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Annex 2: Review of Financial Management Relating to CPO Fraud

Contractual review of the financial
management of regeneration projects

18th September 2018

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Kevin Bartle
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18 September 2018

Dear Kevin

Project Rose - Support in relation to fraud investigation

We have pleasure in enclosing the seventh draft of our report (the 'Report') containing the contractual review findings of Project Rose, our engagement to provide support in relation to a fraud investigation ('the Project') on behalf Barnet Council ('the Council').

Scope of work and limitations

The scope of this project was agreed in Grant Thornton's contract with the Council dated 22 January 2018 ('the Terms of Engagement') and the variation letter dated 19 February 2018. A further amendment to scope was agreed with the client in writing (via e-mail) on 20 March 2018. This contractual review Report is based on our findings to date. Our review of the affairs of the Council and its partner organisations does not constitute an audit in accordance with Auditing Standards and no verification work has been carried out by us; consequently we do not express an opinion on the figures included in the report. At your behest it has been shared with Capita representatives of Re and CSG Finance and is updated to reflect our consideration of their detailed comments.

Limitation of liability

We draw the Council's attention to the limitation of liability clauses in paragraphs under section 18 in the Terms of Engagement.

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Disclosure and reliance

We agree that the Council may disclose our Report to its professional advisers directly involved in the Project, and also to officers and members of the Council solely in relation to the Project, or as required by law or regulation, court or supervisory, regulatory, governmental or judicial authority without our prior written consent but in each case strictly on the basis that prior to disclosure you inform us that (i) disclosure by them is not permitted without our prior written consent, and (ii) we accept no duty of care nor assume responsibility to any to any person other than the Council.

The Report should not be used, reproduced or circulated for any other purpose, in whole or in part, without our prior written consent, such consent will only be given after full consideration of the circumstances at the time. These requirements do not apply to any information, which is, or becomes, publicly available or is shown to have been made so available (otherwise than through a breach of a confidentiality obligation).

To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Council for our work, our Report and other communications, or for any opinions we have formed. We do not accept any responsibility for any loss or damages arising out of the use of the report by the Council for any purpose other than in connection with the Project.

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Forms of report

For the Council's convenience, this Report may have been made available to the Council in electronic as well as hard copy format, multiple copies and versions of this Report may therefore exist in different media and in the case of any discrepancy the final signed hard copy should be regarded as definitive.

Confidentiality

This work is confidential. No information relating in any way to our work, is to be disclosed to any third party (other than those the Council has confirmed are assisting it in connection with this investigation) without the Council's prior written consent.

General

The Report is issued on the understanding that the management of the Council have drawn our attention to all matters, financial or otherwise, of which they are aware which may have an impact on our Report up to the date of signature of this report. Events and circumstances occurring after the date of our report will, in due course, render our report out of date and, accordingly, we will not accept a duty of care nor assume a responsibility for decisions and actions which are based upon such an out of date report. Additionally, we have no responsibility to update this report for events and circumstances occurring after this date.

Notwithstanding the scope of this engagement, responsibility for management decisions will remain solely with the Council and not Grant Thornton. The Council's management team should perform a credible review of the recommendations in order to determine which to implement following our advice.

We understand this advice is being sought for the purpose of enabling the Council to receive legal advice in respect of the fraud investigation and the actions the Council should take as a result.

We would like to thank the Council's officers and those of the other key partners for making themselves available during the course of the project.

Contacts

If there are any matters upon which you require clarification or further information please contact the Engagement Lead Guy Clifton on 0207 7282903.



Guy Clifton

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1. Executive Summary

Executive Summary

Background to the review

Grant Thornton was commissioned by the London Borough of Barnet (the Council) to provide support in its response to the discovery of an alleged fraud.

The fraud has since been verified and relates to transactions associated with Compulsory Purchase Orders (CPOs) in the context of the Council's Regeneration programmes.

We understand that the fraudulent transactions were initiated by a perpetrator ("the Individual") from within Regional Enterprise Limited (Re), the Council's joint venture with Capita plc through the Development and Regulatory Services "DRS" Contract.

These transactions were then processed by Capita, but this time in their separate role as Service Provider of the Council's finance function via the Customer Support Group "CSG" contract.

The purpose of this report

This is the second annex ("Annex 2") to the Review of Financial Management Relating to CPO Fraud – Findings and lessons learned.

