



WHAT THE BEST COMPANIES DO

CORPORATE INTEGRITY PRACTICE
AUDIT DIRECTOR ROUNDTABLE®

Fraud Risk Management

Trends in Fraud Risk Detection and Mitigation

7 April 2011

Milan

A FRAMEWORK FOR MEMBER CONVERSATIONS

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WHAT THE BEST COMPANIES DO

Audit Director Roundtable®



A View of The Corporate Executive Board

To drive corporate performance, senior executives at the world's leading organizations use CEB to help them and their teams with actionable insights, analytic tools, and advisory support.

25+ Years of Experience

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85% of the Fortune 500



70% of the FTSE 100



50% of the Dow Jones Asian Titans 50

Finance and Strategy

Legal and Compliance

Human Resources

Information Technology

Sales, Marketing, and Communications

ROAD MAP FOR THE PRESENTATION

Introduction to
the Audit Director
Roundtable



**Costs and Causes
of Fraud**



Detecting
and Mitigating
Fraud



Case Profiles



Common examples of fraud include:

- Kickbacks (including the receipt of excessive gifts of cash)
- Expense Report Fraud
- Loss of Intellectual Property
- Conflicts of Interest
- Vendor Fraud
- Embezzlement
- Cheque Fraud
- Payroll Fraud
- Bribery and Corruption
- Fraudulent Financial Reporting
- Improper Pricing Activity
- Physical Theft
- Financial or Information Mismanagement
- Regulatory Breach
- Management Conflict of Interest

FRAUD ON THE RISE

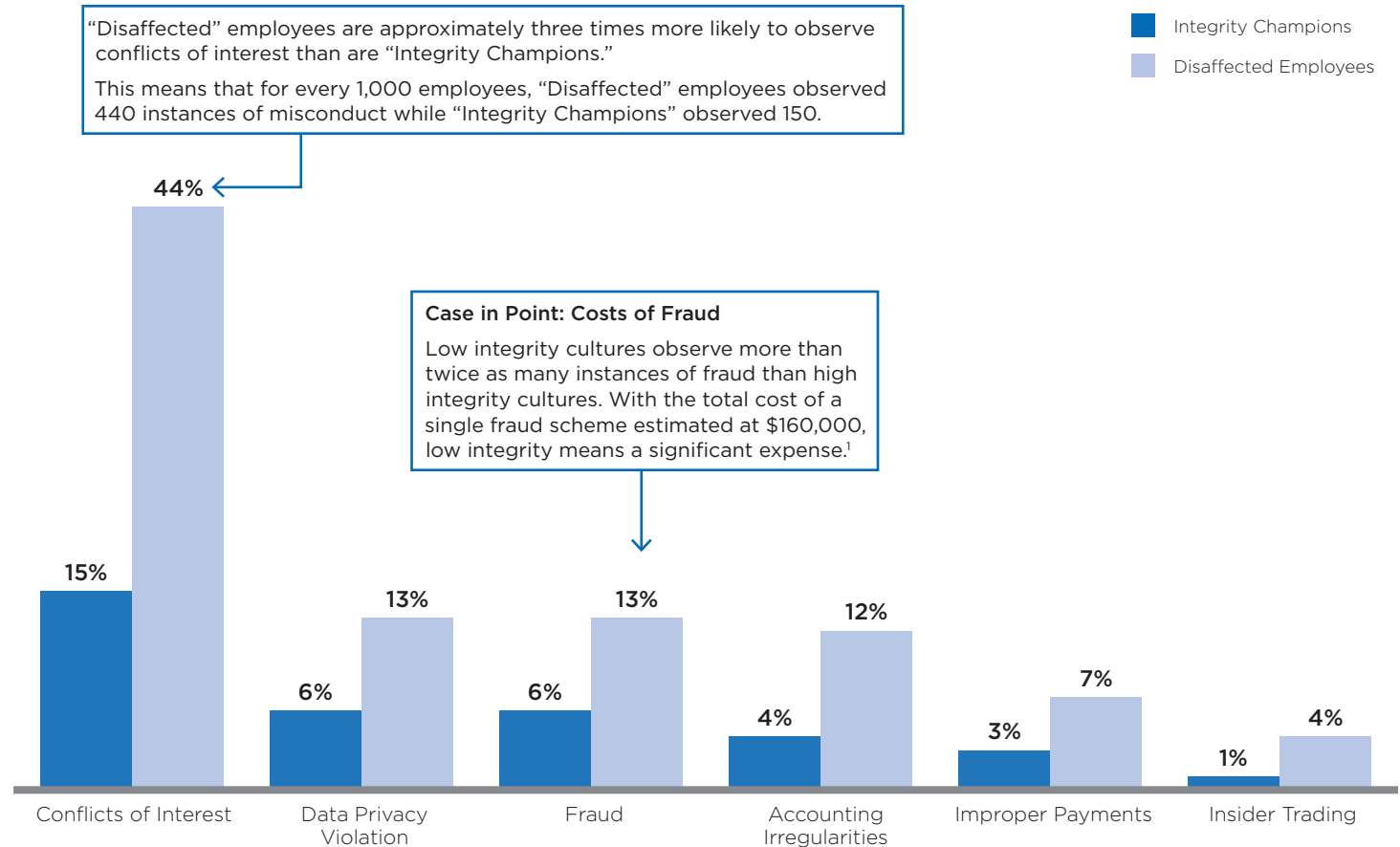
Fraud has gained unprecedented importance in the current economic environment because of the following:

