

“Frauditing” Preventing and Detecting Fraud in Your Association

Greg Plotts, CPA, Nonprofit Partner, Aprio

Jennifer Cassidy, VP of Finance & Administration

Julie Broadway, CAE, President of American Horse
Council and American Horse Council Foundation



Agenda

- Fraud and Your Organization
- The Perpetrator
- Discussion of Fraud at NFP
- Anti Fraud Programs and Controls
- Taking Action
- Risk Universe
- Association of Certified Fraud Examiners (ACFE) – Fraud Prevention Check-UP

NFP Fraud

An arts center lost \$1.48 million over five years in a scheme by a low-level accounts receivable employee. The employee created fake companies, assigned vendor numbers to them, and then submitted invoices for work never performed.

A nonprofit lost \$500,000 when it was discovered that its former chief financial officer wrote fraudulent checks to herself and forged her supervisor's signature on them. Her crime was uncovered when she resigned from her position, and the new CFO discovered the missing checks.

NFP Fraud

An employee embezzled \$1.4 million from a nonprofit. The woman made over 350 unauthorized wire transfers and issued over 250 checks to herself, her husband, and several of her creditors. She was arrested and placed on a pretrial release with the condition that she refrain from illegal activities. However, that didn't deter her. She used a different name to secure employment with a different nonprofit and failed to disclose her prior indictment. She stole \$57,000 from the second nonprofit during her pretrial release period.

An administrative assistant working at this nonprofit admitted to embezzling over \$5.1 million in a scheme that went unnoticed for eight years. The employee had access to critical financial systems, and she created fake invoices in the names of legitimate groups. She approved the invoices for payment, and when the checks were ready, she cashed them herself.

NFP Fraud

74% of nonprofit fraud was perpetrated by individuals at the officer and management levels

Top three causes of nonprofit were:

- Lack of internal controls
- Lack of management review of existing internal controls
- Override of existing internal controls

Nonprofit organizations that utilized recommended fraud controls at far lower rates than did other organizations

NFP Fraud

21% of nonprofits conducted surprise audits, whereas 40% of other organizations did

24% of nonprofits conducted formal fraud risk assessments, whereas 43% of other organizations did

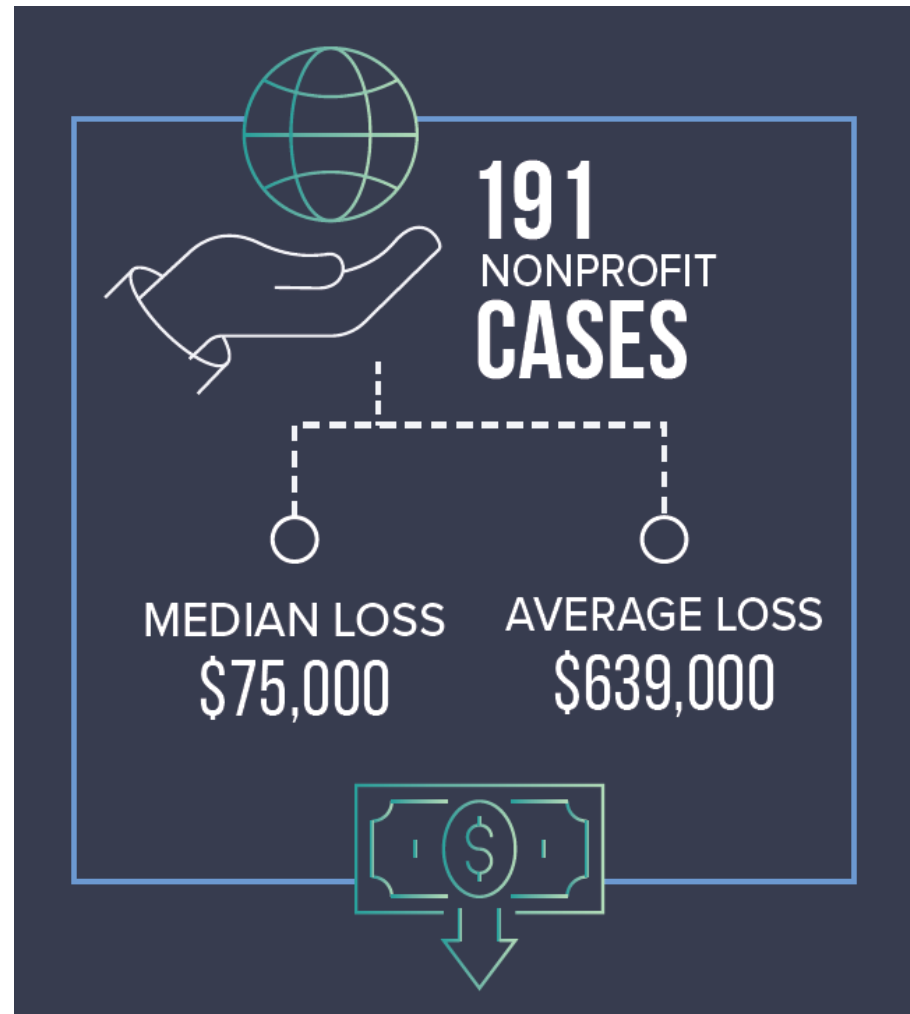
44% of nonprofits instituted management review of internal controls, whereas 68% of other organizations did

57% of nonprofits utilized an internal audit department, whereas 76% of other organizations did



Fraud and Your Organization





Source: ACFE Report to the Nations

The Fraud Triangle














- Personal debt
- High medical bills
- Supporting a habit
- Work-related pressures

- Inadequate segregation of duties
- Rapid turnover/lack of oversight
- Absence of mandatory vacations
- Constant “crisis” mode
- Controls not followed

- “I’m not hurting anybody.”
- “This organization owes me.”
- “I’ll pay it back.”

