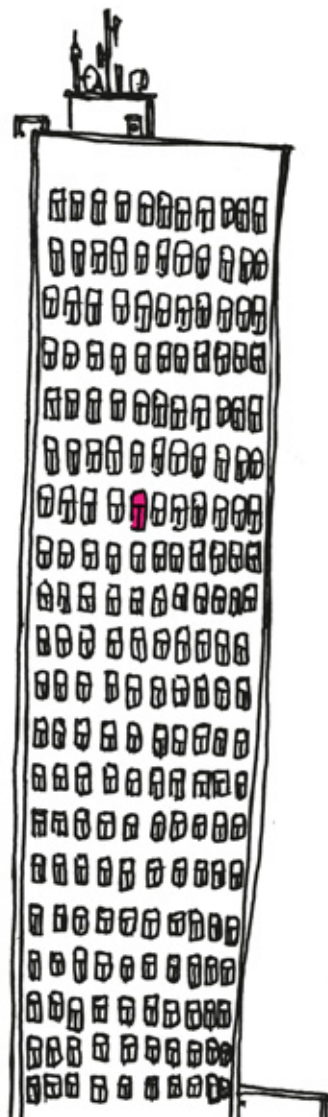


# The Fraud Advisory Panel

Sixth Annual Review 2003-2004

There is nothing inevitable about fraud. Insight and initiative can turn the tide. **This year's Review focuses on organisations which are getting it right.**



“[Let us] explode the myth sometimes spread that economic crime is somehow less evil than other criminal activity because it does not damage people. I reject this argument. Economic crime fuels terrorism. Money laundering is essential to serious and organised crime. Revenue fraud... is one of the major threats to the UK from organised crime. The cost to the UK economy of fraud has been put at £14billion a year, which is the equivalent of £230 for each member of the population. It is not victimless but is indiscriminate, hitting both rich and poor. Fraud may involve no violence... but it can be devastating in its effects.”

The Attorney General, the Rt Hon The Lord Goldsmith QC, 7th September 2003

## Sounding the Alert on Fraud: The Role of The Fraud Advisory Panel

The Fraud Advisory Panel's role is to raise awareness of the immense social and economic damage caused by fraud and help both public and private sectors fight back. It is dedicated to a holistic approach and the long view.

The Panel works to:

Originate proposals for reform of the law and public policy on fraud.

Develop recommendations that will enhance the investigation and prosecution of fraud.

Advise business as a whole on fraud prevention, detection and reporting.

Assist in improving fraud related education and training in business and the professions.

Establish a more accurate picture of the extent, causes and nature of fraud.

The Panel is an independent body of volunteers drawn from the law and accountancy, financial services, commerce, government departments, law enforcement, regulators, public agencies and academia. It is not restricted to seeing the problem from any single point of view but works to encourage a truly multi-disciplinary perspective. No other organisation has such a range and depth of knowledge, both of the problem and of the means to combat it.

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## Chairman's Overview: Three Keys to Tackling Fraud

This year's Review takes the novel stance of welcoming, albeit with a degree of caution, the progress that is being made in the fight against fraud. This isn't because fraud is declining, quite the reverse; but a crucial part of the solution involves directing attention to notable success and new initiatives. The case studies in this Review encourage a well-founded hope that stemming - and reversing - the tide of fraud is a realistic aspiration, not an utopian dream.

The time has come to start dispelling the mood of pessimism about fraud. The very seriousness of the situation is forcing radical thinking and bolder actions; both police and government are now well aware of the urgent threat posed by organised crime's involvement in fraud. Business too is learning lessons, even if it is usually less willing to talk publicly about its efforts. The growth of self help in the private sector is a highly positive development - and, in view of limited police resources, a very necessary one.

There are, broadly speaking, three keys to "getting it right".

### Strategic thinking

Fraud is a national issue and the response to it needs to be directed at a high level rather than through piecemeal local initiatives. The Association of Chief Police Officers, by expanding the scope and membership of its Economic Crime Forum, is one organisation addressing a key fraud policing problem identified by the Panel in our 2001 review, when we identified a general lack of "joined up thinking". Indeed, all the organisations discussed in the following pages are prepared to do the hard work of serious analysis and long-term planning. All refuse to think solely in terms of the headlines that derive from 'quick wins'.

### Policing partnerships

Closer co-operation between the police and business, notably in the pooling of intelligence, is becoming increasingly common. The North East Fraud Forum is a particularly interesting regional example and, at a national level, so is the development of a closer relationship between the police and the financial sector. Even the best resourced police service will be unable to cope with all the demands imposed by economic crime; a constructive and open relationship with business is essential.



## Cultural change

Long-term fraud reduction also depends on informing, training and motivating the widest possible range of employees. Economic crime is too widespread to be tackled by only a few specialist staff and consultants. The success of the NHS and Norwich Union in slashing fraud losses illustrates the benefits of mobilising the workforce.

Of course fraud is very far from disappearing; this year has seen many instances in the courts and the press of new variations on old ways of committing familiar frauds. So our rapture is modified. Progress has been made but it needs to be consolidated and built on.

The Panel has played a part in creating this changing climate of opinion, not least in Whitehall and at board level. Given our sustained representations on the subject we are particularly pleased that the new National Policing Plan 2004-2007 treats fraud and money laundering as examples of serious and organised crime, one of the Home Office's "key priorities" for national policing. And, after many years of our advocating the introduction of a generic offence of fraud the Home Office has at last consulted on implementation of the Law Commission's 2002 proposals. We have earned a reputation as an authoritative voice on fraud, indeed as the only body that seeks to address the whole issue from an expert and independent perspective.

The Panel depends almost entirely on its members, all volunteers who give generously of their time and energy. I would like to pay particular tribute to those directors who have stood down over the last year, albeit while remaining active members. They include Gerry Acher, Deputy Chairman since our foundation in 1998; Mike Hoare, another founding Director; and Ruth Eisenberg who served from 2000-2003. Martin Robinson stood down as a Director upon his appointment as our Adviser on Education, Events and Training in which post he continues to make an important contribution.

Thanks also to Mia Campbell, our invaluable Executive, the Panel's single full-time employee; Peter Alvey who supervises our financial affairs; Bill Cleghorn for his continuing help with special projects; Simon Pearce who has researched and drafted this Review (his fifth); and Wayne Martin, its designer.

Finally, I wish to express the deepest gratitude to our members, individual and corporate, whose support makes the Panel viable. Chief amongst these is the Institute of Chartered Accountants in England & Wales which played a vital role in establishing the Panel and remains its principal supporter.



Rosalind Wright CB  
September 2004



## Getting it Right (i) The Fraud Advisory Panel 2003-2004

The Panel is a think tank and educator, providing ideas, advice and information to Whitehall, Parliament, business, the professions and the general public. Since it was formed in 1998 it has:

Raised the profile of fraud in Whitehall, helping to push the issue to the top of the legislative agenda.

Developed major proposals for the reform of criminal and company law.

Worked to improve the anti-fraud content of business and professional education and training.

Commissioned new research, notably on cybercrime, SMEs and the extent of fraud.

Raised awareness of fraud and right responses to the problem through conferences, seminars and the media.

The Panel operates as a company limited by guarantee; every penny raised is ploughed back into its activities.

### Structure

The Panel is led by a Board of Directors, chaired by Rosalind Wright, Director of the Serious Fraud Office from 1998-2003. A Projects Sub-Committee develops and supervises research and publications. The Panel is supported by a full-time Executive, Mia Campbell, and an Education and Training Adviser, Martin Robinson, who identifies fraud training issues and develops appropriate training packages.

One of the Panel's principal aims is to ensure a cross-fertilisation of thought and experiences. To this end much of its work is carried out by four multi-disciplinary groups.

**Investigation, Prosecution and Law Reform:** Reviewing the legal process and the law as it relates to fraud. Chaired by Neil Griffiths.

**Cybercrime:** Promoting greater understanding of cybercrime and the safeguards against it. Chaired by Steven Philippsohn.

**Education, Events & Training:** Identifying and disseminating best practice in fraud prevention, detection and investigation. Chaired by Martin Robinson.

