INSTITUTIONAL RISK ASSESSMENT
BEST PRACTICES COMPENDIUM
(ANTI-CORRUPTION – INTEGRITY AUDITING)

An Applied Methodology to
• identify corrupt practices,
• conduct audits,
• report findings and
• recommend solutions
in the public sector by executive
and/or legislature entities

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(A Private Publication) November 2009
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PART 1 - INTRODUCTION

Executive Summary

In this compendium, we refer to ‘anti-corruption audit’ and ‘institutional risk assessment review’ interchangeably. A ministry or a government that conducts such process mostly identifies it as an ‘institutional risk assessment review’ (hot spot detection) whereas National Supreme Audit Institutions (SAI) conducting the exercise refer to it as an ‘anti-corruption audit’ (including hot spot detection)\(^1\).

The authors of this compendium draw from their multi-country and multi-donor experiences with national executive, legislature and supreme audit institution entities that are mostly involved in financial oversight. They document applied and tested approaches, procedures and capacity development methods that support national anti-corruption endeavours.

This publication targets entities that are part of national integrity systems (as defined by Transparency International) and which are key players in the effective and sustainable enhancement of national accountability and transparency. This approach or methodology deals with government areas and entities that are particularly prone to corrupt practices as identified by governments, supreme audit institutions, inspectorates general, the international donor community, non-governmental organizations (NGOs), civil society organizations (CSOs) as well as the authors.

Additionally, this publication sets out recurrent types of findings as well as strategies to address these findings. As the health of a national economy depends to a great part on using resources effectively and efficiently, the importance of financial oversight bodies and their respective roles in safeguarding public monies from misuse and waste are crucial.

Institutional systems based on good governance, transparency, accountability, integrity and impartiality are pivotal in preparing an Institutional Risk Assessment/Anti-Corruption Manual to assess the impact of corrupt, ineffective and inefficient practices, report findings and recommend solutions to national authorities.

\(^1\) Accordingly, we use the terms ‘review’ and ‘audit’ as well as ‘reviewer’ and ‘auditor’ interchangeably.
INSTITUTIONAL RISK ASSESSMENT BEST PRACTICES COMPENDIUM

The compendium focuses on corruption and malfeasance of administrative, technical and financial nature within all government administrative units and institutions thus seeking to counteract by revealing cases of corruption, fraud, inefficiencies and wastage. It also aims at enhancing the protection of public resources from wastage and misuse, upgrading the effectiveness and efficiency of operations as well as enhancing employee commitment to laws, regulations, instructions and government policies.

The compendium is therefore meant to offer a summary view of the theoretical foundations used to develop and apply a methodology and the ensuing documentation to different national contexts and donor requirements. Working papers such as comprehensive checklists developed and used are not included but are available. Institutional risk assessment reviews, anti-corruption audit findings, recommendations and dispositions are also not integrated into the compendium but are also available.

For the purposes of the present document, the definition of “integrity” includes honesty, commitment to the organization’s aims and values, principles of loyalty, legality, reliability, objectivity, political neutrality, responsibility and accountability.

Acknowledgments

This document results from and is largely based on the authors’ extensive international experience in accountability and transparency issues including the pilot audits that they have conducted since 2006 in line-ministries and public entities in Sierra Leone, Bulgaria and Iraq.

The basic concept of this work originates from a methodology to conduct integrity self-investigations as developed by the Netherlands’ Ministry of the Interior and the Bureau of Integrity of the City of Amsterdam. It was assessed that the original concept would not entirely apply to developing countries’ settings and issues, and was initially refined and streamlined for a 2006 Sierra Leone mission funded by the UK Department for International Development (DFID) and subsequently for a Bulgaria anti-corruption assignment funded by the European Union (EU). The mandates were tailored to the specific needs of two Bulgarian ministries – Health and Education – where pilot audits were conducted after developing procedures, programmes and manuals, and training internal ministerial country teams mostly composed of experts within internal inspectorates general. Subsequently, it was further refined and integrated into the
Iraq Supreme Audit Institution – the Board of Supreme Audit (BSA) – through a 30 month (2006-09) project carried out by the United Nations Development Program (UNDP) Iraq country office and funded by the Canadian International Development Agency (CIDA).

The authors wish to acknowledge the commitment of the staff of the Corruption Prevention Department of the Anti-Corruption Commission of Sierra Leone, the management and staff of the Ministries of Education and Health of Bulgaria and the President and staff of the Board of Supreme Audit (BSA) of Iraq. The financial support of the international funding community which contracted the authors for several bilateral and multilateral assignments allowed them to document their experience in this compendium. Additionally, their numerous years of thematically related work within the United Nations Organization development units and programmes allowed them to become familiar and develop initial assessment tools which were refined and adapted to institutional risk assessments (hot spots detection) mandates and later integrated into national anti-corruption strategies.

The authors are part of the Anti-Corruption Network (ACN), a group of highly experienced international experts who have applied and adapted this methodology to national anti-corruption settings with national institutions that are front line players in the national integrity system. The ACN works frequently through IMAGOS UG, an independent consulting firm based in München (Germany) specialized in helping governments, NGO’s and private corporations find specific methodologies and tools to effectively address corruption and mismanagement.

**General Objectives**

This compendium documents administrative and financial corruption corrective endeavours that national governments undertake either internally through their executive or as part of their legislature oversight mission i.e. national Supreme Audit Institution (SAI). For example, as its primary mission statement, an SAI seeks to promote good governance, transparency, accountability, integrity and impartiality by carrying out the following:

- financial/performance audits of public accounts, entities and projects while complying with a high level of quality;
- report on audit findings to relevant authorities on a timely basis and disseminate them to the public at large;
• ensure that all stakeholders at national and local levels acknowledge the independence, integrity and impartiality of the oversight entity;

• apply most up-to-date auditing practices with the highest effectiveness at the lowest cost;

• develop professional relationships with clients and auditees, and issue reports that facilitate the procedures and work of the audited entity;

• ensure best value for money from resources provided by public monies;

• establish cooperative relationships with governmental partners, audit sections in ministries as well as anti-corruption authorities and

• support the oversight entity in holding the government accountable in its use of public resources.

Specific Objectives
This publication describes the phases to acquire and develop the skills for the anti-corruption role of governmental internal or external oversight entities:

• develop a country specific anti-corruption methodology;

• develop institutional anti-corruption manuals;

• develop auditee-specific programmes;

• set up and train national expertise teams;

• conduct pilot anti-corruption reviews and audits;

• formulate the anti-corruption report;

• follow up on findings and recommendations;

• integrate the methodology and procedures in the executive units and/or the external oversight entity and

• formulate a follow up/benchmarking mechanism.

Intended Users
This compendium is meant to be used by integrity and transparency partners and stakeholders of the public sector who focus on anti-
corruption, fraud, embezzlement and wastage. It may be used at the national and local levels by practitioners in the,

- public sector oversight body such as the national *Supreme Audit Institution*;
- inspectorate general;
- ministerial internal audit department;
- ministerial internal control department;
- anti-corruption agencies;
- training institutions and
- international donor organizations at bilateral and multilateral levels.
PART 2 - METHODOLOGY

Assumptions

The methodology is a step-by-step guide to assess and identify potentially vulnerable spots (hot spots) within an executive entity and is based on three assumptions:

• **Preventive investigation**: The process does not aim at detecting corruptible persons or at testing employees’ personal integrity. It focuses instead on identifying potentially vulnerable areas or procedures within the organisation, with ensuing development of measures, to reduce their negative impact and on optimising the organization’s defences against violations, fraud or corrupt actions.

• **Self-examination**: It is often the organisation’s own decision and responsibility to carry out the project. The organisation’s management should initiate the process and commit itself to implementing it through its employees. The organisation should also determine the standards for the required level of anti-corruption measures and degree. Experience has shown that the greater the involvement of an organisation in implementing the methodology:
  o the more the management feels responsible for it;
  o the greater the chance that integrity awareness will be embedded within the organisation;
  o there will be broader-based support and acceptance for the conclusions and recommendations and
  o this will lead to a greater possibility that the recommendations will be implemented.

• **Focus on improving the organisational structure.**

This approach targets the rules, procedures, processes and systems. It also takes into account a number of other integrity-related instruments such as codes of conduct, dilemma training and official function/organization oaths.

Objectives and Principles

The strategy’s objective is to reduce administrative corruption and high-level corruption. This ultimately leads to a substantially improved
level of confidence in the institutions, of trust in the rule of law and of equality before it. Corruption should not hinder free economic initiatives, normal functioning of the market economy and effective/efficient governance of the country. More specifically the strategy has the following goals:

- raise public confidence in the institutions and strengthen the civil control;
- increase the effectiveness of measures to prevent corruption practices and limit associated risks;
- create guarantees for transparency and accountability in a government’s activities and decision-making by politicians and public administrators;
- regulate clear and effective rules for relations and interactions between citizens and administration officials and
- establish values of honesty, integrity and ethics for government officials and staff.

