Embezzlement: It Can Happen to Any Organization

Embezzlement by employees can take many forms -- from the simple use of a company credit card to buy inexpensive personal items to complex check forging schemes that result in massive losses. Take a look at these court cases, which illustrate some of the ways not-for-profit organizations can be defrauded:

- A former chief financial officer of the Capital Area United Way in Michigan pleaded guilty to embezzling nearly $2 million by writing checks to herself and forging the co-signatures of superiors. The financial executive's fraudulent activity was only discovered after she resigned her position and the new CFO discovered the trail of missing checks.

- A former employee of a West Virginia not-for-profit, chartered to assist senior citizens and the mentally ill, pleaded guilty to a theft scheme in which she embezzled nearly $800,000. Responsible for the organization's finances, she charged more than $200,000 to an American Express Account as well as made direct deposits into her personal bank accounts.

- A former program administrator of a Washington, DC, organization that supports science education pleaded guilty to embezzling more than $200,000 that was earmarked for public schools.

These are just a few of the countless cases that wind up in courtrooms nationwide. However, don't think it doesn't happen in your own backyard. Annually, KerberRose SC and other public accounting firms in Wisconsin assist organizations who have fallen victim to embezzlement. When a not-for-profit falls victim to embezzlement, the perpetrator is often an unlikely suspect. Fortunately, there are warning signs and ways to detect and prevent internal theft. Here are some steps your organization can take to help avoid becoming another embezzlement statistic:

Where there’s Smoke, there May Be Fire

According to the Association of Certified Fraud Examiners, workplace fraud typically takes a year and a half to discover. One of the most important tools management has in uncovering potential embezzlement early is critical observation. Behavioral warning signs may suggest employee wrongdoing.

Some traits sometimes exhibited by those convicted of embezzlement include:

- Abrupt shifts in work schedules.
- Declining to take vacations.
- Sudden changes in lifestyle such as buying a larger home and driving a more expensive car.
- Problems with drug abuse, alcoholism or gambling.

On their own, these behavioral changes may be explainable. But take note if they arise in conjunction with financial abnormalities.

Listen to Employees. They May Know About Colleagues' Fraudulent Behavior

Embezzlement usually occurs when motive combines with opportunity. In the workplace, if an employee is disgruntled or has financial problems, fellow staff members are often the first to hear about it. Having a system in place for colleagues to report suspicious behavior often makes
the difference between embezzlement going undetected and having the information reach the desks of upper management.

One of the most useful and cost-effective internal controls is a hotline where employees can immediately report concerns or suspicious activity with a degree of anonymity. The Association of Certified Fraud Examiners found that workplaces with an employee hotline were able to detect fraud an average of nine months earlier than those that did not have a reporting system in place.

When a hotline is part of a system of internal controls, concerns can be investigated quietly and without necessarily confronting employees who may be innocent of wrongdoing. If circumstances are thoroughly investigated and suspicions found to be unwarranted, the employees involved may not have to know about them. Keep in mind that false accusations can lead to discrimination charges and other legal actions.

Our firm provides a service, that includes a hotline, for individuals to report fraud. Employee tips are the number one way fraud is detected. Please contact KerberRose SC if this is something your Organization may be interested in.

Consider Consulting a Forensic Accountant

When it comes to embezzlement, it is best to err on the side of caution because detecting crimes early can save your organization considerable further losses. Many times, a convoluted paper trail makes it difficult to determine whether embezzlement has occurred.

A forensic accountant can efficiently ascertain whether fraudulent activity is underfoot at your not-for-profit organization. Like the old saying goes, an ounce of prevention is worth a pound of cure.

KerberRose has forensic accountants on staff – contact us for additional information.