**The Anti-Money Laundering Monitoring Group:** Studying the implications of the money laundering regulations for the reporting, policing and prosecution of fraud. Chaired by Monty Raphael.





## Activities

### Briefing Business

Two major publications: "Have You Been Scammed? Identifying Internet and e-mail Scams" and "Cybercrime and the Proceeds of Crime Act: A practical guide for business".

Staging seminars on identity and employee fraud, ethics in the workplace and money laundering. Speakers included representatives from the Home Office, the DTI and the Metropolitan Police as well as the Panel.

Providing training and support to business and educational bodies. Panel representatives also spoke at a wide range of conferences and events.

Revising and updating the 2002 publication "Fighting Fraud: A guide for SMEs" which continues to be the Panel's most frequently downloaded document.

Re-formatting the Panel's public and members' websites ([www.fraudadvisorypanel.org](http://www.fraudadvisorypanel.org)) to make them a 'one-stop-shop' for people who want to know more about fraud, and to serve as a portal to other relevant sites.

### Advising Government and the Police

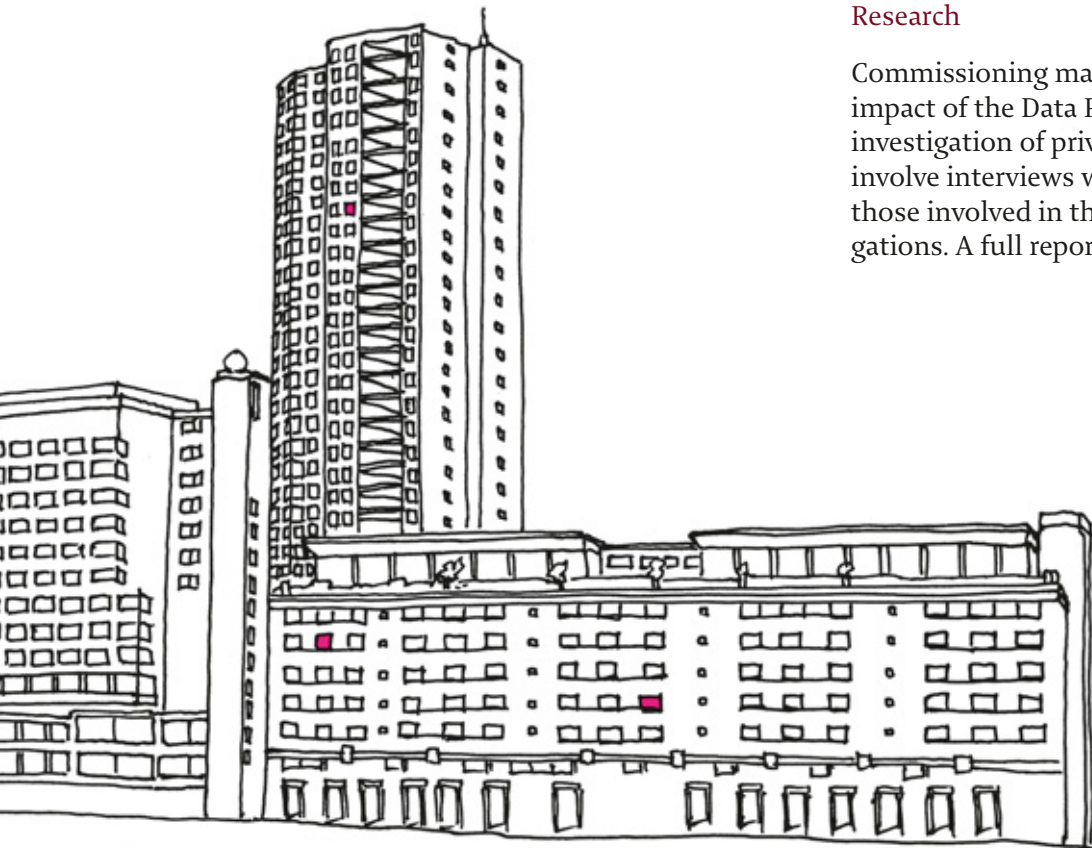
Submitting detailed responses to the Home Office's consultation papers on policing, defeating organised crime and reforming the law of fraud.

Meetings with ministers and officials at the Home Office and Treasury.

Participation in the new Economic Crime Forum set up by the Association of Chief Police Officers.

### Research

Commissioning major new research into the impact of the Data Protection Act 1998 on the investigation of private sector fraud. This will involve interviews with corporate victims and those involved in the actual conduct of investigations. A full report will be published in 2005.



## Membership

The Panel has 40 corporate, 130 individual members and 87 observers (mostly public sector bodies precluded from taking out formal membership).

Individual Membership costs £50 a year. Corporate Membership costs £1,000 and allows up to 20 employees to participate in Panel activities. All members are required to conform to a Code of Conduct.

Membership offers significant benefits:

Networking and exchange of news and insights. Members meet a wide range of experts from banking and insurance, accountancy, the legal profession, academia, and the IT and security industries.

Involvement in specialist working groups on Investigation, Prosecution and Law Reform; Education, Events and Training; Cybercrime and Money Laundering. Working group deliberations can be accessed through the member's only section of the FAP website.

Speaker meetings. Hear informed, and sometimes alternative, points of view.

Influence public policy via the Panel's proposals to government.

Address business and the professions through the Panel's seminars and publications.

For further information please contact Mia Campbell at The Fraud Advisory Panel, Chartered Accountants' Hall, PO Box 433, Moorgate Place, London, EC2P 2BJ; 020 7920 8721; [info@fraudadvisorypanel.org](mailto:info@fraudadvisorypanel.org).





### Corporate Members

Argos Ltd  
Association of British Insurers  
Association of Certified Fraud Examiners  
Association of Chartered Certified Accountants  
Aviva Plc  
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Chartered Institute of Management Accountants  
CIFAS - the UK's Fraud Prevention Service  
Control Risks Group  
Deloitte & Touche LLP  
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Royal Mail Group Plc  
The Accountants' Joint Disciplinary Scheme  
The Institute of Chartered Accountants in England & Wales  
The Law Society of Scotland  
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### Supporters

Organisations making donations above the corporate subscription:

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Royal Sun Alliance Plc  
The Institute of Chartered Accountants in England & Wales

The Board is deeply grateful to all those individuals and organisations whose generous support makes the Panel's work possible.

## The Board



**Rosalind Wright CB (Chairman)**; Director of the Serious Fraud Office 1997-2003; General Counsel and Executive Director in charge of the Investor Protection Policy and Legal Division at the Securities and Futures Authority 1987-97; Head of the DPP's Public Prosecution's Fraud Investigation Group for the City of London and Metropolitan Police areas 1983-1987; Independent Member of the Board of the Office of Fair Trading; Independent Member of the Department of Trade and Industry's Legal Services and Companies Investigation Branch boards; Vice-Chairman, Jewish Association for Business Ethics; Bencher of the Middle Temple.



**Gerry Acher CBE LVO FCA (Deputy Chairman)**; Board member, KPMG and former Senior Partner of its London office; Deputy Chairman of London First; member DTI Committee on reporting through the Operating and Financial Review; former Chairman, DTI Foresight Panel working party on crime and business; founder Chairman of the Audit Faculty of the Institute of Chartered Accountants in England & Wales 1996-2001. Retired from the FAP Board 4th March 2004.



**Felicity Banks MSc FCA**; Head of Business Law at the Institute of Chartered Accountants in England & Wales; represents the ICAEW on economic crime issues; represents the accounting profession on HM Treasury's Money Laundering Advisory Committee.



**Ruth Eisenberg BSC FCA**; former Director, Special Projects at the Institute of Chartered Accountants in England & Wales. Retired from the FAP Board 4th September 2003.



**Neil Griffiths** (Chairman, Investigation, Prosecution and Law Reform Working Group); a partner in the Insolvency Group at Denton Wilde Sapte; Vice-Chairman of the Creditors Rights Committee of the International Bar Association.



**Mike Hoare MBE**; Hon. Chairman of the Risk and Security Management Forum having been Chairman from 1990-2002; former Metropolitan Police Commander and Director of the Investigation Department of the Post Office; former Chairman of the Panel's Research, Information and Intelligence Working Group. Retired from the FAP Board 27th November 2003.



