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INTOSAI
Working Group
on Environmental
Auditing

Integration of Fraud and Corruption Issues into the Auditing of Environmental and Natural Resource Management

Guidance for Supreme Audit Institutions

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Chapter 1:
Fraud and corruption risk factors at the governance and sector levels

The purpose of this chapter is to: First, briefly describe what fraud and corruption is and what challenges it poses to the world community (1.1). Second, provide a first introduction to the link between fraud and corruption and environmental and natural resource management (1.2). Finally, give a summary of the content and structure of the guide (1.3).

1.1 A GLOBAL CHALLENGE

1.2 FRAUD AND CORRUPTION IN ENVIRONMENTAL AND NATURAL RESOURCE MANAGEMENT

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Chapter 2:
Background to fraud and corruption and environmental and natural resource management

Fraud and corruption is a multi-faceted concept which refers to practices that take place at all levels of the public sector, and which cover a long continuum spanning from unacceptable behavior at the one end to criminal behavior at the other. Furthermore, the causes of fraud and corruption are also various, and auditors must take this into account when approaching these issues. Among the various sectors which are negatively affected by fraud and corruption, the environmental and natural resource sectors are no exception, although the impacts and their particular features vary a lot from topic to topic and from region to region around the world.

This chapter is organized into three main sections. In the first section, various definitions of fraud and corruption are discussed, and a working definition which combines the two concepts is suggested. Furthermore, this section also presents different levels and different forms of fraud and corruption. Section 2.2 describes the main drivers of fraud and corruption based on the conceptual framework provided by the 'fraud triangle'. The last section, section 2.3, is divided into three parts. The first part presents some of the particular features of natural resources and the environment in relation to fraud and corruption, based on the 'fraud triangle'. The second part describes some common trends with regard to fraud and corruption in environmental and natural resource management, while the third and last part provides some examples from the INTOSAI WGEA portfolio on sectors where fraud and corruption may have a negative impact.

2.1 DEFINITIONS OF FRAUD AND CORRUPTION

As mentioned in the introductory chapter, the primary target group of this Guide is public sector auditors working for the various SAIs around the world. Consequently, the primary focus of this Guide will be on fraud and corruption in the public sector. This also will be reflected in how these two concepts are defined in the Guide.

2.1.1 Why fraud *and* corruption?

There are many different – both general and specific – definitions of fraud and corruption in use today. This great variety of definitions reflects the various ways in which people perceive and conceptualize fraud and corruption.[1] As a consequence, on the global level, these terms are often used interchangeably by organizations working in this field, in public debate and in the academic discussion on the subject. As regards INTOSAI in particular, this is reflected in the Uruguay Accords from XVI INCOSAI in 1998, where fraud and corruption to a large

[1] ASOSAI, 2003. ASOSAI Guidelines for Dealing with Fraud and Corruption, adopted by the 9th ASOSAI Assembly on 22 October 2003. [Online] Available at www.asosai.org/asosai_old/guidelines/guidelines1.htm Accessed on 11 January 2011]

extent are referred to as 'two sides of the same coin' and/or are applied interchangeably.[2] On the other hand, however, depending on whether these terms are given a wide or narrow definition, there are also examples on "fraud" being referred to as one specific kind of corruption – and vice versa.

Hence, taking this into account, fraud and corruption will be applied as one concept in this Guide. However, as the definitions of the two terms quite often seem to differ as to which aspects they attach the most importance to, we will first briefly discuss each of the two terms below before we suggest a synthesis definition in the next subchapter.

Corruption:
According to the UN, there is no single, comprehensive, universally accepted definition of corruption.[3] This is reflected in the fact that the UN Convention against Corruption (UNCAC) does not contain a single definition of "corruption", but lists several specific types or acts of corruption.[4] At the same time, however, there are several so-called 'working definitions' of the concept which are in use. According to the UN, common working definitions of "corruption" after the turn of the millennium are variations of "the misuse of a public or private position for direct or indirect personal gain".[5] This is quite similar to the definition used by Transparency International (TI), which is "the abuse of entrusted power for private gain".[6]

Taking into account that this Guide primarily will focus on fraud and corruption in the public sector, however, the working definition of "corruption" adopted by the World Bank Group is more to the purpose: "[Corruption is] the abuse of public funds and/or office for private or political gain."[7]

Fraud:
The definition of "fraud" applied by the International Auditing and Assurance Standards Board (IAASB), and also adopted by INTOSAI, is the following: "An intentional act by one or more individuals among management, those charged with governance, employees, or third parties, involving the use of deception to obtain an unjust or illegal advantage."[8] A quite similar definition has been applied by the Institute of Internal Auditors (IIA), the American Institute of Certified Public Accountants (AICPA) and the Association of Certified Fraud Examiners (ACFE): "Fraud is any intentional act or omission designed to deceive others,

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[2] Theme I, Preventing and Detecting Fraud and Corruption, Uruguay Accords of the XVI INCOSAI in Montevideo, Uruguay, 1998.
[3] UNODC, 2004. The United Nations Anti-Corruption Toolkit, 3rd Edition. [Online] Available at www.unodc.org/documents/corruption/publications_toolkit_sep04.pdf [Accessed on 11 January 2011], p. 10.
[4] UNODC, 2005. Draft United Nations Handbook on Practical Anti-Corruption Measures for Prosecutors and Investigators. [Online] Available at www.unodc.org/pdf/corruption/publications_handbook_prosecutors.pdf [Accessed on 11 January 2011], p. 21.
[5] UNODC, 2005, p. 21.
[6] Transparency International: Frequently asked questions about corruption. [Online] Available at www.transparency.org/news_room/faq/corruption_faq [Accessed on 11 January 2011]
[7] Paterson, William D. O. and Chaudhuri, Pinki, 2007. Making Inroads on Corruption in the Transport Sector through Control and Prevention, p. 160, in: Campos, J. Edgardo; Pradhan, Sanjay (eds.), 2007. The many faces of corruption. Tracking Vulnerabilities at the Sector Level, The World Bank. [Online] Available at www.u4.no/pdf/?file=/document/literature/publications_adb_manyfacesofcorruption.pdf [Accessed on 11 January 2011].
[8] IAASB, 2009. ISA 240. The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements, in ISSAI 1240, The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements, endorsed by INTOSAI in 2010. [Online] Available at www.issai.org/media(734,1033)/ISSAI_1240_E_Endorsement.pdf [Accessed on 11 January 2011], p.241.

resulting in the victim suffering a loss and/or the perpetrator achieving a gain".[9] None of these definitions distinguishes between the private and the public sector, however.

Compared with the definitions of corruption above, these two definitions introduce two additional aspects, that is, *intention* and *deception*. By including intention, the definition distinguishes fraudulent acts from mistakes. The rationale for including deception is that fraud and corruption, by their nature, often are concealed activities. According to the UN, this motivates many of those involved to distort or falsify any information which they provide.[10] On the other hand, however, including this aspect in the definition involves the risk of excluding all those cases of 'state capture'[11] where fraud and corruption might occur more or less openly.

2.1.2 Fraud and corruption combined – a definition:

Based on the discussion above, the definition of fraud and corruption in this Guide will be a synthesis of the World Bank definition of corruption and the INTOSAI definition of fraud. Hence, the working definition of "fraud and corruption" in this Guide will be the following:

> ***"an intentional act by one or more individuals to obtain an unjust or illegal advantage by abusing public funds and/or office"***

This definition implies the following:

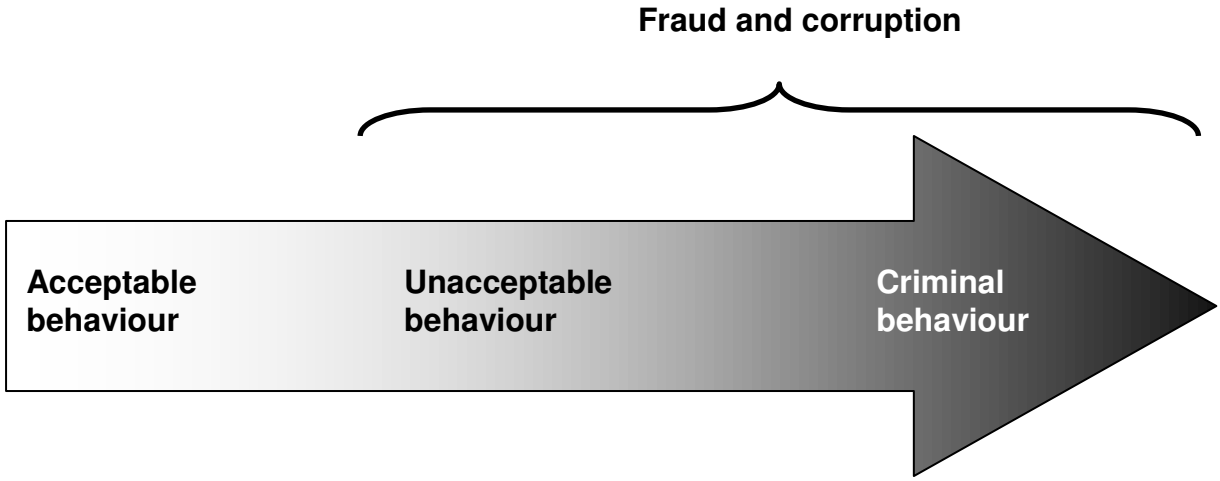
- By "individuals" we refer to individuals at all levels, that is, from government officials at the highest level to public servants at the lowest level;
- By "advantage" we both refer to direct/indirect private gain and to political gain;
- The act may both involve the use of deception and/or be carried out openly.

The definition applies both to unjust and to illegal acts due to several reasons. First, the legal systems may vary a lot from country to country around the world. Hence, acts of fraud and corruption which are illegal in one country may be legal in another. Secondly, focusing only on illegal cases may to a large extent limit the potential scope of action for SAIs seeking to prevent and detect fraud and corruption, as such cases often are within the jurisdiction of the investigation and prosecution authorities. Thirdly, by relating abuse also to unjust advantages, the definition also applies to acts that are unethical, in breach of written/unwritten codes of conduct, norms, etc., but not necessarily illegal. Among other things, such acts/breaches are closely related to the issues of 'rationalization'[12] and 'control environment'[13], which also must be properly addressed by auditors to ensure that their antifraud/-corruption programmes are as effective as possible. Furthermore, by focusing also on unjust and unethical acts, the definition also includes acts of 'state capture', where for instance the law itself is changed for

[9] IIA, AICPA, ACFE: Managing the Business Risk of Fraud – A practical Guide. [Online] Available at www.acfe.com/documents/managing-business-risk.pdf [Accessed on 12 January 2011], p. 5.
[10] UNODC, 2004, p. 73.
[11] See subchapter 2.1.4.
[12] See subchapter 2.2.3.
[13] See chapter 4.

private or political gain.[14] Finally, this definition reflects the fact that the boundaries between acceptable and unacceptable behaviour, and between unacceptable and criminal behaviour are seldom static and clear-cut. This is illustrated in figure 2.1.

Figure 2.1 The fraud and corruption continuum



2.1.3 Fraud and corruption – a multi-faceted concept

Just as there are many different definitions of fraud and corruption in use today, these two concepts can also be divided into many different types or categories of acts and practices. To start with, one fundamental distinction is between *internal* fraud and corruption, on the one hand, and *external* fraud and corruption on the other.[15] For the purpose of this Guide, the former category consists of fraudulent and corrupt acts which are committed by employees, management or the political leadership within the public sector, while the latter category refers to such acts committed against the public sector by individuals or groups in the private sector. Very often, however, fraud and corruption is taking place in the interface between the two sectors, i.e. a combination of internal and external fraud and corruption through collaboration between those on the inside and those on the outside.

Different levels of fraud and corruption:

Another categorization can be made in respect of the *level* on which the fraud and corruption is taking place. For this purpose, this Guide will use the classification suggested by UNDP (2008)[16] as the point of departure. According to UNDP, fraud and corruption can be divided into: (1) 'petty corruption', (2) 'grand corruption' and (3) 'state capture'.

These three categories can be described as follows:

[14] See subchapter 2.1.4.
[15] ASOSAI, 2003.
[16] UNDP, 2008. Tackling corruption, transforming lives. Accelerating Human Development in Asia and the Pacific. *Asia Pacific Human Development Report.* [Online] Available at http://hdr.undp.org/en/reports/regionalreports/asiathepacific/RHDR_Full%20Report_Tackling_Corruption_Transforming_Lives.pdf [Accessed on 20 January 2011], pp. 17, 36, 92.

(1) 'Petty corruption':

'Petty corruption' refers to fraud and corruption which usually involves smaller sums of money and which is committed by public servants at lower levels. It relates to 'everyday' fraud and corruption taking place where officials and the public interact with each other, that is, at the implementation end of laws, rules, regulations and policies.[17] Petty corruption may for instance involve bribes and 'kickbacks', direct theft of cash and other assets, or exchange of favours for personal allovances.[18]

In the water sector for example, petty corruption may involve paying bribes to officials to get access to household connections or sewage disposal services, or paying so-called 'speed money' to advance in the queue for repairs.[19] In the fisheries sector, another example could be a landing inspector who is offered a large tuna in exchange for 'turning a blind eye' to flaws in the logbook.[20]

Although the amounts of money that are exchanged in connection with petty corruption may be quite small, and seldom result in newspaper headlines such as cases of 'grand corruption' (see below), however, the *aggregate* costs for society of the former may be as great if not greater than the latter.[21] This also applies to the management of natural resources in particular.[22] In addition, the poor suffer the most from petty corruption, as they usually are most directly affected by it.[23]

Furthermore, it should be emphasized that petty corruption also can be referred to as 'administrative' or 'bureaucratic' corruption[24], concepts which usually are defined more widely when it comes to the level and scale of fraud and corruption. According to the World Bank, for instance, administrative corruption can cut through various levels of government, from the higher to the lower levels.[25] Administrative corruption can also involve large sums of money.[26]

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[17] UNDP, 2008, p. 230.
[18] Dorotinsky, William and Pradhan, Shilpa, 2007. Exploring Corruption in Public Financial Management, p. 268, in: Campos and Pradhan, 2007.; Shah, A., and M. Schacter, 2004. Combating Corruption: Look Before You Leap, in Finance and Development 41 (4) [Online] Available at www.imf.org/external/pubs/ft/fandd/2004/12/pdf/shah.pdf [Accessed on 27 January 2011], p. 41.
[19] Plummer, Janelle and Cross, Piers, 2007. Tackling Corruption in the Water and Sanitation Sector in Africa. Starting the Dialogue, p. 236, in: Campos and Pradhan, 2007.
[20] Tsamenyi, Martin and Hanich, Quentin, 2008. Addressing Corruption in Pacific Islands Fisheries (Draft) A Report prepared for the IUCN PROFISH Law Enforcement, Corruption and Fisheries Project. [Online] Available at http://www.illegal-fishing.info/uploads/IUCNfishcorruptionpacificdraft.pdf [Accessed on 28 January 2011], p. 12
[21] World Bank, 1997. Helping Countries Combat Corruption. The Role of the World Bank, September. [Online] Available at www1.worldbank.org/publicsector/anticorrupt/corruptn/corrptn.pdf [Accessed on 25 January 2011], p. 10.
[22] Mock, Gregory, 2003. Undue Influence: Corruption and Natural Resources. Adapted from Box 2.4, pp. 36-37 in World Resources 2002-2004. [Online] http://earthtrends.wri.org/pdf_library/feature/gov_fea_corruption.pdf [Accessed on 18 March 2011], p. 1.
[23] World Bank, 1997, p. 19; UNDP, 2008, pp. 2, 20.
[24] See, for instance, Shah and Schacter, 2004, p. 41; UNDP, 2008. p. 230; UNODC, 2004, pp. 121, 179; Campos, J. Edgardo and Bhargava, Vinay, 2007 Introduction. Tackling a Social Pandemic, endnote 23, p. 22, in: Campos and Pradhan, 2007; Plummer and Cross, 2007, p. 225.
[25] World Bank, 2000. Anticorruption in Transition. A Contribution to the Policy Debate [Online] Available at http://info.worldbank.org/etools/docs/library/17506/contribution.pdf [Accessed on 26 January2011], p. 2.
[26] Campos and Bhargava, 2007, p. 9.

(2) 'Grand corruption':

'Grand corruption' refers to fraud and corruption which usually takes place at the highest levels of government – by members of the political or administrative elite, or people associated with them – and which generally involves substantial amounts of money. Grand corruption may for instance involve direct theft or embezzlement of vast amounts of public sector funds through diversion of revenues, or the acceptance of large bribes from contractors or other companies in exchange for contracts or other business advantages. Such bribery transactions may be carried out entirely outside the country in question, and grand corruption is therefore also frequently associated with international business transactions.[27]

In the petroleum sector, an example could be the payment of substantial 'consultancy fees' to a person or firm with good political connections – also referred to as 'big men' – to secure oil and gas contracts.[28] As to climate change mitigation, fraud and corruption could for instance take place in connection with carbon measurements as part of REDD+.[29] More specifically, political elites or public sector officials could inflate REDD+ revenues by over-estimating the amount of emission reductions and avoided emissions against the baseline, and thereafter 'skim off' and embezzle the additional revenues which this over-estimation generates.[30]

In addition to the costs associated with the direct financial losses and harmful effects on the environment or natural resources, grand corruption can also seriously undermine the rule of law and economic stability, and the trust in good governance.[31]

(3) 'State capture':

'State capture' refers to the acts of individuals, groups, or companies both in the private and public sectors to manipulate the shaping of laws, policies and regulations for private or political gain. This manipulation can be achieved through illegal practices, for instance when companies are bribing public officials to shape legislation to their advantage. As a result, the activities of the companies in question may now be legal, but they are still corrupt. This is a way of 'legalizing' fraud and corruption.[32]

The manipulation can also be achieved through legal means, however, by making donations to political parties or by intense political lobbying. State capture is therefore often associated with 'political corruption', where politicians exchange favours for financial or other support to sustain or strengthen their political power. 'Cronyism' is another variant, where political

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[27] See, among others, UNODC, 2005, p. 21; Shah and Schacter, 2004, p. 41; UNDP 2008, pp. 2, 230; McPherson, Charles and MacSearraigh, Stephen, 2007, Corruption in the Petroleum Sector, p. 199, in: Campos and Pradhan, 2007; World Bank, 1997, pp. 9-10.

[28] McPherson and MacSearraigh, 2007, pp. 201, 204.

[29] Reducing Emissions from Deforestation and Forest Degradation (REDD) is a UN-programme aiming at providing incentives for developing countries to reduce emissions from deforestation and to achieve sustainable development trough low-carbon paths by creating financial value for the carbon stored in forests. 'REDD+' goes beyond deforestation and forest degradation, and includes enhancement of carbon stocks in forests, sustainable forest management and conservation. Source: UN-REDD [Online] Available at www.un-redd.org/AboutREDD/tabid/582/Default.aspx [Accessed on 17 February 2011].

[30] UNDP, 2010. Staying on Track – Tackling Corruption Risks in Climate Change. [Online] Available at http://climate-l.iisd.org/news/undp-publishes-report-on-tackling-corruption-risks-in-climate-change/?referrer=climate-change-daily-feed [Accessed on 17 February 2011], p. 40.

[31] UNODC, 2005, p. 21.

[32] See, among others, Campos and Bhargava, 2007, p. 3; UNDP, 2008, pp. 7, 21-22, 92, 231; Paterson and Chaudhuri, 2007, p. 161.

leaders use the executive, legislative or judicial branches of government to enrich themselves, friends and associates through illegal and 'legal' means.[33]

Although both state capture and grand corruption may involve exceptionally large side payments, the former should be distinguished from the latter, as it focuses on the distortion of legal and regulatory frameworks. Grand – and petty – corruption on the other hand, concerns fraud and corruption in the implementation and enforcement of laws, regulations and policies.[34]

In the mining sector, an example of state capture could be senior politicians at the highest levels of government which intervene in 'the shadows' when mining contracts are negotiated, using their power to influence negotiators and/or those who sign the contracts in an inappropriate manner.[35] In the forestry sector, an example could be 'rent seizing' by politicians during timber booms. When timber prices are beginning to reach levels which generate exceptionally high profits, state officials may seek to acquire the authority to allocate these rents by weakening the legal and regulatory measures and the institutions which previously were established to maintain logging at sustainable levels and to protect the rights of forest inhabitants.[36]

The costs associated with state capture are to a large extent the same as those generated by grand corruption. However, an additional element when it comes to state capture is that fraud and corruption at this level more often occurs in the 'grey zone' between the legal and the illegal spheres. The transactions involved can be both more indirect and subtle, and fraud and corruption at the state capture level is therefore generally more difficult to comprehend for the media and the public. Consequently, given its nature, it can sometimes also be difficult to distinguish state capture from pure mismanagement of natural resources. State capture is therefore possibly the most venal form of fraud and corruption.[37]

Box 2.1
Various forms of fraud and corruption:

As mentioned, fraud and corruption can also be divided into many different types or categories of acts and practices. Among the various typologies in use, a rather exhaustive one is provided by UNODC.[38] Here, we will present only a selection of the most common types:

Bribery:

[33] UNDP, 2008, pp. 7, 92; Campos and Bhargava, 2007, p. 9

[34] Kishor, Nalin and Damania, Richard, 2007. Crime and Justice in the Garden of Eden. Improving Governance and Reducing Corruption in the Forestry Sector, endnote 5, p. 110, in: Campos and Pradhan, 2007.

[35] Global Witness, 2006. Digging in corruption. Fraud, abuse and exploitation in Katanga's copper and cobalt mines. [Online] Available at www.globalwitness.org/library/digging-corruption [Accessed on 18 February 2011], p. 42.

[36] Kishor and Damania, 2007, p. 94.

[37] See, among others, Paterson and Chaudhuri, 2007, p. 162; Campos and Bhargava, 2007, p. 3; UNDP, 2008, pp. 21-22, 92.

[38] According to UNODC, corruption can be divided into the following categories: 1. 'Grand' and 'petty' corruption; 2. 'Active' and 'passive' corruption; 3. Bribery; 4. Embezzlement, theft and fraud; 5. Extortion; 6. Abuse of discretion; 7. Favouritism, nepotism and clientilism; 8. Conduct creating or exploiting conflicting interests; 9. Improper political contributions. (UNODC, 2004, pp. 10-16.) For further reading, see also, among others, UNODC, 2005, pp. 21-27, and UNODC, 2003, UN Guide for Anti-Corruption Policies. [Online] Available at www.unodc.org/pdf/crime/corruption/UN_Guide.pdf [Accessed on 22 February 2011], pp. 28-34.

For the purpose of this guide, bribery refers to the act of promising, offering or giving, to a public official – either national, foreign or in a public international organization – money, services or other benefits to persuade her or him do something in return. It also refers to the act of solicitation, that is, to the acceptance by the public official of the money, services or benefits offered.[39] As already mentioned, bribery can take place at both the lowest and the highest levels of government, and it can involve everything from 'small change' to extraordinarily large side payments. According to UNODC, bribery is probably the form of corruption which is most common.[40] Hence, this is probably also what many first and foremost associate with the term 'corruption'.

According to UNODC, bribery can also be divided into various specific types. Two of these could be worth mentioning here, as they illustrate the 'grey zones' between acceptable, unacceptable and criminial behavior.

- The first is so-called 'influence-peddling', where Government insiders, politicians or public officials sell or trade the exclusive access they have to decision makers or their influence on Government decision-making. According to UNODC, influence-peddling must be distinguished from legitimate lobbying or political advocacy.[41] However, as already indicated, the boundaries between what is legitimate and acceptable – and what is not – are not always clear-cut and unambiguous. Influence-peddling take place along a *continuum* which spans from acceptable lobbying to criminal behavior.[42]
- The second is offering or receiving improper gifts, gratuities, favours or commissions. This is central in influence peddling, for example where lobbyists offer or provide various benefits to public officials or elected representatives such as meals and entertainment, trips and other gifts in exchange for the use of their political influence to benefit the former or his/her clients.[43] UNODC points out that such improper benefits are difficult to distinguish from bribery as links are always developed between benefits and results.[44] However, the perceptions as to what qualifies as reasonable and appropriate gifts, payments, etc. differ very widely between various cultures. This form of bribery can therefore be difficult to address.[45]

Embezzlement:

This refers to the misappropriation or stealing of money, property or other public assets by public officials who are not entitled to these assets, but have been entrusted to them through their position or employment. 'Theft' is also associated with embezzlement, but has a wider

[39] The full definitions of bribery of a) national public officials, and b) bribery of foreign public officials and officials of public international organizations are found, respectively, in articles 15 and 16 of the United Nations Convention against Corruption (UNCAC).
[40] UNODC, 2004, p. 11.
[41] UNODC, 2004, p. 12.
[42] McPherson and MacSearraigh, 2007, p. 201.
[43] Kupferschmidt, David, 2009. Illicit Political Finance and State Capture, International Institute for Democracy and Electoral Assistance. [Online] Available at www.idea.int/resources/analysis/upload/IDEA_Inlaga_low.pdf [Accessed on 22 February 2011], p. 35-36.
[44] UNODC, 2004, p. 12.
[45] Pope, Jeremy, 2000. Confronting Corruption: The Elements of a National Integrity System, TI Source Book 2000, Transparency International. [Online] Available at www.transparency.org/publications/sourcebook [Accessed on 24 January 2011], pp. 8-9.

meaning than the latter concept, as it also includes the stealing of property or other assets which have not been entrusted to the person in question.[46]

Extortion:

In contrast to bribery, extortion or blackmailing involves the use of negative incentives such as threats of exposure of harmful information or threats or use of violence to achieve cooperation. Government officials and public servants can both commit extortion or be the victims of it. In some cases, the difference between extortion and bribery may only depend on the extent of coercion involved. Furthermore, through the acceptance of a bribe, a public official also becomes much more vulnerable to extortion.[47]

Intentional misrepresentation and deception:

This refers to the giving or receiving of misleading or false information to obtain an unjust or illegal advantage. In contrast to embezzlement, intentional misrepresentation and deception is used to induce the owner of money, property or other assets – here: the State – to relinquish it voluntarily. It can be commited both internally, for instance when public officials create artificial expenses, and externally, for example when individuals, groups, or companies are receiving public funding on false premises.[48] This type of abuse of public funds and/or office is perhaps what is most commonly associated with the term 'fraud'.

Favouritism, nepotism and clientilism:

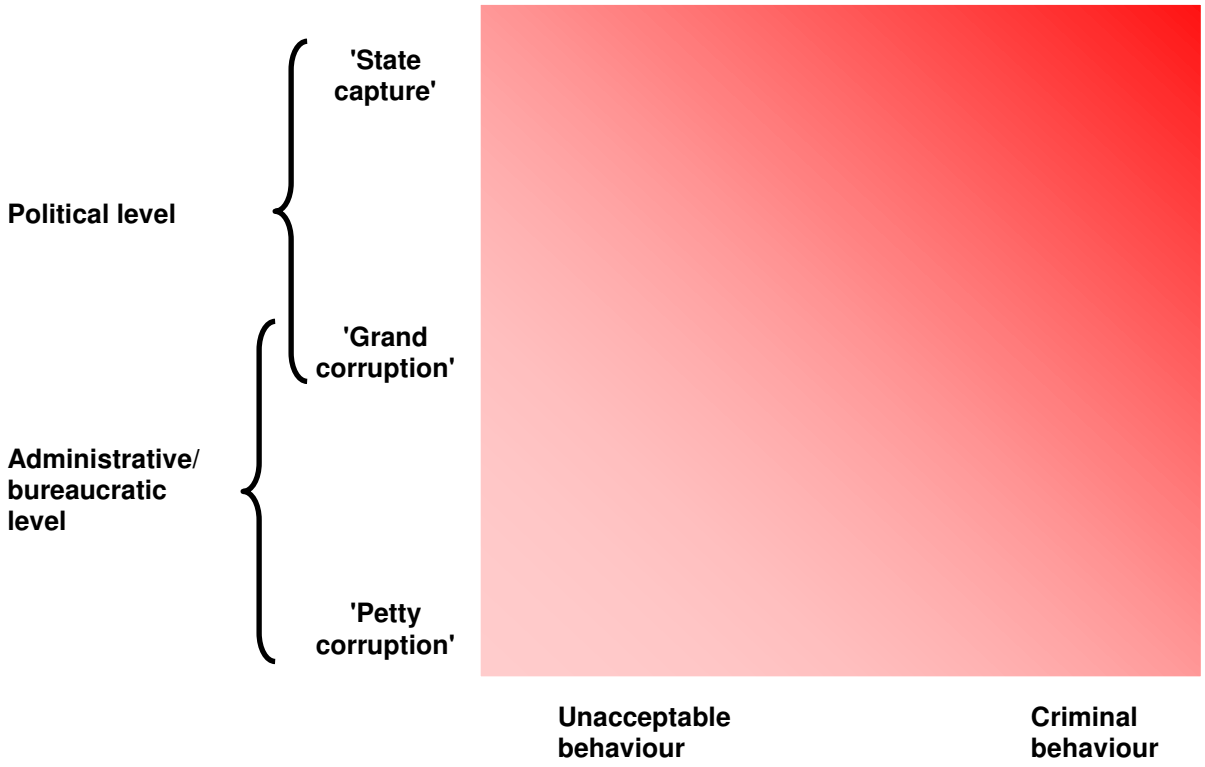
In general, this form of fraud and corruption involves abuse of discretion. However, this type of abuse is not initiated by the self-interest of the government official in question, but by the interests of relatives, friends, tribe or clan members, fellow party members, etc. Among other things, it involves the exploitation of power and authority to procure jobs and positions for relatives irrespective of their objective qualifications (nepotism).[49] According to UNODC, there is a number of States which have not criminalized the conduct of favouritism, nepotism and clientilism.[50] Hence, as with influence-peddling and the offering or receiving of improper gifts etc., this type of fraud and corruption also illustrates the 'greyzones' between acceptable, unacceptable and criminial behavior.

The presentation above of the various types and levels of fraud and corruption is summarized in figure 2.2. The figure is based on the two continuums presented, that is, a) from unacceptable behavior to criminal behaviour, and b) from petty corruption to state capture. Most of the types of fraud and corruption described in Box 2.1 – bribes, theft, exchange of favours, embezzlement, improper gifts, influence-peddling, abuse of discretion, etc. – can be plotted many different places in this quadrant. Naturally, however, depending on the context and the particular challenges involved, the figure will vary from country to country as to the types of fraud and corruption which are most prevalent and their 'co-ordinates' in the quadrant.

[46] UNODC, 2004, pp. 13-14.
[47] UNODC, 2004, pp. 12, 14-15.
[48] See, among others, UNDP, 2010, p. 8; UNODC, 2004, p. 14; UNDP, 2008, p. 19.
[49] UNODC, 2004, p. 15; UNDP, 2010, p. 8.
[50] UNODC, 2005, pp. 26-27.

