

MIDDLESBROUGH COUNCIL

COMMITTEE REPORT

CORPORATE AFFAIRS AND AUDIT COMMITTEE

29 January 2015

Internal Audit – Counter Fraud Report

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PURPOSE OF REPORT

1. To update Members on the impact of fraud on the UK by summarising the main findings from the Audit Commission's annual report on Protecting the Public Purse 2014. To consider the potential impact of fraud on Middlesbrough Council and its residents, the key fraud risks to be managed, the existing counter fraud arrangements in place and the further action that could be taken to safeguard the Council from fraud and loss.

WHAT IS FRAUD AND CORRUPTION?

2. Fraud is defined as the intentional distortion of financial statements or other records by persons internal or external to the organisation, carried out to conceal the misappropriation of assets or otherwise for gain.
3. Corruption is defined as the offering, giving or soliciting or acceptance of an inducement or reward, which may influence a person to act against the interests of the organisation.
4. The term fraud is often used to describe acts such as deception, bribery, forgery, extortion, corruption, theft, conspiracy, misappropriation, false representation, concealment of materials, facts and collusion, dishonesty and intent to make a gain or cause loss or damage to the interests of an organisation.
5. Fraudulent activity may result in internal disciplinary action, civil court proceedings or prosecution by the Police. Fraud may also be linked to other serious criminal activity taking place outside of an organisation including extortion and money laundering.

THE IMPACT OF FRAUD

6. Fraud costs the UK public sector more than £20 billion per annum and most recent estimates suggest that local government alone loses more than £2 billion. This almost certainly underestimates the true cost of fraud. For

example, it does not include fraud in major services such as education and social care. Each pound lost to fraud represents a loss to the public purse and reduces the ability of local government bodies to provide services to people who need them. Fraud is never a victimless crime.

7. Fraud has an obvious financial impact but the harm caused is not solely financial as it may also damage local people and communities. Internal fraud, for example, can cause great distress and loss of morale to the team affected whilst the fraudulent sub letting of local authority houses for profit could deny a local family the chance to have a home. In addition, fraud often causes reputational damage and undermines trust in public services.

PROTECTING THE PUBLIC PURSE 2014 (PPP 2014)

8. Each year, the Audit Commission has requested that all local government bodies submit data relating to detected frauds. This information has then been used to help formulate its annual Protecting the Public Purse report. The 2014 report will be the last report in the PPP series due to the Audit Commission's closure at the end of March 2015. When the Commission closes, the National Fraud Initiative's (NFI) data matching service will transfer to the Cabinet Office. The remainder of the Commission's counter-fraud staff and functions, including the *PPP* series and fraud briefings, will transfer to the Counter Fraud Centre, run by the Chartered Institute of Public Finance and Accountancy (CIPFA). Other changes include the creation of the National Crime Agency, established in 2014, which has taken over some of the activities previously carried out by the Serious and Organised Crime Agency (SOCA).
9. PPP 2014 aims to inform the development of effective counter fraud in local government after the Commission closes and is aimed at those responsible for governance, including councillors. The report describes:
 - the amount of detected fraud reported by local government bodies in 2013/14, compared with 2012/13;
 - longer term trends in levels of detected fraud, and the lessons local government bodies can draw from this information;
 - the effective stewardship of the public purse, including taking measures to recover losses from fraud and
 - measures to build on *PPP's* legacy, so that local government bodies can continue to protect the public purse.
10. A summary of the PPP key findings is as follows:
 - Overall, local government bodies detected fewer cases of fraud in 2013/14 than in 2012/13, continuing the decline noted in 2012/13. The number of detected cases fell by 3 per cent to just over 104,000, although the associated value of these cases increased by 6 per cent to over £188 million.

