

**HM Treasury**



**Parliament Street  
London SW1P 3AG**

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Second Treasury Officer of Accounts**

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Dear Accounting Officer

**ESTATES AND BUILDINGS SERVICES PROCUREMENT: PREVENTION OF FRAUD AND IRREGULARITY IN THE AWARD AND MANAGEMENT OF CONTRACTS**

DAO(GEN) 3/90, "Works Services Projects: Fraud and Irregularity", issued on 12 December 1990, reminded departments of the risks of fraud on works services projects, set out departmental responsibilities and provided general guidance. This followed the untying from PSA Services in April 1990.

2. Since 1 April 1996 departments have been completely responsible for their accommodation and properties on the Common User Estate, formerly managed by Property Holdings, have been transferred to departments. As a result, departments are now responsible for dealing direct with landlords and their agents, for placing contracts for capital works and the maintenance of accommodation and for commissioning consultants to provide estates management and design and related services.

3. This change in responsibility required a revision of the 1990 DAO letter. This letter, which has been prepared in conjunction with the Central Advice Unit, Property Advisers to the Civil Estate, therefore supersedes DAO(GEN) 3/90. Departments should send copies to any non-departmental public bodies (NDPBs) which they sponsor.

***Purpose***

4. The purpose of this letter is:
- a. to remind departments of the risks of fraud, corruption and irregularity in handling construction projects and in the management of property and maintenance services, and of the need to ensure that they have adequate and effective systems of control in these areas;
  - b. to alert departments to the types of risk faced in this context;

- c. to provide general guidance on how to deal with these risks; and
  - d. to remind departments of sources of advice and the value of exchanging information to ensure the proper screening of contractors and consultants. The Department of Environment's Contractor Management Information System (CMIS) for works contractors, and the Consultants Register (ConReg), are two focal points for such exchange of information.
5. This letter provides guidance for all staff involved in estates and building services procurement. This includes such activities as:
- buildings construction
  - refurbishment projects
  - minor works
  - property maintenance
  - grounds maintenance
  - disposal/acquisition of land and buildings
  - termination/surrender/assignment of leases
  - facilities management.

### ***Definitions***

6. Fraud may be defined as the use of deception with the intention of obtaining an advantage. Corruption is the giving or receiving money, goods or services for favours provided. The risks of fraud and corruption can be reduced by awareness of their nature and good procurement practice.

### ***The risks***

7. Construction projects and property maintenance services have long been considered to carry a high risk of fraud, corruption and other irregularity. Contributory factors include the complexity of schemes, the difficulties of measuring the quality of the product, and the levels of malpractice found historically in parts of the industry. The frauds can take a number of forms, some involving collusion with departmental staff or the department's agents. For example, an officer rigs a contract by inviting to tender only the corrupt supplier with whom he or she is in league and dummy companies set up by the same supplier.

8. One fraud risk encountered in this context is the "ringing" of contracts, whereby a group of contractors get together in a "ring" to submit tenders ostensibly in competition but in fact having arranged amongst themselves which firm will bid the lowest. Even the lowest tender will be overpriced. The aim of the ring will be to win the majority of the contracts available and share them.

9. Frauds can be perpetrated in the execution or pricing of work in new construction and maintenance projects. This can take a variety of forms from failure to perform to specification,

for example, using lower quality materials, to deliberate falsification of suppliers' invoices or labour records leading to overpayment for the services.

10. Ground maintenance contracts also provide opportunities for a contractor to claim for more work than has been done with or without collusion.

11. The pricing of contracts not let by competitive tender carries the risk that costs may be deliberately overstated. This can be a particular problem in "cost plus" contracts' and in small value non-competitive contracts which can add up to large amounts of expenditure over the year.

12. Property transactions involving acquisition or disposal, rent reviews and lease renewals also present scope for fraud or corruption. As with works contracts there can be collusion between departmental staff, or by consultants employed by departments, in the form of confidentiality breaches. Confidentiality regarding bids and prices is essential in property acquisitions, sales of land and buildings and in negotiating leases and rents with landlords.

### ***Gifts and hospitality***

13. As in other procurement activities, particular care needs to be taken about the acceptance of gifts, hospitality and other benefits, and to ensure there is no conflict of interest in the award of contracts.