The whole quadrant is coloured red to illustrate that all sorts of acts described – and at any level – are unacceptable. However, to indicate that some acts – and their magnitude and the level at which they are committed – may be more serious and detrimental than others, there are different shades of red in the figure. There might for instance also be some merit in suggesting a continuum from the most needy (light red) to the most greedy (dark red). In a discussion of 'areas of ambiguity', the UNDP introduces the concept of 'ethics of survival' as one possible area of uncertainty.[51]

Figure 2.2 Shades of red: From unacceptable behavior at the 'petty level' to 'state capture' with criminal means



It is important to note that various forms of fraud and corruption can be carried out simultaneously at different levels, and involve complex networks between political elites, public officials and private businessmen. In reality, therefore, the continuum between petty corruption and state capture might not be as simple and linear as it is presented above.[52]

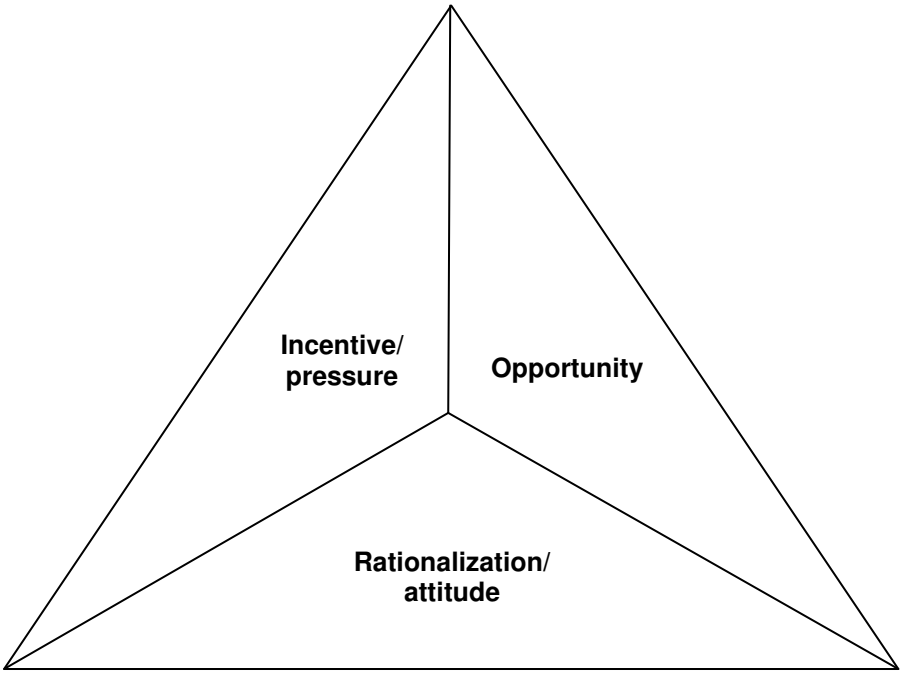
2.2 Drivers of fraud and corruption. What causes fraud and corruption?

According to the criminologist Donald R. Cressey, there are three key elements which normally are present when people commit fraud and corruption: 1. Incentive/pressure; 2. Opportunity; 3. Rationalization/attitude. Together, these three elements constitute the so-

[51] UNDP, 2008, p. 21.
[52] See UNDP, 2008, p. 92.

called 'fraud triangle'.[53] (See figure 2.2). According to ISSAI 1240, these conditions are also often present in the public sector in various ways.[54]

Figure 2.3 The fraud and corruption triangle



The three elements of the fraud triangle can be described as follows:

2.2.1 Incentive/pressure:

Incentive/pressure is also referred to as "motivation" or "greed or need".[55] When it comes to pressure or need felt by the person committing fraud and corruption, this may reflect a real financial difficulty caused, for instance, by personal debt, medical bills or gambling/drug addictions.[56] The need may also arise because the salary of the person in question is inadequate for economic survival. According to surveys in many countries, low salaries have been identified as an important factor explaining corruption among civil servants.[57] Furthermore, the need felt to commit fraud and corruption may also be induced by the pressure to deliver services of high quality with scarce resources and without exceeding budgetary limits, which is often the situation for public sector employees. This may be

[53] Lou, Yung-I and Wang, Ming-Long, 2009. Fraud Risk Factor Of the Fraud Triangle. Assessing The Likelihood Of Fraudulent Financial Reporting, in Journal of Business & Economics Research – February, Volume 7, Number 2. [Online] Available at www.cluteinstitute-onlinejournals.com/PDFs/1065.pdf [Accessed on 18 January 2011], pp. 61-62.
[54] ISSAI 1240, p. 222.
[55] CIMA, 2008. Fraud Risk Management: A Guide to Good Practice. [Online] Available at http://www.cimaglobal.com/Documents/ImportedDocuments/cid_techguide_fraud_risk_management_feb09.pdf.pdf. [Accessed on 18. January 2011], p. 13.
[56] The Fraud Triangle and What You Can Do About It, in The Certified Accountant, 1st Quarter 2009 – Issue #37. [Online] Avilable at www.lacpa.org.lb/Includes/Images/Docs/TC/TC363.pdf [Accessed on 18 January 2011], p. 69.
[57] UNDP, 2008, p. 114.

particularly relevant when the economic conditions are tough.[58] Finally, the need felt to commit fraud and corruption may also arise as a result of threats and extortion.[59]

On the other hand, the incentives for committing fraud and corruption may also simply come from greed and the wish to maintain a lavish lifestyle. According to the UNDP, greed is often more relevant as explanatory factor than need, especially when it comes to 'grand corruption'.[60]

However, although some of the indicators and so-called 'red flags' for greed or need may be well-defined and detectable, it must at the same time be emphasized that the aspect of motivations behind fraud and corruption can be extremely complex.[61] For auditors wishing to prevent and detect fraud and corruption, it may therefore be even more effective to focus on the opportunity element, as this is something which managers and those entrusted with governance can influence to a much a higher degree than they can with motivation.

2.2.2 Opportunity:

In principle, almost any condition can provide opportunities to commit fraud and corruption.[62] Among other things, opportunity reflects on the one hand the extent of authority that government officials, managers and employees have been entrusted with, and the degree of access they have to assets, information and/or systems.[63] On the other hand, opportunity is also a function of the likelihood of detection and the clarity and strictness of rules and policies regarding acceptable behavior.[64] Furthermore, change – whether it is changes in personnel, technical changes, changes in location, etc. – can also provide opportunities for fraud and corruption as it often may give rise to confusion. So is the case with long-term stability, as it can result in complacency.[65]

In general, these opportunities are typically dealt with through internal controls.[66] Consequently, to investigate the opportunity element within particular organizations and sectors, auditors also must focus on internal controls – or the lack thereof. More specifically, auditors must check for weaknesses with regard to, inter alia, ethics/code of conduct, 'tone at the top', human resource policies and practices, segregation of duties, controls over access to resources and records, records management, etc., as described in, for instance, INTOSAI GOV 9100.[67, 68]

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[58] ISSAI 1240, p. 222.
[59] UNODC, 2004, pp. 14-15.
[60] UNDP, 2008, pp. 9, 60.
[61] Jones, Peter, 2004. Fraud and corruption in public services: a guide to risk and prevention, Gower Publishing Limited, England, pp. 2-3.
[62] Jones, 2004, p. 3.
[63] The Fraud Triangle and What You Can Do About It, p. 69.
[64] CIMA, 2008, p. 13.
[65] Jones, 2004, p. 3.
[66] Wells, Joseph T., 2001. Why Employees Commit Fraud. It's either greed or need. [Online] Available at www.acfe.com/resources/view.asp?ArticleID=41 [Accessed on 20 January 2011].
[67] INTOSAI GOV 9100 Guidelines for Internal Control Standards for the Public Sector. [Online] Available at www.issai.org/media(574,1033)/INTOSAI_GOV_9100_E.pdf [Accessed on 21 January 2011].
[68] These elements will be further accounted for in chapter 4.

As to opportunity on the governance level, this also must be addressed through proper 'checks and balances' as provided for in internal control systems, but the content of the control systems at this level is different in many respects. Basically, opportunity and abuse of power at the governance level is addressed through a system of 'horizontal accountability', that is, a dispersion of power between the different agencies and branches of government. Together, these agencies and branches constitute the 'pillars' of the so-called 'National Integrity System' (NIS). The ultimate goal of this system is to prevent fraud and corruption from taking place by increasing the risks and decreasing the returns involved. Some of the key institutional pillars of this system are the Legislature, the Executive, the Judiciary, the Auditor-General, other 'Watchdog' Agencies, the Media, etc. In addition to the pillars themselves, another important part of the NIS is the core rules and practices which are employed by or underpins the various agencies.[69] As the most usual pillars most likely are in place in most countries around the world – albeit to a varying extent – the rules and practices part of NIS is probably the most important for auditors. That is, when investigating the opportunities for fraud and corruption at the governance level, auditors should focus on whether the 'toolkit' each of these institutions and agencies has at their disposal is sufficient to maintain their integrity and to be effective.[70]

2.2.3 Rationalization or attitude:

Lower salary levels in the public sector compared with the private sector can lead to the justification of fraudulent and corrupt acts among public sector employees.[71] Depending on how close the salary level is to the poverty line, this also must be seen in connection with the question of need, mentioned under 2.2.1 above. At the same time, however, there is no clear evidence that increasing wages in the public sector is sufficient to reduce fraud and corruption. The existence of 'grand corruption' and 'kleptocracies', among other things, also supports this finding.[72]

Other factors that may demoralize public sector employees and lead to the rationalization of fraud and corruption are, inter alia, career advancements which are unconnected to merit and performance, inadequate and delayed budgets, insufficient supplies and equipment, and the lack of a clear and shared purpose for the organization in question.[73] Another rationalization might be that the employee in question considers the fraudulent or corrupt act as 'harmless' because the damage caused is so small compared to the size of the organization and its resources.[74]

The 'everyone-else-is-doing-it'-syndrome, i.e. where an ethos tolerant of fraud and corruption has been entrenched as a cultural norm in large parts of the organization, may be a particularly serious risk factor as it tends to be very difficult to reverse.[75] This is also closely linked to the issue of 'peer pressure', that is, where honest employees who recognize the wrongdoings of others are unable to prevent it because of too much pressure from their colleagues.[76]

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[69] Pope, Jeremy, 2000, pp. 32-37.
[70] The elements of NIS will be further accounted for in subchapter 3.2.
[71] ISSAI 1240, p. 222.
[72] Pope, 2000, pp. 9-10.
[73] World Bank, 1997, p. 12.
[74] CIMA, 2008, p. 13.
[75] Jones, 2004, p. 3; UNODC, 2004, p. 244.
[76] Jones, 2004, p. 3.

Furthermore, these risk factors may be further exacerbated if it is the senior officials or political leadership in the organization who 'lead the way' when it comes to abuse of power for private or political gain.[77] Among other things, these risk factors are closely related to the elements of internal control relating to ethics and 'tone at the top'. Both elements are among those auditors should check for weaknesses when investigating the opportunity element within particular organizations and sectors.[78]

Finally, the most favourable climate for rationalization is probably found when fraud and corruption are *endemic* or *systemic*. These terms are used to describe a situation where fraud and corruption are fundamental features of a society, pervading its entire political, economic and social system. In such a situation, corrupt individuals and groups are usually dominating and using the most important institutions and means of the state, and, due to lack of alternatives, most people are forced to deal with corrupt officials.[79]

2.3 FRAUD AND CORRUPTION IN ENVIRONMENTAL AND NATURAL RESOURCE MANAGEMENT – FEATURES, TRENDS AND IMPACTS

A fundamental aspect of many environmental goods – whether it concerns land, air, water, forests, minerals, fisheries, wildlife, etc. – is that many of these, in principle, are 'common-pool' resources. These are resources where there is a rivalry in consumption at the same time as it is impracticable or difficult to prevent users from accessing them. This often leads to problems of 'collective action' as individuals or corporations utilize these resources to fulfil their needs. As these actions aggregate, the environmental and natural resource (renewable and non-renewable) capacity of a country – and of the world – comes under pressure. Conservation and sustainable management measures are therefore adopted with the aim of preventing people and businesses from depleting natural resources and abusing the environment.[80]

Through fraud and corruption, however, individuals and corporations are able to circumvent the regimes and regulations in question, thereby overusing resources and degrading the environment. Depending on the level of government and the stage in the value chain, many different forms of fraud and corruption may be used to avoid regulations or to stop them from being adopted and implemented in the first place. Furthermore, in the exploitation of natural resources, many of the various forms of fraud and corruption involved may also often be overlapping.[81]

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[77] World Bank, 1997, p. 12.
[78] These two elements will be further elaborated in subchapters 4.1 and 4.2 respectively.
[79] Source: Corruption glossary, U4 Anti-Corruption Resource Centre. [Online] Available at www.u4.no/document/glossary.cfm [Accessed on 26 January 2011].
[80] UNDP, 2008, p. 91; Transparency International, 2007. Corruption and Renewable Natural Resources, Working Paper # 01/2007. [Online] Available at www.transparency.org/publications/publications/working_papers/wp1_2007_corruption_renewable_resources [Accessed on 21 March 2011], p. 2.
[81] UNDP, 2008, p. 91; Transparency International, 2007, p. 2; Dillon et al., 2006. Corruption & The Environment. A project for: Transparency International. Environmental Science and Policy Workshop. Columbia University, School of International & Public Affairs, April 2006. [Online] Available at www.columbia.edu/cu/mpaenvironment/pages/projects/spring2006/Transparency%20International%20final%20report.pdf [Accessed on 16 March 2011], p. 14.

Put simply, fraud and corruption in the environmental and natural resource sector is to some extent a result of the conflict between private interests in the profits from natural resource exploitation and reduced production costs – inter alia by using cheaper and lesser environmentally friendly technologies – on the one hand, and the public interest in a healthy environment on the other.[82] Below, this conflict of interests will be further elaborated through three different perspectives: 1. The 'fraud triangle'; 2. Common trends with regard to fraud and corruption in environmental and natural resource management; 3. The impacts of fraud and corruption in the environmental and natural resource sectors.

2.3.1 The 'fraud triangle' and environmental and natural resource management

Taking the 'fraud triangle' as our point of departure, some of the particular features of natural resources and the environment in relation to fraud and corruption can be described as follows:

Incentive/pressure:

As a source of much wealth in the form of environmental services (e.g. as sink for pollution) and natural resources, the environment is a natural object for fraud and corruption. Natural resources often have high commercial value and the large amounts of formal and informal revenues which can be generated through their exploitation provide a lot of incentives for fraudulent and corrupt behaviour. Such revenues – and incentives – can be present in all stages of the value chain. That is, from the allocation and distribution of resources and licenses – which can generate so-called 'rent-seeking' behavior – to the extraction and management phase. It also must be emphasized that it is not only where natural resources are abundant that there may be fertile ground for fraud and corruption – this can also happen when resources are scarce. Such limited resources can both comprise resources which are vital and essential for people – such as water – and rare species of animals and plants which can create lucrative 'black markets'. Furthermore, in addition to public officials who are tempted to 'fill their own pockets' by illegally providing access to such resources and/or selling them to the highest bidder, access to natural recourse rents can also give governments and politicians incentives to stay in power through paying off political supporters.[83]

Opportunity:

One central aspect of the environmental and natural resource sectors is the technical complexity involved in the regulation and management of these sectors. This complexity is present in all processes, that is, in regulation, licencing, exploration, monitoring, distribution, sale, reporting, ect. As a consequence, except from a few 'insiders', most people do not fully comprenhend how these sectors actually work. This results in informational imbalances which limit oversight and transparency, and which provide many entry points for manipulation, fraud and corruption for those who control the processes and have the proper knowledge.[84]

[82] Winbourne, Svetlana, 2002. Corruption and the Environment. Management Systems International. November 2002. [Online] Available at http://pdf.usaid.gov/pdf_docs/PNACT876.pdf [Accessed on 17 March 2011], p. 6.
[83] Dillon et al., 2006, p. 9; Mock, 2003, p. 2; Winbourne, 2002, p. 7; Kolstad, Ivar; Søreide, Tina and Williams, Aled, 2008. Corruption in natural resource management – an introduction. U4 Brief. Chr. Michelsen Institute. February 2008 – No. 2. [Online] Available at www.cmi.no/publications/file/2936-corruption-in-natural-resource-management-an.pdf [Accessed on 22 March 2011]; UNDP (2008), p. 91.
[84] Gillies, Alexandra, 2010. Fuelling Transparency and Accountability in the Natural Resources and Energy Markets. Conference Paper prepared for the 14th International Anti-Corruption Conference. 10-13 November 2010 - Bangkok, Thailand. [Online] Available at http://14iacc.org/wp-

Another feature of the environmental and natural resource sectors in relation to fraud and corruption, is that the risk of being caught often is low. In many cases, the exploitation of natural resources – and, possibly, the environmental degradation – takes place in remote locations, far from the centres of government, public oversight and scrutiny by the media. In addition, the areas in question may also be sparsely populated and physically vast. Furthermore, as much of the natural resources are being extracted or exploited for the purpose of export, these commodities are frequently traded via complex routes, which also involves smuggling. Hence, it is quite common that fraud and corruption in the environmental and natural sectors transcend national borders. This makes monitoring – both of the exploitation itself and of possible collusion between companies and public officials – difficult.[85]

Thirdly, in many countries the people who are the primary vicitims of the resource depletion, environmental degradation and/or economic losses caused by fraud and corruption are often the rural poor, who generally have little power and influence and therefore seldom pose a political threat to those people in government who abuse their office.[86]

Rationalization/attitude:

When it comes to rationalization of fraud and corruption in the environmental and natural resource sectors in particular – in addition to the generic factors described above, such as low salaries, unmerited career advancements, 'peer pressure', etc. – another aspect might be that the environment quite often are given lower priority when important political or economic decisions are made in other places. One possible consequence of this, among other things, is that the penalties for infringements in these sectors often are small compared to the potential profits. Another possible consequence is that the market prices for some natural resources – especially the ecosystem services they provide – are lacking, which makes fraudulent and corrupt behavior 'low cost'.[87] Furthermore, where monitoring is lacking and the people most affected by fraud and corruption are poor and powerless – as mentioned above - these effects are probably exacerbated. Also, where environmental standards in reality are unattainable because businesses do not have sufficient resources and/or the proper technology to fulfil these standards, and the relevant regulations have not taken this into account, fraudulent and corrupt acts may also be easier to justify.[88]

content/uploads/AlexandraGillesNaturalResourcesIACC.pdf [Accessed on 30 March 2011], p. 2; Mock, 2003, p. 2;

[85] Mock, 2003, p. 2; UNDP, 2008, pp. 91, 96, 104; Dillon et al., 2006, pp. 26-27.

[86] Mock, 2003, p. 2; UNDP, 2008, p. 91

[87] Dillon et al., 2006, pp. 9, 14; Mock, 2003, p. 2; UNDP, 2008, p. 91; Winbourne, 2002, p. 9.

[88] Winbourne, 2002, p. 15.

2.3.2 Fraud and corruption in environmental and natural resource management – common trends[89]

Weaknesses in governance systems prevents good governance and foster fraud and corruption in the environmental and natural resource sectors[90]

In countries where there is a concentration of power and the proper 'checks and balances' are lacking because the relevant institutions[91] are weak, environmental governance also tends to be inadequate. If, for instance, the legislative and judicial branches of government are corrupt themselves or they are weakened by a corrupt executive branch, they may be unwilling or incapable to hold companies liable for the environmental degradation – and associated social and environmental costs – they have caused. This can soon turn out to be a vicious circle: To the extent that companies or businesses are not held accountable for the harmful impacts of their actitivities in the first round, the lesser the likelihood that they will take into account these impacts in the second.[92]

One of the most fundamental factors when it comes to weak governance and lack of accountability in the environmental and natural resource sectors is transparency, or more correctly – the lack thereof. As access to information may be considered as a threat to their control, the people in power may feel a strong impetus to prevent or restrict this access. This again may lead to impunity and decisions which are contrary to the public interest. Another factor which also is closely related to weak governance, are insufficient laws and regulations. Among other things, 'loopholes' in the legislation may both give room for very wide interpretations and provide public officials with broad authority. This weakens oversight and accountability. Furthermore, where the insufficiencies also include laws which pertain to lobbying and financial disclosure, this may give wealthy external interests disproportionate influence when important decisions are made.[93]

Hence, the level of fraud and corruption in the management of environmental and natural resources is not only a product of the wealth which these resources offer, but also a result of the governance systems in place to manage these resources.[94]

Countries which are dependent on natural resource exploitation are more prone to high levels of fraud and corruption, and – consequently – weak environmental governance

There are many examples showing that countries with economies that are heavily dependent on the exploitation of natural resources tend to be more vulnerable to fraud and corruption than others. This is not always the case, but economic activities in these sectors have some features which may facilitate fraudulent and corrupt practices, for instance the act of rent-seeking and a close link between control of resources and political power. Particularly in developing countries, if there is an abundance of natural resources on the one hand, and little alternative economic incentives on the other, it can be difficult to avoid dependency on these

[89] The structure and content of this subchapter are first and foremost based on chapter 5 in Dillon et al., 2006. "Common Trends in Corruption and Environmental Degradation", pp. 39-42. This chapter is a summary of findings from various case studies on corruption and the environment.
[90] This will be further addressed in subchapter 3.2.
[91] See subchapter 2.2.2 and 3.2.
[92] Dillon et al., 2006, p. 40.
[93] Dillon et al., 2006, p. 40; Winbourne, 2002, pp. 12-15.
[94] Kolstad, Søreide and Williams, 2008, p. 2.

resources when trying to foster development. At the same time, it may also be difficult to offer favourable conditions for alternative industries. The lack of economic diversification which may result, combined with a lack of transparency makes poor countries vulnerable to exploitation – both by politicians and government officials who aim at sustaining or strengthening their power and by external companies willing to 'jump the queue' to maximize their profits from foreign resources.[95]

The countries in question are often associated with the term 'the resource curse', also known as 'the paradox of plenty'. These terms refer to the well documented phenomenon that the economic growth in countries with plenty of natural resources on average is slower than in countries without such resources. This inverse relationship between resources and growth is especially associated with so-called 'point source' resources such as minerals and petroleum.[96] A central element here is another inverse relationship, that is, between the extent of control of natural resources, on the one hand, and the level of domestic taxation on the other. Revenues from the exploitation of natural resources reduce or remove the incentives for establishing separate tax systems or raise domestic taxes. In other words, governments who control such revenues have little or no need to tax their own people. Thereby another source of accountability between governments and citizens is eliminated, as the need of the former to satisfy the demands and the scrutiny of the latter, i.e. the taxpayers, is greatly reduced.[97]

State controlled or privately controlled monopolies provide opportunities for fraud and corruption within the environmental and resource sectors

This is closely related to the two trends described above, and refers to situations where the state or private companies have excessive discretion over natural resources. In contrast to most other industries, which are characterized by open markets and many players, the exploitation of many natural resources has a tendency of being centralized. And the resources are quite often controlled by the state, which – as already mentioned – can provide politicians and officials at the highest levels with undue influence and access to revenues. Where state monopolies exist – and transparency and 'checks and balances' are lacking – this may create favourable conditions for favouritism based on family ties or friendship, also referred to as 'cronyism' or 'patronage'.[98] Furthermore, monopolies also undermine the 'watchdog role' that competition between businesses can play with regard to fraud and corruption, i.e. that competitors will be looking out for unjust practices or exploit inefficiencies caused by corruption.[99]

Fraud and corruption within the environmental and natural resource sectors is particularly common where there is low economic development

Fraud and corruption is not an unavoidable result of poverty – rather, it is among the factors which limit development. Furthermore, empirical studies indicate that environmental

[95] Dillon et al., 2006, pp. 41-42. See also Winbourne, 2002, p. 7; Transparency International, 2007, p. 2.
[96] Karl, Terry Lynn, 2005. Understanding the Resource Curse, pp. 21-23, in: Tsalik, Svetlana and Schiffrin, Anya (eds.), 2005. Covering Oil: A Reporter's Guide to Energy and Development. Revenue Watch/Open Society Institute. Initiative for Policy Dialogue. [Online] Available at www.revenuewatch.org/files/covering-oil-072305.pdf [Accessed on 29 March 2011]; Kolstad, Ivar, 2007. The Resource Curse: Which Institutions Matter?, WP 2007:2. Chr. Michelsen Institute (CMI). [Online] www.cmi.no/publications/file/2678-the-resource-curse-which-institutions-matter.pdf [Accessed on 29 March 2011], p. 1.
[97] Gillies, 2010, p. 2; Karl, 2005, p. 24.
[98] See also subchapter 2.1.4.
[99] UNDP, 2008, p. 91; Gillies, 2010, p. 2; Dillon et al., 2006, p. 41.

performance has a tendency of being stronger in countries where the levels of GDP per capita are higher. The relationship between fraud and corruption and poverty, on the one hand, and between poverty and environmental performance, on the other, suggest that the probability of ecological degradation increases where there are negative synergies between fraud and corruption and poverty. Hence, despite the fact that fraud and corruption, and poor environmental performance is prevalent all over the world, it has a tendency of being particularly common in lesser developed countries.[100] In developing countries and countries in transition, environmental issues are typically placed very low on the national policy agenda as economic and social difficulties often have a higher priority. As a consequence, the challenges posed by fraud and corruption in the environmental and natural resource sectors are seldom in focus and these sectors are also given low priority in the anti-corruption efforts of both the countries in question and of international organizations.[101]

Another aspect of this is that, in many countries, governmental programmes in the environmental and natural resource sectors are underfunded due to insufficient national or local budgets. To supplement the budgets public agencies are then allowed to engage in various commercial activities such as logging, construction, banking etc. By doing this, the government paves the way for fraud and corruption and financial abuses due to a blurring of the roles of the public and the private sectors and frequent conflicts of interests. For one thing, direct participation in the marketplace through state-owned companies may weaken the willingness of the government to adopt fair regulations. Furthermore, government officials may also often have direct or indirect interests in the same firms as they provide with financial or other support, or business opportunities.[102]

The extent of fraud and and corruption and illegal activities – and consequent environmental degradation – is often linked to export partners' demand for natural resources

In general, fraud and corruption flourishes when there is a market for goods that can be provided through this kind of activities. Hence, although fraud and corruption and poor environmental performance has a tendency of being especially prevalent in lesser developed countries, as mentioned above, such practices are often facilitated through the trade relations between these countries and developed countries. The more importance the latter attaches to transparent practices, the less the chance that the former – i.e. the supplier of the goods – can carry out fraudulent and corrupt activities. Consequently, for better or worse, the governments and private companies in developed countries also have an important role to play when it comes to the management of the environment and natural resources in developing countries. For instance, by entering into trade partnerships with countries which export illegal animal, timber or forest products, etc., developed country governments also become involved in such practices.[103]

Furthermore, although donor countries in principle intend to play a constructive role in (potential) recipient countries when it comes to promoting good governance, transparency, integrity, etc., they do not necessarily have sufficient levers to make a substantial change. First, because the revenues from natural resource exploitation often are much larger than

[100] Dillon et al., 2006, p. 39.
[101] Winbourne, 2002, p. 9.
[102] Winbourne, 2002, p. 12; Gillies, 2010, p. 2.
[103] Dillon et al., 2006, p. 41

international development assistance budgets, and secondly because many donor countries also are dependent on importing natural resources from developing countries.[104]

Although fraud and corruption is common across a wide variety of political systems, it is most pervasive in countries where democracy is weak

Despite that democracies probably provide the best institutional framework for transparency and accountability in government and among elected representatives, democracies are also vulnerable to fraud and corruption. Still, fraud and corruption in the environmental and natural resource sectors seems to be most severe in countries where traditions of democracy are weak or in newly democratized countries.[105]

2.3.3 The impacts of fraud and corruption in the environmental and natural resource sectors

As mentioned in subchapter 2.1.2, by their nature, fraud and corruption are often – but not always – concealed activities. It is therefore difficult to measure directly the impact of fraud and corruption both on society in general[106], and on the environment in particular.[107] The lack of reliable statistics and systematic documentation of fraud and corruption committed by government officials or businesses makes such measuring even more challenging.[108] Hence, the extent and impact of fraud and corruption is therefore often measured *in*directly, through various indices such as Transparency International's "Corruption Perception Index" (CPI) and "Global Corruption Barometer", and the World Bank's "Control of Corruption Index" (CCI). These indices are based on perceptions of fraud and corruption, and/or direct experiences with it, and/or observed data.[109]

When it comes to the costs of fraud and corruption on the environmental and natural resource sectors in particular, the number of empirical studies has so far been quite limited.[110] One way to establish – and measure – the link between fraud and corruption, on the one hand, and environmental performance on the other, however, is to combine indices for the former with indices for the latter. This was done in 2001, when researchers for the first time drew attention to the very high correlation between the two, that is, the higher the degree of fraud and corruption in a country, the lower the degree of environmental sustainability.[111] More specifically, this was done by combining the Environmental Sustainability Index (ESI) developed for the World Economic Forum with the CCI. Although corruption was only one of the 67 variables in the ESI, with a correlation factor of -0,75 it was the variable which most strongly correlated with the overall ESI. Furthermore, corruption also had a high correlation with many of the more specific environmental indicators in the ESI.[112] In addition, although

[104] Gillies, 2010, p. 2.
[105] Dillon et al., 2006, p. 39. For a discussion of fraud and corruption and democracy, see, among others, UNDP, 2008, pp. 25-28.
[106] UNDP, 2008, p. 24; Mock, 2003, p. 1.
[107] Winbourne, 2002 p. 5; Transparency International, 2007, p. 2.
[108] Mock, 2003, p. 1; Winbourne, 2002, p. 8.
[109] UNDP, 2008, pp. 24-25; Mock, 2003, p. 1.
[110] Winbourne, 2002, p. 8; Dillon et al., 2006, pp. 9-10; Transparency International, 2007, p. 2.
[111] Winbourne, 2002, p. 8
[112] Levy, Marc, 2001. Corruption and the 2001 Environmental Sustainability Index, pp. 300-302, in: Hodess, Robin (ed.), 2001. Global Corruption Report 2001. Transparency International. [Online] Available at www.transparency.org/publications/gcr/gcr_2001#download [Accessed on 17 March 2011].

