



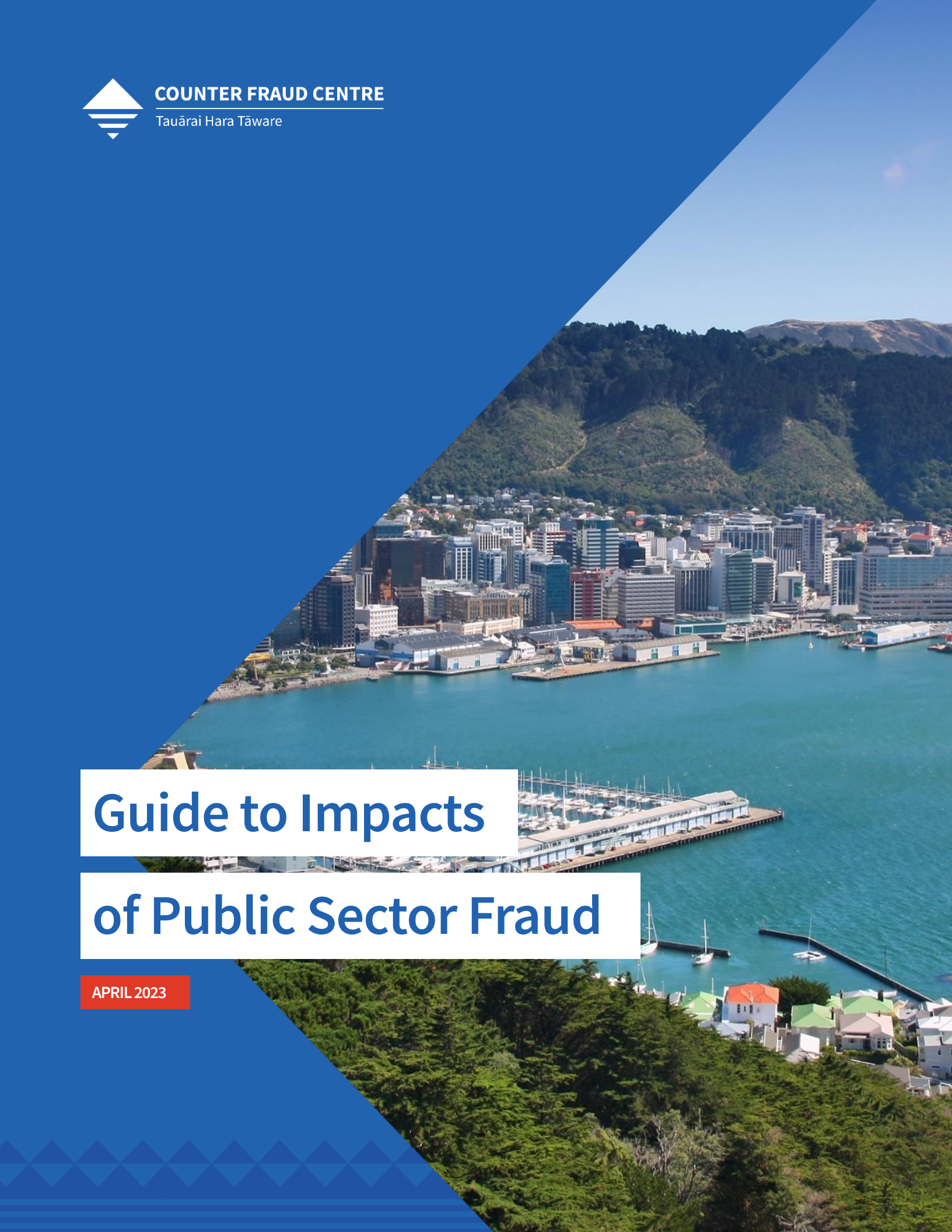
COUNTER FRAUD CENTRE

Tauārai Hara Tāware

Guide to Impacts

of Public Sector Fraud

APRIL 2023



Impacts of Public Sector Fraud

This guide is designed to assist organisations to identify the key impacts of fraud. It provides examples of what the impacts could look like to individuals, whānau and organisations; and identifies key questions you can ask about impact of fraud on your operations or programme.

Fraud impacts on people, industries, public bodies, services and the environment. Having a detailed understanding of the real impact of fraud, and not just the financial impact, helps the public sector to have a better understanding of the risk environment and make more informed decisions to prevent it.

