

Fraud and corruption controls - will they work when called upon?

Risk management is a central part of good corporate governance. This is reflected in recent Australian standards, for example AS 8001 *Fraud and Corruption Control*¹, where many different examples of fraud type are listed. The standard also refers to principles of risk management that should be considered and applied where possible.

It is fine to have controls in place – but will they work when called upon? Judging from recent cases, we should be asking this question of ourselves.

Identifying and treating risks

Every organisation understands the need to identify typical fraud and corruption risk scenarios pertinent to the business.

It is important that organisations remain aware of what is happening in their industry. Without this knowledge, it may be difficult to identify scenarios that occur infrequently but have severe consequences.

Control and mitigation actions are applied. This will necessarily include ways to detect fraud, dealing with suspected perpetrators, managing whistleblower schemes and the like.

A further stage

Too often organisations invest significant effort into developing a control plan – yet fail to follow up with its implementation. Tracking the effectiveness of a program is inherently difficult and easily lost in the flurry and urgency of the next business imperative.

Directors, owners and other stakeholders are continually trying to uncover flaws and weaknesses in programs, in the hope of addressing them before they can cause serious harm.

Risk assessment offers a way for spotting weaknesses in existing control programs so that resources can be applied where most needed. Actions are able to focus on the identified weak areas for maximum leverage, making the overall task simpler and more effective.

The Australian Prudential Regulation Authority said this about National Australia Bank's risk control framework:

“The control failures in this case have more to do with poor implementation than poor design. On paper, NAB's existing control framework – despite its weaknesses – should have been able to identify and contain the risk positions of the traders.”²

Practical tips and simple tools

Start by looking at the business processes where fraud and corruption could be an issue. Examples of such processes might include:

- Accounts payable, Payroll, Cash management, Procurement, Warehousing, Data and information management, Physical security, etc

Next, use knowledgeable people, working in teams, to consider the types of fraud that might give rise to risk scenarios in each of these processes.

- A practical problem: Should all of the risk types listed in AS 8001 be applied to every business process? Or should some filtering occur?
- Use key words and prompt phrases to find risk situations. Ask “What if?”, so that work team members begin to develop a growing awareness of risk scenarios – and ways of countering risk at the earliest possible stage in the process.
- Capture actions for follow up.

Is this enough?

Organisations are readily caught up by the next business imperative. It is easy to sign off on a set of control measures with a misplaced confidence that they will work when called upon to do so.

More tips:

- Treat each control measure as a function, designed to deliver a required outcome.
- Look for things that can threaten the outcomes. Some examples:
 - Tolerance limits may be too high (too few exceptions reported), or too low (too many exceptions reported – cannot practicably address them all).
 - Suitable information is provided, but wrong decisions are made
 - A problem is detected, a correct decision is made, action is applied – but the action is ineffective (eg due to poor timing)

Conclusion

Simple, practical methods are available to help identify risks so that controls may be implemented. Equally important, there are simple ways to test the effectiveness of the controls in advance, to help avoid the pitfalls that NAB discovered.

References:

1. Published by Standards Australia
2. Report into Irregular Currency Options Trading at the National Australia Bank, 23 Mar 04

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