- New technologies have increased the number of employees accessing corporate systems—opening doors to theft and fraud.
- Mergers and acquisitions, new product expansions, and general complexity of business operations and processes have increased the opportunity for fraud.
- The transient nature of current workforce produces gaps in controls increasing the risk of fraud.
- Slow economic times bringing increased incidences of fraud. In particular, employee misconduct becomes a greater concern due to the pressures of operating in a business environment of severe cost-reduction demands.
- Increased legal attention through new laws and increased prosecutor focus.
- Media interest in allegations of corporate misconduct, fraud, bribery, or corruption.

Employees' perceptions of the culture of integrity at their companies play a significant role in the levels of high risk compliance violations observed in the workplace.

DECLINING INTEGRITY SIGNIFICANTLY INCREASES HIGHEST-RISK BUSINESS MISCONDUCT

Percentage of Employees Who Observed Misconduct in the Past 12 Months



¹ Association of Certified Fraud Examiner, 2010 Report to the Nations on Occupational Fraud and Abuse.

From the AUDIT DIRECTOR ROUNDTABLE* of the CORPORATE INTEGRITY PRACTICE www.adr.executiveboard.com

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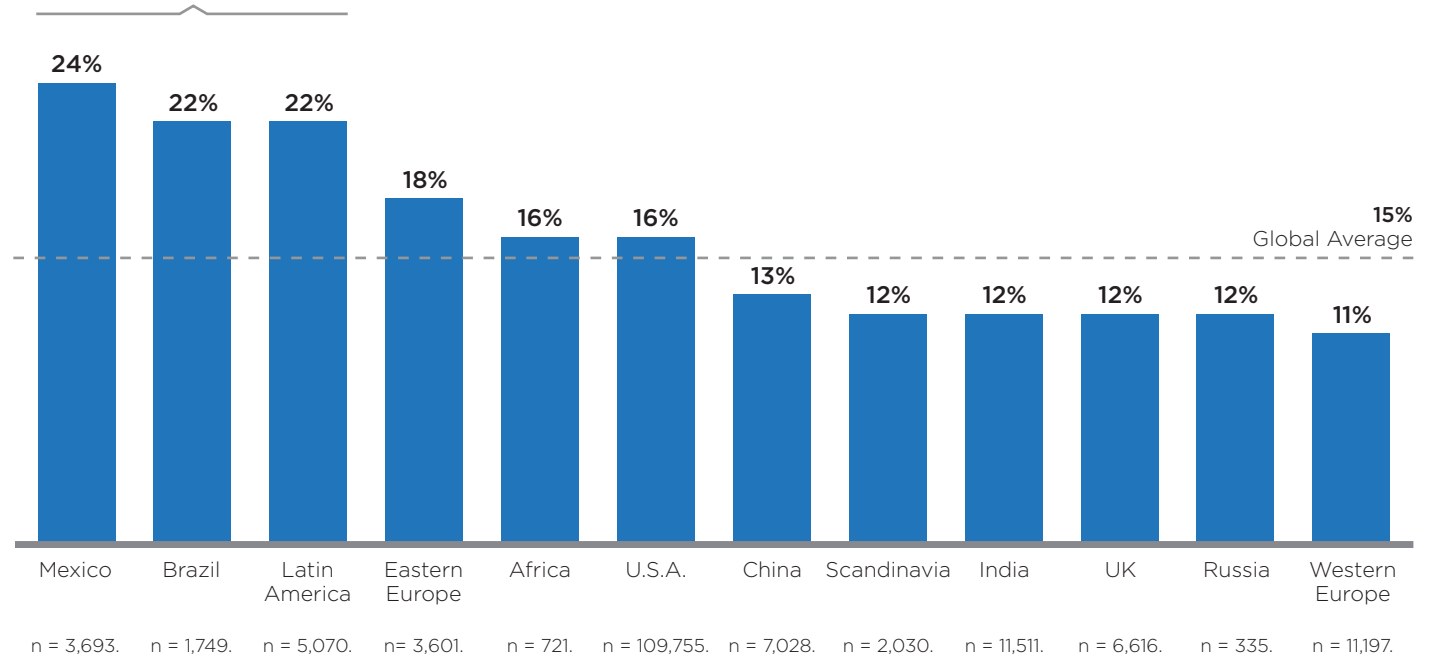
Levels of business misconduct vary widely across countries and regions.

- We examined our CELC data from more than 500,000 corporate employees around the world to analyse patterns of behavior at the regional and country level.
- High overall levels of misconduct are often driven by heightened observances of HR-related issues.

LEVELS OF OBSERVED BUSINESS MISCONDUCT

Percentage of Employees Who Observed Business Misconduct
 CELC Cultural Diagnostic Data: All Employees by Country, 2009-2010

Rates of observed misconduct substantially higher across Mexico, Central, and South America



Source: CELC's Cultural Diagnostic.

