NONPROFIT PERSPECTIVES

How Could This Fraud Have Been Prevented?

Joe Doe, a beloved associate program director, worked at a nonprofit social service agency for 15 years. When the executive director retired and he was passed over, Joe stayed on with the organization. During the transition between executive directors (EDs), he took on interim ED duties. His responsibilities included signing privileges for the agency's accounts.

When a new ED was hired, she couldn't figure out why the not-for-profit didn't have a positive bottom line. The organization's revenue streams included rent from tenants in its building and it had been financially healthy in previous years. While Joe was initially helpful in responding to her inquiries, as time went on he became evasive in his answers, stopped attending staff meetings, and took on an extremely low profile.

Uh-oh

One day, the new director came across some paperwork that included bank wire transfer instructions for a small checking account and a line-of-credit statement from an area bank. An investigation into these documents revealed that, while acting as interim director, Joe had deposited advance rental payments into the checking account and made withdrawals on a regular basis. During that time, he also opened the line of credit, deposited the proceeds in the checking account and withdrew those amounts as well.
After a two-week investigation, the nonprofit determined that Joe had embezzled approximately $1 million. By that time, Joe had fled the country unnoticed.

Implementing controls

This sad scenario, which caused severe reputational and financial damage to the nonprofit, could likely have been prevented if the following policies and practices had been in place:

- All bank statements should be delivered unopened to a member of management or the board who has no signing authority.
- The finance committee — with members knowledgeable in finance and accounting — should review monthly bank reconciliations and financial statements and question any transactions that are new or unusual.
- New bank accounts, both depository and loan accounts, should be approved by the board prior to opening.

Additionally, employees should be trained to be alert to changes in employee behaviors and possible motivations for fraud. In this case, the fraudster felt entitled to become the next executive director. His fraudulent acts — at first involving small sums — began shortly after he realized he wouldn't be appointed to the position.

Getting expert advice

Do you ever wonder if your operation may be too lax in terms of presenting opportunities for inside fraud? If so, you may want to ask your CPA to review your controls and offer suggestions for improvement.