

NORTH LINCOLNSHIRE COUNCIL

AUDIT COMMITTEE

ANTI- FRAUD WORK

1. OBJECT AND KEY POINTS IN THIS REPORT

- 1.1 The purpose of this report is to summarise:
- the outcome of the fraud risk assessment carried out across the council
 - the results of the further detailed work to evaluate the council's current position in relation to the Chartered Institute of Public Finance and Accountancy (CIPFA) requirements for counter fraud.
- 1.2 To approve the improvement actions, produced as part of the risk assessment and evaluation.

2. BACKGROUND INFORMATION

- 2.1 North Lincolnshire Council has a proven track record of sound internal control, financial probity and management of resources. Good internal controls exist to deter, prevent and detect fraud, and there are a number of effective methods for customers and staff to refer suspected fraud for investigation. Cases are investigated effectively as they occur, minimising losses and reducing the likelihood of further cases. As a result our fraud experience has been relatively infrequent and of a low value. This is substantiated further through the National Fraud Initiative (NFI), which provides potential fraudulent data matches for the council to investigate. The last NFI exercise, returned fewer cases than would be expected of an authority this size and investigations revealed few instances of actual frauds that had occurred.
- 2.2 As part of the assessment of the effectiveness of the Audit Committee it was agreed that the Audit and Risk Manager would evaluate counter fraud arrangements against the CIPFA publication "Managing the Risk of Fraud – Actions to Counter Fraud and Corruption", which defines best practice in this area.
- 2.3 The report to Members in June 2008 indicated that most of the best practice requirements are either fully or partially met, with some areas for improvement identified. However it was agreed that further work would be required to assess the risk of fraud, evaluate in detail the council's current arrangements and determine, given the low levels of

fraud experienced, the optimum level of compliance with best practice balanced against added value and additional cost of implementation.

- 2.4 The self assessment states that the council should seek to assess the risk of fraud, but does not recommend any particular methodology for doing this. The HM Treasury has published a useful document titled 'Managing the Risk of Fraud – A Guide for Managers' which includes a 6-step risk assessment model, and includes useful checklists and examples of best practice that can be used as part of the process.
- 2.5 Appendix A shows a summary of the risk assessment results for each of the steps. The results are generally positive and only a few areas for improvement were identified, all of which were already been planned as part of ongoing fraud development work by Internal Audit.
- 2.6 The areas most vulnerable to the risk of fraud were identified to create an exposure profile. This is based on previous audit work and the existing profile was updated using this methodology. The work shows for each potential area for fraud that controls are in place and there are mechanisms for providing assurance that they are operating effectively. Opportunities to improve current arrangements were identified, including the increased use of analytical review as an early indicator of potential fraud, and these are also shown at Appendix A.
- 2.7 The risk assessment indicates that the council has a relatively low risk of fraud. CIPFA's counter fraud self-assessment was revisited to identify any areas of partial compliance and determine whether improvements are necessary to further raise compliance levels.
- 2.8 The self-assessment indicated a high level of full compliance and implementation of the action plan results at Appendix B will ensure full compliance for all but 2 indicators (3%). Most of the actions proposed were being considered as part of the 2008/09 fraud development exercise by Internal Audit. Compliance will be mainly improved through the refresh of the Anti Fraud Theft & Corruption Strategy and conclusion of the fraud development exercise.
- 2.9 The risk assessment substantiates the council's history of low-level infrequent instances of fraud experienced by the council. Given this it is considered acceptable that there are a small number of partially compliant areas remaining after implementation of the actions shown at Appendix B. The criteria we do not consider it necessary to meet due to the low fraud risk are;

To accurately identify the nature and scale of losses to fraud and corruption using: <ul style="list-style-type: none">- proper definition of fraud based in civil law for making accurate estimates	This is not considered best use of resources available at this time given council's low risk profile and efforts to promote deterrent measures are preferred.
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<p>- statistical methodology for making accurate estimates and building in a proper level of independent validation.</p>	
<p>The council should use accurate estimates of losses to make informed judgements about the level of budgetary investment in work to counter fraud and corruption.</p>	<p>Arrangements to monitor and quantify the nature and scale of losses will be maintained. Changes to budgetary investment decisions will be considered if the risk profile rises in specific areas.</p>

3. **OPTIONS FOR CONSIDERATION**

- 3.1 The first option is to remain static and do no further work other than the work already carried out to self assess the council's counter fraud arrangements.
- 3.2 The second option is to implement the actions identified in appendix B to achieve the levels of compliance deemed necessary through the risk assessment exercise.

