

*POSSIBLE GRANT FRAUD
INDICATORS*

NSF-OIG HANDBOOK

INTRODUCTION

Fraud is often difficult to detect and is a conclusion that is determined only after a careful examination of all the facts and circumstances. It is best understood as a general term that encompasses a wide range of behavior, including such acts as deception, bribery, forgery, extortion, theft, conspiracy, embezzlement, misappropriation, false representations, false statements, concealment of material facts, and collusion. Under federal law, such acts are proscribed by a variety of statutes, including 18 U.S.C. §1001 governing false statements or representations; 18 U.S.C. §287 governing false claims; 18 U.S.C. §§201-208 governing bribery, gratuities and conflicts of interest; 18 U.S.C. §641 governing theft, embezzlement and destruction of public money, property or records; 18 U.S.C. §666 governing theft and bribery concerning programs receiving federal funds; and 18 U.S.C. §1341 and 18 U.S.C. §1343 governing mail and wire fraud.

Fraudulent schemes are as varied and unique as the individual perpetrators, their motives, and the situations they seek to exploit. Some examples of possible fraudulent activity might include the misappropriation of NSF funds for personal purposes, commingling NSF grant funds with other funds, and submitting false or altered documents when requesting reimbursement from NSF.

The *first step* in detecting fraud is to identify the presence of certain facts and conditions that may be indicators of fraud. This *Handbook* contains a compilation of possible indicators of fraud drawn from a wide variety of sources, including the Yellow Book, the Association of Independent Certified Public Accountants, other Inspector General offices, statutes, actual cases and the collective experience and wisdom of our office. This *Handbook* is organized in three parts reflecting the analytical underpinnings necessary to understand and detect fraud: *Motive, Opportunity and Method*. Under each part, there is a definition of the category and a list of several possible indicators that fall under it.

The critical notion to keep in mind when using the *Handbook* is it deals only with *possible* indicators, or, in other words, particular facts and conditions which may, under certain circumstances, be indicators of fraud. It is also possible that they may *not* be indicators of fraud in the particular situation in which they are found. Further, given the inventiveness of wrongdoers, it is safe to say these are not the only indicators one might encounter. Thus, please view this *Handbook* as a starting point for thinking about fraud and use it as a guide rather than as a definitive list.

PART A - POSSIBLE MOTIVES FOR FRAUD

People commit fraud for a variety of reasons. A motive might be personal and direct (as in the case of someone using a company car for personal purposes like a beach vacation) or organizational and indirect (a faltering project is made to look more successful than it is, enabling the staff to keep their job or gain status in their peer group). Some possible motives for fraud are easier to identify than others and some may be discovered inadvertently, such as by observing someone's expensive lifestyle. While it is always possible a particular motive will remain hidden, it is nonetheless useful to be aware of some of the more common reasons that people commit fraud.

1. Possible Personal Motives

- 1.1.*** Personnel believe they receive inadequate compensation and/or rewards (recognition, job security, vacations, promotions etc.)
- 1.2.*** Expensive lifestyle (cars, trips etc.)
- 1.3.*** Personal problems (gambling, alcohol, drugs, debt, etc.)
- 1.4.*** Unusually high degree of competition/peer pressure associated with particular project, at the grantee institution or in research field
- 1.5.*** Related party transactions (business/research activities with personal friends, relatives or their companies)
- 1.6.*** Conflict of interest
- 1.6.*** Disgruntled employee (recently demoted, reprimanded etc.)
- 1.7.*** Recent project failure associated with specific individual
- 1.8.*** Personal animosity or professional jealousy
- 1.9.*** Other

2. Possible Organizational Motives

For our purposes, an "organization" includes the particular project itself, the academic department and school it falls within, and the grantee institution. Pressure at any one of these organizational levels may produce an individual motive for committing fraud. It is understood that not all of the possible indicators listed below will apply at each organizational level. For example, the project may be the only organization with a for profit component, but disagreements about the project, its management or any other contentious issue, financial or otherwise, might arise at any level. A useful way to view

many of the possible indicators below are as trigger points or situations that may result in a climate conducive to fraud.

