



Department of Foreign Affairs and Trade (DFAT)

Fraud and Risk Health Check of the Bougainville Partnership Program

17 May 2019

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Executive Summary

The Australian Department of Foreign Affairs and Trade (DFAT) engaged KPMG as an external service provider to conduct a Fraud and Risk Health Check of the Bougainville Partnership Program (BP). BP is managed by Abt Associates (the Managing Contractor).

This Health Check was limited to considering the fraud and risk management of the Managing Contractor undertaking activities under contract to DFAT in compliance with DFAT's policies.

Specific scope items included:

- Advice on Managing Contractor's process for overseeing funding arrangements across the three pillars with respect to addressing fraud;
- Assess the following: the Managing Contractor's process for identifying, addressing and reporting fraud risk at the project delivery level; the Managing Contractor's compliance with DFAT policies and guidelines to mitigate potential fraud; whether fraud risks to the program are being identified, monitored and managed effectively; the processes and practices of the DFAT Bougainville team particularly around the issue of verification of invoices received;
- Consider and advise on the following: the systemic fraud risks to program implementation; the fraud risks to program implementation stemming from current project designs; and
- Making recommendations for possible improvement in all areas covered, including the Managing Contractor's operational manuals and internal guidelines.

Our detailed findings are contained from page 6 onwards.

Summary of conclusions and recommendations:

The Managing Contractor makes an organisational commitment to deter, prevent, and detect fraud as part of corporate governance and has established comprehensive fraud risk management policies and procedures. We have no indication of non-compliance to DFAT policies and guidelines.

The Managing Contractor considers fraud risk as part of ongoing risk management efforts, and performs regular fraud risk assessments.

The Managing Contractor promotes fraud deterrence through preventive and detective fraud control activities. Fraud control activities are designed to address risks identified in the program's risk assessments. The control activities include preventive controls, such as policies and procedures, as well as detective controls, such as forms and checklists.

The Managing contractor has established formal processes for the receipt, evaluation, and communications of potential fraud. Investigation and communication in the context of fraud cases is performed in coordination with DFAT.

Across all Pillars, the key fraud risks identified are potential misappropriation of funds from grants and procurement fraud. Controls put in place by the Managing Contractor aim to reduce the risk to a reasonable level.

We recommend to ensure ongoing communication with bank branches and to further enhance the document archiving process (see section 2 of this report). Overall, the Managing Contractor has implemented robust fraud risk management procedures and we have not identified major weaknesses. We note that, due to the challenging political and socioeconomic context and the nature of the Program, future incidents of fraud cannot be ruled out completely.

Introduction and scope

Engagement Objectives and Scope

The Bougainville Partnership Program (BP) is a Department of Foreign Affairs and Trade (DFAT) funded program managed by Abt Associates (the Managing Contractor). The BP is delivered under the Papua New Guinea Governance Facility (PGF) Deed which commenced in 2016 and which aims to realise greater coherence and co-ordination of Australia's investments in improved governance in PNG and with greater flexibility to respond to PNG's complex political and operating environment. The BP is structured around three thematic pillars that are integral to strengthening peace and stability in Bougainville and implementing the Bougainville Peace Agreement: (1) Autonomy and effective governance (2) Economic development and (3) Peace, security and community cohesion.

DFAT engaged KPMG as an external service provider to conduct a Fraud and Risk Health Check of the BP. This Health Check was limited to considering the fraud and risk management of the Managing Contractor undertaking activities under contract to DFAT in compliance with DFAT's policies.

Specific scope items included:

- Advice on Managing Contractor's process for overseeing funding arrangements across the three pillars with respect to addressing fraud
- Assess the Managing Contractor's process for identifying, addressing and reporting fraud risk at the project delivery level and determine whether the current control systems in place are appropriate for mitigating fraud
- Assess the Managing Contractor's compliance with DFAT policies and guidelines to mitigate potential fraud
- Consider and advise on systemic fraud risks to program implementation stemming from the local context political and development context
- Consider and advise on fraud risks to program implementation stemming from current project designs,
- Assess if fraud risks to the program are being identified, monitored and managed effectively
- Make recommendations for possible improvement in Managing Contractor's operational manuals and internal guidelines and procedures for consideration by DFAT and the Managing Contractor
- Assess the processes and practices of the DFAT Bougainville team particularly around the issue of verification of invoices received and make recommendations for improvement.