Through the SFO's work in investigations and prosecutions, and collaborating with our international counterparts, we have identified nine key impacts of public sector fraud.

Not all impacts will be relevant to every public body and/or programme but knowing them could be beneficial for planning your key prevention activities.

<u>Human</u>	Fraud against public bodies is not a victimless crime. Fraud can be a traumatic experience that often causes real and irreversible impacts for victims and their whānau.
<u>Government Outcomes</u>	Fraud against the public bodies compromises its ability to deliver services and achieve intended outcomes.
<u>Government System</u>	Fighting fraud drains resources across key areas such as welfare, health, education, national security and justice.
<u>Environmental</u>	Fraud against public bodies can lead to immediate and long-term environmental damage through pollution and by damaging ecosystems.
<u>Industry</u>	Fraud against public bodies can result in distorted markets where fraudsters obtain a competitive advantage and drive out legitimate business.
<u>Reputational</u>	If fraud against a government programme is handled poorly, it can result in an erosion of trust in government and institutions, and lead to a reduction in New Zealand's international reputation.
<u>Security</u>	Fraud against public bodies can compromise national defence and security, putting New Zealanders at risk.
<u>Business</u>	Fraud against government programmes can result in significant business costs that go well beyond the direct financial loss.
<u>Financial</u>	Based on international estimates, fraud against public bodies can result in the loss of between 0.5% and 5% of their spending.



Human Impact

Public bodies exist to improve the lives of the citizens they serve. Taking into consideration the human impact of fraud will help you to approach fraud in a way that is more meaningful to members of the public.

While the direct financial loss is borne by public bodies, behind every story of fraud, there are real individuals, whānau and communities whose lives have been impacted or even destroyed. The damage to these individuals can be financial, physical, or mental.

Opportunistic individuals and serious organised crime groups target public bodies, including programmes designed to assist vulnerable people, with little regard for the victims of that fraud.

What impacts can look like

- ▶ **Direct impacts on those who rely on government services:** Fraud committed against public bodies can have direct financial, social, physiological and mental health impacts on those who rely on government services and are not able to access them.
- ▶ **Identity theft:**
Fraud against public bodies can result in individuals having their identity stolen. This can have long term impacts, exposing the person to re-victimisation and potentially impacting their eligibility for services or benefits that they are reliant on.
- ▶ **Family and community impacts:**
Fraud can have far-reaching impacts beyond the individual, causing stress and disruption to families and carers as they try to help resolve the situation.
- ▶ **Physical safety:**
Fraud can put people's lives or health at risk by denying them essential services, or exposing them to unsafe activities, items or environments.
- ▶ **Damage to reputations:**
Fraud can damage people's professional reputations and erode trust in individuals and organisations.

Key questions to ask

- ▶ What would be the potential human impacts if your programme was defrauded?
- ▶ Could fraud against your programme result in mental health problems, psychological or emotional problems by individuals who should be benefiting from your programme?
- ▶ If fraud diverted money out of your programme, would the victims of fraud miss out on services, opportunities or payments they rely on?
- ▶ Could fraud against your programme impact on the family or carers' of individuals who should be benefiting from your programme?
- ▶ Could fraud against your programme result in financial stress or further fraud against individuals who should be benefiting from your programme?
- ▶ Could fraud against your programme put people's health or lives at risk?
- ▶ What more can your organisation do to take into account the human impact of fraud?

Example

In New Zealand, a government funded charitable trust set up to provide community services to people with intellectual disabilities was defrauded. The misappropriation of funds resulted in individuals with mild to challenging intellectual disabilities not receiving the engagement that was intended to improve the quality of their lives. The decreasing quality of service provided by the trust over time caused distress to the individuals accessing services, which in turn imposed additional emotional burdens on their caregivers.

In the United Kingdom, fraudsters were convicted of claiming £775,000 from a government fund that was created for victims of the Grenfell Tower tragedy. This fraud diverted money from victims of the tragedy who have been left homeless and added to the distress of victims of the disaster.



Government Outcomes

Fraud against public bodies compromises the government's ability to deliver services and achieve intended outcomes. Money and services are diverted away from the intended targets and the services delivered can be substandard or unsafe.

This can lead to programme failure. It also leads to lost opportunities for individuals and businesses.

