

# FRAUD AND THE PANDEMIC

Internal audit stepping up to the challenge

*A joint research report by the  
Internal Audit Foundation and Kroll*



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# Introduction and methodology

**In 2020, before the start of the pandemic,** Kroll and the Internal Audit Foundation (the “Foundation”) surveyed Institute of Internal Audit (“IIA”) members across the globe to better understand their views on the role of internal audit in fraud risk management (the “2020 Survey”/the “Survey”). The Survey focused on the role of the internal audit profession in strategic fraud risk management and risk assessment; how the profession was involved in the practical operational tasks of fraud prevention, detection, and response; the barriers to internal audit having a more profound involvement in fraud risk management; and a consideration of the trends in investment in internal audit teams around fraud risk management.<sup>1</sup>

Since then, the world has undergone something of a seismic shift. Against the backdrop of the unbridled impact of the pandemic on the global economy, national health systems, and people’s livelihoods, high-profile and large-scale corporate fraud cases have continued to make the headlines. Considering the factors that drive instances of fraud higher (opportunity, rationalization, and pressure/incentive), the unprecedented changes in the past two years have presented something of a perfect storm in terms of the likelihood of fraud occurring and going undetected. Opportunity has increased in many areas through changing working practices and rapidly recalibrating control frameworks. Rationalization has increased due to a deterioration of loyalty and sense of belonging, which stems from an increase in remote working and impacts on reward and remuneration structures. Finally, both organizations and individuals face mounting pressures due to a challenging and unpredictable financial situation triggered by a widespread but inconsistently managed state of emergency.

**Given all the changes, we found it timely to revisit the Survey’s findings, which were based on pre-pandemic data, and understand how auditors feel their organizations have adjusted to the evolving landscape and potential increase in fraud risk. We sought to discover what lessons can be learned and applied to emerge more robust and more resilient to future changes.**

To do this, we held a series of focus groups in 2021 with a number of internal audit professionals, some 18 months into the pandemic. The focus groups discussed the Survey findings, how the participants’ organizations had evolved during the past 18 months, and how the profession might need to further adapt to the changing fraud risk landscape.<sup>2</sup>

This report sets out the themes and considerations that the Foundation and Kroll gathered during the series of roundtable focus groups as well as analysis of data collected through other polls.

1. The survey report, “[Internal Audit’s Role in Fraud Risk Management](#),” is available on Kroll’s and the Internal Audit Foundation’s website

2. Note the participants of the focus groups were not the same participants as those who completed the survey but were intended to provide a wide representation of sectors and geographies.



# Methodology

## ***Roundtable discussions***

Kroll and the Foundation held a series of focus groups in October and November 2021. In total, the roundtables were attended by 50 participants from a wide range of industries across 24 countries. The participants were asked to consider the findings of the 2020 Survey and share experiences on the changes that occurred since the survey was conducted. The first aspect focused on the consideration of the themes from the 2020 Survey, namely:

- To what extent does the involvement of internal audit in fraud risk management impact the perceived effectiveness of the fraud risk management process?
- Where does responsibility for strategic fraud risk management lie within the organization?
- What role does internal audit have in the prevention, detection, and investigation of fraud?
- What are the challenges and barriers to internal audit's involvement in fraud risk management?
- What are the trends in investment in fraud risk management in recent years?

Against this backdrop, the participants were asked to discuss their experiences of how the pandemic had impacted fraud risk and their role in combatting fraud. These discussions focused on the following themes:

- The impact of the pandemic on the fraud landscape and how organizations have dealt with this impact.
- The evolution of the role and expectations of internal audit in response to this evolution.
- Whether there has been any change with the barriers to internal audit being more involved in fraud risk management.
- What trends were there in investment into fraud risk management coming out of the pandemic?

In this report, we set out the themes that emerged from the focus groups both in consideration of the 2020 Survey and in the context of how the landscape has evolved since the Survey.