Approach and methodology

- Desk-based review of relevant documents
- Meetings and interviews with management and staff of DFAT and the Managing Contractor in Port Moresby
- In-country field work and meetings in Bougainville (Buka and Arawa)
- Production of the draft and final report

We performed the following:

Assessment of the Managing Contractor's efforts to address the following Fraud Risk Management points of focus across the three pillars:

- Fraud Risk Governance and Compliance with DFAT Policies
- Fraud Risk Assessment
- Fraud Risk Control Activities
- Fraud Investigation and Corrective Action

Assessment of fraud risks to the program across the three pillars

- Conducted interviews to identify potential fraud risks and schemes
- Rated risks by likelihood and significance
- Identified existing anti-fraud controls
- Evaluated the effectiveness of existing controls and made recommendations, if applicable

For a list of interviews conducted please see Appendix I on page 13.

Detailed Findings

1. Assessment of the Managing Contractor's Efforts to Address Fraud Risk Management Points of Focus

1.1 Fraud Risk Governance and Compliance with DFAT Policies

Approach:

During our review of documents and interviews conducted in Port Moresby and Bougainville we assessed whether the Managing Contractor:

- *Makes an organisational commitment to deter, prevent, and detect fraud as part of corporate governance*
- *Provides a solid foundation of fraud risk management by establishing a comprehensive fraud risk management policy*
- *Established fraud risk governance roles and responsibilities*
- *Communicates fraud risk management at all organisational levels*
- *Is compliant with DFAT policies and guidelines to mitigate potential fraud*

Observations

The Managing Contractor has provided the organisation's Fraud & Corruption Control Policy as per May 2018 and the APNGMS Operations Manual as per November 2018. The policies state that Abt Associates is committed to establishing and maintaining an organisational culture where effective fraud and corruption prevention is an integral part of day-to-day operations and that Abt maintains a 'zero tolerance' approach to issues of fraud and corruption.

The policies outline fraud risk management roles and responsibilities, fraud control strategies, conduction of regular fraud awareness trainings for all Abt personnel, conduction of regular fraud risk assessments, and reporting and investigation procedures.

We obtained an example of a fraud and corruption awareness training given to Abt employees.

During the field visit, interviewees confirmed that they have been provided policies and procedures and are required to attend regular training on fraud prevention.

Clause 25 of the Deed of Standing Offer dated: 4 April 2016 (DFAT Agreement Number: 72404) details DFAT's requirements and the Managing Contractor's obligations in relation to fraud.

It includes the Managing Contractor's:

- Obligation to manage fraud in compliance with the Commonwealth Fraud Control Framework
- Responsibility for preventing and detecting fraud
- Obligation to report fraud within a defined timeframe
- Obligations in the context of investigations
- Obligations to recover DFAT funds

The review of the Managing Contractor's policies and procedures, as well as interviews during the field visit gave us no indication of non-compliance to DFAT policies and guidelines.

Conclusions and recommendations:

The Managing Contractor makes an organisational commitment to deter, prevent, and detect fraud as part of corporate governance and has established comprehensive fraud risk management policies and procedures. We found no indication of non-compliance to DFAT policies and guidelines.

1.2 Fraud Risk Assessment

Approach:

During our review of documents and interviews conducted in Port Moresby and Bougainville we assessed whether the Managing Contractor:

- *Performs regular fraud risk assessments and considers a wide range of possible fraud schemes and exposures*
- *Estimates the likelihood and significance of risks identified*
- *Focuses on incentives and pressures, opportunities, and attitudes and rationalizations to commit fraud*
- *Identifies and evaluates existing controls for effectiveness to determine residual fraud risks that require mitigation*
- *Formulates effective and appropriate responses to all fraud risks*
- *Repeats the risk assessment process periodically and considers changes affecting the organization*
- *Thoroughly documents the fraud risk assessment*

Observations

The Managing Contractor conducted a fraud risk assessment at commencement of the Papua New Guinea - Australia Governance Partnership Program and utilised it to assist with compiling a fraud control strategy in compliance with the Commonwealth Fraud Control Framework. This assessment contains fraud prevention, detection, investigation and reporting processes and procedures. The program's fraud control strategy and risk assessment is reviewed annually.

