

GAO

Report to the Chairman, Subcommittee  
on Administrative Oversight and the  
Courts, Committee on the Judiciary,  
U.S. Senate

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September 1998

# DOD PROCUREMENT FRAUD

## Fraud by an Air Force Contracting Official



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**Office of Special Investigations**

B-280720

September 23, 1998

The Honorable Charles E. Grassley  
Chairman, Subcommittee on Administrative  
Oversight and the Courts  
Committee on the Judiciary  
United States Senate

Dear Mr. Chairman:

This report responds to your request that we review the actions of Mark J. Krenik, a former civilian employee of the U. S. Air Force, 7th Communications Group, the Pentagon, who was convicted of submitting false invoices and fictitious receiving reports for contractor services and materials.<sup>1</sup> Specifically, you asked us to provide detailed information on the scheme or schemes that Mr. Krenik used to commit fraud, including the level of involvement by contractor staff. Mr. Krenik did not consent to our request for an interview. Accordingly, the information contained in this report is based on the testimony of others and an examination of pertinent records. We agreed to also provide you a summary of internal fraud cases involving the Defense Finance and Accounting Service (DFAS).<sup>2</sup> The summary is included as appendix I.

In a separate report, GAO's Accounting and Information Management Division will (1) provide information on the history of the two contracts associated with the schemes that Mr. Krenik used and (2) discuss examples of internal control weaknesses that contributed to Mr. Krenik's, and similar instances of Defense-related financial theft.

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**Background**

Hughes STX had a contract with the Air Force to provide office automation hardware, software, maintenance, training, and contractor support services.<sup>3</sup> The July 30, 1986, contract award, in the amount of

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<sup>1</sup>In 1996, Mr. Krenik pleaded guilty to three counts of submitting false claims to the United States, was sentenced to 3 years probation, and was required to pay restitution.

<sup>2</sup>DFAS—established to improve Department of Defense financial management through the consolidation, standardization, and integration of finance and accounting operations—took over responsibility for 332 military installation finance and accounting offices in December 1992. Prior to this, the Air Force District of Washington/Accounting and Finance Office processed invoices under the contracts discussed in this report.

<sup>3</sup>The contractor providing services for the Air Force's Air Staff Automation Systems changed over time. In July 1986, the contract was awarded to SASC Technologies, Inc., which later became ST Systems Corporation (STX). When Hughes Aircraft (owned by General Motors Corporation) acquired STX in October 1991, it became known as Hughes STX. Since the December 1997 merger of Raytheon and Hughes Aircraft, the company has been referred to as Raytheon STX.

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\$49.6 million, included options and modifications that extended performance until December 31, 1991.

Effective January 3, 1992, the work performed by Hughes STX continued under a separate contract. This contract required delivery of hardware and software maintenance, technical support, and training; it resulted in approximately \$8 million in obligations through September 1996.

Mr. Krenik was the Contracting Officer's Technical Representative<sup>4</sup> on both Hughes STX contracts. He was authorized, among other functions, to interpret the statement of work, direct the performance of contractor efforts within the scope of the statement of work, accept deliverables, control all government technical interface with the contractor, and monitor contractor performance. A Technical Representative is authorized to perform these functions only when they are exercised in a manner consistent with the statement of work, terms and conditions of the contract, and any delivery orders issued under the contract.

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## Results in Brief

In the fall of 1992, Mr. Krenik successfully encouraged certain Hughes STX employees to bill the government over \$300,000 for services that were not rendered. He then attempted to obtain these funds by directing Hughes STX to pay a nonexistent subcontractor<sup>5</sup> for consulting services based on a bogus subcontractor invoice that he supplied.<sup>6</sup> Had this scheme worked, the government would have paid Hughes STX for work "performed" by the fictitious subcontractor; and Hughes STX would have "reimbursed" the subcontractor by sending the money to a post office box controlled by Mr. Krenik.

When Hughes STX contract administration personnel learned of the participation of Hughes STX employees in the billing incident, they conducted an internal investigation and returned the government checks, which the company had not negotiated, for the over \$300,000 that had been billed. However, they did not notify government authorities of either

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<sup>4</sup>The Technical Representative is not authorized to modify any contract terms nor to approve expenditures beyond the funded amount of the delivery order.

<sup>5</sup>Mr. Krenik told Hughes STX employees that the government had failed to pay the contractor for consulting services and that Hughes STX would act merely as a conduit for reimbursement to the contractor. At the time, Hughes STX employees were unaware that the contractor did not exist.

<sup>6</sup>Mr. Krenik and Hughes STX staff were investigated by the U.S. Attorney, Eastern District of Virginia, but were not charged in this scheme.

