Internal Audit Report 2019/20

Corporate Fraud Risk Assessment

January 2020

Contents

Distribution List	
For action	Kate Mulhearn, Corporate Governance Manager
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For information	Audit Committee

1. Executive summary

OVERALL RISK RATING SUMMARY

Fraud Risk Category	RESIDUAL FRAUD RATING			PRIORITY		
	Low	Medium	High	Urgent	Important	Routine
1.0 PROCUREMENT	4	0	0	0	0	4
2.0 HR & Payroll	5	0	0	0	0	4
3.0 FINANCE	6	0	0	0	0	6
4.0 COUNCILLORS' INTERESTS & EXPENSES	2	0	0	0	0	2
5.0 CORPORATE COUNTER FRAUD	0	0	0	0	2	0
				0	2	16

Refer to Appendix 1 for definitions.

Summary of findings

The Fraud Risk Assessment did not identify any 'urgent' priority risks. Overall the results of our assessment indicate that there is an established control environment designed to mitigate the risk of fraud occurring. Those officers that we met had good awareness of the fraud risks and internal controls in their area.

Two 'important' priorities have been identified. These relate to training and guidance being provided to relevant staff, and the inherent risk of fraud occurring prior to the transition to the new unitary Buckinghamshire Council in April 2020. One action has been raised to address this risk. With a number of officers, particularly at a senior level, vacating posts, and not being replaced, this may have an impact on the control environment and the ability to ensure sufficient coverage of authorisation and an adequate segregation of duties. In the lead up to vesting day, some this risk will be mitigated through increased oversight from the new Buckinghamshire Council Corporate Management Team.

There were also 16 'routine' priority risks identified, which relate to inherent risks. No actions have been raised to address these risks as, provided controls continue to operate effectively, these risks should be effectively managed.

Good practice noted

A number of areas of good practice were noted which help mitigate fraud risks, provided the internal control environment is maintained to an adequate level and is reviewed accordingly in line with staffing changes, as set out below:

PROCUREMENT & CONTRACT MANAGEMENT
- Procurement hierarchies are electronically built into the procurement purchase order process through the Scheme of Delegation.
- Due to approaching Unitary Authority status, no new contracts are being entered into, existing contracts are having contract extension clauses activated if required or winding down to Unitary Authority status.

HR & PAYROLL
- Finance monitor actual salaries against budgeted establishment and highlight any unplanned overspends.

FINANCE
- The Corporate Finance team has implemented a verification process to assure itself that changes to the Creditors standing data record are genuine and evidence to support this process is maintained through the running of twice weekly change reports.
- The Transaction Team operated strong controls when inputting supplier invoices into the system to be matched to a purchase order and ensure that all the appropriate checks have been undertaken before setting up new creditors on the system.
- Forecasting and budgetary control allow income actuals to be monitored against budget and forecasts.

COUNCILLORS' INTERESTS & EXPENSES
- Democratic Services has established processes in place to identify and investigate potential conflicts of interest and use "intelligence" through a variety of sources to highlight any unreported potential conflicts.

CORPORATE COUNTER FRAUD
- AVDC has an online whistleblowing form and process to ensure that any disclosures made are logged and followed up.

2. Background and Scope

Background

According to the Annual Fraud Indicator 2017, which provides the last set of government sanctioned estimates, public sector fraud accounts for 21.2% of all UK fraud, with an estimated cost of £40.4bn and of this total, £7.81bn is specifically in local government.

Fraud is one of the fastest growing areas of crime in modern society and the residents and stakeholders of Aylesbury Vale have a right to expect that their public funds are secure and handled honestly. They also have a right to expect that their elected Members and Council employees are honest and that their integrity is above reproach. Any dishonest act reflects badly on both the Authority and the wider public sector.

Aylesbury Vale District Council is due to become a unitary authority in 2020 along with the four other councils in Buckinghamshire. In light of this, a Fraud Risk Assessment is being undertaken to help prioritise the Council's approach to address fraud, corruption and bribery risks, and to assess the suitability of the arrangements in place to help mitigate these risks prior to the transition.

