

Fighting Project Fraud

By: Richard B. Lanza and Steve Rollins

What is the Definition of Project Fraud?

Project Fraud, for purposes of this article, is defined as:

- the misrepresentation of a project's mission or progress to secure project financing
- misuse of project resources
- improper dealings with project vendors for personal enrichment.

To date, there has been no true definition of project fraud. For instance, the Association of Certified Fraud Examiners identifies many types of fraud, some of which border the concept of project fraud (i.e., corruption, misappropriation of assets, etc.), but never specifically identify it. The authors believe that over time, this will change as projects become more the way business gets done. This is also in light of the increased awareness in the global economy to fraud reduction and improved corporate governance.

In Plain English, What is Project Fraud?

Although the above definition is technically correct, it does not provide the full flavor of this malfeasance. Yet, we all know the signs of project fraud. For example, how many projects did you see at least one of the below symptoms?

Project Fraud Symptoms

- Over-reported and unsubstantiated business case
- Unsubstantiated project decisions
- Under-reported initial estimates of project lifecycle costs (to get project approved)
- Under-reported initial estimates of project maintenance costs (to get project approved)
- Under-reported costs
- Over-reported schedule progress
- Over-reported quality progress
- Project asset misuse
- Vendor conflict of interest and kickbacks
- Vendor “overselling” of their capabilities
- Inappropriate vendor charges

Why Should Auditors Fight Project Fraud?

Projects are now making up over \$ 2.3 trillion in the U.S. economy (25% of gross domestic product) according to a recent PMI study using data from the U.S Department of Commerce. Projects are ripe for fraud given they are creative new ventures. Unlike an operational process that has controlled itself over time, projects have not had that luxury and therefore, many times are completed in an uncontrolled manner. For instance, the Standish Group reports that more than \$275 billion relate to application software where the following trends were noted:

- Only 16.2% of projects are completed on-time and on-budget
- 31.1% are cancelled
- The average cost overrun was 189% of the original time estimate

Given the above negative trends, project managers, vendors, and executives sponsoring projects all have an incentive to defraud the organization. Egos are at stake, jobs are at stake, and unfortunately, many times company finances are wasted in the process.

How Can Auditors Fight Project Fraud?

Understanding that projects represent some of the most risky investments in an organization, auditors should become more involved and their scope needs to extend beyond computer security and computer system controls. Auditors have many traits but their most important ones are that they are independent verifiers. Such traits can be maximized to root out project fraud and ultimately save on their company's project investments.

Although this article cannot provide all of the details in fighting project fraud, some simple proactive measures can be provided which are aligned to two of the most common fraud symptoms below:

- ***Over-reported and unsubstantiated business case*** – Although this may be completed in error by the project team (rather than due to fraud), many times the need for the project is over-estimated and the effort is under-estimated. To combat such issues, the auditor should review the business case with various independent parties. For example, if the project is installing a new virtual private network which is expected to save network costs, such claims should be reviewed with other companies results. The auditor could meet with a peer auditor who may have had a similar installation in their company or could review industry periodicals. Further, the auditor could talk to benchmarking companies such as Gartner Group to get more defined insights.
- ***Under-reported initial estimates of project plan effort required*** – There is no better way to understand how long a project will take and therefore, cost than by reviewing past projects. Auditors should seek out similar project teams so that they may benchmark the project under review. They should also consider using estimation techniques that calculate a probabilistic estimate of the time to complete the project. Such estimation techniques utilize Monte Carlo statistical engines to arrive at a more realistic project plan/budget. For more on these tools, please see the following link:

<http://www.auditsoftware.net/community/how/tool/tools/Monte%20Carlo%20Article-Auditors.doc>

Where Can Auditors Get Help?

Auditors should seek out and team up with Program Management Departments (“PMOs”) who are experts in project management and can assist auditors in their improved understanding of this area. In return, PMOs will receive project audit expertise from internal auditors and a “bad cop” to root out any injustices within the project portfolio.

There is also a wealth of Internet resources. One popular site focused on auditors using project management is www.pmousa.com (check out their audit community). They have various links and tools to help auditors improve their project audit, and therefore, their project fraud fighting capabilities.