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REDUCING RISK

Ten Ways to Detect and Prevent Fraud in Nonprofits

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This article was originally published on March 9, 2015. It was updated to reflect the 2016 statistics related to fraud occurring in religious, charitable, and social services organizations. It is important to note that the majority of cases involved fraud related to billing, check tampering, corruption, and expense reimbursements.

The culture of most nonprofits is based on trust, honesty, and a commitment to the public interest. But a noble mission and sparkling public image are not bullet-proof protection against fraud. According to the Association of Certified Fraud Examiners’ (ACFE) 2016 Report to the Nations, while only 2.4 percent of fraud found in 2016 was attributed to religious, charitable, and social services organizations, the median fraud loss for these groups was $82,000.

For an organization already operating on a shoestring, such a loss could spell disaster.

That’s why administrators, boards of directors, and financial managers need to be proactive in their approach to detecting and preventing fraud. Most of the actions that follow carry a price tag, so fraud prevention usually begins with the setting of goals, priorities, and budgets.

“The Association of Certified Fraud Examiners (ACFE) defines occupational fraud as, “The use of one’s occupation for personal enrichment through the deliberate misuse or misapplication of the employing organization’s resources or assets.”
1. Hire the right people.

Although the majority of fraud perpetrators are first-time offenders, weeding out the criminally inclined is not impossible. A great deal can be learned from a candidate’s references, work history, credentials, pre-employment drug testing, and criminal background checks. If nothing else, background checks put job applicants on notice that the organization values integrity.

2. Develop a formal fraud policy and code of conduct.

Put policies in writing and have all employees sign documents saying they will follow the rules. This is an area where you will probably want to work with an attorney to make sure you’re staying within the law.

3. Prosecute offenders.

Cost and fear of notoriety keep some organizations from exposing fraud and taking legal action, but lax attitudes make it that much easier for the next person to commit fraud without fear of reprisal.

4. Establish internal controls.

Controls can be preventive or detective. Preventive controls might include keeping blank check stocks under lock and key, setting authorization limits, and requiring multiple signatures on checks. Detective controls include having an independent employee reconcile bank statements, surprise inventory counts, and independent reviews of accounts payable lists.

5. Require vacation and job rotation.

When an employee stays in the same position for a long period, or never takes a vacation, there are ample opportunities for that person to design, commit, and conceal fraud. Mandatory vacations and job rotation make it difficult for an employee to continue concealing a crime.

6. Create a whistleblower’s hotline.

Studies show that most frauds are initially detected through tips from employees, clients, and outside vendors. The reporting system should be anonymous, managed by a third party, and available 24/7. This service doesn’t have to break the bank, either. Some vendors charge as little as $500 a year for a hotline.

7. Educate employees and volunteers.

Employees and volunteers are the eyes and ears of your organization, but they can’t report fraud if they don’t know what it is. For a moderate investment, you can locate self-training resources online. If the budget allows, send employees to training or conduct internal training on a regular basis.

8. Discourage a “win at all costs” attitude.

Keep the organization’s purpose and mission at the center of everything. Undue pressure to meet goals, or an overly generous bonus structure, can lead employees to bend the rules, falsify
records, or commit other offenses in order to meet expectations.

9. Institute appropriate personnel policies and procedures.
Employees might commit fraud because they have been passed over for a promotion, believe they have been underpaid, or are otherwise treated unfairly. Make sure that all policies are applied equally and fairly.

10. Provide counseling services.
An employee assistance program or similar outreach initiative can help prevent fraud by providing professional help with personal problems such as alcoholism, drug abuse, marital problems, and gambling.

How we can help
Preventing fraud can be costly, but it’s not necessarily unaffordable and you don’t have to do it all at once. Prioritize this list so it makes economic and organizational sense for your nonprofit. We can help you set goals, analyze your resources, and take action toward an effective solution.

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