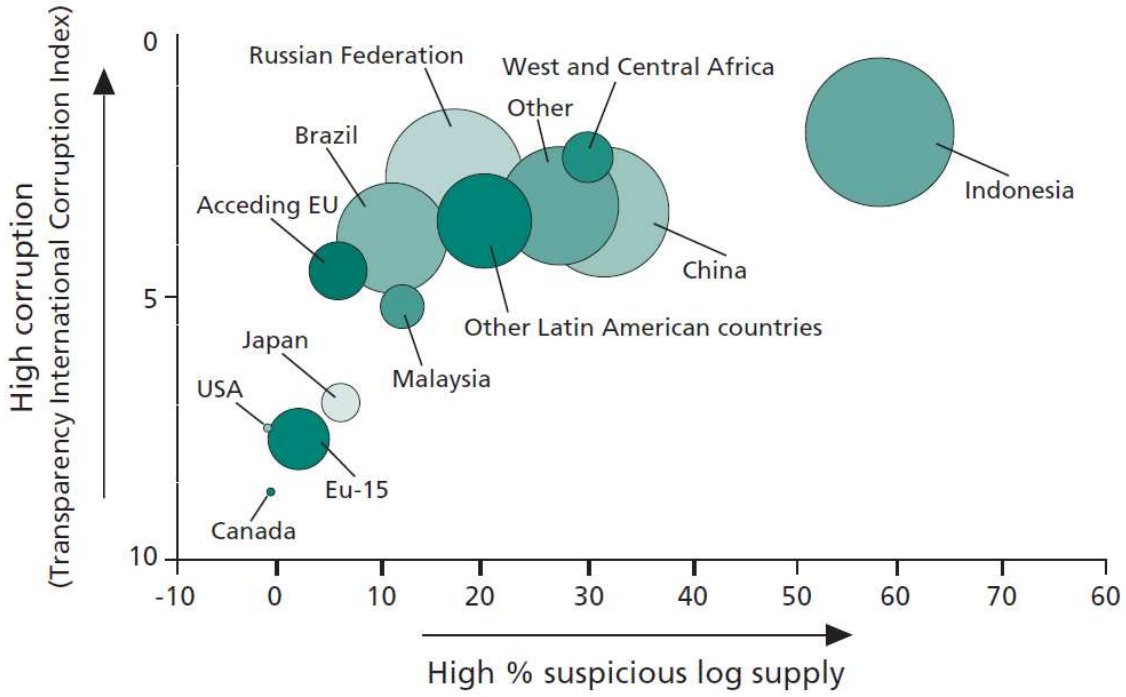
the link between fraud and corruption and environmental degradation/natural resource depletion is far from straightforward and can be difficult to quantify, there is now a growing body of evidence which clearly indicates that the magnitude of the problem is substantial.[113]

Below, we will present some examples from various sectors within the INTOSAI WGEA portfolio to illustrate the potential impacts of fraud and corruption in the environmental and natural resource sectors.

Forestry:

According to the Environmental Investigation Agency (EIA) and Telapak Indonesia, 'black market timber' constitute at least 50 percent of the total global timber trade, amounting to billions of US dollars each year. Furthermore, EIA/Telepak also makes it clear that corruption is a key factor when it comes to illegal logging.[114] The link between fraud and corruption and illegal logging is also supported in reports by, inter alia, the UN Food and Agriculture Organization (FAO), the World Resources Institute (WRI), and the UNDP.[115] Figure 2.4 illustrates the correlation between corruption and illegal logging on the global level.

Figure 2.4 Relationship between corruption and suspected illegal forest activities



Source:
FAO,2005. Forestry Paper 145. Food and Agriculture Organization of the United Nations/International Tropical Timber Organization. [Online] Available at www.fao.org/docrep/008/a0146e/a0146e00.htm [Accessed on 4 April 2011], p. 13. Note: Bubble size represents the volume of suspect roundwood, including imports.

[113] Mock, 2003, p. 2; Kolstad, Søreide and Williams, 2008, p. 2.
[114] Environmental Investigation Agency/Telapak Indonesia, 2001. Timber Trafficking. Illegal Logging in Indonesia, South East Asia and International Consumption of Illegally Sourced Timber, September. [Online] Available at www.eia-international.org/files/reports26-1.pdf [Accessed on 4 April 2011], pp. 5, 21-22.
[115] FAO, 2005. Forestry Paper 145. Food and Agriculture Organization of the United Nations/International Tropical Timber Organization. [Online] Available at www.fao.org/docrep/008/a0146e/a0146e00.htm [Accessed on 4 April 2011], pp. 10-14; Mock, 2003, p. 2; UNDP, 2008, p. 95.

Due to the low risks of getting caught and the high profits involved – the prices per cubic metre for some sorts of timber can reach up to USD 500 – forests in the Amazon, in West and Central Africa and in East Asia are all threatened by illegal logging.[116] According to studies presented by the World Resources Institute, approximately 80 per cent – 25,5 million cubic meters – of all the timber harvested in Brazil in 2000 was illegal. Furthermore, in Indonesia, the percentage of illegal logging has been estimated to range from 50 to 70 percent, and in Russia it is believed to be at least 20 percent in total, and up to 50 percent in some parts of the country.[117] This last estimate also applies to Cameroon, according to the EIA. Three of these countries are among the largest suppliers of tropical timber in the world.[118] Hence, at the same time as the forest cover in developed countries has had a slight increase since 1980, it has declined in developing countries by approximately 10 per cent.[119]

According to EIA/Telapak, the Asia-Pacific region as a whole had lost 88 per cent of its original frontier forest area in 2001. In the same year, EIA reported that the Philippines had experienced a reduction in their natural forest from 16 million to only 700.000 hectares, and that the forest cover in Laos had dropped from 70 to less than 40 per cent of the land area since 1940. In both countries a large part of the reduction in forest cover is attributable to illegal logging.[120] According to a UNEP study, more recent estimates for Indonesia suggest that 98 per cent of the natural rain forest may be destroyed by 2022, and that the lowland forests may be destroyed even sooner than this.[121]

According to the World Bank, more than 10 billion USD in assets and revenues are lost each year due to illegal logging, which is more than six times the total amount which is used for sustainable forest management through official development assistance. In addition, 5 billion USD is estimated to be lost each year due to uncollected royalties and taxes from legal logging. Another effect of fraud and corruption and illegal logging is that people are deprived of their livelihoods. The World Bank points out that illegal logging and exploitation of timber and non-timber products threatens the livelihood and security of as many as 350 million people who live in and around forests in the developing countries.[122] In South East Asia, this 'industry' has already forced away hundreds of thousands of people from their homes according to EIA/Telepak.[123]

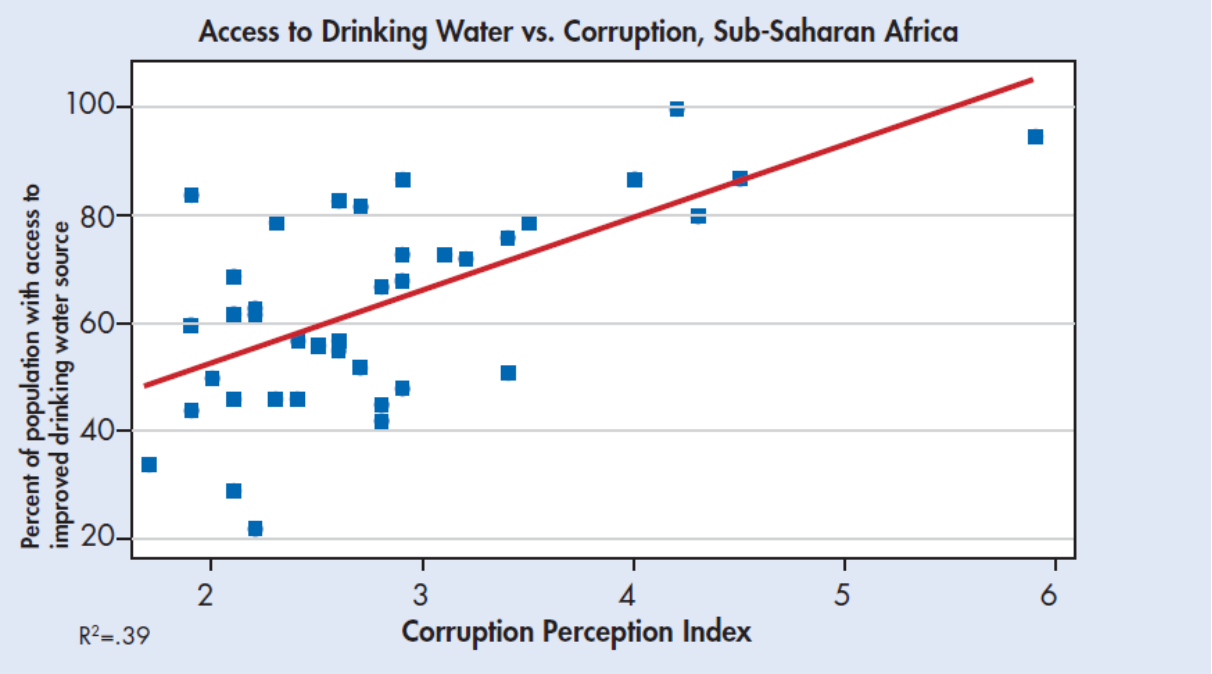
Water:

Water is a vital resource without any substitutes. Still, billions of people in many regions around the world today are experiencing a water crisis which threatens their health, lives and livelihoods. According to Transparency International's Global Corruption Report 2008 (GCR

[116] EIA, 2008. Environmental crime. A threat to our future. October 2008. [Online] Available at http://www.eia-international.org/files/reports171-1.pdf [Accessed on 5 April 2011], p. 6; UNDP, 2008, p. 95.
[117] Mock, 2003, p. 2
[118] EIA/Telapak, 2001, p. 1.
[119] UNDP, 2008. p. 94
[120] EIA/Telapak, 2001. pp. 6, 9.
[121] Nellemann, C., Miles, L., Kaltenborn, B. P., Virtue, M., and Ahlenius, H. (Eds), 2007. The last stand of the orangutan – State of emergency: Illegal logging, fire and palm oil in Indonesia's national parks. United Nations Environment Programme. GRID-Arendal. Norway[Online] Available at www.grida.no/files/publications/orangutan-full.pdf [Accessed on 4 April 2011], p. 43.
[122] The World Bank, 2006. Strengthening Forest Law Enforcement and Governance. Addressing a Systemic Constraint to Sustainable Development. Report No. 36638-GLB. August 2006. [Online] Available at http://siteresources.worldbank.org/INTFORESTS/Resources/ForestLawFINAL_HI_RES_9_27_06_FINAL_web.pdf [Accessed on 4 April 2011], pp. 1-2.
[123] EIA/Telapak, 2001, p. 2.

2008), there are almost 1.2 billion people around the world who are without guaranteed access to water and the number exceeds 2.6 billion for those who lack adequate sanitation. As a consequence, about 80 per cent of health problems in developing countries can be traced back to inadequate water and sanitation. In this connection, the UN reports that more than five million people around the world die each year due to lack of access to safe water. Furthermore, agriculture is the most important sector for employment for the 2.5 billion people who live in low-income countries, and the sector also consumes 70 per cent of the world's water resources. Lack of access to water therefore also seriously affects the value of land and the potential for livelihood. Naturally then, this has very detrimental impacts on development and poverty reduction in many countries. Water-based ecosystems are already regarded as the most degraded natural resource in the world, and the competition for water resources is expected to become even stronger in the coming decades.[124]

Figure 2.5 Relationship between corruption and access to drinking water in Sub-Saharan Africa



Source:
Stålgren, P., 2006. Corruption in the Water Sector: Causes, Consequences and Potential Reform. Swedish Water House Policy Brief Nr. 4. SIWI. [Online] Available at www.siwi.org/documents/Resources/Policy_Briefs/PB5_Corruption_in_the_water_sector_2006.pdf [Accessed on 5 April 2011], p. 5. [NB reproduction in the final draft requires permission from Stockholm International Water Institute]

Transparency International and the Stockholm International Water Institute, among others, point out that this global water crisis first and foremost is a crisis of water governance, and fraud and corruption is at the core of this crisis. Although the extent differs a lot across the

[124] Zinnbauer, Dieter and Dobson, Rebecca (eds.), 2008. Global Corruption Report 2008. Corruption in the Water Sector. Transparency International. [Online] Available at www.transparency.org/publications/gcr/gcr_2008 [Accessed on 5 April 2011], pp. xxiii, xxv; Stålgren, P., 2006. Corruption in the Water Sector: Causes, Consequences and Potential Reform. Swedish Water House Policy Brief Nr. 4. SIWI. [Online] Available at www.siwi.org/documents/Resources/Policy_Briefs/PB5_Corruption_in_the_water_sector_2006.pdf [Accessed on 5 April 2011], pp. 3, 11; UNDP, 2008, p. 94.

water sector and between various countries and governance systems, fraud and corruption is widespread and affects all aspects of this sector, from water resources management to drinking water services, irrigation and hydropower. Fraud and corruption in the water sector undermines development by scaring off investments, decreasing efficiency in the management of water resources and provision of services, and weakening the quality of public institutions.[125]

World Bank estimates indicate that between 20 % and 40 % of the funding to this sector is lost due to fraudulent and corrupt practices. Another study suggests that efficiency in water utilities in Africa would enhance by 64 % if they could operate within an environment free for fraud and corruption. Furthermore, considering the aim of raising USD 6.7 billion annually to the water and sanitation sector in Sub-Saharan Africa (SSA) to meet the Millenium Development Goals (MDG), and taking into account an average level of 30 % loss due to fraud and corruption[126], this would imply a potential loss over the next ten years of USD 20 billion.[127] Figure 2.5 illustrates that there is a correlation between corruption and access to improved drinking water in SSA. The higher the level of fraud and corruption in a country, the smaller the percentage of its citizens who have access to improved drinking water.

Another illustration of the problem is found in a case study from the water supply and sanitation sector in India. The study showed that 41 % of the customer respondents – to reduce their bills through falsification of the meter reading – had paid more than one small bribe during the last six months. Furthermore, 30 % of the respondents had paid more than one small bribe during the same period to speed up repair work, and 12 % had paid bribes to speed up connections to water and sanitation. According to the same study 50 % of the contractors within the water and sanitation sector had either paid kickbacks to public officials every time they signed a new contract or it was quite common for them to do it. The value of the kickbacks usually varied between 6 % and 11 % of the value of the contract.[128]

Finally, however, it also must be emphasized that fraud and corruption also affects the water sector in developed countries. In these countries, there are for instance substantial fraud and corruption risks involved in the awarding of contracts for the construction and operation of water infrastructure at the local level. For North America, Western Europe and Japan alone it is estimated that this market is worth USD 210 billion annually.[129]

Fisheries:

During the last few decades, as the fisheries sector has become both industrialized and globalized, fishing has developed into a multi-billion dollar business. Parallel to this, the world's total production from marine capture fisheries has peaked – in 2002 – and the proportion of overexploited, depleted or recovering stocks has increased from 10 % in 1974 to 32 % in 2008. This trend is partly due to so-called 'illegal, unregulated and unreported' (IUU) fishing, which has grown into a serious global problem. According to an estimate in 2002, the global trade in products from IUU-fishing amounted then to USD 9.5 billion. In addition to the huge revenue loss, IUU-fishing also threatens food security, in particular in the less developed regions of the world. Although fraud and corruption in the fisheries sector has yet

[125] Zinnbauer and Dobson, 2008, pp. xxiv-xxv; Stålgren, 2006, p. 3, 10.
[126] Based on the World Bank's estimated range of 20-40 %.
[127] Stålgren, 2006, pp. 3, 12.
[128] Stålgren, 2006, p. 7.
[129] Zinnbauer and Dobson, 2008, p. xxiv.

to be studied as closely and extensively as other natural resource sectors, there are good reasons to believe that IUU fishing also is facilitated by fraud and corruption, for instance when fisheries inspectors are ignoring violations of quotas and other regulations as a result of bribery. Both FAO and the U4 Anti-Corruption Resource Centre, among others, have also pointed to the lack of transparency as a critical factor in this sector, for instance when it comes to the negotiation of agreements on fisheries access and licensing decisions.[130]

An illustration of the possible challenges posed by fraud and corruption in the fisheries sector on the global level can be found when comparing figure 2.5 ("World Fisheries Hotspots (2004)") with figure 2.6 ("Control of Corruption (2004)"). As can be seen from these two figures, some of the largest marine fish catches in the world are also taken in areas where the control of corruption is weak or in need for improvement.

According to one study, the value of IUU-fishing in Africa was estimated to be approximately USD 1 billion per year in 2005. Two different cases, from West and East Africa respectively, illustrate the link between fraud and corruption and IUU-fishing on this continent. In the first case, the Ministry of Fisheries in Guinea became subject to an official audit in 2008 as a result of mounting pressure on the government. The audit revealed that the country had lost millions of euros in revenues due to large irregularities. Among other things, the audit revealed that a large number of fisheries licenses had been awarded without any corresponding records that these licenses actually had been paid for. In the second case, based on an investigation of violations of a United Nations embargo of Somalia, it was claimed by a UN Expert Panel that large amounts of revenues from commercial fisheries had been embezzled and funneled into private bank accounts or used to finance private militias.[131]

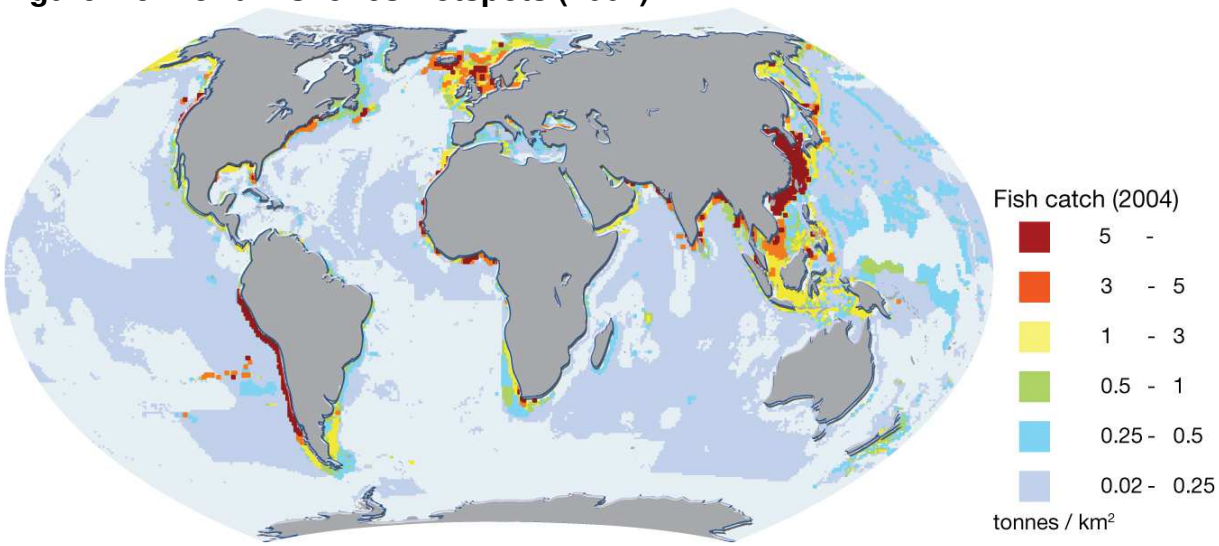
A similar case can be found in the Pacific region, where an audit carried out by the SAI of Solomon Islands revealed, among other things, that the country had lost several millions of USD in revenues due to, among other things, embezzlement, misappropriation and unpaid fees for fishing licenses. In this connection, it was also highlighted in the SAI report that bribery had reached systemic levels in parts of the fisheries administration.[132]

[130] Transparency International, 2007, pp. 3-4; FAO, 2010. The State of World Fisheries and Aquaculture 2010. [Online] Available at www.fao.org/docrep/013/i1820e/i1820e.pdf [Accessed on 11 April 2011], pp. 8, 105; UNDP, 2008, p. 94; Standing, André, 2008. Corruption and commercial fisheries in Africa. U4 Brief. Chr. Michelsen Institute. December 2008 – No. 23. [Online] Available at http://www.cmi.no/publications/file/3189-corruption-and-commercial-fisheries-in-africa.pdf [Accessed on 11 April 2011].

[131] Standing, André, 2008. Corruption and industrial fishing in Africa. U4 Issue 2008:7, Chr. Michelsen Institute. [Online] Available at www.cmi.no/publications/file/3188-corruption-and-industrial-fishing-in-africa.pdf [Accessed on 12 April 2011], pp. 8, 19.

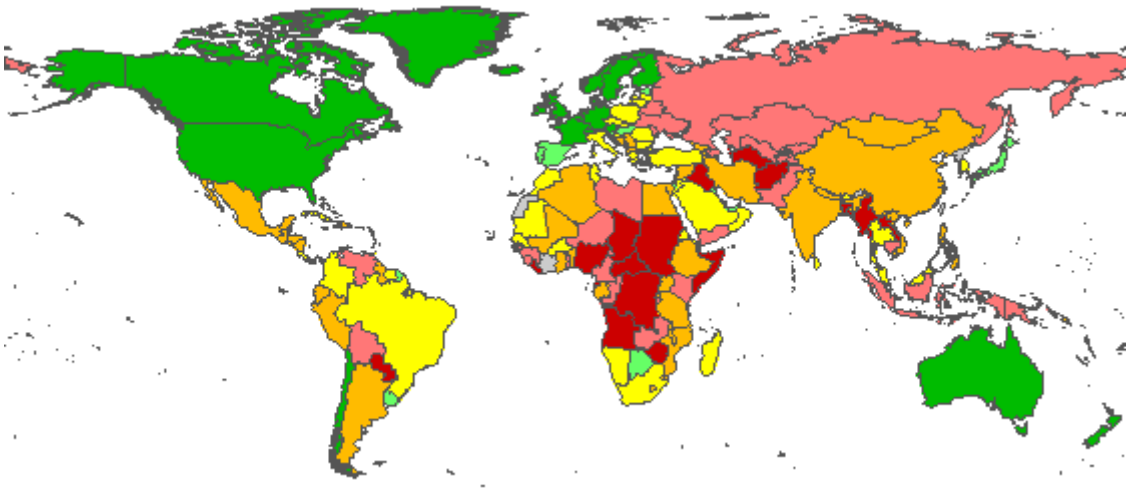
[132] Tsamenyi and Hanich, 2008, p. 10. See also Box 3.1 in subchapter 3.2.1.

Figure 2.5 World Fisheries Hotspots (2004)



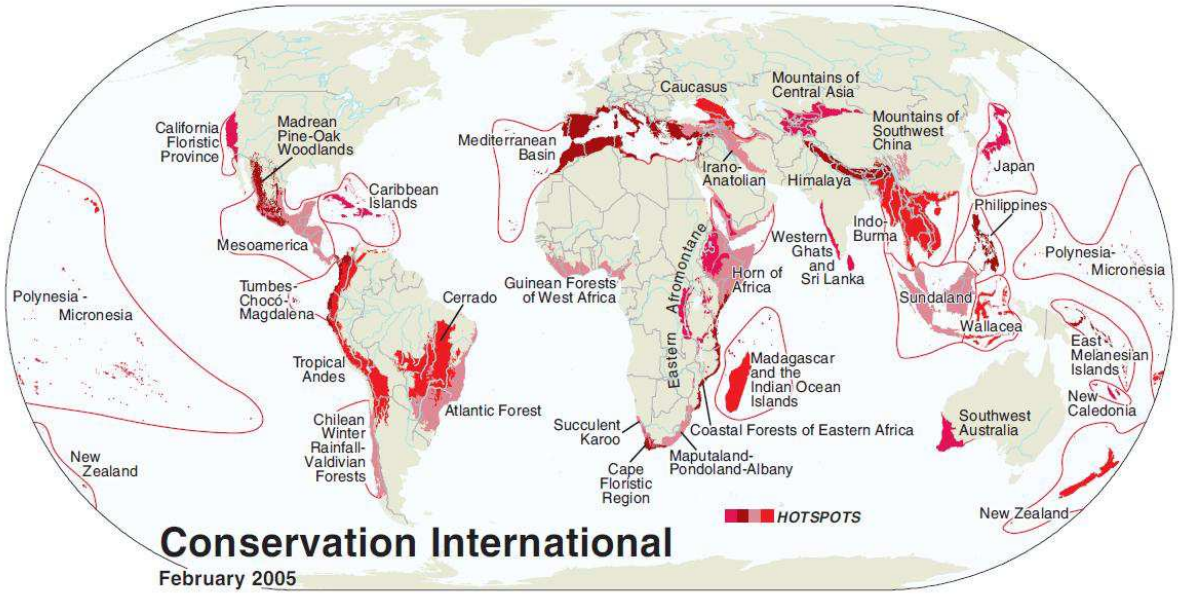
Source:
UNEP/GRID-Arendal, February 2008. World Fisheries Hotspots. UNEP/GRID-Arendal Maps and Graphics Library [Online] Available at http://maps.grida.no/go/graphic/world-fisheries-hotspots-2004 [Accessed on 5 April 2011]

Figure 2.6 Control of Corruption (2004)



Source:
The World Bank Group, 2010. Worldwide Governance Indicators, based on Kaufmann, Daniel; Kraay, Aart and Mastruzzi, Massimo, 2010. The Worldwide Governance Indicators: Methodology and Analytical Issues. [Online] Available at http://info.worldbank.org/governance/wgi/worldmap.asp# [Accessed on 5 April 2011].
[NB reproduction in the final draft requires permission from the World Bank Group]

Figure 2.7 World Biodiversity Hotspots (2005)



Source:
Conservation international, 2007.Biodiversity Hotspots. Conservation International Maps & GIS Data [Online] Available at www.biodiversityhotspots.org/xp/hotspots/resources/Pages/maps.aspx [Accessed on 5 April 2011]
[NB reproduction in the final draft requires permission from Conservation International]

Biodiversity:

Although both fraud and corruption and environmental degradation are worldwide problems, these two issues are particularly overlapping in the so-called 'biodiversity hotspots'[133]. These areas comprise the richest, but at the same time the most endangered diversity of animals and plants around the world. With a few exceptions, these 'hotspots' are mostly located in parts of the world where the levels of corruption are perceived to be moderate or high. An illustration of this can be found when comparing figure 2.6 ("Control of Corruption (2004)") with figure 2.7 ("World Biodiversity Hotspots (2005)"). As fraud and corruption has consequences for the environment, the impacts of fraudulent and corrupt practices can be particularly severe in the hotspots. The reasons for this are both that the ecosystems in question are particularly vulnerable to threats, and that degradation of the environment in these areas causes biodiversity losses which have global implications.[134]

In a study initiated by Transparency International, which focuses on five hotspots chosen from a total of thirty-four hotspots around the world[135], it is shown that the ecosystems in question are threatened by various economic activities such as mining, logging, dam construction, and hunting. Furthermore, it is also shown that fraud and corruption are present in all of these activities. Among these, illegal logging is among the activities where fraud and

[133] According to Conservation International, 'biodiversity hotspots' are areas which contain at least 1,500 species of vascular plants (more than 0.5 % of the world's total) as endemic species, or species that cannot be found in any other places in the world, and which have lost at least 70 % of its original habitat. Source: Dillon et al., 2006, p. 18.
[134] Dillon et al., 2006, p. 18.
[135] The five hotspots are the Tropical Andes, the Guinean Forest of West Africa, the Caucasus, Sundaland, and the Mountains of Southwest China.

corruption is most widespread, and it is also an activity which has devastating effects in respect of species loss and habitat destruction.[136]

According to a survey referred to in the EIA/Telapak report, of 200 areas of high biodiversity around the world almost two thirds were found to be threatened by illegal logging. At the same time EIA/Telapak also add that illegal logging is 'high impact logging', with no consideration for future sustainability, and that it has a disproportionate focus on protected forest areas.[137] This latter aspect is also confirmed by the UNEP-study, which points out that the decline in the supply of timber due to deforestation in turn leads to increased illegal logging in national parks, of which many risk serious degradation already during the next few years.[138] As a concrete example of species loss, the Transparency International study refers to the population of orangutans in Indonesia, which has shrinked by half during the last decade.[139] According to the UNEP-study, the orangutans at Borneo and Sumatra are now classified as Endangered or Critically Endangered species respectively by the World Conservation Union (IUCN).[140]

In addition to the ecological degradation caused by illegal logging and deforestation, biodiversity hotspots are also inter alia threatened by poaching of wild animals and illegal trade of endangered species. According to a report by the Wildlife trade monitoring network (TRAFFIC) and the World Wide Fund For Nature (WWF), the global legal trade in live animals and plants, and products and derivatives thereof was estimated to amount to roughly USD 15 billion per year early in the 1990s.[141] Although it is not possible to establish exactly how large share the illegal activities represent of the overall trade in wildlife products, this still gives an indication of the potential profits and, consequently, incentives for illegal trade and fraud and corruption. Of the illegal trade in wildlife products, timber is estimated to comprise approximately 65 %, followed by game and other food, forest products, animal products, and the trade in pets and decorative plants. Often, but not always, fraud and corruption in this area is driven by demand for illegal products in Western countries.[142] The problem is especially severe in Asia, which is hosting nine of the ten species which are most endangered. In this region, the demand for traditional medicines is one of the main forces behind the illegal trade in wildlife products.[143]

[136] Dillon et al., 2006, pp. 18-38.
[137] Environmental Investigation Agency/Telapak Indonesia, 2001, p. 5.
[138] Nellemann et al., 2007, p. 43.
[139] Dillon et al., 2006, p. 28.
[140] Nellemann et al., 2007, p. 9.
[141] WWF/TRAFFIC, 2002. Switching Channels. Wildlife trade routes into Europe and the UK. December 2002. [Online] Available at www.wwf.org.uk/filelibrary/pdf/switchingchannels.pdf [Accessed on 12 April 2011], p. 4.
[142] Dillon et al., 2006, p. 26.
[143] UNDP, 2008, pp. 95-96.

Chapter 3:
Fraud and corruption risk factors at the governance level

As described in chapter 2, fraud and corruption can take place at all levels of government – from public servants at the lowest level to government officials at the highest level. Furthermore, the challenges in respect of level and type of fraud and corruption may also vary a lot from country to country around the world. Consequently, these challenges also must be approached differently depending on the SAI in question. *'One size does not fit all.'* This also must be taken into account by auditors wishing to address fraud and corruption in the environmental and natural resource sectors as efficiently and effectively as possible.

Hence, with a particular focus on the 'opportunity'-element presented in subchapter 2.2.2, in this chapter some of the most important fraud and corruption risk factors that auditors should be aware of at the governance level will be presented, while chapter 4 will provide a similar presentation of some of the most important fraud and corruption risk factors at the sector/agency level.

This chapter consists of two main parts. In subchapter 3.1, the 'governance' concept is introduced, the aspect of poor governance in the environmental and natural resource sectors and the concept of governance indicators are briefly discussed, and the 'National Integrity System' (NIS) mentioned in subchapter 2.2.2 is introduced. In subchapter 3.2 the elements of NIS believed to be most relevant for public sector auditors will then be described further. In this connection, their relevance for the environmental and natural resource sectors will be illustrated with cases and examples, and various basic questions for auditors will also be suggested.

