

# Tees Valley Audit & Assurance Services

## Appendix 3 Audit and Assurance Report – FINAL

Middlesbrough Council

# Counter Fraud Policy Framework

Finance Governance & Support Services



Audit Ref: CCS033/16

**Report issued by:** Helen Fowler, Audit & Assurance Manager  
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**Date:** 02 November 2017

**Distributed to:**

**Draft**

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**Final**

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Ernst & Young

## Counter Fraud Policy Framework Executive Summary

### 1. Overall Opinion

- 1.1 Tees Valley Audit and Assurance Services (TVAAS) considers there to be a **Moderate** control environment with some weaknesses in relation to the areas examined. Based on the audit work undertaken, an acceptable internal control environment is in operation, but there are a number of improvements that could increase its consistency and effectiveness.
- 1.2 The focus of this report has been predominantly based on the counter fraud policy framework in place and the extent to which the Council has applied resources to demonstrating a proactive stance to identify potential existing fraudulent activity.
- 1.3 The audit identified areas where the Council's counter fraud policy framework could be further developed to help strengthen the control environment and Management are addressing these areas. Audits of the financial systems have confirmed that there is a good control framework in place which, if complied with, will reduce the likelihood and impact of loss through fraud and error. There is currently no evidence to suggest that the Council has or is suffering significant losses through fraudulent activity but there may be scope for the Council to be more proactive in demonstrating a zero tolerance approach to fraud, bribery and corruption. As with many local authorities, increasingly limited resources has affected the level of proactive counter fraud work that can be undertaken but it is suggested that consideration be given to carrying out some level of proactive work (even if only in one of the national fraud risk areas e.g. council tax discount) as this could result in financial gains and help demonstrate that the Council takes immediate and decisive action in response to any reported or suspected concerns.

### 2. Main Conclusions and Findings

- 2.1 The Council's counter fraud policy framework consists of a Whistleblowing Policy for staff (authored by HR) and an Anti Fraud, Bribery and Corruption Policy (authored by Internal Audit). Although the Council has a Whistleblowing Policy for staff to refer to, comparison of the content of this Policy against best practice and taking into account the Enterprise and Regulatory Reform Act 2013 changes affecting whistleblowing provisions would indicate that there is scope to expand the Policy further in order to encourage those who have concerns to raise in good faith have the confidence to do so. The areas where it is suggested that changes could be made are as follows:
  - reference to the efforts that the Council will take to safeguard whistleblowers from reprisal;
  - improved clarity as to the scope of the Policy; at present it refers to staff but does not clarify whether staff includes elected Members, agency workers and contractors;
  - signposting those that are not covered by the Policy to where they may raise concerns for example, local residents may become aware of some form of malpractice and there should be a clear mechanism for how such concerns can be raised in confidence. This will be included in the Anti Fraud, Bribery and Corruption Policy so that the Whistleblowing Policy can signpost to it;
  - the Policy and Procedures would benefit from providing more examples of the type of concerns that should be raised in order to emphasise the different

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types of fraudulent activities that can occur such as abuse of position, recruitment fraud, falsification of timesheets, and claims;

- the Policy should suggest what action a whistleblower may take if they are not satisfied with the response taken to a concern;
- the Policy could cross reference to the Department for Works and Pensions arrangements for reporting benefit related fraud.

- 2.2 Should the Policy be updated as recommended, it is suggested that the Council then undertakes a communication programme in order to raise awareness of the Policy's existence but also of the risks of fraud in general and the many forms that this may take. Although the Council has an e learning package on counter fraud, records indicate that only three staff have completed it. In addition, although the Policy is available on the Intranet, there may be stakeholders that do not have regular access to IT facilities therefore paper copies of the Policy should be distributed across Council sites. Consideration should also be given to conducting fraud awareness briefing sessions.
- 2.3 The Council has a nominated Anti Money Laundering Reporting Officer in the Head of Financial Governance and Revenues but documented anti money laundering policy and procedures require updating to reflect all changes in regulation and Management has stated that this will be carried out as soon as possible. The Intranet does not include reference to the existence of an Anti Money Laundering Policy and supporting procedure so it is suggested that the updated policy and procedures be made available on the Intranet for all staff to refer to after it has been updated and formally approved.
- 2.4 During the year, anti fraud controls have been tested as part of a number of different assignments and 2016/17 audits have resulted in 18 recommendations relating to improving anti fraud controls. Implementation of those actions will be followed up as part of the usual process. At the start of the 2016/17 year, an audit on Cash Handling Controls gave only Moderate assurance but the actions from that audit have since been implemented.
- 2.5 Although a fraud and loss risk assessment is maintained by Internal Audit, there is limited reference to specific fraud risks on the Council's risk register. Some national fraud risks will be more relevant to the Council than others, for example, as the Council does not have its own housing stock, right to buy fraud is of lesser relevance than the risk arising from frauds relating to direct payments, insurance, business rates and council tax. The Council should have an increased understanding of which areas of fraud it is most susceptible to in terms of loss and these should be reflected on the risk register. As a result, the fraud risk assessment will be shared with DMTs during the latter part of 2017. The relevant service areas should consider where there is scope and resources available to adopt a more proactive approach to minimising high fraud risks which could include the use of data analytics and data sharing agreements with other agencies.