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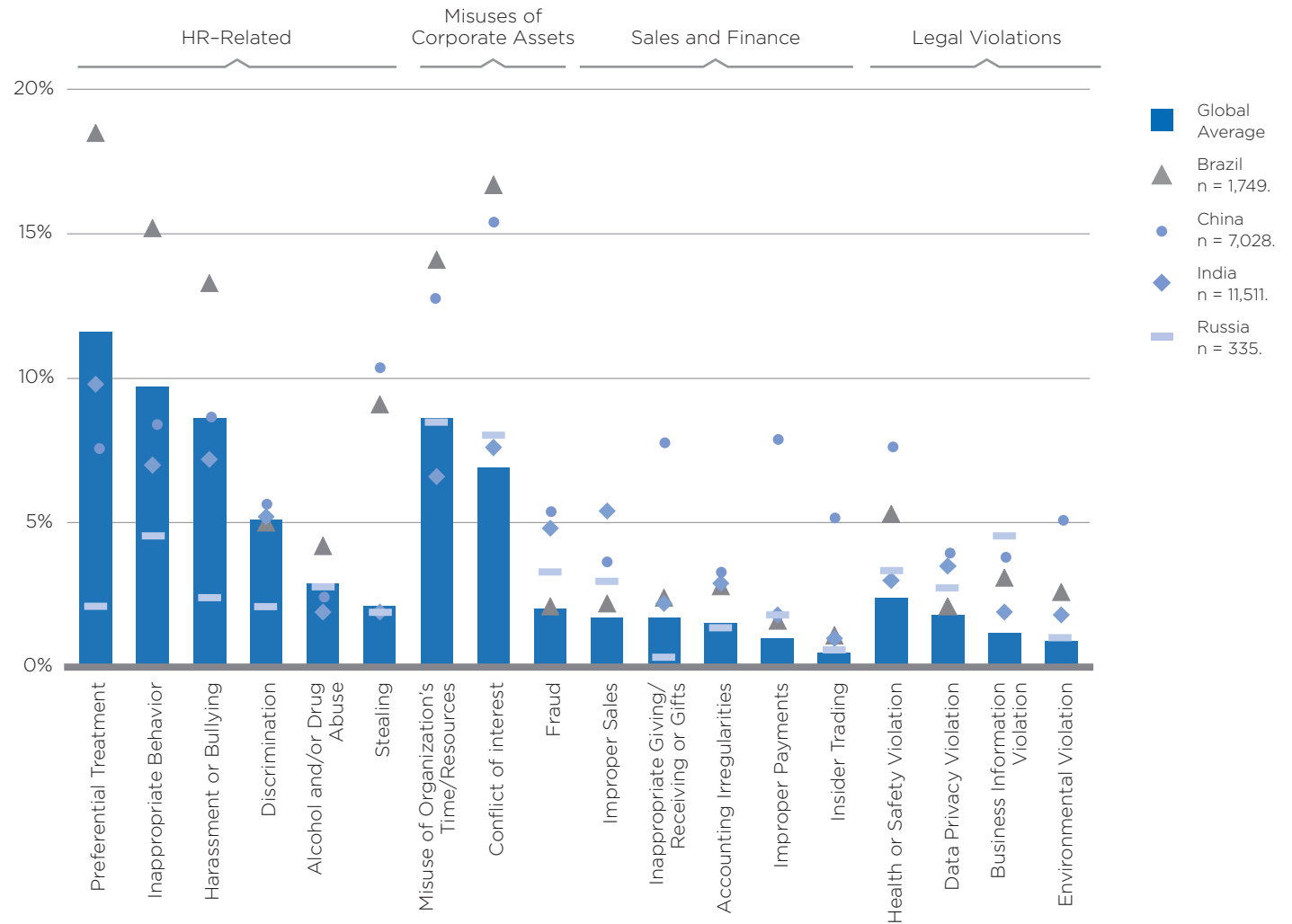
Council research indicates that business misconduct is often greater in BRIC countries.

- Brazil shows a high incidence of interpersonal HR issues.
- By contrast, Chinese employees observe more improper payments, gift giving, and conflicts of interest.

BUSINESS MISCONDUCT ELEVATED IN MOST EMERGING MARKETS

Observed Misconduct by Type

CELC Cultural Diagnostic Data: Distribution of Misconduct by Type



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Source: CELC's Cultural Diagnostic.

