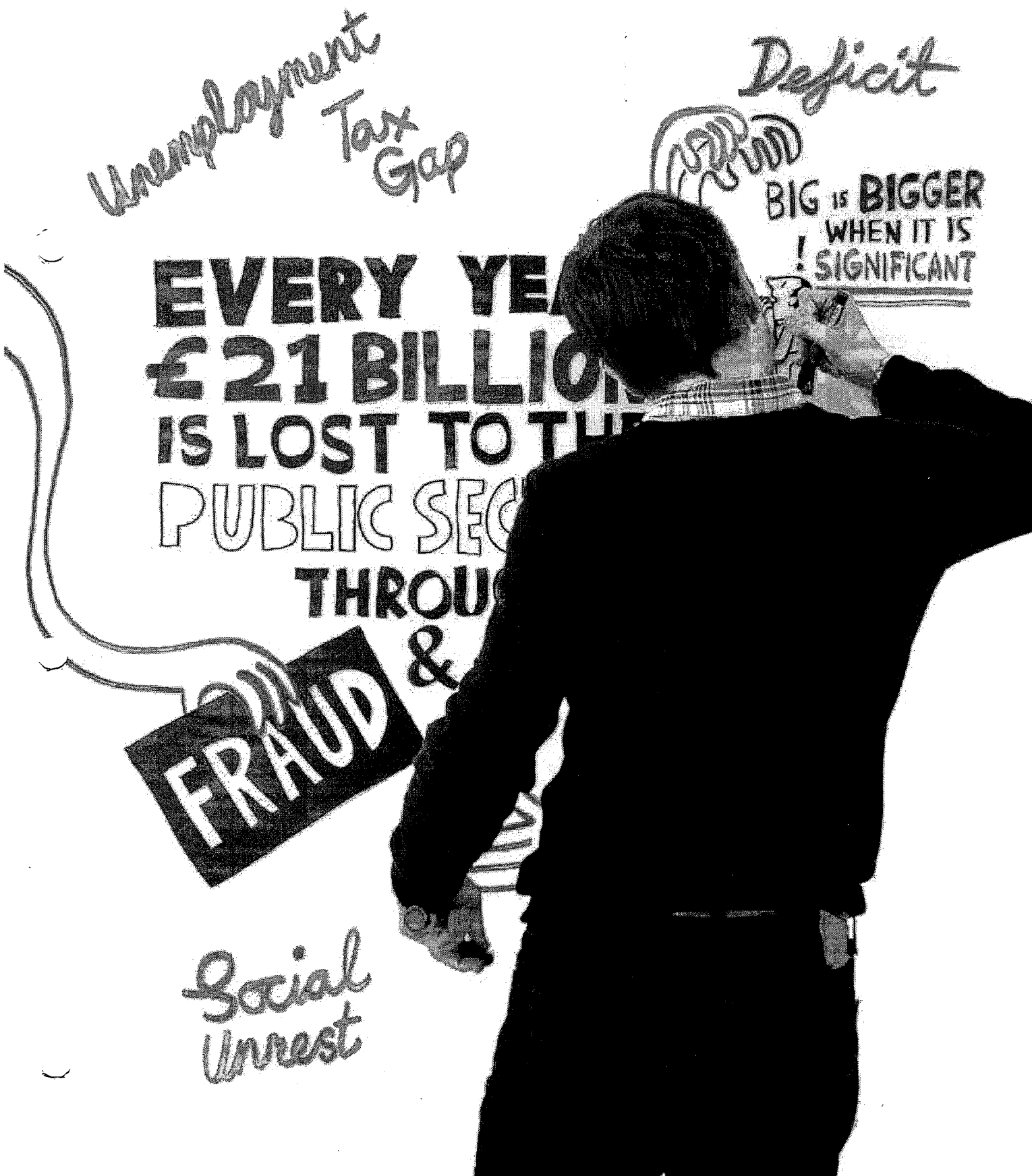


Spotlight

Deloitte
Public Finance
SUPPLEMENT ON
FRAUD &
ERROR





FOREWORD



According to the National Fraud Authority, the public sector lost £21.2bn through fraud in 2010, accounting for 55% of all fraud loss in the UK. This covers tax fraud, which accounts for the bulk of losses, but also illegal practices in the benefit system, procurement processes and expenses.

The problem is growing. Fraud losses rose from £17.6bn in the previous year. And, of course, the numbers are even more significant now with the backdrop of the UK government's fiscal deficit, rising unemployment, challenging economics and a tightening public purse.

To support public sector organisations in tackling this urgent problem, Deloitte hosted a collaborative workshop in our iZone, which is an innovative way of helping clients to step out of their comfort zones, encouraging them to come up with new ideas and solutions to their business challenges and opportunities. This was intended to help understand the scale and nature of the problem, share best practice and identify how public bodies can work to reduce the drain on valuable funds.

