

Fraud in focus – March 2017

Fraud & Corruption in the Victorian Public Sector – learnings and insight for 2017 and beyond



Introduction

“The Victorian Public Sector has a comprehensive integrity framework with specific accountabilities and referral channels covering fraud and corruption. In particular, legislative changes occurred in 2016 providing greater scope for the Victorian Auditor General’s Office (VAGO) to audit, and the Independent Broad-based Anti-corruption Commission (IBAC) to investigate, risks of fraud and corruption.

Compliance obligations have also increased including mandatory reporting to IBAC as well as various other parties per the 2016 Standing Directions of the Minister for Finance.

With 2017 now well underway, it is helpful to consider key learnings identified from reports issued by VAGO and IBAC in recent years in order to better understand fraud and corruption risks facing the Victorian Public Sector for the year ahead, as well as to share our own insights as to challenges these present and what can be done about them.”

Shane MacDonald
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Compliance

VAGO: Performance audits 2017-18

Risks of non-compliance with legislative requirements, standing directions, best practice standards and guidelines will be assessed, particularly by the Victorian Auditor General's Office (VAGO). The VAGO Audit Plan 2016-17, includes a performance audit of fraud and corruption prevention strategies in the public sector planned for 2017-18, wherein it is stated that:

"Fraud and corruption investigations by the Independent Broad-based Anti-corruption Commission and various performance audits have found that the integrity systems intended to control fraud risks have been applied inconsistently and that these systems require regular testing"

This planned performance audit effectively extends the 2012 VAGO audit Fraud Prevention Strategies in Local Government, which concluded that:

"The five councils examined had not effectively managed their exposure to fraud risk, as none had developed a strategic and coordinated approach to controlling fraud"

Standing Directions of the Minister for Finance 2016

A significant change in compliance obligations impacting on integrity frameworks across much of the Victoria Public Sector, are the updated Standing Directions of the Minister for Finance.

In summary, from 1 July 2016 the Standing Directions require that Accountable Officers (e.g. agency heads) must immediately report significant and systemic incidents of fraud to the respective Portfolio Department. Incidents of fraud need to be reported both internally (e.g. to an audit committee) and to the government (e.g. the minister, department and the

auditor-general) together with remedial plans. Critically, Chief Executive Officers and Chief Financial Officers are now personally accountable for strong financial management in accordance with the Standing Directions.

In addition and in accordance with transitional arrangements *Standing Direction 1.4.3*, from 1 July 2017 Responsible Bodies (e.g. governing boards) must have established a Fraud, Corruption and Other Losses prevention and management policy that is implemented across the agency.

Whilst it is not mandatory for local councils to adhere to the Standing Directions, it is always good practice to at least consider and potentially adopt industry best practice.

IBAC: Mandatory reporting

Effective from 2 December 2016, the relevant principal officer of a Victorian public sector body must notify IBAC of any matter they suspect on reasonable grounds to involve corrupt conduct occurring or occurred.

The 'principal officer' is the Head of the public sector body, the Chief Executive Officer of a council and of Court Services Victoria. Public sector bodies include departments, state government or statutory authorities and corporations.



Whilst proof of corrupt conduct is not required, the principal officer's suspicion must be based on facts and circumstances that would be sufficient to make a reasonable person suspect corrupt conduct.

Key learnings

We have reviewed conclusions and recommendations from several audits and investigations by VAGO and IBAC respectively and identified below common opportunities for Victorian Public Sector Bodies to strengthen their integrity frameworks to mitigate risks of fraud and corruption:







- Risk assessments
- Controls
- Employee screening
- Training & communication
- Reporting
- Leadership

