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Internal Audit Fraud and Whistle Blowing:

PRESENTED BY

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Whistle blowing

Introduction

Most organizations worldwide are vulnerable to fraud and misconduct in the workplace.

By establishing a **proactive approach** and engaging stakeholders to promote an ethical workplace, an organization can significantly limit financial liability and loss, and protect its corporate hard image in the market place.

A successful strategic approach undertaken by many organizations is the implementation of an anonymous employee whistle blowing line.

Current whistle blowing tools

Tool	Risks	Benefits on anonymity
Suggestion boxes	Lack of anonymity	None
Telephone calls to a senior member of management	Ability to trace the caller	None
Telephone calls to audit committee members	Ability to trace the caller	None
Emails to top management and/or to audit committee members	Ability to trace the sender	None
Whistle blowing tool managed by an external organisation or third party	No trace Toll free number Anonymous email system	Yes

Whistle Blowing and Corporate Governance

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There is a strong tie between employees reporting misconduct in the workplace and a company's ethics programmes.

Whistle Blowing and Corporate Governance

Employees tend to prefer an anonymous telephone whistle blowing line because they have more confidence that they can remain anonymous. They often fear that electronic communication can be traced back to them. This fear can cause them to either not report their concern, or worse, report it to a source outside of the organization.

Internal vs. Independent Whistle Blowing Lines

Some organizations provide an internally managed whistle blowing line as an option for employees who are uncomfortable discussing issues face-to-face. Reports to the whistle blowing line are frequently routed to an employee somewhere in the organization, generally in Human Resources, Legal or the Ethics office.

An internal programme may seem attractive, but there are some serious potential drawbacks.

For instance;

- if employees realize they are calling an internal number, they may be afraid that their identity could be traced and decide not to submit the report.
- There are also operational issues, such as the potential for inconsistent handling of sensitive information and callers encountering voicemail.
- An internal whistle blowing line also leaves the organization vulnerable to charges of covering up issues involving management.

Internal vs. Independent Whistle Blowing Lines

In comparison, an independent external process provides greater safeguards of anonymity and avoids even the appearance of impropriety. An external facility is also more attractive to use from home or another location outside the office, as there is less fear of detection. It is also important to evaluate what happens on the back end of the whistle blowing line.

While there are costs associated with an external whistle blowing line, the financial investment is small compared to the potentially disastrous financial repercussions associated with malfeasance that could go undiscovered.

With the expertise, trained personnel, resources and technology already established to operate a whistle blowing line and conduct quality assurance, a professional whistle blowing line provider can usually provide these services for much less than it costs to implement them internally.

Whistle Blowing Must be Supported by Corporate Culture

Communicating the purpose of the whistle blowing line should ideally help create and maintain an ethical culture in the workplace. A communications team that includes top management should be involved in developing an ongoing ethics communication campaign.

An ethics communication campaign is essentially an internal marketing campaign that seeks to inspire certain behaviour within an audience, from the top down.As with any such campaign, the first step is to determine desired behaviours and the key messages that will help motivate these behaviours.

What can be reported ?

1. Any wrong doing - Theft, Fraud and Criminal activities
2. Not obeying company policies or procedures
3. Abuse of Company Property and Equipment
4. Theft of Time
5. Bribery and/or corruption
6. Collusion with external and internal parties
7. Highly Sensitive issues e.g. Sexual harassment, nepotism, racism

Means of communication

- **Telephone**
- **Email**
- **Fax**
- **Post**
- **Website (generic or customised website)**

