

# Fraud risk management

## Oil and gas sector



**EY**

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# Contents

<b>Why should you be concerned about fraud risks?</b>	<b>1</b>
<b>Key risks in the oil and gas sector</b>	<b>2</b>
<b>Five key factors your business should consider to mitigate fraud risks</b>	<b>3</b>
<b>Benefits to your organisation</b>	<b>4</b>
<b>What can EY do to help?</b>	<b>4</b>
<b>What you can expect from us</b>	<b>5</b>
<b>Our experience</b>	<b>5</b>
<b>Contacts</b>	<b>6</b>

# Are you doing enough?

Ask yourself the following questions ...

What are our  
specific fraud  
risks?

Who really  
owns them?

How are we  
effectively  
managing  
them?

Can we  
actually  
demonstrate  
that?

# Why should you be concerned about fraud risks?

Fraud is a persistent and significant problem faced by all companies and organisations, and the oil and gas sector is no exception.

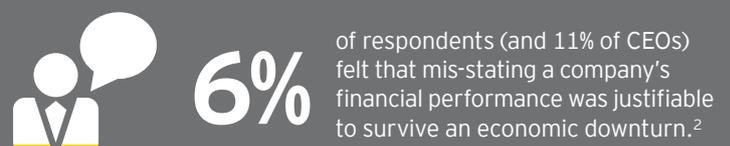
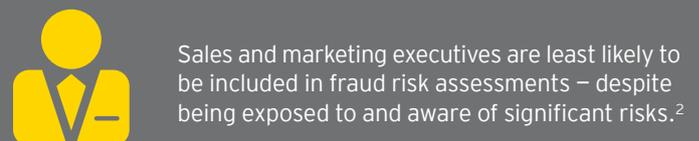
The scarcity of natural resources in more established markets is leading oil and gas companies to explore new markets for new reserves. In countries where the government may wholly or partially own the sector, it is often necessary for oil and gas companies to engage government officials, which is frequently done through well connected intermediaries. Oil and gas companies may contract with National Oil Companies and form joint ventures ('JV') where JV partners may appoint government officials to sit on the board of directors. Oil and gas companies also frequently hire third parties, such as Engineering, Procurement and Construction Management ('EPCM') firms, to manage their in-country operations. These characteristics expose oil and gas companies and providers to increased levels of fraud, bribery and corruption.

A drop in oil prices severely impacts the sector, as oil and gas companies face significant spending cuts and continuous pressure to continue delivering desired levels of production. This issue is cascaded down to the oilfield service providers. This added pressure creates an imbalance between compliance and business operations and potentially induces activities which are not aligned with corporate policies.

The Association of Certified Fraud Examiner's ('ACFE') 2014 'Report to the Nations' states that 3.6% of fraud cases reported to them are in the oil and gas industry. Of these cases 57.1% relate to corruption schemes. However, with increased pressure for both majors and oilfield service providers, new risks are constantly emerging and the matters that regulators and the public consider inappropriate or fraudulent are evolving. Examples of these emerging risks are cybercrime and fraud risks associated with poor information governance and detection mechanisms.

Increasingly, regulators, board members, audit committee members, independent auditors, investors and other stakeholders are seeking better information from executive management as to how they are preventing, detecting and responding to fraud risk.

If businesses lack a consistent, well thought-out and coordinated program that demonstrates an understanding of key fraud risks and their potential impact they are at risk of value leakage. An effective plan to mitigate and monitor risk is key.



<sup>1</sup> Source: Report to the Nations on Occupational Fraud and Abuse, ACFE, 2014.

<sup>2</sup> Source: EY Global Fraud Survey, 2014.

# Key risks in the oil & gas sector

	Up-stream	Mid-stream	Down-stream		
<b>Exploration</b>	Obtaining exploration licences	<b>Transport</b>	<b>Refining, processing</b>		
	Unrealistic assumptions and improper assessment of projected returns on investment			Theft of inventory	Misrepresenting the quality of product being refined and processed
	Inappropriate calculation of royalty payments due to unclear requirements				
<b>Production</b>	Obtaining and retaining production licences	<b>Storage</b>	<b>Marketing and distribution</b>		
	Large scale expenditure and construction of production facilities			Theft of inventory	Improper pricing, market allocation, or bid rigging
	Use of EPCM companies to manage construction and/or operations of production facilities				
	Manipulation of expenditure of fly-in, fly-out workforce				Misrepresentation of inventory valuations as a result of fluctuating commodity prices and exchange rates and the need to reconcile production, shipping and sales volumes
	Manipulation of production cut-off amounts to meet performance targets				
	Creative compliance with environmental regulations by manipulating vague reclamation and rehabilitation provisions				

## Business operations

<b>Operation locations</b>	Remote location of operations provides less oversight and control, and potential to by-pass controls
<b>Cultural considerations</b>	Managing cultural differences and attitudes towards control environments
<b>IT</b>	Intellectual property theft, network breaches
<b>Information governance</b>	Poorly structured systems to manage information
<b>Procurement</b>	Ambiguous tender scope, irregularities in the tender evaluation and/or award, poor contract management (including being invoiced for greater number of hours than actually worked, higher labour rates than in contract, incorrect equipment/materials, incorrect services, improper third party costs)
<b>Accounts payable</b>	Lack of third party due diligence, limited choice of vendors and use of non-approved vendors
<b>Payroll, expense claims</b>	Lack of employee background checks prior to on-boarding, potential ghost employees, insufficient information captured as part of the expense reimbursement claim process
<b>Accounting</b>	Misstatement of depreciation as a result of the manipulation of the market resale value, useful life and permitted depreciation methods. Incorrect capitalisation of expenses associated with expanding and improving existing sites and undertaking new site developments
<b>Market disclosure and reporting</b>	Intentional misstatement of reserve valuations as a result of manipulation of engineering reports, recovery rates, declining production profiles and/or price fluctuations

# Five key factors your business should consider to mitigate fraud risks



# Benefits to your organisation

An anti-fraud programme will help executive management to address fraud risk by assessing each element of the company’s anti-fraud defences, identifying opportunities for improvement, providing a process for implementing the improvements, and helping management understand how to monitor the effectiveness of the programme going forward.