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the extent of the company's involvement in the billing incident or the bogus subcontractor invoice.

After Hughes STX employees refused to participate in the scheme involving the bogus subcontractor invoice, Mr. Krenik executed another plan in December 1992, without Hughes STX involvement, by which he created and submitted 11 bogus invoices totaling over \$500,000. In January 1993, the Air Force issued payment checks for the invoices and mailed them, unwittingly, to a post office box that Mr. Krenik had opened in December 1992. Mr. Krenik's theft was detected after officials of the bank in which he had deposited the checks became suspicious of what they considered to be unusually large transactions and reported them to the U.S. Secret Service.

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## Mr. Krenik Attempted to Defraud the Government

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### Contractor Employees Prepared/Submitted False Invoices and Receiving Reports

According to current and former contractor employees, in September 1992 Mr. Krenik asked Hughes STX management staff to bill the government for work not yet performed by the company so that unobligated funds could be used before the end of the fiscal year.<sup>7</sup> On October 14, 1992, using specific instructions provided by Mr. Krenik, the Hughes STX Contract Administrator<sup>8</sup>—the individual responsible for invoicing—prepared five false invoices, totaling \$342,832.<sup>9</sup>

The five sequentially numbered Hughes STX invoices were dated October 14, 1992, and provided the following details (see table 1) for the product or services purportedly rendered and billed.

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<sup>7</sup>An appropriation cannot be used to purchase services or supplies that are not needed until after the appropriation expires. A fiscal year appropriation may generally be obligated only to meet a legitimate, or bona fide, need arising in the fiscal year for which the appropriation is made. The government's fiscal year ends on September 30.

<sup>8</sup>In other documentation, this position was also referred to as Program Administrator.

<sup>9</sup>Former Hughes STX employees who were involved in this transaction told us that they were following Mr. Krenik's specific instructions and did not realize at the time that preparation of these invoices was illegal.

**Table 1: False Hughes STX Invoices  
Dated October 14, 1992**

Invoice number	Description	Price
921036	Principal programmer - 1,100 hours @ \$61/hour	\$67,100
	Parts	31,393
	Hourly maintenance	30,000
	Maintenance PPM	700
921037	Training	27,412
921038	Principal programmer - 1,679 hours @ \$61/hour	102,419
	Parts	33,008
	Hourly maintenance	30,000
921039	Technical assistance	10,400
921040	Technical assistance	10,400
<b>Total</b>		<b>\$342,832</b>

Source: Hughes Aircraft

On October 20, 1992, the Hughes STX Project Manager<sup>10</sup> signed a DD-250<sup>11</sup>—the Material Inspection and Receiving Report—for each invoice, falsely indicating that Hughes STX had provided to the government the materials/services itemized on the invoices. On the same date, Mr. Krenik picked up the invoices and DD-250s at the Hughes STX office in Vienna, Virginia.

Mr. Krenik signed the five DD-250s dated October 26, 1992, falsely certifying the Air Force’s receipt of the materials and services, and submitted the paperwork for payment. The government subsequently processed the paperwork for all five invoices and paid three of them. The accounting classification codes on the affiliated government vouchers indicate that the funds used were from 1991 and 1992 appropriations.

## Mr. Krenik Attempted to Obtain the Money From Hughes STX

Having caused the government to begin payment to Hughes STX for services that it had not rendered, Mr. Krenik instructed Hughes STX employees to make payment to a fictitious subcontractor, “Applied Quantitative Systems” (AQS), for entirely different services.

<sup>10</sup>In other documentation, this position was also referred to as Program Manager.

<sup>11</sup>By signing this document, the contractor certifies that the items listed have been provided and are ready for the government’s use. The government representative’s signature on the DD-250 certifies that the items have been received from the contractor.

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On October 20, 1992, Mr. Krenik opened a McLean, Virginia, post office box in the name of AQS.

Hughes STX received a memorandum dated October 14, 1992, (see fig. 1) from Mr. Krenik, instructing Hughes STX to order \$500,000 in consulting services from AQS and to bill \$125,000 for “markup” (administrative handling). Appended to the memorandum was the bogus AQS invoice (see fig. 2). According to the former Hughes STX Project Manager, Mr. Krenik told him that he wanted to apply work performed by AQS to the contract. The former Project Manager told us that the incentive for Hughes STX to participate in this was Mr. Krenik’s proposed 25-percent markup, i.e., \$125,000.<sup>12</sup>

Specifically, Hughes STX was to bill the Air Force \$342,832 for these consulting services, using Hughes STX invoice numbers 921036 through 921040 (the same invoice numbers and the same dollar amounts as shown in table 1, but for different services). Hughes STX was to bill the Air Force the balance of the \$625,000—\$282,168—later in fiscal year 1993, after determining a delivery order number.

