

IS NONPROFIT FRAUD ON THE RISE?

The Problem...The Impact...The Solutions

Presented to the
Finance and Administrative Roundtable
by Gary R. Snyder
The Nonprofit Imperative
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Learning Objectives

1. Identify the extent and trajectory of the fraud and embezzlement problem in the nonprofit sector
2. Recognize the warning signs associated with a potential fraudster
3. Determine the role of leadership and staff in preventing fraud
4. Apply preventative measures for reducing fraud

Is Nonprofit Fraud on the Rise?

The Route for Today

- Nonprofit Sector Overview
- Public's View
- Fraud Facts
- Fraud Examples
- Why Does It Occur
- Solutions
- Moving Forward
- Your Thoughts

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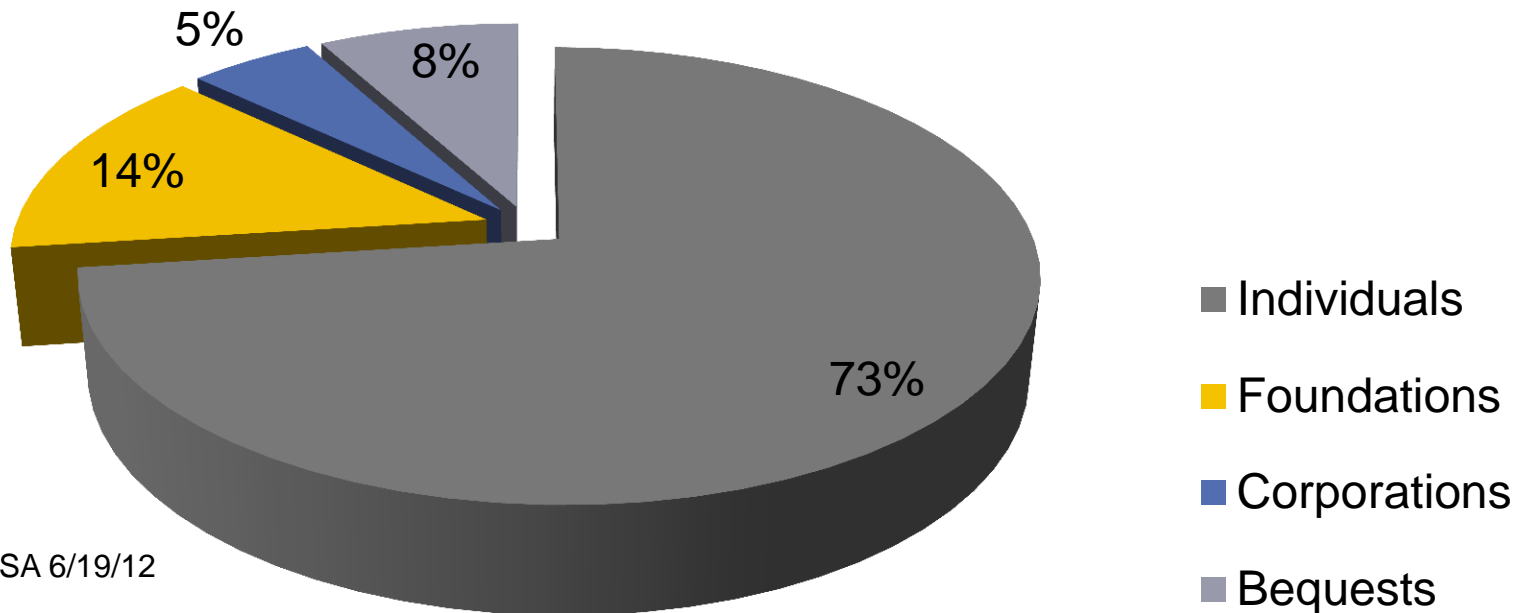
Nonprofit Sector Overview

- 10% of all Salaries and Wages = \$670 Billion
 - 13 Million Employees
 - 5.4% of GDP

