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2016 Edition

# Frauds in the financial sector Survey report

# Frauds in the financial sector

## Survey Report

2016 EDITION



**The Conference of Financial Companies in Poland** was established on October 27, 1999, and brings together more than eighty key companies from many sectors of the Polish financial market, including banking, receivables management, advisors and financial intermediaries, loan institutions, management of economic and credit information, reverse mortgage and insurance. CFC is a Member of the Financial Market Development Council, created by the Polish Minister of Finance and a Member of the prestigious organization EUROFINAS (European Federation of Finance House Associations) which brings together seventeen national organizations, representing more than 1,200 financial institutions. CFC is the author of several hundred research reports, focusing on the area of credit.



**EY** is a worldwide leader of professional services market, including audit services, tax consulting, business consulting and transaction consulting. EY employs more than 212 000 workers who share common values and a commitment to provide customers with high quality services. EY's mission is to continuously improve reality which they express in the slogan "Building a Better Working World". The company helps its employees, customers and the community in which it operates to exploit their potential.

EY has offices in more than 150 countries which makes it possible to provide assistance for clients in almost every corner of the world. It has more than 1,800 professionals in Poland, working in 7 offices: in Warsaw, Gdansk, Katowice, Krakow, Lodz, Poznan and Wroclaw. EY has been repeatedly rewarded with titles of the best and most effective tax advisory firm by Dziennik Gazeta Prawna's Ranking of Tax Firms. The company has also won Rzeczpospolita's Ranking of Auditors .

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Mariusz Witalis,  
Partner EY

*Dear Sir or Madam,  
the problem of fraud in financial institutions does not lose its validity. Every day, banks, insurance companies, loan companies and leasing companies are subject to extortion, both external and internal.*

*For the past several years, EY, together with the Conference of Financial Companies, has been examining the phenomenon of fraud. The study allows us to know the extent of the problem, direction of changes and trends in the fight against extortion.*

*The summary of this year's survey results is a report that we present to you and encourage you to read it. We wish you continued success in the fight against fraud.*



Andrzej Roter,  
President of the  
Management Board  
Conference of Financial  
Companies in Poland

*Fraud is a growing and increasingly dangerous phenomenon for, not only financial, institutions. Because of that, it is very important for business practitioners to acquire up-to-date knowledge on the subject. The study has developed as a result of our joint research project has been a source of practical and useful tips to help you understand "warning signals" and design tools to deal with this negative phenomenon. The knowledge of experts - authors of the report, as well as persons representing companies that participated in the study, provides a unique opportunity to learn about the scale of new and evolving techniques of fraud or extortion, or the effectiveness of methods used to fight against fraud. At the same time, the analysis of data, conclusions and recommendations contained in this report can help to develop and implement preventive systems in financial institutions.*

*I would like to thank those who wished to share their experiences in this edition of the survey for the common good of the whole financial market.*



Andrzej Sugajski,  
Director General  
Polish Leasing  
Association

*As shown by the data of the Ministry of Internal Affairs, the number of people suspected by the police of economic crimes has been steadily decreasing since 2009 with a simultaneous increase of the identified crimes.*

*This may indicate the commission of increasingly complex economic crimes, including those committed by organized crime groups. The proceedings of law enforcement authorities are initiated mainly on the basis of state bodies' information, and therefore a matter of priority should be to strengthen cooperation between law enforcement authorities and financial market participants. An equally important factor is the exchange of experiences between institutions operating in the financial market, which is reflected in this report. The leasing industry systematically strengthens measures that aim to combat the problem of extortion. One of its elements is cooperation in the next edition of the survey and co-creation of a report devoted to the problem of fraud in the financial sector.*



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## Introduction

This report summarizes the research project “Investigation of fraud in the financial sector” conducted by EY, together with the Conference of Financial Companies (KPF).

The study on fraud in the financial sector has been conducted by EY and KPF since 2009. The developed formula has allowed to reach a wide range of representatives in the financial sector. The subject of study has gradually increased in size. Initially, the subject concerned only frauds on the Polish market of loans in the retail segment, and currently the survey has become more universal, covering the whole problem of fraud. The new formula has allowed to study diverse financial institutions such as retail banks, corporate banks, leasing companies and loan companies. The above changes have also increased the number of respondents in comparison with the previous years.

The primary objective of the study is to present the problem of fraud with particular emphasis on:

- › the scale of the phenomenon of fraud,
- › assessing the effectiveness of tools used by institutions to prevent fraud,
- › difficulties that institutions have to face in the fight against fraud.

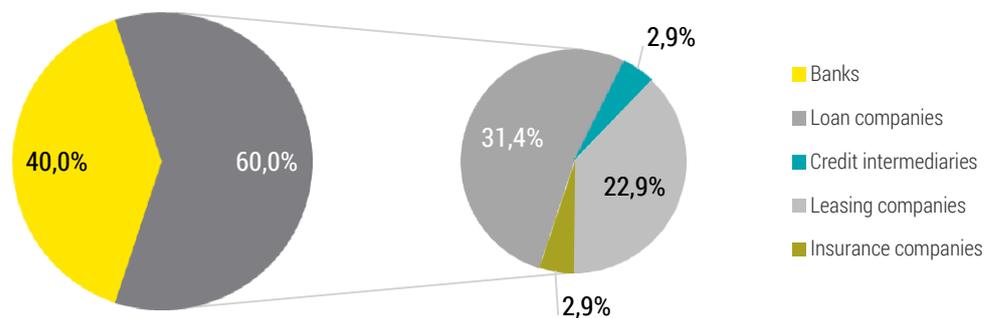
The study was conducted in the form of an anonymous survey in 2016.

On behalf of EY and the Conference of Financial Companies in Poland, we would like to thank all respondents for their time and insights.

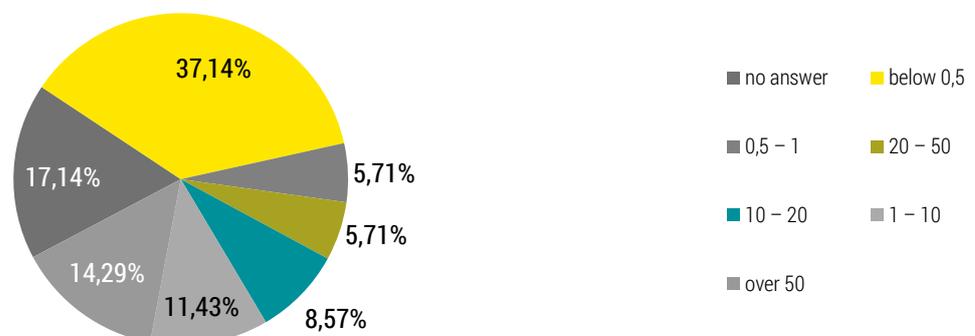
## Participants of the research

This year's study involved 30% more financial institutions than the year before. The largest group of participants in this year's study is constituted by, as in previous years, banks. Representatives of banks, including universal banks, banks specializing in retail lending, cooperative banks, corporate and mortgage banks account for almost 40% of respondents. Apart from banks, the most numerous groups in the study were representatives of retail lenders – 31% of respondents, and leasing companies – 23%. A high percentage of leasing companies among the survey respondents allowed to grasp specific problems associated with the phenomenon of fraud encountered by these companies. The respondents were also representatives of insurance companies and institutions dealing with credit intermediaries.

**Figure 1. Types of institutions participating in the study**



**Figure 2. The size of institutions participating in the study divided according to the balance sheet total at the end of 2015 (in billions of PLN)**



The number of respondents representing organizations whose balance sheet total did not exceed PLN 0.5 billion increased by nearly 8 pct., compared to the previous year. Only 14.29% of the respondents represented organizations with balance sheet total of over PLN 50 billion (11.1% in last year's survey).

