

White Paper

Audit Committee oversight of the Fraud and Corruption Investigations Activity

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Background

Purpose

This White Paper outlines a practical approach for Audit Committees to maintain effective oversight of the fraud and corruption investigations activity to minimise the risk of internal investigative process failures within their organisation, whilst ensuring confidentiality and secrecy of individual investigations is maintained.

Background

Inevitably, every investigation conducted internally by corporate investigators (including contracted service provider specialists) has inherent downside risks irrespective of whether or not allegations are substantiated.

Where allegations are substantiated, management will consider disciplinary action commensurate with the seriousness of the matters, and will assess the broader impacts on other workers, operations, internal controls and culture in the same business unit.

Even where employees who are the subject of investigations

are cleared of the allegations (or the allegations are not proven), there is likely to be an adverse impact on their productivity through their disengagement, loss of morale, and de-motivation because of the stresses involved in any investigation that calls into question their integrity.

Audit Committees and management typically maintain an 'arms length' approach that enables investigators to perform their role in an independent, impartial and confidential manner. This is appropriate.

However, Audit Committees (where mandated to oversight the investigations activity) require absolute transparency on the outcomes of investigations; protections accorded to employees under investigation; capability of investigative resources; investigations standards, independence, and principles applied; and, overarching quality assurance.

This paper focuses on five elements that the Chief Audit Executive (or other reporting line executive) needs to periodically deliver to the Audit Committee:

1. High-level reporting on the outcomes of investigations.
2. The availability and application of a 'charter of rights' for persons being investigated.
3. Profile of the capability, qualifications and experience of investigators.
4. Assurance on the reasonableness of documented investigation protocols.
5. Establishing and maintaining effective quality assurance arrangements.

This approach can be applied to any organisation that handles more than a handful of investigations of wrongdoing each year. In this context, 'investigations' primarily include internal fraud and corruption, though the approach can equally apply to other behavioural wrongdoing, mismanagement, waste, and abuse.

Corporate investigators often work directly for (or with) the internal audit activity. If they have a direct reporting line within the internal audit activity, the Chief Audit Executive can implement the approach articulated in this paper. Where corporate investigators work to others in the organisation, the Chief Audit Executive can influence the adoption of these better practices in consultation with the Audit Committee or investigation management.

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Discussion

Issue

Audit Committees will have greater confidence in the integrity of investigation processes and outcomes when they have adopted the five focus elements covered in this paper.

Often, allegations will not be substantiated, or if they are substantiated they will be at the lower end of the scale of seriousness. In these situations senior management will consider and apply appropriate sanctions if necessary.

Where serious allegations and / or complex wide-reaching issues are involved, Audit Committees might be called upon to provide advice to Chief Executives or Boards, and this will usually require them to review an investigation report for a specific matter. The investigation reports might involve or implicate senior executives or their decision-making. The credibility of the investigation report is imperative.

History

There have been instances where Audit Committees have been unintentionally misled by investigation reports that have (or could have) compromised the committee's objective analysis. Examples include:

- On considering a 'final investigation report' it became apparent that there remained 'loose ends' that were never clearly identified in the report.
- There were errors of fact in the report, and incomplete and un-validated data. For example, total amounts quoted in the report were not backed up by schedules of individual amounts contained in the investigator's work-papers; it then took eight weeks to substantiate the total amounts (which ultimately highlighted flaws in the investigator's analysis).
- Interpretations of legislative requirements were not supported by expert advice (and this was not disclosed).
- The outcome (or conclusion) was inconsistent with the facts reported.
- Procedural fairness was not demonstrated, and a reasonable due process was not followed. For instance, interviews were conducted without proper notice, interviews were recorded without actual confirmed consent and positive agreement, and a relatively junior staff member interviewed senior executives.

Section 5-2 of Australian Standard: Fraud and Corruption Control (AS8001–2008) provides guidance on response when a fraud event occurs and requires¹:

- Qualified investigation resources (qualification is determined by both formal qualifications and experience).
- Independence from the business unit involved.
- Principles-based investigation process dealing with inter alia transparency of process, independence and objectivity, compliance with all legislation, and adequacy of records.