The strategy’s implementation is based on the following principles:

- rule of law to guarantee the effective protection of human rights, separation of powers and equality of the citizens before the law;
- good governance and government’s obligation to take clear, effective decisions and actions that meet citizens’ needs;
- transparent and active consultations with the civil society and businesses in formulating policies and making governmental decisions;
- prevent corruption through effective measures, identify reasons and conditions which lead to corrupt behavior and limit and/or eliminate them and
- counteract corruption effectively through mechanisms that quickly identify and interrupt existing corrupt practices.

**Audit Conduct**

**Audit Scope**

A pilot audit is meant;

- to be a process learning experience for a ministry’s substantive
to produce a report that contains realistic and substantive recommendations to the ministry in order to identify areas prone to corruption, malfeasance and errors and

• to assist the ministry’s authorities in addressing vulnerabilities and implementing corrective measures.

The approach to the pilot and the findings are initially based on:

• a focused internal review and tools development/fine tuning that include an integrated framework checklist, personnel questionnaires, scrutiny and understanding of the ministry’s constitutive laws and regulations;

• a workshop organized to identify vulnerable areas and

• relevant experience and documentation from best practices in countries that conduct anti-corruption audits.

Audit Objective

Identify, through various means, areas and processes exposed to corruption pressure in order to include them in the yearly plans of the internal audits and inspections, and estimate how employees assess the integrity of the following:

• identify and understand the ministry’s strategic planning;

• organizational activities;

• regulation of the obligations;

• activity control;

• human resources development;

• internal and external communications;

• compare employees’ assessment to the actual situation by, for example, using document checks and

• formulate recommendations to strengthen the organization’s capacity to develop anti-corruption and integrity policies that agree with the principles and standards outlined in the legal framework and national anti-corruption instruments.
Audit Methodology

The methodology consists of four stages.

**Stage 1 - Prepare**

The following activities should take place before executing the mandate:

- allocate responsibilities for the work;
- form a task group;
- introduce and explain the activity to the staff and
- create a group that will act as sounding board.

The following three stages form the essence of the project:

**Stage 2 - Identify vulnerable activities**

- meet all relevant stakeholders;
- task group to meet relevant senior managers and explain the nature of vulnerable organizational activities;
- organize a workshop for relevant stakeholders;
- list vulnerable activities and organizational vulnerabilities dealing with handling money, critical assets, sensitive information and important services and
- identify, with the assistance of senior managers, situations or processes that may constitute an integrity risk such as unreliable personnel and functions that may lead to a conflict of interest.

**Stage 3 - Review vulnerable activities**

- Non-specific vulnerable activities:
  - are there applicable and relevant rules and regulations?
  - are these rules and regulations effective and qualitatively adequate?
- Organizational vulnerabilities:
  - is there a policy or are measures taken to deal with organizational vulnerabilities?
are such policy and measures effective enough?

is the staff aware of such policy and measures and do they act accordingly?

Stage 4 - Recommend solutions

- to improve the quality and awareness of rules, regulations and policies;
- to institutionalize these;
- to maintain the policies, rules and regulations up-to-date;

The methodology focuses on examining vulnerable activities and organisational weaknesses based on a sequential approach:

- fully understand key activities in the ministry/entity:
  - institutional framework: laws, bylaws, ordinances;
  - tools: methodologies, instructions and documents regarding relevant activities;
  - scope of key activities of the ministry/entity;
  - objectives and results of tasks, ways and means to achieve them;
  - organization: organizational chart of the ministry/entity;
- identify directorates (organizational functional units) prone to corrupt practices;
- identify processes within these directorates that are especially prone to corruptive practices;
- analyze each process in line with their operational procedures;
- identify responsible civil servant for each of the operational procedures;
- determine within these procedures the,
  - separation of functions;
  - authorizing functions;
  - documentation and records;
  - flow of documentation (sign-off, authorization initials, OKs, etc.);
o review by responsible functionary;

o approval;

o confirmation;

- Identify reality and reliability of internal control measures;
  - collect information from auditees;
  - interview auditees;
  - fill out questionnaires;
  - check the actual functioning of controlling procedures (gap analysis);

- Report results for;
  - gap analysis;
  - explanations and/or reasons for the gap;
  - recommend improvements to the current situation.

Following the principle of institutional internal review, this methodology enables a government entity to conduct its own audits. It focuses on gaining insight into the organization’s vulnerabilities and on finding out what measures it can develop to protect itself against corruptive practices. This resistance capability can be assessed by examining regulations, policies, procedures, guidelines and measures that govern and guide the organization’s operations. In addition to enhancing the organization’s capability to identify vulnerable sports, this approach helps to prevent violations and/or threats to the organization’s control systems. It consists of:

- identifying vulnerabilities;

- assessing the organization’s resistance capability to compensate for such vulnerabilities;

- developing measures to enhance this resistance capability and

- providing a “tool kit” with checklists, examples and background information.

This methodology uses the less labour-intensive method of customized interviews tailored to the organization’s structure, focuses on its vulnerabilities and produces the best and most
tangible short-term results.

The audited entity can carry out its own audit using self-assessment tools that were specially developed and approved:

- organize a workshop with the staff to identify and assess vulnerable areas, processes and activities in relevant areas;
- conduct a survey with questionnaires filled by some members and representatives of various directorates;
- conduct anonymous surveys with randomly selected representative specialists from the managerial staff (Directors of Directorates, Heads of Departments);
- inspect documents;
- interview representatives of the entity.

**Audit Evidence**

The purpose is to:

- set standards and provide guidance on what constitutes evidence in the review process, including financial statements;
- determine the quantity and quality of required evidence and outline procedures for obtaining it.

The reviewer/auditor must obtain sufficient and appropriate evidence to draw reasonable conclusions.

**Concept of evidence**

Evidence refers to all the information used to draw conclusions and express an opinion from all records underlying the organization and its finances to other relevant sources. However, reviewers are not expected to inspect all data that may exist. Evidence which is cumulative in nature includes both information collected through procedures applied during the review and obtained from other sources such as previous reviews and the government entity quality control procedures. Records generally include initial entries and supporting data such as cheques and electronic fund transfers, invoices, contracts, general and subsidiary ledgers, journal entries and other adjustments to the financial statements and others such as worksheets and spreadsheets supporting cost allocations, computations, and reconciliations. Entries in accounting records are often initiated,
recorded, processed and reported in electronic form and records may also be part of integrated systems that share data and support all aspects of the entity’s reporting, operations and compliance objectives. Management is responsible for preparing all statements based upon the records. The reviewer/auditor may obtain some evidence from testing records - through analysis and review - by performing procedures that were followed in the reporting process, reconciling related types and applications of the same information. The reviewer/auditor may then determine that the accounting records are internally consistent and agree with the financial statements. However since accounting records alone do not provide sufficient evidence on which to base an opinion on the financial statements, then further evidence needs to be obtained. The reviewer/auditor may also collect evidence from minutes of meetings, confirmations from third parties, analysts’ reports, comparable data about competitors (benchmarking), controls manuals, information obtained by the auditor from such audit procedures as inquiry, observation and inspection with other information developed by or available allowing the reaching of conclusions through valid reasoning.

**Appropriate and sufficient evidence**

Appropriateness is the measure of the *quality* of evidence. This refers to the relevance and reliability of the evidence in supporting or detecting misstatements in the classes of systems, transactions, account balances, disclosures and related assertions. Sufficiency is the measure of the *quantity* of audit evidence and is affected by the risk of misstatement and the quality of evidence. The greater the risk of misstatement, the more evidence is likely to be required but, the higher the quality of audit, the less evidence is required. A given set of procedures may provide evidence that is relevant to certain assertions but not others. For example inspection of records and documents related to the collection of receivables after the period-end may provide evidence regarding both existence and valuation but not necessarily the appropriateness of period-end cut-offs. On the other hand, the reviewer often obtains evidence from different sources or of a different nature that is relevant to the same assertion. For example, one may analyze the aging of receivable and their subsequent collection to obtain evidence relating to the valuation of the allowance for doubtful accounts. Furthermore, obtaining evidence relating to a particular assertion - for example, the physical existence of inventory - is not a substitute for
obtaining evidence regarding another assertion, as in the case of the valuation of inventory.

The reliability of evidence is influenced by its source and nature and depends on individual circumstances under which it is obtained. Generalizations about the reliability of various kinds of evidence can be made, however such generalizations are subject to important exceptions. Even when evidence is obtained from sources external to the entity circumstances can affect the reliability of the information obtained. For example evidence obtained from an independent external source may not be reliable if the source is not knowledgeable. While recognizing that exceptions may exist, the following generalizations about the reliability of evidence can be stated:

- evidence is more reliable if obtained from independent sources outside the entity;
- evidence generated internally is more reliable when the entity’s related controls are effective;
- evidence obtained directly by the reviewer (for example, observing how a control is applied) is more reliable than that obtained indirectly or by inference (for example inquiring about how a control is applied);
- evidence is more reliable if it is documented, whether on paper, electronically, or through other media (for example, a contemporaneously written record of a meeting is more reliable than a subsequent oral representation of the matters discussed);
- evidence provided by original documents is more reliable than that provided by photocopies or facsimiles.

