

POLICY BRIEF

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Key Findings

- Albanian Internal Auditing Units are limited at detecting intra-institutional corruption;
- Malpractices and corruption go unobserved mainly because, in practice, IAUs are not independent;
- This situation causes much financial loss for Albania, which could otherwise be prevented if IAUs were more effective at detecting corruption and malpractices.

Key Issues

- There is an excessive control over the IAUs;
- The work of IAUs is focused at low risk investments, where the possibility of detecting corruption is also limited;
- No record of audit requests for high risk investments is kept and the reports are not transparent, therefore it is difficult to track many investments in the future;
- The Supreme State Audit Institution has limited capacity to audit in detail every institution therefore, much corruption can go undetected.

Recommendations

- Increase the independence of IAUs from political leadership;
- Improve transparency about IAUs' work;
- Establish an effective system of checks and balances between IAUs and institutional leadership: "independent but accountable".

About the Project

This policy brief was prepared as part of the TRAIN program (Think Tanks Providing Research and Advice through Interaction and Networking), funded by the German Federal Foreign Office and implemented by the German Council on Foreign Relations (DGAP), with the aim of fostering policy dialogue between think tanks and political actors in the Western Balkans

Fighting Corruption in Albania: Improving the Efficiency of Internal Auditing

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1. Executive Summary

Corruption is one of the biggest problems that Albania faces at present, hence the issue of institutional accountability is one of great importance. As the leading mechanism of internal control within public institutions, the Internal Audit can be very effective in detecting and preventing corruption 'at its roots', when employed correctly. Unfortunately, every year the Supreme State Audit Institution detects cases of financial damages between two and eight times higher than what is reported by the Internal Audit Units (IAUs) all combined. Even more worrying is the fact that these violations should have easily been detected by the IAUs of the respective institutions. Consequently, this conundrum raises doubts about the *efficiency* of the work of the IAUs.

This policy brief discusses the fundamental causes of this incongruence and concludes that the causes of this limited efficiency of the IAUs is primarily related to the lack of independence from institutional leadership resulting in limited capacities to provide effective 'checks and balances' and hold institutions accountable and transparent. It then argues for the establishment of an Independent Commissioner of the Internal Audit to best tackle these problems and uphold the principle of 'independent but accountable' IAUs.

2. Introduction

Corruption within state institutions directly impacts institutional integrity and lowers public trust. One of the mechanisms which states use to limit intra-institutional corruption are Internal Auditing Units (IAUs). The IAUs are monitoring and, risk assessment & mitigation bodies whose purpose is to help institutions increase the effectiveness and efficiency of risk management and governing processes within those institutions. In order to provide added value to their organization, internal auditing needs to remain independent

and objective. These principles allow for the IAUs to enhance institutional accountability, improve the system of checks and balances and ultimately contribute to reducing corruption within institutions.

This policy brief assesses the effectiveness of the IAUs in reducing corruption within Albanian public institutions. According to Albanian legislation, the purpose of IAUs is “to provide an independent and objective counseling to management, aimed at improving the activity of the given public unit [(institution)].”¹ Having efficient IAUs implies an improved ability to detect and provide countermeasures in tackling corruption. However, the high rate of corruption within Albanian institutions suggests that such risk assessment and accountability mechanisms might not be operating very efficiently.² In brief, the IAUs are not delivering on their expectations. Currently, the work of the IAUs sets the standard for a weak practice of “checks and balances”, unable to deter future corruption. This lack of effective monitoring contributes to increased corruption and causes irreparable damage to the management of public funds. On the other hand, the Supreme State Audit Institution (SSAI), which conducts external auditing, is limited in its ability to *exhaustively and timely* oversee all state institutions due to a lack of resources and capacity. This policy brief argues that expanding the freedom of action of the IAUs enhances the institutions’ ability to fight internal corruption and improves institutional efficiency.

The brief will proceed as follows. First, it will discuss the current situation regarding the ineffectiveness of IAUs and how it damages democratic governance. Second, it will highlight the indispensable role of the IAUs in fighting corruption. Next, it will present the current challenges the IAUs are facing, and finally, offer some concise policy recommendations and ways to implement them.

3. The importance of the IAUs as mechanisms for fighting corruption

The Internal Auditing Units (IAUs) in Albania have been operating for almost a decade and a half (since 2003); yet, they display consistent inefficiency in detecting irregular and/or corruptive practices. On the other hand, it is external oversight institutions, like the SSAI, that will usually identify corruptive practices on issues which could have easily been detected by the IAUs.

