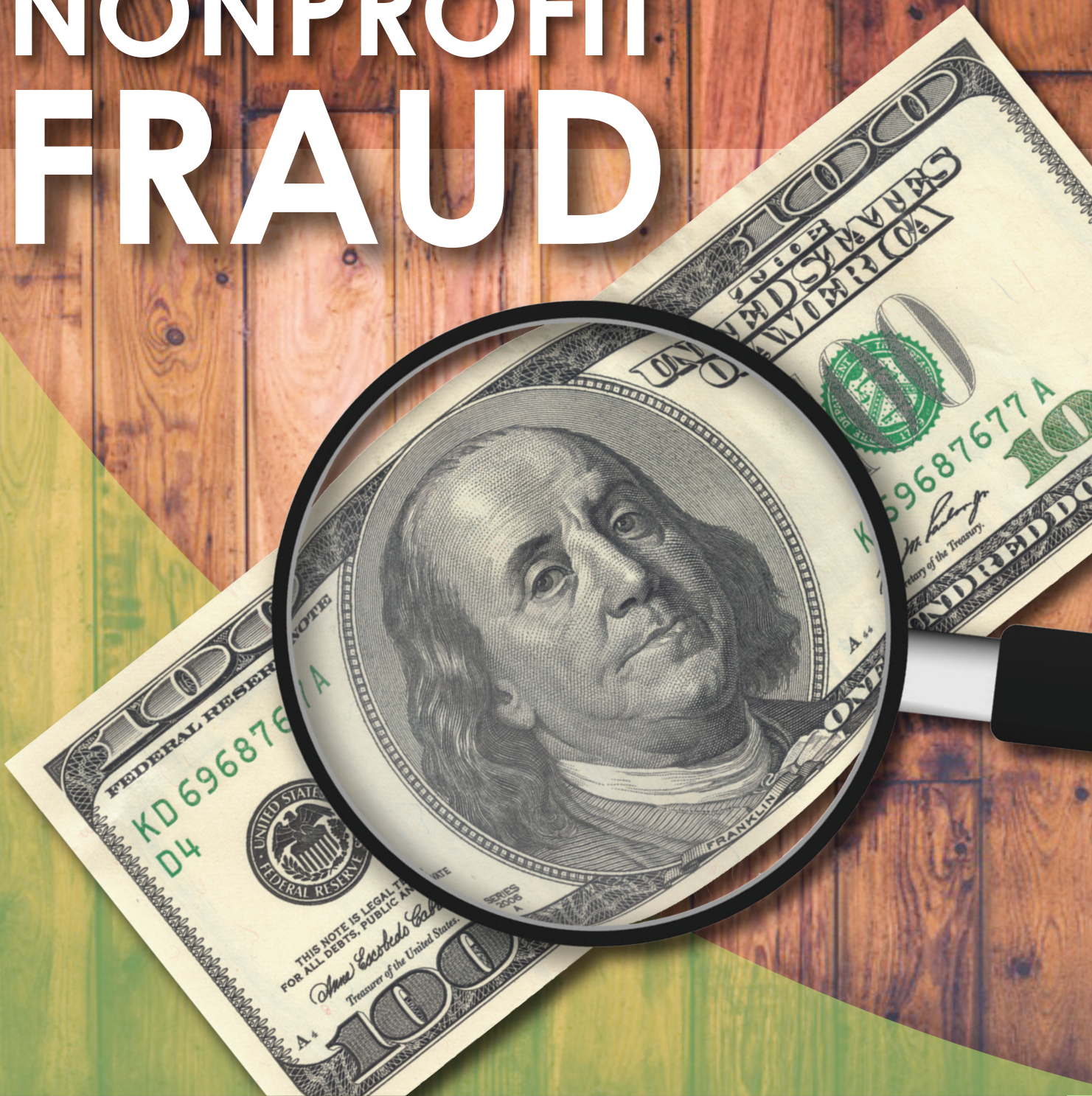


# 8 Ways

To Recognize

# NONPROFIT FRAUD



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## Who will benefit from this eBook?

This eBook is intended for board members, business owners, non profit executives and leaders, bookkeepers, office managers, or anyone else responsible for the integrity of their organization and the financial systems that are used.

## Introduction

It can be difficult to imagine that someone who seems like a dedicated and trustworthy volunteer or staff member could be stealing from your organization.

Sadly, financial fraud, theft, and embezzlement at nonprofits are all too common. Fraudsters have been uncovered at organizations of all sizes serving even the most vulnerable and needy members of society.

You cannot afford to just hope it never happens at your nonprofit.

*Want to protect your nonprofit from fraud? Keep reading!*



## Why You Should Be On Guard Against Fraud

Nonprofits of all sizes are susceptible to financial fraud, but small nonprofits are the most vulnerable and least able to recover. Money lost to theft and embezzlement is money that doesn't go toward improving the organization or serving the cause.