**Will Kenyon**; partner in PricewaterhouseCoopers' Forensic Services group; founding head of Forensic Investigations, PricewaterhouseCoopers GmbH, Germany 1998-2001; involved in investigations and recovery actions for some of the most significant fraud cases of the last decade.

**James Perry**; a Director of International Compliance Services Limited; former Detective Chief Superintendent with the Metropolitan Police and Commander in Charge of its Economic and Specialist Crime Unit; former Chair of the Association of Chief Police Officers' National Financial Investigation Working Group; represented the police service in the official studies which led to the Proceeds of Crime Act 2002 and Money Laundering Regulations 2003.



**Steven Philippsohn** (Chairman, Cybercrime Working Group); founder and Senior Partner, Philippsohn Crawfords Berwald; Co-Editor of the UK Manual of the Association of Certified Fraud Examiners; member of the editorial boards of "E-Commerce Law & Policy" and "Inside Fraud Bulletin".



**Alex Plavsic**; Head of Financial and Fraud Investigation at KPMG Forensic; conducted independent reviews for regulators and government departments; investigated serious fraud cases including Polly Peck and Group Torras.



**Monty Raphael** (Chairman, Anti-Money Laundering Monitoring Group); Senior Partner, Peters & Peters; conducted fraud enquiries for regulators, Inland Revenue and HM Customs & Excise; Visiting Professor in Law at Kingston University; former President, London Criminal Courts Solicitors Association; founder of the Business Crime Committee of the International Bar Association and Chair of its Anti-Corruption Working Group.



**Martin Robinson FCIS, FIIA** (Chairman, Education, Events and Training Working Group); Training Development Adviser to the Institute of Internal Auditors UK and Ireland; Audit Adviser to the Institute of Chartered Secretaries and Administrators. Retired from the FAP Board 2nd September 2004 upon his appointment as the Panel's Adviser on Education, Events and Training.

## Getting it Right (ii)

### Case studies

The Panel has long argued for fundamental changes in the way the public and private sectors attack fraud. These include:

Systematic analysis of the extent and causes of fraud.

A strategic and co-ordinated national approach.

Grass-roots business educational campaigns.

Creating additional and dedicated police resources.

Cultural change within organisations involving every employee.

The case studies which follow show these ideas in action.

### Strategic Co-ordination

#### The ACPO Economic Crime Forum: Getting an Overview

The Home Office acknowledges that it has no integrated strategy to fight fraud against business. Though it is committed to discussions with industry an important step has already been taken by the Association of Chief Police Officers (ACPO).

Chaired by Dr James Hart, Commissioner of Police for the City of London, the Association has broadened its Economic Crime Forum to include representatives from business. "There was no scope for input from the consumers of policing" says Commissioner Hart. "Good anti-fraud policing is hard without good feedback and that demands a positive effort to obtain it".

In early 2003 ACPO asked business associations, major financial institutions, regulators, government departments and the Fraud Advisory Panel to send representatives to the Forum. The first step has been to identify areas where common practises and procedures could be created and this has resulted in a number of practical changes. The Commissioner notes that "People naturally look at fraud from their own perspective. For instance, a fraud risk manager may not see the need for certain types of evidence which the law demands if a conviction is to be secured". There has also been a strong focus on tackling identity fraud and the growing problem of corrupt or intimidated bank employees working with criminal gangs.

In the absence of a national commission on economic crime (which the Panel called for three years ago) the Forum is the only public body considering fraud at a strategic and multilateral level. ACPO is already considering the advantages of encouraging a number of regional fora operating along similar lines.

#### The National Intellectual Property Crime Strategy: A Holistic Approach to Fraud

Counterfeit goods are a virulent form of fraud, worth at least £9billion a year, deceiving honest customers and often cheating those seeking an illegal bargain buy. Some fakes are threats to health and safety. Tax and VAT revenue is lost and genuine manufacturers of software, videos, music, clothes, home furnishings and perfumes lose income. Even more alarming is the advent of medicines, foods, beverages and car parts which are not only sold under fake labels but are also produced below safety standards. Counterfeiting is also seen by organised crime as an easy way to launder money, allowing it to be redirected into other criminal enterprises.

The Department of Trade & Industry (DTI), through its executive agency, The Patent Office, has organised an alliance of brand owners, HM Customs & Excise, police and local government trading standards officers in a holistic national strategy devised to defeat intellectual property (IP) crime. This puts into practice, albeit on a single issue, the co-ordinated approach for which the Panel has argued since 2001 when it pointed out that the range of public bodies involved in combating fraud led to what the Patent Office itself describes as duplicated effort, wasted resources and ambiguous signals.

A new annual “National Enforcement Report” will draw together the work carried out by the main participants. Its findings will be fed to a Strategic Tasking and Co-Ordination Group charged with setting priorities for prevention and enforcement. The strategy will also involve legislation, international co-operation, training, and publicity aimed at raising public awareness, as well as demonstrating that counterfeiting is not a ‘victimless crime’.

Another of the Panel’s principal goals has been to ensure that government, police and business develop a clear picture of the nature, volume and value of fraud. The Patent Office acknowledges that “producing and sharing expert information is essential in driving strategic and operational decisions”. The National Criminal Intelligence Service (NCIS) is working with the Patent Office to produce an analytical model which will inform enforcement targeting.

### The North-East Fraud Forum: Mobilising the Grass Roots

Law enforcement and business need closer regional and local, as well as national relationships. Northumbria Police has recognised this, creating the North-East Fraud Forum (NEFF) in early 2003. Detective Inspector Phil Butler, head of its Economic Crime Unit and Forum Chairman says that his force was committed “to developing an initiative to bring the public and private sectors together, to promote a strong anti-fraud culture in the region.”

Working with the support of some local firms, Cleveland and Durham police and the Government Office for the North-East the Forum held an inaugural conference at Newcastle-upon-Tyne in March 2003 attended by 400 representatives. NEFF aims to:

- Provide training. More than 1,000 representatives from 200 organisations have attended “fraud master classes” and other events.

- Share intelligence and disseminate innovative ideas from both the public and private sectors.

- End the sense of embarrassment and isolation which makes some businesses reluctant to report fraud.

- Promote partnership and develop a common vision. “Our ultimate aim is for all of us within the public and private sectors to adopt a single common sense fraud reduction strategy” says DI Butler.

In April 2004 a NEFF team gave a presentation in Vienna to the United Nations Commission on International Trade (UNCITRAL) colloquium on commercial fraud. UNCITRAL has used NEFF as the model for its new International Fraud Forum and has announced its intention of creating regional fora too.



## Policing

### The City Police as the Lead Force in the South-East: Resourcing the Investigators

The Panel has often pointed to the declining numbers of fraud squad officers across England and Wales and the loss of experienced officers to other duties. A new initiative may signal a break in this trend as well as giving county forces access to additional specialist fraud investigators in serious cases.

The City of London Economic Crime Department was designated “Lead Force” for fraud investigations in the 14 counties of south-east England (including East Anglia) in April 2003. Jointly funded to the tune of £1 million each by the Home Office and the Corporation of London the Force has recruited an additional 24 trained investigators. The Government has already indicated interest in creating similar units as regional foci for intelligence and expertise.

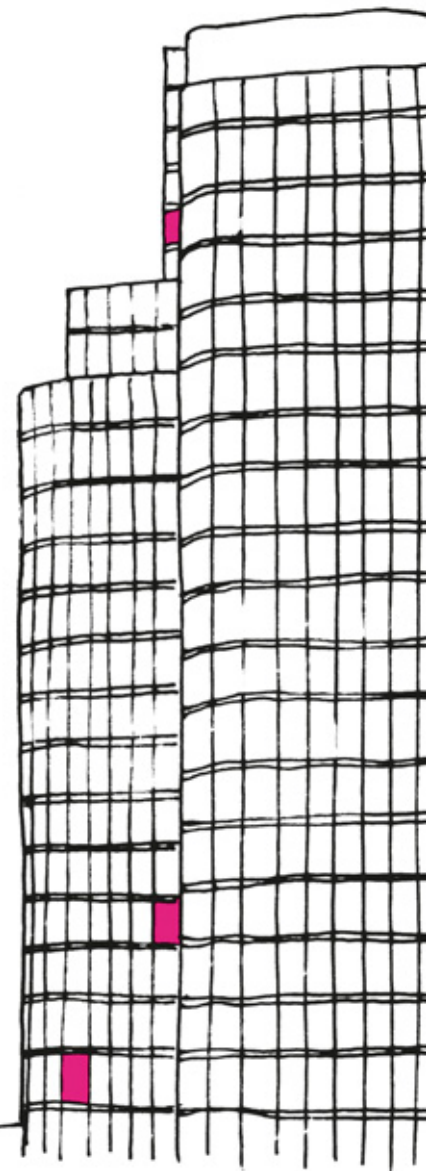
The Lead Force will serve as an investigatory arm of the Serious Fraud Office (SFO) in about 50 cases a year. Detective Chief Superintendent Ken Farrow says that his team will also investigate its own cases; some of these will be major cases which fall below the SFO acceptance criteria.