<p>What impacts can look like</p>	<ul style="list-style-type: none">▶ Key services not delivered: Money and resources are diverted away from the intended target, or services are not delivered to the standard required.▶ Programme objectives not met: The vision, goals and objectives of programmes are compromised or not met.▶ Programme or services shut down: In some circumstances programmes and services are shut down, which can negatively impact those relying on that service.▶ Negative customer/client experience: The customer/client experience is compromised. <p>Opportunity costs: Lost opportunities for a programme or service if it is shut down because of fraud or constrained by financial losses and the business costs of responding to fraud.</p>
<p>Key questions to ask</p>	<ul style="list-style-type: none">▶ If your programme was defrauded, how would this impact on government outcomes?▶ Could fraud result in services not being delivered? Which services? What would the impact be?▶ How would fraud impact your programme's objectives and outcomes?▶ Could widespread fraud result in your programme being shut down or restructured?▶ If the money had not been diverted by fraud, what impact might it have had?▶ What, if any, impact would there be on the delivery of services by other parts of the government or partners involved in your programme?

Example

In New Zealand, fraud was committed against a government funded Māori immersion school. The misappropriation of funds diverted government resources that were intended to improve educational outcomes for students. The specific goal of revitalising Māori language, culture and knowledge through developing and expanding institutions (like Māori immersion schools) was not met. The broader government goal of improving educational outcomes for Māori students was undermined.

In the United Kingdom, a law firm created thousands of legal aid cases which never took place. An investigation found that out of the 24,658 mental health tribunal cases claimed for, a legal hearing had only been held for 1,485 of them. The firm had a turnover of over £11 million annually and £8 million of this turnover came from the public purse. Fraud like this diverts government money from being used for its intended purpose.



Government Systems

Fighting fraud drains government resources across multiple key areas such as welfare, health, education, trade, national security and justice.

The occurrence of fraud can result in costs and capacity being drained across a wide range of government systems and services.

Finite resources are diverted to deal with fraud responses and outcomes. This reduces governments' abilities to deal with other issues.

What impacts can look like

- ▶ **Drain on investigations and compliance agencies:** Public bodies with compliance and investigatory functions, including police and law enforcement, have finite resources.
- ▶ **Drain on prosecution services, courts, tribunals and legal aid:** Court proceedings and legal representation are extremely expensive and there can also be victim support costs.
- ▶ **Drain on prison system:** If prosecution of fraudsters leads to conviction, this results in prison costs.
- ▶ **Drain on welfare system:** Fraudsters who are caught may move to government welfare and other services for support and assistance. This results in additional costs on welfare and other government services.
- ▶ **Drain on identification system:** Identity fraud can lead to costs for authorities that regulate passports, permits and licences, eligibility to other programmes, vetting systems and other person checks.
- ▶ **Fraud against other public bodies:** Where a fraudster has been accepted as a service provider, programme recipient or employee in one public body, the documents generated can be used as proof of identity by another public body. Fraud occurring against one public body can enable fraud against another.

Key questions to ask

- ▶ If your programme was defrauded, how would this impact on government services?
 - ▶ If your programme was defrauded, how would this impact on other public bodies? What would be the impact on the law enforcement and compliance system? What would be the impact on the prosecution service, the courts, tribunals and legal aid system? What would be the impact on the prison system?
 - ▶ What would be the costs of retrofitting controls to your programme?
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Example

In the United Kingdom, a husband and wife were found guilty of property fraud totalling £1.6 million. Between them they were convicted of 31 charges. Over a two-year police inquiry, 48 properties were investigated under a property fraud scheme. The trial heard evidence for 320 days and was said to have cost around £7.5 million, including more than £2.4 million in legal aid paid for defence.

In the United States, a building product supply company provided unsuitable and unsafe tools to a construction company that was contracted to build a tunnel. This resulted in a ceiling collapse which resulted in service disruption, as well as loss of life.



Environmental

Fraud against public bodies can have an impact on the environment. Environmental damage can be immediate and direct, such as increasing levels of pollution, reducing biodiversity and disturbing ecological balance. These impacts can be medium to long term, or in some cases irreversible. Environmental impacts also include any clean-up and maintenance costs.

Fraud can also undermine efforts and the real or perceived effectiveness of green measures to improve the environment.

Studies have found that in countries where there are higher levels of fraud and corruption, environmental sustainability decreases.