The purpose of conducting a Fraud Risk Assessment is to identify areas of risk in key departments and develop strategies to mitigate these risks.

This is an advisory project and therefore has not resulted in an assurance opinion.

Scope & Methodology

Scope
The review covered the following corporate fraud risk areas:
- Procurement
- HR and payroll
- Finance
- Councillors' Interests and Expenses
- Corporate Counter Fraud

Fraud affecting the Revenues and Benefits service was not included in the scope of this review. Controls to prevent the risk of fraud in the areas of council tax, business rates and housing benefit are assessed in separate internal audit reviews.

Methodology
The control environment was established through a series of meetings with key officers for the risk areas reviewed. The residual fraud risk was then assessed using the likelihood of fraud occurring, based on the current control environment, and the impact that this fraud occurring would have on AVDC, to generate a fraud risk score for each area.

The results of these assessments were plotted on a residual risk heat map to provide a diagrammatical view to highlight the urgency of actions. Additionally, the urgency was mapped onto a pie chart to provide a visual reference and enable AVDC to focus their efforts on those areas posing the highest fraud risk.

3. Findings and action plan

1. Overview

No high risk fraud areas have been identified following this exercise.

Our discussions with key officers around controls highlighted that in the majority of areas AVDC is effectively mitigating its fraud risk in the lead up to unitary authority status, providing established controls surrounding segregation of duties, authorisation, financial and budgetary controls continue to operate effectively. However two 'important' risks have been raised as follows:

- As AVDC moves closer to the unitary authority status, with a number of senior officers (including Senior Managers and Assistant Directors) having vacated their roles and not being replaced, there is the risk that the remaining structure does not allow for sufficient segregation of duties or enable adequate authorisation processes to remain in place. We are aware that staff below a senior officer level will transfer to the new Unitary Authority under the Transfer of Undertakings (Protection of Employment) (TUPE) regulations. Therefore there is potential for less fraud related or control risk occurring due to continuity of employment, however it does not mitigate the risk completely. One action point has been raised to address this issue.

- Discussions with the Corporate Governance Manager indicated that there has been a gap in fraud awareness training being provided to staff in recent years; the last Fraud Awareness training was provided for all managers in summer 2017. Whilst it is acknowledged this is an area to be addressed, no action has been raised in this report for AVDC due to the imminent Unitary Authority status. There will be a requirement for the new Authority to identify the staff that should undertake this training and develop a training plan to ensure staff have adequate knowledge relating to how to identify and respond to fraud risks.

'Routine' risk areas have also been identified relating to inherent risks. In any organisation, including ones that are going through significant change, a risk of collusion will always remain where internal controls are bypassed by two or more employees. This is often enhanced due to structural changes creating resourcing gaps, meaning there may no longer be a segregation of duties, and providing an opportunity for existing controls to be bypassed. This risk is more likely to materialise during a period of change due to 'disgruntled employees' who may be provided with a motivation to commit fraud, as well as the opportunity presented by these gaps in the control framework. The controls currently in place at AVDC, including independent checks on changes to standing data, such as the creditors system, and timely and effective budgetary control will continue to remain as compensating controls in these instances providing there is sufficient independence in these areas.

In the lead up to the transition to the unitary the Shadow Executive, the newly appointed Buckinghamshire Council Chief Executive, Corporate Directors and Senior Managers, including Section 151 Officer, will have increasing oversight of the transitioning authorities as well as developments for the new unitary authority. We would expect that this Corporate Management Team will become increasingly core to some of the higher risk/value decisions and within AVDC which will help to maintain segregation and a sound control environment.

As the new Authority takes on the routine processing of transactions, it is vital to ensure a robust control environment is established as it will take time for departmental structures to settle, processes to develop and officers and teams to effectively know their roles within the new organisation. The new Authority should establish, at an early opportunity, staff groups and departments which would benefit from fraud

awareness training to ensure controls are managed effectively and assist in identifying possible indicators of fraud.

