

The role of Supreme Audit Institutions (SAIs) in Combating Corruption

Paper prepared for Workshop on “Public Sector Financial Transparency and Accountability: The Emerging Global Architecture and Case Studies.”
9th International Anti-Corruption Conference, Durban, October 1999.

Author: Mr Magnus Borge

Position: Director General,
INTOSAI Development Initiative (IDI), Norway

Abstract

The XVI INCOSAI (International Congress of Supreme Audit Institutions), Uruguay November 1998, dealt with the role of Supreme Audit Institutions (SAIs) in Preventing and Detecting Fraud and Corruption. There was consensus that corruption has surfaced in all forms of government. Moreover, it occurs not only in government but also in all spheres of society. The INCOSAI delegates acknowledged that corruption in government results in waste of resources and reduces economic growth and the quality of life, and it undermines government credibility and reduces its effectiveness.

In general, it was considered that the socio-economic environment of the population cannot be ignored when analysing and dealing with corruption, since social injustice, poverty, and violence are often linked to corruption, which makes it virtually impossible to isolate corruption as a separate problem.

It is INTOSAI's hope that SAIs can, through concerted action, play a role in promoting a culture that rejects waste and values honesty, responsibility, and the rational utilisation of economic wealth. The fight against fraud and corruption should be presented as a long-term national effort that must be sustainable; it is not feasible to promise unrealistic progress in a short period of time.

INTOSAI Development Initiative (IDI) is an important instrument for the development of more professional and efficient SAIs in developing countries.

I INTRODUCTION

One of the main themes of the XVI INCOSAI (International Congress of Supreme Audit Institutions) in Uruguay, November 1998 was “Supreme Audit Institutions and the Prevention and Detection of Fraud and Corruption”.

Choosing fraud and corruption as a main theme I for XVI INCOSAI reflects the growing awareness on the part of the INTOSAI (International Organization of Supreme Audit Institutions) membership of this problem, which exists in varying degrees and forms in member countries.

The development of the theme began with the preparation of the principal papers for Subtheme A, “The Role and Experience of the SAI in Preventing and Detecting Fraud and Corruption” and Subtheme B, “Methods and Techniques Used in Preventing and Detecting Fraud and Corruption”. Based on these papers, 70 SAIs prepared 130 country papers describing their individual experiences. The resulting contributions were then analysed by the theme chair and subtheme rapporteurs and served as the basis for the theme's keynote speech and the discussion papers. These also served to stimulate debate during the congress.

The conclusions of the debate is summarised in the following accords.

II XVI INCOSAI URUGUAY'98 - ACCORDS

II a. General Statement

Among the numerous considerations expressed, there was consensus that corruption has surfaced in all forms of government. Moreover, it occurs not only in government but also in all spheres of society.

The INCOSAI delegates also acknowledged that corruption in government results in waste of resources and reduces economic growth and the quality of life, and it undermines government credibility and reduces its effectiveness. Some SAIs commented that they have observed a strong correlation between the level of corruption and the weakening of the lawful state and its institutions, along with the violation of individual rights.

In general, it was considered that the socio-economic environment of the population cannot be ignored when analysing and dealing with corruption, since social injustice, poverty, and violence are often linked to corruption, which makes it virtually impossible to isolate corruption as a separate problem.

The membership is also aware that a country's traditions, principles, and values influence the nature of corruption and although the SAI can do little about the fabric of society it can influence the approaches used to combat this problem. It is INTOSAI's hope that SAIs can, through concerted action, play a role in promoting a culture that rejects waste and values honesty, responsibility, and the rational utilisation of economic wealth.

Further, SAIs agreed that it is difficult to detect many acts of corruption and to estimate their financial impact, as the loss to the state does not necessarily show in the accounting records or the financial statements of the public entity. Nevertheless, statistical indicators exist that point to a likely relationship between various indices of public finance and perceived levels of corruption.

There is consensus that laws and regulations, along with adequate oversight and enforcement, can deter fraud and corruption. Some SAIs noted that excessive laws and regulations might, in fact, encourage corruption and that over regulation is a danger in itself

Examples areas of government particularly vulnerable to corruption are

- collection of taxes and other sources of revenue;
- administration of procurement and contracts;
- concession of subsidies, permits, and licenses;
- hiring and administration of personnel;
- customs; and
- privatisation process.

Some of the most common forms of corruption mentioned included misappropriation of assets, patronage, influence peddling, and bribery.

The fight against fraud and corruption should be presented as a long-term national effort that must be sustainable; it is not feasible to promise unrealistic progress in a short period of time.

II b. Discussions results

During the discussion sessions, the delegates made numerous contributions. The debate also provided a confirmation of most of the concerns and ideas that the membership expressed in the country papers.

