

## ABERDEEN CITY COUNCIL

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|---------------------------|-----------------------------------------------------------------------------------------|
| <b>COMMITTEE</b>          | Council                                                                                 |
| <b>DATE</b>               | 5 February 2025                                                                         |
| <b>EXEMPT</b>             | No                                                                                      |
| <b>CONFIDENTIAL</b>       | No                                                                                      |
| <b>REPORT TITLE</b>       | Accounts Commission Findings – s102 report Council<br>Tax refunds – a significant fraud |
| <b>REPORT NUMBER</b>      | CORS/25/031                                                                             |
| <b>DIRECTOR</b>           | Andy MacDonald                                                                          |
| <b>CHIEF OFFICER</b>      | Jonathan Belford                                                                        |
| <b>REPORT AUTHOR</b>      | Jonathan Belford                                                                        |
| <b>TERMS OF REFERENCE</b> | 21                                                                                      |

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### 1. PURPOSE OF REPORT

- 1.1 To seek Council approval to accept the Accounts Commission findings relating to the significant fraud perpetrated against the Council.

### 2. RECOMMENDATIONS

That the Council:-

- 2.1 Note the content of the Accounts Commission report and accept the Commission findings contained therein;
- 2.2 Commend the individual who identified the fraud, with the Chief Executive writing to them to express the Council's gratitude;
- 2.3 Note the Commission finding (4) in respect of the Internal Audit function regularly considering areas that might be perceived as low risk when developing audit plans and instruct the Chief Internal Auditor to consider this finding within the proposed Internal Audit Plan for 2025/26-2027/28, which is due to be presented to the Audit, Risk and Scrutiny Committee in February 2025;
- 2.4 Ask the External Auditor to set out in their Annual Audit Plan for 2024/25 and future years how, in light of the Commission's findings, the tests of assurance they undertake may be revised in respect of the significant risks of material misstatement due to control weaknesses and fraud caused by management override of controls; and
- 2.5 Refer the matter to the Audit, Risk and Scrutiny Committee, with the Chief Officer – Finance and Chief Internal Auditor providing a joint report on the implementation of the Commission findings and action plan no later than September 2025.

### 3. CURRENT SITUATION

- 3.1 At a meeting on 12 December 2024, the Accounts Commission was presented with a statutory report, see Appendix 1, by the Controller of Audit on the significant fraud perpetrated against Aberdeen City Council.
- 3.2 The Accounts Commission agreed to make findings on the Controller of Audit's statutory report which are noted below.
- 1 *The member of staff who identified this fraud should be commended, for having the confidence to initially raise the issue and to then escalate it when they remained concerned by the response received. The Commission wishes to stress the importance of the council keeping its policies, training, and procedures in relation to counter-fraud and whistleblowing up to date and communicated to all staff. This will ensure that staff continue to have the confidence to raise concerns if they suspect something fraudulent may be happening.*
  - 2 *The Commission recognises that the council reacted quickly once the suspected fraud was brought to their attention and has made progress to recover lost funds. However, this case exposed real weaknesses in internal controls, allowing the perpetrator's actions to go unnoticed for 17 years. While controls and policies were in place, reports were not routinely run or reviewed and there was no scrutiny by the council to ensure the effectiveness of controls, something that is of concern to the Commission.*
  - 3 *The Commission is pleased to see evidence that the council is taking the matters highlighted by this fraud seriously, including the segregation of duties immediately following the issue coming to light, the development of an improvement plan by the service, and the engagement of internal audit to further strengthen key controls. However, controls have yet to be embedded in a way that fully addresses all the issues identified. December 2024 was identified as a key implementation date for improvement actions, but the absence of interim milestones makes it difficult to assess progress on the ground. As a matter of priority, the Commission asks the council's 'Task and Finish' Group to confirm to elected members and management when all actions will be complete, given it has now been more than a year since the perpetrator was charged.*
  - 4 *There is an important obligation on Aberdeen City Council to have and to implement effective financial controls, which safeguard public assets, across all its functions, irrespective of the level of income and expenditure involved. Building on this experience, the Commission would urge the council to ensure that no areas are neglected within their control environment and that the council's internal audit function regularly considers areas that might be perceived as low risk when developing audit plans. Through governance processes, we expect to see evidence that the council's management team is acting upon and applying recommendations from both external and internal auditors to address potential weaknesses and risks.*