Nonprofit schemes

Percent of cases

Corruption		41%
Billing		30%
Expense reimbursements		23%
Cash on hand		17%
Noncash		16%
Skimming		15%
Check and payment tampering		14%
Cash larceny		12%
Payroll		12%
Financial statement fraud		11%
Register disbursements		3%

Source: ACFE Report to the Nations

Schemes

Billing schemes include: false vendors or shell companies; resubmitting valid invoices for duplicate payment; and including personal expenses as company charges.

Corruption includes: conflict of interest, bribes, kickbacks, bid rigging, and sales schemes.

Skimming includes: theft of incoming payments before they are entered into the system hidden by lapping receivables or unrecorded sales.

Schemes (Cont.)

Expense reimbursement schemes include: mischaracterized expenses, overstated expenses, fictitious expenses, and duplicate reimbursements.

Check tampering includes: forged maker, forged endorsement, and altered payee.

Payroll schemes include: ghost employee, retaining an employee on payroll after termination, falsified wages, and commission schemes.

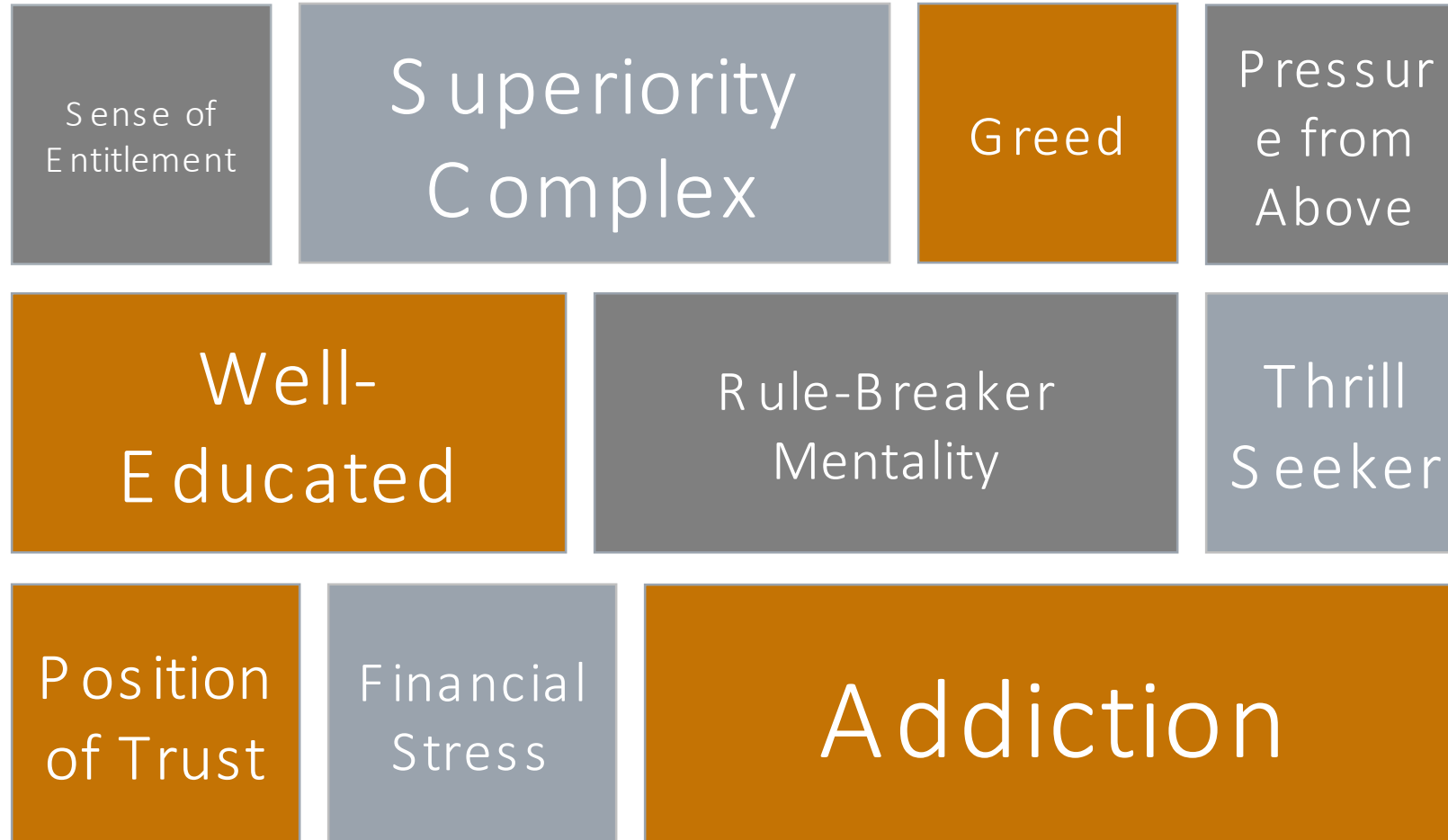
Case Study: False Vendor Invoices

- Nick is the A/P clerk at ABC, a rapidly growing company
- Nick's responsibilities include A/P, cash disbursements, and new vendor approval
- Nick knows his bosses don't pay attention to vendor invoices under \$2,500
- Nick forms a shell company (XYZ), with a PO box address
- Nick adds XYZ as an ABC-approved vendor
- Nick generates a few \$500 monthly invoices from XYZ for "consulting services" and arranges for ABC to pay them
- Thinking he's in the clear, Nick later increases the XYZ invoices to \$2,499 and submits them on a semi-monthly basis



