Contract and Procurement Fraud

Fraud in Procurement Without Competition
Sole-Source Awards

- The procurement process is noncompetitive through the solicitation of only one source.
- Procurement through sole-source contracting provides more opportunities for fraud and therefore requires justification and a higher level of approval.
Sole-Source Awards

Examples of exceptions to justify sole-source contracting include:

- Only one responsible source, and no other supplies or services satisfy requirements
- Unusual and compelling urgency
- Industrial mobilization; engineering, developmental, or research capability; or expert services
- International agreement
- Authorized or required by statute
- National security
- Public interest
Red Flags of Unjustified Sole-Source Awards

- Complaints by competing contractors
- Frequent use of sole-source contracts
- High number of sole-source awards to one supplier
- Requests for sole-source procurements when a pool of contractors is available
Red Flags of Unjustified Sole-Source Awards

- Sole-source procurement justification involves:
  - False statements
  - Approval by employees without authority
- Failure to obtain the required review for sole-source justifications
- Restrictions included in solicitation documents that restrict competition
Detecting Unjustified Sole-Source Awards

- Determine whether two or more similar or identical items were purchased:
  - In different quantities within short periods
  - From the same contractor in amounts just above or just below review or competitive bidding limits

- Determine whether the sole-source awards were proper under the applicable policies and procedures.
Detecting Unjustified Sole-Source Awards

- Search for a pattern of sole-source procurements:
  - Sole-source awards when there is an available pool of vendors to compete
  - Sole-source awards just below upper-level review or competitive bidding limits
  - Sole-source awards followed by a change order increasing scope/cost
Purchases for Personal Use

- Employees with purchasing authority might exploit their position to obtain items for their personal use or resale.
Preventing Purchases for Personal Use

- Policy prohibiting use of company funds to make personal purchases
- Policy requiring an after-the-fact review of small purchases to validate their reasonableness
- Segregating duties of originating purchases and approving them
- Establishing maximum purchasing limits for each employee
- Routinely checking for goods delivered to external addresses
Red Flags of Purchases for Personal Use

- Unusual or unexplained high volume of purchases of products or services suitable for personal use or resale
- Consumer items purchased and then replaced in a relatively short amount of time
- High number of purchases from vendors that sell consumer products
- Items suitable for personal use or resale missing from inventory or unaccounted for
Red Flags of Purchases for Personal Use

- Purchased items are unnecessary or unrelated to the entity’s needs.
- Purchased items are returned to a vendor without vendor credit or refund.
- A suspect employee operates an outside business.
Detecting Purchases for Personal Use

- Search for questionable purchases of items suitable for personal use or resale.
- Identify unexplained or unusual increases in the purchase of certain goods or services.
- Examine reasonability of amounts, types, and timing of purchases:
  - By purchasing employee or unit
  - In comparison with previous purchases or industry averages
Detecting Purchases for Personal Use

- Identify purchases that are unrelated to or inappropriate for the purchasing organization.
- Compare purchase volumes to appropriate inventory levels.
- Check whether suspect items can be accounted for in inventory or usage records.
Detecting Purchases for Personal Use

- Review returns of suspect items to confirm that the vendor issued credit or a refund.
- Conduct background and asset checks of suspect employees to determine if any have an outside business or live beyond their means.
- Examine shipment-receiving reports for merchandise ordered and paid for but not delivered.
Bid Splitting

- Employee splitting large contracts into smaller contracts to avoid the scrutiny required for larger contracts
- Might be used to avoid competitive bidding
Preventing Bid Splitting

- Review purchase orders, grouped by employee, to identify:
  - Identical items purchased in different amounts simultaneously or within short periods
  - Contract split by type of work (e.g., one purchase order for labor and another for material)
  - Recurring requirements that fall just under review, authorization, or competitive bid thresholds
Red Flags of Bid Splitting

- Purchases that fall just under review or competitive bidding limits and are:
  - Similar or identical purchases from the same supplier
  - Consecutive related purchases from the same contractor
  - Unjustified split purchases
  - Sequential purchases, particularly those that are followed by change orders
Detecting Bid Splitting