As a result of Mr. Krenik’s October 14, 1992, memorandum and discussions with Hughes STX management, the staff asked the company’s Contract Administrator in early November 1992 to prepare an invoice to the Air Force for the services purportedly provided by AQS. The Contract Administrator prepared the invoice<sup>13</sup> and subsequently advised the Hughes STX Group Business Manager.<sup>14</sup>

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<sup>12</sup>The then Project Manager and the then General Manager met to discuss the AQS invoice proposal, decided that the proposed markup was too “steep,” and discussed lowering the markup amount.

<sup>13</sup>According to the Contract Administrator, the invoice was later destroyed.

<sup>14</sup>In other documentation, this position was also referred to as Manager, Contracts and Pricing.

Figure 1: October 14, 1992, Memorandum for AQS Services

FROM: DEPARTMENT OF THE AIR FORCE  
 7th Communications Group  
 7CG/GABB Room 3A147  
 Pentagon, DC 20032

14 OCT 92

SUBJECT: ASCAF Work Order Number 047

TO: HUGHES STX Corporation  
 1577 Spring Hill Road  
 Vienna, VA 22182

1. Please order the following:

ASCAF CLIN	Description	Price Each	How Many	Total Cost
5AA	Technical Services			\$500,000.00

2. Please order these services from:

Applied Quantitative Systems (Invoice attached)

3. This service is to be billed as follows:

5000	\$129,193.00	921036	011	
5001	\$ 27,412.00	921037	006	
5002	\$165,427.00	921038	009	
5004	\$ 10,400.00	921039	001	
5005	\$ 10,400.00	921040	001	
FY93	\$282,168.00	Pending FY93 D.O.		
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\$625,000.00		(Price includes 25% STX markup)		

4. If you have any questions please give me a call at 703-614-2564.

*Mark J. Krenik*  
 Mark J. Krenik  
 Office Automation Systems Support Branch



Figure 2: Bogus AQS Invoice Dated October 1, 1992



APPLIED QUANTITATIVE SYSTEMS

TYSONS ENTERPRISE CENTER  
PO BOX 3294  
MCLEAN VA 22103-3294

1 Oct 92

YOUR ACCOUNT NUMBER 3510-016474-4	INVOICE NO. 1854042	EFFECTIVE DATE 10/01/92	AMOUNT DUE \$500,000.00	PURCHASE ORDER NO. FA827
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PAGE 1 OF 1

CUSTOMER:

AFDW AFO/PENTAGON/OSD-SC  
USAF 1100 NCR SPTG AFDW FMAOA  
WASHINGTON DC 20330

TO INSURE PROPER CREDIT - Please return a copy of this invoice with payment.

MAIL YOUR REMITTANCE TO:

APPLIED QUANTITATIVE SYSTEMS  
TYSONS ENTERPRISE CENTER  
PO BOX 3294  
McLEAN VA 22103-3294

INVOICE

DESCRIPTION	AMOUNT	DUE DATE	PAYABLE AMOUNT
RENEWAL SUBSCRIPTION LEGISLATIVE CONSULTING AND ANALYSIS	500,000.00	11/06/92	500,000.00

TAX EXEMPT

(Price includes early payment discount.)

TOTALS 500,000.00

Please retain a copy for your records.

Robert Vaughn, Brig Gen (Retired)  
Chairman

92 OCT 29 PM 3 29

P.O. Box 3294 • McLean, VA 22103-3294

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## Hughes STX Management Discovered and Canceled the Transactions

The Hughes STX Group Business Manager became concerned about the AQS invoice, which Mr. Krenik had attached to his October 14, 1992, memorandum, because it appeared to be outside the scope of the contract.<sup>15</sup> Therefore, the Group Business Manager contacted the Director of Contracting in Lanham, Maryland, and, on November 9, 1992, sent Mr. Krenik's October memorandum, along with the AQS invoice, to the Director via facsimile. The following day, the Director of Contracting visited Hughes STX in Vienna, Virginia, to discuss the AQS invoice. While there, the Director learned of the billing for services not rendered (the five false invoices), determining that the AQS invoice and the invoices for services not rendered were improper and that corrective action was necessary.<sup>16</sup>

Over the next 2 weeks, Hughes STX senior management met to discuss the false invoices.<sup>17</sup> They determined that the Air Force had already processed three (totaling \$322,032) of the five invoices for payment. Reportedly, at the request of Hughes STX, Mr. Krenik had the Air Force withdraw the remaining two invoices (totaling \$20,800). Had Hughes STX followed through on Mr. Krenik's instructions, it would have eventually billed the government \$625,000; sent AQS (Mr. Krenik) \$500,000; and kept \$125,000 as markup.

