FRAUD, CORRUPTION AND ETHICS

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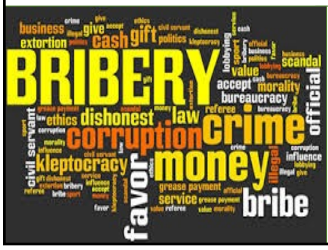
ACCRA



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LEARNING OBJECTIVES

- Discuss Fraud and Corruption
- Discuss Unethical Practices
- Discuss the Procurement Fraud and Corruption Schemes
- Discuss Red and Yellow flags in Procurement
- Ethical Practices

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CHECK THIS?

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VOICES FROM AFAR!!!

- "Let's not mince words: we need to deal with the cancer of corruption."
- "In country after country, it is the people who are demanding action on this issue. They know that corruption diverts resources from the poor to the rich, increases the cost of running businesses, distorts public expenditures, and deters foreign investors. They also know that it erodes the constituency for aid programs and humanitarian relief. And we all know that it is a major barrier to sound and equitable development.
- Corruption is a problem that all countries have to confront. Solutions, however, can only be home-grown."

-- James Wolfensohn,
World Bank President (1996)

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VOICES FROM AFAR!!!

- "Corruption is an insidious plague that has a wide range of corrosive effects on societies. It undermines democracy and the rule of law, leads to violations of human rights, distorts markets, erodes the quality of life and allows organized crime, terrorism and other threats to human security to flourish."
- "This evil phenomenon is found in all countries -big and small, rich and poor but it is in the developing world that its effects are most destructive. Corruption hurts the poor disproportionately by diverting funds intended for development, undermining a Government's ability to provide basic services, feeding inequality and injustice and discouraging foreign aid and investment. Corruption is a key element in economic underperformance and a major obstacle to poverty alleviation and development."

– Kofi A. Annan, U.N. Sec. Gen. (1997-2006)

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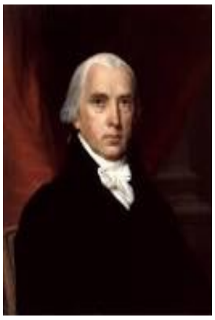
VOICES FROM AFAR!!!

- "The essence of Government is power; and power, lodged as it must be in human hands, will ever be liable to abuse".

  James Madison 1751-1836



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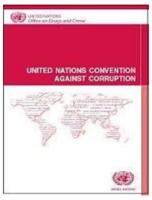
WHAT IS CORRUPTION?



The U.N. Convention Against Corruption doesn't define "Corruption."

The African Union Convention on Preventing and Combatting Corruption says "Corruption means the acts and practices including related offenses proscribed in this Convention."

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ECONOMIST DEFINITIONS

- Klitgaard's Equation:
  - C = M + P - R, where
  - C is corruption, M is Monopoly, P is Discretionary Power, and R is Responsibility.

- https://www.imf.org/external/Pubs/FT/fandd/1998/03/pdf/klitgaar.pdf

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WHAT IS CORRUPTION?

- In common usage, the word “corruption” means different things in different contexts. However, some basic working definitions of corruption include among others the following:
- “the abuse of an official position for personal gain.” Anechiarico and Jacobs (1996)
- “the sale by government officials of government property for personal gain” Schleifer and Vishny (1993).
- “the misuse of entrusted power for private gain” Transparency International (2001)
- “the abuse of public office for private gain” World Bank (1997)
- “the abuse of public or private office for personal gain” Asian Development Bank

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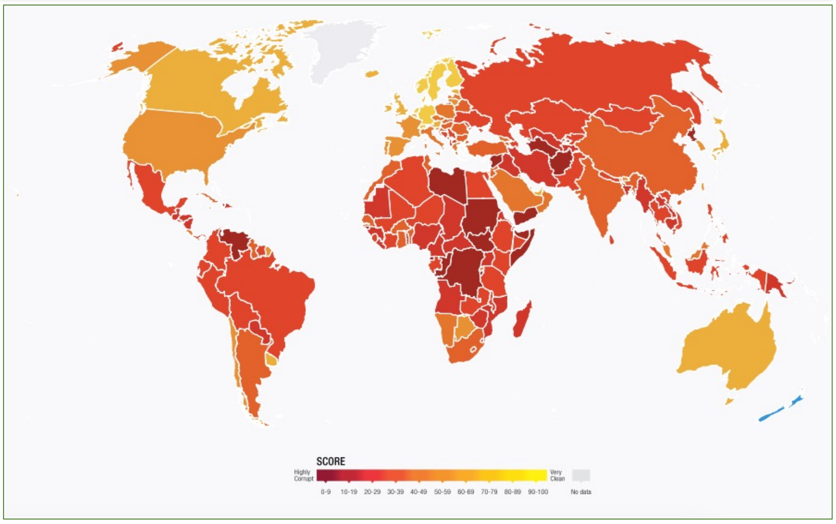
CORRUPTION PERCEPTIONS INDEX 2020