## Results of research

### The scale of the fraud phenomenon

One of the fundamental objectives of the conducted study is to assess the scale of fraud. For this purpose, we asked respondents to provide a quantitative and qualitative description of irregularities existing in institutions. In particular, we asked respondents about:

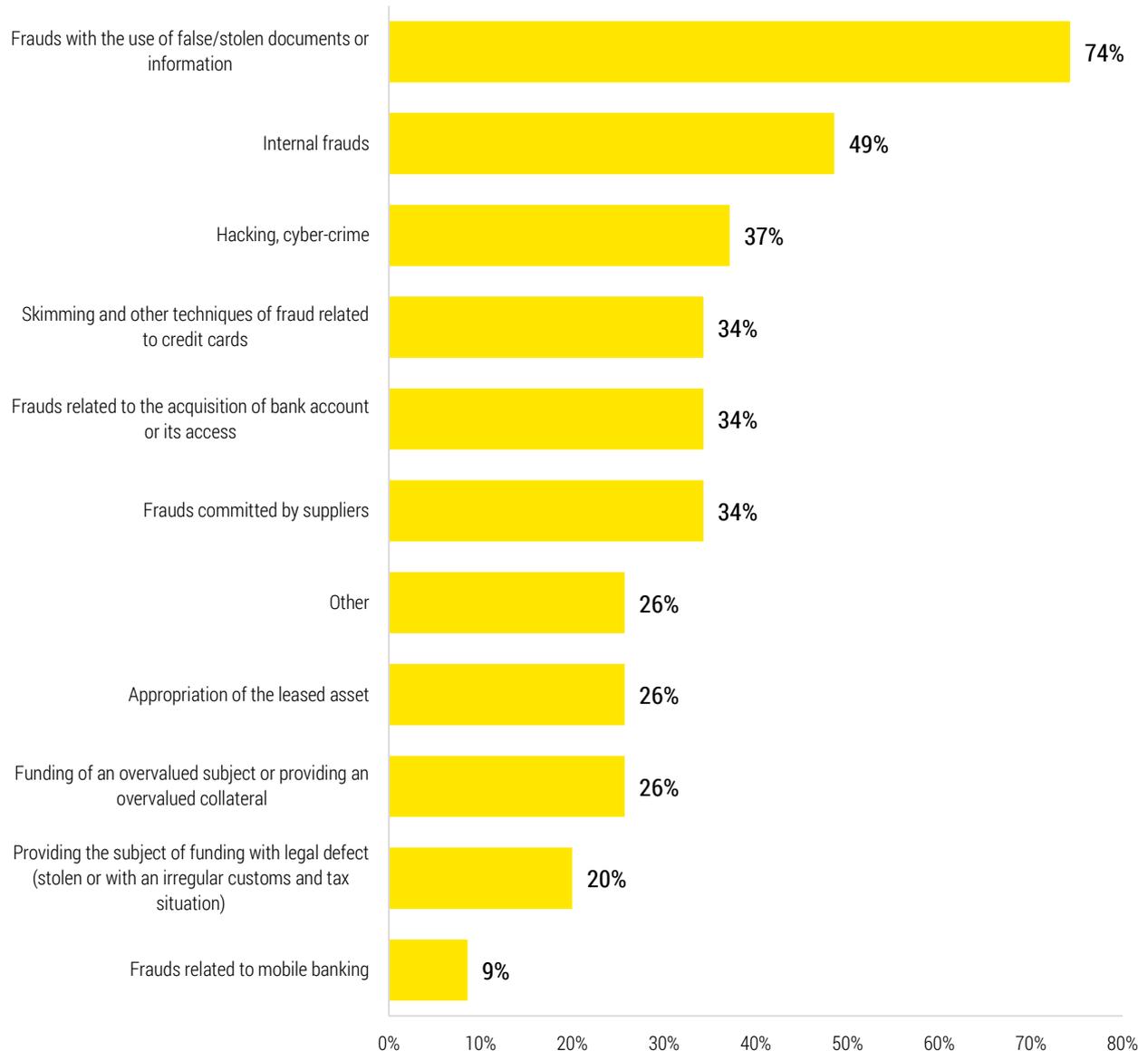
- 1) the number and type of identified cases of abuse,
- 2) the number of explanatory proceedings related to the suspected occurrence of fraud,
- 3) the number of notifications submitted by the institution on suspicion of a crime,
- 4) the estimated value of loss resulting from fraud,
- 5) the perception of fraud risk level.

Responses were analysed and aggregated in the form of the following charts.

Chart 3 shows that most respondents encountered extortion with the use of false/stolen documents or information (including the so-called money mules). This kind of fraud was identified by 74% of the respondents, that is 11 percentage more than in last year's survey. Preparation and selection of candidates for money mules takes an organized form and is carried out on a large scale by organized criminal groups. The notion of the so-called qualified money mules has emerged in response to this phenomenon. A qualified money mule is a person that was already facing other criminal charges before becoming a mule. The reason why organized crime groups invest in this type of candidates is that they usually refuse to cooperate with law enforcement authorities.<sup>1</sup> Mules with a criminal record, as persons experienced in dealing with investigators, may also easily mislead authorities conducting the proceedings.

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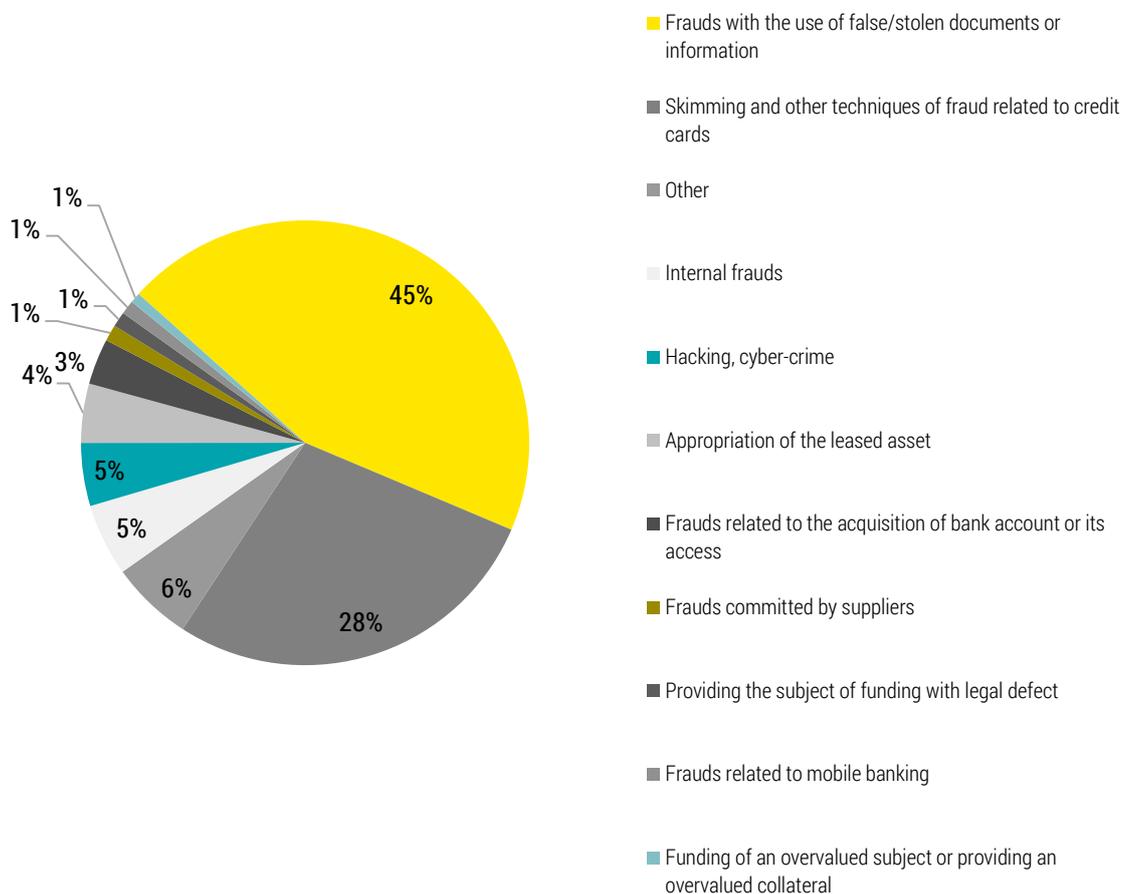
<sup>1</sup> Kamil Nowak, Wybrane zagadnienia dotyczące działalności tzw. słupów w ramach zorganizowanych grup przestępczych dopuszczających się oszustw podatkowych w związku z obrotem wyrobami stalowymi [Selected issues concerning the activity of the so-called mules on organized criminal groups committing tax fraud in connection with marketing of steel products], Przegląd Bezpieczeństwa Wewnętrznego No. 10 (6) 2014, pp. 174-175.