At many nonprofit organizations, the number of staff and volunteers is small enough so everyone knows everyone else. Members often feel a sense of united purpose and camaraderie with others that are working toward the same goal. This sense of trust between members isn't a bad thing, but fraudsters can take advantage of it if the organization does not have controls.

A small nonprofit may not have enough members or volunteers to ensure financial responsibilities are adequately spread out. This leads to the same person wearing multiple hats, sometimes with limited or no oversight. This

makes it even easier for a fraudster to conceal illegal activities. If the thief is not detected and dealt with in a timely manner, the behavior can spread to others. When other employees or volunteers see someone stealing without suffering any consequences, they may be tempted to start stealing themselves.

Standard audits are not an effective tool for detecting financial fraud because they are not designed to detect it. Even outside audits rarely detect fraud. According to the National Organization of Fraud Examiners, less than 4% of frauds are uncovered by an audit.

If a privately-owned business suffers a loss due to fraud, they have the option to keep information about the theft internal. Nonprofits have no such protection. IRS regulations stipulate nonprofits must disclose any fraud that results in losses of more than \$250,000, 5% of the gross, or 5% of total assets. Sometimes, the media picks up on the story, which can result in a public relations disaster for the organization. Donors may be angry that their money did not go to the cause and be reluctant to contribute again. If the victimized nonprofit received public funds, the government may get involved with their own investigations.

### *Stats from ACFE report on the cost of fraud.*

A study of 1,483 cases showed **\$3 billion dollar** losses due to fraud.

The median loss caused by a single case of fraud is **\$145,000 dollars.**

22% of occupational fraud cases cause losses more than **\$1 million dollars.**

Financial statement fraud causes significant damage, at **\$1 million dollar** losses.

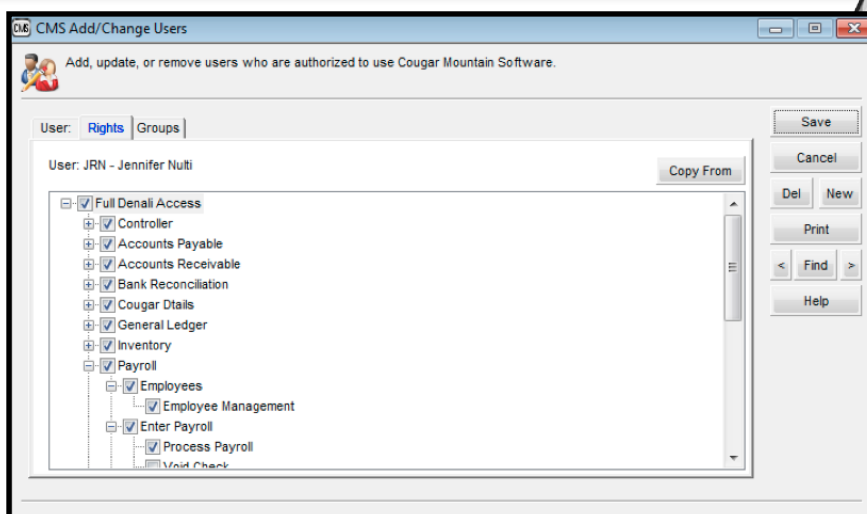
## Fraudster Warning Signs

While anyone with access to money can commit fraud, potential fraudsters tend to have common behaviors or backgrounds. These traits don't necessarily indicate a problem, but they can serve as red flags. Many victimized organizations recognize them only after it's too late.

- **Reluctance to take time off.** The last thing a fraudster wants is someone else stepping in, taking over their duties, and going over their records while they're gone.
- **Reluctance to share duties.** Beware the workaholic who wants to do everything on their own. Some fraudsters act disagreeable and defensive to ward off scrutiny, but others can act excessively nice.
- **Disgruntled or dissatisfied about their pay.** A staff member who feels they are not being paid enough may stoop to theft or embezzlement to make up the difference.
- **Keeps indecipherable, sloppy, or confusing records.** This is another tactic for warding off oversight.
- **Financial or drug addiction problems.** Excessive debt is often a trigger for fraud. A drug addict must use more drugs to satisfy their cravings as their addiction progresses, and will often steal when they can't afford their fix.
- **Excessive gambling habits.** This one can be difficult to detect, but if the person often talks about gambling or trips to casinos it could be a sign of trouble.
- **Living beyond their means.** Is the person with access to money spending extravagantly and buying things their salary doesn't support? There are legitimate reasons someone could come into money, but it could be coming out of the organization's bank account.
- **Has worked for the nonprofit for some time.** Fraudsters rarely start stealing as soon as they join the organization. They may wait months or even years.