A review rarely involves authenticating documentation nor is the reviewer trained or expected to be an expert in doing so. However, one considers the reliability of the information to be used as evidence, for example photocopies, facsimiles, filmed, digitized or other electronic documents that have relevant controls over their preparation and maintenance. When using the information provided by the entity to perform procedures, the reviewer should obtain evidence about the accuracy and completeness of the information. In order to obtain reliable evidence, the reviewer should ensure that the information upon which the procedures are based is sufficiently complete and accurate. For example, in
verifying revenue by applying standard prices to records of sales volume, one considers the accuracy of the price information and the completeness/accuracy of the sales volume data. If the evidence about the completeness and accuracy of the information produced by the entity’s information system forms an integral part of the review procedure itself, one may perform concurrently the procedure that applies to that information. Otherwise, he/she may have obtained evidence of the accuracy and completeness of such information by testing controls over the production and maintenance of the information. However, the reviewer may sometime determine that additional procedures are needed as in the case of additional procedures for computer-assisted audit techniques (CAATs) in order to recalculate information.

The reviewer normally collects more reliable information from consistent evidence obtained from different sources or from sources of different nature. Moreover, obtaining evidence from different sources or from sources of different nature may indicate that an individual evidence is not reliable. For example, information obtained from a source independent of the entity that corroborates the one obtained from a management representation would increase the validity of the evidence. Conversely, if the evidence obtained from one source is inconsistent with the one obtained from another the reviewer must determine what additional procedures are necessary to resolve the inconsistency. One compares the cost of obtaining evidence to its usefulness but the issue of difficulty or expense is not sufficient in itself for omitting a procedure that has no alternative.

In forming an opinion the reviewer does not have to examine all the information available because conclusions can usually be reached through sampling approaches and other means of selecting items for testing. The reviewer may also find it necessary to rely on evidence that is persuasive rather than conclusive but, to gain reasonable assurance, the reviewer should not be satisfied with evidence that is less than persuasive but should use professional judgment and exercise professional skepticism in evaluating the quantity and quality of evidence, thus its sufficiency and appropriateness to support an opinion.

**Assertions in obtaining evidence**

Management is responsible for the fair presentation of financial statements that reflect the nature and operations of the entity. In representing that these give a true and fair view – or are presented
fairly in all material respects – in accordance with the applicable financial reporting framework, management implicitly or explicitly supports and approves the recognition, measurement, presentation and disclosure of the various elements of financial statements and related disclosures.

The reviewer should use assertions for classes of transactions, and account balances, and prepare sufficiently detailed presentations and disclosures to assess the risks of material misstatement and to develop and carry out further tests and procedures. In making such assertions the reviewer considers different types of potential misstatements that may occur and thereby designs procedures that are responsive to the assessed risks. Other *International Standards on Auditing (ISA)* discuss specific situations where one is required to obtain evidence at the assertion level. Assertions thus fall into the following categories;

- **assertions about classes of transactions** and events for the period under review;
  - Occurrence – transactions and events that pertain to the entity, have happened and were recorded;
  - Completeness – transactions and events that should have occurred and were recorded;
  - Accuracy – amounts and other data relating to recorded transactions and events that were recorded appropriately;
  - Cut-off – transactions and events that were recorded in the correct accounting period;
  - Classification – transactions and events that were recorded in the proper accounts.

- **assertions about account balances** at the period end:
  - Existence – assets, liabilities and equity interests do exist;
  - Rights and obligations – the entity holds or controls the rights to its assets and is accountable for its liabilities;
  - Completeness – all assets, liabilities and equity interests that should have been recorded were recorded;
  - Valuation and allocation – the financial statements properly record assets, liabilities, equity interests and any resulting valuation or allocation adjustments.
• assertions about presentation and disclosure:
  o Occurrence, rights and obligations – disclosed events, transactions and other matters that pertain to the entity have occurred;
  o Completeness – disclosures that should have been included in the financial statements were included;
  o Classification and comprehension – financial information is appropriately presented and described and disclosures clearly expressed;
  o Accuracy and valuation – financial and other information are disclosed fairly in appropriate amounts.

The reviewer may use the above-mentioned assertions or may express them differently provided that all aspects are covered. For example, he/she may choose to combine the assertions about transactions and events with the assertions about account balances.

**Obtain evidence**

The reviewer obtains his/her evidence to draw reasonable conclusions that support the opinion by performing the following procedures:

• obtain an understanding of the entity and of its environment, including its internal control system, to assess the risks of material misstatement in the financial statements and assertion levels (the ISA’s refer to such procedures as “risk assessment procedures”);

• if necessary or when the reviewer has determined to do so, test the controls’ effectiveness in preventing or detecting and correcting material misstatements at the assertion level (the ISA’s refer to such audit procedures as “tests of controls”) and

• detect material misstatements at the assertion level (the ISA’s refer to such audit procedures as “substantive procedures” which include testing detailed classes of transactions, account balances and disclosures and substantive analytical procedures).

The reviewer always performs risk assessment procedures to properly assess risks at the financial statement and assertion levels. However, risk assessment procedures alone do not provide
sufficient appropriate audit evidence to support the audit opinion and, if required, must be supplemented by further procedures in the form of tests of controls and substantive procedures. Tests of controls are necessary in two circumstances:

- when the assessment includes an expectation of the operating effectiveness of controls he/she is required to test those controls to support the risk;

- when substantive procedures alone do not provide sufficient appropriate evidence he/she is required to perform tests of controls to obtain evidence about their operating effectiveness.

The reviewer plans and performs substantive procedures to be responsive to the related assessment of the risks of material misstatement which includes the results of tests of controls, if any. The reviewer’s risk assessment is judgmental, however, and may not be sufficiently precise to identify all risks of material misstatement. Furthermore, there are inherent limitations to internal control including the risk of management override, the possibility of human error and the effect of systems changes. Therefore, substantive procedures for material classes of transactions, account balances and disclosures are always required to obtain sufficient appropriate audit evidence. The reviewer can use one or more types of procedures or combinations thereof to be used as risk assessment procedures, tests of controls or substantive procedures depending on the context in which they are applied. In certain circumstances evidence obtained from previous reviews/audits may provide contemporary evidence.

The nature and timing of the procedures to be used may be affected by the fact that some of the accounting data and other information may only be available in electronic form or at certain points or periods in time. Source documents, such as purchase orders, bills of lading, invoices and cheques may be replaced with electronic messages. For example entities may use electronic commerce or image processing systems. In e-commerce, the entity and its customers or suppliers use connected computers over a public network such as the Internet to transact business electronically. Purchase, shipping, billing, cash receipt, and cash disbursement transactions are often consummated entirely by the exchange of electronic messages between parties. In image processing systems documents are scanned and converted into electronic images to facilitate storage and reference with source
documents not retained after conversion. Certain electronic information may exist at a certain point in time but such information may not be retrievable after a specified period of time if files are changed and if backup files do not exist. An entity’s data retention policies may require the auditor to request retention of some information for the auditor’s review or to perform procedures at a time when the information is available. When the information is in electronic form, the auditor may carry out some of the audit procedures described below through CAAT’s.

**Inspect records and documents**

Inspection consists of examining records and/or documents, whether internal or external, in paper, electronic form or other media. Inspecting records and documents provides audit evidence of varying degrees of reliability depending on their nature and source and, in the case of internal records and documents, on the effectiveness of the controls over their production. An example of inspection used as a test of controls is one that considers records or documents for evidence of authorization. Some documents provide direct evidence of the existence of an asset, for example, a document constituting a financial instrument such as a stock or bond. In addition, inspecting an executed contract may provide audit evidence relevant to the entity’s application of accounting policies such as revenue recognition.

**Inspect assets**

This consists of physically examining tangible assets and thereby providing reliable evidence of their existence but not necessarily about the entity’s rights and obligations nor their valuation. Inspecting inventory items ordinarily accompanies the observation of inventory counting.