The Review of Financial Management relating to CPO Fraud contains an action plan for controls (Appendix A p20) and an action plan for the forensic review (Appendix B p34). Annex 1 supports the summary findings with a detailed review of financial and other controls across the Council's regeneration activities through Re and the financial back office services provided by Capita to both Re and the Council, in relation to the fraud.

This Annex 2 to that report provides a narrative of what contractual obligations were in place within the DRS and CSG agreements, if and how they were followed and any potential breaches arising from our understanding of the fraud.

Overview of findings

Our review findings highlight the following events:

- The Individual is believed to have committed a fraud to a detected value of £2,063,972 by directing CPO payments to personal bank accounts.
- The fraudulent payments were ultimately identified by a bank in receipt of those payments rather than through the Council's own control processes. Within our agreed scope, we found the fraud exploited the following control failures for which Capita are directly or indirectly contractually responsible:
 - There was a lack of control arising from a poorly maintained Scheme of Delegation and the absence of a supporting scheme of financial authorisation for non-council employees. This meant the Individual could gain unscrutinised access to cost centres on the financial ledgers. This is discussed more fully in Annex 1.
 - The lack of effective review controls over the financial ledgers and resulting treasury-enabled payments, allowed the Individual to request and receive 62 inappropriate payments to personal bank accounts.
 - A lack of effective review of journal amendments requested by the Individual enabled fraudulent costs to be concealed on the ledger.
 - The monthly and annual budgetary control process provided by CSG Finance for capital projects in Re lacked sufficient rigour to challenge unusual transactions and journal entries.
 - Within the scope of our review, the control environment did not identify or mitigate significant financial control weaknesses prior to the fraud.
 - Poor accounting controls, meant reporting errors and fraudulent accounting entries designed to mislead Re and CSG Finance were not detected.
 - Weakened scrutiny over regeneration scheme KPIs reduced Re's ability to identify these failings.

Scope and approach

The contracts we reviewed

This Report considers the contracts the Council relies upon both for the execution of its regeneration programme, and for its back office services.

The Council's relevant contracts from which our key findings are drawn are both dependent on Capita:

Contract 1: The London Borough of Barnet and Capita (BDRS) Limited relating to the provision of Development and Regulatory Services signed 5th August 2013 "DRS"

The contract is delivered by the property and infrastructure business of Capita and was expected to be worth £154m to Capita over 10 years from the 1st October 2013 under a joint venture: Re (Regional Enterprise) Limited, company number 8615172 to act as Service Provider to the Authority for the Council's regeneration programme.

Prior to its renaming, the joint venture was originally called "Capita BRDS" in the DRS contract. Re Limited is 51% owned by Capita plc and 49% owned by the Council. Capita holds 4 of the 6 Board positions with 2 held by members of the Council giving Capita majority ownership and control.

Under Clause 41 "Bond, Deed of Guarantee and Collateral Warranties" the DRS contract Guarantor is Capita Plc company number 02081330. The Bond itself forms Schedule 6 of the contract. Substantively this means Capita Plc is responsible for any control deficiencies discovered within Re during our investigation.

Contract 2: New Support and Customer Services (NSCSO) Partnering Agreement between the London Borough of Barnet and Capita Business Services Limited. "CSG"

Under this contract Capita delivers a range of services including corporate programmes, customer services, estates, finance, human resources and

payroll, information systems, procurement, revenues and benefits. The contract was expected to be worth £320m over 10 years commencing September 1st 2013.

Our approach to the contractual review

This contractual review summarises the most significant breaches that have or may have taken place on each contract, which we consider enabled the fraud to take place.

Our evidence-based approach incorporated a review of the DRS and CSG contracts, evidence from the accounting and purchase ledger systems and interviews with staff from across the Council, Re Limited and CSG Finance.

In light of the evidence and understanding of control deficiencies captured by our investigation into the fraud, we reviewed the contractual obligations under each contract.

Each contract contains binding Clauses, Output Specifications and Key Performance Indicators that have or may have been breached by Re or Capita as Service Providers to the Council, who are referred to in both contracts as the "Authority".

We initially sought to determine how Private Treaty Acquisition (PTA) and Compulsory Purchase Order (CPO) payments would normally be recorded in the Council's financial and reporting systems. We wished to determine if there was a difference between legitimate and fraudulent transactions.

The report that follows highlights the contractual review points arising from that exercise. Please note the list is not exhaustive.