## ***Poll questions***

In addition to the qualitative discussions in the roundtables, we also gathered data from a series of poll questions during the roundtables which are summarized in this report. In addition to this, we conducted three short polls on LinkedIn in October 2021. The poll questions were as follows:

1. Has your organization experienced an increase in fraudulent activity since the start of the COVID-19 pandemic in any of the following areas (phishing or cyber/misappropriation of assets/financial statement fraud/none of the above)? – 631 participants
2. Where has your organization added resources to support internal audit's role in fraud risk management during the pandemic (staffing/investigation resources/technology/training and communication)? – 519 participants
3. Where has your organization devoted additional resources to identify fraud and corruption since the start of the pandemic (controls/investigations/data analytics/enterprise risk assessment)? – 885 participants



# Executive summary of conclusions

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**The focus groups and polling data revealed** some consistent themes about the evolution of the nature of fraud risk, the response to it, and the changing focus and adaptation of internal audit in response to these changes. While the pandemic acted as a catalyst for change in some areas, such as technology in fraud and fraud prevention, in others, such as the need for continuous assurance, the pandemic created new challenges which required flexible solutions. The most successful organizations were flexible enough to respond quickly by implementing changes that positioned them for future risk planning.

In terms of the fraud landscape, while many participants felt that the overall prevalence of fraud had not necessarily increased, they felt that the type and nature of fraud had changed, partly driven by changing working practices. Many respondents felt that their organizations were much more exposed to cyber, social engineering, and phishing attacks, as well as impersonation of senior management to embezzle funds out of the business. There was a perception that the internal control framework had been weakened due to the challenges of remote working and, in many cases, a reduction of staff through illness, furlough, and headcount. Supply chain challenges were also highlighted. In some cases, the opportunity for fraud to go undetected was enhanced due to fluctuating prices and more fragmented supply chains and a reduction in visibility of third-party activity due to the inability to travel. There was also a perception that while reports of fraud may not have increased in some organizations, this was partly because it had gone undetected due to challenges in monitoring and detection presented by a more fragmented working environment.

## What shifted?

- The type and nature of fraud has changed driven by new workforce practices.
- Organizations have made investments to support cybersecurity and strengthen systems.
- The need for more continuous assurance has brought internal audit to the forefront.
- Investment in fraud risk management is likely to increase.

In response to this changing fraud landscape, there was a theme running through the focus groups that there had been enhancements and investment in technology to ensure cybersecurity, and the pandemic had in many cases acted as a catalyst to accelerate the strengthening of the organizations' systems. The use of data analytics also emerged as an area that had received particular focus.

Internal audit, like any other business function, experienced significant challenges presented by the pandemic in undertaking its day-to-day work. The inability to get onsite to check inventory levels or form relationships and partnerships with business leaders was particularly challenging. Many of the participants responded to this through the engagement of new and developing technologies, such as increased use of video conferencing to allow remote working and also through more creative use of technologies such as satellite imagery, open-source intelligence tools and drones to check the existence of assets and assess risk in business relationships. Internal audit, again like everyone else, also faced resource challenges with illness and furlough, meaning that in many cases, audit plans had to be reconsidered and frequently took significantly



longer than initially planned. The increase in the use of technology and the trend toward more flexible, lean working was, in the experience of many of the participants in the focus groups, already happening as part of a broader trend in how we all work. The pandemic has the impact of catalyzing these changes and forcing them to happen even quicker.

From the more strategic perspective, many participants felt that the pandemic put internal audit more in the driving seat when it comes to fraud risk management. Many talked about how internal audit had been put at the forefront of the operational challenges faced by organizations in the pandemic, with a requirement for continuous assurance and more collaboration with other business functions. A number of participants cited more strategic engagement with management from a fraud risk perspective, and more involvement in examining enterprise-wide fraud risk through a risk assessment. As was noted in the 2020 Survey, balancing the opportunity of being more involved in the strategic dialog with the threat of losing independence remained a significant concern of the participants.

Another significant challenge highlighted by the participants included an increasing gap in skills, particularly with the increased requirements for internal auditors to have more data analytics capabilities and to be involved in fraud investigation.

Overall, there was a perception that investment in fraud risk management was, as identified in the 2020 Survey, likely to continue to increase, in particular through investment in technology and in specific skills such as data analytics and open-source intelligence analysis being most frequently noted by participants. Based on the themes discussed during the roundtables, the pandemic appears to have provided the profession with some future-proofing and created an awareness of the need for flexibility and dynamism to be able to rapidly respond to the changing environments.



# Detailed findings from roundtables

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**In this section, we consider how** the participants in our focus groups felt that the main themes from the 2020 Survey were impacted as a result of the pandemic and how they responded to such changes.