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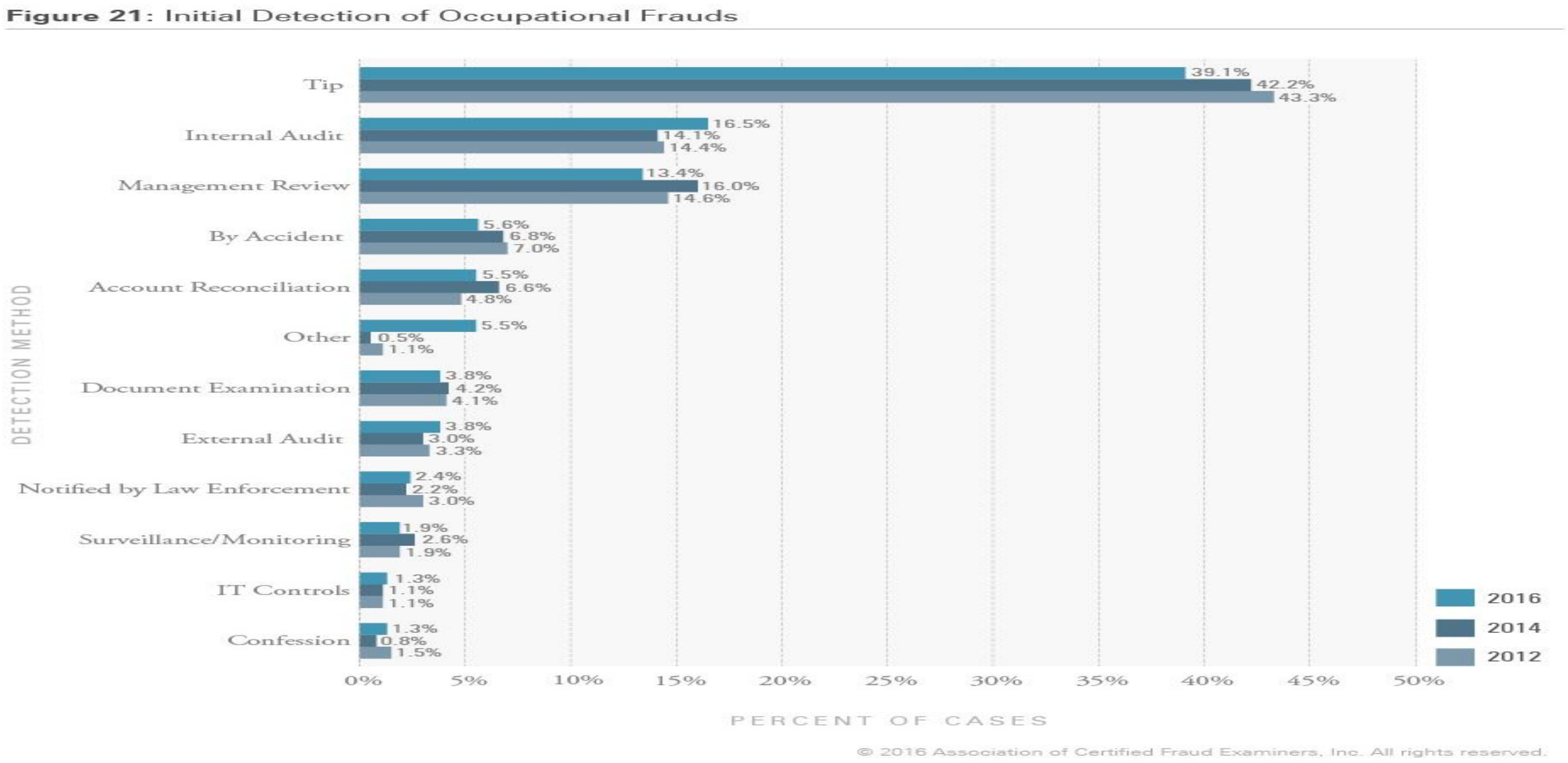
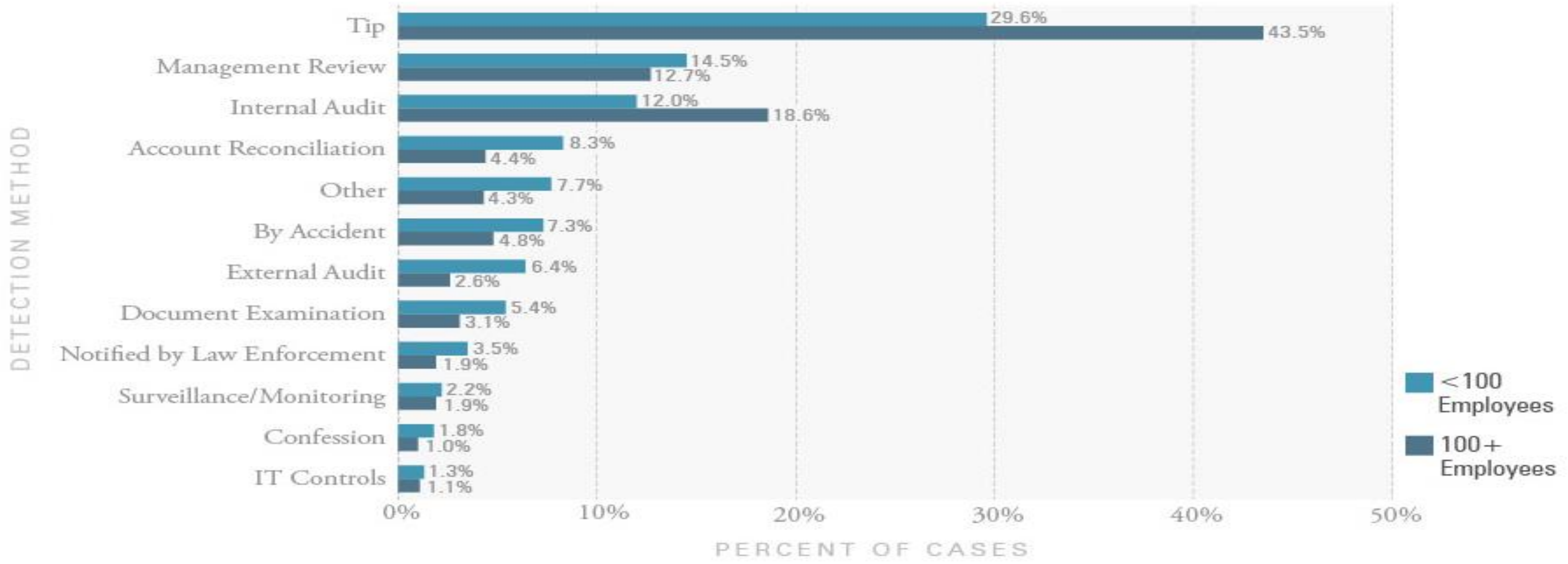
Initial Detection of Occupational Frauds (source: ACFE)



