

THE FACT OF THE MATTER: NONPROFIT FRAUD



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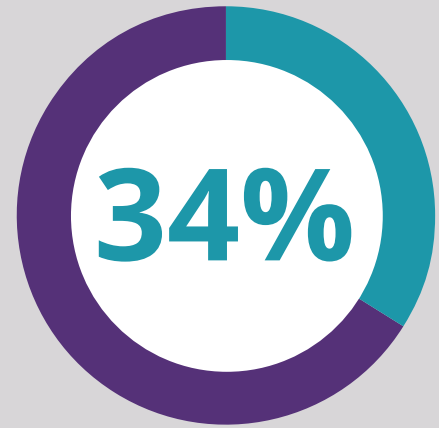
NonProfit Fraud

A Real Concern for Organizations

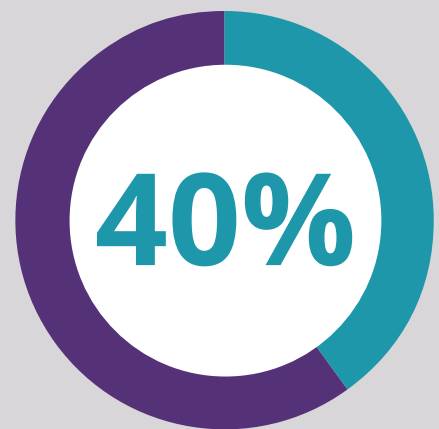
Fraud is a very real concern for nonprofits. According to the [2016 Nonprofit Finance Study](#), 34 percent of nonprofit finance professionals feel their organization undertakes actions that may put it at risk for fraud, and only 40 percent say their organization puts some or minor effort into helping prevent fraud.

Dig deeper into the topic of nonprofit fraud awareness and prevention with intel and insight from two leading experts in the field of nonprofit fraud.

From preventing fraud, to surviving the aftermath, to every protocol, process, and best practice in between, your organization can never be too prepared.



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Fraud Myths Uncovered

MYTH 1

Fraud rarely happens

Debunked: In reality, fraud at nonprofits happens more often than you might think. Many nonprofits keep this quiet, so as not to create a stigma for the organization or deter potential donors.

MYTH 2

Only “bad” people commit fraud

Debunked: Unfortunately, the reality is good people can still do bad things, driven by necessity, greed, or opportunity.

MYTH 3

We only hire good people, so that won't happen to us

Debunked: No one intentionally hires someone who will commit fraud, and it may be hard to spot the signs of a perpetration until it's too late.

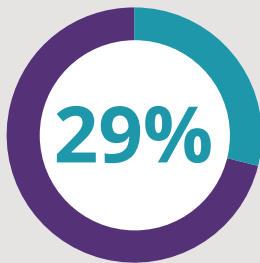
MYTH 4

Audits easily and always catch embezzlement and fraud

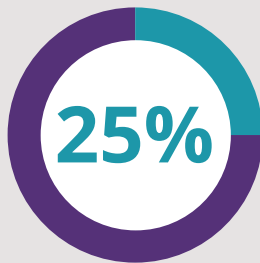
Debunked: While audits can at times help identify fraud, they aren't specifically designed to uncover fraud.

Stats from the Association of Certified Fraud Examiners 2016 Global Fraud Study:

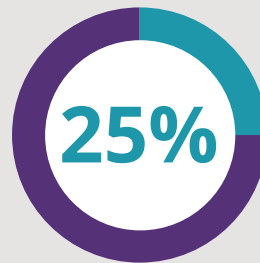
Top fraud schemes at nonprofits:



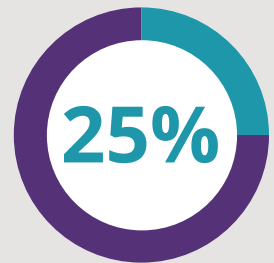
Corruption



Billing



Expense Reimbursements



Check Tampering

Preventing Fraud: Being Proactive Versus Reactive

Awareness

- Open lines of communication and ongoing dialogue are key. Ignoring fraud won't deter it.
- Board members, management, staff, and volunteers should all be involved in the conversation, feel safe to express concern, and be aware of what the red flags are.

Involvement

- Fraud preparedness is not a one man (or woman) show.
- Board members hold a fiduciary responsibility.
- Management holds responsibility and oversight.
- Staff and volunteers have a hand in responsibility.
- All have a duty to be aware and to inform.

Understand Risk

- Talk about specific risks YOUR organization may face, based on YOUR business operations, vendors, employees, service providers, and transaction activity levels.

- When it comes to significant operations and activities (for example, handling money or cutting checks to vendors), ensure key finance staff members know the answers to these questions:

- ▶ How does this process work?
- ▶ Who is involved in this activity, both inside and outside the organization?
- ▶ Who initiates transactions?
- ▶ Who authorizes transactions?
- ▶ Who reviews transactions?
- ▶ Have we had anything go wrong here before? Why did it go wrong? What can we do to ensure the process and outcome are correct?
- ▶ How are staff members in the department feeling and functioning?