More Steps to Consider

• Require two signatures on checks. Don't use payroll signature stamps.
• If cash deposits are made, send only trusted, long-term employees to the bank.
• Check bank account statements and make sure accounts payable and accounts receivable match up. Don't allow the employee who writes or deposits checks to balance bank statements.
• Establish transaction controls for electronic fund transfers from company bank accounts.
• Review credit card statements for personal charges. Ensure every credit card transaction has a receipt to support the charge.
• Do credit and criminal background checks on employees prior to hiring them, especially those handling payroll, checks or cash. Conduct an Internet search on applicants.
• Have more than one employee handle duties when it comes to payroll and handling cash and checks.
• Set a good example and make workplace ethics clear.
• If records are disorganized or important financial documents can't be located, call in a forensic accountant to follow the paper trail.

An Insurance Review

From natural disasters to frivolous lawsuits, bad things sometimes happen to good organizations. Unfortunately, the good your organization does is of little help in most of these situations.

Assessing and managing risk is a board responsibility. Do you meet annually with your insurance agent to perform a risk assessment? If not, you should be! Begin the process with some serious “scenario” planning. What might go wrong and what could happen if it does? When a risk is insurable, and many are, find out if your organization has the necessary insurance to cover it. You may also find that you are over insured and you are paying unnecessary insurance costs.

No single insurance policy will provide all the protection your organization needs. It will probably require several different policies to ensure adequate coverage. Here are some of the most common types of insurance for not-for-profits:

Commercial General Liability (CGL). This insurance provides coverage for accidents involving people who are not employed by the organization, such as visitors and clients who are injured on the organization's property.

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Directors & Officers (D&O). As the name implies, D&O insurance protects directors and officers when they are sued personally for things that allegedly happened in the course of their work with the organization and led to financial loss.

Errors & Omissions (E&O). In the medical world, E&O is known as malpractice insurance. The focus is negligence that occurs in the ordinary course of a nonprofit’s activities. For not-for-profit organizations, E&O and D&O insurance can overlap. Be clear about which risks are covered by which policy.

Commercial Property. This covers damage to physical property, including the organization’s equipment, supplies, and office space, from storms, fire, and similar events.

Auto. This insurance is essential if a nonprofit’s staff or volunteers drive vehicles in the course of their work for the organization.

Umbrella/Excess Liability. These policies increase the amount of the organization’s liability insurance protection. As with the other types of insurance, read the fine print carefully to understand exactly what protection is provided.

Specialty Policies. These are policies and endorsements that cover unique circumstances and risks. It is wise to thoroughly research any nontraditional insurance products you are contemplating to ensure they will actually cover your needs.

As a final note, be sure to inform your insurance company of any changes that might affect coverage. For example, adding programs or activities or changing the structure of your organization could void a policy.

Fiscal Sponsorship

What is fiscal sponsorship and why would a program/organization want to be sponsored?

“A fiscal sponsor is a not-for-profit organization (501c3) that provides fiduciary oversight, financial management, and other administrative services to help build the capacity of charitable projects/organizations.”

Fiscal sponsorship is often used by newly formed not-for-profits that need to raise money during the start-up phase, before they are recognized as tax-exempt by the IRS.

Biggest Reason for Fiscal Sponsorship – Tax Exemption and Donor Deductibility:

Using a fiscal sponsor enables a program or organization that does not itself qualify as tax-exempt to attract funding for its operations that will, through the fiscal sponsor, be tax-deductible to donors. Donors can only claim a tax deduction when their donations are given to a qualified organization (one that is recognized for tax exemption – 501(c)3). Additionally, many private foundations require that grantees be recognized by the IRS as tax-exempt.

Other reasons:

• TEST-DRIVE AN IDEA: Fiscal sponsorship might be chosen by a newly formed nonprofit that seeks to test-drive its ideas, to determine whether there is a market, or a desire among the donating public, to fund the end product.

• COMFORTABLE: Some organizations/programs remain in a fiscal sponsorship relationship for a long time, deciding that their mission can be achieved in that structure without creating a new entity.

• COST/BENEFIT: Some organizations - including those that are tax-exempt - find that utilizing a fiscal sponsor to outsource administrative responsibilities, whether back-office tasks, or those relating to fundraising and disbursement of funds, is the right business model for them. This structure might be particularly well-suited for all-volunteer organizations.