Initial Detection of Frauds in Small Organizations (source: ACFE)

Figure 22: Detection Method by Size of Victim Organization



Detection Method by Region (source: ACFE)

Figure 24: Detection Method by Region—Sub-Saharan Africa

Detection Method	Percent of Cases
Tip	37.3%
Internal Audit	16.2%
Management Review	10.2%
Account Reconciliation	7.4%
By Accident	5.3%
Other	4.9%
Document Examination	4.9%
External Audit	4.9%
IT Controls	3.2%
Notified by Law Enforcement	2.1%
Surveillance/Monitoring	2.1%
Confession	1.4%

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Fraud

Definitions

Fraud

Fraud is generally defined in the law as an intentional misrepresentation of a material existing fact made by one person to another with knowledge of its falsity and for the purpose of inducing the other person to act, and upon which the other person relies with resulting injury or damage.

Fraud may also be made by an omission or purposeful failure to state material facts, which nondisclosure makes other statements misleading.

Procurement

Procurement refers to those processes, procedures and entities involved in the purchase of goods and services by public and private entities.

http://mobile.nation.co.ke/news/Why-CJ-is-yet-to-occupy-Sh300m-house/-/1950946/2294676/-/format/xhtml/-/6gt8ts/-/index.html

http://www.politics.co.ke/news/see-the-nyamira-hospital-gate-that-cost-the-county-just-8m-shillings-only-to-construct/

Bungoma County Assembly leader of majority Majimbo Okumu and residents looking at the special Wheelbarrow that costs Sh109,320 at Bungoma town slaughter house. Local leaders and residents want officers involved in the procurement of the 10 Wheelbarrows. PHOTO: TITUS OTEBA/STANDARD Read more at: http://www.standardmedia.co.ke/article/2000175707/protests-rock-bungoma-over-most-expensive-wheelbarrow