A prudential inquiry in 2018 reflected on changes in the governance landscape and the importance of mature practicesⁱⁱ. These reflections are equally appropriate for an investigation activity. They include: aligning processes and practices of Audit Committees to global better practice; reporting of non-financial risk information including early indicators of emerging risks; addressing root causes in a timely and effective manner; maintaining specialist capability development; identifying systemic issues.

Discussion

This section provides commentary on the five elements that an Audit Committee should periodically expect in respect to the investigation activity, in line with global better practice. Exhibit 1 on the following page summarises how the elements add value for the Audit Committee.

Element 1 – High-level reporting on the outcomes of investigations

This element looks at broader high-level reporting needs and expectations, recognising that corporate investigators are usually solid at undertaking their investigations and delivering a report specific to the allegations investigated.

As the governance landscape continues to evolve (as experienced by other governance, risk and audit specialists), investigators have an opportunity to shape a profile as 'trusted advisors' by implementing contemporary practices that expand the investigative mindset into strategic, leadership, human resource, and damage control considerations that senior executives need to address when they receive investigation reports.

As an example, 'root cause analysis' would enable investigators to inform management of what they really need

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Exhibit 1 – How the Five Elements Add Value to the Audit Committee

Element	Relevance for Audit Committee	Interest to Audit Committee		
		Availability	Insights	Assurance
High-level reporting on the outcomes of investigations.	Understanding themes, root causes, and systemic issues.		✓	
Availability and application of a 'charter of rights' for persons being investigated.	Confidence in fairness and equity principles applied for persons investigated.	✓		
Profile of the capability, qualifications and experience of investigators.	Confidence in the credibility of investigation outcomes.			✓
Reasonable documented investigation protocols.	Confidence in an established principles-based process.	✓		
Establishing and maintaining effective quality assurance arrangements.	Ongoing assurance on the credibility of overarching investigation processes.			✓

to address beyond the specific allegations that have been investigated. These insights can enhance the reporting on specific allegations, and on the control framework as a whole.

This element deals with the high-level reporting on the outcomes of investigations which is achieved through consolidated information rather than specific personal details related to an individual matter. In all cases, the confidentiality of individual investigations (including names) must be preserved on a strict 'need to know' basis.

Open Investigations

Where more than a handful of investigations is completed each year, Audit Committees require consolidated quarterly reporting on open investigations, including:

- Running tally (number of investigations brought forward from last period, new investigations, closed investigations, matters referred elsewhere (eg law enforcement agency), new total carried forward to next quarter).
- Number of investigations (or allegations) currently open per category (eg (i) corruption – conflicts of interest; bribery; illegal gratuities; economic extortion; (ii) asset misappropriation – cash; inventory; other assets; (iii) financial statement fraud – net worth / net income overstatements; net worth / net income understatements)ⁱⁱⁱ.
- Source of investigations (which can be through internal channels including 'whistleblowers', or external channels including corruption / law enforcement agencies).

- An ageing of investigations to indicate whether investigations are completed in a timely manner.
- Information on the number of employees who have been stood down (on pay or without pay) or reassigned while investigations are being completed, with assurance that the status of these employees is being actively managed and the Chief Executive (or equivalent) is being kept informed.

Completed Investigations

Audit Committees require consolidated quarterly reporting on completed investigations, including:

- Number of completed investigations (or allegations) per category and whether they were substantiated, not substantiated, or other result.
- The sanctions applied (where allegations have been substantiated) so the Audit Committee has visibility, to assess consistency of decision-making.
- Root cause/s for each substantiated allegation.
- Themes, systemic issues, or early indicators of emerging risks and how they will be handled, including strategic, leadership, human resource, and damage control considerations.
- Lessons learned that can be incorporated into corruption prevention (or similar), risk management, and compliance activities, including training, ongoing reinforcement / education, and internal communications.

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Element 2 - Availability and application of a 'charter of rights' for persons being investigated

Audit Committees should determine whether a 'Charter of Rights' is available for people who are the subject of investigations, given that the substantiation rate of allegations globally is around 40% (which is consistent with investigation outcomes for many organisations in Australia).