- 2.1.** Organization experiencing financial difficulty
- 2.2.** Project's commercial counterpart experiencing financial difficulty
- 2.3.** Project under unusually tight time deadlines
- 2.4.** Organization facing unusual degree of competition
- 2.5.** Project closely identified with/dominated by one individual
- 2.6.** Organization under pressure to show results (budgetary, programmatic etc)
- 2.7.** Organization recently suffered disappointment/reverses/consequences of bad decisions
- 2.8.** Project wants to expand its scope, obtain additional funding
- 2.9.** Project award up for continuation
- 2.10.** Project award up for an NSF approved extension
- 2.11.** Project has requested rebudgeting of its award
- 2.12.** Cooperative Agreement up for renewal or extension
- 2.13.** Project due for a site visit by NSF
- 2.14.** Project preparing for a reverse site visit (PI comes to NSF)
- 2.15.** Project has for profit component
- 2.16.** Organization faces pressure to use or lose funds to sustain future funding levels
- 2.17.** Organization recently affected by new/changing conditions (regulatory, economic, environmental etc.)
- 2.18.** Disagreements about project, management, financial issues/contentious atmosphere
- 2.19.** Record of previous failure(s) by one or more organizational components
- 2.20.** Sudden change in organization practice or pattern of behavior, e.g., in obligating funds, meeting milestones or submitting reports

2.21. Other

PART B - POSSIBLE OPPORTUNITIES FOR FRAUD

*The opportunity to commit fraud often flows from the person's environment or the situation in which they find themselves. Factors such as the attitude of management, the existence and use of effective internal controls and the particular nature of a project, transaction or account all may be important in that they may make fraud either easier or harder to commit. While fraud does not occur in a vacuum, please remember that this is a list of **possible** indicators which enable a snapshot to be taken of the environment the PIs and other relevant people find themselves in. The existence of any of the possible fraud indicators listed below does not necessarily mandate further action, such as a formal referral by Audit to Investigations or the opening of a case by Investigations. .*

3. Internal Controls Are Below Par

- 3.1. Management demonstrates lack of attention to ethical values (lack of communication regarding importance of integrity and ethics, lack of concern about presence of temptations and inducements to commit fraud, lack of concern regarding instances of fraud, no clear policy)
- 3.2. Management fails to specify needed levels of competence
- 3.3. Management displays a penchant for taking risks (e.g. aggressive accounting principles, liberal estimates)
- 3.4. Lack of an appropriate organizational structure with defined lines of authority and reporting responsibilities
- 3.5. Institution lacks policies and communication relating to individual accountability and best practices
- 3.6. Personnel policies do not demonstrate a commitment to hire competent and trustworthy people
- 3.7. Institution lacks personnel performance appraisal measures or practices
- 3.8. Management displays lack of commitment towards the identification and management of risks relevant to the preparation of financial statements (does not consider significance of risks, likelihood of occurrence or how they should be managed)
- 3.9. There is inadequate comparison of budgets with actual performance and costs,

- forecasts and prior performance; no regular reconciliation of control records (total expenditures charged to and drawn down from funds with records for particular projects, etc)
- 3.10.** Management of information systems is inadequate (no policy on information technology security, computer use and access, verification of data accuracy completeness or authorization of transactions)
 - 3.11.** There is insufficient physical security over facilities, assets, records, computers, data files, cash; failure to compare existing assets with related records at reasonable intervals
 - 3.12.** There is inadequate or inappropriate segregation of duties regarding initiation, authorization and recording of transactions, maintaining custody of assets
 - 3.12.** Accounting systems are inadequate (ineffective method for identifying and recording transactions, no tracking of time periods during which transactions occur, insufficient description of transactions and to which account they should be allocated to, no easy way to know the status of funds on a timely basis, no adequate procedure to prevent duplicate payments or prevent missing payment dates, etc)
 - 3.14.** There is a lack of internal, ongoing monitoring of controls which are in place; failure to take any corrective actions, if needed
 - 3.15.** Purchasing systems/procedures inadequate (poor or incomplete documentation of purchase, payment, receipt; poor internal controls as to authorization and segregation of duties)
 - 3.15.** Subcontractor records/systems reflect inadequate internal controls (please specify)
 - 3.16.** Management is unaware of or displays lack of concern regarding applicable laws and regulations
 - 3.17.** Specific problems and/or reportable conditions identified by prior audit (A-133 or other audits), oversight or by other means have not been corrected; history of problems; slow response to past findings or problems; unresolved present findings
 - 3.18.** No mechanism exists to inform management of possible fraud
 - 3.19.** General lack of management oversight
 - 3.20.** Other

4. Projects, Transactions, Accounts or Circumstances Susceptible to Fraud

Please remember that by including certain specific projects on the list below, it means that experience has taught us that they may be more susceptible to fraud, not that fraud has occurred in the past or will necessarily occur in the future. Further, it is understood that if the only possible fraud indicator identified is that it is a specific type of project, chances are high that identification of that factor alone means little.