2. Residual Risk Heat Map

The 'Residual Risk Heat Map' below shows the calculated residual risk of the areas reviewed (see Appendix 1 for details of the definitions used). Residual risk was assessed through discussions with key officers to determine the likelihood of fraud occurring based on the current control environment and the potential impact this would have on AVDC, either in terms of disruption to service delivery, financial impact or reputational damage.

impact		1	2	3	4	5
Likelihood		None	Minor	Moderate	Major	Catostrophic
1	Rare	2.1 2.2	1.1 1.2 1.3 1.4 ROUTINE			
2	Unlikely	3.3 3.5 3.6	2.3 2.4 2.5 3.1 3.2 3.4			
3	Possible		4.1 4.2	5.1 5.2 IMPORTANT		
4	Likely					URGENT
5	Almost certain					

Key to colour coding and processes reviewed

1.0 PROCUREMENT	
1.1	Bribery & Kickbacks
1.2	Conflicts of Interest
1.3	Contract Splitting
1.4	Adherence to the Scheme of Delegated Authority
2.0 HR & Payroll	
2.1	False Identity and Immigration Status
2.2	Failure to undertake pre-employment checks
2.3	False expenses
2.4	Ghost employees
2.5	New starters added incorrectly
3.0 FINANCE	
3.1	Bank Mandate Fraud
3.2	Post Contract Supplier Fraud: False Invoices / Inflated Invoices / Duplicate Invoices / Invoices for Work not Carried Out
3.3	Insider Enabled Fraud/Fictitious suppliers / shell companies, payments to employees accounts
3.4	Forged signatures on payment authorisations/failure to comply with SFI sign off limits
3.5	Unrecorded sales or receivables
3.6	Improper use of company credit cards / payment cards
4.0 COUNCILLORS' INTERESTS & EXPENSES	
4.1	Undeclared interests or a lack of monitoring of declared interests unknowingly influence decision making for personal gain
4.2	Expenses are paid which are not in line with the relevant expenses procedure
5.0 CORPORATE COUNTER FRAUD	
5.1	There is a lack of training and guidance in place for staff to follow to assist in the prevention, identification and reporting of fraud
5.2	Inherent risk prior to unitary status in April 2020

3. Residual Risk Pie Chart

The pie chart below shows each of the areas reviewed and their calculated residual risk rating.

The two 'important' priority risk areas relate to the residual risk of fraud occurring in the lead up to Unitary Authority status if the control environment significantly changes due to loss of key staff at an operational and senior officer level, or through the bypassing of controls. Additionally, as staff transition to the new Authority, it will take some time for roles to become established and team structures to settle down. This can give a higher risk to fraud occurring whilst the control environment is being established.

An inherent risk for potential fraud occurring or break down in the internal control environment remains due to the loss of senior officers resulting in a weakened authorisation structure. If vacant posts are not replaced, and responsibilities are increasingly reallocated, there is a risk that the capacity of existing staff to fulfil their responsibilities for internal control becomes too wide and the controls can become ineffective if they are not performed to the required standard. In any large scale reorganisation there is always an inherent risk of collusion and bypassing of internal controls.

