

Red flags

Procurement



Prepared for Auditors
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Introduction

Procurement fraud in the UK is not defined but industry experts put the figure at billions of pounds a year. Although data analytics to identify fraud are on the increase, manual detection techniques are an important part of fraud prevention approaches.

As auditors, we're all aware of that feeling in our gut when something isn't quite right. This is our professional scepticism at work! But we can't rely on our gut alone and there are often 'red flags' – where things appear a bit out of the ordinary or not as we'd expect – which point us in the direction of needing to do some further work to allay our concerns or indeed to highlight where something is wrong.

This document draws on information developed by the National Audit Office and Wales Audit Office and is supported by Police Scotland. It sets out some red flags to identify circumstances which may indicate the need for further audit work. While red

flags don't always mean there is an issue, they are intended to help you reflect, consider what the issue may be and potentially raise your concern in the first instance with your manager. A list of controls to help mitigate the risk of fraud and error is provided, and controls may be relevant to more than one risk area. We also give some examples of where things have or could go wrong.

This document aims to help auditors recognise a red flag when they see it and consider what it means for their audit. Auditors might want to review their programmes to ensure the expected controls are covered and may also want to enquire about what an audited body does to detect red flags.

You should not do anything that may compromise evidence or an ongoing investigation by internal audit or Police Scotland, or tip off a 'suspect'. Seek advice if you are unsure. (See contacts on [page 12.](#))

Red flags take a number of forms, such as:

- behaviour that falls short of what the public would expect
- behaviour that is ethically or morally wrong
- mismanagement by error or mistake, negligence or inadvertence
- intentional or wilful wrong-doing, and which may be considered criminal.



Key stages for audit



Procurement



Contracts



Payments



Processes



Procurement

Collusion among contractors

Red flags

- Evidence or suggestion of a close relationship between the bidding organisations.
- Limited competition in the sector. *Increases the chance that suppliers can manipulate the contract value.*
- The same contractors bid for each job. *May indicate price fixing.*
- All the bids appear expensive/are above the tender amount. *May indicate price fixing.*
- Certain contractors don't bid whom you would expect to. *May be the result of a pre-agreement between contractors.*
- Submission of suspicious bids. *Bids from fake companies to give appearance of competition.*
- Winning bidder sub-contracts some work to the losing bidder or a non-bidder. *May have agreed this arrangement prior to bidding.*
- There is a pattern to winning bidders or losing bidders, due to an agreement with bidders to manipulate their bids/not bid. *Could indicate bid manipulation.*
- Only one bid covers all requirements and the others are poor. *Could indicate bid manipulation.*
- Not declaring a connection with another bidder. *Could indicate bid manipulation.*

Example: Numerous bidders acted together during the procurement process for a large engineering contract in the public sector and worked collaboratively to submit bids that favoured a particular company. Some bids were exceptionally low, some withdrew their bids and some were content to wait until the next time round to submit a bid. Some of the losing bidders were used as sub-contractors, so they did benefit in some way. Collusion amongst bidders distorts true competition and reduces public confidence in the procurement process achieving value for money.

Controls

- **Joined-up working across the organisation**
- **Training on awareness of procurement process and procurement fraud**
- **Centralised contract register which is regularly reviewed and analysed**
- **Conducting due diligence to establish legitimacy of suppliers**
- **Strong controls around sub-contracting processes**



Procurement

Collusion between procurer and bidder

Red flags

- The person overseeing the award of a contractor has a relationship with the successful contractor, eg the public official holds a post with/owns shares/has a close family or friendly relationship with someone in the winning company. *A conflict of interests.*
- The contractor provides inappropriate gifts or rewards to a public official who accepts them. *Bribery.*
- The procurer requests gifts, a loan, fee or reward in return for competitive advantage. *Corruption.*
- Contract specification changes after preferred bidder is appointed. *Could represent malpractice against losing bidders.*
- One officer specifically deals with a particular supplier. *Could be corruption.*
- Supplier wins multiple bids. *Could be 'insider information' or 'hand holding' through the process.*
- Contract awarded to the unknown or 'surprising' contractor, such as one with previously reported underperformance (eg contracts terminated or exited). *Could indicate bid manipulation.*
- Losing bidder(s) has publicly expressed concerns regarding the process/decision to award. *Could be the result of a poorly defined process, creating risks to VFM.*
- Presence of a 'middle-man' whose existence cannot be easily explained or justified. *Could indicate a bribe or 'kickback' to an intermediary.*
- Favouring getting procurement done quickly over following proper process with appropriate evidence/documents. *Could indicate bid manipulation.*