Getting to Know the Perpetrator

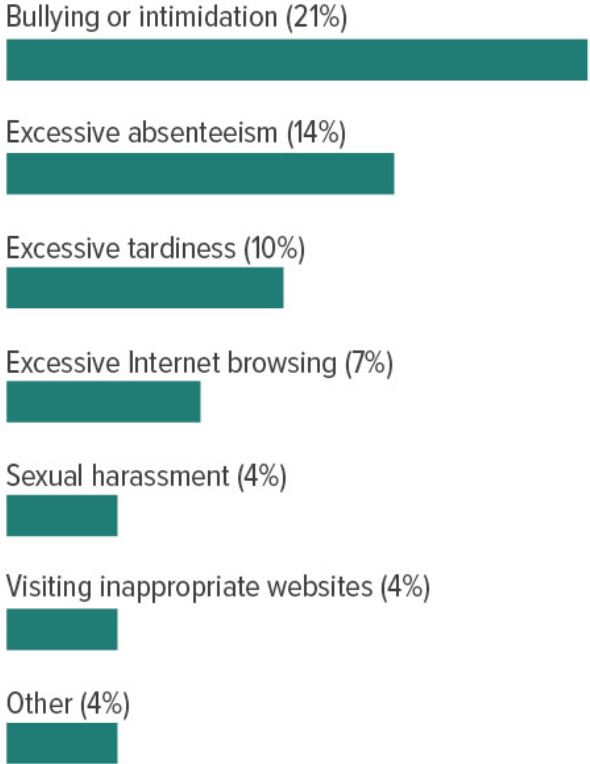
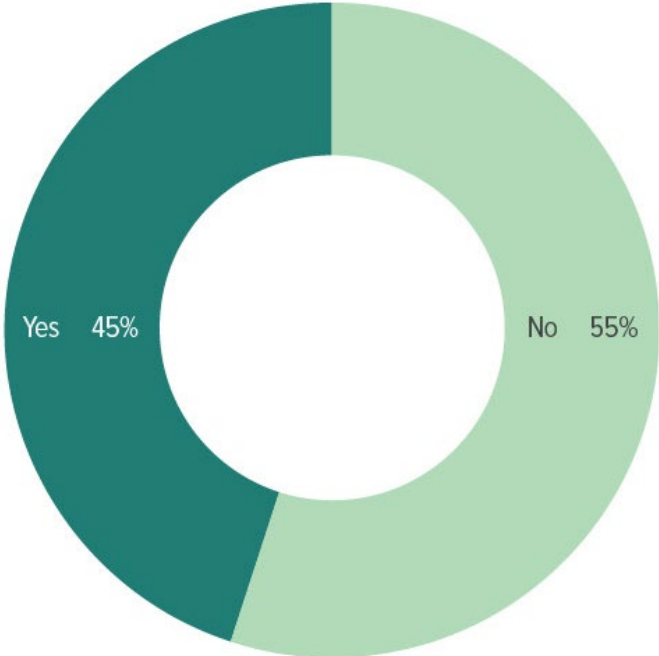
Attributes of an Embezzler



What does someone that commits these types of acts look like?

- 72 percent of incidents committed by those who held finance/bookkeeping and accounting positions
- Average scheme lasted nearly 5 years
- Most common embezzlement scheme involved the issuance of forged or unauthorized company checks.
- Of the cases where the motivation was known, nearly 22 percent of perpetrators had gambling issues
- Only 5 percent had prior criminal history
- The average embezzler stole \$15,189 per month from employers
- 64 percent were female, but male perpetrators on average embezzled about 25 percent more.
- 90 percent of the cases involved individual perpetrators
- Average age at the beginning of the theft: just under 43.

Do fraud perpetrators also engage in non-fraud related misconduct?



Source: ACFE's Report to the Nations: Global Study on Occupational Fraud and Abuse

AHC's unfortunate experience

Background on AHC & AHC Foundation

- Who we are, What we do
- Annual Revenues
- Internal Controls and Checks/balances

Forgery, Embezzlement & Deceit

- Our story of discovery
- Diversity of methods used by employee embezzled
- Ramifications of the embezzlement
- Legal actions we took and why
- Explain the outcomes (criminal case, civil cases, etc.)
- Outline changes we made to our policies, practices and controls
- Now for the rest of the story – another association's sad tale...

**Mission of the American Horse Council (501C6)
To Protect & Strengthen the United States Equine Industry**

Legislative Advocacy/ Regulatory Liaison
Industry Initiatives
Education and Leadership Development

**Mission of the American Horse Council Foundation
(501C3) Perform charitable, scientific and educational activities associated with the equine industry**

Economic Impact Studies
Equine Research
Workforce Development



*8mo
1/11/2018*



410-01-01-00 12201 U O C 001 30 T 63 001
AMERICAN HORSE COUNCIL FOUNDATION INC
1616 H ST NW FL 7
WASHINGTON DC 20006-4918

December

Your account statement

For 12/29/2017

Contact us



BBT.com



(800) BANK-BBT or
(800) 226-5228

BB&T is pleased to announce that beginning on Dec. 11, 2017, the available balance in your account will be updated multiple times throughout the day upon receipt of a same-day, electronic, direct deposit transaction. If a same-day direct deposit is received to your account by 5 p.m. local time, Monday through Friday, on regular business days you will have intraday access to these funds earlier in the day which allows you to better manage your cash positioning.