Subtheme A. The Role and Experience of the SAI in Preventing and Detecting Fraud and Corruption.

The discussion group emphasised the fact that most SAIs believe that their main contribution as regards the prevention and detection of fraud and corruption lies in improving overall transparency and accountability, supporting an environment that limits the opportunity for acts of corruption, and creating a climate of good governance. The following issues were among those addressed in the country papers and the discussion sessions.

Strong Financial Management

When describing how they address fraud and corruption and the extent to which they are involved in their prevention and detection, SAIs generally agreed that fostering strong financial management-based on reliable, sufficient, and timely reporting, including disclosure of deviations-and effective internal control systems, represent the

basic elements of the SAI's role. A strong standards framework provides the basis for this. They also agreed that the establishment of internal auditing and audit committees would contribute to strong financial management.

Mandates

Most SAIs consider their audit mandate sufficient, although some think more investigative powers could be practical. SAIs normally do not have the powers to prosecute acts of corruption that could lie behind audit findings. Others discussed the difficulty in carrying out investigations, in view of the fact that the findings that usually results from the SAI's audit work is not usually designed to confirm the public servant's improper behaviour. Those SAIs that have investigative authority may expand the audit to collect evidence of improper behaviour. Further, some SAIs indicated that specific investigative authority is unnecessary, since the responsibility for investigation and prosecution lies within the sphere of other specialised public bodies and within the management of the audited body itself. They noted that the SAI can maintain close collaboration with all these organisations identifying better practices and using these practices as indicators.

Public Service

Another issue that was raised during debate is the need for honest, able, and well-motivated public servants. In fact, SAIs should encourage the selection of public servants exclusively **according to their integrity and capability**. Although few SAIs report the existence of government-wide formal codes of ethics, many have in place some set of standards of conduct. When establishing a code of ethics for this purpose, (such as the INTOSAI Code of Ethics) it was suggested that certain principles for the conduct of public servants be defined, such as integrity, objectivity, impartiality, honesty, and professionalism.

Resources

Many SAIs indicated that they lacked the necessary resources to do the work they felt is required. This is a serious problem that will have to be addressed in some manner. INTOSAI itself could be a possible vehicle to help address the problem.

Subtheme B. Methods and Techniques Used in Preventing and Detecting Fraud and Corruption

Although the mandates and activities of SAIs in preventing and detecting fraud and corruption vary widely, it was generally agreed that the auditor and the audit work are significant elements in reducing fraud and corruption. It was agreed that it is more cost effective to deter and prevent rather than to detect and investigate fraud and corruption. Some of the more significant aspects specifically addressed in the country papers and the discussion sessions were the following.

Most subscribe to the need to make SAI audit reports readily available to the public in a timely fashion; however, a wide range of practices exists concerning how and when

audit findings are made public. Giving more attention to developing the relationship of the SAI with the media was also mentioned as an issue that might merit consideration.

SAIs noted that some programs have more inherent control weaknesses than others and that these high risk programs by their nature or function foster an environment that favours fraud and corruption.

SAIs generally agreed that they should make the aggressive follow-up on recommendations more effective, although most reported that they do not have a formal system that tracks implementation of recommendations.

It was frequently mentioned that fraud indicators are usually difficult to identify; however, generic indicators are almost always present and auditors must rely on technical experience, professional judgement, and a firm understanding of how fraud is committed to successfully recognise these indicators. Most SAIs consider that lack of experience and training is their biggest obstacle in this respect.

SAIs generally agreed that there should be a closer collaboration between SAIs for an exchange of experiences relating to fraud and corruption.

The position of SAIs concerning financial disclosure (declaration of assets and interest) by public servants varied widely: who must disclose, what should be disclosed, how often disclosures should be filed, and who should be responsible for reviewing these disclosures. Many SAIs stated that the responsibility for reviewing disclosures should be with the government and not the SAL. Some reported that disclosures had proven useful in the prevention of fraud and corruption, while others do not believe that such disclosure is useful. However, most SAIs report that in their countries some form of financial disclosure reporting, mostly by senior public officials and politicians, is required.

Although few SAIs have systems in place to receive information by the public, others consider that such a system could strengthen a preventive environment and help identify fraudulent activity.