4. **ANALYSIS OF OPTIONS**

- 4.1 Having carried out the risk assessment and a further detailed evaluation, failure to implement the action identified will mean there is only partial compliance several areas of best practice. This could result in a missed opportunity to
 - strengthen counter fraud arrangements
 - further enhance corporate governance arrangements on which the preparation of the Annual Governance Statement relies, and
 - demonstrate better use of resources and achieve more positive CPA judgements
- 4.2 This may in turn limit the effectiveness of the council's arrangements for creating a strong counter fraud culture, one of the criteria for an effective Audit Committee.
- 4.2 The risk assessment confirms that the council is at a low risk of fraud but there are some opportunities for development that can be implemented and would provide services that reflect the best practice counter fraud requirements where it is appropriate to do so.

5. **RESOURCE IMPLICATIONS (FINANCIAL, STAFFING, PROPERTY.IT)**

- 5.1 Resources are met from Internal Audit and Risk Management budgets.

6. **OTHER IMPLICATIONS (STATUTORY, ENVIRONMENTAL, DIVERSITY, SECTION 17 – CRIME AND DISORDER, RISK AND OTHER)**

6.1 The Chief Financial Officer has a statutory duty under the provisions of the Local Government Act 1972 to ensure the proper administration of the council's financial affairs. The council also has a duty under the Local Government Act 1999 to make arrangements to secure continuous improvement in the way in which its functions are exercised, having regard to a combination of economy, efficiency and effectiveness. The requirement for an internal audit function is set out in the Accounts and Audit Regulations 2003. Internal Audit will continue to assist the Chief Financial Officer discharge his statutory duty.

7. **OUTCOMES OF CONSULTATION**

7.1 The risk assessment and evaluation is the result of research into best practice, networking and benchmarking with other authorities and discussions with key members of staff within finance and human resources.

8. **RECOMMENDATIONS**

8.1 To note this report, and to approve the action plan of further work to establish improvements to anti fraud arrangements designed to meet the council's identified needs at Appendices A and B.

SERVICE DIRECTOR FINANCE

Pittwood House
Ashby Road
SCUNTHORPE
North Lincolnshire
DN16 1AB
Author: D Baker/ C Andrews
Date: 9th September 2008

Background Papers used in the preparation of this report

Cipfa Better Governance Forum Counter Fraud Advisory Panel publication Managing the Risk of Fraud – Actions to Counter Fraud and Corruption

HM Treasury Managing the Risk of fraud – A manager's guide

Appendix A

Risk Assessment methodology¹	Purpose	Approach taken	Outcome	Further action required
1. Assessment of the council's overall vulnerability to fraud	A quick assessment of the overall risk of fraud as a starting point	The checklist provided was used to identify areas of compliance and improvement	Overall the results were positive with no areas of concern. The areas for improvement have been included within the Cipfa counter fraud self assessment summary at Appendix B	None
2. Identification of the areas most vulnerable to the risk of fraud	An overview to show the scale and nature of fraud faced by the council to determine if there is a need to perform a more detailed assessment	The risk assessment of all key systems was updated with further audit knowledge, networking/benchmarking information and reference to fraud alerts/ warning bulletins. This generated an exposure profile of possible fraud areas that was used to consider control requirements necessary to deter, prevent or reduce the likelihood fraud occurrence. An evaluation of the controls and the sources of assurance that are in place to confirm that controls are working effectively to mitigate risks was then considered to identify any further areas for improvement.	The results were largely positive all areas of research suggested by the methodology were considered. Some areas for improvement were identified and this was largely anticipated and already in progress.	<p>Audits to incorporate more analytical review were appropriate</p> <p>Consideration given to using data matching techniques to data not currently included within the NFI exercise</p> <p>Define the council's response to money laundering legislation</p> <p>Follow up the actions agreed as part of the debit cards and grants audit reports recently issued</p> <p>Monitor the progress of ePayroll and eProcurement projects</p>
3. Assignment of ownership	To ensure that all those responsible for managing resources are aware of the associated fraud risks	The best practice approach contained within the methodology was considered	Whilst responsibilities in relation to fraud, are set out in a variety of documents, The Anti Fraud, Theft and Corruption Strategy (AFT&C), the Audit Plan, the Finance Manual, Annual Assurance Statements and publicity material, the best practice approach brings all this information together	The best practice wording will be adapted for the council and included within the AFT& C refresh