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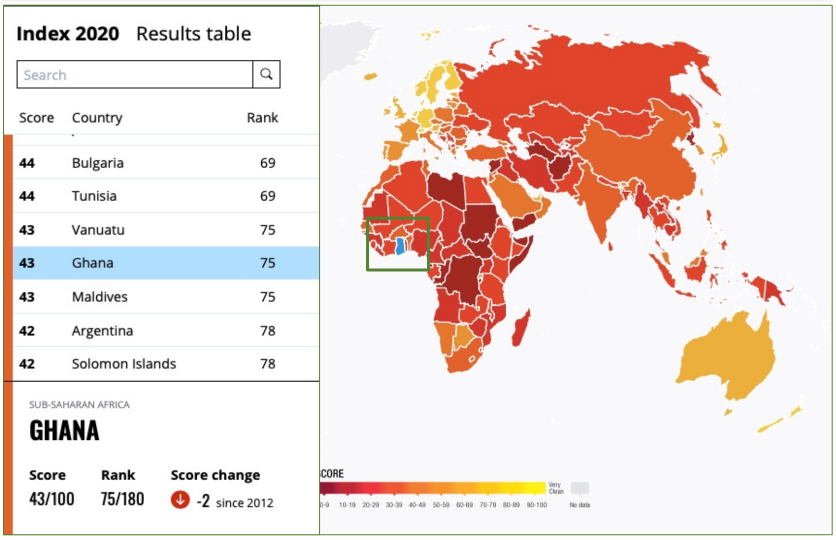
CORRUPTION PERCEPTIONS INDEX 2020



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CAUSES OF CORRUPTION - DISCUSSION

- Discuss and present the potential causes of corruption in public procurement.
- **Some possible causes**
  - Greed and the pursuit of power
  - Low pay
  - Commercial usage
  - Culture
  - State of market development
  - Political rent-seeking etc

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EFFECTS OF CORRUPTION

- The effect of corruption is generally agreed to be damaging in both developed and developing countries and there is little doubt about this accession.
- Bradhan (1997) argues that corruption has adverse effects not just on static efficiency but also on investment and growth.
- A payment of bribe to get a permit or license can potentially reduce the incentive to invest in a particular country.

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THE RISK OF CORRUPTION IN PUBLIC PROCUREMENT

- Corrupt practices are by nature covert and clandestine and it is only when the perpetrators are found out that the existence and extent of the corruption becomes known. In the end, it is a question of the risk for the perpetrator of being found out.
- The easier it is for the corrupt agent to hide his activities, the more likely it is that he will engage in those activities; the greater the risk of being found out, the less likely he is to run that risk.
- The implication of this is that, it is difficult providing an exhaustive list of corrupt practices in procurement since new and more ingenious methods will always be found. Notwithstanding, it is possible to identify the tried and tested methods which appear to be common to most systems globally.

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FRAUD

- The definition of fraud varies among countries and jurisdictions.
- But in simple terms, fraud is any **act or omission** that **intentionally misleads, or attempts to mislead**, a party to obtain a **financial or other benefit** or to **avoid an obligation.**
- Corrupt practices are generally understood as the **offering, giving, receiving, or soliciting**, directly or indirectly, anything of value to influence improperly the actions of another party.
- In a broader sense, it includes, but is not limited to, **theft, embezzlement, forgery and corrupt practices.**

