

FINANCIAL FRAUD AND CORRUPTION: A COMPARATIVE STUDY OF ZAMBIA AND IRELAND

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ABSTRACT: In this paper, two countries, one developing the other developed are compared, from the perspective of fraud and corruption. The levels of fraud and corruption are examined through league tables and cases of fraud. An explanatory framework is developed for the observed phenomena. The conclusion is reached, based on the evidence presented that over the past ten years, both Zambia and Ireland have become increasingly more corrupt and fraudulent.

Keywords: *Corruption, Fraud, Forensic Accounting*

INTRODUCTION

Financial fraud is now a worldwide phenomenon. Both in the developed and the developing world we are frequently confronted with incidences of fraud. These frauds involve considerable sums of money and adversely affect the economic functioning of companies and countries. Shareholders, management, employees, suppliers, tax authorities, other stakeholders and citizens suffer when fraud occurs. The main elements in the fight against fraud are good national and corporate governance and a strong code of professional ethics together with adequate protection for those who blow the whistle on illegal activity. This paper explores the phenomenon of financial fraud and corruption from a comparative perspective. Two countries are selected for consideration, one Ireland classed as a developed country and the second, Zambia a lesser developed country. Some instances of financial fraud in both countries are discussed and explanations are offered why financial fraud occurs. The role of the accountant in combating fraud is also explored and recommendations are made on how national accountancy bodies can support their members in the fight against financial fraud.

NATURE OF FRAUD AND CORRUPTION

While there is widespread discussion about fraud and corruption, the terms are rarely defined and explained. In this paper we consider two definitions of fraud. Michael Comer¹ in his book *Corporate Fraud* defines fraud as "any behaviour by which one person intends to gain a dishonest advantage over another". A more comprehensive definition is offered by Simmons² as follows:

- An individual or an organization intentionally makes an untrue representation about an important fact or event;
- The untrue representation is believed by the victim;
- The victim relies upon and acts upon the untrue representation; and
- The victim suffers loss of money and/or property as a result of relying upon and acting upon the untrue representation.

The major financial frauds include embezzlement, kiting, lapping, conflicts of interests, false claims, financial statement misrepresentation, credit card abuses, money laundering, counterfeiting and education frauds. There are many more that could be cited and they all involve an element of deception and the victim suffers financial loss. Corruption is sometimes used interchangeably with the term fraud but strictly it has its own specific meaning.

According to Holloway³ "corruption has

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broadly been defined as the abuse of public power for private gain. It involves a monopoly of resources and the abuse of discretion." Other writers make no distinction between the terms fraud and corruption. Some examples of acts of corruption include bribery, illegal gratuity, and extortion. But as pointed out by Transparency International⁴ in their report for the year 2000, there are two sides to corruption. On the one hand there is the receiver of the bribe and there is the giver of the bribe. One may receive because of need while the other may give because of greed. In the developing world corruption is to a large extent associated with the awarding of government contracts. We now go on to consider a number of cases of fraud as reported in the media or the subject of official enquiries.

RECENT FRAUD REPORTS

The recent UK government report into the collapse of the Maxwell Group of Companies, highlights once again, the role which auditors are expected to play in both combating and detecting fraud. You will recall that Robert Maxwell⁵ was both the Chairman and CEO of the Maxwell Group. In 1991 he fell off his yacht in the middle of the Atlantic Ocean and was drowned. Subsequent investigations revealed that he had been involved in massive frauds involving his companies. One of the most alarming activities was his raiding of the pensions fund to shore up his ailing enterprises. The question that was asked at the time was where were the auditors? Coopers & Lybrand were the auditors and were criticised for their handling of the audit. They were fined a considerable sum of money, by the joint disciplinary committee. It was also pointed out that in 1991 there was a government enquiry into how Maxwell was running his companies. That report stated *inter alia* that Maxwell was not a proper person to be in charge of a public company. He was forceful, domineering, dictatorial to the point of bullying. He was secretive. He was impulsive, opportunistic and a heavy gambler.