<p>March 2017 IBAC Operation Liverpool Bendigo Health</p>	<ul style="list-style-type: none"> • Review integrity and corruption prevention policies and procedures in the following areas to ensure they have been addressed, and that employees fully understand their obligations: <ul style="list-style-type: none"> - code of conduct and values - gifts, benefits and hospitality - conflict of interest - audit and risk management - procurement - asset management - information security, particularly in relation to tendering information for major projects. • Consider the introduction of a 'declarable associations' policy to require employees to identify, declare and manage associations that may be incompatible with an employee's professional responsibilities 	● ●
<p>March 2015 IBAC A review of integrity frameworks in six Victorian councils</p>	<ul style="list-style-type: none"> • It is important councils maintain sight of corruption risks, particularly in risk-assessment models that are incorporated into business processes and focus on impediments to achieving operational objectives. Perhaps more importantly, once risks are identified, appropriate controls must be implemented and actively monitored to ensure risks are being managed effectively • Other areas for improvement included possible refinement of management's approach to leadership to ensure there is an appropriate balance between developing a values-based organisational culture and enforcing relevant controls, recognising that neither should be pursued to the exclusion of the other • Councils could do much more to broadcast their intolerance of misconduct and corruption. Key statements of ethical practice could also be tailored to ensure relevant stakeholders understand council's position on corruption-related issues such as gifts, bribes and conflicts of interest, making it clear that council will not tolerate corrupt activities • In order to encourage reports of suspected corruption, management must reassure employees they will not be penalised and they do not need hard evidence to make a report, and take appropriate action in response to reports that are made." 	● ● ● ● ●
<p>June 2012 VAGO Fraud prevention strategies in local government</p>	<ul style="list-style-type: none"> • Develop and maintain an up-to-date fraud control plan clearly documenting their fraud prevention, detection and response initiatives and responsibilities • Conduct thorough, periodic fraud risk assessments to assure they identify and effectively manage all major fraud risk exposures • Provide induction and periodic fraud awareness training to all council staff, to assure they understand their fraud control responsibilities • Systematically monitor and report on the effectiveness of their fraud control strategies • Establish arrangements that assure effective ongoing scrutiny by executive management, internal audit and audit committees, of the effectiveness of the fraud control framework • Establish effective pre-employment screening processes that provide sufficient assurance over the integrity, identity and credentials of all council staff • Make sure accounts payable systems have effective preventative and/or compensating 	● ● ● ●

	<p>controls that adequately mitigate the risk of fraudulent purchases and/or payments</p> <ul style="list-style-type: none"> • Maintain accurate and an up-to-date asset registers that are regularly reviewed to mitigate the misuse and/or misappropriation of asset • Systematically review the operation and effectiveness of all their internal control systems to assure they adequately prevent, deter and detect major frauds. 	
<p>October 2014 IBAC Operation Fitzroy Public Transportation Victoria</p>	<ul style="list-style-type: none"> • Processes for employees and contractors to raise concerns (potential and actual) about procurement misconduct and corruption, and that these processes are effectively promulgated (in an ongoing manner and not just as one-off activities) • Controls over sub-contracting arrangements, and that integrity and other risks associated with sub-contracting are effectively identified and managed. • Controls to ensure suppliers have the requisite skills, qualifications, financial viability and experience to deliver the required goods and services • Mechanisms to engage with suppliers regarding procurement policies and procedures, probity obligations, standards and requirements • Processes for screening prospective employees in potentially high risk positions related to finance and procurement, and that validation of screening occurs on a regular basis for appointed employees • Ongoing training for all relevant employees regarding procurement policies and procedures, and associated corruption risks 	
<p>April 2016 IBAC Operation ORD Department of education and training</p>	<ul style="list-style-type: none"> • Employees' understanding of and compliance with public sector values and the code of conduct, and departmental policies and procedures related to conflicts of interest, declarable associations, and gifts and benefits • Employment policies and practices, including pre-employment vetting of prospective employees and regular revalidation for employees in identified positions, the potential for rotation of employees in identified positions and executive roles, and any steps taken to improve disciplinary and dismissal processes for employees found to have engaged in serious misconduct or corruption • Financial management, procurement and contracting systems and controls, and associated employee training and compliance measures • School governance and financial management arrangements, including the proposed new model to deliver 'shared services' to schools (i.e. any new approach to program coordinator schools) and relevant policies, procedures and other controls • Audit and risk management programs to provide assurance in areas of identified risk • Mechanisms to encourage and support employees to speak up and report suspected misconduct or corruption, and to ensure appropriate assessment, escalation and investigation of such matters • Leadership and management programs to ensure executives are accountable for modelling integrity and public sector values, and to set the right tone. 	

