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The Institute of
Internal Auditors
Australia

Whitepaper

Corruption Indicators in Internal Audit

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Level 5, 580 George Street, Sydney NSW 2000 | PO Box A2311, Sydney South NSW 1235

T +61 2 9267 9155 **F** +61 2 9264 9240 **E** enquiry@iia.org.au **www.iia.org.au**

Corruption Indicators in Internal Auditors

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Background

Purpose

Corruption is often a significant risk to organisations in the public and private sectors and non-government organisations (NGOs). It is a threat not just to revenue, assets and resources, but may be a substantial threat to brand or reputation and additionally result in significant penalties and political consequences.

Background

The negative consequences of corruption have been well documented. For example: “Corruption is an insidious plague that has a wide range of corrosive effects on societies. It undermines democracy and the rule of law, leads to violations of human rights, distorts markets, erodes the quality of life and allows organized crime, terrorism and other threats to human security to flourish.”⁽¹⁾

The perception of corruption is significant in Australia, for example more than a third of respondents said they were discouraged from seeking a government contract because of corruption.⁽²⁾

Internal auditors may be involved in many activities where corruption is an issue, including detecting corruption, evaluating systems where corruption a threat, recommending enhancements in internal controls to protect against corruption and investigating instances of suspected corruption. In all of these activities it is useful to be aware of indicators of corrupt activity.

Most definitions of corruption focus on the abuse of office for personal gain. This paper uses this definition. However it is not used purely for public sector agency or activities as many private sector organisations and NGOs are subject to similar corruption. Examples of corruption include misuse of position in the issue of loans or debt forgiveness in banks, the payment of claims in insurance companies, the level of discounts in retail companies, procurement decisions in all entities and granting of licences or permits by all levels of government.

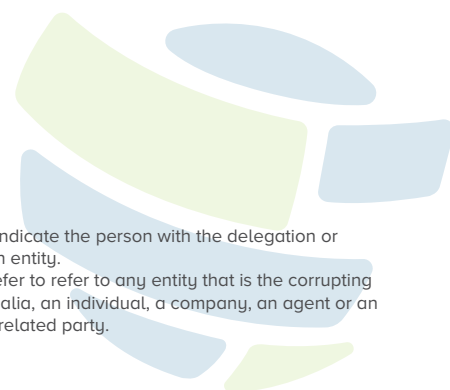
There are many kinds of corruption. This paper focuses only on indicators of corruption involving the official¹ granting something to the entity² concerned. This could include a contract, an approval, the disposal of valuable resources or assets, a purchase, or the exercise of a discretion to favour the entity.

Corruption is inherently difficult to detect because it is invariably intentionally hidden. It is, unfortunately, often not detected by internal control processes or audits.

This paper is presented to better enable those working with internal controls, probity activities and auditing to detect instances of corruption involving officials improperly granting something to an entity.

¹ We use the term official to indicate the person with the delegation or authority to grant benefit to an entity.

² The term entity is used to refer to any entity that is the corrupting party and could include, inter alia, an individual, a company, an agent or an employee of an entity or any related party.



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Discussion

Issue

When designing, assessing or monitoring internal controls, undertaking probity activities, or conducting internal audits of areas that are prone to corruption it is considered appropriate to take cognisance of the indicators of corruption.

History

Using indicator is useful for compliance with IIA Standards, especially 2010 and 2300. Indicators have long been used in audits and internal control management. Fraud indicators have proven especially useful in many environments. There has typically been relative paucity in the use of corruption indicators. It is hoped that this white paper will help to advance the field.

Discussion

When developing corruption indicators it is helpful to consider the evidence that is left behind by a corrupt act. You may think of indicators as the indentation in mud that is left by feet bearing a person's weight. Leaving a trail is not intentional, but is often unavoidable. This paper has identified the indicators by considering various examples of reported corruption as well as hypothetical instances based on corruption risk assessments.

Some of the indicators exist because of the way in which the official or the entity treated the documentation. These include poor quality of documentation and signs that the official produced, destroyed, altered, ignored or received documentation. Other indicators are related to the transaction, the entity and the official.

Poor quality of application documentation

This set of indicators reflects that the entity applying for the licence, contract, position or decision, knows that the outcome of their application is that a favourable decision for them will be made. They do not have to be convincing in their application or the information that they provide. It is usually human psychology that entropy sets in and people will not put in more effort than is required. The indicators may be thought of as those showing the avoidance of unnecessary effort, or simply stated, signs of laziness. The indicators include:

- › Inadequate documentation in the application, including schedules and other supporting documentation being missing, less documentation for this application than is the norm and parts of the form not being filled in and information that would normally be considered as important has not been provided
- › Parts of the form appear to have been copied from other applications, especially prior ones or publicly available ones
- › The quality of the documentation or information is very poor, contains obvious errors or otherwise shows a lack of serious effort by the entity
- › The size of the electronic file containing the application or information is considerably smaller than comparable applications.