Residual Risk
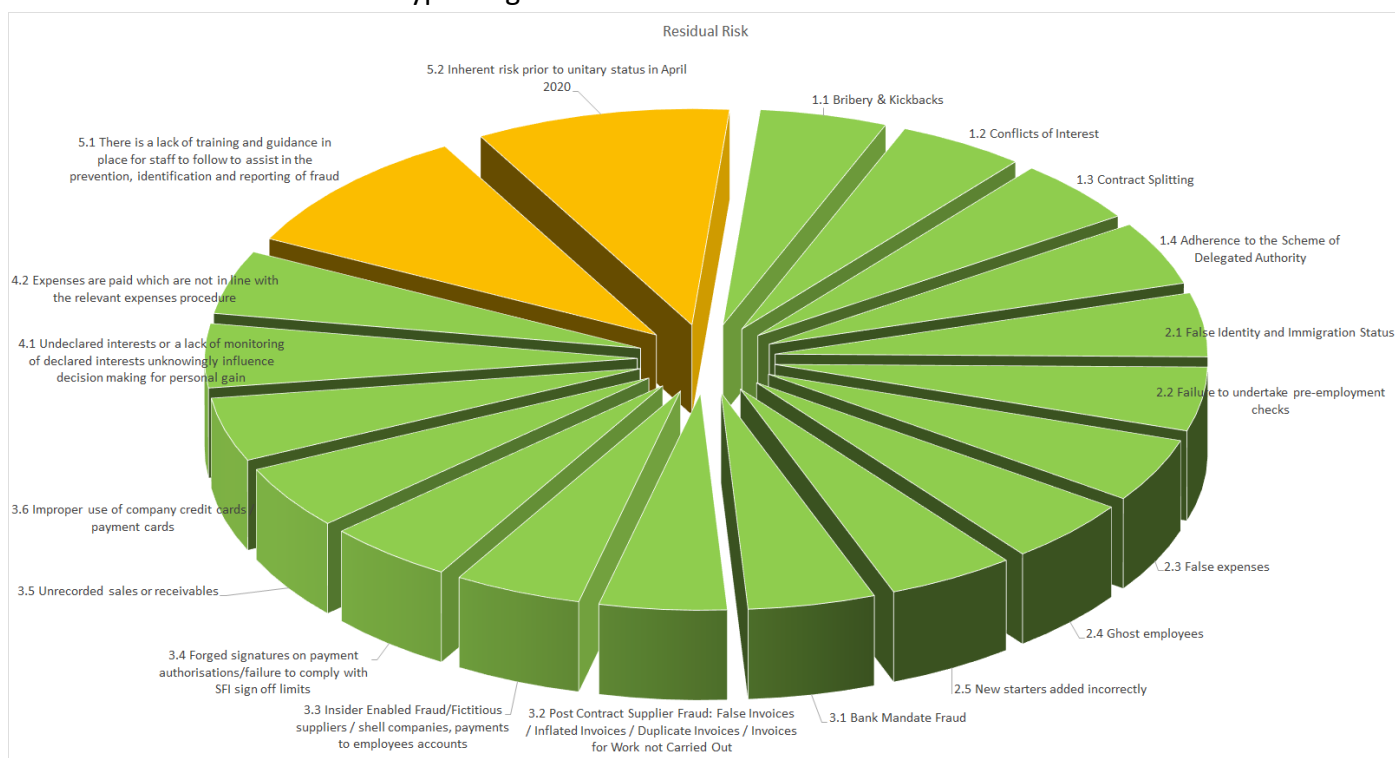
4. Action Plan

Action Plan	Responsible person / title	Target date
CORPORATE COUNTER FRAUD To address the inherent risk present during a period of change, including the loss of key members of staff, AVDC should ensure a review is undertaken as they become aware of any structural or staffing changes. This should identify any authorisation or review responsibilities under this staff member in order to reassign these in a timely manner to maintain a segregation of duties and adequate oversight of key processes.	*Andrew Small, Section 151 Officer* *Kate Mulhearn, Corporate Governance Manager*	*Ongoing in the lead up to 31 March 2020.*

Appendix 1.   Definitions used

Likelihood

Level	Likelihood of the fraud occurring
5	Certain – will occur frequently, given existing controls
4	Likely – will probably occur, given existing controls
3	Possible – could occur, given existing controls
2	Unlikely – not expected to occur, given existing controls
1	Rare – not expected to occur, except for exceptional circumstances, given existing controls

Impact

Level	Grade	Impact on Service/Department (not an exhaustive list)	Impact on Service/Organisation/Reputation
1	None	Very minor fraud easily identifiable, good prevention, controls already in place	No service disruption Low financial value (<£100)
2	Minor	No harm to service disruption. Fraud identifies poor management practices. Good controls and systems identify fraud early	Litigation / financial loss of £100-£1,000 Reputation of service not jeopardised
3	Moderate	Fraud does get reported but not immediately. Fraud demonstrates key weaknesses in controls and / or management. If allowed to continue, fraud loss may have increased significantly	Litigation / financial loss of £1,000 - £20,000 Failure / disruption of support services. Moderate business interruption. Adverse local publicity
4	Major	Fraudulent behaviour goes unreported and / or unchallenged. Existing policies, procedures and protocols undermine likelihood of detection and / or successful prosecution	Litigation of £20,000 - £500,000 Adverse national publicity. Temporary service disruption. Underperformance against key targets. Reportable to External Agencies / Regulatory Bodies.
5	Catastrophic	Fraud results in severe harm to the service's reputation. Financial repercussions severely affect service provided.	Litigation / financial loss > £500,000 International adverse publicity. Severe loss of reputation. Significant overspend.