- Group payments by vendor and manually check invoices for split purchases.
- Identify multiple payments in the same or similar amounts.
- Examine purchases lacking invoices or purchase orders.
Detecting Bid Splitting

▪ Perform a background check on the contractor to determine whether companies that received awards for similar work are affiliated or have common ownership.
▪ Determine whether checks for different vendors are mailed to the same address.
▪ Examine endorsements on vendor checks where bid splitting is suspected.
Purchasing Card (P-Card) Schemes

- Making personal purchases
- Purchasing gift cards for personal use
- Using p-cards to split purchases
- Purchasing items for resale
- Paying kickbacks
- Making payments to employee’s own shell company
Preventing P-Card Schemes

- Perform background checks on all p-card holders.
- Implement and regularly update p-card policies and procedures:
  - What cardholders can and cannot purchase
  - Disciplinary action for p-card abuse
Preventing P-Card Schemes

- Impose a cardholder agreement that must be signed by every cardholder and supervisor.
- Impose reasonable monetary limits on p-card purchases.
- Appoint a permanent administrator who is responsible for and has authority over the p-card program.
Preventing P-Card Schemes

- Use merchant classification codes to prohibit transactions at certain establishments.
- Require supervisors to conduct monthly reviews.
- Implement a purchase approval process.
- Require original receipts for every p-card purchase.
- Use a p-card design that reduces the likelihood that cardholders accidentally use their p-cards for personal purchases.
Red Flags of P-Card Schemes

- Monthly reconciliations are always late or not performed.
- Receipts are missing from the reconciliation.
- Employee submits several reconciliations at one time.
- Employee tries to rush the reconciliation process.
Detecting P-Card Abuse

▪ Reconcile transactions, explanations for purchases, and receipts of purchases in a timely manner.
▪ Implement a hotline that allows employees to report suspected p-card abuse.
▪ Use software monitoring to identify questionable p-card transactions.
▪ Require p-card service providers to provide cumulative p-card data, and mine and analyze the data for known fraud risk factors.
Petty Cash Abuse

- False requests for reimbursement of expenses
- Altered receipts/vouchers for cash fund reimbursement
- Personal or unauthorized expenditures
- Duplicate payments
Preventing Petty Cash Abuse

- Segregation of duties
- Mandatory job rotation
- Surprise cash counts and supervisory observations
- Periodic reconciliation of cash and vouchers
Preventing Petty Cash Abuse

- Vouchers should be pre-numbered and properly accounted for.
- The custodian should only accept original documentation.
- Cash funds should be kept in a locked, limited-access safe or vault.
Preventing Petty Cash Abuse

- Set dollar limits for purchases, and make sure the custodian observes them.
- Set clear rules on what can be reimbursed.
- Cash fund transactions should be periodically reviewed to identify payments for identical items, quantities, and amounts.
- Cash fund policies should be distributed to employees.
Red Flags of Petty Cash Abuse

- Dramatic increase in expenses charged to petty cash
- Physical alterations on support documents
- Charges to petty cash without proper documentation or approval
- Unusually large petty cash balance
- Cash fund voucher records that do not match issuing office records
Red Flags of Petty Cash Abuse

- Use of petty cash accounts for unauthorized purposes, loans, or amounts
- Vouchers not accompanied by original documentation
- Unusually large quantities of a single item purchased over a short period
- Inadequate, altered, copied, or missing supporting documents
Detecting Petty Cash Abuse

- Review the date and other entries on relevant documents.
- Prepare and analyze an inventory of all funds by purpose, amount, custodian, date, and location.
- Periodically review petty cash vouchers and receipts to ensure that proper procedures are being followed.
Detecting Petty Cash Abuse

- Review the petty cash funds to identify:
  - Marketing, travel, entertainment, gifts, political contributions, or lobbying expenses and donations that are not adequately explained and supported
  - Payments to agents not already reviewed
  - Payments to decision-makers in the government entities