**Observe**

Observation consists of reviewing a process or procedure being performed by others. Examples include observing the counting of inventories by the entity’s personnel and observing the performance of control activities. Observation provides evidence about the performance of a process or procedure but is limited to the point in time at which the observation takes place and by the fact observation may be affected how the process or procedure is performed.
Inquire

Inquiry consists of seeking information, both financial and non-financial, from knowledgeable persons throughout the entity or outside of it. Inquiry is a procedure that is used extensively throughout the audit and often complements other procedures. Inquiries may range from formal written to informal oral ones and evaluating responses to inquiries is an integral part of the process. Responses to inquiries may provide the auditor with information that was not obtained or which validate other evidence. Alternatively responses might provide information that differs significantly from other evidence obtained, for example information regarding the possibility that management overrides controls. In some cases responses to inquiries may lead the auditor to modify or perform additional audit procedures. The auditor performs procedures, in addition to using inquiry, to obtain sufficient appropriate evidence. Inquiry alone does not normally provide sufficient evidence to detect a material misstatement. Moreover inquiry alone is not sufficient to test the operating effectiveness of controls. Even if corroborative evidence through inquiry is often important it may be of limited reliability as in the case of inquiries about management’s intent. In such cases understanding management’s past history of carrying out its stated intentions with respect to assets or liabilities, management’s stated reasons for choosing a particular course of action and management’s ability to pursue a specific course of action may provide more relevant information about management’s real intentions. In some situations the auditor will obtain written representations from management to confirm responses to oral inquiries. For example the auditor usually obtains written representations from management on material matters when other sufficient appropriate evidence cannot reasonably be expected to exist or when that other evidence obtained is of a lower quality.

Confirm

Confirming is a specific type of inquiry to obtain information that represent existing condition directly from a third party. For example the auditor may seek direct confirmation of receivables by communicating with debtors. Confirmations are frequently used in relation to account balances and their components but need not be restricted to these items. A further example is that of an auditor’s request to confirm the terms of agreements or transactions an entity has with third parties. Such request is meant
to determine if the agreement were modified and, if so, to get relevant details. Confirmations are also used to obtain evidence about missing conditions such as “side agreement” that may influence revenue recognition.

Recalculate

Recalculating consists of checking the mathematical accuracy of documents or records. Recalculations can be performed through the use of information technology, for example, by obtaining an electronic file from the entity and using CAAT’s to check the accuracy of the summary of a file.

Reperform

Reperforming is the auditor’s independent execution of procedures or controls that were originally performed as part of the entity's internal control, either manually or through the use of CAAT’s, as in the case of redoing the aging of accounts receivable.

Analyse

This consists of evaluating financial information arising from plausible relationships between financial and non-financial data. It also leads to investigating identified fluctuations and relationships that are inconsistent or deviate from other relevant information.

Audit Documentation

The purpose of documenting work and procedures is to set standards and guide staff in attesting financial statements. The auditor should document matters which are important in providing evidence to support his/her opinion and evidence that the work was carried out in accordance with ISA’s. Documentation means the material (working papers) prepared by and for or obtained and retained by the auditor in connection with the performance of the audit. Working papers may be in the form of data stored on hardcopy, film, electronic or other media.
Review Manual

Planning

*Plan and perform effectively*

- Adequately planning the work helps ensuring that it will focus on important areas, identify potential problems and be completed expeditiously. It also assists in properly assigning work to the review staff and ensures proper coordination of work conducted by other auditors and experts;

- The extent of planning will vary according to the size of the entity, its complexity as well as the auditor’s experience with the entity and knowledge of the business;

- Acquiring knowledge of the business is an important part of planning as such knowledge will assist the auditor in identifying events, transactions and practices which may have a material effect on the review findings;

- The auditor may wish to discuss elements of the overall plan and certain procedures with the entity’s management and staff in order to improve the effectiveness and efficiency of the work and to coordinate procedures with the work of entity’s personnel. However the overall plan and programme remain the auditor’s responsibility.

*Describe the expected scope and conduct of the review*

The plan will consider the following matters:

- Knowledge of the business such as general economic factors, the entity’s characteristics, financial performance and reporting requirements;

- Understanding the accounting and internal control systems such as accounting policies and pronouncements;

- Risk and materiality such as assessing controls, risks, materiality levels, potential material misstatements and identifying complex accounting areas;

- Nature, timing and extent of procedures such as the effect of information technology on the review and on the work of
internal auditors and Inspectorate General;

- Coordination, direction, supervision and review: involvement of other auditors in components, experts, number of locations and staffing requirements.

**Specify the nature, timing and extent of procedures to implement the plan**

The programme provides a set of instructions to assistants involved and helps control and record the proper execution of the work.

It may also contain the objectives of each review area and a budget that covers the required hours for specific areas or procedures.

**Risk analysis and internal control**

The auditor should understand the accounting and internal control systems and the design of such systems in order to plan the work and develop an effective approach. The auditor should initially assess the control risk for each material account balance or class of transactions and identify major classes of transactions such as accounting records, supporting documents and the reporting process. A “walk through” test that traces a few transactions through the accounting system should also be conducted. The auditor should use professional judgment in assessing the risk and in keeping procedures at an acceptable low level. Risk refers to the acceptable level so that the auditor may express an appropriate opinion.

**Files**

Files document standards and provide guidance for the work carried out for a review. The auditor should document important evidence that support his/her opinion that the review was carried out in accordance with ISA’s.

**Working papers**

- assist in planning and performing the review;
- assist in supervising and reviewing the work and
- record the evidence that support the auditor’s opinion.
Form and content of working papers

- the auditor should prepare working papers, sufficiently complete and detailed, to provide an overall understanding of the review;

- the auditor should record information on the nature, planning, timing, procedures, results and conclusions of the review work.

The working papers should include the auditor’s rationale on all significant matters which require judgment and on the ensuing conclusions. In areas involving questions of principle or judgment, the working papers should record relevant facts that have been taken into account in reaching conclusions. The auditor thus determines how detailed the working papers should be since it is neither necessary nor practical to document every matter considered. However, without going into details, the auditor should provide information that would help another auditor not familiar with the audit to understand the work performed and the basis of the decisions reached. The other auditor can discuss the details of the audit with the auditor who prepared the working papers. The form and content of working papers can be affected by such matters as:

- nature of the engagement;
- form of the reviewer’s report;
- nature, size and complexity of the business;
- nature and complexity of the entity’s internal control;
- needs for direction, supervision and review of work performed by assistants;
- specific audit methodology and technology used in the course of the review.

Working papers are designed and organized to meet the circumstances as well as the needs of each review. Using standardized working papers (e.g. checklists and specimen letters) may contribute to more efficient preparation and review processes, facilitate the delegation of work and provide a means to control quality. The auditor may utilize schedules, analyses and other documentation that the entity has prepared in order to increase efficiency but he/she should be satisfied that such materials were properly prepared.
Working papers ordinarily include the following:

- information about the entity and its environment, including internal controls and others such as:
  - the legal and organizational structure of the entity;
  - extracts or copies of important legal documents, agreements and minutes;
  - the industry, economic and legislative environments of the entity;
  - extracts from the entity’s internal control manual.

- evidence of the planning process including programs and any changes thereto;

- evidence that the auditor considered and reached a conclusion about internal auditing;

- analyses of transactions and balances;

- analyses of significant ratios and trends;

- identified and assessed risks of material misstatements at the financial statement and the assertion levels;

- record of the nature, timing, extent and results of procedures performed in response to risks at the assertion level;

- evidence that the work performed by assistants was supervised and reviewed;

- indication of who performed the procedures and when;

- detailed procedures of another auditor who reviewed the financial statement of another component;

- copies of communications with other auditors, experts and third parties;

- copies of letters or notes concerning audit matters communicated to or discussed with management or those charged with governance, including terms of the engagement and material weaknesses in internal control;

- letters of representation received from the entity;

- conclusions concerning significant aspects including how exceptional and unusual matters were actually resolved or
treated;

- copies of financial statements and auditor's report.

- In the case of recurring audits, some working paper files may be classified as:
  - permanent files which are updated with new information of continuing importance or
  - current files which contain information relating primarily to the review of a single period.

Confidentiality, safe custody, retention and ownership of working papers

The auditor should maintain the confidentiality and safe custody of the working papers and retain them long enough to meet the needs of the practice in accordance with legal and professional requirements of record retention. While owning the working papers the auditor may use discretion in making part of that information available to the entity. However they are not a substitute for the entity’s accounting records.

Using work of others

When an auditor uses the work of another auditor, the lead one should determine how the work of the other will affect the review. When planning the work, the auditor should initially assess the internal audit/Inspector’s General control function, if relevant to the review to be undertaken.

Conclusions and Reporting

The auditor should review the conclusions drawn from the evidence as the basis for expressing an opinion on the findings of his/her review and the report should clearly express an opinion on the situation as a whole. The report includes the following basic elements:

- title, addressee, identification of the procedures, processes and/or statements reviewed;

- scope describing the nature, work performed, opinion, date and auditor’s identification.
Review Programme

Findings

*Types of findings - a practical example*

The “hot spot detection” review carried out by the *Iraqi Board of Supreme Audit (BSA)* in accordance with the manual (see Annex III) was meant to identify weaknesses in relevant departments and administrative units. Most of these flaws were grouped as follows:

- inflated personnel numbers and masked unemployment;
- abuse of powers, authority and conflict of interest;
- waste of resources;
- theft and embezzlement;
- manipulation;
- misuse of transportation means;
- illegitimate privileges;
- aid and grants used for other than intended purposes;
- fictional debt accounts and ensuing payments;
- collusion in contracting;
- failure to refer contract violations to legal authorities to benefit financially and
- spending on fictional projects.