- The number of detected cases of **housing benefit and council tax benefit fraud** fell by 1 per cent to nearly 47,000, whilst their value rose by 7 per cent to nearly £129 million.
- The number of detected cases of **non-benefit fraud** fell by 4 per cent to just over 57,400 although their associated value rose by 2 per cent to £59 million.
- Between 1991 and 2000, nearly all fraud detected by councils was for housing benefit and later council tax benefit. During this time, councils had financial incentives to look for this type of fraud but these incentives ended in 2006, meaning that councils have increasingly focused on non-benefit fraud in the past five years. Despite this, benefit frauds still comprise 45 per cent of all cases of detected fraud, and 69 per cent of their value.
- By 2016, all benefit fraud investigation will have transferred from councils to the Single Fraud Investigation Service (SFIS), run by the Department for Work and Pensions.
- Between 2009/10 and 2013/14, councils consistently detected more **council tax discount fraud** than any other type of non-benefit fraud. In the most recent year, nearly 50,000 cases were found, worth £16.9 million.
- Detected **Right to Buy** fraud cases have increased nearly five-fold since 2009/10 to 193 per year. In 2013/14 these were worth £12.3 million. The rise in the number of these frauds followed large increases in the discount threshold over this period.
- The number of detected cases of **social care** fraud has more than trebled since 2009/10 to 438. In 2013/14, they were worth £6.2 million.
- Detected cases of **insurance** fraud rose from 72 in 2009/10 to 226 in 2013/14 and were worth £4.8 million.
- Overall, councils are detecting more non-benefit frauds, for example, the number of **social homes** recovered from tenancy fraudsters increased by 15 per cent in the last year to 3,030. Detected cases of fraud in **maintained schools** have risen by 6 per cent to 206, worth £2.3 million (there is no data on fraud in non-maintained schools). Most of these frauds were committed by staff, suggesting that some schools may have weak governance arrangements that mean they are more vulnerable to fraud.
- Detection rates for some types of frauds have fallen. For example, in 2010/11, councils detected 319 cases of **business rates** fraud worth £5.7 million compared to just 84 cases worth £1.2 million in 2013/14. Similarly, in 2010/11, councils detected 145 cases of **procurement** fraud worth nearly £14.6 million compared to 127 cases worth less than £4.5 million in 2013/14.

11. A small minority of 39 councils (35 districts, 3 unitaries and 1 metropolitan) failed to detect any non-benefit frauds in 2013/14. This number is down by more than half since 2012/13 when 79 district councils had not detected a single non benefit fraud and is therefore encouraging. The Commission's experience suggests it is extremely unlikely that no non-benefit fraud occurred at these councils. Councils believe that organised criminals present a low risk

of fraud, but there is concern that organised crime is more prevalent in procurement fraud.

12. According to PPP2014, a summary of the key fraud risks (nationally) is as follows:

- Procurement fraud – 127 cases detected in 2013/14 at a loss of £4.4 million compared to 165 cases detected in 2009/10 valued at £2.9 million.
- Housing tenancy fraud – the number of social homes recovered from tenancy fraudsters increased by 15% in the last year. A total of 3,030 properties were recovered nationally in 2013/14, of which, 59 were in the north east and 1,807 in London.
- Housing and council tax benefit fraud – nationally, 46,690 cases were detected in 2013/14 to a value of £129 million which is not significantly different to the previous year's figures (46,964 cases at £120 million).
- Payroll fraud – 432 cases detected in 2013/14 valued at £1.4 million (2012/13 – 319 cases at £2.4 million).
- Council tax discount fraud – in 2013/14, 49,428 cases were detected nationally at a value of almost £17 million (2009/10: 48,253 cases at £16.4 million).
- Disabled parking concessions (blue badge) – 4,055 cases in 2013/14 valued at just over £2 million (2009/10: 4,097 cases valued at £2.2 million).
- Grants and loans fraud – 36 cases detected in 2013/14 valued at £742k (2009/10 – 47 cases valued at £968k).
- Business rates - £1.2 million detected on 84 cases in 2013/14 (2009/10 – 29 cases at £661k).
- Right to Buy fraud – 193 cases in 2013/14 valued at £12.3 million (2009/10- 34 cases valued at £740k).
- Social care payment fraud – 438 cases detected in 2013/14 valued at £6.2 million (2009/10 – 131 cases at £1.5 million).
- False insurance claims – 226 cases detected in 2013/14 with a total value of 4.77 million (2009/10 – 72 cases valued at just over £3 million).
- Internal fraud (e.g. abuse of position, payroll and expenses fraud) – 1,474 cases detected with a total value of £8.4 million in 2013/14 (2009/10 – 1,659 cases worth £8.6 million).
- Fraud in schools – 206 cases detected in 2013/14 valued at £2.33 million (2012/13 - 191 cases detected in 2012/13 worth £2.32 million. Over half of the 2013/14 cases were committed by staff.

THE MAIN ISSUES FACING COUNCILS WHEN TACKLING FRAUD

13. The 2014 survey asked councils to identify the top three issues they face in tackling fraud. Councils reported that the single most important issue is the need to ensure they have enough counter fraud capacity. Other issues related to effective data sharing, effective fraud risk management, having staff with the appropriate investigatory skills,

improved partnership working and greater public support for combatting fraud. In addition, 39% of councils stated that one issue faced was the lack of corporate appreciation as to the potential financial benefits in tackling fraud.