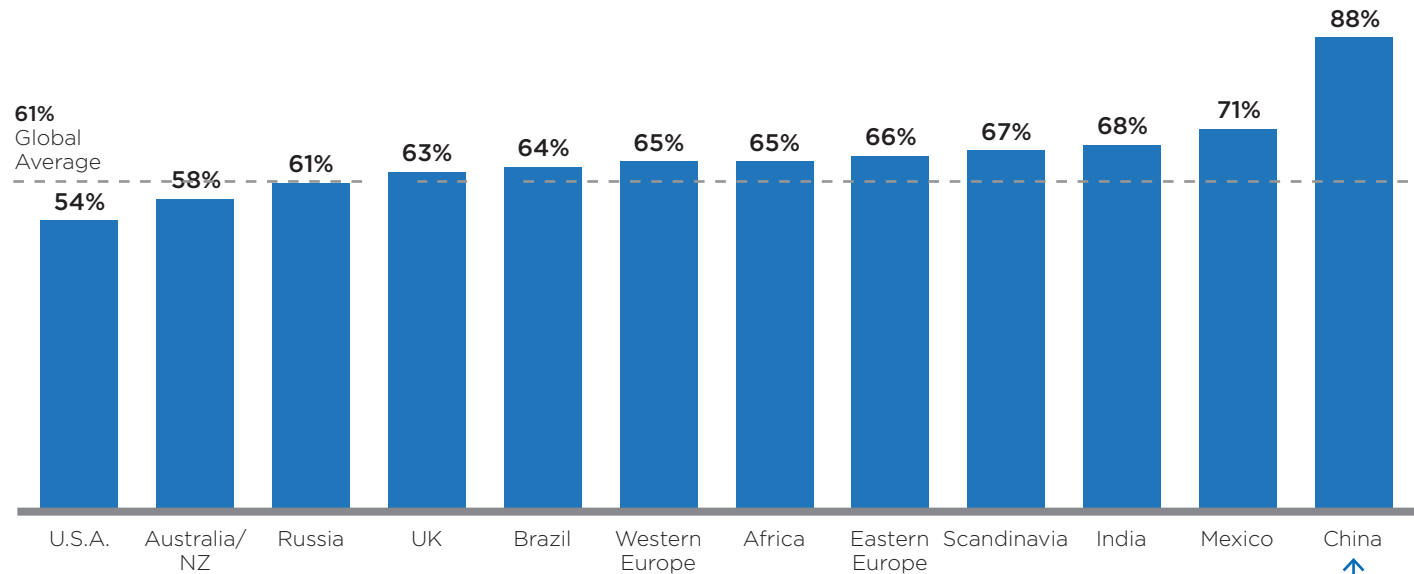
The reporting of misconduct varies widely across regions.

- Employee reporting of business misconduct is the single best source of risk information about local conditions.
- Low reporting rates signify slower detection, allowing simple misconduct to grow in seriousness while undermining the local culture.

MORE THAN HALF OF OBSERVED MISCONDUCT GOES UNREPORTED

Nonreporting Rate of Observed Business Misconduct at MNCs

CELC Cultural Diagnostic Data: All Employee Reporting by Country, 2009–2010



Why Don't People Report?

The two reasons cited most by employees as to why they failed to report misconduct are "Fear of retaliation" and "I did not think the company would do anything about my report." In Asia, the top two reasons are "Did not think I had enough information" and "Not certain it was a violation," indicating some uncertainty about what constitutes misconduct.

Chinese employees are four times less likely to report business misconduct than employees in the United States.