### 3. Detailed Findings and Management Actions

- 3.1 Where action is required to improve controls, Appendix 1 to this report details the findings of this audit together with the associated risk and the remedial action required. Management are required to respond to each management action, detailing how they will address the finding, the responsible officer and the target date by which the proposed action will be taken. Please note that progress to implement all

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management actions will be followed up at the appropriate time.

### **4. Acknowledgements**

4.1 The assistance given by Middlesbrough Council staff is gratefully acknowledged.

## **Appendices**

Appendix 1 Summary of Management Actions – Implementation Schedule

Appendix 2 Terms of Reference

Appendix 3 Assurance and Priority Definitions

**Detailed Findings and Management Actions**

**Appendix 1**

**Audit Ref: CCS033/16 Title: Counter Fraud Policy Framework**

Priorities: 1 - Fundamental, 2 - Significant, 3 - Prudent

Priority Rating	No	Finding	Risk	Management Action	Status	Agreed	Responsibility	Target Date for Implementation
2	1	<p>The Audit &amp; Assurance Officer completed the Whistleblowing Policy Check List and found that the current policy, which also includes supporting documents &amp; procedural guidance, does not fully reflect best practice and legislation as follows:</p> <ul style="list-style-type: none"> <li>• There is insufficient information regarding the safeguarding of whistleblowers as required by the Enterprise and Regulatory Reform Act 2013;</li> <li>• The current version does not really provide examples (for the benefit of the whistleblower) of the type of concerns that should be raised under the Policy;</li> <li>• The Policy does include contact information for raising concerns with a number of external agencies but not all;</li> <li>• It is not clearly identified what action a whistleblower should take if they do not receive a response to a concern or if they are not satisfied with the outcome of an investigation;</li> <li>• It does not include a reference to the reporting route for raising a concern in relation to an issue involving suspected benefit fraud in that the contact details for the Department of Work and Pensions is not included;</li> </ul>	<p>That weak whistleblowing arrangements result in potential concerns not being reported at all or else not being reported in an appropriate way. This in turn increases the risk of reputational damage and financial loss as a result of undetected fraud, bribery and corruption.</p>	<p>The Head of Human Resources should fully review the current Whistleblowing Policy and Supporting Documents &amp; Procedural Guidance to ensure that the content of the Policy and Procedure reflects best practice and is aligned to other related Council policies. Consideration should be given to:</p> <ul style="list-style-type: none"> <li>• including more detail in the Whistleblowing Policy on the safeguards available to a whistleblower. In particular, the Policy should reflect the requirements of the Enterprise and Regulatory Reform Act;</li> <li>• including examples of the type of issues that potential whistleblowers should raise under the Policy;</li> <li>• including contact details of all outside agencies to whom concerns can be raised if the Council's response does not meet with the whistleblower's satisfaction. Examples include the Police non emergency number, external audit and Public Concern.</li> <li>• detailing the steps that can be taken by a whistleblower in the event that they are dissatisfied</li> </ul>	Action Underway	Y	Head of HR	31/12/17

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- The Policy does not echo the zero tolerance approach as stated in the Anti Fraud, Bribery and Corruption Policy.
- with the response to a concern they have raised;
- referring to the reporting route for suspected fraud and/or misuse of benefits and include the contact details for the Department of Works and Pension hotline number;
- including a statement of a zero tolerance approach to fraud and other wrongdoing.

**Management Comments:** Actions agreed by Head of HR. Work has started on reviewing the Whistleblowing Policy and Procedures to reflect the above management actions.