## The change in fraud landscape and the response to it

The 2020 Survey found that among the internal audit community, respondents surveyed felt that when internal audit was more involved in fraud risk management, it positively impacted the effectiveness of fraud risk management programs. In considering this point, we asked the participants of the focus groups to comment on:

- The change in the landscape of fraud within their organizations; and
- How this has impacted fraud risk management as a whole.

The topics under this theme are considered below:

### ***The change in the landscape in fraud risk management during the pandemic***

The participants drew a distinction between the threats posed internally and externally to the organization.

With regard to external threats, several of the focus group participants indicated that they had noted a shift in the nature of fraud during the pandemic. Participants noted an uptick in frauds involving social media and cyberattacks, with people taking advantage of the pandemic to scam members of the public and employees of their organizations. For example, people selling the “cure” for the virus, and others preying on the fear that was so prevalent at the beginning of the pandemic to exploit human vulnerabilities in control frameworks.

This trend resonates with Kroll’s experience of the development of corporate fraud. Compared to 7 to 10 years ago, when corporate frauds tended to be internal and involved employee misconduct and collusion, today every employee, telephone, and computer represents an access point for organized crime to infiltrate, extract information, and exploit. While the old frauds have not gone away, there is a massive increase of reported fraud driven largely by the evolution of external fraudsters into sophisticated criminal enterprises.

The participants of the focus groups shared their experiences that fraudsters took advantage of the pandemic to utilize technology in a more coordinated way to target companies and individuals, and phishing, cyberattacks, and social engineering increased in sophistication with new techniques exposing organizations to increased risk.

From an internal fraud perspective, a number of participants identified that the remote working environment presented additional challenges that can lead to more fraud — particularly the inability to have any visibility over staff members or consultants, which resulted in the opportunity to misrepresent working hours without any real oversight. The difficulties of effectively managing people in a fragmented remote environment were also seen to directly impact culture, which some participants cite as key in terms of fraud prevention.



Not only with remote working, but also from a resource management perspective, many participants cited a dilution or weakening of the internal control framework resulting from a change in working environment due to layoffs, furlough, and the lack of a consistent team. This has presented issues to internal audit as they have been required to reassess the procedures and processes and so in effect, were auditing a moving target. One participant highlighted an increase in forged documents presenting additional risk, both from a “fake CEO”<sup>3</sup> fraud perspective and also relating to third-party contracts being faked which allowed funds to be extracted from the business.

From a fraud reporting perspective, some participants noted a reduction in the reporting of fraud during the period of remote working and a corresponding uptick in whistleblowing reports as the organization moved back to a more “business as usual” status.

Another theme that was identified by several participants was the challenge relating to visibility over the supply chain to ensure the quality and quantity of the supply of key goods. This was particularly highlighted by a number of participants in the medical supply industry, as supplies were in such high demand that new solutions had to be sought in order to meet the demand, which presented opportunity not only for excessive profiteering but also for exploiting the high demand and required quick turnaround to subject an organization to fraud. In some cases, this was compounded by a challenge in identifying fraudulent transactions due to fluctuating prices in supply chains, which meant that traditional analytical techniques were ineffective. The challenges faced by a reduction in visibility through the supply chain presented a further risk of third-party fraud. A number of participants also cited an increased risk of employee misappropriation of assets due to weaker physical controls over inventory and supply chain challenges that left the organization open to potential exploitation.

There was an acknowledgment from certain participants that fraud risks were not created as a direct result of the pandemic but had either been accelerated and had evolved because of the opportunities presented by the pandemic, or in some cases had revealed themselves through a change of focus and through management being forced to consider things from a different angle.

While some participants noted that from their perspective there remained a relatively low prevalence of fraud in their organization, in some cases they felt that this highlighted the increased challenges in detection and prevention activities that arose due to the pandemic. Some participants identified a decrease in the occurrence of fraud or embezzlement due to the decrease of activities resulting in reduced opportunity for fraud to occur.

Data obtained from the LinkedIn poll and through the polling questions during the focus groups was consistent with the points in the discussion — cyber/phishing fraud was the most prevalent increase across the board, with 54% of respondents stating that they noticed an increase in these kinds of instances. The second most prevalent area was misappropriation of assets, with 12% of poll respondents saying that they experienced an increase in frauds relating to asset misappropriation.