- 4.1.** Small Business Investment Research (SBIR) award or Small Business Technology Transfer (STTR) award
- 4.2.** Major Research Instrumentation awards (particularly cost sharing arrangements)
- 4.3.** Related party transactions with inadequate, inaccurate or incomplete documentation or internal controls (business/research activities with friends, family members or their companies)
- 4.4.** Not for profit entity has a for profit counterpart with linked infrastructure (shared board of directors or other shared corporate functions and personnel)
- 4.5.** PIs have one or more outside businesses
- 4.6.** Overly decentralized grant administration/grantee delegates too much authority to PI's to determine allowable charges
- 4.7.** Specific transactions that typically receive minimal oversight
- 4.9.** A-133 audits with findings of questioned costs, evidence of non-compliance with applicable laws or regulations and weak internal controls; inadequate management response to any of above; A-133 audit with a qualified opinion
- 4.10.** Transactions and/or accounts, which are difficult to audit or subject to management judgment and estimates
- 4.11.** Cost sharing, matching or leveraging arrangements where there is inadequate documentation of industry support (numbers of supporters, amount contributed, etc), or any indication that industry money or other contributions (equipment, physical facilities, etc) have not been adequately tracked (lack of documentation, inaccurate documentation, imprecise or inaccurate valuation of in kind contributions, charges appropriately allocated to in kind contributions, other deficiencies with internal controls)
- 4.12.** Multiple sources of governmental funding with inadequate, incomplete or poor

- tracking; failure to segregate funds and/or existence of pooled funds (existence of multiple funding may surface in annual/final project report, acknowledgement of support in project publications, current and pending support disclosures in grant proposal)
- 4.13.** Unusual, complex or new transactions, particularly if occur at year end, or end of reporting period
 - 4.14.** Transactions and accounts operating under time constraints
 - 4.15.** Projects with special requirements regarding qualification of participants (e.g. residency requirements)
 - 4.16.** Unusual reliance on students, particularly if an SBIR/STTR award
 - 4.17.** Cost sharing, matching or leveraging arrangements where industry money or other donation has been put into a foundation (as in a foundation set up to receive gifts) without adequate controls to determine if money or equipment has been spent/used and whether it has gone to allowable costs and at appropriate and accurate valuations; outside entity such as foundation provided limited access to documentation
 - 4.18.** Inventory scrap accounts or write-off accounts with increased incoming transfers
 - 4.19.** Travel accounts with inadequate, inaccurate or incomplete documentation or internal controls such as appropriate authorization and review; variances between budgeted amounts and actual costs; collecting in excess of actual expenses; reimbursement for personal expenses; collecting for non-existent travel; collecting duplicate payments
 - 4.20.** Credit card accounts with inadequate, inaccurate or incomplete documentation or internal controls such as appropriate authorization and review
 - 4.21.** PI or other interested party in charge of internal service center accounts (copy center, labs, etc.) combined with many charges to that same PI's or other party's award
 - 4.22.** Accounts in which activities, transactions or events involve handling of cash or wire transfers; presence of high cash deposits maintained with banks
 - 4.23.** Project assets and inventory are of a nature to be easily converted to cash (small size, high marketability, lack of ownership identification, etc.) or easily converted to personal use (cars, boats, etc.)
 - 4.24.** Accounts with large discrepancies between budgeted amounts and actual costs

- 4.25. Accounts with large or frequent shifting of budgeted costs from one line item to another without adequate justification
- 4.26. Project shows little or no results for money granted; final reports slow in coming or fail to come at all; required interim reports not submitted; conflict between progress reported and actual progress observed
- 4.27. Payroll (including fringe benefits) system controls inadequate to prevent an individual being paid twice, or paid for a longer time period than permitted under the grant; distributions of salary as direct and indirect costs and as costs cited for cost sharing come from more than one system so that more than 100% of time can be distributed; lack of personnel activity reports (or time and effort reports) to support claimed salaries; support that is provided based on budget estimates rather than actual activity/costs
- 4.28. Consultant agreements which are vague as to work, time period covered, rate of pay, product expected; lack of proof that product or service actually delivered
- 4.29. Subcontract agreements which are vague as to work, time period covered, rate of pay, product expected; lack of proof that product or service actually delivered
- 4.30. Project experiences high turnover of staff
- 4.31. Accounts which have distinctive charging patterns, sudden shifts in charging, a large amount of indirect charges or a decrease in charges when near budgeted ceiling
- 4.32. Program under which award made was mandated by Congress rather than originating with NSF
- 4.33. Other

