Counter Fraud and Corruption

Audit Committee

5th November 2007

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Fraud and Corruption

- Definition

- Who Commits Fraud

- Responsibility for Managing Fraud

- Management Controls

- Role of Internal Audit

- Managing the Risk of Fraud

Definitions

- ## FRAUD

  "the intentional distortion of financial statements or other records by persons internal or external to the organisation which is carried out to conceal the misappropriation of assets or otherwise for gain."

- ## CORRUPTION

  "the offering, giving, soliciting or acceptance of an inducement or reward which may influence the action of any person"

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Impact of Fraud

- Financial loss
- Damaged reputation
- Loss of public trust
- Disruption to service
- Loss of morale/motivation
- Loss of confidence in management
- Investigation costs
- Diversion of management time

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Who commits Fraud?

- Employees
- Competitors
- Suppliers
- Professional criminals
- Business partners
- Customers

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Who Commits Fraud?

KPMG review of 100 frauds revealed:

- Directors and senior managers commit almost 2/3 of all frauds
- 50% discovered by whistle blowing
- 51% had two to five conspirators
- 70% of fraudsters employed for over 2 years
- 42% work in Finance

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Common examples of public sector fraud

- Corruption
- Contractors/suppliers invoicing for goods/services not ordered or provided
- Misdirection/misuse of funds
- Falsifying information on job applications
- Staff working elsewhere when on sick leave
- Falsification of timesheets/mileage claims
- Benefit Fraud

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Conditions for Fraud to exist

- Lack of effective internal controls
- Failure of management information systems
- Undocumented procedures
- General laxity by management/employees
- Fraud Triangle
  - Opportunity
  - Motivation
  - Rationalisation

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Fraud Triangle – what drives fraud?

Opportunity

Motivation

Rationalisation

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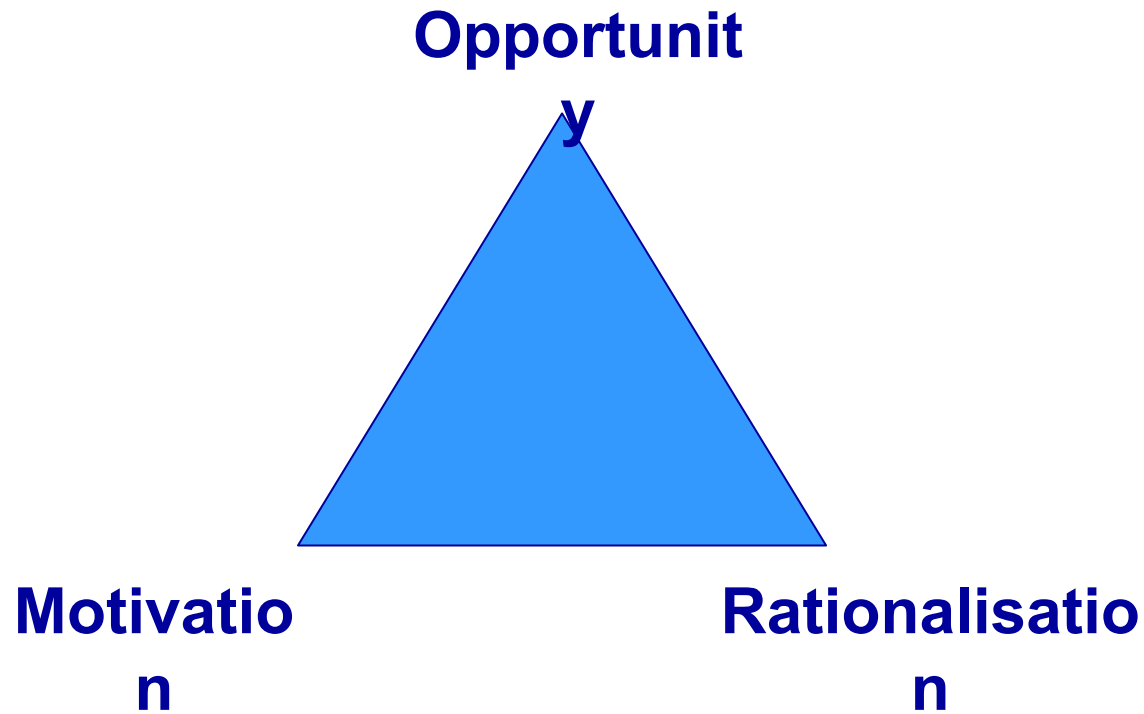
Fraud Triangle - Motivation