- 5 *The Commission expects all councils in Scotland to ensure that fundamental internal controls are in place and working effectively. Such controls include appropriate segregation of duties, ensuring systems reconciliations are carried out, maintenance of system documentation (detailing key controls), and budget monitoring. All councils should also be self-assessing controls and processes through their annual governance statement. It is also important that across all councils, internal and external auditors raise and discuss any areas of potential concern.*

### **Action Taken by Aberdeen City Council**

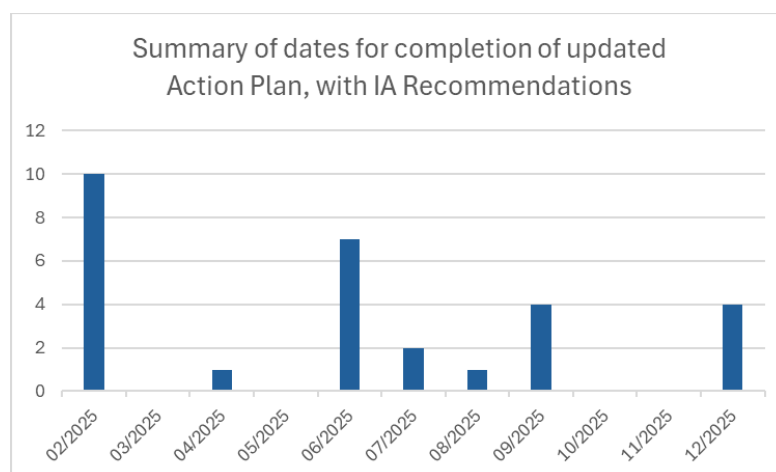
- 3.3 The subject of the statutory report was already known to the Council, having been reported confidentially by the Chief Officer – Finance to both the Audit Risk and Scrutiny Committee (RES/24/058) and Council (CORS/24/113) in February and April 2024 respectively. The timeline of events that was included in these reports has been updated and is shown as Appendix 2.
- 3.4 The findings of the Commission draw specific attention to the action plan put in place, which was intended to be the further actions required following the revision and strengthening of the Council Tax refunds process in the aftermath of the embezzlement discovery. These actions immediately improved segregation of duties, approval and scrutiny for Council Tax accounts that were 'in credit'.
- 3.5 While the control weaknesses were closed down immediately and the Chief Internal Auditor has provided to management some level of assurance that the controls and the application of those controls is in place, there were ten overarching actions identified that would go further than simply resolving and restoring control in respect of this one process. The Chief Officer – Finance acknowledges this has taken longer than had been initially intended, as highlighted by the Commission, with resources being prioritised on a risk based approach.
- 3.6 A summary of actions is included in the table below.

| <b>Subject</b>                                   | <b>Number of Actions</b> | <b>Has action been taken by management to address these actions?</b> | <b>Has Internal Audit (IA) provided positive assurance on controls to date?</b> | <b>Did IA suggest further actions to implement?</b> | <b>Updated Action Plan with milestones in place?</b> |
|--------------------------------------------------|--------------------------|----------------------------------------------------------------------|---------------------------------------------------------------------------------|-----------------------------------------------------|------------------------------------------------------|
| Changes to Processing and Approval of CT Credits | 2                        | Yes                                                                  | Yes                                                                             | No                                                  | n/a                                                  |
| Wider Council Tax Scrutiny and Controls          | 3                        | Yes                                                                  | Yes                                                                             | Yes                                                 | Yes                                                  |
| Applications to other Council Systems            | 7                        | Yes                                                                  | Yes, for 6 out of 7                                                             | Yes                                                 | Yes                                                  |