On November 24, 1992, Hughes STX voided four U.S. Treasury checks (in payment of three of the five invoices) totaling \$322,032. On December 4, 1992, the Hughes STX Director of Contracting forwarded the four voided checks to the Air Force. The memorandum (see fig. 3) accompanying the returned checks indicated "that invoices . . . were prepared and submitted improperly." Hughes STX did not provide details to the government about the AQS/advance billing issues or Mr. Krenik's involvement.

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<sup>15</sup>The AQS invoice was purportedly a bill to the Air Force District of Washington/Accounting and Finance Office in the amount of \$500,000 for "renewal subscription for legislative consulting and analysis." The Hughes STX contract called for the delivery of hardware and software maintenance, technical support, and training.

<sup>16</sup>Hughes STX staff attempted to verify the existence of AQS with the telephone company and were advised that there was no such listing.

<sup>17</sup>Mr. Krenik attended at least one of these meetings.

Figure 3: December 4, 1992, Hughes STX Memorandum Concerning the Voided Checks

CERTIFIED MAIL

December 4, 1992

United States Air Force  
7CG/MSX, Room 1D164  
Pentagon, Washington, DC 20330

Attention: Ms. LaWanda Jackson

Subject: Contract Number F49650-92-D-0002,  
ASCAF Program

In Reply Refer To: DLS-339-01

Dear Ms. Jackson:

As previously discussed with the Office Automation Systems Support Branch Representative, Mr. Mark Krenik, Hughes STX Corporation (HSTX) has determined that invoices 921036, 921037, and 921038 were prepared and submitted improperly.

Accordingly, HSTX has voided and is returning herewith the following checks which were issued by the Government in response to said invoices:

<u>Check No.</u>	<u>Amount</u>
5037-09373803	\$ 27,412
5037-09373717	\$129,193
5037-09373743	\$ 90,575
5037-09373725	<u>\$ 74,852</u>
	\$322,032

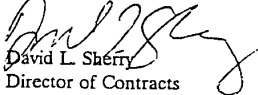
HSTX is currently reconciling its service reports and will resubmit invoices for FY92 activity in the near future. It is currently estimated that these billings will total to approximately \$180,000.

We apologize for any inconvenience this may have caused your office.

In the event you should have any questions concerning this matter, please contact the undersigned at (301) 794-5306.

Sincerely,

HUGHES STX CORPORATION

  
David L. Sherry  
Director of Contracts



HUGHES STX CORPORATION  
A Subsidiary of Hughes Aircraft Company

4400 Forbes Boulevard, Lanham, MD 20706-4392  
(301) 794-5000  
FAX: (301) 794-7106

## Mr. Krenik Defrauded the Government

In a separate scheme, Mr. Krenik, without contractor involvement, falsely invoiced the government for \$504,941.19; received checks at his personal post office box for the amount invoiced; deposited the moneys into

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accounts he controlled; and attempted to withdraw the funds. Suspicious bank officials notified the Secret Service. After being contacted by the Secret Service and in an attempt to conceal the fraud, Mr. Krenik wrote two checks and forged a contracting official's signature to an accompanying letter, stating that the invoices had been the result of billing errors.

On December 15, 1992, Mr. Krenik opened post office box 215 in Vienna, Virginia, in his own name. On December 24, 1992, Mr. Krenik delivered to the Air Force Finance Office 11 bogus invoices totaling \$504,941.19. Accompanying the invoices were the respective DD-250s, on which Mr. Krenik had falsely certified that work had been performed and deliveries made. Special instructions included on the invoices directed that payments be remitted to ST Systems Corporation at the Vienna, Virginia, post office box. The 11 invoices, the majority of which were dated October 22, 1992, provided the following information (see table 2) for the products or services purportedly rendered and billed.

