Types of Fraud & Ways to Mitigate Fraud

info@jmco.com | www.jmco.com
Daytona Beach 386.257.4100 | DeLand 386.738.3300 | Gainesville 352.378.1331 | Tallahassee 850.386.6184

James Moore
Certified Public Accountants and Consultants

Continue reading to learn more about the types of fraud prevalent in nonprofit organizations, signs and behaviors you can detect to determine if someone is engaging in fraudulent activities, and precautionary steps your organization can take to protect your organization.

info@jmco.com | www.jmco.com
Daytona Beach 386.257.4100 | DeLand 386.738.3300 | Gainesville 352.378.1331 | Tallahassee 850.386.6184

James Moore
Certified Public Accountants and Consultants

Where Does Fraud Occur and How Can it Happen to Your Nonprofit

Nonprofits often lack the number of personnel required to properly segregate duties, which in turn makes it difficult to create effective internal control systems. This places additional duties on Executive Directors, management and sometimes board members, who ultimately become a part of the internal control solution. As such, these controls are often overlooked for seemingly more urgent matters.

According to The 2014 Global Study of Fraud, created by the Association of Certified Fraud Examiners, 11 percent of the fraud cases examined were committed against nonprofit organizations. The median loss from fraud activities for nonprofits was $108,000! Despite your best efforts to implement controls and mitigate fraud, it can easily happen to you!

CASH FRAUD

Understanding the cash cycle and accounting process of your organization will help you understand how cash fraud occurs. Skimming occurs when money is taken from the organization prior to its entry into the accounting software. The opportunity for skimming is higher when the organization doesn't properly segregate duties. Cash fraud also occurs when money goes out; for example, payment of falsified expense reports, taking checks and depositing them into a personal account, and payment for nonexistent vendor services. Organizations that implement internal controls such as mandatory back-up documentation for invoice payment, and utilizing an approved vendor list have a better chance than other organizations of preventing fraud.

FINANCIAL STATEMENT FRAUD

The opportunity for fraud can wield a great deal of influence over the individuals responsible for managing and creating the financial statements. Financial statement fraud is the deliberate misrepresentation or omission of financial statement data for the purpose of misleading board members, bankers, funders, etc., about the financial performance of the organization. Examples of financial statement fraud include, delaying the payment and recording of expenditures, adjusting journal entries, improper revenue recognition, and overstatement of assets.

Board members and executive directors should be aware of the three circumstances that lead to the commission of fraud:

1. MOTIVATION

Economic factors such as personal financial distress or overspending may provide motivation.

2. RATIONALIZATION

A motivated individual generally finds a way to rationalize fraud. This can include perceived injustice in compensation as compared to their colleagues, the idea that they are simply “borrowing” from the organization and fully intend to return the assets at the future date.

3. OPPORTUNITY

The individual has sufficient access to assets and information that allows him or her to believe that fraud can be committed and also successfully implemented.

Understanding your organization’s financial process and then utilizing your board in your internal control process will help prevent fraud within your organization. We continue our discussion with 10 tips to mitigate fraud on the following page.

info@jmco.com | www.jmco.com
Daytona Beach 386.257.4100 | DeLand 386.738.3300 | Gainesville 352.378.1331 | Tallahassee 850.386.6184

James Moore
Certified Public Accountants and Consultants

10 Circumstances to be Aware of to Avoid Fraud

Financial fraud is easily undetected and difficult to prove. However, nonprofit executive directors and/or board members can help identify and prevent fraud by simply being aware of and observant to suspicious activities and troubling financial situations.

POTENTIAL PROBLEMS TO BE AWARE OF:

1. The organization continues to lose money year after year.
2. Payroll taxes not being paid timely.
3. Sales tax not being made timely.
4. Be skeptical of the common assumption that in board meetings, "things always look good in the future."
   (You won't get a bank loan if every year you're losing profit.)
5. Concentration risks: When funding comes from one grant.
   (What if that one grant accounting for 75% of your business goes away?)
6. Significant turnover in the accounting department.
   (This might warrant further investigation)

CONTINUED ON THE FOLLOWING PAGE.

info@jmco.com | www.jmco.com
Daytona Beach 386.257.4100 | DeLand 386.738.3300 | Gainesville 352.378.1331 | Tallahassee 850.386.6184

James Moore
Certified Public Accountants and Consultants

10 Circumstances to be Aware of to Avoid Fraud

POTENTIAL PROBLEMS TO BE AWARE OF (CONTINUED):

7. **Employee Overtime:** Are employees being paid for overtime hours not worked or timesheets altered before or after management approval?

