

AUDIGATORS!

Fraud Risk and How Auditors and Investigators Can Work Together

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Today's Topics

- We'll consider three major topics in this four-hour session:
- First, how to consider and assess fraud risks in both our annual audit schedule and in specific engagement plans
- Second, how to align risks with both audit and investigative resources
- Finally, a strategy for auditors and investigators to work effectively together

Initial Overview of Fraud Risk

- “Macro” or annual level:
 - Based on **Risk**
 - Tied to audit plan
 - Topic selection approved by your audit office or audit committee
 - Focuses audit and investigative hours and resources on riskiest areas
- “Micro” or assignment level:
 - Based on **Resources** and staff time (staff hours)
 - Tied to specific audits and investigations
 - Planned by staff and management

Essential Postulates of Fraud Risk

- Time is a limited resource.
- Audit time should be leveraged to match the organization's **risks** and **risk appetite**.
- Audits and investigations should happen when and where they reduce risk and help the organization achieve its goals.
- Since fraud can impact the organization, this is the lens to examine fraud risk.

Today's Outline

- Overview and Risk Postulates
- Macro Fraud Planning
- Micro Fraud Planning
- Examples from state and federal levels
- Aligning Risk with Audit/Investigative Resources
- Examples of Working Together
- Questions

Auditor? Investigator? **AUDIGATOR!!!!**



What's an Audigator?

- Part auditor. . . Part investigator.
- Audigators could be one individual, or in many cases, can be a team of auditors and investigators who work together, bringing synergy to both the audit and investigative process.
- Kirk and Spock? Mulder and Scully? Consider optimizing office strength by combining skill-sets and knowledge.

Introductions

- Level of government?
- Auditor, Investigator, Other?
- Current project or current concern?
- Audit/investigative interactions
 - Hotlines
 - Federal training, examples
 - State nexus between audits/investigations

Example – Overtime

- An audit identifies employee overtime well above normal rates.
- Audit process identifies specific individuals claiming unusual amounts of overtime.
- Discuss process, handoff to investigators, and results.

Example – Vehicle Registration

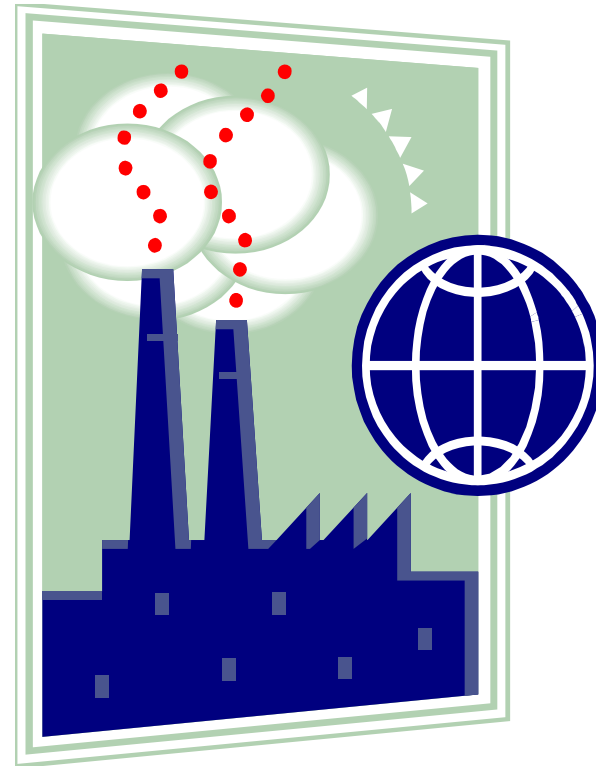
- Audit identified unusual registration activities tied to specific residence addresses.
- Audit identified specific records that pointed to potential individual connections to improper or illegal activities.
- Discuss process, handoff to investigators, and results.

Your Examples?

- Have you made or received topic handoffs between auditors and investigators?
- How and why did you make a handoff and what were the results?
- We'll cover some specific handoff tools and options later in this session.

Why Risk?

- Risk: “the possibility of loss or injury” – Webster’s
- Risk is the likelihood that the organization will fail to meet its goals.
- Given limited audit resources, auditors should focus on risk.