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Nonprofit Sector Overview

2011 Giving = \$298.4 Billion*

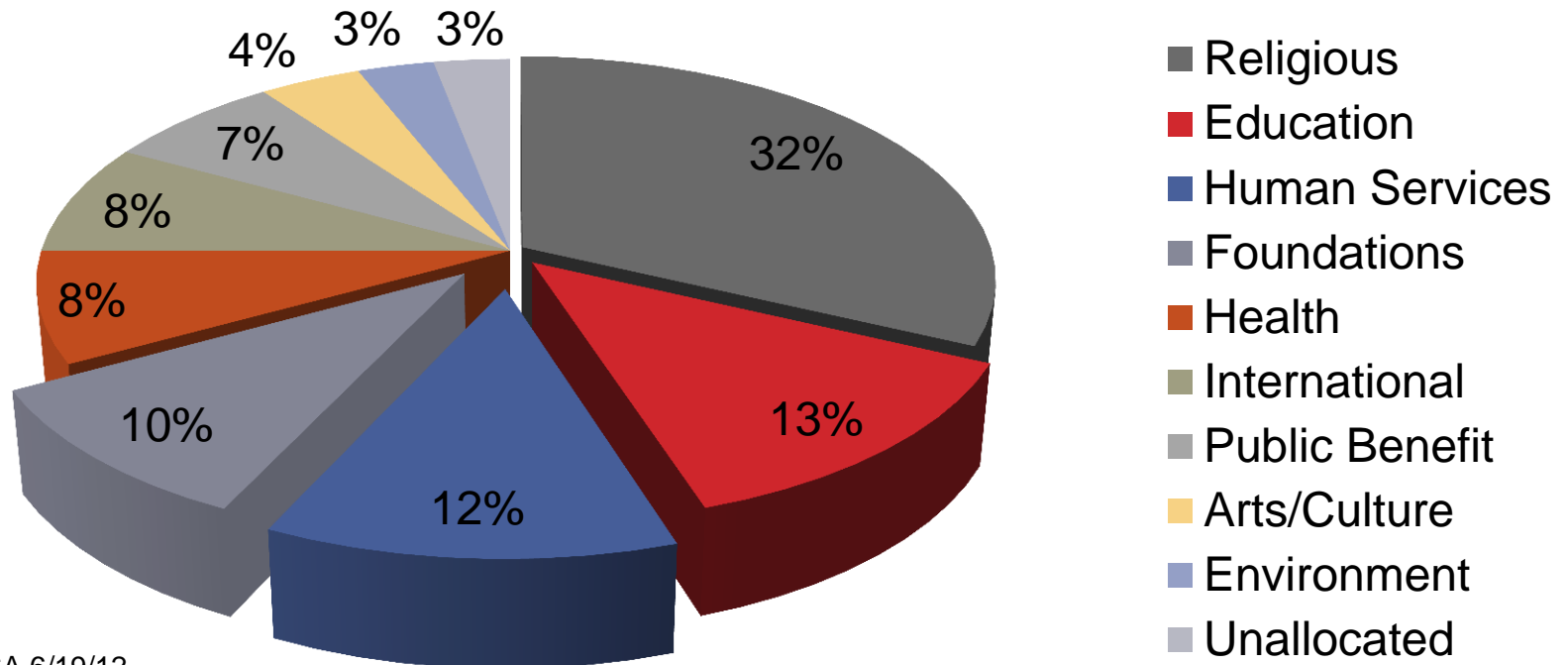


*Giving USA 6/19/12

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Nonprofit Sector Overview

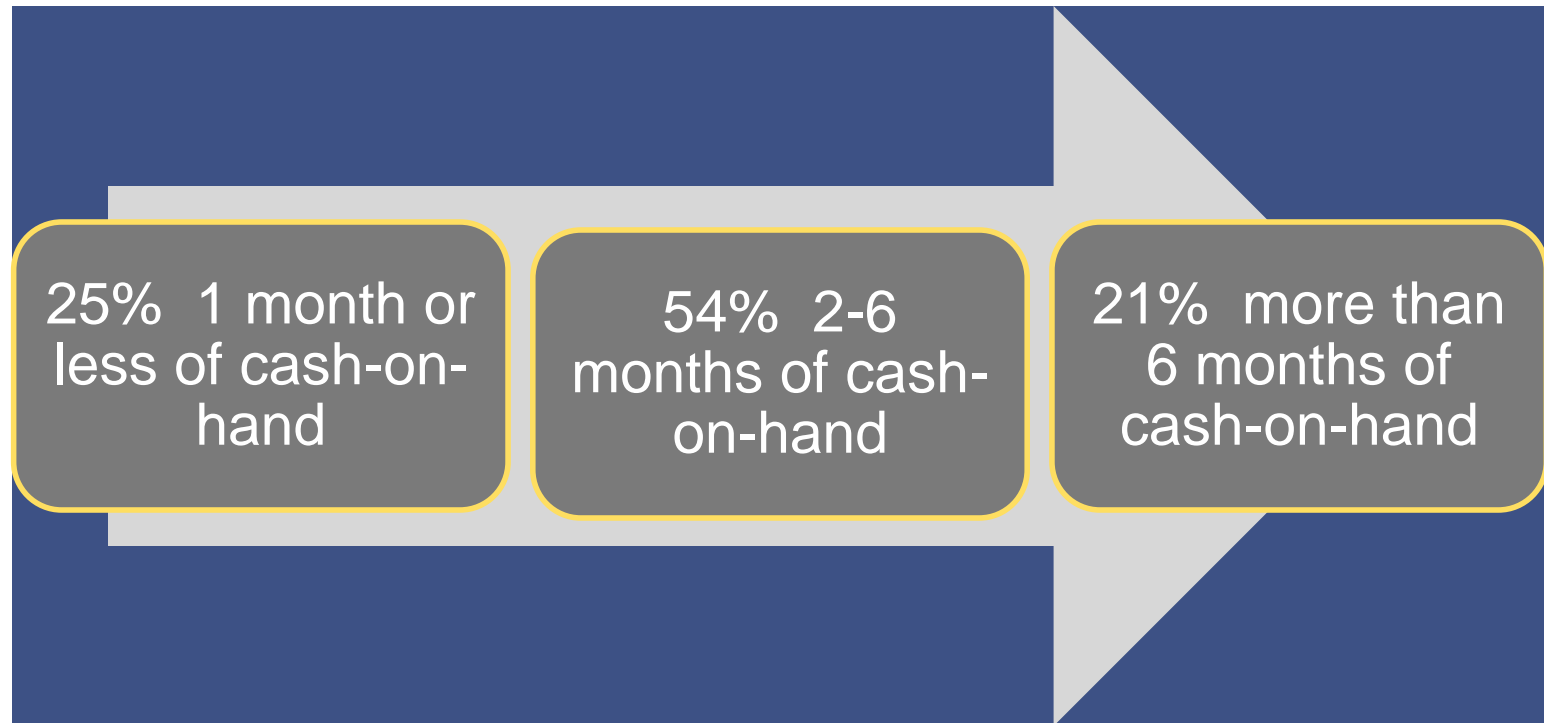
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Nonprofit Sector Overview



- Nonprofit Finance Fund 2012 State of the Sector Survey Results (3,944 Respondents)

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Public's View

- 18% Trust charitable decisions - NYU Study
- 32% Have less than a positive feeling – Harris Poll
- 62% Do not like how funds are spent – Ellison Research
- 79% Would not give if donor's wishes betrayed – Zogby Poll
- Nonprofits are declining ethically – Ethics Resource Center
- There is significant diversion of charitable assets - IRS

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Fraud Facts

Charity fraud is one of the two areas that continue to escalate. The other is financial sector fraud.”

Marquet Report on Embezzlement, 1/17/12

Research shows that theft in the nonprofit sector accounts for 13% of annual donations or about twice the ratio of fraud in the for-profit sector. Do More Than Give, Mark Kramer, 2011

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Fraud Facts

Annual Estimated Charity/Nonprofit Fraud

\$40 Billion* in 2007

Nonprofit and Voluntary Sector Quarterly/New York Times

\$51 Billion* in 2010

Inspector General for Texas

\$67 Billion* in 2011

The Nonprofit Imperative/ACFE

