



Northern Ireland
Assembly

Public Accounts Committee

OFFICIAL REPORT (Hansard)

NIAO Report: 'Northern Ireland Water's
Response to a Suspected Fraud'

25 September 2013

NORTHERN IRELAND ASSEMBLY

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Members present for all or part of the proceedings:

Ms Michaela Boyle (Chairperson)
Mr John Dallat (Deputy Chairperson)
Mr Trevor Clarke
Mr Michael Copeland
Mr Alex Easton
Mr Paul Girvan
Mr Daithí McKay
Mr Adrian McQuillan
Mr Sean Rogers

Witnesses:

Mr Gary Fair	Department for Regional Development
Ms Deborah McNeilly	Department for Regional Development
Mr Richard Pengelly	Department for Regional Development
Ms Sara Venning	Northern Ireland Water

In attendance:

Mr Kieran Donnelly	Comptroller and Auditor General
Ms Fiona Hamill	Treasury Officer of Accounts

The Chairperson: We have with us Mr Kieran Donnelly, the Comptroller and Auditor General (C&AG); Ms Fiona Hamill, the treasury officer of accounts; Mr Richard Pengelly, accounting officer in the Department for Regional Development (DRD); Ms Deborah McNeilly, the acting deputy secretary of DRD; Ms Sara Venning, the interim chief executive officer (CEO) of NI Water; and Mr Gary Fair, the director of the shareholder unit of NI Water. Richard, you and your team are very welcome. Today we are considering the Audit Office report on the inquiry into NI Water's response to a suspected fraud. Does any Member want to declare an interest? There are no declarations. We have a line of questioning, and I will start.

At the heart of the Audit Office report is the commercial relationship between NI Water and contractor company E. Invoice slicing, a practice that brings payments to contractors under the radar of proper control arrangements, drew attention to this case. However, the unauthorised extension of the contract, unapproved expenditure under the contract, and an additional £1.4 million of survey work awarded over and above the original contract, also suggests that that contract operated in the interests of company E rather than those of NI Water. Was that the case?

Mr Richard Pengelly (Department for Regional Development): Chair, thanks for that. It is difficult to say that getting over £1.4 million worth of work, as you suggest, that was not within the terms of the

defined contract is not somehow in the interests of the company. However, I am confident that there was no malign act at play. It was a point in time. The Committee has very helpfully looked at the issue and drawn out some conclusions that we are working on. The issue was that it was a time when there were well-acknowledged difficulties in contract management, particularly contract extensions, throughout 2009 and 2010. The reality was that all the work was needed. The work was undertaken, and it was paid for in accordance with rates that had been agreed under the terms of the appropriately-let contract, recognising that it was inappropriately extended. The nub of your question was whether there was any malign force at play in the extension. None of the work undertaken shows that to be the case.

The Chairperson: Obviously, it is a key accountability control and long-established Department of Finance and Personnel (DFP) guideline that the C&AG is notified of suspected fraud. Why did the Department not take that important step at that time to inform the C&AG?

Mr Pengelly: We absolutely recognise the importance of doing that. It is a widely-accepted principle. It should have been done in that case, but was not. It was an administrative oversight. There was a small tangential reference to it in an e-mail that went to the C&AG about that time, but that does not excuse the lack of formal and appropriate notification that should have been made at the time that the suspected fraud —

The Chairperson: You say that there was a small reference in an e-mail.

Mr Pengelly: There was an e-mail from the accounting officer of the time updating the C&AG on some other work that was happening. There was a small reference in it, but I am just mentioning that, Chair; that does not excuse the lack of formal notification to the C&AG that should have happened but did not.

The Chairperson: The Committee will now draw out key aspects of the case — each member will do so — particularly the aspect of learning for investigative good practice. I ask members to keep their questions brief and to the point.

Mr Girvan: I will attempt to keep my questions brief, but that will be very difficult.

Thank you very much for coming along. I have concerns about why a disciplinary procedure was in place before a fraud investigation was called for or completed. I have concerns about how that transpired. Richard, maybe you could explain what brought that about.

Mr Pengelly: I will say a few words on this, but the disciplinary case was a matter for the employer. The legal employer was Northern Ireland Water, so Sara might want to supplement what I say.

The guidance, then and now, is clear that disciplinary procedures should not precede the fraud investigation. That should not have happened. I will make one contextual point. I want to be very careful about how I express it to the Committee. I do not offer it as an excuse; it is just a contextual point. There were previous difficulties in Northern Ireland Water with contractual issues. This was at the height of that time. The senior management team and other key officials, such as the head of the internal audit team, were very heavily loaded with carrying out that work. To be fair to Northern Ireland Water, there was a rapid response to the identification of the issue. To be critical, more speed and less haste might have been the plan that it should have adopted. The then chief executive asked for investigations to proceed under the disciplinary process. Part of that was lax language on his part, because it was about saying that those team members put their hands up and said that they were doing something which we believe was inappropriate and that it was also recognised as a potential indicator of fraud. He clearly wanted to find out more about that, but he was also cognisant of the fact that you need to tread carefully when interviewing somebody in those circumstances to capture the evidence. That process preceded the full fraud investigation.

As I said, the guidance recognises that that should not happen. It is not a position that we would want to allow to happen again. Our guidance has been refreshed and renewed; we have drawn the point out. Northern Ireland Water's guidance, our guidance and DFP guidance brings that out very clearly.

Ms Sara Venning (Northern Ireland Water): I concur with what Richard has said. We accept that disciplinary proceedings should not precede any fraud investigation. We are very clear on that internally, and we have been very clear on that internally as we have communicated with staff since

we have received the report. Again, I would back that up by saying that, at that time, the former chief executive wanted to establish the facts. He asked for interviews to be carried out under the disciplinary process, and we believe that that was to afford the individuals and the company the protection that the facts would have been gathered in a way that meant that they could be used in any subsequent investigation if required. However, we accept that in no circumstances should a disciplinary proceeding happen before a fraud investigation.

Mr Girvan: That makes me wonder why a fraud investigation was ongoing at the same time as disciplinary proceedings were going ahead. The report mentioned someone receiving a telephone call about disciplinary proceedings being taken. I do not know whether that sort of process is the norm. It does not seem right to me that you would do anything associated with disciplinary proceedings over the telephone; you would deal with it in a proper format. Who instructed that that phone call happen or who made that phone call?

Mr Pengelly: I think that Sara may want to come in with more of the detail, but the telephone call you refer to was made around 20 January. I made a point about lax language: the chief executive instructed that interviews under the disciplinary process should take place, and the telephone call that followed soon after was not made under the formal disciplinary process. The employee concerned was on leave at the time, so it was an initial contact to try to find out the facts of the case.

One key reason why it is very important not to undertake disciplinary proceedings in advance of a fraud investigation is because it could put people on alert. While not excusing it, in this particular case the individuals concerned were already well aware of that because their involvement had come out in the review by the head of internal audit that was commissioned in early January. To answer your main question, it was not a formal disciplinary interview; it was a fact-finding discussion.

Mr Girvan: You must appreciate that, in the interests of openness and transparency, that would definitely not be encouraged. It should not have been dealt with on that basis.

Mr Dallat: Can you tell the Committee whether it was Laurence MacKenzie, the former CEO, who, in his usual cavalier fashion with no regard for any kind of procedures, ordered this disciplinary procedure thereby jeopardising the investigation?

Mr Pengelly: The chief executive at the time was Mr MacKenzie.

Mr Dallat: Yes. I think that that helps to give a flavour to it given all the other things that were going on at NI Water at the time, for which your Department was responsible.
Thanks, Paul.

Mr Girvan: You mentioned a couple of dates, there. I appreciate that the CEO directed staff to begin the investigations on 23 January. What role did senior managers play in advising him of the risks of running both concurrently? Procedurally, that seems wrong.

Mr Pengelly: I have to confess, I do not have any documentary evidence of any advice given to the chief executive at the time, and I was not privy to any conversations that were taking place at senior management level. Sara, I do not know whether you want to add anything?

Ms Venning: No, other than that the senior team made the chief executive aware of the fraud policy and the need to escalate the suspected fraud in line with the fraud policy. That was communicated to our corporate governance team on 27 January, and the initial investigation and confidential inquiry form was completed on 28 January, which kicked off our notification formally to the Department. There would have been advice and conversations between the management team and the chief executive in that regard at that time.

Mr Girvan: I want to just step back slightly from that date. What was the first indication that the problems were associated with suspected fraud? How many weeks or months prior to the telephone call was that?

Mr Pengelly: The key indicator of fraud was the invoice-slicing. I do not know the precise date, but the chief executive commissioned work from internal audit on 3 December 2009, and the report was presented to the executive committee on 11 January; so, it was sometime within that piece of work that the head of internal audit identified invoice-slicing.

I hope that this does not come across as being overly pedantic, but invoice-slicing is an indicator of fraud. There was no evidence of actual fraud at that stage. That said, to internal audit, that should get the antennae wobbling. It was an indicator of fraud, so it was brought forward some time in that period between early December and 11 January.

Mr Clarke: I have difficulty with respect to what you are saying, Richard, and what Sara has said. Sara talked about an instruction under the former chief executive to carry out the disciplinary process, which was a process. Your words were that it was just initial contact. Can we clear up whether the telephone call that my colleague is talking about was initial contact or was part of the disciplinary process? Given that you said earlier that you do not have responsibility for Northern Ireland Water, albeit you oversee it, if what Sara is saying, which is that the former chief executive said that it was part of the disciplinary process, then it was part of the disciplinary process, but can we get clarification on that?

Mr Pengelly: The instruction was to carry out an investigation under the disciplinary process.

Mr Clarke: So, it was not just initial contact.

Mr Pengelly: No, but the person who then undertook the disciplinary process prior to going into the full disciplinary review conducted an initial telephone conversation with the employee.

Mr Clarke: My reading of the report was that the process started with a telephone conversation. Sara, when a member of staff is off, does Northern Ireland Water conduct disciplinary processes over the telephone?

Ms Venning: Absolutely not. We have a well defined disciplinary process.

Mr Clarke: So, that is not your process. Can you see how some of us were sceptical that you were tipping off some of those who were alleged to have been involved in invoice-slicing and suspected fraud?

Ms Venning: If I can take you back to the CEO's instruction to conduct interviews under the disciplinary process, which is in the report and was given via e-mail on 20 January. Following that, there were a series of telephone conversations between the chief executive and the person asked to do this work, thereby setting the scene from the chief executive to the then director of customer services asking him to establish the facts. The formal disciplinary hearings took place in July. Are you satisfied with that answer?

Mr Clarke: OK.

Mr Dallat: Was the disciplinary process that we are talking about initiated by the chief executive by way of a telephone call?

Ms Venning: No. The chief executive set out, in an e-mail on 20 January which is laid out in this report, to the director of customer services asking him to conduct interviews under the disciplinary process to clarify the three points that are in the report, to understand the reasons, to find out who gave the instructions and to consider what steps might need to be taken. It was not, under our policy, a formal disciplinary hearing. Those hearings were conducted later in the year when charges were framed and individuals were written to. You cannot have a disciplinary process unless you have evidence of a charge to put to the individuals, so what was happening was fact-finding in order to understand what the facts were.

To take you back to alerting staff if a suspected fraud had happened; to be very clear, in this instance, the invoice-slicing was offered up unprompted by the individuals involved. So, there was no danger through the telephone conversations that were had in this particular instance that they were alerted to us being aware of the activity that they had carried out because they made us aware of the activity.

Mr Clarke: That is not my understanding from reading the report. The person had suggested in the initial conversation that it was his line manager. Then, later, he changed that to the director. So, I am still concerned about NI Water's fishing exercise. At the very start of today's conversation, my colleague talked about starting the disciplinary process before the fraud investigation. I think there has been an acceptance that that may have been the case here. How, Sara, can you then suggest

that you can go on fishing exercise, when we already have a suspected fraud? Now, you are telling us that you went on a fishing exercise to try to get some information before you started the disciplinary process. That is what it sounds like.

Mr Pengelly: I think that —

Mr Clarke: Maybe if Sara could answer.

Ms Venning: The director of customer services was —

Mr Girvan: Is that Liam Mulholland?

Ms Venning: It is.

The interviews that Liam carried out, in conjunction with the head of internal audit and a member of the human resource (HR) team, were to understand the reasons behind suppressing the invoices to £20,000, to get clarity on who gave that instruction and to then take that back to the chief executive to consider what the next steps would be.

Mr Clarke: Do you think that the best way to carry that out was over the telephone?

Ms Venning: No, I do not think that the best way to carry that out was over the telephone. There was an initial telephone —

Mr Clarke: Given that this arose two to three months prior to the telephone call, what was the urgency to make the phone call, as opposed to waiting until that member of staff had returned to work? Has somebody else something to cover up?

Mr Pengelly: I think that it was a matter of days before the phone call.

Ms Venning: The report came —

Mr Clarke: The internal audit bringing forward the suspected fraud was some months —

Mr Pengelly: The report was on 11 January.

Ms Venning: The report came to light on 11 January.

Mr Pengelly: The phone call was on 20 January, I think.

Mr Clarke: I make it 3 December actually.

Mr Pengelly: On 3 December the work was initiated, but the internal audit work ran from 3 December —

Mr Clarke: The work may have been initiated on 3 December, but it had already come to light at that stage that there was a problem.

Mr Pengelly: At 3 December, the chief executive was aware that the contract had been extended. The invoice-slicing became —

Mr Clarke: And also on 3 December, they knew that they did not have budget approval for spending that extra £465,000. So, they knew, on 3 December, that something was going wrong. The telephone call did not take place until 20 January.