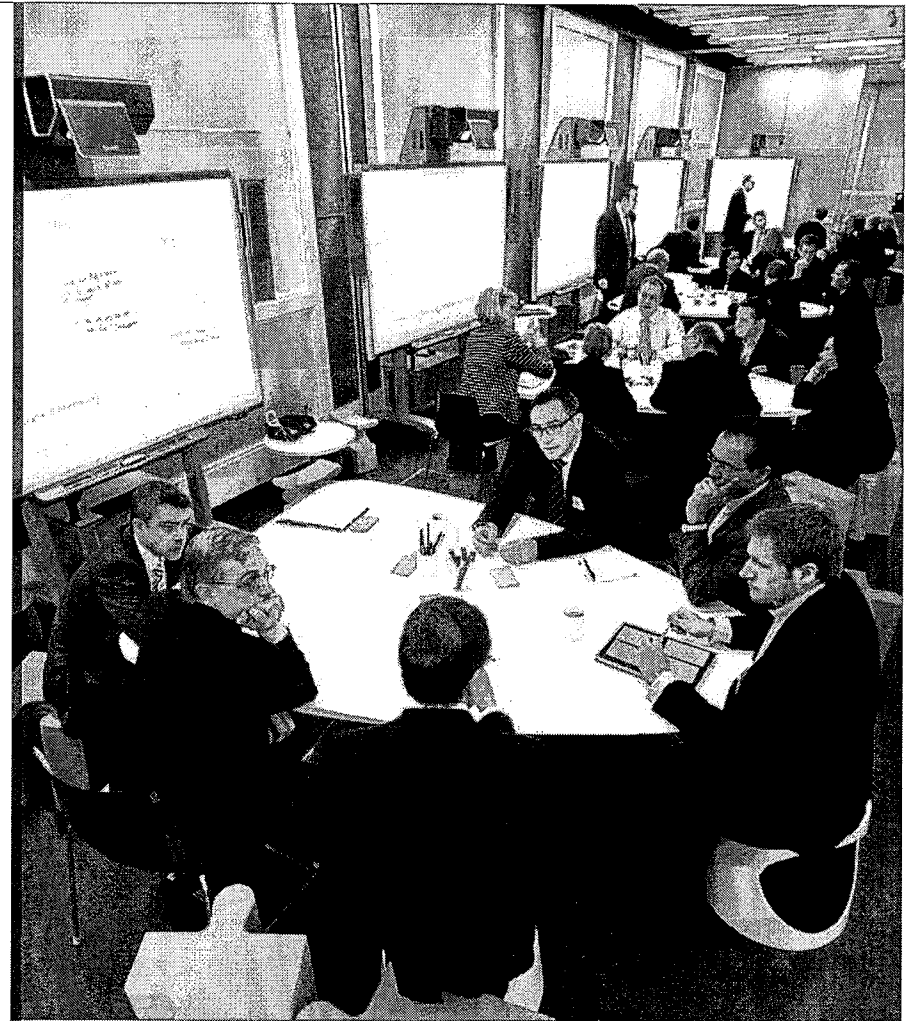
The 30 external attendees were selected in order to achieve a range of perspectives from organisations and roles, from chief information officers and directors of finance through to fraud investigation managers themselves. Despite a variety of backgrounds, all shared a common goal: to improve the identification and reduction of fraud and error within their organisations.

The workshop, which was jointly hosted with *Public Finance*, combined collaborative work with thought-provoking presentations. The morning session explored the nature and extent of fraud and error within participating organisations, assessing the barriers to its reduction and realistic scenarios for tackling the problem. The afternoon session looked at the recurring areas of concern and established a consensus for progress.

Four priority areas were identified where public sector bodies can take action to tackle fraud and error: organisational culture, awareness and identification, investment and incentive, and the importance of knowledge share. These points are developed in this special supplement.

But one of the key messages was that the responsibility for the detection of fraud and error should not just be restricted to senior management; it must be in the mindset of all employees, particularly those closest to service delivery on the front line.

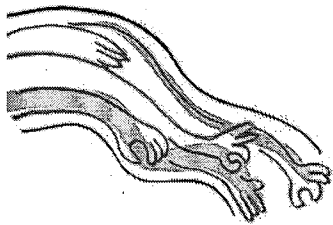
Michael Cullen,
Deloitte Partner,
Fraud & Error



ERASING ERRORS, FIGHTING FRAUD

WHAT ACTION SHOULD THE PUBLIC SECTOR TAKE TO STEM THE £21BN LOST THROUGH ERROR AND FRAUD?
ANAT ARKIN REPORTS ON THE DELOITTE/PF WORKSHOP





Participants identified organisational and cultural barriers to tackling fraud

The government is cracking down on fraud, recently unveiling plans for a counter-fraud checking service that will share data on known fraudsters with both public and private sector organisations. Details of how the new service will work have yet to be released, but it is intended to help public services check suspicious applications for benefits, tax credits and other public funds before making any payments.