WHAT ROLE SHOULD COUNCILLORS PLAY

14. According to PPP2013, councillors have a crucial role to play in supporting the organisation's approach to prevention and detection of fraud. Councillors therefore should encourage their council to focus on deterrence by publicising actions taken against fraudsters, by understanding the local fraud risks and ensuring that resources are deployed to counter fraud work proportionate to the risk involved. Many councils now have a councillor with portfolio responsibility for fighting fraud.

WHAT ARE THE COUNTER FRAUD ARRANGEMENTS IN PLACE AT MIDDLESBROUGH COUNCIL

15. Middlesbrough has the following counter fraud arrangements in place:

- Whistleblowing Policy.
- Anti Fraud and Corruption Policy.
- Anti Money Laundering Policy.
- Information on the standards expected of employees including general conduct, disclosure of information, undertaking private paid work, private unpaid work, the interest of employees in contracts, writing of books, political neutrality etc. Specific reference to the Social Media Policy and the Gifts and Hospitality Policy.
- Procedures for declaring gifts, hospitality and interests.
- Internal audit reviews of the control environment.
- Internal audit plan which includes contingency allocation for investigating alleged fraudulent activity.
- Annual fraud and loss risk self assessment.
- Benefit Fraud Team which includes accredited counter fraud investigators.
- Prosecution Policy
- Data matching – housing benefit matching service (HBMS), credit reference agency matches, National Fraud Initiative (NFI).
- Employers' surveys and residency exercises.
- Joint and partnership working e.g. the Benefit Fraud Team works closely with Job Centre Plus.
- Communications with other local authorities and bodies e.g. TVAAS circulate fraud alerts to other regional internal audit teams and notify National Action Against Fraud Network (NAFN) where appropriate.

HOW SIGNIFICANT IS FRAUD A PROBLEM TO MIDDLESBROUGH AND WHAT IS IT DOING TO MINIMISE LOSSES?

Benefit Fraud

16. For Middlesbrough Council, the figures for benefit fraud investigation for the last five years are as follows:

	2013-14	2012-13	2011-12	2010-11	2009-10
Referrals	574	589	753	697	614
Investigations	251	249	354	396	413
Investigation Rate	43%	42%	47%	57%	67%
Positive Results	135	192	255	239	208
Success Rate	53%	77%	72%	60%	50%
Sanctions	50	102	146	115	99
Conversion Rate	37%	53%	57%	48%	48%

Benefit Fraud Team

17. For Middlesbrough Council, the investigation of benefit fraud is carried out by the Benefit Fraud Team under the Mouchel contract. All fraud officers are qualified as Accredited Counter Fraud Investigators and as Authorised Officers under section 110 Social Security Administration Act 1992.

18. During 2013/14, in the absence of any sanctions targets/reward scheme, the Fraud Team decided to investigate more cases, including more allegations of non residency based with the emphasis not solely based on sanctions. During 2013/14 the Benefit Fraud Team (Mouchel) had fewer investigators but still investigated 251 cases of benefit fraud from a total of 574 cases referred or 43% of the cases referred. From the 251 investigations carried out there were 135 positive outcomes where there was an adjustment to benefit due to fraud or error, a success rate of 53%. A total of 50 sanctions was achieved from the positive investigations, a conversion rate, (successful investigations to sanctions) of 37%. The sanction return in the year 2011/12 of 57% had been the team's largest since the Council's Prosecution Policy was introduced in 2000.

19. In 2013/14, as a consequence of fraud investigations a total of £343,476 in overpaid housing and council tax benefits was discovered.

20. In 2012/13, of the 135 cases, where benefit was found to be incorrect as a result of an investigation, formal action was taken in 50 instances, or 37%. Formal action is only taken when the evidence is sufficient to show beyond doubt that an offence has been committed. The total amount of overpaid benefit included in successful prosecutions was as follows:

Housing Benefit	£113,237
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Council Tax Benefit	£ 24,898
DWP Benefits	<u>£ 142,495</u>
TOTAL	£280,630

21. In addition to prosecutions, there were 8 cautions and 6 administration penalties offered and accepted in 2013/14, as an alternative to formal criminal proceedings. Cautions are offered to benefit claimants where prosecution is not the first option for the disposal of the case but formal recognition of the deception needs to be recorded. The decision to offer a caution is made in accordance with the guidelines contained in the Prosecution Policy, with a record of the caution being retained both at the Council and with the DWP. Administration penalties are governed by section 115A of the Social Security Administration Act 1992 and are an additional alternative, where prosecution is not the first option. The Act allows the Council to impose an additional penalty of 30% on top of the overpayment, where benefit fraud is found to have been committed. The Prosecution Policy contains guidance on when the offer of a penalty is appropriate. As a consequence of administration penalties being accepted in 2013/14, an additional £3,471 was added to the overpayment created as a result of the fraud.