DCS Farrow points to three major advantages of the Lead Force model:

75 investigators in six teams allows a heavy concentration of resources in the crucial early stages of complex investigations.

Officers wishing to specialise in fraud and financial investigation work now have the prospect of a lateral or upward career path within the Economic Crime Department. This in turn deepens and widens the Force's pool of knowledge and contacts. This is in marked contrast with many provincial forces which have suffered heavy losses of skilled fraud squad officers in recent years.

The Economic Crime Department is overseen by a Detective Chief Superintendent who has direct access to the Commissioner on financial crime issues. Provincial fraud squads are usually managed by Detective Inspectors who may also have other responsibilities.

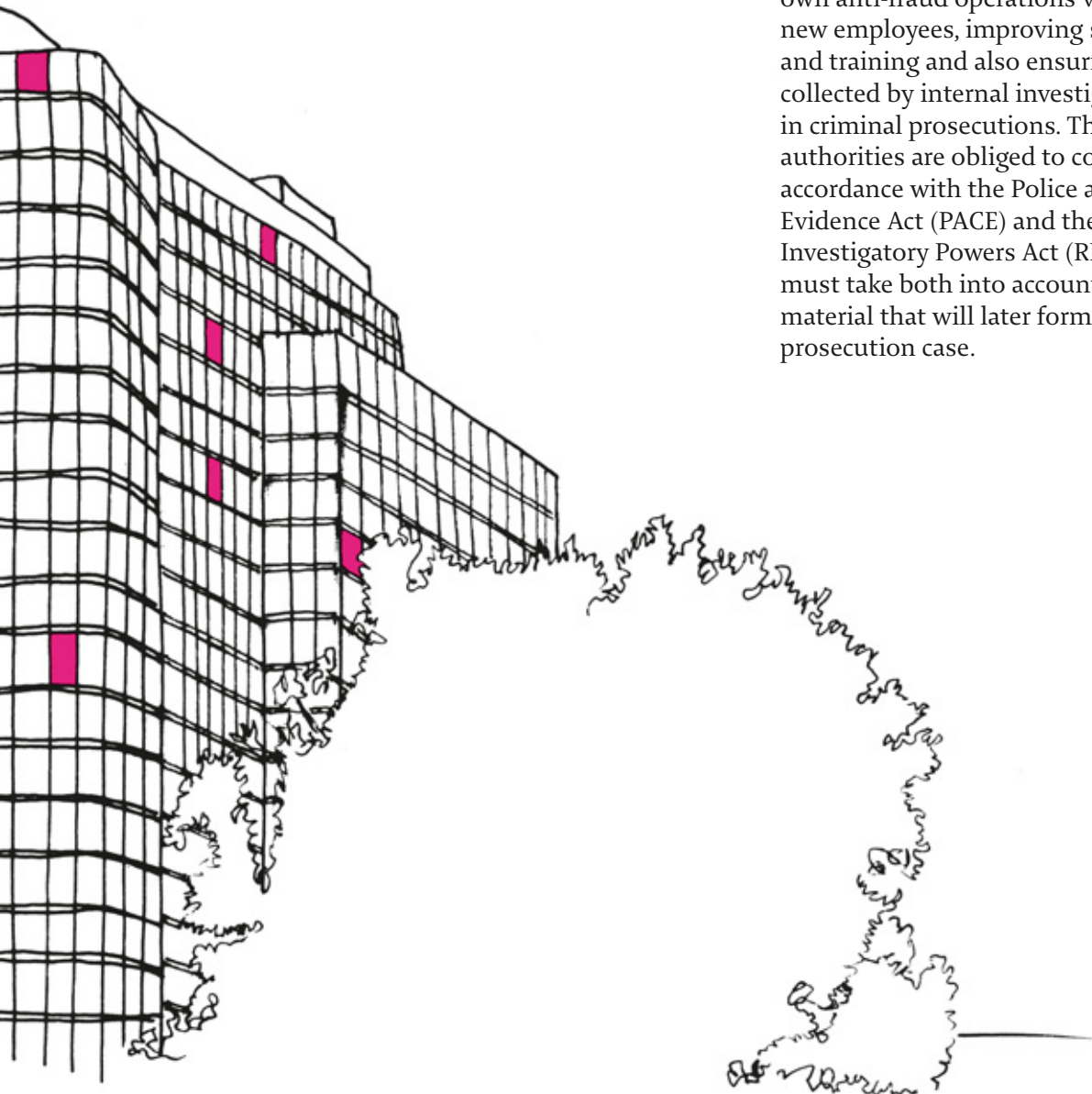


### The Met's "Operation Sterling": Intelligence-led Policing

"Sterling" is a Metropolitan Police operation focusing on serious and organised economic crime in Greater London. An intelligence cell has been created to identify trends in both the private and public sectors, key suspects and sectoral and geographic "hotspots". Investigatory resources can then be directed at strategic problems on the basis of detailed analysis.

This intelligence-led approach has been successful in other drives such as Operation Trident (black-on-black gun crime), and Operation Bumblebee (burglary). Stopping the growth of organised criminal activity is a priority; gangs have moved into economic crime in a way almost unknown 20 years ago. Detailed analysis of London-wide patterns has national implications and information and analysis is already being forwarded to regional police forces.

Operation Sterling also involves the Police as leader and co-ordinator of joint public-private sector projects. Fraud by bank employees, leading to theft of customer data as well as funds, is one key area of study. The Met's team is working with the banks to strengthen their own anti-fraud operations via better vetting of new employees, improving staff awareness and training and also ensuring that evidence collected by internal investigators can be used in criminal prosecutions. Though only public authorities are obliged to collect evidence in accordance with the Police and Criminal Evidence Act (PACE) and the Regulation of Investigatory Powers Act (RIPA) businesses must take both into account when gathering material that will later form part of a prosecution case.



### The Dedicated Cheque and Plastic Crime Unit (DCPCU): Police-Business Collaboration

The DCPCU is a joint operation between the Association for Payment Clearing Services (APACS - which represents the major British banks and building societies on non-competitive payment issues), the Home Office, and the Metropolitan and City of London police. Losses from plastic card crime more than tripled from £135 million in 1998 to £424.6 million in 2002. Yet this area of crime has seen a considerable decline in dedicated police resources; most forces no longer have a 'cheque squad'.

DCPCU was launched in April 2002 with a remit to investigate these crimes in the Greater London area. The banks supply intelligence and administrative support; two-thirds of police staffing is seconded from City of London Police, the rest from the Metropolitan force. This unique partnership was made possible by 75% APACS and 25% Home Office funding (though APACS now bears the whole cost of the Unit).

In its first two years of operation to April 2004 DCPCU made 171 arrests resulting in convictions, recovered over 36,000 stolen cards and identities and saved £65 million. The conviction figures underplay the overall impact of operations as the Unit has concentrated on breaking up and disrupting gangs rather than targeting petty criminals. Organised crime is responsible for the lion's share of British card fraud and often operates via technically sophisticated factory operations. The Unit is now receiving funding from APACS which will allow it to expand its operations.

## Business

### CHIP & PIN: Direct Action for the Consumer

Card payments are set to overtake cash as the country's most popular method of payment. In 2003 the value of cash payments only exceeded those made in card transactions by £268 billion to £244 billion. A recent PricewaterhouseCoopers survey found that 49% of the public have either been a victim of credit card fraud, or know someone who has suffered the same fate.