*Disposition of findings*

- discuss findings with relevant reviewed departments/entities after obtaining necessary evidence;
- obtain responses and opinions of parties involved and amend findings in accordance with evidence provided;
- consolidate findings in a final report;
- deliver final report to relevant authorities in accordance with the nature of the given case:
- immediate auditees;
• relevant sector ministry hierarchy for final disposition;

• General Inspector’s office in the ministry;

• Commission on Public Integrity, or similar Committees or Commissions such as an Integrity Commission, a Financial Committee, a Supervising Committee for the Economic sector and/or judicial authorities.

**Management Risks**

Administration/management is the main component of any governmental unit as it sets out the lines of authority of the organizational structure from top to bottom. It also sets out responsibilities for the division of labour according to specialties and functions. Flaws in these relationships may lead to negative practices such as delaying reports, taking wrong or uniformed decisions, increasing bureaucracy and creating gaps that allow for administrative corruption.

Common recurrent risks in the organization’s administration or management are:

• inappropriate administrative structures for the entity’s or department’s activities;

• unnecessary administrative structures leading to appointing unqualified or superfluous employees on the basis of nepotism;

• unnecessary structures that may allow for blackmailing citizens;

• appointing employees not identified as regular personnel;

• weak central supervision and decision making centres at unqualified lower structures which may encourage abuse of authority for personal benefit;

• delegating authority and assigning tasks to people who do not have the required qualifications or competencies thus leading to misconduct or gain of personal benefits;

• no division of tasks and responsibilities which can allow a single employee to undertake non authorized transactions for personal benefit;

• no clearly identified steps and procedures to complete required tasks and transactions thus leading to delayed work,
blackmailing citizens and the misuse of discretionary powers;

- hiring staff who do not have the required academic qualifications or experience;

- no documentation system that discloses officials’ financial interests;

- contradictory and inconsistent orders that create confusion for personal benefit;

- no formal system to replace employees in case of sudden vacancies and

- improper authorization or control over nominating employees for academic leaves.

**Relevant Review Checklist Extracts - (see PART 7)**

- compatibility of the organizational structure with the administrative unit;

- powers and functions;

- division of labour and level of supervision;

- conflicts of interest;

- recruiting, staffing and promotion;

- leaves, assignments, relocations and

- procedures for rendering services and implementing transactions.

**Financial and Accounting risks**

Any error in these procedures will result in lack of control over assets, liabilities and cash and might lead to embezzlement, theft and waste of an institution’s resources. Furthermore, such errors may also cause inefficiencies in the performance of a government entity.

Common recurrent risks associated with financial accounting are:

- incomplete accounting system information and documentation discrepancies;

- failing to adopt the principle of authorizing documents such as signatures and stamps;
lack of division of labour and tasks thereby allowing one person to perform a sequential number of tasks possibly resulting in illegal transactions or disbursing excessive amounts of money;

lack of system to document and confirm ownership by registering properties and all other assets;

lack of control over fixed assets and cash especially in large institutions that have several branches;

lack of control over administrative and financial units in branches with lack of centralized follow up;

lack of safeguarding fixed assets from misuse, damage and theft;

weak security systems and failure to use passwords;

weak control over assets lent to other governmental units and failing to obtain required authorizations to move them;

weak control over the use of seals/stamps allowing for fake transactions;

failing to segregate employees dealing with cash and failing to issue orders for people authorized to deal with cash;

weak control over items and amounts received as grants or gifts and failing to identify people authorized to receive them;

failing to identify responsibilities for disbursements and receipts in a clear manner;

weak control over payables/liabilities;

weak control over important documents (sales lists and receipts);

inaccurate calculation of deductions and commissions;

failing to use authorized sales lists in releasing goods out of warehouses;

granting credit to clients without authority to do so and lack of guarantees or documentation for such credits;

no distribution plan, especially in crucial areas such as the pharmaceutical sector which can lead to misuse and negligence in adhering to regulations;
• inefficient programs for the procurement and distribution of medicine which might result in inconsistencies;

• importing medicines from unreliable sources which would jeopardize their quality and expiry date;

• delay the deposit of cash payments in the current account so as to use these amounts to gain personal benefit;

• disbursing the wages of people who have quit their jobs, resigned or retired;

• recording false expenditures such as wages, salaries, equipment disposition and rental;

• receiving cash payments that exceed the authorized limit;

• inefficient control over services provided, especially when related to cleaning, paving and sanitary works – risks in this field include falsifying lists of workers with weak supervisory systems thus increasing risks in dealing with sub-contractors;

• collusion between officials to undertake irregular transactions as in the taxation and customs departments;

• failing to list tax payers and identify tax exemptions for vendors and service providers. Risks may also occur from failing to follow up on due payments;

• more than one file for the same employee, where the information in such files vary with tax estimates and does not comply with instructions;

• contradiction in estimating taxes for real estate located in one geographical area as a result of collusion or nepotism;

• failing to record the actual income of professionals, such as doctors, lawyers and engineers;

• granting grace periods that exceed those set out in taxation laws and regulations;

• spending grants and loans for other than intended purposes and

• inefficient control over important documents such as warehouse release documents.
Relevant review checklist extracts - (see PART 7)

- Assess accounting systems – records, documents and procedures;
- Evaluate controls over fixed assets and inventory;
- cash flow;
- sales and marketing – industrial products, medicines, oil, etc.;
- salaries, wages, rewards and benefits;
- grants and subsidies (extra-budgetary);
- investments and return on investments (RoI);
- lending and borrowing;
- creditor and debtor balances;
- other expenditures and budget

Technical and Organizational Risks

Production activities represent the main process in the industrial sector (e.g. producing goods, extracting oil or producing electrical energy) and most often use modern techniques and advanced technologies. Failing to do so might lead to such problems as wasting resources, damaging raw materials and squandering financial resources. Production activities can also be jeopardized by fraud, embezzlement and wastage.

Common recurrent risks associated with technical and substantive activities are:

- failure to keep up with new technological developments resulting in not addressing problems and complications in the production process, wastage of resources thus increasing the cost of production or the quality of products;
- importing raw materials that do not meet quality criteria or specifications;
- failure to use scientific methods and standard measures in assessing the suitability of the material thus possibly leading to inaccurate percentages and weak accountability and
monitoring over damage and overuse of material;

- lack of a reliable and efficient inventory system causing lack of control of materials which might lead to deterioration and manipulating stored goods;

- lack of an efficient system to monitor the aging of stored goods as in the case of pharmaceutical products;

- lack of or inefficient cost accounting system to identify areas that waste resources;

- weak control over production wastage and inefficiencies;

- errors and misstatements in oil production, from pumping to distributing oil products. This accounting depends on measurements with meter devices that can often be outdated or tampered with. The same goes for the electricity sector;

- exploiting oil pipes and electricity networks by citizens or employees and

- lack of an effective and equitable system to distribute oil products and electricity outputs.

**Relevant review checklist extracts - (see PART 7)**

- verifying production and services;

- wastage and misuse in the production and services sector;

- actual costs and planned costs of production and services;

- quality of production and services;

- controlling wastage in production and services.

**Contracting and Procurement Risks**

Contracting and procurement activities involve large sums of public monies. They must therefore respect the principles of free competition, require accurate and objective analyses to choose the best products and services at the lowest possible price, and involve extensive procedures with legal and financial aspects. Legal risks include granting contracts or procuring products and services from unreliable and inefficient sources thus wasting public money. Financial risks include disbursing money without getting adequate/pre-specified products or services in return.

Common recurrent risks associated with contracting and
procurement activities are:

- entering into contractual agreements without ensuring the availability of pre allocations in the budget which may lead to excessive expenses resulting in personal gain;
- not conducting a feasibility study for works or services to be procured thus leading to implementing bad projects and works or the procurement of unnecessary products;
- executing contracts to procure goods that might be already available in government warehouses;
- making contractual arrangements without the required authorizations;
- dividing tasks or procurement requirements to avoid announcing a public tender and/or favour certain contractors resulting in personal benefits;
- dealing with contractors who do not meet the legal requirements or do not have the required financial capacity for the intended works or services;
- disbursing payments to contractors and vendors for works and projects that are not completed or do not exist (ghost projects);
- failing to collect due taxes and charges from contractors and/or vendors or failure to obtain sufficient guarantees from them;
- accepting bids and offers after opening the tender documents, which often suggests that prices included in the first bids were revealed. This practice allows for collusion with contractors;
- failing to change the members of the analysis/awards committee periodically;
- accepting incomplete works that do not meet the required specifications or accepting defective or expired goods;
- lack of provisions regarding penalties especially for delayed delivery and failing to take legal actions when delivery does not occur or does not meet the conditions stated in the contract;
- using the method of direct invitation instead of public tenders in order to deal with specific vendors or contractors to gain personal benefit;
- giving advances to contractors and vendors with no guarantees
in return;

- paying the total fees for vendors without confirming that the goods were delivered or met specifications;
- contracting a national or foreign company without having the required authorizations;
- granting extensions to contractors without deducting the due fines from their fees;
- paying the contractors amounts that exceed the value of the accomplished work and
- failing to identify accurately the project requirements thus possibly resulting in costly change of orders.