3.1 INTRODUCTION TO THE 'GOVERNANCE'-CONCEPT

As with 'fraud and corruption', the concept of 'governance' also has many facets, and there is a wide array of definitions. This is reflected in a comprehensive literature on the subject. As a fundamental point of departure, the World Bank defines "governance" as "the manner in which public officials and institutions acquire and exercise the authority to shape public policy and provide public goods and services".[144] More specifically, 'governance' can be divided into the following four dimensions:

- The processes by which governments are selected, monitored, renewed or replaced;
- The constitutional-legal framework for, and systems of interaction between the legislative, executive, and judicial branches of government;
- The capacity of government to provide and manage its resources, and implement public polices, in an efficient and effective manner;

[144] World Bank, 2007. Strengthening World Bank Group Engagement on Governance and Anticorruption, March 21, 2007, p. 1, Annex C in: Implementation Plan for Strengthening World Bank Group Engagement on Governance and Anticorruption, September 28, 2007. [Online] Available at http://siteresources.worldbank.org/PUBLICSECTORANDGOVERNANCE/Resources/GACIP.pdf [Accessed on 10 May 2011].

- The mechanisms of participation, and voice and exit, where citizens and groups define their interests, and make government accountable through interaction with those in authority and with each other.

Central attributes of *good* governance are, inter alia, transparency, accountability, capability, participation, efficiency, effectiveness, responsiveness, legitimacy and the rule of law. In addition, the political dimension is also an important part of the governance concept.[145]

Fraud and corruption is to a large extent a product or an outcome of *poor* governance, that is, weaknesses both in the attributes described above and in the public institutions in place to promote and protect them.[146] This fact is also to a large extent recognized in article 5 of the United Nations Convention against Corruption (UNCAC) which states, inter alia, that states should "develop and implement or maintain effective, coordinated anti-corruption policies that promote the participation of society and reflect the principles of the rule of law, proper management of public affairs and public property, integrity, transparency and accountability."

3.1.1 Poor governance in the environmental and natural resource sectors:

The link between fraud and corruption and poor governance is also relevant within the environmental and natural resource sectors. In countries where there is a concentration of power and the proper 'checks and balances' are lacking because the relevant institutions are weak, environmental governance also tends to be inadequate. If, for instance, the legislative and judicial branches of government are corrupt themselves or they are weakened by a corrupt executive branch, they may be unwilling or incapable to hold companies liable for the environmental degradation – and associated social and environmental costs – they have caused. This can soon turn out to be a vicious circle: To the extent that companies or businesses are not held accountable for the harmful impacts of their actitivities in the first round, the lesser the likelihood that they will take into account these impacts in the second.[147]

One of the most fundamental factors when it comes to weak governance and lack of accountability in the environmental and natural resource sectors is transparency, or more correctly – the lack thereof. As access to information may be considered as a threat to their

[145] See, among others: Kaufmann, Daniel. 2005. Myths and Realities of Governance and Corruption, p. 82, in: Global Competitiveness Report 2005-2006, the World Economic Forum. [Online] Available at http://siteresources.worldbank.org/INTWBIGOVANTCOR/Resources/2-1_GCR_Kaufmann.pdf [Acessed on 10 May 2011]; Shah, Anwar, 2007. Tailoring the Fight against Corruption to Country Circumstances, p. 234, in: Shah, Anwar (ed.), 2007. Performance Accountability and Combating Corruption, the World Bank. [Online] Available at http://siteresources.worldbank.org/PSGLP/Resources/PerformanceAccountabilityandCombatingCorruption.pdf [Accessed on 9 May 2011]; OECD, 2007. Policy Paper and Principles on Anti-Corruption. Setting an Agenda for Collective Action. [Online] Available at www.oecd.org/dataoecd/2/42/39618679.pdf [Accessed on 10 May 2011], p. 19; Bhargava, Vinay, 2011. Practioners reflections: Making a difference in high corruption and weak governance country environments. U4 Practice Insight 2011:1, Chr. Michelsen Institute. [Online] Available at www.cmi.no/publications/file/3962-practitioners-reflections.pdf [Accessed on 12 May 2011], p. 1; Unsworth, Sue, 2007. Rethinking Governance to Fight Corruption. U4 Brief. Chr. Michelsen Institute. September 2007 – No. 7. [Online] Available at www.cmi.no/publications/file/2757-rethinking-governance-to-fight-corruption.pdf [Accessed on 11 May 2011].

[146] See, among others: Theme I, Preventing and Detecting Fraud and Corruption, Uruguay Accords of the XVI INCOSAI in Montevideo, Uruguay, 1998; Campos and Bhargava, 2007, pp. 11-12; Shah, 2007, p. 234; Bhargava, 2011, p. 1; Unsworth, 2007; OECD, 2007, p. 19.

[147] Dillon et al., 2006, p. 40.

control, the people in power may feel a strong impetus to prevent or restrict this access. This again may lead to impunity and decisions which are contrary to the public interest. Another factor which also is closely related to weak governance, are insufficient laws and regulations. Among other things, 'loopholes' in the legislation may both give room for very wide interpretations and provide public officials with broad authority. This weakens oversight and accountability. Furthermore, where the insufficiencies also include laws which pertain to lobbying and financial disclosure, this may give wealthy external interests disproportionate influence when important decisions are made.[148]

Hence, the level of fraud and corruption in the management of environmental and natural resources is not only a product of the wealth which these resources offer, but also a result of the governance systems in place to manage these resources.[149] [Copied directly from subchapter 2.3.2]

3.1.2 Governance indicators:

In parallel to the growing interest in recent years in governance issues more generally, and between governance and fraud and corruption more specifically, the number of governance indicators – i.e. measures of one or more particular aspects of governance – has also increased. Hence, today, there is a large supply of different governance indicators available which vary quite extensively in respect of, inter alia, type of governance aspect in focus, scope, data sources and methodology.[150] One of the most widely used and quoted governance indicators among international organizations, in media and academia is the World Bank's Worldwide Governance Indicators (WGI)[151], which cover 213 countries over the period 1996-2009, and which measures the following six dimensions: 1. Voice and Accountability; 2. Political Stability and Absence of Violence; 3. Government Effectiveness; 4. Regulatory Quality; 5. Rule of Law; 6. Control of Corruption.[152]

As a first step in understanding the governance context in a particular country, and for making a preliminary assessment of the more general fraud and corruption risks in this country, looking into any available indicators for key governance aspects could be a good point of departure. Furthermore, in addition to the indicators, there are also usually country studies and reports available, either accompanying the index in question or from other sources.[153] In addition to aid donors, companies, academics and the media, such indicators and reports can also be useful for auditors. This can be relevant both for auditors investigating environmental

[148] Dillon et al., 2006, p. 40; Winbourne, 2002, pp. 12-15.
[149] Kolstad, Søreide and Williams, 2008, p. 2.
[150] For a rather thorough account of various governance indicators in use, and some further advise on what data to get, how to get them, and how to use them, see: UNDP, 2009. Governance Indicators: A User's Guide. Second Edition. [Online] Available at www.undp.org/oslocentre/docs07/undp_users_guide_online_version.pdf [Accessed on 12 May 2011].
[151] See http://info.worldbank.org/governance/wgi/index.asp.
[152] For a discussion and a word of caution regarding the use of the WGI and other governance indicators, see, among others: Arndt, Christiane and Oman, Charles, 2006. Uses and Abuses of Governance Indicators. OECD, Development Centre Studies. [Online] Available at www.oecd.org/dataoecd/21/16/40037762.pdf [Accessed on 13 May 2011], in particular chapters 3 and 4, pp. 35-76; Maurseth, Per Botolf, 2008. Governance Indicators: A guided Tour. NUPI Working Paper 754. Department of International Economics, Norwegian Institute of International Affairs. [Online] Available at http://english.nupi.no/Publications/Working-Papers/2008/Governance-Indicators-A-guided-Tour [Acessed on 13 May 2011], in particular chapter 5, pp. 27-32.
[153] Bhargava, 2011, pp. 1-2.

and/or development co-operation projects in other countries, but also for auditors wishing to carry out investigations in the environmental and natural resource sectors in their own country. Especially for auditors having limited previous experience with, and knowledge of, governance issues and associated fraud and corruption risks in their own country, such indicators and national reports could make a good basis for asking the first, basic questions.

Tip for auditors:
Look into governance indicators and national governance reports at an early stage in the audit

For auditors, such indicators and reports can provide a good overview of where the greatest challenges are in respect of the various governance dimensions for the country in question. This again could also give some indication as to where the greatest fraud and corruption risks can be found.

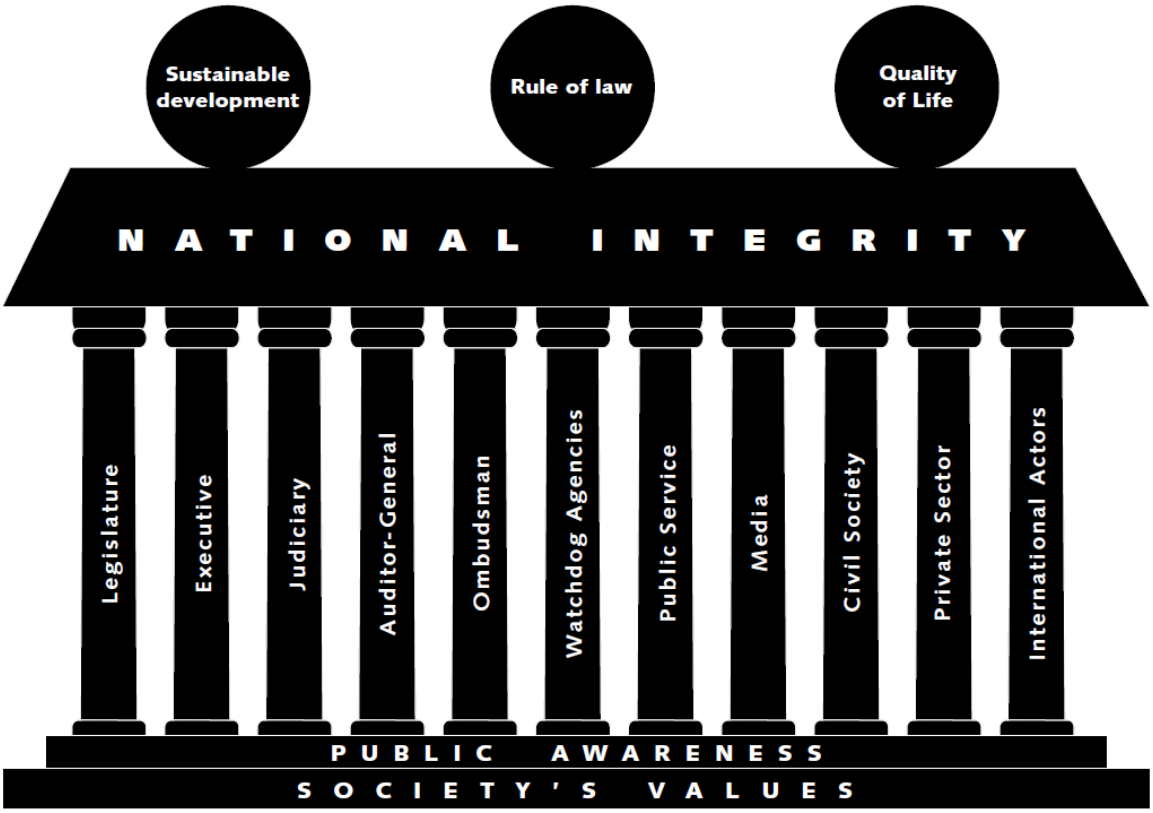
3.1.3 Introducing the 'National Integrity System' (NIS):

There is no single and simple solution to the governance problems of any particular society. These are indeed very complex issues, and the challenges involved also may be quite different from one country to another. Still, some attempts at finding more 'holistic' solutions and remedies to poor governance do exist, however. Among these, one of the most comprehensive and complete frameworks – if not *the* most comprehensive and complete framework – is the 'National Integrity System' (NIS), presented in subchapter 2.2.2.

The purpose of NIS, as described in this subchapter, is to address abuse of power and fraud and corruption at the governance level through a system of 'horizontal accountability', i.e. a dispersion of power between the different agencies and branches of government. The complete NIS framework can be illustrated as a Greek temple, as shown in figure 3.1. As the figure illustrates, in addition to the eleven pillars, NIS also consists of a foundation comprising 'public awareness' and 'society's values', and, on the roof, 'sustainable development', 'rule of law' and 'quality of life'. The last three elements are depicted as round balls to make it clear that the roof must be kept level to prevent them from rolling off and being destroyed.

However, to give a full account of the various elements of NIS, or to apply the complete framework on the environmental and natural resource sectors would extend the scope of this Guide by far. Hence, although the presentation below of various fraud and corruption risks at the governance level to a large extent will be based on NIS, it will only contain those elements which are believed to be most relevant for public sector auditors to address, and the elements themselves will also to some extent be modified to suit the purpose of the Guide. In the following, we will therefore present the following governance elements and associated fraud and corruption risks: 1. The Auditor General; 2. The Legislative; 3. The role of the Media, Civil Society and Citizens; 4. Provision of, and access to information; 5. The Judiciary and prosecution services; 6. Legislation pertaining to fraud and corruption. The Executive branch of government will be accounted for in chapter 4.

Figure 3.1 The National Integrity System (NIS)



Source:
Pope, Jeremy, 2000. Confronting Corruption: The Elements of a National Integrity System, TI Source Book 2000, Transparency International. [Online] Available at www.transparency.org/publications/sourcebook [Accessed on 24 January 2011], p. 35.

In addition to the variations from country to country in respect of their performance on the individual governance dimensions, however, auditors should be aware that there also will be substantial differences between countries as regards their *general* level of governance. This latter aspect will to a large extent decide which governance dimensions will be relevant for auditors to address first, and which will be relevant to address at later stages.[154]

3.2 GOVERNANCE PILLARS OF PARTICULAR CONCERN TO PUBLIC SECTOR AUDITORS

3.2.1 The Auditor General

A fundamental, if not existential question for auditors wishing to address fraud and corruption, is the role of their own organization in the integrity system. Indeed, as the Auditor General in many respects is supposed to be at the heart of this system – that is, as an

[154] Shah, 2007, p. 249. For an illustration of the relevance of various anti-fraud/-corruption measures, given the level of governance in the country in question, see table 7.3 in Shah, 2007, pp. 247-248.

independent and authoritative provider of reliable information to the public on the efficiency and effectiveness of the government – this seems to be a natural place to start.[155]
For SAIs to be as efficient and effective as possible in their fight against fraud, corruption and mismanagement, several fundamental prerequisites must be in place. These prerequisites are reflected in several central ISSAI-documents – in particular the Lima Declaration of 1977 (ISSAI 1) [156] – and in the more specific INTOSAI- and UN/INTOSAI-documents relating to the prevention and detection of fraud and corruption.[157]

Independence:

One of the most vital prerequisites is that of independence, which has several aspects. The first aspect is that the independence of SAIs is inseparably linked to the independence of its members. (ISSAI 1, Section 6). Hence, ideally, the head of the SAI should not be appointed or removed by the executive branch of government, but by the parliament, and preferably by a substantial majority of the representatives. Naturally, if the Executive unilaterally can recruit or dismiss the head of the SAI as they wish, this provides the former with substantial leverage against the latter, which again may constrain the ability of the SAI to address fraud and corruption in the Executive.[158]

The second aspect of independence for SAIs is that of having sufficient financial means to carry out their work, and to use these funds freely as they find most appropriate. (ISSAI 1, Section 7). Hence, as with the appointment of the office-holder, the budget for the Auditor-General's office should also ideally be decided by the Legislature. If the Executive controls the SAI's budget, it has the power both to influence directly the prioritization of audit objects and audit reporting, and the ability to indirectly limit the range of the SAI's work. Such control and influence can soon turn out to be unhealthy.[159]

The third aspect of independence for SAIs is the freedom to organize, manage and carry out their work as they see fit. (ISSAI 1, Section 5.2 and 13.1). One central element in this regard is to have the discretionary authority to decide every year which aspects of a government entity or public service they wish to examine.[160] Another central element in this regard is the freedom to choose the audit approach or discipline – or combination of approaches/disciplines – and the tools which are believed to be most adequate for the purpose. All the three main disciplines – i.e. financial, compliance and performance auditing – contain elements which are

[155] Pope, 2000, p. 75; Van Zyl, Albert, Ramkumar, Vivek and de Renzio, Paolo, 2009. Responding to challenges of Supreme Audit Institutions: Can legislatures and civil society help? U4 Issue 2009:1, Chr. Michelsen Institute. [Online] Available at www.u4.no/document/publication.cfm?3287=responding-to-the-challenges-of-supreme-audit [Accessed on 18 May 2011], p. 8.
[156] ISSAI 1. The Lima Declaration. [Online] Available at www.issai.org/media(622,1033)/ISSAI_1_E.pdf [Accessed on 10 December 2010]. Other relevant documents in this regards are, inter alia, ISSAI 10 Mexico Declaration on SAI Independence and ISSAI 11 INTOSAI Guidelines and Good Practices Related to SAI Independence.
[157] Uruguay Accords of the XVI INCOSAI, 1998; The Role of SAIs in Fighting Corruption and Mismanagement. Report on the 12th UN/INTOSAI Seminar on Government Auditing. Vienna, October 21 – 25, 1996. [Online] Available at http://intosai.connexcc-hosting.net/blueline/upload/3vn1996e2.pdf [Accessed on 1 September 2010]; INTOSAI: Active partner in the international anti-corruption network; Ensuring transparency to promote social security and poverty reduction. Conclusions and Recommendations 20th UN/INTOSAI Symposium. 11 – 13 February 2009, Vienna, Austria. [Online] Available at www.intosai.org/blueline/upload/sympconcl1602e.pdf [Accessed on 24 September 2009].
[158] Van Zyl, Ramkumar, and de Renzio, 2009, p. 12; Pope, 2000, pp. 75-76.
[159] Van Zyl, Ramkumar, and de Renzio, 2009, p. 12; UNODC, 2004, p. 103; Pope, 2000, p. 79.
[160] UNODC, 2004, p. 101.

relevant for the prevention and detection of fraud and corruption.[161] Such a 'multi-disciplinary' approach is also more in accordance with the 'hybrid' nature of fraud or forensic auditing, which in practice often involves a broad spectrum of activities and methods. Furthermore, SAI's also should have mandates which specifically enable them to prevent and detect fraud and corruption.[162]

Finally, naturally, as Legislatures also are political bodies consisting of people who do not always appreciate the independent scrutiny of auditors and other 'watchdogs', ideally, the functional and organizational independence of SAIs also must apply to a large extent to their relationship with the Legislature.[163]

Power of investigation:

Another fundamental prerequisite for SAIs is that of the power of investigation. That is, to have full access to all documents and records in the archives of the Executive regarding the subject matter, and to be empowered to request any other information, including through interviews, which is considered necessary to get the complete and correct picture. (ISSAI 1, Section10.1).[164]

Reporting:

A third prerequisite is that of reporting. That is, that the SAIs should be empowered to report their findings on an annual basis – ideally to the Parliament – and that their reports must be published. Furthermore, where findings are of particular importance and significance, SAIs should also be empowered to report during the year. (ISSAI 1, Section 16.1-2). The value of public sector audits is closely associated with the extent of transparency and public disclosure. The real power of SAIs therefore rests on whether or not their audit reports are made public. Furthermore, those receiving the reports should neither have the opportunity to alter nor withhold them.[165] There may be circumstances, however, where the publicizing of specific information regarding fraud and corruption in the public sector may compromise particular investigations or legal actions. In that case, SAIs must be empowered to report directly to other relevant bodies or officials, such as law enforcement agencies, and there should ideally also be procedures for deciding what can be publicized or not.[166]

Follow-up of reports:

A fourth prerequisite regards the follow-up of reports. To facilitate the enforcement of their findings, SAI's should be empowered to approach the responsible government entities to require them to accept responsibility, and the latter should also describe the measures they have implemented in response to the audit findings. (ISSAI 1, Section 11).[167]

Relationship with other anti-corruption agencies:

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[161] Van Zyl, Ramkumar, and de Renzio, 2009, pp. 8-9, 11-12; Dye, Kenneth M., 2007. Corruption and Fraud Detection by Supreme Audit Institutions, pp. 311-313, in: Shah (ed.), 2007.
[162] Uruguay Accords of the XVI INCOSAI, 1998.
[163] UNODC, 2004, p. 104. For a further discussion of the question regarding whether SAIs also should audit the legislature and its members, see UNODC, 2004, p. 104.
[164] See also UNODC, 2004, p. 105.
[165] UNODC, 2004, pp. 100, 103.
[166] Dye, 2007, p. 320; UNODC, 2004, p. 105. See also ISSAI 1, Section 16.3.
[167] See also UNODC, 2004, p. 108; Recommendation no. 2 in Uruguay Accords of the XVI INCOSAI, 1998.

Another important aspect when it comes to the role of SAIs in fighting fraud and corruption, is their relationship with other anti-corruption agencies. Both to exchange information, to share skills and experiences, and to co-ordinate and harmonize roles and responsibilities, close co-operation with other national bodies such as the law enforcement agencies is clearly an advantage. In that case, to avoid conflicts between audits and the investigations carried out by other officials and agencies, confidential communications should be established, and regular meetings and/or use of liaison personnel should also be considered. Ideally, the mandates of the other anti-corruption agencies should also be adjusted, as required, to accommodate the work of the SAI. In some circumstances, a small, interdisciplinary team of investigators, carefully selected from the SAI and other relevant government agencies, have proved to be an effective method against fraud and corruption.[168]

Confidential information channel:

Furthermore, to receive valuable information from so-called 'whistleblowers', civil society organizations, citizens, etc. on suspected irregularities within the public sector and/or in the management of public funds, SAIs should also consider establishing confidential information channels such as fraud and corruption 'hotlines', as well as the necessary internal apparatus to process and follow up such information. Such an information channel should also be well publicized.[169]

A legal basis:

In general, all of the above prerequisites and requirements should ideally be laid down in the Constitution and/or in legislation as appropriate, and be complemented by rules, regulations and procedures.[170]

On this background, the following questions can be relevant to consider for auditors:

- **Does your SAI have the financial, organizational, functional and operational independence necessary to carry out its tasks in an objective and efficient manner?**

- **Does your SAI have the powers to audit all public funds, resources and operations, and the discretionary authority to decide which aspects of a government entity or public service it wishes to examine?**

- **Does your SAI have full access to all documents and records in the archives of the Executive, and the powers to request any other information which it considers necessary for the investigation?**

- **Does your SAI have the freedom to choose the audit approach or method (i.e. financial, compliance or performance audit) which it believes to be most adequate for the purpose?**

[168] UNODC, 2004, pp. 108-109; Pope, 2000, p. 80; Recommendation no. 6 in Uruguay Accords of the XVI INCOSAI, 1998.
[169] Recommendation no. 11 in Uruguay Accords of the XVI INCOSAI, 1998; Van Zyl, Ramkumar, and de Renzio, 2009, p. 23.
[170] ISSAI 1; Recommendation no. 1, Resolution of the Presidents of Supreme Audit Institutions of Central and Eastern European Countries, Cyprus, Malta and the European Court of Auditors, Prague, October 1999. [Online] Available at http://eca.europa.eu/portal/pls/portal/docs/1/191289.PDF [Accessed on 23 May 2011].

- **Does your SAI have in its mandate to detect and prevent fraud and corruption?**

- **Is your SAI able to report its findings freely and without restrictions directly to Parliament, and are the reports made public promptly after this?**

- **Does your SAI have the powers to follow up its reports and inquire whether the responsible authority has implemented the necessary measures? Are follow-up reports also made public promptly?**

- **Has your SAI established good and adequate working relationships with other relevant anti-corruption agencies in your country?**

- **Has your SAI established a confidential information channels to receive and process information from the public regarding possible fraud and corruption?**

- **Does your SAI have the legal base in the Constitution, in the law, and in rules, regulations and procedures which is necessary to meet the above requirements?**

- **If the answer is "no" to any of the questions above – what can your SAI do to improve the situation?**

Box 3.1 provides an illustration of some of the elements presented in this subchapter within an environmental and natural resource management context.

Box 3.1
Case: The Solomon Islands Office of the Auditor General and their audit of the Department of Fisheries

The audit:

The fisheries sector in the Solomon Islands, which primarily is based on tuna fisheries, is very important for the national economy. The sector is also one of the major revenue sources for the Government, especially through licence fees from both domestic and foreign fishing vessels. The Solomon Islands Ministry (formerly Department) of Fisheries and Marine Resources is responsible for the management of these fisheries, including the collection of revenues, trough the National Tuna Management and Development Plan.

In 2003, the Office of the Auditor-General (OAG) of Solomon Islands carried out an audit of the Ministry, covering the period from 2001 to 2003, which mainly focused on collection of revenues from licence and observer fees.

On the general level, the audit uncovered many serious flaws, including: Breaches of the Fisheries Act and the Tuna Management Plan; lack of compliance with the Public Finance and Audit Act, Financial Instructions and General Orders; collapse of procedures and practices, as well as serious weaknesses in internal controls, leaving the Ministry open to fraud and corruption.

More specifically, the audit revealed that a major part of the fishing licence fees for the years 2001 – 2003 had been channelled to other accounts than the one prescribed, i.e. the so-called

'Consolidated Fund', and could not be properly accounted for due to poor management, fraud and misappropriation of funds. For instance, it was revealed that there was a systematic collection of licence and observer fees in cash by fisheries officers, and most of these funds could not be accounted for. The OAG managed however to trace some of these collections to the personal bank accounts of the fisheries officers or their relatives.

At the same time it was also discovered that an official at one of the highest levels in the Ministry many times had acted in breach of laws and regulations pertaining both to tuna fisheries and to management of public finances. Moreover, some of the decisions in question had been done verbally, thereby seriously undermining both accountability and transparency as well. In addition, it was also revealed that the official in question was experiencing a serious conflict of interests as he was involved in the fisheries business himself through his ownership of a company within this sector.

General recommendations to the Parliament:

The report from this audit was one of ten special audit reports which were tabled in the Parliament during 2005 and 2006. Together, these reports documented maladministration and fraudulent and corrupt behaviour across various government agencies in the Solomon Islands for the period 2001 – 2004. In 2007, the OAG submitted a summary report based on these audits called "An Auditor-General's Insights into Corruption in Solomon Islands Government", which both highlighted the most important systemic weaknesses identified in the audits, and which also provided several recommendations on how to address fraud and corruption in the Solomon Islands Government in a holistic manner. Among other things, the recommendations included:

- The development of detailed action plans to strengthen internal and financial controls as well as transparency and accountability mechanisms in the ministries[171];
- Review of training materials and programmes for public servants concerning accountability[172];
- Provision of specialist training to members of the Public Accounts Committee (PAC) and senior public officials to facilitate parliamentary committee hearings[173];
- Strengthening of ethical guidance provided to Ministers, Permanent Secretaries and relevant public officials[174];
- Conduct an analysis with a view to identify possible obstacles to the successful investigation and prosecution of fraud and corruption and related offences revealed in the special audits[175];
- Review of the corruption provisions in the Penal Code[176];
- The establishment of an inter-agency task force to investigate and prosecute identified cases of fraud and corruption[177];
- Media advertisement of meetings and hearings in the PAC in advance, to increase public awareness and confidence[178];

[171] See subchapter 4.3.
[172] See subchapter 4.3.
[173] See subchapter 3.2.2.
[174] See subchapter 4.3.
[175] See subchapter 3.2.5.
[176] See subchapter 3.2.6.
[177] See subchapter 3.2.1.
[178] See subchapter 3.2.2.

- Media release when the PAC submits a report to Parliament to highlight the report, and possibly also the holding of a public meeting, together with Transparency Solomon Islands, to discuss the most important findings in the report and responses to these[179];
- Conduct a study to assess the viability and prerequisites for the introduction of Freedom of Information legislation into the Solomon Islands[180].

The OAG:

The OAG on the Solomon Islands has a legal basis in section 108 of the Constitution of 1978 and in Parts VI to VIII/sections 34 to 48 of the Public Finance and Audit Act, also of 1978. The Constitution and the Act generally establish the independence of the OAG, and also stipulate that the OAG shall have full access at any time to all records, books, documents, etc. in the Executive, and also the powers to request any other information or carry out enquiries and examinations as required. The OAG also has the discretionary authority to choose the audit approach believed to be most adequate for the purpose, and to choose the audit topics.

The OAG does not have an explicit mandate to prevent and detect fraud and corruption, but cooperates with the Royal Solomon Islands Police Fraud Squad in such matters. Hence, if the OAG comes across evidence or receives confidential information regarding fraud and corruption, this is passed on to the Fraud Squad.

Furthermore, the reports of the OAG are sent directly to Parliament, without any possibility for alterations. Once the report has been tabled in Parliament it is also distributed to the media by the OAG. There is no explicit mandate for the OAG to follow up their reports, but as it is within the discretion of the OAG to choose their audit topics at any time, they are in reality free to follow up any matter they wish.

However, according to the OAG, they do not have financial independence and their staffing is also subject to strong restrictions by the Solomon Islands Ministry of Public Service. Moreover, although the OAG can send their reports directly and unaltered to the Parliament, there is little opportunity to table the reports and, hence, publicize them. The reports can only be tabled when the Parliament is assembled, which in total only adds up to a few weeks each year. Attempts at passing new legislation which inter alia would make it possible to table reports 'out-of-session' have so far been futile.

The follow-up of the audit:

The PAC in the Solomon Islands Parliament did review the summary-report on corruption, mentioned above, but they never finalized a report on these hearings. Hence, there is no official document which reflects the viewpoints of the Parliament on the findings of the OAG on corruption in the Ministry of Fisheries and other government entities on Solomon Islands. Therefore, according to the OAG, very little action has so far been taken in response to any of the reports in question.

In this connection, the OAG points out that the level of corruption in the country is high, and the same is the threshold for possible political consequences of corruption. Politicians can spend considerable time in court for fraudulent and corrupt practices and still be re-elected.

[179] See subchapter 3.2.2.
[180] See subchapter 3.2.4.

This is partly seen in connection with cultural factors, as the interests of the family and the local community seem to take a higher priority than both self- and national interest on the Solomon Islands.

Consequently, according to the OAG, no one has so far had any significant motivation to take action on the findings in their reports. Neither have there so far been any consequences on the bureaucratic or political level if people do not take action.