The report went on to catalogue a series of serious corporate offences committed by Maxwell. From the Maxwell case we can draw a few useful

conclusions. Firstly, when major fraud occurs there is sufficient evidence available to arouse suspicion and put auditors on their guard. In the Maxwell case there was evidence going back over twenty years. Secondly, there can be a tendency by auditors to put commercial interests before ethical and professional duties. Thirdly, internal audit as an organizational function needs to be strengthened.

In the case of Botswana Housing Corporation,⁶ the subject of a presidential enquiry the report stated that their internal audit function was very weak. This led to the senior management perpetrating serious fraud on the company. These frauds involved both top management and selected customers. In this country, there is some evidence from recent cases that the internal audit function needs to be strengthened. Both the Cadbury⁷ and King⁸ reports on good corporate governance have enunciated the principle that management is responsible for good governance. Good governance rests on proper checks and balances in the financial system and adequate disclosure. Fraud thrives where concealment is successful. Thus management should strive to achieve a high degree of transparency and openness in their operations. This means that the corporate culture should be formed to operate in a democratic and transparent way. But the corporate culture is a microcosm of national culture and there are varying views on what constitutes a crime in different parts of the globe. In some countries financial fraud is considered a necessary part of holding the political system in place and the only crime is in getting caught. Other countries see absolutely nothing wrong in paying a bribe to obtain a lucrative contract. It is considered part of the price one pays for doing business in that country. We even have the situation where a country will declare an activity illegal at home but perfectly acceptable abroad.

KEY FINDINGS ON FINANCIAL FRAUD

Ernst & Young⁹ have produced biennial reports for some time on corporate fraud. Some of the important findings from the 1998 report are outlined below. Their reports are based on large

scale global questionnaire surveys. Their findings on the nature of fraud are as follows:

These findings clearly point to the role of management in combating fraud. Of course this can prove elusive if top management are the ones perpetrating the fraud. Another key issue is that directors should have a very good understanding of the business. In the case of Botswana Housing Corporation, it was reported that the directors did not fully understand their role as directors. For example, some of them stated that they did not realize that they had to declare an interest in an agenda item and abstain from voting.

In the case of Barings Bank, Nick Leeson in his book, *Rogue Trader*¹⁰ states that his directors did not understand what he was doing in trading in derivatives. Thus he was able to demand more and more money from Head Office and at the same time conceal his huge losses. The survey also points out that more than 50% of respondents reported that they had suffered fraud with the previous year. This statistic should shake us out of our complacency. In the United States it has been estimated that about 80% of the population will engage in fraudulent activity given the right motive and opportunity.

PROFILE OF IRELAND AND ZAMBIA

The Republic of Ireland is a small country on the periphery of Western Europe. It got its independence from Britain in 1922 and has had a republican constitution and a democratic form of government since that time. It has a population

of about 3.5 million people and the majority of the population are Roman Catholic. Since joining the European Community its economy has grown significantly to the extent that today it is called the "Celtic Tiger." It has a relatively young, highly educated population with virtually 100% literacy levels, free secondary education and generous access to tertiary institutions. The life expectancy of its citizens according to the latest United Nations *Human Development Report*¹¹ is 76.6 years and it has a GDP of US\$ 21,482 per capita, making it among the richest countries in Europe. It is ranked 18 out of 174 countries worldwide and is firmly in the classification of developed countries.

Zambia is a large country in Southern Africa. It is over ten times the size of Ireland with a population of 10 million people. It gained independence in 1964 from Britain and in 1991 it became a multi-party democracy. Its main economic activities consist of farming and mining for copper and cobalt. It is classified as a developing economy and is considered one of the poorest countries in Africa. It is estimated that over 85% of the population live below the poverty line. The latest United Nations report ranks it 153 out of 174 countries. Its literacy level is 76% but only a small proportion of the population have access to secondary schooling. Its latest GDP figure is US\$719 per capita, ranking it with the poorest countries in the world. Its biggest challenge at present is how to cope with the AIDS pandemic which is wiping out a significant portion of the working population.