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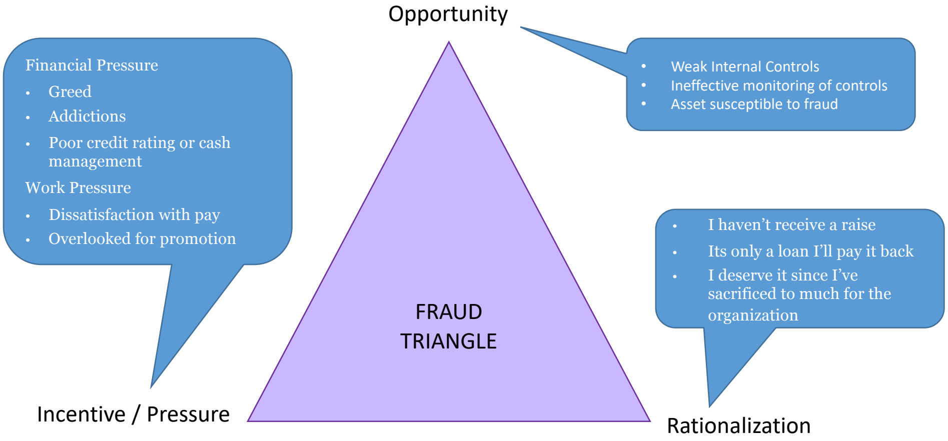
THE FRAUD TRIANGLE

It is generally accepted that the following three conditions must be present for fraud to occur:



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DISTINCTION BETWEEN FRAUD AND ERROR

Fraud	Error
• Intentional • Knowingly • Willfully • motive of gaining advantage • cheating or causing loss or injury • collusion	• Unintentional • Negligence • Genuine misunderstanding

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FRAUD

- **Symptoms - What do corrupt officials do?**
- Illegally award contracts
  - e.g. single source procurement
- Distort process (may not be illegal)
  - Commission unnecessary procurement
  - Manipulate choice of procurement method
  - Manipulate qualification/evaluation criteria
- It is not easy to spot legal distortion

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FRAUD

- **Symptoms – examples (bribery)**
  - Communications with one supplier
  - Drafting terms of solicitation to favour one supplier
  - Qualification/evaluation criteria to favour one supplier
  - Finalising contracts – "negotiations"

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EXAMPLES OF FRAUD

- Forging documents, preparing false entries in the Institution's systems or making false statements to obtain a financial or other benefit to which a person is not entitled;
- Offering or receiving something of value to improperly influence a procurement process;
- Asking for or receiving money for providing information to a vendor in the procurement of goods and services;
- Collusion or other anti-competitive scheme between suppliers during a tender process;

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CORRUPTION & FRAUD

CORRUPTION		FRAUD
Offering or receiving something to Influence improperly the action of another party	VS	Action of misrepresentation that knowingly is misleading to gain financial benefit or avoid obligation

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CLASSIFICATION

“GRASS EATERS	“MEAT EATERS”
Officers who **occasionally** engage in illegal and unethical activities, such as accepting small favors, gifts, or money for ignoring violations of the law during the course of their duties.	• Officers who **actively** seek ways to make money illegally while on duty.

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FRAUD AND CORRUPTION

- Contract implementation prone to fraudulent and corrupt practices.
- Section 93 of Public Procurement Act, 2003 (Act 663) as Amended on Corrupt Practices, states the following:
  - "Entities and participants in a procurement process shall, in undertaking procurement activities, abide by the provisions of article 284 of the Constitution".
  - "An act amounts to a corrupt practice if so construed within the meaning of corruption as defined in the Criminal Offences Act,1960 (Act 29)".
- Section 3. (1) of the office of the special prosecutor Act, Act, 2017, Act 959 "To achieve the object, the Office shall *(a)* investigate and prosecute cases of alleged corruption and corruption related offences under the Public Procurement Act, 2003 (Act 663);

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UNETHICAL PRACTICES

- "corrupt practice" is the offering, giving, receiving or soliciting, directly or indirectly, of anything of value to influence improperly the actions of another party;
- "fraudulent practice" is any act or omission, including a misrepresentation, that knowingly or recklessly misleads, or attempts to mislead, a party to obtain a financial or other benefit or to avoid an obligation;
- "collusive practice" is an arrangement between two or more parties designed to achieve an improper purpose, including to influence improperly the actions of another party;

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UNETHICAL PRACTICES – CONT'D