Table 2: Mr. Krenik's 11 False Invoices

Invoice number	Description (quantity ordered)	Price
921051	Technical assistance	\$ 10,400.00
921052	Technical assistance	10,400.00
921053	Tempest serial mouse (23)	9,361.00
921054	Tempest serial mouse (4)	1,628.00
	25-foot Tempest serial cable	142.00
921055	Tempest color monitor (2)	5,130.00
	Tempest 386 CPU (2)	19,800.00
	140 MB hard drive (2)	4,066.00
	LIM EMS 4.0 (7)	252.00
	Technical assistance	101.19
921056	Power 6/32 disk controller (1)	3,993.00
	Installation	500.00
921058	Maintenance PPM	700.00
	Hourly maintenance	19,000.00
	Parts	5,835.00
921059	Training	27,250.00
921060	Principal programmer - 490 hours @ \$61/hour	29,890.00
	Hourly maintenance	24,800.00
	Parts	29,275.00
921105	Technical support	28,600.00
	Hourly maintenance	24,960.00
	Parts	21,144.00
921106	Technical support	199,899.00
	Hourly maintenance	13,954.00
	Parts	13,861.00
<b>Total</b>		<b>\$504,941.19</b>

Source: U.S. Air Force

On January 19, 1993, the Finance Office approved the 11 invoices for payment; and 3 days later, the checks were issued and mailed to post office box 215.<sup>18</sup> On February 4, 1993, Mr. Krenik deposited the \$504,941.19 into two Maryland National Bank accounts he had opened using the corporate names, Hughes STX and ST Systems.

<sup>18</sup>According to the accounting and finance certifying officer, it was policy at the time to make payments to the company and address indicated on an invoice (regardless of what the computer system indicated as the contractor's address). In addition, the accounting technician who prepared the payment packages told us that, at the time, many staff members had open access to the payment system and were able to alter payment addresses.

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When Mr. Krenik attempted to withdraw \$50,000 from one of the accounts on February 8, 1993, the bank teller became suspicious and notified her supervisor.<sup>19</sup> Mr. Krenik was told that the recently deposited checks had not cleared and he was allowed to withdraw only \$500. The next day, he tried to withdraw \$503,000 from the accounts at another Maryland National Bank branch and was advised that funds would be available in 2 days, on February 11, 1993.

On February 10, 1993, Maryland National Bank officials reported to the Secret Service their suspicions of possible fraudulent negotiation of U.S. Treasury checks. On February 11, 1993, in an interview conducted by the Secret Service, the Hughes STX Vice President of Finance disavowed all knowledge of the 11 invoices Mr. Krenik had submitted to the Air Force.

On February 12, 1993, investigators from the Secret Service and the Air Force Office of Special Investigations (AFOSI)<sup>20</sup> interviewed Mr. Krenik, at which time he admitted to having received 11 Treasury checks at his post office box and opening two accounts at Maryland National Bank from which he attempted to withdraw the funds he had deposited. Finally, Mr. Krenik gave written consent for investigators to search his vehicle. Incriminating evidence was discovered during the search, and Mr. Krenik declined to answer further questions.

On February 18, 1993, the 7th Communications Group, U.S. Air Force received two checks totaling \$504,941.19 (see fig. 4) and dated February 11, 1993, to be drawn from Mr. Krenik's corporate accounts at Maryland National Bank.<sup>21</sup> The letter (see fig. 5) accompanying the checks (also dated February 11, 1993, and purportedly written by the Hughes STX "Director of Contracting") noted that the funds were being returned because a review of past invoices had revealed overbilling errors. Mr. Krenik, in an effort to conceal the fraud, had written the letter and forged the Hughes STX Group Business Manager's signature.

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<sup>19</sup>The teller recognized Mr. Krenik as a long-time customer at that bank. She became suspicious because previously he had never had that much money in his accounts.

<sup>20</sup>Because Mr. Krenik was a civilian employee of the Air Force, the Secret Service brought AFOSI into the matter.

<sup>21</sup>These checks were not cashed. The moneys were returned to the U.S. Treasury after the case against Mr. Krenik was adjudicated in 1996.