Summary of findings

Erroneous or misleading reporting

Both the DRS and CSG contracts emphasise the importance of their Service Provider not providing erroneous or misleading reports. We were able to identify errors that occurred around the same time as the fraud as well as where fraudulent entries from the Individual were accounted for erroneously.

Unusual transactions appearing in control accounts that should have been challenged by CSG business partners as part of the monthly review and reconciliation process, but were not include fraudulent costs, mis-posted receipts and unusual journal transactions:

- Annex 1 of this report details our concerns regarding how CSG business partners were using control account ledgers to record CPO / PTA transactions without reference to the either the Council's fixed asset register or the estates systems.
- Our forensic accounting work identifies how fraudulent amounts appear capitalised and netted off against income at Year End, which should not have been, under the CIPFA code of practice on local authority accounting.

We believe this demonstrates a lack of control and scrutiny that contributed to the fraudulent transactions passing unreported – particularly as the fraud exploited other accounting errors and incomplete bookkeeping.

We would have expected to see knowledge of documented procedures for a consistent accounting of this class of transactions, and in particular the recognition of what was spent, owed or recovered at any point in time, depending on the specific PDA agreement under which the transactions were executed.

In our judgement the resulting reports contained undetected errors arising from the fraud, which misled regeneration managers, and consequently the Council, via its Growth & Regeneration Oversight Board (GROB), into believing the Service Provider's accounting for CPO / PTA payments and related income was complete.

Practical implications

The overall practical implication of our analysis is that Re and Capita may not have been in sufficient control of their Regeneration accounting or treasury contractual obligations.

Though our report has a particular focus on CPO / PTA transactions, we conclude Capita must demonstrate to the Council how its accounting practices with respect to the Council's assets and resources now meet the performance and commitments made in their DRS and CSG contracts.

Each contract clause could be viewed in isolation, however the combined effect appears systemic:

- Though both contracts had different goals, the Council and its Service Provider in each must ensure proper stewardship and control over Council assets and cash.
- The collective contractual control over contract standards, reporting quality, record keeping, treasury and budgetary management that should have been in place requires constant focus from the Council, Re and Capita.

Summary of findings by key contractual obligation

Our key findings are summarised against the following contractual clauses, service obligations and key performance indicators:

DRS Contract:

- Clause 5.2.1 Contract Standards: Good industry practice compromised by lack of supervision; Council not warned of gaps in the scheme of delegation or performance gaps against Capita's method statements; and concerns regarding the training and knowledge of Capita personnel.
- 9.2 Authority Monitoring Clause 9.2.3 fraudulent, erroneous or misleading reporting: The fraud led to erroneous and misleading reports.
- REGEN015 Budgetary Control: Costs accrued out of phase.
- REGEN016 Recovery of Authority's historic costs within 12 weeks: Accrued CPO / PTA spend not tracked against developer repayment.
- REGEN017 Maintaining effective financial records: Unmatched receipts appropriated to conceal fraud and fraudulent costs capitalised.
- REGEN018 File monthly returns for each regeneration: Lack of detail with respect to land acquisitions or developer receipts.
- REGEN002 and REGEN003: Securing and implementing a CPO: Record keeping concerns undermining confidence in CPO procedures.
- REGEN089: Active monthly regeneration budget management: Lack of detail with respect to land acquisitions or developer receipts.
- REGENKPI02 – Budgetary and Financial Controls: Insufficient control / evidence of recovery of developer receipts against target (85% in 2 months)
- Policy KPI: Adherence to information security policy for system access.

CSG Contract:

- 25.2 Authority Monitoring Clause 25.2.3 fraudulent, erroneous or misleading reporting: The fraud led to erroneous and misleading reports.
- FIN001 Financial Administration and Stewardship: Inconsistent administration of accountability procedures and financial regulations; lack of maintenance of the Finance Scheme of Delegation (and scheme of financial authority for non-council employees).
- FIN005: Budget Monitoring: Control deficiencies in tracking and controlling project, capital and revenue expenditure against budget.
- FIN006: Strategic Projects: Concerns regarding the level of scrutiny, understanding and financial leadership from CSG.
- FIN007: Corporate Reporting: Cost of fraud not detected in 2016/17 accounts
- FIN009: Treasury Management: Lack of control regarding CHAPS payments processing checks on documents and signatures.
- FIN004: Financial Statements, Costing, Modelling and Options Appraisal: Concerns regarding the level of scrutiny provided by CSG.
- FIN016: Systems Accounting: Fixed asset register to be maintained all year.
- FIN019: Payments (Accounts Payable): CSG business partner training questioned.
- PS001: Compulsory Purchase Order: System and reporting concerns.
- PS013, PS019 and PS020 Acquisitions and Disposals: Property valuation concerns.