BOX 1: EXTENT AND NATURE OF FINANCIAL FRAUD

- MORE THAN 50% OF THE SURVEYED FIRMS HAD SUFFERED FRAUD WITHIN THE LAST YEAR
- 84% OF THE WORST FRAUDS WERE COMMITTED BY EMPLOYEES
- MOST OF THE WORST FRAUDS WERE COMMITTED BY MANAGEMENT
- ONLY 13% OF FRAUD LOSSES HAD BEEN RECOVERED
- THE BETTER DIRECTORS UNDERSTAND THE BUSINESS, THE LOWER THE INCIDENCE OF FRAUD SUFFERED

Source: Ernst & Young (1998) *Fraud: The Unmanaged Risk*

CORRUPTION COMPARISONS

There are no accurate statistics in lesser developed countries on the extent of fraud and corruption. Criminologists claim that a large proportion of financial frauds are never reported. This is due to tacit acceptance of corruption in government to companies being reluctant to report fraud because of the negative effects of such disclosure on their operations. In Zambia, the World Bank planned to have a survey undertaken in 1999 on the extent of fraud and corruption in the country. Parliament expressed alarm at this proposal and promptly had it stopped. In Ireland, we have witnessed large scale concealment of tax fraud and widespread corruption by government ministers including a Prime Minister. Concealment is the main device used by fraudsters to get away with their illegal activities. Remarkably, it can succeed for a considerable number of years. In Africa, one of the major factors leading to dictatorships is the need to keep acts of fraud and corruption concealed from the general public.

The principal source of information on corruption comes from the work of Transparency International.¹² It is important to point out that

what they produce is a perception index. Perception captures information on the opinion of a selected group of individuals on the level of corruption in a country. It does not provide hard facts on the number of frauds committed or even on the number and nature of fraudulent offences reported to the police.

Box 2 contains the data on corruption for selected countries in the developed and developing world. The data consists of world rankings and the actual perception scores for corruption. Countries are ranked on the basis of the perception score which varies from 10 signifying minimal corruption to 0 which would be widespread and expensive corruption.

Ireland is ranked 18 with a score of 7.5 for the year 2001. Box 2 shows clearly that Ireland has been declining in the rankings since 1997 when its rank was 12. It dipped to a low of 19 in the 2000 report. Finland has been ranked either 1 or 2 for the past five years. The scores for the United States and Britain have been reasonably stable. Clearly, Ireland has suffered due to the spate of disclosure and public tribunals on fraud and corruption witnessed over the last five years. It is ironic that the corrupt acts took place in the eighties and early nineties. It indicates that

BOX 2: The Corruption Index

YEAR COUNTRY	2001		2000		1999		1998		1997	
	R	S	R	S	R	S	R	S	R	S
DEVELOPED										
FINLAND	1	9.9	1	10.0	2	9.8	2	9.6	2	9.48
U. K.	13	8.3	10	8.7	13	8.6	8	8.7	14	8.22
USA	16	7.6	14	7.8	18	7.5	17	7.5	16	7.61
IRELAND	18	7.5	19	7.2	15	7.7	14	8.21	12	8.28
DEVELOPING										
RSA	38	4.8	34	5.0	34	5.0	32	5.20	33	4.95
MALAWI	61	3.2	43	4.1	45	4.1	45	4.1		
ZIMBABWE	65	2.9	65	3.0	45	4.1	43	4.2		
ZAMBIA	75	2.6	57	3.4	56	3.5	52	3.51		

R= Rank of Country S= Perception Score

RANGE 10-0
10= No corruption
0= Maximum corruption

Source: Transparency International www.transparency.org

disclosure and transparency are vital for a proper perception on the state of a country.

Zambia has a ranking of 75 and a perception score of 2.6 for the latest year under consideration. Four years ago its ranking was 52 and it had a perception score of 3.51. Here again there has been a considerable worsening of the perception of Zambia as a corrupt country. This is due to the large number of corruption scandals reported in the media and the reports from government tribunals together with the work of the anti-corruption commission. It appears that the ushering in of multi-party democracy in Zambia in 1991 has led to the widespread abuse of power by government ministers. In the next section, we offer some examples of fraud and corruption in both Zambia and Ireland.