**Estimates*

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Fraud Facts

- Reported frauds lasted a median of 18 months before detection
- The smallest organizations suffered the largest median losses
- Owners/Executives committed median losses at \$573,000
- Managers caused median losses of \$180,000
- Employees caused \$60,000 in median losses
- Approximately 87% of occupational fraudsters are first-time offenders

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Fraud Facts

- Occupational fraud is more likely to be detected by a tip than any other method
- 77% of frauds were committed by individuals in one of 6 departments: accounting, operations, sales, executive/upper management, customer service and purchasing
- In 81% of cases, fraudsters displayed one or more behavioral red flags:
 - ✓ Living beyond means – 36%
 - ✓ Financial difficulties – 27%
 - ✓ Close association with vendors/customers -19%
 - ✓ Excessive control issues – 18%

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Fraud Facts - Outcomes

- 40-50% of victim organizations do not recover any of their fraud losses*
- Only 29% of perpetrators received criminal or civil charges**
- Just 16% were incarcerated or received probation**
- Only 3% resulted in fully-paid restitution**
- Just 4% resulted in partial restitution**

• *ACFE 2012 Survey

• **IRS Diversion/Governance Study 2012

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Fraud Facts - Outcomes

- Limited Enforcement By:
 - ✓ Congress
 - ✓ Internal Revenue Service
 - ✓ State Attorneys General
 - ✓ Watchdog Agencies
 - ✓ Sector Leadership
 - ✓ Other Gatekeepers

