



# The Five Faces of Procurement Fraud, Abuse, and Noncompliance

This article focuses on the personalities of the people that place procurements at risk for fraud, abuse, and/or noncompliance.

Procurement fraud, procurement abuse,<sup>1</sup> and/or acts of noncompliance to procurement policy are, by its very nature, a product of human behavior and performed with willful intent. These types of misdeeds expose organizations or companies to significant financial losses, damage to their reputations, and jeopardize current and future business. With more than 70 years of combined experience, the authors have identified five unique personality types that will either commit procurement fraud and/or abuse or deliberately expose an organization or company to fraud and/or procurement abuse by not complying with procurement policy.

People who fall in each of the personality risk profiles are motivated differently and create a different risk or vulnerability to the organization or company. Therefore, it is important that the entity determine what its tolerance level is and how it will develop procurement integrity controls<sup>2</sup> to mitigate its risks.

The Association of Certified Fraud Examiners' (ACFE) "2008 Report to the Nation on Occupational Fraud & Abuse"<sup>3</sup> primarily focused on statistics related to specific areas of fraud, such as losses by industry, the effectiveness of internal controls, and the average cost of different fraud schemes. The report's same statistics can also be used to identify the traits and behaviors of those who might commit fraud. Neither the ACFE results nor this article alone will build a complete personality risk profile of a suspected fraudster or abuser or someone that will not comply with procurement policy. However, both will help you recognize the broad degree of risk your procurement systems need to protect against.

The five personality risk profiles, each one is motivated differently, creates a different risk or vulnerability to organizational or company procurements.

The five personality risk profiles are:

- "Situational fraudster"
- "Deviant fraudster"
- "Multi-interest abuser"
- "Well-intentioned noncompliance employee"
- "Disengaged noncompliance employee."

The "situational" and "deviant" fraudsters, along with the "multi-interest abuser," can cause a direct financial loss, damage to the organization or company's reputation, and can create media embarrassment and potential litigation. The "noncompliance employees," who, like the others, are knowingly violating procurement policy, can create unnecessary exposure to fraud, increase contract disputes, and waste organizational or company resources and funds. Although one would

not think the “noncompliance employee” to be a threat, entities must be aware of this type of employee, as they are easy pathways for creating opportunities and vulnerabilities for fraudsters.

In order to understand the personality risk profiles, you need to have a basic knowledge of the “Fraud Triangle,” which is universally accepted by nearly all practitioners developing anti-fraud and abuse mitigation strategies and in almost every setting in which fraud or abuse is described or analyzed. The theory, which was developed in the mid-1970s and credited to Edwin Sutherland and Donald Cressey, is that for any fraud to occur, three elements need to exist:

- 1) A perceived pressure, which can be created by the person or the organization or company;
- 2) A perceived opportunity, normally through weak procurement integrity controls; and
- 3) A rationalization that the inappropriate act is deserving.

In 1979, KPMG-granted research into the study of fraud also identified three elements:

- 1) Situational pressures,
- 2) Opportunity to commit the act; and
- 3) Personal integrity.

The KPMG situational pressures referred to the immediate pressures within the environment of the person and further identified that opportunity can be created by the individual or by the organization or company—e.g., the person can create opportunity by learning the organization or company’s operations, increasing his or her access and influence over procurement controls, and developing a trusted status. An entity can develop opportunity for fraud and abuse by not demonstrating a commitment to procurement integrity; failing to link specific organizational/company risks to effective preventive, deterrent, and/or detection procurement integrity controls; or fostering performance matrixes of profit over ethical business practices.

In both studies, it was shown that perceived pressure and perceived opportunity does not have to be real to trigger the inappropriate act as long as the person can rationalize his or her actions as warranted. Neither study specifically addressed the severity of financial impact or frequency of occurrence in relationship to the person’s ability to rationalize his or her actions or his or her perception of being caught. However, there is in fact a relationship of financial severity and frequency of occurrence proportionate to the person’s ability to rationalize committing procurement fraud and/or abuse.

### **Situational Fraudster**

The first profile of the people who will commit procurement fraud and the one many anti-fraud professionals will identify as the traditional “fraudster,” is the “situational fraudster.” This employee appears to be frustrated at work, has rationalized his or her perceived entitlement to an illegal enrichment, and perpetrates the fraud when the right occasion occurs, usually because of weak procurement controls. When the situational fraudster is caught, other employees are not surprised that the individual was involved in the fraud because of the fraudster’s poor work attitude.

The situational fraudster had no intentions of committing any type of fraud when he or she joined the organization or company and many times has had no other involvement with violating the law. The situational fraudster usually becomes upset with an event at work that has a direct financial impact to the fraudster. He or she perceives the event as unjust, rationalizes that he or she is not deserving of the financial losses, and observes a weakness in the entities procurement controls, which he or she decides to exploit.