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http://citizentv.co.ke/news/bungoma-residents-protest-ksh-100000-wheelbarrows-100195/

Ruto prayers in Meru: MPs sustain attack on CORD, P.10

Crazy Monday THE PERFECT WAY TO START THE WEEK

WHEN WEDDINGS GO AWRY

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THE STANDARD

Kenya's Bold Newspaper

Monday, October 12, 2015

Laugh at how they misuse your cash but it does hurt

State officials devise hilarious but devious ways of spending public money, raising suspicion of graft

The Presidency
Sh1.4 billion spent on hospitality alone

National government
Sh4.2 billion on hospitality alone

Kisumu
County Assembly spent Sh60 million in two years to fund MCAs' trips

National government
Fisheries department spent Sh1.1 billion to buy boats

Foreign Affairs
Spent Sh181 million on donations and Sh79 million to ship household goods

National government
No documents given to support Sh67 billion spent

Interior ministry
Sh275 million spent on firewood and gas and Sh70 million on legal fees

Bungoma County
Sh1 million spent on just ten wheelbarrows

STORIES ON PAGES 4, 6 & 7

Smoking costs 'Dereva Chunga Maisha' hit singer a foot

By PETER MUIRURI

More than two-and-a-half decades ago, his authoritative voice ruled the airwaves. His hit single was inescapable in majority of Kenyan households that had radio sets. It was the voice of reason, which scolded and cajoled drivers on the road to be vigilant.

Appropriately titled "Dereva Chunga Maisha" (Driver save life), Sam Muthee's most popular hit became like the national anthem for road safety campaigners.

Twenty-seven years later, fate has played a cruel joke on Mr Muthee and he regrets not heeding his own counsel. Muthee, who composed the song back in 1988 after watching what he terms as

CONTINUED ON PAGE 3

Sam Gatheru Muthee

KQ now suspends undisclosed number of staff in fraud probe

May. 25, 2016, 5:00 am

By JOAN WAIRIMU

OneSource

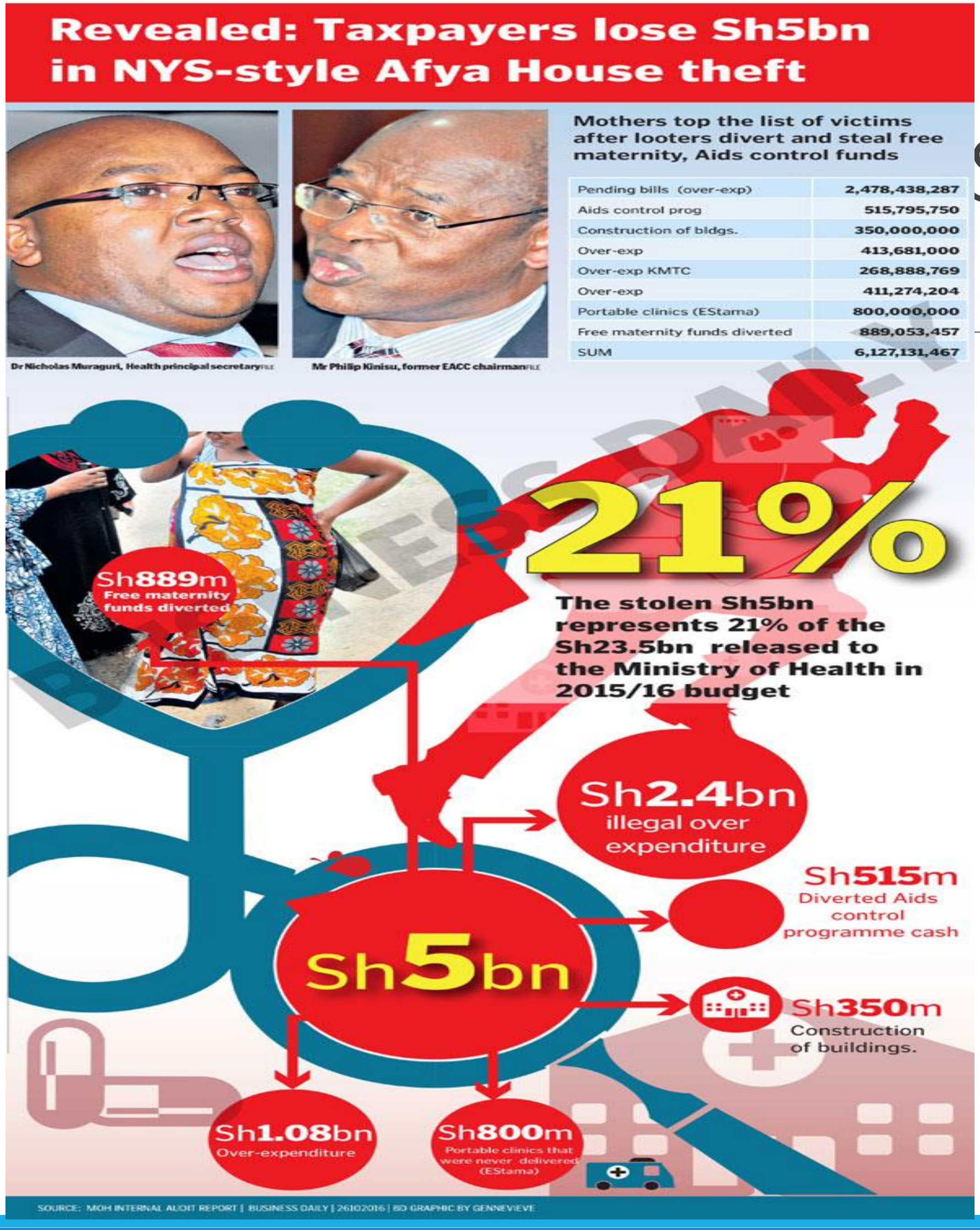
Former Kenya Airways finance director Alex Mbugua with managing director Mbuvi Ngunze during the investor briefing In Nairobi on July 30, 2015. /ENOS TECHE