Recommendations and next steps

Recommendations arising from our contractual review

Our review of the DRS and CSG Contracts has identified a number of clauses where Re or Capita as respective Service Provider has or may have been in contractual breach.

We are mindful that several contractual remedies are available to the Council in both the CSG and DRS contracts, the Service Provider might be invited to rectify, repair or improve their services to the Council's satisfaction.

This contractual review Report points to specific clauses in each contract that may need to be re-emphasised as part of those discussions, most notably with regard to contractual governance, reporting, quality, cost recovery, reconciliations, and training.

From a contractual review perspective it is outside of the scope of this Report to make specific recommendations on remedies available to the Authority. Nevertheless, the Council is at liberty to take appropriate action as they see fit based on the findings of this contractual review.

Important caveat

Our findings are based on interpretation of the information provided by Capita and meetings we had with CSG and Re staff. A draft of this report has been shared with Capita and feedback on the findings and comments on factual accuracy has been provided by them and considered. However, this does not constitute full validation and agreement of the findings by them. Actions to address the recommendations set out in the action plan have been agreed with Capita and are in the process of being implemented.

Steps taken since discovering the fraud

Initiating an independent investigation into the fraud

We note that the Council's Interim Director of Finance brought in Grant Thornton UK LLP as independent advisors in January 2018 with respect to identifying the suspected fraudulent transactions, capturing the control weaknesses and identifying which contractual obligations need to be repaired to prevent this incident recurring.

The Interim Director of Finance also notified Capita of the investigation.

Implementing new Treasury Management procedures

We understand the Director of Finance reset authorisation levels and sign-off procedures for expenditure across the Council commencing with new Treasury Management Procedures issued on 25th January 2018.

Recovering the monies lost to the Council

Under DRS Contract Schedule 31 Clause 3 Fidelity Guarantee Insurance, the Council's Commercial Director sought recovery of the circa £2m identified as part of the fraud from Re (underwritten by Capita), which we understand was reimbursed on 18th May 2018.

Acting on recommendations and informing the Audit Committee

On receiving our initial draft Report, the Council's Interim Director of Finance with support from the Council's Commercial team began implementing control recommendations in consultation with Capita.

We understand the Audit Committee was briefed on 31st January and kept updated at the 19th April meeting.

2. Contractual Review

Introduction

Context

Grant Thornton UK LLP was asked by the London Borough of Barnet to consider whether the fraud, and actions and responsibilities associated with this event, constitutes a breach of contract by Re or Capita. Our response is captured in this section of our review.

In this report we refer to the London Borough of Barnet as “the Council” unless we are referring to its contractual role, when it is described as “the Authority”. Re is the “Service Provider” of the DRS contract. Capita is “the Service Provider” of the CSG contract.

The fraud is significant in terms of volume (62 identified incidents), value (circa £2m) and duration (approx. 18 months of transactions) and the Authority wants to ensure no breach of contract has occurred.

The Individual was employed by the Council before being transferred under TUPE to CSG Finance in 2013. They then moved to Re in 2015.

In this section we look at the relevant contracts, highlight the weaknesses identified in the earlier phases; and consider whether they constitute a breach of contract.

There are two contracts in question which pertain to the fraud.

Contract 1: The London Borough of Barnet and Capita (BDRS) Limited relating to the provision of Development and Regulatory Services signed 5th August 2013

This contract is known as the “DRS” contract, under which Re manages services for the Council including highways management, planning and development, regeneration, environmental health and trading standards services. The contract is delivered by the property and infrastructure business of Capita (at time of contract signature this was Capita Symonds Limited) and was expected to be worth £154m to Capita over 10 years from the 1st October 2013.

Following contract signature, Capita (BDRS) Limited was renamed “Re (Regional Enterprise) Limited” (Re). Re is a joint venture with the Council and is majority owned by Capita. Re’s services are underwritten by Bond, Deed of Guarantee and Collateral Warranties by Capita Plc.

Contract 2: New Support and Customer Services (NSCSO) Partnering Agreement between the London Borough of Barnet and Capita Business Services Limited.