Sources:

The Constitution of Solomon Islands. Statutory Instruments, 1978 No. 783, Pacific Islands. [Online] Available at http://www.paclii.org/sb/legis/consol_act/c1978167/ [Accessed on 24 May 2011]; Solomon Islands Public Finance and Audit Act [Cap 120] [Online] Available at http://www.paclii.org//cgi-bin/disp.pl/sb/legis/consol_act/pfaaa189/pfaaa189.html [Accessed on 24 May 2011]; E-mail from Deputy Auditor General Peter Johnson of 26 July 2011; Office of the Auditor-General Solomon Islands, 2007. An Auditor-General's Insights into Corruptionin Solomon Islands Government. 31 October 2007. National Parliament Paper No. 48 of 2007. [Online] Available at http://www.oag.gov.sb/OAG%20REPORTS/2007%20REPORTS/An%20Auditor%20General's%20Insights%20into%20Corruption%20in%20SIG%20-%20October%202007.pdf [Accessed on 20 May 2011]; Office of the Auditor-General Solomon Islands, 2003. Audit report on the Department of Fisheries and Marine Resources. Received by e-mail from Deputy Auditor General Peter Johnson on 10 August 2011.

3.2.2 The Legislature

Another cornerstone of the NIS is an elected Legislature or National Assembly which can hold the Executive accountable on a regular basis. Indeed, as 'watchdog' on the Executive, as legislator and as representative of the people, Parliament is at the core of every country's endeavours to achieve and maintain good governance and to prevent and detect fraud and corruption. To perform these tasks as efficiently and effectively as possible, the National Assembly must consist of individuals of integrity.[181] This has implications both for the way in which these individuals are elected, and for the way in which they conduct their business.

Elections:

To start with elections, there are, inter alia, at least two aspects which can be relevant for auditors to address. The first concerns the existence of an independent Electoral Commission, and the second concerns the issue of party funding.

An independent Electoral Commission:

To ensure the integrity and legitimacy of the members of the Legislature, it is of course of vital importance that elections are free, fair and transparent. If they are not, they can easily be subject to various fraudulent and corrupt practices. To avoid this, there are many conditions that must be in place both before, under and after the election process. These conditions should ideally be laid down in the Constitution and/or in legislation as appropriate, and these provisions should ideally reflect best international practice in respect of transparency and openness. Furthermore, the election process should preferably be supervised by an official body – an Electoral Commission – which is independent of the government, and which also has its legal basis laid down in the Constitution and/or in legislation. The independence of the Commission first and foremost depends on the way in which its members are elected. Preferably, the Commissioners should therefore be appointed by all the major political parties

[181] Pope, 2000, p. 47.

competing in the election, and definitely by all the political parties which are represented in the Parliament.[182]

Transparency in party funding:

Political parties need money both to run their daily business and to carry out election campaigns, and at least to some degree, it is thought to be legitimate for the parties to receive funding from their supporters. This, however, can make the parties vulnerable to fraudulent and corrupt influences from the outside. To collect small contributions from large numbers of individuals are time-consuming and expensive, and the private sector is therefore the primary financing source for political parties in the majority of democracies. In many instances, this financial support is given with the expectation that there will be a 'payback', i.e. that the sponsor will enjoy some sort of patronage and favouritism when the party and its representatives are elected. If this is the result, the credibility and the integrity of the latter will be undermined, and their ability to fight fraud and corruption will be greatly reduced. The risks are particularly high when it comes to financing of election campaigns, both because the stakes are highest for the parties in these periods, and because the money has to be collected and disbursed fast, making accounting complicated.[183]

Hence, to avoid this, there must be some sort of transparency system in place. Although this can be difficult to establish, there should be rules and regulations in place which ensure, inter alia, that all contributions and other sources of party income are publicized, that sponsors and the size of their contributions are registered in a public register, and that links to lobbyists are disclosed. Both incomes and expenditures should be available for public review and audit. In addition to active and investigative media[184], there should also be an independent and authoritative entity such as the Electoral Commission to oversee this system and enforce the regulations. Furthermore, the use of public servants, and state funds and assets by parties in government for political purposes such as election campaigns should be banned. Finally, to reduce the opportunities for private companies and other actors to 'buy influence', partial public financing of political parties and the allocation of free time slots on radio and TV to qualifying parties should also be considered.[185]

In office:

When it comes to the work of the elected Parliament, there are also several aspects which are of relevance for auditors wishing to address fraud and corruption. Inter alia, these include standards or codes of conduct, particular anti-fraud/-corruption provisions for parliamentarians, transparency, freedom of speech, follow-up mechanisms through a dedicated committee in parliament and public hearings.

Code of Conduct:

Once elected, there should also ideally be mechanisms in place which ensure that parliamentarians maintain their integrity, that they are credible in their efforts against fraud and corruption, and that they can be held accountable for their actions as elected representatives. A core element in this regard is a well established and disseminated code of

[182] Pope, 2000, pp. 165-166, 168.
[183] Pope, 2000, pp. 50-51; UNODC, 2004, p. 182.
[184] See section 3.2.3.
[185] World Bank, 2000, p. 42; Pope, 2000, pp. 52, 167-168. See also article 7.3 in UNCAC.

conduct for parliamentarians which, among other things, contains rules for reporting, preventing and in any other way handling conflicts of interest. As part of this, parliamentarians should declare their campaign financing, their assets, their business interests etc., and systems for monitoring these incomes, assets and interests are also essential. Furthermore, a disciplinary committee with the power to follow up complaints and to impose disciplinary reactions as appropriate should also be in place.[186]

Criminalization of unethical actions:

Closely related to the issue of a code of conduct is the question of criminalization of unethical actions by parliamentarians. Traditionally, Westminster-style parliaments have dealt with such actions themselves through a disciplinary committee and disciplinary reactions – as mentioned above – rather than referring such cases to the Judiciary. Among other things, this separation of the Legislative from the Judicial branches of government is merited by the former's need for independence and some level of legal immunity. However, such legal immunities of parliamentarians should be restricted to what is absolutely required to secure a free and exhaustive debate and to protect the proceedings of Parliament from undue influence. Hence, parliamentarians do not need to be shielded from review by watchdog institutions such as the Auditor General due to their immunity, nor should their immunity shield them from laws and regulations pertaining to fraud and corruption. Bribery of legislators has therefore been explicitly criminalized in several countries.[187]

Transparency:

Another important aspect when it comes to the accountability of elected members of the Legislative, is the question of transparency with regard to the business of the parliament and the activities of its members. There are several ways in which this can be facilitated, inter alia, by giving media access to the legislature, by publicizing minutes and decisions from its meetings, through establishment of websites for the legislature and its members, and by giving as much access as possible for members of the public to the meetings, either physically or through broadcast media.[188]

Freedom of speech:

Although their immunity cannot be unlimited, however, legislators must at the same time enjoy the freedom of speech. That is, they must have the legal immunity to express any opinion and anxiety, and argue freely in parliament without the risk of being sued in the courts afterwards for libeling. Another aspect of this freedom is that there must be procedural rules in place which ensure that every elected member of parliament has sufficient time to speak.[189]

[186] UNODC, 2004, pp. 180, 183; Pope, 2000, p. 52. See also subchapter 4.3.1 for a further discussion of the 'Code of Conduct'- concept.
[187] Pope, 2000, p. 53; UNODC, 2004, pp. 180-182.
[188] UNODC, 2004, pp. 180-181. Obviously, as will be mentioned in connection with the issue of hearings, transparency in the proceedings of parliament is also important with regard to the accountability of the Executive.
[189] UNODC, 2004, p. 182; Pope, 2000, p. 54.

The role of the PAC:

Of direct relevance to SAIs is the existence of a parent body in parliament to receive and follow up on their reports. In the majority of audit systems, it is the Public Accounts Committee (PAC) or its counterparts which is most central in the relationship between parliaments and SAIs. This committee and this relationship is particularly important in countries with SAIs operating under the 'Westminster model' or the 'Board/Collegiate model', as these models to a very large extent depend on the parliament being inclined to and capable of making the executive accountable. Where parliaments are weak, the effectiveness of these models is also limited, irrespective of the competence and resources of the SAI in question. The legislature in countries with SAIs operating under the 'Judicial/Napoleonic model' may also play a certain role in respect of holding the executive to account, but to a more limited extent, however.[190]

Hence, to fulfil its role as a 'controller' of government expenditures and to ensure that the reports and the recommendations of the Auditor General are properly implemented by the Executive, it is important that the PAC or its equivalent has the necessary powers to do this. Among other things, this includes the authority to obtain all relevant documents regarding government activities both in the present and in the past, to call all relevant officials to give evidence, and also, if required, to request Ministers to appear for the committee for questioning. Also, by following up implementation on a regular basis, i.e. *before* the Auditor General has submitted its subsequent report, and by setting a time limit for the Executive's implementation of audit findings, the PAC can provide additional support to the work of SAIs. Ideally, the Chair of the committee should also be appointed by the opposition in parliament.[191]

Public hearings:

Finally, public hearings in parliament of audit reports – and the follow-up of these reports – can also provide the Auditor General and the Legislative with further leverage over the Executive. First, by giving access to non-parliamentarian actors such as Civil Society Organizations (CSOs), academics and businesses, parliamentarians can get further evidence and knowledge regarding the audited entities. Second, by making the hearings open to the public, further pressure is exerted on the Executive to take audit findings into account. Third, when the recommendations of the Auditor General and the parliament are made public, they will also be referred to in the media. This makes even more people aware of these recommendations, which will increase the pressure on government.[192]

On this background, the following questions can be relevant to consider for auditors:

- **Are there provisions in place – in the Constitution and/or in legislation as appropriate – which ensure that elections for the national assembly are free, fair and transparent?**

[190] UNODC, 2004, p. 109; Van Zyl, Ramukmar, and de Renzio, 2009, pp. 13-15, 17. For a further discussion of the relationship between SAIs and parliaments under the 'Westminster model', the 'Board/Collegiate model' and the 'Judicial/Napoleonic model', see Van Zyl, Ramukmar, and de Renzio, 2009, pp. 13-15.
[191] Pope, 2000, p. 57; Van Zyl, Ramukmar, and de Renzio, 2009, pp. 15, 17.
[192] Van Zyl, Ramukmar, and de Renzio, 2009, pp. 16-17.

- **Are the elections organized and supervised by an independent Electoral Commission or similar body?**

- **Is there a system in place, supported by appropriate rules and regulations which ensures that party funding is transparent and that all major sponsors of political parties are made public?**

- **Is there an independent body in place, such as an Electoral Commission in place to supervise the system and enforce the regulations?**

- **Is there a code of conduct in place for parliamentarians (MPs) which, inter alia, prevents and deals with conflicts of interest?**

- **Is there a system in place for monitoring the incomes, assets and business interests of MPs, as well as a disciplinary committee to follow up breaches of the code as appropriate?**

- **Does the immunity of MPs also include fraudulent and corrupt acts?**

- **Are there systems and mechanisms in place which ensure that the business of parliament and the activities of its members are as transparent as possible?**

- **Do all MPs enjoy the freedom of speech, and is this freedom supported by appropriate legislation? Are there also procedural rules in place which ensure that all MPs have sufficient time to speak?**

- **Is there a Public Accounts Committee (PAC) or equivalent 'watchdog' entity in parliament which can hold the Executive accountable and ensure that the latter implement the recommendations of the Auditor General? Is the Chair of the PAC independent of the present government?**

- **Does the PAC or its equivalent have the authority obtain all relevant documents from the Executive and to call all relevant officials and Ministers for questioning if necessary?**

- **Are the debates and hearings in parliament of audit reports – and the follow-up of these reports – open to the public?**

Box 3.2 provides an illustration of some of the elements presented in this subchapter within an environmental and natural resource management context.

Box 3.2
Case: The role of the Legislature in 'land swaps' in Bulgaria

According to a report from the Open Society Institute in 2002, the parliament in Bulgaria was then considered to be highly vulnerable to corruption. On the one hand, elections were considered to be free and fair, and these were organised and supervised by electoral commissions both at the national, regional and local level. Furthermore, the central/national commission was composed in a way which reflected the size of the various parties at the same

time as no party or coalition was allowed to have a majority in this commission. On the other hand, however, several flaws were found in respect of party financing and regarding the conduct of business in parliament.

As regards party funding, there is an Act in place which regulates several aspects of such funding. Among other things, according to the Act, political parties are entitled to state subsidies according to past election performance. At the same time, however, the rules also allow for large anonymous donations, and in 2002 transparency were considered to be low both with regard to the system for allocating such subsidies and in respect of the parties' reporting on income and expenditures. In addition, supervision and control was found to be lax. Together, these weaknesses were believed to allow for extensive illegal funding and corruption.

When it comes to the business in parliament, it was found that the regulation of conflicts of interest among the MPs were minimal, and also that the PAC's supervision of their assets and reception of gifts/other material benefits was inadequate. Hence, MPs were believed to have widespread external financial and other commercial interests. Furthermore, lobbying of MPs was completely unregulated in 2002, and they also enjoyed full immunity from criminal prosecution. The parliament also lacked a mechanism to enforce the findings of the Auditor-General.

With respect to the environmental and natural resource sectors, the role of the parliament was actualized in connection with a large-scale corruption case relating to so-called 'land swaps', which has been revealed in recent years. The 'swaps' implied that state-owned land was exchanged with privately-owned land with the authorization of local authorities. According to EurActiv, the land owned by the state had a much higher value than the land owned by private entities, inter alia because the former was located in areas which were very attractive for tourism. The profit rate from the 'swaps' was estimated to be 100 to 1 on average, and the beneficiaries usually had close connections with the government. EurActiv furthermore points out that some of these profits reportedly have been channeled to the political parties' 'slush funds'. Estimates indicate that the Bulgarian state has lost several billion euros in land value due to the 'swaps', in addition to the loss of valuable natural areas and damages caused to ecosystems.

At the end of 2008, a group of members of the Bulgarian parliament suggested to revise the country's law relating to forests, apparently with the aim of protecting the forests from further 'swaps'. According to WWF, however, closer scrutiny of the proposal revealed that it contained several 'loopholes'. First, one of the amendments would have allowed for tax exemptions amounting to €150 to 250 million for developers of ski resorts. Second, another amendment would have permitted the sale of state forests without any justifications or criteria or restrictions for such sales. Third, as a result of the proposed amendments, the hunting period for a particular type of bird would also have been changed, in contravention of the EU Bird Directive. Finally, according to the proposal, the ban on 'forest swaps' would enter into force only after a 'grace period' of several months, thus allowing for further 'swap deals' to be made. WWF also points out that the proposal was prepared in very short time and in a very non-transparent manner. There were no consultations or discussions in parliament regarding the proposed amendments, neither were they publicized on the parliament's website.

It was only after several rounds of public protests and demonstrations that the proposed amendments were withdrawn or adjusted in accordance with the recommendations of WWF and other protesters.[193]

Sources:

Open Society Institute, 2002. Corruption and Anti-corruption Policy in Bulgaria. Monitoring the EU Accession Process: Corruption and Anti-Corruption Policy. [Online] Available at http://info.worldbank.org/etools/antic/docs/Resources/Country%20Profiles/Bulgaria/OpenSocietyInstitute_CorruptionBulgaria.pdf [Accessed on 23 May 2011], pp. 79-131; European Union Information Website (EurActiv): Large-scale corruption exposed as Bulgaria's president visits Brussels. Published 24 February 2010. [Online] Available at www.euractiv.com/en/enlargement/large-scale-corruption-exposed-bulgaria-s-president-visits-brussels-news-282241 [Accessed on 23 May 2011]; World Wide Fund For Nature (WWF): Success – after thousands of Bulgarians take to the streets to protect their forests. Published 24 January 2009. [Online] Available at http://wwf.panda.org/about_our_earth/all_publications/?154941/Success----after-thousands-of-Bulgarians-take-to-the-streets-to-protect-their-forests [Accessed on 30 May 2011].

3.2.3 The role of the Media, Civil Society and Citizens

Media, civil society and the citizenry at large are all vital in the protection and promotion of transparency, accountability and participation in a society – all fundamental attributes of good governance. Hence, they also have fundamental roles in fighting fraud, corruption and mismanagement. Inter alia, this is reflected in the Uruguay Accords of the XVI INCOSAI in 1998, and reaffirmed in the Conclusions and Recommendations from the 20th UN/INTOSAI Symposium, where the importance for SAIs of having good contacts with the media and close cooperation with other national and international anti-corruption bodies are emphasized.

In the environmental and natural resource sectors:

Moreover, as with fraud and corruption more generally, media and civil society organizations (CSOs)[194] are also fundamental in combating fraud and corruption in the environmental and natural resource sectors more specifically. As independent 'watchdogs', inter alia reporting and publicizing any discovered misconduct by public officials leading to environmental degradation and/or siphoning of revenues from natural resource exploitation, they are instrumental in creating greater openness and making government more accountable also in this area. In the end, this may also empower the citizens themselves to have greater influence on decision-making, thereby ensuring that policy making in the environmental field is more in the interest of the public than in the interests of the few.[195]

For instance, as regards transparency in respect of the management of oil and gas revenues, the importance of the media has been summarized as follows: First, media is important to raise overall awareness in the public regarding the issues at stake. Second, media is important to break the monopoly which the private sector and governments often have as information

[193] See also subchapter 3.2.3.

[194] The World Bank defines "civil society" as "the wide array of non-governmental and not-for-profit organizations that have a presence in public life, expressing the interests and values of their members or others, based on ethical, cultural, political, scientific, religious or philanthropic considerations. Civil Society Organizations (CSOs) therefore refer to a wide of array of organizations: community groups, non-governmental organizations (NGOs), labor unions, indigenous groups, charitable organizations, faith-based organizations, professional associations, and foundations". [Online] Available at http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/CSO/0,,contentMDK:20101499~menuPK:244752~pagePK:220503~piPK:220476~theSitePK:228717,00.html [Accessed on 5 June 2011].

[195] See, among others: UNDP, 2008, p. 98; Dillon et al., 2006, p. 14; Winbourne, 2002, pp. 25-26.

providers. Third, media is an important instrument for controlling the conduct of government officials.[196]

An example on the role of CSOs in the same area can be drawn from the Extractive Industries Transparency Initiative (EITI), which was established in 2006 to provide for greater transparency in respect of revenues generated from extractive industries around the world. A core element in the implementation of the EITI system in member countries is the establishment of multi-stakeholder steering groups to govern and oversee the implementation process. CSOs have a central role in these steering groups, and in many countries this is believed to have had a greater impact on transparency and accountability than the actual disclosures of revenue flows.[197]

Furthermore, the more CSOs and the media can act in combination, the greater the possible impact on government policy. Most government officials are concerned about their public reputation and are usually sensitive to what the media says and writes about them. Hence, by having their studies and reports on particular issues presented in the media, the influence of CSOs will increase, and the greater the chances of improving governance in the areas in question. An example in this regard are the reports by Global Witness regarding smuggling of diamonds, trade in illegal timber and embezzlement of oil revenues, which – in combination with effective media work – were instrumental in altering public policies and in establishing international efforts such as EITI.[198]

Prerequisites:

Fundamental prerequisites when it comes to the role of the media, CSOs and the citizenry in combating fraud and corruption, are the freedoms of opinion and expression, and of peaceful assembly and association. These freedoms should ideally be laid down in the Constitution and/or in legislation as appropriate.[199] Global benchmarks in this regard are found, respectively, in Articles 19, 21 and 22 in the International Covenant on Civil and Political Rights (ICCPR)[200] and in Article 13 of UNCAC.

To start with *the media*, the limitations of the freedoms of opinion and expression are often connected with the rights or reputations of private citizens or related to national security matters. To some extent such limitations are considered to be appropriate. However, if they are not narrowly interpreted, they involve the risk of being abused to muzzle the media. For instance, national laws and regulations in this area should not contain any constraints – or be interpreted in a way – which inhibit the media from publishing matters just because this could harm the public reputation of ministers or other holding high positions in government. If so, this would de facto compromise the freedom of expression. This is the situation in many countries, where anti-libel laws are used without proper justification to protect public office

[196] Shultz, Jim, 2005. Follow the Money: A Guide to Monitoring Budgets and Oil and Gas Revenues. Open Society Institute. [Online] Available at www.soros.org/initiatives/cep/articles_publications/publications/money_20041117/follow_money.pdf [Accessed on 5 June 2011], p. 62.
[197] Dillon et al. 2006, p. 32; Gillies, 2010, p. 8; UNDP, 2008, p. 101.
[198] Shultz, 2005, p. 62.
[199] Pope, 2000, pp. 122, 134.
[200] Adopted and opened for signature, ratification and accession by General Assembly resolution 2200A (XXI) of 16 December 1966. Entry into force 23 March 1976. 167 parties as of 5 June 2011.

holders. However, still, secrecy to protect personal privacy or commercial interests is perhaps more often justifiable than secrecy due to national security interests.[201]

In addition to overzealous libel or security laws, another possible restriction on the watchdog function of the media is the existence of licensing and permit systems for journalists. Such systems can take many forms and may frequently approximate to harassment. To avoid this, media licensing should therefore be reduced to an absolute minimum and managed with total transparency – by independent regulators. Moreover, the same liberal licensing practices should also apply to foreign correspondents, as it is crucial for transparency and accountability in a country that these have the same working conditions as their local colleagues. Finally, a third possible impediment to the work of journalists are provisions and/or decisions which require them to disclose their sources. If journalists are unable to protect their sources without facing the risk of financial penalties or imprisonment, it becomes extremely difficult for them to freely carry out their work. Hence, protection of confidential information sources should also be part of the legislation protecting the freedom and independence of the media.[202]

Another risk area when it comes to the role of the media is the possible existence of media monopolies, which potentially are even more harmful than are monopolies in other sectors of the economy. In the case of privately-owned media, these can only be really free when there is real competition in the media market. Hence, to ensure a diversity of newspapers, magazines, television and radio stations etc., there should be rules and regulations in place which prevent potentially harmful takeovers and mergers in this market. Furthermore, another critical measure in this regard is the removal of restrictions on the Internet.[203] In many countries, however, it is the government itself which is the largest media owner – a situation which represents a particular challenge to the independence of the media. Therefore, in addition to legislation which allow for sufficient competition in the media market, there should also be legislation in place which protects the independence and freedom of journalists in media organizations owned by the state. Ideally, there should also be an independent body in place to oversee and protect the rights of the media – regardless of whether these are state- or privately-owned.[204]

As to *CSO's and the citizenry*, the same prerequisites which are crucial for the work of journalists – i.e. the freedoms of opinion and expression supported by appropriate legislation and bodies – are equally important for the watchdog role of the former. In addition, to fully contribute to transparency and accountability in society, CSO's and the citizenry are also completely dependent on the freedoms of peaceful assembly and association. As mentioned, these freedoms should ideally be laid down in the Constitution and/or in legislation as appropriate. Moreover, as with licensing practices for journalists, any accreditation or registration procedures for CSO's should also be managed by an independent body.[205]

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[201] Pope, 2000, pp. 122-123, 127; World Resources Institute (2003) World Resources 2002-2004. Decisions for the Earth: Balance, Voice, and Power. [Online] Available at http://pdf.wri.org/wr2002_fullreport.pdf [Accessed on 18 January 2011], p. 222.
[202] Pope, 2000, pp. 126-127.
[203] Of course, journalists in privately owned-media can also be corrupt irrespective of the influences of the state. This is a serious problem in many countries around the world. This is not something that auditors can address directly, however, but which must be dealt with through appropriate legislation (see section 3.2.6) and by the law enforcement authorities.
[204] Pope, 2000, pp. 119-122.
[205] Pope, 2000, p. 134.

Two additional prerequisites which generally apply to all three groups – i.e. the media, CSO's and the citizenry – are the existence of an informed, independent and impartial Judiciary, and the provision of, and access to information. Inter alia, an independent judiciary is important for protecting the 'four freedoms' from unjustified restrictions, for preventing biased and unfair treatment of representatives from any of the three groups, and for protecting the latter from harassment, persecution and violence. Provision of, and access to information is vital for the media, CSO's and the citizenry to monitor and scrutinize the conduct of government, thereby enabling and empowering them to raise their voice against fraud, corruption and mismanagement. This will be further accounted for in subchapter 3.2.5 and 3.2.4 respectively.

On this background, the following questions can be relevant to consider for auditors[206]:

- **Are the freedoms of opinion and expression laid down in the Constitution and/or in legislation as appropriate?**

- **Do journalists and/or media entities need some sort of permit or license to do their job? If so, is this permit/licensing system being managed in a transparent, fair and unbiased way by the authorities?**

- **Do foreign correspondents enjoy the same rights to cover and report stories as the domestic media?**

- **Are publicly-owned media free to decide editorial content, independent of government control? If so, is there legislation in place which protects the independence and freedom of journalists in these media?**

- **Is there an independent body in place to oversee and protect the rights of both state- and privately-owned media?**

- **Are anti-libel or security-laws often used without proper justification and/or in a non-transparent manner to prevent journalists from publishing information regarding possible misconduct by government officials?**

- **Is protection of sources accounted for in the legislation protecting the freedom and independence of the media?**

- **Are there any restrictions on the access to or use of the Internet?**

- **Is there legislation in place which allow for sufficient competition between the different media (i.e. television, radio, print media)? If so, is this legislation enforced?**

- **Are the freedoms of peaceful assembly and association laid down in the Constitution and/or in legislation as appropriate?**

- **Are civil society subject to any restrictions if they wish to organize themselves through the establishment of non-governmental organizations (NGOs)? If so, are**

[206] For a more comprehensive checklist when investigating the freedom of the media, see: Freedom House. Freedom of the Press 2010. Broad Setbacks to Global Media Freedom. [Online] Available at www.freedomhouse.org/uploads/pfs/371.pdf [Accessed on 5 June 2011], pp. 13-19.

such restrictions often imposed without proper justification and/or in a non-transparent manner?

- **Do CSOs and the citizenry need some sort of permit or license if they wish to hold public meetings? If so, is this permit/licensing system being managed in a transparent, fair and unbiased way by the authorities?**

3.2.4 Provision of, and access to information

The aspects of provision of, and access to information is closely related to the role of the media, civil society and the citizenry at large, mentioned in subchapter 3.2.3. Without information there is no transparency or accountability. Hence, access to information for the media, CSOs and citizens is also a fundamental element of the integrity system of a country. Citizens who are informed and continue to be informed of governance matters which concern them develop expectations regarding standards of government performance and are better positioned to pressurize officials to satisfy those standards. Provision of, and access to information regarding public affairs is therefore also crucial to prevent and detect fraud and corruption. Inter alia, this is reflected in article 10 and article 13, subparagraph 1 (b) of UNCAC.[207]

In the environmental and natural resource sectors:

As already indicated, lack of transparency is a core factor when it comes to weak governance, lack of accountability and fraud and corruption in the environmental and natural resource sectors. Hence, promotion of transparency is also one of the most important measures when it comes to the prevention and detection of fraud and corruption in these sectors. One of the most prominent efforts in this regard so far is the Extractive Industries Transparency Initiative (EITI), mentioned in subchapter 3.2.3. At the heart of this initiative is the idea that disclosure of resource revenue payments will have deterrence effects and thereby lead to increased accountability. The standard of transparency established by EITI has also inspired other initiatives in other sectors, such as forestry.[208]

The demand side in the water sector is another example on how greater transparency can create disincentives for fraudulent and corrupt activities. In water management, transparency can be improved at various levels – both at the sector, community and project level – through publication of the accounts of utilities, budgets, contracts, and annual reports, and through the holding of public hearings by the responsible officials. These are all examples on *tangible* measures, i.e. measures which can be checked and further scrutinized by auditors and others. Usually, consumers have very limited knowledge about overhead expenses and the costs of capital, which enables public officials to deliberately misappropriate or tap resources into other budgets without being detected. Hence, to increase the demand for accountability by water consumers, access to information is key. In addition to the measures already mentioned,

[207] Pope, 2000, p. 119; UNODC, 2004, p. 301.

[208] Gillies, 2010, p. 6. At the same time, however, it should be noted that transparency initiatives like EITI seldom uncover cases of fraud and corruption by themselves. Among other things, this is reflected in the fact that several countries, including EITI-members, have high scores on transparency at the same time as they are subject to high levels of corruption and weak accountability. Part of the explanation for this is that the data and reports being disclosed in practice are inaccessible or not being properly utilized. Consequently, the informational imbalances which provide fertile ground for fraud and corruption still remain. (Gillies, 2010, p. 7).

consumers should also have access to information regarding complaints mechanisms as well as their rights as citizens and consumers. Moreover, improving the role of the media[209] and better utilization of so-called 'e-government' in record management[210], can also have a significant impact on transparency and accountability in the water sector.[211]

The issue of transparency in the environmental and natural resource sectors is also reflected in principle 10 of the Rio Declaration on Environment and Development, adopted at the United Nations Conference on Environment and Development (UNCED) in Rio de Janeiro in June 1992. Among other things, principle 10 states the following: "At the national level, each individual shall have appropriate access to information concerning the environment that is held by public authorities, including information on hazardous materials and activities in their communities, and the opportunity to participate in decision-making processes. States shall facilitate and encourage public awareness and participation by making information widely available."

Principle 10 is further operationalized in the 'Aarhus Convention', adopted by the UN Economic Commission for Europe (UNECE) in June 1998, which is the only legally binding instrument implementing this principle. Among other things, the Aarhus Convention provides practical principles on access to environmental information (Article 4), collection and dissemination of environmental information (Article 5), and regarding public participation in specific decisions and during the preparations of plans, programmes, policies, regulations and other legislative instruments relating to the environment (Articles 6-8). Although this convention currently has a regional focus as most of the parties are countries in Europe and central Asia, it still sets important standards on rights to information and participation in the environmental and natural resource sectors which have relevance on the global level as well.[212]

Prerequisites:

A fundamental prerequisite for the provision of, and access to information for the public is the existence of Freedom of Information (FOI) legislation. Among other things, FOI legislation and associated regulations and procedures should contain[213]:

- *Provisions requiring government agencies to publicize basic information* regarding their structure, functions, operations and performance. By doing this, the agencies both provide a basis for general information and transparency, and also enable the media and the citizens to make more focused inquiries and ask for more specific information. Such publications could, inter alia, include information about budgets, new legislation, reports on activities, etc. Moreover, publications of general interest should be made in a format which makes them understandable to the public at large. Ideally, such publications should also be made available on the Internet;

[209] See subchapter 3.2.3.
[210] See subchapter 4.3.5.
[211] Plummer and Cross, 2007, p. 239.
[212] Stanley-Jones, Michael, 2011. The Aarhus Convention. A blueprint for inclusive and accountable climate governance?, pp. 87-88, in: Sweeney, Gareth et al. (eds.), 2011. Global Corruption Report. Climate Change. Transparency International. [Online] Available at www.transparency.org/content/download/60586/970870/Global_Corruption_Report_Climate_Change_English.pdf [Accessed on 9 May 2011].
[213] Pope, 2000, pp. 236-37, 239-40, 245-46; UNODC, 2004, pp. 302-03.

