

# Fraud in the Public Sector

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Even though there are signs that the worst of the recession may be over, this new report by PricewaterhouseCoopers (PwC) warns of the increased risk of fraud in the public sector as staff reductions increase the risk of fraud and economic crime.

## Fraud in the public sector now in the spotlight - are you prepared?

The report ‘Fraud in the public sector’, analyses the responses of senior representatives from government and state-owned enterprises across the world, including Ireland. Over a third (37%) of respondents reported that their organisation had suffered economic crime in the last 12 months. Of these, over two-thirds (69%)

reported asset misappropriation and nearly a third (28%) reported incidents of financial statement fraud.

Most respondents believe their organisations are at greater risk to fraud in the current economic environment. The survey reveals that the top reason for an increased risk of economic crime in the current environment is the fear of staff reductions. With further spending cuts expected in the coming months, this risk is set to increase further and organisations must ensure that they are ready to face this challenge. There is increased vulnerability as staff reductions mean fewer resources being spent on internal controls and internal auditors are being asked to do more with less.

According to Bob Semple, Partner, PwC “Our experience tells us that increased economic pressures directly affect peoples’ ability to rationalise fraudulent actions. And we know that these pressures are going to be felt sharply in the public sector in the coming years.”

The report also finds that public sector fraud has a disproportionately negative effect on reputation, employee morale, business relationships and relationships with regulators. Organisations need to make sure that they have regular reviews and the right fraud prevention and detection policies in place.

### Who is committing fraud?

Organisations that suffered from economic crime reported that 57% of perpetrators were internal and 37% were external. Government organisations participating in the survey revealed that nearly half (49%) of internal fraudsters were junior management with a quarter (24%) being senior management. Organisations must ensure that they are not under-estimating either the cost or the collateral damage caused by internal fraudsters.

Nearly three-quarters (71%) of respondents attributed greater risk of fraud to increased ‘incentives or pressures’. The most commonly reported factor contributing to these increased pressures was that ‘people are afraid of losing their jobs’ (41%).

### How is fraud detected?

The fact that a relatively large proportion of frauds for government/state-owned organisations were detected by accident (14%) and only 5% uncovered through formal whistle-blowing procedures reinforces the need for internal fraud prevention know-how and/or fraud prevention procedures. 45% of organisations detected fraud through informal procedures via tip-offs (both external and internal).

Furthermore, even though the majority (61%) of government/state-owned enterprises had performed a fraud risk assessment during the year, only 5% of frauds were detected by fraud risk management procedures. Robust fraud risk assessments are essential for identifying potential weaknesses in controls that create opportunities to commit fraud. Government/state-owned enterprises are under

increasing pressure to cut costs and deliver efficiencies. This pressure can only become even more onerous in the current economic climate. There is a danger that as fewer resources are employed in the fight against economic crime, more frauds will go undetected.

### Disciplinary action and prevention – key steps

The survey also revealed that only half (51%) of internal fraudsters in the public sector faced dismissal. This lack of visible action may send the message to other staff that this type of behaviour is tolerated by management. There is also the risk that employees who have been disciplined in one part of the public sector, but not dismissed, may go on to work for another area without hindrance and continue their fraudulent behaviour elsewhere.

Bob Semple, Partner, PwC Ireland concluded “The best way to address these increased threats is to carry out a comprehensive fraud risk assessment. In practice, that is the only way those responsible for governance can be sure they have discharged (and can be seen to have discharged) their duties.”

## Appendix

Figure 2: Types of economic crime experienced by government/state-owned enterprises who reported experiencing fraud in the past 12 months

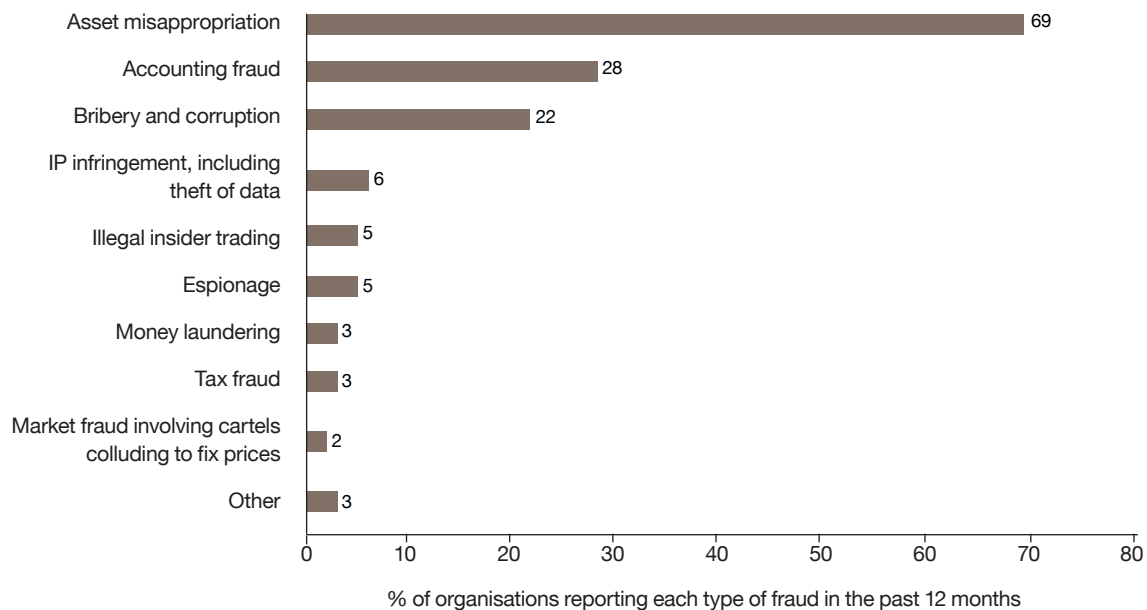


Figure 5: Factors given by respondents from government/state-owned enterprises as contributing to increased incentives to commit fraud