What about the sponsor organization’s tax exemption?
The fiscal sponsor must first determine that serving as a fiscal sponsor is consistent with its mission (and does not...
Meet a Member of Our Not-for-Profit Audit Team

Jamie is a senior manager in our Fox Cities office. She has more than eight years of accounting and auditing experience and has been with KerberRose SC for six years. Jamie spends her time providing financial auditing and accounting services for not-for-profit organizations, housing projects, low income housing organizations and employee benefit plans. She also provides A-133 compliance audits of federally funded programs and prepares Form 990, Return for Organizations Exempt from Income Tax.

In her free time, Jamie volunteers as the treasurer of a local not-for-profit as well as spending time with her husband. She also enjoys her time with family, cooking, working out and reading a good book.
How well the economy is recovering from the “great recession” is debatable. And in spite of an increase in charitable giving in 2013, two 2014 surveys paint a troubling picture for the nonprofit sector.

The 2014 State of the Nonprofit Sector Survey* involving more than 5,000 nonprofits revealed the following:

- 80% experienced an increase in demand for services in 2013 -- for the sixth straight year
- 56% were unable to meet demands in 2013
- 55% had three months or less cash on hand
- 41% said achieving long-term financial stability is a top challenge

On the positive side, organizations responded to the continuing stress in several ways:

- 49% collaborated with another organization to improve or increase services
- 48% invested money or time in professional development
- 40% improved efficiency by upgrading hardware or software

Many organizations rely heavily on the government to pay for the services they provide. A recent study by The Urban Institute** examined trends in government contracts. According to that study:

- 54% said payments do not cover the full cost of contracted services
- 72% said application and reporting processes are too complicated
- 44% reported that agencies change their contracts midway through the contract period
- 45% complained of late payments

The study went on to show that funding cuts caused 38% of the organizations to end 2012 with a deficit. As a result, over half of them froze or reduced employees’ salaries, and 42% dipped into their financial reserves. Surprisingly, only 11% reduced services or programs.

* Conducted by the Nonprofit Finance Fund
** The National Study of Nonprofit-Government Contracts and Grants 2013: State Profiles, April 2014, The Urban Institute

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**Computer Security Tips from KerberRose Technology**

By Jenni Beyer, System Manager for KerberRose and KerberRose Technology Division.

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Most Americans rely on computers to stay in touch and be more productive. When there’s a computer failure or security breach, it becomes painfully obvious how important computers are in our daily lives. Here are a few tips for securing your computer and protecting your personal data.

1. Install security software and update it on a regular basis. Antivirus software is a must have. When installing Antivirus software, be sure to turn on the automatic update feature. New viruses and spyware are created every day, so it is important that your software is up-to-date and can detect new threats.

2. Use multiple, strong passwords to secure your computer as well as your online accounts. Never use the same password to secure all of your accounts. A helpful hint is to use a root password in all passwords, but vary the beginning and the end. For example, one website may be 14KingCobra14, and another may be AmazKingCobra01!. The pre and post portions may relate to the website or account they secure.

3. Be suspicious of email from anyone you do not know. Spam emails often look legitimate but can be used to carry viruses or take you to malicious websites that will download software to infect your computer. When in doubt, do not open any email from someone you don’t know.

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1. Backup your important data. This protects you against accidental deletion, file corruption and hardware failure. Storing important documents in a central location and backing up that data on a daily basis is highly recommended. One option is to use one of the companies that offer online backup services. If you backup your data to a removable storage device, remember to store the backup in a location other than where your main computer is located. You may lose both your main computer and your backup if there is a fire at your facility or home and your backups are not stored remotely.

If you would like to learn more about keeping your data secure, KerberRose Technology can help. Our team provides traditional networking, computer repair, server maintenance, and workstation setup for businesses throughout northeastern Wisconsin. Our team, with a combined 30 years of experience, can help you align your technology solutions with your business objectives and operational requirements.

Visit us online:
http://kerberrose.com/services/kerberrose-technology/

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**Payroll for Tax-Exempt Organizations**

Tax-exempt organizations generally don’t have to pay any federal income tax. But an organization that has paid employees must collect payroll taxes and timely remit them to the IRS. As tempting as it may be to use those funds to relieve financial pressures, don’t do it.