The retail and banking industries are fighting fraud through the CHIP & PIN scheme. There are two elements involved in making a plastic card transaction secure. The first is ensuring that the card is genuine; the second is establishing that the person presenting the card is its true owner. The electronic chip embedded in the card ensures the former and the owners' unique Personal Identification Number (PIN) facilitates identification. The scheme's promoters predict that it will more than halve predicted UK fraud losses. A similar system for debit cards has largely contributed to an 80% reduction in French card fraud over the last decade.

CHIP and PIN was tested in a three month trial in Northampton in 2003 and is currently being extended across the nation. The programme involves 42 million cardholders, 122 million new cards and 40,000 cash machine upgrades.

It is recognised that criminals will seek to divert their efforts to "card not present" telephone and Internet transactions. Plans are therefore being developed to verify cardholder's addresses and to cross check card security codes.

### Norwich Union: Knowledge the Basis of Success

Successive reports from the Fraud Advisory Panel have highlighted uncertainty about the extent, incidence and value of fraud. This lack of visibility has tended to marginalise its importance in the minds of senior managers and unintentionally ensures its growth. Norwich Union, the UK's largest insurer, has adopted a highly systematic risk-based approach. The Company's fraud savings have risen from £46 million in 2002 to £71 million last year, with £51m delivered in the first 6 months of 2004. Continuing growth is anticipated. £10 is saved for every £1 spent.

Reliable performance Management Information (MI) and detached analysis come first and this requires patience as there are no early economic benefits. Yet reliable and fully credible data is an essential prerequisite for any accurate cost benefit analysis.

Next comes the optimisation of fraud detection by staff dealing with customers. To be effective, fraud detection should be part of every day claims handling and this requires a sustained effort to secure staff commitment and enthusiasm. Relatively simple procedures help. For instance, claims handlers have historically used an unwieldy list of over 80 fraud indicators. This has been refined down to a hard core of 15 key indicators delivering 95% of historic fraud savings values while reducing 'false positives' by approximately 50%. This is freeing claims handlers to focus on genuinely suspect claims while simultaneously reducing delays to genuine customers.

Continuing emphasis has also been laid on raising staff awareness. Specialised training is key. Full time anti-fraud "champions" in every branch deliver localised training, while reporting back on staff ideas and practical problems. Norwich Union's Head of Fraud Chris Hill notes that "Our central fraud team has only 17 staff. Harnessing the skills and enthusiasm of our 3,000 plus claims handlers has been central to our success."

### CIFAS-the UK's Fraud Prevention Service: Self-Help in Action

CIFAS is a not-for profit company which enables its members to pool information on consumer credit fraud. Member organisations exchange details of credit applications which fail verification checks. Member's assessments of the savings they have made have grown from £10.5 million in 1990, to £487 million in 2003 and a projected £650 million in 2004.

CIFAS was established in 1988 when a number of retailers responded to police advice that consumer credit fraud was a non-competitive issue and that co-operation and communication between lenders was necessary. It has since expanded to include companies operating in the telecommunications, factoring, insurance, utility, share dealing and commercial credit industries. It works closely with the police and the National Consumers' Council (which also nominates a representative to the Board). Both the Office of Fair Trading and the Information Commissioner have been regularly consulted since the outset and there are close working relationships with many public sector organisations.

Any member placing a warning on the CIFAS database must have sufficient evidence to justify reporting the matter to the police (although it is not obliged to make a report in every case). Members must also be able to demonstrate they have either suffered, or would have suffered, a financial loss. Former Information Commissioner Elizabeth France has said that "CIFAS has provided an early blueprint for the way the balance can be struck between the need to share information to prevent fraud, and protecting the privacy of the law abiding citizen".



## Public Sector

### The NHS Counter Fraud Service: Towards an Anti-Fraud Culture

The NHS Counter Fraud Service (NHS CFS) is dedicated to the development of a pervasive anti-fraud culture within Britain's biggest public sector organisation. More than 460 professionally trained and accredited Counter Fraud Specialists have been put into place across the NHS.

Figures released in April 2004 showed that £478 million had been saved since 1998, enough to pay for 60,000 kidney transplant operations or 100,000 hip replacements - a 13:1 return on the Government's budgetary investment. Losses to pharmaceutical, dental and optical patient fraud fell by 59.8%, 25.6% and 23.2% respectively. Overall losses from patient fraud have been cut by 48.9%. In some areas, claims by NHS professionals have fallen by 31-46%. There have been 216 convictions (a 97% success rate) and 275 successful civil and disciplinary cases.

The CFS has made particular efforts to raise NHS staff awareness, increase their knowledge and secure their commitment. Over 1,100 Fraud Awareness Presentations have been delivered to key staff throughout the NHS and October 2003 saw the first ever Fraud Awareness Month, with 140 events being held in hospitals throughout England and Wales. Publicity about the strong processes which now exist within the NHS to prevent, detect and investigate fraud has also helped build a deterrent effect. A recent internal survey showed that 74% of participants recognised that countering fraud was their individual responsibility, up from 34% in 2000.

Accountability has been strengthened by tailored training for key staff such as directors of finance. This has been coupled with new contracts of employment setting out anti-fraud responsibilities for senior employees.