Announcing the plans, Cabinet Office minister Francis Maude said: 'Criminals don't work in silos, and neither should we. A successful partnership between the public and private sectors will make a dramatic difference to the speed and accuracy of detecting fraud.'

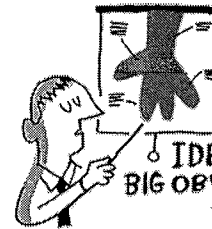
The government has already taken steps to reduce fraud, which costs public services more than £21bn a year, according to the latest estimate by the National Fraud Authority. The Fraud, Error and Debt task force

set up in 2010 has delivered savings of £72m from pilot projects, some of which involve sharing information across organisations and sectors. The task force is now developing a co-ordinated approach to tackling fraud across Whitehall and a new strategy for local authorities is due to be launched later this year.

FRAUD ON THE INCREASE
Yet despite all these efforts, losses from fraud are likely to increase if, as is widely expected, the economy dips back into recession.

This was a recurring theme at the recent Deloitte/*Public Finance* workshop, where participants, including senior public sector finance staff, counter-fraud experts and risk managers, spent a full day exploring ways of mitigating those growing risks. Two talented 'scribes' – Chris Wilson and Dan Porter from graphics firm Scriberia – captured the essence of the discussion with cartoons and captions in Deloitte's new iZone.

Speaking at the event, Tom



IDENTIFY
BIG OBVIOUS RISK
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Harris, head of research at Deloitte's public sector practice, highlighted the strong link between economic decline and fraud, predicting higher levels of fraud as unemployment continues to rise.

He warned that changes to the benefits system, such as the introduction of the Universal Credit, are also likely to be exploited by fraudsters.

"When any system is in transition there are always opportunities for people who want to commit fraud to take advantage of the uncertainty of that transition. The whole public sector is in fundamental transition at the moment and that can generate risks around fraud," he said.

Deloitte's Dame Sue Street, former permanent secretary at the Department for Culture, Media and Sport, emphasised the importance of an ethos of trust and vigilance within organisations, over and above good controls and systems.

Citing the case of a multimillion pound fraud in one of the bodies overseen by the DCMS, she said what had worked badly was the reluctance of the organisation in question to report bad news quickly and openly. What had worked well was the vigilance and persistence of a member of the frontline staff who noticed irregularities, trust among those holding senior responsibilities, and a readiness

to confront the true scale of the possible risk.

But not all public bodies are ready to admit to the risks they face. One local government officer suggested: 'Some councils have been denying for years that they had any problem other than benefit fraud, and are now finding it difficult to move from that position and tackle other types of fraud.'

ATTITUDES TO DETECTION
Other public finance professionals agreed that procurement fraud, in particular, was often ignored, despite being a growing problem across the public services.

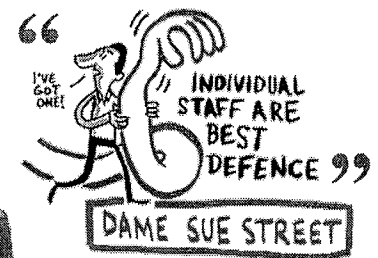
Such 'head-in-the-sand' attitudes often reflect poorly on an organisation's culture, which a straw poll of participants identified as the biggest barrier

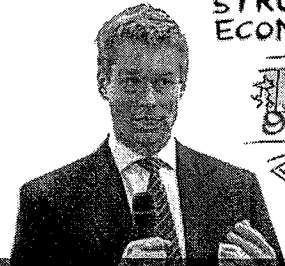
to detecting and preventing fraud. For example, it can discourage members of staff from reporting suspicious activities. Cultural factors can also inhibit public sector bodies from sharing information on fraud with other organisations, with the result that the problem is then displaced to other areas.

Detection can also be affected by society's toleration of some types of fraud. For example, tax fraud is often seen as a 'victimless crime' and therefore relatively harmless. However, the NFA estimates that losses from tax fraud come to £15bn a year – ten times more than those from benefit and tax credits fraud. One attendee argued that this was unacceptable. 'We need to change attitudes so that tax evasion becomes as socially unacceptable as smoking has become in recent years,' she said.

But the barriers to countering fraud extend beyond cultural factors to the way organisations are designed and the systems and processes they use. For example, separate departments for dealing with income and expenditure can prevent organisations from detecting fraud. When they do detect it

“ IT'S DIFFICULT TO DEFINE...
WHAT IS FRAUD
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“ **TOM HARRIS**
**STRONG LINK BETWEEN
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 BEHAVIOURS
 CHANGE WHEN
 CASH IS SHORT ”

within their own ranks, disciplinary procedures tend to go on for months. 'Meanwhile, the fraudsters stay on the payroll,' said a participant. Or it ends in legal settlements that results in the culprits 'leaving with their characters unblemished'.