Ms Venning: There was no —

Mr Clarke: Two months had passed by that date. Then, there seems to have been an urgency to make a phone call, as opposed to waiting until the member of staff returned to work.

Mr Pengelly: The phone call was very much in the context of the invoice-slicing. That became apparent only in the period between 3 December and 11 January. That was the indicator of fraud. It was the invoice-slicing that prompted the suspected fraud investigation, not the contract extension. That was a contract management issue on which a parallel piece of work was ongoing, and a series of actions and recommendations have been taken forward. This was a particular fraud indicator.

Mr Girvan: Was this the first fraud investigation in Northern Ireland Water?

Ms Venning: I would not think so. There was a well-established fraud response plan. So, no, I would not say that it was the first, although I could not say to the Committee what the previous frauds that have been investigated were. However, I am aware that we have investigated fraud since.

Mr Girvan: I appreciate that there might well have been lessons learned from that, which have probably led to some changes being made to how the organisation deals with matters such as that.

At that stage, I wonder what the capacity was to do internal investigations — because it is internal. If there was a lack of capacity, was there ever a time when you thought that you should look outside your organisation and bring some other independents in to undertake such a body of work?

Ms Venning: Yes. In the context of this review, external assistance was sought in the form of forensic accountants. So, it was recognised, even through this investigation, that the internal team could benefit from some external support. Those forensic accountants were brought in and carried out some forensic work in relation to electronic data by looking at hard drives and e-mail communication that had been carried out. They also gave some ad hoc and informal-type advice to the head of internal audit on how the investigation was being framed. However, their main remit was to provide support in relation to the electronic data.

Mr Girvan: I just want clarification on one point. I want to know what the capacity in Northern Ireland Water was, at that time, to deal effectively with that type of investigation. Was it just its own internal accounting department or was there expertise to actually deal with that?

Ms Venning: At that time, we had an internal audit department, so qualified auditors were part of the company. We also had a finance department. However, the internal audit team was asked to head up the investigation.

Mr Dallat: Paul's question is very useful, but we have not got to the bottom of why your former chief executive went about this in such a cavalier fashion. Can I be helpful, perhaps, in jolting your memory? He was having problems with his non-executive directors, he needed to sack them, and invoice-slicing was commonplace in NIW for years. He found the reason, and he succeeded in what he wanted to achieve, namely to dump the non-executive directors who were causing him problems with the manner in which he was running NIW. Is there any element of truth in that? Remember that your Minister has apologised for that.

Mr Pengelly: From my perspective, Mr Dallat, I know that those issues have been aired before. I have no personal memory of that; I was not in the organisation at the time. I have not sought to look at the detail of that, because it is not within the scope of the report that I am here to answer questions on today. I cannot offer you any assistance with that point.

Mr Dallat: That is the problem. There are people who came before you who do know about that. However, I understand that your Department is resisting having those people appear before this Committee. Therefore, a lid can be kept on the most appalling period in NIW's history. Quite frankly, this Committee needs to know about that.

Mr Girvan: I appreciate that the audit would have looked at papers and ensured that they all followed, but I have heard a statement that paper reviews mean nothing.

Mr McQuillan: Sara, in an earlier answer to Paul, you talked about the period when the investigation started. At what stage did you decide that it was to be a fraud investigation?

Ms Venning: On 23 January, the chief executive wrote to the head of internal audit and asked her to commence an investigation into suspected fraud.

Mr McQuillan: You went on to say that you had a well-rehearsed fraud response plan. Was that enacted when it should have been or was it veered away from? I envisage that what John Dallat said is correct — it was not enacted at all but was left sitting on a shelf while the chief executive went off on a solo run.

Ms Venning: On 23 January, the chief executive instructed the head of internal audit. That was a Saturday. There was a delay from 23 January to 27 January, and, on 27 January, the head of corporate governance was made aware that there was to be an investigation into suspected fraud, at which point the fraud response plan —

Mr McQuillan: — should have been enacted.

Ms Venning: — should have been enacted.

Mr McQuillan: Was it enacted?

Ms Venning: There were certainly deficiencies. It was enacted in the sense that that was when the initial confidential inquiry form was completed and passed to the Department, but the deficiencies that we are discussing today are about the fact that the disciplinary interviews and that disciplinary work had commenced in advance.

Mr Copeland: Richard, do you think that a fraud took place?

Mr Pengelly: Based on the evidence that I have reviewed, no; I do not.

Mr Copeland: You do not think a fraud took place?

Mr Pengelly: I do not believe that the invoice-slicing was fraudulent.

Mr Copeland: I am no great believer in coincidence, but 386 invoices is four short of 390, and 390 looks to have a certain connection with £3.9 million. I am not saying that that is case, but it just looks like it to me. Paragraph 48 states that 18,000 meters were checked and 50,000 properties were surveyed. In my view, it uses a very curious form of words. It says that they checked the values against the invoices. In other words, the rates for the work that had been invoiced were correct. It does not say whether the work was done or whether anyone checked that it was done. It also wanders into rather strange language when it states:

"against relevant customer billing records; meters were not physically inspected".

That takes me back to how company E ever became involved in Northern Ireland, what the structure of the company was, how it got the work, and what it actually did. It seems that its main function was to send out invoices that correlated to the requirements of the slicing operation. I will come back to that later.

Mr Pengelly: Again, I will cover my knowledge of it, and Sara can add any detail that I miss. The contract was for the installation of meters. It states that invoice rates were agreed. You need to bear in mind that, at that stage, there had been a contract extension that should not have happened. However, as for the contract that was let and erroneously extended, the check was to make sure that the rates on the invoice agreed with the contract so that the company was being charged what the contract anticipated it being charged.

Mr Copeland: Was there a check that the company had done the work that justified the raising of the invoice?

Mr Pengelly: There were three stages to check whether the work had been done. After every meter was installed, the company took a photograph of it and sent it to Northern Ireland Water. The meter was then added to Northern Ireland Water's billing system. The first check was to make sure that there was a post-installation photograph of every meter for which there had been an invoice.

Secondly, there was a check that they were all on the billing system. The third check, which was conducted after the first two had been concluded satisfactorily — this is specifically drawn out in the

report — was to see whether a meter reader, who was independent of the whole process of installation and had nothing to do with the company, had physically visited the installation to take a meter reading to confirm its existence. Of the sample, the report highlights that there were, initially, 14 cases in which that was not possible. In a number of cases, the reason was that the meter had not reached the point at which it was due to be read by the independent reader. In the other eight cases, the report concluded that that needed to be followed up. That takes us beyond the quality of the investigation. Post the investigation, those eight cases were followed up and the meters were physically inspected.

Mr Copeland: And found to be there?

Mr Pengelly: And found to be there.

The Chairperson: I remind members to stick to their line of questioning. I know that some members will be covering that area later. Mr Girvan, are you finished?

Mr Girvan: I am happy enough for now. I think that Trevor is going to follow up on the issues that I raised.

Mr Clarke: Actually, I want to go back, because I still do not have clarity in my mind. We are struggling with the timing of the suspected fraud and the disciplinary procedure. I am not satisfied with what Sara said about the disciplinary procedure because, clearly, the chronology in the Audit Office report suggests that the chief executive sent an e-mail on 20 January instructing interviews under the disciplinary process to start. Are we to accept that it was not a fishing exercise on 20 January, but that it was the start of a process? Sara, are you satisfied with the report, how the Audit Office has presented it and the facts in it?

Ms Venning: I am satisfied that this is an accepted report. On that basis, we have to accept what is laid before us.

Mr Clarke: So you accept that it was not a fishing exercise? I think that the words that you used —

Ms Venning: Fact-finding.

Mr Clarke: If you accept the report, it was not fact-finding; it should have been a disciplinary process — if you accept the report, that is.

Ms Venning: We are accepting the report.

Mr Clarke: So the chief executive sent an e-mail to start a process on 20 January. Is that right?

Ms Venning: He did.

Mr Clarke: And instead of starting a process, you went fact-finding?

Ms Venning: The chief executive e-mailed on 20 January to start the disciplinary process, but he qualified his e-mails with telephone conversations with the person whom he had e-mailed, advising what he wanted, which was to find the facts. The formal hearings —

Mr Clarke: In that comment, you will accept the difficulty that we have with telephone calls. It is the same as the difficulty with starting a process with telephone calls. Let us work on the facts. We have e-mails in which the chief executive contacted someone to start a process. Anything else other than that, including telephone conversations, is hearsay. Is that fair?

Ms Venning: I can accept that.

Mr Clarke: Someone suggested that the audit team was a qualified audit team; is that correct?

Ms Venning: Yes.

Mr Clarke: And you accept the report?

Ms Venning: Yes.

Mr Clarke: Will you then accept the criticism that the audit team was not qualified in dealing with fraud?

Ms Venning: Yes.

Mr Clarke: So you will understand the scepticism because, although Richard has said that he is satisfied that fraud has not taken place, by your own admission, your internal audit team was not experienced in dealing with fraud cases.

Ms Venning: I accept that our audit team had limited experience in fraud cases. It was supplemented by a forensic team that was external to the company, which had extensive experience in fraud cases and provided the internal team with some support. I back and support Richard's comments about the belief over whether fraud had happened in that case.

Mr Pengelly: May I add, Mr Clarke, that DFP guidance, our departmental advice and the Northern Ireland Water fraud response plan recognise that there is a range of people who may be appropriate to lead fraud investigations. Sometimes, it is the head of internal audit and, sometimes, it is an external specialist. Indeed, our normal default position is to use the relevant director within the business area. The key is to supplement that person with the right skills, as happened in this case, or, in more complex or novel cases, to bring in a lead investigator who has the appropriate skills. I am not saying that, in this case, it was perfectly right, I am just highlighting the subtlety that the guidance recognises that it does not have to be a qualified fraud specialist that leads every fraud investigation.

Mr McQuillan: On that point, the recommendation in paragraph 42 states that investigations should be carried out by people who have knowledge of:

"collecting evidence in accordance with the provisions of the Police and Criminal Evidence (Northern Ireland) Order 1989."

Did the external auditors that you brought in have that experience?

Ms Venning: Yes. They were brought in to carry out the electronic data capture, and they had that experience. However, at that time, the head of internal audit was not qualified. She since has qualified, and has taken six members of staff from across NI Water and is taking them through training and getting them qualified in the gathering of evidence. However, the answer to your question is yes; they did have that knowledge.

Mr McQuillan: Things may look up in the future if those six qualify.

Ms Venning: Yes. It is a range of people from across the organisation, from internal audit, corporate governance and our accounting and legal teams.

Mr Clarke: I just want to come back on that point and follow up on your last response, Richard. I accept that internal audit is not always looking for fraud, but, looking at paragraph 43, why were the services of the PSNI not engaged, given that they would have relevant experience? Also, bearing in mind that there was a suspicion of fraud on 23 January, and given your admission that there would not have been expertise internally, why did no one go to an external organisation such as the PSNI, which does have that experience and has people trained in looking for fraud?

Mr Pengelly: Unfortunately, I can only speculate in answer to that. I suspect that, at the time, the guidance was not absolutely prescriptive about contact with the likes of the PSNI. The view was that the individuals concerned had held their hands up and said that that is the operating procedure. It was not seen as particularly complex. I think that, in hindsight, the phone call should have been made to PSNI. In conversations that I have had with Sara over the past couple of days, she has assured me that, in every case of suspected fraud since, contact is made with the PSNI at an early stage.

Mr Clarke: I accept what you are saying Richard, and I think that that is useful. However, for someone who is a bit cynical about how this stuff works or someone from the outside looking in, can you see that you have not invited in an organisation that has expertise, you have taken on board people allegedly putting their hands up to a degree, but that you could also read this as a bit of a cover-up within Northern Ireland Water — that it did not want to uncover the fraud?

Ms Venning: You could, but I would not accept that as being the case in any shape or form. I would suggest that the thinking in the organisation at that time was that they had uncovered an indicator of fraud but, at that time, they had no evidence of fraud. In dealings with the PSNI, it is always useful to be able to bring to them the evidence. Before they will take anything forward or offer a case number, they will seek evidence, although I assure the Committee that we are very clear on this and have engaged with the PSNI on every case of fraud, no matter how small, since this report was issued. We have very close links with the crime unit.

The Chairperson: Before I let Mr Easton in to ask a question, the Deputy Chair wants to ask a follow-up.

Mr Dallat: Just remind me, as I just skim through this, who were the external people brought in to look at this fraud.

Ms Venning: The company was Deloitte. It had been engaged by us at that time to look at another major contract.

Mr Dallat: So Deloitte was already well immersed and involved in NIW's activities?

Ms Venning: It had an assignment and was working for us at that time. We were able to go to Deloitte with this assignment, and we engaged it to take on that work.

Mr Dallat: I asked that question, Chairperson, because the issue has arisen previously. We have internal auditors and we have external auditors, and then we have auditors who investigate alleged fraud. You were using the same people who were already well immersed in NIW. They were in a position to be biased, if you like.

Ms Venning: They were engaged in a specific commission for NIW. They were neither our internal nor external auditors; they were engaged in a specific piece of forensic accountancy work for NIW at that time.

Mr Dallat: Were Deloitte the only people who were involved? Was Ernst and Young involved in anything?

Ms Venning: Initially, it was the company that provided internal audit services —

Mr Dallat: Chairperson, why do I have to drag everything out? I expected, Sara, that you would say that. Ernst and Young was involved.

Ms Venning: Ernst and Young was the company that provided NI Water's internal audit services in advance of NI Water establishing its own internal audit department.

Mr Dallat: Yes.