Tees Valley Audit and Assurance Services (TVAAS)

22. Tees Valley Audit and Assurance Services (TVAAS) investigate suspected internal fraudulent activity and also review anti fraud controls whilst carrying out audits across the Council.

23. Internal Audit, along with other assurance processes of the Council, have a statutory obligation under the Accounts and Audit (Amendment) (England) Regulations 2011 and the PSIAS to provide assurance from the work they undertake in respect to the internal control systems operating within the Council.

24. The best way to reduce fraud losses is to prevent the opportunity in the first place by ensuring that the Council has an effective governance and control environment in place. The annual programme of work carried out by TVAAS assists in providing this assurance both on the material financial systems but also in relation to other high fraud risk areas within the Council. In order to help minimise the risk of fraud and corruption, TVAAS have been involved with the following:

- Ensuring that the annual audit plan includes time to focus on the significant fraud risks facing the Council. In 2014/15, for example, audits have or will have been carried out to review the controls in relation to purchasing cards, vehicles, fuel and tools, leisure centres and cafes.
- Monitoring the number of recommendations being made relating to anti fraud controls to identify trends in both control weaknesses and in service areas. Audit work carried out in 2012/13 resulted in 51 recommendations specifically aimed at improving anti fraud controls with 38 identified in 2013/14. Recommendations were aimed at improving authorisation

processes, increasing segregation of duties and the level of monitoring undertaken.

- Creating an Anti Fraud and Corruption Policy that was approved by Members of the Audit and Governance Committee in 2012.
- Circulating fraud alerts to local authorities and National Action Against Fraud Network (NAFN).
- As TVAAS provides audit services to both Middlesbrough and Redcar Councils, it has been possible to share intelligence regarding possible risk areas.
- Developing a counter fraud action plan in response to the publication of Fighting Fraud Locally Strategy in 2012 and carrying out a review of the Council's counter fraud arrangements – detail will be reported to the Chief Financial Officer once completed.
- Assisting with the coordination of the National Fraud Initiative exercise (please see 25 below).
- Investigating a number of allegations of theft/misappropriation of funds and assets and making recommendations where appropriate to improve the anti fraud/theft controls (please see **Appendix 1** for details of cases investigated since 1 April 2013 to date).

NATIONAL FRAUD INITIATIVE (NFI)

25. The NFI is a data matching exercise, via a secure website, that compares information held by and between approximately 1,300 organisations including councils, the Police, hospitals and almost 100 private companies. The purpose of the exercise is to identify potentially fraudulent claims, errors and overpayments. Each of these organisations submits various data sets relating to those services where it is anticipated that fraud and error is most likely to occur, for example, housing benefits, council tax (single person discounts), payroll, insurance claimants, private supported care home residents, licenses (taxi, personal alcohol) electoral roll, trade creditors payments, transport passes and permits (blue badge, residents parking permits and concessionary travel passes). Data has to be submitted according to specified timescales. Once the data has been submitted, the matching process is undertaken and it is this process that results in 'matches'. The 'matches' relevant to each public body are passed back to the organisation for further investigation to either clear the 'match' i.e. confirm that the match is acceptable or take action in response to a potential fraud or error. One example of a 'match' could be a person in receipt of pension but who, according to other data, is deceased. This 'match' would require further investigation by the organisation paying the pension. In the UK, the NFI exercise has produced significant results, identifying £1.17 billion of fraud, overpayment and error since it started in 1996.

26. The Chief Financial Officer has overall responsibility for NFI in Middlesbrough Council. TVAAS (Internal Audit) act as the Key Contact for the Council with the NFI Team and are responsible for the administration of the web-based application. Service managers are responsible for submitting accurate data for the matching process and for investigating any subsequent matches

produced, and for updating the NFI web application with their findings and results.