This contract is known as the “Customer Support Group” or “CSG” contract. Under this contract Capita delivers a range of services including corporate programmes, customer services, estates, finance, human resources and payroll, information systems, procurement, revenues and benefits. The contract was expected to be worth £320m over 10 years commencing September 1st 2013.

Our approach

Our approach

We have focused on the contractual clauses most relevant to the fraud where there may have been a breach of contract by Re or Capita, as Service Provider. We also considered whether there is a concern regarding the relevant accounting standards because Schedule 1 of the CSG contract requires the Service Provider's adherence to all relevant legislative and regulatory frameworks.

We note that the DRS and CSG contracts were let separately and that a third party organisation could have won either contract in open competition.

We have therefore reviewed the findings and recommendations from the Report including Annex 1 against each contract's specific clauses, output specifications and key performance indicators.

We also reviewed the findings and recommendations against Council policy and any relevant codes (e.g. CIPFA) under which this contract is also governed.

Given there are two separate contracts, we have considered whether there is a breach in either or both of the contracts irrespective of the fact that the same parent organisation (Capita Plc) is substantively responsible for the Service Provider's performance under both agreements.

A deed of variation exists which sets up the CSG Service Provider as the provider of services to the DRS Service Provider. This means that remedies to breach of the CSG Contract should fix all but breach of the governance aspects of the DRS contract.

Our review of both contracts has identified a number of significant weaknesses which may have resulted in contractual breaches. We have identified and reported what we believe are fundamental weaknesses in budgetary control and financial accounting.

Reporting potential breach

We understand "breach" to be a general legal definition used to refer to a failure to satisfactorily meet the demands of a legally binding contract.

Both the DRS and CSG contracts contain detailed and extensive contractual terms and conditions as well as service requirements and key performance indicators ("KPIs") for the Service Provider. We looked for evidence of compliance with these demands leading up to, during and following the fraud. We also looked at where a Service Provider failure to satisfactorily meet contractual demands led directly or indirectly to losses incurred. To ensure our findings were reported consistently, we researched how previous breaches of contract had been raised and how they were acknowledged or rectified by Capita.

We note both the DRS contract and CSG contract detail consequences for the Service Provider of "Persistent Breach".

3. Key Findings: DRS (Re) Contract

Summary of key findings – DRS (Re) Contract

Contract Details: The London Borough of Barnet and Capita (BDRS) Limited relating to the provision of Development and Regulatory Services signed 5th August 2013. The “DRS” contract.

The DRS contract delivers a range of Development and Regulatory Services for the Council through the Re Limited joint venture.

Our Review of the financial management of regeneration projects demonstrates where Capita failed to provide sufficient control of their Regeneration accounting or treasury obligations in Re Limited and for the Council: We believe Re’s commercial governance was undermined by a lack of supervision of key performance indicators where the Head of Regeneration was responsible for data collation, particularly for CPO / PTA transactions. Specifically, financial control procedures designed to prevent erroneous or misleading reporting and ensure timely receipts from developers were not followed effectively.

In this regard Re has or may have been in breach across several DRS contract clauses, service requirements or KPIs. Specifically:

- Clause 5.2.1 Contract Standards: Good industry practice compromised by lack of supervision; the Council was not warned of gaps in the scheme of delegation or performance gaps against Capita’s method statements; or of concerns regarding the training and knowledge of Capita personnel.
- 9.2 Authority Monitoring Clause 9.2.3 fraudulent, erroneous or misleading reporting: The fraud led to erroneous and misleading reports.
- REGEN015 Budgetary Control: Costs appear to have been accrued out of phase.
- REGEN016 Recovery of Authority’s historic costs within 12 weeks: Accrued CPO / PTA spend was not tracked against developer repayments.
- REGEN017 Maintaining effective financial records: Incomplete bookkeeping and accounting errors used to conceal fraud and some fraudulent costs capitalised.
- REGEN018 File monthly returns for each regeneration: There was a lack of detail with respect to land acquisitions or developer receipts.
- REGEN002 and REGEN003: Securing and Implementing a CPO: Record keeping concerns undermine confidence in CPO procedures.
- REGEN089: Active monthly regeneration budget management: Lack of detail with respect to land acquisitions or developer receipts.
- REGENKPI02 – Budgetary and Financial Controls: Insufficient control over the evidence/recovery of developer receipts against target (85% in 2 months)
- Policy KPI: Adherence to information security policy for system access.