- *A legal and enforceable right of access for citizens to documented information*, including records, controlled by the government. To ensure that disclosure is the rule instead of the exception, exemptions to this access - for instance to protect national security or personal privacy – should be used with caution. Hence, it also follows that it is the government agency concerned which should bear the burden of justifying non-disclosure. That is, where access to documents and records is rejected, the state agency in question should be required to inform the person concerned of the grounds for the denial, with reference to the specific exemption which applies to the documents requested;
- *Provisions which require government to facilitate this access*, and with time limits for responding to requests. As part of this, most FOI laws contain provisions which stipulate that state agencies must publicize lists of the records series they have in their archives. Access should either be provided by giving the person making the inquiry a copy of the document(s) in question or by giving her or him sufficient time to study the document(s).[214]
- *Provisions that establish a review mechanism* for deciding whether the requested information can be released or be exempt from access. Ideally, if the review concludes that only a part of the information requested should be exempt from access, a copy of the document including only the information which can be released should be provided instead of denying access completely;
- Furthermore, in case of denial, the requester should also have *the opportunity to appeal for a second review* – at a higher level than the first review – in the state agency concerned. Time limits for responding to appeals should also be provided for.

In case the denial of access is upheld after the second review, it is important that the requester then can turn to *an independent arbitrator outside of government*, for instance an ombudsman. This should also be provided for in legislation, as appropriate.

On this background, the following questions can be relevant to consider for auditors:

- **Are government agencies required to publicize basic information on what they do and how they do it on a regular basis?**

- **Are publications of general interest made in a format which makes them understandable to the public at large?**

- **Are publications and the lists of the records series held by the various government agencies available on the Internet?**

- **Do citizens have a legal and enforceable right of access to documented information, including records, controlled by the government?**

- **Are exemptions to this access clearly specified in the relevant legislation?**

- **Is there a review mechanism in place for deciding whether the requested information can be released or be exempt from access?**

[214] UNODC also points out, however, that the disclosure of, and facilitation of access to information is not sufficient to ensure full transparency. It is also required that this information is produced and collected in a format which is reliable and easily comprehensible. (UNODC, 2004, p. 243). For a discussion of records management and quality criteria for public reports and records, see subchapter 4.3.5.

- **In case of denial of access, is it required for government agencies to inform the person concerned of the grounds for the denial, with reference to the specific exemption which applies to the documents requested?**

- **Are such exemptions often used without proper justification and/or in a non-transparent manner to prevent citizens and journalists from getting access to information?**

- **Are government agencies required to facilitate access, so that disclosed information is available not only in principle, but also in practice?**

- **In case of denial of access, does the the requester have *the opportunity to appeal for a second review* – at a higher level than the first review – in the state agency concerned?**

- **Are there clear time limits in place for responding to requests and appeals?**

- **In case the denial of access is upheld after the second review, is there an independent body in place such as an Ombudsman to oversee and protect the rights of the citizens?**

- **Does the right of access to information include information held by local authorities and state-owned companies?**

Box 3.3 provides an illustration of some of the elements presented in this subchapter within an environmental and natural resource management context.

Box 3.3
Case: Transparency in forest management in Bolivia

The forests in Bolivia cover almost 50 % of the total area of the country. The majority of these forests are located in the tropical lowlands and in the subtropical valleys which lead to the highlands, and approximately 1.4 million people in these parts of the country are to some extent dependent on the forests for their livelihoods. From the beginning of the 1990s there was a growing concern in the country that the forests were in danger, partly due to political patronage, corruption and forest crime. Hence, there was also a growing recognition that the old forest management regime in Bolivia was not functioning properly, and that something had to be done to improve governance and to ensure sustainable management of these resources.

During the mid-1990s, the Bolivian government therefore introduced several policy and institutional reforms, of which a new forestry law was one but several measures. These reforms are among the most far-reaching anywhere, and many of the measures introduced are in conformity to 'textbook' models of forest management.

As to the forestry law itself – Forestry Law 1700 of July 1996 – it was the result of a very transparent process with exceptionally wide participation which was unprecedented in the history of law-making in Bolivia. In addition to the central government, political parties and

local authorities, the main actors also included environmental NGOs (ENGOs), indigenous groups, international organizations such as the World Bank and FAO, private companies, settlers and farmers, the media, as well as an NGO representing the chain saw operators.

The new forest management regime, established by the Forestry Law and associated legal norms and regulations, contains several specific measures to combat forest crime and corruption, of which transparency is a key element. Among other things the new regime included:

- Free access for any citizen to information regarding the activities of public authorities and to request copies of official documents;
- Special authorizations for citizens and ENGOs to inspect logging operations in the fields ('libramiento de visita'), providing them with the same opportunities as public inspectors to detect and call attention to illicit acts;
- Participation by local community associations in decision-making regarding forest management issues in order to achieve a better system of 'checks and balances' at the local level;
- A new and transparent procedure for the setting of fees for timber concessions, replacing the former practice which provided too much room for discretion – and corruption;
- Allocation of all new concession contracts through open auctions;
- Requirement for the logging companies to carry out audits by recognized independent bodies every five year, to make sure that management plans are being implemented in accordance with government guidelines;
- The holding of annual public hearings by the head of the executive forestry agency to report to the public on the work carried out and on the use of financial, human and capital resources, and to provide the public with the opportunity to raise questions regarding performance.

The reforms in the forestry sector in Bolivia have not been without difficulties, and have yet to deliver on several of their promises. Still, they have received wide recognition for the successful reduction of fraud and corruption in this sector.

Sources:

Kishor and Damania, 2007, p. 106; FAO, 2001. State of the World's Forests 2001. [Online] Available on www.fao.org/docrep/003/y0900e/y0900e00.htm [Accessed on 25 August 2011], pp. 96, 98; Contreras-Hermosilla, Arnoldo and Rios, Maria Teresa Vargas, 2002. Social Environmental and Economic Dimensions of Forest Policy Reforms in Bolivia. Forest Trends. [Online] Available at www.cifor.org/publications/pdf_files/Books/BoliviaEnglish.pdf [Accessed on 30 June 2011], pp. 1-5, 8; Colchester, Marcus et al., 2006. Justice in the forest. Rural livelihoods and forest law enforcement. Center for International Forestry Research (CIFOR). [Online] Available at www.cifor.org/publications/pdf_files/Books/BColchester0601.pdf [Accessed on 1 June 2011], pp. 10, 21, 25, 43, 55-56.

3.2.5 The Judiciary and prosecution services

The Judiciary is also a cornerstone of the NIS. An informed, impartial and independent Judiciary is crucial to ensure that the government acts in a transparent, just and accountable manner. To carry out its constitutional role of reviewing the conduct of government and public officials to decide if they abide by the standards prescribed by the Constitution and the laws passed by the Legislature, and of ensuring that laws enacted by the Legislature are in accordance with the constitution or other legal requirements, the Judiciary must be

independent of both the Executive and Legislative branches of government. As such, it is right at the centre of the separation of powers. In addition, due to its unique position, the degree to which the Judiciary strives for and attains a high level of integrity will also set a standard for other institutions and officials in society.[215]

Furthermore, judicial decisions which are in accordance with the law, and which are fair and consistent with one another – i.e. which maintain the Rule of Law – will also support an environment where legitimate economic activities can thrive and fraud and corruption can be prevented, detected and penalized. Hence, the integrity, professionalism and competence of judges are also vital if efforts to fight fraud and corruption are to be successful. The crucial role of the Judiciary is therefore also recognized in Article 11.1 of UNCAC.[216]

At the same time, there is mounting evidence that fraud and corruption is widespread in the Judiciary in many parts of the world, and surveys also indicate that the citizens in many countries consider their judiciaries to be hopelessly corrupt. In many instances, this is a primary indicator that fraud and corruption is spiraling out of control in the country in question and approaching systemic levels.[217]

Fraud and corruption in the Judiciary may take many different forms. One example, which is a very blatant one, is where the Executive appoints as many as possible of its supporters or allies to the court system. Another example is where the assignment of cases is manipulated by the Executive to make sure that it is the 'right' judge who is responsible for a case which is important to the government. A third example is various forms of bribery. These can be subtle – such as awarding of honours or favourable rankings – or more obvious – for instance providing cars, houses, and privileges to the children of judges. Moreover, it may also be the other way around, i.e. that the Executive employs various negative incentives to pressurize judges to make the 'right' decisions by posting them to unattractive locations, withdrawing benefits, downsizing court facilities, etc. In addition, the Judiciary may also be vulnerable to fraud and corruption due to the misconduct of those around them. Court officials may for instance receive bribes to 'lose' files, delay cases or assign them to corrupt judges at lower levels, or lawyers may be bribed to act contrary to the interests of their clients.[218]

When the Judiciary is corrupt, the institutional and legal mechanisms which are designed to curb fraud and corruption remain ineffective. Moreover, if the fraud and corruption is too prevalent, the general utility and status of the courts and the judges also tend to diminish, thereby setting a poor standard for other institutions and the society at large. Hence, a corrupt Judiciary will have a negative impact on the fight against fraud and corruption both directly and indirectly. This poses a major challenge for SAIs around the world.[219]

At the same time, however, the independence of the Judiciary raises unique difficulties for SAIs and others wishing to address fraud and corruption within this particular pillar of the national integrity system. The independence of the Judiciary is absolute, and only the Judiciary itself can review its own judicial decisions through the appeal courts. Hence, any measure intended to prevent and detect fraud and corruption in the Judiciary must at the same time have due regard to the independence of judges and their need for protection from threats

[215] Pope, 2000, p. 63; UNODC, 2004, p. 118.
[216] UNODC, 2004, p. 110.
[217] Pope, 2000, p. 64; Dye, 2007, pp. 308-309
[218] Pope, 2000, pp. 65-66.
[219] Dye, 2007, pp. 308-309; UNODC, 2004, pp. 116, 118.

or intimidation, and must also ensure that judicial decision-making is not adversely influenced.[220]

Taking this into account, the following aspects of the Judiciary can be relevant for further scrutiny by auditors and other relevant actors:

- ***Appointments to the judiciary, promotion and remuneration:*** The ways in which judges are selected are critical to their independence. Hence, the appointment process should focus on selecting judges that have high standards of integrity and fairness, and appropriate training and competence in the field of law. Similarly, promotion of judges should also be based on objective criteria such as professional experience, merit and performance. Moreover, remuneration should also be adequate. Transparency in the nomination and appointment process and with regard to the qualifications of the nominated candidates is therefore crucial, as this will permit close examination and make it difficult to apply improper procedures.[221]

- ***Security of tenure, removal and protection of judges:*** To protect their independence, the tenure of office for judges also must be secured, ideally by written law. Similarly, in case of removal of a judge from office or his/her suspension, this should only happen in accordance with appropriate and clearly defined procedures, and only due to incapacity or other circumstances which make them unfit to do their job. The grounds for removal should also be presented before a body which has a judicial character. Furthermore, where there is a risk that judges may be subject to negative incentives such as threats, harassments or assaults, appropriate mechanisms must be in place to protect them and their family members.[222]

- ***Code of Conduct (CoC):*** A judicial Code of Conduct (CoC) is also important to maintain the integrity and impartiality of judges. Such codes do not necessarily have to be formulated by the judges themselves to ensure judicial independence, but judicial participation in this process is still advisable, however. Judicial participation is important both to make sure that the provisions being developed are appropriate, and subsequently to ensure that judges adhere to them. It is also advisable that it is the judges themselves who have the power to apply such codes to individual judges. Furthermore, judges should also receive training to make them familiar with the code, and to inform them of the consequences if they are found to violate its provisions. To ensure transparency, the code should also be publicized.[223]

- ***Disclosure of assets and incomes:*** As for other key officials, a requirement also for judges to disclose relevant information on their assets and incomes can be an important tool to prevent and detect fraud and corruption also within the Judiciary. In that case, to ensure that this requirement is complied with, judges must be subject to audits. If these audits are to be performed by officials outside the Judiciary, however, they must be

[220] UNODC, 2004, pp. 110, 114, 117-18.
[221] UNODC, 2004, pp. 113, 116; Pope, 2010, pp. 67-68. For a further discussion of human resource policies and practices, see subchapter 4.3.3.
[222] Pope, 2000, p. 68; UNODC, 2004, p. 115.
[223] Pope, 2000, p. 69; UNODC, 2004, pp. 112-13, 119. For a further discussion of the 'Code of Conduct'-concept, see subchapter 4.3.1.

carried out on a random basis to protect judicial independence. In case of follow-up investigations, these should under any circumstance be conducted by fellow judges.[224]

- ***Transparency of legal proceedings:*** To the extent possible, legal proceedings should be held in an open court, where also the media and civil society – in addition to the parties directly involved – should have access. Furthermore, public commentaries by the media and others on, inter alia, the fairness, integrity and efficiency of the proceedings and their outcomes are also important for the transparency of the Judiciary. Hence, such commentaries should not be unduly restricted by laws, court orders or 'contempt-of-court' sentences/fines. Finally, the appropriate management structures should also be in place in the administrative apparatus of the courts, including a proper system for records management and tracking of cases.[225]

- ***Assignment of judges and cases:*** A corrupt judge is not sufficient if someone wants to influence the outcomes of legal proceedings in an improper manner. The judge in question also must be assigned the specific case where a specific outcome is wanted by offenders. Hence, to prevent this from happening, procedures must be in place which make it difficult for people outside the Judiciary to foresee or affect decisions regarding which judges will have the responsibility for which cases. Randomness and transparency in the assignment process, as well as regular rotation and reassignment of judges are among the measures which can be relevant in this regard.[226]

- ***Complaints mechanism:*** The appeal courts are the primary forums for reviewing judicial decisions. However, when it comes to possible misconduct and wrongdoings within the Judiciary itself, there should also – to protect judicial independence – be some sort of 'self-regulation bodies' such as judicial councils or similar disciplinary bodies in place, where the judges themselves could investigate complaints, impose disciplinary actions and remedies, and develop preventive measures.[227]

Prosecution services:

In criminal matters the Judiciary also must rely on other actors. It will be difficult, if not impossible for the criminal process to deal with major fraud and corruption cases which affect the interests of those in political power if investigators and prosecutors at the same time are under the control of the politicians. Hence, to ensure that prosecutions on behalf of the state are conducted in a fair and reasonable manner – i.e. to maintain the Rule of Law – public prosecutors should enjoy the same independence as judges, and not be subject to any undue influence from politicians or other interested parties. One fundamental prerequisite in this regard is the existence of clear and transparent guidelines which govern the decisions on whether or not to investigate/prosecute, and how to conduct these processes.[228]

The importance of the integrity and independence of the prosecution services is also reflected in article 11.2 of UNCAC, which recommends that the measures taken to promote integrity and prevent fraud and corruption in the Judiciary also should apply to the prosecutions services in those states where these services are not part of the Judiciary.

[224] UNODC, 2004, pp. 114-15. Disclosure of assets, incomes, etc. is also further discussed in subchapter 4.3.1.
[225] UNODC, 2004, pp. 114, 116. Records management is further accounted for in subchapter 4.3.5.
[226] UNODC, 2004, pp. 113-14.
[227] UNODC, 2004, pp. 112, 114, 119.
[228] Pope, 2000, pp. 71-72.

On this background, the following questions can be relevant to consider for auditors[229]:

- **Does the Judiciary have a professional recruitment system in place to ensure that applicants have the proper education and experience and the integrity required to carry out their job?**

- **Is the recruitment process transparent? Among other things, are vacant positions and recruitment criteria publicized?**

- **Are judges offered adequate remuneration, taking into account the level of economic development in the country in question?**

- **Are salary increases, promotion and other forms of compensation for judges closely connected with professional experience, merit and performance?**

- **Is the tenure of office for judges appropriately secured? In case of removal from office – are the appropriate procedures and apparatus in place?**

- **Are judges and their family members appropriately protected against threats, harassments or assaults?**

- **Does the Judiciary have a Code of Conduct (CoC) in place and the appropriate mechanisms to ensure that it is applied in a fair and proper manner? Have judges received appropriate training to make them familiar with the CoC?**

- **Is there a system in place for monitoring the incomes, assets and business interests of judges, as well as a judicial body to monitor follow-up investigations?**

- **Are legal proceedings transparent and – as far as possible – held in an open court? Are the media and others free to make public commentaries on the legal proceedings and their outcomes? Are the appropriate management structures to support transparency in place?**

- **Are there procedures in place to prevent improper assignments of judges and cases?**

- **Are there 'self-regulation bodies' in place to deal with cases of possible misconduct and wrongdoings within the Judiciary itself?**

- **Are clear and transparent guidelines which govern the decisions on whether or not to investigate/prosecute, and how to conduct these processes, in place?**

- **If the prosecution services are independent of the Judiciary – are the measures to promote integrity and prevent fraud and corruption in the Judiciary, described above, also implemented for the prosecution services as appropriate?**

Box 3.4 provides an illustration of some of the elements presented in this subchapter within an environmental and natural resource management context.

[229] For a more comprehensive checklist when investigating the role of the Judiciary in fighting fraud and corruption, see UNODC, 2004, pp. 488-495.

Box 3.4
Case: The role of the Judiciary in an oil pollution case in Ecuador

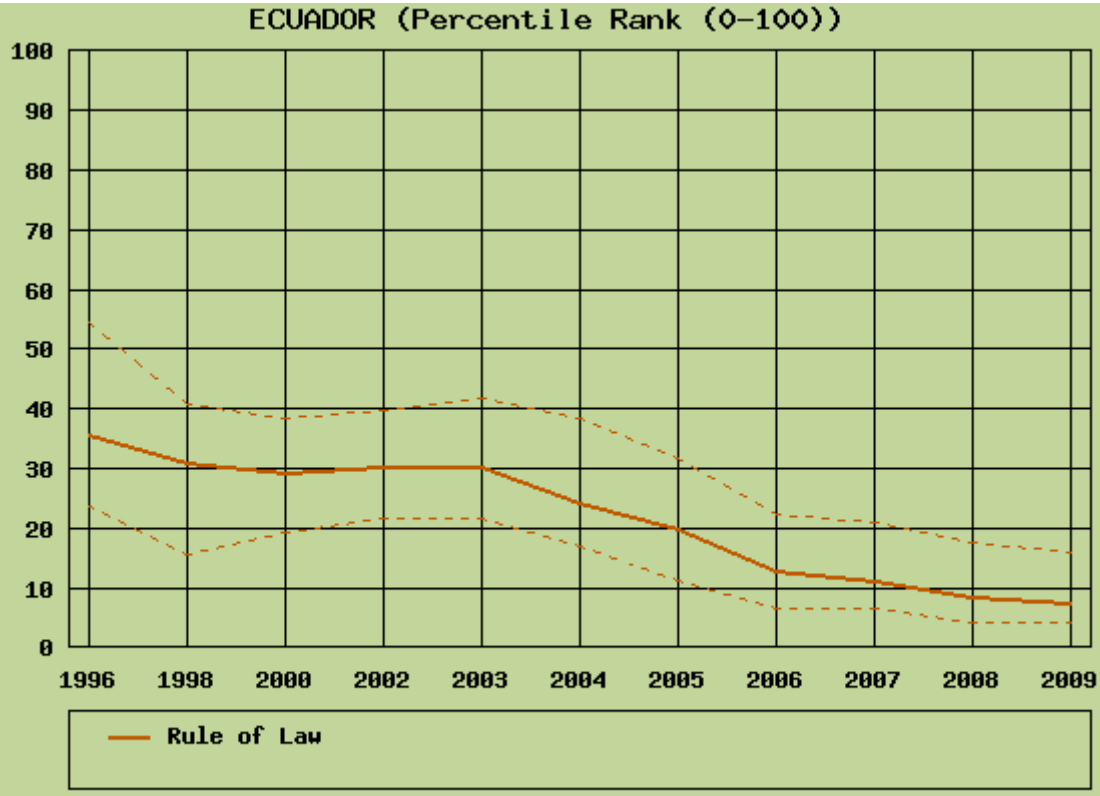
Fraud and corruption in the Judiciary in Ecuador:

In its 'Freedom in the World'-report for Ecuador in 2003, Freedom House pointed out that the corruption which was afflicting the whole political system in Ecuador, also generally undermined the Judiciary in the country. In 2005, due to growing concern arising from reports on a severe institutional crisis within the justice system in the country, the International Bar Association (IBA) and the Human Rights Institute (HRI) went on an investigative mission to Ecuador in April 2005. In its report from the mission, IBA reported, inter alia, the following: Although Ecuador had laws guaranteeing the independence of the Judiciary and due process, in many cases this independence was non-existent, partly due to extensive politicizing of the legal system. Furthermore, although official data were lacking, the information gathered through the investigation supported the perception that the Judiciary in Ecuador was pervaded by a high level of corruption, thereby further obstructing its independence. Moreover, it was also discovered that there were no adequate controls in place to address 'conflicts of interest', which both led to the violation of due process, at the same time as it provided opportunities for holding posts inappropriately. In addition, the investigation revealed that the procedures provided for in the constitution and in legislation to redress injustices – such as disciplinary proceedings and dismissal processes – were not always applied as they were supposed to.

On this basis, IBA presented, inter alia, the following recommendations: Urgent reform of relevant rules and regulations to provide for due process and to prevent interference in judicial processes by external actors; stronger control of those responsible for constructing and maintaining the justice systems; stricter adherence to the system prescribing appointments within the legal profession based on qualifications and merits; independent and just appointment of the Attorney-General, and regulations in place which ensure that she or he fulfils her/his duties in a proper, ethical and independent manner; and, more generally, strengthening of the mechanisms to control corruption.

The concerns raised by IBA were also reflected in the Freedom House's 'Countries at the Crossroads'-report for Ecuador in 2007 – particularly in respect of the politicization issue. In this report, it was pointed out that political factions – both in government and among the opposition parties – systematically violated judicial independence and judicial review. As an example in this regard, the report refers to the dismissal of individual judges and later the entire Supreme Court in the period December 2004 to April 2005 through congressional resolution and presidential decree. Moreover, according to the report, even the new judges of the Supreme Court appointed in November 2005 – who were selected through a lengthy, rigorous and merit-based selection process, monitored by the UN, the Organization of American States (OAS) and NGOs – seemed to be vulnerable to political pressures. This is also reflected in Freedom House's 'Freedom in the World'-report for Ecuador in 2010, where it is emphasized that the Judiciary – in addition to the general threat from corruption within all government agencies – in recent years also has been subject to substantial political pressures.

This tendency can also be seen in the WGI-indicator for the 'Rule of Law'-dimension in Ecuador, which shows a downward trend during the entire period in question – from a low level in 2003 to a very low level in 2009.



Source: Kaufmann D., A. Kraay, and M. Mastruzzi (2010), The Worldwide Governance Indicators: Methodology and Analytical Issues

The oil pollution case:

The oil pollution became a judicial case in 1993 when a group of Ecuadorian citizens brought a class action lawsuit against Texaco, a U.S. oil company, in a U.S. federal court. The plaintiffs alleged that the company – as part of its operations in the Oriente region – from the beginning of the 1970s until 1992 had discharged billions of gallons of crude oil and toxic chemicals into the land and waterways in the Amazon rainforest. In addition to the reported damages to the environment and the wildlife in the region, the extraction of oil also have had serious negative impacts on the local indigenous communities, of which two groups allegedly also have been brought close to extinction. The cancer rate in this region is also among the highest in Ecuador, and the pollution of the Oriente region has been referred to as 'the Amazon's Chernobyl'.

In 1996, four years after Texaco had ceased all operations in Ecuador, the company agreed to spend approximately USD 40 million to clean up and remediate the damages caused. In 1998, the government in Ecuador also signed an agreement with Texaco, where the former confirmed that the latter had completed the remediation. The plaintiffs disagreed with this conclusion, however, and they also maintained that this agreement did not affect third-party claims as it only concerned Texaco's obligations towards the government in Ecuador.

In 2001, Texaco was bought by Chevron, another U.S. oil company, which then 'inherited' the oil pollution case from the former. In 2002, after Texaco's and later Chevron's lawyers had argued that the case should be transferred to Ecuador, the US federal court dismissed the case on the grounds that it was the Judiciary in Ecuador which had jurisdiction. In 2003, the plaintiffs – approximately 30.000 people – then brought the lawsuit against Texaco/Chevron in Ecuador instead, claiming USD 6 billion in damages.

However, the same year as the case was filed in Ecuador, the Review of International Social Questions (RISQ) pointed out that – although the costs of the damages in the case against Texaco/Chevron was estimated to be more than USD 1 billion – the civil justice system in Ecuador had never imposed fines larger than USD 1 million on any international oil company. For several years after 2003, the plaintiffs also experienced serious challenges in bringing their case through the Ecuadorian court system. Contrary to what the plaintiffs claimed, Chevron denied that the oil-production sites which they had remediated still contained toxic substances at levels which posed significant risks to human health, and in 2006, the Supreme Court in Ecuador supported the findings of the company.

Furthermore, later in 2006, the International Commission of Jurists (ICJ) sent a letter to the Ecuadorian authorities where it expressed its grave concern regarding the reported severe and continuous harassment of lawyers in Ecuador representing the plaintiffs in the case against Chevron. ICJ was particularly concerned that some of the acts of harassment also reportedly involved government officials. On this background, the ICJ urged Ecuadorian authorities to ensure that the case ('Aguinda v. ChevronTexaco') be conducted "in a fair, independent and impartial manner in compliance with the international standards on the administration of justice." Moreover, according to a study from 2006 sponsored by Transparency International, although evidence of bribes being paid is lacking, there are many reports which assert that the ties between Texaco and the Ecuadorian judiciary were strong.

Gradually, however, the situation changed. Although the executive branch in Ecuador for quite some time had been known to interfere in the business of the Judiciary, the interference seemed to become even more common after a new president came into office in 2007. In 2008, a new constitution was drafted, which for the first time made it possible to review the rulings of the Ecuadorian Supreme Court by a 'constitutional court' controlled by the government. Furthermore, reportedly, the new president also involved himself more and more in the 'Aguinda v. ChevronTexaco'-case. In 2006, and again in 2009, Chevron brought a claim for international arbitration before the Permanent Court of Arbitration (PCA) in the Hague, Netherlands, against Ecuador. Although the arbitration claim had its origin in seven claims filed by Texaco in Ecuador between 1991 and 1993, it also had direct relevance for the oil pollution case, however. This because Chevron, in its claim, asserted that the Ecuadorian Government had unduly influenced the Judiciary in the country, thereby compromising its independence – and thereby also violating US-Ecuador bilateral treaties and international law.

In February 2011, the PCA also ruled in favour of the company, as it ordered Ecuadorian authorities to suspend enforcement of any judgement in the Ecuadorian legal proceedings against Chevron relating to the oil pollution-case. Almost simultaneously, on 9 February 2011, a U.S. federal judge made the same decision regarding enforcement in the United States of judgements in the case against Chevron. Then, on 14 February 2011, just a few days later, a judge in the Lago Agrio court in Ecuador ruled that Chevron should pay USD 8,6 billion in damages and remediation costs – a fine that later increased to USD 18 billion as Chevron would not issue a public apology for the damages caused. Then again, in a U.S. federal court on 8 March 2011, the temporary restraining order from 9 February was further extended. In the ruling, the judge raised serious concerns regarding the legitimacy of the Lago Agrio-judgement. Among other things, he pointed out that the Ecuadorian judiciary had been corrupt for years, but that the situation had worsened since 2007. More specifically, he pointed out that Ecuadorian judges at all levels, in particular those dealing with cases of interest to the Government, were subject to continuous threats and pressure from the president.

On 19 September 2011, a U.S. appeal court reversed the 9 February restraining order. [To be updated].

Sources:

Freedom House, 2003. Freedom in the World – Ecuador. [Online] Available at www.freedomhouse.org/template.cfm?page=22&year=2003&country=381 [Accessed on 20 September 2011]; International Bar Association, June 2005. Ecuador: Strengthening of the Judiciary. Executive Summary. [Online] Available at www.ibanet.org/Article/Detail.aspx?ArticleUid=d80193cf-3363-4235-96cb-05358ecb888b [Accessed on 26 September 2011]; Freedom House, 2007. Countries at the Crossroads – Ecuador. [Online] Available at www.freedomhouse.org/uploads/ccr/country-7169-8.pdf [Accessed on 26 September 2011]; Freedom House, 2010. Freedom in the World – Ecuador. [Online] Available at www.freedomhouse.org/template.cfm?page=363&year=2010&country=7815 [Accessed on 20 September 2011]; The Rule of Law-indicator for Ecuador is available at http://info.worldbank.org/governance/wgi/sc_chart.asp [Accessed on 26 September 2011]; Business & Human Rights Resource Centre. Case profile: Texaco/Chevron lawsuits (re Ecuador). [Online] Available at www.business-humanrights.org/Categories/Lawlawsuits/Lawsuitsregulatoryaction/LawsuitsSelectedcases/TexacoChevronlawsuitsreEcuador [Accessed on 29 September 2011]; Dillon et al., 2006, p. 31; The New York Times: Judge at Heart of Landmark Oil Pollution Case Unfazed by Spotlight. Published 17 May 2011. [Online] Available at www.nytimes.com/gwire/2011/05/17/17greenwire-judge-at-heart-of-landmark-oil-pollution-case-89753.html?pagewanted=all [Accessed on 31 May 2011]; The Independent: Chevron's dirty fight in Ecuador. Published 16 February 2011. [Online] Available at www.independent.co.uk/environment/nature/chevrons-dirty-fight-in-ecuador-2216168.html [Accessed on 31 May 2011]; The Guardian: Chevron fined $8bn over Amazon 'contamination'. Published 14 February 2011. [Online] Available at www.guardian.co.uk/business/2011/feb/14/chevron-contaminate-ecuador [Accessed on 28 September 2011]; The New York Times: Chevron Allegations About Justice System Strike a Nerve in Ecuador. Published 23 May 2011. [Online] Avaialable at www.nytimes.com/gwire/2011/05/23/23greenwire-chevron-allegations-about-justice-system-strike-5160.html?pagewanted=all [Accessed on 31 May 2011]; Review of International Social Questions (RISQ): Landmark Trial Against Chevron-Texaco In Ecuador. Published 25 October 2003. [Online] Available at www.risq.org/article196.html [Accessed on 20 September 2011]; The Economist: Justice or extortion? Published 21 May 2009. [Online] Available at www.economist.com/node/13707679 [Accessed on 28 September 2011]; International Commission of Jurists (ICJ): Press Release – International Commission of Jurists Condemns Harassment of Lawyers involved in Case Against US Oil Company in Ecuador. Published 14 June 2006. [Online] Available at www.icj.org/dwn/database/PR_Ecuador_14062006.pdf [Accessed on 29 August 2011]; The New York Times: Chevron Looks to Arbitrators to Save It From $18B Pollution Payout. Published 2 June 2011. [Online] Available at www.nytimes.com/gwire/2011/06/02/02greenwire-chevron-looks-to-arbitrators-to-save-it-from-1-53361.html?pagewanted=all [Accessed on 29 August 2011]; Reuters: Chevron awarded $96 mln in Ecuador govt dispute. Published 31 August 2011. [Online] Available at http://www.reuters.com/article/2011/08/31/chevron-ecuador-idUSN1E77U1OL20110831 [Accessed on 28 September 2011]; The Economist: Monster or victim? A court in Ecuador controversially fines Chevron a whopping $ 9 billion. Published 17 February 2011. [Online] Available at www.economist.com/node/18182242 [Accessed on 28 September 2011]; New York Times: Chevron Wins Injunction Against Ecuadorean Plaintiffs. Published 8 March 2011. [Online] Available at www.nytimes.com/gwire/2011/03/08/08greenwire-chevron-wins-injunction-against-ecuadorean-pla-52066.html [Accessed on 26 September 2011]; San Francisco Chronicle: U.S. court rules against Chevron in Ecuador case. Published 20 September 2011. [Available at http://www.sfgate.com/cgi-bin/article.cgi?f=/c/a/2011/09/19/BU5B1L6N82.DTL [Accessed on 29 September 2011].

