime.

According to Slovak respondents, major negative non-financial impacts of economic crime include impacts on employee morale (40%) and on business relations (25%). This data almost corresponds to the global average.



Companies are most vulnerable from the inside – the number of perpetrators coming from middle and senior management is increasing

This year's economic crime survey has confirmed the bitter truth – companies are most vulnerable from the inside. Compared to 2007, the percentage of fraud committed by internal staff has globally increased from 50% to 53%, which is not a dramatic increase, but the percentage itself is a clear warning: no company is fully protected from internal fraud!

There is a major shift also in answers to the question concerning the main perpetrator within the organization. In more than 56% of incidents, the main perpetrator was a member of senior or middle management. Compared to 2007, this is an increase of over 15%. This figure supports the conclusions stated above – the economic downturn has significantly increased pressure on corporate management, which has led to new types of fraud committed by these employees.

The success rate of detecting fraud is proportional to the knowledge of specific fraud risks in each company

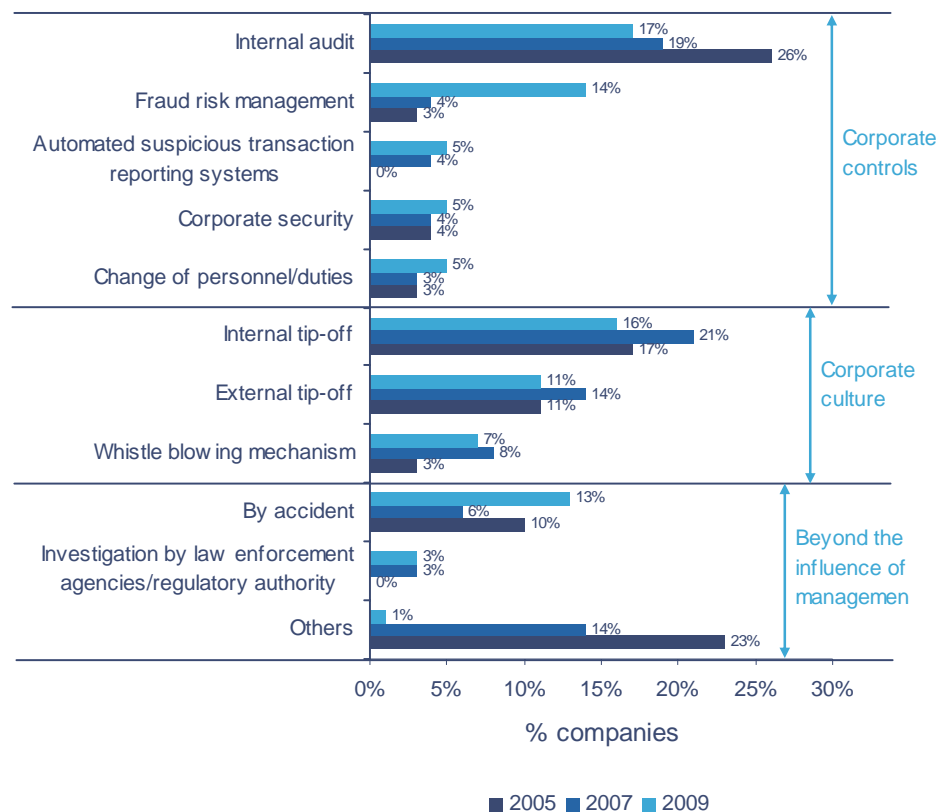
With the increasing number of incidents committed by middle and senior management, and with higher losses, the issue of how to detect these incidents becomes more and more critical. The current survey has brought, for the first time, practical confirmation that measures recommended by surveys conducted in the past were efficient. There was a significant increase in the number of incidents detected as a result of the implementation of complex anti-fraud programmes, from 4% to 14% of incidents detected globally.

However, the survey has also confirmed that fraud is still most frequently detected by accident. A total of 40% of all incidents were detected after an informal warning or by mere accident.

The survey conducted in 2009 has also confirmed a decreasing percentage of incidents detected by internal audit. Partially, it is probably due to segregating the role of internal audit and the specialized anti-fraud teams that have been established in certain companies,

and partially we can attribute this trend to the reduction of costs for internal controlling functions, as reported by respondents to the survey.

Methods of economic crime detection



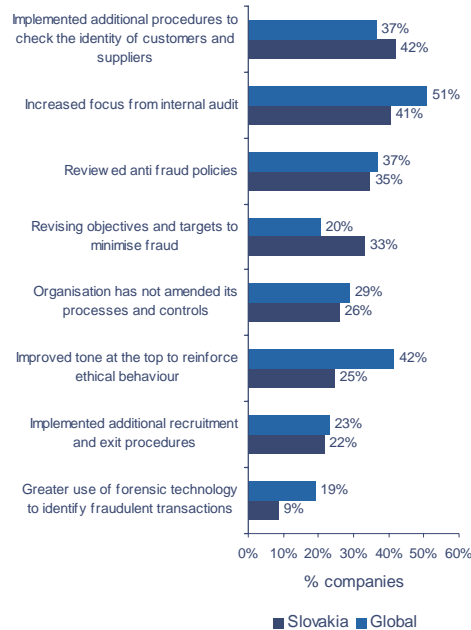
Prevention is not a rule

Despite an evident increase in incidents detected thanks to complex anti-fraud programmes, almost 70% of all respondents stated that, in their companies, an analysis of economic crime risks was not performed either at all, or only once in the last 12 months. Considering the changing economic environment, this approach is very dangerous. Specific identification of economic crime risks related to the company is a basic condition for successful identification of actual incidents.