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3. Fake CEO fraud refers to an external fraudster impersonating a senior manager in the business and requesting that funds or other assets are moved/deployed urgently to a fraudulent account. Weakened internal control frameworks and skeletal staff during the pandemic made some organizations more susceptible to this kind of fraud.



## AREAS WITH FRAUDULENT ACTIVITY SINCE THE START OF THE PANDEMIC



Source: LinkedIn survey running Oct. 5 –7, 2021. Question: “Has your organization experienced an increase in fraudulent activity since the start of the COVID-19 pandemic in any of the below areas?” Total number of responses = 631.

### ***The development of fraud risk management in response to the changes***

Several participants cited examples of how they had responded to the changing risks highlighted above through the implementation of a more robust control framework tailored to specific areas. For example, in response to the technological challenges presented by remote working and increasing cyberattacks, participants’ organizations increased their focus on investing in cybersecurity, with several of them saying the pandemic provided a catalyst for their organization to upgrade their systems to ensure their organizational data was protected from the increase in external attacks. This included not only system upgrades but also investment in education against ransomware and other cyber threats. In some cases, the pandemic provided a chance for a reconsideration and reflection of the existing threats that may not have been recognized during a “business as usual” ordinary business cycle.

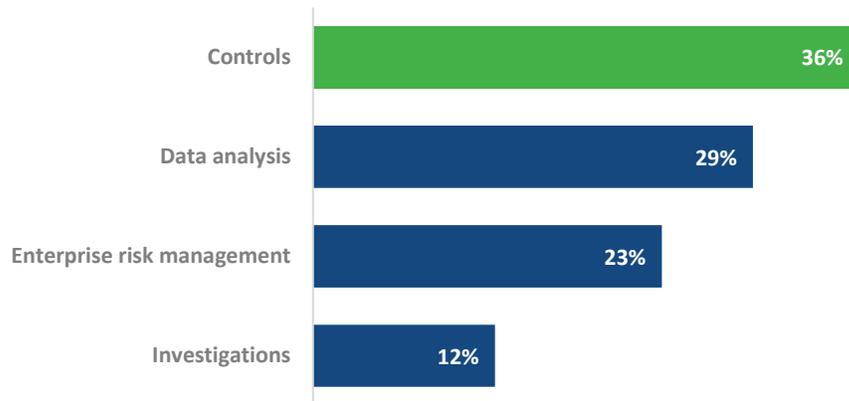
With regard to fraud prevention through education, several participants turned the inability to get in front of people throughout the business for larger training events to their advantage. One participant described how the education/training program had been much more focused on gathering specific information from across the business and the conversion of this data to quick “micro-training” on particular areas of fraud risk which was identified throughout the organization.

There has also been an increased focus on ensuring that data is more effectively used to prevent and detect fraud. Examples included the gathering of specific analytics around the movement of smaller inventory items to counter high-volume, low-value fraud and the consideration of the analysis of overtime using data drawn from around the organization. A number of participants in the focus group emphasized that data analytics needed to be applied with a strong dose of professional skepticism — the reasons for anomalies and other red flags need to be considered and tailored according to the specific industry and type of organization.

In the LinkedIn poll, 36% of respondents said they had devoted additional resources to internal controls, and 29% had devoted resources to data analytics.



## RESOURCES ADDED TO IDENTIFY FRAUD AND CORRUPTION SINCE THE START OF THE PANDEMIC



Source: LinkedIn survey running Oct. 9 –11, 2021. Question: “Where has your organization devoted additional resources to identify fraud and corruption since the start of the pandemic?” Total number of responses = 855.

## The changing nature of the role of internal audit

The 2020 Survey identified that internal audit was more focused in taking a strategic role in the reactive side of fraud risk management, i.e., taking the lead to investigate when a potential issue had been identified. We asked the focus group participants to comment on how internal audit’s role in fraud risk management had changed during the pandemic, both from the perspective of being able to provide the assurance that was required, and also from a more strategic perspective, how has the pandemic changed the role of internal audit and how well positioned was internal audit to be involved in fraud risk management in the current climate.