Please feel free to contact your local financial center or call Phone24 at 800-BANK-BBT (800-226-5228) if you have any questions.

Thank you for banking with BB&T.

BB&T, Member FDIC

■ COMMUNITY INTEREST CHECKING 0005162950020

Account summary

Your previous balance as of 11/30/2017	\$541,155.03
Checks	- 7,889.06
Other withdrawals, debits and service charges	- 35.00
Deposits, credits and interest	+ 10,100.94
Your new balance as of 12/29/2017	= \$543,331.91

Checks

DATE	CHECK #	AMOUNT(\$)
12/19	10160	7,889.06
Total checks		= \$ 7,889.06

Other withdrawals, debits and service charges

DATE	DESCRIPTION	AMOUNT(\$)
12/21	SERVICE CHARGES - PRIOR PERIOD	35.00
Total other withdrawals, debits and service charges		= \$35.00

Deposits, credits and interest

DATE	DESCRIPTION	AMOUNT(\$)
12/18	DEPOSIT	10,000.00
12/19	DEPOSIT	100.00
12/29	EFFECTIVE DATE 12-31-17 INTEREST PAYMENT	0.94
Total deposits, credits and interest		= \$10,100.94

Interest summary

Interest paid this statement period	\$0.94
2017 interest paid year-to-date	\$19.81
Interest rate	0.01%

410-01-01-00 12201 U O C 001 30 T 63 001
AMERICAN HORSE COUNCIL FOUNDATION INC
9432 PARAGON CT
OWINGS MILLS MD 21117-1407

BANK

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BB&T, Member FDIC

■ COMMUNITY INTEREST CHECKING 0005162950020

Account summary

Your previous balance as of 11/30/2017	\$218,590.16
Checks	- 7,889.06
Other withdrawals, debits and service charges	- 124,769.95
Deposits, credits and interest	+ 10,101.29
Your new balance as of 12/29/2017	= \$96,032.44

Checks

DATE	CHECK #	AMOUNT(\$)
12/19	10160	7,889.06
Total checks		= \$ 7,889.06

Other withdrawals, debits and service charges

DATE	DESCRIPTION	AMOUNT(\$)
12/04	BB&T BUSINESS ONLINE TRANSFER TRANSFER TO CHECKING 0005162950012 12-04-17	50,000.00
12/08	BB&T BUSINESS ONLINE TRANSFER TRANSFER TO CHECKING 0005162950012 12-08-17	25,000.00
12/12	BB&T ONLINE EXTERNAL TRNSF-DR TRIALDEBIT USAA FSB 1172853351	124,734.95
12/12	INTERNET PAYMENT LOAN USAA.COM PAYMNT 5100260	49,734.60
12/21	SERVICE CHARGES - PRIOR PERIOD	35.00
Total other withdrawals, debits and service charges		= \$124,769.95

Deposits, credits and interest

DATE	DESCRIPTION	AMOUNT(\$)
12/12	BB&T ONLINE EXTERNAL TRNSF-CR TRIALCREDIT USAA FSB 3347 ASHLEY FURST	0.10
12/12	BB&T ONLINE EXTERNAL TRNSF-CR TRIALCREDIT USAA FSB 3349 ASHLEY FURST	0.25
12/18	DEPOSIT	10,000.00
12/19	DEPOSIT	100.00

continued

Anti-Fraud Programs & Controls



Weaknesses at Nonprofits



Source: ACFE Report to the Nations

What is the frequency and median loss by initial detection of fraud?

Detection Method	Frequency	Median Loss
Tip	40%	\$147,000
Internal Audit	15%	\$100,000
Mgmt. Review	13%	\$135,000
By Accident	7%	\$250,000
Account Reconciliation	6%	\$85,000
External Audit	4%	\$470,000
Police	2%	\$1,000,000
Surveillance	2%	\$48,000
Confession	1%	\$500,000

Source: ACFE's Report to the Nations: Global Study on Occupational Fraud and Abuse

NFP Fraud

QUESTION:

Would you be a whistleblower of fraud in your organization?

A) Yes

B) No

FIG. 22 How does the presence of anti-fraud controls relate to median loss?