As a hypothetical example of a situational fraudster, let's examine a Government Agency (GA) employee overseeing a contractor's performance at the same time the (GA) employee becomes upset with the loss of one day of pay each week for 10 weeks due to sequestration.<sup>4</sup> The (GA) employee rationalizes that the failure of elected officials to approve a budget was the only reason he lost his pay. While his frustration grows, the contractor he has been overseeing for several years' offers to "lend" him a small amount of money just to help out, which the (GA) employee perceives as his only solution for paying down his expected debt. What started out as a "loan" with potentially the intent to repay, becomes an offer of a "gift" from the contractor. Feeling gratitude, the (GA) employee returns the "favor" by providing procurement-sensitive information of a future procurement opportunity.

Once the (GA) employee experiences the ease of providing the sensitive information, the fraud potentially continues by accepting additional payments for more sensitive information. In this hypothetical example, the (GA) employee had no intention of becoming a situational fraudster, but had a perceived pressure to regain the lost income from sequestration, and saw the opportunity of providing the sensitive information as a solution, which he rationalized as deserving because of the failure of the elected officials and related financial loss. The "gifts" are legally defined as "bribes" and the total amount of payments will continue as long as the (GA) employee believes he has a low probability of being caught, he continues to rationalize his entitlement of the payment, and the corrupt contractor continues to make the payments.

## **Deviant Fraudster**

The next profile is the "deviant fraudster," which is a person that is the most serious threat to the organization or company because he or she can cause the most damage. These fraudsters are always proactive in their search for opportunities to commit fraud, are quite possibly perceived as some of the organization or company's hardest workers or best contractors, and carry a "veil of trust" from others within the entity. This fraudster will have a strong group of advocates who will deny assertions that the fraudster is involved with any wrongdoing. The deviant fraudster, when internal to an organization or company, is also the employee that will take only a few days of leave each year and seems to have his or her hand in every process within his or her business unit. This person is sometimes described as a "wheeler-dealer."

An example of a deviant fraudster would be a corrupt contractor that offered our previous (GA) situational fraudster the "loan" that turned into a "gift" that rolled over into a "bribe." The deviant fraudster offered the loan, which he redefined as a gift, expecting it would allow him access to sensitive procurement information. The more the (GA) situational fraudster provides sensitive procurement information to the deviant fraudster, the more willing the deviant fraudster is to pay bribes. This progressive fraud situation can easily become a "kickback" scheme where the deviant fraudster and corrupt (GA) situational fraudster agree to share profit from fraudulent billing. This example also illustrates how a situational fraudster can develop into a deviant fraudster if he or she

continues to provide procurement-sensitive information or agrees to be a co-conspirator in a kickback scheme.

In this hypothetical example, the deviant fraudster seized on a frustrated (GA) employee who desired to regain what the (GA) employee perceived as “lost” income. The deviant fraudster justifies this action due to a perception that the government is underpaying him within his contract with (GA) employee by only paying a 6-percent profit when the deviant fraudster wanted 12 percent. Research by the ACFE also revealed that 13 percent of such frauds go undetected for nearly five years before being detected.

### **Multi-Interest Abuser**

Where most published articles or classes on procurement fraud will talk almost exclusively about the two types of fraudsters previously mentioned, additional vulnerabilities exist with other types of people. For example, one often-overlooked profile of a person who is not by definition a “fraudster,” but who still manipulates the process to a negative effect is the “multi-interest abuser,” who knowingly manipulates the procurement process to advance his or her own interests and/or the interests of another person. This is not done to obtain any financial advantage, but instead to help a friend in getting a contract, or to ensure the award goes to a preferred contractor of the abuser—like the incumbent, or even helping family members.

This abuser of the procurement process is the one who inappropriately drafts contract specifications to a specific contractor, embellishes the need for a sole-source justification to avoid a fully competitive process, or “slants” technical evaluations to a specific bidder. Again, this abuser knows he or she is violating the procurement rules, but his or her actions are not motivated by any direct financial compensation that would come back to him or her. However, this person still raises significant risk to the procurement process due to the increased risk of contract protest or in potentially paying higher-than-needed costs for items due to not having a competitive process. Clearly, if the inappropriate actions of this person were motivated for personal financial gain, then this person would be categorized as a procurement *fraudster* and not an *abuser*.

When applying the elements of the Fraud Triangle, the multi-interest abuser can be pressured by a family member or friend to inappropriately manipulate the procurement process in the third party’s favor. The multi-interest abuser, having noticed no validation was occurring on sole-source contracting in the organization or company, drafts an unwarranted sole-source procurement to help his or her family or friend. The multi-interest abuser can rationalize that the organization or company is getting the service it needed anyways, so no harm has occurred, or the rationalization can be that the abuser is obligated to help a family member or friend. Sometimes, the inappropriate action of the abuser is to sole-source to the current incumbent, which the abuser has worked with for years and enjoys working with. In this situation, the pressure could be coming from the incumbent (the opportunity is the limited verification of sole-sourcing) and the rationalization is the incumbent would have won the contract anyway—so by sole-sourcing, the abuser saved the funds and wasted resources.