14. The Civil Service Management Code emphasises that civil servants must not receive gifts, hospitality or benefits of any kind which might be seen to compromise their personal judgement or integrity. Departments should have detailed and specific rules, informing staff of the circumstances in which they need to report offers of gifts, hospitality and other benefits and those occasions when they need to seek permission before accepting them. In their guidance departments must draw the attention of staff to the Prevention of Corruption Acts 1906 and 1916. Departments should also keep records of invitations and offers of hospitality accepted.

15. The Code also states that departments must require their staff to report any business interest relevant to their work.

### ***Key principles of control***

16. There are a number of basic principles of control to minimise the risk of fraud in estates and building services procurement.

- **Separation of duties.**

Duties should be separated to ensure that no single member of staff has control over the procurement process. For example, there should be a separation of duties between staff who place orders, those who receive the services, and those who authorise payments. Failure to separate duties is one of the most common elements of fraud.

- **Authorisation**

All transactions or specified activities should be approved or sanctioned by a manager or other responsible person before they are undertaken. Limits for these authorisations should be specified. Authorisation seeks to ensure that proper responsibility is taken for all transactions and activities. Authorisation should ensure that delegated limits are complied with, provide an independent scrutiny and consistency in the procurement process.

- **Competitive tendering**

Contracts should normally be let by competition. A decision not to use competitive tendering should require a higher level of authority.

- **Regular supervision**

There should be positive supervision of the procurement process including regular and unannounced checks of transactions. In addition managers should carry out pre-commitment checks to confirm the need for the service; that the type of contract is appropriate; and that estimated costs are realistic.

- **Record keeping**

Appropriate records must be kept to enable every decision and transaction to be traced through the system. The requirement to keep proper records is an important deterrent to fraud.

- **Documentation**

Standard documentation can help to enforce conformity with procedures and legal requirements.

- **Budgetary control**

Budgetary control matches resources and costs to responsibilities for objectives and outputs. Managers should be fully accountable for the achievement of their objectives and targets. Budgets should be closely linked to planning (including a capital expenditure programme) and review procedures to ensure that proposed expenditure is essential. This will help minimise the risk of fraud.

17. Departments should satisfy themselves that their control arrangements enable them to discharge effectively their responsibilities for minimising the risk of fraud. However internal controls cannot by themselves be proof against fraud, given that it may involve people holding positions of authority and trust. Separation of duties can be circumvented by collusion. Authorisation controls can be abused by the person to whom the authority is given. Therefore

departments should also ensure that all staff are aware of the risks of fraud and of their responsibilities for reporting any fraud or suspicions of fraud to the appropriate level of management.

18. The annex looks in greater detail at how controls should be used to counter specific risks.

### ***Fraud “indicators” in the contract process***

19. The following may be “ indicators” of the occurrence of fraud in the tendering and award of contracts for estates and building services:

- contracts that do not make commercial sense
- contracts that include special but unnecessary specifications that only a favoured supplier can meet
- suppliers who are awarded contracts disproportionate to their size
- acceptance of late bids
- change in tender after other bids are opened, often by the drafting of “mistakes” into initial tender
- unusual patterns of consistently high accuracy in estimating tender costs - this is used to deflect the attention of auditors and senior managers, who tend to look for adverse rather than favourable variances
- consistent use of single source contracts
- disqualification of suitable tenderer
- unexplained changes in contract shortly after award
- contracts awarded to contractors with poor performance record
- poor documentation of contract award process
- undue patronage, by consistently favouring one firm over others
- split ordering to circumvent contract conditions
- close personal relationships between staff and suppliers
- withdrawal of the lowest tenderer without obvious reason and who may then go on to become a sub-contractor of a high tenderer

- contractors who are qualified and capable of tendering but who do not do so for no apparent reason
- the successful tenderer repeatedly sub-contracts work to companies that submitted higher tenders
- there appear to be patterns in tenders from a grouping of firms for example, fixed rotation of lowest tender
- a certain contractor may tender substantially higher on some tenders for no logical cost justification
- tender prices appear to drop whenever a new tenderer submits a bid
- a consistent pattern of the same winners and losers (from the tender lists)
- obvious links between contractors tendering for these works (these links range from companies sharing the same address, having the same directors, managers and professional advisers e.g. accountants, lawyers etc.).

### ***Fraud “indicators”: estate management***

20. The following may be “ indicators” of the occurrence of fraud in estate management:

- leases and rents higher than normal for the sector
- purchase price above the norm for the area
- fronting companies used to hide the identity of purchasers in the sale of land and buildings
- close personal relationships between staff and suppliers.