Key findings – DRS (Re) Contract

Contractual clauses where there has or may have been a breach

Contractual obligation	Evidence and observations
<p>Clause 5.2.1 Contract Standards</p> <p>Aside from meeting specific key performance indicators, the Service Provider must perform the contract in accordance with:</p> <ul style="list-style-type: none">(a) Good Industry Practice;(c) must warn the Authority of anything likely to prejudice the quality or purpose of the Services;(f) must ensure the Services are performed by appropriately qualified and trained personnel.	
<p>Clause 9.2 Authority Monitoring - 9.2.3 fraudulent, erroneous or misleading reporting</p> <p>The Service Provider must not submit fraudulent or erroneous reports. The Authority may increase monitoring if it reasonably believes the Service Provider's reports to be misleading.</p>	

Key findings – DRS (Re) Contract cont'd.

Output specifications where there has or may have been a contractual breach

Contractual obligation	Evidence and observations
<p>REGEN015, REGEN016, REGEN017 and REGEN018 Estate Regeneration Financial Management and Monitoring</p> <p>The Service Provider must manage the budgets for each regeneration scheme, shall recover the Authority's historic costs (revenue and capital) from the development partners, shall maintain effective financial records and file monthly returns for each regeneration.</p>	<p>[This area is currently blank in the provided image.]</p>

Key findings – DRS (Re) Contract cont'd.

Output specifications where there has or may have been a contractual breach

Contractual obligation	Evidence and observations
<p>REGEN015, REGEN016, REGEN017 and REGEN018 Estate Regeneration Financial Management and Monitoring</p> <p>The Service Provider must manage the budgets for each regeneration scheme, shall recover the Authority's historic costs (revenue and capital) from the development partners, shall maintain effective financial records and file monthly returns for each regeneration.</p>	

Key findings – DRS (Re) Contract cont'd.

Output specifications where there has or may have been a contractual breach

Contractual obligation	Evidence and observations
<p>REGEN089 – Active monthly regeneration budget management</p> <p>The Service Provider shall ensure that budgets assigned to the regeneration service are effectively managed and reported to the Authority monthly.</p>	
<p>REGEN002 and REGEN003 Securing and Implementing a CPO</p> <p>The Service Provider must project manage the CPO process working with legal, property services departments and external advisors.</p>	

Key findings – DRS (Re) Contract cont'd.

Key performance indicators where there has or may have been a contractual breach

Contractual obligation	Evidence and observations
<p>Key Performance Indicator REGENKPI02 – Budgetary and Financial Controls</p> <p>This KPI demands good financial management to recover all monies due from developers. It sets the bar at recovering 85% of monies due within 2 months of the due date.</p>	
<p>Policy KPI</p> <p>The DRS Partnership Manager is responsible for ensuring compliance with all Authority Policies.</p>	

4. Key Findings: CSG Contract

Key findings – CSG Contract cont'd.

Finance service requirements where there has or may have been a contractual breach

Contractual obligation	Evidence and observations
<p>FIN001 Strategic Finance and Financial Statements; Financial Administration and Stewardship</p> <p>The Service Provider shall work with the CFO to ensure good financial administration and stewardship on behalf of the general public and to ensure that the Authority's resources are managed in accordance with Legislation, financial regulations and guidance provided by CIPFA and other relevant Guidance.</p> <p>Specific obligations relevant to the fraud:</p> <p>"The Service Provider shall ensure that there are effective systems of internal financial control in place including (but not limited to) reviewing, maintaining and updating on an on-going basis the following:</p> <ul style="list-style-type: none"> • the accountancy procedures manual; • financial regulations; • the finance scheme of delegation; and • the recommended scheme of delegation for services (finance responsibility section)." 	

Key findings – CSG Contract cont'd.

Finance service requirements where there has or may have been a contractual breach

Contractual obligation	Evidence and observations
<p>FIN004: Financial Statements, Costing, Modelling and Options Appraisal</p> <p>The Service Provider is required to support project managers at the Authority in budget monitoring of projects by reviewing, checking and challenging the assumptions and information provided to enable informed decision making within the timelines specified in the project.</p>	

Summary of key findings – CSG Contract

Contract Details: New Support and Customer Services (NCSO) Partnering Agreement between the London Borough of Barnet and Capita Business Services Limited. The “CSG” contract.

In this section we have focused the interaction between the CSG contract and the DRS contract, and in particular the CSG contract’s finance services requirements (p25-30), and property and estate management service requirements (p31).