Media has been the chief exposor of fraud

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Fraud Examples

Food Charity in Georgia

- Excessive executive compensation - \$69K to \$588K in one year
- Undocumented travel - \$1.08M
- Substantial insider transactions
- Lack of standard operational policies
- FBI investigation
- Media uncovered fraud

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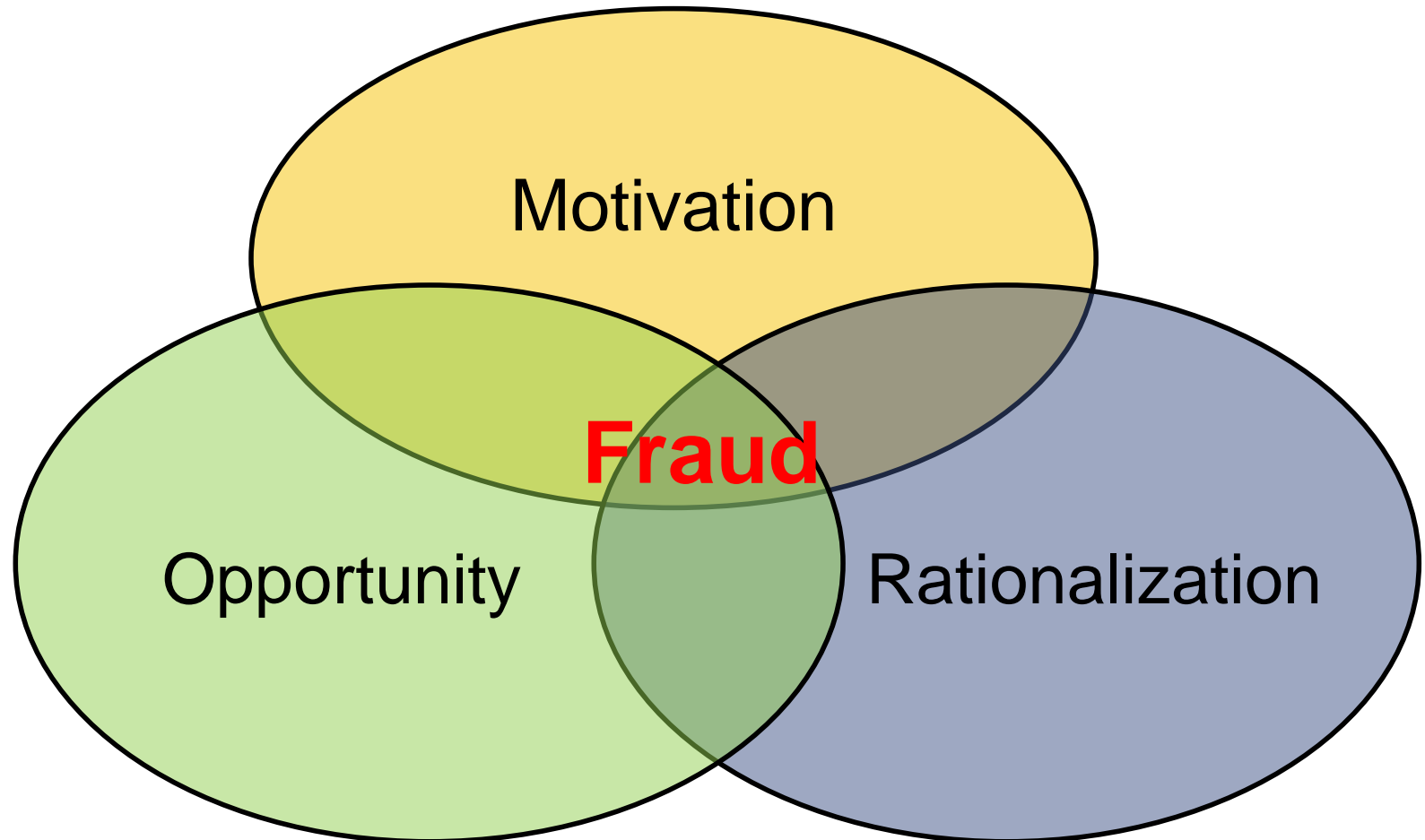
Fraud Examples

Religious Institution in New York

- Payroll manager in accounting department
- No background check (two previous convictions)
- Issued 468 checks under supervisory approval limit of \$2500
- Fraud undetected for 7 years
- Funds used to buy expensive items