II c. Recommendations

SAIs agree that fraud and corruption are significant problems affecting all countries in varying degrees and that the SAIs can and should endeavor to create an environment that is unfavorable to fraud and corruption. As provided in the Lima Declaration adopted by INTOSAI in 1977, SAIs agreed that they should be independent and have adequate mandates that enable them to effectively contribute to the fight against fraud and corruption. It was also agreed that, where possible, SAIs should

1. seek an adequate level of financial and operative independence and breadth of audit coverage;

2. take a more active role in evaluating the efficiency and effectiveness of financial and internal control systems and aggressive follow up in SAIs recommendations;
3. focus audit strategy more on areas and operations prone to fraud and corruption by developing effective high risk indicators for fraud;
4. establish an effective means for the public dissemination of audit reports and relevant information including, establishing good relationship with the media;
5. produce relevant audit reports that are understandable and user-friendly;
6. consider a closer co-operation and appropriate exchange of information with other national and international bodies fighting corruption;
7. intensify the exchange of experiences on fraud and corruption with other SAIs;
8. encourage the establishment of a personnel management procedures for the public service that selects, retains, and motivates honest, competent employees;
9. encourage the establishment of guidance for financial disclosure by public servants and monitor compliance as part of the ongoing audit process;
10. use the INTOSAI Code of Ethics to promote higher ethical standards and a code of ethics for the public service;
11. consider the establishment of a well publicised means to receive and process information from the public on perceived irregularities; and
12. committees and working groups, for example the Auditing Standards Committee will consider these issues as part of developing implementation guidance as part of a broader standard framework.

III Subtheme A - The Role and Experience of the SAI in Preventing and Detecting Fraud and Corruption

The following is the content of a discussion paper based on country papers from INTOSAI members.

III a. Introduction

Emphasis on the fight against fraud and corruption is increasing throughout the world, and joint strategies are being developed to combat this so-called "social disease" that threatens to undermine and weaken democratic systems and economic growth.

By choosing "The Role and Experience of the SAIs in Preventing and Detecting Fraud and Corruption" as the main theme for the XVI INCOSAI, INTOSAI has encouraged SAIs to participate in this struggle and to pool their expertise on this matter. Sixty-eight SAIs world-wide responded to the questions raised in the principal paper prepared by Austria. This response seems to be sufficient proof that SAIs find this topic relevant and that the need exists for designing efficient audit strategies to tackle this problem.

Quite rightly, the country papers contributed their individual perceptions of the phenomenon "corruption;" nevertheless, a broad general consensus of the meaning of the term became apparent. Differences in definition mainly concern to what extent actions and practices are deemed fraudulent or corrupt from an ethical or moral point of view and what specific actions are penalised. Therefore, it seems advisable not to waste precious energy with attempts to find a globally accepted definition of this phenomenon but to focus on the role of SAIs in their fight against fraud and corruption.

The following paper summarises the valuable contributions and information presented in the numerous country papers and puts forward questions that should be deliberated in depth at the XVI INCOSAL

III b. Role of SAIs in preventing and detecting fraud and corruption

While some SAIs consider that the level of corruption in their countries is not yet of major concern, most of the responding SAIs describe corruption as being of grave significance, a massive plague, or a widespread presence in their society. It is important to note that at the same time only a few SAIs could provide estimates about the extent of corruption in their countries.

SAIs generally agree that the primary responsibility for the prevention and detection of corruption rests with the administrative authorities, the police, and other investigative institutions and cannot be counted among the main tasks of SAIs. Nevertheless, most of the SAIs agree that SAIs shall contribute their efforts in this ongoing struggle, especially by improving overall financial accountability and thereby creating a climate of transparency and good governance. Also most of the SAIs make

clear that they see their main goal more in preventing corruption than in the field of actually detecting such illegal activities.

Only a few SAIs support the idea that their authority should be extended to audit the private sphere of politicians and public servants or should be invested with the power to sanction illicit acts.

Some SAIs think it advisable to be charged with monitoring the income and assets declarations of politicians and high-ranking civil servants; other SAIs point out that this task should remain with special parliamentary committees or the courts.

Most of the SAIs consider their audit mandate sufficient, although some mention that more investigative powers would be practical.

Questions for discussion:

1. In order to determine the extent of their own roles in detecting and preventing corruption, should SAIs individually assess the extent of corruption in the public sector and develop suitable counter strategies?
2. Should SAIs seek additional authority for reviewing declarations of assets and income submitted by politicians and high ranking officials?

Sound financial management and efficient internal controls

SAIs responding generally agree that the reliability of financial management systems is essential in preventing fraud and corruption. They also consider effective internal control systems to have an inhibiting effect on potential perpetrators.

Most of SAIs ensure that evaluating the soundness of financial systems and internal controls is done regularly as an integral part of compliance audits.

Questions for discussion:

3. Should SAIs be encouraged to evaluate governmental financial systems and internal controls as to what extent they act as safeguards against fraudulent activities?
4. Should SAIs play a more active role in the development of sound financial systems ?