Employers (both for-profit and nonprofit) essentially act as tax collectors for the IRS. The federal income taxes and FICA (Social Security and Medicare) taxes deducted from employees’ paychecks are considered to be held “in trust” for the government. Employers are required to remit the withheld taxes, along with the organization’s FICA contributions, on a defined schedule. Failure to pay could spell trouble for both the organization and any “responsible person(s)."

**What are the FICA tax rates?**

The current Social Security tax rate is 12.4%, evenly split between employee and employer, on the first $118,500 of an employee’s wages (for 2015). The current Medicare tax rate, also split down the middle, is 2.9% on all wages. An additional 0.9% Medicare tax must be withheld once an employee’s wages go over $200,000. Employers are not required to match the additional 0.9% Medicare tax.

**Who are “responsible persons”?**

The definition of a responsible person is very broad. It includes anyone with the duty to collect, account for, and pay the withheld taxes. The IRS is interested in who has the power to see that the taxes are paid. An organization’s paid executives as well as volunteer board members who are involved in an organization’s activities or financial operations are among those who may be considered responsible persons.

**What are the penalties?**

The IRS may collect a penalty equal to 100% of the unpaid payroll tax amount from a responsible person(s) who willfully failed to collect, account for, and/or pay over the taxes. Note that the IRS does not distinguish between for-profit and nonprofit organizations when it comes to collecting unpaid payroll taxes. It pursues both with equal gusto.

**How can you protect yourself?**

Follow the rules and use common sense. Don’t use the payroll taxes you collect for other purposes. Make sure everyone who is a responsible person is fully aware of his or her roles and responsibilities. And make sure your directors and officers (D&O) liability insurance policy provides adequate coverage.

**Here are some additional employment tax issues:**

Worker classification: Properly distinguishing between employees and independent contractors can be a thorny issue because they are treated differently for income-tax withholding and employment-tax purposes.

**Federal Unemployment (FUTA):** Are you paying it? If so, contact your accountant as you may be exempt from paying this tax.

**Fringe benefits:** Fringe benefits are taxable and must be included in the recipient’s pay and reported on the employee’s Form W-2 unless specifically excluded under the tax code.

**Reimbursed expenses:** Employee or officer business expenses reimbursed under an “accountable plan” are not subject to employment taxes. However, amounts paid under a nonaccountable plan represent taxable income and are subject to all applicable employment taxes.
The Council on Financial Assistance Reform (COFAR) was established in October 2011 to lead efforts to improve delivery, management, coordination and accountability of Federal Grants and cooperative agreement.

As part of this effort, the threshold for requiring a single audit was increased from $500,000 to $750,000 and the type A program threshold was increased from $300,000 to $750,000 or 3% of federal awards expended. The percentage of coverage was also changed from 25% to 20% for a low risk auditee and from 50% to 40% for an auditee that does not meet the criteria for low risk.

The COFAR developed the new Uniform Grant Guidance and Single Audit Requirements which will become effective for fiscal years beginning after December 26, 2014. The new guidance will become effective for fiscal years ended December 31, 2015 and after. See Frequently Asked Questions for New Uniform Grant Guidance at https://cfo.gov/cofar/

KerberRose SC is a full service professional accounting and auditing firm. If you would like more information on how KerberRose can assist your non-profit organization, please visit our web site or call Joe Galarowicz, Karen Kerber, Leah Lasecki or Jamie Rosin.

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As experienced advisors, we can provide you and your organization with a wide range of accounting and auditing services. Please visit our website for a complete listing of our services.

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**Non-Profit Perspectives** is published for clients and friends of KerberRose SC As you read the newsletter, you may find that you wish to discuss some of the points brought up in the articles. Please feel free to call us, we’d be happy to answer any questions that you may have.

If you know of someone who would like to receive **Non-Profit Perspectives**, please give Cinda a call at 715-526-9400 or forward their name to cinda.paiser@kerberrose.com. We’d be happy to share information with them!