Insights

Grant Thornton's forensic practitioners share their own insight into key learnings and opportunities to increase the effectiveness of public sector integrity frameworks:

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Risk assessments Too often we see they are not been done appropriately. They must be conducted regularly and as material organisational changes occur, which identify and assess specific fraud and corruption risks and critically their residual risk, which are communicated to and understood by those charged with governance of those bodies. They also need to be tailored for the organisation and not an "off the shelf" generic product.
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Controls Too often we see internal controls are not adequately aligned to the organisations fraud and corruption risks, including where accepted practices mean controls don't exist, are overridden or ignored
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Employee screening Many frauds and incidents of corruption could have been prevented by stronger screening of not just employees but also contractors and suppliers to avoid those with integrity risks from been employed or engaged from the outset
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Training & communication Policies and procedures for managing fraud and corruption risks are often not adequately communicated through training and other communications, including communicating instances of enforcement of non-compliance which is often an effective deterrent
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Reporting We have seen indicators of possible over reliance on Protected Disclosures as the mechanism for people to report suspected fraud, corruption and other potentially serious misconduct. There is an opportunity for a 'safety net' for people to report their concerns of potentially serious misconduct that falls outside the scope of the Protected Disclosure Act 2012. This includes reporting of serious misconduct suspected to have been perpetrated by contractors and suppliers to public sector bodies which may or may not involve fraudulent or corrupt conduct by a public sector employee
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Leadership Managing risks of fraud and corruption is a responsibility for everyone, not just senior leaders in organisations and reliance on 'tone from the top'.

Challenges

Culture

There are a significant variety of Victorian Public Sector bodies impacted by risks of fraud and corruption and no two organisations are the same. On its own, a culture of compliance is typically not sufficient to adequately mitigate risks of fraud and corruption. What is required is a culture whereby people **want** to do the right thing regardless of rules and penalties.

In reality, there needs to be a balance of adequate compliance obligations, principles and values all of which are driven by strong leadership from all employees.

Organisations cannot just rely on “tone from the top”; everyone can and should be a leader within their organisation by influencing others in terms of acceptable behaviours.

Reporting

Victorian Public Sector bodies are still faced with a significant challenge of identifying what to report and to whom as follows:

- IBAC mandatory reporting requires that principal officers must know the facts and circumstance which support their suspicion of corrupt conduct for reporting to IBAC. But how are these facts and circumstance to be determined?
- Without at least some form of initial assessment or indeed investigation by a Victorian Public Sector body, it can be difficult to determine who to report or refer a matter to, which can be one or more of IBAC, VAGO, Victoria Ombudsman, Victoria Police and the Local Government Investigations and Compliance Inspectorate.

In addition, sometimes fraudulent and corrupt conduct impacting on the Victorian Public Sector can involve potential offences under Commonwealth laws, especially as they may relate to the conduct of private sector individuals and corporations. In such circumstances, obligations can exist for reporting matters to the Australian Federal Police, the Australian Securities and Investments Commission, Australian Transaction Reports and Analysis Centre, the Australian Competition and Consumer Commission and the Australian Criminal Intelligence Commission.

In addition, given the varying resources, size, complexities and other circumstances impacting on numerous bodies covered by the Standing Directions, there will be various degrees of readiness for compliance, including non-compliance.