The SSAI and IAUs share certain similarities with regard to their processes and functions. Both institutions have similar guiding principles, and procedures in their line of work. Where they differ is in their focus and reporting channels. The IAUs can only audit their designated institution and report only to the head of the institution, whereas the SSAI is an independent body that conducts auditing at its discretion, reports to various institutions on its own accord and can audit any public institutions in Albania.

Although they share similar competences and authority, in recent years, not one of the *major* corruption cases uncovered by the SSAI were previously detected by the IAUs of the given institution. Some of the most well-known cases of the past two years are shown in Table 1:³

Table 1: Most prominent cases of corruption detected by the SSAI in the past two years				
	Date	Case # reported by SSAI	Description	Economic Damage
1	30 June 2017	Decision 72	Property Registration Unit, Korça – unlawful privatization of property	€426 thousand
2	30 June 2017	Decision 75	Psychiatric Hospital, Vlora – director manipulates the tendering contracts	€232 thousand
3	02 May 2017	Report 1330/11	Property Registration Unit, Lezha – unlawful	€140 thousand

¹ Law No. 114/2015, “On Internal Auditing of the Public Sector” (Article 2), *Parliament of the Republic of Albania*, https://shtetiweb.org/wp-content/uploads/2015/12/ligj_nr_114_dt_22_10_2015_24469_1.pdf.

² *Corruption Assessment Report: Albania, 2016*, http://seldi.net/fileadmin/public/PDF/Publications/CAR_Albania_2016/Raporti_i_Vleresimit_te_Korrupsionit_2016.pdf.

³ Reports by the SSAI, accessed through their online portal via http://www.klsh.org.al/web/Raporte_Auditimi_201_1.php

			registration of property	
4	30 April 2017	Decision 39	Municipality of Tepelena - violation of public procurement laws leading to financial loss	€560 thousand
5	29 April 2017	Decision 37	Municipality of Himara – officials prosecuted for violation of public procurement procedures	€571 thousand
6	30 April 2017	Decision 44	Municipality of Librazhd – Four officials prosecuted for corruption	€226 thousand
7	27 April 2017	Decision 32	Municipality of Saranda – violation of public procurement and tendering laws	€967 thousand
8	31 December 2016	Decision 184	State police – issues tenders at seven times higher than the normal price	€1.56 million
9	24 December 2016	Decision 157	Municipality of Lushnja – infringements in tendering procedures	€464 thousand
10	30 June 2016	Decision 88	Electoral Commission – director improperly uses state funds	€2.56 million

The decisions above are a sample of the various ‘high stakes’ cases dealing with corruption and malpractice where most infringements occur at top institutional level.⁴ As various international and national sources would attest, this is typically a result of high centralization within institutions, which have led to *limited oversight* and high ineffectiveness due to *political interference*.⁵

Institutional politicization is much more prevalent within the IAUs than in other independent oversight institutions.⁶ This is largely the result of the regulatory mechanisms in place, which give the IAUs very little freedom of action to audit *at their discretion* within the institutions that they exist. As former head of the Prison’s Directorate IAU confirms, all of the IAUs’ activity is approved by the head of the institution, and auditors cannot audit outside of the approved plan because doing so could result in incurring disciplinary actions, to include being discharged of their duties under the specific institution.⁷ This places the IAUs under undue duress to comply with the policy preferences of institutional leaders while giving little freedom of action to conduct independent work.⁸

Why the IAUs are being ineffective

The inability of the IAUs to detect and act upon malpractices and corruption cases depends on a series of legal and procedural conditions which cumulatively prevent the IAUs from being as effective as they could be within the context of Albanian public institutions.

First, there is a persistent culture of centralization within Albanian public institutions, which is also reflected on the work of the IAUs, at both the planning and the execution level.⁹ Second, there is a slight legal ambiguity when addressing the competences and authority of the IAUs in relation with the

⁴ See: (1) European Commission Country Report, Albania 2016, on high levels of corruption and the need to “tackle corruption at high levels”, accessed from https://ec.europa.eu/neighbourhood-enlargement/sites/near/files/pdf/key_documents/2016/20161109_report_albania.pdf; (2) *Corruption Assessment Report: Albania, 2016*, by SELDI and ACER, stating that “state institutions... remain significantly vulnerable to political pressure and influence”, pg. 24; (3) GAN Business Anti-Corruption Portal stating that corruption is a serious problem in Albania and anti-corruption mechanisms perform poorly due to political influence, accessed from <http://www.business-anti-corruption.com/country-profiles/albania>

⁵ Transparency International website link: https://www.transparency.org/news/pressrelease/albania_lacks_independent_oversight_institutions_leaving_the_door_open_to_corruption

⁶ Interview with key informant, former Advocate of the State, A.J., 2 June 2017

⁷ Law No. 114/2015, Article 12/ç. Also confirmed in an interview with former internal auditor at eh Prison’s Directorate.