**Figure 3. Percentage of respondents who encountered a particular type of fraud**

The above list contains three types of frauds specific to leasing companies: appropriation of the leased asset, funding of an overvalued subject and providing the subject of funding with legal defect. These responses were indicated each time by nearly all surveyed leasing companies.

Frauds with the use of false and stolen documents or information do not only affect the largest number of financial institutions, but also account for nearly half of all identified frauds. The chart below shows how the share of individual types of frauds has shaped in the last year.

**Figure 4. Identified types of frauds (by number of occurrences)**



The high percentage of skimming and other cases of fraud associated with credit cards is also particularly noteworthy. Although skimming constitutes more than 30% of frauds identified by the survey respondents, it is still about 10 percentage less compared to last year's results. Reducing the incidence of skimming is not confirmed by the NBP survey which shows that the number of card frauds, identified by the banks and settlement agents, that took place in the second half of 2015 remains one of the highest numbers in relation to the periods previously surveyed by the NBP (National Bank of Poland)<sup>2</sup>. However, it should be noted that Poland, according to the European Central Bank<sup>3</sup>, is the fourth country with the lowest ratio of extortion in relation to the total amount of transactions made with credit cards. The countries with lower ratio are Romania, Lithuania and Hungary.

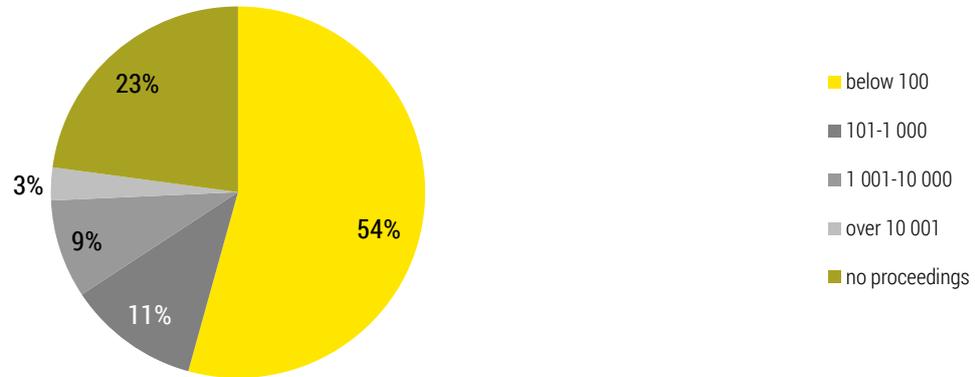
Skimming is a fraud typical for banks. Leasing and loan companies do not record this type of fraud cases.

The following graph illustrates the intensity of responding to potential fraud cases by the surveyed institutions in the last 12 months.

<sup>2</sup> Assessment of the Polish payment system in the second half of 2015, May 2016, p. 89.

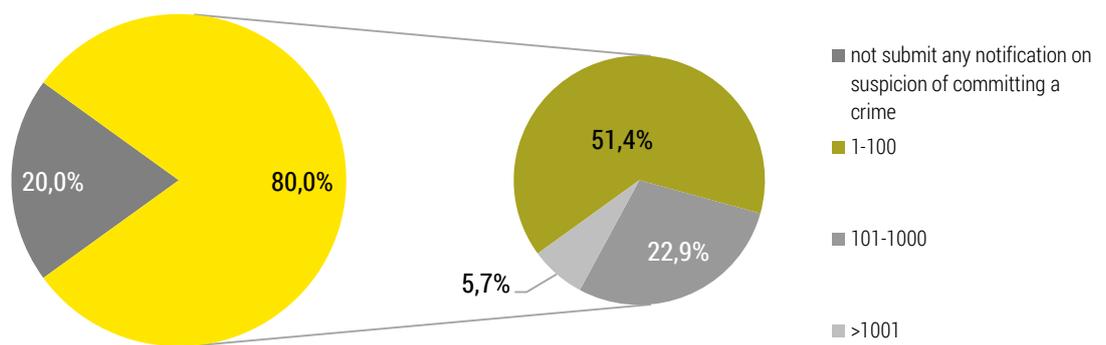
<sup>3</sup> Fourth report on card fraud, July 2015, ECB, p. 20.

**Figure 5. Number of explanatory proceedings initiated in connection with the fraud cases**



The largest group was constituted by institutions that carried out less than 100 procedures in the last year (up to 77% of responses). Included in this group were also leasing companies which conducted an average of 30 explanatory proceedings in the last year. According to the results of this year's survey, one in 4 surveyed institutions did not conduct any explanatory proceedings. A very large group of subjects from the previous study with a score of 100 – 1000 proceedings has been reduced by half in this year's survey (from 22% to 11%). Over 1000 proceedings were conducted by 12% of the surveyed institutions. At the same time surveys show that the number of conducted proceedings depends on the size of institutions. Institutions with the balance sheet total of PLN 0.5 billion conducted an average of 4 proceedings in the past year, and those with the balance sheet total of PLN 0.5 to 50 billion conducted an average of 400 proceedings.

**Figure 6. The number of notifications on suspicion of committing a crime**



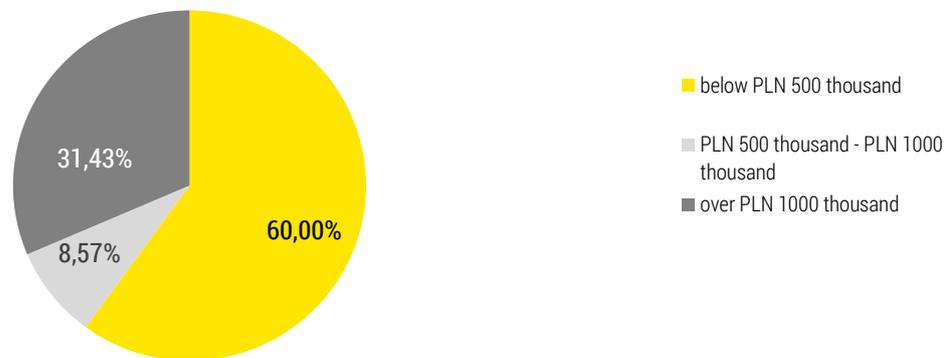
On average, each of the surveyed institutions reported approx. 425 fraud cases each year to law enforcement authorities, where 70% of all frauds within the surveyed group were reported by loan companies.