Accordingly, Victorian Public Sector bodies need to have access to sufficient resources and expertise to conduct preliminary assessments of suspicions and/or allegations of misconduct so that they can identify and report the facts and circumstances to the appropriate authorities.

Actions

There are practical and cost effective steps that Victorian Public Sector bodies can take to help meet their compliance obligations and better practice in the prevention, detection and response to risks of fraud and corruption. Whilst not intended to be an exhaustive list applicable to every Victorian Public Sector Body, we summarise some of the most common actions that should be undertaken as follows:

Action	Description
Gap assessment	<p>Assessments should be done to identify gaps in existing integrity frameworks benchmarked against:</p> <ul style="list-style-type: none"> • IBAC mandatory reporting obligations • Standing Directions of the Minister for Finance • Australian Standards, including 8001-2008 Fraud & Corruption Control, 4811-2006 Employee Screening and 8004-2003 Whistleblowing Protection Programs for Entities
Risk assessment	<p>Assessment of risks of fraud and corruption should be conducted to identify and assess the likelihood and consequences of risks occurring and determine the residual risk with reference to ISO 31000 Risk Management – Principles and Guidelines</p>
Remediation	<p>Remediation plans need to be established and actioned to implement new or strengthened internal controls proportionate to assessed gaps, risks and compliance obligations, as well in response to actual incidents of fraud, corruption or other loss</p> <p>This will need to include tasks required to strengthen existing policies or even to establish and implement new policy such as required by the <i>Standing Direction 3.5.1 (b) Fraud, Corruption and Other Losses prevention and management policy</i></p>
Whistleblowing programs	<p>Whistleblowing programs including independent hotline reporting services, should be implemented to provide a 'safety net' support for employees, contractors, suppliers and the community for providing information in addition to protected disclosures covered by the Protected Disclosures Act 2012</p>
Communication & training	<p>It is imperative that the organisations tolerance for misconduct is consistently and effectively communicated to employees, contractors and suppliers, including information on accountability and enforcement</p> <p>It is also critical that adequate training be provided on a regular and tailored basis supporting by awareness and satisfaction surveys to help ensure people know how to recognise unacceptable conduct and how to respond to it</p>

Grant Thornton Australia Ltd

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Grant Thornton has a dedicated Public Sector Advisory practice, which is supported by teams of subject matter experts covering such key areas as leadership and culture, performance improvement, financial viability and restructuring, financing and due diligence, risk advisory and forensic consulting.

Our forensic consulting team include subject matter experts in fraud and corruption risk management and investigation, drawing from employment experience with Big 4 and boutique consulting firms, the Australian National Audit Office, the Australian Securities and Investments Commission, the WA Corruption & Crime Commission and the Victoria Police fraud squad.

Our team have advised and assisted Victorian Public Sector bodies with the following forensic services:

- Fraud & corruption gap assessments
- Fraud & corruption risk assessments
- Fraud & corruption awareness training
- Whistleblowing hotline reporting services
- Review of and updating fraud & corruption control plans
- Preliminary assessment of suspicions or allegations of serious misconduct
- Forensic audits and compliance reviews, particularly procurement and contract management activities
- Fraud and corruption investigations
- Conflict of interest investigations

In addition to the above forensic services, Grant Thornton assists public sector organisations with broader services including:

Governance & Compliance

- Internal audit
- Statutory and financial statement audits
- Technical accounting advice and training
- Governance and enterprise risk management
- Policy strategy governance
- Organisation design & implementation

FBT & Remuneration

- Salary packaging policies and implementation
- Fringe benefits tax technical issues, systems and compliance procedures
- Remuneration structuring

Financial & Operational Advisory

- Financing and financial modelling
- Transaction advisory & due diligence
- Restructuring & change management
- Operational improvement and effectiveness

Leadership, Talent & Culture

- Leadership & cultural transformation
- Talent & capability

Technology

- Technology audit & reviews
- IT security
- Technology strategy & optimisation

For further information, please contact

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