The DRS contract delivers a range of Development and Regulatory Services for the Council through the Re Limited joint venture. Re relied on the CSG finance team for proper control over Council assets. Our controls review has highlighted where Capita, as Service Provider under the CSG contract, failed to provide sufficient control of their estates management, accounting or treasury back office service obligations to Re Limited and the Council.

In this regard Capita has or may have been in breach of contract across several CSG contract clauses, service requirements or KPIs. Specifically:

- 25.2 Authority Monitoring Clause 25.2.3 fraudulent, erroneous or misleading reporting: The fraud led to erroneous and misleading reports.
- FIN001 Financial Administration and Stewardship: Inconsistent administration of accountability procedures and financial regulations; lack of maintenance of the Finance Scheme of Delegation (and scheme of financial authority for non-council employees).
- FIN005: Budget Monitoring: Control deficiencies in tracking and controlling project, capital and revenue expenditure against budget.
- FIN006: Strategic Projects: Concerns regarding the level of scrutiny, understanding and financial leadership from CSG.
- FIN007: Corporate Reporting: Cost of fraud not detected in 2016/17 accounts
- FIN009: Treasury Management: Lack of control regarding CHAPS payment processing checks on documents and signatures.
- FIN004: Financial Statements, Costing, Modelling and Options Appraisal: Concerns regarding the level of scrutiny provided by CSG.
- FIN016: Systems Accounting: Fixed asset register to be maintained all year.
- FIN019: Payments (Accounts Payable): CSG business partner training questioned.
- PS001: Compulsory Purchase Order: System and reporting concerns.
- PS013, PS019 and PS020 Acquisitions and Disposals: Property valuation concerns.

Key findings – CSG Contract

Contractual clauses where there has or may have been a breach

Contractual obligation	Evidence and observations
<p>Clause 25.2 Authority Monitoring - 25.2.3 fraudulent, erroneous or misleading reporting</p> <p>The Service Provider must not submit fraudulent or erroneous reports or risk Persistent Breach or Service Provider Default. The Authority may increase monitoring if it reasonably believes the Service Provider's reports to be misleading.</p>	

Key findings – CSG Contract cont'd.

Finance service requirements where there has or may have been a contractual breach

Contractual obligation	Evidence and observations
<p>FIN005: Budget Monitoring</p> <p>The Service Provider is required to provide monitoring of all Authority budgets to maintaining accurate, consistent and complete financial records and providing timely, correct, relevant information to the Authority and its services. Pertinent to this investigation, and amongst other requirements there is a special focus on:</p> <ul style="list-style-type: none"> • Projects - information on variances from budget • to enable analysis, comment and decision making; and • Capital and revenue – updating and reporting on information on variances from budget to enable analysis, comment and decision making. 	

Key findings – CSG Contract cont'd.

Finance service requirements where there has or may have been a contractual breach

Contractual obligation	Evidence and observations
<p>FIN006: Strategic Projects</p> <p>The Service Provider is required to provide finance or project management support to those projects which are of critical importance to the Authority, enabling it to deliver its business strategy – acting as a finance lead.</p>	
<p>FIN007: Corporate Reporting</p> <p>The Service Provider is required to ensure financial information in reports to external bodies, individuals, members and senior officers is accurate, consistent, complete and timely.</p> <p>Decisions must be made within the Authority's constitution, relevant financial regulations and the Authority's scheme of delegation. The Service Provider needs to produce capital and revenue monitoring reports and covering reports for committees in line with committee papers deadlines and the committee timetable.</p>	

Key findings – CSG Contract cont'd.

Finance service requirements where there has or may have been a contractual breach

Contractual obligation	Evidence and observations
<p>FIN009: Treasury Management</p> <p>The Service Provider is required to provide treasury management services including (but not limited to) the management of cash flows, banking, money-market and capital-market transactions, the effective control of the risks associated with those activities and the pursuit of optimum performance consistent with those risks.</p>	

Key findings – CSG Contract cont'd.

Finance service requirements where there has or may have been a contractual breach

Contractual obligation	Evidence and observations
<p>FIN016 Systems Accounting</p> <p>The Service Provider shall maintain and update the fixed asset register throughout the year and as part of the process of closing the accounts and shall ensure that it is accurate.</p>	
<p>FIN019 Payments (Accounts Payable)</p> <p>All appropriate training and support to staff to minimise the making of incorrect payments and to ensure that procedures are maintained.</p>	

Key findings – CSG Contract cont'd.