The results of this year's survey indicate that institutions are more likely to report fraud cases to law enforcement authorities than in the previous year. Only 20% of respondents did not submit any notification on suspicion of committing a crime in the past year, which is an incomparably lower result than in 2015, when that response was given by nearly 3 to 5 subjects.

The subject that most frequently submitted notifications on suspicion of committing a crime was, according to the survey results, a lending company which submitted approx. 10,000 notifications. The second subject was a bank specializing in retail lending that submitted 1 324 notifications.

The last request summarizing the scale of fraud in the surveyed institutions was to estimate the total loss incurred by the surveyed institutions in the past year.

**Figure 7. Estimated total loss incurred as a result of frauds in the past 12 months.**



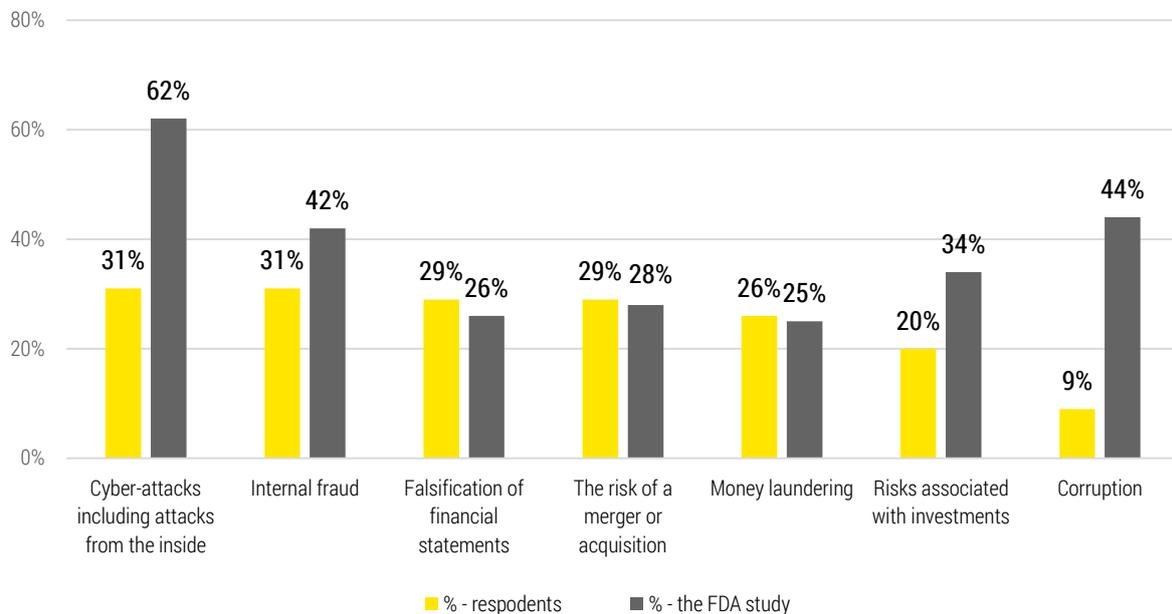
The majority of respondents (60%) affected by the problem of fraud declared a total loss in the amount not exceeding PLN 500 thousand. One in three of the surveyed institutions declared more than PLN 1 million in losses. Two types of institutions that incurred a loss of over PLN 500,000 are universal banks and leasing companies.

In case of leasing companies, it can be observed that the loss per one identified case of fraud is relatively high and amounts to approx. PLN 250 thousand.

In addition to specifying the scale of fraud, we asked respondents to identify the dynamics and direction of changes in the perception of fraud risk level associated with particular areas of the institution.

The following chart presents which areas, in the respondents' opinion, are nowadays more exposed to the risk of fraud. The answers of survey respondents were compared with the results of the study conducted in 17 countries worldwide, known as EY FIDS Global Forensic Data Analytics Survey 2016 (hereinafter: "the FDA study").

**Figure 8. Areas in which the risk of fraud has increased or has significantly increased in the past two years.**



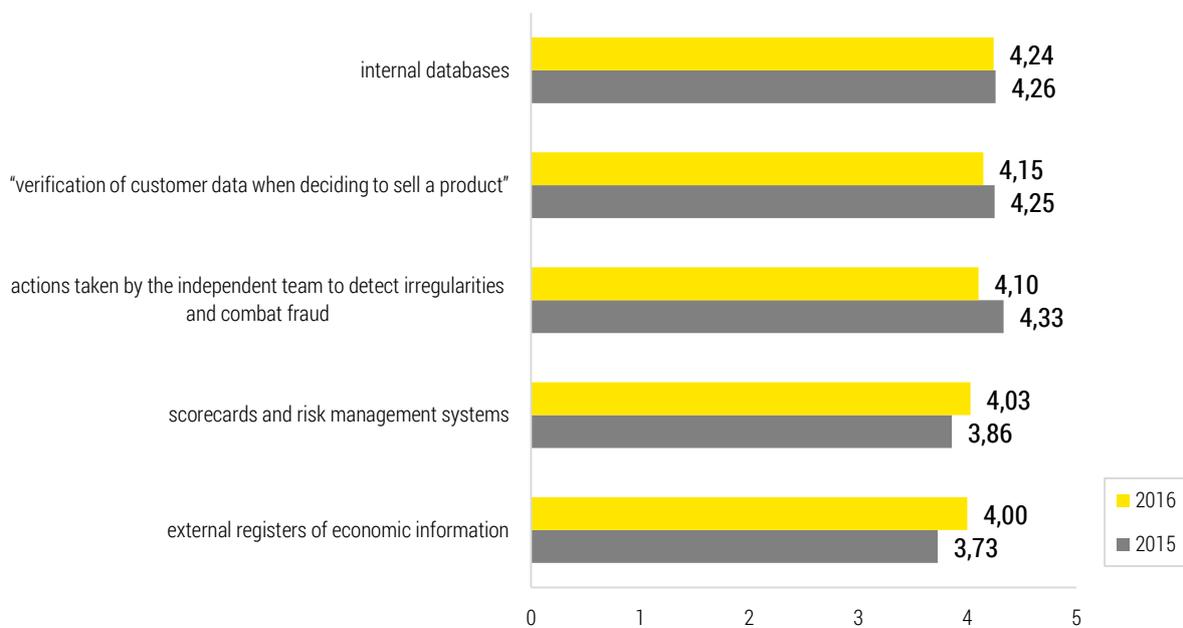
The surveyed institutions assess changes in the level of fraud risk in a more optimistic manner than respondents of the FDA study. On average, only 25% of respondents indicated that the risk of fraud has increased or has significantly increased in specific areas. That rate for the FDA study is 37%. A particular divergence in the perception of risk concerns the area of corruption (four times less indications of “has increased/has significantly increased” than in the FDA study) and cyber-attacks, including attacks from the inside (twice less indications than in the FDA study). Only one in three respondents indicated that the risk of cyber-attacks has increased in the past two years. Given that the number of hacking attacks identified in the surveyed institutions has nearly doubled in comparison with 2015, these results may indicate that there is still too little awareness of cyber risks and fraud risks among financial institutions.

## Preventing Fraud

In response to the risk of fraud, the surveyed institutions use a variety of methods to prevent irregularities and to identify frauds that could potentially occur. These tools, in the opinion of respondents, have different efficiency. In this survey, respondents were asked to indicate tools used by institutions to reduce fraud, as well as a scoring scheme for their effectiveness.

