

## Environmental Fraud (or EHS Fraud):

### How Auditing Programs Can Address the Challenge

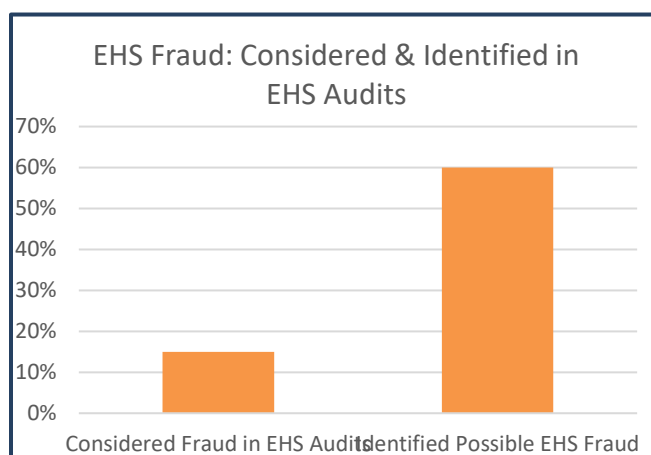
Fraud involving environmental or safety issues has been in the news. Yet environmental fraud (or EHS) fraud<sup>1</sup> is probably more common than organizations know. This tip sheet provides some highlights of a presentation at the Institute of Internal Auditors' EHS Audit Exchange<sup>2</sup> in Washington, DC in October 2018. The session's objectives were to raise awareness of environmental fraud, convey environmental auditors' role in detecting fraud, and to develop a sense of urgency for professional commitment.

#### POLLING QUESTIONS: Gaps and Opportunities

The audience (a packed house!) yielded information on how environmental auditors perceive fraud, views on the profession's most urgent needs, and other data (see chart).

#### SCENARIOS

The session featured discussion of scenarios that would be familiar to any environmental professional – or auditor. The scenarios included the true and the hypothetical. Mr. Hileman facilitated discussion to help attendees recognize areas for potential environmental fraud, how they might gather and interpret evidence, and how to establish appropriate boundaries for the audit. These techniques are common practice in Internal Audit and external assurance engagements – but still scarce in the EHS auditing profession.



#### TIPS FOR AUDITORS CONSIDERING ENVIRONMENTAL / EHS FRAUD

1. **Internal Audit:** Recognize that fraud awareness, brainstorming & testing is still uncommon in EHS auditing. Promote fraud awareness, brainstorming, and testing.
2. **Environmental Auditors/ EHS Auditors:** Obtain, read, and become familiar with key IIA publications, including the IPPF, fraud practice guides and resources. Learn more about fraud from key industry publications. Develop and implement procedures for fraud brainstorming and testing. Know when to stop – and to escalate to others, if necessary.

<sup>1</sup> "Environmental" is used throughout, although EHS, HSE or other variations are applicable for fraud and auditing.

<sup>2</sup> See <https://www.theiia.org/centers/ehsac/Pages/about-the-center.aspx>



*Environmental auditing is a “second line of defense” function to mitigate against risks. Most environmental auditing programs arose to mitigate the risk of penalties from regulatory enforcement action. It is time to reconsider and reassess risk and modify environmental auditing programs accordingly.*

**3. Internal Audit and EHS Audit:** Invest in training and program development for environmental fraud. Consider using specialists – at least in the engagement planning stage. This is where you can derive great benefit at nominal cost.

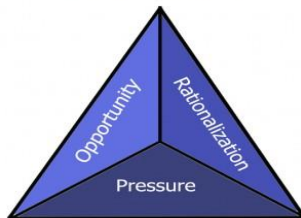
## FUNDAMENTALS

**Internal Audit** is regarded as the “third line of defense” (3LOD) in mitigation of risk. The IIA ([www.theiia.org](http://www.theiia.org)) is the world’s leading organization for Internal Auditors, with 180,000+ members. The IIA’s International Professional Practices Framework includes several sections that outline obligations with regard to fraud.



**Enterprise Risk Management** is widely used as a framework to consider risk – including the risk of fraud. Categories of risk include those that apply to environmental risk. These include operations contracted via supply chain, compliance with contractual requirements, and non-financial reporting (e.g., of environmental goals or performance).

**The Fraud Triangle**



**Fraud** involves any deceit to gain unlawful or unfair advantage, at the expense of another party(ies). Monetary gain is not the only type of advantage. The three factors noted in the Cressey Triangle – opportunity, rationalization, and pressure – are applicable to the world of EHS. Corruption is the most common type of fraud scheme. Fraud originates in many departments where environmental auditors perform procedures.

### Doug Hileman’s Experience with Fraud and Auditing

2002: supporting financial audits, after Sarbanes-Oxley (contingent environmental liabilities)  
2004: COSO Enterprise Risk Management, Internal Audit, on EHS audits  
2008: Sustainability reporting assessments  
2012 – 2016: IIA’s Guidance Development Committee (including Fraud Risk Assessment in Engagement Planning)  
2014: Independent Private Sector Audits (Dodd-Frank Conflict Minerals)  
2015: First IIA presentation on fraud in operations, compliance, EHS  
2017: “Environmental Fraud” publication in Bloomberg BNA

