Welcome to the NVFC’s Webinar Series.

Today’s webinar is “How to Protect Your Nonprofit Organization from Financial Fraud.”
How to Protect Your Nonprofit Organization from Financial Fraud
The National Volunteer Fire Council (NVFC) is the leading nonprofit membership association representing the interests of the volunteer fire, EMS, and rescue services. The NVFC serves as the voice of the volunteer in the national arena and provides invaluable resources, programs, education, and advocacy for first responders across the nation.

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INTRODUCTION

• Chris Rauch
  – Director of Vault Consulting LLC’s Outsourced Accounting Group
  – More than 21 years of experience serving the nonprofit industry
  – Provides CFO level services helping nonprofits establish sound financial reporting, controls, and systems to support their organization’s mission
AGENDA

• Types of Fraud
  – Internal Fraud
  – External Fraud
• Internal Controls
• Continuity of Business Operations
• Questions
TYPES OF FRAUD

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INTERNAL FRAUD
INTERNAL FRAUD

• Perpetrated from within the organization
  – Employee
  – Board Member
• Misappropriation of Assets
  – Theft of Cash
  – Theft of Equipment/Inventory
• Financial Statement Fraud
INTERNAL FRAUD – THEFT OF CASH

• Can occur in a number of different ways

  – Petty cash or cash on hand
  – Writing checks to self or to fictitious vendors
  – Wire transfers, ACH’s, withdraws from account
  – Payroll
INTERNAL FRAUD – THEFT OF CASH

• Petty cash or cash on hand/incoming checks
  – If it is in your office or building, it can be stolen
  – Don’t keep large amounts of cash onsite
  – Secure it!
    • Place it in a safe, or a locked room or closet
    • Manage who has access to it
    • Perform periodic reconciliations of cash involving more than one person, preferably with someone who normally doesn’t access cash
    • Install surveillance
  – Maintain a check log of incoming checks
    • Should be kept by someone other than the person applying payments and making deposits
INTERNAL FRAUD – THEFT OF CASH

• Writing checks to self or fictitious vendors
  – Blank check stock can be stolen
    • Secure check stock like you would cash – lock it up! Control who has access to it
  – Keep a check log noting beginning and ending check numbers for each check run. Make sure that all check numbers are accounted for – no gaps in sequence

INTERNAL FRAUD – THEFT OF CASH

• Writing checks to self or fictitious vendors – continued
  – Require authorization and examination of new vendors
  – The person writing the checks should not be a signer on the accounts (at least not the only signer)
  – A person independent of the a/p process should reconcile the bank account, paying close attention to what checks are clearing the bank
INTERNAL FRAUD – THEFT OF CASH

• Writing checks to self or fictitious vendors – continued
  – Checks should be mailed out by someone other than the person who cut the checks
  – Enroll in positive pay with your bank
  – Consider an online bill payment option that allows for custom approval and payment authorizations that limits how much each person can do on their own
INTERNAL FRAUD – THEFT OF CASH

• Wires, ACH’s, withdraws from account
  – Just like checks, if someone has access to the bank account, they can steal money directly from it
  – Control who has online access to the bank account
  – Set up access rights by user for online banking
  – Apply internal controls to outgoing wires – require more than one person to be able to initiate a wire
  – Do not issue debit cards to staff
  – A person independent of the wire process should reconcile the bank account
INTERNAL FRAUD – THEFT OF CASH

• Payroll
  – Employee processing payroll increases their pay or leave balance
  – Employee sets up a fictitious employee and routes their payment to an account they hold
• Review every payroll both before and after it is processed
• Examine pay rates, overtime, and employee names to make sure that everything is in order
INTERNAL FRAUD – THEFT OF EQUIPMENT/INVENTORY

- Inventory and equipment can be stolen and sold by employees
  - Log all purchases and receipts of equipment
  - Someone independent of the purchasing process should receive inventory and equipment
  - Match any purchase orders with the items delivered
    - Did you receive what was ordered?
    - Did you get the number of items that were ordered? More, less?
    - Tag all equipment and record the information in the equipment and inventory log noting serial numbers
    - Make note who equipment is issued to
    - Keep all inventory and unissued equipment in a secured area
    - Do periodic and random counts of inventory and equipment
    - Make sure that inventory and equipment logs are kept up to date with authorized purchase and issuances to allow for accurate counts
INTERNAL FRAUD – Financial Statement Fraud

• Knowingly and willingly preparing inaccurate financial information with the intent to deceive the users of the financial statements
INTERNAL FRAUD – Financial Statement Fraud

• Why commit financial statement fraud?
  – Personal financial gain – salaries, bonuses, etc. based on results of operations
  – Hide how the organization is doing – fear of losing job
  – Cover up fraud
INTERNAL FRAUD – Financial Statement Fraud

• Most likely areas for financial statement fraud to occur
  – Recording of fictitious accounts receivable
  – Not fully reporting accounts payable
  – Recording revenue before it is earned
  – Leaving expenses in prepaid expense after it should be recorded
INTERNAL FRAUD – Financial Statement Fraud

• How do we prevent this from happening?
  – Management should review outstanding receivables on a routine basis and question why old amounts have not been collected
  – Be aware of what all balance sheet items represent – have they changed much or do they remain the same?
  – Board should review financial statements on a routine basis
    • Question odd balances or results that seem out of line with what you and other members are experiencing in your own businesses
  – Undergo an annual audit by an independent auditor
INTERNAL FRAUD - SUMMARY