11 NYS scandal suspects charged with money laundering

Aug. 22, 2016, 9:00 am

By CAROLE MAINA and ZIPPORAH WERU @thestarkenya

A file photo of Nairobi businesswoman Josephine Kabura



Pending bills (over-exp)	2,478,438,287
Aids control prog	515,795,750
Construction of bldgs.	350,000,000
Over-exp	413,681,000
Over-exp KMTC	268,888,769
Over-exp	411,274,204
Portable clinics (EStama)	800,000,000
Free maternity funds diverted	889,053,457
SUM	6,127,131,467

Revealed: Taxpayers lose Sh5bn in NYS-style Afya House theft

PHOTO | BD GRAPHIC

By STELLAR MURUMBA, smurumba@ke.nationmedia.com

Posted Wednesday, October 26 2016 at 09:56

IN SUMMARY

•A leaked internal audit report says the theft, which is five times the infamous Sh791 million NYS scandal, also involved payments of millions of shillings to phony suppliers in the financial year (2015/2016).

•Top on the list of fraudulent transactions identified in the audit report was the diversion of Sh889 million meant to be disbursed to county governments to support the free maternity care programme.

•The Principal Secretary in the Ministry of Health, Nicholas Muraguri, did not deny the existence of the audit report, but dismissed the author as “incapable of understanding how government works.”

Youth Fund CEO is suspended as probe launched over cash

SUNDAY OCTOBER 25 2015

email print

Youth Enterprise Development Fund Chief Executive Officer Catherine Namuye. Ms Namuye has been suspended, the Sunday Nation has established. FILE PHOTO | PHOEBE OKALL | NATION MEDIA GROUP

In Summary

- *Daily Nation* established that the Fund's documents had been forged and used to transfer between Sh180 and Sh200 million to an account of a top official of the organisation.
- Banking Fraud Unit also flagged Sh65,718,946 on April 27, 2015, which was wired to the same bank account belonging to Quondum Ltd.
- However, she was not among the officials who stepped down as had been directed by the President.

Toshiba

Toshiba announces a massive writedown and its chairman resigns.

(Reuters) - After a day of delays and confusion, Japan's Toshiba Corp said on Tuesday it would book a $6.3 billion hit to its U.S. nuclear unit, a write down that wipes out its shareholder equity and leaves the loss-making group scrambling for capital.