<p>What impacts can look like</p>	<ul style="list-style-type: none">▶ Environmental harm and damage: Increased levels of pollution, reduction in biodiversity and irreversibly disturbed ecological balance.▶ Drain on resources: Clean-up and maintenance work can use a significant number of public resources.▶ Health risks to communities: Communities may face serious immediate and long-term health risks if unqualified organisations are awarded work, especially when people are relying on projects being delivered safely.▶ Damage to environmental protection image: The effectiveness of green measures to improve the environment, either real or perceived, can be undermined.
<p>Key questions to ask</p>	<ul style="list-style-type: none">▶ If your programme was defrauded, what environmental impacts may result? Would there be any immediate environmental damage? Would there be any medium to long term environmental impact?▶ Could fraud lead to any clean-up costs or ongoing environmental maintenance costs?▶ Could fraud in your programme undermine green initiatives?

Example

In New Zealand, an alleged corruption occurred within a local government body in relation to the awarding of a contract for an important local infrastructure project. The tender process under scrutiny resulted in the contract being (initially) awarded to an unqualified organisation and risked serious immediate and long-term health risks to the community who were relying on this project being delivered safely.

In the United States, contractors substituted “clean dirt” for legitimate soil samples in order to fake the results of radiological remediation efforts at a former Navy shipyard. The falsification and potential public exposure to radioactive material at and near the shipyard put the community and environment at risk.



Industry

Fraud against public bodies can have a flow-on impact on legitimate business and industry as a whole.

Fraud can affect services delivered by business and expose other sectors to further instances of fraud. It can also result in greater burdens on charities and community services who assist those affected by fraud against public bodies.

What impacts can look like

- ▶ **Market distortion and competition:** Fraudsters can gain a competitive advantage by engaging in fraudulent conduct which leads to legitimate competitors being priced out of the market. Fraud can also result in disruption to supply chains.
- ▶ **Services not being fit-for-purpose:** When fraudulent conduct leads to market distortion and competitors closing down, recipients can be left with no or limited service options.
- ▶ **Exposure of other industries and sectors:** Fraud against public bodies can expose other sectors to risk, such as the banking and insurance sectors.
- ▶ **Extra burdens placed on community services:** Community services and charities can have extra burdens placed on them by fraud victims who seek out additional support.
- ▶ **Increased regulation:** Fraud within an industry can lead to additional regulation and legitimate businesses bearing the cost of additional checks and processes.
- ▶ **Compliance resources impact:** Industrywide fraud can use up capacity within an industry for compliance assessments and checks.
- ▶ **Compromised industry integrity:** Where there is systemic fraud the integrity of the entire industry can be compromised, and legitimate businesses tainted merely because they are part of an industry.

Key questions to ask

- ▶ If your programme was defrauded, how might this impact on industry? Would other industries and sectors be exposed, or their integrity impacted?
- ▶ Could fraud result in market distortion or impact legitimate competition in business? What would be the impact on services provided and supply chains? What would be the wider system impact?
- ▶ Would regulation be needed to deal with systemic fraud if it occurred in an industry?

Example

In the United Kingdom, a group of education agents working at a number of government funded private colleges provided students with bogus qualifications in exchange for a share of their student loan. For a fee students could fake their attendance at lectures, have their coursework completed by agents in another country and receive a formal qualification. This resulted in unqualified individuals being appointed in jobs they were not qualified or trained to do.



Reputational

Fraud happens and can affect any public body. However, when it is handled poorly, fraud against government programmes can result in an erosion of trust in New Zealand's public institutions. This in turn can lead to a loss of international reputation. This is particularly true when fraud is facilitated by corruption.

Public bodies that proactively manage their risks may be less vulnerable to reputational harm and can use their response to build confidence with other public bodies and industries, customers, the public and politicians. However, reputational harm occurs when fraud could have been prevented or is mismanaged.

What impacts can look like

- ▶ **Erosion of trust in government:** Significant fraud against a public body may result in the general erosion of trust in government and integrity of the public sector. This can negatively impact how people conduct business at personal, industry and regional levels. Other parties may not trust government with information, may feel a lack confidence in the government's ability to deliver programmes or policies, or view government as a soft target for further exploitation.
- ▶ **Erosion of trust in industry:** Fraud can result in not only loss to government but can have further impacts on industry. Legitimate businesses can be tarnished by association in an industry where fraud has occurred against a government programme.
- ▶ **Decrease in employee morale and performance:** Knowledge of fraud occurring against or within the public sector can reduce employee morale and performance. This decreases productivity and can compromise organisational culture. This can also lead to a culture of non-compliance where some level of fraud is seen as acceptable.
- ▶ **Damage to international reputation:** Fraud can impact the international reputation of countries. Widespread fraud can be a contributing factor in assessments of whether a country is safe to conduct international trade and business, particularly where this is combined with corruption.