A Charter of Rights compiles in a single document all the information that respondents to allegations of wrongdoing may require. It should be written in an easy to understand style to meet the needs of its target audience. The Charter of Rights is made available to persons being investigated as soon as they are notified of the allegations; it should also be available on the organisation's intranet site.

The benefits of a Charter of Rights include:

- Minimises the risk of lost productivity through disengagement, loss of morale, and de-motivation when there is no basis to allegations.
- Minimises the long-term detrimental impacts on employees (and ultimately the organisation) where the process for handling allegations of fraud or wrongdoing is not consistent, in a well-defined, fair, equitable and effective manner.
- Clearly demonstrates to external parties (eg Human Rights Commission, Industrial Relations Commission, courts etc) that there was a well-defined process that was fair, equitable and effective in the event that allegations are substantiated (when a Charter of Rights is available and followed).

Audit Committees need to consider the risk impacts on the 6 out of 10 employees where investigations are not substantiated or there is no basis; one step is to confirm the availability and application of a Charter of Rights.

Note: A separate White Paper outlines the process for developing and implementing a Charter of Rights^{iv}.

Element 3 - Profile of the capability, qualifications and experience of investigators

While the Board, Audit Committee and Chief Executive rely on the expertise of investigators in the completion of investigations and in preserving an appropriate 'tone at the

top', these leaders rarely have a good understanding of the individual and collective backgrounds of investigation staff (ie business experience, qualifications, certifications, years of investigative experience (including level of complexity), and continuing professional development).

An approach used with leading practice organisations is to provide a report to the Audit Committee each year on the profile of specialist governance, risk and audit professionals. That approach can (and should) be explicitly established for investigation staff with the profile of investigators reported to the Audit Committee as least annually.

Element 4 - Assurance on the reasonableness of documented investigation protocols

Because investigations need to be undertaken confidentially, investigators typically complete their work with much less direct oversight and scrutiny than other governance, risk, compliance and audit roles.

The conduct of fraud and corruption investigations typically involves eight stages as summarised below^v.



Audit Committees need to understand all elements of investigation activities, which should be documented in an approved and up-to-date investigation manual including appropriate information on:

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- Mandate of investigators and their rights to undertake investigations.
- Legislative requirements and compliance obligations.
- Standards, principles, protocols, methodology and techniques applied.
- Rules of evidence and documentation requirements, including secure storage and preservation of evidence.
- Process for determining action for allegations.
- Management of conflicts of interest and impartiality.
- Planning, approval and escalation points.
- Conduct (including proper protocols for recording interviews and timeframe KPIs).
- Referrals to law enforcement and other outside agencies (eg police, corruption watchdog).
- Reaching conclusions and recommendations.
- Delivering internal reporting.
- Process for taking action against substantiated allegations.

Whilst Audit Committees will not need to have a detailed knowledge of the investigation manual, they should seek assurance that it is and remains 'fit-for-purpose'.

Element 5 - Establishing and maintaining effective quality assurance arrangements

A study conducted in 2017 established that 94% of stakeholders believe there is value for internal auditors to conform to recognised standards^{vi}. A similar response could be reasonably expected for corporate investigators.

Effective quality control processes will ensure (amongst others) that:

- Investigations are not reported until the work is completed and reviewed by someone independent for reasonableness.
- Any qualifications on the scope, objectives and approach for an investigation are clear and unambiguous.
- Recommendations are clear, understandable and practical.

- Emotion and personal bias are eliminated.
- Boards and Audit Committees are never delivered reports that are incomplete and unclear.

Corporate investigators are encouraged to adopt a quality assurance and improvement approach that is consistent with the approach applied by internal auditors (in line with standard 1300 of the International Professional Practices Framework). This includes the typical elements illustrated in exhibit 2.

Exhibit 2 – Key Features of a Quality Assurance and Improvement Program



Internal quality reviews cover every stage of an investigation – from initial receipt and response, to planning, through evidence collection and assessment, into reporting, and ultimately through to the close-out. This ensures the output of investigators is reasonable, their conclusions are defensible and have a firm basis, and recommendations are reasonable, practical, actionable, and useful. It also ensures conformance with applicable standards, protocols, methodology and techniques.