From an operational perspective, participants commented on the challenges of maintaining the continuity of the delivery of the audit program. Many participants shared their experiences of how their teams had responded to the challenges faced due to the pandemic and how the potential increase in fraud risks had forced them to consider more creative ways to obtain comfort over the audited area. This was particularly challenging where more traditionally there would be a requirement to be onsite (for example, in conducting inventory audit and reviewing documents of an overseas subsidiary). Some examples that the participants highlighted around being more

**In general, the participants commented that the role of internal audit in fraud risk management had increased, particularly in the more strategic prevention and detection areas of fraud risk management, rather than the reactive areas that were identified in the 2020 Survey. There was a perception that internal audit was being asked to upskill and provide more direction in certain areas, particularly in cybersecurity, which was driven by the increased risk identified in this area.**



creative included the use of video equipment and drones to confirm the existence of assets. Many expressed the view that limited access to data and documents onsite had in many cases extended the timeline of completion of the audit program, also partly due to absence because of illness/isolation.

Another challenge that remote working presented was the difficulty of internal audit teams to engage with and build the relationships with audit clients through video conferencing. There was a perception that although the remote working environment allowed certain areas to continue to function effectively, there were some areas that were adversely affected.

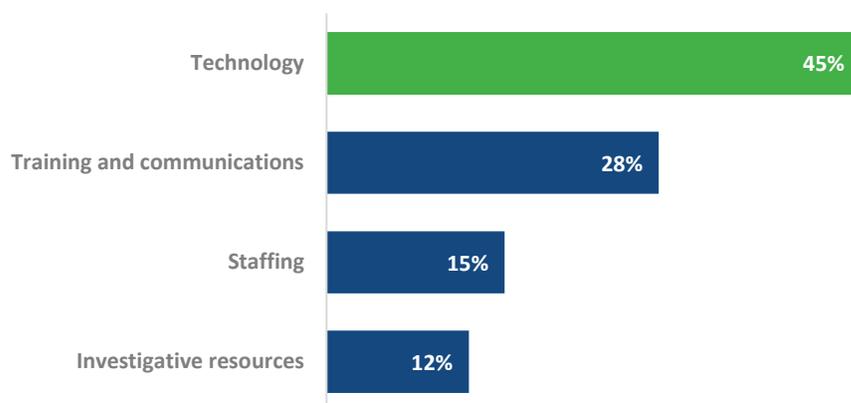
From the perspective of changing roles and responsibilities, one participant noted that due to the pandemic internal audit had been frequently used as a “stopgap” to deal with many additional operational areas, including procurement, human resources, and fraud risk management, as well as being more involved in cyber and information security. This was described by one participant as “building the plane as you fly.” Another described his internal audit team as being required to provide “continuous assurance” in response to the rapid changes in business practices. For some, this requirement for continuous assurance required a much more joined-up approach and more collaboration with first and second lines of defense in the fight against fraud. Examples that related specifically to fraud risk management included engaging more with management and conducting an enterprise-wide fraud risk assessment for the first time. As organizations have started to emerge from the most significant restrictions caused by the pandemic, internal audit teams have revisited the processes that had to operate under emergency circumstances and are considering longer-term recommendations to redesign and develop the legacy controls.

Some participants felt that the pandemic could have a long-term positive impact on both fraud risk management and the value of internal audit through driving strategic change in the governance structures and encouraging more investment in fraud risk management to respond to the changing environment. There was a perception from a number of participants that this investment would directly improve the internal audit function through improving the skill set of internal auditors, including in data analytics and fraud risk management and enhancing the level of professional skepticism with which internal auditors approach their audits. This could allow internal auditors to focus their attention and work more efficiently with the resources that they have. There was also a shift from “surprise” audits and one-off annual audits to more ongoing audits to provide continuous assurance. One participant also highlighted the need to focus more externally on third parties and the role that internal audit can play in activities around screening and ongoing audit of third parties, where significant fraud risk can occur.

The data gathered from the LinkedIn poll showed that the largest group of respondents (45%) had invested more resources in supporting internal audit with enhancements in technology.



## RESOURCES ADDED TO SUPPORT INTERNAL AUDIT'S ROLE IN FRAUD RISK MANAGEMENT DURING THE PANDEMIC



Source: LinkedIn survey running Oct. 12 –14, 2021. Question: “Where has your organization added resources to support internal audit’s role in fraud risk management during the pandemic?” Total number of responses = 519.