Key questions to ask

- ▶ If your programme was defrauded, what could be the reputational impacts?
 - ▶ Could fraud result in a loss of reputation or erosion of trust in your programme and organisation?
 - ▶ Could fraud against your programme lead to an erosion of trust in government as a whole? What would be the effect of an erosion of trust?
 - ▶ Could there be reputational impacts to industry or your international reputation?
 - ▶ What would be the impact on employee morale and productivity?
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Example

In the United States, a Department of Motor Vehicles employee and trucking school owner fraudulently issued commercial driving licenses to truckers who did not pass the required tests. People with fraudulent commercial licenses were driving passenger buses, tractor-trailers, and trucks hauling hazardous materials on interstates all over the country. The agency's failure to prevent unqualified drivers from receiving these licenses affected citizens' trust in the agency, as well as public safety.

In the United Kingdom, a council Mayor was removed from office after an election was overturned, due to evidence of vote-rigging and malpractice. An investigation found that ballots were double-cast or cast from false addresses. This case resulted in a drop in public confidence of those in trusted positions.



Security

Fraud against public bodies can compromise national defence and security, putting service men and women, and citizens at risk. It can also damage international standing. Fraud against government programmes can be used to fund organised crime groups and terrorism, potentially leading to further crime and terrorist attacks.

Fraud can compromise national security and community safety when perpetrated by organised crime groups and terrorist groups. It can also compromise border security resulting in biosecurity risks and enabling trafficking of illegal goods.

What impacts can look like

- ▶ **National defence is compromised:** Where fraud compromises security, it can impact a nation's ability to effectively defend its sovereignty and its citizens. This can put the lives of its service men and women, as well as citizens, at risk.
- ▶ **National security is compromised:** Fraud can compromise national security and community safety when perpetrated by organised crime groups and terrorist groups.
- ▶ **Damage to international standing:** Fraud can result in a country's falling in international standing, for example where operations fail or are compromised due to faults in defences, weapons, technology or machinery.
- ▶ **Organisation security is compromised:** Fraud can compromise the security of private sector or non-public bodies.
- ▶ **Erosion of trust in information security:** Where information leaks from public bodies due to fraud, this can lead to reduced trust, and reluctance by the public to provide government with secure information.
- ▶ **Threats to other nations:** International entities can use material obtained fraudulently in one country to commit fraud in another (for example, obtaining false passports) or transfer fraud methodologies to target programmes in other countries.

Key questions to ask

- ▶ If your programme was defrauded, what impacts might there be on security? Would fraud impact on the security of other organisations that you engage with?
 - ▶ Could fraud in your programme impact on national defence or national security?
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Example

In the United States, a review found a significant number of passports that had been issued to applicants who used identifying information of deceased or incarcerated individuals, had active felony warrants or used an incorrect Social Security Number. Fraudulent passports can be used to facilitate further crime such as drug trafficking or international terrorism.

In the United States, the Department of Defense was defrauded of more than US \$11.2 million by an international conspiracy supplying non-conforming and defective parts for military aircraft, vehicles, weapons and systems. This fraud put the military at significant risk of harm.



Business

Public bodies exist to improve the lives of the citizens they serve. Taking into consideration the human impact of fraud will help you to approach fraud in a way that is more meaningful to members of the public.

While the direct financial loss is borne by public bodies, behind every story of fraud, there are real individuals, whānau and communities whose lives have been impacted or even destroyed. The damage to these individuals can be financial, physical or mental.

Opportunistic individuals and serious organised crime groups target public bodies, including programmes designed to assist vulnerable people, with little regard for the victims of that fraud.