An external quality review of the investigation activity provides an opinion as to whether the activity conforms to the standards, protocols, methodology and techniques adopted by the organisation, and whether the investigation manual is 'fit-for-purpose'. (The external quality review could, perhaps, be completed at the same time as the mandatory external quality review of the internal audit activity, required at least once every five years). The assessment can potentially help to identify improvements to the investigation methodology, policies and practices, and provide an opinion on skills, knowledge and experience within the activity.

The features of professional development are encompassed within the earlier discussion on the 'profile of the capability, qualifications and experience of investigators'.

Whatever quality assurance and improvement approach is adopted for the organisation's investigation activities, the outcomes of ongoing internal quality reviews and periodic external quality assessments should be reported to the Audit Committee.

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Conclusion

Summary

The governance landscape continues to evolve, with contemporary practices being embraced by governance, risk and audit specialists. Corporate investigators also play an important role in an organisation's governance and have an opportunity to shape a profile as 'trusted advisors'.

As the roles, responsibilities and demands of Audit Committees continue to expand, corporate investigators have an opportunity to demonstrate and report to Audit Committees by applying contemporary practices, such as reporting on the outcomes of investigations; according protections to employees under investigation; demonstrating the capability of investigative resources; applying investigations standards, independence, and principles; and, maintaining overarching quality assurance practices. This can be either through being proactive, or reacting to demands placed on them by Audit Committees.

Five Action Steps

1. Introduce (or enhance) high-level reporting to the Audit Committee on the outcomes of investigations.
2. Develop a 'Charter of Rights' for persons being investigated, ensure it is made available to those who require it, and ensure corporate investigators apply its commitments in practice.
3. Periodically deliver to the Audit Committee (at least annually) a profile of the capability, qualifications and experience of investigators.
4. Maintain a consolidated Investigations Manual that clearly documents investigation standards, protocols, methodology, techniques, and quality assurance arrangements.
5. Establish and maintain effective quality assurance arrangements, and periodically report the results to the Audit Committee.

Conclusion

Whilst there is never a guarantee that internal investigative process failures will not occur, there are practical steps that Audit Committees can take to maintain effective oversight of the fraud and corruption investigations activity without

affecting the confidentiality and secrecy of individual investigations.

Bibliography and References

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- ⁱⁱ Prudential Inquiry into the Commonwealth Bank of Australia, April 2018, 102-104
- ⁱⁱⁱ Report to the Nations – 2018 Global Study on Occupational Fraud and Abuse, Occupational Fraud and Abuse Classification System (the Fraud Tree), Austin: Association of Certified Fraud Examiners Inc, 2018, 11
- ^{iv} White Paper – Introducing a 'Charter of Rights' for Employees being Investigated, Turner B., Institute of Internal Auditors–Australia, January 2020
- ^v White Paper – Conducting Fraud and Corruption Investigations, Davidow B. And Lyon M., Institute of Internal Auditors–Australia, January 2020
- ^{vi} IIA–Global Council 2017 Summary Report, 19-22 February 2017, Rome Italy, Stakeholder Expectations, Section 3, p10

Purpose of White Papers

A White Paper is an authoritative report or guide that informs readers concisely about a complex issue and presents the issuing body's philosophy on the matter. It is meant to help readers understand an issue, solve a problem, or make a decision.

Author's Biography

Written by: Bruce Turner AM
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Bruce remains active as an audit and risk committee chair, company director, executive coach, mentor, and white ribbon ambassador. He has held board and independent audit committee roles over the last decade in 30 diverse organisations, including six years on the IIA–Australia Board to mid–2018.

His 40 years of practitioner and leadership experience in internal auditing across the globe traverses the energy, financial services (commercial, merchant and central banking), government, manufacturing, and transport sectors. Prior to his retirement in 2012, he held Chief Audit Executive roles at the State Rail Authority of NSW, Integral Energy Australia, and ultimately the Australian Taxation Office.

For much of the last 20 years Bruce has held roles involving the direct management and co-ordination of investigations,

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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'.

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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