This year's results were compared with the results of the previous study and presented in the following graphs

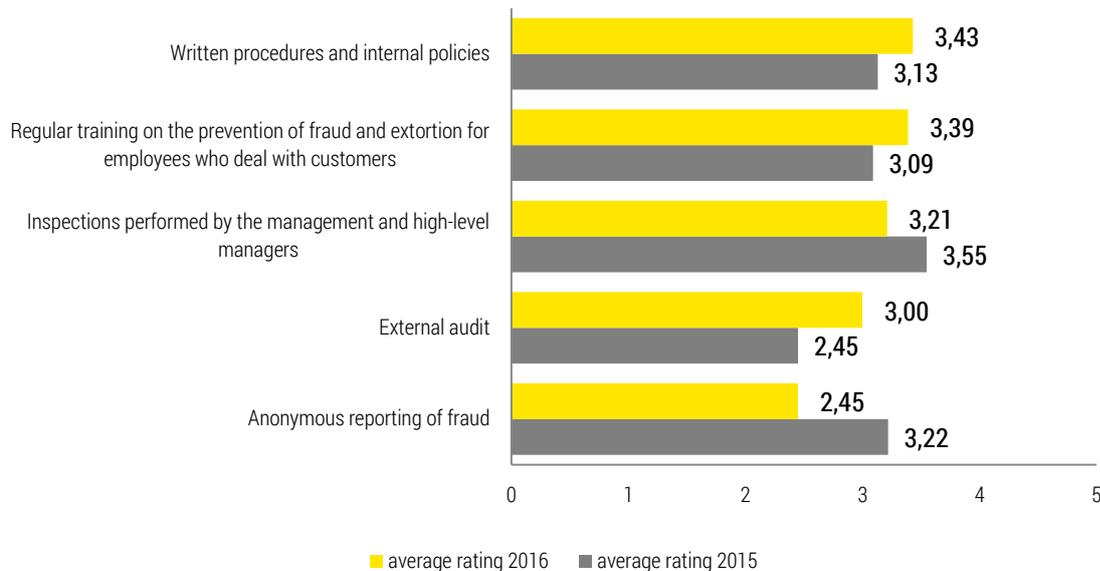
**Figure 9. The most effective methods for combating fraud (average rating above 4 out of 5)**



This year's list of the most effective methods for combating fraud is not significantly different from last year's list. Changes in the group of survey respondents and changes in the structure of the survey do not affect the assessment of the most effective methods for combating fraud. The survey respondents highly appreciate all methods of prevention, i.e. activities carried out by employees before establishing any business relationship with the customer. Internal databases and verification of customer data when deciding to sell a product were given highest scores. High scores were also given to a preliminary assessment of the customer's risk with the use of scorecards and external databases. These methods are aimed at preventing the occurrence of fraud, i.e. at preventing the establishment of any relationship with a fraudulent customer. Preventive methods for combating fraud received an average rating of 3.80 in this year's survey.

According to the survey respondents, one of the most effective method for combating fraud is having an independent, internal team to detect irregularities and combat fraud.

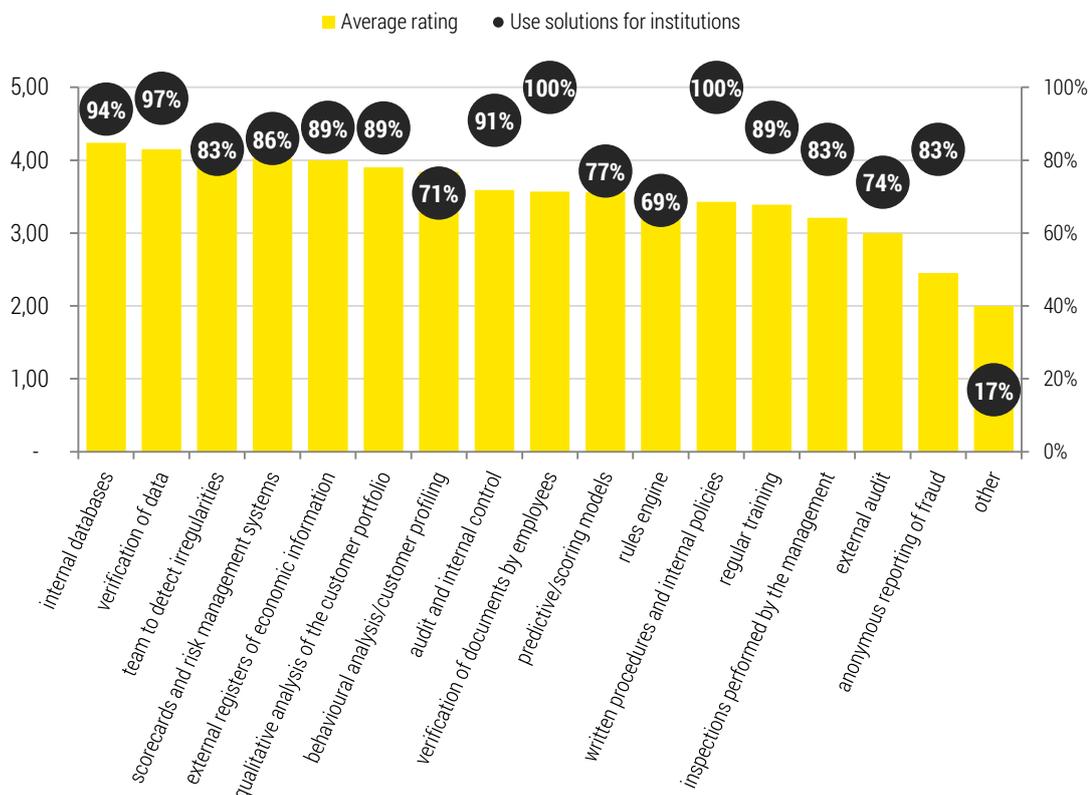
**Figure 10. The least effective methods for combating fraud (average rating below 3,5 out of 5)**



On average, detection methods were evaluated as performing less well than preventive methods (medium rating of 3.39), for example external audit, written procedures and training for workers. Low ratings were also given to anonymous reporting of fraud. Furthermore, assessment of the effectiveness of whistleblowing has dropped significantly compared to the previous survey (from 3.22 to 2.45). However, this does not mean that this method of fraud detection is, as a rule, inefficient. On the contrary. As indicated by the latest global survey ACFE (Association of Certified Fraud Examiners), the knowledge of one in two frauds comes usually from anonymous submissions. Low rating of whistleblowing may result from the fact that this solution, although quite commonly implemented in Polish financial institutions, is not used frequently. Upcoming regulatory changes can reverse that situation. Provisions requiring banks to introduce an anonymous channel for reporting irregularities, which are to come into force in January 2017, will certainly contribute to the dissemination of this tool.

Detailed answers to the question about the use and effectiveness of various methods were presented in the chart below. The left axis contains an average rating of a given solution. On the right one can find the percentage of respondents who declared the use of this method by the represented institution.

Figure 11. The tools used by institutions to combat the problem of fraud.