FINANCIAL FRAUD AND CORRUPTION COMPARISONS

Obtaining reliable information on acts of fraud and corruption is extremely difficult as

previously alluded to. In this section data on selected acts of fraud and corruption are presented. The data in the case of Zambia was collected from the print media and in the case of Ireland, all the information was sourced from the recent publication by Kerrigan & Brennan¹³- *This Great Little Nation*.

These cases and many more investigated and reported in the last decade of the twentieth century have shattered the myth of Ireland as a relatively corrupt and fraud free country. The spate of scandals involving significant sums of money, indicate that increasing affluence in Ireland has encouraged widespread greed and dishonesty. Two significant trends are worthy of some comment. The first is the high level of corruption in public life by politicians and businessmen. A number of tribunals (including the Beef, Flood, Moriarty, and McCracken) have produced damning evidence indicating how senior politicians have allowed themselves to be

BOX 3: *Cases of Fraud and Corruption in Ireland*

ENTITY	NATURE OF THE FRAUD	AMOUNT
Ansbacker Bank	Tax Evasion by Bank for its rich depositors by Some of the wealthiest Irish used secret foreign Bank accounts to evade paying tax on interest	Bank US\$45M
Goodman	Tax evasion scheme involving export of beef Government tribunal requested to establish the facts. No one was jailed despite serious wrongdoing established.	Multi-Million
Guinness & Mahon Bank	Major involvement in Tax evasion. Over 35% of their total deposits constituted illegal deposits.	US\$38M
National Irish Bank	Involved in tax evasion. Also had for a number of Years secretly overcharged customers for its services.	Multi-million
Moriarty Tribunal	Established by the government to investigate allegations of illegal payments to politicians including one Prime Minister. This tribunal has unearthed evidence of widespread corruption in Irish public life.	Multi-Million

SOURCE: Kerrigan G. & P Brennan (1999) *This Great Little Nation*, Dublin, Gill & Macmillan

corrupted by successful businessmen. Secondly, One is struck by the frequency with which major Irish banks have featured in tax evasion cases. They include not only National Irish Bank and Guinness Mahon already cited but also the two largest and allegedly respectable Irish banks, Bank of Ireland Allied Irish Banks. In a later section, the possible reasons for this sorry state of affairs in Ireland will be explored.

In the case of Zambia, there is a considerable amount of opaqueness about the level of fraud and corruption. Similar to most African countries, power tends to be centralised in the Head of State and transparency is not a common characteristic of the *modus operandi*. One of the problems in Zambia is that it is ostensibly a multi-party democracy but in reality it more resembles a dictatorship. Accountability by the President and Government ministers is low and the area of political and economic discretion wide. Presidential power is wide and all encompassing and the Presidential fund is used by the President to increase power. In the latest year the Presidential fund amounted to US\$5million. This fund is available to the President to decide how it is to be spent and it is not subject to parliamentary approval. In addition, all tenders for significant government contracts have to be approved by the Office of the President. This arrangement provides scope for bribery and corruption.

Box 4 contains alleged cases of fraud and corruption in Zambia. All the information in the Table have been obtained from the *Post*¹⁴ newspaper using the internet. The *Post* is the only independent newspaper in the country. The other two national newspapers are owned by the Government. Four of the five cases concerns government operations and decisions of government. In Zambia the activities of government are quite pervasive and it is probably the most significant player in the economy. Government is a high purchaser of all types of supplies from oil to maize and is also the largest purchaser of services including the development of roads, airports and railways. Even though there has been some progress in the privatisation of state assets, there are a considerable number of parastatals controlled by government. It should be stated that government ministers tend to become actively involved in the decision making and management of parastatals.