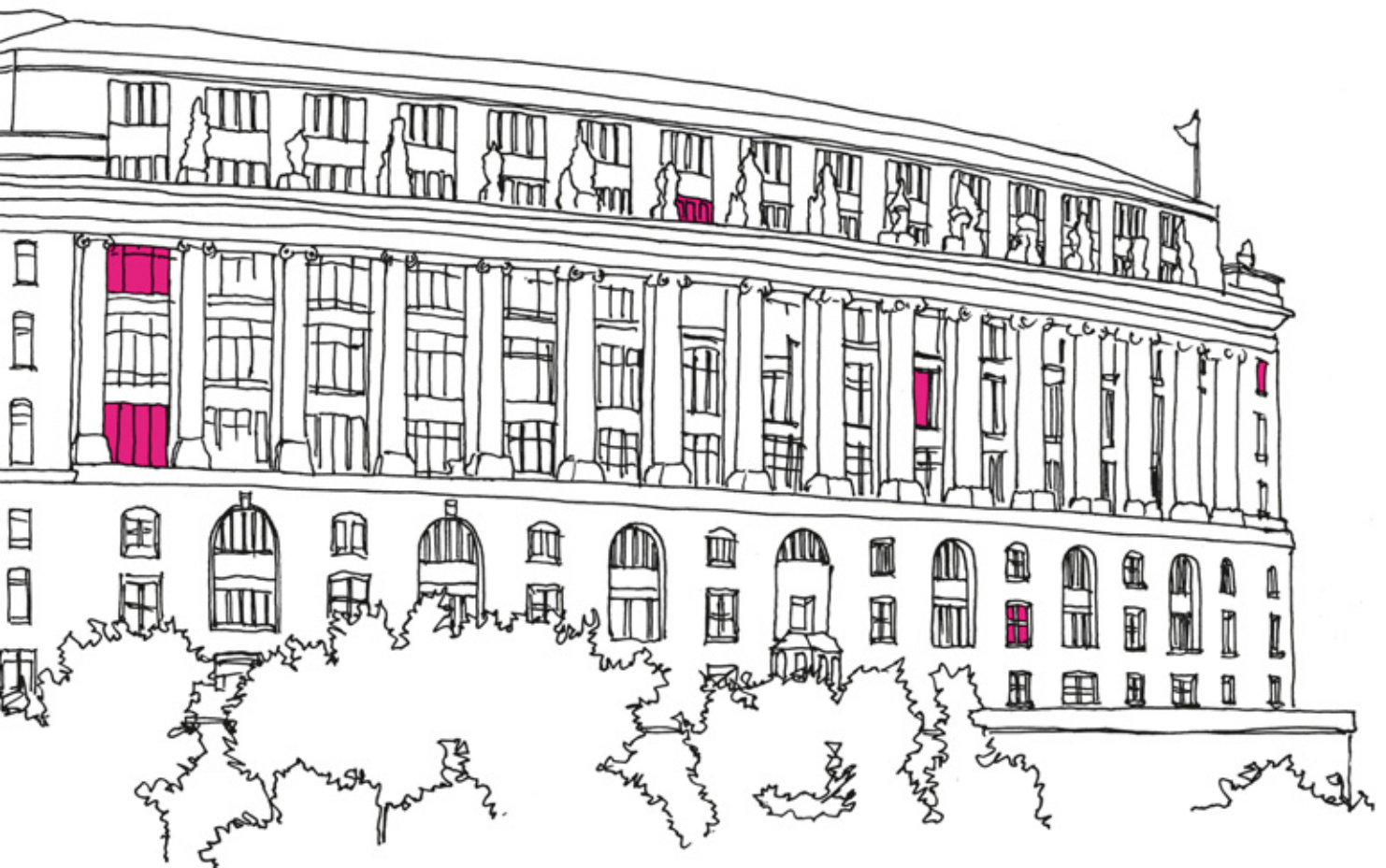


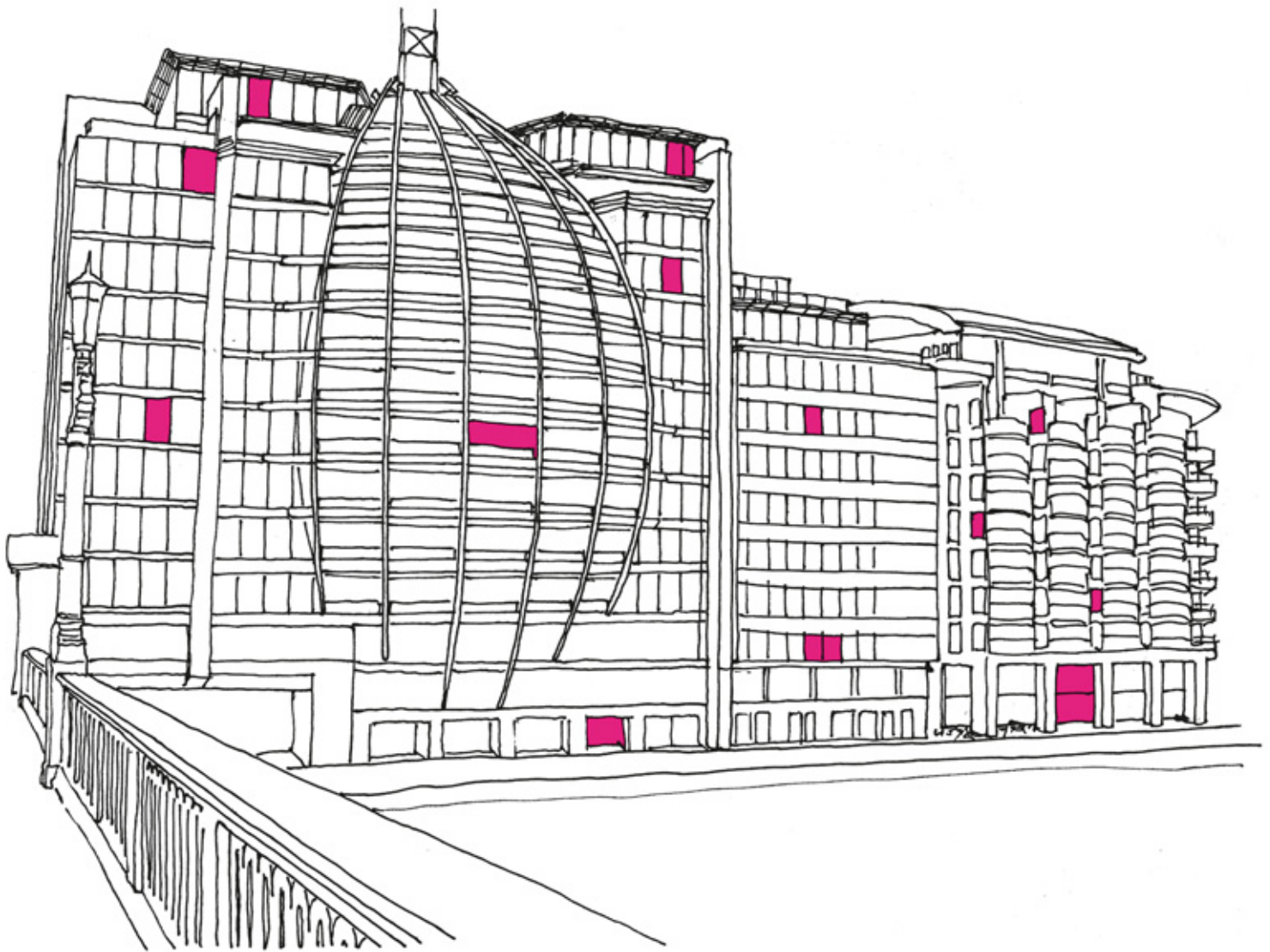
### The Audit Commission's National Fraud Initiative: The Benefits of Data Mining

Public bodies have huge databases; matching the information held on different systems is a crucial tool in detecting, and therefore deterring, fraud. The Audit Commission's National Fraud Initiative (NFI) involves 1,150 local councils, the NHS and central government in the analysis of over 14 million data records. Data matching identifies potential inaccuracies and instances where fraud may be occurring, for example, an individual claiming Housing Benefit whilst receiving a salary or pension which precludes a claim. The Audit Commission returns these matches to participating bodies for investigation together with guidance on action to take.

NFI matches resulted in the detection of over £83 million of fraud and overpayments in 2002-2003, up from £50 million in NFI 2000-2001 – a 66% increase. Total savings to date exceed £190 million. The major areas of fraud detected to date are housing benefits, council tenancies and occupational pensions. Record levels of fraud and overpayments were detected for the latter, with more than 2,000 incidences of an occupational pension continuing to be paid after the death of the pensioner. Over 100 public sector employees resigned or were dismissed as a result of frauds revealed by NFI 2002-2003.

A number of new data matching partnerships and techniques are planned in order to address issues such as corrupt tendering, abuse of parking permits and payment to residential homes for deceased residents. As the Commission points out, data matching demonstrates “the importance of joined-up government to protect the public purse.”





### The National Audit Office: Raising Awareness of External Fraud

The National Audit Office (NAO) has made a particular drive this year to tackle the threat of external fraud in the public sector. In a new guide, “Good Practice in Tackling External Fraud”, to which the Panel contributed, the NAO highlights ways in which different government organisations are working to combat and detect fraud by outsiders against public funds. The document gives examples of actual frauds; contains checklists to help managers assess their current anti-fraud practices; and gives advice on identifying fraud risks.

Among the many examples of good practice highlighted in the guide is HM Customs & Excise’s publicity campaign on tobacco smuggling, designed to inform the public, would-be smugglers and key trade groups of what the law is and to help persuade them to comply with it. Evaluation of the campaign has shown consistently high levels of awareness and support for Customs’ messages among the targeted trade groups, and increasing public awareness of the link between smuggling and organised crime, together with the penalties that can be imposed.

## Fraud and the Nation 2003-2004

### Definition, Cost, Impact

Fraud can cover activities as diverse as stealing company assets; financial manipulation and false accounting; obtaining goods and money by deception; impersonating an individual or a company to obtain credit or goods; or conspiracy to do all these things.

The overall cost of fraud, including remedial action, was estimated in 2000 at £13.8 billion by National Economic Research Associates for the Home Office, around £230 per head of the UK population. These figures take no account of undetected fraud. And fraud is growing fast; it cost £1 billion in 1985 and £4 billion in 1994. Drug-related crime is estimated to be worth £6.6 billion and vehicle thefts £900 million.

Recorded fraud and forgery offences grew from 174,742 to 317,900 between 1991 and 2003-2004. It is generally accepted that the Home Office crime counting rules are not accurately and consistently applied to fraud offences, and that as a result there is significant under recording. For instance, the Financial Services Authority (FSA), notes that even existing data “suggests the incidence of fraud in the financial sector is significant and rising”. As the FSA points out, the lack of official statistics on the true scale of fraud means that the issue is politically marginalized.

A more comprehensive picture of the damage done by fraud must be assembled from various pieces of evidence.