Toshiba

"Finally, now people are starting to recognise that internal control problems, the accounting issues and governance issues are very real and no longer abstract," said Zuhair Khan, an analyst at Jefferies in Tokyo.

"They impact the viability of the company."

Shares in the group slid 8 percent, putting the company's market value at 973 billion yen ($8.6 billion), less than half its value in mid-December. Just under a decade ago, the firm was worth almost 5 trillion yen.

Internal Audit’s Role

ISA 240

Paragraph	Details
2.	Misstatements in the financial statements can arise from either fraud or error. **The distinguishing factor between fraud and error** is whether the underlying action that results in the misstatement of the financial statements is **intentional or unintentional**.
4	The primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the entity and management. It is important that management, with the oversight of those charged with governance, place a strong emphasis on fraud prevention, which may reduce opportunities for fraud to take place, and fraud deterrence, which could persuade individuals not to commit fraud because of the likelihood of detection and punishment. This involves a commitment to creating a culture of honesty and ethical behavior which can be reinforced by an active oversight by those charged with governance. Oversight by those charged with governance includes considering the potential for override of controls or other inappropriate influence over the financial reporting process, such as efforts by management to manage earnings in order to influence the perceptions of analysts as to the entity's performance and profitability.

ISA 240

Paragraph	Details
5.	An auditor conducting an audit in accordance with ISAs is responsible for obtaining reasonable assurance that the financial statements taken as a whole are free from material misstatement, whether caused by fraud or error. Owing to the inherent limitations of an audit, there is an unavoidable risk that some material misstatements of the financial statements may not be detected, even though the audit is properly planned and performed in accordance with the ISAs.
10.	The objectives of the auditor are: (a) To identify and assess the risks of material misstatement of the financial statements due to fraud; (b) To obtain sufficient appropriate audit evidence regarding the assessed risks of material misstatement due to fraud, through designing and implementing appropriate responses; and (c) To respond appropriately to fraud or suspected fraud identified during the audit.

1200 – Proficiency and Due Professional Care

1210.A2 – Internal auditors must have sufficient knowledge to evaluate the risk of fraud and the manner in which it is managed by the organization, but are not expected to have the expertise of a person whose primary responsibility is detecting and investigating fraud.

1210.A3 – Internal auditors must have sufficient knowledge of key information technology risks and controls and available technology-based audit techniques to perform their assigned work. However, not all internal auditors are expected to have the expertise of an internal auditor whose primary responsibility is information technology auditing.

1210.C1 – The chief audit executive must decline the consulting engagement or obtain competent advice and assistance if the internal auditors lack the knowledge, skills, or other competencies needed to perform all or part of the engagement.

Internal audit professional standards

IIA Standard 2120:Risk Management

2120.A2–"The internal audit activity must evaluate the potential for the occurrence of fraud and how the organization manages fraud risk."

IIA Standard 2210:Engagement Objectives

2210.A2–"Internal auditors must consider the probability of significant errors, fraud, noncompliance, and other exposures when developing the engagement objectives."

IIA Standard 1200:Proficiency and Due Professional Care

1210.A2–"Internal auditors must have sufficient knowledge to evaluate the risk of fraud and the manner in which it is managed by the organization, but are not expected to have the expertise of a person whose primary responsibility is detecting and investigating fraud".

Internal audit professional standards

IIA Standard 2060: Reporting to Senior Management and the Board

"The chief audit executive (CAE) must report periodically to senior management and the board on the internal audit activity's purpose, authority, responsibility, and performance relative to its plan. Reporting must also include significant risk exposures and control issues, including fraud risks, governance issues, and other matters needed or requested by senior management and the board.

Fraud & Internal Audit

Internal Audit (IA) supports management by determining whether the organization has adequate internal controls and promotes an adequate control environment.

Since IA is a centralized, independent, and objective function, it is in a prime position to address fraud risk management programs, and to affect change.

Different organizational structures and IA charters affect IA's role and ability to achieve that role.