Example: John is a procurement officer in a Scottish council. He has developed a good relationship with a particular company involved in several contracts related to construction. He indulges in gifts and hospitality, which was fairly low level at the start but over several years has increased to a point where he now depends on his 'perks'. John starts to look upon the company favourably and often designs the tender specification in a way that benefits the company. Without realising it, John is committing a bribery offence at the expense of the public purse.

Controls

- **Maintaining and actively monitoring the Register of Interests and the Register of Gifts & Hospitality**
- **Improving the culture of compliance with standing orders and OJEU requirements**
- **Training on the Bribery Act**
- **Segregation of duties**
- **Due diligence on suppliers**
- **Investigation of complaints**
- **Rotation of employees**



Procurement

Pre-tender

Red flags

- There is a lack of evidence that a needs assessment has been carried out as well as a lack of evidence around the decision to go ahead with the procurement. *Could be collusion with a supplier.*
- The need for or timing of a contract is altered. *Could be used to benefit a specific supplier.*
- Weak justification for the use of single-sourcing. *Could be used to favour a supplier.*
- Multiple procurements for the same goods/services. *Could circumvent approval and tender thresholds.*
- Tenders appear narrow or vague. *Could be to favour a supplier.*
- Abuse of waivers to extend or modify existing contracts. *Could be used to circumvent approval limits.*
- Contract splitting to circumvent approval thresholds.
- A lack of due diligence on potential suppliers. *Could result in significant financial and/or reputational risks.*

Example: Jane is a head of service and is concerned at unusually high levels of stock within a particular business area, which seems to have been the case for a number of years. She decides to investigate and finds that the stock comes from a certain supplier, the need appears questionable and is later established as unjustified. The internal investigation reveals that the manager in charge of stock was related to the supplier of the goods.

Controls

- **Training on procurement processes**
- **Internal audit activity**
- **Spend analysis to identify a large spend to a supplier which, when aggregated, breaches approval thresholds**
- **Tender evaluation framework agreed at procurement planning stage**



Procurement

Bid manipulation

Red flags

- Placing bid adverts in obscure places, or during holidays possibly including poorly articulated rules/unclear documentation. *Could imply the procurer has a bidder in mind before placing the advert, a desire to restrict the number of bidders or wants to circumvent procurement rules.*
- Altering bids or timetables. *Could imply the procurer has a bidder already in mind or has a desire to restrict the number of bidders.*
- Accepting late bids. *May indicate favouritism towards a bidder as well as breaking procurement regulations.*
- A limited number of bids or certain contractors do not bid. *Bidders may have agreed this arrangement prior to bidding.*
- Fictitious companies submit bids. *May indicate bid manipulation.*
- Sharing information between bidders. *May result in different bidders receiving different information, providing unfair advantage.*
- Manipulation of tender scoring process and disqualifying bids for unjustified reasons. *May indicate favouritism towards a bidder as well as breaking procurement regulations.*
- Contractor falsifies documents to secure a contract. *Could indicate fraud.*
- Bids are high priced and/or similar bid documentation received. *May indicate bid manipulation.*
- Same suppliers bid for every contract and/or a pattern emerges over time of which contractors submit bids. *May indicate bid manipulation.*
- Prices unusually close to procuring organisation's estimates. *May indicate collusion and bid manipulation.*

Example: A public body received anonymous information that a procurement manager was manipulating the bidding process by providing the details of competitors' bids to a favoured contractor. An internal investigation revealed that the procurement manager was sending details of competitors' bids from his work email to his home email address. The investigation established that the procurement manager thereafter altered the process to accept late bids, benefitting the favoured contractor. Workplace gossip suggested that the procurement manager often indulged in a round of golf at expensive Scottish golf courses at the expense of the favoured contractor. No record was found of the alleged Gifts and Hospitality.