- "coercive practice" is impairing or harming, or threatening to impair or harm, directly or indirectly, any party or the property of the party to influence improperly the actions of a party;
- "obstructive practice" is:
  a. deliberately destroying, falsifying, altering or concealing of evidence material to the investigation or making false statements to investigators in order to materially impede investigations into allegations of a corrupt, fraudulent, coercive or collusive practice; and/or threatening, harassing or intimidating any party to prevent it from disclosing its knowledge of matters relevant to the investigation or from pursuing the investigation, or
  b. acts intended to materially impede the exercise of the an inspection and audit rights of a Donor/PPA

Source: World Bank Procurement Guideline, January 2011 Revised Version

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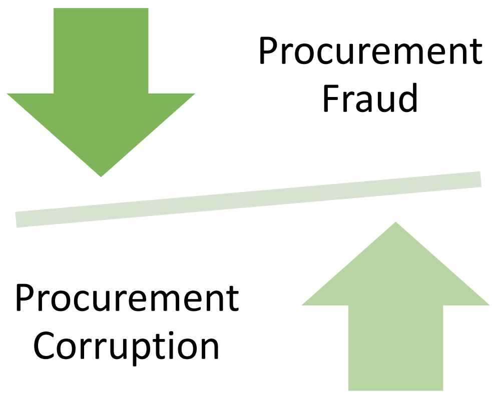

THE SCHEMES

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Admin/Civil/Criminal

- **Administrative –** Mistake and not amounting to gross negligence or criminal act
- **Civil -** Failure to perform or act appropriately – gross negligence
- **Criminal Act –** Intentional commission of a crime

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ADMINISTRATIVE

Breach of contract is a legal cause of action in which a binding agreement (contract) is not honored by one or more of the parties by non-performance or interference with the other party's performance.

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CIVIL FRAUD

Gross negligence is the "lack of diligence or care" or "a conscious, voluntary act or omission in reckless disregard of a legal duty and of the consequences to another party, who may typically recover exemplary damages.

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CRIMINAL FRAUD

Fraud is an intentional misrepresentation of the truth, involving trickery and deception in order to illegally enrich the fraudster.

- Fraud is cheating for profit.

•Fraud is characterized by acts of guile, trickery, concealment, or breach of confidence, which are used to gain some unfair or dishonest advantage.

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OUTCOME OPTIONS

- Criminal Fraud
- Civil Fraud
- Contract administrative adjustment
- Suspension
- Debarment

Recovery of Funds?
Civil Claim or Administrative

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COMPONENTS OF PROCUREMENT FRAUD

- There are five components that influence the likelihood and type of procurement fraud that can be perpetrated against an organization.
- It also represents the five bodies of knowledge necessary to be effective in procurement fraud prevention and detection.

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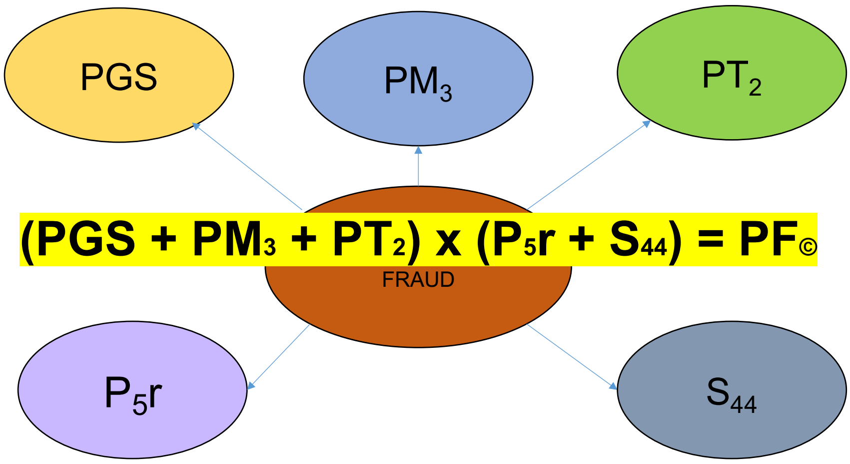
COMPONENTS OF PROCUREMENT FRAUD



$(PGS + PM_3 + PT_2) \times (P_5r + S_{44}) = PF$ ©

Source: Sheryl Steckler and Tom Caulfield, Procurement Integrity Consulting Services 33

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$(Pgs + PM3 + PT2) \times (P5r + S44)$ ©

PGS = **product (goods/services)**

PM_3 = the 3 procurement methods

PT_2 = the 2 payment types

P_5r = the 5 personality risks

S_{44} = the 44 traditional schemes

Source: PROCUREMENT INTEGRITY CONSULTING SERVICES, LLC

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GOODS OR SERVICES

$(PGS + PM_3 + PT_2) \times (P_5r + S_{44}) = PF_{©}$

Type of products be it "goods" or "services" will influence the fraud scheme that can be deployed!