2	2	<p>Although the Whistleblowing Policy is available on the Intranet for staff reference, not all staff may have easy access to the Intranet. In addition, there is no reference on the Council's external website to the appropriate route by which non employees should raise suspected concerns.</p>	<p>That weak whistleblowing arrangements result in potential concerns not being reported at all or else not being reported in an appropriate way. This in turn increases the risk of reputational damage and financial loss as a result of undetected fraud, bribery and corruption.</p>	<p>Consideration should be given to circulating hard copy versions of the Whistleblowing Policy to sites where employees may not have regular IT access. Consideration should also be given to clarifying how non employees may raise suspected concerns with the Council. This could be captured in the Anti Fraud, Bribery and Corruption Policy with the Whistleblowing Policy signposting to which policy non employees should refer to. The Anti Fraud, Bribery and Corruption Policy will then need to be made available on the Council's external website so that non employees understand the appropriate route to follow when raising a suspected concern.</p>	<p>Action Underway</p>	Y	<p>Head of HR</p>	31/01/18
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**Management Comments:** From January all MBC employees will have access to the Council's intranet so hard copy versions of the policies should not be needed. However consideration can be given to ensuring all Council buildings have an up to date Whistleblowing Policy poster on display. TVAAS will update the Anti Fraud Bribery and Corruption Policy accordingly and make it available externally.

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3	3	<p>Although a counter fraud report is submitted annually to the Corporate Affairs and Audit Committee on the number of concerns raised with and/or investigated by Internal Audit; this is only one route by which concerns may be raised within the Council and therefore does not necessarily capture all concerns that may have been raised. As an example, the number of contacts made via the Monitoring Officer is not currently formally reported.</p>	<p>That weak whistleblowing arrangements result in potential concerns not being reported at all or else not being reported in an appropriate way. This in turn increases the risk of reputational damage and financial loss as a result of undetected fraud, bribery and corruption.</p>	<p>Information on the number and type of concerns raised via the Council's whistleblowing arrangements should be reported at least annually to an appropriate forum, for example, as part of the annual counter fraud report to the Corporate Affairs and Audit Committee. The information should be anonymised and include the number of contacts made via the whistleblowing arrangements, how the concerns were raised (i.e. letter, email, telephone, hotline etc), how many were investigated, referred to the Police and how many of the concerns were substantiated. The reported statistics should reflect concerns reported via all whistleblowing routes i.e. Audit &amp; Assurance, the Monitoring Officer and the S151 Officer.</p>	Action Pending	Y	Head of Legal Services	31/01/18
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**Management Comments:** The information requested will be provided at the earliest opportunity.

3	4	<p>Although it is understood that there are anti money laundering procedures in place and that the Head of Financial Governance and Revenues is the nominated Anti Money Laundering Reporting Officer for the Council, the current Anti Money Laundering Policy has not been recently updated to reflect changes in the regulations and is not available on the Intranet for staff to refer to.</p>	<p>That there is poor or no communication of all counter fraud related policies and strategies meaning that staff have little awareness of the Council's policy on fraud prevention and detection. This in turn can lead to the impression that the Council does not take a proactive or firm response to fraud prevention and detection leading to an increased risk of fraud, bribery and corruption incidences going undetected and resulting in loss and reputational damage.</p>	<p>The Council should ensure that its Anti Money Laundering Policy and supporting procedure is updated to reflect all changes in regulations, including the most recent changes in 2017. The Policy should be made available on the Council's Intranet for staff to refer to.</p>	Action Underway	Y	Head of Financial Governance & Revenues	31/12/17
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**Management Comments:** The Policy is being updated to reflect the 2017 Regulations so this action is in hand. The policy will be made available on the intranet.

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3	5	<p>There is limited evidence that any fraud awareness training has been carried out within the Council with only three members of staff having taken the online course available. Kier Business Services informed the Audit &amp; Assurance Officer that they do not have any formal training but do highlight risk areas or issues as and when they arise via briefing sessions.</p>	<p>That there is poor or no communication of all counter fraud related policies and strategies meaning that staff have little awareness of the Council's policy on fraud prevention and detection. This in turn can lead to the impression that the Council does not take a proactive or firm response to fraud prevention and detection leading to an increased risk of fraud, bribery and corruption incidences going undetected and resulting in loss and reputational damage.</p>	<p>The Council should consider raising awareness of the existence of the online Anti Fraud e Learning Course and identifying which staff should complete this training. Consideration should be given to other means of raising and publicising key fraud risk areas.</p>	Action Pending	Y	<p>Head of Financial Governance &amp; Revenues</p>	31/12/17
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**Management Comments:** The Head of Financial Governance and Revenues and Audit & Assurance Officer, Counter Fraud have agreed to arrange for the Council's bankers to deliver some fraud training sessions for key staff. The e-learning course will also be re-targeted to key staff to ensure that this training is carried out.