Figure 4: Checks Dated February 11, 1993, Sent to U.S. Air Force by Mr. Krenik

HUGHES STX CORPORATION  
1577 Spring Hill Road  
Vienna, VA 22182

000102

11 February 19 93 <sup>7-16</sup>/<sub>520</sub>

PAY TO THE ORDER OF ADSN503701 \$ 459,968.00

Four Hundred Fifty-Nine Thou, Nine Hund Sixty-Eight and xx/100 DOLLARS

MARYLAND NATIONAL BANK  
BALTIMORE, MARYLAND 21202

FOR ASCAF Refund 2-11-93 Diane Whitmoyer

⑈000102⑈ ⑆052000168⑆ 0300487642⑈

ST SYSTEMS CORPORATION  
1577 Spring Hill Road  
Vienna, VA 22182

000102

11 February 19 93 <sup>7-16</sup>/<sub>520</sub>

PAY TO THE ORDER OF ADSN503701 \$ 44,973.19

Fourty-Four Thou, Nine Hundred Seventy-Three and 19/100 DOLLARS

MARYLAND NATIONAL BANK  
BALTIMORE, MARYLAND 21202

FOR ASOAS Refund 2-11-93 Diane Whitmoyer

⑈000102⑈ ⑆052000168⑆ 0300487634⑈

Figure 5: Bogus Letter Dated February 11, 1993, Accompanying the Checks

HUGHES STX CORPORATION  
1577 Spring Hill Road  
Vienna, VA 22182

7CG/MSX  
Ms. Wanda Jackson  
Room ID164  
Pentagon, DC 20330

February 11, 93

Dear Ms Jackson,

A review of some past invoices that were submitted to 7CG/GABB revealed some mistakes in these billings. Mr Mark Krenik from 7CG/GABB discovered these mistakes and brought them to our attention. The incorrect invoices amount to \$44,973.19 of overbillings from the ASOAS contract, and \$459,968.00 of invoices that need to be redone from the ASCAF contract. To correct this matter, we are returning these payments to you now, and will resubmit the corrected ASCAF invoices in the future.

If you have any questions about these invoices please contact Mr Mark Krenik of 7CG/GABB, at ext 42564.



Diane Whitmoyer  
Director of Contracting

Refund Checks Enclosed

## Corporate Internal Investigation

After contact by the Secret Service, Hughes and its parent, General Motors Corporation, conducted an internal investigation. We were advised that the internal investigation of the Krenik matter revealed that Hughes STX was not timely in notifying government officials regarding Mr. Krenik's bogus AQS invoice and the improper billing for services not rendered. General Motors also determined that Hughes STX had been deficient in providing its employees required ethics training, which includes instruction on the prompt reporting of questionable or improper activities.

## Methodology

We conducted our investigation from October 1997 to August 1998. We interviewed Air Force personnel and contractor staff who had knowledge of the circumstances surrounding the Krenik matter. In addition, we reviewed records maintained by the Department of Defense (Air Force



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contracting, AFOSI, and the Air Force Audit Agency); Hughes STX (now Raytheon STX); the Department of the Treasury (U.S. Secret Service); and the Department of Justice, Office of the U. S. Attorney, Eastern District of Virginia. Mr. Krenik declined our request for an interview. During the course of our investigation, we referred irregularities that we uncovered regarding the Hughes STX contracts to the Defense Contract Audit Agency and the Office of Inspector General, Department of Defense.

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As agreed with your office, unless you announce its contents earlier, we plan no further distribution of this report until 30 days after the date of this letter. At that time, we will send copies of the report to interested parties and make copies available to others upon request. If you have any questions concerning this report, please contact me or Assistant Director David Buckley at (202) 512-6722. Major contributors to this report are listed in appendix II.

Sincerely yours,

A handwritten signature in black ink, reading "Eljay B. Bowron". The signature is written in a cursive style with a long, sweeping underline.

Eljay B. Bowron  
Assistant Comptroller General  
for Special Investigations

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## Abbreviations

AIMD	Accounting and Information Management Division
AQS	Applied Quantitative Systems
DFAS	Defense Finance and Accounting Service
GAO	General Accounting Office
OSI	Office of Special Investigations

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# Examples of Fraud Cases Involving the Defense Finance and Accounting Service Between 1991 and 1998

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Following are summaries of 13 cases of fraud involving the Defense Finance and Accounting Service (DFAS). These case summaries from the Defense Criminal Investigative Service, Air Force Office of Special Investigations, and Naval Criminal Investigative Service exemplify the types of internal crimes that have beset various Department of Defense financial systems. The schemes usually entailed creating or altering documents (e.g., claims, travel vouchers, invoices); forging signatures; or establishing false accounts for fictitious people or companies. For the most part, the perpetrators were able to receive funds by having checks sent to post office boxes or street addresses the perpetrators controlled or by having checks sent electronically to controlled bank accounts. In the examples discussed, just over half of the crimes were discovered by coworkers or other internal sources. Others were uncovered by external sources and through internal control systems.

1. A military clerk in an accounting and finance office at Hanscom Air Force Base (AFB), Massachusetts, embezzled more than \$316,000 by altering previously paid contractor claims and resubmitting them for payment. The clerk obtained a fictitious business license and opened a business bank account under the fictitious business name on the claim forms. He had the claims checks sent to a post office box from which he retrieved them and deposited them into the fictitious business bank account. The clerk's wife discovered the scheme and threatened to report the theft. The clerk later confessed the embezzlement scheme to a coworker. In September 1996, the clerk was convicted at a general court-martial, receiving a dishonorable discharge and a 6-year prison term. He was also fined \$296,000.