Indicators that the official produced documentation

This set of indicators reflects the fact that the official knows that he or she will make the decision to approve the matter. There have been many cases where the official completes the documentation or helps the entity complete it. This is sometimes done as part of the service and sometimes because the official wants to ensure that the documentation is good enough to ensure that decision based on it will not be questioned. The indicators are the evidence of the assistance provided by the official in the documentation and include that parts of the form/information are:

- › filled in after the date that it was received by your organisation
- › written in the official's handwriting
- › in different fonts, language spell checks or sizes
- › in different grammatical styles, vocabularies, etc.
- › completed using official jargon and word-usage that is unlikely to be used by people outside of your organisation
- › in the same style as the employee normally uses, e.g. paragraphing, spelling, sentence structure, telegraphing, font style, font size, effects, etc.
- › are not signed by the entity or the signature appears to have been copied or added later.

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Indicators that the official ignored documentation

There have been many instances of corruption where the official has given the approval without requiring there to be an adequate application or information provided to support the granting of the approval. Indicators of this include:

- › there is no application or the information provided is vastly inadequate
- › significant amounts of the information provided do not appear to be relevant
- › the application or information were received by the official after the approval was granted
- › there is no evidence that the approval or information were scrutinised when there is normally evidence of scrutiny
- › the electronic files containing the application or information were not opened by the official or opened after the approval was granted.

Indicators that the official destroyed documentation

When an official makes a decision that is not justified by the application or information provided the official may destroy the application or information provided. Indicators of this are:

- › the logs show that the electronic file was deleted, especially where the logs show that the official deleted the file
- › the official instructed another employee to delete the file
- › different versions of the application or information provided show that significant parts of the application or information have been deleted
- › the deleted documents are sitting in the electronic waste bin.

Indicators that the official altered documentation

There have been many instances of officials changing applications or information received to justify the approval. This has been done, for example, in many instances of procurement where the quote, bid or proposal cost, delivery dates, deliverables or other key terms or conditions have been altered to make the entity appear as

the most desirable of the competitors. Indicators of altered documentation include:

- › changes to the application or information after the date it was received by your organisation
- › changes to the application or information made from the official's computer
- › supplementary documents deleted and replaced so that the dates of supplementary documents are later than the date the application or information was received by your organisation
- › inconsistencies in information provided, for example a cost in the official form being lower than the total of the individual costs in supplementary schedules
- › differences in fonts, size, spell check language or other evidence that parts of a document were pasted in from another document.

Indicators concerning the receipt of documentation

The way that documentation is received by the official may be indicative of corruption. The reasons for this include that the documentation is not received through the normal process because the official wants to save time and effort for the entity, because the official wants to give the approval before the documentation would get to him or her in the normal course, because it is considered inconvenient for the entity or the official to produce the documentation and so on. Indicators concerning the receipt of documentation include:

- › where the documentation is normally emailed to your organisation, the documentation was not received attached to an email or the email address was not the normal email address for these matters or was a personal address or the official's address
- › where the documentation from all applicants is normally placed in a folder together on receipt and the documentation from the entity was not in the folder
- › it appears that the official was the one who sent the documentation to its proper point of receipt or it was sent there from within your organisation
- › there is no evidence of logging of receipt of the application or other forms when this is part of the receipts procedures.

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The transaction

The indicators here are that the transaction stands out as suspicious:

- › Checks which are normally performed, have not been undertaken
- › The transaction is an override or was entered in the IT system before or after work hours or when other people are absent
- › Tenuous or spurious reasons are given to support the official's actions,
- › recommendations or decisions in relation to the matter
- › There is a lack of supervision, guidelines, scrutiny or transparency of the transaction
- › Changing the location, form, volume, total of the transaction, decision or matter so that it will fall within the employee's discretion or jurisdiction
- › The results of this matter are clearly unsatisfactory, e.g. cost overruns, permission for illegal or improper activity, potential legal liability, etc. or the official has taken steps to hide the unsatisfactory results or blame them on others.

The entity

There may be indicators that the entity should be regarded with suspicion because of this matter or previous matters:

- › The entity has offered bribes to people in your organisation or other organisations
- › The entity, key people in the entity, people from the entity dealing with your organisation or agents associated with the entity have a history or reputation for corruption or illegal practices
- › The industry, geographical area, suppliers to the industry or customers of it have a history or reputation for corruption or illegal practices
- › The entity only ever wants to deal with the official
- › The entity has a history of inability in, or indifference to, this area of endeavour.