2	6	<p>Although Internal Audit maintains a fraud and loss risk assessment, this is prepared in order to inform the compilation of the annual audit plan rather than to instigate a proactive campaign by the Council to minimise losses due to fraud and error. There are a number of national fraud risks that are relevant to the Council and which are currently not reflected on the Council's risk registers and do not appear to be subject to any level of reporting via LMT.</p>	<p>That the Council's corporate counter fraud culture is ineffective leading to increased incidences of fraud, bribery and corruption going undetected or concerns not being investigated leading to financial loss and reputational damage.</p>	<p>The Council should consider the current national fraud risks and identify those most relevant to the Council. Those risks should then be reflected on the corporate risk registers and consideration given to a proactive campaign to minimise the risks of any resultant losses. This could be done in conjunction with Internal Audit's own fraud and loss assessment or as a separate exercise. There should be some level of reporting on the management of those fraud risks by the relevant service managers via LMT and/or the Corporate Affairs and Audit Committee.</p>	Action Pending	Y	<p>Head of Financial Governance &amp; Revenues/Audit &amp; Assurance Manager</p>	31/12/17
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**Management Comments:** The Audit & Assurance Manager will discuss this action with the Head of Financial Governance and Revenues.

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2	7	The Accounting Service Manager informed the Audit & Assurance Officer that the segregation of duties and authorisation controls are currently still under the requirement of the previous SAP financial system and they require reviewing taking into account the requirements of the new Agresso financial system.	That the Council has little or no understanding of where its highest areas of fraud risk are resulting in inadequate controls in those areas and undetected incidences of fraud and loss.	The Accounting Service Manager should review the various key financial systems to ensure that the appropriate segregation of duties and authorisation controls are relevant to the Agresso Finance System.	Action Pending	Y	Chief Accountant	31/01/18
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**Management Comments:** The Chief Accountant will be reviewing workload and controls in the accountancy team as part of the implementation of the service review to ensure they are fit for purpose.

**Tees Valley Audit & Assurance Service**

**Terms of Reference**

<b><u>Audit Title:</u></b>	Counter Fraud Policy Framework
<b><u>Start Date:</u></b>	05 September 2016
<b><u>Audit Lead:</u></b>	Helen Fowler (Audit & Assurance Manager)
<b><u>Auditors:</u></b>	Ian Johnson [Audit and Assurance Officer (Counter-Fraud)]

**Background**

Most organisations are at an increased risk of fraud and corruption with the fastest areas of growing risk being cyber crime and fraud caused by insiders (including acts of theft or data destruction/manipulation by employees). The latest Annual Fraud Indicator 2016 was published by Experian, PKF Littlejohn and the University of Portsmouth's Centre for Counter Fraud Studies, who have created a partnership to help consistently gauge, analyse and quantify the true scale of fraud in the UK. The total estimated fraud losses for local government amounted to £7.3bn.

Fraud is defined by the Chartered Institute of Public Finance and Accountancy (CIPFA) as the intentional distortion of financial statements or other records by persons internal or external to the authority, which is carried out to conceal the misappropriation of assets or otherwise for gain, or to mislead or misrepresent. Corruption is defined as the offering, giving, soliciting or acceptance of an inducement or reward which may influence the action of any person; or the failure to disclose an interest in order to enjoy financial or other pecuniary gain. Bribery is the receiving or offering of undue reward to persons in order to influence their behaviour contrary to ordinary standards of integrity and honesty.

Recent years have witnessed significant changes in the counter-fraud landscape in local government including the closure of the National Fraud Authority in March 2014 and the Audit Commission a year later. CIPFA established a new 'centre of excellence' to combat fraud which works closely with the Department for Communities and Local Government (DCLG), the Cabinet Office, the National Crime Agency (NCA) and other agencies to develop policies, tools and guidance to help public sector organisations to identify and address fraud. Significant funding reductions since 2010 for councils has contributed to a near 20 per cent reduction in counter-fraud investigators and a general reduced capacity to take a proactive approach to fraud detection. A significant change has also been the transfer of most of the benefit fraud investigators to the Single Fraud Investigation Service (SFIS), which is managed by the Department for Works and Pensions.