Relevant review checklist extracts - (see PART 7)

- contracting procedures including evaluation;
- contracting jurisdiction: authorities and competencies;
- public tendering and awarding:
- tender invitations;
- tender documents;
- tender bids: opening, analyzing and awarding;
- verification of contract articles and items;
- technical aspects;
- legal aspects;
- financial aspects and
- contract implementation

Risks in National Investment Plan Projects and Reconstruction Activities

The investment plan stimulates the economic development process through projects financed from allocations not included in the regular budget and governed by different regulations. Reconstruction projects (grants and donations) have a special status that require specific procedures and regulations.

Common recurrent risks associated with investment and
reconstruction plan projects are:

- using the allocations of the investment budget to finance non-investment plan projects;
- failing to create independent records and documents for investment plan projects and recording the transactions of these projects in the logs of the current budget projects;
- weak office and field supervision;
- executing projects, within the reconstruction plan or investment budget, that are unnecessary nor have economic feasibility;
- lack of control over funds received as grants and donations;
- using grants and donations to finance other types of projects;
- financing “ghost” projects;
- paying contractors’ fees without verifying completed works on site and
- paying for work that was not delivered.

**Relevant review checklist extracts - (see Part 7)**

- investment plan projects;
- reconstruction projects.

**Risk in the Banking Sector**

The national banking sector comprises the central bank and the banking institutions and sectors directly operated and in control of the national governments authorities such as agricultural and enterprise development banks. In many transitional and developing economies, multilateral financial institutions often require that international auditing firms be contracted to carry out conventional audits and report on the operations and adherence to credit agreements. Eventually, the aforementioned institutions may be audited by their own national SAI’s once the multilateral institutions have assessed that they have the capacity to render quality and especially reliable assurance services.

The above does not preclude internal inspectorate, internal control units or SAI units, competent in using programmes developed for such work, from carrying out institutional risk assessment reviews.
Areas and processes that must be especially evaluated are:

- sector dealing directly with either the public or other national development entities;
- loan legal documentation;
- adherence to credit requirements;
- use of lent funds;
- performance of investments;
- bad debt allowances;
- loan defaults;
- multilateral institution requirements and covenants;
- proceeds recuperation and
- interference or implication of governmental officials.

**Relevant review checklist extracts - (see PART 7)**

- accounting department;
- vault safekeeping;
- treasury operations;
- current accounts;
- savings accounts;
- fixed term deposits;
- bills;
- loans and bank facilitation;
- employee loans;
- letters of credit;
- letters of guarantee and
- international transactions and functions.
PART 4 - PILOT AUDITS

Section 1 – Audit Programme

(Based on Part 7 checklist)

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Audit Staff

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Management Risks

- compatibility of organizational structure with administrative units;
- powers and functions;
- division of labour and level of supervision;
- conflicts of interest;
- recruiting, staffing and promotion;
- leaves, reassignments and relocations and
- procedures for rendering services and executing transactions.

Financial and Accounting Risks

- control of all assets and inventory;
- cash management;
- sales and marketing;
- grants and subsidies;
- accounts payable and receivable;
- payroll;
• taxes;
• securities;
• loans and
• investments.

**Contracting and Procurement Risks**
• contracting procedures including evaluation;
• contracting jurisdiction: authorities and jurisdictions;
• advertisement and awards procedures;
• tender documents;
• reception of bids;
• tender opening and analysis/awards committees;
• appeals and complaints department;
• contract awards and provisions;
• accounting and auditing procedures;
• contracting jobs and
• delivery of goods/services confirmation committee.

**Risks in Investment Plan Projects and Reconstruction Activities**
• investment plan projects and
• reconstruction works.

### Section 2 – Institutional Risk Assessment Report

**Objective**
Identify the gaps and weaknesses that could allow for administrative and financial corruption in order to enhance standards, procedures and practices to correct weaknesses or corruption prone areas.
Results

The audit results are generally presented in the same sequence set out in the table of contents of the institutional risk assessment review programme and focus on findings that identified weaknesses or system flaws.

Implementation, follow up and action plan

(see Section 3 on the Audit Report)

Management risks

• weakness observations;
• summary of findings and
• recommendations.

Risks in the financial and accounting functions

• weakness observations on
  o accounting systems and
  o budget controls
• summary of Findings and
• recommendations.

Risks in the contracting and procurement functions

• weakness observations;
• summary of findings and
• recommendations.

Section 3 – Detailed Institutional Risk Assessment Report

Report

(including disposition of findings)

General

Upon completing the review, a report should include:
• audit opinion;
• purpose and intended use;
• auditing standards that were applied and the effect of non adherence;
• respect of INTOSAI and/or ISA standards;
• detailed overview of observations and recommendations and the
• audit opinion that:
  o states whether statements present a true and fair view:
    ✓ of the financial situation at the particular date;
    ✓ of the results of operations and
    ✓ of cash flows for the period;
  o confirms that such statements were prepared in accordance with International Accounting Standards and comply with statutory requirements;
  o includes such issues as:
    ✓ deficiencies noted in the internal control system and
    ✓ an overview of the government entity follow up on observations of previous year(s). It is especially important to ensure that all internal systems include a feedback mechanism for improvement.

**Types of findings**

The “hot spot detection” review that a government entity or an SAI carries out in accordance with specialized manuals is meant to identify weaknesses in relevant departments/administrative units. Most of these flaws can be grouped as follows:

• inflated personnel numbers and masked unemployment;
• abuse of powers, authority and conflicts of interest;
• waste of resources;
• theft and embezzlement;
• manipulation of records;
• misuse of transportation means;
• illegitimate privileges;
• using aid and grants for other than intended purposes;
• fictional debt accounts and ensuing payments;
• collusion in contracting;
• failure to refer contract violations to legal authorities and
• spending on fictional projects.

Disposition of findings
• discuss findings with relevant departments after obtaining the necessary evidence;
• obtain responses and opinions of parties involved and subsequently amend findings accordingly;
• consolidate findings in a final report;
• deliver final report to relevant authorities sequenced below in accordance with the nature of the given case:
  o immediate auditees;
  o relevant sector ministry hierarchy for final disposition;
  o General Inspector’s office in the ministry;
  o Anti-Corruption or similar body such as an Integrity Commission, a Financial Committee or a Supervising Committee for the Economic sector.

Review of previous year’s regular audit reports
An overview of the reviewed entity’s follow up on audit observations of previous year(s). It is especially important to ensure that the systems’ design includes a feedback mechanism for improvement.

Review of internal controls
The report should include a detailed overview of the deficiencies noted in the system of internal control.

Review of corruption incidents
The above-mentioned “hot spot detection” in “Types of findings” will identify weaknesses in relevant departments and administrative units. For future reference, it may be necessary to
conduct an additional review of such incidents as abuse of powers, authority and conflict of interest, theft and embezzlement, records manipulation, illegitimate privileges, fictional debt accounts and ensuing payments, collusion in contracting, failure to refer contract violations to legal authorities, spending on fictional projects and other sought after results.

**Specific risk areas**

In addition, it may be necessary to conduct an in-depth analysis of “hot spots of corruption”:

- to ensure that measures will be taken to amend the programme for future reviews;
- to assist management in taking appropriate actions to deal with identified risks. “Risk areas” may include inflated personnel numbers, waste of resources, records manipulation, misuse of transportation means, using subsidies and grants for other than intended purposes.

**Stakeholders’ inputs and queries**

It is standard practice in the transaction assurance world to involve auditees and other stakeholders in dealing with audit findings. In fact it has become an auditee’s right to respond and react to the findings and to include such response in the final report.
PART 5 - OTHER ACKNOWLEDGEMENTS

Institutions

- Bureau of Integrity of the City of Amsterdam, Netherlands
- CIDA - Canadian International Development Agency, Ottawa, Canada
- GTZ - Deutsche Gesellschaft für Technische Zusammenarbeit GmbH, Eschborn, Germany
- Ministry of the Interior, The Hague, Netherlands
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PART 6 - GLOSSARY

Accounting policies
Principles, bases, conventions, rules and practices to prepare and present financial statements

Accounting systems
Tasks to process transactions and maintain financial records. Such systems identify, assemble, analyze, calculate, classify, record, summarize and report transactions and other events having an impact on the financial situation/results.

Accrual accounting
Principle whereby transactions and other events are recognized when they occur rather than when related cash or equivalent is received or paid. Such transactions and events are recorded in the accounting records and recognized in the financial statements for the periods to which they relate. Elements recognized under accrual accounting are assets, liabilities, net assets/equity, revenue and expenses.