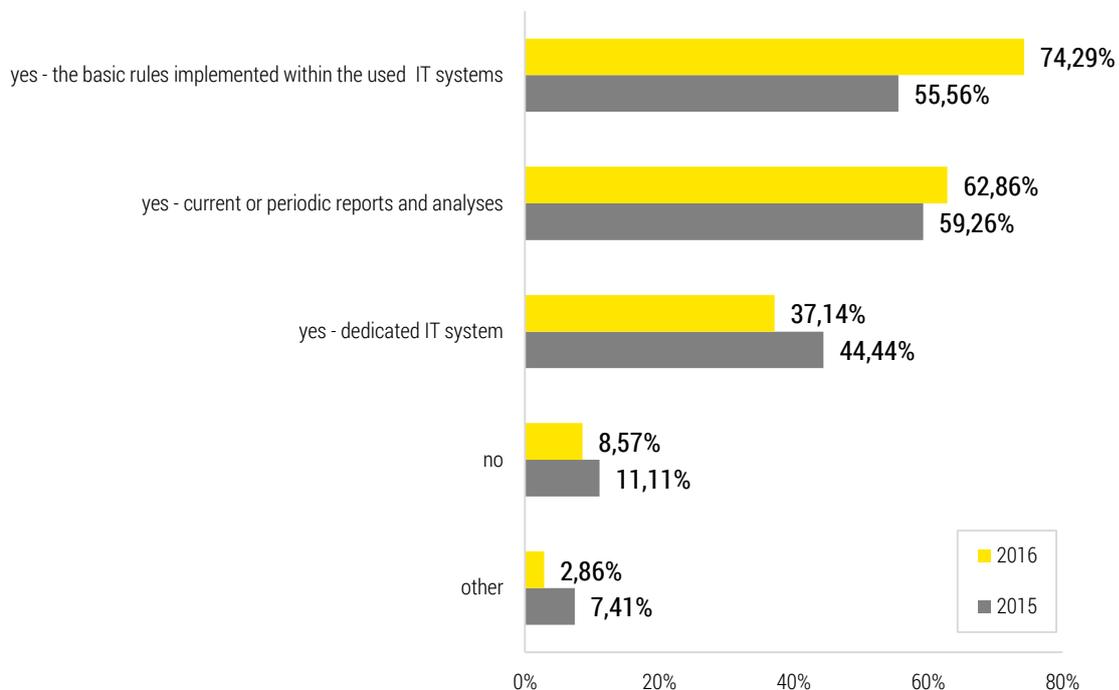
When analysing the popularity of various methods it can be observed that on average institutions use more methods from combating fraud than the year before. This difference, however, as in the case of assessment of the effectiveness, is not relevant. Each of the surveyed institutions in the past year used an average of 14 from the above-mentioned 17 anti-fraud methods. That rating in the previous study was 12 out of 16.

As in previous studies, there is no correlation between the assessed method and frequency of its application. Some of the methods assessed as relatively less effective, e.g. verification of documents by employees and written procedures, constitute an indispensable element of the anti-fraud system, hence they are used by 100% of respondents.

## IT solutions

As in the previous survey, we asked respondents a series of questions regarding the kind of IT solutions used by institutions to prevent and detect cases of extortion. We asked respondents to indicate the types of IT solutions which are used in the institutions they represent.

**Figure 12 The use of IT solutions dedicated to the prevention and detection of fraud (% of institutions)**



Over 90% of respondents pointed to the use of IT tools dedicated to fighting fraud.

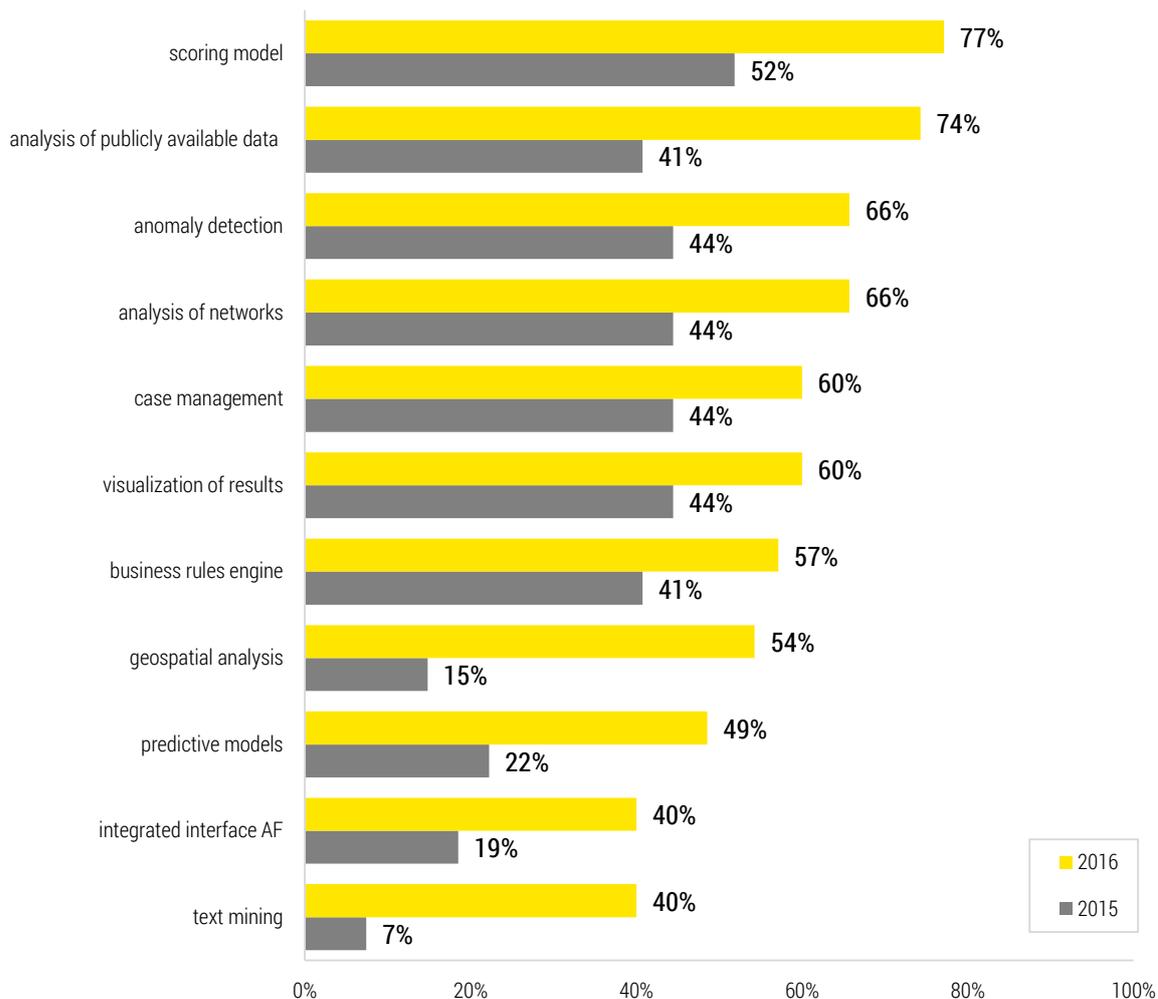
As many as 3 out of 4 surveyed institutions declared that they use solutions designed to detect potential fraud. This is a significantly higher number than in the previous study, where the possession of such solutions was declared by slightly more than half of the respondents.

Over 60% of respondents create current or periodic reports and analyses carried out on the basis of data collected in the primary (operating) IT systems.

This year's respondents included less institutions with a dedicated anti-fraud system. According to the results of the survey, this fact results from the numerous participation of representatives of loan companies, among which only 18% possess such a system. Excluding loan companies, a special, separate anti-fraud system is possessed by 46% of the respondents, which is slightly more than in the previous survey, in which participation of loan companies was small.

We then asked the respondents to identify specific IT techniques used to combat fraud and to assess their effectiveness.