¹ Source HM Treasury

Appendix A

Risk Assessment methodology ¹	Purpose	Approach taken	Outcome	Further action required
			and is considered a further improvement to the AFT&C	
4. Evaluation of the scale of fraud risk	In order to determine how to deal with the risks identified at step 2, the scale of fraud risk is to be evaluated by assessing the threats and controls	As per step 2 the previous risk assessment updated and compared against the risks shown in the methodology, to ensure that it is up to date and comprehensive, and identify any areas for improvement	Controls are in place and there are mechanisms in place, such as annual audits, to confirm they are operating effectively. Some further work, particularly introduction of analytical review techniques and introduction of audit software to provide high level assurance and the proactive identification of fraud is needed, this had largely been anticipated and progress is being made	See above
5. Response to the risk of fraud	Having identified and evaluated the risk of fraud consideration is given to identify the appropriate responses that should be taken.	Best practice suggests developing <ul style="list-style-type: none"> • An anti fraud culture • Cost effective internal controls • Skills and expertise • A fraud response plan • Avenues for reporting frauds • Monitoring implementation of specific actions to reduce fraud, and continually monitoring the environment 	An AFT&C exists including a fraud response plan and is suitably publicised, this combined with various ethical codes in place and completion of and acting on findings of the counter fraud assessment demonstrate commitment to an anti fraud culture. Internal controls were considered in steps 2 and 4 and are considered comprehensive, follow up work is carried out to confirm the appropriate implementation of controls	The Audit Plan includes time set aside to develop the fraud approach A periodic refresh to continually monitor the fraud environment will be incorporated in the Audit Plan
6. Measure the effectiveness of the fraud strategy	To obtain assurance about the effectiveness of actions taken to reduce the risk of fraud	Best practice contains a number of sources for obtaining assurance including; <ul style="list-style-type: none"> • Reporting mechanisms – annual assurance statements • Internal audit activities 	All the sources are available to provide assurance on the effectiveness of the fraud strategy.	The AFT&C will be refreshed periodically and the risk assessment updated and reported periodically.

Appendix A

Risk Assessment methodology ¹	Purpose	Approach taken	Outcome	Further action required
		<ul style="list-style-type: none"><li data-bbox="772 310 1031 367">• Results of external inspection work		The sources of assurance will be summarised and reported to members more effectively.

Appendix B

Actions identified from the self assessment against the Cipfa Counter Fraud publication

Action	Purpose of Action	Target date for completion
Revise the Anti Fraud Theft and Corruption Strategy (AFT&C)	<ul style="list-style-type: none"> • Make clear the link to the ambitions • Make explicit that the remit is to reduce losses • Make explicit the effective the link between policy and operational work • Make explicit the range possible actions, including insurance and civil recovery action, that can be taken on each fraud • To make clear the counter fraud work and intended outcomes 	December 2008
Review internal audit investigation procedures and assess training needs	Ensure a best practice, consistent approach and standard documentation is in use, and the audit manual updated	March 2009
Improve the format of the Audit Plan	The audit plan shows fraud work but differentiate between policy and operational work	February 2009
Human Resources be reminded of the need to maintain full records of their cases, the outcome and an assessment of the loss. Details to audit to be forwarded to Internal Audit to record potentially fraudulent cases	To ensure: <ul style="list-style-type: none"> • all cases and outcomes are identified • the potential impact on the councils control environment can be evaluated • full cost of frauds cases can be calculated and reported if applicable to insurance 	December 2008
Draft framework agreements to be in place for working with other agencies	To cover the practicalities of work and liaison arrangements and ensure a joined up approach to fraud investigation with	December 2008

Action	Purpose of Action	Target date for completion
	clear roles and responsibilities	
Consider the benefits/costs of Internal Audit accessing the National Anti Fraud Network	To highlight potential fraud threats and evaluate controls in place accordingly. Also to assist with fraud investigation if appropriate	December 2008
Governance arrangements for partnerships will include audit and fraud investigation requirements	To ensure a joined up approach to fraud investigation with clear roles and responsibilities	December 2008
Carry out a survey to determine the level of awareness of the AFT&C including whistleblowing arrangements and publicise revisions accordingly	To evaluate the level of awareness and where appropriate, supplement with training or targeted publicity if necessary.	December 2008
Consider publicising successful outcomes of fraud investigations	To enhance the deterrent effect and promoting the council's anti fraud culture	December 2008
Publicise that audit are to be made aware of system changes and new systems implemented – via quarterly progress reports to Service Directors	To ensure that every effort is made to 'design fraud out' of any system implementation or change	September 2008
To consider the further use of analytical intelligence techniques, such as data matching and use of audit interrogation software	To proactively identify potential fraud and corruption	December 2008
Incorporate risk assessment results in audit planning	To ensure sufficient checks against the risk assessment exposure profile and as a source of assurance that risks are mitigated	February 2009
Records to be maintained of losses and recovery actions	To help determine the cost of fraud and demonstrate that all possible sanctions have been considered, and success rates of sanctions and recovery are monitored to inform future investigations	December 2008