Focusing audit planning on high risk areas

Few SAIs have analysed and determined circumstances that indicate high inherent and control risks of illicit influence on governmental activities. Some SAIs argue that they are handicapped by insufficient manpower to undertake this kind of assessment.

However, SAIs consider staff skills and abilities, lack of function separation, procurement of goods and services without competitive bidding, weak internal control systems, low managerial capability, and political appointments as examples of high risk indicators.

Question for discussion:

- 5 Should SAIs be encouraged to analyse high risk indicators and areas prone to corruption in order to focus their audit strategy and planning on these identified issues?

Recommendations to the legislature

Most SAIs indicate that there are sufficient legal provisions in place to penalise and prosecute corrupt practices. Also in most countries procurement and tendering procedures are governed by regulations and rules aimed to ensure transparent and free competition.

While some SAIs comment on certain loopholes in the framework of regulations, other SAIs say that they do not have the mandate to make recommendations to the legislative authorities on perceived shortcomings in the practical implementation of regulations and rules.

Question for discussion:

- 6 Should SAIs be empowered to comment on the efficiency and effectiveness of regulation and rules, drawing the attention of the legislative body to rules and regulations that bring about unintended or negative consequences?

Providing expertise in the prevention and detection of Fraud and Corruption

Almost all SAIs state that there are other institutions, for example, the prosecution, police authorities, or parliamentary task forces in place fighting corruption. Most SAIs agree that the exchange of information with these bodies should be improved. Only a few SAIs argue that such a policy could endanger their independence.

Some SAIs already have regulations about how to proceed when audits uncover indicators of illicit acts. Few SAIs are obliged by law to refer these suspicions directly to the prosecution offices.

All the responding SAIs indicate that an intensified exchange of experiences and information on cases of corruption and fraud among the SAIs on an international level is highly recommendable. Although in some cases this is already done, a more universal approach is thought to be necessary.

Questions for discussion:

- 7 Can SAIs profit from a closer co-operation with other public institutions that play significant roles in the prevention and investigation of fraud and corruption?
- 8 Should SAIs - given the need - establish specialised units within their organisations providing investigative and forensic skills and expertise?
- 9 Should SAIs be empowered to report cases of possible criminal acts directly to the prosecution authorities? Is it advisable to have internal guidelines on how to cope with sufficient indicators of corruption or other illegal acts?
- 10 How can SAIs improve their mutual exchange of experiences on this topic and should they develop co-ordinated procedures in case more than one country is affected by certain acts of corruption or unethical influence?

Improving public awareness

Quite generally, it is felt that SAIs should play an active role in raising awareness of the risks of fraud and corruption and in fostering good governance and standards of conduct.

The majority of SAIs responding publish their audit reports annually after submitting them to parliament. SAIs generally confirm that the audit findings get sufficient coverage in the media. Although some SAIs argue that their main objective is to provide parliament with an independent opinion, other SAIs feel it necessary to maintain and strengthen ties with the press. In some cases, excessive time lags between actual audits and the publication of the reports prevent their timeliness and relevance.

While many SAIs regard it as important to promote the implementation of codes of conduct and ethical standards into the training of public servants, some SAIs consider such recommendations as excessive interventions into internal affairs of governmental bodies.

Responding SAIs generally agree that they must also safeguard themselves from the risks of fraud and corruption.

Questions for discussion:

- 11 Taking into account the interest of parliament and the media in topical and significant audit reports - especially on such important issues as cases of fraud and corruption - how can SAIs contribute to a timely presentation and publication of their findings?
- 12 Do SAIs agree that strengthening ties with the media can be an adequate instrument in focusing public awareness on cases of corruption brought to light by SAIs, thus producing a deterrent effect against corruption and bribery? Or do

SAIs fear that this might have an adverse effect of undermining the public confidence in governmental institutions?

- 13 Should SAIs make sincere attempts to safeguard themselves as an institution and their individual auditors from all kind of corruption and unethical influence?

IV Subtheme B - Methods and Techniques used in Preventing and Detecting Fraud and Corruption

The following is the content of a discussion paper based on country papers from INTOSAI members.

IV a. Introduction

In choosing "Preventing and Detecting Fraud and Corruption" as Theme 1, the XVI INCOSAI focuses on the role of the SAI in helping create an environment where political, financial, and legal accountability and transparency exist at all levels of government. This subtheme B summary paper highlights SAI views and experiences concerning methods and techniques that can be used to prevent and detect fraud and corruption.

In their country papers, 59 SAIs described how they addressed fraud and corruption and the extent to which they were involved in prevention and detection. The mandates and subsequent activity of the SAIs varied widely, depending on country and culture, but generally all respondents agreed with the importance of the auditor and the significance of audit work in reducing fraud and corruption.