We obtained and reviewed the Fraud Control Strategy and Risk Assessment as per March 2019 which sets out the internal and external fraud risks and the controls, including prevention, detection, monitoring and reporting which the Managing Contractor adopts to maintain zero tolerance to fraud for the Papua New Guinea-Australia Governance Partnership and the Managing Contractor's PNG Management Services Platform. The risk assessment outlines key fraud related risks identified for the program in areas such as Finance, Human Resources, Procurement, Grants, and IT.

Every 6 months, the Managing Contractor prepares the Bougainville Partnership Outcomes Report to communicate outcome achievements to DFAT. These reports include the BP Risk Matrix which describes and rates key risks to the program, and outlines existing and planned risk mitigations. The risk matrix also includes risks around fraudulent activities.

Conclusions and recommendations:

The Managing Contractor considers fraud risk as part of ongoing risk management efforts, and performs regular fraud risk assessments.

1.3 Fraud Risk Control Activities

Approach:

During our review of documents and interviews conducted in Port Moresby and Bougainville we assessed whether the Managing Contractor:

- *Promotes fraud deterrence through preventive and detective fraud control activities*

- Ensures that the design and implementation of fraud control activities link directly to the fraud risk assessment
- Ensures that fraud control activities include a range, variety, and mix of preventive and detective controls

Observations

As a preventive control, the Managing Contractor implemented detailed Small Grants Operation Manuals for the Bougainville Partnership Program. The manuals cover all aspects in the granting process for grants managed by BP Pillar 2 (Commodity Support Facility) and Pillar 3 (Bougainville Community Grants, District Peace and Security Committees, District and Urban Youth Associations, Bougainville Youth Federation). The five volumes of the Operation Manual detail the general granting process and include templates, training materials, and procurement rules.

The District and Urban Youth Associations Handbook includes measures to prevent and detect fraud in the respective grants program.

We obtained and reviewed examples of templates used to manage grants. In interviews with Grants Officers it was explained, that these forms have been set up to be easily understood and populated by both the grantee and the Grants Officers.

The Small Grants Operation Manuals include examples of fraudulent activities and detail the recipient's duties to immediately report incidents to the Managing Contractor.

The Managing Contractor's Fraud Control Strategy and Risk Assessment outline control strategies for certain fraud risks. The BP Risk Matrix (appendix to the Bougainville Partnership Outcomes Reports), includes risk mitigations and control measures to address fraud and mismanagement of grants. We have included an overview of existing fraud control activities in the second part of this report.

We acknowledge that the BP faces specific challenges in terms of fraud prevention and detection, stemming from the historical, cultural, political and local context. Traditional measures such as contracts and law enforcement may be less effective than in other locations. To address this issue, the BP also promotes alternative measures to prevent fraud in the context of community driven development and social accountability.

Conclusions and recommendations:

The Managing Contractor promotes fraud deterrence through preventive and detective fraud control activities. Fraud control activities are designed to address risks identified in the programs risk assessments. The control activities include preventive controls, such as policies and procedures, as well as detective controls, such as forms and checklists.

1.4 Fraud Investigation and Corrective Action

Approach:

During our review of documents and interviews conducted in Port Moresby and Bougainville we assessed whether the Managing Contractor:

- Establishes, formally documents, and maintains a process for the receipt, evaluation, and treatment of communications of potential fraud
- Undertakes investigations of potential fraud, giving due consideration to the scope, severity, credibility, and implications of the communicated matter
- Communicates the results of the investigation to the appropriate internal authority and, when necessary, to external third parties
- Selects discipline, remediation, asset recovery, or other activities to address the findings of the investigation

Observations

The Managing Contractor is aware that any case of suspected or detected fraud must be reported within five working days from discovery to DFAT's Fraud Control Section.

The Fraud Control Strategy outlines the steps to be applied when incidents of fraud occur and refers to the DFAT Fraud Reporting Template. In the Managing Contractor's Operational Manual the tasks and responsibilities of Fraud Control Officers are described.

The Fraud Control Officers are required to notify the Chief Operating Officer and the Home Office Risk and Assurance Manager immediately upon being notified of an internal fraud incident.

All details of the case are documented on the DFAT prescribed Fraud and Corruption Report form by the Legal and Compliance Team. For further details see the Fraud Management section of the APNGMS Operations Manual.

The approach to fraud investigation and remedial action are determined in consultation with DFAT

The Managing Contractor updates DFAT on fraud cases in monthly meetings. This includes actions taken to recover funds.