We believe that a robust anti-fraud programme will:

- ▶ **Help prevent fraud and avoid the related costs**
- ▶ **Facilitate early detection of fraud events to help mitigate the effects**
- ▶ **Augment the business brand**
- ▶ **Limit fraud events that affect reputation, credibility, and share price**
- ▶ **Increase confidence of major stakeholders**
- ▶ **Reduce the risk of non-compliance with laws and regulations and protect the business from regulatory authorities**

# What can EY do to help?

## Our approach

We have developed an approach to fraud risk management that can be tailored to suit particular client needs, be that a broad-based review or addressing particular concerns. This approach is summarised in the illustration below and addresses the three main objectives of robust fraud risk management: Prevent, Detect and Respond.



# What you can expect from us

- ▶ **An independent and objective assessment of your anti-fraud programme's strengths and weaknesses**
- ▶ **Sector-specific insights to the fraud risks affecting your business through our work with other clients in the oil and gas industry**
- ▶ **Practical recommendations on what could be done to help strengthen and improve your anti-fraud programme**
- ▶ **Findings presented in a format which will facilitate the consideration of fraud risk and the related mitigating controls**
- ▶ **Experienced professionals from forensic accounting, forensic IT (including data analytics) and compliance backgrounds, who will work with you to help you improve your organisation's anti-fraud capabilities.**
- ▶ **A consistent approach from our global network of professionals supported by 15 Global Oil & Gas Centres.**

## Our experience

### Global oil and gas company

EY performed an anti-fraud assessment for a Global oil and gas company to create an effective fraud risk programme comprising of risk assessments (via stakeholder meetings and workshops), control evaluation and training. Following the stakeholder meetings and workshops we were able to determine the fraud risk profile and identify gaps in the control environment. We also developed a client branded training pack to be delivered internally to help raise fraud awareness.

### Energy provider

EY undertook an assessment of the existing anti-fraud activities of a major energy provider and conducted a fraud risk assessment across the business. We developed an anti-fraud programme, including a comprehensive fraud response plan, which enhanced existing anti-fraud activities, leveraging existing processes and procedures without overloading personnel with onerous requirements.

The anti-fraud programme provided a framework to support future enhancements of anti-fraud risk management within the business. The business was able to demonstrate to key stakeholders an increased focus on, and proactive approach to, fraud risk management and supported the Board in providing an appropriate 'tone from the top'.

### National oil company

EY assisted a national oil company with an anti-fraud programme relating to procurement fraud risk. The client had assets and investments in various African countries. We provided ongoing defined scope due diligence procedures for all procurement matters >\$ 150,000 as a means of reducing the risk of procurement fraud and compliance risks.

### Global oil and gas company

Working with management of an Australian subsidiary of a global oil and gas company, we performed an assessment of its internal control environment. We conducted interviews with the relevant people across various levels in the company, including the CEO and other C-suite members to understand the company's appetite for and attitude towards fraud risk management. The areas covered in this project included Community Affairs, Procurement and Accounts Payable, Asset and Land Management Finance.

The company was able to better understand the key fraud risks in their organisation and gaps in the control environment from a fraud perspective. Our observations assisted the company in aligning their efforts with the guidance provided by the Australian Standard 8001:2008.

### Global oil and gas company

Following a very significant fraud, a global oil and gas company located in the United States required assistance with their fraud risk management programme to enable it to better determine what types of fraud exposure the company had in the areas of fraudulent statements, corruption and misappropriation of assets schemes.

Through the use of surveys, interviews and facilitated sessions of selected employees throughout the Company, we identified the most relevant fraud risks, gathered the participants perspectives on the control environment and their thoughts on the likelihood and impact of each risk identified.

Our assessment helped the Company work to change the 'Tone at the Top' and 'Culture' with respect to how fraud risk management is perceived in the Company.

# Contacts

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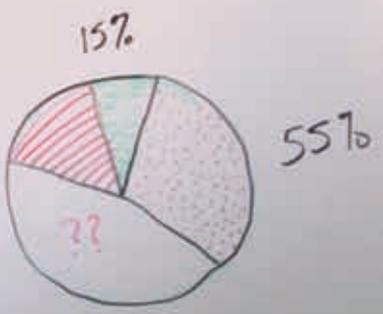
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Goals → Overseas production = 50%

15% of Market  
Goal for  
New Year 70%



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SPACE







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#### About EY's Fraud Investigation & Dispute Services

Dealing with complex issues of fraud, regulatory compliance and business disputes can detract from efforts to succeed. Better management of fraud risk and compliance exposure is a critical business priority – no matter what the industry sector is. With our more than 3,000 fraud investigation and dispute professionals around the world, we assemble the right multidisciplinary and culturally aligned team to work with you and your legal advisors. We work to give you the benefit of our broad sector experience, our deep subject matter knowledge and the latest insights from our work worldwide.

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