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GOODS AND SERVICES

- Wrong categorization of Goods, Works, Consultancy and Technical Services
- Understatement of the need
- Overstatement of the needs
- Misrepresentation of needs
- Impractical timeframe
- Packaging contracts inappropriately
- Dividing contracts
- Probity/Integrity/Ethical issues

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GOODS AND SERVICES

- Narrow definition or commercial specification (e.g. use of brand name) Narrow terms of reference
- Definition of inappropriate product or service
- Biased specification / TORs (Probity & Ethical issues)
- Inadequate statement of requirement. TORs

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PROCURMENT METHODS

$$(PGS + PM_3 + PT_2) \text{ x } (P_5r + S_{44}) = PF_{\copyright}$$

1. Open Competitive
2. Restricted/Limited Competitive
3. Direct Procurement/Sole-Source

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PROCUREMENT METHODS

ABUSE OF METHODS

- Failure to identify potential sources
- Unqualified tenders
- Competitive Procurement Screwed
- Frequent use of Single or Sole Source Procurement
- Selecting inappropriate method

PROCUREMENT METHODS

BAD EVALUATION PANEL

- Unqualified Panel Members
- Failure to follow effective evaluation procedures.
- Use of minor deviations to disqualify tenderers
- Breaches of confidentiality.
- Failure to identify a clear winner.

PROCUREMENT METHODS

<u>BAD CONTRACT TERMS</u>

- Not understanding the details of Contract
- Undefined terms and conditions

PAYMENT TYPES

$$(PGS + PM_3 + PT_2) \times (P_5r + S_{44}) = PF_{©}$$

1. Fixed-Price
2. Cost Reimbursement

Fixed-Price Contracts

Under fixed-price contracts the government agrees to pay the contractor a mutually agreed upon compensation for contract performance.

Therefore, with a fixed-price contract the fraudster needs to create a scheme that reduces their cost margins without the government knowing, but appears to stays within the terms and conditions of the contract, for example through inappropriate manufacturing, counterfeit parts, falsifying delivery amounts, or using lower cost laborers.

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PAYMENT TYPES

- Possible malpractices at the payment stage include the following:
  - Corrupt contract amendments
  - Unjustified complaints
  - Overbilling/overpayment.
  - Lower than specified quality.
  - Fraudulent justification of delays.
  - Flagrant theft.

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PAYMENT TYPES

- Corrupt or fraudulent practices in financial management of projects may include:
  - Duplication of payments
  - Alteration of and tampering with invoices and other supporting documents.
  - Adulteration or duplication of accounting records.

Cost Reimbursement

Under cost-reimbursement contracts, the government agrees to pay the contractor a mutually agreed percentage of the contractor's cost to perform, plus profit.

With cost-plus contracts the fraudster will create a fraud scheme that allows them to increase profit through deception related to the companies' cost, for example by inflating cost, or submitting the same cost multiple times, or submitting reimbursement request for cost not incurred at all.

PERSONALITY TYPES

$(PGS + PM_3 + PT_2)\ x\ (P_5r + S_{44}) = PF_{\copyright}$

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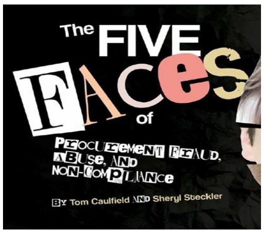
PERSONALITIES



1. Situational Fraudster
2. Deviant Fraudster
3. Multi-Interest Abuser
4. Well Intentioned Non-Compliance Employee
5. Disengaged Non-Compliance Employee

Source: https://www.procurement-integrity.net

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PERSONALITIES

SITUATIONAL FRAUDSTER

WELL-INTENTIONED NONCOMPLIANCE EMPLOYEE

The well-intentioned noncompliance employee believes that his or her willful deviation from the procurement process causes no harm to the organization or company. As a matter of fact, he or she sometimes believes that he or she is helping the organization or company in obtaining greater efficiency or obtaining better services. The well-intentioned noncompliance employee is normally an employee who has been with the organization or company for several years and has a good working knowledge of the procurement processes or requirements, and therefore knows how to advance his or her idea of efficiency. .

