

Fraud indicators (or red flags)

All people involved in and project implementation may see potential signs of fraudulent activity and are obliged to take appropriate steps in response. **Critical thinking** is a desirable quality in this respect, especially on the part of the people who perform control tasks.

In order to enhance above-mentioned critical thinking and to facilitate the detection of fraud, the Managing Authority prepared the list of the most important fraud indicators, which can be used for identification of fraudulent behaviour. If any red flags emerge during Programme implementation, immediate response is required to verify whether further actions are required.

The list is divided into 2 parts: **public procurement** and **labour charges and consultancy services**. It is connected with European Commission Guidance *Fraud Risk Assessment and Effective and Proportionate Anti-Fraud Measures* where it is indicated that 2 above-mentioned fields are especially exposed to potential fraudulent behaviour. Each part is divided into types of possible fraud, which has their own fraud indicators.

The list of fraud, which is non-exhaustive and can be **extended** by adding new indicators, which might appear during Programme implementation, e.g. types of detected fraud within the Programme, which are currently not listed.

Public procurement:

1. CORRUPTION – BRIBES AND KICKBACKS

- unexplained favourable treatment of a contractor by a contracting employee over a period of time,
- close socialisation between a contracting employee and service or product provider,
- unexplained or sudden increase in wealth by the contracting employee,
- contracting employee has an undisclosed outside business,
- contractor has a reputation in the industry for paying kickbacks,

- undocumented or frequent changes to contracts increasing the value of the contract,
- contracting employee declines promotion to a non-procurement position,
- contracting employee fails to file or complete conflict of interest declaration;

2. UNDISCLOSED CONFLICT OF INTEREST

- unexplained or unusual favouritism of a particular contractor or seller,
- continued acceptance of high priced, low quality work etc,
- contracting employee fails to file or complete conflict of interest declaration,
- contracting employee declines promotion to a non-procurement position,
- contracting employee appears to conduct side business.

3. COLLUSIVE BIDDING

- winning bid is too high compared to cost estimates, published price lists, similar works or services or industry averages and fair market prices,
- persistent high prices by all bidders,
- bid prices drop when new bidder enters the competition,
- rotation of winning bidders by region, job, type of work,
- losing bidders hired as subcontractors,
- unusual bid patterns (e.g. the bids are exact percentage apart, winning bid just under threshold of acceptable prices, exactly at budget price, too high, too close, too far apart, round numbers, incomplete, etc),
- apparent connections between bidders, e.g. common addresses, personnel, phone numbers etc,
- contractor includes subcontractors in its bid which are competing for the main contract,
- qualified contractors fail to bid and become subcontractors or low bidder withdraws and becomes a subcontractor,
- certain companies always bid against each other, others never do;

- losing bidders cannot be located in the Internet, business directories, have no address etc (in other words they are fictive),
- correspondence or other indications that contractors exchange pricing information, divide territories, or otherwise enter informal agreements,
- collusive bidding has been found in the following sectors and is also relevant for structural funds: asphalt paving, building construction, dredging, electrical equipment, roofing, waste disposal.

4. UNBALANCED BIDDING

- particular line item bids appear to be unreasonably low,
- changes are issued soon after contract awards to delete or modify line item requirements,
- line items for bids are different than the actual contract,
- bidder close to procurement personnel or participated in drafting specifications.

5. RIGGED SPECIFICATIONS

- only one or a few bidders respond to request for bids,
- similarity between specifications and winning contractor's product or services,
- complaints from other bidders,
- specifications are significantly narrower or broader than similar previous requests for bids,
- unusual or unreasonable specifications,
- high number of competitive awards to one supplier,
- socialisation or personal contacts between contracting personnel and bidders during the bidding process,
- the buyer defines an item using brand name rather than generic description.

6. LEAKING BIG DATA

- poor controls on bidding procedures, e.g. failure to enforce deadlines,

- winning bid just under the next lowest bid,
- some bids opened early,
- acceptance of late bids,
- late bidder is the winning low bidder,
- all bids are rejected and contract is re-bid,
- winning bidder communicates privately with contracting personnel by e-mail or otherwise during bidding period;

7. MANIPULATION OF BIDS

- complaints from bidders,
- poor controls and inadequate bidding procedures,
- indications of changes to bids after reception,
- bids voided for errors,
- a qualified bidder disqualified for questionable reasons,
- job not re-bid even though fewer than the minimum number of bids were received.

8. UNJUSTIFIED SINGLE SOURCE AWARDS

- single source awards above or just below competitive bidding thresholds,
- previously competitive procurements become non-competitive,
- split purchases to avoid competitive bidding threshold,
- request for bid mailed only to one service provider;

9. SPLIT PURCHASES

- two or more consecutive, related procurements from the same contractor just under competitive bidding or upper level review thresholds,
- unjustified separation of purchases, e.g. separate contracts for labour and materials, each of which is below bidding thresholds,
- sequential purchases just under the thresholds.