- 3.7 The Chief Internal Auditor, having been asked by the Chief Officer – Finance to review the matter, indicated that most of the initial actions were partially complete, and included in the briefing note to management a wider range of actions that would benefit the control environment. Any outstanding actions and these additional, more specific actions have been allocated to the team, and incorporated into the updated action plan.
- 3.8 The Accounts Commission finding was clear that the actions must be completed and for milestones to be created to support the successful progress, tracking and implementation of these actions. The Chief Officer – Finance, in consultation with other Council Officers, has updated the action plan and progressed the implementation and embedding of the wide range of actions.

| <b>Subject</b>                          | <b>Number of Areas for Action</b> | <b>Number of Sub-actions recommended by IA?</b> | <b>Has action been taken by management to address these actions?</b> | <b>Are milestones and target dates in place?</b> | <b>How many have been closed off by end Jan 2025?</b> |
|-----------------------------------------|-----------------------------------|-------------------------------------------------|----------------------------------------------------------------------|--------------------------------------------------|-------------------------------------------------------|
| Wider Council Tax Scrutiny and Controls | 3                                 | 14                                              | Yes                                                                  | Yes                                              | 9/14 (64%)                                            |
| Applications to other Council Systems   | 7                                 | 24                                              | Yes                                                                  | Yes                                              | 0/24 (0%)                                             |

- 3.9 The outstanding actions will be managed by the Task and Finish Group and overseen by the Risk Board to increase scrutiny around the progress. The target timeline for completion of these actions, subject to a number of these being dependant on decisions that have yet to be taken, can be summarised as presented in the following graph.



- 3.10 The timeline reflects the indicative date on which the action will be completed, there are milestones between now and those dates, in some cases the result

of an iterative process where completion can only be achieved after one or more decision points. The dates will be reviewed based on progress.

- 3.11 Chief Officer – Finance and the Chief Internal Auditor intend to provide a joint report to the Audit, Risk and Scrutiny Committee in September 2025 to provide an update on the work completed, including the Commission's findings, and assurance level that can now be relied upon.

**Audit:**

- 3.12 As required for local authorities, internal and external auditors have carried out audit work and testing on the Council finances and systems of internal control during the entire period that the embezzlement has taken place. Specific internal audit work on Council Tax, systems, processes and controls, has been carried out periodically based on the assessment of risk and the priorities set out in the Internal Audit Plan annually. Annually the Council has received an assurance opinion on the adequacy and effectiveness of the framework for governance, risk management and control from the Chief Internal Auditor, as detailed in their Annual Audit Reports.
- 3.13 Similarly the External Auditor has provided an audit opinion on the annual Financial Statements of the Council and basis for that opinion is included in their Annual Audit Report.
- 3.14 The findings from the Commission draw attention to both internal and external audit raising and discussing areas of potential concern; while it is incumbent on the Council management to act on the recommendations of our auditors to address weaknesses and risks.
- 3.15 Taking account of this, and noting the Commission's findings with specific reference to Internal Audit, the Chief Internal Auditor is due to present their internal audit plan for 2025/26-2027/28 to the Audit, Risk and Scrutiny Committee in February 2025. Despite the short timescale between the publication of the findings and the presentation of the internal audit plan, it will be important for the Chief Internal Auditor to have considered the impact of the finding on their plan and to have responded to the risk. That response should be incorporated into their Internal Audit Plan in February.
- 3.16 The External Auditor should provide details of any changes that they intend to make to their approach to significant risks that exist in the audit of the Council Financial Statements, when their Annual Audit Plan is next presented to the Audit, Risk and Scrutiny Committee.

**Refunds to Council Tax payers:**

- 3.17 The report makes specific reference to the fact that the Council has not yet contacted taxpayers that have been affected. For clarity the process of managing Council Tax credits includes, and included throughout, the Council trying to contact the Council Tax account holder once a credit was identified on their account. This often results in no contact being made and no replies being received.