## What are the challenges and barriers to internal audit's involvement in fraud risk management?

The 2020 Survey highlighted a number of factors that respondents felt were barriers to internal audit being more involved in fraud risk management. The most common barriers noted were lack of appropriate resources, lack of mandate, a potential conflict of interest, and to a lesser extent the lack of adequate skills to undertake such work. A high proportion of those surveyed (over 80%) felt that these challenges and barriers prevented internal audit from being more involved and taking more of a leadership role when it comes to fraud risk management.

### In 2020

- Over 80% of respondents perceived that there was any barrier to internal audit's involvement in fraud risk management.
- Of these, a third felt that limited resources was the biggest barrier.
- Lack of mandate and potential conflict of interest had a similar perception as a barrier, with 23% and 21% respectively citing these areas.
- Of particular interest, only 11% of respondents felt that they did not have the skills to get more actively involved in fraud risk management.

In the roundtable discussions, a number of these barriers and challenges were discussed by the participants. Many participants felt that there was an increasing requirement/mandate for internal audit to get more involved in fraud risk management. A number of participants highlighted that the most effective internal audit



contribution from a fraud risk management perspective, and in other areas of risk management, requires a proactive mindset from internal auditors to stretch the boundaries where necessary rather than stick rigidly to the specific scope of the audit in which they are currently engaged. Some participants felt that maintaining this level of skepticism can be extremely effective at helping internal audit to identify risks and challenge the organization. While it is not the role of internal audit to take full responsibility for fraud risk management, there was a broad consensus in the focus groups that internal audit taking an active role in fraud risk management alongside good collaboration with other functional teams can add significant value.

There was some concern expressed by the participants, which resonated with the findings of the Survey, that internal audit might be brought too deeply into driving the agenda in terms of fraud risk management and their involvement in reactive investigations could hinder the delivery of the existing program. Participants considered the challenge of maintaining independence while contributing to the strategic dialog. Many participants felt strongly that it can still be valuable to have external parties engaged to avoid these kinds of issues in the investigation space.

In terms of the confidence level in being more involved in fraud risk management, a number of participants felt that in their organizations and internal audit teams, there was a particular skill gap that precludes internal audit being more involved in fraud risk management. With regard to investigation, one participant stated that their internal audit team was too small to be able to adequately conduct a detailed investigation, but they still had some involvement. Several participants stated that they deploy specific external resources to fill skill gaps.

There remains, however, a reluctance to take more of a strategic role for fear of being blamed if things go wrong. There was a theme that it was important to strike a good balance in order to maintain that collaborative approach while being sufficiently distanced from the control design and investigation of fraud.

## Trends in investment

In general, there was a trend that broadly aligned with the findings of the 2020 Survey in that the investment in fraud risk management and engagement of senior management and board members in the fraud risk management program continues to increase and the pandemic has acted as a catalyst for this increase. From an internal audit specific standpoint, as also supported by the LinkedIn survey data, a number of participants cited additional investment not only in internal audit staff, but increased focus on technology and training to enhance the capacity and capability of internal audit.

There was also a recognition that at times there needs to be an appetite for investment in external providers, who are required to fill gaps and enable internal audit to complete their existing responsibilities.



# Conclusion

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**In summary, the focus group participants** demonstrated that they — as internal auditors — have responded rapidly and dynamically to the changes in the fraud landscape and working practices presented by the pandemic. It appears that the pandemic has not only increased the expectation of internal audit to be even more involved in helping to rapidly reassess and improve operational processes, it has also pushed internal auditors closer to the strategic decision makers. This has been driven not necessarily by the profession and the auditors themselves, but by the circumstances that have required them to step up to the role. While many of the barriers highlighted in the 2020 Survey remain, particularly the discussion around balancing the expectation of value add versus providing independent assurance, there seems to be an emerging theme of building a leaner, more flexible, and more dynamic internal audit team that actively applies technology to improve effectiveness and responsiveness for the future.



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The Internal Audit Foundation strives to be an essential global resource for advancing the internal audit profession. The Foundation's research and educational products provide insight on emerging topics to internal audit practitioners and their stakeholders and promote and advance the value of the internal audit profession globally. Through the Academic Fund, the Foundation supports the future of the profession by providing grants to students and educators who participate in The IIA's Internal Auditing Education Partnership Program. For more information, visit [www.theiia.org/Foundation](http://www.theiia.org/Foundation).

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