Ms Venning: It was not involved —

Mr Dallat: Is it not rather interesting that Ernst and Young, which runs international awards for the most successful businesspeople, has, this year, nominated Peter Dixon, whom your former chief executive appointed to head up the independent review team that sacked the four directors? I think that, from this moment on, we want to get all the details and not just have another skimming process. We want to hear exactly what was going on. This Committee's work is of no value if we are just having something that was rehearsed for two or three days presented to us. I am sorry, but that is not on.

The Chairperson: I remind the Deputy Chair that Mr Dixon has nothing to do with this inquiry. That is just for information.

Ms Venning: We are looking at 2010. In 2010, the internal audit function was entirely provided by NI Water by its own internal audit team. Ernst and Young had no input into the internal audit function in NI Water in 2010, when these events took place.

Mr Easton: I want to focus on the disciplinary investigation. The disciplinary letters issued to two members of staff contained an error of fact. Sara, can you tell us more about that, please?

Ms Venning: Certainly. Under the disciplinary procedure, letters needed to be framed and charges placed to the individuals concerned. Given the procurement issues that had arisen in the organisation, the head of HR considered herself conflicted in that regard and felt that she could not take any part in advising on the disciplinary process. Therefore, not having access to HR advice internally, external advice was sought. The external people were provided with the information available at the time and asked to frame charges letters. That was done, and the letters were put to the individuals. The disciplinary hearing then proceeded to hear the case, based on the charges letters that were framed.

Mr Easton: What were the errors in the letters?

Ms Venning: The letters stated that the individuals were in breach of the financial delegations because they had limited invoices to £20,000 — the emphasis being on the value of £20,000 — when, in fact, those individuals had authority, under financial delegations, to authorise invoices of up to £50,000.

Mr Easton: Why were the facts not checked before the letters went out?

Ms Venning: That is a very valid point. We had, I suppose, outsourced that activity to specialists, and we took the output of their work and used it. We had engaged them in a professional capacity, we had given them all of the information that was available, and we had accepted their professional output.

Mr Easton: So you are placing blame for the mistake on the outsourced work?

Ms Venning: I suppose that we have to hold our hands up and say that those letters were not sufficiently checked internally.

Mr Easton: OK, but you did it because of the outsourcing.

Ms Venning: We bought that expertise.

Mr Easton: To put my mind at ease, and so that we all know where we are coming from, can you tell me who was in the fraud team and who was in the disciplinary team? Can you break that down slowly?

Ms Venning: Certainly. The fraud investigation was carried out by the head of internal audit and supported by Liam Mulholland. Paddy Murray was involved. He is a member of the HR team. I was chairperson of the disciplinary panel for the disciplinary hearing and was accompanied by a member of the HR team.

Mr Easton: Who was that?

Ms Venning: Kathleen Simpson. To give some context, I was the chair of the disciplinary panel, but I joined NI Water in late April/early May 2010. When I was asked to be the chair, as someone who was in no way involved with any of the preceding events, I specifically asked that those charges be framed for me, having not had sufficient knowledge of the events that had taken place. I specifically asked that those charges be framed. That was done via the external advice.

Mr Easton: Why was Northern Ireland Water's policy for disciplinary processes not followed?

Ms Venning: With regard to the earlier phone calls?

Mr Easton: Yes.

Ms Venning: I can only say that, at that time, I suppose that it occurred in the interests of trying to achieve speed over substance. There was an intention to try to get to a speedy conclusion with the suspected fraud; the organisation did not want a delay. I cannot condone that. We are all very clear on the disciplinary procedure that must be followed: of the need to notify people and the need to afford people representation. That is what happened in the part of the process in which I was involved.

Mr Easton: So the people who messed up in the process, with the letters, before you came along, should have known the process for disciplinary hearings?

Ms Venning: The external advisers? They were aware of our process.

Mr Easton: And what about your staff, before you came along? Would they have known all of that; known the process?

Ms Venning: Yes.

Mr Easton: Who was in charge before you came along?

Ms Venning: My role was split between two individuals.

Mr Easton: Were they both doing the disciplinary work before you came along?

Ms Venning: Initially, the disciplinary process was headed by Liam Mulholland.

Mr Easton: Is that not a conflict of interest because he was dealing with the fraud at the same time?

Mr Pengelly: That is one of the key issues, and it goes to the points that Mr Clarke was asking about. I could take the line that the disciplinary process did not start until after the fraud investigation, because those preliminary investigations were not disciplinary investigations, and it was really July, when the letters kicked off. The fact is that, in January, the chief executive e-mailed, asking for interviews under the disciplinary procedure. To my mind, the first time you mention it, it is started. The substantive nature of the work and the early interviews that Liam Mulholland did were, realistically and pragmatically, more part of the early fraud investigation work than a disciplinary process. That is why we refer to them as preliminary inquiries and interviews.

It is interesting — I suspect that we may get to this later — that the terms of reference for the fraud investigation report do not refer to any interviews with the key players. That in itself would be a key failing were it not for the fact that there was a parallel process of ongoing interviews. Those were much more part of the fraud investigation than of a disciplinary process. As I said earlier, the terminology was very lax. I do not think that it was so much a conflict of interest with Liam leading those early interviews; that was done more with a fraud investigation hat on. It was really around July that the charges were framed, and you —

Ms Venning: I took over.

Mr Pengelly: — took over the panel. There was not much happening, disciplinary wise, before July.

Mr Easton: I do not accept that. We have the director of customer services, Liam Mulholland, directly involved in a disciplinary process, and you took over that and the fraud. That is a complete conflict of interest because he was doing both roles. Somebody in that senior position should know 100% how to do a disciplinary hearing, and the process. It is quite clear that he must have known about those phone calls and letters. Would he not have given —

Ms Venning: The letters were within my time. It goes back to the crux of the matter being the conversations — I accept that they can only be called hearsay — that Liam had with the former chief executive. Liam would tell us that he is very clear that he was asked to find facts.

Mr Easton: He was doing the disciplinary process. It is not about facts. He was doing both roles. Did he know about those two letters going out?

Ms Venning: He had no involvement in that because he had been involved in the initial investigation.

Mr Easton: Did he see those letters?

Ms Venning: No. He had no involvement in that.

Mr Easton: He did not see those letters at all?

Ms Venning: No. He had no involvement.

Mr Easton: Who saw those letters apart from you?

Ms Venning: The letters came into the organisation through the company secretary because they engaged the external advice.

Mr Easton: Who was the company secretary?

Ms Venning: The company secretary's name is Mark Ellesmere. The letters were not checked internally. We took the advice of the external advisers.

Mr Easton: Is that not gross incompetence?

Ms Venning: The HR team also saw the letters, but it did not check them.

Mr Easton: And Mark Ellesmere appointed the legal firm to advise on the disciplinary case?

Ms Venning: Yes.

Mr Easton: So really nobody in your organisation knows how to carry out a disciplinary process. Nobody seems to know how to do it properly.

Ms Venning: We do know how to carry out a disciplinary process, but I have to accept that, in this case, it was not handled well.

Mr Easton: Do you accept that the disciplinary process was extremely flawed and not carried out in line with the proper rules and regulations?

Ms Venning: Yes.

Mr Easton: Who is holding those people to account for this debacle of a disciplinary process? Has anybody been held to account for not knowing how to carry out a disciplinary process?

Ms Venning: The disciplinary process has concluded. The interviews have taken place with the individuals involved. I am comfortable that the account that was given to me through that process indicates that, in relation to the invoice-slicing or the facts that were put to those people, there was nothing further to take through that disciplinary process.

Mr Easton: You reached that decision because the letters that you sent out were flawed in the first place.

Ms Venning: I accept that the letters that were sent out in the first place were flawed. However, the delegation authority that those people had was clear to me when I spoke to them. That was subsequently picked up in the letter that I issued to them following the disciplinary proceedings, which accepted that their delegation authority was £50,000 and not £20,000.

Mr Easton: Do you not think that, because the whole process was flawed, the whole thing should have been done again properly?

Ms Venning: On the issue of the £50,000 and the £20,000 figures, the individual who spoke to the company was clear that he asked for those invoices to be limited. From the conversations that I have had with individuals since and from the way in which we have managed the metering contract since, it is clear to me that, in limiting the invoices, the intention was to limit the amount of work that needed to be checked and thereby make it easier to manage the contract.

I will take you back to the work that was carried out. There were large volumes of low-value transactions, and when invoices were very large, if one transaction was queried — if one meter could not be found or if one photograph was not there — the whole invoice could get held up, and the contractor would not get paid. Subsequently, we have made sure that we issue and call for work in smaller batches so that we can check and clear that work, and, if there is a query, we are not holding up large amounts of work and money to which people are rightfully entitled.

Mr Pengelly: There is a wider point about the disciplinary process being run again. The disciplinary process concluded, and we accept that it was flawed. The first thing to recognise is that, as an employer, NI Water owes a duty of care to the people who were subject to the disciplinary proceedings and, given that it concluded that there was a flaw in the process — you could debate the significance of the flaws for quite a while — it would have been unfair to those two individuals to rerun the process. As I said in answer to Mr Copeland's question, based on all the evidence that I have seen, I have not seen any evidence of fraud. I have seen evidence of poor practices in contract management. That was rife throughout Northern Ireland Water at the time, and this Committee has had a number of sessions on that. It was about organisational failings, not about singling out two individuals and rerunning a disciplinary process a couple of times to have a go at them. The vast majority of the recommendations from the earlier internal audit work were very much focused on contract management. They have been picked up and actioned organisationally, and that is the right way to deal with the culture of contract management throughout the organisation rather than targeting two individuals who were caught up in the process.

Mr Easton: I am not here to have a go at the two individuals. I am trying to point out to you the gross incompetence of staff in NI Water and how they handled the whole process. Not only were the two individuals, whether they were innocent or guilty, tipped off before a fraud investigation but there were numerous phone calls and messing about with letters, and so on. For such senior management, the whole process is beyond belief. I want to know why that happened. We need to get to the bottom of it because that is not acceptable, and we need to know that that has been rectified and will never happen again. It is up to you to convince me of that.

Mr Pengelly: I appreciate that, and I hope that I can go some way towards doing that. In looking forward, NIW and the Department have refreshed their guidance. Indeed, we will certainly do so again in light of the report from the Committee in due course. There were problems with the disciplinary process. If, in a hypothetical situation, we were able to airbrush the then chief executive's e-mail in January that said to conduct investigations under the disciplinary process, the work that took place would be valid as part of an early fraud investigation. There was work by internal audit, and there were preliminary interviews with the employees concerned. That led to a report that formed the basis, in and around July, of the framing of disciplinary charges. The reason we say that the disciplinary process started early was because of that e-mail, but there were no other substantive elements of a disciplinary process that started ahead of July. However, I do not want to argue that a disciplinary process did not start because the word was used, and, as I said, I absolutely take the point that it should not have started then because there was a real risk of putting individuals who would be subject to disciplinary mechanisms on guard or on alert. In this case, we need to keep reminding ourselves that the two individuals concerned identified the problem to management in the first instance. So, to the extent that they needed to be on alert, they were, and they were put on alert by their telling management about what they had done.

Mr Easton: I have one final question. Why did DRD fail to inform the Auditor General of the suspected fraud, in accordance with the Department of Finance and Personnel's guidance? Is that not a serious breach of procedure by DRD? Who made the decision not to report that? It is in the report.

Mr Pengelly: I will start at the back. Nobody made a decision not to inform the C&AG. The notification to the C&AG did not happen because of an administrative oversight. It was a serious lapse on our part, for which we apologise to the Committee and to the C&AG. It should have been reported the first time we knew about it, but it was purely an administrative oversight. It was not a conscious decision not to tell the C&AG.

Mr Easton: Has it happened before?

Mr Pengelly: I suspect that it may have done, but I do not know what I do not know. If I did not know about something and did not tell the C&AG, I am not aware of it.

Mr Easton: Do you not know your guidelines?

Mr Pengelly: We do. This should not have happened. It was an oversight.

Mr Easton: How many oversights were there? There were oversights in how you handled grievance procedures, and so on, and now this one. How many oversights were there in Northern Ireland Water?

Mr Pengelly: You used the word "oversight". I think that the grievance procedure could have been handled better, but there was no oversight with that. This was a notification.

I want to be absolutely clear that this was important: it should have been done, and it is a matter of regret that it was not. However, the failure to notify the C&AG in no way undermined the way that we treated the issue from that point on. Notification to the C&AG just puts it on his radar. The C&AG is not part of the investigative process, and he certainly does not come along at that stage and make sure that we are doing things correctly. It is a much more reflective view, so I do not think that it undermined the process. However, it was an oversight on our part, and it should not have happened.

Mr Easton: Whose job would it have been to inform the C&AG if there had not been that oversight?

Mr Pengelly: It should have been the shareholder unit in the Department when it received notification from Northern Ireland Water about the suspected fraud. There is a standard form, and the details should have been put on that and sent to the C&AG.

Mr Easton: Did anyone discuss not informing the C&AG? Were you party to anything like that?

Mr Pengelly: The explanation that I have been given, which I fully accept, is that it was an administrative oversight.

Mr Easton: If the staff of Northern Ireland Water were politicians, they would not get elected if they kept doing what they are doing. They might need to buck their ideas up a wee bit.

The Chairperson: Thank you, Mr Easton. A number of members want to ask supplementary questions. Alex, are you finished with your line of questioning?

Mr Easton: Yes.

The Chairperson: Trevor Clarke, Paul Girvan and Adrian McQuillan want to ask supplementary questions. Please keep them brief, because I want to move on to Mr Rogers's questions.

Mr Clarke: Thank you, Chairperson. My question is along the same lines as my colleague's. I suppose that it is back to the idea of perception. With the catalogue of all the different things that happened, one could perceive that there may have been a different motive.