Property and estates management service requirements where there has or may have been a contractual breach

Contractual obligation	Evidence and observations
<p>PS001: Compulsory Purchase Order</p> <p>The Service Provider is required to provide 6 reports per annum with respect to the Authority's powers to make CPOs including details of timings and costs. They shall also act for the Authority where any CPO transaction is required.</p>	
<p>PS013, PS019 and PS020 Acquisitions and Disposals</p> <p>The Service Provider undertakes to follow the RICS Appraisals and Valuations "Red Book" to achieve the Authority's Real Estate objectives.</p>	

5. Appendices

Appendix A
Appendix B

Glossary of key terms
Control themes relevant to the fraud – 5 Pillars

Appendix A: Glossary of key terms

To help the reader of this report we set out below a glossary of the key technical terms used in the report.

BACS	Bankers Automated Clearing Service – automated payment service used for the majority of Council transactions.
Bankline	The electronic application through which CHAPS and BACS payments are made.
CHAPS	Clearing House Automated Payment System - automated payment service used to make same day payments at short notice.
CIL	Community Infrastructure Levy – a planning charge paid to the local authority by developers.
Control Account	A ledger account used to record balances of a number of subsidiary accounts, that may contain debit or credit entries that net off.
Cost Centre	A section of the Council's financial ledger (Integra) which to which costs may be allocated for accounting purposes.
CPO	Compulsory Purchase Order – Legal function allowing local authorities to obtain land or property without the consent of the owner.
CSG	Customer Support Group – The organisation that provides back office services, including financial management (CSG Finance) to the Council under contract with Capita (formerly the New Support Customer Organisation (NSCSO)).
GROB	Growth and Regeneration Operations Board – Council Governance body that oversees the progress and cost of development schemes
Integra	The IT system run by Capita that houses the Council's financial ledger system.
Journal	A record of financial transactions recorded on a financial ledger, including the movement of cost or revenue from one cost centre to another.
PDA	Principal Development Agreement – The overarching legal agreement between the Council and a development partner (i.e. a developer), that underpins a regeneration scheme.
POB	Partnership Operations Board – Council Governance body that oversees performance against contract terms for both Re and CSG.
PTA	Private Treaty Agreement – A means of buying a privately owned property whereby the Council negotiates terms with the owner via an agent, as an alternative to compulsory purchase.
Re	Regional Enterprise Limited – The arms length organisation that delivers the Council's development and regulatory services, a joint venture between Capita and the Council under the Development and Regulatory Services (DRS) contract.
S106	Section 106 of the Town and Country Planning Act 1990 governing payments to the Council from the Developer to help mitigate the impact of any proposed development.

Appendix B: Control themes relevant to the fraud – 5 Pillars

We have identified five broad themes to describe aspects of financial control that relate to the management of regeneration schemes, and the related finance support services provided by CSG – the Five Pillars. In our view, if any one of these control pillars were functioning effectively during the period, it should not have been possible for the Individual to perpetrate the fraud for such an extended period of time through prevention of the means and opportunity, or through detection or deterrence.

Key control themes – 5 Pillars				
<p>Pillar I</p> <p>Delegated authority and control over access to systems (CSG Finance Treasury, the CSG Finance, the Council)</p> <p>A lack of clarity over the lines of delegated authority and a lack of control over system access, created the opportunity to access cost centres for inappropriate use.</p>	<p>Pillar II</p> <p>Control over the processing of transactions (CSG Finance)</p> <p>A lack of robust review and challenge in the authorisation of payments and a lack of reconciliation to amounts due back from developers, allowed fraudulent payments to be made.</p>	<p>Pillar III</p> <p>Control over journals within the Integra ledger (CSG Finance)</p> <p>A lack of robust challenge and review in the authorisation of journals that enabled fraudulent transactions to be disguised.</p>	<p>Pillar IV</p> <p>Budgetary control and financial reporting (CSG Finance, the Council, Re)</p> <p>A lack of robust challenge from CSG Finance business partners and a lack of scrutiny at transactional level resulted in a lost opportunity to identify and question unusual payments.</p>	<p>Pillar V</p> <p>The financial control environment for regeneration projects (CSG Finance, Re, the Council)</p> <p>Insufficient review and professional scepticism by managers in CSG Finance and Re, contributed to significant financial control weaknesses in relation to regeneration projects. Many of these weaknesses persisted over a long period of time and should have been identified and mitigated as part of routine management activity. There was also insufficient oversight by the Council.</p>
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