Auditors are required to specifically ask about fraud, and responses can be telling!

Auditors typically look at:

THE WHAT

Is management and the board really considering the potential for fraud when assessing risks to the achievement of goals and objectives?

THE HOW

Are they considering various types of fraud and continually assessing incentives, pressures, opportunities, and attitudes that may lead to fraudulent behavior within the organization?

THE TRAIL

How do we actually know if and when fraud occurs? Auditors dive into meeting minutes, policies and procedures, governance inquiries, and discussions with management and staff.

Reducing Fraud Risk: Fostering a Fraud-Free Environment

The Team

Make it a goal at your organization to have a fraud- and fear-free culture.

- Foster an environment of awareness, information, open communication, kindness, and trust.
- Put policies in place, including whistleblower policies and HR policies, and keep your employee handbook up to date.

The Talk

Stay aware, and don't be afraid to talk about fraud (before the money walks out the door).

- **Attitude** – Maintain awareness and safety in communications.
- **Plan of Action** – Have a crisis management plan and disaster recovery plan that includes all of the who, what, when, where, and how to deal, should fraud ever take place.
- **Fraud Drill** – Actually simulate fraudulent behavior (fictitious vendor, fake transaction) within your fund accounting system to see what it looks like when it goes through, discover how easy it might be, understand what controls/ processes may need to be put in place, and how to spot potential future fraudulent behavior within the system.
- **Forward-Looking** – Be alert and aware of how to handle fraud prevention if your organization gains opportunities for larger fundraising programs, increases in funding streams, etc.

The Technology

The right technology can help an organization be both proactive and reactive when it comes to detecting and deterring fraud.

- Create thorough and accurate audit trails.
- Promote sound accounting policies and procedures.
- Use built-in functionality to assign users, permission rights, alerts, and more.
- Support and promote proper segregation of duties.
- Take advantage of robust reporting tools to dig deeper and investigate suspicious behavior further, if needed.



Finding Fraud:

Spotting the Signs and Knowing What to Look For

Who Commits Fraud?

- The Fraud Triangle: Perceived pressures/ incentives, Opportunity, Rationalization.
- Anyone around you or even sitting next to you at work (fraud perpetrators don't fit any particular mold).

Why Does Someone Commit Fraud?

- An opportunity for fraud is perceived by an individual:
 - ▶ Individuals who perceive they have a need and intend to pay it back later
 - ▶ Individuals who feel they have been treated unfairly by their employer
 - ▶ Individuals who are angry at their employer
 - ▶ Individuals who feel they deserve it
 - ▶ Individuals who may have a need, based on addiction (for example, lottery, gambling, etc.)
 - ▶ Outsiders who trick staff into sending them money for their own personal benefit or as part of a scam

Types of Nonprofit Fraud

- Revenue and cash receipts schemes, via skimming or theft of donated merchandise
- Purchasing and cash disbursement schemes, such as credit card abuse, fictitious vendor schemes (fake company and fake invoices), and payroll and employee expense reporting schemes (ghost employees, overstatement of hours, fictitious expenditures on reimbursement reports)
- Other asset misappropriations, such as property and equipment schemes, personal use of organization assets and resources, fraudulent billings by vendors, unauthorized use of funds, fraudulent grant expense reporting, etc.
- Fraudulent financial reporting, such as misclassifying restricted donations, misclassifying expenses to mislead donors or grantors, failing to correctly report asset and liability balances, etc.



Surviving Fraud: The Aftermath of Fraud

First steps after finding possible fraud:

- ▶ Consult legal counsel (do not confront the individual who you believe committed the fraud until after consulting with legal counsel)
- ▶ Inform your insurance carrier
- ▶ Preserve any documents or other evidence
- ▶ Correct the system that allowed the fraud to occur
- ▶ If instructed by legal counsel, inform law enforcement

Tips to managing a fraud crisis:

- ▶ Remain calm, do not over react
- ▶ Check to see if your organization has a whistleblower policy; if so, follow it
- ▶ If no whistleblower policy, then engage only people who are your superiors, unless they are the suspect, then only engage those who supervise the individual
- ▶ If you're in charge, engage your professionals to verify your suspicions of the fraud
- ▶ If you work at a large organization, you may want to engage a public relations firm



About the Authors



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Dena Jansen is the Lead Client Service Partner for the nonprofit niche at Maxwell Locke & Ritter. She serves as an audit partner and trusted business advisor to the nonprofit industry with a focus on facilitating technical and nontechnical training to internal associates, clients, and external groups. With more than 13 years in public accounting, Dena enjoys creating connections for others, and is proud to serve on boards in her community.



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