• Perpetrated from within the organization
  – Employee
  – Board Member

• Misappropriation of assets
  – Theft of cash
  – Theft of equipment/inventory

• Financial statement fraud
EXTERNAL FRAUD
TYPES OF FRAUD – EXTERNAL FRAUD

• Perpetrated from outside the organization
• Fraudulent checks written against your bank account
• Fraudulent credit card sales followed by request for refund in a different manner than payment
• Phishing schemes
External Fraud – Fraudulent Checks

• Much like internal fraud, individuals from outside your organization can write fraudulent checks against your bank account
  – Usually someone that works for one of your vendors
External Fraud – Fraudulent Checks

• How it works
  – You write a check to a legitimate vendor for a legitimate expense
  – Someone in the vendor’s office steals your bank information from the check and creates check stock using that information
  – They guess at the next check numbers in the sequence based on what they see coming in from you
External Fraud – Fraudulent Checks

• How to prevent it
  – Enroll in positive pay with your bank – they will not honor unauthorized checks
  – Consider online bill pay that pays vendors by ACH or with check stock not directly written on your bank account
External Fraud – Fraudulent Credit Card Payment

• How it works
  – You have a new customer that says they want to become a member or attend an event
  – They generally contact you out of the blue
  – They arrange for payment via credit card, and within a day or two contact you with an excuse and they need a refund
  – They state that their credit card company does not allow refunds to be issued to their card and they must receive a wire for the refund
  – They are using a stolen credit card and are racing against the owner of the card issuing a fraudulent charge alert
  – You issue the refund via wire, the actual cardholder disputes the charge, and your organization is out the money
External Fraud – Fraudulent Credit Card Payment

• How to prevent it
  – Never issue a refund using a different method than how you collected the original funds
  – Question any organization that states that their credit card cannot accept refunds – this is never the case
  – They will be pushy, don’t let them get to you
EXTERNAL FRAUD – PHISHING SCHEMES

• Phishing schemes are becoming more and more prevalent and more sophisticated
• Starts with an email posing as someone within your organization
  – Usually posing as the CEO/President
  – Usually directed to someone in the accounting or finance department
EXTERNAL FRAUD – PHISHING SCHEMES

• Types of requests in phishing emails
  – An urgent wire request to be issued to an unknown vendor
  – Need a vendor added to payroll as a 1099 vendor and needs to be paid immediately
  – Gift cards to be purchased discreetly for employee recognition gifts – send gift card information to the person requesting it
  – Employee W-2’s for the year just ending
  – And it goes on
EXTERNAL FRAUD – PHISHING SCHEMES

• What to watch for
  – The email address is usually very close to the person’s email requesting the action
  – In some cases the email address has been hacked and it is the actual email address
  – Look for suspicious language that is out of character for the person sending it
  – Hover over the email address of the sender to see if it changes
EXTERNAL FRAUD – PHISHING SCHEMES

• How do you prevent this?
  – Always contact the person requesting the action via phone to confirm any request like this
  – Never reply to the email requesting verification
  – Educate staff on phishing schemes
  – Increase security surrounding email accounts and incoming email
INTERNAL CONTROLS
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Internal Controls: Mechanisms, rules, and procedures implemented by an organization to ensure the integrity of financial accounting information, promote accountability, and prevent fraud.
INTERNAL CONTROLS

• Segregation of duties: Dividing duties up amongst multiple staff so that no one staff has full control over a particular function in the accounting function:
  – Accounts payable: Expenses should be approved by the appropriate personal outside of accounting and sent to the accountant for processing the payment
  – Someone else (other than the initial approver and accountant) should sign the check and review the supporting documentation
  – The checks should be mailed out by someone other than the accountant
  – Should have multiple people who can sign checks in the event that someone is out sick, on vacation, etc.
INTERNAL CONTROLS

Small organizations face larger obstacles than larger organizations when it comes to setting up effective and efficient internal control structures – simply because they have fewer people available to help with segregation of duties. Do the best that you can with the staff that you have available. Talk to your auditors and have them help you devise a good system of internal controls.
CONTINUITY OF BUSINESS OPERATIONS
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Many small businesses have a limited number of staff, and often only one person is set up to sign checks. If that person gets sick or has to take an extended leave of absence, things can often fall apart quickly in terms of paying vendors and employees.
CONTINUITY OF BUSINESS OPERATIONS

• What can we do?
  – Make sure that you have at least two people who can sign checks and authorize wires. Work with your bank to ensure that you have the appropriate number of signatories that you can remove another signatory and act on behalf of the organization if needed
  – It can be the President/CEO, COO, Treasurer, etc., but it should be people involved in the management of the organization
  – Check stock should be kept in a place where it is accessible to authorized personnel, not at the Treasurer’s home, etc.
CONTINUITY OF BUSINESS OPERATIONS

What can we do?

- Get online access to all bank accounts
  - Set up users with assigned access rights
  - Follow the same protocols for wire transfers that you follow for check issuance (# of authorizers should be the same as the number of signers required, etc.)

- Consider online bill pay
  - Either offered through your bank or from a third party provider
  - Allows you to pay bills no matter where you are as long as you have internet access
CONTINUITY OF BUSINESS OPERATIONS

• In Response to COVID-19
  – Many organizations are experiencing difficulty paying bills, getting mail, making deposits, etc.
  – Mail can be forwarded temporarily to a PO Box or to someone’s home so that checks can be collected and deposited, bills can be collected and paid, etc.
  – Work with your vendors to pay via wire or ACH if possible if you do not have an online bill pay system
  – Consider ordering a remote deposit check scanner from your bank
Q&A SESSION
POST WEBINAR THOUGHTS OR QUESTIONS?

JOIN THE CONVERSATION!

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THANK YOU!

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