- Revenge
- Debts
- Addiction – drink, drugs
- Coercion or blackmail
- Results at any costs
- Family pressures
- Illness
- "I need the money"

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Fraud Triangle - Opportunity

- Poor controls
- Exploiting errors
- Lack of segregation of duties
- Poor corporate governance
- Hidden in complex transactions
- Abuse of authority
- Lack of effective oversight

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Fraud Triangle - Rationalisation

- "they do not pay me enough!"
- "Everyone else does it"
- "Rules are made to be broken"
- "It's only a small amount"
- "It's a victimless crime"
- "They can afford it"
- "I'll never get caught"

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Relevant Legislation

- Fraud Act 2006

- Theft Acts 1968 and 1978

- Public Interest Disclosure Act 1998

- Data Protection Act 1998

- Police and Criminal Evidence Act 1984

- Regulation of Investigative Powers Act 2000

- Human Rights Act 1998

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Responsibility for Fraud

Auditing Practices Board's *Guidance for Internal Auditors* states:

"It is a management responsibility to maintain the internal control system and to ensure that the organisation's resources are properly applied in the manner and on the activities intended. This includes responsibility for the prevention and detection of fraud and other illegal acts."

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Key Management Controls

- Financial Regulations

- Contract Procedure Rules

- Code of Conduct – members/officers

- Whistleblowing Policy

- Counter Fraud and Corruption Strategy

- Register of Interests/Gifts/Hospitality

- Local Code of Corporate Governance

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Management Controls

Segregation of duties

Organisaton

Authorisation

Personnel

Supervisory

Physical

Access

Management

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Role of Internal Audit

- Planned work undertaken following risk based assessment including:
  - Budgetary control
  - Value of system
  - Satisfaction with system controls
  - Historic problems
  - Changes in service
  - Public sensitivity

- Proactive fraud work including NFI

- Co-ordination of counter fraud strategy

- Receiving and investigating allegations of fraud

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Managing the Risk of Fraud

- CIPFA issued *'Managing the Risk of Fraud'* in 2006

- Describes what action is needed for an organisation to be effective in countering fraud and corruption

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Managing the Risk of Fraud

1. **Strategic approach**
2. **Identifying risks**
   – Measuring fraud and corruption losses
3. **Strong anti-fraud and corruption culture**
   – Authority
   – Training
   – Propriety checks
   – Relationships with other organisations
4. **Taking action to tackle problem**
   – Culture
   – Deterrence
   – Prevention
   – Detection
   – Investigation
   – Sanctions
   – Redress
5. **Defining Success**

Managing the Risk of Fraud

- The creation of an **ANTI-FRAUD** culture.

- Maximum **DETERRENCE** of fraud.

- Successful **PREVENTION** of fraud which cannot be deterred.

- Prompt **DETECTION** of fraud which cannot be prevented.

- Professional **INVESTIGATION** of detected fraud.

- The application of effective **SANCTIONS**,including appropriate legal action against people committing fraud.

- Effective methods for seeking **REDRESS** in respect of monies defrauded.

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Way Forward

- Self assessment against CIPFA Guidance completed

- Generally perform well against the guidance

- 56 questions in total over the 5 sections

- 8 action points identified

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Way Forward

1.1 Existing anti-fraud and corruption policy and fraud response plan needs updating

1.2 Include remit to reduce losses

1.3 Link strategy to operational work

2.2 Clarification of nature and scale of losses to fraud and corruption

3.1 Link service based strategies to corporate fraud and corruption strategy

3.8 Propriety checking under review and to be completed shortly

4.5 Assessing extent of anti fraud culture

4.29 Clear policy on redress of losses

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Use of Resources Assessment – Level 4 Criteria

- The council can demonstrate that its members and staff exhibit high standards of personal conduct.

- The council can demonstrate a strong counter fraud culture across all departments. Staff have clearly acknowledged and accepted their responsibility to prevent and detect fraud and corruption.

- The risk of fraud and corruption is specifically considered in the council's overall risk management process.

- The use of publicity in successful cases of proven fraud/corruption is routinely considered to raise awareness.

- The council has a track record for effective action in response to whistleblowing disclosures. There are periodic reviews of the effectiveness of the whistleblowing arrangements, and there are effective arrangements for receiving and acting upon disclosures from members of the public.

- The council can demonstrate that effective action has been taken to maximise the potential savings available through NFI.

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