Sara, from the report, I am a wee bit unclear about the telephone call. I am concerned about how that happened. I accept that you said that it should not have happened in the way that it did and that it should not happen in the future. In the first telephone conversation with the individual concerned, he suggested that it was his line manager. What grade was that line manager at that time?

Ms Venning: The line manager is what is known in NI Water as a level 3.

Mr Clarke: Is that individual still with the organisation?

Ms Venning: Yes.

Mr Clarke: He then suggested that it was someone else. Is that person still with the organisation?

Ms Venning: No. There was an initial suggestion that the instruction came from a director. However, that was subsequently clarified in face-to-face interviews, in which the contract manager was very clear that the instruction had come from his line manager.

Mr Clarke: Sorry, from whom?

Ms Venning: His line manager.

Mr Clarke: Is that the grade 3 who is still with the organisation?

Ms Venning: Yes. However, he absolutely and categorically denied that that was ever the case. No evidence was uncovered in the electronic sweep, which was able to pick up any deleted material. There was no evidence to back that up, and the team was unable to categorically discover who gave that instruction.

Mr Clarke: Given that you have depended on other telephone conversations and verbal material, there is nothing to suggest that, in this case, given that verbal is acceptable in other cases, that it was not a verbal instruction.

Ms Venning: That is correct, and you have no means to —

Mr Clarke: So you could cast reasonable doubt on that.

What level is the person at now who was the level 3 manager at that time?

Ms Venning: That person is still a level 3 manager in the organisation.

Mr Girvan: I want to come back to Alex's earlier question. Given that Northern Ireland Water was seen as a Go-co, did that make a cultural change to the organisation whereby it felt that it was less in the line of scrutiny or accountability? Was there a possibility that that was the case? It appears that the company did things that do not necessarily equate with a well-run Department. It is evident that a culture may have been created in the organisation when it became a Go-co in 2007. A few years in, and things have been quite lax.

Ms Venning: I am not sure that that would necessarily be the case, in that the obligations on a company under the Companies Act are equally onerous on ensuring that money is properly accounted for and that contracts are properly let. Therefore, there is no freedom to say that a company can have a culture of not having expenditure properly approved because it is a Go-co. I accept that a number of irregularities were uncovered. From 2010, there has been an extensive programme to regularise contracts. Last year, the NI Water accounts were clean in that regard; they were unqualified, as they were the previous year. Therefore, I would not link it to the fact that the company was a Go-co. I would say that there was work to be done, but extensive work has been carried out in that regard.

Mr Girvan: I accept that there have been dramatic improvements in the accounts of the past two years with regard to their being signed off and clarified, and everything has been OK. Is that not due to the fact that, had the spotlight not be shone on certain issues, what happened would have continued, and we could be investigating much more had it not been picked up? By today, it could have been a lot worse. As I said, I appreciate that paper refuses nothing; accounts can be signed off, but that does not mean that everything is 100%. It seems to me that there was a culture whereby NI Water felt that it could do what it wanted. To allow that to happen, somebody was giving certain people cover, which allowed them to slice invoices — or whatever way you want to put it. That culture must have been there. Maybe it did not happen with one contract only; it could have happened with several.

Mr Gary Fair (Department for Regional Development): I will speak from the Department's point of view at the time. The governance letter that was put in place, which outlined the governance relationship between DRD and Northern Ireland Water when it was established as a Go-co in 2007, was still in place. There would have been expectations that the company was not doing what you

were describing and that it was managing its affairs properly and in every way that would be appropriate.

Mr Girvan: Expectations.

Mr Fair: Yes, but the company was established at arm's length from the Department. Changes came about from January 2009 with the reclassification to a non-departmental public body rather than a public corporation, which the Go-co was when it was established. It had an immediate impact on the Department's budget and there were public expenditure (PE) implications. Further to that — it was probably when all this came to light — it was at a transitional time when the governance relationship between DRD and Northern Ireland Water was being strengthened, and we were requiring more information than would have been anticipated if charging had been introduced as planned and the company had become self-financing. So it was a transitional period from everyone's point of view. Things would have developed automatically around that time and onwards, and things such as this probably would have come to light because of the more stringent governance requirements as a result of the amount of public money that was going into the company.

Mr Copeland: Perhaps Richard or one of his colleagues could answer this question. How does invoice slicing occur? Did that happen in Northern Ireland Water when it was realised that a specific invoice from company E exceeded the permitted payments? Was there any communication between that person and the person in company E who would have been required to rejig the invoices to suit the requirements? What is the mechanism for that?

Mr Pengelly: It goes back to the point that a lot of this emerged through oral interview as opposed to being documented. The view that was put forward from the contract manager, who did not initiate the instruction to company E to slice invoices but who inherited that position, made a lot of sense. His view was that the volume of installations, which are of fairly low value individually but were being rolled up and put on one invoice, meant that when it came into Northern Ireland Water, it was a monumental task to check each and every one. If there was one query on one small installation, it delayed the payment of a very substantial invoice, which caused cash flow difficulties for the company and, presumably, for its subcontractors.

The view was that each and every one of those items must be checked to a certain standard, but rather than send us an invoice for a very large amount, the company should invoice us more frequently, which means that we can do the checks in smaller batches. It means that, if there is a query, it does not delay the processing and payment. The problem is that as an indicator of fraud, looking at it from the other end of the telescope, an invoice value of £20,000 in this case needs to be checked by a certain level of employee in the company. If an invoice goes over £50,000, a more senior manager needs to check that and approve it for payment. The reason why invoice slicing is an indicator of fraud is that it can bring the level of scrutiny of invoices prior to payment down a notch, and senior managers do not see them.

No one has admitted to giving the instruction so we cannot know definitively, but the contract manager who was in place post-April 2009 had a view that, perversely, it led to a stronger control environment because it meant that more checking of individual items could be done at a quicker pace.

Mr Copeland: Did it require any actions in company E?

Mr Pengelly: Company E, again based on information from interviews, received the instruction to do it. It was not about inflating invoices; instead of sending us an invoice every fortnight, it was asked to send us an invoice every week. That was the sort of instruction that was given.

Mr Copeland: Do we know who sent the company that e-mail?

Ms Venning: We know that the contract manager gave that instruction to the company. We know that, in a meeting with the company, he asked the company to send us invoices with lower amounts of work in them and to keep them below a certain value.

Mr Copeland: Was he acting within his own employment remit in doing that?

Mr Pengelly: His story is that it was either his level 3 or his director —

Mr Copeland: I did not ask you that. I asked whether he was capable, within the terms of his employment, of taking that decision.

Ms Venning: He did not take the decision.

Mr Pengelly: He maintains that he did not take the decision and that he was instructed by his boss to pass that instruction to the company. According to the contract that was in place, the company invoices for work done.

Mr Copeland: Is it correct that this individual's computer hard drive was examined?

Ms Venning: Yes, and his boss's.

Mr Copeland: And his boss's?

Ms Venning: Yes.

Mr Copeland: And there was no evidence?

Ms Venning: There was no evidence.

Mr Copeland: Was a director involved somewhere above that?

Mr Pengelly: There was a director, but the director left the company about six months previously.

Ms Venning: In June 2009.

Mr Copeland: Did he take his hard drive with him?

Ms Venning: He had left six months previously. What usually happens is that computers are redistributed.

The Chairperson: I do not want to go over old ground, but given that the disciplinary process happened before there was an opportunity in advance of any internal fraud investigation — we talked about the lack of best practice and good governance and what should have happened — was there a concern at any time about further exposing NI Water's funds? In other words, was there a concern for the organisation's assets? If so, when did that arise?

Mr Pengelly: There was. At no point in the documentation that I worked through did I read about anyone expressing a concern about the assets or cash flow of Northern Ireland Water. The only thing identified in the initial work, and then the fraud investigation, was that there was an indicator of fraud in the invoice slicing. No evidence was uncovered at any stage of actual fraud being perpetrated on Northern Ireland Water or company E by employees or by company E. There was no evidence of fraud. All payments were traced to invoices; all invoices were traced back to agreed rates in a contract; and it was confirmed that the work on all items charged on those invoices, on a sample basis, had been done. So there was no evidence of fraud.

The Chairperson: You were satisfied at that time that the organisation's assets were —

Mr Pengelly: Yes.

Mr Rogers: Apologies for missing the start of the meeting. You said something that struck me when you talked about a well-established fraud investigation plan. Was the PSNI part of that plan?

Ms Venning: Yes. The plan stated that early involvement of the PSNI would be beneficial. That was in the policy at the time.

Mr Rogers: So it was not followed.

Ms Venning: That is correct.

Mr Rogers: What were the plan's recommendations on when you should bring in the central investigation service experts? You did not have real expertise to deal with fraud. What did your plan say about that?

Ms Venning: The plans state that a case manager is assigned when a fraud investigation is kicked off, and the case manager can decide what assistance is required. In any fraud investigation, you need to decide on the appropriate team to form around the investigation. The plan allowed for that. In this instance, the additional support that was provided came in the form of the forensic accountants who were used for the electronic work.

Mr Rogers: In retrospect, do you believe that that was sufficient?

Ms Venning: In retrospect, it is preferable if those tasked with conducting the investigation and the investigatory interviews are qualified to take them in line with the Police and Criminal Evidence (Northern Ireland) Order 1989 (PACE). That is why we have taken six individuals in our company through the CIPFA qualification, which means that we have internal capacity. We engage with the PSNI at an early stage, and we also have links with the team in DARD. We work through that team to agree terms of reference, speak to them as investigations proceed and take feedback from them. I hope that that answers your question.

Mr Rogers: I have heard on a number of occasions that there was no evidence of fraud. Could that possibly be down to the fact that the investigation was not sufficiently forensic to uncover the fraud?

Mr Pengelly: I genuinely do not believe so, because fraud would be defined as a payment by NIW in excess of agreed rates or for work that was not completed. That work is financial accountancy investigation. It was undertaken by a fully qualified chartered accountant who headed the internal audit team. Forensic audit techniques are much more sophisticated techniques that are undertaken very rarely. There is, therefore, some expertise. This was fairly standard audit work that was undertaken by a professionally qualified individual, and no irregularities were found. I genuinely do not think that additional forensic work is the issue in this case. The big point from my perspective and from Sara's is this: had there been more subtleties to a case, other than this, and we had not brought in that additional resource, there could have been significant problems. However, in this case, I do not think that it led to any problems.

Mr Rogers: However, there is an acknowledgement that it was not the plan that was the problem but the implementation of the plan.

Mr Pengelly: Yes and no. We need to bear in mind that when Sara talks about the plan, it is guidance for those undertaking investigations. Guidance is only guidance: it is not a prescriptive, tick-box approach that says that in certain circumstances, you do this, because it covers a range of circumstances. The guidance states that you should consider drawing in other experts or that early engagement with the PSNI would be beneficial, but it does say that it is mandatory. The flaw was that the full thinking on whether those options should have been pursued was not taken or documented. I do not believe that the fact that those options were not pursued undermined the legitimacy of this investigation.

Mr Rogers: Why were only two hard drives to be investigated? In answer to Mr Copeland, you said that a previous director had left six months previously and you told us what happened to his hard drives. Are these hard drives stand-alone computers? Surely there must be a backup. All the systems that we use in our offices allow us some form of backup. Is there no way that you could go back into the records of the person who left six months previously?

Ms Venning: You could, and, given that the terms of reference were framed and the initial work asked for the hard drives of the two individuals to be examined, if any evidence that pointed to the director had been uncovered, the scope could have been widened. However, there was not, and it was felt that, in securing evidence, the financial system that the invoice was passed through meant that the evidence was secure. It could not have been tampered with, was held centrally and was examined. The other two individuals had contact with the company — they had a transactional interaction with company E — which is why their hard drives were selected to be isolated and forensically examined.

Mr Rogers: In the context of the wider investigation, this happened on this director's watch as well. Would it not have been advisable to examine the hard drives of other people involved?

Ms Venning: The team leading the investigation felt very clearly that nothing pointed towards the director that would have warranted that hard drive to be lifted and searched.

Mr Pengelly: Given that the team was looking at the machines of the level 3 and the contract manager, any direction from the director to either of those two individuals would have been present on the machines. They were being examined because an e-mail or an instruction goes somewhere, so it would have been within the scope. I accept your point; the terms of reference should have been more specific about looking at the directors to the furthest extent possible. I absolutely accept the assurances that I have been given by Sara and the team who were doing the work that, had any evidence emerged, it would have been pursued. However, looking at one side of the situation would have uncovered whether there had been anything in the form of a direction from the director.

Mr Rogers: When you talk about the team, are you referring to your team or the forensic experts that you brought in?

Mr Pengelly: It is the internal team led by the head of internal audit.

Mr Rogers: The internal audit team had limited expertise in forensic audits.

Mr Pengelly: Yes, that is right.

Mr Rogers: Was that a possible weakness?

Mr Pengelly: Its obvious weakness was in interrogating IT, and it secured external expert help for that. Other forensic techniques may have been useful — clearly, I am not a forensic expert — but we are not aware of any obvious gaps when the team could have utilised external skills.

Mr Rogers: Why did the investigation not cover all aspects of that suspected officer's work, his earlier place of employment and so on? Is that down to your team doing this rather than the forensic experts?

Mr Pengelly: No, it is because we were dealing with a specific issue in a well-defined area. If the initial investigation had uncovered actual fraud, we would have taken stock and looked at how we could have investigated other areas. As for investigating previous work, I do not know how you would begin to do that. The nature of the allegation did not point to anything else in his previous work. This was about the splitting of invoices for one company. They were subject to examination. Had that identified anything, the chain of evidence and indicators would have been pursued.

Mr Rogers: The man on the street would say that you did not dig deeply enough.