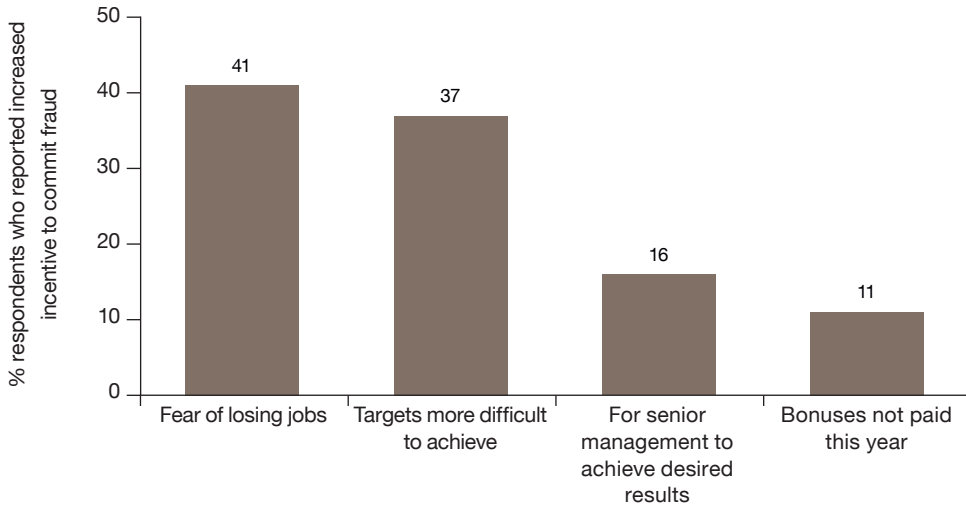
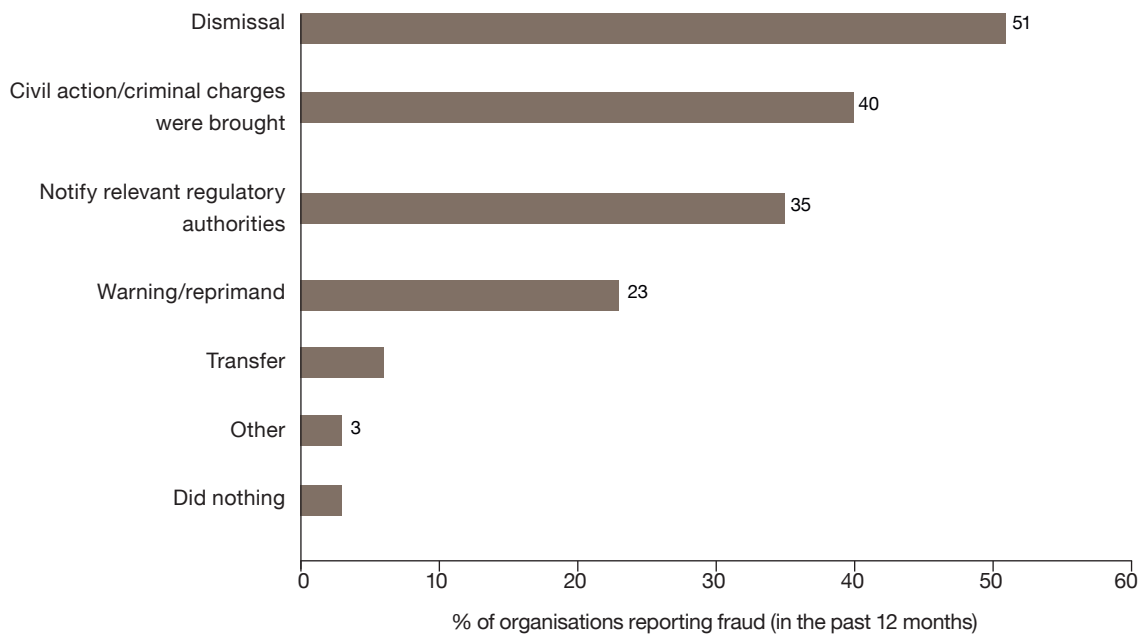


Figure 7: Actions taken against internal fraudsters by government/state-owned enterprises



A comprehensive fraud risk assessment should:

- Identify the potential inherent fraud risks;
- Assess the likelihood and significance of occurrence of the identified risks;
- Evaluate which people and departments are most likely to commit fraud and identify methods they are likely to use;
- Identify and map existing preventative and detective controls to the relevant fraud risks;
- Evaluate whether relevant controls and processes are effectively designed to address identified fraud risks;
- Identify and evaluate residual fraud risks resulting from ineffective or non-existent controls; and
- Respond to residual fraud risks.

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