
Multiple Subcontractors

The Scenario

An auditor working abroad was reviewing Department of Defense contract files for local construction projects. Construction projects were varied and included medical facilities, roads, and bridges. When reviewing a bridge contract file, the auditor observed the following:

- One prime contractor reported over 50 subcontractors.
- Audit work disclosed an additional 10 subcontractors were also working on the project.

Although it is a normal contracting practice to employ subcontractors, the auditor noted that the number of subcontractors employed by the prime exceeded established business practices. As a result, the auditor continued to review the contract file, and, when possible, coordinated interviews with subcontracting officials. The auditor also analyzed subcontractor billings and designed tests to determine whether the subcontracting companies were legitimate businesses.

The auditor determined the following:

- Ten employees were listed as employees of five or more subcontractors, which resulted in the prime contractor double billing the Government for each employee's services.
- Six of the subcontracting companies were phony. Consequently, the agency was charged for invalid labor costs.

General Comments / Lessons Learned. Organizations that do not actively monitor the prime contractors' relationship with subcontractors provide many opportunities for fraud. A prime contractor, in collusion with multiple subcontractors, can engage in multiple billing schemes. For example, a single individual can be listed as an employee of two or more subcontractors, enabling the prime contractor to double bill the Government for the employee's services. Similarly, when conducting audit work, auditors should be alert to schemes that involve dishonest prime contractors using phony subcontracting companies and/or subcontractor employees billing the Government for invalid labor costs. Auditors should be also be aware of the potential for fraud when prime contractors employ an excessive number of subcontractors.

FRAUD INDICATORS

- **Excessive numbers of subcontractors working on a contract.**
- **Individuals listed as employees of more than one subcontractor.**
- **Subcontracting companies that are not legitimate businesses.**
- **An organization does not actively monitor the prime contractor's relationship with the subcontractor.**