Mr Pengelly: That goes back to my point: the guidance says that you should consider other work and previous employment. The guidance is to guide and inform. If there was a failure in that circumstance, it was not the consideration of that point. Its legitimate elimination in the early work was not appropriately documented. The evidence when the investigation was initiated contained the phrase "look at earlier periods of employment". Look at what? If it were a middle-aged man, I do not know how far we go back or what we look at. We need a signpost to point us where to go. The preliminary work was to see whether there was any fraud.

Mr Rogers: Is the guidance inadequate?

Mr Pengelly: The guidance is absolutely adequate. However, before we talk about arm's-length bodies, we need to bear in mind that there are 25,000-odd employees in the Civil Service dealing with a massively complex range of different scenarios. The guidance is there to try to help us all through the process; it needs to be used intelligently. If there is a failing, it is not a failing of the guidance; it is the failing in saying that we need to think about this and document the thought process and the conclusion drawn from it.

Mr Rogers: Do DFP guidelines and NI Water's fraud policy not require you to investigate all aspects of that particular person in employment?

Mr Pengelly: No. DFP may have a view, but my view is that they do not require it. It is a piece of guidance that it should be considered, and, where appropriate, pursued. DFP may want to clarify that.

Mr Rogers: In light of the investigation, are there any plans to revisit the guidance to tighten it?

Mr Pengelly: Our guidance and Northern Ireland Water's guidance flows from the DFP guidance. As I said, DFP might want to — Fiona is here — clarify whether, in the light of that, it wants to revisit its guidance.

Ms Fiona Hamill (Treasury Officer of Accounts): In this instance, Mr Pengelly is absolutely right. The guidance is clear: if there are indicators, consideration should be given to investigating an employee in their previous positions. However, it is a "consideration"; it is not a requirement. It has to be a judgement case by case.

Mr Rogers: We have talked about invoice slicing as well. Are there other examples of invoice slicing in Northern Ireland Water?

Ms Venning: Not to our knowledge.

Mr Kieran Donnelly (Comptroller and Auditor General): The guiding principles on handling fraud are in figure 1 of the report. Principle 5 states:

"All aspects of the suspected officer's work should be investigated, not just the area where the fraud (or suspected fraud) was discovered."

That was not challenged when we were clearing the report.

Mr Pengelly: To be clear, I am not challenging it now as a guiding principle. It is not a mandatory requirement for each and every circumstance.

Mr Rogers: Should it not be?

The Chairperson: Should it be made a mandatory requirement?

Mr Pengelly: My personal view is no, but, ultimately, it is DFP's guidance; it might want to consider that.

Ms Venning: It is included in the fraud response plan of NI Water.

Mr Rogers: This is not the first time that NI Water has been before the Public Accounts Committee, and it may not be the last. Could you be back in two years' time with the same story again?

Ms Venning: I do not believe so.

Mr Rogers: Why?

Ms Venning: Because we have taken on board the report and the investigations. I have seen evidence of changes since March 2013 in investigations that have happened. However, I have to bear in mind that people run processes. The responsibility on us is to make sure that people are aware of our plans and the standards to which they should operate. We do that. We have communicated that with people. It is our responsibility to provide them with training, and we do that. I cannot give an absolute guarantee that I can control every action of every individual in an organisation. However, we do all in our power to take the recommendations from reports such as this and incorporate them into our guidance to make sure that the guidance lives in the organisation, because if people are familiar with it and live with it day and daily, when something is invoked in a crisis they are much more likely to say, "I know the plan: on day one, I must escalate this" rather than get caught up in a well-intentioned set of actions that possibly falls outside a plan.

Mr Pengelly: One small indicator, Mr Rogers, is that since the work with the Audit Office on this report, I think that I am right in saying that in every incident of suspected fraud, without exception,

there has been a conversation at an early stage with the PSNI about taking forward the investigation. That is one small indicator of the change in approach.

Mr Rogers: In future, will that "should" become "must"?

Ms Venning: In every aspect of a suspected officer's work?

Mr Rogers: Yes.

Ms Venning: There has to be proportionality and judgement. It is guidance, and we have to balance risk with being thorough. I think that, as it is, the fraud plan is sufficient and allows for terms of reference to start and to widen. It certainly encourages that. A case manager is assigned to each fraud case and is responsible for interrogating, setting the scene and ensuring that adequate people are brought into the investigation and that the investigation is wide enough.

Mr Rogers: With all due respect, that sounds great in theory, but the practice has worked out to be different. You said that there was no evidence of other examples of invoice slicing in NI Water, is that right?

Ms Venning: Yes.

Mr Rogers: Has an investigation been carried out in that area in other departments?

Ms Venning: Other departments outside NI Water?

Mr Rogers: No, in NI Water. You say that this —

Ms Venning: I am not aware of any evidence. Through our annual internal audit plan, we now have contracts that we check routinely. You could say to me, "How can you know?" Through our internal audit plan, we carry out checks on some of our larger contracts and contracts of importance, and none of that work has indicated any invoice slicing. We have a routine programme whereby we look at contracts and rotate that around the variety of contracts that we have, and we have not uncovered any evidence of that.

Mr Rogers: That leads me to another point about the rigour of this. The sample of invoices was just 8% of the total, and a sample of meter installation represented 0.8% of the total number and 3% of the total value of invoice to meter. Are those not very small samples?

Ms Venning: The sample was 8%, which accounted for nearly 15% of the value of money spent under the contract, which was significant, reasonable and proportionate. For that 15% of value in all the invoices that were checked, we were able to link the work back the whole way through to the contract rates.

Mr Rogers: In your previous answer about invoice slicing, you said that you take a sample. I am concerned that if you have such a small sample in this case, there could possibly be other examples of invoice slicing slipping through the net.

Mr Pengelly: That is an issue when you take a sample, but we said earlier that the guidance says, "You must consider the use of appropriate experts." That was in the context of, for example, forensic auditing techniques. The use of sampling is very basic; it is one of the first things that you learn when you start to train as an accountant or auditor. The sample size was determined by someone who was both a fully qualified chartered accountant and a qualified internal auditor, and it was her professional judgement that the sample size was appropriate. She is appropriately and professionally qualified. That is the basis upon which the sample was determined; it was not determined by people at head office plucking a number out of the air. In my experience as an auditor, many years ago, it is not out of line with any sample size that I would have used.

Mr Rogers: You emphasise the bigger percentage, but the sample of meters that was installed was 0.8% of the total.

Ms Venning: The work under that contract involved meter installation and carrying out surveys. Think about carrying out a survey. There is no physical evidence; you cannot physically verify a survey, because a survey is a piece of work that says which property is supplied from where. For the invoices in the sample that had meter installations, a number of the meter installations on each invoice, either five or three, were then selected to be checked further to verify them. We asked to see a picture of the meter as it was installed in the ground; we checked to ensure that the meter reading appeared in the billing system and that matched the photograph of the meter installed in the ground; finally, we checked to see whether we ever saw the meter-read for the meter that was photographed, subsequently in the billing system, and then verified by a meter reader. That is where the 140 meters that were selected came from. They were the installations that you could physically go and look at. You cannot physically see a survey.

Mr Rogers: Was it that eight of those 140 meters could not be located? There was no evidence of site visits to look for them.

Ms Venning: For each of those eight we saw a photograph so that we could see it in situ. The contractor said: "Here is the photograph of this meter as installed in the ground." For each of those eight, we were further able to see that it was recorded and uploaded in the billing system. The final check was for the meter reader to read the meter, and, in those instances, they had not got to it in their reading schedule. NI Water reads meters once every six months, so the team had agreed with management that once the meters had been read, that that information would be fed back. That was the third check in a series of three. The first two checks were deemed to be sufficient to substantiate the existence of the meter.

Mr Rogers: How do you know that it was that particular meter and not some other?

Ms Venning: The meters have unique serial numbers.

Mr Rogers: OK. The team did not interview any suspects or witnesses as part of the investigation, but placed its reliance on the interviews conducted as a part of the disciplinary investigation, which had started before the fraud investigation commenced. Were no interviews of suspects carried out as a part of the fraud investigation? Is that what happened?

Ms Venning: Yes. That goes back to the blurring of the distinction between the disciplinary and the fraud investigation. The same people carried out interviews at the outset in order to establish facts, and, based on those interviews, conclusions were reached and transactional testing occurred. What we have been talking about at this point in the hearing has been the transactional testing that took place. Yes, you are correct.

Mr Rogers: I apologise if this question was asked before: was it done the wrong way round? Should the fraud investigation have happened first?

Ms Venning: Absolutely. The fraud investigation should have come first.

Mr Clarke: I want to ask about some matters supplementary to the questions that Sean has asked. Let us go back to the guidance. I am a bit sceptical, as usual, as to how this has been treated. Sara said that procedures would be put in place, people would be trained and they would live with it day and daily. Yet and all, the person who started the disciplinary process was a director. When you made that statement, I assumed that we were talking about middle management rather than directors. Surely your director should have been living with it day and daily — I am not talking about guidance, but disciplinary procedures. What confidence are you giving us with that bland statement that you are going to bring these people in, basically re-educate them and that they are going to live with it day and daily? Are you for one moment suggesting that they were not familiar with their procedures on a day-and-daily basis up until today?

Ms Venning: No; I am not suggesting that at all. I suppose that I have to go back to the instructions that were given to Liam and the clarification that he received from the chief executive, whereby he was to find out the facts.

We have taken six people from the organisation and put them through training. I have seen, at first hand, the rigour that is now put into our fraud investigations. This document has been used in the organisation, if you like, in check-list format to make sure that we are doing what is in our fraud

response plan and how that meets what is in this document. I know that you need to see the evidence of that, and I suppose that the evidence will be that you do not see me here again. I see the evidence of it working in the organisation.

Mr Clarke: Paragraph 32 of the report states that company E admitted that this came from it since 2008. Sara, what is your definition of invoice slicing?

Ms Venning: Invoice slicing is limiting the value of invoices to below a certain value.

Mr Clarke: In Richard's answer to, I think, Sean, he gave two aspects of what fraud could mean. However, Richard, there was a third one that you left out. When you have an opportunity with an organisation that is in agreement with the contract manager to slice an invoice, you also have the opportunity, which was not touched on, to increase an invoice as a benefit to the person who sliced it in the first instance. Is that not a third aspect of fraud?

Mr Pengelly: I think that it is a third aspect of fraud —

Mr Clarke: You did not touch on that one.

Mr Pengelly: — but my answer was about invoice slicing. Invoice slicing is about chopping a big invoice into smaller pieces; it is not about making a small invoice bigger.

Mr Clarke: It is. The practice should never have started in the first place. Whenever you allow contractors the opportunity to slice invoices, there is also a possibility that, as an inducement to them for doing that, they could benefit on the other end of that invoice.

Mr Pengelly: There is. Absolutely. I would point —

Mr Clarke: The difficulty with the fraud investigation that we are looking at is that, given some of the people who have been involved in it, there is no way of proving categorically whether fraud took place with the invoice slicing or the meters. However, the practice makes you suspicious that fraud could take place.

Mr Pengelly: The only way to prove categorically that no fraud took place would be through a 100% check of all payments. However, a commonly applied audit technique is sampling. From the samples that were selected, there was evidence in all cases that the rate used was the appropriate rate for the contract and that the work charged for had been completed.

Mr Clarke: If you take that to its conclusion, the person who signed off on that is most likely the contract manager, who had entered into the arrangement of invoice slicing in the first place. He could also sign off on work that had not necessarily been done.

Mr Pengelly: There is separate and independent evidence of the work having been done. For the sample selected there was physical verification. We have talked at length about the installation of meters.

Mr Clarke: How was that carried out and by whom?

Mr Pengelly: In this case, it was by physical inspection by a meter reader. In eight cases, that information was not available, because the meter had not been due to be read by the time the audit investigation was done. However, it subsequently became available and was checked. The meter reader was totally separate from this line management chain and this part of the business. Is that correct?

Ms Venning: Yes; that is correct.

Mr Copeland: Returning to what Trevor said, how was that sample, which gave such a magnificent response, selected?

Mr Pengelly: It was the professional judgement of the qualified accountant who headed the audit team.

Ms Venning: She looked at the number of meters on the invoice. Depending on the value, she took a random sample — perhaps three or five — and randomly selected whether to take the first, third, fifth or seventh meter. It was a random selection based on an algorithm.

The Chairperson: I will bring in Mr Dallat in a moment. Who was responsible for designing and approving the process for making and monitoring payments to company E?

Ms Venning: That would have been the members of what was known as the customer service team at the time. When that contract was established, a manager was in place and those processes would have been set up when the contract was initially let.

The Chairperson: Would that have been a line manager?

Ms Venning: It would have been a level-3 manager, so a fairly senior individual in the organisation.

The Chairperson: Sara, in response to Mr Clarke's earlier question, you said that six individuals are being trained. Will they be trained in the expertise and knowledge in fraud investigation for NI Water? Will they be the in-house expertise?

Ms Venning: They are in-house, and they are trained not in fraud investigation in NI Water specifically but in fraud investigation in general. They will be the team that we can draw on if we need fraud investigation officers to carry out a fraud investigation. The case managers will still be able to seek external assistance should it become necessary. For example, we do not possess forensic expertise in examining hard drives and IT, so we could still go outside the company for that. However, we have trained six people in the organisation to gather evidence in accordance with the Police and Criminal Evidence Act (PACE).

The Chairperson: Has NI Water trained them?

Ms Venning: They have been on a Chartered Institute of Public Finance and Accountancy (CIPFA) course. We released them to train.