The management of the parastatals tend to resemble civil servants whose job is to implement orders from the government. There is also a blurring of the boundaries between the legislative and administrative arms of government. Only recently, it was stated and accepted as fact at the Lewanika¹⁵ tribunal hearings in the case of the sum of money taken for party political purposes. In the case of Zambia, four of the five cases

BOX 4: Cases of Fraud and Corruption in Zambia

ENTITY	NATURE OF THE FRAUD	AMOUNT
Government	Oil contracted by State House for importation into Zambia, goes missing.	US\$18M
Government	Two Ministers accused of taking a large sum of State money to be used for party political Purposes	600,000
Government	Unaccounted for sales proceeds in a parastatal mining Company prior to privatisation	160M
Government	Unaccounted for expenditures in connection with the hosting of the AIDS conference in Lusaka	26,000
Barclays Bank	Lusaka businessman conspired with a bank clerk To defraud the bank	486,000

Source: *The Post Newspaper*, April-May 2001 www.zamnet.zm/post

selected concern the government. In all four cases the government is accused of involvement in the misuse of funds or even more seriously, embezzlement. Only one of these cases has been fully investigated through a government tribunal. The judgment of the tribunal in the case of the misuse of state funds for party political purposes, was that two ministers were guilty of gross abuse of office and should be asked to resign. The other three cases are at varying stages of investigation, even though some of the events took place over two years ago. Some commentators do not hold out much hope of any significant remedial action being taken by government in any of the cases involving government ministers and the State House. The fifth case involves one of the major international banking groups in the country. This type of fraud is quite common and illustrates the fact that banks provide one of the best opportunities for financial fraud. In the next section we draw the significant data together and offer an explanation for the prevalence of financial fraud and corruption in both countries.

ANALYSIS AND EXPLANATION

Notwithstanding the fact that Ireland and Zambia are significantly different in terms of geographical location, language, ethnicity, economic and social development, there are a number of similarities with regard to fraud and corruption.

1. *Both countries have a high tolerance for financial fraud.* Rarely does one find a person receiving a jail sentence for fraudulent crimes. In Ireland tax evasion is in some quarters looked upon as a "clever thing" to do. It would appear that in the last decade when fraud was rampant in Ireland, that the tax authorities adopted a binary system of tax collection. They hounded the small taxpayer for the last penny while adopting a "kid glove" approach to wealthy taxpayers, especially those with political clout.

In Zambia, where the fraud tends to be concentrated on stealing state funds, it is looked upon as part of the reward of public office. In a perverse sense, fraud and corruption are seen by many as the necessary price to pay for a

government. As a result the citizen is quite philosophical about this activity believing that even if the government changes with an election, the fraud and corruption will continue.

2. *Fraud in both countries is based on greed.* There is no evidence to suggest that fraud and corruption is committed out of need. On the contrary, the large frauds are invariably committed by people who have significant amounts of wealth. Perpetrators have relied on the notion that they are unlikely to be detected or if they are unlucky enough to get caught, they will rarely be given a prison sentence.

3. *Both countries are former British colonies.* It is fashionable to blame colonialism on all the ills of a country. But it would appear that colonialism has infused into national culture a certain disrespect for the rule of law. This is particularly strong when it comes to state funds. In the colonial days, these funds were seen as belonging to an oppressor. There may still be a residue of this sentiment left although one hopes in time that it will be rejected.

4. *Government as Chieftdom.* Ostensibly, both countries are Republics with multi-party democracy. The reality is sometimes different. As stated previously, Zambia is in reality a dictatorship as the opposition is small, weak and ineffective. Power is concentrated in the President and he acts more in the style of a village chief. He dispenses privileges and positions to his faithful followers similar to a feudal King.

In Ireland, during Prime Minister Charles Haughey, his leadership style resembled that of an African Chief. He developed and promoted a culture of financial dishonesty and fraud based on naked greed. This culture was imbibed not only by politicians but also by successful businessmen. His *modus operandi* was not dissimilar to Robert Maxwell in the Maxwell case above. Kerrigan & Brennan (1999:144) put it well:

Although describing itself as the "We publican Party", Fianna Fail displayed towards Haughey the kind of deference and timidity more usually associated with royalty.

5. *Christian Countries.* Both countries are considered highly Christian. Ireland's population

is about 99% Christian and Zambia has even gone so far as to declare the country a Christian nation. Ethical philosophers can be forgiven for being puzzled by the fact that two highly Christian countries can have such a poor record in relation to financial fraud and corruption. It would appear that religion plays no part in informing them when it comes to fraud. In the scheme of things these types of offences are not considered to have major ethical implications. On the other hand, Christianity can be used as a smoke screen to hide these illegal activities.