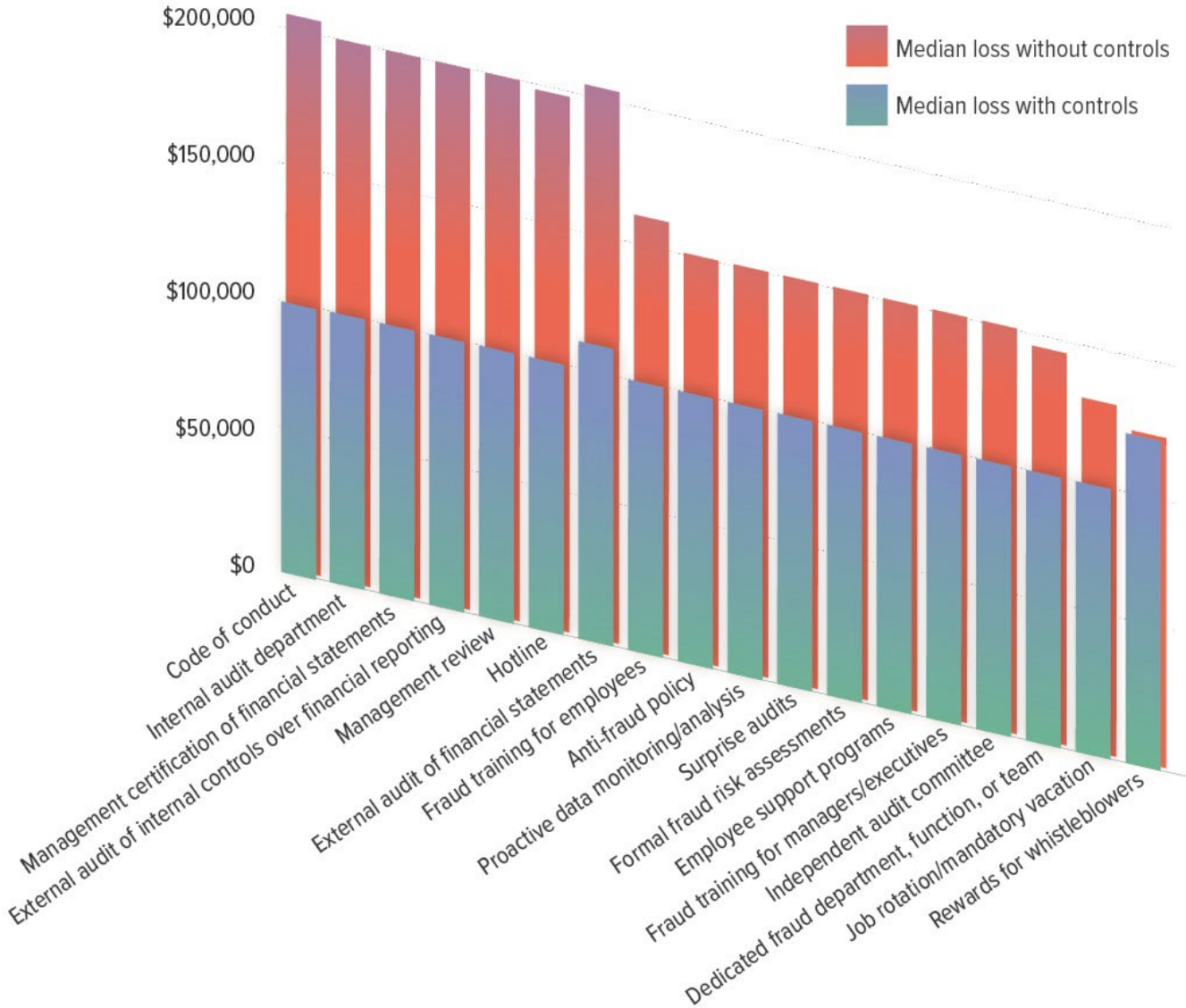
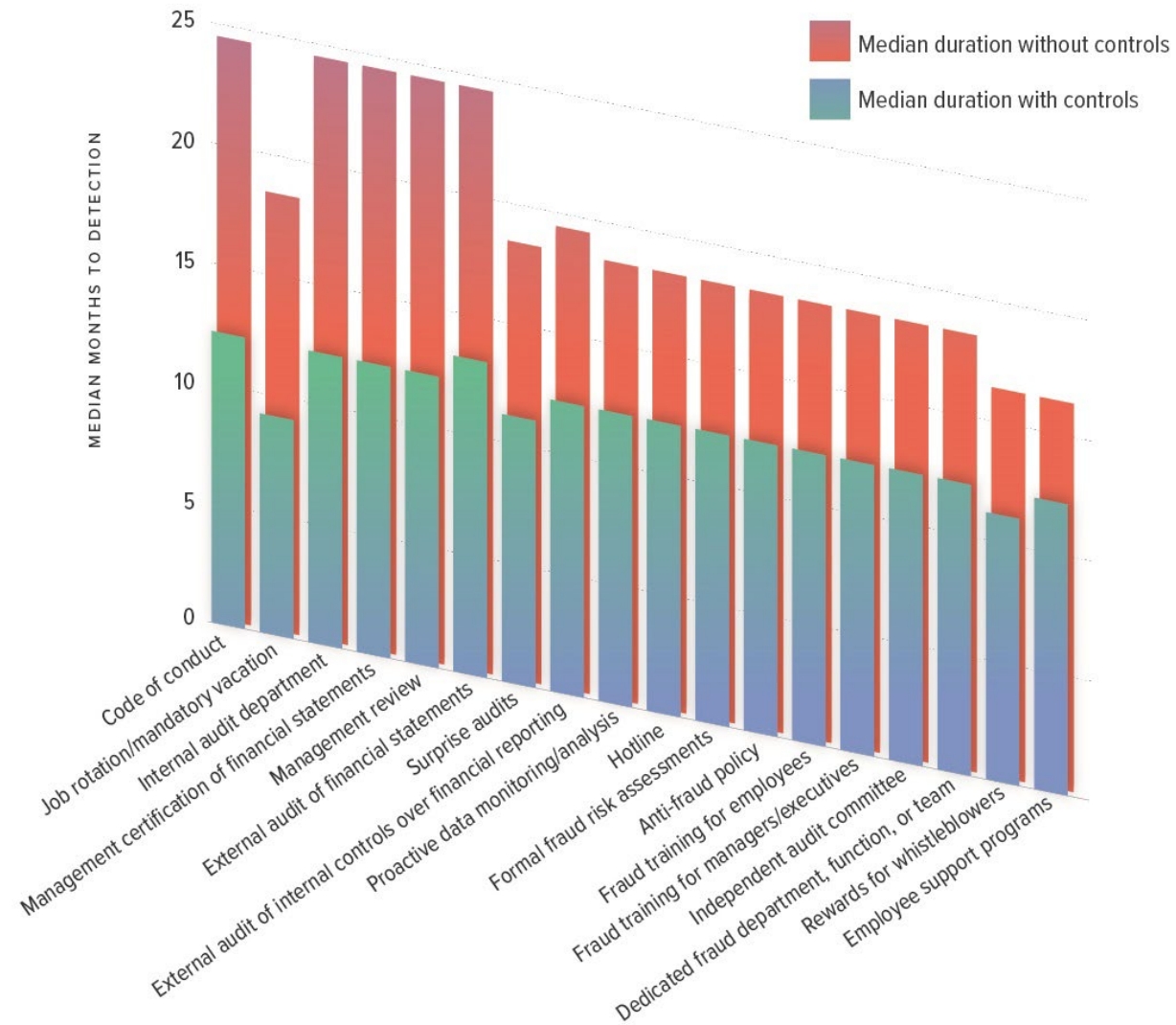