IV b. Prevention

Fraud and Corruption: Maintaining a Preventive Environment

Experts agree that it is easier to prevent fraud and corruption than to detect it. Key elements in creating and fostering a "preventive" environment against fraud and corruption include strengthening financial management systems, evaluating internal control systems to identify and correct weaknesses, and heightening public awareness of SAI findings.

Strengthened Financial Management

Annual financial reporting (that includes financial, compliance, and performance information) as part of a strong financial management system is considered to be necessary for effective accountability. Almost all SAIs agreed that strong financial management, based on reliable, complete, and timely financial reporting, supports a preventive environment by limiting the opportunity for fraud and corruption. Even those SAIs who felt they had little experience on which to base a judgement considered sound financial management a precondition for preventing fraud and corruption. Most countries require the heads of departments of their respective governments to prepare annual financial statements. These annual statements are

audited by the SAI and, in some cases, public accounting firms, thus limiting opportunities for irregularities.

Evaluating Internal Control Structures to Identify and Correct Weaknesses

Evaluating systems of internal control, recommending improvements to internal controls, and following up on recommendations are described in the principal paper as the main components of a control environment designed to prevent fraud and corruption.

However, most SAIs do not develop standards for internal controls but rather serve in an advisory capacity. Acceptance of the guidance they provide is not mandatory. While almost all SAIs assess internal controls, nearly one-third of the SAIs report that no requirements exist for program officials in their governments to assess and report on the internal controls systems they have in place. One SAI reported that over 70 percent of fraud it found over a 3-year period was attributable to either failure of existing controls or absence of proper controls.

Following up on recommended improvements to internal controls, while within most SAIs' authority, appears to be a practice that is approached less aggressively. Most SAIs follow up on recommendations annually, at the time of the next scheduled audit.

In some cases, the responsibility for following up on recommended changes lies solely with the government official responsible for the audited department. Further, none of the papers identified a formal system that tracked recommendations to ensure that they had been implemented.

Several of the SAIs referred to the significance of the personal and professional integrity of the civil servant in their discussion of internal control systems. They point to management weakness and management failure as significant elements in corruption cases they have experienced. The SAIs suggest more comprehensive penal provisions, greater co-operation among government authorities, and public disclosure as possible mitigating elements. Conversely, one SAI raised the possibility that overly strident, authoritarian controls could contribute to fraud and corruption by causing managers to break rules to achieve results and meet program objectives.

Questions for Discussion

1. Should there be aggressive follow-up to recommendations?
2. Would a formal system for tracking recommendations result in better implementation?

3. How can SAIs use the work of INTOSAI's Internal Control Standards Committee to evaluate systems of internal control? Delegates will be invited to explore this possibility in Theme 11 discussions.

Heightening Public Awareness of SAI Findings

In addressing prevention of fraud and corruption, the principal paper points to heightened public awareness as one means of increasing accountability through timely public disclosure of audit findings. Reporting audit findings and any resultant legal action enhances fraud prevention by making government officials and the public aware that effective internal controls are in place and working.

The degree to which SAIs publicise audit findings ranges from SAIs who report only to the parliament, a few who make restricted distribution of audit findings, to those who make findings public as a matter of routine as soon as the results are issued. Some SAIs include only particularly noteworthy findings in an annual report to the parliament that is then made available to the public.

Views of the SAIs differ regarding the preventive value of making audit results public. Some SAIs say that public disclosure deters fraud and corruption. They suggest that, at best, public disclosure of corrupt officials deters collusion and other corrupt practices by managers; and, at the very least, increases public awareness, however modestly. Others question that premise, and a few countries expressed concern that public disclosure of fraud could lead to more sophisticated schemes and better informed criminals.

The principal paper discussed one technique that is directly tied to public involvement-promotion of a mechanism for citizens to report fraud and corruption. Establishing a means for anonymous reporting by the public can strengthen a preventive environment and identify fraudulent activity. However, few SAIs have formal systems in place to receive such information. Use of technology (such as the Internet) or a telephone hotline is very limited, and most SAIs rely on correspondence as the primary mechanism for receiving information from the public.

Questions for Discussion:

1. What methods can SAIs use to heighten public awareness of audit findings?
2. Should SAIs have a publicised system available as a means for citizens to report fraud and corruption?

IV c. Standards of Conduct and Financial Disclosure

As tools in preventing fraud and corruption, government-wide standards of conduct and financial disclosure play an important role. According to the principal paper, public awareness of standards of conduct increases the probability of detecting fraud. Similarly, financial disclosure promotes adherence to standards of conduct, exposes

potential conflicts of interest, and supports transparency in the government. Financial disclosure declarations that are updated annually and subject to review help promote an environment that is not favourable to fraud and corruption. And yet, SAIs report widely varying degrees to which standards of conduct are applied, and some question the usefulness of public financial disclosure in preventing corruption. Further, INTOSAI's Audit Standards Committee has addressed the issue of a Code of Ethics for SAIs, which could serve as a model for standards of conduct for civil servants.