The matrix below is used to calculate the risk assessment rating for each area. A traffic light system indicates the level of risk identified, to which is attached a priority for mitigating action, where appropriate.

Risk (Impact x Likelihood)

Likelihood	Impact				
	1 – None	2 – Minor	3 – Moderate	4 – Major	5 - Catastrophic
1 - Rare	Low	Low	Medium	Medium	High
2 - Unlikely	Low	Low	Medium	Medium	High
3 - Possible	Low	Low	Medium	High	High
4 - Likely	Medium	Medium	Medium	High	High
5 – Almost certain	Medium	Medium	Medium	High	High

Priority Grading

Level	Grade	Definition
1	Urgent	Fundamental control issue on which action should be taken immediately
2	Important	Control issue on which action should be taken at the earliest opportunity
3	Routine	Control issue on which action should be taken

Appendix 2.   Terms of reference

The key risks agreed in the Terms of Reference are set out below.

Sub-process	Risks	Objectives
Procurement	Bribery and kickbacks Conflicts of interest Contract splitting Adherence to the Scheme of Delegation Failure to adhere to procurement processes	• Policies and procedures are clear, understood and followed to ensure the objectives of activity are met • Staff receive adequate training to enable understanding of the approved procurement process • Controls are in place to identify any breach of controls • Access to procurement is adequately restricted and monitored for any changes in roles
HR and payroll	False identity and immigration status Failure of agency to undertake pre-employment checks False expenses Ghost employees New starters added incorrectly	• Adequate identity and immigration checks are undertaken prior to employment commencing • Confirmation received that agency have undertaken any required pre-employment checks • Adequate segregation of duties when processing new starters to ensure incorrect people cannot be added to the payroll system • Adequate segregation of duties when processing expense payments to ensure false expenses are not paid • A review of team structures is undertaken regularly to ensure any additional payments being made are identified
Finance	Bank Mandate Fraud Post Contract Supplier Fraud: False Invoices / Inflated Invoices / Duplicate Invoices / Invoices for Work not Carried Out Insider Enabled Fraud/Fictitious suppliers / shell companies, payments to employees accounts Forged signatures on payment authorisations/failure to comply with sign off limits Unrecorded sales or receivables Improper use of credit cards / payment cards	• Changes to customer bank data is undertaken with segregation of duties and appropriate approval • Payments are only made to suppliers upon receipt of supporting evidence for work completed and approval in line with the Scheme of Delegation • There is adequate recording of all payments to ensure duplicate payments are not made • New suppliers can only be set up after appropriate due diligence has been undertaken to confirm the legitimacy of the organisation • Credit cards are only issued to authorised employees, with monitoring and review undertaken by an unrelated individual

Sub-process	Risks	Objectives
Councillors' Interests and Expenses	Undeclared interests or a lack of monitoring of declared interests unknowingly influence decision making for personal gain Expenses are paid which are not in line with the relevant expenses procedure	• Councillors declare any business or pecuniary interests on a regular basis • The register of interests is monitored at every meeting, with the Councillor removed from decision making should there be a conflict • There is clear guidance in place for what expenses are deemed appropriate • Expenses are monitored, in line with guidance, and only paid if they can be supported and deemed appropriate
Corporate Counter Fraud	There is a lack of training and guidance in place for staff to follow to assist in the prevention, identification and reporting of fraud	• Corporate policies are in place which are regularly updated and available to all staff • Training is provided to all staff relating to fraud risk management • There are dedicated individuals responsible for fraud risk management who have received an appropriate level of training