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THE SCHEMES

$$(PGS + PM_3 + PT_2) \times (P_5r + S_{44}) = PF^{©}$$

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"THE SCHEMES"

Bribes – Gratuity – Kickbacks – Extortion

- Rigged Specifications
- Collusive Bidding
- Excluding Qualified Bidders
- Unbalanced Bidding
- Leaking Bid Data
- Manipulation of Bids
- Unjustified Sole Source
- Change Order Abuse
- Split Purchases

- Conflicts of Interest
- Defective Pricing
- Cost Mischarging
- Co-mingling of Contracts
- Defective Products
- Product Substitution
- Counterfeit Parts
- Phantom Vendor
- False Statements & Claims

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BID RIGGING SCHEMES

- Complementary bidding
- Bid rotation
- Bid suppression

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COMPLEMENTARY BIDDING

- Competitors submit token bids without seriously attempting to win.
  - Bids too high to be accepted.
  - Bids that appear to be competitive in price but deliberately fail to meet other requirements of the tender.
  - Bids that contain special terms known to be unacceptable to the buyer.

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BID ROTATION

- Two or more contractors conspire to alternate business on a rotating basis.
  - Exchange information to guarantee that each wins a share of the purchasing entity's business.
- Might involve:
  - Subcontracts awarded to losing bidders.
  - Agreement to share a percentage of the winning company's profits.

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BID SUPPRESSION

- Contractors agree that at least one will refrain from bidding or withdraw a previously submitted bid.
- May involve threats.

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MARKET DIVISION

- Competitors divide markets among themselves and refrain from competing in each other's designated portion of the market.
- Markets are generally divided according to:
  - Geographic area
  - Customer

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PROPOSAL SCHEMES

- Altering/changing submission
- Accepting late proposal
- Unnecessary rebidding
- Limiting days to submit
- Unnecessary pre-qualification criteria

- **For what purpose?**

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RIGGED SPECIFICATION OR REQUIREMENTS

- These schemes are vey common. Essentially, an insider would like to procure goods or services from a specific contractor for whatever reason.

- The specifications or requirements are tailored so that only that particular contractor can successfully respond to the solicitation.

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RIGGED SPECIFICATION OR REQUIREMENTS

- Narrowing Requirements or Specifications
- Broadening Requirements or Specifications

- Let me stop and ask you – what protections are in place to stop these type schemes?

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UNBALANCED BIDDING

- Contracting personnel advising a favored bidder that specific line items in a bid request will not be included in the contract due to later budget cuts

- This allows the favored bidder to become the lowest bidder and win the contract.

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LEAKING BID DATA

- An insider sharing to help a favored bidder formulate a proposal
- This includes proprietary information, trade secrets pricing
- Such actions allows a contractor to know all about the bid of its competitors hence allowing them an unfair competitive advantage
- This can be extremely difficult to detect.

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CHANGE ORDER ABUSE

• After the procuring entity awards the contract, the corrupt contractor and insider submits fraudulent change orders.

  - To increase its price.
  - To improperly extend or expand contracts.
  - To avoid rebidding.

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Think about all the opportunities

- Presolicitation
- Solicitation
- Bid evaluation and award
- Post-award and administration

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"RED FLAGS"

- A good approach to the prevention of corrupt practices is to identify the potential indicators of the potential of corruption.
- They aimed at providing indications of those activities or elements of a procurement process which might be an indication of a corrupt act taking place.
- They can only give rise to a suspicion and hence, they should be used with caution
- Knowledge in using 'red flags' as a basis for investigation also requires the investigation team to be knowledgeable and competent in the procurement processes to ensure the investigation is meticulously carried out.