PART C - POSSIBLE METHODS OF COMMITTING/CONCEALING FRAUD

The actual methods for committing fraud and concealing it are as diverse as the people involved and the means available to them. Under certain circumstances, falsification of signatures or documents or results, inaccurate or shifting journal entries and writing large checks to cash may all be fraudulent acts or signs that fraudulent acts are being concealed. Please remember that people can be quite inventive once they've crossed that line and decided to cheat. Surprisingly, they can also be both inartful and obvious in their methods. Pay particular attention to trends and repeat occurrences.

- 5.1. Refusal or reluctance to turn over documents
- 5.2. Trying to control the audit process (timetables, access, scope)

- 5.3. Deviation from standard procedures (all files but one handled a particular way; all documents but one included in file, etc.)
- 5.4. Auditee blames a mistake on a lack of experience with NSF grant requirements or federal regulations governing grants.
- 5.5. Missing documents
- 5.6. Documents are copies, not originals; documents in pencil
- 5.7. Unreasonable explanations; annoyance at questions
- 5.8. Altered documents
- 5.9. False signatures/incorrect person signing
- 5.10. Excessive journal entries
- 5.11. Shifting costs from one account to another, or one program to another
- 5.12. Transfers to or via any type of holding or suspension account
- 5.13. Inter-fund loans to other programs
- 5.14. Records maintained are inadequate, not updated or reconciled
- 5.15. Inaccurate/incomplete description of PI and other key personnel credentials; PI not actually employed by grantee
- 5.16. Use of several different banks, or frequent bank changes; use of several different bank accounts
- 5.17. Failure to disclose unusual accounting practices or transactions
- 5.18. Changing accounting practices
- 5.19. Too much forgetfulness
- 5.20. Promises of cooperation followed by subsequent excuses to limit or truncate cooperation; subtle resistance
- 5.21. Answering a question that wasn't asked; offering more information than asked; providing wealth of information in some areas, little to none in others
- 5.22. Explaining a problem by saying "we've always done it that way", or "someone

- at NSF (or elsewhere) told us to do it that way” or “Mr. X said he’d take care of it”
- 5.23. A tendency to avoid personal responsibility (overuse of “we” and “our” rather than “I”); blaming someone else
 - 5.24. Uncharacteristic willingness to settle questioned costs
 - 5.25. Non-serial numbered transactions or out of sequence invoices or other documents
 - 5.26. Duplicate invoices
 - 5.27. Eagerness to work unusual hours
 - 5.28. Access to/use of computers at unusual hours
 - 5.29. Reluctance to take leave, insistence on doing job alone, refusal of promotion or reluctance to change job
 - 5.30. Creation of fictitious accounts, transactions, employees, charges
 - 5.31. Writing large checks to cash or repeatedly to a particular individual
 - 5.32. Excessive or large cash transactions
 - 5.33. Payroll checks with unusual/questionable endorsements
 - 5.34. Payees have similar names/addresses
 - 5.35. Non-payroll checks written to an employee
 - 5.36. Employees submitting blank time cards or time cards completed in advance
 - 5.37. Reclassifying employees/salaries from indirect cost to direct cost
 - 5.38. Actual employee hours billed consistently at or near budgeted amounts
 - 5.39. Reliance on one source for items, spare parts and services without adequate explanation or review
 - 5.40. Defining what project needs in ways that can only be met by one source
 - 5.41. Unexplained price increases or failure to achieve logical/expected price decreases

- 5.42. Existence of contracts with “sweetheart” provisions (longer time periods for performance, first refusals, etc.)
- 5.43. Contracts with numerous and/or high dollar value change orders
- 5.44. Release of confidential information to outside party
- 5.45. Continued reliance on person/entity despite poor performance
- 5.46. Same research project funded by different agencies
- 5.47. Hiding unallowable costs in accounts which do not receive close audit scrutiny (office supplies); unallowable costs not broken out
- 5.48. Charging items to project account for personal purposes (books and supplies bought for family members, home gym equipment charged to project account etc)
- 5.49. Materials erroneously reported as purchased; repeated purchases of same items; identical items purchased in different quantities within a short time period
- 5.50. Equipment not used as promised, doesn’t work, doesn’t exist
- 5.51 Trying to rush the audit process
- 5.52. Other