

Non-Profit Fraud – A Canadian Overview

By James F. Finlay

A Canadian Overview

Fraud occurs every day in Canada. Now that we are in an economic down turn it is more likely that fraud will show its ugly head as pressures start to take hold on individual lives. In a recent report *Detecting Occupational Fraud in Canada* (a report by the Association of Certified Fraud Examiners and Dr. Dominic Peltier-Rivest, Ph.D,M.Acc,CFE of Concordia University), the non-profit median loss was \$72,000 per fraud occurrence and represented 10.1% of the total organizations studied. Fraud in a non-profit not only affects the organization economically, it also hits the organization where it really hurts—in its reputation. Because non-profits rely heavily on private or government support, a blow to an organization's credibility would be crippling. So it is vital to understand how and why fraud is so prominent in nonprofits. The culture in a non-profit is one of trust. The general perception of non-profit workers is that they are compassionate and ethical people. Because it is difficult to imagine trusted colleagues perpetrating any sort of fraud, the organization frequently does not have the basic, formal controls in place that discourage fraud. This trusting environment is exactly what a dishonest employee exploits.

So what is fraud?

The legal definition in The Criminal Code of Canada S. 380(1) - Everyone who, by deceit, falsehood or other fraudulent means, whether or not it is a false pretence within the meaning of this Act, defrauds the public or any person, whether ascertained or not, of any property, money or valuable security or any service.

In other words:

- theft by lying or cheating;
- using acts of forgery and false documents;
- engaging in deceptive behaviour; and
- manipulating information.

Fraud vs Theft

- fraud is hidden, victim will part with property based on representation and there is a time lag.
- theft is overt, victim is unwilling to part with property and it is immediate.

Key indicators

In order for fraud to occur the following highlighted elements must exist, Dr Donald Cressy who is a criminologist calls this the fraud triangle;

- **Pressure** comes from a 'non-shareable' financial problem that can't be shared or solved in a legitimate way. It might a drug or gambling addiction, desire to impress friends or problems with a loan that must be re-paid urgently. Non-shareable problems involve some sort of

embarrassment or shame. They threaten the fraudster's status as a person who is trusted by others. In almost every fraud case, their financial problem relates to gaining or maintaining status.

• **Opportunity** arises when the fraudster sees a way to use their position of trust to solve the financial problem, knowing they are unlikely to be caught. In a non-profit this may include a position of authority, segregation of duties and lack of policies or policies not enforced.

• **Rationalisation** is the third part of the triangle. Cressey says most fraudsters are first-time offenders with no criminal record. They see themselves as ordinary, honest people who are caught in a bad situation. This lets them justify the crime to themselves in a way that makes it acceptable or justifiable. They may say they were 'just borrowing it', felt they were entitled to it, had to look after their family or felt they were being underpaid and therefore deserved it. Sometimes they feel the employer is dishonest and should be 'sharing the spoils'.

The fraud may be further driven by these specific indicators:

- financial problems, possible due to marriage breakdown or heavy debt load;
- delusions of grandeur;
- an inflated ego;
- a craving for success;
- reluctance to take vacations;
- living beyond one's means;
- sudden mood swings or personality changes; and the
- inability to keep up with regular work responsibilities. an atmosphere of trust;
- many cash donations, which are difficult to control;
- financial restraints, resulting in limited availability of qualified staffing resources;
- high staff turnover;
- management pressures;
- a mixture of volunteers and employees with a lack of business/financial experience involved in operations.

These factors are frequently characterized as the typical 'red flags' that may indicate the potential for fraud. If in addition, the non-profit has lax or non-existent internal controls, fails to segregate duties and has a willingness to put its trust in the wrong hands, you have the explosive combination that spells opportunity.

In the next article, we will look at the types of schemes that the fraudsters use.

Acknowledgements

ACFE, Dr. D. Peltier-Rivest, J Miller, S Douglas, K Wilson, K Mills, G Moulton, Deloitte & Touche

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