The official

- › The official appears to have an unacceptably close relationship with the entity, key personnel of the

entity, agents associated with the entity

- › The official or people close to the official have accepted or are rumoured to have accepted large gifts, benefits or hospitality or engaged in corruption
- › The official appears to be living beyond his or her means, is a gambler, has an addiction or appears to have a significant need for funds
- › The official appears to have an attitude to ethics, the organisation, the industry or those associated with the industry that would indicate a willingness to engage in corruption
- › The employee made contact or held meetings with the entity or third parties, etc. outside of normal work hours, where this is unusual
- › The approval or decision is outside of the jurisdiction of the official or would not normally be handled by him or her
- › The official was not with another team member when making contacts with third parties, giving advice, decision making, etc. when this is normally done accompanied
- › The official has been unusually secretive about this matter
- › Some third parties, especially those who have never transacted with your organisation before indicate a preference for dealing with the employee
- › Other organisations with a reputation for integrity prefer not to deal with the official
- › People who should normally be involved in the decision or process have been kept totally or partially out of the process by the official
- › The official appears to have removed evidence of prior refusals about this matter
- › The official's notes of checks, inspections, meetings and other events are less detailed than normal
- › The official has backdated or added information or supposed events
- › Checks, inspections, meetings and so on which should have happened are not evidenced

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- › The official has not reported corrupt approaches when other officials have
- › The official appears to have had an urgent financial need met
- › Employees with a reputation for honesty are reluctant to work with the official
- › The official took less time over this matter than is the norm
- › The official has instructed others to refer all enquiries about this matter to him or her
- › The official has provided inaccurate or incomplete information about the transactions to others

Conclusion

Summary

Incorporating indicators of corruption into internal controls and audits helps ensure that the organisation's resources, reputation and integrity are protected, key stakeholders are satisfied and strategic and operational objectives achieved.

The indicators should be relevant to the particular organisation and may include indicators related to the transaction, the entity, the officials and the way in which officials or the entity treated the documentation.

Conclusion

When designing, assessing or monitoring systems of internal control to limit the risks of corruption it is considered that significant value can be derived from incorporating the indicators of corruption into the systems of control.

When conducting internal audits and investigations, taking cognisance of the indicators of corruption can substantially reduce the audit risk and increase the likelihood of detecting corruption that could be significant for the organisation, its operations or strategies.

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1. United Nations Convention Against Corruption, New York, United Nations, 2004, p.iii
2. Perceptions of Corruption, Melbourne, Independent Broad-based Anti- corruption Commission, 2016

Purpose of White Papers

A White Paper is a report authored and peer reviewed by experienced practitioners to provide guidance on a particular subject related to governance, risk management or control. It seeks to inform readers about an issue and present ideas and options on how it might be managed. It does not necessarily represent the position or philosophy of the Institute of Internal Auditors–Global and the Institute of Internal Auditors–Australia.

Author's Biography

Written by: Barry Davidow BCom, BAcc, MTaxLaw, ACA, CFE, CRMA, PFIIA

Barry has over 20 years of experience in internal audit, fraud and corruption control, investigations, governance and compliance. He has contributed to books on fraud control, computer fraud, communications and sociology. He is the Vice-Chairperson of the Corruption Prevention Network. HE lives in Sydney, Australia.

Matthew Lyon
BComm, CPA, MIAA

Matthew has been involved in internal audit for 10 years in the NSW Government. Prior to this he was Financial Accountant for Catholic Education Office Parramatta. He spent 15 years with the Audit Office of NSW, the last four as engagement manager. He has also served in a number of charities and the Wollongong Council Audit and Finance Committee. He lives in Sydney, Australia.

Edited by: Bruce Turner AM
CRMA, CGAP, CISA, CFE, PFIIA, FFin, FIPA, FAIM, MAICD, JP



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As the chief advocate of the Internal Audit profession, the IIA serves as the profession's international standard-setter, sole provider of globally accepted internal auditing certifications, and principal researcher and educator.

The IIA sets the bar for Internal Audit integrity and professionalism around the world with its 'International Professional Practices Framework' (IPPF), a collection of guidance that includes the 'International Standards for the Professional Practice of Internal Auditing' and the 'Code of Ethics'.

The IIA-Australia ensures its members and the profession as a whole are well-represented with decision-makers and influencers, and is extensively represented on a number of global committees and prominent working groups in Australia and internationally.

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