Mr Pengelly: The training is provided by the Chartered Institute of Public Finance and Accountancy, a respected independent body. That is in NI Water. I think that we have trained eight people in the Department's internal audit unit, but two have subsequently moved on to other posts outside the Department. Therefore, since the time of the report we have trained six people and are building up a cadre of people who understand the legal requirements of a fraud investigation.

Mr Dallat: I was just checking up. Richard, you were before the Public Accounts Committee in July 2010. Is that right?

Mr Pengelly: Can you remember the title of the report? Off the top of my head, I cannot.

Mr Dallat: Sorry, when I said "you", I meant the Department.

Mr Pengelly: Yes, we were here to discuss the governance issues, Mr Dallat.

Mr Dallat: Your Department was here to answer for its stewardship of NI Water. It was not you personally. Who was it?

Mr Pengelly: In July 2010? That would have been Mr Priestley.

Mr Dallat: Paul Priestley?

Mr Pengelly: Yes.

Mr Dallat: Your former chief executive was then exposed as a person who was at least economical with the truth. What happened between July 2010 and January 2011 when he resigned and headed off with a bag of money under his arm? What was your Department doing?

Mr Pengelly: I am not sure —

Mr Dallat: How did you try to control the man?

Mr Pengelly: I am sorry, Mr Dallat, but I cannot be particularly helpful with this, as I was not in the Department at the time. In preparation for today, I focused on the report that is before the Committee.

Mr Dallat: Perhaps we need those who came before the Committee. There is a serious overlap between that.

Paragraph 11 rightly raises concerns about the role of Mr MacKenzie and the audit committee and how it exercised its oversight. Was an audit committee in place at NIW at the time?

Mr Pengelly: Yes, there would have been.

Ms Venning: Yes.

Mr Dallat: Will you please tell us who its chair was?

Mr Fair: Don Price.

Mr Dallat: Does that name mean anything?

Mr Fair: He was a non-executive director at the time.

Mr Dallat: Was he the non-executive director who did not get sacked?

Mr Fair: Yes, that is correct. He was not removed by the Minister.

Mr Dallat: Enough said about that, I think. He signed some kind of document that the other four who were sacked refused to sign to give obedience to Mr Laurence MacKenzie, who got NIW into all the trouble. What was your Department doing about that? Was this a credible person to be the chairperson of an audit committee?

The Chairperson: Sorry, Deputy Chairperson; that relates to the 2010 inquiry and not this inquiry.

Mr Dallat: I am talking about paragraph 11 of this report. I may have been too clever by half by raising it. If it is uncomfortable for the Department, we will go back, but I assure you that there will be another opportunity.

Company E received £1.4 million in survey work over and above the original contract. Who in NIW was involved in that decision?

Mr Pengelly: Would the extension have been agreed at director level?

Ms Venning: Yes. At that time, the extension was signed off in the organisation by the procurement team.

Mr Dallat: I asked who was responsible for it. Is that a reasonable question?

The Chairperson: Yes.

Mr Dallat: Can we hear who was responsible for that? I will tell you why. Since day one, the Assembly has put a lot of emphasis on procurement and the opportunities for small and medium-sized businesses to get government contracts from the work of the Assembly. Company E got £1.4 million from contracts that it did not have to tender for, and we know why: it was slicing invoices. That has now been dressed up as fraud, and we know fine well that it was never fraud. It was practice because you could not be bothered drawing up new contracts. Who was responsible for that £1.4 million?

Mr Pengelly: Chair, I do not mean to be unhelpful, but our preparation work for today has focused on the report on the investigation of a potential fraud. I accept absolutely that the matters about the award and the erroneous extension of contracts are legitimate questions; unfortunately, however, that

was the subject of a previous hearing and was examined. If the Committee wants to put further questions to us, I would need time to prepare.

The Chairperson: Yes, Mr Pengelly, perhaps put that in writing.

Mr Pengelly: Yes, certainly.

Mr Dallat: Chairperson, do I have to scrap that one as well? I have several more here.

Company E charged NIW £111,000 for 12,000 unsuccessful attempts to install meters at new properties. That was a 67% error. Who was the contractor exploiting the lack of controls in that instance?

Ms Venning: The information that was given to the contractor and how they were directed to do their work was flawed to the extent that when they got to sites that were not ready for metering, they had contractual arrangements in place that they could charge for an abortive visit. There were a number of procedural issues with how the work was being issued at that time that resulted in a high level of abortive visits. That was picked up, recognised and dealt with at the time. However, it is absolutely recognised that that is an horrendously high level of abortive visits.

Mr Dallat: I still have not heard who the contractors were.

Ms Venning: The name of company E is Enterprise.

Mr Dallat: Paragraph 49 lists what internal audit calls "significant control weaknesses" that, together, prevented proper monitoring of the contract with company E. Was the contract set up intentionally so that no one could check that the correct payments were being made?

Ms Venning: No, I do not believe that.

Mr Dallat: That is one answer that I can understand. In light of those weaknesses, why was the scope of the investigation not broadened and more time allocated to complete that?

Ms Venning: The weaknesses were highlighted, recognised and passed to management for resolution. In other words, the new contract that was put in place to regularise the expenditure took on board all the weaknesses that were inherent in the old contract and addressed them.

Mr Pengelly: There is a point of clarification about paragraph 49. It is talking about the difficulty of reconciling the totality of charges against the totality of work done in one reconciliation, which is a different issue from an invoice-by-invoice case and it being verified that the work that underpinned the raising of the invoice had been conducted satisfactorily.

Mr Dallat: Chairperson, without wanting to sound a wee bit flippant, you could put this report in the Linen Hall Library, it is so dated. If I have made some mistakes in confusing old with new, you will understand why. Why was there a hold-up in signing off the Audit Office's report, and why is the Public Accounts Committee only now discussing material that happened then?

Mr Pengelly: I am not aware of any delay in signing off on the report.

The Chairperson: This is a relatively recent report.

Mr Dallat: It certainly relates to stuff back in 2009.

The Committee Clerk: Some of these things happened at the same time as the events that the Committee inquired into in 2010, which you were here for, Deputy Chairperson.

Mr Dallat: I suggest that some effort is made to make sure that these reports are more up to date and more relevant to the present time, rather than conducting history lessons.

I have a question for Ms Hamill. Paragraph 45 states that DFP was considering setting up a centralised public sector investigation service; that was in March this year. Did the Department proceed with that?

Ms Hamill: DFP was considering, in relation to the core Departments, developing a centralised internal audit service, which would have brought the fraud services for central Departments together. We made some recommendations to the permanent secretaries group, but the permanent secretaries were of the view that they wished to continue with the governance structures around fraud and internal audit that they have currently. However, I re-emphasise that it was not in relation to a public sector fraud investigation service; it was in relation to internal audit services for central government Departments. It would not have created a fraud service that would, in any way, be intended to have —

Mr Dallat: So, whatever it was, it is not going to happen anyway.

Ms Hamill: No.

Mr Dallat: Wonderful. One of your recommendations is to establish a Northern Ireland public sector fraud investigation service. That seems a plausible plan which, apparently, has the eye of DFP. Would it not be highly desirable that you put your house in order, remove the opportunities for fraud and make people responsible for ensuring that there is zero tolerance towards fraud?

Mr Pengelly: As an organisation, we have a zero tolerance to fraud. That is prevalent in DFP's guidance, our guidance and the guidance at each organisational level. We believe that there is zero tolerance, and we actively promote that. We point our staff towards the relevant guidance, and we do everything in our power to encourage that culture.

Mr Dallat: Are you of the opinion that the current fraud legislation is adequate?

Mr Pengelly: I would not be an expert on the adequacies of legislation.

Mr Dallat: Maybe I will address this question to myself as well: is it not time that we were in the real world?

Mr Pengelly: I am not sure that I follow your question.

Mr Dallat: OK. I am just suggesting that the public sector should follow pace with what happens in the real world outside and not exist in a bubble.

Mr Pengelly: My understanding was that fraud legislation applied to fraud. It does not differentiate between fraud in the public sector and fraud in the private sector.

Mr Dallat: Chairperson, I have nothing else.

The Chairperson: There is no mention of legislation in the inquiry, and that is probably the difficulty.

Mr Clarke: I have not covered this part of the report, because I knew that somebody else was supposed to be looking after it. However, to go back to your response, Sara, with regard to the sampling, the report states:

"although eight of the sample of 140 meters could not be located ... no site visits were undertaken," You were trying to build me up with some confidence that all that work would be done and that you could check that we were getting value for money. According to the report, some of that work was not carried out or could not be carried out.

Mr Pengelly: I am familiar with that, because I had a similar concern. The report is on the conduct of the investigation, as opposed to what underpins it. With regard to the investigation, that is a very valid criticism.

Mr Clarke: There is more than that, Richard. It is clear. The other thing that is clear in the report is the fact that it was not possible to reconcile invoices because centralised records were not maintained. We cannot blame the contractor; we can blame only Northern Ireland Water for that. We have here a case of suspected fraud where invoice-slicing has taken place, but the record-keeping in NI Water was, obviously, substandard as well. I am struggling to find out what has been working properly within guidance rules or anything else, Sara, with regard to NI Water. Can you answer as to what you have done with regard to invoicing since you came into position?

Ms Venning: In this kind of work, the controls in place now are such that we would be able to source the whole way back to the work instruction. Work instructions are issued to the contractor in small, manageable batches and further work is not issued to him until he has satisfied us that he has completed the batch that we have issued, so we have —

Mr Clarke: Why was it not done then?

Ms Venning: A process such as this was not in place then. This was at the start of widespread, wholesale meter installation across Northern Ireland, and I think that the people involved in it learned from the process.

Mr Clarke: Do you think that it is good accounting of public money that the centralising of invoices has not been kept?

Ms Venning: The checking that was done has verified that the question of value regarding public money was answered. The work was carried out under competitively tendered rates —

Mr Clarke: No, sorry; where you have paid a company or companies, there is no record of the invoice. The centralisation of the records were not maintained, so how can you verify that something is giving you value for money if you do not maintain invoices to prove that?

Ms Venning: The invoices are held. The references to central maintenance of records was in relation to how the work instruction was issued, so the work instruction —

Mr Clarke: Paragraph 49 of the report states:

"it was not possible to reconcile invoices to instructions".

Ms Venning: Yes, to instructions. That is because centralised records of instructions were not maintained. Invoices are held and they are all maintained and available centrally.

Mr Clarke: In relation to company E, and I am sure that other contractors work with you, do they all enjoy the same privilege whereby, if they turn up, they get paid for not carrying out the work?

Ms Venning: In the contract, if we instruct —

Mr Clarke: The question about all the other companies that operate with NI Water is whether they enjoy the same privilege as NI Water, whereby, if they turn up to carry out work and the works are not ready, are they paid a fee? A yes or no will be OK.

Ms Venning: If I can clarify for you, if I instruct a contractor to go to a site to fit a meter, if I give him a direct instruction to go to a site and fit a meter and he organises a man and a van and goes to that site and the site is not ready, he is entitled to claim an aborted visit fee. If I have instructed him to go there —

Mr Clarke: I did not actually ask about that; I am sure that you have contractors who do more than install meters. I am asking a specific question about any kind of work for which your company allocates a job to a particular firm. If they turn up to do their job and the site is not ready, do they get a fee?

Ms Venning: All contracts will be different and I cannot speak for every single contractor we have, so —

Mr Clarke: So, this is a privilege for company E.

Ms Venning: In general, the contracts are set up in a way whereby the contractor is paid for the work that they do. We issue them with a work instruction and ask them to do a job of work. In general, that is what we track back to when we are going to authorise their invoice. In this specific instance, for a meter installation, there is an allowance in that contract whereby if we have instructed those contractors to go and fit a meter and the site is not ready, an aborted visit allowance is paid.

Mr Clarke: For this contract, then, who instructed company E to carry out the installation of meters?

Ms Venning: Company E at that time was instructed by what was our outsourced partner. The instructions to company E came from a variety of sources, which comes back to the difficulty around the reconciliation of work instructions. For new connections, that instruction could have come from what was then known as the Crystal Alliance, the company that handled customer contacts. It was instructing the company to go and fit meters. Also, our own NI Water internal team was issuing instructions to go and do work under this contract. Under the current process, the work instruction —

Mr Clarke: Sorry, we will stick with the previous process. Do you think it is reasonable that 12,000 instructions for the installation of meters were not carried out?

Ms Venning: No, I think it absolutely was not reasonable.

Mr Clarke: How did that happen?

Ms Venning: There were poor processes whereby contractors were being sent to sites that were not ready, or where address data was insufficient and they could not find where they were to go and fit the meter. There were also instances in which circumstances were beyond our control; where an installation had been requested, perhaps for a large housing development, but that by the time it had gone through our internal processes, and the guys went out to the site, it had been closed and the contractor had disappeared because of the economic climate. So, a combination of factors contributed to the number. However, the number is much too large.

Mr Clarke: Let me give you an example of the opposite side of this aspect. In my constituency, a community facility received no water bill for five years and then received a disconnection notice. That was because your organisation could not, or did not, follow-up when mail was returned to it. Here you have company E, with 12,000 applications to fit meters, for which it was paid; whereas, we have a hall for community use which received five years worth of bills all at once and then NI Water disconnects it. Is that parity in the conduct of business?

Ms Venning: No. There are certainly processes in place to deal with circumstances such as that, where a large bill is issued, and there are facilities to put in place a repayment plan for customers. I am happy to take away that individual example and look at it. However, we have processes for dealing with situations where a large bill is issued in order to help the customer through that.