Board Audit Committee And Fraud Related Risks

The Audit Committee and Fraud-Related Risk

Headlines of financial reporting scandals, sweeping corporate governance reforms, and unprecedented scrutiny by regulators and shareholders have elevated awareness of fraud to an all-time high.

These pressures, along with increased corporate sensitivity to fraud, are driving many audit committees to focus greater attention on the organization's approach to risk management as well as the audit committee's own processes and policies for addressing fraud.

Internal Audit and Fraud-Related Risk

The incentives for the audit committee to implement an effective oversight approach are compelling. They include:

- Meeting the audit committee's fiduciary responsibilities and duty of care in over-seeing the integrity of the organization's financial reporting process
- Addressing regulatory requirements, such as section 404 of the Sarbanes-Oxley Act of 2002 regarding internal control over financial reporting and Statement on Auditing Standards (SAS) No. 99, *Consideration of Fraud in a Financial Statement Audit. Also ISA 240.*
- Strengthening confidence among investors, rating agencies, and other stakeholders
- Identifying opportunities to improve performance and efficiency as a result of an effective internal control environment

Board Responsibility

“management, along with those who have responsibility for oversight of the financial reporting process (such as the audit committee, board of trustees, board of directors, or the owner in owner-managed entities), should set the **proper tone**; **create and maintain a culture of honesty and high ethical standards**; and **establish appropriate controls to prevent, deter, and detect fraud**.

When management and those responsible for the oversight of the financial reporting process fulfill those responsibilities, the opportunities to commit fraud can be reduced significantly.”

Evolving Roles and Responsibilities

Audit committees typically play a prominent role in overseeing investigations into alleged or suspected fraudulent actions, and often retain legal, accounting, and other professional advisers for assistance.

In addition, from a *proactive* perspective, the audit committee is often charged with overseeing the company’s risk management approach—and facilitating a process for, and environment that is conducive to, preventing, detecting, and mitigating fraud.

Evolving Roles and Responsibilities

To this end, audit committee responsibilities might encompass such core activities as:

- Evaluating management's process for the identification and mitigation of fraud risk, including the measures implemented by management designed to help detect and prevent fraud
- Assessing, monitoring, and influencing the tone at the top and reinforcing a zero-tolerance policy for fraud
- Evaluating management's processes and procedures for screening potential employees, including whether background checks are performed
- Providing oversight to management's internal control over financial reporting and contemplating the potential for management override of—or inappropriate influence over—those controls
- Comparing the reasonableness of financial results with prior or forecasted results and considering quarterly analysis of key reserves

Evolving Roles and Responsibilities

- Evaluating management's processes, procedures, and documentation of all significant estimates used in the financial reporting process
- Evaluating management's approach and documentation with respect to the processing of manual journal entries and the reporting cycle closing process
- Establishing a program for employees and others to report anonymous concerns about fraud and unethical behavior, i.e., a whistleblower process, and implementing a detailed process for the audit committee to monitor and follow through on these communications
- Providing other insight into and guidance on implementing or strengthening antifraud measures

These activities should both complement and serve as a check on senior management

Antifraud programs must be designed to address the audit committee’s and the organization’s distinct needs and objectives—one size does not fit all

Conclusion

The New York Stock Exchange requires that audit committees of listed companies discuss risk assessment and risk management policies set by management, including “major financial risk exposures and the steps management has taken to monitor and control such exposures.” As part of this process, the audit committee should also discuss fraud-related risk exposures. Considering that the NYSE also requires its listed companies to “maintain an internal audit function to provide management and the audit committee with ongoing assessments of the company’s risk management process and system of internal control,” audit committees should be cognizant of internal audit’s involvement in and knowledge of the prevention and detection of fraud. Audit committees should also understand whether the internal or external auditors have identified or reported any suspected cases of fraud.

Open Discussion

QUESTIONS

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Thank you

Services Offered

- Unclaimed financial assets compliance services
- Fraud Risk Assessment
- Forensic Investigations
- Fraud Training & Awareness Programs
- Anti-money Laundering
- Pre-employment Integrity interviews
- Loss Prevention Consulting
- Dispute Advisory
- Due Diligence Investigations
- Background Screenings

Contact Details

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