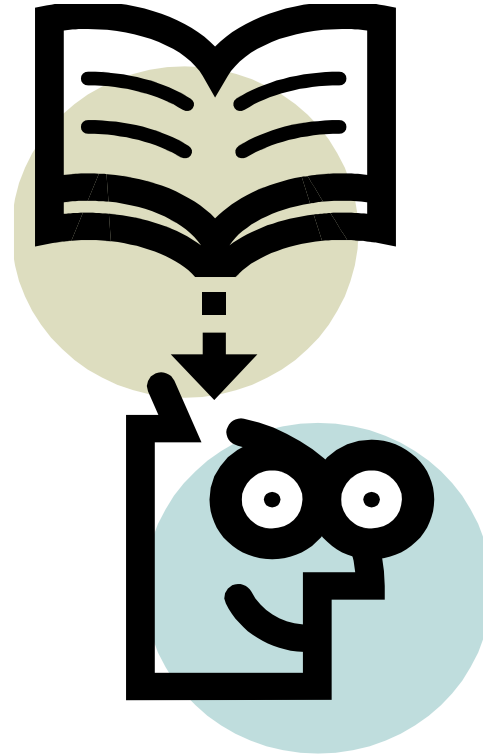


Approaches to Fraud Risk

- Accept (take the risk with no other action)
 - Transfer (refer, make someone else's case)
 - Mitigate (take action to reduce the risk)
 - Avoid (don't take the action or accept risk)
-
- See “risk appetite” for other approaches (some organizations would accept risks that others would avoid)

Managing Risk with Auditing

- Auditing is designed to assess the risks that the organization won't achieve its mission.
- Management and auditors should pay attention to core risks.
- Fraud may be significant.



Planning and Risk Recognition

Audit plans – at both the annual (macro) level and the assignment (micro) level – can alert management to risk, even before audits are completed!



When the Committee Asks “So What”?



- Audit committees and audit directors should ask how each risk can impact the mission.
- No impact should mean no audit!
- Audits vs investigations on the “target”.

How Risk and Plans “Hit Home”

Fraud risk should be explained to the Audit Committee and elected officials in ways that link each risk to the core objectives of the organization. What would fraud risk mean to them?



Macro Audit Planning

- For annual plans, auditors need to consider the organization's risks and the organization's risk appetite.
- Key factors might include issues core to the organization's mission.
- Audits and investigations may have different focus – audits tend to look at operation-wide issues and be forward-looking, investigations can look for specific causes of issues that happened.

Examples and Exercise

- Library copy machine fraud (describe)
- Kiting daily deposits over the weekend (describe)
- Similar cases?
- How else can auditors and investigators work together?
- Take five minutes with a small group to discuss and report back!

Tools for Macro/ Annual Planning

- Annual plans should be based on reviews of the major issues facing the organization.
- Consider matching audit resources to specific risk areas or organization areas.
- For example, if 50% of your organization's time and budget are spent on construction, you may want to spend 50% of your audit time and budget on auditing construction.
- If fraud risk is significant, spend more time there!

Developing the Annual Plan

- Once risks are identified, assign audit budget to each risk and audit topic.
- A strong Audit Charter or legal authority is vital to the audit organization's success.
- Distribute the plan to key managers and staff. Consider posting on Internet, Intranet or in a newsletter. Audit topics are often more “public” than investigative topics.

Annual Plan Establishment

- Use vital phrases that speak to the key risk as audit titles.
- For example, a transportation organization's use of the audit title, "bid rigging" is less effective and less descriptive than the title, "audit of likelihood of bid rigging" or "Are we identifying unusual bidding patterns?" as audit title descriptors.

Annual Plan Budgeting

- Each full-time employee has a base time budget of around 2,080 hours per year (40 hours per week X 52 weeks per year)
- Excluding leave, holidays, training, and other overhead, many staff are 60%-75% “billable” or efficient. At a 72% rate, we budget 1,500 hours per employee per year of productive time.
- 3 full-time employees = 4,500 hours/year.

Annual Plan Example (1)

- Audit unit in a government office has 4,500 available hours.
- Risk assessment process identified three major risks:
 - Inefficient hospital billings may cause lost revenue,
 - Slow passport issuance may hurt customer satisfaction,
 - Government may not be reacting to causes of fraud or financial irregularities.

Annual Plan Example (2)

- For manufacturing:
 - 4,500 audit hours available:
 - Audit of Hospital Billing Efficiency:
2,500 hours
 - Audit of Causes of Delayed Passports:
1,000 hours
 - Audit of Reaction to Potential Fraud:
1,000 hours

Micro Audit Planning

- Within each audit, we should use risk to allocate audit time and focus within the budget.
- This works for any audit plan or investigation plan.
- Many organizations divide the budget into phases: Survey/Planning, Field Work, and Reporting.

Micro Audit Planning

- Within the time allowed, a rule of thumb is to allocate:
 - 25% to planning and survey (includes defining specific scope/objectives and planning all field work, preparing documentation),
 - 50% to field work, and
 - 25% to reporting (includes the written report, exit conferences, briefings, etc).

Examples

- Planning for a manufacturing audit might include risks causing slow production or low production.
- Planning for a service organization audit might include risks causing poor customer relations or poor communication.
- Planning for a hotline call review might focus on confirming or refuting allegations.

Exercise

- How would you plan for an audit with potential fraud impact?
- Planning vs. field work vs. reporting?
- Discuss with your group how you would stage the work and get the audit/investigative resources – collaboration or staffed within your office? Outside assistance? Referral?
- Take five minutes to discuss and report back!