Source: CELC's Cultural Diagnostic

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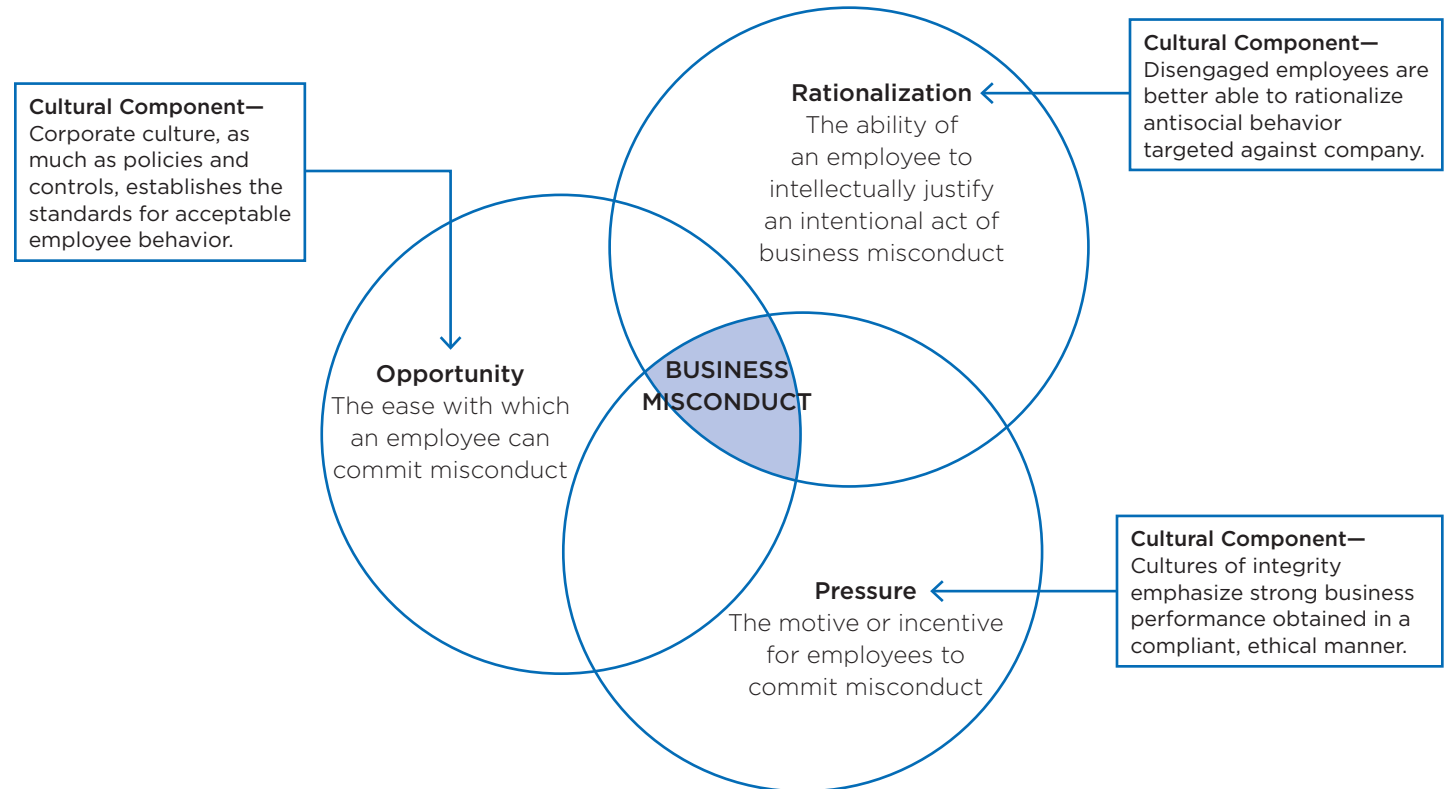
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While noncompliance and misconduct stem from many factors, organizational culture, not process failure, often lies at its root.

- Pressure and rationalization can be reduced by promoting a strong sense of ethical behavior amongst employees and creating a positive work environment.
- CELC research finds that the most significant forms of noncompliance stem from intentional employee actions, suggesting the limits of control and awareness-based mitigation strategies.

CULTURE IS A ROOT CAUSE OF MISCONDUCT

Three Underlying Conditions for Business Misconduct and Their Cultural Components



Translating for Emerging Markets

The conditions which give rise to misconduct are often exacerbated in emerging markets:

Opportunity

- Lax local control environments
- Country managers indifferent to Corporate standards

Rationalization

- Local employees possess different conception of 'fair and just' than the company

Pressure

- Business, familial, and even physical pressures often more extreme than in developed world

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Source: Based on the Fraud Triangle, developed by Donald Cressy; Corporate Ethics and Leadership Council research; Audit Director Roundtable research.