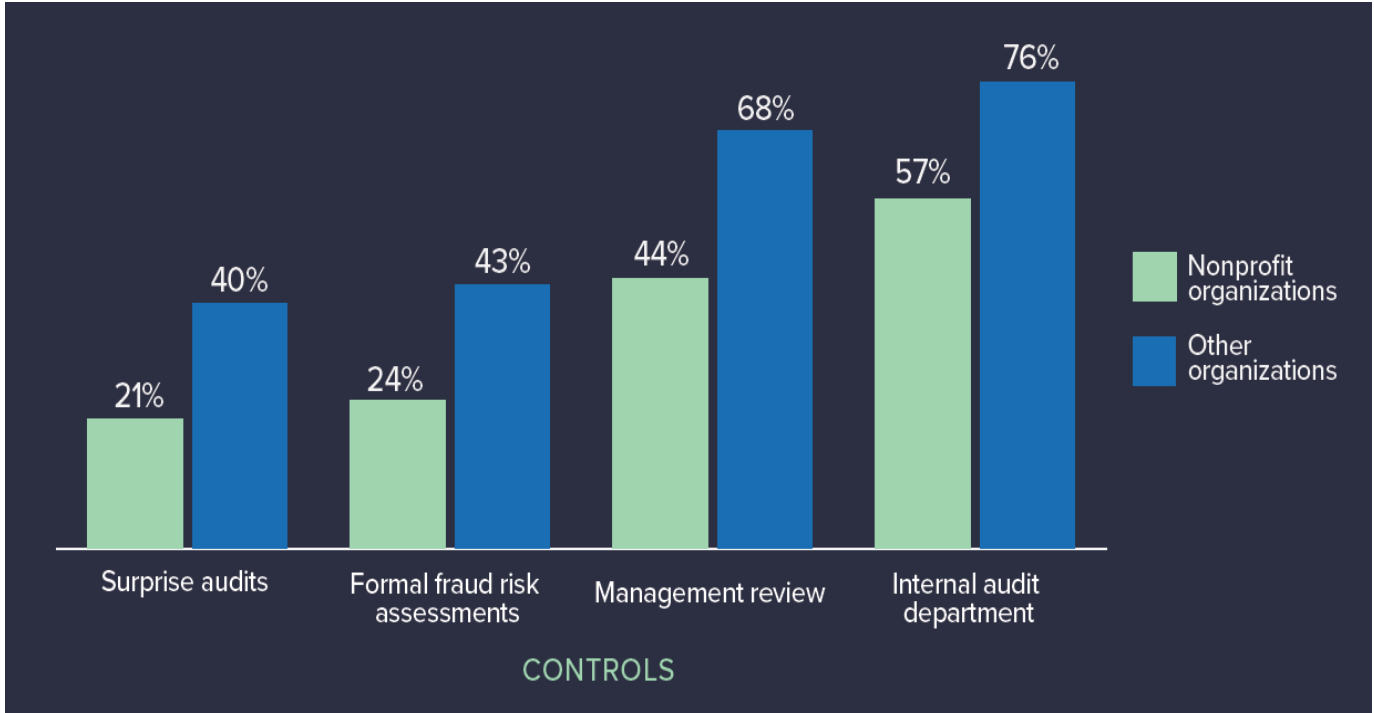


