

Protecting against Fraud



By Anne Marie Minogue

Don't let cheats and swindlers tarnish your organization.
And don't think it couldn't happen to you.

Benevolence, trust, and compassion traditionally form the cornerstone of nonprofit organizations and facilitate their success. But these same characteristics can contribute to an organization's vulnerability.

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Schemes Orchestrated against Nonprofits

Embezzlement and other fraud schemes executed against nonprofits are as bountiful and resourceful as the organizations themselves. Popular schemes include skimming (accepting a donation or payment without recording it), unauthorized fraudulent disbursements, and the payment of personal expenses with charity funds.

A nonprofit is especially vulnerable if it uses an acronym of its initials as one of its names. Checks payable to the organization's acronym can be easily altered and deposited to a personal account; for instance, CFA can become C. F. Anderson.

Other employee-perpetrated embezzlement schemes involve creating fraudulent invoices and disbursing them to fictitious vendors. Employees with access to the organization's checks may use them to pay themselves, or they can create counterfeit checks for personal gain. A donor's credit card number can be used to purchase personal goods. Also common are kickback schemes in which a vendor pays a bribe to a nonprofit employee in return for preferential treatment.

“Also common are kickback schemes.”


Nonprofit organizations are often used by tax cheats to substantiate fictitious deductions on their tax returns. Some fraudsters will go so far as to send a donation to a charity and then request a refund; the fraudster uses the original check to receive a tax deduction. There have also been instances of collusion between tax cheats and trusted individuals within the tax-exempt organization who refund 90% of the original contributions.

How to Protect Your Organization

How can you avoid such schemes in your organization? Create an environment with zero tolerance for fraud, including:

- **A code of conduct.** Be sure not only to have a clear code of ethical conduct but to communicate it to everyone in the organization and monitor compliance. Require all employees to commit to the code on an ongoing basis. Provide training to reinforce the code's principles. If the code is violated, enforce disciplinary action consistent with the level of infraction.
- **Employee screening.** Incorporate screening procedures into your hiring process. Check credit reports. Verify the candidate's education, employment, and reputation. (See “Five Ways to Avoid Hiring a Liar” on page 28).
- **A whistleblower process.** Establish a procedure to receive complaints. People need to feel confident that someone will follow up and address all concerns promptly.

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- **Tone at the top.** The Association of Certified Fraud Examiners (ACFE) reports that having an ethical “tone at the top” can be the most effective way to avoid fraud. Any appearance of hypocrisy will make it easier for others to rationalize their own unethical behavior. Earn people’s trust by treating them fairly and ensuring that managers at all levels follow the rules.
- **Audit procedures.** Conduct frequent audits, focusing on areas that could be vulnerable to fraud. To ensure independence, use an outside auditor. Studies show that twice as many frauds occur in organizations that perform internal audits rather than bringing in an external auditor.
- **Internal controls.** Assure that your internal control system is effective and that you have a strict segregation of duties. Separate tasks within each financial function so that one person doesn’t have responsibility from beginning to end of the process.
- **Education.** Train all employees to recognize symptoms of fraud. 

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Guard Your Reputation

Even if you have adequate employee-theft insurance, an instance of fraud can cause people’s confidence in your organization to plummet. For more advice on preventing such a catastrophe, see these articles at NonprofitWorld.org/members:

- **Want to Avoid Fraud? Look to Your Board** (Vol. 28, No. 5)
- **How to Find the Perfect Auditor** (Vol. 22, No. 3)
- **Setting Up a Control System for Your Organization** (Vol. 16, No. 3)
- **Protecting your Organization against Financial Misuse** (Vol. 17, No. 4)
- **How to Conduct Discipline Interviews** (Vol. 24, No. 6)
- **Nonprofits without Audit Committees Risk Disaster** (Vol. 22, No. 2.)
- **Fraud: How to Prevent It in Your Organization** (Vol. 26, No. 3)
- **New Internal Control Guidance: What You Need to Know** (Vol. 28, No. 1)
- **Can Your Organization Afford to Lose \$100,000? Safeguards Every Nonprofit Needs to Implement** (Vol. 30, No. 3)



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