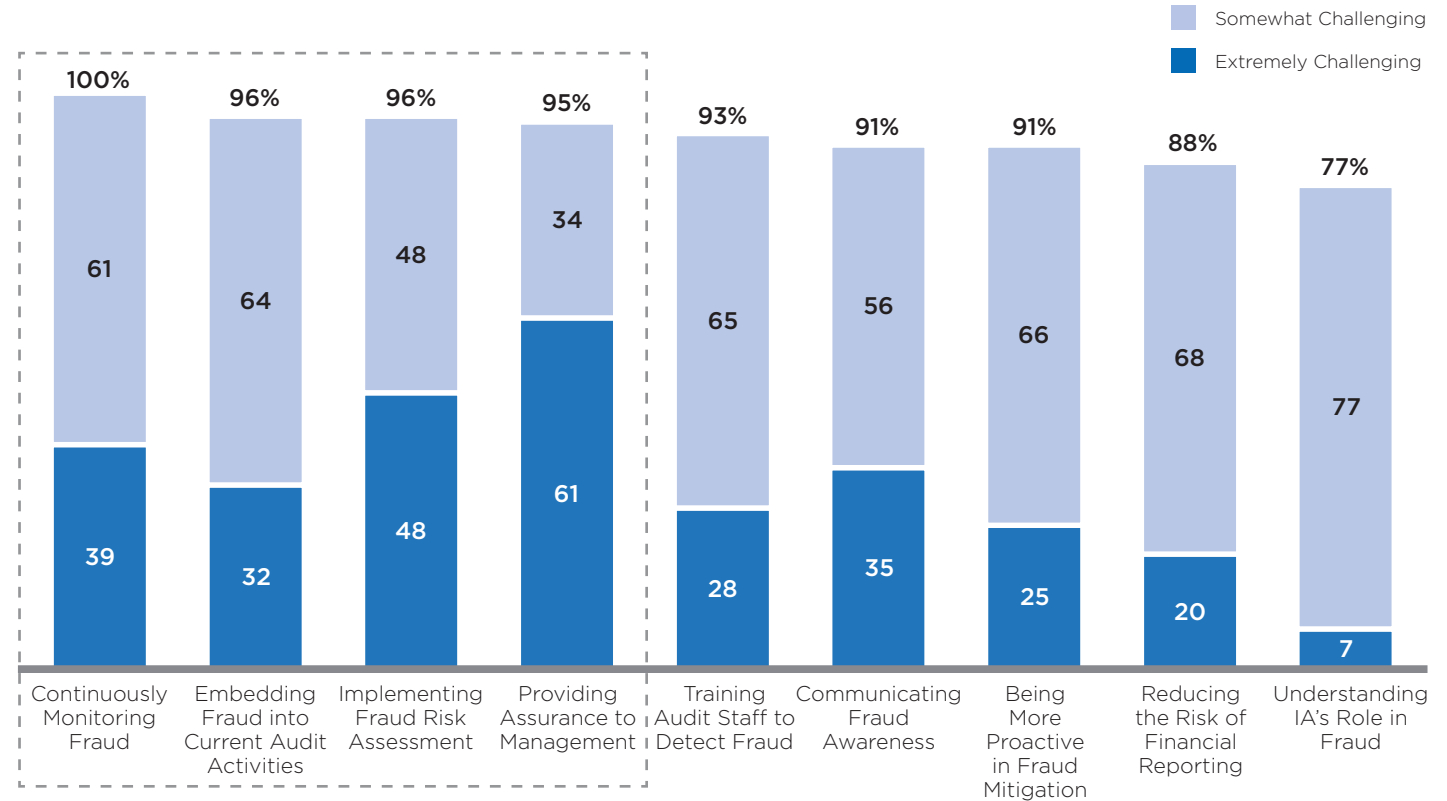


The complexity of fraud risk management leads to numerous challenges throughout the process.

WHAT'S HARD ABOUT FRAUD?

Challenges Across the Fraud Risk Management Process

Percentage of Respondents Rating as "Somewhat Challenging" or "Extremely Challenging"



n = 44.

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