Mr Clarke: I know that I digress slightly, but in this instance no such facility was offered. The water supply to the community facility was cut off in summer of this year. There was no postal address for the facility, but NI Water went to the organisation that governed the facility and told it that money was due, but no effort was made to go to the facility until five years had elapsed, and then NI Water decided just to send out engineers to turn the water off. Here we have an organisation suspected of fraud which is paid for 12,000 meters that it did not fit. I definitely think that there is a problem of parity in how you treat people.

Ms Venning: We have processes in place, and I apologise if they have fallen down. I am happy to contact you outside the Committee to discuss the details because I would like to feed the information back into our organisation. We do not want people to be hit with a large bill and then a disconnection. We can work with customers in order to put in place repayment arrangements and we have done so on a number of occasions.

I accept that the number of aborted visits is very high. I must also accept that we have a duty of care to the people we employ and engage. If we give a mis-instruction and they allocate a man, a van and time in going to a site, that has a cost and we should bear the cost. The number of those is far too high.

The Chairperson: Michael, you had a question. Do you want to ask it now before I bring in Mr McKay?

Mr Copeland: I have a number of questions to ask, but I can ask them at my allotted point in proceedings.

Mr McKay: Gary, when did you become aware of the suspected fraud?

Mr Fair: I became aware of the issue during the week of 18 January. As has already been mentioned, emails, written correspondence and a lot of telephone conversations were taking place, as you will understand, given the nature of the events of that week.

Mr McKay: When did you contact the C&AG in regard to it?

Mr Fair: The contact with the C&AG is normally handled by our finance division. We acknowledged that that process failed and held up our hands. We have apologised for that.

Mr McKay: So, you passed the information to the finance division, which was to pass it to the C&AG. Is that right?

Mr Fair: The communication comes from the company, usually directly to the finance division. However, the process was not followed accurately in that case.

Mr McKay: So it was nothing to do with you? It was just DRD and the finance division?

Mr Fair: At the time, I and a senior finance director were being kept informed of what was happening. The wider report and contract approvals had been referred to the Department that week as well. We were kept informed of events.

Mr McKay: Were you aware, or should you have been aware, that it should have been passed on to the C&AG? You were in contact with the finance director.

Mr Fair: I was aware that that was the process. I hold up my hands, for any involvement in my part, that it was missed. It was in the context of an awful lot that was going on at that particular period. However, that does not excuse failure to follow the process.

Mr McKay: What was going on during that time period?

Mr Fair: It was the start of that week — 18 January — that Laurence MacKenzie forwarded the draft internal audit contract's approval report to us. In that context, the invoice-slicing situation was drawn to the Department's attention.

Mr McKay: Richard helpfully pointed out that the shareholder unit was represented in agreeing flawed terms of reference, including the conflict of interest and the failure to communicate the suspected fraud to the C&AG. Will you tell us more about your role in agreeing those terms of reference?

Mr Fair: The terms of reference were shared with the Department and me. I took the view at the time that they seemed broadly reasonable for kicking off the process. It was up to the company and the chief executive of the company at the time to take that forward.

Mr McKay: And you had no concerns about the terms of reference as you saw them?

Mr Fair: I am not necessarily saying that they were perfect, but, at the time, they seemed reasonable to me in order to let an investigation take place as soon as possible.

Mr McKay: Did you have any training in fraud investigations?

Mr Fair: No.

Mr McKay: What was your role as one of the officials who agreed the terms of reference?

Mr Fair: My role at the time was to give a view. It was not necessarily an approval role. Given the nature of all that was going on at the time, the company took some security in getting agreement from other stakeholders.

Mr McKay: You had no concerns about agreeing the terms of reference at that time?

Mr Fair: Not at the time.

Mr McKay: Looking back now, what concerns would you have about the terms of reference, or what is your view of them?

Mr Fair: With the benefit of hindsight, if terms of reference were being shared with me again, I would share them with others in the Department who perhaps have more expertise in that area.

Mr McKay: Were you concerned that others with more expertise were not involved in the process at that time?

Mr Fair: I certainly had assurances from the accounting officer in Northern Ireland Water that the head of internal audit had the appropriate experience, albeit that she was not trained in the Police and Criminal Evidence (Northern Ireland) Order 1989 (PACE) provisions. I would have taken assurance from that. It was ultimately the responsibility of the company to take forward the investigation. It was not a departmental-led investigation.

Mr McKay: Did you have any concerns at that time? A lot of this seems to come from the former chief executive, his actions, and his disregard of certain procedures. Were you alarmed at all during that period by any of his actions?

Mr Fair: Not alarmed. The primary concern from my and the Department's point of view was to be kept informed of what was happening. The chief executive brought things to light at an earlier stage about contract approvals. He initiated the head of internal audit's taking forward the investigations. I think that there was a sense in the Department that we wanted to be supportive of what the company's accounting officer was seeking to do.

Mr McKay: When the terms of reference were being drawn up, was there a series of meetings that led to that, or what was the process?

Mr Fair: There were not meetings; not that I was involved in. There would have been meetings internal to Northern Ireland Water because this was a Northern Ireland Water-led investigation. I was being kept informed and was asked for a view on the terms of reference.

Mr McKay: By e-mail?

Mr Fair: Yes.

Mr McKay: Were you aware of any other views through an e-mail loop or something to that effect?

Mr Fair: Concerns about the terms of reference?

Mr McKay: Yes.

Mr Fair: No.

Mr McKay: Were you aware of any independent advice being sought about that?

Mr Fair: Again, do you mean to the terms of reference?

Mr McKay: Yes.

Mr Fair: I think back to what Richard said earlier: the head of internal audit was a professionally qualified accountant. We took assurance from the accounting officer in Northern Ireland Water that she had sufficient expertise to take that forward.

Mr McKay: Sara, you were just new to the company at that stage.

Ms Venning: I was not in the company at that stage.

Mr McKay: When did you join?

Ms Venning: I joined the company in April 2010.

Mr McKay: On what date did you become involved in the process?

Ms Venning: July 2010.

Mr McKay: At that time, were you aware of any concerns about the process?

Ms Venning: No, not at that time.

Mr McKay: When did you first have concerns about the process? Or, did you have any after that point?

Ms Venning: I think that it was when the internal audit work was being done on how the investigation was conducted. It asked questions of us, and that brought this to light. When I was asked to carry out a disciplinary investigation, my concerns were such that I asked for the charges to be framed, and I took the disciplinary from that point forward. We took the disciplinary from that point and advised, in line with the disciplinary process, but I did not revisit what had gone before.

Mr McKay: Richard, why, in your view, did the senior management team and the head of internal audit not recognise the dangers and advise against the approach of the chief executive?

Mr Pengelly: Very little of this is documented, and we talked earlier about the difficulty in trying to subsequently interpret oral evidence. Subsequent to the chief executive's direction for the interview under the disciplinary process, my sense was that it was challenged sufficiently, because the formal disciplinary process did not reignite until July. The initial interviews were much more part of the fraud investigation process, as they should have been, but they should have been formally brought within that. Unfortunately, I can only speculate, but it suggests to me that there was sufficient push-back from the senior management team to try to take this forward in line with normal policy.

Ms Venning: I think that it was the senior management team that would have brought to the chief executive's attention the need to inform the head of corporate governance and bring this within a fraud response plan.

Mr McKay: Certainly, there is a significant corporate failing throughout all of this, but, in your view, Richard, who is the most culpable, in respect of the timeline that we have in front of us?

Mr Pengelly: I am not sure that I would point to any individual as being culpable. As I said earlier, I am not seeking to make excuses. It was a very difficult time for the company. As Gary mentioned, the other contract approval emerged in the week commencing 18 January. That was a much more substantial piece of work, so, clearly, the chief executive, the senior management team and the head of internal audit were very much focused on that. If anything, I would characterise this as a desire for speed rather than complete quality, and there was a compromise in quality.

Mr McKay: We keep hearing the excuse that things were quite busy at that time and that there were a lot of other pressures, etc, but, at the end of the day, the senior management team and the chief executive of the organisation had responsibility to ensure that things did not get too much for the senior team or the organisation. Somebody, somewhere, has to be culpable for this.

Mr Pengelly: Before I answer that, my question to myself is this: what exactly are we saying they are culpable for? A slightly flawed process? I do not think that this undermines —

Mr McKay: Do you think that this is only slightly flawed?

Mr Pengelly: I think that this is a flawed process; I do not think it is a flawed outcome.

Mr McKay: You said "slightly flawed".

Mr Pengelly: It was a slightly flawed process, but it was headed by a professionally qualified accountant who unearthed no evidence of any fraud.

Mr McKay: Do you accept the seriousness of the process?

Mr Pengelly: I think that the process showed that it was treated seriously. It was not treated in perfect alignment with the guidance. So, I think it was a slightly flawed process; I do not think that it undermined the conclusions reached.

Mr McKay: On page 20 of the report, it is stated that:

"The suspected fraud was reported by NI Water to the Department's Shareholder Unit by mid-January. The Department failed to inform the C&AG of the suspected fraud in accordance with DFP guidance."

How seriously do you take that guidance?

Mr Pengelly: I think that it is serious. It is something that should happen without exception. I do not think that it is a disciplinary offence.

Mr McKay: It was a significant enough failure.

Mr Pengelly: It is a failure, but I think we need to be clear that the failure was a failure to notify the C&AG. It is not a failure that in any way goes to the quality of the fraud investigation, because the C&AG has no role in the fraud investigation.

Mr McKay: It is still a significant failure.

Mr Pengelly: It is absolutely a significant failure.

Mr McQuillan: I have very few questions at this stage, but a couple of things strike me. There have been two massive blunders in this whole thing. The first one was that the DRD failed to inform the C&AG of the fraud to start with. The second one was that they failed to enact the fraud response plan. Sara, you said that you saw a difference since March 2013, and you said that investigations have taken place since that. Can you tell us how many investigations have taken place since the report has been produced and who investigated them?

Ms Venning: I can, but I cannot tell you off the top of my head. I can find that information out for you.

Mr McQuillan: Can you forward that information to us?

Ms Venning: Yes.

Mr McQuillan: The shareholder unit is getting off very lightly. I think that you should have had a much more hands-on approach when this was alerted. Alarm bells should have been ringing throughout the whole process to ensure that everything was followed by the book. I do not think that you did that, and I think that you are getting off very lightly in this whole report. NI Water is taking the brunt of it, but I think that you are as much to blame because you did not take a hands-on approach on the whole thing.

Mr Fair: I will hold my hands up in terms of the process point, and I acknowledge that. My point is that I feel that it is a reflection of the close governance relationship between DRD and Northern Ireland Water that all the issues were brought to light because of the regular meetings that we had with the chief executive. They possibly would not have come to light if it had not been for that. I am not making excuses for the failure in the process — it was a significant point — but that particular week we were dealing with an awful lot, and a lot of telephone conversations took place as well. Sometimes, it is just difficult, and, again, I am not making excuses, but when there is a lot happening at the one time, some things can be missed, and I hold my hands up for that, but there was a close working relationship and governance relationship there, which has since been strengthened.

Mr Pengelly: It is worthwhile clarifying, because this goes on to your next question. We need to bear in mind that Northern Ireland Water was established as a Go-co in April 2007. When the issue arose, the relationship was defined in a governance letter between the Department and Northern Ireland

Water. The position now is that we have a management statement and financial memorandum, which is a much more comprehensive document. That is as a consequence of the Office for National Statistics deciding that because water charges have not been introduced, Northern Ireland Water is much closer to Government, but at the time of the incident, the governance letter specifically says that things like Government Accounting Northern Ireland, which applies to each of us, specifically does not apply to Northern Ireland Water. It was a completely different relationship. There was no obligation whatsoever on Northern Ireland Water to seek departmental approval for the terms of reference. So, the relationship, as defined by the governance letter —

Mr McQuillan: There was no obligation, but it would have been good practice for them to do so.

Mr Pengelly: But, if there is no obligation —

Mr McQuillan: Still, if you want to cover your back, you cover all the bases.

Mr Pengelly: That is exactly right. That is why the relationship that Gary had fostered meant that the terms of reference were shared with the Department and the Department looked at them. I agree with Gary. Looking back at them, I will not stand over them and say that they were perfect, but were they fit for purpose in terms of the investigation that needed to happen in the coming days? I think that they were.

I think that your next question is this: where are we now? There is a much more substantial document in place, which more clearly defines the relationships and the times when the Department needs to be involved. In my tenure in the post, I have had three substantial governance stocktakes with the chief executive and non-executive members of the Northern Ireland Water board, looking through governance issues and issues such as the use of single-tender action in respect of contract awards and reporting of fraud. So, I have come into an organisation that I feel is well managed. It has its finger on the governance issues, and there is a very good and open relationship. There is no sense whatsoever that any issue that the Department needs to know about is not brought to our attention immediately. So, we have moved way beyond the position in 2010.

Mr McQuillan: That is reassuring. Funnily enough, I get that feeling myself. Since the beginning of this year, things have moved on a bit, and I know that it has been alluded to about going back into history, but we do not want to do that.

Just one more thing, Sara, in answer to Sean, you said that the fraud response plan was enacted, but in paragraph 43 of the report it states that the fraud response plan stated:

"consultation with the PSNI at an early stage is beneficial in enabling them to examine the evidence available at the time."

That did not happen at the time. It did not happen at the start, so the plan was not enacted at all.

Ms Venning: You could say that the answer is yes and no. The plan was enacted but that piece of advice in the plan did not happen. I accept that it did not happen. The plan was enacted on 27 January when the head of corporate governance became aware of what has happening, and, in line with the plan, he initiated the initial confidential inquiry form and informed the Department. That is the part of the plan —

Mr McQuillan: It was a very important piece of the plan because it was to bring in the PSNI to investigate, and that did not happen.

Ms Venning: Yes; we accept that. Again, I point to what we have done since we received this report. You have asked for that evidence and you will see it.