**Figure 13 The use of specific techniques to detect fraud in 2015 and 2016.**

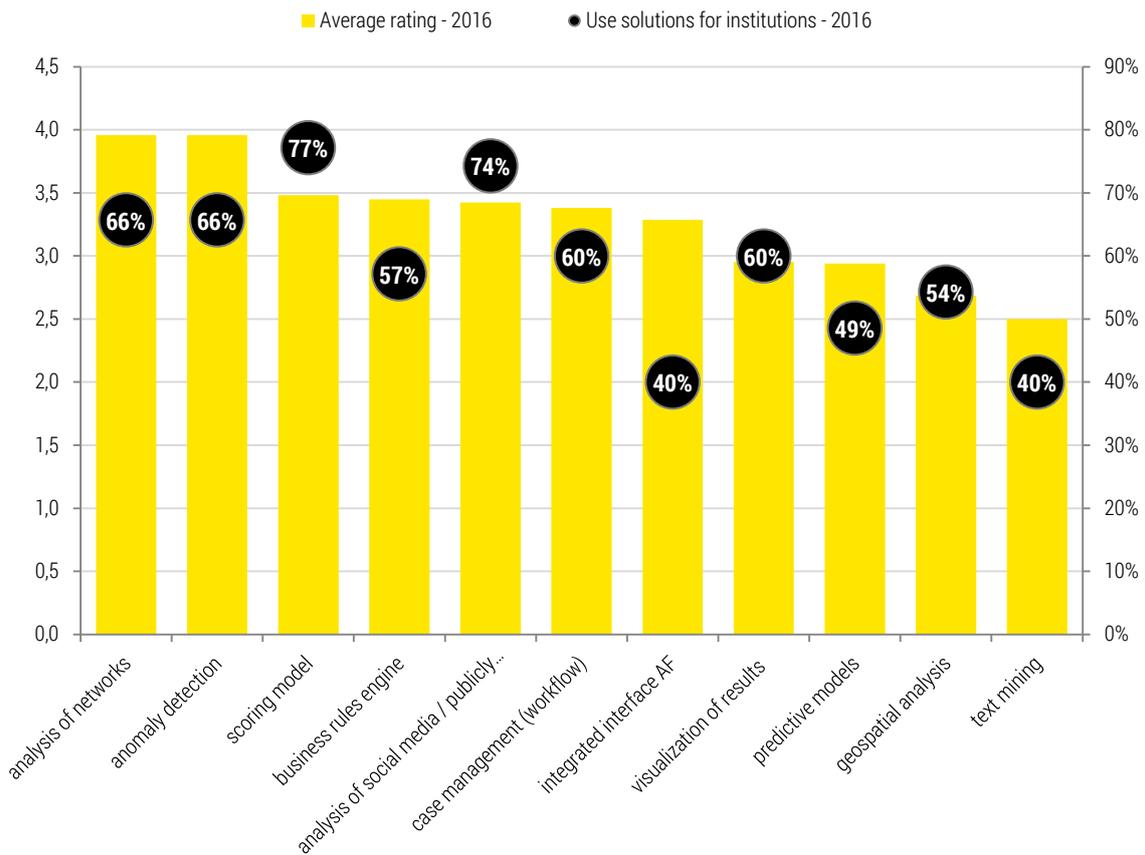


All the results gathered in the above chart confirm that institutions are nowadays more likely to apply IT technology in order to reduce the phenomenon of fraud. Each of the IT techniques indicated in the diagram was used more often in 2016 than in 2015. The geospatial analysis and analysis of publicly available data have increased in the most significant way, with respectively 39 pct. and 33 pct. more than in 2015.

34% of respondents indicated the use of at least 10 out of 11 of these techniques. This means that the Polish market has a lot of institutions which apply modern, comprehensive anti-fraud systems, using a variety of analytical techniques to detect and prevent fraud.

The graph below shows the ratings given to individual IT techniques compared with the popularity of their use.

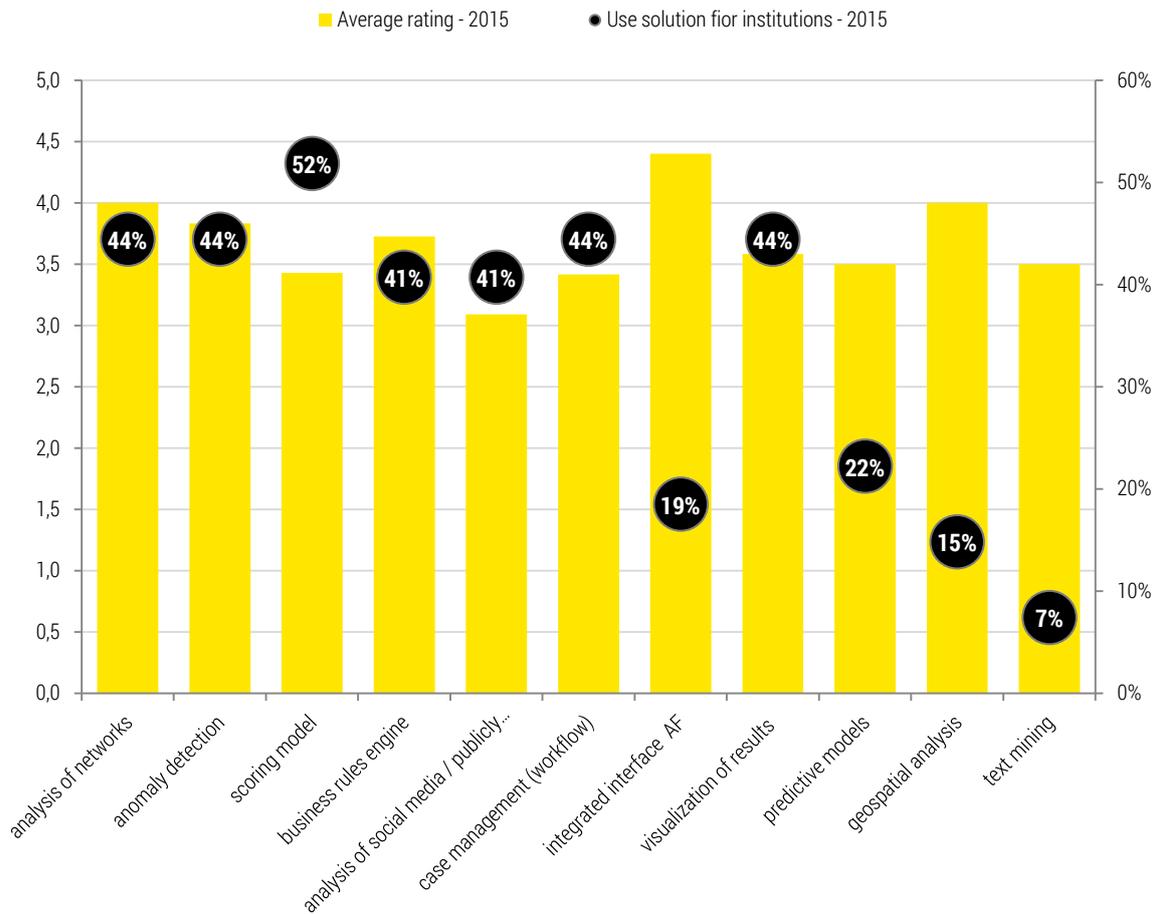
**Figure 14. Average rating of individual techniques used by computer systems to detect fraud in 2016.**



Scores, assigned to individual tools, clearly indicate that IT solutions which support the fight against fraud enjoy great trust among the respondents. According to respondents, the most effective IT tool for combating fraud is the analysis of networks and tools used to detect anomalies. These solutions are used by 66% of respondents

The survey results allow to state that there is a growing interest in analytical techniques which add value to anti-fraud systems. Each of the listed techniques was used more often than in 2015 (chart below).