⁸ Interview with former head of the Prison’s Directorate IAU, 4 September 2017

⁹ Interview with key informant, A.G.; current employee at the IAU sector at the SSAI; former IAU chief at the Directorate for the Harmonization of Internal Control at the Ministry of Finance

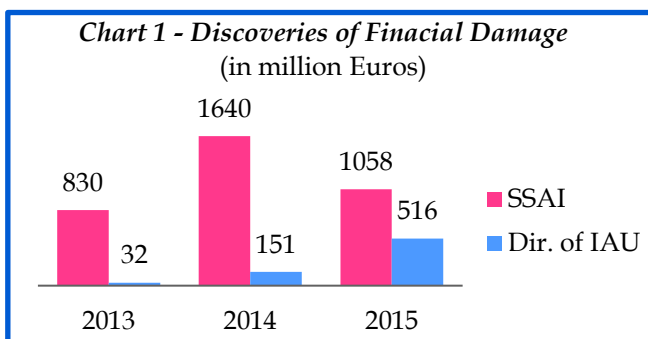
head of the institutions. For example Law 114/2015 states that IAUs are independent in their function to audit anything they deem of high risk while also stipulating that they can only do this after being approved by the institution's head.¹⁰ So, in practice, IAUs *only* audit cases which are pre-approved by their leaders. Such culture of centralization mixed with legal ambiguity leaves room for interpretations on the practical application of the law, and naturally, leaders are inclined to be risk averse and approve audits with low levels of risk.¹¹

The current institutional and legal set-up implies that if corruption occurs at high levels within a given public institution, there is little incentive for institutional leaders to approve such audits by the IAUs. At a minimum, this would damage their political capital; in the worst case, it would link them or possible affiliates to the corruption case. This makes institutional leaders more inclined to deny auditing that may expose them to potentially incriminating evidence (from possible corruption allegations to accusations of incompetence). Doing so, they also limit the freedom of action of the IAUs in providing effective assessment of institutional efficiency.

In brief, leadership which might be involved in corruption is often shielded from detection by the mechanisms that were, in fact, designed precisely to uncover corruption. This suggests that the IAUs are not very effective at detecting malpractices and bad performance within their institutions. Not surprisingly, this is seen when comparing the yearly reports of the SSAI and the Directorate for the Harmonization of the IAUs on the financial damages caused to the state budget.

Although it is the IAUs which should be more specialized in determining the economic damage to the state, almost all reports have shown them to be less effective, in comparison to the SSAI, in identifying cases of malpractices and economic loss (see chart 1).¹²

What has led to such a situation is a combination of the centralization of power, politicization and some lack of legal clarity. This has produced either in the limited ability of the IAUs to monitor the entirety of the institution or a misguided focus on the activity of the IAUs. In other words, leadership is



prone to only approve auditing which presents no risk of detecting corruption within their institutions. And because the work of the IAUs is consequentially shifted towards auditing the routine budgetary expenses, their reports inevitably indicate no major illegal activity or cases of corruption. This was also noted in Report No. 184 of the SSAI where they had discovered inefficiencies in the work of the IAU of the Police Force, resulting in a failure to detect various

malpractices in tendering procedures.¹³ The intended 'checks and balances' system is therefore hindered as it does not offer a comprehensive accountability process.¹⁴

4. Effective IAUs are essential, there is no realistic substitute for them

If the IAUs fail to rise to the responsibility of their office, unfortunately no other units will be able to shoulder the burden. This is mainly attributed to the large breadth (quantity) and depth (specificity) of

¹⁰ Law No. 114/2015, Article 10 and Article 12

¹¹ Interview with key informant, former internal auditor at the Ministry of Foreign Affairs, B.B.