2. A retired Navy chief petty officer and former Civil Service merchant mariner served as a supply officer aboard Military Sealift Command ships. Between January 1989 and December 1992, he defrauded the U.S. Navy of over \$3 million. He filed bogus invoices for materials allegedly supplied to the Military Sealift Command by a company that did not exist. DFAS mailed payments to a Norfolk, Virginia, post office box. His fraud was uncovered when someone noted that shipments and services were going to decommissioned ships. Indicted on 430 counts in 1994, he was sentenced to 87 months in prison (without parole) and 180 months probation. He was also ordered to pay \$3,025,000 in restitution and \$250 in a special assessment.

3. A civilian accounting technician at Bolling AFB, Washington, D.C., embezzled approximately \$32,000 by altering authentic travel vouchers.

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**Appendix I**  
**Examples of Fraud Cases Involving the**  
**Defense Finance and Accounting Service**  
**Between 1991 and 1998**

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She changed the names and Social Security numbers (SSN) slightly, then electronically transferred the funds to her personal bank account. Individuals who had not been paid resubmitted their vouchers and were paid, since records with the actual names and SSNs indicated nonpayment. The scheme was discovered when an employee called to complain about nonpayment of his travel voucher. Another technician saw the similar name and SSN, connected the transaction to the perpetrator, and informed law enforcement. When authorities investigated the perpetrator's transactions, they found a pattern of similar payments. In December 1996, the accounting technician was convicted in federal court and received 5 years probation. She made restitution amounting to \$29,325 and voluntarily resigned her position.

4. On three occasions at the Air National Guard Station, Birmingham, Alabama, a military comptroller fabricated payment vouchers using fictitious contract numbers and fictitious contractor names, resulting in \$118,000 being sent to a bank account that the comptroller controlled. An accounting technician uncovered the scheme when he noted a discrepancy in the records. In January 1996, the comptroller was convicted in federal court, ordered to pay \$128,000 in restitution, and sentenced to 18 months in prison.

5. A military supply clerk at the Norfolk, Virginia, Naval Station submitted false claims to the Navy for supplies or services under the names of four legitimate companies and one that he had registered for the purpose of his fraud. All invoices were bogus, as no materials or services were ordered or delivered. He was discovered when the Norfolk Police Department, which was investigating him concerning the sale and/or possession of narcotics, seized his computer and found bogus invoices. The Norfolk police reported the matter to the Naval Criminal Investigative Service as a possible fraud. In May 1997, the clerk was sentenced to 13 months confinement and 2 years supervised-release probation. He was also ordered to make full restitution of \$83,576.63 to the Navy and to pay a \$50 special assessment fee.

6. A military travel pay technician embezzled more than \$17,000 on each of three occasions at Kadena Air Base, Japan, for a total of approximately \$51,000. He obtained permanent change-of-station advances under a false name by altering authentic travel orders, thus generating standard travel advance requests. The technician possessed the necessary passwords to authorize each advance and have them sent electronically to the technician's bank account. A civilian technician discovered the false travel

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orders, and the matter was referred to law enforcement. A review of documents at the military technician's former duty station disclosed that the technician had committed fraud at that location as well. In June 1996, the technician was convicted at a general court-martial and received a dishonorable discharge. He was sentenced to 36 months in prison, was reduced in rank, and paid \$10,000 in fines and \$48,000 in forfeiture.

7. It is alleged that a finance office technician—at Bolling AFB—attempted to embezzle at least \$22,800 by filing a fraudulent travel voucher under a fictitious name and having the funds sent to the technician's bank account. The technician asked a coworker to input the voucher. The coworker thought the request was strange and reported it to a supervisor. The supervisor failed to recognize the voucher's fraudulent nature and proceeded with its processing. DFAS rejected the voucher due to an error in the electronic filing transfer address. The supervisor sent two letters to the address on the voucher to notify the claimant of the problem. Both letters were returned, marked "Return to Sender, No Such Street." The supervisor forwarded the voucher to DFAS twice more; DFAS finally processed a check for payment and attempted to send it to the address with the same results as above. A source notified law enforcement of the unusual transaction. The case is pending adjudication.