There are few incentives to tackle fraud. Frontline staff are generally judged on how quickly and efficiently they complete processes, and are rarely rewarded for reporting suspicions that others may be abusing those processes. Also, as several participants pointed out, prevention, by definition, involves organisations spending money on something that has not happened, and that can be difficult to justify in these austere times.

NOT EXPENSIVE

But private sector experience shows that measures to combat fraud are not necessarily expensive. Michael Cullen, a partner at Deloitte, suggested that public services could learn from the intensity that companies bring to the task of identifying fraud. 'That's driven by the way their accounts are audited,' he said. 'So in the private sector when you audit the accounts and you have a suspicion of fraud, it goes right to the top of the tree straight away. That's what shifted over the last few years, so that there's now a specific onus on financial accounts to look for and identify fraud.'

Andrew Davies, director of public sector at credit reference

agency Callcredit, recalled that when private sector organisations were faced with 'massive bad debts' as a result of a recession and high levels of fraud, they responded by carrying out risk assessments on all potential customers – a process that is cheap and easy to get right, according to Davies.

Private sector firms also share information on fraud with each other and keep a close watch on their own staff. 'So one of the things we do in our organisation is we electronically identify all of our colleagues,' said Davies. 'We also monitor them. Given that some of our people are close to highly sensitive data... we ask how likely they are to be induced to do something they shouldn't do.'

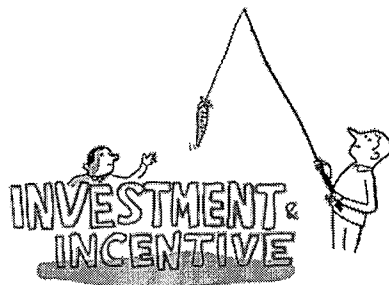
He said Callcredit had found that public services were getting significant returns on small sums of money spent on checking whether people living in social housing were entitled to be there or if individuals applying for

the single occupant's council tax discount actually lived on their own. 'What we are finding – and what the financial services have found – is that fraudsters are really loyal,' Davies said. 'So if you make it easy for them to transact with you, they will do it lots of times. Equally, they are very disloyal [if you make things difficult for them].'

Fraudsters are also resourceful, according to Kent MacKenzie, senior manager in the fraud department of Lloyds Banking Group. Outlining how his industry manages fraud, he said that banks constantly revise their strategies for detecting fraud. This enables them to keep one step ahead of the fraudsters, who quickly discover what is likely to trigger investigations and then change their tactics.

While there is much that public services can learn from the private sector's experience of countering fraud, some participants questioned whether it would be socially acceptable to rank their benefit claimants for risk in the way that banks rank their customers. There was also little appetite for delaying payments to people to perform checks on them.

Attendees recognised that fraud and error were complex



There was agreement on the need for a common understanding of the Data Protection Act

issues that did not lend themselves to quick fixes. They agreed that any attempted solutions need to be based on clear definitions of what constitutes fraud, on the one hand, and error on the other.

There also needs to be a common understanding across organisations of legislation such as the Data Protection Act 1998, which, as a result of misinterpretation, often acts as a barrier to data sharing. In fact, as several people at the workshop stressed, the law allows data to be shared for fraud prevention purposes.

INFORMATION SHARING

The discussion revealed broad agreement on the need for public services to share information with each other and with the private sector. How this could be done was more of a problem, but one suggestion was to give every person in the UK a unique reference number and set up a system enabling organisations to alert other public services whenever someone was under investigation. Only if that investigation produced evidence

of fraud would the information be shared with the private sector, which could have dire consequences for the individual's credit rating.

Participants also agreed that people at the top of organisations had a critical role to play in countering fraud. Chief executives set the tone for their organisations through their actions, and need to recognise their own accountability for the way public funds are spent when they sign off the accounts. The same goes for managers signing off expenses claims or procurement contracts.

There was widespread recognition that repeated tinkering with systems to prevent fraud sometimes creates so much complexity that it opens the door to error. 'Every time there is a benefit change, you get an anti-fraud bolt-on,' said one participant. Systems need to be robust and simple to operate if fraud is to be detected and prevented, participants concluded.

However, most thought it was staff education and training, more than anything else, that would enable public services to

tackle fraud and error. Effective training would not only help staff understand the impact that fraud and error can have on their own organisations and society as a whole, but also help them identify both problems.

The government might be coming up with grand counter-fraud strategies, but as Michael Cullen said in his round-up of the workshop: 'Sometimes individual members of staff are the best defence against fraud and error.'