8. **Excessive Vacation Balances:** Although you might be impressed by an employee who hasn't missed a day of work in years, it could be a sign that they have something to hide and are concerned that someone will detect their fraud if they were out of the office.

9. **Photocopied or Missing Documents:** If you're undergoing an audit and can't provide requested documents, this could be a red flag for fraud. Or, if documents appear to be altered or photocopied, this could also signify fraudulent behavior.

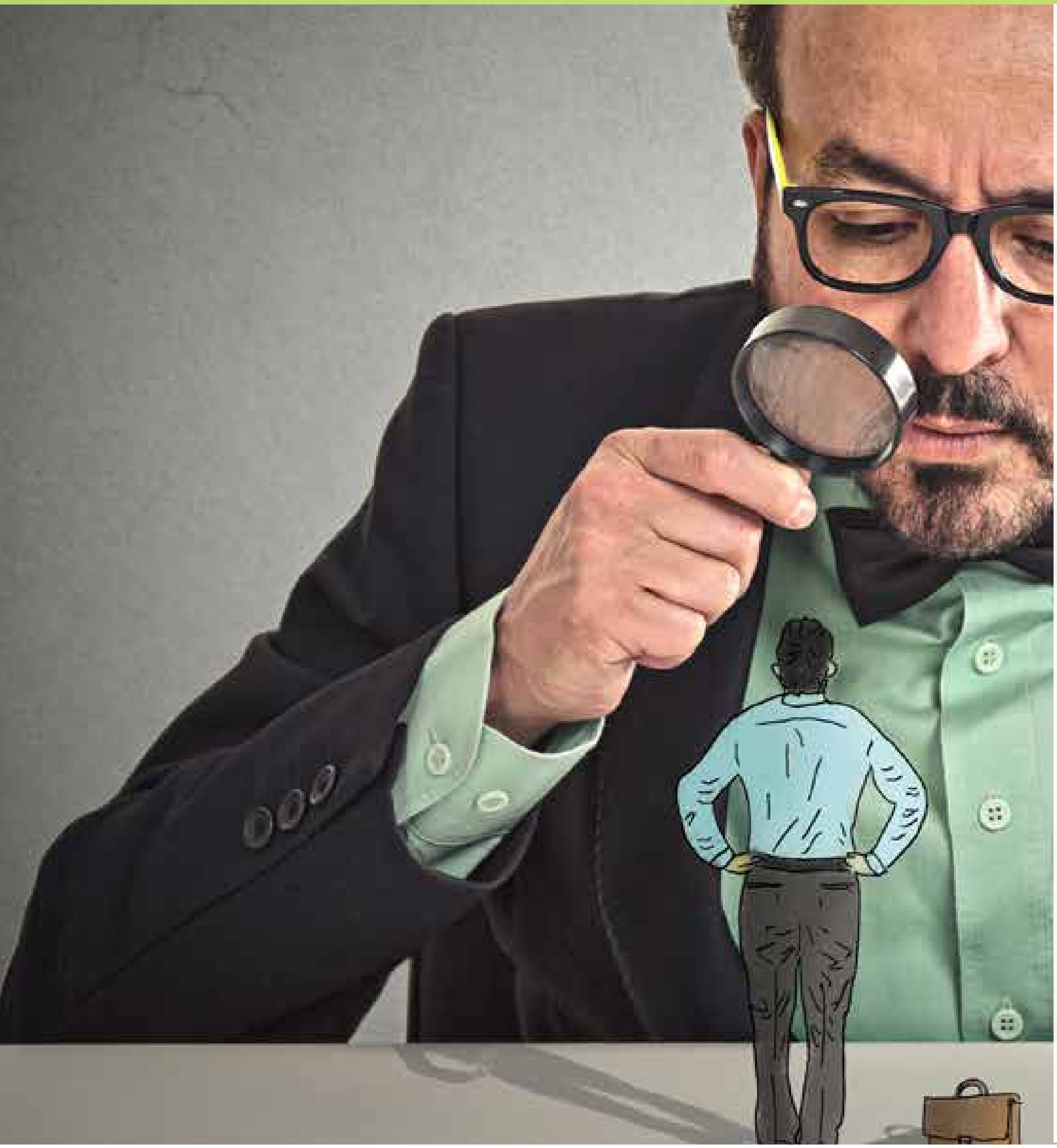
10. **Excessive credit memos and voids.**