COMBATING FRAUD AND CORRUPTION

When we come to make proposals for combating fraud and corruption we must realise that it is not feasible to eliminate it completely. Similar to other types of crime, the aim should be to reduce it to manageable levels. We offer a five step approach in the strategy to reduce fraud and corruption.

Education

Forensic accounting should be part of the core curriculum of business studies degrees and diplomas. It should also become an important component in the professional accountancy syllabus. In addition, there should be a vigorous and sustained media campaign on the inherent evils of fraud and corruption and the dangers they pose to the social fabric and economic prosperity of a country. Where there is a statutory body responsible for anti-corruption activities, it should be well funded, autonomous and free from political interference.

Prevention

Organizations can make a considerable contribution in this area through good corporate governance systems. Proper and comprehensive financial disclosure together with effective internal controls as recommended by the Cadbury Report are essential. Accountants need to be aware of the possibility of fraud occurring and have a proactive internal audit system in operation. Accountants should always adhere to a comprehensive code of ethics. It is ironic, that

in Ireland, in the past two decades, the major frauds and acts of corruption have invariably involved accountants. The professional accountancy bodies should develop an effective system for protecting whistleblowers. Without suitable protection accountants and others are reluctant to take appropriate action when they discover wrongdoing. Good systems of internal controls and professional ethics are likely to deter some would-be fraudsters and bribers.

Detection

Fraud detection is a complex and difficult area. It is not easy to detect fraud as those involved are at pains to conceal their activities. One way of increasing the likelihood of detection is for organizations to have a policy of rotation for its public auditors. A new auditing firm is unlikely to be the victim of the "tyranny of familiarity" which is a phenomenon which is known to affect those professionals who develop a cosy relationship with the client.

One of the great myths of the modern business world is that of the effective internal auditor. We have seen sufficiently often to conclude that internal audit is probably fine for the compliant organization, but it is next to useless for those firms who are determined to act illegally. Honest and professional advice provided by internal auditors in these situations is invariably ignored. It would be a good development if Public Companies and large government institutions were required say every four years to have a comprehensive and systematic financial and management audit undertaken by independent auditors who have had no prior contractual relationship with the organization. The audit report based on this comprehensive study should be made available to all the major stakeholders including shareholders, employees, bankers, tax authorities and the relevant monitoring bodies.

Prosecution

It is suspected that only a small proportion of fraudulent activities are ever detected. Due to lack of sufficient evidence and political interference an even smaller number of those detected are

successfully prosecuted. It is difficult to see how this situation can be improved until national cultures are changed and there is the same tolerance for fraud as there is now for murder. But while citizens are ambiguous about fraud and corruption, we cannot expect much improvement in the prosecution of this type of offence. It is worth noting that one of the important aspects of prosecution for fraud is that it is extremely expensive for the prosecuting authorities. There is usually a considerable amount of time and travel involved in collecting the evidence which might be spread over a number of countries.

Conviction

Where fraud and corruption cases are successfully prosecuted the sentence should be appropriate to the seriousness of the offence. But we have seen in Britain where the serious fraud office devote enormous resources to bring a prosecution and find that the sentence handed down is equivalent to that for a misdemeanor. Until the courts start giving custodial sentences on a regular basis, fraud offenders will reckon that their chances of serving a prison sentence are fairly slim.

CONCLUSION

Fraud and corruption are a cancer eating away at the soul of a nation. Not only do they attack the social fabric of a country but they also have the potential to hinder economic progress. Foreign direct investment desires an economic environment with minimal fraud and corruption. We have seen in this paper how two countries, one developed and the other developing have slipped into the mire of fraud and corruption. While accountants and other professionals can contribute to an honest society, it is vital that the political leaders are imbued with the sense of public service and integrity we expect from our elected representatives. Transparency and good government are the keys to a corruption free society. When cases of fraud and corruption are discovered the law should be allowed to take its course. Those found guilty should be given the appropriate sentence including custodial

sentences. Finally, it is only when the majority of the citizens decide that they will not tolerate fraud and corruption that we can expect a reasonably fraud and corrupt free society.

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