ACN
Anti-Corruption Network: a group of highly experienced anti-corruption experts who have adapted and applied the methodology described in this compendium to various country settings with substantive institutions that are front line players and/or stakeholders in the national integrity system.

ARABOSAI
Arab Organization of Supreme Audit Institutions.

Assets
Resources controlled by an entity as a result of past events and from which future economic benefits or service potential are expected to flow to the entity.

Audit evidence
Information obtained to draw conclusions that support the audit opinion.

Audit objective
The objective of auditing financial statements is to enable the auditor to express an opinion on whether the financial statements adhere, in all material aspects, to an identified financial reporting framework.
Audit opinion

A clearly written assessment of the financial statements as a whole. An unqualified opinion is expressed when the auditor concludes that the financial statements give a true and fair view, in all material respects, in accordance with the identified financial reporting framework.

Audit programme

Sets out the nature, timing and extent of planned audit procedures required to implement the audit plan. The audit programme serves as a set of instructions to assistants involved in the audit and as a means to control the proper execution of the work.

Audit risk

Risk of giving an inappropriate audit opinion when the financial statements are materially misstated.

Audit sampling

The application of audit procedures to less than 100% of the items within an account balance or class of transactions in order to obtain and evaluate audit evidence about some characteristics of the items. Such evidence must support a conclusion with respect to the entire set of data.

BSA

Board of Supreme Audit of Iraq.

CAAT

Computer Assisted Audit Techniques.

Cash

Comprises cash on hand and demand deposits.

Cash flow

Inflow and outflow of cash and cash equivalents.

CIDA

Canadian International Development Agency.

Contractor

An entity that performs construction work pursuant to a construction contract.
Control environment
Comprises the overall attitude, awareness and actions of directors and management regarding the internal control system and its importance in the entity.

CoR
Council of Representatives of Iraq (Legislature).

CSO
Civil Society Organization.

Data base
A collection of data that is shared and used by a number of different users for different purposes.

Depreciation (amortization)
The systematic allocation of the depreciable amount of an asset over its useful life.

DFID
Department for International Development (United Kingdom).

Documentation
The material (working papers) prepared by and for, or obtained and retained by the auditor to conduct the audit.

EU
European Union.

Events after the reporting date
Favourable and unfavourable events that occur between the reporting date and the date when the financial statements are authorized for issue.

Exchange rate
Rate at which a currency may be converted into another.

Fair value
The amount for which an asset can be exchanged or a liability settled between knowledgeable and willing parties in an arm’s length transaction.
Financial asset
An asset that is:

- Cash,
- a contractual right to receive cash or another financial asset from another entity,
- a contractual right to exchange financial instruments with another entity under conditions that are potentially favourable or
- an equity instrument of another entity.

Financial liability
A liability that is a contractual obligation:

- to deliver cash or another financial asset to another entity or
- to exchange financial instruments with another entity under conditions that are potentially unfavourable.

Financial statements
The balance sheet, income statement (profit and loss), statement of changes in financial position, notes and other explanatory material which are identified as being part of the financial statements.

Fixed price contract
A construction contract in which the contractor agrees on a fixed price or on a fixed rate per unit of output which is sometime subject to cost escalation clauses.

Foreign currency
A currency other than the reporting currency of an entity.

Fraud
An intentional act by one or more managers, other persons in authority, employees or third parties. It implies the use of deception to obtain an unjust or illegal advantage.

Governance
A code of conduct for people associated with the entity (directors, supervisory board members, investors, etc.) that sets rules for sound management, proper supervision and an adequate division of duties.
Government business enterprise

An entity that has all the following characteristics:

- has the power to contract in its own name;
- has the financial and operational authority to carry on a business;
- sells goods and services in the normal course of its business to other entities at a profit or full cost recovery;
- does not rely on continuing government funding as an ongoing concern (other than purchases of outputs at arm’s length) and
- is controlled by a public sector entity.

IMAGOS

An independent consulting firm based in München (Germany) specialised in helping governments, NGOs and private corporations find specific technologies and tools to effectively address corruption and mismanagement. IMAGOS calls upon the specialised expertise and experience within the ACN.

Impairment

A loss in the future economic benefits or service potential of an asset over and above its normal depreciable life.

Internal audit

An appraisal activity established within an entity as a service to the entity: its functions include examining, evaluating and monitoring the adequacy and effectiveness of the accounting and internal control systems.

Internal control system

Policies and procedures adopted by management to ensure the orderly and efficient conduct of an entity’s business, the safeguard of assets, the prevention and detection of fraud and error, the accuracy and completeness of the accounting records and the timely preparation of reliable financial information.

Inventories

List of such assets as:

- materials or supplies to be consumed in the production process;
- materials or supplies to be consumed or distributed in the
rendering of services;

- materials or supplies for sale or distribution in the ordinary course of operations; or
- materials or supplies being produced for sale or distribution.

ISA

International Standards on Auditing

Joint venture

A binding arrangement whereby two or more parties are committed to undertake an activity which is subject to joint control.

Key management personnel

- directors or members of the governing body of the entity and
- other persons having the authority and responsibility for planning, directing and controlling the activities of the reporting entity.

Lease

An agreement whereby the lessor conveys to the lessee the right to use an asset for an agreed period of time, in return for a payment or series of payments.

Legal obligation

An obligation that derives from:

- an explicit or implicit contract,
- legislation or
- other legislative enactment.

Liabilities

Present obligations arising from past events, the settlement of which is expected to result in an outflow of resources embodying economic benefits or service potential.

Market value

The amount obtainable from the sale or payable on the acquisition of a financial instrument in an active market.

Materiality

Information is material if its omission or misstatement could influence
users’ decisions or assessments based on the financial statements. Materiality often depends on the nature or size of the item or error in the particular circumstances of omission or misstatement.

**Monetary items**

Cash and other assets and liabilities to be received or paid in fixed or determinable amounts of money.

**NGO**

Non-governmental Organization.

**OECD**

Organization for Economic Cooperation and Development.

**Operating activities**

Activities other than investing or financing activities.

**Oversight**

The supervision of activities with the authority and responsibility to control or exercise significant influence over financial and operating decisions.

**Property, plant and equipment**

Tangible assets that:

- are used in the production or supply of goods and services for rental or for administrative purposes and
- are expected to be used during more than one reporting period.

**Provision**

A liability of uncertain timing and/or amount.

**Reporting date**

The date of the last day of the reporting period to which the financial statements relate.

**Revenue**

The gross inflow of economic benefit or service potential during the reporting period when such inflow results in increased net assets/equity other than increases relating to owners’ contributions.
SAI
Supreme Audit Institution: Public body of a state which, however designated, constituted or organized, exercises by law, the highest public auditing function of that state. It is usually the appendage of the national legislature.

TI
Transparency International: Global civil society organisation that leads the fight against corruption, brings people together in a powerful worldwide coalition to end the devastating impact of corruption on men, women and children around the world. TI’s mission is to create change towards a world free of corruption.

UNCAC
United Nations Convention Against Corruption

UNDP
United Nations Development Programme

UNO
United Nations Organization

Useful life (of property, plant and equipment)
- period of time over which the entity is expected to use an asset or
- number of production or similar units that the entity is expected to obtain from the asset.

Working papers
A record of the auditor’s planning: nature, timing and extent of the procedures performed; results of such procedures; and conclusions drawn from evidence obtained. Working papers may be data stored on paper, film, electronic or other media.
PART 7 - CHECKLISTS

705 questions covering themes formulated in this compendium

Management risks

59 questions to assess:

- Compatibility of the organizational structure with the administrative units;
- Powers and functions;
- Division of labour and levels of supervision;
- Conflicts of interest;
- Recruiting, staffing and promotion;
- Leaves, assignment, relocations/reassignments and
- Procedures for rendering services and implementing transactions.

Financial and Accounting Risks

203 questions to assess:

- Accounting systems – records, documents, procedures, controls of current, fixed and inventory;
- Cash management;
- Sales and marketing;
- Grants and subsidies;
- Accounts receivable and payable;
- Payroll;
- Taxes;
- Securities;
- Loans and
- Investments.

Organizational Risks

36 questions to assess:

- Effectiveness and organization of production and service units;
- Wastage and misuse in the production and services sectors;
- Actual costs versus planned costs of production and services;
• Quality of production and services and
• Controlling waste in production and services.

**Contracting and Procurement Risks**

*157 questions to assess:*

• Contracting procedures including bid evaluation;
• Contracting jurisdiction: authorities and competencies;
• Advertisement and award procedures;
• Tender documents;
• Reception of bids;
• Tender opening and analysis/award committee;
• Appeals and complaints procedures and or department;
• Contracts award provisions;
• Accounting and auditing procedures;
• Contracting jobs and
• Contractual delivery confirmation committee/process.

**Risks in Investment Plan Projects and Reconstruction Activities**

*24 questions to assess:*

• Investment plan projects and
• Reconstruction works.