### **Audit Approach**

The review will be both risk and systems/procedures based. A high level review will be undertaken of the overall anti fraud policy and strategy framework in place to ensure that combatting fraud is positioned at an appropriate level within the Council. Consideration will be given to the adequacy of the existing policies in terms of their scope and content, compliance with legislation, their communication and review. The review will be based around the principles and recommendations contained within the national Fighting Fraud Locally Strategy and the CIPFA guidance. The annual fraud and loss risk self assessment will be completed which will identify key fraud risks to the Council. Sample testing will be carried out in the areas of highest risk identified in order to establish compliance with relevant criteria and process requirements and to assess the adequacy of the control environment. The review will seek not only to assess compliance with existing procedures and controls but also to assess the effectiveness of those systems and controls with a view to identifying areas of improvement that may assist the Council in attaining its objectives.

### **Scope & Objectives**

The scope of the assignment will be to review the overall counter fraud arrangements in place across the Council (with the focus being on the areas with the highest fraud risk) with a view to identifying areas where controls could be strengthened. Processes and procedures will be reviewed in areas of high fraud risk to ensure that they are suitable, robust, and are operating effectively. In the event that any weaknesses in the control environment are identified, any processes and procedures which are currently being revised will be evaluated in order to ensure that they adequately address any issues arising from the review, and ensure that the governance and control framework going forward is fit for purpose.

The objectives of the review will cover the following main areas:

1. Review the Council's whistleblowing framework to provide assurance that it is fit for purpose, clearly communicated, compliant with legislation/best practice and provides a clearly defined route for potential concerns to be raised.
2. Review the level of corporate commitment being demonstrated towards counter fraud, bribery and corruption i.e. the level of authorisation and consultation on the policies/strategies and the extent of communication of counter fraud matters to all employees and partners of the Council.
3. Complete an assessment of the Council's counter fraud, bribery and corruption arrangements against the recommendations contained within national guidance e.g. Fighting Fraud Locally Strategy and the CIPFA counter fraud tools.
4. Identify the highest fraud, bribery and corruption risks to the Council and confirm that effective and proportionate controls are in place to minimise those risks.

### **Reporting**

A draft report will be issued for review and consultation by the appropriate levels of management. Management actions will be prioritised to identify clearly their respective risk and these will be agreed prior to the issue of the final report. A final report will then be issued, in a timely manner, with the aim of prompting management to implement management actions for change, leading to improvements in

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performance and control. It is the responsibility of departmental management to ensure that management actions, which are agreed, do actually get implemented within the agreed timescales and this action is reported back to Internal Audit. The Council's internal audit function monitors and reports to Corporate Affairs and Audit Committee on the implementation of their management actions.

**Reporting Definitions**

**Audit Assurance Levels**

Audit & Assurance have five categories by which to classify the level of assurance offered over the system or area we have examined, these are defined as follows:

<b><u>Assurance Level</u></b>	<b><u>Definition</u></b>
Strong Control Environment	Overall, a Strong Control Environment in relation to the areas examined. Based on the audit work undertaken, an effective system of internal control is in operation and is applied consistently.
Good Control Environment	Overall, a Good Control Environment with room for improvement in relation to the areas examined. Based on the audit work undertaken, an effective system of internal control is in operation but is not always applied consistently.
Moderate Control Environment	Overall, a Moderate Control Environment with some weaknesses in relation to the areas examined. Based on the audit work undertaken, an acceptable internal control environment is in operation, but there are a number of improvements that could increase its consistency and effectiveness.
Cause for Concern	Overall, Cause for concern in relation to the areas examined. Weak management of risk exists within a key area(s) that is/are crucial to the achievement of objectives. Major improvements need to be made to the system or area in order to ensure the control environment is effective.
Cause for Considerable Concern	Overall, Cause for Considerable Concern in relation to the areas examined. Fundamental failures exist within the control environment and the Council is exposed to unacceptable levels of risk. Key areas that are crucial to the achievement of objectives need fundamental improvements.

**Priority Ratings**

In order to assist management in using our reports, we categorise our management actions according to the level of priority as follows:

<b><u>Priority Rating</u></b>	<b><u>Definition</u></b>
1 - Fundamental	A fundamental risk exists to the achievement of the system/service objectives and it is of an unacceptable level. Management should initiate immediate action to address this system weakness.
2 - Significant	A significant risk exists which has the potential to adversely affect the achievement of the system/service objectives. Management should initiate timely action to address the weakness.
3 - Prudent	System objectives are not exposed to significant risk but the issue merits attention by management as it offers service improvements by complying with best practice, and strengthening the overall control environment.