In this example, the perceived pressure could have also been created when the organization or company required its employees to expend end-of-year funds on new contracts at an unrealistic rate, and the rationalization of the abuser would be that the organization or company placed

unrealistic demands, so the only solution would be to rush the procurement process to the incumbent.

### **Well-Intentioned Noncompliance Employee**

The next two personality risk profiles are rarely considered, but present a significant risk to procurements and are harder to identify than the “fraudster” or “abuser.” Where the fraudster and abuser create a direct financial loss or damages to reputation, or create media embarrassment, the noncompliance employee creates an indirect and unnecessary exposure to fraud, potential contract disputes, and may waste organizational or company resources and funds. Also, the noncompliance employee creates countless opportunities for the fraudster, which is why you must address the vulnerabilities these employees create.

The well-intentioned noncompliance employee believes that his or her willful deviation from the procurement process causes no harm to the organization or company. As a matter of fact, he or she sometimes believes that he or she is helping the organization or company in obtaining greater efficiency or obtaining better services. The well-intentioned noncompliance employee is normally an employee who has been with the organization or company for several years and has a good working knowledge of the procurement processes or requirements, and therefore knows how to advance his or her idea of efficiency. This is the employee who consciously decides not to identify to the procurement staff the true scope of a requirement, thus ensuring the contract remains under a particular dollar threshold—thereby allowing the award to be expedited. This is also the employee who knows what key descriptions in a purchasing document to use, or not use, to avoid any additional procurement steps.

As an example, one well-intentioned noncompliance employee works on developing a product over the course of several years and his efforts are ready to be manufactured by an external contractor. The well-intentioned employee is familiar with a contractor that historically provided good service and has an outstanding record of customer service. The well-intentioned employee is asked by the procurement staff to develop the technical evaluation criteria for a fully competitive procurement. Being fully aware that the organizational or company procurement policy requires the technical evaluation criteria to not be tailored to any specific contractor, the well-intentioned noncompliance employee disregards the policy and intentionally develops technical requirements that best matches the contractor that the well-intentioned employee preferred. The well-intentioned employee can easily rationalize the benefit in efficiency and potential services because of his or her noncompliance with the procurement policy.

### **Disengaged Noncompliance Employee**

The “disengaged noncompliance employee” is the person who knowingly decides to put little or minimal effort into a specific procurement step. This person will disregard his or her responsibility to verify a contractor’s bond, to not examine a contractor’s past performance record, or to not confirm a contractor’s deliverable prior to approving payment. The actions, or lack of actions, by the disengaged person is usually done willfully and are the byproducts of a disgruntled or dissatisfied employee. Adding to the risk presented by the disengaged noncompliance employee is that if a deviant fraudster observes the lack of proper oversight by the disengaged noncompliance employee, the deviant fraudster could theoretically submit false or inflated cost data, believing the disengaged employee will not identify the mischarging. The deviant fraudster could also substitute

low-cost parts during manufacturing, thereby increasing profit after observing the disengaged organization or company inspectors are not performing required testing.

The disengaged noncompliance employee can be anywhere in the procurement process and could be disgruntled or dissatisfied because of an entire list of items, from perceived inadequate pay to perceived poor management to one's own low self-worth. Where the research clearly demonstrates the statistical probability of these employees being within the organization or company, the protection starts with knowing the workforce's job satisfaction.

## **Conclusion**

In closing, procurement fraud, abuse, and noncompliance to procurement policy is performed by people with willful intent and different motivations. The organization or company must recognize these five personality risk profiles and develop mitigation steps to protect their procurements against them.

## **Endnotes**

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<sup>1</sup> *Abuse* is a procurement action that a prudent person would not consider reasonable or a necessary business practice given the same facts and circumstances.

<sup>2</sup> *Procurement integrity controls* are the aggregate of the organization or company's people, processes, procedures, and management systems that are designed to provide reasonable assurance regarding the prevention, deterrence, detection, and prompt reporting of abuse, fraud, or noncompliance with organizational or company procurements.

<sup>3</sup> Available at [www.acfe.com/uploadedFiles/ACFE\\_Website/Content/documents/2008-rttn.pdf](http://www.acfe.com/uploadedFiles/ACFE_Website/Content/documents/2008-rttn.pdf).

<sup>4</sup> Simply put, sequestration is the employment of automatic, across-the-board spending cuts in the face of annual budget deficits.