27. The reports of 'matches' returned by the NFI Team to the Council for further investigation in relation to the 2012 data matching were classified into 'key reports' (of which there were 18) and the others (of which there were 57). Within all of these reports, certain matches are highlighted as 'recommended'. The 'recommended' matches are those that the NFI Team believe represent the greatest risk to the Council, usually in terms of financial value, and so priority should be given by the Council to investigating them. Due to the level of resources required to investigate matches and the limited number of meaningful outcomes obtained, Council resources used for investigating matches have tended to concentrate on examining the recommended matches within the key reports.
28. **Appendix 2** shows Middlesbrough Council's progress against the 18 NFI key reports. Within the 18 key reports, the Council was provided with a total of 1,964 recommended matches. To date, a total of 1,055 matches have been cleared and 11 are still in progress. The table in **Appendix 2** shows an outcome of £93,742.82 being recoverable as overpayments. The Council is currently in the process of recovering £26,288.97 of that amount.
29. Participating in NFI is a mandatory requirement and is a time consuming exercise. In preparation for the next matching process, the Council's data sets have recently been uploaded again with any resultant matches available for checking in February 2014.

FURTHER ACTION TO BE TAKEN TO FIGHT FRAUD

30. Having a strong anti fraud and corruption culture underpins any Council's objectives by ensuring that resources are appropriately used. It is the responsibility of all staff to prevent fraud but the work of both the Fraud Team and TVAAS helps to identify fraud risks and areas where anti fraud controls need to be strengthened. In order to tackle fraud, the Council should embrace the national guidance set out in the Fighting Fraud Locally Strategy published April 2012 which is based on three key principles:
- Acknowledge and understand fraud risks
 - Prevent and detect fraud
 - Pursue those found to be guilty of fraud and seek to maximise recovery of losses.
31. As part of its annual programme, TVAAS will further develop its approach to preventing and detecting fraud. This has included carrying out an assessment of the counter fraud arrangements in place at Middlesbrough Council by completing the checklist provided in PPP2014. Completion of the checklist has identified the following actions that could be taken:
- Liaise with officers in Revenues and Benefits to prepare a strategy for the Council's response to the implementation of the Single Fraud Investigation Service and to identify the action that needs to be taken.

- TVAAS Fraud Auditor to work in conjunction with service managers across key fraud risk areas – council tax discount, benefits, social care payments, blue badge – in order to ensure strong control frameworks are in place and to review stance on prosecution.
- Consider fraud awareness campaign aimed at raising awareness of fraud risks with both employees and residents.
- Request allocation of portfolio responsibility for fraud to a Councillor.
- Ensure that Audit and Assurance training programme includes fraud awareness briefings and develop fraud awareness guidance for managers.
- Carrying out a survey across the Council to establish the current level of awareness of existing counter fraud and whistleblowing arrangements.
- Presenting the updated counter fraud policies to a future meeting of the Governance Committee.
- Continue to update the mapping of the high fraud risks across the Council and targeting resources accordingly.
- Continued involvement in the NFI and ensuring that deadlines are met.
- Linking in with Human Resources in order to raise awareness of everyone's responsibility towards minimising fraud e.g. via induction and appraisal processes.
- Publicising cases of fraud that have resulted in prosecution (subject to legal and Data Protection considerations).
- Exploring joint ways of working, for example with other local authorities, housing associations etc. in order to tackle high risk areas of fraud outlined in PPP2014 e.g. tenancy fraud.

FINANCIAL CONSIDERATIONS

32. Fraud costs the public sector an estimated £20.6 billion per year and local government over £2 billion. The prevention and detection of fraud is therefore crucial to all councils. The Benefit Fraud Team is provided by Mouchel whilst Redcar & Cleveland Council charges Middlesbrough Council for the provision of an internal audit service.

FINANCIAL, LEGAL AND WARD IMPLICATIONS

33. The financial implications of fraud and the measures required to mitigate the risks are highlighted throughout this report. There are no specific ward implications arising from the Fraud Report.

RECOMMENDATIONS

34. Members are requested to note and comment upon the report and highlight any concerns or areas where additional resource should be given to fraud prevention. It is recommended that more detail on the proposed fraud action plan together with the revised policies will be provided to Members of this Committee at a future meeting.

REASONS

35. A strong anti fraud and corruption culture will underpin the Council's strategic

objective of being an effective and efficient Council by ensuring that resources are appropriately used.

BACKGROUND PAPERS

- Protecting the Public Purse 2014
- Annual Fraud and Loss Risk Self Assessment
- Public Sector Internal Audit Standards (PSIAS)
- Various reports issued by Internal Audit

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