Major financial fraud has brought down large companies (BCCI, Maxwell, Barings and many others), resulting in heavy job losses and a “ripple effect” of economic suffering for smaller customers, investors and suppliers. A PricewaterhouseCoopers survey in 2003 found that 51% of British businesses have been victims of fraud in the last two years. 16 investors took their own lives in the aftermath of the Barlow Clowes fraud.

HM Customs & Excise reports that VAT fraud and error cost the British taxpayer approximately £11.9 billion in 2002-2003 - up 12% from £10.6 billion lost in the previous year.

The Association of British Insurers estimated in 1998 that 3.7% of all premiums charged were directly attributable to fraud losses. In April 2003 it calculated that fraudulent motor and household claims alone amounted to £20 million per week.

The Home Office reported in its 2002 consultation paper on identity fraud that it can take victims up to 300 hours to rebuild their credit history. A Cabinet Office report in 2002 suggested that £1.3 billion a year is the minimum quantifiable cost to the economy arising from identity fraud.

Fraud feeds organised crime. NCIS has reported that gangs derive as much money from financial crime as from drug trafficking.

Fraud can fund terrorist groups. The involvement of republican and loyalist paramilitaries in Northern Ireland is well known. Two Algerians were convicted in 2003 under the Terrorism Act 2000 for credit card fraud on behalf of the Al Qaeda network.



## Changing the Law

### A Single Offence of Fraud at Last?

The current law on fraud is mainly contained in eight statutory deception offences in the Theft Acts 1968-1996, the companies act offence of fraudulent trading and the common law offence of conspiracy to defraud. These fail to cover the infinite variety of fraudulent behaviour. The appropriate offence in a particular case is not always readily apparent; sometimes the facts of an undeniably dishonest transaction cannot be encompassed by the wording of any existing law. As a result defendants have successfully argued that their deceptive behaviour did not fit the definition of the offence with which they had been charged. It is unrealistic to add yet more specific offences; not only does piecemeal reform generate further complexities, it also condemns the law to lag behind the ingenuity of fraudsters as well as developments in technology.

The Government's June 2004 consultation paper (building on some of the recommendations in the Law Commission's Paper 276), proposed replacing this position with a general offence of fraud which could be committed in three ways: false representation; wrongfully failing to disclose information; and abuse of

office. Behaviour in each case would have to be dishonest and aimed at securing a gain for the defendant, or a loss for another person. A gain would not have to be realised, as is the case under existing law, for an offence to occur. Current offences of deception would be repealed.

The Panel has welcomed the Government's proposals; it makes sense to focus on malevolent intention and the dishonest character of the conduct in question. It has also urged the Government to consider the following arguments:

A person should be guilty of fraud not only when he knows a representation to be false or misleading, but also when he is aware that it might be false or misleading.

Abolishing the offence of conspiracy to defraud will severely restrict the ability to prosecute the largest and most serious fraud cases. The current offence can be adopted by the courts to fit new situations, a considerable advantage given the rapid development of new financial instruments and technology.



### Non-Jury Trials in Serious Fraud Cases

Courts in serious fraud cases tend not to consider all, or anything like, the total evidence of dishonesty because the prosecution is often reluctant to burden jurors with large amounts of highly complex material. Lengthy and repetitious explanations, cross-examination and speeches are also introduced to 'help' jurors. Moreover juries are effectively restricted to those who can afford to devote six months or more to such cases.

Part 7 of The Criminal Justice Act 2003 provides that cases of unusual length and/or complexity may be tried by a judge alone if the interests of justice so require. Section 43 of the Act would enable both prosecution and defence to make applications to the trial judge for the case to be heard without a jury. As a result of the intense controversy surrounding the limitation of trial by jury the Government has agreed not to implement these measures except by positive resolution of both Houses of Parliament. Ministers are looking again at the possibility of special juries or panels of assessors.

Whatever the final outcome the Panel has long argued for methods which would ensure swifter trials in major criminal cases:

Judges must be given thorough training in trial management techniques.

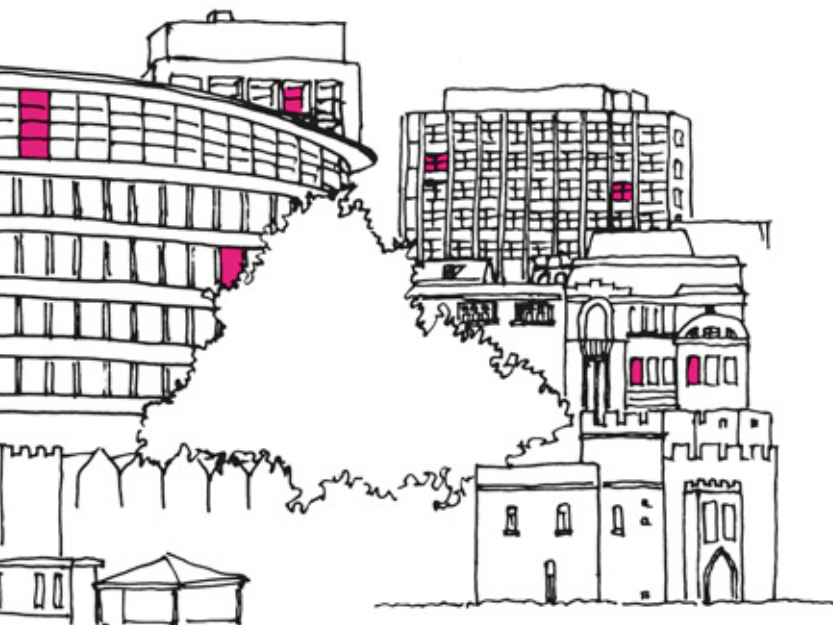
More intensive efforts must be made before a trial starts to bring prosecution and defence to agreement on undisputed issues which need never be brought before the court.

More robust and consistent efforts must be made to improve the way evidence is presented, for instance by better and greater use of visual presentations.

### The Data Protection Act 1998

The recent White Paper on organised crime proposes increased private sector involvement in police intelligence-gathering. The Panel is concerned that this fails to consider a gap in existing law. Whilst the Data Protection Act 1998 gives exemptions to law enforcement agencies, the same privileges have not been extended to investigators working in the private sector, making it increasingly difficult for the two sides to work together as they did before the Act came into force.

The Panel has commissioned a research project to establish the full extent of the problem and to examine whether there is a case for creating exemptions for private sector investigators which would allow more effective and clearly legal retention, sharing and generation of information. A full report will be published in 2005.





## Resourcing Investigations

The Government has a solid record of achievement in fighting economic crime. Recent developments include the Home Office's recognition of fraud and money laundering as examples of serious and organised crime; and proposals to create a Serious Organised Crime Agency (SOCA) by 2006, incorporating NCIS, the National Crime Squad and elements of HM Customs & Excise.

Yet the Attorney General, Lord Goldsmith, acknowledged last year that "large amounts of fraud are going uninvestigated". The Director of the Serious Fraud Office has said the same of many cases which would previously have been taken on by local forces. The Commissioner of Police for the City of London and Chairman of ACPO's Economic Crime Forum recently noted that "Police forces have been distancing themselves from fraud investigations for years".