What impacts can look like

- ▶ **Increase in fraud assessment costs:** As allegations or referrals of fraud are received, resources (staff, time and systems) are required to assess whether to investigate.
- ▶ **Increase in fraud detection costs:** If public bodies are detecting fraud, this will take resources. Detection activities can include compliance checks, tip-off arrangements, data analytics programmes, technology tools and data sharing between public bodies.
- ▶ **Increase in fraud investigation costs:** Fraud investigations can be resource intensive and will vary depending on the size and complexity of the fraud.
- ▶ **Increase in fraud response costs:** Once fraud is identified and a decision is made to take action, it will require additional resourcing.
- ▶ **Restitution for third party victims:** Public bodies may need to allocate resources to restoring services to members of the public impacted through fraud and potentially compensating them for losses due to fraud.
- ▶ **Reviewing or auditing programmes:** Once fraud is identified the programme may need be reviewed or audited. This has a cost in terms of time and resources.

Key questions to ask

- ▶ Do you understand the wider business costs required to respond to fraud in your programme?
- ▶ Do you know how many allegations of fraud are made per year? What is the business cost of assessing whether to investigate these allegations of fraud against your programme?
- ▶ Do you understand the costs related to your countermeasure resources and activities?
- ▶ Would identified fraud result in a review of your programme? How much would this cost in terms of time and resources?
- ▶ Would identified fraud result in retrofitting or redesigning your programme? How much would this cost in terms of time and resources?

Example

In Australia, a Home Insulation Programme subsidised insulation as part of an economic stimulus package. The scheme was plagued with fraud, cost overruns, home fires, injuries, as well as the deaths of four installation workers. These outcomes had significant business costs, required the establishment of a royal commission (AUD \$20 million), an independent review, audit costs, compensation costs to insulation companies (AUD \$500,000) and remediation for impacted individuals.



Financial

Measuring the financial cost of fraud is challenging. Fraud is a hidden crime and by its nature difficult to detect. In many cases, public bodies might not be able to detect all fraud occurring against them. In addition, public bodies might not be able to identify whether a matter was fraud until many years after it occurred. However, measuring the financial cost of fraud is crucial in order for agencies to conduct their business effectively.

Calculating the financial loss that results from fraud helps to demonstrate the significance of the problem. Measuring the financial loss resulting from fraud provides a metric from which public bodies can make decisions on how much they should invest in fraud prevention.

What impacts can look like

- ▶ **Indicated fraud:** There are a range of metrics that can be used to indicate potential instances of fraud within an organisation. These metrics can include referrals, intelligence, investigations started and, potentially, identified anomalies in the system.
- ▶ **Detected fraud:** Detected fraud is a measure of the financial loss that a public body is aware of. It is not a measure of total loss in the organisation. It is the amount that has been uncovered and accepted (at some level) by the organisation.
- ▶ **Estimated fraud levels:** Only a proportion of fraud against an organisation is ever detected. Organisations can estimate the level of fraud within their payments and systems by testing statistically valid samples and extrapolating the results across the population.
- ▶ **Unknown fraud:** There is always likely to be an element of unseen, unmeasurable fraud loss within an organisation. It is not possible to consider all fraud risks when undertaking a fraud measurement exercise as the nature of fraud is so diverse and quickly evolving.
- ▶ **Recovered fraud loss:** Sometimes detected fraud is subsequently recovered by organisations. In some circumstances, organisations can offset these recovered losses against their detected loss to give a more accurate view of the financial impact of the detected loss.

Key questions to ask

- ▶ Do you have any reliable data on the financial cost of fraud against your programme?
 - ▶ Do you know the level of detected fraud in your programme? Does your organisation understand the limitations of these numbers?
 - ▶ Do you have an estimate of the total level of fraud in your programme (noting that the detected level and total level are not the same)?
 - ▶ Are there any comparators you could use from other public bodies to provide a view of the potential level of fraud to your programme?
 - ▶ Is the nature of measuring the financial loss as a result of fraud understood by those who will be reviewing the numbers or taking decisions based on them?
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Example

In the United Kingdom, a fraud measurement exercise was undertaken on its use of bus operator grants. The grant had several exemptions including school buses and bus tours (where the bus company makes its own financial gain). The exercise identified several cases where the grant had been misused for school bus routes and that some recipients had inflated mileage claims. Over 9% of the tested expenditure was found to be fraud and error.

In the United Kingdom, a fraud measurement exercise was undertaken to quantify patient prescription fraud. Some groups of people are exempt from paying for prescriptions based on their income and age. The exercise wanted to identify those who were fraudulently claiming for free prescriptions. The measurement exercise identified 2.8% of fraud and error combined, equating to £167.8 million lost to fraud.



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