### ***Screening of contractors and consultants***

#### **CMIS and ConReg.**

21. The Department of Environment’s Contractor Management Information System (CMIS) for works contractors and the Consultants Register (ConReg) are lists which can be consulted as part of a screening process. These lists consist of firms who are considered to be financially sound and professionally and technically capable of undertaking various types and sizes of contracts/commissions. The validation procedure involves their submission of financial accounts, tax certificates and any relevant certificates relating to their profession, as well as biannual technical audits to establish whether the firm has the ability to perform the functions shown on the listing.

22. The use of these systems, while not comprehensive, can provide a useful contribution to deterring fraud in that they enable checks to be made on:
- a. the bona fide status of firms prior to listing;
  - b. undeclared links between firms and/or directors.
23. The information held on CMIS and ConReg can also be used to identify:
- a. instances of excessive patronage of a firm, through frequent invitations to tender;
  - b. an unusually high rate of success in competition for any one firm;
  - c. instances of tender "ringing", i.e. firms banding together to submit artificially high tenders.
24. It would be helpful if feedback on experience of firms, especially where there are concerns about performance, could be provided to DOE to ensure that information on CMIS and ConReg is both accurate and up to date. The contact point for CMIS and ConReg is the DOE Procurement and Pre-Qualification Systems Division (PPSD), Room P1/162, 2 Marsham Street, London, SW1P 3EB, tel: 0171 276 0470, fax: 0171 276 0450.

#### **Other Sources of Information**

25. Companies House has an on-line service covering all companies registered in Great Britain which provides the names and addresses of directors and company secretaries. It also provides the appointment history of all those listed (since October 1991), lists of documents filed by the company in the last five years, dates of accounts and returns filed and details of any disqualified directors (since 1989) together with an explanation of disqualification. For further information ring General Enquiries on 01222 380801 who can also provide screen print outs of this service by fax or post. For Northern Ireland company information ring 01232 234488.
26. There are also commercial organisations such as Dun & Bradstreet which specialise in providing information, financial and otherwise, on companies. Information provided from these commercial organisations and Companies House can be helpful in the assessment of tenderers and therefore contribute to the prevention of fraud.

#### ***Networking***

27. In addition to the use of CMIS and ConReg there are benefits in the informal exchange of information about performance of consultants, contractors, agents, developers and landlords. In the case of agents, developers and landlords Property Advisers to the Civil Estate (PACE) will facilitate such exchange.

## *Enquiries*

28. Enquiries should be addressed as follows:

- a. general guidance on prevention of fraud and irregularity on property and construction-related procurement and advice on firms experienced in the investigation of fraud to Central Advice Unit, Property Advisers to the Civil Estate (PACE), Room 7/30, St Christopher House, Southwark Street, London SE1 0TE, tel: 0171 921 4250, fax: 0171 921 4347;
- b. initial enquiries about agents, developers and landlords to The Chief Executive, Property Advisers to the Civil Estate (PACE), Room 7/44, St Christopher House, Southwark Street, London SE1 0TE, tel: 0171 921 4584, fax: 0171 921 4877.

*Yours sincerely*  
*Frank Martin*

**FRANK MARTIN**

**ESTATES AND BUILDING SERVICES PROCUREMENT: PREVENTION OF FRAUD AND IRREGULARITY IN THE AWARD AND MANAGEMENT OF CONTRACTS**

**Risks and controls - award of contract**

1. Departments should consider at invitation to tender acknowledgement stage or at bid submission formally requesting the tenderer to sign that no fraud or corrupt practice has occurred when developing the bid. This has two effects:
  - a. it deters - the contractor is alerted to the fact that the client is aware of the risk of fraud and will be on the look out for any evidence that it has occurred;
  - b. it ensures that should something fraudulent come to light , there can be no excuse that the company was not aware of Government policy.
2. Departments will need to handle such a declaration with sensitivity so as not to impair good working relationships with suppliers.

Activity	Risk	Control
Scoping of Contract	The contract specification is written in a manner which favours a particular supplier	Use of contract panel consisting of Technical, End User and Buying representatives, to ensure that more than one person is involved in drawing up the specification.
Contract Documentation	Conditions of contract are changed to accommodate a favoured supplier and/or exclude competitors who cannot meet the varied conditions.	Standard contract conditions and specification to be used. Any variations to be approved by Senior Management.
Setting Evaluation Criteria	Original evaluating criteria are changed after the receipt of submissions to ensure that favoured suppliers are short listed.	Use evaluation criteria as agreed by the contract panel prior to tendering. Where EC procurement rules apply evaluation criteria are required to be stated in advance.