8. Between December 1991 and August 1993, sixty-two unauthorized payments, totaling approximately \$271,000, were fraudulently issued and cashed by two employees of the DFAS Indianapolis, Indiana, Center. Checks were issued in the names of various U.S. military retirees but were sent to addresses controlled by the two perpetrators. The checks were forged and negotiated using false identification at various check-cashing establishments. Subsequently, the two employees recruited others to participate in the fraud scheme. The checks made payable to the recruited individuals were negotiated at banks, and the recruits received a percentage of the proceeds. A complaint from a retiree who questioned the income amounts that the military had reported to the Internal Revenue Service triggered a review of payment operations. The investigation resulted in the conviction of 12 individuals for theft of government funds. The sentences ranged from probation to 18 months incarceration. Approximately \$80,115 was recovered.

9. Between 1994 and 1997, a military member and a private citizen allegedly embezzled approximately \$938,000 from the DFAS Dayton, Ohio, Center. The military member was a supervisor of data entry personnel in the vendor pay section and allegedly created fraudulent invoices and

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checks made payable to the private citizen. They then allegedly divided the proceeds. A technician who had no part in the scheme noticed a check made out to the private citizen for \$210,000 when she was trying to discover the source of an automated input error. The check was suspicious, as it was for a large amount made payable to an individual rather than a business and the transaction did not match a valid contract. The private citizen pleaded guilty to one count of conspiracy to steal government funds, but no sentencing date has been set. The military member was found guilty of attempted larceny, conspiracy, and violation of Article 134 of the Uniformed Code of Military Justice and was sentenced to 12 years in prison.

10. Between October 1994 and April 1997, a military pay supervisor and a private citizen at Fort Myer, Virginia, schemed to embezzle approximately \$169,000 of government funds. The supervisor established a payroll account in the name of a fictitious military member. The supervisor used the ghost payroll account<sup>22</sup> as a basis for issuing 57 electronic fund transfers to bank accounts controlled by the perpetrators. Sources outside DFAS reported the scheme. The supervisor pleaded guilty to theft of government funds and was sentenced to 21 months incarceration, 3 years probation, and \$168,872 in restitution. According to the Department of Defense's Inspector General report, had responsible DFAS employees followed established procedures by comparing payroll information to personnel data on a monthly basis, they could have detected the fraud themselves.

11. In late 1995, a civilian employee of the DFAS Cleveland, Ohio, Center diverted \$11,000 by using electronic funds transfers to a bank account controlled by the employee and an accomplice. The employee diverted military retirement benefits by issuing two separate "one-time credit" allotments, thus triggering the electronic transfer. The employee withdrew the diverted funds. The fraud was discovered as a result of a DFAS internal control that automatically generated reports on payments over a predetermined amount. When the report was reviewed, DFAS personnel questioned the payments. The employee was convicted of embezzlement and making false statements and was sentenced to 1 year and 1 day incarceration, 3 years probation, restitution of \$6,520, and a special assessment of \$100. The accomplice pleaded guilty to aiding and abetting the theft of government funds and was sentenced to 6 months home

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<sup>22</sup>In July 1993, we testified that the Department of Defense had not responded effectively to many long-standing problems, including those involving ghost employees. (Financial Management: DOD Has Not Responded Effectively to Serious, Long-standing Problems, [GAO/T-AIMD-93-1](#), July 1, 1993)

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confinement, 3 years probation, restitution of \$1,200, and a special assessment of \$50.

12. Between October 1994 and January 1996, a civilian DFAS accounting technician embezzled \$28,940 in funds from DFAS - Tinker AFB, Oklahoma. The technician falsified educational expense vouchers using his wife's name as the payee and his own mailing address. The technician attached used copies of supporting documents from legitimate vouchers to support the fraudulent vouchers, knowing the certification official would not verify the expenses or the identity of the claimant. The technician cashed the checks and used the proceeds to pay debts. The scheme was discovered after a confidential source provided information to law enforcement. The technician pleaded guilty to one count of mail fraud and was sentenced to 90 days incarceration and 5 years probation. He was required to pay \$29,990 in restitution and a special assessment.

13. In 1991, two military members assigned to the DFAS Indianapolis Center conspired with seven individuals to receive approximately \$37,000 in fraudulent benefits paid to beneficiaries of military personnel killed during Operation Desert Storm. One military member created the necessary paperwork within DFAS to issue a check against the accounts of deceased U.S. service members. The other military member recruited seven individuals to receive the fraudulent checks. These seven individuals each received a minimal portion of the proceeds for facilitating the embezzlement. The scheme was discovered as a result of an anonymous call to law enforcement. Four members of the scheme, including the two military members, were indicted and convicted of theft of government funds and sentenced to up to 6 months "community confinement" and 3 years probation. They were ordered to pay up to \$16,350 in restitution and special assessments. The remaining participants who had been implicated in the scheme were not prosecuted in exchange for their cooperation.



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