- 3.18 Looking at the data and Council Tax accounts that are affected the vast majority of these remained in credit for a period of time, often years, the system prepared to provide a refund if contact was made by the account holder.
- 3.19 It should also be noted that for anyone moving within the city boundaries, any credit that arose due to moving home in Aberdeen, is, and always was, moved from the old property to the new property, with the credit being applied to the new Council Tax liability. It means that these historically, long standing credits are highly likely to have arisen from individuals who left the city.
- 3.20 The Council currently has 2 experienced Council Tax officers working on correcting the c.5,700 individual transactions and they are retracing the steps taken by former-employee, Michael Paterson, to embezzle the money in the first place, establishing how to reinstate the correct position to each Council Tax account.
- 3.21 As at the time of writing the number of accounts that have now been checked is 1,908.
- 3.22 Beyond this, the Council has also started to identify if a refund can be processed for any of the account holders. The 1,908 accounts amount to £563,434 (51%) of the embezzled money. The investigation of these accounts indicates that there are partial details of account holders for 597 accounts. The Council has started to make contact with those individuals, so far approximately 100 have been contacted, and this number is rising on a weekly basis.
- 3.23 The Council will continue to correct and reinstate all Council Tax accounts affected. Due to the historic nature of the transactions and the limited information that would allow the Council to trace former account holders the Council may not be able to reunite the money with the rightful owner but will continue to pursue all options and where an individual is identified in the future the entitlement to a refund will not be removed.

**Raising awareness more widely:**

- 3.24 The Commission recognise the wider implications for Local Government sector and have drawn attention to this in their findings (4 & 5). In order to assist other Council's in understanding this embezzlement and to share knowledge the Chief Officer – Finance has agreed with the CIPFA Directors of Finance Section that a presentation will be provided at an upcoming meeting.
- 3.25 In December 2024 a Counter Fraud Officer provided briefings and attended meetings of the Scottish Local Authority Investigators Group (SLAIG) and to the shared Internal Audit team on this embezzlement. The presentations provided context and detail as to how the crime was committed, and the safeguards which could have prevented it. Presentations were delivered to both groups, with question and answer sessions adding to the understanding on the day.

**Accounts Commission meeting:**

- 3.26 The Chief Executive, Chief Officer – Finance and Group Leaders are due to meet with representatives of the Accounts Commission on 3 February 2025.

#### 4. FINANCIAL IMPLICATIONS

- 4.1 There are no direct financial implications arising from the recommendations of this report. Resources to retrace and correct Council Tax accounts are being paid for from within existing budgets.
- 4.2 In respect of having the money available to make refunds to the rightful owners, where possible, action was taken at the end of financial year 2023/24 to set aside the full value (£1.106m) of the money embezzled. This was accounted for in the 2023/24 Annual Accounts and has prepared the Council to be able to recompense former Council Tax account holders whose accounts were affected by the embezzlement.
- 4.3 Where the Council can locate and establish a former Council Tax account holder as part of the actions then the Council has the financial resources to refund all individuals.

##### **Recouping Funds**

- 4.4 To date the Council has received the maximum value possible, £417,523, from former-employee Michael Paterson's pension. This money will be included in the Council's income for 2024/25, offsetting the cost of setting aside £1.106m last year.
- 4.5 In respect of the balance of the money set aside, £0.689m, a claim against the Council's fidelity guarantee insurance policy has been made, the outcome of which is still being assessed by our insurers. The outcome of the claim will be included in a future financial performance report to the Finance and Resource Committee.

#### 5. LEGAL IMPLICATIONS

- 5.1 There are no direct legal implications arising from the recommendations of this report.

#### 6. ENVIRONMENTAL IMPLICATIONS

- 6.1 There are no direct environmental implications arising from the recommendations of this report.

