Financial Reporting Fraud Deterrence and Detection
Action Steps for Internal Auditors

Tone at the Top

A strong ethical culture starts with an organization’s most senior leaders and cascades down through the entire organization to create a “mood in the middle” and a “buzz at the bottom” that reflects and reinforces the company’s operating values.

1. Work proactively with the audit committee to develop a clear, shared vision of the internal audit function in order to reinforce the integrity and importance of the function throughout the company.

2. Require basic fraud detection training, including the detection of financial reporting fraud, for all internal auditors.

3. If warranted, consider allocating one internal audit position for a fraud specialist, ideally someone with appropriate experience and certifications.

4. Take an active and visible role in supporting the ethical culture, including evaluating hotline results, conducting ethics surveys of employees, and collaborating with other departments to address results and remediate applicable findings. Analyze year-over-year changes in key metrics.

5. Evaluate soft controls and the corporate culture, including assessment of the company’s fraud risk management program, and involve appropriate departments in addressing the results.

6. Establish or otherwise ensure there is a formal process to educate the board and audit committee on the risks and red flags of financial reporting fraud, with a particular focus on the risks of management override of controls.

Skepticism

Skepticism—a questioning mindset and an attitude that withholds judgment until evidence is adequate—promotes risk awareness and is inherently an enemy of fraud.

1. Suggest to the board and audit committee specific ways in which internal audit can provide support, with a particular focus on the risk of financial reporting fraud.

2. Take the lead role in assessing the company’s program to mitigate the risk of financial reporting fraud, and report annually to the audit committee on that assessment.

Communications

Each of the participants in the financial reporting supply chain has a separate but interconnected role in the shared responsibility to deter and detect fraud. Fulfilling this responsibility successfully requires leveraging each party’s complementary activities by sharing and communicating information and concerns and identifying any gaps in the collective efforts to mitigate the risk of financial reporting fraud.

1. Establish a regular schedule of face-to-face meetings with senior management, the audit committee, and the external auditor to exchange insights and perspectives. Explore opportunities for the external auditor to leverage the work of internal audit.

This information originally appeared in the Center for Audit Quality’s Report, Deterring and Detecting Financial Reporting Fraud: A Platform for Action. For more resources on this topic visit our website at www.THECAQ.org.