Controls

- **Training on fraud awareness and procurement processes**
- **Internal audit on the security around bids and sensitive tender documentation**



Procurement

Where there is a single tender award

Red flags

- Overuse of single tender applications. *May indicate favouring certain suppliers (conflict of interest/bribery/corruption).*
- One supplier often favoured. *May indicate favouring certain suppliers (conflict of interest/bribery/corruption).*
- No records of why supplier was appointed. *May indicate procurement team has a related party interest in the supplier (conflict of interest/bribery/corruption).*
- Surprising supplier appointed. *May indicate an abuse of power/conflict of interest/bribery/corruption).*

Controls

- **Internal audit review, eg of suppliers and spend analysis**
- **Training on procurement and counter-fraud**
- **Clear procurement procedures**
- **Effective categorisation of spend in the ledger, eg all vehicle costs should be in the same codes**

Example: A contracts manager was heavily involved in influencing the procurement of a council's roads maintenance contract. A variety of plausible reasons were given as to why there should be a single tender award and the contract was awarded. The council participated in the National Fraud Initiative and found a match between the contracts manager's personal bank account (where his wages were paid into) and the bank account of the roads contracting company (where invoices were paid). Further investigation revealed that the contracts manager was a shareholder in the roads maintenance company concerned. There was no disclosure of this conflict of interests.



Contracts

Red flags

- A contractor invoices for work but there are no/inadequate checks that the work has been done to required standards before paying the invoice. *Inadequate validation of deliverables.*
- Costs/margins look unreasonable or are not clear in the context of risk/nature of contract and contractor performance. *Excessive profits or lack of transparency around the margins made.*
- Design of contract leaves it vulnerable to manipulation. *Elements of payment by result or targets can create risks for data manipulation.*
- Internal audit or the audit committee has raised concerns about a contract, eg its award or how it is managed.
- Evidence of underperformance through published data, user feedback or whistle-blowing, client concerns, internal audit, audit committee or the media. A contractor is performing below expectations, but no penalties have been imposed. *Underperformance not acted upon.*
- Client or contractor reluctant to meet or talk about contract. *Poor relationships exist.*
- Contract is awarded on the basis of an unrealistically low bid which is then made up for by contract variations, duplicate invoices, sub-standard delivery etc. *Fraudulent variation of contract.*
- Unspecified items on invoices and invoice prices/amounts do not match contract. *Fraudulent charging.*

Example: A roofing company submitted an attractive low bid for a council's lucrative roofing repairs contract, with the full intention of submitting further multiple variations during the contract term to compensate for the initial low bid. The contract was awarded and the roofing company targeted the contracts manager with excessive gifts and hospitality. This led to the manager feeling indebted to the roofing company and inclined to return the favour through manipulating contract variations. Knowing his authorisation level was £50,000, the contracts manager split a quote for £250,000 into 5 separate bids to avoid supervisory-level authorisation. Tactics also included duplicate fraudulent invoices and inferior product substitution, which resulted in a poor service and greater health and safety risks, all at the added expense to the public purse.

Controls

- **Effective contract management and monitoring**
- **Internal audit review of contracts including checking goods/services have been received**
- **Proactive monitoring, eg spend analysis**
- **Setting of appropriate authorisation limits**
- **Segregation of duties**
- **Effective budget monitoring**
- **Contract variations agreed at an appropriate level in the organisation**



Payments



Red flags

- The same person has responsibility for both signing off and paying invoices, or the same person who approves expenses also counter-signs them. *Conflict of interest within the process.*
- Irregular payments or gifts given to staff.
- Increasing amounts paid in expenses or large payment(s) paid to an individual. *Abuse of system.*
- Transactions carried out at an odd time, odd frequency, unusual amount or to unexpected recipients.
- Internal controls which are not enforced are compromised through intervention by more senior colleagues.
- Discrepancies in accounting records and unexplained items on reconciliations.
- Bank reconciliations are not up-to-date.
- VAT charged on invoices but no VAT reg number.
- Poor budget monitoring.
- Missing documents/only photocopied documents available.
- Excessive/spurious voids or credits.
- Common names or addresses of payees or customers.
- Unusual discrepancies between the client's records and confirmation replies.
- Missing inventory or physical assets which cannot be adequately explained.
- Evidence of alterations on documents, eg backdating signatures.
- Duplicate or inflated invoices.
- Employees unwilling to share duties, take leave or may have a lifestyle above their apparent means.
- Unusually high payments in a certain cost centre.
- A large number of small payments to one supplier.
- Receiving and paying for poor quality goods/services.