## How Denali Controls Security Settings



Denali provides a very detailed user rights management. Rights are granted to specific areas of the software allowing you to segregate responsibilities for accounting roles. The separation of duties is one of the best practices for securing your company against fraud.

## Fraud Prevention Steps



Have the board create a set of financial controls, and review them at least once a year to verify they are adequate. The exact nature of the controls will depend on how your nonprofit is organized. Because board members can come from non-financial backgrounds, enlist the aid of an outside expert if none of the members possess the right skills.

Determine in advance what actions management will take if fraud is uncovered. Confronting the fraudster without adequate justification can invite retaliation, cause the offender to take steps to destroy evidence, and make them more difficult to successfully prosecute.

Perform financial, process, and internal control audits at least once a year, and vary the timing. While audits are of limited use in uncovering fraud, knowing the records can be checked at any time is a powerful deterrent. Because many fraudsters are in management positions, internal audits should be performed by an audit committee independent of management. The committee should also have the power to hire outside

help and advisors if necessary. Cultivate an ethical environment from the top down. Management should project and promote a strong sense of integrity. Doing so will make it more likely employees who suspect fraud will step forward.

Most fraud is uncovered through employee tips. Give employees options for reporting their suspicions. Some organizations use tip hotlines, anonymous email accounts, or even a simple drop box. For any of these methods, make sure multiple people have access to fraud that is reported. If the fraudster is the only one who checks the hotline, email account, or drop box, it won't do much good.

Spread financial responsibilities across multiple people. No one employee or volunteer should be completely responsible for duties like payroll, accounts payable, or accounts receivable. If possible, train multiple people for each job and rotate between them. Assign a member of management to check their records against one another, and follow up on any discrepancies. Require staff members to take vacation time. If an employee with access to money is accruing large amounts of unused time off, find out why. If they say it is because they are overloaded with work, assign someone to help out. Have the financial statements sent directly from the bank to a designated member of the board or management who does not have anything to do with processing or receiving payments or payroll. They should review the statements carefully, follow up on any concerns, and share their findings with the board.

Denali provides a set of Red Flags reports that will allow you to quickly

## 10 Reports that can help identify fraud.

- AP Control Report
- AP GL Expense Distribution Report
- AR Control Report
- BR Missing Check Report
- GL Reprint Posting Report
- IN Control Report
- IN Movement Report
- PO Open Purchase Order Report
- SA Price Variance Report
- SA Invoice Tracking Report

identify areas within your accounting system and data that may require your attention. For example, the missing check report will draw your attention to gaps in sequence that should be analyzed and understood as quickly as possible.

Check Number	Payee Name/Description	Date	Amount	Totals
<b>BR Missing Check Report</b>				
08/13/2010 11:23:43 AM <span style="float: right;">Page 1</span>				
All Books Surplus (ALLB00)				
Bank Code: BA	Bank of America (Checking)			
12323423423	Cameron Lamb	08/13/2010	\$50.00	
<b>Total for BA</b>	<b>Number of Ranges of Missing Checks:</b>	<b>0</b>		<b>\$50.00</b>
<b>Report Selection Criteria</b>				
<b>Bank Accounts:</b>	<b>Start</b>	<b>End</b>		
<b>Date Range:</b> Custom				
<b>Check Date:</b> 01/01/2009		08/13/2010		
<b>Check Numbers:</b> Start		End		
<b>Both Missing and Existing Checks</b>				

## Credits

### Cougar Mountain Software

Cougar Mountain Software was founded in 1982 with a vision to develop powerful business accounting, nonprofit accounting, and point of sale software solutions. Our [30 years of success](#) comes from two key practices; (1) employing in-house accounting and business professionals for our sales, support, training, and development teams, and (2) listening to our clients. These two practices make our accounting solutions unique to competitors who outsource their support and build fixed and un-scalable solutions to meet the general needs of the masses.

[www.cougarmtn.com](http://www.cougarmtn.com)

[Cougar Mountain Payroll Site](#)

[Cougar Mountain Business Site](#)

[Cougar Mountain Non Profit Site](#)

[Cougar Mountain Retail Site](#)



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## Appendix: Further Resources

These additional resources will help you understand the potential for fraud with your nonprofit and help identify ways you can protect your organization.

Association of Certified Fraud Examiners  
[www.acfe.com](http://www.acfe.com)

American Institute of CPA (AICAP)  
<http://www.aicpa.org>

United States Securities and Exchange Commission (SEC)  
[www.sec.gov](http://www.sec.gov)

[Cougar Mountain Nonprofit Blog](#)

[CPA Practice Advisor review of Denali Fund](#)

[Setting up budgets using Denali Nonprofit Software](#)

[Viewing budgets using Denali Nonprofit Dashboards](#)

[How to import and export budgets to csv or xml file formats](#)

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