Standards of Conduct

While SAIs recognised the value of employees whose background and experience demonstrate high ethical standards, few report government-wide codes of ethics. However, standards of conduct are in place in a majority of SAIs reporting. In some countries, standards of conduct are agency-specific; in others, the standards are components of a penal code or other regulations. Several countries see moral qualities - trustworthiness, loyalty, and righteousness - as characteristics of strong ethical conduct imbued in their officials by virtue of their academic achievement or professional qualifications. Yet another states outright that its civil servants know what is expected of them and, consequently, would not engage in fraudulent activities.

Question for Discussion:

How can SAIs use the Code of Ethics prepared by INTOSAI's Audit Standard Committee as a model for use throughout government? Delegates will be invited to explore this possibility further in Theme II discussions.

Financial Disclosure

A comparison of responses by SAIs concerning financial disclosure reporting requirements shows a wide range in what is reported, who must report, and how often reports must be filed. Many SAIs report that financial disclosure requirements extend only to political appointees or high-ranking civil servants, such as ministers. Disclosure is often limited to reporting private assets upon assuming office and when leaving office. Some countries note that such a requirement is only for those (whether executive, manager, or staff) in situations that could give rise to a conflict of interest. One SAI looks for discrepancies between declared assets and signs of wealth. In several countries, disclosure also includes family members of a civil servant. As many as one-third of the respondents say that public disclosure is not required in their respective countries.

As to the efficacy of public disclosure of private assets, opinions vary. For instance, one SAI reports that financial disclosure declarations are kept in a register that the public may examine. Any member of the public may write to the country's Chief Justice or President to report violations or questionable disclosures. Conversely, some countries require no public disclosure at all, to the extent of one SAI considering such a requirement to be a breach of personal privacy.

A number of developing countries defer an opinion, based on limited experience in this area; others say that in the framework of fighting fraud and corruption, they have not considered public disclosure as a useful tool.

Question for Discussion:

Would annual disclosure declarations and subsequent reviews of private assets by government employees at the managerial level help prevent fraud and corruption?

IV d. Detection

As a natural outgrowth of SAI audit and oversight responsibilities, detection of fraud and corruption is practised on three levels, depending on each SAI's particular mandate and government structure. Some SAIs refer fraud indicators to investigative bodies and work with those entities to determine if fraud and corruption has occurred. At the other end of the spectrum, a few SAIs report possible wrongdoing only to the responsible department head of the agency being audited. Most, however, notify appropriate legal authorities, after establishing reasonable confirmation, of indicators through extended audit steps.

In considering the most effective methods SAIs can employ to detect fraud and corruption, SAIs were asked to address how they determine program vulnerability and high risk areas and describe their experiences in identifying fraud indicators through examination of internal controls.

High Risk Reviews

Defined as those areas that have more inherent control weaknesses than others, high risk programs, by their nature or function, foster an environment that favours fraud and corruption. SAIs follow many practices in identifying high risk areas, from reviews of a previous year's audit work as a base for planning for the coming year's work to systematic, across-the-board evaluations of program vulnerability based on internal controls, past history of program abuse, and management strength or weakness. These two approaches represent different concepts of risk assessment. In the first, programs and departments scheduled for review are ranked as low, medium, or high risk in order to prioritise a comprehensive audit plan. This allows SAIs to allocate resources according to a program's particular level of vulnerability and build in additional audit procedures where appropriate. SAIs report that high risk audits have identified significant fraudulent activity.

The second approach focuses more on program areas, rather than departments or units of government, and becomes the basis for a strategy to target a particular area that poses a continued, significant threat to public resources. For instance, one SAI identified road construction as a high risk area. Its efforts to address fraud and corruption in road construction went well beyond a program audit. Specifically, it identified the causes, effects, and forms of corruption in that program. It also developed options for preventing and detecting fraudulent activity and presented seminars for internal auditors to increase awareness and offer specific training. Its

efforts are culminating in the issuance of a comprehensive report on fighting corruption in public road construction.

Most SAIs occupy a middle ground, with *de facto* risk assessment. In other words, within the framework of planning annual audit activities, consideration may be given to those areas that historically hold the greatest potential for abuse: procurement and contracting, construction projects, licensing and issuing of permits, and activities-with a large number of daily transactions and limited staff. Priority is often based on previous audit findings and recommendations, in addition to any information or complaints from the public.