10.CO-MINGLING OF CONTRACTS

- similar invoices presented under different jobs or contracts,
- the contractor invoices for more than one job for the same time period;

11.COST MISCARGING

- excessive or unusual labour charges,
- labour charges inconsistent with contract progress,
- apparent changes to time sheets,
- time sheets cannot be found,
- the same material costs charged to more than one contract,
- charging indirect costs as direct costs.

12.DEFECTIVE PRICING

- contractor refuses, delays or is unable to provide supporting documents for costs,
- contractor provides inadequate or incomplete documentation,
- out-of-date pricing information,
- apparent high prices compared to similar contracts, price lists or industry averages.

13.FAILURE TO MEET CONTRACT SPECIFICATIONS

- discrepancy between test and inspection results and contract claims and specifications,
- absence of test or inspection document or certificates,
- low quality, poor performance and high number of complaints,
- indications from the contractor's expense records that the contractor did not e.g. purchase materials necessary for the works, does not own or did not lease equipment,

- necessary for the work or did have the necessary labour on the site (NB: this type of cross-checking can be valuable).

14.FALSE, INFLATED OR DUPLICATE INVOICES

- invoiced goods or services cannot be located in inventory or accounted for,
- no acknowledgment of receipt for invoiced goods or services,
- questionable or no purchase order for invoiced goods or services,
- contractor's records do not reflect that the work was done or that the necessary costs were incurred,
- invoice prices, amounts, item descriptions or terms exceed or do not match contract items, purchase order, receiving records, inventory or usage records,
- multiple invoices with the same amount, invoice number, date etc,
- sub-contracts in cascade,
- cash payments,
- payments to off-shore companies.

15.PHANTOM SERVICE PROVIDERS

- service provider can not be found in any directories, the Internet, Google and other search engines etc,
- service providers address can not be found,
- the service provider lists incorrect street address or phone number,
- off-shore company used.

16.PRODUCT SUBSTITUTION

- unusual or generic packaging: packaging, colours or design different than the norm,
- discrepancy between expected appearance and actual appearance,
- product identification numbers differ from published or catalogue numbers or numbering system,

- above average number of test or operation failures, early replacements, or high maintenance or repair costs,
- compliance certificates signed by unqualified or non-certified person,
- significant difference between estimated and actual costs for materials,
- contactor is behind schedule but quickly catches up,
- unusual or obliterated serial numbers; serial numbers are not consistent with legitimate manufacturer's numbering system,
- invoice or inventory item numbers or descriptions do not match purchase order terms.

Labour charges and consultancy services fraud:

1. INCURRED LABOUR COST

- distinctive charging patterns,
- sudden, significant shifts in charging,
- decrease in charges to projects/contracts in overrun or near ceilings,
- a disproportionate percentage of employees charging indirect,
- large number of employees reclassified from direct to indirect or vice versa,
- same employees constantly reclassified from direct to indirect or vice versa,
- weak internal controls over labour charging, such as employee time cards signed in advance, employee time cards filled in by the supervisor, time cards filled in with pencil or time cards filled in at the end of the pay period,
- actual hours and euros consistently at or near budgeted amounts,
- use of adjusting journal entries to shift costs between contracts, R&D, commercial work,
- significant increases or decreases in charging to sensitive accounts,
- employee's time charged differently than associated travel costs.

2. UNCOMPENSATED OVERTIME

- professional staff required to work a significant amount of unpaid overtime on a variety of projects-both direct and indirect,
- salaried employees only charging the regular hours worked during any day for an extended period,
- a pattern of management directed unpaid overtime with employee bonus based on the extra hours worked,
- overrun contracts/projects worked on only during unpaid hours.

3. CONSULTING/PROFESSIONAL SERVICE

- no formal signed agreements or contracts; however, large sums paid for "services rendered" based on invoices with few specifics,
- formal agreements or contracts exist but are vague as to services to be rendered, and no other documented support, such as detailed invoices, trip reports or studies, exists to justify the expenses,
- services paid for were used to improperly obtain, distribute or use information or data protected by law or regulation,
- services paid for were intended to improperly influence the content of a solicitation, the evaluation of a proposal or quotation, the selection of sources for contract award or the negotiation of a contract, modification or claim. It does not matter whether the award is by the prime contractor or any tier subcontractor,
- services paid for were obtained or performed in some way that violated a statute or regulation prohibiting improper business practices or conflict of interest.

4. LABOUR CATEGORIES

- significant differences between proposed and actual unit costs or quantities with no corresponding changes in work scope or job requirements,

- task-by-task invoicing consistently at the ceiling level established in the contract. An exception would be if the contract/work order specifies how many hours to bill,
- specific individuals proposed as "key employees" not working on the contract,
- proposed labour not based on existing work force,
- massive new hires needed,
- new hire labour rates significantly lower than proposed,
- employees' skills do not match the skill requirements as specified for their labour category or the contract requirements,
- employees typically charged indirect by the company being charged direct to the contract,
- partners', officers', supervisors' and other employees' time being charged in noncompliance with the contract terms or with the company's established accounting policies and procedures.