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Why Does It Occur



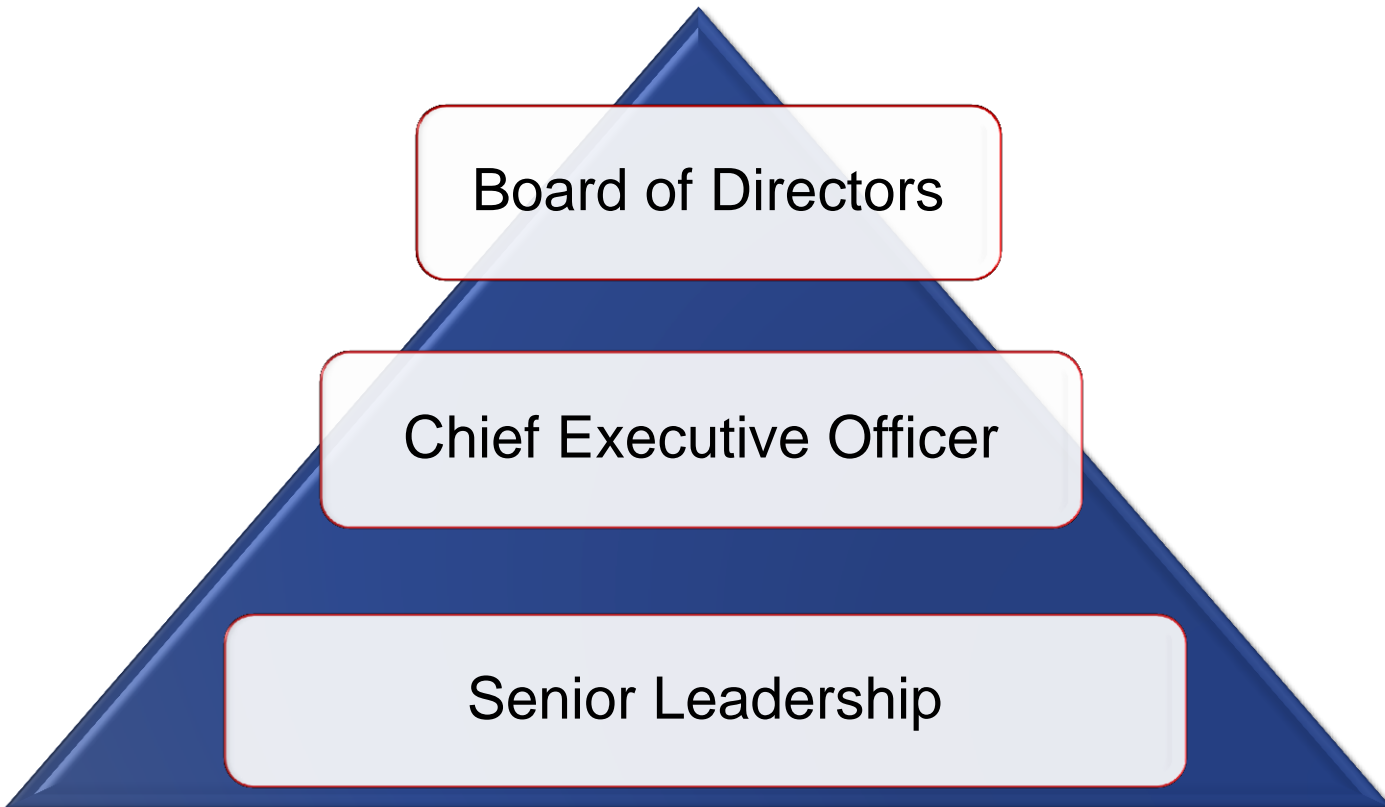
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Why Does It Occur

- Management and Board of Directors are more trusting
- Smaller staffs limit segregation of duties
- Limited resources for internal controls and anti-fraud programs
- Belief that audits will catch the fraud

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Solutions: Tone is set from the top



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Board Solutions

- Sound financial and legal decisions
- Professional interests over personal interests
- Understand implications of financial statements
- “Beef up” the expertise/skill set for Board membership

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Internal Solutions

Comprehensive compliance program with:

- A Code of Ethical Behavior
- Proactive Oversight and Control
- Regular Education and Training
- External and Unexpected Audits

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Internal Solutions – Some Specifics

1. Dual signatures and layers of approval
2. Back-up documentation
3. Checks and signature stamps secured
4. Segregation of duties
5. Background checks
6. Bidding process
7. Fixed asset inventory review

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Internal Solutions – Some Specifics

1. Means for anonymous communication of tips
2. Automated controls
3. Employee education
4. Protect your financial network
5. Regular monitoring of accounts, petty cash
6. Unexpected audits

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Moving Forward

What's Needed

- Regulations for accountability and excess malfeasance
- Serious commitment by the sector to prosecute perpetrators that tarnish the good work of the nonprofit community
- Increased resources at all levels for oversight

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Questions and Discussion

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