Question for Discussion:

What strategies can SAIs use to predict those areas that may become high risk?

Identifying Fraud Indicators

Several commonly held beliefs are expressed in the SAI responses concerning fraud indicators. Fraud indicators are generally difficult to identify. While commonality can be found in fraud cases and generic "red flags" are almost always present (see the principal paper for an explanation of the elements of fraud and many common indicators), an auditor must rely on technical experience, professional judgement, and a firm understanding of how fraud is committed to successfully recognise its indicators. Transactions that may be fraudulent and circumstances made to appear legitimate must be viewed through a lens of auditor scepticism. Most SAIs considered lack of experience and training as the biggest obstacles to maintaining such scepticism as it relates to fraud and corruption.

The SAIs report different methods for promoting fraud awareness among auditors. Formal training is offered in several SAIs. Countries with fewer resources to devote to specialised training try to take advantage of training opportunities offered by neighbouring countries. One SAI participates in a co-operative effort with penal authorities to expose auditors to investigative perspectives, and several SAIs have developed fraud-related audit guides specific to particular program areas. In light of the generally held opinion that successful identification of fraud indicators is dependent on successful auditor training, the following questions are posed.

Questions for Discussion:

- 1 Can standards and methods for identifying fraud indicators be developed that would assist auditors in recognising the potential for fraud and corruption?
- 2 With only 20 percent of responding SAIs describing adequate resources to pursue fraud identification and awareness training, how can INTOSAI best support members' efforts to share expertise and exchange information?

Options for Resolving Issues Raised by Indicators of Fraud

The principal paper acknowledges that the mandate of each SAI and its resident skills will determine the role it plays in detecting fraud and the action it takes when fraud is suspected. In their responses, SAIs describe many different levels of involvement and approaches they use in addressing fraud indicators.

SAI action on suspected fraud generally falls into three categories, each with its own strength and weakness. One course of action calls for immediate referral of questionable activity to the appropriate legal authority. Immediate referral puts potential criminal matters squarely in the hands of those best qualified to pursue them-trained investigators. However, matters that initially appear suspicious may have reasonable explanations, and this course of action could involve legal authorities unnecessarily.

A second approach-making referrals for investigation only after fraud indicators are clearly identified and confirmed through extended audit steps - resolves the issue of involving legal authorities in matters that are not criminal. However, this approach risks losing time, revealing the potential investigation to those involved, and perhaps tainting the evidence.

In the third course of action, an SAI investigates the matter to confirm an illegal act. The advantages of this approach - timeliness and confidentiality - are achieved because the initial investigation remains within the SAI's control. However, the investigation itself can be successful only if the SAI has the authority, resources, and expertise necessary to carry out the investigation.

Many SAIs expressed the concerns cited above when describing their procedures for handling fraud indicators. Some worried that reporting mechanisms may slow referrals, afford the opportunity for document destruction, and leave fraud trails cold. As a remedy, several SAIs have or are establishing forensic audit units focused on the investigative review of fraud indicators. Others have a process to immediately involve anti-fraud units or other subject-specific investigators in their work when fraud or other wrongdoing is suspected.

Question for Discussion:

To what extent should indicators of wrongdoing be confirmed before referring the matter to legal authorities?

V INTOSAI DEVELOPMENT INITIATIVE (IDI) – A BRIEF PRESENTATION

V a. History of the IDI

In the first half of the 1980s, it was recognised that many countries needed to improve their public accounting and auditing. This was especially true of developing countries, but other countries, too, saw a need to introduce better systems of accounting and more modern auditing methods. Assistance was sought from countries that had progressed further. Both donor and recipient countries noted that there is a connection between the effects of aid to developing countries and their management and control systems: the better their financial management and the more efficient their auditing, the greater the chances are that aid will be really put to effective use and devoted to the intended purpose.

There were already frequent contacts between the SAIs of individual countries, most often after a SAI with a special need had made direct contact with a sister organisation capable of helping. Such bilateral co-operation in individual cases was not enough, however, to meet the need for assistance that had come to light. An inquiry was undertaken under UN auspices into the possibility of establishing an international centre for public accounting and auditing, but this proved impracticable. The interest was there, but financing proved impossible to arrange.

In 1984, it was proposed to the Governing Board of INTOSAI that the organisation's secretariat should undertake to organise such a centre. The proposal was rejected because the INTOSAI secretariat was not big enough to deal with such an assignment. In 1985, Canada's Auditor General proposed to the Governing Board of INTOSAI that a special body be established, to be known as the "INTOSAI Development Initiative (IDI)", to realise the intentions of the original UN proposal. The new proposal also entailed that the IDI would operate within INTOSAI's organisational structure, be funded mainly by contributions from national and international development aid agencies, and co-operate actively with the SAIs of contributing countries. The SAIs of Canada and the United States would jointly head a commission which would spend a year developing the IDI concept and preparing the ground for its realisation. The proposal was adopted by the Governing Board, and the two SAIs began preparations in co-operation with other SAIs and potential donors.