Activity	Risk	Control
Selection of tenderers	The selection of a group of tenderers with a view to ensuring that the favoured tenderer will win.	Selection by panel against clearly defined and objective criteria; where applicable, in accordance with the requirements of the EC procurement directives.
Tendering	Contract rings - repeat orders using a narrow sourcing list. Links between contractors - uncompetitive tendering.	Firms should be selected by someone other than the officer commissioning the work. Widen the sourcing list by the introduction of new firms and examine tender records for a pattern of pricing and tenderers who have won. Check for links in names, addresses and telephone numbers plus tendering partners. Refer to CMIS/ConReg for instances of contract ringing/information on links between contractors as appropriate.
Tender Evaluation	Collusion to ensure that the favoured supplier is chosen.	Technical and commercial evaluation to be carried out independently by the contract panel.
Post Tender Negotiation	Modification of favoured supplier's tender to ensure that they are successful.	Where necessary, identify reasons for negotiation and negotiate with a minimum of two suppliers.
Single Source Procurement	Overstating of prices.	Competitive tendering and advance purchase planning. Tight budgetary control and a comprehensive system of price checking.

**Risks and controls - management of contracts**

Activity	Risk	Control
Contractual Correspondence	Altering terms and conditions to suit favoured supplier.	Contract terms and conditions will be the purchasing department's and may not be altered without senior management approval.
Contract Management	False claims for work not carried out or exaggerated claims for actual work done.	Clear audit trail with written records. Authorisation of changes, by Senior Management, to original document. Site checks, random and systematic.
Claims Negotiation	Assisting the contractor to justify claims.	Claims negotiation should be carried out using professional advisers.
Certification of Completion	Inadequate certification may lead to overpayments or payment for work not carried out.	Clear separation of duties between ordering the work, certification and authorisation of payment. Ensure that certified documents are not returned to the originator.
Authorisation	Contract splitting to keep contract values under particular staff member's authorised financial limit.	The splitting of contracts should not be allowed unless authorised by Senior Management. Management and Supervisors checks and sampling should be constructed to detect this.

Activity	Risk	Control
Acceptance of documentation to support claims.	Documentation has been modified or fabricated.	Act on original documents. Do not accept copies/faxes. Do not accept use of correction fluids etc. without obtaining full explanation for any amendments.
Supervision	Payment for work not done and duplication. Failure to monitor daywork on site. Duplication of names on more than one return or 'ghost' workers. Work paid for under one contract and provided in a different format on another contract. Lack of separation of duties, lack of reporting of gifts and hospitality or conflicts of interest.	Good site supervision and audit of site diary. Look for similar work in same building and enforce contract management controls. Separate duties, ensure hospitality rules are formulated and understood, have clear conduct and discipline code, including conflicts of interests and penalties, take disciplinary action against those staff who fail to declare a conflict of interest.
Security of Documents	Duplication and manipulation of accountable documents.	Restricted access to accountable documents such as works and stores orders, tender documents and claim forms. Serial numbering should be used.

**Risks and controls - estates management**

Activity	Risk	Control
Lease Negotiations	Lease terms agreed which are too favourable to landlord.	Issue Agent with Client's Standard Heads of Terms. Exception reports to be produced highlighting the difference between the agreed terms and the Standard Head of Terms with explanations for the variation.
Purchase of Land and Buildings	If in collusion with departmental staff the owner becomes aware of the exclusivity of interest, price could be inflated.	Maintain flexibility of choice and confidentiality.
Disposal of Land and Buildings	Suppressed price as a result of inducements being paid.	Disposal by competitive sealed bids using approved agents.
Payment of Rent	Diversion of payment due to change of payee or fictitious property.	Audit, physical checks to ensure that the property exists. Authorisation of rent paid. Separation of duties.
Dilapidations ie the cost of bringing a property up to a previously agreed state of repair.	Landlords frequently inflate claims for damages, with collusion excess monies could be paid out.	Appoint legal and property advisers well in advance of the end of the lease to consider the repair obligation and extent of repairs required.

<b>Activity</b>	<b>Risk</b>	<b>Control</b>
Valuations used in the acquisition and disposal of property	Inflation of property values on acquisitions to maximise profit. Deflation of property value on disposals for selling on at a profit.	Use professional advisers.