FIG. 23 How does the presence of anti-fraud controls relate to the duration of fraud?

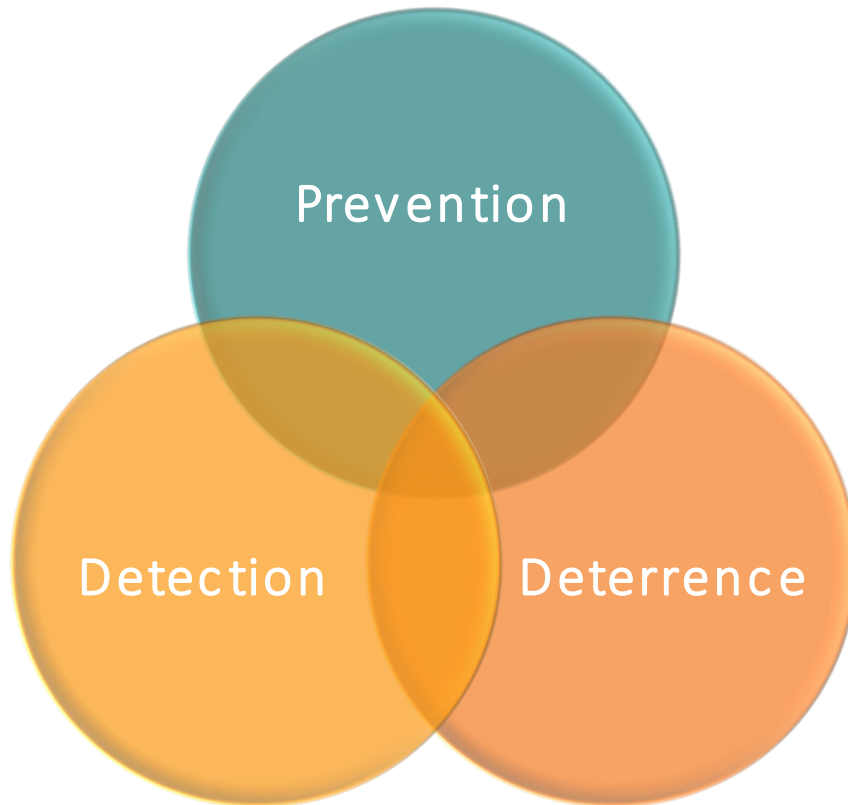


Controls at Nonprofits Compared to Others



Source: ACFE Report to the Nations

Effective Controls



Prevention

- Code of conduct
- Employee counseling services
- Fraud training
- Employee background checks
- Mandatory vacations, job rotation
- Segregation of duties

Detection

- Fraud hotline
- Financial statement trend analysis
- Monthly financial statement preparation and review
- Monthly reconciling of accounts
- Surprise (internal) audits
- External audit
- Employee exit interviews

Deterrence

- Prosecuting fraud perpetrators

Segregation of Duties

Human Resources

- Is there a mandatory vacation policy?
- Is the hiring function separate from payroll processing?

Cash Receipts

- Is the sales function separate from credit approval?
- Does the A/R clerk also handle customer complaints?

Cash Disbursements

- Does the person who signs checks also perform bank reconciliations?
- Do checks over a certain threshold require dual signatures?
- Who approves new vendors?

Financial Management

- Are financial statements prepared monthly and reviewed by an executive?
- Are A/R and A/P reports reconciled to the G/L on a monthly basis?



Taking Action



Fraud Prevention Check-Up

ACFE has a Fraud Prevention Check-Up tool available here:
<http://www.acfe.com/fraud-prevention-checkup.aspx>

Questions include:

- Risk Assessment
 - To what extent has the organization established a process for oversight of fraud risks by the board of directors or others charged with governance?
 - To what extent has the organization created “ownership” of fraud risks by identifying a member of senior management as having responsibility for managing all fraud risks?
- Anti-fraud controls
 - To what extent has the organization implemented measures to eliminate or reduce each of the significant fraud risks identified in its risk assessment?

Fraud Risk Assessment

Understand the controls that are in place

- Are they being followed?

What controls should be added?

- Prioritize based on level of risk
- Costs vs. benefits

Are there ineffective controls in place that should be removed?

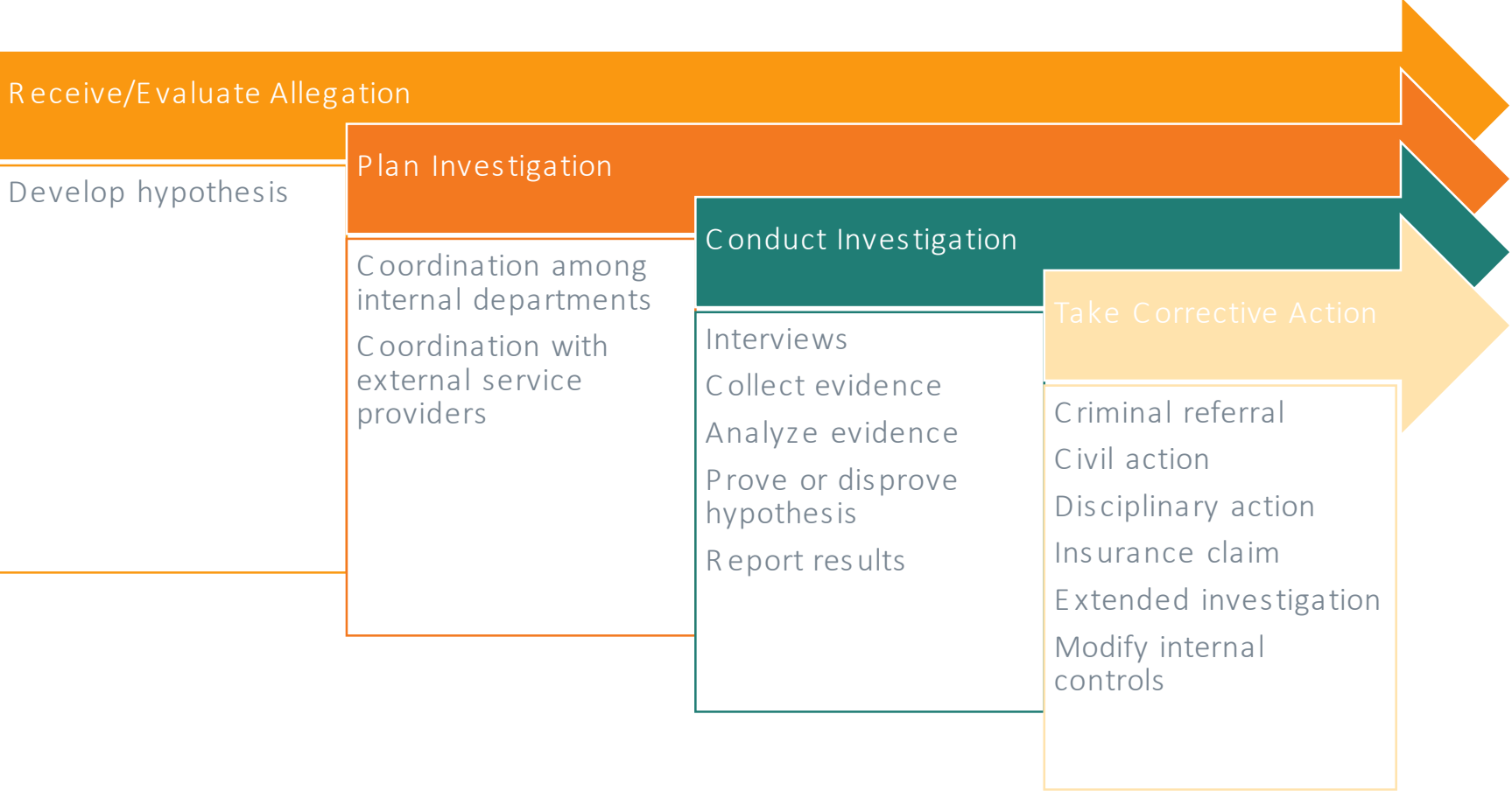
Risk assessment should consider:

