Preventing and Detecting Fraud and Corruption

Internal Audit’s Role

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Richard F. Chambers, CIA, CGAP, CCSA
President and CEO
The Institute of Internal Auditors
Agenda

• Internal Audit’s Role in Preventing and Detecting Fraud & Corruption
• Experiences and Reflections from a Retired IG
• The IIA Fraud-related Standards and Guidance
• Final Thoughts
Internal Audit’s Role in Preventing and Detecting Fraud & Corruption
## Top Internal Audit Activities

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<thead>
<tr>
<th>Internal Audit Activity</th>
<th>Currently</th>
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<tbody>
<tr>
<td></td>
<td>Percentage</td>
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<tr>
<td>Operational audits</td>
<td>88.9%</td>
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<tr>
<td>Audits of compliance with regulatory code (including privacy) requirements</td>
<td>75.1%</td>
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<tr>
<td>Auditing of financial risks</td>
<td>71.6%</td>
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<tr>
<td>Investigations of fraud and irregularities</td>
<td>71.2%</td>
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<tr>
<td>Evaluating effectiveness of control systems (using COSO, COBIT, etc., frameworks)</td>
<td>68.8%</td>
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<td>Auditing of IT/ICT risks</td>
<td>61.7%</td>
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<tr>
<td>Auditing of information risks</td>
<td>61.4%</td>
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<tr>
<td>Audits of enterprise risk management processes</td>
<td>56.6%</td>
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<tr>
<td>Project management assurance/audits of major projects</td>
<td>55.4%</td>
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IIA 2010 Common Body of Knowledge (CBOK) Study
Fraud Prevention and Detection

Potential fraud, waste, and abuse → Preventive controls

Lessons learned influence future use of preventive controls → Detection and monitoring

Potential fraud, waste, and abuse → Potential fraud

Investigations and prosecutions
Best Practices

- IA dual reporting lines – to the highest level of authority within the ministry, and an independent audit committee

- Proper allocation of responsibilities of prevention, detection and investigation
  - Coordinate efforts with other functions involved in the fraud and corruption investigation

- Reference to fraud and corruption in IA mandate

- Communication among audit committee, external audit and internal audit
  - Increased coordination of external audit and internal audit

- IA plays a key role in:
  - Advocating formalization of an internal control and risk management framework going beyond purely financial controls to include wider control environment, code of ethics/conduct and F&C prevention plans
  - Educating the public officials on the potential risks related to operations
Best Practices - Continued

• Recommend the inclusion of fraud and corruption in the internal control framework

• Assess the effectiveness of the fraud and corruption management program
  – Including ethics, conflict of interest policy, managers’ assertions etc
  – Communicating the findings in its annual report to the highest authority
  – Using data analysis and monitoring tools: continuous search for suspicious transactions or trends or controls overridden, such as segregation of duties or approval levels

• Improve proficiency and professionalism to increase auditors’ ability to evaluate fraud and corruption risks and to detect fraud and corruption as swiftly as possible.
Experiences and Reflections of a Retired IG
The U.S. Inspector General Model: My Perspectives

• The US IG Act of 1978: one of the world’s strongest ministry audit/investigation models
• However, experience reflects:
  – The dual reporting relationship fosters independence but can stifle relationships
  – Joint responsibility for audit and investigations presents numerous challenges
  – Transparency can be a blessing and a curse
  – Continuous coordination with multiple partners fosters more effectiveness in combating fraud and corruption
From My Experience:

- Internal auditors often stumble onto fraud when they least expect it.
- Fraud schemes will often be exposed by “a tip” during the course of the audit.
- It is critical to have a “predetermined protocol” for instances when fraud is exposed.
- We are not “Sherlock Holmes” – leverage the advice and expertise of legal counsel.
- The “higher up the perpetrator,” the more intense the investigation process can become.
- The personal side of fraud schemes make investigations even more challenging.
The International Professional Practices Framework:
Fraud-related Standards and Guidance
The IIA Fraud-related Standards

Internal auditors must:

• “….have sufficient knowledge to evaluate the risk of fraud…..” (Standard 1210.A2)

• “….exercise due professional care…..” (Standard 1220.A1)

• “CAE must report periodically to senior management and the board ..... on fraud risks....” (Standard 2060)
The IIA Fraud-related Standards

Internal auditors must:

• “….evaluate the potential for the occurrence of fraud and the manner in which the organization manages fraud risk.” (Standard 2120.A2)

• “….consider the probability of significant errors, fraud, noncompliance, and other exposures when developing the engagement objectives.” (Standard 2210.A2)
IIA  Fraud Related Guidance

IPPF Practice Guides
Final thoughts:

Questions the Internal Auditors should Ask

- Does the organization have a **fraud governance structure in place** that assigns responsibilities for fraud investigations?
- Does the organization have **a fraud policy** in place?
- Has the organization identified **laws and regulations relating to fraud** in jurisdictions where it does business?
- Does the organization’s fraud management program include **coordination with internal auditing**?
Questions