Mr Copeland: I will begin with an observation related to something that John Dallat, the Deputy Chair, said earlier. In some respects, I share his view that we are, perhaps, talking to the wrong people. You are giving us, as you must, a historical interpretation of the facts, as opposed to those who were there at the time who could give us their recollections of the facts. That is neither here nor there.

Before I come to my two main questions, my understanding is that this was a generic contract. What does "generic" mean in this context? Was the contract specifically designed to purchase specific

types of goods and services over a specific time frame? Were other types of contract available at the time when this generic contract was offered? Was it unusual? Should another type of contract have been offered, or was the generic contract the appropriate and normal way of doing things?

Ms Venning: The contract was put in place for the installation of water meters. The generic element of the contract also allowed for other associated activities. That is where the survey work came into play. Although the installation of the meters had a defined price for that specific work activity, the survey work happened after the contract was awarded. That was identified as needing to be carried out after the contract was awarded, but it was included within the scope of the contract.

We have learned from that when drawing up subsequent contracts. When you undertake a programme such as this, you think that, because you are going to install water meters, you need a price for that work. As you go through the process, you learn that the first thing you need to do is to carry out a survey to ensure that, where the meter is installed, it supplies only a single property. Subsequent contracts have reflected that learning. We do that with all contracts: we learn through the work activity whether we need to refine the prices for specific work items that we ask for. There were specifics in and around fitting meters, but the carrying out of surveys was additional work.

Mr Copeland: Was the same degree of oversight that was applied at the time when the contract was issued for the types of work covered in the contract applied to the work that was subsequently added to it? Were the mechanisms the same?

Ms Venning: A team was in place that oversaw the work that was instructed through that contract. They had — I have seen them — some very rigorous checklists so that, when the contractor came back detailing the work that he had done, they carried out a series of checks to ensure that the invoice could be paid. That is part of the reason why we go back to the limiting of the invoices. Because of those rigorous checks, in some instances, large invoices were being held up while work on points of verification was carried out. To answer your question, there were a number of points of verification through this contract.

Mr Copeland: That is not what I am driving at; it is how a contract was arrived at that said that X, Y and Z will be done and A, B and C will be paid for doing it. I am talking about the period when the bits that were not covered in the original contract were added to the work programme. Was there the same degree of scrutiny to ensure that the rates set for that work were commensurate with what one would expect? Were they subject to the same degree of oversight and control?

Ms Venning: In any contract that sets a given rate, and you then discover that additional work has to be done, the management practice is to relate any additional costs back to what was in the original contract. In other words, we ask whether the rate for the additional work is commensurate with the rates that were originally submitted in order to deliver value for money.

Mr Copeland: Even though the task might be different?

Ms Venning: You use the same basic principles on which the first set of costs were based to derive any additional costs so that you can demonstrate that you are achieving the same quantum of value.

Mr Copeland: Richard, I think that we accept that the control weaknesses that were identified during the internal audit and the investigation could be seen, with a fair degree of certainty, as indicators of fraud. If that is the case, why were they not treated as such and investigated more deeply?

Mr Pengelly: They were. The initial work, which started in early December 2009, highlighted invoice-slicing, which is an indicator of fraud. That is what led to the initial confidential inquiry and the fraud investigation. The fraud investigation concluded that there was no actual fraud and made a series of recommendations. The concern, from my perspective, is that it pointed to some significant shortcomings in contract management practice, as opposed to a fraud. The balance of the recommendations was heavily skewed towards contract management issues. That is my sense of where the real issue lay, but no evidence at all of fraud was uncovered. There is a separate debate about whether the sample size was sufficient to come to the conclusion that there was no evidence of fraud. My sense, this far out, is to lay that on the professional judgement of the qualified accountant who led the team, and her opinion was that it was a sufficient sample size. It is difficult to second-guess that from my perspective.

Mr Copeland: Paragraph 52 indicates that the audit committee did not follow up on the serious control weaknesses that we have discussed. Why?

Mr Pengelly: I do not know why. Perhaps Sara can speak about the detail. The audit committee did not robustly and systematically follow up on these recommendations. It did not give the suite of recommendations an owner and a target date for implementation. However, the recommendations have all been actioned and implemented, so I take comfort from that. There are new mechanisms in place so that, in future, the audit committee will take ownership of the recommendations from such investigations.

Ms Venning: At the time, the remit of the audit committee was such that it followed up on audit recommendations from investigatory audits where there was a category 1 or a category 2 finding. Those were systematically followed through, and that is what was reported to the audit committee. These ad hoc investigations were not routinely reported to the audit committee, but that has subsequently changed and fraud investigation recommendations are now raised and tracked at the audit committee.

Mr Fair: I started to attend the Northern Ireland Water audit committee meetings as a departmental representative. I think that May 2010 was my first audit committee meeting. An update was given at that meeting, and, at that stage, the committee was told that there was no evidence of wrongdoing. A lot of the discussions in the audit committee at that time ended up driving forward changes in the organisation to improve dissemination and understanding of delegations, and so on, throughout the organisation. Contract management issues were also discussed. Therefore, I do not think that the audit committee was passive during that time.

Mr Copeland: We have already established from previous comments that Richard and Sara consider that no fraud took place, which is very welcome. Can you indicate whether you have total faith that the processes that were in place at the time would have detected fraud if it had taken place?

Mr Pengelly: I cannot answer that question with 100% confidence. If fraud had been prevalent and had manifested itself in either invoices for work that was not done, or inflated charges, the question is whether the sample size would have uncovered that. It depends of the scale. If it were one or two very small invoices among 18,000 meter installations, it is possible that that could have escaped. I think that the sample size was sufficiently representative, and, as Sara mentioned, it was chosen randomly. There was no inherent bias in selecting the sample. If it had been on any material scale, I think that the sample size would have uncovered it.

Mr Copeland: So, in truth, it is an opinion that no fraud took place at this stage.

Mr Pengelly: Yes; absolutely.

Mr Copeland: I suppose that it has to be seen and judged in that context.

Mr Rogers: I want to go back to the issue of the meters. You talked about the rigorous checks. You could not discover eight meters out of that sample of 140. Why was nothing done about that?

Ms Venning: It is not that we could not discover them. For each of those eight meters, a photograph was in place that evidenced it in the ground. It was present on the billing system, but they had not been read at that point. That was not for any untoward reason; the meter reader had simply not got to them yet. The management action was that, once those meters were read, it would be fed back that that had happened. They were subsequently viewed and read by the meter reader.

Mr Rogers: But the report says that they could not be located.

Mr Pengelly: In viewing the report now, I think that, at that stage, a meter reader should have been sent out to look at the eight meters. Subsequent to the closing down of the investigation report, a meter reader, when the natural cycle came around, visited and physically inspected those eight meters. We can be confident now, looking back, that those eight meters existed and were installed. It would have been neater had the investigation taken that to a conclusion by the time the investigation was signed off.

The Chairperson: Mr Pengelly, I understand from paragraph 43 that the claim that DRD had access to DARD's central investigation service was an error because no such arrangements existed. What are DRD's current arrangements for investigating suspected fraud?

Mr Pengelly: There is no formal service-level agreement in place, but we work quite closely with that Department. Deborah is our expert on that.

Ms Deborah McNeilly (Department for Regional Development): We will telephone for informal advice on specific issues that we are dealing with. We also ring colleagues in DSD for informal advice on certain issues. As Richard said earlier, we also have access and are training our staff, and I think that six of them have now completed the training on PACE. Our guidance requires that case manager be appointed to determine who should be on the investigation team. That investigation team may well pool from internal audit and other sources, including HR, and seek technical advice. You mentioned earlier the proposal for a centralised investigation service, and the Department was previously supportive of that. We do not have a service-level agreement with DARD at the moment, but we go to it for informal advice as a second check. We also speak to colleagues in DFP about points of guidance.

The Chairperson: How many cases are currently being investigated by DRD, and by whom?

Ms McNeilly: I do not have that information to hand. I can get that for you.

The Chairperson: Deborah, you came from DFP's financial planning branch, and you are now the finance director in DRD. Since you joined, what concerns have you had about the investigation?

Ms McNeilly: The investigation predated my arrival in the Department. I arrived in, I think, October 2011. Since the report was published, the Department has reviewed its guidance in line with its guiding principles and recommendations. The guidance is now much clearer, and we have process maps for staff. Staff have also undertaken fraud awareness training over the past 12 to 18 months, and we do quite a lot of liaising with the head of internal audit. We have a departmental anti-fraud group that looks at issues of best practice and sharing lessons learned, and that group includes representatives from both the sponsor branches in the Department and from NIW and NITHCo. Therefore, there is high awareness. We might not get everything right. No system is perfect. However, we have taken the lessons and recommendations from the report and made sure that they are reflected in our guidance. That said, after today's session, we will review it again to make sure that we have picked up everything that needs to be picked up

The Chairperson: Following on from that, I have a question for you, Ms Hamill. The Committee's 2008 report on tackling public sector fraud recommended a stocktake across the public sector of trained staff for front line investigation work. What was the outcome of that? When will it be updated? How was that work quality-assured, and what was the position of the implementation of that in 2010?

Ms Hamill: We took away an action to do a stocktake on the levels of training. That was rolled into the work that we undertook in looking at the review of internal audit services and fraud. It became part of that work and part of the headcount for that. That work has been concluded, and the recommendations were shared with the Permanent Secretaries Group.

The Chairperson: Are you concerned that most of DFP's guiding principles were ignored in this case?

Ms Hamill: I do not know that most of them were ignored. They certainly were not followed particularly well. That is disappointing, because our aim is to get our guidance as widely circulated and used as possible. This hearing is another reminder that we need to raise that profile again, recirculate the guidance and bring its importance back to everybody's attention.

Mr Clarke: Richard said earlier — I am paraphrasing — that he would probably have taken guidance fairly lightly, given that it is only guidance. Are you going to reinforce that? I think that Richard said earlier that it was not mandatory. Can you see a possibility of DFP making it mandatory, as opposed to guidance?

Ms Hamill: We will consider what the Committee has to say, but we are always trying to strike a balance between mandatory action, and allowing organisations scope to decide what is appropriate in certain circumstances. At the moment, we are issuing guidance for a wide range of organisations —

multiple bodies across different sectors on different scales and in different situations. Therefore, we want to put in place key principles and key actions that should be taken, such as the sequence for what needs to be put in place and the way in which you need to step through the process. However, we need to leave some flexibility for it to be workable on a case-by-case basis. I am happy to look at the Committee's views and consider whether there are certain aspects that might need to be —

Mr Clarke: I have not been in public for as long as John Dallat. However, in the short time that I have been in it, which is relatively short compared with John, I have learned that, whether it be the Planning Service or other agencies — Richard has been an example of this again today — when a Minister issues guidance, we, as elected Members, are reminded quite often that it is only guidance. There seems to be a policy among civil servants that guidance does not have to apply; they do not necessarily follow it. Given this report, today is an example that, where there is any ambiguity, that should be tightened up and made mandatory. There would then be no ambiguity about how that is interpreted by whatever agency.

Mr Pengelly: I point to the fact that, prior to sitting in this particular seat, some seven months ago I sat in a job in which I spent a greater part of my life berating people for not following my guidance.

Mr Clarke: I was thinking that just a few minutes ago.

Mr Pengelly: The guidance is mandatory in that you must apply the guiding principles. They state that you must initiate a fraud investigation plan and you must follow certain steps. It is an issue when it gets to the seven or eight bullet points about the specific things that must be in it. Some of them could be mandatory, but some will always be best practice. DFP guidance is mandatory; it is a question of how it is applied at a very granular level.

Mr Clarke: That needs to be looked at because of the ambiguity. I am using your example today. From my experience, in the short time in which I have been in public life, of working with planners, Ministers and guidance documents, planners are very quick to tell us that it is "only guidance", when, clearly, the instruction from the Minister, whoever that may be at a particular time, is that the guidance is to direct them in a particular way. People are very quick to waive that and say that that is guidance as opposed to policy.

Mr Pengelly: The main flaw is that, when you go down a particular path, you should think about why you are not applying it and document those reasons. At least it would be on the record and others would be able to critique your decision. Just saying, "It is guidance, and I am deciding not to apply it", is not enough.

Mr Donnelly: There is an important principle regarding guidance about "comply or explain". Richard has touched on that. When guidance is not complied with, there needs to be a written explanation. The difficulty in this case is that there were no written explanations.

The Chairperson: How can the guidance, Ms Hamill, be reinforced in the public sector in the future?

Ms Hamill: It is about communication. The guidance follows good practice and approaches in the wider UK. We need to reinforce it. We also need to look at fraud investigation to see how we can strengthen services and what we, as DFP, can do to strengthen the quality assurance role that we have in the training that people receive. It is always about education.

The Chairperson: Do members have any other questions?

Mr Dallat: Did we mention whistle-blowers? Are policies in place to protect them? Hopefully, the issue will not arise in the new format, but does NIW have a policy on whistle-blowing?

Ms Venning: Yes; we have a whistle-blowing policy.

The Chairperson: I think that we will be dealing with that during our next session.

Mr Copeland: Does that whistle-blowing policy extend to non-contracted agency staff?

Ms Venning: Yes. They would be afforded the same protections if they wanted to raise a whistleblower report.

The Chairperson: Thank you, Richard, and your team. You said at the outset that it was a slightly flawed investigation and that you believed that there was no fraud. It is important to the Committee that public assets are protected. I think that the Committee will take the view that, if that is not the case, there should be serious consequences. I reiterate that the Committee will now consider the evidence that has been put before us today by you and your staff. We may well want to write to you for further information. Thank you and your team for your time.