Example: A council procured a buildings maintenance contract worth several million pounds. As the contract neared the extension period, a performance review was conducted and found that the contract was significantly overspent to the value of £8 million. An internal investigation revealed that several contracts managers had utilised a number of different budgets, which masked the overspend. The underlying issue was identified as a lack of communication between the different departments involved in the entire 'procure to pay' process. This resulted in a failure of governance and reconciliation between what was procured and what was actually spent over the contract term.



Controls

- **Whistle-blowing policy and open culture**
- **Strong segregation of duties and duplicate payment controls**
- **Active management of conflicts of interests and Gift & Hospitality Registers**
- **Internal review of controls**
- **A 'zero tolerance of fraud' message from the top of the organisation**



Processes

Red flags

- One employee has control of a process from start to finish with no segregation of duties. *Conflict of interest within process and risk of fraud.*
- Little or no supervision. *Risk of collusion among employees.*
- Deliberate manipulation of financial statements, accounting records and/or missing files. *Risk of fraud.*
- Lack of validation checks within the process, eg verification of qualifications on application forms. *Risk of fraud.*
- Some areas of public sector business attract a higher risk of investment by Serious Organised Crime (SOC) groups. *Risk of money laundering and fraud.*

Example: A senior manager within a council is very keen that a certain contract is awarded to a particular company and implores the procurement officer to do so. This puts the procurement officer under significant pressure to write the technical specification in a way that supports the senior manager's request. This practice is not transparent, is illegal and puts the council at risk of significant reputational damage.

Controls

- **Effective internal audit service**
- **Effective reconciliation processes**
- **Segregation of duties (eg a technical specification written by two officers and the tender submission checked by a separate two officers)**
- **Due diligence carried out by the procurement team. It is essential that managers within these SOC risk business areas are aware of these threats and effectively manage their staff. Specialist training should be considered (see further reading on [page 12](#))**

Glossary

- **Bribery** – the act of giving or receiving something of value in exchange for some kind of influence or action in return, that the recipient would otherwise not offer.
- **Collusion** – agreement between people to act together secretly or illegally in order to deceive or cheat someone.
- **Conflict of interest** – a situation in which a person or organisation is involved in multiple interests (financial or otherwise), and serving one interest could involve working against another.
- **Corruption** – the abuse of entrusted power for private gain.
- **Fraud** – an act of deception carried out for personal gain or to cause loss to another party.
- **Gifts and hospitality** – means anything of value that you give or accept, either directly or in kind. Gifts and hospitality can often be abused and Police Scotland suggests that this is the source of many fraud or corruption type inquiries.
- **Money laundering** – the concealment of the origin of illegally obtained money, typically by means of transfers involving banks or legitimate businesses. The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 impose an obligation on the Auditor General for Scotland to inform the National Crime Agency if they know or suspect that any person has engaged in money laundering or terrorist financing.
- **Professional scepticism** – having a questioning mind, being alert to issues that may indicate fraud or error, and making a critical assessment of evidence.
- **Whistle-blower** – a worker who reports wrong-doing in an organisation. A whistle-blower is protected by law.

Further reading

[Fraud and irregularity update 2018/19](#) , Audit Scotland, July 2019

[The National Fraud Initiative in Scotland 2016/17](#) , Audit Scotland, July 2018

[Business exploitation](#) , Police Scotland SCD Divert Deter team

[Serious Organised Crime strategy](#) , Scottish Government, June 2015

[Protecting Public Resources in Scotland: counter fraud strategy](#) , Scottish Government, June 2015

Information about our counter-fraud work


<https://www.audit-scotland.gov.uk/our-work/counter-fraud> 

<https://www.scotland.police.uk/> 

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