3.2.6 Legislation pertaining to fraud and corruption

As mentioned in subchapters 3.2.2 and 3.2.5 – and which also will be accounted for more in depth in subchapter 4.3.1 – the existence of ethical guidelines/Codes of Conduct and other administrative guidelines are important to address conflicts of interests and prevent fraud and corruption in the Legislative, Judicial and Executive branches of government. However, to provide for effective deterrence – and hence prevention – of more serious cases of fraud and corruption, such cases also must be sanctioned through criminal or administrative law. Moreover, in addition to the acts of fraud and corruption per se, sanctions also must apply to

actions which make fraud and corruption possible as well as the incentives behind such activities, i.e. the proceeds of fraud and corruption.

Furthermore, penal provisions pertaining to fraud and corruption must – as far as possible – be applicable to any public official, irrespective of level or position, and generally be applied in the best interests of the State and its citizens. Finally, legislation – with appropriate sanctions – which provides for effective detection of fraud and corruption also must be in place.

National legal sanctioning instruments:

UNCAC provides a fundamental global benchmark when it comes to national legal instruments for the criminalization and sanctioning of fraudulent and corrupt behaviour, more specifically in its Chapter III on "Criminalization and law enforcement". Here, the UN Convention prescribes or suggests that State Parties adopt measures through legislation and otherwise to criminalize several of the acts described in Box 2.1 in subchapter 2.1.3.[230] In addition, UNODC suggests that states – under special circumstances – also consider sanctioning, through criminal or administrative law, other acts such as conflicts of interests, nepotism and favouritism, and party funding. [231]

Furthermore, in Article 20, UNCAC also suggests that State Parties shall consider adopting measures to criminalize so-called 'illicit enrichment'. This term refers to a substantial increase in the standard of living and/or the assets of a (former) public servant or government official which is significantly disproportionate to her or his known legal income in the past or the present, and which she or he cannot explain in a satisfactory manner. Both at the national and at the international levels there is an increasing tendency to criminalize the possession of such 'unexplained wealth' as it has been recognized as a relevant measure in the fight against fraud and corruption.[232]

As to actions which make fraud and corruption possible, UNCAC also addresses this, inter alia in Article 23 which pertains to money laundering. In this article, the UN Convention stipulates that State Parties adopt measures through legislation and otherwise to criminalize, inter alia, the intentional transfer or conversion of assets, disguise or concealment of the true origin or ownership of assets, the acquisition or possession of assets, etc. knowing that such assets are the proceeds of crime. Moreover, to facilitate the implementation of the provisions on money laundering, paragraph 2 in this article prescribes that State Parties shall seek to apply these provisions to as many relevant criminal offences as possible (so-called 'predicate offences'), including offences established in accordance with UNCAC.

When it comes to the incentives behind fraudulent and corrupt activities, i.e. the proceeds or profits from such activities, this is dealt with both in Article 31 of UNCAC, which stipulates that State Parties shall do their utmost to enable freezing, seizure and confiscation of proceeds of crime, and in Chapter V (Articles 51-59) which deals with asset recovery.

[230] For public officials, the most relevant articles in this regard are the following: Article 15. Bribery of national public officials; Article 16. Bribery of foreign public officials and officials of public international organizations; Article 17. Embezzlement, misappropriation or other diversion of property by a public official; Article 18. Trading in influence; Article 19. Abuse of functions.
[231] UNODC, 2004, p. 429.
[232] UNODC, 2004, p. 429.

As a general principle, UNCAC also sets forth that its provisions only represent minimum standards, so that State Parties are free to keep or adopt measures to prevent and combat fraud and corruption which are stricter or more severe than those stipulated in the Convention.[233]

Amnesty, immunity and reduction of punishment:

In general, the use of amnesty or immunity in cases of fraud and corruption is incompatible with the objectives of deterrence, responsibility for criminal acts, and the dismissal of persons found guilty of fraudulent and corrupt behaviour from positions where they are likely to repeat such behaviour. There are several provisions in UNCAC which support these objectives, in particular Article 30, which stipulates that State Parties shall impose sanctions which have due regard to the seriousness of the offence in question.[234] Article 30 also makes it clear that the jurisdictional privileges and immunities which particular public officials enjoy in order to perform their functions must be carefully balanced against the need for effective investigation, prosecution and adjudication of fraud and corruption offences.

At the same time, however, there are circumstances where amnesty or immunity might be justified. For instance, in instances where the accused person has cooperated with or provided assistance to relevant authorities, for instance by reporting fraudulent and corrupt activities, immunity from prosecution or the reduction of punishment may be offered. Such instances are dealt with in Article 37 of UNCAC. More generally, in fraud and corruption cases where many officials at low levels are involved, it is not unlikely that a general amnesty combined with a subsequent re-training programme may be considered to be a more rational approach than accepting all the expenses resulting from the many prosecutions and the replacement of the many officials involved.[235]

Furthermore, in cases of 'grand corruption', it may also be rational to offer amnesty to government officials at the highest levels as part of a negotiation process aiming at a trouble-free and peaceful transfer of power and/or recovery of assets. Apart from immunity and reduction of punishment according to Article 37, i.e. cooperation with authorities, cases like these often have a political dimension and are normally resolved by the governments involved on a 'case-by-case' basis. Amnesties like these should be used with great caution, however, as repeated use of amnesties inter alia involves the risks of eroding deterrence and of undermining the rule of law. This again may 'pave the way' for fraudulent and corrupt acts in the future, as it may give rise to expectations that also these acts will be forgiven or overlooked. In environments where corrupt officials previously have enjoyed impunity this is a particular concern as an amnesty may be perceived only as a prolongation of previous practices instead of a 'fresh start'. [236]

National legal instruments facilitating detection of fraud and corruption:

As mentioned in chapter 2, fraud and corruption are – by their nature – often covert activities. Hence, in addition to penal provisions to provide for effective deterrence, particular legislation to facilitate the detection of fraud and corruption is also required. Among other

[233] UNODC, 2004, p. 430.
[234] UNODC, 2004, p. 435.
[235] UNODC, 2004, p. 435.
[236] UNODC, 2004, p. 435, 437.

things, this includes legislation to protect 'whistleblowers' and address money-laundering, administrative law and access to information legislation.[237]

Whistleblower protection:

The main objective with legislation on 'whistleblowing' is to protect people who report cases of fraud and corruption, mismanagement, and other illicit or improper conduct. In UNCAC this is dealt with in Articles 32 and 33, respectively, with regard to "witnesses, experts and victims" and "reporting persons". Such protection increases the motivation to report, or, at the very least, reduces the incentives to refrain from reporting due to fear of persecution, dismissal or other kinds of revenge. A culture of secrecy, silence and apathy provides a fertile ground for fraud and corruption, and such cultures continue to thrive when the whistleblowers are intimidated and victimized. However, the existence of a whistleblower protection law per se is not sufficient – either to protect whistleblowers or to motivate them to report misconduct. When the appropriate legislation is adopted, it is therefore also crucial that it is actively implemented and enforced, and that potential whistleblowers are aware of this.[238]

The best way to protect the whistleblower is to keep her or his identity and the content of her/his report secret for as long as it is practicable. In those cases where confidentiality cannot be guaranteed or is not possible to maintain, however, the law also must provide for instant assessments of the gravity of the threats which the person in question is exposed to, and if necessary, relocation to a safe place and then concealment. Furthermore, whistleblower protection legislation also must provide sufficient deterrence by making it an offence for employers and others to punish or in other ways retaliate against whistleblowers for disclosing information which they are allowed to by the law. Also, in those cases where whistleblowers have been subject to intimidation or revenge as a result of their disclosures, the law should also provide for reinstatement in case of dismissal and/or other forms of compensation. Finally, the law should also make it possible for whistleblowers to report their suspicions or provide evidence to entities both within the organization where they work, and – if this is futile or involves the risk of retaliation – to entities outside the organization which are independent of the latter, such as the Auditor General, an ombudsman or an anti-corruption agency.[239]

At the same time, however, it is important to remember that whistleblowing can be a 'double-edged sword'. That is, whistleblowing can also be abused when someone provides false or malicious reports to hide her or his own misconduct, take revenge or for other reasons. Hence, whistleblower protection legislation must strike a balance between the need to protect genuine whistleblowers, and the need to protect innocent people against false, malicious and damaging allegations. In practice, this means that there also must be provisions in the legislation which both provide appropriate sanctions against people who make false and malicious allegations, as well as measures to restore a reputation which has been damaged by such allegations.[240]

Money-laundering measures:

Legislation addressing money-laundering are also important for the detection of fraud and corruption as they provide the basis for financial investigations and evidence-gathering. In

[237] Access to information legislation is accounted for in subchapter 3.2.4.
[238] UNODC, 2004, pp. 448-49.
[239] UNODC, 2004, pp. 449-50. For a further account of fraud and corruption 'hotlines', see subchapter 4.3.6.
[240] UNODC, 2004, pp. 449, 451.

UNCAC, measures to prevent money-laundering are dealt with in Article 14, which inter alia contains provisions on identification of beneficial owners, record-keeping, reporting of suspicious transactions and information exchange. By facilitating the detection of the money-laundering itself, such measures will also assist investigators in following the money back to their origin, i.e. the criminal act – including various forms of fraud and corruption – which generated the illicit proceeds in the first place.[241]

Administrative law:

Administrative law and complementing rules, regulations and procedures which inter alia provide citizens with the right to be heard, as well as notification requirements and the obligation to give the grounds for a decision by a public official, are also important measures for preventing and detecting fraud and corruption. This because these measures – especially when they are judicially supervised – provide civil society with effective mechanisms to protest against abuse of power and authority, and to question non-transparent decision- and policymaking.[242]

On this background, the following questions can be relevant to consider for auditors:

- **Has your country, as a minimum, adopted legislation which criminalizes various acts of fraud and corruption in accordance with the relevant provisions of UNCAC?**

- **Has your country adopted legislation which criminalizes acts of money-laundering, cf. Article 23 in UNCAC?**

- **Has your country adopted legislation which enable the appropriate authorities to freeze, seize and confiscate the proceeds from criminal activities such as fraud and corruption, and which provide for the recovery of assets, cf. Article 31 and Chapter V of UNCAC?**

- **Are amnesty, immunity or reduction of punishment often used without proper justification and/or in a non-transparent manner in cases of fraud and corruption?**

- **Has your country adopted legislation to protect 'whistleblowers', cf. Articles 32 and 33 of UNCAC?**

- **If so, is this protection effective?**

- **Has your country adopted legislation to prevent money-laundering, cf. Article 14 in UNCAC?**

- **Does your country have appropriate administrative legislation in place which, inter alia provide citizens with the right to be heard, as well as notification requirements and the obligation to give the grounds for a decision by a public official?**

[241] UNODC, 2004, p. 432.
[242] UNODC, 2004, p. 434.

Chapter 4:
Fraud and corruption risk factors at the sector/agency level

As mentioned in the previous chapter, the purpose of this chapter is to focus on the Executive branch of government, i.e. on the sector/agency level.[243] When addressing fraud and corruption risks at this level, auditors must inter alia focus on internal controls – or the lack thereof. In line with this, this chapter will first give a brief introduction to the 'internal control'-concept, and then present various fraud and corruption risk factors associated with weak internal controls. In this connection, various basic questions for auditors will also be suggested.

THE 'INTERNAL CONTROL'-CONCEPT:

As a point of departure for this chapter, this Guide will use part of the framework provided in INTOSAI GOV 9100. For the definition of "Internal Control" according to INTOSAI GOV 9100, see box 4.X.[244]

Box 4.X
Definition of "Internal Control" in INTOSAI GOV 9100:

"Internal control is an integral process that is effected by an entity's management and personnel and is designed to address risks and to provide reasonable assurance that in pursuit of the entity's mission, the following general objectives are being achieved:

- executing orderly, ethical, economical, efficient and effective operations;
- fulfilling accountability obligations;
- complying with applicable laws and regulations;
- safeguarding resources against loss, misuse and damage."

As shown in box 4.X, 'Internal Control' is a very comprehensive concept which in principle encompasses every aspect of how individual government entities organize and carry out their work to accomplish their goals. Hence, for the purpose of this Guide, the presentation below will only focus on those elements which are of direct relevance for fraud and corruption risks. In addition, the presentation will also draw on the operationalization of the Internal Control framework with regard to fraud and corruption risks which is provided by IIA/AICPA/ACFE.[245] The elements drawn from these two guidances will also to some extent be modified to suit the purpose of the Guide. In the following, we will therefore present the following internal control elements and associated fraud and corruption risks: 1. Ethics/Code of conduct; 2. 'Tone at the top'; 3. Human resource policies and practices; 4. More specific internal control measures; 5. Records management; 6. Fraud and corruption 'hotlines'; 7. Fraud and corruption risk assessment:

[243] It must be emphasized, however, that all elements presented in this subchapter also apply to SAIs, the Legislative and the Judiciary and the Prosecution services, as appropriate.
[244] INTOSAI GOV 9100, p. 6.
[245] Appendix I: COSO Internal Control Integrated Framework, p. 79, in: IIA, AICPA, ACFE: Managing the Business Risk of Fraud – A practical Guide.

4.1 ETHICS/CODE OF CONDUCT:

The preferences and value judgments of public sector employees – and thereby their standards of conduct – are determined by their ethical values and personal and professional integrity. Hence, since the 1990s, in addition to prevention and detection of fraud and corruption, more attention has also been drawn to the importance of ethical conduct in the public sector. Public ethics are a precondition for, and support the confidence of the people in the public sector and are at the core of good governance.[246]

Consequently, measures to fight fraud and corruption both can and should be underpinned by more universal standards of ethics and behavior to encourage high quality in public services, good relations between public sector employees and those they work for, i.e. the people, as well as efficiency, determination and spirit. Such principles can, at the same time, both encourage a culture of professionalism in the public sector, and also strengthen the expectation among the general public that the standards are high in this sector. The principles should therefore ideally be reflected in written documents such as a Code of Conduct (CoC) or a similar document, and this document should be made public.[247]

The basic purposes of a CoC are, among other things: (i) To make it clear what should be expected of individual employees or a group of employees, thereby contributing in promoting basic values which restrain fraud and corruption; (ii) To form the basis for training of employees, discussion of standards and, when required, adjustment of standards; (iii) To form the basis of disciplinary reactions, including discharge, in instances where employees contravene or fail to satisfy a standard as stipulated.[248]

As to the more general content, a CoC normally prescribes common standards of conduct in line with fundamental ethical principles such as independence, integrity, impartiality, transparency, accountability, justice, responsible use of public resources, diligence, loyalty towards the organization, and propriety of personal conduct. More or less, all these principles have their sources in legislation, delegated legislation or regulations, and contract law. Hence, a CoC will often draw most of its basic principles from existing legislation, and supplement it as appropriate. Where necessary, a CoC can be 'tailor-made', that is, include more specific standards which apply to specific groups of employees. At the same time, however, it is important to ensure that such specific standards are not in conflict with more general standards which already apply in legislation or elsewhere.[249]

Central elements in a CoC for public officials when it comes to fraud and corruption are, inter alia: 1. Standards concerning impartiality; 2. Standards concerning conflicts of interests; 3. Standards concerning administration of public resources; 4. Standards concerning confidentiality.

1. Impartiality:

Impartiality is crucial to the proper and uniform conduct of public tasks and to make sure that the public is confident in them. In general, the impartiality principle applies to any public employee who makes decisions. However, stricter or more specific requirements should

[246] INTOSAI GOV 9100, pp. 10, 17.
[247] UNODC, 2004, p. 136; INTOSAI GOV 9100, p. 18. For SAIs in particular, see ISSAI 30 Code of Ethics.
[248] UNODC, 2004, p. 133.
[249] UNODC, 2004, pp. 133-135. See also article 8 in UNCAC.

normally apply to more influential or powerful decisionmakers, such as public servants at senior level, judges and office holders in the legislative or executive branches of government. In essence, impartiality demands that decisions are made on the basis of facts only, i.e. without the possible influence of extraneous or immaterial considerations.[250]

2. Conflicts of interests:

Among other things, the extraneous and immaterial considerations just mentioned may arise when the private interest of a public official conflicts with her or his public duty. Hence, a central element of a CoC is to address such conflicts. One general requirement in this regard is for public officials to steer clear of undertakings which might result in conflicts of interests. For instance, officials responsible for decisions which affect financial markets should be extremely cautious with personal investments at the same time. Another requirement is that public employees avoid conflicts of interest by pleading partiality or prejudice in situations where they directly/indirectly can affect their own personal interests.[251]

A third requirement is that public officials should not accept gifts, favours or other benefits.[252] In more serious cases, where a direct link can be proved between a gift and a decision, bribery provisions in the penal code may apply. However, usually, the link is more subtle. Therefore, to prevent such situations from arising and make sure that there is no impression of partiality, the safest measure would probably be to have a general prohibition in the CoC on the acceptance of gifts, benefits, etc. with exceptions only, perhaps, for very small gifts, i.e. gifts of 'symbolic value'. In cases where government officials – in particular situations – nevertheless are permitted to accept gifts, the CoC can also stipulate that information regarding the type and value of the gift and the identity of the giver be disclosed, so that the question of whether the gift is inappropriate or not can be subject to an independent assessment.[253]

Finally, a fourth requirement is that officials disclose all their incomes, assets, business interests etc. which may raise conflicts. Often, this is reflected in provisions stipulating a general disclosure when officials are beginning in their new job and on a regular basis after that. As part of this, there are also frequently provisions which prescribe that potential conflicts of interests due to officials' financial positions should be disclosed as soon as they become apparent. Central questions in this regard are, inter alia: Who should receive the disclosures, and to what extent should these be made public? When it comes to non-political officials, i.e. civil servants – at what levels of seniority should these also be required to disclose this type of information?[254] On a general basis, however, it can be suggested that disclosure becomes more important, the higher the level of the official in question. The same argument goes for the degree of publicizing of officials' financial positions.

3. Administration of public resources:

Officials responsible for managing public funds or assets may represent a particularly high risk of fraud and corruption, as they normally are in a position to allocate financial or economic benefits and to manipulate systems which are established to prevent or detect

[250] UNODC, 2004, p. 136.
[251] UNODC, 2004, p. 137.
[252] See also section 2.1.4 for a brief account of this type of fraud and corruption.
[253] UNODC, 2004, p. 137
[254] UNODC, 2004, p. 137; Pope, 2000, pp. 187-88.

irregular practices in this area. Normally, these are officials who make decisions relating to expenditures, procurement of goods or services, management of public property or other assets – in addition to those responsible for the supervision and auditing of such officials. Hence, stricter rules may be required for officials in this category, although with many of the same characteristics as the more general rules pertaining to conflicts of interests. In addition to rules which prescribes avoidance or disclosure of real or possible conflicts of interests, standards concerning administration of public resources may therefore also focus specifically on maximizing the public benefits of any expenditures at the same time as costs, waste and inefficiency are minimized.[255]

4. Confidentiality:

Government officials and civil servants often have access to a broad spectrum of sensitive information – information which may be misused for fraudulent or corrupt purposes. Hence, a CoC should also contain rules relating to confidentiality. Such rules may include, inter alia, secrecy declarations which provide that sensitive information be kept secret unless otherwise required; classification systems to give guidance to officials on what should be kept secret or not, and how; prohibitions on the use or disclosure of confidential information to make profits or to gain other benefits; prohibition on the use or disclosure of sensitive information for a suitable period after the official in question has left the public service.[256]

Implementation of a Code of Conduct:

To be effective, a CoC must also be properly implemented in the organization in question. To achieve this, there are several prerequisites which ideally should be in place. First, to ensure that the CoC adequately addresses the possible situations and aspirations of employees at all levels in the organization, and that everybody has a feeling of ownership of the CoC, staff at all levels should ideally be involved in its preparation. Second, a CoC must be combined with an ethics programme which both include an effective implementation plan and a strong dedication to make sure that the plan is fulfilled. This should include a combination of both 'soft' and 'hard' measures.[257]

As to the 'soft' measures, these should include as many positive incentives as possible to ensure that every employee becomes aware of the CoC, and to encourage compliance. More specifically, this includes information and education schemes, and regular training on real life ethical dilemmas and on the steps every employee can take to make sure that their colleagues also comply with the CoC.[258]

The 'hard' measures, on the other hand, are aimed at effective enforcement and refer to clear procedures and sanctions to be applied in case of breaches of the CoC. To ensure effective implementation, integrity seminars should therefore also – in addition to the positive incentives – focus on the consequences if employees are found to violate provisions of the CoC. Moreover, to ensure that the disciplinary procedures are carried out in a fair and proper manner, there should be tribunals or similar bodies in place, to investigate complaints, adjudicate cases and decide on and enforce appropriate measures. Finally, disciplinary

[255] UNODC, 2004, p. 138.
[256] UNODC, 2004, pp. 138-139.
[257] Pope, 2000, p. 181; UNODC, 2004, p. 146; Dye, Kenneth M. (2007) Corruption and Fraud Detection by Supreme Audit Institutions, pp. 318-19, in: Shah (ed.), 2007.
[258] UNODC, 2004, pp. 146-147; Pope, 2000, p. 182.

procedures and their results should also be transparent to ensure that the employees involved are fairly treated and to assure other employees and the general public that the CoC is applied fairly and effectively.[259]

Third, to support implementation, the CoC should also be formulated with clarity and in a way which makes it easy to understand both for those who are supposed to comply with it, i.e. the 'insiders', and the citizens who they serve, i.e. the 'outsiders'. Fourth, to provide guidance to employees on how the CoC should be interpreted in particular instances – so that breaches and disciplinary actions can be avoided – consultancy mechanisms should be in place, through a dedicated individual or body. Finally, to improve effectiveness, the CoC should also be widely disseminated and promoted, both throughout the public entity or sector in question and among the general public, so that everybody is informed of its contents.[260]

Questions for auditors:

- **Does the government entity in question have a Code of Conduct (CoC) or similar document which provides guidance on proper ethical conduct by public servants and which, inter alia, is designed to prevent conflicts of interest?**

- **Have staff at all levels been involved in the development of the CoC to ensure ownership throughout the organization?**

- **Is there an implementation programme in place, including, inter alia, information and education schemes, and regular dilemma training?**

- **To ensure effective enforcement of the CoC in case of breaches, are there clear procedures and sanctions in place?**

- **Are there appropriate mechanisms in place to ensure that the disciplinary procedures are carried out in a fair and proper manner?**

- **Are disciplinary procedures and their results transparent?**

- **Is the CoC in question formulated with clarity and in a way which makes it easy to understand?**

- **Are there consultancy mechanisms in place to provide guidance to employees on how the CoC should be interpreted in particular instances?**

- **Is the CoC in question made public?**

[259] UNODC, 2004, pp. 146-48.
[260] UNODC, 2004, pp. 135, 146-47; Pope, 2000, p. 182.

4.2 'TONE AT THE TOP':

As an internal control element, 'Tone at the top' is closely related to the 'Ethics/Code of Conduct'-element described above, as senior management has a key role to play when it comes to the implementation of such standards in the government entity in question.

'Tone at the top' refers to the ethical culture which is created in the government agency or entity in question by the management through its philosophy and operating style. No matter what tone managers set, this will have a 'trickle-down' effect on the staff in the entire organization. If high level officials or senior management set a tone which promotes ethics and integrity, the staff will also be more predisposed towards supporting those same values. On the other hand, if top management seems to be indifferent to ethical issues and pays 'lip service' to internal controls, employees will also be more susceptible to carry out fraudulent and corrupt practices as they perceive that ethical conduct neither is prioritized nor a focus within the agency or entity in question. This even more so if top government officials more or less openly are involved in fraudulent and corrupt practices themselves. In the worst case this may create a corrupt culture which pervades the whole organization. Employees follow closely the conduct and performance of their managers, and they follow their example. In essence, employees will do what they see their managers do.[261]

Hence, to prevent fraud and corruption, and to create a good control environment in the entire organization – characterized inter alia by high ethical standards, loyalty to the entity and its goals, and an attitude towards internal controls which is approving and supportive – top management should do the following: 1. Tell the staff what is expected from them; 2. Be a role model; 3. Make it safe to report violations; 4. Reward ethical behavior.[262]

1. Tell the staff what is expected from them:

First, the values and ethics of the organization and the conduct expected of every employee should be communicated clearly and convincingly by top management. Consequently, as mentioned above, senior management has a key role to play when a code of conduct is prepared and implemented. Furthermore, to continually reinforce the ethics policy of the organization, the leadership should both communicate the values and ethics on a regular basis, and take action when necessary. This includes the rewarding/punishment of, respectively, ethical/unethical conduct.

2. Be a role model:

Second, top management must lead with integrity. The employees will look to those at the top of organization for direction. Hence, top government officials and senior management cannot simply talk about being ethical, they must also 'walk the talk' and show the staff how to act by setting a good example. In practice, this means that, rather than limiting themselves to what is acceptable and or expedient, their conduct should reflect what is considered proper behavior.

3. Make it safe to report violations:

[261] ACFE, 2006. Tone at the top. How management can prevent fraud in the workplace. [Online] Available at www.acfe.com/documents/tone-at-the-top-research.pdf [Accessed on 22 June 2011], p. 1; INTOSAI GOV 9100, pp. 18-19.
[262] ACFE, 2006, pp. 7, 11-12; INTOSAI GOV 9100, p. 19. The responsibility of management for the prevention and detection of fraud in particular also follows from paragraph 4 in ISSAI 1240/ISA 240, p. 239.

Third, top management must create an environment where employees feel it is safe to report wrongdoings. Those who have knowledge of, or have a suspicion of fraudulent and corrupt practices or other breaches of ethical rules, should have the opportunity to report such misconduct without fearing revenge from senior management or fellow staff members. The leadership must therefore give a strong message that the organization is very grateful for receiving reports on wrongdoings, and that those providing the reports will receive the highest degree of protection.[263]

4. Reward ethical behaviour:

Finally, integrity must be rewarded. Hence, management should not only reward employees for fulfilling the goals set by the organization – in addition they should reward them for ethical conduct when they see it. The staff, on their hand, should also be aware that meeting the set goals is not the sole criterion for success, i.e. that ethical conduct and integrity also will be rewarded by the organization. One way to encourage this, is to integrate ethical criteria into employee incentive programs.

Questions for auditors[264]:

- **Has the top management in the government agency in question explicitly set a tone which promotes ethics and integrity in the organization?**
- **Does the top management 'lead the way' by behaving in a proper manner?**
- **Has the top management been central in the preparation and implementation of a Code of Conduct in the organization?**
- **Does the top management communicate the values and ethics of the organization on a regular basis?**
- **Does the top management take action when necessary, i.e. rewarding ethical/punishing unethical conduct?**
- **Has the top management communicated clearly that reports on wrongdoings are welcomed, and that 'whistleblowers' will be protected?**
- **Has the top management implemented measures to reward ethical conduct and integrity by the employees?**

4.3 HUMAN RESOURCE POLICIES AND PRACTICES:

The staff itself is also crucial when it comes to internal control. For controls to be effective, it is imperative that employees are both competent and reliable. Hence, the methods for recruiting, hiring, training, remunerating, promoting, etc. public servants and other non-elected officials are a central part of the control environment. Consequently, these methods

[263] See also subchapter 4.6.
[264] The conduct of sensitive interviews will be accounted for in subchapter 6.6.

are also important for fraud and corruption prevention and detection.[265] This is accounted for in article 7.1 (a)-(c) of UNCAC. (See box 4.X).

To start with the *recruitment* process, it is important that decisions on hiring and staffing include assurance that applicants have the right education and experience and the integrity required to do their job properly. Screening of candidates should therefore be as exhaustive and careful as possible. Such screenings and background checks should include, inter alia, close scrutiny of the applicant's educational certificates, employment history, criminal record, and references. The background checks should be particularly thorough when it comes to managers and other positions which are considered to be especially vulnerable to fraud and corruption. The recruitment process should also be as transparent as possible, among other things, by publicizing vacant positions and recruitment criteria.[266]

When employed, *positive incentives* are called for to prevent fraud and corruption among the staff. Among other things, this includes adequate salaries, improvements in working conditions and job security, and enhancements of job or professional status. Furthermore, and at least as important, such incentives also involve compensation – such as bonuses, salary increases or promotion – which is closely connected with merit and performance.[267] When it comes to integrity and ethical conduct in particular, this can – as mentioned above – for instance be encouraged by integrating ethical criteria into employee incentive programs.

