



Owners and Contractors Beware! Electronic Payments in Construction Are Subject to Increased Fraud

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While electronic funds transfer is considered a convenient and quicker way to process payments and receive funds on construction projects, this practice presents significant risk to project participants. Contractual and processing controls are necessary to prevent fraud, which is on the rise locally and nationally.

The construction industry, not surprisingly, continues to be a prime focus for fraudulent internet and email schemes, spear phishing tactics, and other sophisticated scams designed to direct funds from the contractor's intended account into an account created to permit swift transfers of funds overseas. Construction projects undoubtedly are targeted because they routinely involve large monthly billings for labor, materials, and equipment. Furthermore, many large projects are the subject of press releases, media coverage, and public and internet marketing campaigns that make it easy to identify projects, owners, and funding sources. Additionally, social media accounts and corporate websites easily permit perpetrators of fraud to identify payables and other accounting personnel for purposes of targeting emails.

Fraudulent schemes vary widely, but they all move rapidly. Thefts range in value from tens of thousands to multi-million dollar losses. In most instances, by the time the scheme is discovered, and the absence of funds are reported, there is limited ability to track most, if not all, of the funds from the United States through China, Russia, North Korea and other countries.

The thefts can be devastating because, among other things, insurance typically limits dollar amounts covered and insurers cannot reimburse stolen funds fast enough to avoid project impacts. Likewise, lenders disclaim responsibility for reimbursement of funds to the extent that the payor directed the funds be sent to a specific account, and the lenders also expect repayment on loans regardless of the thefts. Therefore, the thefts directly impact project budgets and future funds availability, jeopardizing project completion.

Payment disputes frequently result as parties argue to assign culpability. Meanwhile, payments to contractors, suppliers, and vendors that furnished work and materials typically are unreasonably and, sometimes, indefinitely delayed. In some instances, the immediate involvement of state and federal law enforcement may track funds before they clear United States accounts, but such recovery fails to successfully resolve most payment issues.

Project participants need to consider and implement project controls. In addition to educating accounting employees of these schemes and implementing basic audit principals and process controls, the parties should consider specific contract terms covering (i) who may authorize a change in payment process or deposit accounts; (ii) how requests to change payment processes or accounts must be sent and how they must be specifically confirmed; (iii) who bears responsibility for losses; (iv) who shall procure and maintain available insurances; and (iv) re-confirmation of account numbers and payments before transfers and electronic funds transfers occur.



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