#### 7. RISK

| Category       | Risks                                 | Primary Controls/Control Actions to achieve Target Risk Level | *Target Risk Level (L, M or H)<br><br>*taking into account controls/control actions | *Does Target Risk Level Match Appetite Set? |
|----------------|---------------------------------------|---------------------------------------------------------------|-------------------------------------------------------------------------------------|---------------------------------------------|
| Strategic Risk | Fraud on this scale if repeated could | Underlying control environment is in place, including         | L                                                                                   | Yes                                         |

|                    |                                                                                                                                                                               |                                                                                                                                                                                                                                 |   |     |
|--------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---|-----|
|                    | impact the finances of the council to an extent that strategic direction would have to be altered.                                                                            | scrutiny by internal and external auditors. Review of other systems and payment controls has been undertaken to identify improvements and implement new controls.                                                               |   |     |
| <b>Compliance</b>  | Failure of controls leads to failing to meet legal obligations to CT payers – and other customers and bill payers.                                                            | Underlying control environment is in place, including scrutiny by internal and external auditors. Actions have been taken to enhance specific control arrangements and requirements to mitigate the specific frauds identified. | L | Yes |
| <b>Operational</b> | Staff are vulnerable to allegations if controls do not manage the work they undertake.                                                                                        | Changes to the processes and procedures in Council Tax and other systems improve segregation of duties and reporting to provide dual insight into refunds protecting staff.                                                     | L | Yes |
| <b>Financial</b>   | Loss of money received by the Council may have to be replaced and refunded, which will have to be funded by General Fund. There is a cost to correct our systems and records. | All avenues will be explored to recoup funds from the accused. The Annual Accounts for 2023/24 include provision for the full value of the embezzled monies.                                                                    | M | Yes |

|                              |                                                                                                                                                                                                                      |                                                                                                                                                      |   |     |
|------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------|---|-----|
| <b>Reputational</b>          | Loss of trust from the population and our customers that the Council cannot manage finances adequately. Increase in non-payment as CT payers uncertain about their account being managed accurately and effectively. | Developing a communications strategy will help to ensure consistent messages are used to inform citizens and council tax payers about the situation. | M | Yes |
| <b>Environment / Climate</b> | None                                                                                                                                                                                                                 |                                                                                                                                                      |   | n/a |

## 8. OUTCOMES

| <b><u>COUNCIL DELIVERY PLAN 2023-2024</u></b>                                                          |                                                           |
|--------------------------------------------------------------------------------------------------------|-----------------------------------------------------------|
|                                                                                                        | <b>Impact of Report</b>                                   |
| <b>Aberdeen City Council Policy Statement</b><br><br><b><u>Working in Partnership for Aberdeen</u></b> | There are no direct implications for the stretch outcomes |
| <b><u>Aberdeen City Local Outcome Improvement Plan 2016-26</u></b>                                     |                                                           |
| Prosperous Economy Stretch Outcomes                                                                    | There are no direct implications for the stretch outcomes |
| Prosperous People Stretch Outcomes                                                                     | There are no direct implications for the stretch outcomes |
| Prosperous Place Stretch Outcomes                                                                      | There are no direct implications for the stretch outcomes |

## 9. IMPACT ASSESSMENTS

| <b>Assessment</b>                        | <b>Outcome</b>                                                                               |
|------------------------------------------|----------------------------------------------------------------------------------------------|
| <b>Integrated Impact Assessment</b>      | It is confirmed by Chief Officer – Finance that no Integrated Impact Assessment is required. |
| <b>Data Protection Impact Assessment</b> | Not required.                                                                                |

|              |                                                    |
|--------------|----------------------------------------------------|
| <b>Other</b> | No other impact assessments have been carried out. |
|--------------|----------------------------------------------------|

## **10. BACKGROUND PAPERS**

10.1 None

## **11. APPENDICES**

Appendix 1: Accounts Commission report: The 2023/24 audit of Aberdeen City Council - Council tax refunds – a significant fraud

## **12. REPORT AUTHOR CONTACT DETAILS**

|                      |                              |
|----------------------|------------------------------|
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