**Risks in the Banking Sector**

*226 questions to assess:*

• Accounting departments;
• Vault safekeeping;
• Treasury operations;
• Current bank accounts;
• Savings accounts;
• Fixed term deposits;
• Bills;
• Loans and bank facilitation;
• Loans to employees;
• Letters of credit;
• Letters of guarantee and
• International transactions and functions.
ANNEX I – National Supreme Audit Institution Proposal

ANTI-CORRUPTION AUDITING APPROACH

(Template)

Step 1 – METHODOLOGY
for conducting anti-corruption audits in all administrative structures of the executive and judiciary

The methodology is a step-by-step guide in assessing and identifying the potentially vulnerable areas (hot spots) within all executive or state entities. Its strategy is directed at reducing administrative and high level corruption and is meant to increase confidence in state institutions, enhance trust in the rule of law and all citizens’ equality.

Step 2 - FRAUD AWARENESS
Workshops for SAI audit programme preparation

Fact-finding workshops are conducted for each government entity to be reviewed in order to orient the formulation work and thus make step 3 more efficient and less time consuming. Institutional areas more prone to malfeasance and corruption are thus pre-identified by the government entity stakeholders and the SAI audit team.

Step 3 - ACTION PLAN
for conducting anti-corruption audits within the central and territorial structures of the executive power

The SAI manual/programme focuses on rules, procedures, processes and systems. In addition, attention is paid to a number of other integrity-related instruments such as codes of conduct, dilemma training and official function/organization oaths. The first objective of the action plan is
to formulate an anti-corruption audit manual and the second objective is to develop individual audit programmes for each targeted government entity.

**Step 4 – ANTI-CORRUPTION MANUAL**

**Model Table of Contents**

1. Introduction
2. Purpose
3. Findings: actions and follow up
   a. Types of findings
   b. Disposition of findings
4. Assessing administrative risks
   a. compatibility of the organizational structure to the administrative unit
   b. powers & functions
   c. labour division & level of supervision
   d. conflict of interest
   e. recruiting, staffing & promotion
   f. leaves, reassignment and relocation
   g. procedures for rendering services & implementing transactions
5. Assessing risks in the industrial & energy sectors
   a. production unit inputs
   b. used raw material
   c. actual & standard loss percentages in industry
   d. waste & loss in oil & electricity
   e. actual & projected production costs
   f. production quality
   g. control over production waste
6. Assessing financial & accounting risks
   a. existing accounting systems
   b. records
   c. documents
   d. computerized systems
e. control of fixed assets & inventory
f. cash flows
g. sales & marketing
   i. industrial products
   ii. pharmaceuticals
   iii. oil products
   iv. others/public revenues
h. salaries, wages, rewards & benefits
i. grants & aids (extra-budgetary)
j. investment & return on investment
k. lending & borrowing
l. creditor & debtor balances (approval and reconciliation)
m. other expenditures (transportation, allowances, delegation, etc.)
n. budget controls

7. Assessing contracting & procurement risks
   a. contracting procedures
   b. contracting jurisdictions
   c. public tendering & awarding
   d. tender invitations
   e. tender documents
   f. tender opening, analyzing and awarding committees
   g. final awarding
   h. contract articles & items
   i. technical aspects
   j. legal aspects
   k. contract implementation procedures

8. Assessing risk of investment plan projects & reconstruction
   a. investment plan projects
   b. reconstruction projects
   c. current budget financed projects
   d. extra-budgetary financed projects

9. Assessing risk in the banking sector
   a. accounting functions
b. safekeeping

c. treasury operations

d. current accounts

e. savings accounts

f. term deposits & bills

g. loans and credit facilitation

h. employee loans

i. letters of credit

j. letters of guarantee

k. international transactions and functions

10. Governmental unit specifics

a. review of previous years’ regular audit reports

b. review of unit’s internal controls

c. review of corruption incidents

d. auditee’s inputs, queries and analysis of specific risk

Step 5 - PILOT AUDIT PROGRAMME

(for e.g. Iraq State Company for Agricultural Products)

A government entity allowing for the testing of the programme is selected and a designated SAI – Anti-Corruption review team is appointed and the necessary training is conducted.

Step 6 – PREPARATION

of Anti-Corruption Audit/Review Report

Findings and recommendations for follow up are presented initially to the auditee’s entity which is responsible for follow up. The report can be divided into the following topics and substantive areas:

a. Anti-Corruption audit findings

b. its purpose, intended use and dispositions

c. indication of applied auditing standards such as INTOSAI, ISA, etc.

d. review and analysis of specific risk areas (corruption prone areas)

e. observations and recommendations
f. deficiencies noted in the system of internal control

g. follow up by auditee of previous year’s observations

Step 7 – FOLLOW UP
on anti-corruption audit/review findings and recommendations

The pilot audit team submits its initial report and recommends to the ministry/government unit authorities to incorporate a detailed implementation chronology in its upcoming budget year and in its work plans. A 24-month implementation schedule for the recommendations and related observations and findings is often a realistic calendar. An implementation monitoring and benchmarking calendar/schedule allows for the necessary follow up as the initial step in the government wide implementation of the anti-corruption audit mechanism.
ANNEX II - National Line Ministry Review Experience (Bulgaria)

- A Best Practice in executive entities –
  (hot spot detection)

INSTITUTIONAL RISK ASSESSMENT (IRA)

Part 1 – INTRODUCTION

1. preamble;
2. distinction between regular audit and institutional risk assessment;
3. methodology of institutional risk assessment

Part 2 – SCOPE

1. introduction;
2. selection of the targeted ministry, subject to an institutional risk assessment;
3. context and qualification of the IRA;
4. objective;
5. methodology;
6. detailed work programme:
   a. preparation;
   b. identification of vulnerable activities and processes;
   c. review of vulnerable activities and processes;
   d. recommendations to management
7. work schedule for IRA

Part 3 – DOCUMENTATION

1. appropriate working papers;
2. samples;
Part 4 – REPORT on FINDINGS and RECOMMENDATIONS

1. contents of the report;
2. purpose and intended use of the report;
3. findings and recommendations by theme and topic;
4. recommendations in the area of process and approach;
5. recommendations in the area of prevention and combat of corruption;
6. recommendations in the area of internal and external controls;
7. recommendations in the area of human resources;
8. recommendations in the area of access to information;
9. recommendations for implementation

Part 5 – ANNEXES

1. Annex I – workshop report;
2. Annex II – questionnaires:
   a. for structured interviews with management;
   b. anonymous questionnaires for managerial and technical staff;
3. Annex III - composition of the IRA working group;
4. Annex IV - findings and observations of the IRA
ANNEX III – Supreme Audit Institution Experience (*Irak*)

- A Best Practice in legislature entities -

(*anti-corruption audit/hot spot detection*)

**ANTI-CORRUPTION MANUAL**

Part 1 – INTRODUCTION

Part 2 – PURPOSE

Part 3 – ADMINISTRATIVE RISKS

1. compatibility of the organizational structure to the administrative units;
2. powers and functions;
3. labour division and level of supervision;
4. conflicts of interest;
5. recruiting, staffing and promotion;
6. leaves, reassignment and relocation;
7. procedures for rendering services and implementing transactions

Part 4 – TECHNICAL and SUBSTANTIVE RISKS

1. Production Audit:
   a. audit of production-technical aspects:
      i. usage of raw material:
         1. actual and standard;
         2. loss percentages in industry;
         3. waste and loss in oil and electricity sectors;
   2. actual and projected production costs;
   3. production quality;
   4. control over production wastage

Part 5 – FINANCIAL and ACCOUNTING RISKS
1. assessment of existing auditing systems:
   a. records;
   b. documents;
   c. computerized systems
2. control of fixed assets and inventory;
3. cash flow;
4. sales and marketing:
   a. industrial products;
   b. medicine;
   c. oil products;
   d. others
5. salaries, wages, rewards and benefits;
6. grants and subsidies (extra-budgetary);
7. investment and return on investment;
8. lending and borrowing;
9. creditor and debtor balances (approval and conformity);
10. other expenditures (transportation, special allowances, delegation);
11. budget controls

Part 6 – CONTRACTING and PROCUREMENT RISKS

1. assessing contracting procedures;
2. verifying adherence to instructions and jurisdictions;
3. verifying public tendering and awarding:
   a. public tendering;
   b. tender documents;
   c. tender opening, analyzing and awarding committees;
   d. final awarding
4. verification of contract articles and items:
   a. technical aspect;
   b. legal aspect
   c. verification contract implementation procedures

Part 7 – RISKS of the INVESTMENT PLAN PROJECTS and RECONSTRUCTION
1. investment plan projects;
2. reconstruction projects:
   a. current budget financed projects;
   b. extra-budgetary financed projects

Part 8 – REPORT on AUDIT FINDINGS and RECOMMENDATIONS

Actions and follow up:
1. types of findings;
2. disposition of findings
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