Box 4.X
Article 7.1 (a)-(c) in UNCAC relating to recruitment, hiring, retention, promotion and retirement of civil servants:

Each State Party shall, where appropriate and in accordance with the fundamental principles of its legal system, endeavour to adopt, maintain and strengthen systems for the recruitment, hiring, retention, promotion and retirement of civil servants and, where appropriate, other non-elected public officials:

(a) That are based on principles of efficiency, transparency and objective criteria such as merit, equity and aptitude;

(b) That include adequate procedures for the selection and training of individuals for public positions considered especially vulnerable to corruption and the rotation, where appropriate, of such individuals to other positions;

(c) That promote adequate remuneration and equitable pay scales, taking into account the level of economic development of the State Party;

As mentioned in subchapter 2.2.1, however, according to surveys in many countries, low salaries have been identified as an important factor explaining fraud and corruption among civil servants. Hence, in many instances, the question of adequate salaries also must be seen in connection with the issue of 'right-sizing'. That is, to achieve appropriate salary levels,

[265] INTOSAI GOV 9100, p. 20; UNODC, 2004, p. 277.
[266] INTOSAI GOV 9100, p. 20; ACFE, 2006, pp. 7-8; UNODC, 2004, p. 122.
[267] UNODC, 2004, pp. 245, 277.

public administration must first be made 'affordable', and this again often necessitate cut-backs, rationalization of management and other structural reforms.[268]

Closely related with the matter of positive incentives are the issues of organizational structure and *assignment of proper authority and responsibility*. That is, in addition to recruiting competent staff with high ethical standards, and providing them with positive incentives such as appropriate remuneration, organizations should also ensure that employees have well-defined job descriptions and performance goals at any time. This implies, inter alia, that performance goals are regularly reviewed to make sure that they are realistic, and that training is provided on a frequent basis to ensure that the staff maintains the skills they need to do their job efficiently and effectively.[269]

Finally, and as mentioned above, public servants and government officials often have access to a wide range of sensitive information which may be misused for fraudulent or corrupt purposes. Furthermore, depending on their influence on decision-making while in office, public servants and government officials may also receive secret job offers from companies which are more or less directly affected by these decisions. In addition, as a result of their previous position, former government officials may also have undue influence on colleagues who are still in office. Hence, depending on the circumstances, *post-employment constraints* such as temporary prohibitions on employment within particular sectors or companies may be called for. Moreover, and as mentioned, *rules prohibiting the use or disclosure of sensitive information* for a suitable period after the official in question has left the public service should also be considered. As a general rule, it can be suggested that such rules should be stricter, the higher the level of the official in question.[270]

Questions for auditors:

- **Does the government agency in question have a professional recruitment system in place to ensure that applicants have the proper education and experience and the integrity required to carry out their job?**

- **Is the recruitment process transparent? Among other things, are vacant positions and recruitment criteria publicized?**

- **Are employees offered adequate salaries, taking into account the level of economic development in the country in question?**

- **Are salary increases, promotion and other forms of compensation closely connected with merit and performance?**

- **Is there a clear assignment of authority and responsibility in the organization? Do all employees have well-defined job-descriptions and performance goals? Does the organization have an exhaustive list over all employees and what they do?**

[268] UNODC, 2004, pp.124, 127-28.
[269] ACFE, 2006, p. 8; INTOSAI GOV 9100, p. 19-20.
[270] UNODC, 2004, p. 141; Pope, 2000, pp. 201-202, 210-211.

- **Are there rules and procedures in place to address conflicts of interests and/or disclosures of sensitive information in connection with resignations, retirements, etc.?**

4.4 MORE SPECIFIC INTERNAL CONTROL MEASURES:

The more specific internal control measures comprise a wide range of arrangements and activities which are established to address risks – including fraud and corruption risks – and to achieve the objectives of the government agency in question. To give a full account of these measures would extend the scope of this Guide by far, so here we will only give a brief summary of those elements which are believed to be most important. One way to categorize these measures, is to divide them into structural/preventive measures, operative/detective measures, enforcement measures, and monitoring of the functioning of these measures:

Structural/preventive measures:

As mentioned above, the issues of organizational structure and assignment of proper authority and responsibility are important when it comes to the efficiency and effectiveness of employees in doing their job. However, the questions relating to how government agencies organize themselves, how they assign authority and responsibility, and how they run their daily business are also crucial when it comes to the conduct of more specific control activities.

Hence, as a more general point of departure, it can be suggested that very complex structures and procedures increase the opportunities for fraud and corruption, as they inter alia obstruct the functioning of internal structures relating to the use of discretion, the functioning of external structures relating to transparency, and the conduct of controls such as audits. Government administrations with too many layers, too complicated rules or ambiguous lines of reporting, authority and accountability create environments where the distinction between acceptable, and fraudulent and corrupt behavior may be blurred. Furthermore, they undermine the effectiveness of disciplinary and criminal justice measures by making it much more difficult to apportion individual responsibility. The way to address such problems – in addition to appropriate training – is inter alia by reducing complexity to levels which are compatible with the fundamental administrative functions involved. This again involves, as mentioned above, structural reforms such as de-layering and rationalization of management.[271]

As to the more specific preventive control activities, INTOSAI GOV 9100 suggests the following three[272]:

1. Authorization and approval procedures: Having such procedures implies that only individuals who act within the range of their authority can authorize and execute transactions and events, and the procedures should also tell them how and when to do it. Authorization is the primary method to ensure that only legitimate transactions and events are initiated;

2. Segregation of duties: Having such procedures implies that no single individual or group is/are allowed to control all central stages of a transaction or event by herself/themselves. This

[271] UNODC, 2004, p. 242.
[272] INTOSAI GOV 9100, pp. 29-30.

is crucial to reduce the risk of mistakes, misuse, or misconduct and the risk of not discovering such problems. Hence, to ensure that the proper checks and balances are in place, tasks and responsibilities should be systematically allocated to a sufficient number of employees. If there is a risk of collusion, however, for instance because the agency in question has too few employees to achieve sufficient checks and balances, rotation of personnel may be a way to address this problem;

3. Controls over access to resources and records: Having such controls implies that access to resources and records is given only to those individuals who are authorized and accountable for the use and/or custody of the resources/records. By restricting access to resources and records, the risk of unauthorized use or loss to the government is reduced.

Operative/detective measures:

As to the more specific detective control activities, INTOSAI GOV 9100 suggests the following three[273]:

4. Verifications: Having such controls implies that transactions and significant events are confirmed both before and after they are processed;

5. Reconciliations: Having such controls implies that records are harmonized at regular intervals with relevant documents, for instance that bank account records are harmonized with relevant bank statements;

6. Reviews of operating performance: Having such procedures implies that efficiency and effectiveness are assessed on a regular basis by reviewing operating performance against a set of standards.

Both structural/preventive and operative/detective measures:

In addition to the six control activities described above, INTOSAI GOV 9100 also suggests the following two control activities which are both preventive and detective[274]:

7. Reviews of operations, processes and activities: Having such controls implies that operations, processes and activities are evaluated on a regular basis to make sure that they comply with relevant regulations, policies, procedures, or other requirements;

8. Supervision: This refers to the role and responsibility of management for ensuring that internal control objectives are attained. Inter alia, supervisors should clearly communicate to each employee what tasks, responsibilities and accountabilities are assigned to him or her; systematically review, to the degree necessary, the performance of every staff member; approve work at crucial stages to make sure that it proceeds as planned.[275]

Furthermore, as mentioned in subchapter 4.1 in respect of conflicts of interests, another important measure to prevent fraud and corruption is that officials disclose all their incomes, assets, business interests etc. which may raise conflicts. It was also mentioned that disclosure

[273] INTOSAI GOV 9100, p. 30.
[274] INTOSAI GOV 9100, pp. 30-31.
[275] Regarding the roles and responsibilities of management and supervisors regarding internal controls, see also subchapter 4.2.

becomes more important, the higher the level of the official in question. Hence, in addition to the measures already mentioned, another important internal control activity – being both preventive and detective – is to monitor officials' financial positions on a regular basis.[276]

Enforcement:

As mentioned in subchapter 4.1, to ensure proper implementation of a Code of Conduct, effective enforcement with clear procedures and sanctions to be applied in case of breaches is called for. The control environment will only be effective if disciplinary measures are applied consistently in case of ethical violations. Consistency in enforcement requires that the sanctions for various violations are well-defined, and that these are strictly adhered to. If one staff member is punished for a particular infringement while another is not punished for the same infringement, the moral force of the ethics policy of the government agency in question will be reduced. Furthermore, to deter – and prevent – breaches, the levels of the various sanctions also must be sufficient. Finally, in addition to responding appropriately to detected violations, organizations must also take all necessary steps to prevent similar violations in the future.[277]

Monitoring:

Finally, to ensure that internal controls are operating as planned over time and that they are appropriately adjusted when conditions change, they should also be subject to monitoring on a regular basis, separate evaluations or a combination of both. Ideally, this monitoring should be conducted by an internal audit unit with sufficient independence, competence, resources and authority to gather information or evidence.[278]

Questions for auditors:

- **Does the government agency in question have proper authorization and approval procedures in place?**
- **Is there a sufficient segregation of duties in the organization? In case of limited resources, are there routines in place for rotation of personnel?**
- **Are there sufficient controls over access to resources and records in the organization?**
- **Are there proper verification and reconciliation procedures in place?**
- **Is the performance of the organization – both in respect of efficiency and effectiveness, and compliance with relevant regulations, procedures, etc. – reviewed on a regular basis?**
- **Is there a system in place to monitor officials' financial positions – especially the financial positions of government officials at the highest levels – on a regular basis?**

[276] UNODC, 2004, p. 249.
[277] ACFE, 2006, pp. 8-9.
[278] INTOSAI GOV 9100, pp. 40-41; UNODC, 2004, p. 247.

- **Is there sufficient supervision of the internal controls in the organization?**

- **Are the Code of Conduct and other relevant rules and procedures enforced effectively and consistently?**

- **Is the functioning of the internal controls subject to independent monitoring on a regular basis?**

- **Does the organization have an internal audit unit?**

4.5 RECORDS MANAGEMENT:

A fundamental objective of internal controls in the public sector is the fulfilment of public accountability obligations. As mentioned in subchapter 3.2.4, ensuring that any public employee can be held accountable for her/his actions is a central part of this. Without a paper trail, however, the chances of identifying and sanctioning public servants guilty of misconduct are small. Hence, to be accountable, government entities must have record-keeping systems in place which ensure that appropriate records are stored, protected from alterations and made accessible for audits or similar evaluations – and, ultimately, for the public at large.[279]

Furthermore, as legal – and enforceable – rights of access to information are worthless if public records are in a state of chaos, the records also must be classified and organized in a way which makes information easy to find. If information cannot be found, nor can it be made available for citizens, the media or for auditors – irrespective of the rights of access they may have according to law. In addition to the negative impact this will have on the accountability and credibility of government towards the citizens, it will also have serious negative effects for the capacity and ability for government to carry out its tasks efficiently and effectively, including its internal control obligations. Finally, whether information is operational, financial/non-financial or compliance-related, it also must have sufficient quality. Box 4.X summarizes the most important quality criteria for public reports and records according to INTOSAI GOV 9100 and 9200.[280]

Box 4.X
Quality criteria for public reports and records according to INTOSAI GOV 9100 and 9200:

Accessible:	Can the information be obtained easily by the relevant parties?
Accurate:	Is the information correct?
Appropriate:	Is the information relevant – does it meet the needs of the users?
Comparable:	Does the information have a format which enables the users to identify similarities and differences – either between two or more government entities at the same time, or within the same entity over time?
Complete:	Is the information sufficient to cover all relevant aspect of the subject matter?
Consistent:	Is the information presented on the same accounting basis?
Current:	Is the information the latest available?

[279] INTOSAI GOV 9100, p. 37; UNODC, 2004, p. 246; Pope, 2000, pp. 245.
[280] Pope, 2000, p. 245; INTOSAI GOV 9100, p. 37.

Material:	Can the information – with reasonable limits – be expected to influence the activities of the users?
Timely:	Is the information available when it is required?
Understand-able:	Is the information presented in a precise, clear and simple way?

Sources:
INTOSAI GOV 9100, pp. 37-38; INTOSAI GOV 9200. Accounting Standards Framework. [Online] Available at www.issai.org/media(1065,1033)/INTOSAI_GOV_9200_E_(scanned_version).pdf [Accessed on 24 June 2011], pp. 18-19.

Questions for auditors:

- **Does the government agency in question have an appropriate record-keeping and record-management system in place?**
- **Is the information in the records easy accessible for all relevant parties?**
- **Does the information in the records meet the criteria as provided for in INTOSAI GOV 9100 and 9200?**

4.6 FRAUD AND CORRUPTION 'HOTLINES'[281]:

The establishment of a confidential 'hotline' where both employees and people outside the government agency in question can provide tips on fraud, corruption and other kinds of misconduct can be a very effective reporting mechanism.[282] In other words, it can be a very effective tool to *detect* fraud and corruption. In addition, however, it can also be a very effective *prevention* mechanism as the mere existence of and reference to such a hotline can give employees a strong perception of being detected, thereby being a strong deterrent. Moreover, by establishing and promoting a fraud and corruption 'hotline', i.e. by allowing employees and others to report misconduct without fear of retaliation, the organization will also send the message that it is sincere in its efforts to create an environment of ethics and integrity.[283]

Confidentiality is – as already indicated – a fundamental prerequisite in this regard. That is, the reporting mechanism must be constructed in such a way that employees and others are allowed to report or seek advice anonymously or confidentially regarding actual or potential misconduct by others within the government agency or entity in question. Furthermore, the anonymity and confidentiality provided by the hotline should also be clearly emphasized in all communications regarding this mechanism, so that 'whistleblowers' can be assured that their reports and their identity will be kept confidential. Also, in addition to the technical arrangements, the organization also must have a 'whistleblower' policy in place which makes

[281] The various elements of a fraud and corruption hotline will be further accounted for in subchapter 5.1.
[282] According to the 2010 Global Fraud Study, carried out by ACFE, tips were by far the most effective detection method in the period of study (2008-2009), as they resulted in the detection of almost three times as many fraud cases as any other method. This is also consistent with the findings in ACFE's previous studies. Moreover, the 2010 study also showed that there was a correlation between the presence of fraud hotlines and an increase in the number of cases detected by a tip. Source: ACFE, 2010. Report to the Nations on Occupational Fraud and Abuse. 2010 Global Fraud Study. [Online] Available at www.acfe.com/rttn/rttn-2010.pdf [Accessed on 30 March 2011], pp. 16-17.
[283] ACFE, 2006, pp. 8-9; Dye, 2007, pp. 318-319.

it clear that employees and others reporting misconduct do not have to fear retaliation under any circumstance as they will receive the necessary protection. Just as critical as confidentiality, however, is to ensure that hotlines are not abused, that is, to protect the rights and reputations of individuals against false allegations. Both prerequisites – i.e. confidentiality and protection against abuse – necessitate inter alia proper procedures for dealing with tips and competent and experienced interviewers.[284]

Questions for auditors:

- **Has the government agency in question established a 'hotline' where employees and people on the outside anonymously or confidentially can report on actual or potential misconduct?**

- **Has the government agency also established a supporting 'whistleblower' policy which ensures that those reporting misconduct do not have to fear retaliation?**

- **Are there also mechanisms in place to protect innocent employees from false allegations?**

- **Does the agency have sufficient competent staff and the appropriate procedures for managing a 'hotline'?**

4.7 FRAUD AND CORRUPTION RISK ASSESSMENTS:

As accounted for in INTOSAI GOV 9100, general risk assessment is a fundamental element in the internal controls of an organization, and fraud and corruption risks in particular should also be a natural part of such assessments.[285] The more specific content of fraud and corruption risk assessment will be dealt with separately in chapter 5, however.

Question for auditors:

- **Has the government agency in question established procedures to identify and assess possible fraud and corruption risks, and to respond to these risks in an appropriate manner?**

Box 4.X
Case: The U.S. Minerals Management Service

On 20 April 2010, there was an explosion and fire on the Deepwater Horizon oil drilling rig in the Gulf of Mexico, killing 11 of the crew and resulting in the largest oil spill ever in U.S. Waters. In the aftermath of the explosion, large amounts of crude oil washed into river mouths and onto beaches in Louisiana, Mississippi, and Alabama. In addition to the short- and long-term effects on the ecology and wildlife of the coastal wetlands in the Gulf, the oil spill also had major negative impacts on the tourist industry and commercial and recreational fisheries in the region.

[284] ACFE, 2006, p. 9; Dye, 2007, p. 319. See also subchapters 3.2.6 and 4.2, and article 8.4 in UNCAC.
[285] INTOSAI GOV 9100, pp. 22-27.

This accident drew further attention to management challenges already identified at the Minerals Management Service (MMS) in the U.S. Department of the Interior (DOI), and also brought new dynamics into reform efforts already in process in this organization. Inter alia, MMS was responsible for inspecting oil and gas platforms for safety and compliance with relevant laws and regulations, and, if required, for enforcing these laws and regulations in cases of non-compliance. At the same time, it was also responsible for issuing 'safe awards' to those oil and gas and production companies which had the best record in respect of compliance. These awards were very valuable for the companies, as they were used in the promotion and marketing of their businesses.

Prior to the Deepwater Horizon accident, investigators in the DOI and in the U.S. Congress had identified a number of management flaws, ethical failures among the employees, and conflicts of interest at the MMS. As to the Gulf of Mexico region in particular, these challenges were illustrated in two reports which were released from the Office of Inspector General (OIG) of the DOI in May 2010. The reports concerned misconduct revealed at the Lake Charles and New Orleans district offices of MMS prior to 2007.

The OIG investigation of the Lake Charles office was initiated as a result of an anonymous tips to the U.S. Attorney's office in New Orleans, claiming that several employees in MMS had accepted gifts from representatives of oil and gas production companies. To a large extent, the investigation also confirmed the claims, as it revealed that a number of employees at the Lake Charles office had attended sporting events sponsored by oil and gas companies, as well as received lunches and gifts from the same companies. It also revealed that one inspector at this office had carried out four inspections of the platforms of one particular company at the same time as he was in the process of negotiating employment with this company – a post which he later accepted. No incidents of non-compliance were reported at these inspections.

At the same time, the OIG investigation showed that the Gulf of Mexico offices of MMS had – at least formally – established the practice of reporting the reception of gifts and other benefits through confidential financial disclosure reports, and it also confirmed that all MMS employees in this region received ethics training on an annual basis. In addition, the provisions in both federal regulations and agency ethics rules regarding the solicitation or acceptance of gifts from so-called 'prohibited sources', and/or in association with the official position of the federal employee in question, were very strict.

Apparently, however, this was not sufficient to prevent misconduct from taking place at the Lake Charles office and in the Gulf region more generally. The OIG investigation discovered that, in the period from 2005 through 2009, only one individual among all the Gulf of Mexico employees of MMS had reported receiving gifts and travel refunds in confidential financial disclosure reports. Moreover, the investigation gave the impression that – prior to January 2007 – a culture of accepting gifts from oil and gas companies such as fishing and hunting trips, admission to sporting events, meals, etc. was prevalent among MMS supervisors and inspectors in the Gulf region.

The 'catalyst' that radically changed this situation seems to be the investigation and later termination of the supervisor of the New Orleans office of MMS for accepting gifts. The supervisor in question had accepted gifts amounting to several thousand USD from one particular oil company which was affected by MMS regulations and decisions. After receiving

these gifts, and apparently at the request of the oil company, the supervisor had improperly issued a letter regarding the salvage of a sunken offshore drilling rig operated by the company. Seemingly, at the time, the letter was essential to the efforts of the oil company to collect 90 million USD in insurance proceeds. As a result of this, the supervisor in question was terminated in January 2007. He was later also sentenced to one year of probation, 100 hours of community service and a fine of 3000 USD. After this, the practice in MMS of accepting gifts from the oil companies seemed to decline drastically.

The misconduct disclosed in the two OIG reports was also a symptom of the more fundamental and structural challenges faced by MMS and other government agencies in the same situation, that is, the potential conflicts of a regulatory body which is intrinsically linked to the industry which it regulates. In some instances – according to the concerns raised in reports and testimonies of the OIG and in oversight hearings in the U.S. Congress – portions of MMS were even perceived to be captured by the industry it regulated. In a remark on the oil spill after the Deepwater Horizon accident, the U.S. President described this as the "cozy relationship between the oil companies and the federal agency that permits them to drill."

Another aspect of this relationship is the environment in which the MMS inspectors operated. More specifically, the OIG investigation also discovered that many of the individuals – both in government and in the industry – who were involved in fraternizing and exchanges of gifts, had often known each other since childhood. Hence, their relationships were established long before they joined government or industry. Also, and which raised particular concern in the OIG, the individuals in question seemed to move quite easily between industry and government.

Later, OIG also received anecdotal evidence that MMS inspectors, in particular in the Gulf of Mexico region, operated quite independently, with little guidance regarding what to inspect, or how. In other words, according to this information, the inspectors were left with much discretion when conducting inspections on the platforms. Finally, the OIG has also discovered that MMS had difficulties recruiting qualified inspectors as the oil and gas industry generally could offer considerably higher salaries and bonuses.

The responses of the DOI to these challenges, which were announced both before and after the Deepwater Horizon accident, were both specific and targeted, and also of a more fundamental and structural character. As to the more specific measures, these included, inter alia: More ethics training for MMS inspectors to deal with the particular challenges associated with the 'greyzones' between government and industry; assignment of a full- time ethics lawyer to provide advice and guidance to MMS employees; and control measures, such as temporary prohibitions on employment within particular sectors or companies, to reduce the possibilities for conflicts of interests.

On the more fundamental level, a reorganization process was initiated in May 2010 with the aim of dividing MMS into three new offices: 1. The Office of Natural Resources Revenue; 2. The Bureau of Ocean Energy Management; 3. The Bureau of Safety and Environmental Enforcement. Behind this process was the acknowledgement that the three distinct functions which all had been vested in MMS until then – (i) collection of revenues, (ii) energy development, and (iii) enforcement of safety and environmental regulations – in fact were conflicting, and hence that they had to be divided. On 18 June 2010 the name of the MMS was changed to Bureau of Ocean Management, Regulation, and Enforcement (BOEMRE).

Sources:

Hogue, Henry B., 2010. Reorganization of the Minerals Management Service in the Aftermath of the Deepwater Horizon Oil Spill. CRS Report for Congress. 10 November 2010. [Online] Available at www.fas.org/sgp/crs/misc/R41485.pdf [Accessed on 5 July 2011]; Hagerty, Curry L. and Ramseur, Jonathan L., 2010. Deepwater Horizon Oil Spill: Selected Issues for Congress. CRS Report for Congress. 30 July 2010. [Online] Available at www.fas.org/sgp/crs/misc/R41262.pdf [Accessed on 5 July 2011]; Office of Inspector General, United States Department of the Interior: Investigative Report - Island Operating Company, et. al. 31 March 2010. [Online] Available at www.doioig.gov/images/stories/reports/pdf//IslandOperatingCo.pdf [Accessed on 5 July 2011]; Testimony of Mary L. Kendall, Acting Inspector General for the Department of the Interior, before the House Committee on Natural Resources Subcommittee on Energy and Mineral Resources, 17 June 2010. [Online] Available at www.doioig.gov/images/stories/KendallTestimony17June2010.pdf [Accessed on 8 July 2011]; Testimony of Mary L. Kendall, Acting Inspector General for the Department of the Interior, before the Committee on Oversight and Government Reform United States House of Representatives, 22 July 2010. [Online] Available at http://democrats.oversight.house.gov/images/stories/Hearings/Committee_on_Oversight/2010/072210_MMS_Reorganization/TESTIMONY-Kendall.pdf [Accessed on 8 July 2011]; Letter from Mary L. Kendall, Acting Inspector General for the Department of the Interior to Secretary Salazar of 24 May 2010. [Online] Available at www.doioig.gov/images/stories/reports/pdf//IslandOperatingCo.pdf [Accessed on 5 July 2011].

Chapter 5:
Fraud and corruption risk assessment through the value chain

The purpose of this chapter is to give an introduction to fraud and corruption risk assessment through the value chain in the environmental and natural resource sectors. The first part of this chapter (5.1) will provide a condensed presentation of some of the basic theory and tools on fraud and corruption risk assessment, including an Excel scheme to assist the auditor in this process. The scheme is enclosed in Appendix A. The second part (5.2) will then seek to provide a brief description of a generic and 'typical' value chain within the environmental and natural resource sectors, and some of the associated fraud and corruption risks. Finally, the third part (5.3) aims to elaborate a bit further some of the most important links or stages in such a value chain, and then – through the use of various examples/cases – suggest possible fraud and corruption risks, associated red flags and possible audit procedures. The scheme enclosed in Appendix A will be a central tool in this regard.

5.1 INTRODUCTION TO FRAUD AND CORRUPTION RISK ASSESSMENT

5.2 FRAUD AND CORRUPTION RISKS IN THE ENVIRONMENTAL AND NATURAL RESOURCE VALUE CHAIN

5.3 RISK FACTORS/'RED FLAGS' AT VARIOUS STAGES IN THE VALUE CHAIN AND POSSIBLE AUDIT PROCEDURES

5.3.1 Legislation

5.3.2 Research

5.3.3 Adoption of regulations

5.3.4 Determination of concession/licence/grant terms

5.3.5 Applications/tenders

5.3.6 Negotiation/licencing/certification

5.3.7 Allocation of funding

5.3.8 Monitoring and inspection of industrial activities/exploration of natural resources

5.3.9 Royalty/revenue collection

5.3.10 Verification of projects/reporting

Chapter 6:
Audit procedures to confirm or invalidate suspicion of fraud and corruption in the environmental and natural resource sectors

The purpose of this chapter is to present some of the most important detection methods and audit procedures to confirm or invalidate suspicion of fraud and corruption. As with the previous chapters, the aim is also here to find relevant cases and examples from the environmental and natural resource sectors around the world to illustrate the various audit methods and procedures.

6.1 PROCEDURES FOR HANDLING CONFIDENTIAL INFORMATION

6.2 FRAUD AND CORRUPTION-RELATED RESEARCH

6.3 ASSOCIATION ANALYSIS

6.4 TRANSACTION ANALYSIS

6.5 WAYS TO ADDRESS MONEY LAUNDERING

6.6 SENSITIVE INTERVIEWS

6.7 CO-OPERATION WITH OTHER AUTHORITIES

6.8 DOCUMENTATION/REPORTING

Appendix A:
Fraud and corruption risk assessment scheme

FRAUD AND CORRUPTION RISK ASSESSMENT — MAIN SCHEME

Fraud and corruption risk in the various stages of the value chain - WHERE (Chapter 5.3)	Type of fraud and corruption risk - WHAT	Fraud and corruption method - WHO/HOW	Red flags	Checks and balances' at the governance level and/or internal controls implemented by management to address the risks of fraud and corruption (Chapters 3 and 4)	Prioritization	Probability	Possible consequences	Audit procedures (Chapter 6)
This column is for a brief description of the stage in the value chain which is being assessed for fraud and corruption risks	This column is for a brief description of the fraud and corruption risk. One should try to give an adequate description of an act which involves the abuse of public office and/or funds to obtain an unjust or illegal advantage for the actor himself, his family, his business partners or others. Every stage in the value chain may be associated with a number of different fraud and corruption risks.	This column is for a more thorough description of the actmethod. The auditor should give an accurate description of **who** is/are involved, and **how** the act is carried out.	This column is for a description of the **features**, or 'symptoms' that characterize the fraudulent and corrupt acts in question, and **how** and **where** these can be detected.	If the appropriate 'checks and balances' are in place at the governance level, and/or controls have been implemented by the governament entity in question to address the risks of fraud and corruption, these controls should be described here. (NB The accounts of control measures in chapters 3 and 4 should not be considered as exhaustive)	The prioritization between 'high' and 'low' is done in this column on the basis of the evaluation and ranking done in the subscheme.	This part is based on the calculation of probability done in the subscheme - consisting of an evaluation of opportunity and frequency. An explanation of **why** the probability is believed to be 'high' or 'low' should be given.	This part is based on the evaluation of consequences done in the subscheme, where the impact on: 1. The environment and/or natural resources and, possibly, livelihood and or human health; 2. The economy of the state; 3. The reputation of the Government in general and of the state agency in particular - is assessed. Consequences considered **most important** are commented on here.	This column is for brief descriptions of possible audit procedures to follow up the risks identified.

FRAUD AND CORRUPTION RISK ASSESSMENT SUBSCHEME

Sum after weighing and calculation	Fraud and corruption method	Probability	Possible consequences		
		Opportunity, frequency and time perspective	Impact on environment/ natural resources, livelihood and/or human health	Economy	Reputation
Ex: 65 = 5 * (5 + 3 + 5)		HIGH	HIGH	MODERATE	HIGH
Ex: 27 = 3 * (3 + 5 + 1)		MODERATE	MODERATE	HIGH	LOW
Ex: 5 = 1 * (1 + 3 + 1)		LOW	LOW	MODERATE	LOW

FURTHER SPESIFICATION OF COLUMNS

Probability

Here, the auditor assesses the probability that a person or persons (internal or external) could carry out a particular act of fraud and corruption leading to the realization of the associated risk factor. As mentioned in subchapter 2.2, the probability that each of the various fraud and corruption methods in fact will be applied is considered a function of the following three factors: 1. Incentive/pressure; 2. Opportunity; 3. Rationalization or attitude.

The probability that the risk factor will occur within the relevant accounting period also is taken into consideration.
The greater the probability that the risk factor may occur within the relevant accounting period, the greater the risk.

Possible consequences

Environment/natural resources, livelihood and/or human health

Here, the auditor assesses possible environmental consequences and/or impact on natural resources, and possibly, livelihood and/or human health if the relevant act of fraud and corruption is carried out. Will the act of fraud and corruption result in depletion of resources? Will it result in loss of biodiversity? Will it result in pollution of land, water and/or air, land degradadition, or obstruct the remediation of such damages? Will it have a negative impact on climate change mitigation/ adaptation in particular? Will it deprive people of their livelihood? Will it have harmful effects on human health?

Economy

Here, possible financial consequences for the State if the relevant act of fraud and corruption is carried out, are assessed. Will the act of fraud and corruption result in a loss of Government revenues? Will it lead to an (unmerited) increase in Government expenses? Will it decrease efficiency in the state agency in question?

Reputation

Here, consequences for the Government in general, and the relevant state agency in particular, if the fraudulent and corrupt act is made public, are assessed. Will the fraudulent and corrupt act weaken people's confidence in the public sector/state agency?

FRAUD AND CORRUPTION RISK ASSESSMENT SUBSCHEME

WEIGHING

Probability

HIGH	There is high probability that the act of fraud and corruption will be carried out.
MODERATE	There is moderate probability that the act of fraud and corruption will be carried out.
LOW	There is low probability that the act of fraud and corruption will be carried out.

Consequences

HIGH	The act of fraud and corruption will have a major negative impact on the environment/natural resources, livelihood, human health, economy, and/or public trust in Government. The materiality of the potential damages is considered to be high.
MODERATE	The act of fraud and corruption will have a negative impact on the environment/natural resources, livelihood, human health, economy, and/or public trust in Government. The materiality of the potential damages is considered to be significant.
LOW	The act of fraud and corruption will have few or no negative impact s on the environment/natural resources, livelihood, human health, economy, and/or public trust in Government. The materiality of the potential damages is considered to be insignificant.

FRAUD AND CORRUPTION RISK ASSESSMENT SUBSCHEME

RANKING AND PRIORITIZATION

HIGH	5
MODERATE	3
LOW	1

The ranking of the fraudulent and corrupt acts (methods) is done by adding the weightings from the assessment of consequences, and multiplying the sum with the weighting for probability.

Total ranking (prioritization) = S * (C1 + C2 + C3)

TRANSFER TO MAIN SCHEME

When prioritizing the various fraudulent and corrupt acts (methods) in the main scheme, these are only categorized as "high priority" or "low priority".
The categorization is done on the basis of the ranking in the subscheme, and for every single risk factor the sum (from the column in the subscheme called "Sum after weighing and calculation") must be assessed with the aim of dividing it into either high or low priority. For instance, one could decide that all acts of fraud and corruption with a total sum larger than 40 should be given a high priority in the main scheme.

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