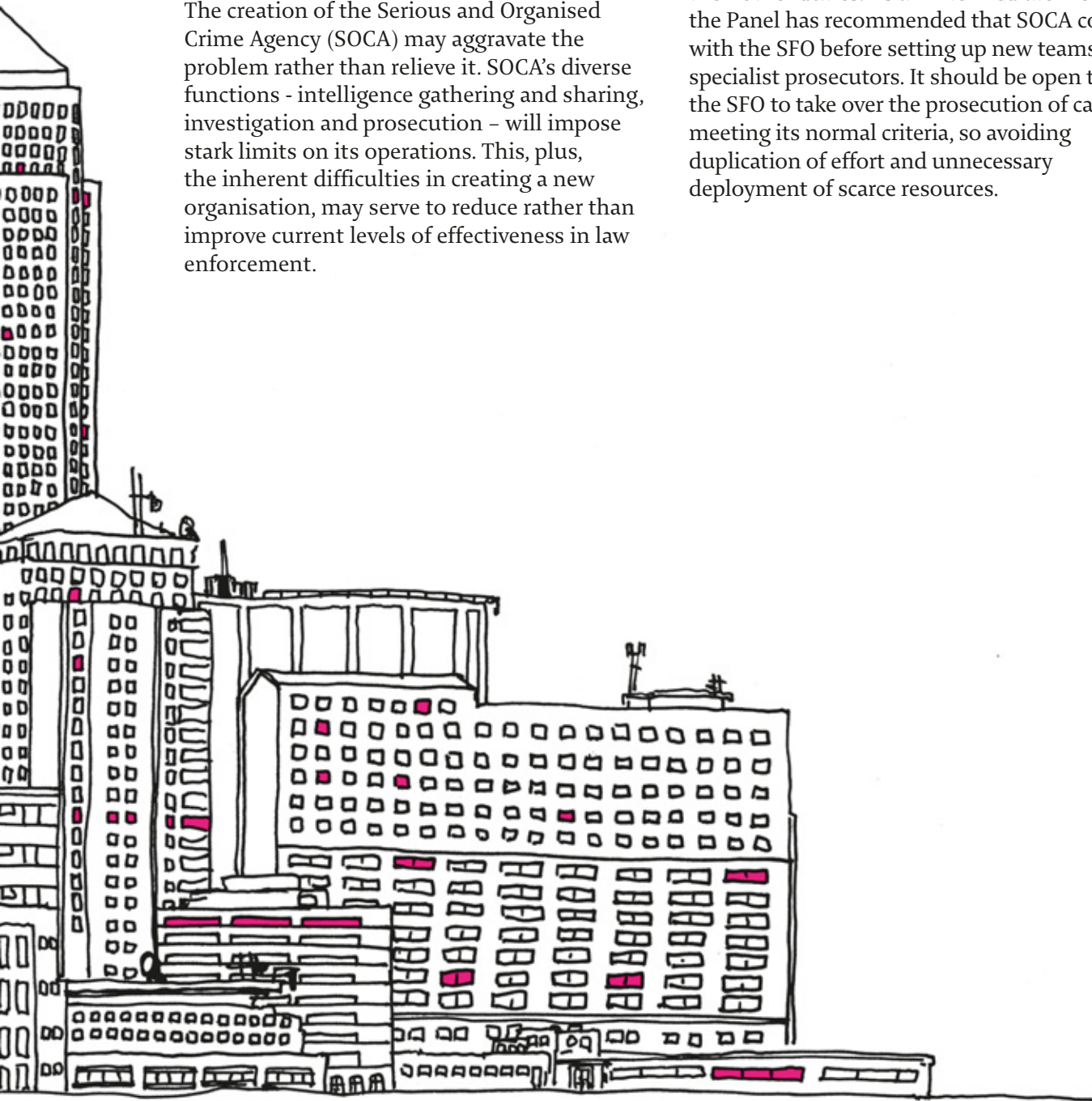
The Panel believes that the value of the Government's many anti-fraud initiatives are diminished by this long-standing weakness in law enforcement. As both the legislative armoury and institutional structure of policing are brought up to date attention must shift to the human resources required to maximise the impact of the Government's reforms. A focus on more high-profile kinds of organised crime may also lead to equally damaging commercial and financial fraud receiving insufficient police attention.



The number of officers tasked to fraud squads has declined steeply since the mid-1990s. There were 869 mainstream fraud investigators in 1995 and around 600 today. Supervising officers normally have other, non-fraud related, responsibilities and all officers are liable to be, and often are, called away to other duties. Skills are being lost to law enforcement as fraud squads are reduced in size and officers leave the Force altogether, disillusioned with the outcomes of successive policing cutbacks in their specialist areas.

The creation of the Serious and Organised Crime Agency (SOCA) may aggravate the problem rather than relieve it. SOCA's diverse functions - intelligence gathering and sharing, investigation and prosecution - will impose stark limits on its operations. This, plus, the inherent difficulties in creating a new organisation, may serve to reduce rather than improve current levels of effectiveness in law enforcement.

Particular attention must be paid to funding the recruitment, training and retention of specialist prosecutors and investigators, the need for which is growing fast in county forces as money laundering and confiscation legislation becomes more widely used. Where will SOCA find such staff? If the intention is to recruit them from the ranks of existing agencies such as the SFO or Crown Prosecution Service these already hard pressed bodies will be further depleted. Training prosecutors to do this specialised work will inevitably take time and distract trainers from their other duties. As an intermediate measure the Panel has recommended that SOCA consult with the SFO before setting up new teams of specialist prosecutors. It should be open to the SFO to take over the prosecution of cases meeting its normal criteria, so avoiding duplication of effort and unnecessary deployment of scarce resources.



## Business and Accountancy

### Restoring Professional Scepticism in Auditing

The Panel has called for some time for a return to a proper “professional scepticism” in auditing, recognising that it can be a powerful means of fraud detection and prevention. There are two essential elements to this; standard setting plus changes in the procedures and culture of auditing firms themselves.

The post-Enron period has seen standard setters place a growing emphasis on the detection of material fraud. The International Auditing and Assurance Standards Board (IAASB) has recently introduced new measures in the critical areas of audit risk, fraud, and quality control. The most notable is International Standard of Auditing (ISA) 240, “The Auditor’s Responsibility to Consider Fraud in an Audit of Financial Statements” which goes into far more detail than its British predecessors in describing the necessary level of professional engagement. The UK Audit Practice Board sees ISA 240 as a significant strengthening of British standards and is in the process of implementing it. Britain, in common with other members of the EU, has pledged to adopt international auditing and accounting standards by 2005.

ISA 240 requires auditors to obtain an understanding of a client’s organisation and its environment, including internal controls. Detailed risk assessment procedures are laid down with a requirement for the audit team to discuss “the susceptibility of the entity’s financial statements to material mis-statement”. They must consider “the attitudes, awareness and actions” of senior executives, the prevailing ethical culture and tone as well as systems and structures. Auditors must make “those charged with governance” aware of material weaknesses in the design or implementation of controls.

The IAASB has also issued a revised standard 220 on “Quality Control for Audit Engagements”. Audit firms will need to promote an internal culture that values professional independence and scepticism, supported by training, documented procedures and policies. Ultimate responsibility for this will rest with the firm’s senior partner.

The Institute of Chartered Accountants in England and Wales (ICAEW) has built on these initiatives by publishing “Fraud: Meeting the Challenge through External Audit”. This ten point action plan focuses on the cultivation of a culture of professional rigour, scepticism and judgement originating from the highest levels of a firm, especially when a client is deemed to be at risk from fraud. Auditors are also enjoined to prepare a specific and separate assessment of fraud risk, to tailor audit procedures accordingly and remember that management fraud (including so-called “aggressive earnings management”) is most likely to result in material misstatement rather than outright theft.

### Corporate Governance

The Panel expressed disappointment when neither the Smith or Higgs reports placed serious emphasis on the problem of corporate fraud. Two welcome opportunities to reconsider the issue have now arisen:

The Financial Reporting Council’s (FRC) first regular review of the Combined Code on Corporate Governance. The revised Code was published in July 2003, and applies for reporting years beginning on or after November 2003.

The FRC’s review of the Turnbull guidance on internal control and risk management (first published in 1999). Any revised guidance to directors will apply to accounting periods commencing on or after 1st January 2006.

The Panel's submission to Higgs argued that non-executive directors should have an explicit role in assessing whether fraud risks have been properly identified, and whether adequate preventive measures are in place.

This means that:

Non-executives must be satisfied that the company has clear and properly communicated anti-fraud policies.

All directors (and non-executive directors in particular) must be assured that the company has conducted a proper risk assessment and has installed adequate risk management and internal control procedures.

Non-executives must ascertain that staff can report suspicions of fraud to managers untainted by those suspicions; that they will receive reports of material problems; and that appropriate actions will be taken.

All non-executives must undergo appropriate training and the entire Board must submit to the procedures it imposes on employees.

Listed companies should be required to report material matters involving director, or senior management, malpractice to the shareholders. A more open approach should be seen as enhancing a company's reputation rather than diminishing it.

The Panel would also like the Combined Code on Corporate Governance to oblige listed companies to report to shareholders on anti-fraud policies and programmes.





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