¹² The reports have been taken from 2013-2015 because those are the latest on record. They include:

- 1) Yearly budget reports from the SSAI, accessed from http://www.klsh.org.al/web/Raporti_mbi_Buxhetin_e_Shtetit_82_1.php
- 2) Yearly reports on the work of the IAUs throughout the state institutions, Ministry of Finance, accessed from <http://www.financa.gov.al/al/ministria/drejtoria/drejtoria-e-pergijthshme-e-harmonizimit-te-kontrollit-te-brendshem-financiar-publik/raportet-vjetore>

¹³ SSAI, Decision 184, 31.12.2016, "Audit of Police Force" http://www.klsh.org.al/web/vendimi_policia_e_shtetit_3123.pdf

¹⁴ Former director at the Ministry of Defense for the Management of Defense Resources, P.K.

institutional operations which require a *specialized, systematic* and a *consistent* approach to their monitoring. **Hence, building effective IAUs can help detect corruption at its roots.**

As previously mentioned, many major cases of institutional corruption in Albania have remained undetected by the IAUs and have been detected by the SSAI. One may therefore assume that the SSAI can compensate for the inability of IAUs to detect high-level corruption, which might occur within public institutions, thus, reducing the need to reform the IAUs' mandate. This implies that the IAUs focus on ensuring the regularity of everyday institutional operations, while leaving the detection of high-level corruption to the SSAI. Although this scenario seems rational, in practice, however, such a division of tasks is not feasible due to limitations and constraints that the SSAI encounters.

First, the SSAI is forced to conduct selective auditing due to a lack of personnel and time to cover the needs of all institutions.¹⁵ Second, the SSAI monitoring is rather inconsistent and slow, which puts little pressure on institutions to be more transparent. Third, the SSAI often selects randomly the institutions they will audit, the types of auditing they will conduct and the specific institutional aspects that will undergo auditing; hence, there is little consistency on the type of issues that are audited by the SSAI. Fourth, the SSAI is an outsider to the institution, which implies that they are less aware of the institutional intricacies than the respective IAU, making them less precise in their judgment, particularly when it relates to performance auditing. Finally, due to the large volume of work, sometimes, the SSAI will monitor a given institution only for the specific year in which the auditing is taking place, thus missing the opportunity of detecting malpractices and corruption in the previous years and further limiting the ability of Albania's oversight institutions to ensure effective accountability.

All these factors lead to the conclusion that the SSAI, by itself, is limited in its ability to serve as an effective deterrent against corruption within Albanian public institutions and as a substitute mechanism for the IAUs, in detecting intra-institutional corruption.

5. In summary

IAUs in Albania enjoy a restricted independence in their line of work; thus, have a restrict ability to provide independent and uninfluenced oversight. This reduces institutional transparency and accountability while increasing the risk of corruption and damaging institutional integrity. Hence, the main reasons why the current functioning of the IAUs in Albania should be reviewed and improved to better fulfill their obligations are:

Problems:

1. *Extensive control over the IAUs – no independent oversight;*
2. *Institutions are centralized, political leadership influences the work of IAUs by shifting the focus to low risk cases;*
3. *Over time, IAUs have developed a culture of not questioning authority – thus allowing high corruption cases to go unchecked;*
4. *Ineffective system of intra-institutional 'checks and balances';*
5. *Lack of transparency on the work of IAUs.*

1. The *extensive control over the work of the IAUs leads to decreased accountability* within the institutions, especially in areas which involve high levels of political control. This also creates a situation where there is less transparency in particular institutional sectors. Less control over the work of our public institutions creates favorable conditions for potential malpractices and corruption.
2. The *inability of the IAUs to detect risky and corruptive practices erodes public trust in public institutions* and emphasizes the lack of institutional integrity. Experts agree that many of the challenges stem from an institutional culture of control and centralization. Although the law also

¹⁵ Institute for Democracy and Mediation *Financial Oversight and Integrity in Albania's Security Sector*, pg. 8-10, <http://idmalbania.org/wp-content/uploads/2017/05/Financial-Oversight-and-Integrity-English-ilovepdf-compressed.pdf>.

provides limitations on the activity of the IAUs, it is mostly a matter of interpretation. Hence, the IAUs are limited in their effectiveness due to their focus on ‘small’ aspects of institutional work.¹⁶

Fortunately, expanding the activity of the IAUs within public institutions in Albania is mostly a matter of good will and institutional culture rather than legal limitations – and this is a problem. It is worth noting that the Albanian law on IAUs does not restrict their activity to specific sectors of institutional work. Therefore, it is entirely possible that within the current legal framework, the breadth and depth of the work of IAUs can be expanded to a point where it serves as a democratic system of checks and balances while not being over controlling and policing to the institutional leadership.¹⁷

“IAUs should be independent but accountable”

6. Recommendations

The key challenge consists in striking a balance between allowing the IAUs to exercise their competencies in a way which serves the institutional leadership, while at the same time having enough flexibility and autonomy in monitoring the institution in order to dissuade any attempts at corruption. It is therefore imperative that the IAUs’ activity stretches throughout the entirety of the jurisdiction of the institution in which they work. Therefore, efficient auditing must ensure:

- Consistent monitoring of all public funds, all the time;
- Greater cooperation between oversight bodies; and
- More transparency about auditing reports.