Possible Tracks – Audit and Investigation

- Many federal Inspector General offices are split into two functions –
 - Audit
 - Investigation
- Most have Regional I.G.s for each area
- Federal employee classifications have both auditors (often “311”) and investigators (“1811”).

Fraud Risk “Heat Map”

- Consider both “likelihood” and “severity” of fraud risk
- Focus efforts on likely and severe risks (or at least likely or severe risks)
- Consider joint staffing with auditors and investigators if fraud is a significant possibility
- Discuss co-sourcing with outside organizations (examples)

Synergy Examples – How Auditors Can Help

- Bolster detailed financial and operational causes
- Potentially go further back in time
- Assess organizational risk and odds of the problem happening again
- Look for other examples in the organization or in other organizations
- “Public health” vs. treating one patient

Synergy Examples – How Investigators Can Help

- Evidence may be more admissible in court or other proceeding
- May be able to read suspects their rights and seize records/property
- May have arrest powers
- May have subpoena powers beyond what auditors have
- Experienced in testifying in legal environments

Examples of Working Together

- Natural resources enforcement
- Construction fraud (interstates)
- Office supply fraud
- Other collaboration (audits with investigative nexus)
- Your examples?

Toolkit to Assign Projects

- SCH AI-IA (say “Skyayaya!”)
- Solo
- Collaborative
- Handoff (Auditor to Investigator)
- Handoff (Investigator to Auditor)
- Followup (either can pick up a file and work)

When to be Solo?



When to be Solo?

- Topic is clearly restricted to an audit area
- Topic is clearly restricted to an investigative area
- Auditors would wade into potential criminal areas without investigative help
- Investigators would wade into audit areas without audit help (if either one would impact the conduct of the work negatively)

When to Collaborate?

- Bid rigging example
- Intergovernmental collaboration (Federal with State and/or Local, as well as multiple jurisdictions at the same level collaborating)
- Your examples?
- Great nexus and efficiency from collaboration
- Wildlife management example
- Office supply example

When to Hand Topic Over

- Typically, hand-offs happen when a normally-seeming audit runs into potential criminal issues
 - Bid rigging
 - Specific fraud indications (overtime)
 - Indications of intent rather than negligence
 - Concept of intent / “scienter”
- Hand-offs can also happen when auditors follow up on the extent or overall impact of a specific prior investigative finding

Timing of Referrals?

- Often, an audit that finds potential fraud can stop/pause the moment the hand-off to investigators happens. This avoids auditors impacting a potential case. Audit can resume when investigation is done.
- Other options include both engagements continuing simultaneously.

Can Auditors Ask Questions?

- Yes! Some laws and policies anticipate that audits may be occurring around areas that are later investigated
- Investigators can also refer information for further audit
- Garrity and Weingarten cases on employment law – when employees are interviewed about conduct on the job

Follow-On Work

- Auditors and Investigators can each open audits/cases from the prior work of others
- Discuss “capstone” and annual reports as options for collaboration
- Investigators can ask “who?”
- Auditors can ask “why?”
- Overtime fraud example
- Library copy card example

Next Steps

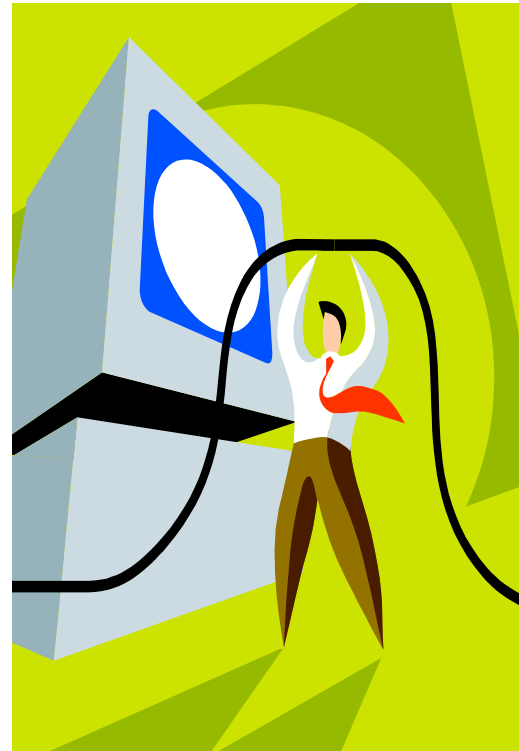
- Link core fraud risks to planning process
 - Macro
 - Micro
- Ensure that Audit Committee and other important stakeholders understand the concepts and processes
- Develop risk-based planning and resource allocation to link resources to mission!
- Identify areas for collaboration/cooperation!

Cumulative Exercise

- Individually, list two or three things you can do back at the office to best leverage audit and investigative work – handing off, collaborating, or even solo efforts?
- How can these improve your audit and investigative process?
- Take five minutes and we'll hear from some colleagues!

Questions?

- Let's discuss any questions, concerns, or remaining issues!



Thank You!



- Please contact me with any questions or suggestions.

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