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RED FLAGS – FRAUD PROCUREMENT

- significant changes in behaviour that you've noticed
- an individual has large personal debts or financial losses, and a desire for personal gain
- audit findings deemed too be errors or irregularities
- transactions take place at odd times, odd frequencies, or involving unusual amounts or
- to odd recipients
- internal controls that are not enforced, or often compromised by higher authorities
- discrepancies in accounting records and unexplained items on reconciliations
- missing documents, or only photocopied documents available
- inconsistent, vague or implausible responses arising from inquiries

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RED FLAGS – FRAUD PROCUREMENT

- unusual discrepancies between the client's records and confirmation replies
- missing inventory or physical assets
- excessive voids or credits
- common names or addresses of payees or customers
- requests for change of bank details supposedly from suppliers then requests for
- refunds into the
- alterations on documents (such as back dating)
- duplications (such as duplicate payments)
- collusion among employees, where there is little or no supervision
- one employee has control of a process from the start to finish with
- no segregation of duties

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EXAMPLES OF 'RED FLAGS' IN BID RIGGING:

- Identical tenders are submitted by different tenderers either for individual line items in the tenders or the total bid.
- All tenders submitted are substantially higher than the procuring entity's cost estimate of the contract or than comparable tenders submitted by the same tenderers for similar work.
- A winning tenderer subcontracts performance of part of the contracted works to one or more losing bidders with or without the knowledge of the procuring entity.
- There is indication of a physical alteration of one or more bids, particularly at the last minute or after submission.

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EXAMPLES OF 'RED FLAGS' – CONT'D

- A tenderer submits different tender prices for the same line item on different contracts that are tendered close together in time.
- Qualified tenderers do not tender, especially if they initially took steps to tender, such as applying to prequalify. (this may be a sign that they have been coerced by the procuring entity or another tenderer not to bid).
- There is physical evidence of collusion in the bids submitted, such as different tenderers submitting tenders with the same handwriting or in the same type of envelope, or containing the same mathematical or spelling errors, or with the same contact information such as telephone or fax numbers.

(Adapted from Ware et al, World Bank Document, 2007)

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TRACKING CONTRACT ADMINISTRATION - "YELLOW FLAGS"

- "Yellow flags" give indications of potential corrupt practices likely to take place during the contract administration phase of a particular procurement. Some examples of "yellow flags" include:
- Contract specifications or scope of work are altered after contract is awarded
- Site inspection indicates that work performed was not in accordance with the technical specifications
- Site inspection indicates that project completion is less than that certified or that a completed project is not operational.

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Yellow Flags – cont'd

- Goods or services are not being used, or are being used for purposes inconsistent with intended purposes.
- Wrong quantities of goods and materials are delivered.
- Delays in the delivery of goods or services occur in part of the contract implementation process
- Site diaries and meeting minutes are not maintained.
- Cost overruns are inadequately explained or justified.
- Evaluations of contractors' performance are not recorded.

(Adapted from Ware et al, World Bank Document, 2007)

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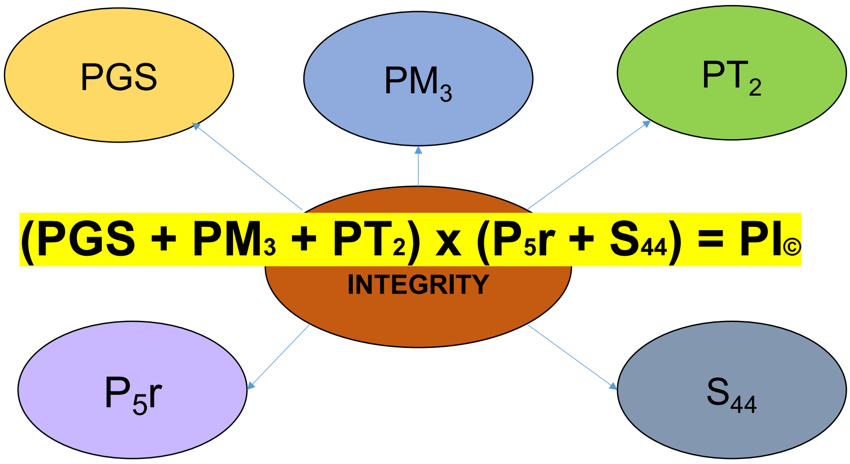
PROCUREMENT INTEGRITY



$$(PGS + PM_3 + PT_2) \times (P_5r + S_{44}) = PI^{©}$$

Source: PROCUREMENT INTEGRITY CONSULTING SERVICES, LLC

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The Procurement Integrity

Procurement Integrity Controls

(Prevention and Detection)