As far as the IAUs are concerned, some practical measures for generating the outcomes mentioned above could be:

1) Create an effective system of checks and balances between the IAUs and institutional leaders.

a) First and foremost, allow IAUs more autonomy by abiding to the principle of **“independent but**

accountable”. This implies that the IAUs have unhindered authority to audit anything within their jurisdiction while still being responsible for fulfilling their obligations towards the head of the institution. This can be done by allowing the IAUs *to be appointed from a centralized structure outside of the jurisdiction of the executive but being accountable to their appointed institution in routine operations*. So, auditors are simply ‘attached units’ to the institutions they audit, but are administratively appointed and processed by a centralized unit which is independent of the influence of the political leadership. The best method of achieving this purpose is by **creating an independent institution (commissioner)**. This

might require small, but nonetheless feasible, modifications to

current structures (such as the General Directorate for the Harmonization of Internal Financial Control) and practices (law on internal auditing).

b) **Set up internal regulations and standard operating procedures (SOPs)** which delineate the limits of authority which the IAUs can exert, such as:

- i. *Establishing criteria for automatic auditing of tenders which go beyond a specific sum of money or involve a specific percentage of the institution’s budget*. This implies developing a more precise alerting system for IAUs to audit in those areas where risk might be the highest. Furthermore, the mechanism not only provides a greater scrutiny over public funds

Recommended Solutions

1. **Applying the principle of “Independent but accountable” IAUs;**
2. **Establish an independent commissioner of IAUs**
3. Establish a system of intra-institutional ‘checks and balances’;
4. Set up SOPs to regulate actions and commitments of IAUs and institutional leaders;
5. Improve capabilities of IAUs;
6. Make the process more transparent.

¹⁶ Former director at the Ministry of Defense for the Management of Defense Resources, P.K.

¹⁷ Department Head at the SSAI, A. H.

but it also protects the auditors from feeling under pressure while auditing cases which could place them in compromising positions with the leaders of the institutions. This procedure would both prevent institutional leadership from finding justification for not authorizing high risk auditing while protecting auditors from the potential blowback they might face in high risk cases involving corruption and their institution's leadership. Some of these standard procedures can also be cross-applied from the European Parliament's Directive 2014/56/EU on auditing.

- ii. *Allowing the IAUs to have free access for auditing anything within the jurisdiction of the institution while informing the head of the institution.* As an additional mechanism to limit the potentially abusive or irrelevant work of the IAUs, the institutional leader would still reserve the right to prevent an auditing from taking place. However, the reasons would have to be argued in writing. The difference between the current practice and this one is that at present it is impossible to know what specific auditing the IAUs have proposed and which ones have been rejected – because the institutions would only have records of what has been approved. The new practice would allow the IAUs to store records of refusals for an internal audit. This written record could be used as evidence in future auditing cases by external oversight bodies. Including such a practice is likely to dissuade institutional leadership from actively trying to 'bury' risky practices within their institutions.

2) Improve the capacities of the IAUs

- a) *Increase cooperation between the IAUs and the SSAI* in order to maximize the use and efficiency of human resources in delivering effective monitoring and oversight. This can be done through establishing mutual practices for auditing as well as maintaining a certain degree of communication about the types of auditing which have been performed. Furthermore, the SSAI could request the assistance of specific auditors within the institutions, to assist in the audit and to deliver a more effective performance auditing.
- b) *Increasing the resources and training for the IAUs.* This is particularly important as it would increase the competencies and readiness of the IAUs.
- c) *Raise awareness of institutional leaders on the role of the IAUs.* Such practice would enable institutional leaders to be more aware of the authority and responsibilities of the IAUs, their capabilities and how to harness them for fighting corruption within their institutions. Furthermore, it benefits the auditors of the IAUs by ensuring that they cooperate with informed decision-makers.

- 3) **Enhance transparency** by making IAUs' reports available for the public to view (with limitation when required). This builds public trust; it establishes a *culture of transparency* and *accountability* thus making it more difficult for political leaders to deviate from established norms.

- 4) **Modify the current law** to allow for greater exercise of autonomy of the internal auditing units as well as to reflect some of the proposed suggestions of this policy brief, particularly on issues relating to the command and control structure of the IAUs and how the "independent but accountable" principle should be implemented.

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