The IDI was established by resolution of the INTOSAI Congress in 1986, and the Canadian SAI undertook to host it. It was organised in accordance with Canadian corporation law, and had a board, a manager, its own secretariat and its own advisory committee. The IDI secretariat was located in the Canadian SAI, with which it has had close co-operative relations from the start. The secretariat has remained in Canada since 1986.

V b. Activities, previous courses/seminars and current long-term programme of the IDI

Since its establishment the IDI has been responsible for the arrangement of a number of professional seminars and courses, chiefly in the field of public auditing. Having surveyed training needs in co-operation with its users, principally the SAIs of developing countries, the IDI has planned and carried out courses designed to meet the most urgent needs. The IDI works through and within each of INTOSAI's Regional Groups in preference to directing its efforts at particular countries. Until 1995, the courses held were generally single courses in auditing subjects for auditors and managers from the regions in question.

By means of a special information program, the IDI disseminates information on auditing methods, course programs, and training models to all the SAIs in INTOSAI. The main element of the program is a comprehensive information catalogue. It contains descriptions of some 120 courses, about 40 case studies tailored to fit the courses, and likely procedures for surveying training needs and evaluating measures that have been implemented. On the basis of the information in the catalogue, any SAI that wishes to hold a course or the like may contact the SAI which developed the plans directly and be sent the materials. The IDI also publishes seminar reports and specialised articles.

Following an extensive evaluation in 1991-92 of activities in the first five years, a decision was taken to aim efforts in a different direction. Through a special regional training program for the 1996-2000 period, LTRTP ("long-term regional training program"), the aim is to enable INTOSAI's regions themselves to assume responsibility for their own training. The IDI strategy is to help the regions and individual SAIs to boost their own training capacity and extend their training and information activities. Co-operation between the IDI and the regions largely takes place through the regional training committees.

LTRTP consists of four main elements, in a particular order: workshops respectively on strategic planning for Heads of SAIs, on course design and development, on instruction methods and -techniques, and finally regional audit training workshops. The programs for these final workshops are developed and the instructors trained in earlier stages of the program. When the program has been completed in all the regions in question, the role of the IDI in arranging training will presumably diminish, giving way instead to co-ordination, support and advice to the regions in their development and training work and assistance in obtaining funds internationally. How realistic this assumption is will depend, however, on the ability of the regions and the individual SAIs to assume responsibility for training themselves. Implementation of the program so far has shown that regions vary somewhat in their progress, with delays in some of them.

V c. Transfer of the IDI Secretariat from Canada to Norway

In reply to an inquiry from the Governing Board of INTOSAI (International Organisation of Supreme Audit Institutions), the Office of the Auditor General of Norway (OAG) has declared itself willing to take over the role of host to the INTOSAI Development Initiative (IDI) with effect from 2001.

In its assessment of the work of the IDI, the OAG considered that in public auditing the problems confronting auditing bodies are often similar in nature. The auditing methods applied in solving the problems often have the same theoretical basis and include numerous comparable features. Many useful inputs can accordingly be obtained from international co-operation.

In its audits of Norwegian assistance to developing countries, the OAG has found that the SAIs of recipient countries in many cases had not been put in a position enabling them to carry out sufficient audits. Training, strengthening and improving the efficiency of SAIs in developing countries could clearly be important means of ensuring that grants really was put to its intended uses. This is thought also to be helpful to donors. There are many areas in which the OAG with its experience can contribute to the advancement of other SAIs. For this reason, the OAG has also in certain cases entered into bilateral development cooperation with the SAIs of other countries.

The OAG regards the IDI as an important instrument for the development of more professional and efficient SAIs in developing countries. Through the IDI's definition of needs and targeted investment in training efforts in INTOSAI's regions, valuable work has for several years been done on a world-wide scale aimed at developing better public financial control and auditing. The results achieved in the form of enhanced competence in many SAIs should be kept up and improved still further. The OAG considers the continuation of the IDI's activities to be important to user countries and in accordance with the objectives of Norwegian development aid policy.

Norway has made regular financial contributions to the IDI both through the OAG budget and through agreements between the Norwegian Agency for Development Cooperation (NORAD) and the IDI. The OAG has also contributed course plans and auditing guides to the IDI's information program, and instructors from the OAG have assisted with the implementation of a number of the IDI's professional courses. As a supporter and contributor, the OAG has had a permanent seat in the IDI's Advisory Committee.