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Charitable Fraud

University of Dayton, Ohio (url: http://www.udayton.edu/index.php)

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04.25.2008 | Service and Giving, Faculty Janet Greenlee, accounting professor at the University of Dayton, would like to see more of the money donated to nonprofit organizations go into charitable efforts – not into the pockets of thieves.

But Greenlee fears that charities are slow to discover losses and reluctant to go public when they do catch losses.

Greenlee is the lead author of new, nationally recognized research that for the first time estimates the amount of nonprofit fraud each year at a staggering $40 billion. She's been invited to talk about her findings this fall at the National Association of Attorneys General/National Association of State Charity Officers meeting.

"I don't think that charities are any different from many small businesses. Charities tend to be understaffed," she said. "It's common that one employee does multiple tasks," she said, adding that it's often those most-trusted employees who are the culprits.

Because of the nature of charity, "nonprofit organizations tend to assume that everyone involved with the organization is dedicated to the cause. Accordingly, employees and volunteers operate in an atmosphere of trust," according to Greenlee's report, published in the Dec. 2007 issue of Nonprofit and Voluntary Sector Quarterly.

She offered six tips for nonprofit managers to help them protect their organizations against fraud or at least detect it early:

* Institute basic internal controls such as separation of duties. "Have different people authorize and sign checks, and in double-signature systems, don't sign blank checks."

* Pay attention to what's going on. "If someone appears to be living beyond their means, take notice. It doesn't mean there is a fraud, but it can be tip-off."

* Use common sense. "Look for numbers that don't make sense. For example, it isn't logical that two employees travel to a conference and it costs one employee $300 and the second one $3,000. Most frauds can be caught simply by being aware of what's going on."

* Do background checks on employees. Those who had previously committed fraud are more likely to do it again and be more successful. "Background checks won't stop fraud, but it may stop a bigger loss."

* Have a confidential hotline so people can report fraud. "It's not enough to do an annual financial statement audit. Most fraud is caught by accident, or by a tip. Only 25 percent of fraud is caught by the internal audit."

* Avoid blind trust. "Don't overlook the employee you feel you can't do without."

Nonprofit organizations could do much more to catch or minimize losses from fraud, she said. Executive directors of nonprofit organizations are often not alert enough, too trusting, shorthanded and so distracted by the multiple demands of small organizations that they may not be aware a loss has even occurred.

"Fraud is not like coming in and robbing a bank. They may not know they've been victimized," she said.

Greenlee's research, which examined 2004 data collected by the Association of Certified Fraud Examiners, found that the typical nonprofit fraud case resulted in a loss of less than $50,000. These kinds of fraud were most often committed by a woman with no criminal record, earning less than $50,000 who had worked for the organization for at least three years.

The most costly frauds were committed by male managers and executives who earned between $100,000 and $149,000 a year.

When a fraud is discovered, the loss is often kept quiet with the employee permitted to resign.

"Many charities don't report fraud because they fear that if it's publicized, contributions will decline," she said.

But Greenlee advocates a stronger, more open approach. "When a charity catches a fraud and publicizes it, it may actually help decrease fraud. It enhances the credibility of the nonprofit sector because they are demonstrating good management and showing that more donated dollars are going to the intended purpose."

The research was co-authored with Mary Fischer of the University of Texas at Tyler; Teresa Gordon of the University of Idaho; and Elizabeth Keating of the Harvard Law School.

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