

# Don't Let Employee Theft and Embezzlement Be A Hidden Employee Benefit Funded Through Your Organization

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**H**ave you seen the news recently? During the second week of April 2011 alone eight news stories appeared highlighting nonprofits victimized by employee embezzlements. They included Beville State Community College, Nicolas Valley Elementary School's Parent Teacher Association, Long Beach Pee Wee Football League, Compton Community College, Revere Public Library, Mecklenburg County Open Door (MOD), Maine Trial Lawyers Association, and Eastern Shore's Own Arts Center. Unfortunately, the attention brought to each of these organizations was not the attention each likely wanted.

And that does not tell the whole story. People don't hear about most of the cases like this. In fact, it's been estimated only one in nine is ever reported in the media. Most embezzlement cases, eight out of nine, are quietly resolved, avoiding any publicity. So what does that mean? We can assume there's a lot more employee

embezzlement cases among non-profit than most of us know. If you take that week and multiply those eight stories by nine, it means that there were an estimated seventy-two instances of employee theft or embezzlement during the same time period, one week. Now multiply that by 52 weeks, and you get a sense of just how a big a problem employee theft and embezzlement has become.

There are few enough dollars for non-profits as there is. Considering the state of our economy, decreased federal and state funding, and the expected decline in continued support for non-profit organizations. That means that it is incumbent on every organization to ensure that every dollar is appropriately collected, deposited, tracked, recorded and used for your organization's programs, and not susceptible to being diverted by an employee for personal purposes. Individuals today are living beyond their means and at times are trying to make ends meet under a significant level of stress. These conditions are ripe for employees to cross the line of honesty and trustworthiness, rationalizing their behavior while stealing your funds.

When it comes to identifying an approach to minimize the risk for employee theft and embezzlement, there are three measures any organization can implement. First, controls, policies and procedures must be used to prevent as many opportunities as possible. Second, every organization needs to implement measures to detect any instances of fraud, theft or abuse as quickly as possible to minimize the loss to the organization. Third, and arguably most important, the organization needs to ensure that they maintain adequate employee crime or dishonesty insurance coverage. An insurance claim may be your organization's only way to reclaim diverted funds because recovering funds from the suspect is often futile.

Adequate coverage is subjective to every organization, but the minimum for determining adequacy should start at \$100,000. Also, make you're your policy covers the costs of the investigation. This price tag could easily be in the tens of thousands or substantially more.

When evaluating the strength of your internal controls start with its overall culture and environment. What is the "tone" that the board sets for the employees and volunteers? Are they clear about things like ethical standards and zero tolerance? What mechanisms have they put in place to report employee concerns about fraud? In a recent fraud survey, employee tips accounted for more than 40 percent of the reported cases. Knowing the largest percentage of cases is brought to light in this fashion rather than through controls and procedures, every organization needs to ensure that 1) they establish a means to solicit employee tips and information; 2) they expect every individual within the organization to come forward when they suspect potential fraud or illegal acts; and 3) they have established means for communicating such information throughout in the organization.

What about the detailed financial policies and accounting procedures of an organization? Where should you start? I strongly suggest starting with cash receipts no matter where or how funds come into the organization. Every organization collects payments, receipts and funds for the programs and services they provide. Often there are multiple revenue sources, and each must be objectively evaluated to determine where opportunities for fraud exist. In many cases, organizations receive grant proceeds, program reimbursements and other payment sources electronically that go directly into the organization's bank account. This goes a long way towards eliminating opportunities for



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employees to steal inbound funds. However, most organizations do receive other sources of payments in the form of checks, credit cards, debit cards and cash. These can make embezzlement all too tempting for some employees with doubtful morals. Fundraising and special events often create the most vulnerability, as strong internal controls are seldom incorporated into these events, creating an opportunity to skim proceeds with little risk of detection.

It is critical to the organization's cash flow that it incorporates internal controls, checks and balances, segregation of duties and other measures into all processes. Theft of receipts and payments intended for the organization are a high risk because it is relatively easy to divert these payments and conceal the diversions.

If the organization does any development, this area too has become a breeding ground for employee theft. Often the development department operates with their own system, and the finance department records whatever development provides. The question is this: has development provided everything that was generated and collected? To ensure that all activity within development is recorded and reconciled completely, accurately and in a timely they need to involve the finance departments.

Although cash receipts are the vulnerable areas for fraud in nonprofits, don't overlook all the other areas, such as purchasing, cash disbursement, payroll, electronic banking, recon-

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**And as always, there is no substitute for vigilance. Nonprofits are the keepers of the funds that can and do change lives. You have an obligation to use them wisely and protect them for their intended use. It is the covenant you have with your donors and the people they expect you to benefit.**

ciliations and monthly reporting. Those intent on fraud are very good at compromising these as well, so make sure they too have stringent internal controls placed on them.

I highly recommend every organization assess their current level of internal controls, and consider having someone independent and outside of the organization provide an objective evaluation of their systems. This will minimize the risk of becoming a victim of an embezzlement scheme. If the organization has an annual financial statement audit, talk about the internal controls with the auditors. Find out what they do, and determine how they will provide feedback to improve existing controls as well as lesson risks and opportunities. It is not only a great idea, it is required of them under current financial statement auditing standards.

For those without an audit, consider engaging someone outside of the organization to evaluate the internal controls of the organization, and provide written observations and recommendations on how to improve the controls to minimize the risk of theft and embezzlement.

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#### *About the Author*

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