- fraud **prevention** controls
- fraud **detection** controls

Trying to prevent **all** fraud generally is **not** cost-effective

- No guarantee you can prevent **all** fraud, no matter what controls you have

Fraud Investigations



WHAT are we assessing?

RISK UNIVERSE

Strategic

Governance:

- Board Performance
- Tone at The Top
- Control Environment
- Corporate Social Responsibility

Planning and Resource Allocation:

- Organizational Structure
- 3rd Party Relationships
- Strategic Planning
- Annual Budgeting
- Forecasting
- JV's /Alliances and Partnerships
- Outsourcing Arrangements

Major Initiatives:

- Vision and Direction
- Planning and Execution
- Measurement & Monitoring
- Technology Implementations
- Technology Support

Market Dynamics:

- Competition
- Macro-Economic Factors
- Lifestyle Trends
- Socio-Political

Communication & Investor Relations:

- Media Relations and Investor Communications

Marketing:

- Marketing
- Fundraising
- Membership Development
- Intermediary Relationships

People/Human Resources:

- Culture
- Recruiting & Retention
- Development & Performance
- Succession Planning
- Compensation & Benefits

Information Technology:

- IT Management
- IT Confidentiality
- IT Availability/Continuity
- IT Spend
- IT Integrity
- IT Infrastructure

Operations

Business Interruptions:

- Natural Events
- Terror & Malicious Acts
- Outages

Assets:

- Real Estate
- Physical Assets
- Information Assets/Records

Core Operating Processes:

- Portfolio Management
- Pricing and Valuation
- Investment Accounting
- Investment Performance and Attribution
- Safeguarding of Client Assets
- Service Provider Oversight
- Contract Management

Financial

Liquidity Risk Management:

- Liquidity Risk
- Cash Management
- Funding
- Insurance

Credit Risk Management:

- Credit Risk
- Credit and Collections
- Settlement Risk
- Counterparty risk

Accounting and Reporting:

- Accounting, Reporting and Disclosure
- Internal Control

Code of Conduct : Legal & Regulatory:

- Ethics
- Fraud

Legal & Regulatory:

- Federal Laws
- International Compliance
- State Laws
- Intellectual Property

Legal & Regulatory (Cont):

- Litigation and Discovery Response
- Supervision
- Customer Protection
- Data Protection and Privacy

Compliance



ACFE FRAUD PREVENTION
CHECK-UP

ACFE Check-Up

One of the ACFE's most valuable fraud prevention resources, the ACFE Fraud Prevention Check-Up is a simple yet powerful test of your company's fraud health. Test fraud prevention processes designed to help you identify major gaps and fix them before it is too late.

- Proactively identify and manage your fraud risks
- Pinpoint opportunities to save you money
- Organization that fails to protect itself appropriately faces increased vulnerability to fraud
- Most organizations score very poorly in initial fraud prevention check-ups
- Fraud prevention processes help increase the confidence of Audit Committee and public

ACFE Check-Up

- Fraud risk oversight – Audit Committee
- Fraud risk ownership
- Fraud risk assessment
- Fraud risk tolerance and risk management policy
- Process-level anti-fraud controls / reengineering
- Environment-level anti-fraud controls
- Proactive fraud detection - compliance

Thank you!



Greg Plotts, CPA

Partner - Aprio, LLP

301.231.6226

Greg.Plotts@aprio.com



Julie Broadway, CAE

President – American Horse Council
and American Horse Council
Foundation

202.296.4031

jbroadway@horsecouncil.org