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PREVENTION CONTROLS

Prevention: "The action of stopping something from happening or arising." *(Webster's)*

- Segregation of Duties
- Proper Authorizations
- Adequate Documentation
- Background Checks
- Requirements Defined

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DETECTION CONTROLS

Detection: "The action or process of identifying the presents of something concealed."
(Webster's)

- Reporting Mechanism
- Fraud Awareness Training
- Reconciliation Controls
- Surprise Audits

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ETHICS AT PLAY

WHAT IS ETHICS?

- Moral principles that govern a person's behavior or the conducting of an activity.
- A code of values which guides our choices and actions and determines the purpose and course of our lives.

PURPOSE OF ETHICS CODE

- Promote the integrity of government.
- Maintain the trust and respect of taxpayers.
- Ensure objective, fair, and impartial decisions.
- Provide guidance on real or PERCEIVED conflicts of interest.
- Prevent unethical conduct BEFORE it occurs.

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MEANINGFUL ETHICS CODE

It is unrealistic to believe that any amount of training and creation of ethical expectations or other techniques will guarantee that all employees of an organization will always act ethically, but it is the obligation of organizational leaders to improve the odds that employees will conduct themselves consistent with ethical standards.

It is, however, reasonable to be expected to have taken reasonable steps to minimize the odds of ethical misconduct.

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SUSTAINING ETHICAL CULTURE

- Set Clear Expectations.
- Check Tone in the Middle.
- Make Ethics a Priority.
- Enforce and Incentivize the Code.
- Look to internal audit, inspector general or other independent oversight body.

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CAN THE LAW MAKE LEADERS MORE ETHICAL?

"The ultimate answer to ethical problems in government is honest people in a good ethical environment. No web of statute or regulation, however intricately conceived, can hope to deal with the myriad possible challenges to a [person]'s integrity or his devotion to the public interest."

John F. Kennedy, Message to Congress on April 27, 1961

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INTEGRITY IS….

Choosing right over wrong, ethics over convenience, an truth over popularity….these are choices that measure your life.

There is never a wrong time to do the right thing.

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IMPROVING ETHICAL PRACTICES

- Ensure that our personal, business, or other activities does not conflict with the lawful interests of your District/Institution/Office etc
- Avoid behaviors or actions that may negatively influence, or appear to influence, purchasing decisions, compromise actions etc.
- Protect confidential and proprietary information & decline accepting gifts that have the appearance of being improper.

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IMPROVING ETHICAL PRACTICES

- Make the time to gather whatever facts you need to come to a good decision. Don't rush to judgment before all the facts are in?.
- Since in many cases different stakeholders have interests that would be best served by different actions, it is important to carefully vet the facts one gathers to ensure that they represent as unbiased a representation of the situation as possible
- We tend to obey those in authority, including when authorities direct us to perform actions we believe are unethical. Keep in mind that you are ultimately responsible for your own actions, and that others & the Law, will hold you responsible for these actions.

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DO NOT RATIONALISE YOUR ACTIONS

- It's all for a good cause?
- I was just doing it for someone else's sake?
- It doesn't hurt anyone?
- Everyone's doing it?
- It's OK if I don't benefit personally?
- Be mindful that above are rationalizations that we all commonly use – and avoid them.
- Replace such rationalizations with a substantial and rigorous ethical deliberation process.

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SANCTIONS FOR UNETHICAL CONDUCTS

- Rejection of tenders, proposal, offer or quotation (Sec 32, Act 663)
- Fine not exceeding 1000 penalty units or imprisonment for a term not exceeding 5 years or both (Sec 92, 93)
- Debarment
- Cancelation of the portion of the loan allocated to a contract under World Bank funded projects

TAKE AWAYS

- Public service is a serious commitmment that requires a deep sense of social responsibility.
- Never be dismayed. In a culture where some lack of the values and game the system, those operating from a clear set of values can make a difference and move the conduct of others to a higher level.

RECOMMENDATION

- TEAM WORK
- SACRIFICE
- COOPERATION

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The End. Q & A

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