As of April 2019, five unresolved fraud cases in the Bougainville Program were registered in the Managing Contractor's Fraud Register. For each case, the respective recipient of funds, value of alleged fraud, date of notification of the incident, Police report number (if applicable), and a description of the allegation is included in the register. Furthermore, the register includes comments on each fraud case by the Managing Contractor and the Fraud Control Section to outline recommendations and actions taken to recover funds, prosecute offenders, and to mitigate risks related to the incidents.

Capacity restrictions of the Bougainville Police can limit the success of fraud investigations.

Communication between DFAT's Fraud & Risk section (under the Program Strategy and Gender section) and Fraud Focal Points in each Program can potentially be strengthened (for example by inviting Fraud Focal Points to monthly update meetings with the Managing Contractor).

Conclusions and recommendations:

The Managing contractor has established formal processes for the receipt, evaluation, and communications of potential fraud. Investigation and communication in the context of fraud cases is performed in coordination with DFAT.

2. Assessment of Fraud Risks to the Program

2.1 Assessment of Fraud Risks to the Program

Approach:

To assess potential fraud risks to the Bougainville Program, we:

- *Conducted interviews to identify potential fraud risks and schemes*
- *Rated risks by likelihood and significance (gross risk without mitigating controls)*
- *Identified existing anti-fraud controls*
- *Evaluated the effectiveness of existing controls and made recommendations, if applicable*

In interviews with DFAT's and the Managing Contractor's management and staff, potential fraud risks and schemes were discussed. Across the three pillars, misappropriation of funds from grants and procurement fraud were consistently identified as the key risks to the program.

Furthermore, we identified systemic risks to program implementation stemming from the local context political and development context, and risks to program implementation stemming from current project designs. These risks may provide incentives, opportunities, or rationalization for fraudulent behavior.

For a summary of key risks identified and existing anti-fraud controls see Table I below. The ratings of likelihood and significance are based on a combination of the Risk Assessment Scoring Scales found in Appendix 2 and on our professional judgement.

We note that our overview of key risks to the program does not substitute the need to regularly perform a comprehensive fraud risk assessment. The fraud risks assessments conducted by the Managing Contractor described in section 1.2 of this report include the risks and controls identified by us to a certain extent. Our assessment should be used to further enhance risk awareness and efficiency of controls.

Table 1: Overview of Key Risks to the Program

Fraud Risks/Schemes	Likelihood [1-5]	Significance [1-5]	Existing Anti-Fraud Controls	Comments/Recommendations
<p>Misappropriation of funds from grants</p> <p>Examples:</p> <ul style="list-style-type: none"> Cash withdrawals are not used for intended purposes Downstream beneficiaries do not receive benefits Money is not spent on approved project purposes 	<p>4</p> <p>Rationale:</p> <ul style="list-style-type: none"> Past fraud cases Cash payments 	<p>4</p> <p>Rationale:</p> <ul style="list-style-type: none"> In addition to the loss of funds there is a significant reputational risk to the program 	<ul style="list-style-type: none"> Thresholds have been established to limit the amount of cash withdrawals for Youth Associations (K3,000 in areas with easy access to bank branches; K5,000 in remote areas) The Managing Contractor advises the banks via email prior to cash withdrawals In regular field visits, the Managing Contractor verifies that money is spent on approved project purposes. Payments are split into tranche payments. Before the first tranche payment, grantees must participate in fraud, compliance and financial management trainings. Before the next tranche payment is approved, it is verified that program requirements were met. Checklists are used to confirm that program finances are in order (such as the cash book) and that acquittals have been verified. 	<ul style="list-style-type: none"> The Managing Contractor's contact of the BSP branch in Arawa was not aware of the withdrawal thresholds and lists of grantees (the Branch Manager is relatively new to the position). We recommend ongoing communication with bank contacts across all pillars to ensure efficient and effective measures are in place to mitigate fraudulent transactions. The Managing Contractor's Team Leader in Arawa has confirmed that the Branch Manager has been provided all relevant information subsequent to our visit. Furthermore, options to gain online-banking access to grantee accounts are evaluated to increase the efficiency of monitoring. Documents and checklists used in the grants process are uploaded to a file system (Manuabada). Due to connectivity restrictions and the workload of scanning files, not all documents are uploaded. We recommend to define the key documents in the granting process which need to be saved in the file