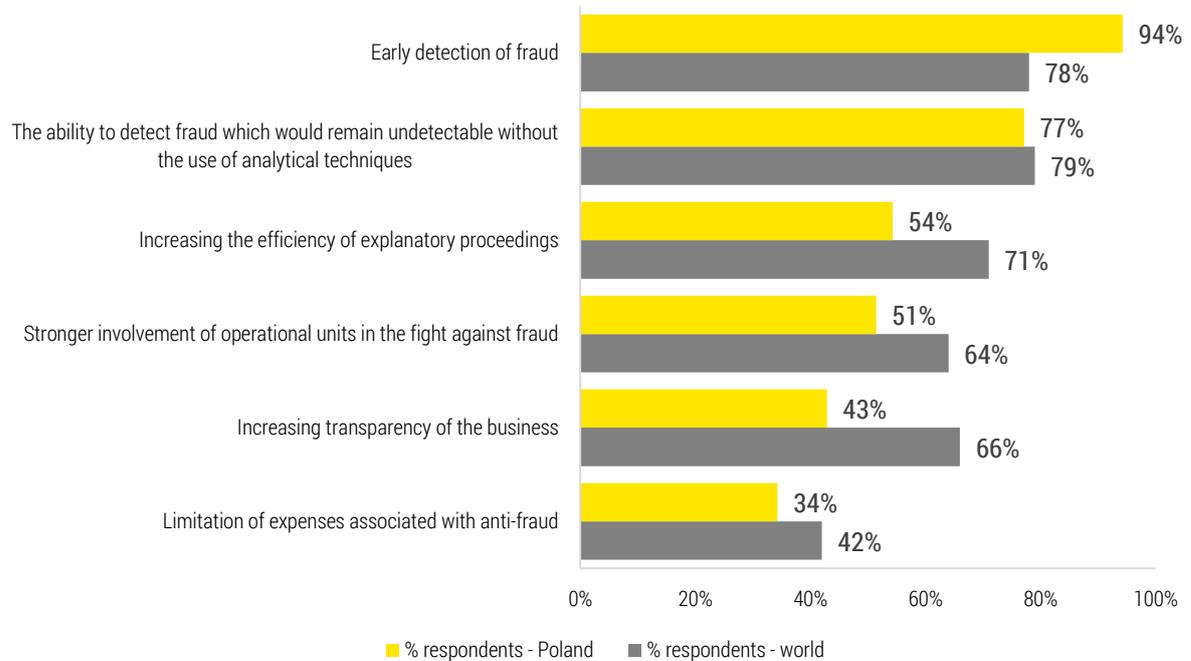
Figure 15. Average rating of individual techniques used by computer systems to detect fraud in 2015



When comparing the popularity and assessment of the effectiveness of individual tools between 2015 and 2016, it can be observed that there is a significantly higher correlation between these two parameters in 2016. Solutions with higher ratings are used much more frequently than solutions with lower ratings. This indicates a higher share of institutions that implement mature, complex anti-fraud systems, based on various analytical techniques.

The use of analytical techniques in fraud prevention programs entails many benefits which were the subject of our next question.

**Figure 16. Key benefits from the use of analytical techniques in fraud prevention programs. A comparison of the CFC study in 2016 and EY FIDS Global Forensic Data Analytics Survey 2016.**



When asked about benefits of the use of analytical techniques in the fight against fraud, the respondents mainly indicated direct benefits in the form of early identification of fraud and fraud detection, which would remain undetected without the use of these techniques. A significantly lower number of respondents indicated benefits associated with efficiency, i.e. increasing the efficiency of explanatory proceedings, increasing involvement of operational units and limitation of expenses associated with anti-fraud. The third type of benefits arising from the use of analytical techniques is the increasing transparency of the business, understood as the promotion and implementation of standards of ethics and social responsibility. 43% of respondents indicated that analytical techniques contribute to increasing transparency of the business.

Direct benefits, such as improving the efficiency and transparency of the business were indicated by a similar percentage of respondents in the FDA study.

A significantly smaller percentage of respondents pointed to the indirect benefits resulting from the use of analytical techniques, in particular to increasing transparency of the business. This may be due to the relatively short practice of using analytical techniques to combat the problem of fraud in Poland. Some of the institutions have not noticed or cannot use the full potential of this type of solutions.

## Challenges related to anti-fraud

As in previous years, in the last part of the survey respondents were asked to indicate what are the greatest, in their opinion, challenges related to preventing fraud and cooperating with law enforcement authorities, as well as to identify solutions that would help in the fight against fraud. Answers given by the respondents do not differ significantly from those given in the previous studies, which means that many institutions still face the same difficulties and solutions have not been implemented.

A summary of responses was presented in the following diagrams.

### The greatest challenges associated with anti-fraud

1. Allowing free exchange of information on discredited entities and individuals between institutions and law enforcement authorities
2. Providing appropriate technical and personal resources, including the construction of comprehensive internal anti-fraud systems for the needs of combating fraud
3. Increasing IT security

### The greatest challenges related to cooperation with law enforcement authorities

1. Not understanding the specifics of frauds occurring in the surveyed institutions
2. Excessive length of proceedings and leniency of sentences
3. Redemption of proceedings due to undetected perpetrators
4. Low punishability for attempting to commit frauds, in a situation where the institution has managed to prevent a crime

## Summary

This report summarizes the results of a study on the phenomenon of fraud in the financial sector. Our questions covered different aspects of the phenomenon of fraud, ranging from the scale, patterns of action and tools used to prevent and combat the problem.

The survey was addressed to people employed in institutions who are experts in their field and hold managerial, expert and specialist positions.

The most important conclusions of the conducted study are:

- › The survey results show no significant change in the approach to fraud compared to previous years.
- › The fastest growing threat is posed by cyber-attacks. Institutions of the financial sector are twice as likely to fall victim to hacking attacks than in the previous year.
- › At the same time, the percentage of institutions that have met with cybercrime is still not high. Cyber-attacks affect two times less institutions than frauds with the use of stolen or false documents or information – the most common type of frauds in the financial sector.
- › When asked about changes in the level of cyber risk, the respondents were less likely to point to its growth than participants of a similar survey.
- › The survey respondents highly appreciate all methods of prevention, i.e. activities carried out by employees before establishing any business relationship with the customer. These methods are designed to prevent the occurrence of fraud, i.e. to prevent the establishment of any relationship with a fraudulent customer.
- › The surveyed institutions are nowadays more likely to apply IT technology in order to reduce the phenomenon of fraud. Over 90% of the surveyed respondents use at least one IT tool in order to reduce the incidence of frauds. Institutions prefer to choose IT solutions with higher efficiency.
- › The most effective IT techniques are, according to those surveyed, the analysis of networks and anomaly detection.
- › A significantly smaller percentage of respondents pointed to the indirect benefits resulting from the use of analytical techniques, in particular to increasing transparency of the business. This may be due to the relatively short practice of using analytical techniques to combat the problem of fraud in Poland.
- › The greatest challenges associated with anti-fraud include: allowing free exchange of information on discredited entities and individuals between institutions and law enforcement authorities, providing appropriate technical and personal resources, including the construction of comprehensive internal anti-fraud systems for the needs of combating fraud and increasing IT security.
- › The greatest challenges related to cooperation with law enforcement authorities include: not understanding the specifics of frauds occurring in the surveyed institutions, excessive length of proceedings and leniency of sentences, redemption of proceedings due to undetected perpetrators and low punishability for attempting to commit frauds, in a situation where the institution has managed to prevent a crime.