Although the risk of fraud in an economic downturn is changing and is increasing in total, almost one-third of companies has not taken any measures leading to greater prevention of fraudulent activities. Other companies have implemented some specific precautions – internal audit most often focuses on detecting fraud (51%), management emphasizes the necessity to behave ethically in the economic downturn (42%), or companies have revised their programmes to minimise economic crime and have implemented additional procedures to examine their business partners (37%).

In principle, Slovak companies comply with these precautions, and the conclusions stated above apply to them as well. An exception is only a significantly lower percentage of companies in which top management appeals to ethical behaviour (25%), and a lower use of forensic technologies to identify suspicious transactions – 9%, compared to the global 19%.

Implemented preventive measures

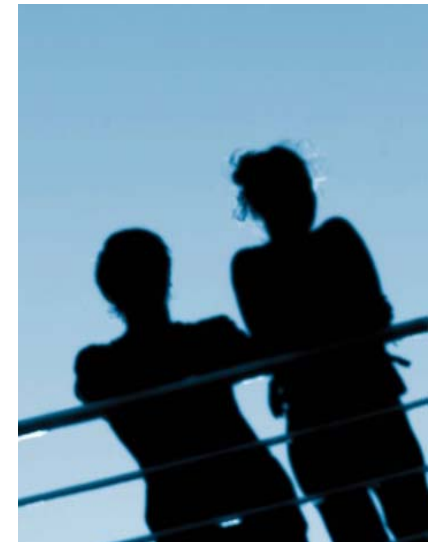
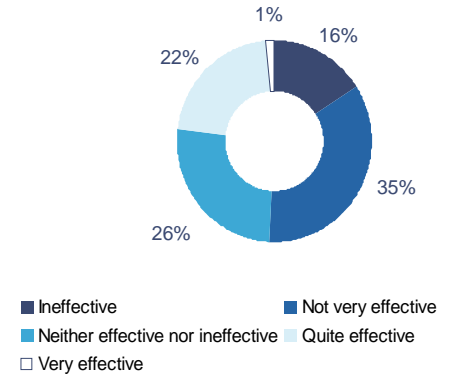


Mistrust in the effectiveness of regulatory and investigatory bodies is not specific to Slovakia

From the point of view of a Slovak enterprise, it is interesting to find out that companies all over the world have significant objections to the effectiveness of regulatory and police bodies. Almost one-half of all companies which participated in the survey have stated that regulatory and police bodies are ineffective.

Another one-fourth considers these bodies neither effective nor ineffective, which also does not manifest their strong belief that these bodies are useful in treating and investigating economic crimes. Slovak respondents have presented an almost identical opinion to the question regarding the effectiveness of regulatory and investigatory bodies.

Perceived effectiveness of regulatory and investigatory bodies



Prospects for the future: Concerns are growing

As we did in the past, we asked respondents to express their expectations regarding the incidence of economic crime in the future. In all previous surveys, these expectations were below the actual number of fraudulent incidents. This year, respondents have mentioned three types of fraud that should be most probable in the future: asset misappropriation, manipulation of financial results, and corruption. However, the expectation of future incidents, expressed in percentages, significantly differs from reality in previous periods. In contrast to the optimism shown in previous surveys, respondents are far more cautious this time. The expectation of economic crime has dramatically increased. However, this development has a positive message: To realize the risk is the first step towards successful protection.

The percentage of respondents who expect that their company will be a victim of economic crime in the following year



Methodology

PwC's fifth Global Economic Crime Survey was conducted between July and November 2009. There were 3,037 respondents from 55 countries (of which 69 were from Slovakia) that took part in answering an online questionnaire. The participants were asked to respond to questions in regard to: (a) their company; and (b) the country in which they are located.

Getting these results prepared has taken six months, during which we worked to meet the highest scientific and analytical standards. Work began with a meticulous selection of questions by the international and interdisciplinary members of the project's Survey Management Board. This was then followed by several weeks of careful data analysis by the PwC survey team. As a result, all findings have gone through several control tests before being released for publication in our survey.

The outcome of the 2009 Global Economic Crime Survey is published on the web site www.pwc.com/crimesurvey.



www.pwc.com/sk/forensic-services

Jan Vylita

Director, Investigation and Forensic Services

Tel.: +421 2 59350 417

E-mail: jan.vylita@sk.pwc.com

Andrea Hubíková

Manager, Investigation and Forensic Services

Tel.: +421 2 59350 550

E-mail: andrea.hubikova@sk.pwc.com

Vladimír Gonda

Manager, Investigation and Forensic Services

Tel.: +421 2 59350 409

E-mail: vladimir.gonda@sk.pwc.com

PricewaterhouseCoopers

Námestie 1. mája 18

815 32 Bratislava, Slovak Republic

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