				<p>system and to ensure complete and save archiving of these files.</p> <ul style="list-style-type: none"> Controls put in place by the Managing Contractor aim to reduce the risk of misappropriation of funds from grants to a reasonable level.
<p>Procurement fraud</p> <p>Examples:</p> <ul style="list-style-type: none"> Collaboration between recipient of project and service provider to inflate bills (kickback arrangement). Falsified receipts 	<p>4</p> <p>Rationale:</p> <ul style="list-style-type: none"> Past fraud cases Cash payments 	<p>4</p> <p>Rationale:</p> <ul style="list-style-type: none"> In addition to the loss of funds there is a significant reputational risk to the program 	<ul style="list-style-type: none"> Purchases by grantees are limited to a value of K10,000. Higher value purchases are performed by the Managing Contractor's centralized procurement function. Policies and procedures relating to procurement are in place (as part of the Operations Manual). Review of invoices. A schedule of rates has been implemented to regulate rates for different services such as travel allowances and vehicle hire. 	<ul style="list-style-type: none"> The controls put in place by the Managing Contractor aim to reduce the risk of fraudulent behavior in the context of procurement to a reasonable level.
<p>Systemic fraud risks to program implementation stemming from the local context, political context, and development context and risks to program implementation stemming from current project design</p> <p>Examples:</p> <ul style="list-style-type: none"> Lack of financial education of recipients 	<p>3</p>	<p>3</p>	<ul style="list-style-type: none"> Training (in areas such as Finance, Fraud and Compliance) is provided to recipients at program initiation and throughout the program. Relationship building and human intelligence to understand the local and political context. Rigorous policy to not pay for information. 	<ul style="list-style-type: none"> We appreciate that the Bougainville Program operates in a challenging political and socioeconomic context. The Managing Contractor is aware of this and focuses on developing suitable mitigating measures to prevent fraudulent activities.

<ul style="list-style-type: none">• Political risk of focusing on certain areas; challenges of information and project development in remote areas• Rent seeking behavior of some public servants• Traditional, customary ways of resolving conflicts• Attempts from individuals to be paid for providing information to resolve high profile conflict cases			<ul style="list-style-type: none">• Politicians are not allowed to be part of recipient groups as decision makers.• Application of the concept of social accountability.	
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Appendices

Appendix I — Overview of Interviews

DFAT	
s22(1)(a)(ii)	Counsellor (Bougainville)
	First Secretary
	Senior Program Manager
	Assistant Program Manager
	First Secretary
	Assistant Program Manager
	Program Manager
Managing Contractor	
s47F(1)	Director (Bougainville Partnership)
	Legal and Compliance Manager (Abt)
	Legal and Compliance (Abt)
	Finance Manager (Abt)
	Operations Manager (Buka)
	Program Manager Commodity Support Facility
	Finance Manager
	Team Leader (Arawa)
	Community Development and Grants Adviser
	Finance Coordinator
	Peace Adviser
	Peace and Security Committee (DPSC) and Operations Coordinator
	Project Officer
	Youth Coordinator
	Project Officer
	Community Grants Coordinator
	Grants Officer
	Administration and Procurement Officer
	Team Leader (Buka Office)
BSP Bank	
s47F(1)	BSP Branch Manager (Arawa)



Appendix 2 — Risk Assessment Scoring Scales

Likelihood - Based on Annual Probability of Occurrence		
Rating	Descriptor	Definition
5	Almost certain	>90% chance of occurrence
4	Likely	65% to 90% chance of occurrence
3	Reasonably possible	35% to 65% chance of occurrence
2	Unlikely	10% to 35% chance of occurrence
1	Remote	< 10% chance of occurrence

Significance		
Rating	Descriptor	Definition
5	Catastrophic	<ul style="list-style-type: none"> Major financial losses and reputational damage resulting in a termination of the BP Widespread employee morale issues and loss of multiple senior leaders
4	Major	<ul style="list-style-type: none"> Major financial losses and reputational damage resulting in a termination of some activities of the BP Widespread employee morale problems and turnover
3	Moderate	<ul style="list-style-type: none"> Moderate financial losses and minor reputational damage Widespread employee morale problems
2	Minor	<ul style="list-style-type: none"> Moderate financial losses and minor reputational damage General employee morale problems
1	Incidental	<ul style="list-style-type: none"> Minor financial losses and no reputational damage Isolated employee dissatisfaction