Developing an understanding of the signs and behaviors most commonly seen in employees engaging in fraudulent activities will help save your organization both time and money. We continue our discussion with 7 quick tips to prevent fraud in your organization's workplace.

info@jmco.com | www.jmco.com
Daytona Beach 386.257.4100 | DeLand 386.738.3300 | Gainesville 352.378.1331 | Tallahassee 850.386.6184

James Moore
Certified Public Accountants and Consultants

7 Tips for Preventing Fraud



Every nonprofit organization should keep the risk of fraud close in mind and should have a basic understanding of the concepts intended to mitigate fraud. It should come as no surprise that an organization with proper internal control systems has a higher chance than other organizations to prevent or detect fraud before financial deception costs the organization big bucks.

WHAT CAN YOUR ORGANIZATION DO TO PREVENT FRAUD?

Implementing the following fraud prevention tips within your organization will help you avoid potential problems now and in the future.

1. Conduct background checks before hiring CFOs or bookkeepers who will be responsible for handling the organization's money. Generally, an accountant with a bad credit score is not the right person for the job.

2. Segregation of duties. No single individual should be responsible for receiving, depositing, recording, and reconciling the receipt of funds. Similarly, no one person should be responsible for authorizing payments, disbursing funds, and reconciling bank statement. Instead, when funds are received, have your receptionist or executive director make copies of all the checks; or create a ledger that details the company or individual, check number, amount and date. Provide the ledger or check copies to a bookkeeper for recording purposes, and later provide them with a copy of the bank receipt for validation.

info@jmco.com | www.jmco.com
Daytona Beach 386.257.4100 | DeLand 386.738.3300 | Gainesville 352.378.1331 | Tallahassee 850.386.6184

James Moore
Certified Public Accountants and Consultants

7 Tips for Preventing Fraud

3. Increase controls over credit cards to prevent unauthorized spending.
Inappropriate spending on credit cards is a common type of fraud within nonprofits because it easily goes undetected. The most common types of credit card fraud are:

1. **Personal charges that benefit employees** such as gas for their own vehicle, meals, groceries and other expenses.
2. **Double dipping by using the organization's credit card to make a purchase and submitting the expense for reimbursement.** To prevent credit card fraud, consider implementing the following controls:
   - Limit the number of credit cards and make sure all authorized users have their unique card. Collect and cancel all cards when the employee leaves the organization.
   - Review the electronic copy of the credit card statement, which cannot be altered; or ensure credit card statements are delivered unopened to the person responsible for reconciling charges.
   - Insist on original receipts for all transactions and compare to credit card statement.
   - Compare expense reimbursement claims to credit card charges.
   - Set the tone at the top. Let your employees know that you're watching and establish clear guidelines.

info@jmco.com | www.jmco.com
Daytona Beach 386.257.4100 | DeLand 386.738.3300 | Gainesville 352.378.1331 | Tallahassee 850.386.6184

James Moore
Certified Public Accountants and Consultants

7 Tips for Preventing Fraud

4. Many nonprofits and accountants use QuickBooks, which is an effective program to document and track your organization's financial position; however the data can easily be manipulated. Executive Directors or board members should implement the lock down provision in QuickBooks which locks down the prior period statements to avoid changes to these numbers.

Additionally, your CFO or bookkeeper should not be allowed to export financial reports and data into excel as a substitute for software generated financial statements because the data in spreadsheets can easily be manipulated.

5. Have a line of credit available for use when necessary. Organizations with large program expenditures that are reimbursed through grants can easily run into cash flow problems. Having a line of credit will help minimize the potential for fraud when cash flow issues occur.

6. Have an approved vendor list and don't allow payments to vendors not included in the list. Create a process that involves more than one individual when adding a vendor to the list.

7. On a monthly basis, provide your board of directors a statement of financial position, statement of activities and a budget to actual report for the overall entity and for any grants.

Remember, accounting is not smoke and mirrors - it should make sense even if you don't know the terminology. If you're spending money, cash should go down; if you've collected revenue, cash should go up. Paying close attention to your financial position and implementing some checks and balances will help your organization mitigate fraud.

info@jmco.com | www.jmco.com
Daytona Beach 386.257.4100 | DeLand 386.738.3300 | Gainesville 352.378.1331 | Tallahassee 850.386.6184

James Moore
Certified Public Accountants and Consultants